Lies that 401(k) Plan Providers May Tell You

By Ary Rosenbaum, Esq.

I'm a huge fan of Fleetwood Mac (the Stevie Nicks-Lindsey Buckingham years) and was able to see them twice on their last tour. One of my favorite songs of theirs is Little Lies. Christine McVie, who never gets the credit she deserves as a singer is the lead singer on this song with Stevie and Lindsey as backup. Christine sings: "tell me lies, tell me sweet little lies." As a plan sponsor looking at your current or prospective plan providers, some of them may tell you lies that they want you to believe. As a plan sponsor, it's hard to distinguish the truth from the lies, so this is what this article is all about.

The most important thing is picking providers with the lowest fees

People love saving money, but sometimes picking something that is cheap is a bad idea when the product or service isn't very good. While plan sponsors have a fiduciary duty to pay reasonable expenses, it does not mean they have to pick the lowest cost provider. Reasonableness is based on the fees paid for the services provided, so you can pay more for a higher level of service. So while fees are a consideration, I think choosing providers that are competent is more important because I have seen too many low-frill providers causing large compliance problems for their clients. Picking a provider just on cost is never a good idea.

Since they are already doing your payroll, let them administer your 401(k) plan

There is nothing wrong with some of the major payroll providers who have added third party administration (TPA) services as a natural outgrowth of their business if they did a quality job as a TPA. But they don't. It's a good idea on paper to have your payroll provider handle the administration of your 401(k) plan, but payroll has very little to do with plan administration, and these payroll providers have shown a lack of detail which is required for quality plan administration. While these payroll providers have lots of plans on their books, they have a high churn rate, which means they have a high turnover of plan sponsor clients because of their shoddy service. Their fees may be more competitive than other TPAs, but I have seen too many plan sponsors ending up having to spend thousands of dollars to fix errors caused by these payroll providers. In addition, the payroll providers require much legwork from plan sponsors, which is a problem because many plan sponsors have no idea how to administer a 401(k) plan. I have had a client for the past 7 years (through 3 different firms) that will always be my client because I helped them avoid making large refunds to their highly compensated employee for discrimination testing failures, simply by making a corrective contribution. A $7,000 QNEC contribution avoided a salary deferral refund of $10,000 to the owner. This is because the payroll provider TPA never bothered to mention the availability of QNEC and the possibility of adopting a safe harbor plan design in the future. Good TPAs do a lot of hand holding, payroll provider TPAs leave you on your own. So if a financial advisor recommends using a payroll provider TPA, take a pass.

Always ditch that 403(b) for a 401(k)

Since 1997, not-for-profits are able to sponsor a 403(b) plan or a 401(k) plan. Since 2009, these-not-for profits have the ability to terminate their 403(b) plan and devote all their retirement savings to a 401(k) plan. Many third party administration (TPAs) and/or financial advisors advise their potential clients to ditch 403(b) plans and opt for a 401(k) plan. Sometimes it's done to benefit the plan sponsor, but most times it's done because the potential provider has absolutely no idea about the benefits of 403(b) plans. While costs may favor 401(k) plans at times, 403(b) plans have two large advantages in plan design. First off, it is possible to have a 403(b) plan that is not subject to ERISA which means no Form 5500 filing. The savings could be huge if the not-for-profit has more than 100 employees (by avoiding the required audit for

the 5500). In addition, unlike 401(k) plans, 403(b) plans don't have a discrimination test for salary deferrals, just a universal availability requirement. So when a TPA salesman or a financial advisor tries to convince you to ditch the 403(b) plan, makes sure it makes economic sense and not what's best for the plan provider.

Since your plan is using an insurance company platform, it's expensive

Blanket statements can be a little harmful and I have done my fair share of making them. One blanket statement that is often made in the retirement plan business is that any 401(k) plan using an insurance company platform is more expensive than using a fully unbundled/ open architecture provider. The strike against insurance company providers was that their fees were cloaked in wrap fees, where they took mutual funds and added a wrap fee that many plan sponsors were unaware of. That is what I call the myth of free administration. Despite the cloaking of fees, the hope is that fee disclosure will make everything transparent, at least that is the hope. So once and for all, plan sponsors can see what insurance company providers charge. The one thing that people don't understand is that an insurance company provider has different sets of programs for plans of different sizes. So it is quite possible that on many of their programs, their fees may be lower than unbundled providers. This is not an endorsement of one provider or another, it just means that you should use those fee disclosures (you are supposed to get one shortly) you get from your insurance company provider and compare them with other providers because it's your fiduciary duty to do so.

You need more than 15-20 mutual funds on your fund lineup

People think more is more, so when a 401(k) financial advisor tells you that more funds needed to be added when you already have 15-20 (I count multiple target date funds as one fund for count purposes), you need to know a certain fact about fund lineups. The assumption is that more funds on a 401(k) plan's lineup will increase participation because more funds equal more choices. The problem is that studies have concluded that more fund choices actually depress participant deferral rates and participation. Why? Too many fund choices lead to such confusion that a plan participant is so frustrated that they don't bother to defer their salary. A 401(k) plan doesn't need five different large cap growth mutual funds in their lineup. You can have a robust fund lineup with 12-15 mutual funds, you don't need 57.

This solution is the perfect solution for your plan and all plans

Unlike a hat or a rain poncho, retirement plan solutions aren't one size fits all. So whether it's the next great thing like a multiple employer plan, the ERISA §3(16), 3(21), or 3(38) solution, or a safe harbor 401(k) plan design, or automatic enrollment, there is no retirement plan design or solution that fits every plan sponsor. Thanks to the plan sponsor's sophistication, or demographics, or economic resources, any solution needs to be tailored to fit the plan sponsor's needs. A diligent plan sponsor may not need to hire an ERISA §3(38) fiduciary and a 401(k) plan with great participation probably doesn't need a safe harbor plan design. So when a plan provider touts the next retirement plan solution as the best thing since sliced bread, there is no guarantee that that solution is the perfect fit for you and your plan.

This solution will completely eliminate your fiduciary liability

As plan sponsor, you have a fiduciary duty to the plan participants, which is the highest duty of care under equity and law. As plan sponsors, you can take steps to minimize liability, but you can never fully eliminate it. You can minimize liability by purchasing fiduciary liability insurance and hiring plan providers. So when people tout products or services and claim that this product of service fully eliminates a plan sponsor's liability, then you know they are selling snake oil. A multiple employer plan doesn't fully eliminate a plan sponsor's liability since joining a multiple employer plan is a fiduciary function. Even hiring an ERISA §3(38) fiduciary who assumes the fiduciary process doesn't fully eliminate a plan sponsor's liability for the fiduciary process because selecting that fiduciary is a fiduciary function which means you are on the hook if the fiduciary is negligent in their duties. So while you could put pieces in place that can help minimize your liability as plan sponsor and individual trustees, you can't fully eliminate it, even if that plan provider is selling you the Brooklyn Bridge.

Most 401(k) plan providers will tell you the truth and some will try to sell you a product or service that they can't deliver. So don't just buy whatever plan providers are selling, it's important to browse because there is nothing worse than buyer's remorse.

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