Why Plan Sponsors Shouldn't Have Too Much Loyalty to Their Plan Providers

By Ary Rosenbaum, Esq.

When I first started in the retirement plan business in 1998, I worked for a law firm that served as the counsel for a third party administrator (TPA), there was an office worker there named Orville. I remember Orville because I never saw someone who was male who sang "My Heart Will Gone On", the Titanic theme song sung by Celine Dion. Orville wasn't much of a worker, but for some reason my boss had an affinity for him. When the office work wasn't panning out, they made Orville a computer tech guy. I think Orville knew as much as about computers as my grandmother did. When the tech thing didn't pan out, they put Orville in an administrative position of dealing with retirement plan distribution to participants. As my boss would probably say: "he's a good guy, he's loyal." Well, one day, Orville tried to overpay a participant $18,000 more than what the participant had in their account. The person managing the daily operation of this TPA had enough and Orville had to go. From what I was told, Tom actually had to call my boss to get permission tom fire Orville. Never understood why my boss had this loyalty towards Orville. I thought it was a lot of misplaced loyalty. The same can be said of some retirement plans and their plan providers where the plan sponsor places too much loyalty on them. So this article is trying to tell plan sponsors why they shouldn't attach too much loyalty to their plan providers.

It's all about fiduciary responsibility

I have been going to the same dry cleaner for years and I won't hold it against him that he roots for the New York Islanders. My daughter knows that's the place to get a free lollipop and when I see him; I always take the time to talk to go. It's always great to have a rapport with your service providers and have a great relationship with them, but if my dry cleaner does a poor job and charges me an extra quarter for laundered shirts than someone down the block, that's on me. Plan sponsors don't have that luxury because they have fiduciary responsibility, which is the highest standard of care in equity and law. Plan sponsors as fiduciaries have important responsibilities and are subject to standards of conduct because they act on behalf of their employees who are plan participants. These responsibilities include: acting solely in the interest of plan participants and their beneficiaries and with the exclusive purpose of providing benefits to them; carrying out their duties prudently; following the plan documents; and paying only reasonable plan expenses. So hiring a plan provider involves two different facets of fiduciary responsibility, carrying out the duties prudently and paying only reasonable expenses. Prudence focuses on the process that the plan sponsors and the plan's trustee use for making fiduciary decisions. So just going to the local TPA or financial advisor or ERISA attorney isn't enough. The plan sponsor needs to document the decisions in hiring plan providers and the basis for those decisions.

It's usually on the Participant's dime

It should be no secret that most defined contribution plans are paid by participants through their account balances. So that is why plan sponsors have to be more vigilant in the selection and retention of their plan providers because the participants are footing the bill, If you are footing the bill, overpay If the participants are paying, you have to be thrifty. All right to have loyalty to the plan provider, but less so if the participants are picking up the tab.

Loyalty can be a one-way street

Outside of the world of fiduciary responsibility, there is nothing wrong with being loyal to a particular product, brand, or service. The problem is that unless the product, brand, or service has some sort of loyalty program, the loyalty is usually a one-way street. I learned that the hard way when a favorite pizza joint of mine gave me food poisoning and the owner didn't seem to care. Loyalty is an admirable trait, but it can do a lot of harm if it's misplaced. I see that with many plan sponsors who have loyalty to their plan providers, which is not reciprocated, but is actually betrayed. Plan sponsors should pick plan providers based on competence and they should check every so often to make sure these plan providers are doing their jobs. Just sticking by providers because you have retained for so long is one reason to maintain that relationship, but it shouldn't be the only reason. I had a client being sued by the Department of Labor because the client had used a TPA for 28 years, who apparently wasn't doing the necessary work in the administration of a defined benefit plan. Saying you used someone for 28 years is nice, that you have longevity. It's not so nice if you discover that they didn't do the work and as a plan fiduciary, you are the one on the hook for what the plan provider did or didn't do. There is nothing wrong with always using the same plan providers, but there is something wrong is that the only reason you keep them because you have been using them for so long. Plan providers should be evaluated every so often to determine their competence because you may have a shock when your long time provider turns out to have thrown you under the boss with poor work.

Don't be schmoozed by your provider

I worked at a TPA where the head of our company was a master salesman and his partner was incompetent in overseeing plan administration. So when a client called to complain, often the client was invited to a dinner, a lunch, or a Yankees game. While that "comp" was nice, it might have been a prohibited transaction. A plan provider furnishing goods, services or facilities to a plan fiduciary like a trustee or plan sponsor might be a prohibited transaction. While it's generally agreed that there is a de minimis exception where a plan provider could furnish up to $250 worth of good and services to a plan fiduciary without being considered a prohibited transaction, it sets a bad precedent that your decisions on whether

to retain said plan provider looks like it was dependent on you "wetting your beak". There is nothing wrong with a plan provider cutting back on fees or making refunds to make good on their errors, but that doesn't benefit the plan fiduciary personally. Consider placing in policies that limit what fiduciaries can or can not accept in gifts from plan providers and how it should be documented to ensure that it does not affect the fiduciary decision making process as well as avoiding a prohibited transaction.

Nepotism has no place with picking plan providers

Years ago, I worked at a semi-prestigious law firm on Long Island (sorry, Lois) where a former client of mine when I was working at a TPA was a corporate client of that firm. The corporate attorney, sensing he can make more money through this client, contacted them about my services. Without even discussing my services and how they didn't conflict with the TPA's work, they snapped back that they had no interest in my services. I was surprised until I found out that the human resources director was a cousin with that TPA's owner. So while hiring your cousin to handle your private money is legally OK, there are a couple of reasons why it's a bad idea. Hiring your cousin as a financial advisor might not be considered a prohibited transaction (hiring your spouse or parent is and will result in penalties), but it certainly can be considered a breach of fiduciary duty if the only reason you picked him was because he was your cousin. Selecting plan providers has to be through a process and there are various parameters you should look at (such as experience, fees, etc.) and any familial relationship isn't one of them. Charity begins at home, but home isn't your company's retirement plan.

It's not adultery

You are not married to your plan providers, so speaking to another provider on their services and fees is not adultery. It's being a good fiduciary. There is nothing wrong with being loyal to providers that are competent and cost effective, but benchmarking those providers against competing providers is part of your job as a plan fiduciary. So when a financial advisor, retirement plan consultant or ERISA attorney asks you to look at other providers as comparison for competence, cost, and list of services, do it because it's your job. Your plan provider will forgive you for your "transgression" because it's part of your job and the nature of the retirement plan business.

THE ROSENBAUM LAW FIRM P.C.

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