

Fiduciary Myths and Misconceptions in the Market



Jessica Marson

3(16) Practice Leader

There are a lot of misunderstandings in the retirement industry regarding fiduciary services and 3(16) plan administrators. Why do they exist? What do they do? How do you find a good one? We'll answer these questions and address some myths in this article.

Setting the Scene

If you're not a business owner, imagine for a minute that you are. You've developed an awesome idea and framework for your business and you're executing your business plan! You are constantly thinking of how you can be growing, improving, and competing in the market.

And oh, by the way, you want to offer your employees a retirement plan to attract and retain talent, gain tax savings, and to help prepare for a brighter financial future.

As you look into it, you find there are a ton of options, IRS and DOL rules to manage, and a myriad of service providers. But you're an expert at your business, not retirement plans. Can't someone just tell you what the best choices are and take care of it for you?

That's where the financial advisor comes in. They help you sort through the many service provider choices available in the marketplace. One of those service providers is a 3(16) plan administrator/fiduciary, and we're going to take a closer look at that one.

Why does a 3(16) fiduciary service exist?

The DOL holds plan sponsors (the business owners) responsible for all aspects of their retirement plans, expecting them to be well-versed in retirement and compliance. As most business owners are typically not, the DOL allows them to hire experts, or fiduciaries, to act on their behalf. That's where these fiduciary service providers enter the scene.

Generally speaking, two types of these fiduciaries – 3(38) and 3(21) – involve investments, while another – 3(16) – involves the daily operations and administration of the plan. Under ERISA's definition, the 3(16) plan administrator takes responsibility for the daily administrative tasks associated with the plan.

Business owners may not realize how many tasks come with offering a retirement plan, but there are many. Different 3(16) providers can perform a variety of tasks, ranging from all or a few, depending on their capabilities and service agreement.

The Market: Myths and Misconceptions

The 3(16) plan administrator definition can leave a lot up to interpretation. Additionally, different providers offer many different levels of service, along with taking on varying levels of liability. Below are some misconceptions to be aware of in the market.

"Third-party administrators are the same as a 3(16) plan administrator." False.

The role of a 3(16) plan administrator is quite different than that of a third-party administrator, no matter how thorough the TPA is. TPAs do not take fiduciary liability. Also, they are not responsible for the tasks required of a 3(16) plan administrator. The highest level of 3(16) plan administration service occurs when the provider acts as the plan sponsor, taking on the fiduciary liability and all the action items the plan sponsor would typically be responsible for when administering the plan. Therefore, with all the differences in the market, plans sponsors should evaluate the services each provider states they will complete in their service agreement and benchmark against other providers.

“All 3(16) plan administrators take fiduciary liability.” False.

Many 3(16) providers in the market take on plan administrative tasks, but they do not take liability for these items as a fiduciary. If this is the case, the plan sponsor is trusting the provider with critical compliance activities, but the provider isn't taking liability for their actions.

This creates a false sense of security for plan sponsors. If the outsourced 3(16) provider's work contains an error and an issue comes up with the IRS or DOL, the outsourced 3(16) service provider is not held liable. Any mistakes are solely the responsibility of the plan sponsor. Therefore, it's important to investigate potential providers and determine if they actually act as fiduciaries for plan sponsors.

“Recordkeepers will check payroll data for accuracy.” False.

One of the biggest misconceptions in the retirement industry is that payroll data is accurate. Payroll data fuels the necessary actions and tasks needed for daily, weekly, monthly, and yearly retirement plan tasks. However, it often contains simple errors that can lead to costly retirement plan mistakes. Examples of common errors include:

- Uploading the wrong payroll file (i.e. the previous payroll cycle)
- Missing or incorrect dates of birth
- Errors in social security numbers
- Ineligible contributions

And these are just a very few that are quite common.

Plan sponsors might believe that the recordkeeper is reviewing for errors like this, but that is not the responsibility of the recordkeeper. Instead, this incorrect data is used to execute plan tasks, leading to incorrect eligibility tracking, notice distributions, vesting, billing, etc.

No one is checking to verify the data is accurate, so these common errors can lead to costly fees – including the cost to fix the error and the potential penalty from the IRS or DOL. Thus, plan sponsors need to ensure their payroll data is 100% error free all the time. But is this really realistic or feasible?

Ask potential 3(16) service providers if payroll data integrity is something they address. It's important to be aware and ask the right questions when evaluating potential providers.