

# PAYING “REASONABLE” PLAN EXPENSES

BY DALE R. VLASEK

**The advisor’s number-one focus should be on serving the plan, even though it may require tough discussions with individuals the advisor may have recommended.**

One of the perennial issues facing the sponsors, participants and fiduciaries of 403(b) plans, as well as the consultants servicing or advising such individuals or plans, is the subject of plan expenses. Section 403(b) plans, particularly those that are covered by the Employee Retirement Income Security Act of 1974 (ERISA), must carefully watch what they spend with their limited resources.

ERISA specifically mandates that a plan may not use plan assets to pay expenses unless such expenses are “reasonable.” Of course, that leads to the question: What is “reasonable?” If a plan pays more than “reasonable expenses” the plan’s fiduciaries have breached their duties to the plan.

The Department of Labor (DOL), which is charged with enforcing ERISA, has repeatedly sidestepped providing any type of direct quantitative answer. Historically, the DOL’s response has been that “reasonable” is determined by the actual services being provided and the surrounding facts and circumstances.

When 403(b) plan fiduciaries review plan expenses, the advisors may find themselves in a difficult ethical situation because they’re normally among the service providers paid by the plan and may have recommended the other service providers engaged by the plan.

### TYPES OF EXPENSES

Generally, 403(b) plan expenses can be divided into two very simplistic and broad categories – administrative expenses and investment expenses.

The administrative expense category would encompass such expenses as fees imposed by the plan for loans and distributions. The plan sponsor typically doesn’t create these fees, they’re usually part of a schedule charged by the third-party administrator or recordkeeper.

The plan sponsor, in most instances, just accepts those charges and passes them along to participants. The DOL has acknowledged that plans may charge such fees – once again as long as they’re reasonable.

In addition to expenses imposed on particular participants for using services or options available under the plan, plans have “global” expenses imposed on all participants. These expenses could include such things as preparation of plan documents, Form 5500 annual reports, and the audit of larger plans required for the Form 5500. Until recently, these expenses were minimal or nonexistent for 403(b) plans. Although ERISA-covered 403(b) plans had been required to have documentation for years, many plans were run with minimal or no documentation. In addition, the Form 5500s required for 403(b) plans were very simple and didn’t require audits even for plans covering 100 or more participants. That changed in 2009 and 403(b) plans require compliance with reporting and disclosure comparable to that required of other retirement plans.

For plans with 100 or more participants, an audit is required. The audit and more elaborate Form 5500 reporting have added expenses for not-for-profit plan sponsors at a time when such



## THE SHORT FORM

- Assist the client in achieving a list of fees more in line with the market.
- While maintaining good referral relationships is important, the advisor's first priority is to the plan's fiduciaries.
- Advisors can serve as a sounding board for fiduciaries or plan sponsors by discussing the need for Form 5500 and audit fees.
- An advisor can provide an invaluable service by making these fees comprehensible.

organizations are suffering revenue and donation declines. The costs for audit services can and are often passed along to the plan itself. Once again, the DOL has indicated it is permissible to do so as long as the expenses are "reasonable."

## INVESTMENT EXPENSES

Under the Internal Revenue Code, 403(b) plans can be invested in only two types of investments – annuity contracts and/or mutual funds. Both of these investment types are subject to internal fees and expenses. Furthermore, some advisors may add additional fees, such as "wrap" fees or investment advisory fees. Once again, ERISA permits a plan to pay such fees so long as they're "reasonable" based on the services provided.

One of the problems plan sponsors and fiduciaries have had is understanding what fees were being charged and the exact amount of those fees. The DOL has been working for years to develop a reporting requirement that mandates disclosure of such fees. Various interim and final regulations have been issued and service providers will need to more fully disclose fees to plan fiduciaries. Plans, including 403(b) plans, will need to disclose such fees to participants on a quarterly basis. Thus, the providers and advisors will need to provide this information. A concern in

the industry is that once plan sponsors and participants view the fees, they may question the charges.

## ACTION STEPS FOR ADVISORS

In the climate of scrutinizing expenses, advisors have an excellent opportunity to provide a useful service to their fiduciary and plan sponsor clients, but in doing so the advisor may be injuring referral relationships and may need to explain and justify his or her own compensation.

First, most fiduciaries and plan sponsors don't understand the nature of the administrative fees imposed by the TPAs. To the extent that it's possible to provide the fiduciary or plan sponsor with data documenting what typical fees are would be a tremendous help. If the "typical" fee for a loan is \$100, why should a plan charge \$125? To the extent such fees are negotiable, it may be possible to assist the client in achieving a list of fees more in line with the market fees. Potential issues for an advisor may arise if the TPA is someone the advisor recommended. While maintaining good referral relationships is important, the advisor's first priority is to the plan's fiduciaries.

Second, although the fees for Form 5500s and audits may be outside the expertise of most advisors, simply serving as a sounding board for the fiduciaries or plan sponsors to discuss the need for these services and to at least test the market from time to time can be of great help.

Third, investment fees are, of course, integral to how advisors are compensated. These fees can be complex and hard for a plan sponsor or fiduciary to understand. An advisor can provide an invaluable service by making these fees comprehensible. Although there may be a tendency for plan sponsors or fiduciaries to gravitate toward products with lower fees and internal costs, that may not always be the correct response.

The reasonableness of fees is measured by what the plan is receiving for those fees. If a provider has higher fees, but in turn generates revenue sharing with TPAs who in turn lower their fees, the fees and

expenses may be very reasonable when all is considered. An advisor can help explain this situation to assist plan sponsors and fiduciaries in reviewing those costs and services.

Likewise, the fees and expenses paid directly or indirectly to the advisors should also be scrutinized:

- What services is the advisor providing?
- Is the advisor providing fiduciary reports to the plan fiduciaries?
- Is he or she attending in-person or telephonic meetings with the fiduciaries?
- Are the meetings quarterly or at least annual?

Does the advisor routinely attend enrollment meetings for plan participants to help explain the investment options available? (Advisors providing general information aren't required to move into the realm of direct investment advice.)

Keep in mind that an advisor who sets up a 403(b) plan and has never had conversations with the plan sponsor or the fiduciaries after the signatures were on the paperwork may have a difficult time helping those fiduciaries justify fees and expenses paid to the advisor as "reasonable."

## CONCLUSION

An advisor can have an ethical dilemma when trying to assist 403(b) plan fiduciaries to understand how to properly pay only "reasonable" plan expenses with plan assets. The advisor's number one focus should be on serving the plan, even though it may require tough discussions with individuals the advisor may have recommended and perhaps explaining and justifying how and how much the advisor is paid.



*Dale R. Vlasek is an attorney with McDonald Hopkins LLC in Cleveland, Ohio.*