Ethics and Professionalism in the Retirement Plan Services Arena

by Richard A. Hochman, APM

This article addresses several different professional ethics issues that one may confront while working within the qualified employee plans arena. Not all situations that are encountered in one’s daily practices have clear-cut correct answers. Instead, work is frequently performed in confusing grey areas.

For retirement industry professionals, meeting the requirements of an hour or two of continuing professional education does not begin to address the larger issues involved with conducting their business affairs in an ethical and professional manner. One key issue to be noted is that there are no industry-wide standards because so many different types of professionals practice in the retirement services area.

Striving for a Higher Standard
In the course of adopting and operating its company’s plan, an employer may work with an attorney, accountant, actuary, recordkeeper or contract service provider, investment advisor, institutional trustee or some combination of the above. Each of these advisors/service providers may belong to a different professional group and each such group has its own practice standards. Some groups may be subject to specific licensing requirements and testing, while others are not. To some degree there may be an overlap in the services being provided by the various professionals, which may, in turn, result in conflicts in the advice that the employer receives. Additionally, some of these professionals may serve as referral sources for the others. This situation could lead to confusion as to who the party is that is actually being serviced (i.e., “the client”). Is the advice that is provided to the employer or the decisions that are being made influenced by a concern about the continuation of referrals? Does the service provider serve multiple roles, such that there are internal conflicts in properly servicing the employer? If the service provider serves as recordkeeper, there is one set of duties and responsibilities, but as trustee, there is a different role and likely fiduciary duties that did not previously exist. For example, the Department of Labor recently issued guidance in Field Assistance Bulletin 2008-1, stating that those serving in the capacity of Trustee are responsible for making sure that the employer is making proper and timely contributions to the plan. Clearly, a recordkeeper has no such duty.

To better understand the roles that practitioners fulfill, it might help to examine how the various professionals interplay with the employers who sponsor retirement plans. A small employer wishes to start a qualified...
retirement plan on behalf of the owner(s) and the employees. How might the employer begin the process? The employer could approach any of the industry professionals listed previously. Depending upon who is approached, questions may receive entirely different answers, and the employer may end up with different plans and arrangements. The first issue is that there is not necessarily one right answer for the employer's fact set. Additionally, the employer may not know exactly what they want or they might not understand the alternatives available. Then the employer will have to confront the issue of what the company may be able to afford or what may work best for the owner(s) and the employees. As we begin to work with the employer, we must convey the important message that adopting a qualified plan is not a one or two-year commitment, but a commitment for a much longer term which, in turn, may mean a significant investment on the employer's part, though not necessarily a long-term relationship with any one practitioner/vendor. The employer may not understand what they really want. Just because one of their business associate's firm has a particular kind of plan, that plan design might not be right for this employer's situation. In other words, just because the 401(k) has become the most popular type of plan does not mean it is the best for every employer.

Before the rules changed early last decade, it often made more sense for small employers to have a basic profit sharing plan than a 401(k) because they could get a larger allocation depending on what their employees deferred. Yet many of these employers were nonetheless sold 401(k) plans, which may have had higher costs and smaller benefits. In trying to obtain a plan, one problem that the employer may confront is that the "plan-in-a-box" approach may be all that certain vendors are looking to sell or capable of selling. Does this approach potentially create a best practices issue? Some might clearly argue yes! Or is this merely a situation where the employer is getting what they are seeking out and/or paying for? As with everything else in the real world, there is no such thing as a free lunch. An employer that looks only at cost will receive a different standard of service than an employer that is willing to pay for what they need. Obviously, cost and pricing become issues in the delivery of services and impact service quality. This article does not address the issue of fee disclosure under ERISA Section 408(b)(2), which is a current hot topic in the regulatory environment and has its own steamer trunk full of ethics issues.

If the employer approaches a provider looking to buy a particular plan type, might it be inappropriate to sell that plan to the employer? Quite possibly the answer is yes! How many service providers, large or small, would let the employer leave without giving them what they asked for? As an illustration, years ago when setting up a new company, we had the need for new computers. Thinking I knew what the possible alternatives were, I approached several computer vendors requesting a quote for computers with a specific type of chip. One vendor had the "nerve" to say to me, "Before I provide a quote, let's discuss what your company does and for what tasks the computers will be used." They wanted to be sure that the computer and the chip that I requested were the right ones for my needs. The vendor's approach resulted in a recommendation for a different computer from a different company and very different technology. When I approached the other vendors about which computer and chip type would better meet my needs, they said that, in fact, the alternative computer would be better. When I asked why they didn't tell me that to begin with, I was told, "You came in with a specific request. Why would we advise you to buy something else?" In other words, I was much better served by the vendor who took the time to inquire and listen and made a recommendation based on all of the facts, not just what I thought I wanted. Would it have been an ethical violation to sell the computer that I asked for to me? Clearly not; but a higher standard of professionalism served me better. As an ASPPA member, should I not also be looking to always engage in a higher standard of practice, understanding that not all employers are going to want to pay for it?

In our industry, how often, when working with takeover cases, do we encounter an employer in a plan (or a combination of plans) that does not meet the employer's needs or goals? How many times has an employer been sold a plan that lacks the necessary flexibility or operates in a way that is counter to the stated objectives that the employer has identified? (We must accept, however, that the employer may have told the prior provider something very different from what you were told.) The employer then approaches your firm for help to remedy the problem. In a depressed economic environment similar to the one in which we now find ourselves, there aren’t many new plans being sold and much of the available new business may be in the mode of takeovers from another benefits provider. Might there be ethical considerations that come into play before you agree to the engagement, especially if you are going to give advice that is contrary to that offered by another industry practitioner?
ASPPA’s Code of Professional Conduct

ASPPA maintains a Code of Professional Conduct that is to be followed by its members. Under the heading “Professional Integrity,” the Code provides, “An ASPPA member shall perform professional services with honesty, integrity, skill and care. A member has an obligation to observe standards of professional conduct in the course of providing advice, recommendations and other services performed for a principal.”

Under the heading “Disclosure,” the Code provides, “If a member is invited to advise a principal for whom the member knows, or has reasonable grounds to believe, that another benefits professional is already acting in a professional capacity with respect to the same matter or has recently so acted, it would normally be prudent to consult the other benefits professional both to prepare adequately for the assignment and to make an informed judgment whether there are circumstances as to potential violations of this Code which might affect the acceptance of the assignment. The prospective new or additional benefits professional should request the principal’s consent to such consultation.”

Finally, under the heading “Courtesy and Cooperation,” the Code provides, “An ASPPA member shall perform professional services with courtesy and shall cooperate with others in the principal’s interest. Differences of opinion among benefits professionals may arise. Discussion of such differences, whether directly between benefits professionals or in observations made to the client by one benefits professional on the work of another, should be conducted objectively and with courtesy. A member in the course of an engagement or employment may encounter a situation such that the best interest of the principal would be served by the member setting out a differing opinion to one expressed by another benefits professional, together with an explanation of the factors which lend support to the differing opinion. Nothing in this Code should be construed as preventing the member from expressing such differing opinion to the principal.”

Real Life Situation

Many years ago, an employer that had been sold a combination of plans approached the firm I was working with for help. They told us that they could not afford the necessary contributions and wanted out of their approved plans. Specifically, they had recently been sold a combination of money purchase, target benefit and defined benefit plans—all covering the same employees. In analyzing their situation, perhaps the most interesting or significant comment that the employer made was that they were in the investment business and did not have consistent cash flow and needed flexibility for their plan contributions from year to year. They assured us that the prior provider was specifically advised of that fact.

How could the employer be in this position to begin with? The employer approached a well-known benefits counsel about adopting a qualified plan arrangement. That attorney sold them three different documents at a significant cost for each one. Was there an ethical breach in light of what was delivered to the employer? While a combination of defined contribution and defined benefit plans would not be that unusual, could there be a need for both a money purchase and a target benefit plan covering the same employees? With all three plans being subject to minimum funding requirements, clearly there was little flexibility for the employer when it came to the amount of their contribution. Looking at the adopted plans, one might wonder if the employer said they wanted to maximize their deduction or wanted flexibility as to their contribution amount.

We spent the next year working to unwind the plans and asking the IRS to allow us to terminate them because the employer did not understand the commitments that were made. Clearly, there was some discussion with the client about why they were in the position in which they found themselves. Either the employer did not properly explain things to the prior professional or the retirement services professional did not clearly explain things to the employer when all the documents were executed. We did not talk to the other provider as we wound down the plans and had the employer’s tax returns adjusted to reflect that they were no longer claiming the plan deductions. We did not initiate any disciplinary proceedings against the prior provider. One question is whether or not we were required to contact ASPPA or the State Bar Association. We did not believe so and did not. Interestingly, the defined benefit plan was covered by the PBGC.

I told the same story during a subsequent lecture that was attended by a PBGC manager.

For the Trustee, the ultimate duty is to the participants and beneficiaries, even for those serving in a self-trusted role.
The PBGC came up to me during the break and let me know that their office was aware of some of the problem practitioners in the industry.

Conflicts of Interest

Whenever a practitioner works with or is considering working with a client, one issue that can arise is that of “conflicts of interest.” The issue addresses the basics of whether or not the professional can represent a specific client. The rules for this area are sometimes very complex and seemingly internally conflicting. The underlying question is whether or not representing a client will negatively impact the professional’s ability to represent another existing client. Does the client hold an interest that is counter to an interest of another client? Does the professional have a personal interest that is counter to the client’s? These considerations frequently bring up the question as to who the client will be. Is the ultimate client the employer/plan sponsor, the plan administrator or the administrative committee, the Trustee(s), the participants and beneficiaries or a combination of the above? Not knowing who the ultimate client is can and will lead to major problems. When representing the employer/plan sponsor, the professional’s duty is to that person or firm and not the participants. For the Trustee, the ultimate duty is to the participants and beneficiaries, even for those serving in a self-trustee role. When a problem arises, a decision may need to be made about retaining an attorney. It is important to remember that only attorneys can have privileged conversations. Non-attorney advisors must be careful not to put themselves in a position where they may end up being a witness against their clients or their clients’ interests because they lack the privilege not to testify.

You might also encounter a situation where a client asks that you do something that is not illegal per se, but may be viewed as ethically questionable. Will practitioners always be able to see the line and know whether or not they can step across it? Per the old cliché, will we know it when we see it? When what is now the EPCR program was first introduced as the Administrative Policy Regarding Self Correction, we were told that the program was not available for “egregious” violations. When we asked what those violations were, we were told that they hadn’t happened yet, but the IRS would know one when they saw one. We were later told that an employer went to jail for such a violation.

Plan Document Issues

In spending a lot of time around and with plan documents, an issue that one hears raised is the proper use of pre-approved plans. While some practitioners attack their allowability, this article will not address that issue. One of the required provisions in all prototype adoption agreements is a statement “that the failure to properly fill out the adoption agreement may result in the disqualification of the plan.” During earlier submission cycles, the IRS discovered that not all prototype sponsors were as concerned with compliance issues as they were with gathering and managing plan assets. To that end, the prototype sponsors were not assuring that the employers were completing the adoption agreements, nor were they making sure that employers were adopting and following amendments made between restatements. Thus, the adoption agreement must contain a statement that the sponsor will inform the adopting employer of any amendments to the plan or of the discontinuance or abandonment of the plan. Perhaps more importantly, adopting employers did not always know who the prototype sponsor was or how to contact them. Accordingly, the IRS added a requirement that each adoption agreement must include the name, address and telephone number of the sponsor or the sponsor’s authorized representative so that adopting employers will know who to contact to ask questions about the qualified status of the underlying document.

With that basic guidance spelled out, an issue to consider is whether all prototype sponsors are or should be held to a single standard of conduct/professionalism when it comes to the maintenance and operation of their prototype documents. One must first determine who can be a prototype sponsor. Revenue Procedure 2005-16 spells out the definition as “any person that has an established place of business in the United States where it is accessible during every business day may sponsor a plan as a word-for-word identical adopter or minor modifier adopter of a plan of an M&P mass submitter, regardless of the number of employers that are expected to adopt the plan.” Those not working with a mass-submitter may sponsor a prototype so long as they represent to the IRS that they have at least 30 employer-clients, each of which is reasonably expected to timely adopt the sponsor’s basic plan document. Those who typically sponsor prototype documents include law firms, accounting firms, actuarial firms, third party administration and recordkeeping firms, financial institutions of all sorts including banks, trust companies, brokerage houses, investment advisory firms, insurance companies, mutual funds and credit unions. With such a diverse group of sponsors, can one standard be applied? An argument can be made that since the ability to sponsor a prototype document is controlled by one agency, namely the IRS, that one standard of conduct could be imposed upon all sponsors. In reality, however, despite the best efforts of the IRS, it is clear that different standards of behavior apply. Law firms not only have to be concerned about the IRS and the Internal Revenue Code, but also have to operate under the rules established by the various State Bar Associations and the American Bar Association. Likewise, accounting firms must operate under the rules of the American Institute of Certified Public Accountants. Enrolled Actuaries must operate under the rules of the Joint Board for the Enrollment of Actuaries and, in addition, the Code of Conduct of any actuarial association to which they may belong. Similarly, an individual who holds an ASPPA credential will have to satisfy ASPPA’s Code of Professional Conduct even if they don’t hold any other credential. The reason for some of the required language listed previously is that some vendors of prototypes felt that their responsibility for amendments stopped at the preparation and mailing. In their belief, they were not responsible to see to it that the employers received the amendment, timely executed it as necessary and modified the operation of their plan accordingly. Other sponsors understood that their responsibilities included those additional pieces to assure proper operation of the employer’s plan with the latest guidance.
Because of this divergence in operations, there are some practitioners who question the use of prototype plans as complying with best practice standards. As a result, the IRS will occasionally impose a different set of rules on adopters of prototype plans, illustrated by the additional limitations imposed on prototypes using cross-tested allocations.

Regardless of the business entity they represent, all sponsors of prototypes and other document types should establish procedures to assure that adopting employers are kept up to date with regard to their plan documents. The recent amendment and restatement of all pre-approved defined contribution plans for the EGTRRA law change gave plan sponsors the opportunity to evaluate their own procedures. For example:

- Did they have a current list of all adopting employers?
- Were they able to contact all of those employers and meet or communicate with them about their plan terms and provisions?
- Did they have a methodology to assure that all employer-clients responded?
- Were procedures in place for employers who did not respond or who did not meet return deadlines?
- Were other document amendments necessary to reflect interim amendments that had not previously been made?
- Did the sponsor or the client have copies of up to date documents?
- Did the old documents reflect operation of the plan? Will the new documents?
- How was the issue of submission for determination letters handled?
- If employers fell through “the cracks,” could they determine how and why?

Client Records

Practice before the IRS is governed by Circular 230. Circular 230 provides in part that, at a client’s request, a practitioner must promptly return records that the client needs to comply with their federal tax obligations. The practitioner may retain copies of the returned records. However, the Circular states that—A return, claim for refund, schedule, affidavit, appraisal or other document prepared by the practitioner or the practitioner’s firm, employee or agent is not considered a client record if the practitioner is “withholding” the document pending the client’s payment of fees required by “its contractual obligation” to the practitioner. That said, can a practitioner just refuse to return documents on the grounds that their bills have not been paid? There are some who argue that, under a reasonable interpretation of ASPPA’s Code of Professional Conduct, the client’s data belongs to the client and not the practitioner, and that the data must be returned even if full payment has not been received. While the practitioner may own its work product utilizing the data and the charts, tables and graphs that it produces as a result, they cannot withhold the raw data. What liability might there be if a practitioner refuses to return data and the annual Form 5500 is late and the employer incurs a penalty?

Control of Work Product

An ASPPA member shall not perform professional services when the member has reason to believe that he or she may be used to mislead or to violate or evade the law. The material prepared by a member could be used by another party to influence the actions of a third party. The member should recognize the risks of misquotation, misinterpretation or other misuse of such material and should take reasonable steps to ensure that the material is clear and presented fairly and that the sources of the material are clearly identified. The member’s opinion could be misused to promote products that result in abusive tax avoidance transactions (ATATs).

Conclusion

In performing our day-to-day duties, it is important to be aware of the types of ethical issues that can sometimes present themselves. When faced with difficult situations, it is common to solicit legal advice or consult with respected industry experts to gather opinions on how best—and ethically—to handle difficult situations.

When faced with difficult situations, it is common to solicit legal advice or consult with respected industry experts to gather opinions on how best—and ethically—to handle difficult situations.

---

Richard A. Hochman, APM, is an attorney with extensive background in the tax and employee benefits field. In his role as president and COO at McKay Hochman, Rich supervises a team of attorneys and consultants in the design, drafting and support of prototype and custom documents for financial institutions, brokerage firms, insurance companies, pension consultants and plan sponsors. As a member of the firm’s training faculty, he regularly participates as an instructor in continuing education programs sponsored by the firm, including in-house programs and at a variety of pension industry forums such as Enrolled Actuaries (EA), as well as forums sponsored by ASPPA and NIPA. Rich provides written commentary and testimony in Washington, DC on regulatory issues on matters relating to qualified retirement plans on behalf of clients. During his benefits career, Rich has been responsible for designing and implementing prototype and individually designed plans. He has also published tax analysis for use by attorneys, accountants and consultants on a broad range of topics. Rich currently serves on the Board of Directors for ASPPA. (rhochman@mhco.com)