

# Which Expert would a Prudent Person Hire?

ERISA describes a heavy burden for employers that sponsor a retirement plan for their employees. Many business owners hire professionals to help shoulder the burden. The key to alleviating the burden is knowing which expert to hire.

The Employee Retirement Income Security Act of 1974 (**E.R.I.S.A.**), applies the "Prudent Man Rule" to explain the fiduciary burden of employers. The "Prudent Man Rule" says that the plan sponsor should make decisions on behalf of the plan participants as a prudent person would if making informed decisions about their own account. In other words, what investments, fees, plan design, and plan provisions would a prudent person choose for their own account? And if that prudent person lacks the expertise to choose the best course, they should hire an "expert." An imprudent person would "wing it" while a prudent person would hire the expertise they lack.

Hence, the first and most important fiduciary decision an employer makes is hiring an expert. But which expert would a prudent person hire?

It should be noted that an easy candidate to eliminate is the person who promises

the employer that they will replace them as a fiduciary. The employer who sponsors a qualified retirement plan is always the fiduciary. There are a variety of services offered that can help mitigate



some of the fiduciary risk. This third party can become a co-fiduciary, but under no circumstances is it possible to completely eliminate all of the fiduciary liability. In fact, as that expert is hired, the fiduciary liability continues for the plan sponsor as they are responsible for oversight of this third party.

The expertise employers use comes from one of five sources, the first form of expertise being internal and the others being external or third party. In other words,

Option A for some employers is to save the cost of hiring a third party and provide the expertise internally. For obvious reasons, a prudent business owner would not choose this route unless their business is actually within the industry that lends itself to that expertise. A prudent person would weigh the cost of not hiring a specialist for the expertise required and assess the cost of having a plan out of compliance. Operating without expertise may increase liability.

The next option is hiring either an insurance broker, financial advisor, or retirement plan consultant. The prudent business owner disregards the ancillary relationships involved and objectively evaluates the expertise. In fact, under ERISA, the employer has every obligation to avoid any potential conflict of interest. For instance, if a business owner wants the same firm to handle both the retirement plan and banking, the owner faces additional burdens to demonstrate that the bank offered the best solution for the retirement plan also. It is a prohibitive transaction to use the retirement plan to receive preferential treatment for another service.

If the business owner needed expertise in insurance (life, health, or disability); "key-man

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insurance" or "buy-sell agreements") their insurance broker may provide that expertise. But if they need expertise in an unrelated field, like retirement plans, the expertise may be lacking. Complicating this matter further is how the insurance agent is paid and whether they take responsibility

for their advice. The DOL is expanding the definition of fiduciary and asking experts to take responsibility, though many insurance brokers are not legally able to take a fiduciary role. The DOL is also working to limit the commissions paid on the underlying investments.

Financial Advisors remain a viable option, if they are able to work on a fee-only basis and take fiduciary responsibility. The key is their "expertise." Is it investments, ERISA, behavioral finance, Retirement Wellness? While "investments" is a related field, studies consistently show the key to Retirement Readiness has less to do with investment choices and much more to do with behavioral choices of how much people save. Additionally, if their expertise is not ERISA, issues of compliance may arise.

To capture the expertise necessary for a healthy plan

(one without compliance issues) and healthy plan participants (closing the Retirement Gap) some employers will have to move

needed expertise. This may be the most expensive route and ironically the route necessitated by business owners who chose Option A to cut cost.

Hiring expertise is prudent, but the prudent employer is careful about the source of that expertise. It may not be prudent for the employer to choose doing it themselves. It may or may not be prudent to hire an insurance agent,

financial advisor, retirement consultant, or independent counsel. The key is hiring someone who will provide the right expertise and take legal responsibility for the expertise they provide. ♦

For questions or information regarding any of this material, please contact us directly.

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## **ERISA's Guideline for Prudence**

- A. Working w/o Third-Party Expertise
- B. Hiring an Insurance Broker
- C. Hiring a Financial Advisor
- D. Hiring a Retirement Consultant
- E. Hiring outside ERISA Counsel

to the next option and hire an independent retirement plan consultant, although prudence must still be given to assessing their fees, and they should be able to operate on a fee-only basis as an RIA and be willing to take fiduciary responsibility.

What's the difference between an advisor and a consultant? A financial advisor has quarterly investment committee meetings but may not discuss measurements of plan health like participation rates and deferral rates. The consultant has quarterly retirement plan committee meetings, of which investments are one element, and measurements of plan health (compliance & participation) are central.

The fifth option for engaging the expertise needed for the retirement plan is for the employer to hire outside ERISA counsel for the



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