[Investment]

Limit Your Retirement Plan Liability

By James E. Demmert

Offering a retirement plan can be one of the most rewarding decisions a business owner can make. It's an excellent way to enhance employee loyalty and build wealth over the long term. However, these plans are regulated by the Department of Labor (DOL) and require careful management by the business owner. Most important, business owners who don't follow the basic DOL standards of conduct may be personally liable to restore any losses incurred by a retirement plan. Therefore, it's essential that business owners keep abreast of DOL laws and responsibilities.

To limit liability, business owners need to understand some basic rules, specifically the Employee Retirement Income Security Act (ERISA). This act was established in 1974 to protect employees. Since business owners act on behalf of participants and their beneficiaries in a retirement plan, the DOL considers business owners fiduciaries subject to specific standards of conduct. By following a few simple guidelines, business owners can enjoy all the benefits that retirement plans offer and avoid potential pitfalls.

Act in your employees' interest. Although business owners may own the lion's share of their company's retirement plan assets, they can't handle the plan's assets and investments as if they were their own. (For example, I once met a business owner who purchased an expensive painting as a retirement plan investment and then proceeded to hang the painting in his home! I don't recommend this.)

Hire a professional. The duty "to act as a prudent investor" is one of a business owner's central responsibilities under ERISA. It specifically requires that business owners have expertise in investments or that they hire a professional investment manager.

Document. One way fiduciaries can demonstrate they've carried out their investment responsibilities properly is by documentation. A well crafted investment policy statement (IPS) describes the age and risk tolerances of plan participants as well as the plan's investment processes. This document demonstrates to the DOL a well thought-out investment process and can protect business owners from disgruntled employees.

Diversify. Diversification, another key fiduciary duty, helps minimize the risk of large investment losses to the plan. Business owners should ensure retirement plan assets are well diversified across multiple assets classes and that no one investment represents too large a percentage of the entire portfolio.

Fees. While the law doesn't specify a permissible level of fees, it does require fees charged to a plan be "reasonable." Business owners should monitor their plan's investment fees and expenses to determine if they are reasonable. For example, your investment management costs should not exceed one percent of plan assets annually.

Monitor your manager. A business owner should establish and follow a regularly scheduled formal review process to assess the quality of their plan's investment management and, if necessary, consider replacement. When monitoring an investment manager, it's important to review the manager's performance, read any reports they provide, check actual fees charged, ask about policies and practices (such as trading, investment turnover and proxy voting) and follow up on participant complaints.

If business owners follow these simple guidelines, they'll enjoy the truly wonderful benefits of retirement plan wealth building…and avoid the big liabilities.

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—REPRINT—
from November 2006
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