FINANCE

Photo by Bob Giglione

CHARLES MASSIMO: A new ruling makes companies responsible for monitoring their 401(k).

What's in your fund?

U.S. Supreme Court makes biz liable for 401(k) plans

BY CLAUDE SOLNIK

In a decision with far-reaching implications, the U.S. Supreme Court has ruled that companies must monitor the performance and fees of 401(k) plan investments.

The court in Tibble v. Edison in May concluded employers are required by law to monitor their 401(k) plans to make sure they're in employees' best interests.

While the decision doesn't make firms responsible if funds lose value, it means they must perform ongoing due diligence in deciding what to offer.

The court, in the suit against the Rosemead, Calif.-based utility, also determined employees can sue companies that fail to monitor plans with excessive fees and poor performance.

"The heart of it is fees but it's more than fees," said Charles Massimo, president and founder of CJM Wealth Management in Deer Park. "It also has to do with how well you monitor the funds in your plan."

While you might file the decision under "no good deed goes unpunished," the court says offering a plan isn't enough, even if it is a perk. Firms can't just launch plans and leave them on auto-pilot, as some do.

"Companies set up plans," said Michael Corkery, a partner at Melville accounting firm Nussbaum Yates Berg Klein & Wolpow. "Once they have it set up, it keeps moving forward year after year."

Many companies rely on 401(k) plan administrators to make and monitor the plan, thinking the firm – such as Fidelity – is responsible for doing the right thing. That can be a crucial error.

"Thousands of people work for those companies," Corkery said. "How do you know that that one person has your company's interest at heart or is achieving the goals for the employees?"

The ruling follows a 2011 U.S. Department of Labor decision mandating mutual fund fee disclosure that Massimo called an "important first step" in informing the public.

"When the Department of Labor reviews these, they can see and provide statistics," Corkery said of disclosure documents. "They can see the average fees paid."

Massimo said the 2011 ruling resulted in lawsuits, settlements and changes in 401(k) plans.

"It's already led to more suits from employees suing employers for having funds on their plan with fees that were never disclosed," Massimo said. "Fiduciaries who took the necessary action made changes to their plan. Those who are lazy or don't believe it's an issue have done nothing."

Steven Brett, president of Marcum Financial Services, with Long Island operations in Melville, said a firm that lacks "a proactive adviser or that has an absent adviser" runs the risk that the plan has not been "appropriately reviewed and hence prudent choices may not have been made."

"Some plans are more expensive and some are less expensive," Brett said. "It really comes down to what is reasonable given the services provided and given that the plan is reviewed on a regular basis."

It's important to understand what's considered customary and excessive charges to employees. Fees themselves aren't necessarily the problem.

"You're always paying a fee," Corkery continued. "To cover themselves, the trustees of the plan have to have a process to evaluate the plan fees."

Excessive fees can come in various forms, including additional charges that employers levy on plans.

Many fund managers offer what's known as an "institutional" and "retail" version of the same fund: the retail version charges higher fees and pays bigger commissions.

"It used to be that you had to be a bigger plan to have institutional shares available. Nowadays, every plan has institutional shares," Massimo said. "You can have the same fund, but the difference between the retail and institutional fund could be 1 percent."

Companies offering plans with retail rather than institutional versions could be found liable – even if it's the plan administrator, not the employer, who gets the fees.

"A vast majority are still offering retail versus institutional," Massimo continued. "A lot of people trust their adviser or broker to guide them appropriately. They're not necessarily getting the right direction."

The Supreme Court ruling comes after some firms settled suits charging they failed to look out for employee interests in 401(k) plans.

Minneapolis-based Ameriprise Financial agreed to pay $27.5 million and Bethesda, Md.-based Lockheed Martin settled for $62 million.

Columbus, Ohio-based insurer Nationwide; Boston-based 401(k) plan administrator Fidelity, Amsterdam-based bank ING and Memphis-based International Paper also settled.

"In most cases, the investment firm is released," Massimo said. "If you're not acting as a fiduciary, your only responsibility is to recommend something suitable, not necessarily in the best interest of the participant."

The latest decision is likely to lead to additional litigation, as employees and attorneys review plans and fees. Massimo said some law firms advertise, seeking employees who may face excessive fees.

"Anytime you have a law suit that's the first of its kind, you tend to have the snowball effect," Corkery said. "I think there's more potential for the lawsuit to change business practices for the better, because companies want to avoid litigation like this."

Massimo said firms and officers designated as fiduciaries for 401(k) plans need to have investment advisory committees or otherwise monitor and benchmark fees and performance.

"You should have a formal process in place," he said. "If they're performing poorly, find out why. As a fiduciary, you want a written process in place that you follow."

The Supreme Court decision also could lead companies, employees and accountants to look more closely at funds, which could benefit everyone.

"A company could see this and say they don't want to be subject to risks," Corkery said. "We don't have an investment committee in place. Let's put one in place and evaluate the plan's performance and the service provider."

Companies' financial advisers already are paying more attention to 401(k) plans, making sure they don't turn into a source of lawsuits.

"We do a significant amount of plan audits," Corkery said. "As we go through the internal controls of the plan, this is going to be a conversation piece for companies to beef up their processes."

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BRIEFS

NEFCU opens in Huntington Station

NEFCU, a Westbury-based credit union, has opened a branch in Huntington Station, its second in Suffolk County.

Located at 721 East Jericho Turnpike, the new branch is the latest expansion for NEFCU, which also operates 10 locations across Nassau County.

The 3,178-square-foot building features ATM service and video teller stations, as well as the standard consumer and business banking services.

– ERIC SANTIAGO

Schein sales edge up, hurt by strong dollar

Henry Schein, a global distributor of healthcare products and services, reported $117.9 million in second quarter income, up from $116.2 million a year ago.

The Melville-based firm, which jumped from 292 to 287 on the Fortune 500 list last month, reported $2.6 billion in sales, up 0.5 percent from a year ago.

CEO Stanley Bergman said revenues were "negatively impacted by the strength of the U.S. dollar against various foreign currencies, in particular the euro."

Sales included 7.5 percent growth in local currencies, almost entirely offset by a 7 percent decline related to foreign currency exchange rates.

Bergman added that "overall the global markets we serve were healthy during the quarter, and we believe we continued to gain market share."

– JAKUB LEWKOWICZ

Pall shareholders vote for sale to Danaher

Port Washington-based high-tech filter manufacturer Pall's shareholders have approved a sale to Danaher Corp., a global conglomerate that makes products in the environment and technology industries.

Investors who own approximately 82 percent of the company's shares voted in favor of the sale at a special shareholder meeting. The deal must first receive regulatory approvals in different jurisdictions.

If approved, each share will be converted to $127.20 in cash in accordance with a plan the company originally outlined in May.

– ERIC SANTIAGO

First of Long Island net rises

The First of Long Island, parent of The First National Bank of Long Island, reported second quarter net income jumped 13.2 percent to $6.3 million and announced plans to add branches.

The Glen Head-based bank said the jump was due primarily to a 13.1 percent or $2.1 million increase in net interest.

Net income for the first six months of the year rose 11 percent to $12.8 million, as net interest income increased by $3.9 million or 11.9 percent.

The bank, which has 41 branches, plans to open four more over the next 15 months.

– CLAUDE SOLNIK

LIFOCUS

Money market investments have fallen out out of favor

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Individuals living on the interest on investments like bonds and CDs have seen that income drop in recent years.

"A five-year CD may pay 2 to 2¼ percent interest per year, whereas in the past it would have been 4 to 5 percent," Montuori said. "If we sat with someone 10 years ago, we might have looked at a CD ladder. If the person had $100,000 to invest, we may have put in $20,000 per year for the five years. But as CDs mature, many investors are finding the interest rates unpalatable, and are looking to invest in stocks and other types of investments."

For someone with a million-dollar portfolio who needs $50,000 per year to live on, "you can't derive it from CDs in today's investment environment," Montuori added.

Money market investments, long a popular vehicle with the risk-averse, have also fallen out of favor.

"The money markets are very low today, motivating some people to take on more risk," said Craig Ferrantino, founder and principal of Craig James Financial Services in Melville. "They're handcuffed – they need the income. The bottom line is, if they're touching their principal to take out their income all the time, there's going to be a day of reckoning. You can calculate on the back of an envelope when some people are going to run out of money."

In addition to the continued low interest rate environment, the cost of living has gone up in recent years.

"A lot of people have to take more of their principal just to stay where they are," Ferrantino said.

Charles Massimo, president and founder of CJM Wealth Management in Deer Park, isn't a fan of fixed-income products like bonds.

"Bonds offer a fixed rate of return with no upside potential," he said. "Over any 20- or 30-year period, a diversified portfolio of equities will always outpace bonds."

Most savvy investors realize they can get a good return on a diversified portfolio of stocks just from the dividends, he said.

"With equities, not only do you get the dividend yield, but you get all the upside potential that comes with those equities – which will keep the portfolio lasting as long as possible," Massimo said. "Many of us are living as many years in retirement as we were working, and we can never lose focus on a portfolio's ability to grow. If you buy bonds instead of equities, you're exchanging one risk for another – the risk of potentially running out of money."

Dividend-paying stocks give investors steady income per quarter, Ferrantino said. But some companies that pay dividends are sensitive to interest rates, and if rates were to rise suddenly, the total value of the investment could decline, he said.

"The blanket advice is to look for well-established companies with a long track record of paying dividends," he said.

Besides high-quality stocks, Ferrantino points the risk-averse to high-quality, tax-free bonds.

"Ten-year U.S. Treasury bonds have a current interest rate of 2.33 percent, while New York State tax-free bonds are in the 3 percent range, going out 13 to 14 years, and with good quality," he added.

On the downside, "Some people look at it and say you're tying up your principal for 10 or more years, in case interest rates go up," he said.

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