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You're Being Sued, but It's Not Who You Think

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Shirley M. Mueller

Kelly is a nurse in a medium-sized medical group of 20 or so physicians in the Midwest. She likes her job and never thought she would be the instigator of a lawsuit against her own doctors. Nevertheless, when her employer changed pension plans several years ago and her 401(k) went south, things changed. Her accountant/lawyer husband prodded her into suing her own doctor group, although she was reluctant. Nevertheless, the evidence that her colleagues were working against Kelly's best interests in the employer pension plan was overwhelming.

This is why. The options that Kelly was offered included load funds with steep expenses. This means the funds she was required to choose had to outperform their index in order to keep up with the market, a feat almost no fund manager can sustain. Also, index funds were not offered in the pension plan.

Who Is to Blame?

At first, Kelly thought the brokerage firm that her employer had signed up with was the problem. Surely, her own doctors could not be at fault. But, her husband disagreed.

He explained to her, "Stockbrokers owe fiduciary duties only to their broker-dealers—not to their investment clients. Registered investment advisors owe fiduciary duties only to their investment clients because they don't have broker-dealers. However, when a broker-dealer has a dual registration as both a broker-dealer and a registered investment advisor, according to something called the Merrill Lynch Rule, the broker-dealer is not necessarily a fiduciary. In simple terms, your doctors are responsible for the choices in your plan, not the broker-dealer that advises and administers your plan." This was difficult for Kelly to believe. She asked her husband to confirm this. He took action and arranged a meeting with a vice president of the advising broker-dealer firm. This man told them flat out, "We are not fiduciaries for this plan."

This clarification left only one group standing to sue for the money Kelly had lost in her 401(k)—the executive committee of doctors who chose the pension plan. Kelly's colleagues joined her in the lawsuit. The physicians soon learned that their own personal net worth was at risk because they were charged with failing to fulfill their fiduciary responsibility to the 401(k)

plan. These physicians could be liable for considerable damages because the group had over 100 employees.

Cold Hard Facts

Kelly's husband told her that the physician group had not shown "stewardship" in directing the plan. Their fiduciary ignorance had generated revenues for the advisors, their firm, and the mutual funds recommended, but had not benefited the employees. Their hard-earned cash had too many hands dipped into it for their return to be any more than mediocre or worse.

Kelly and the other employees felt betrayed by their doctors. The physicians felt deceived by their pension advisors. Everyone wondered what went wrong. The doctors had a legal audit performed on their 401(k) plan. This dissection suggested several irregularities, but did not touch on the real problem—the fees charged to the plan participants.

Although this story is not documenting a specific event, it is a very likely scenario. Class action lawsuits are being filed mainly in Illinois, but elsewhere as well, alleging disturbing fee practices among 401(k) sponsors. The complaints charge that the "prudent man" standard has been violated by the fiduciaries' failure to control expenses in the plan.

W. Scott Simon makes the case for this line of thinking in a recent Morningstar Advisor.com article. Simon is an expert on the Uniform Prudent Investor Act and author of a book on the subject. The following is his argument:

- The funds or money managers recommended by the advisor have superior track records over a short period.
- The advisors promote this active management because it justifies their fees.
- An exceptional active management track record cannot be sustained. Thus, the high expenses are not justified.
- Since wasting beneficiaries' money is imprudent, this "chasing return" puts the fiduciaries of the plan at risk for lawsuits by their employees.

Steps to Be Taken

The easiest time to address the above issue is when you are changing advisors.

Dissecting the recommendations of an advisor can be discouraging and time consuming. They usually sugarcoat any suggestions they make, and physicians simply don't have the knowledge to refute their recommendations, which may be heavily weighted toward the advisor's own self-interest. A group can tackle this by hiring a specialist to do this for them. Some possibilities include:

- www.whitehorseadvisors.com. Provides services designed to enhance 401(k) performance and

maximize value.

- www.littler.com. National employment and labor law firm.

Alternatively, a physician group can hire a third party to take fiduciary responsibility. Some possibilities include:

- www.prudentllc.com. Invests, manages, and monitors money according to a prudent fiduciary process.
- www.erisa-fiduciary.com. Fiduciary audits, reviews, and money management.

Shirley M. Mueller, MD, dissects barriers to effective monetary decisions so they become manageable. Her unique training and experience as a practicing physician board certified in neurology and psychiatry, combined with her 7-year investment advisor career, contribute to her expertise. She welcomes questions and comments at MyMoneyMD@aol.com.

Web's Worth: For more information, visit the following sites:

- [www.prudentllc.com/download/Scott 5-25-05.pdf](http://www.prudentllc.com/download/Scott%205-25-05.pdf). Article by W. Scott Simon from MorningstarAdvisor.com, May 25, 2005.
- www.401khelpcenter.com. For plan sponsors, retirement professionals, and small business and plan participants.
- www.sec.gov/investor/pubs/sponsortips.htm. Ten questions to ask your advisor.
- <http://boss.streamos.com/wmedia/edwork/fc/fc030607.wvx>. View government hearing on pension plans.
- [www.sec.gov/answers/401\(k\).htm](http://www.sec.gov/answers/401(k).htm). 401(k) questions and complaints.