"Now You See Me", the fiduciary version produced by the DOL

- DOL's Fiduciary Standards have not changed the rules. They've sharpened the teeth of enforcement.
- The plaintiff's bar is poised for the next big scandal and I believe one such scandal will be in target date funds
- Good faith, or so-called "empty head and good heart," is not enough.

The DOL's Fiduciary Standards have not changed the rules. They've sharpened the teeth of enforcement by removing the cloak of invisibility called the "suitability standard," and by wetting the appetites of class action attorneys. It's the fiduciary version of the hit movie "***Now You See Me***", a film about magic with a Robin Hood undertone. Most importantly, beneficiaries and their attorneys have a clearer vision of just who is a fiduciary, and what these fiduciaries are obligated to do. Consequently the plaintiff's bar is poised for the next big scandal and I believe one such scandal will be in target date funds, the $Trillion industry that has sprung up in the past decade in 401(k) plans.

The Duty of Care

Fiduciaries, namely plan sponsors and their advisors, routinely violate the Duty of Care in their selection of TDFs and this mistake will prove catastrophic to beneficiaries sometime in the not-too-distant future, leading to successful lawsuits. It's unfortunate that it will take lawsuits to remedy this breach, but that's how the system works. For example, the current focus on lowering 401(k) fees has been generated by successful lawsuits. No one cared before these lawyers won.

The Duty of Care is the heart of the DOL's "Best Interest Standard." Fiduciaries have the obligation to try to do their best on behalf of their beneficiaries. It's like our duty to protect our young – a moral imperative as well as the law. Fiduciaries don't actually have to choose the best, but they do need to try. Good faith, or so-called "empty head

and good heart," is not enough. In the case of TDFs, fiduciaries can't throw darts at the QDIA (Qualified Default Investment Alternative) dartboard, as some believe. Investing in "Safe Harbors" does not relieve a fiduciary of the Duty of Care.

Unsafe Harbors

Fiduciaries generally believe that they are protected from litigation by two safe harbors in their selection of target date funds:

1. Properly structured TDFs are Qualified Default Investment Alternatives (QDIAs) under the Pension Protection Act of 2006. Form over substance.
2. There is safety in numbers, so choosing one of the most popular TDF providers is prudent. Fidelity, T. Rowe Price and Vanguard manage 65% of the blossoming TDF market. You can't go wrong with a brand name. Or can you?

There's more to selecting TDFs than these two simple rules. Specifically, not vetting your TDF selection is a breach of fiduciary duty that will bring lawsuits (loss-suits) when we experience the next 2008. Most TDFs, including the Big 3, are ticking time bombs because they are too risky at the target date.

Fiduciaries are exposed to lawsuits because they are obligated to actually vet their TDF selections and to establish objectives that are truly in the best interests of participants. Fiduciaries are duty bound to seek solutions rather than settling for high-risk products that are oblivious to history. Ignoring the past (especially 2008) and hoping it's different the next time is not an option, and it's certainly not an enlightened view of risk management.

Consequences

Contrary to popular participant need and belief, TDFs do not protect the vulnerable from loss. They sure didn't in 2008, and risk has actually increased since then. Most participants in TDFs are defaulted into this product, which means that most participants rely upon their employers to do the right thing by protecting savings, especially near retirement. There was only about $200 billion in TDFs in 2008. With more than a $trillion today, the next correction will be much more devastating, and there will a much louder public outcry than the 2008 version.