Contracting Thoughts from the Unconflicted Employer Side:

How to Protect Yourself—and Stay Protected— when Negotiating with Vendors

The first of a series of candid bulletins written for employers by a firm that represents employers

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Employers often assume that their third-party vendors act in their plans' best interests when contracting for services. In reality, benefit plan vendors increasingly take great pains to limit their liability and transfer risk to plan sponsors, in-house fiduciaries and plan participants (referenced together as "Plans"). We explain below how Plans can and should push back against these efforts, with specific and actionable suggestions.

More than $20 trillion are invested in U.S. employee benefit retirement plans. Health and welfare plan costs also continue to grow: U.S. employers in 2020 contributed $6,227 per employee in health insurance premiums for single coverage and $15,754 per employee for family coverage. Plans are subject to heightened scrutiny by the Internal Revenue Service, Department of Labor and an active plaintiff bar. Plan sponsors, inhouse fiduciaries and third-party vendors can suffer judgments and penalties that can reach tens of millions of dollars. In this environment, the interests of benefit plan vendors are often adverse to those of Plans. Often, this is reflected in aggressive pro-vendor contract terms as well as negotiation processes and strategies designed to limit the opportunity for Plans to negotiate effectively. Failure to recognize this fact can expose Plans—including fiduciaries individually—to financial and legal risk.

Ivins, Phillips & Barker has negotiated thousands of employee benefit contracts, exclusively representing plan sponsors and inhouse fiduciaries. The firm has made a conscious decision not to represent third-party vendors in the ordinary course to avoid even the appearance of conflict.

As a result, we are uniquely positioned to zealously assist Plans in negotiating the best possible arrangements and to protect employers, fiduciary committees and plan participants.

In this first bulletin, we offer simple but important strategies to maintain negotiating leverage.

Timing Original Negotiations

Plans greatly increase their leverage and reduce the time spent in negotiations by kicking off the negotiation process at the outset of the vendor search and evaluation process. Conversely, vendors regularly attempt to put off the contract negotiation until the work is awarded and, often, until implementation has started and material costs are being incurred. Simply put, the earlier in the process that contract terms and conditions are negotiated, the more cooperative vendors are.

The single most impactful way to strengthen a Plan's negotiating hand is to require prospective vendors to provide markups to the Plan's model agreements or selected terms and conditions before the vendor selection. Procurement consultants regularly do exactly this with respect to pricing terms and conditions. Our suggestion is to do the same with respect to data security, limitations on liability, indemnity and other key terms and conditions or possibly the entire agreement.

Properly Setting Up Renewals/Future Changes

The same leverage concerns that apply to the original contract negotiation apply equally to renewals and contract amendments. This fact is not lost upon vendors, and we have seen a number of vendor strategies that Plans should recognize and avoid. Increasingly common examples include:

- ***Express Reservation of Unilateral Right to Make Changes***: Third party administrators, pharmacy benefit managers, brokers, consultants, and others are increasingly reserving the right to make future contract changes unilaterally. Fees are the most common focus, but such rights often extend to changes necessary to maintain legal compliance or avoid fiduciary status, or more broadly.

  Sometimes the unilateral change right is conditioned on future facts, such as a change in the eligible participant count, but even those conditions are often broad or poorly defined and leave a large degree of discretion to the service provider. Once the unilateral change right is triggered, the vendor's resulting amendment right may extend beyond the triggering event unless the scope of that right is carefully negotiated.

We advise Plans to push back on these provisions. Most vendors will agree to condition all such changes on mutual consent, significantly narrow the circumstances in which unilateral change is permitted and/or limit the degree of permitted change.

- ***Unexpected Unilateral Amendments***: Certain vendors are trying to accomplish contract changes by submitting purported amendments that require no Plan consent. The amendment is submitted with a cover email or letter that asserts that the amendment changes will be effective unless the client recipient formally objects within a limited timeframe (typically 30 or 60 days). Several health and welfare third party administrators have been doing this for a few years. More recently, a couple of the largest 401(k) and other retirement plan recordkeepers have begun doing the same thing. The fact that the original contract conditions amendments upon a writing signed by both parties hasn't prevented certain vendors from asserting unilateral amendments. We advise Plans to establish a process by which any such purported unilateral amendment prompts a firm and automatic rejection as to both the specific amendment and the attempted change to the mutually agreed and documented amendment process.

- ***Asynchronous Renewal Rules***: Vendors across the benefits spectrum are increasingly structuring their template contracts to back Plans into corners by proposing asynchronous renewal provisions. As one example, many vendor template contracts require the Plan to give official notice of non-renewal at least X days prior to the renewal date. Not coincidentally, the template allows the vendor to make fee or other contractual changes upon notice that can be given less than X days prior to the renewal date. A Plan that agrees to such terms will be contractually committed to an extended renewal before it has the right to know the fees and other renewal terms.

Many plan sponsors and fiduciaries find themselves, for a variety of reasons, in vendor relationships with contracts containing sub-optimal terms. Even in such cases, a deliberate strategy can be employed to increase negotiating leverage, better position the company and plans for future negotiations, and improve the contractual position.

We intend to publish further bulletins with respect to benefits contracting. To sign up for such bulletins or for further information or support, please contact Steve Witmer at switmer@ipbtax.com or 202.662.3442, Percy Lee at plee@ipbtax.com at 202.662.3458, or your regular IPB contact. We would welcome the opportunity to discuss contracting strategies and opportunities with you.
