

FA PLAYBOOK

Why employers may not be so quick to jump on the 401(k) bitcoin bandwagon

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KEY POINTS

- Fidelity Investments, the largest 401(k) administrator, said Tuesday it's offering a bitcoin investment to workplace retirement plans.
- Employers have legal duties to ensure their 401(k) investments are prudent. The U.S. Department of Labor said in March that it has concerns about the wisdom of crypto in retirement plans.
- Businesses should undergo and document a thorough vetting process before offering crypto in retirement plans.

Fidelity Investments is offering bitcoin to 401(k) investors. But before retirement savers get access, employers must give the green light — and that's often much more complicated than it sounds.

Fidelity administered almost \$2.9 trillion of 401(k) and other workplace retirement plan assets (representing over a quarter of the market) at the end of 2020, according to Cerulli Associates, serving 26 million investors in roughly 34,000 plans.

The firm said Tuesday it would let employers adopt a new Fidelity-developed bitcoin fund (the Digital Assets Account) as a main 401(k) investment choice, alongside other core investments such as stock, bond and target-date funds. Administrators hadn't previously allowed this.

MicroStrategy, a publicly traded analytics firm, will be the first business to offer the cryptocurrency investment in its 401(k) plan sometime this year. Fidelity is

also “having a lot of discussions” with other employers about adding the bitcoin fund, according to Dave Gray, Fidelity’s head of workplace retirement platforms and offerings.

Here’s the challenge for businesses: They have a rigorous legal obligation when it comes to selecting and overseeing 401(k) investments available to workers. This vetting process governs all 401(k) investments, but most employers aren’t aware these duties exist, say financial advisors.

There are many factors to weigh aside from employee demand — and making a misstep might mean an investor lawsuit down the road, especially given crypto’s volatility, financial advisors said.

“You sponsor a retirement plan, you’re responsible for outcomes,” said Ellen Lander, founder of Renaissance Benefit Advisors Group, based in New York. “Yes, participants make their own decisions, but you’ve made the decision for what to give them.”

Things to consider

The Employee Retirement Income Security Act of 1974 sets legal standards for employers sponsoring 401(k) plans. They operate as “fiduciaries” who must act prudently and with a duty of loyalty to plan participants.

A company CEO’s personal beliefs as to whether crypto is a “good” or “bad” investment doesn’t have a bearing on the business’ fiduciary duty to investors, advisors said. And employers can’t offer an investment solely because employees are clamoring for it.

For example, employers must consider factors such as risk, return, cost and diversification benefits, and whether an investment is in the best interests of the collective workforce, advisors said. They must also monitor these and many other elements on an ongoing basis, too.

The U.S. Department of Labor recently cast doubt on whether plan sponsors can uphold those duties relative to cryptocurrency investments. In a compliance bulletin, the department urged employers to “exercise extreme care” before offering crypto to workers.

The Labor Department cites “significant risks,” such as speculation and volatility, to 401(k) investors; the department also asserts it will investigate plans that offer crypto and, if necessary, “take appropriate action” to protect investors.

“The DOL made it very clear it’s imprudent,” said Philip Chao, founder and chief investment officer of Experiential Wealth in Cabin John, Maryland, referring to offering crypto in 401(k) plans.

Fidelity, which was working on its bitcoin fund before the Labor Department published its memo, believes it structured its bitcoin fund in a way that addresses the agency’s criticisms.

For example, workers can’t choose to allocate more than 20% of their paycheck contributions or total 401(k) savings to the bitcoin fund. (Employers can opt for a lower cap.) Assets are valued daily, like a typical mutual fund. Fidelity provides education material for would-be investors. In addition, Fidelity keeps track of the private keys that have bedeviled other retail investors who’ve lost them, Gray said.

Further, employers — rather than the Labor Department — are the arbiters of their 401(k) investments, Gray added.

“The ultimate decision as to whether or not this digital asset account — or any other investment option — is prudent for a plan belongs to the plan sponsor fiduciary, the employer,” Gray said.

Eleven financial services and business trade groups sent a letter to the Labor Department on April 12 asking it to rescind the crypto notice. Among other things, the letter said there’s no legal basis for judging whether any investments are inherently appropriate or inappropriate.

Some 401(k) savers may already have access to crypto-related funds, like bitcoin futures exchange-traded funds, through a little-used mechanism called a “brokerage window.” (Unlike Fidelity’s offering, those funds buy futures contracts and don’t offer direct bitcoin ownership.) The brokerage window expands the universe of funds available to 401(k) investors, but those funds aren’t traditionally vetted by employers.

“ If you’re including crypto, are you able to document why you did that and all the reasons why you made the decisions to add it?

— Ellen Lander, FOUNDER OF RENAISSANCE BENEFIT ADVISORS GROUP

Some employers who’ve drafted an investment policy governing how they make 401(k) investment choices may be barred from immediately offering a fund like Fidelity’s, Lander said. Many such policies require funds to have existed at least three years before investing.

Employers considering adding a bitcoin fund to their main lineup of choices should also thoroughly document their decision-making process, advisors said.

“If you’re including crypto, are you able to document why you did that and all the reasons why you made the decisions to add it?” Lander asked. “If you answer those questions, you have the answers as to whether it makes sense.”

<https://www.cnbc.com/2022/04/26/why-employers-may-not-be-quick-to-jump-on-the-401k-bitcoin-bandwagon.html>