

CRYPTOCURRENCY AND 401K'S

Guidance on Cryptocurrency as an Investment Option in 401k's

We have received inquiries from participants recently regarding adding cryptocurrency as an investment option to their employer 401k. Cary Street Partners strongly recommends NOT adding based on the speculative nature of "crypto" and the fiduciary standards that guide employer retirement plans. Here is a summary of investment guidance from the Department of Labor published on March 10, 2022 (The DOL is the government agency that regulates 401ks). Notably the department did not mince their words and offered emphatically strong caution regarding the risk of cryptocurrency as a retirement investment option stating: "These investments present significant risks and challenges to participants' retirement accounts, including significant risks of fraud, theft, and loss."¹

FIDUCIARY CONSIDERATIONS

The DOL took a further step beyond highlighting the investment risks of cryptocurrency focused on the fiduciary responsibilities of plan advisors and administrators. "The plan fiduciaries responsible for overseeing such investment options or allowing such investments through brokerage windows should expect to be questioned about how they can square their actions with their duties of prudence and loyalty in light of the [following] risks described."¹

Under ERISA, fiduciaries (i.e. plan advisors and administrators) must act solely in the financial interests of plan participants and adhere to an exacting standard of professional care. Fiduciaries who breach those duties are personally liable for any losses to the plan resulting from that breach.

Our view at Cary Street Partners Retirement Services is that the investment currently does not have a place in 401k plans given the nature of cryptocurrencies and fiduciary standards. Investors who believe that cryptocurrency has a place in their investments may consider purchasing the investment outside of their employer 401k plan.

FIVE REASONS CRYPTOCURRENCY IS NOT SUITABLE FOR 401KS

- **Speculative and Volatile Investments:** Cryptocurrencies have been subject to extreme price volatility. There are also widely published incidents of theft and fraud.
- **The Challenge for Plan Participants to Make Informed Investment Decisions:** These investments easily attract investments from inexperienced plan participants with great expectations of high returns and little appreciation of the risks. Cryptocurrencies are very different from typical retirement plan investments, and it can be extraordinarily difficult, even for expert investors, to evaluate these assets.
- **Custodial and Recordkeeping Concerns:** Cryptocurrencies are not held like traditional plan assets in trust or custodial accounts, that are readily valued and available to pay benefits and plan expenses. Instead, they generally exist as lines of computer code in a digital wallet. With some cryptocurrencies, simply losing or forgetting a password can result in the loss of the asset forever.
- **Valuation Concerns:** Experts have described the question of how to appropriately value cryptocurrencies as complex and challenging, noting that none of the proposed models for valuing cryptocurrencies are as sound or academically defensible as traditional discounted cash flow analysis for equities or interest and credit models for debt.
- **Evolving Regulatory Environment:** Some market participants may be operating outside of existing regulatory frameworks. The Financial Industry Regulatory Authority (FINRA) has cautioned, Bitcoin and other cryptocurrencies have "... been used in illegal activity, including drug dealing, money laundering, and other forms of illegal commerce. Abuses could impact consumers and speculators; for instance, law enforcement agencies could shut down or restrict the use of platforms and exchanges, limiting or shutting off the ability to use or trade bitcoins."²

MAKE SMART DECISIONS ABOUT YOUR RETIREMENT



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¹ US Department of Labor, Compliance Assistance Release No. 2022-11: 401(k) Plan Investments in "Cryptocurrencies" March 10, 2022

² US Department of Treasury, Virtual Currency Guidance Brochure www.treasury.gov

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