401(k) Issues That Could Use Some More Guidance From The Government

By Ary Rosenbaum, Esq.

The reason I continued being an ERISA attorney after my first job was that I enjoyed the subject matter and I enjoyed the definiteness that other areas of the law don't have, such as litigation. However, there are areas of the retirement plan space that aren't so clear. They're cloudy and until the Internal Revenue Service (IRS) or the Department of Labor (DOL) clears things up, 401(k) plan sponsor like you, need to understand.

The liability of self-directed brokerage accounts

I used to joke that the only employers that allowed self-directed brokerage accounts were medical practices, law firms, and accounting firms. The only problem is that for the most part, the joke is reality. I have never been a fan of 401(k) plans offering participants the ability to invest within their self-directed brokerage (SDBA) option. First off, studies have shown that participants that invest within an SDBA do worse than plan participants who direct their investments within the plan's core fund lineup. In addition, it's never been clear whether plan sponsors are truly protected from liability from losses sustained by participants through the SDBA. While common sense would suggest that participants are liable for their losses through the SDBA since it's their choice to have one, there is nothing definite from the IRS and DOL that states that. As a plan sponsor, you're a plan fiduciary, and you are a fiduciary for all the assets in your 401(k) plan. You would be responsible for looking at what participants are doing within the SDBA window, but there is nothing out there that suggests you're free from liability for what participants do. If a participant wants to invest 100% in a double inverse Chinese market exchange-traded fund or 100% in shares in AMC Theaters, are you going to be held harmless? As an ERISA attorney, I don't want to find out for my clients that offer them. Are you supposed to educate plan participants about the dangers of investing in specific stocks and how a core fund lineup has risk and likely higher returns? I don't know. Until there is something definitive from the government, I'm still going to have my doubts about the appropriateness of an SDBA.

Allowing crypto brokerage accounts

In addition to SDBA windows, a couple of plan providers are now offering the ability for plan participants to invest in Bitcoin. These windows will allow participants to likely invest up to 5% of their account balance in Bitcoin. I'm sure these plan providers came up with offering a self-directed Bitcoin option when it was $69,000 a coin and came to the market when the coin was down to about $20,000 a coin. Timing is everything and Bitcoin as I write, is hovering around $17,000 a coin. So the timing for bringing this to market isn't great. Bitcoin is highly volatile, it has wide swings over time. In addition, Bitcoin is not regulated. Why would you offer an unregulated investment within such a heavily regulated 401(k) plan? There is also a question about cybertheft. A crypto wallet is easier to steal from, than a trust account at a well-known custodian of assets. As the FTX scandal sorts itself out, having a crypto wallet at a questionable crypto provider is another worry. The DOL released a compliance bulletin that cautioned fiduciaries from offering crypto investments. The compliance bulletin suggests that the DOL might audit plans that offer a crypto brokerage window. The compliance bulletin offers a lot of DOL's reasoning for why crypto investments are a bad idea, right now. While my

reasoning is within the DOL's boat of logic, it still doesn't mean that Bitcoin is banned as an investment option because a compliance bulletin doesn't have the weight of a regulation. The DOL is being sued over the issuance of this compliance bulletin, so the courts will weigh on whether the DOL has the right to issue those fiduciary cautions in that bulletin. In addition, the DOL may change its thinking over crypto investments if these investments come under some regulation and/or lose their pricing volatility. As someone who invests in Bitcoin in private investments, but thinks that it's a bad bet for 401(k) plans, I don't like some more guidance from the DOL to stomp out that silly notion of allowing crypto 401(k) investments.

Pooled plan providers and the prohibited transaction rules

Pooled Employer Plans (PEPs) are a 401(k) plan that allows unrelated businesses to participate in one plan managed by a pooled plan provider (PPP). They were added to the law in 2020 and became effective on January 1, 2021. Thanks to the COVID pandemic and the quickness of its implementation, the DOL was a little slow to develop regulations concerning PEPs. The registration form for PPPs only came into effect 5 weeks before PEPs became effective. One of the ways where it's cloudy for PEPs are the prohibited transaction rules and whether it applies to PPPs. Prohibited transactions generally include the following transactions: a disqualified person's transfer of plan income or assets to, or use of them by, or for his or her benefit or a fiduciary's act by which he or she deals with plan income or assets in his or her interest. The DOL has asked for comments for a prohibited transaction exemption for PPPs back in 2020, but no guidance since. Can a PPP also be the third-party administrator (TPA) or financial advisor for the very same plan? Will there ever be a chance that they could fire themselves as the other plan provider? It's one of those things where I don't know the answer, but I would assume the DOL would give some leeway for plan providers to wear the PPP hat.

The deconversion fee and other fee disputes

Everything with a plan provider usually goes well until you fire them. When you fire a plan provider, that is when you see the knives come out. When I mean plan providers, I mean TPAs because they are the most important plan provider. In addition, the TPA seems to be the only plan provider to charge a deconversion fee, which is when their services are terminated by the plan sponsor. While I don't understand the need for a deconversion fee, this has become an accepted part of the retirement plan business. The problems are usually that the TPA never cites what the deconversion fee will be. They just cite they may be entitled to one, some TPAs are silent about it. While all fees are now required to be fully disclosed as to what the TPA charges to the plan, there is no requirement for termination and deconversion fees to be disclosed since they're only applicable when the TPA is fired. While most TPAs will charge a reasonable fee for deconversion, there are some TPAs who take their firing as personal, so they will squeeze as much from the plan sponsor as they think they can get away with it. If the plan sponsor protests the deconversion fee, these TPAs will have the plan sponsor over a barrel since they can refuse to cooperate with the successor TPA. In addition, firing a TPA could lead to another billing dispute that I experienced firsthand as a plan sponsor. If you terminate a TPA as of December 31, 2022, and you have paid them on an annual basis, there may be a dispute as to who will do the Form 5500 and valuation for that 2022 plan year since the work must be completed by July 31 or October 15th of 2023. My plan paid for the 2020 Plan Year and all the compliance part of it, yet the TPA that I fired, said they wouldn't complete the 2020 work since it would happen in 2021. They tried to stick my plan with $80,000 in fees, despite making over $150,000 in 2020 fees. An industry leader told me that most fee disputes with a TPA deal with termination/ deconversion fees. I'm still awaiting word from the DOL investigation against the TPA that tried to rip off my plan participants. I expect that this issue will eventually need some DOL intervention since I believe it's an abuse that no one talks about.

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