The Trouble with 401(k) Investment Policies

Labor & Employment Law Update

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If I had a dollar for every time this conversation occurred…

Lawyer: Do you have a copy of your investment policy?

Client: Who would have been the one to write that? Us? Our broker/advisor?

Or, this one…

Lawyer: Is your investment advisor serving as a fiduciary to your plan?

Client: What does that mean? How would I determine that?

The most common area in which 401(k) plans are being scrutinized these days is in their selection and design of investment offerings. While participants often get to direct how their funds are invested, that direction is limited to only those investment offerings that an employer/sponsor makes available as part of the 401(k) plan.

Employers typically rely on investment advisors to help design the options available to participants. In some cases, options are limited depending on the total dollars invested in the plan. In many cases, the investment advisor provides the employer with a model investment selection policy to customize and adopt.

While a model policy is a helpful starting place, in many cases the employer, not quite sure what to do with it, never customizes the model policy and instead sticks it away in a file. The policy is then often forgotten and not reviewed or even referenced each time investment offerings are scrutinized. It is impossible to ensure the selection and design of the investment offerings is in line with the policy if the policy has been completely forgotten.

Every employer that offers a 401(k) plan should ask themselves the following:

1. What fiduciary status does the plan's investment advisor maintain? (i.e., who really has the final say on investment option design and selection for the plan?); and
2. What is our 401(k) investment policy and what are we doing to make sure it's understood and being followed by decision-makers for the plan?

An employer that can't answer these questions is not only vulnerable to potential litigation, but also risks the potential of not maximizing the invested assets of all participants.

In most cases with a 401(k) plan, an employer is supposed to serve as a trusted fiduciary maintaining a multi-million dollar investment portfolio on behalf of their employees. With that much at stake, an employer needs to make sure it is selecting and monitoring investments, along with a skilled investment advisor, carefully and diligently.