Private Equity and Crypto Rejoice

September 16, 2025

The Department of Labor appears to be giving a bright green light to private equity investments and crypto options in our nation's 401(k) plans. Both industries have long salivated at the idea of gaining access to the trillions of retirement plan assets, but there was always a tricky barrier: the rules of the Employee Retirement Income Security Act, more commonly known as ERISA.

You can get an idea of what ERISA requires from the people who manage defined contribution plans on behalf of employee participants from the original 2020 Department of Labor memorandum about these investments that live on the fringe of respectability. It read, in part, that the plans were free to include private equity as an investment alternative in the plan, so long as the inclusion was made "solely in the interest of the plan's participants and beneficiaries, and with the care, skill, prudence and diligence …that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."

The question always was: would a prudent person offer unsophisticated employees an 'opportunity' to invest in a pool of money which has not yet told its investors where it is going to deploy said money, whose fees are somewhat opaque and outrageously higher than an index-hugging ETF, and which would only be seeking money from the plan if it couldn't raise the capital it needed from more sophisticated wealthy investors who passed on the opportunity?

In 2021, the DOL added that private equity investments tend to be more complicated than more traditional ones, and that some of the fiduciaries governing these plans might lack the necessary expertise to properly evaluate them.

Whoa! This (seemingly reasonable) assessment was met with shock and horror by the Wall Street and Silicon Valley dealmakers who are buying up companies using other peoples' money, hoping to win quick profit. The White House got involved, sending a directive to the DOL, which removed the 2021 guidance with extreme prejudice, saying that it would have "a chilling effect on the market," and that it "took a dismissive view of alternative assets and the capabilities of plan fiduciaries."

The new directive also opened up crypto (another 'alternative asset') as another possible 401(k) investment option, provided it was done prudently. People are, of course, entitled to exchange real dollars for spooky assets housed in computer circuitry using the Coinbase exchange or others—on their own. But it's helpful to remember that bitcoin, the most stable of the thousands of coins on the market currently, has been anywhere from 3.8 times to 10 times as volatile as the S&P 500—and very few prudent investors would recommend a retirement allocation exclusively in the index.

Sources:

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