

---

October 24, 2016

AGENDA ITEM 05  
INFORMATION ITEM

CALIFORNIA SECURE CHOICE RETIREMENT SAVINGS INVESTMENT BOARD

*Summary of U.S. Department of Labor Rule Regarding State Savings Arrangements Established by States for Non-Governmental Employees*

---

***Summary***

The Employee Benefits Security Administration (“EBSA”), under the U.S. Department of Labor (“DOL”), developed a rule describing circumstances in which savings arrangements established by states for non-governmental employees can operate without being considered an employee benefit plan subject to the Employee Retirement Income Security Act (“ERISA”). The rule was developed to clarify how state retirement savings plans like the California Secure Choice Retirement Savings Program (“Program” or “Secure Choice”) could operate under federal law. The final rule was [published in the Federal Register](#) August 30, 2016. The rule is set to become effective October 31, 2016.

EBSA first published a notice of proposed rulemaking in the federal register November 18, 2015. The California Secure Choice Retirement Savings Investment Board (Board) provided [public comment](#) to the EBSA January 12, 2016. Additionally, the Board joined three other states seeking to implement retirement savings programs for private-sector workers in providing [public comment](#) January 19, 2016. While the final rule does not incorporate all suggestions made via public comment by the Board, it provides a clear guidance for implementation and operation of Secure Choice.

The content of the final rule generally conforms to the provisions in the proposed rule. The final rule mostly provides states greater flexibility than the proposed rule and makes some clarifying adjustments. Notable conditions in the final rule include the following:

- To the extent employees will be automatically enrolled in the Program—with the right to opt-out—employer participation in the Program must be required by state law to avoid ERISA preemption [§2510.3-2(h)(1)(ix)]
- Removes a condition included in the proposed rule prohibiting state-established savings plans from imposing any restrictions on employee withdrawals from their individual retirement accounts (IRAs).
- Provides additional clarity asserting a state’s right to take actions in addition to or different from those clearly outlined in the rule [§2510.3-2]

Further analysis of the provisions in the final rule is included below as they relate to employers, employees and administration.

## **EMPLOYERS**

*Participation:* Only those employers who fall under the state mandate will be exempt from ERISA. Employers not subject to the mandate, can participate in Secure Choice voluntarily, but would be subject to ERISA if their employees were automatically enrolled. However, if employees are required to affirmatively choose to participate, then the employer would fall under the existing safe harbor.

*Employer involvement must be limited:* The employer's role in the Program must be limited to ministerial activities such as collecting payroll deduction and remitting them to the Program. The employer may also provide information from the Program to the employees and may provide information to the state necessary for the Program's operation.

*Identification of eligible employers subject to the mandate:* The final rule confirms states have authority to define employers and employees subject to the mandate.

*Changes in employer size:* The final rule leaves it up to the states to determine how it handles the issue of mandated employers who at some point, after the Program is implemented, fall below the required number of employees. For example, a state could require an employer that ceases to meet the requirement to remain subject the mandate for a specified period of time, or just require them to maintain the payroll deduction for those employees already enrolled.

An employer that ceases to be subject to the mandate, could continue to facilitate employee deductions to Secure Choice without being subject to ERISA so long as they do not automatically enroll employees into the Program.

*Employer contributions:* Employers are not permitted to contribute to an employee's account.

*State reimbursement of employer costs:* The final rule modifies a provision included in the proposed rule providing conditions for a state-provided reimbursement, such as a tax incentive, for participating employers. The provision was intended to avoid the creation of an economic incentive for employers with plans to drop those plans in favor of the state plan. The final rule provides states more flexibility in providing employer reimbursement of its expenses as long as the economic incentives provided are narrowly tailored to reimburse employers for their actual costs due to enrollment in the Program.

## **EMPLOYEES**

*Employee participation must be voluntary:* Employees covered by automatic enrollment must be provided adequate advanced notice and has the right to opt-out.

*Withdrawal limitations:* The proposed rule released in November 2015 prohibited state savings plans like Secure Choice from imposing any restrictions on employee withdrawals from their Individual Retirement Accounts ("IRAs"). The final rule removes this prohibition giving state plans more flexibility to prevent the use of pre-retirement account withdrawals—otherwise known as 'leakage'—from participant accounts. For example, Secure Choice could consider requiring its participants to wait until a specified age before they can withdraw funds from their Secure Choice account unless they met certain conditions for a hardship withdrawal.

Another reason given by EBSA for removing the prohibition is it would have effectively interfered with a state's ability to offer lifetime income options or investment products with a guaranteed return, such as annuities or other insurance products.

*Consumer protections:* The safe harbor is conditioned on the state's use of IRA's as defined in the existing code which are subject to consumer protections such as prohibitions against fiduciary self-dealing and disallowing categories of conduct between plans and disqualified persons. The regulations also state that the state "must assume responsibility for the security of the payroll deductions..." This condition is satisfied if states have existing wage withholding and theft laws as well as enforcement programs to protect employees from wage theft.

*Employee notification of their rights:* The states must adopt measures to ensure that employees are notified of their rights under the Program and must create a mechanism for enforcing those rights.

## **ADMINISTRATION**

*Ability of governmental agencies and instrumentalities to implement and administer state programs:* The final rule clarifies that a state may delegate a wide array of authorities to a board, committee, department, authority, or other similar governmental agency or instrumentality of the state to implement and operate a state savings plan.

*Ability to experiment:* The final rule includes a provision not initially included in the proposed rule clarifying that states are not prohibited from taking additional or different action from those explicitly prescribed by the safe harbor. While the safe harbor provides certainty about how a state savings program could operate in a way that avoids being considered an ERISA pension plan, the final rule clarifies that aspects of state savings programs not explicitly identified in the safe harbor may not cause the Program to be covered by ERISA.