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DOL Encourages State-Run Retirement Programs

Following the Obama Administration's directive, DOL issued guidance on the application of ERISA to state-run retirement savings programs. A proposed safe harbor describes state-required automatic IRA programs that could avoid ERISA coverage, and an interpretative bulletin articulates DOL's views on other state programs that would be considered ERISA plans. While this guidance is designed to expand access to retirement savings for employees whose private sector employers do not sponsor a retirement plan, it may also be relevant to employers sponsoring plans that do not permit participation by their entire workforce. Comments on the proposed rule are due on January 19, 2016.

Background

Expanding access to retirement savings has been a longstanding goal of the Obama administration, which estimates that approximately 68 million Americans lack access to an employer-based retirement savings program. (See our February 28, 2014 and January 31, 2014 *Legislate* publications for a description of President Obama's auto-IRA proposal and "myRA" savings initiative.)

Meanwhile, this access concern has led some states to enact or consider enacting savings programs. Under the "auto-IRA" approach, now law in California, Illinois, and Oregon, the state establishes a payroll savings program and employers deduct amounts selected by employees from their paychecks to remit to state-administered IRAs. Washington State, for its part, has adopted a marketplace approach where a state program connects small employers of fewer than 100 employees with private sector savings plan providers. And a Massachusetts law enables certain nonprofit organizations with fewer than 20 employees to adopt a prototype plan developed and administered by the state.

According to the Obama administration, the prospect of ERISA preemption has deterred the development, and called into question the viability, of these and other state-run retirement initiatives. As such, at the White

What is ERISA preemption and why does it matter?

ERISA's preemption provision declares that (with some important exceptions) ERISA supersedes state laws that "relate to any employee benefit plan." Additionally, courts have held that state and local laws that "conflict with" ERISA's substantive provisions are preempted — meaning, invalid. For employers operating in more than one state, or with employees residing in more than one state, ERISA preemption permits streamlined administration of ERISA-governed retirement savings plans.

House Conference on Aging in July 2015, President Obama directed DOL to issue guidance supporting state efforts to broaden retirement access, consistent with federal law.

Guidance Supports State-Based Programs

On November 18, 2015, the DOL issued a proposed rule along with an interpretive bulletin (IB) aimed at facilitating state-based retirement programs. A fact sheet and news release accompanied this guidance.

Proposed Safe Harbor Regulation

Designed to give states a roadmap to avoid the application of ERISA, the proposed regulation sets forth circumstances where a state-required payroll deduction savings program would not give rise to an ERISA plan.

Specifically, to meet the safe harbor's requirements, the state must:

- Establish and administer the program under state law, and require certain private sector employers to participate
- Be responsible for investing employee savings, or selecting investment options from which employees can choose — and for the security of payroll deductions and employee savings
- Create and enforce employee notice requirements about participant rights under the program

Participation in the program must be voluntary for employees, meaning that they can opt out of participating. They must also be able to withdraw any portion of their contributions or earnings under Code rules applicable to IRAs generally, without any additional costs or penalties. Rights under the program must be enforceable only by the employee, former employee, or beneficiary (or their authorized representative), or the state.

Roadmap to Avoid ERISA

The safe harbor addresses the concern that payroll deduction programs similar to those enacted in California, Oregon and Illinois could cause employers to inadvertently establish ERISA-covered plans, and thereby become subject to ERISA's many statutory and regulatory requirements.

The employer's involvement in the program must be limited. The employer must not contribute funds to the program, or offer a bonus or other incentive to employees in exchange for participation. Additionally, the employer cannot have discretionary authority, control, or responsibility for the program, or receive any payments in connection with the program — other than reimbursement for their actual costs. The employer can, however:

- Collect employee contributions through payroll deductions and remit them to the program
- Notify employees and maintain records about collection and remittance of payments
- Provide the state with information needed for the program
- Distribute program information from the state to employees, and allow the state to publicize the program to employees

The DOL designed the safe harbor to support a court finding that ERISA does not preempt such state programs. However, as DOL Secretary Thomas E. Perez acknowledged, this result is not guaranteed because courts may disagree with DOL's conclusion.

Comment. The safe harbor could minimize the risk of ERISA preemption if the court reviewing a state-required automatic IRA program defers to DOL's views on this topic.

Interpretive Bulletin on State-Based Programs Covered by ERISA

In IB 2015-2, DOL articulated its view that ERISA preemption is not an "insurmountable obstacle" to certain state programs designed to facilitate ERISA-governed voluntary retirement savings sponsored by private sector employers. While recognizing the absence of legal authority directly on point, the IB points to the following approaches DOL believes states could implement consistent with ERISA's rules, protections and remedies:

State-run marketplaces. Akin to the Washington state law referred to above, the state connects employers with providers of quality products that are suitable to small employers and charge low fees. Participation in the marketplace is voluntary for employers, and is not itself designed to be an ERISA-covered plan. However, products available through the marketplace can include both ERISA and non-ERISA plans. ERISA requirements would apply only to the ERISA plans and not to arrangements like payroll deduction IRA programs that are otherwise exempt form ERISA coverage.

State-administered prototype plans. The state creates and administers prototype plans like those currently available in the private sector, where an individual employer selects particular plan features. An example of this approach is the Massachusetts law that allows nonprofit entities with fewer than 20 employees to adopt a contributory retirement plan developed and administered by the state. Under this model, the employer adopts the prototype plan, serves as plan sponsor, and assumes ERISA fiduciary duties. However, the plan documents could allow the employer to delegate certain fiduciary and administrative duties to other entities, or the documents themselves could designate the state to perform these duties — and then the state or a designated third party could handle most administrative and asset management functions.

State MEPs. The state sets up a multiple employer plan (MEP), which certain employers could join by executing a participation agreement. The MEP would be considered a single ERISA plan, with the state serving as the ERISA plan sponsor (though not necessarily the plan sponsor for Code purposes such as deductions and nondiscrimination testing), named fiduciary and plan administrator. Participating employers' fiduciary responsibilities could be limited to prudent selection of the arrangement and monitoring of its operation. Similarly, participating employers' administrative involvement could be limited to enrolling employees and remitting employee and employer contributions to the plan. According to DOL, this approach would allow the state to take advantage of economies of scale to lower administrative and other costs. Additionally, as DOL would consider the MEP a single ERISA plan, there would be only one Form 5500 filing.

Comment. In past guidance, e.g., Advisory Opinion 2012-04A, DOL rejected the efforts of unrelated employers to join forces and form a single MEP underwritten or administered by a private sector entity (known as an "open MEP"). DOL's rationale has been that, to sponsor an ERISA plan, an entity must either act directly as the employer of the covered employees or "indirectly in the interest of an employer" in connection with the plan. According to DOL, the administering private sector entity lacks the requisite connection to the employees in the open MEP context. This IB, in contrast, provides that a state's "unique

> representational interest in the health and welfare of its citizens" sufficiently ties it to the contributing employers and their employees such that the state is acting "indirectly in the interest of an employer." Some stakeholders have criticized this aspect of the IB as advantaging state-based MEPs above open MEPs without cogent policy reasons for doing so. Likewise, it is not clear how DOL would view a state law that impacts individuals who are not citizens of that state, but who work within the state or who work for an employer operating within the state.

The IB notes that advantages of a state-run ERISA plan (as compared with a state-run IRA approach that meets the safe harbor's requirements for avoiding ERISA coverage) include greater savings opportunities through employer contributions and higher contribution limits, stronger protection from creditors, and potential tax credits for start-up costs.

Relevance to Employer Plan Sponsors

This guidance aims to encourage retirement savings for those not covered by a private sector workplace retirement plan. Neither the proposed safe harbor nor the IB affect an employer's ability to sponsor retirement savings plans for its employees, or an employer's rights and obligations concerning those plans.

However, employer-sponsored retirement plans may not cover an employer's entire workforce. For example, many plans feature minimum age and service eligibility requirements that exclude some part-timers, independent contractors and very young employees. A state might require employer participation for employees who do not meet employer-sponsored plan eligibility standards. This requirement could pose compliance and administrative challenges for employers that operate in multiple states. For example, where an employer operates in both State A and State B, with State A mandating coverage for individuals *residing* in State A and State B mandating coverage for individuals *working* in State B, the employer may need to comply with both state laws for the same employee.

In Closing

It remains to be seen whether DOL weighing in on state-based retirement savings programs will prompt a congressional response. Meanwhile, plan sponsors should consider any employee populations that might be affected by the guidance. Comments on the proposed regulation are due January 19, 2016. Although the IB is not subject to a notice and comment period, some comments on the proposed regulation might include feedback on the IB.

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