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DOL Finalizes Rules for State-Run Retirement Programs

Paltry retirement savings by many American workers spurred the Obama administration to encourage states to pick up the slack. DOL finalized guidance last week that, generally tracking the 2015 proposed rule, created a new safe harbor for state-required automatic IRA programs to fly under ERISA's radar. Along with these final rules, DOL issued a notice of proposed rulemaking, seeking input on extending the safe harbor to cities and counties. While primarily relevant to private sector employers that do not sponsor a retirement savings plan for their employees, the guidance may also affect sponsors of plans with eligibility provisions that limit participation to less than 100 percent of their employee population.

Background

Lack of access to employer-based retirement savings programs prompted the creation of "myRA" — a Roth IRA retirement savings account backed by the Obama Administration, and motivated a handful of states to enact state-run retirement savings programs for private employers. (See our January 31, 2014 *Legislate* for more on the myRA program.) The state-run programs generally come in the form of:

- An "auto-IRA," where employers deduct amounts selected by employees from their paychecks to remit to state-administered IRAs. California, Illinois and Oregon have taken this approach.
- A marketplace, where a state program connects employers with private sector savings plan providers. Washington State has adopted this framework.
- A prototype plan, where an employer adopts a prototype plan developed and administered by a state. Massachusetts has followed this model.

In late 2015, the DOL issued a proposed rule, along with an interpretive bulletin, aimed at facilitating state-based retirement programs. The proposed rule gave states a roadmap to create a program that would avoid application of ERISA. The Interpretive Bulletin, on the other hand, provided guidance for state-run

CA Retirement Saving Program

California is a few steps away from approving a state-run retirement savings program for certain private-sector employees who don't have access to a workplace retirement savings plan. The **bill,** approved by the California Assembly the same day DOL issued its final rule on state-based retirement programs, is expected to be passed by the California state senate and then signed by Governor Brown.

programs that by design would embrace ERISA. (For background on the proposed rule and the Interpretive Bulletin, please see our December 4, 2015 *For Your Information*.)

Final Rule and Notice of Proposed Rulemaking

On August 25, 2016, the DOL issued a final rule setting forth parameters for an IRA — established and maintained pursuant to a state payroll deduction savings program — to be exempt from ERISA under a safe harbor. A DOL news release accompanied the guidance, and the White House issued a fact sheet on the new rule. In addition, the DOL issued a notice of proposed rulemaking seeking input on extending the safe harbor to some cities and counties.

Satisfying the Safe Harbor

Under the guidance, a state-run program avoids ERISA coverage if it satisfies the following conditions:

Program Characteristics	State Responsibilities	Employer Role
Established pursuant to state law Implemented and administered by the state (or through its governmental agency or instrumentality, or by third-party contract with others) Voluntary for employees Provides employees with advance notice and the right to opt out, if there is an automatic enrollment feature	Investing employee savings, or selecting investment options from which employees can choose Ensuring the security of payroll deductions and employee savings Creation and enforcement of employee notice requirements about participant rights under the program	Limited to ministerial activities, such as collecting, remitting and maintaining records of payroll deductions and providing notice to employees and the state Facilitating employee payroll deductions No contributions of any employer funds

Key Changes from Proposed Rule

The final rule reflects important changes from the proposed rule, providing that states:

- May impose direct or indirect restrictions on withdrawals from the IRA
- May provide participating employers with consideration in the form of a reasonable estimate or typical employer costs, rather than limiting reimbursement to an employer's actual costs
- May not provide employer rewards that incentivize employers to participate in state programs in lieu of sponsoring their own retirement plans

No State Nexus Requirement

While the preamble provides that "states have a substantial governmental interest to encourage retirement savings in order to protect the economic security of their residents," the safe-harbor does not limit a state-run program to include only employees who are residents of the state or an employer with a principal place of business in the state. Instead, DOL determined that applicable state law will dictate whether a state-run retirement program can apply to, or otherwise affect, employees and employers lacking a connection to the state.

The "Old" Safe Harbor Remains

Although the DOL's final rule is new, and is specifically applicable to state-run programs, the "old" 1975 safe harbor rule that provides a roadmap for certain private/non-state run payroll deduction savings programs to avoid becoming ERISA plans remains intact. Specifically, under the 1975 regulation, IRA payroll deduction arrangements will not be subject to ERISA if:

- The employer makes no contributions (i.e., funding is limited to payroll deductions)
- The employee participation is "completely voluntary" (i.e., there is no automatic enrollment)
- The employer does not endorse the program (i.e., the employer's role is limited to being a conduit for an IRA vendor to connect with the employees)
- The employer receives no revenue, other than reimbursement for its own expenses

Effects on Employers Who Sponsor Retirement Plans

While primarily relevant to employers that do not sponsor their own retirement savings plans, state-run retirement programs may affect employers with plans that impose eligibility restrictions. Indeed, depending on program design and an employer's demographics, some employers may find themselves subject to more than one state-run program.

Workplace Savings Programs Not Necessarily a Shield

State-based retirement savings programs may impose mandates on employers of employees who are not eligible to participate in their workplace retirement savings programs. For example, a state law could require employers to automatically enroll into state-run IRAs any of their employees who are not eligible to participate in the workplace program because they have not yet met the plan's minimum service requirement.

Potential Burden from Multiple State-Run Programs

It is possible that employers operating in more than one state, or that have employees residing in more than one state, or residing in one state and working in another, could find themselves subject to more than one state-based retirement savings law — which could create burdensome and confusing compliance issues. To illustrate, consider a person that works in State A and lives in State B. If State A's law affects all employees working in State A and State B's law affects all employees living in State B, an employer may need to comply with both states' laws for an employee working in State A and living in State B. If both state laws required payroll deductions for the same employee, ordering or crediting rules may be necessary — burdening both the employer and the employee.

> **Comment.** If the DOL safe harbor is extended to cities or counties — as it is considering doing — the burden could grow.

In Conclusion

DOL designed this safe harbor to support a court finding that the state programs are not subject to ERISA — but courts may disagree with DOL's position. Nevertheless, employers should review their workplace savings programs and consider whether to broaden any eligibility provisions that may otherwise subject them to state-run retirement savings programs in connection with ineligible employees.

Authors
Allison Klausner, JD
Julia Zuckerman, JD

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