Secure Choice: State-Based Retirement Savings Programs Move Forward Despite Regulatory and Legal Headwinds

by Adam J. Thomas

Several states have started individual retirement account plans to help workers who don’t have access to employer-sponsored retirement plans. This article provides an overview of the plans as well as the legal challenges they face.
Several states have enacted laws that require employers to begin enrolling employees in individual retirement account (IRA) plans established by the state. These are commonly referred to as secure choice plans, and they present one more partial solution to the retirement crisis facing millions of Americans.

A recent poll conducted by the National Institute on Retirement Security found that 88% of Americans believe that the United States faces a retirement crisis. In 2016, the Department of Labor (DOL) found that approximately 39 million employees in the U.S. do not have access to any retirement savings plan. The impending retirement crisis is particularly acute in California, where approximately 7.5 million workers do not have access to any employer-sponsored retirement savings plan, and nearly 50% of California workers are on track to retire with incomes below $22,000 per year.

The retirement crisis is a problem that runs from coast to coast. A combined 1.2 million workers in Connecticut and Oregon do not have access to an employer-sponsored retirement program. According to the Connecticut State Comptroller, workers would be 15 times more likely to contribute to a retirement savings plan if it were offered through a payroll-deduction program.

In Illinois, 30% of the workforce, or 2 million workers, lack access to an employer-sponsored retirement plan. A study prepared by the University of Chicago Poverty Lab and the Illinois State Treasurer’s Office found that residents working in low-wage industries are far more likely to lack access to an employer-sponsored retirement plan when compared with employees in higher paid industries.

Secure Choice Legislation: One Way to Address the Retirement Crisis

Designing a solution to the retirement crisis has been a difficult task, and a nationwide solution through federal legislation seems unlikely in this unparalleled time of political discord. As a result, several states have taken on the task of enacting legislation mandating that employers must either sponsor a workplace retirement savings plan (such as a 401(k) plan) or automatically enroll employees in a state-sponsored IRA plan.

This type of plan has different names in various states but is commonly referred to as a secure choice plan, based on a 2011 report published by the National Conference on Public Employees Retirement Systems (NCPERS). The report recommends that states adopt secure choice plans to extend retirement savings opportunities to private sector employees who do not have access to such a program through their employer.

Following the NCPERS report, secure choice legislation has been considered in 28 states, and variations have been fully adopted in nine states. Legislation passed in California, Connecticut, Illinois, Maryland and Oregon shares a common set of features:

- Employers are required to participate in the program under state law.
- The role of the employer is limited to collecting pre-tax employee contributions from employee salary and forwarding the contributions to the state auto-IRA program.
- Employees are automatically enrolled in the program but may opt out at any time.
- Employee contributions are automatically set at a certain percentage, which varies from state to state.

Feasibility studies performed in two states contend that these programs can bring about a significant increase in retirement savings over the next several years. A 2016 study in California projects that 1.6 million participants will accrue a combined total of $3 billion in assets over the first six years following implementation of the state's secure choice program (now called CalSavers). Another study performed in Illinois shows that if 20% of eligible workers remain enrolled in the state's secure choice program, they would accrue a combined total of more than $8 billion in retirement assets within the first ten years of operation.

Secure choice legislation is by no means a panacea, and there has been ample debate over whether these programs can meaningfully address the retirement crisis. One investment group has applauded state efforts to enact secure choice legislation, claiming that it offers an opportunity for employers to reduce the costly compliance burdens associated with operating an ERISA-governed retirement plan.

Alternatively, other business groups and nonprofit trade associations argue that adoption of secure choice legislation provides states with an unfair competitive advantage over private retirement plan providers and will overburden employers by forcing them to navigate differing state laws when operating across state lines. Other groups believe these state programs will ultimately lead to fewer, less competitive solutions.
investment options for participants that are more expensive when compared with employer-sponsored retirement plans. These state programs also will have the burden of tracking frequent changes to participant contact information and will have to continuously monitor and update hundreds of thousands of records to account for changes in employment.

ERISA Preemption Clause
The states that have passed secure choice legislation have done so on the express condition that the program must be deemed exempt from the Employee Retirement Income Security Act of 1974 (ERISA). Without this exemption, the underlying legislation may become automatically invalid under the ERISA preemption clause, which invalidates any state law that “relates to” an employee pension benefit plan. The clause was originally intended to ensure that laws governing employee retirement plans would be uniform across all states, thereby allowing employers to operate across state lines and sponsor a retirement plan without having to comply with a host of varying or conflicting state laws.

Exempting secure choice legislation from ERISA will depend on how courts interpret the ERISA definition of an employee pension benefit plan: “[A]ny plan, fund or program which [is] established or maintained by an employer . . . to the extent [such] plan, fund, or program provides retirement income to employees . . . .”

Some argue that it is unclear from the statutory text of ERISA whether secure choice programs constitute an “employee benefit pension plan” that is “established or maintained by an employer.” They are not “established” by any one or more employers, since the enrollment of employees in the program is mandated by state law. These programs also are not “maintained” by any one or more employers because the state, and not the employer, is responsible for investing plan assets and administering employee access to accumulated retirement funds.

Congress Reverses DOL Clarifying Regulation
In August 2016, DOL found that the uncertainty of ERISAs application to these secure choice programs was preventing more states from adopting legislation. DOL issued a final regulation stating that secure choice plans would not be considered “employee pension benefit plans” under ERISA, provided the underlying state legislation met a detailed set of eight criteria.

Most importantly, the final regulation required that each employee be given advance notice and a reasonable opportunity to opt out of the program. It also required that employer involvement in administering the program must be purely “ministerial” by doing little more than distributing program literature to employees and transmitting employee contributions to the state. These requirements are modeled after a 1975 final regulation that allows employers to avoid establishing an ERISA plan if they merely forward contributions to an employee’s IRA plan.

Congress ultimately rescinded the DOL final rule on May 17, 2017 under the Congressional Review Act. However, this action did not affect the 1975 final regulation, so employers may still avoid establishing an ERISA plan if they merely forward contributions to an employee’s IRA plan. This remaining rule still serves as valuable precedent for arguing that these secure choice arrangements also do not constitute an employee benefit plan under ERISA.
States Proceed With Secure Choice Legislation Despite Regulatory and Legal Headwinds

The five states discussed in this article continue to move forward with secure choice programs even though Congress rescinded the 2016 final regulation. Oregon has completed its pilot program and has implemented its program (now called OregonSaves). Employers are or will be required to begin enrolling employees in the program on a staggered schedule that began November 15, 2017 for the largest employers (100 or more employees) and ending May 15, 2020 for the smallest (four or fewer employees).22 As of this writing, 951 employers had registered with OregonSaves.23

Illinois opened its pilot program in May 2018.24 Employers with 500 or more workers are required to begin enrolling employees in the program starting November 1, and enrollment will be phased in through November 1, 2019 for smaller employers.

California is preparing to open its pilot program in late 2018, and employers with 100 or more employees will be required to begin enrolling employees 12 months following implementation. Those with 50 or more employees will have two years following implementation to enroll workers, and those with five or more will have three years.25

Connecticut continues to work toward implementation of its program; however, no implementation time line has been announced.26 Maryland is in the process of implementing secure choice legislation that took effect on July 1, 2016. An executive director has been selected for the program, although no specific implementation time line has been announced.27

In November 2017, Seattle became the first city to enact a secure choice retirement program through local ordinance.28 Employers of any size that have been operating within Seattle city limits for at least 24 months must enroll employees in the Seattle Retirement Savings Plan, which is scheduled to become operational no later than January 2021.

Washington and New Jersey have passed legislation calling for the creation of “virtual marketplaces” where small businesses with up to 100 employees can select retirement plans for employees. These programs are entirely voluntary for both employers and employees.29,30 The Washington marketplace was launched in March 2018. As of this writing, an implementation date for the New Jersey marketplace has not been announced.

Massachusetts and Vermont have enacted legislation creating voluntary open multiple employer plans (MEPs) that are subject to ERISA. The Vermont program—called the Green Mountain Secure Retirement Plan—is scheduled to open in January 2019 to employers with 50 or fewer employees and self-employed individuals.31 The Massachusetts program—called the CORE Plan—is currently open for enrollment of employees working at nonprofit employers with 20 or fewer employees.32 The CORE Plan offers enrollees 15 different investment options including 11 default target-date funds and four objective-based investment funds.

New York enacted legislation in April 2018 establishing a state-based Roth IRA-style program that will be entirely voluntary for employees and will open to employees working for any employer that has not offered an employee retirement plan in the preceding two years.33 The program is scheduled to open in April 2020.34

Secure choice legislation has been introduced but not passed in 20 additional states. These states may be taking a seat on the sidelines until a clearer picture forms about the future of secure choice plans and whether these plans will be deemed exempt from ERISA, either through future congressional action or as the result of litigation filed against the plan in California.35

Legal Challenges

Legal challenges seeking to block the progress of secure choice implementation have been filed in Oregon and California, and an additional lawsuit may be on the horizon in Illinois.

In Oregon, a nonprofit association filed a lawsuit against the state claiming that it was unlawful for the OregonSaves legislation to require employer-
members of the association to certify that they were exempt from having to comply with the program. The lawsuit was settled in March 2018 after the state agreed to exempt employers from the law, provided (1) they are members of the nonprofit trade association that brought the lawsuit and (2) their membership can be verified by the state. The association claimed that the law was void under the ERISA preemption clause because it constituted a state law that “relates to” an employee pension benefit plan. The same nonprofit association is considering filing another lawsuit in Illinois after that program launches the next phase on November 1, 2018.

A different nonprofit taxpayer association filed a lawsuit in California in May 2017 alleging that the state law establishing the California auto-IRA program (CalSavers) violates the ERISA preemption clause because it “relates to” an employee pension benefit plan. The lawsuit also alleges that the nonprofit association and its members have standing to bring the lawsuit because the law compels them to forward employee contributions to the CalSavers program, thereby making them an “involuntary fiduciary” under ERISA.

The outcome of the lawsuit in California will mostly depend on how the court interprets the definition of an employee benefit plan under ERISA and whether employee participation in CalSavers is “completely voluntary.” Should the court rule that the program is not subject to ERISA, it will likely be for two reasons:

1. Employer involvement is limited to performing a discreet set of functions required by the state law, which means the CalSavers program is not “established and maintained” by any one or more employers.
2. CalSavers is “completely voluntary” on the part of employees because it requires that employees be provided with an opportunity to opt out of the program before they are enrolled.

The claim that employers will become “involuntary fiduciaries” under ERISA also may lack merit. It’s unlikely that ERISA applies to CalSavers, but if it did, the definition of a fiduciary under ERISA does not include persons that perform only “ministerial” functions. Under the CalSavers program, the role of the employer is generally limited to disseminating informational materials to employees, enrolling them in the program and forwarding employee contributions to the program. Federal regulation defines these tasks as ministerial and not fiduciary in nature, because they are performed pursuant to “... rules, practices and procedures made by other persons.”

Conclusion

Statistics show that less than 10% of the U.S. population elects to enroll in an IRA outside of work. Yet many workers lack access to an employer-sponsored retirement savings plan, putting them at risk for poverty during retirement. Although it has faced regulatory and legal hurdles, secure choice legislation maybe one answer to the growing retirement crisis in the U.S.

Editor’s note: Benefits Magazine goes to press about four weeks before distribution. The status of state secure choice plans in this article was current at the time of writing but continues to evolve.

Endnotes

14. James Rufus Koren, “The GOP is tyring to kill California’s new pri-
secure choice plans


17. 29 USC §1144(a).

18. 29 USC §1002(2)(A) (emphasis supplied); See also, 81 Fed. Reg. 59464, 59465 (Aug. 30, 2016).


42. 29 CFR §2509.75-8 D-2.

43. Ibid.

44. 81 Fed. Reg. at 59464.

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