DEPARTMENT OF LABOR

Employee Benefits Security Administration

29 CFR Part 2510

RIN 1210-AB71

Savings Arrangements Established by States for Non-Governmental Employees

AGENCY: Employee Benefits Security Administration, Department of Labor.

ACTION: Proposed rule.

SUMMARY: This document contains a proposed regulation under the Employee Retirement Income Security Act of 1974 (ERISA) setting forth a safe harbor describing circumstances in which a payroll deduction savings program, including one with automatic enrollment, would not give rise to an employee pension benefit plan under ERISA. A program described in this proposal would be established and maintained by a state government, and state law would require certain private-sector employers to make the program available to their employees. Several states are considering or have adopted measures to increase access to payroll deduction savings for individuals employed or residing in their jurisdictions. By making clear that state payroll deduction savings programs with automatic enrollment that conform to the safe harbor in this proposal do not establish ERISA plans, the objective of the safe harbor is to reduce the risk of such state programs being preempted if they were ever challenged. If adopted, this rule would affect individuals and employers subject to such laws.

DATES: Written comments should be received by the Department of Labor on or before January 19, 2016.

ADDRESSES: You may submit comments, identified by RIN 1210-AB71, by one of the following methods:

- *Federal eRulemaking Portal*: *http://www.regulations.gov*. Follow the instructions for submitting comments.

- *E-mail*: *e-ORI@dol.gov*. Include RIN 1210–AB71 in the subject line of the message.

- *Mail*: Office of Regulations and Interpretations, Employee Benefits Security Administration, Room N–5655, U.S. Department of Labor, 200 Constitution Avenue, NW., Washington, DC 20210, Attention: State Savings Arrangements Safe Harbor.

Instructions: All submissions must include the agency name and Regulatory Identification Number (RIN) for this rulemaking. Persons submitting comments electronically are encouraged to submit only by one electronic method and not to submit paper copies. Comments will be available to the public, without charge, online at www.regulations.gov and www.dol.gov/ebsa and at the Public Disclosure Room, Employee Benefits Security Administration, U.S. Department of Labor, Suite N-1513, 200 Constitution Avenue, N.W., Washington, DC 20210. WARNING: Do not include any personally identifiable or confidential business information that you do not want publicly disclosed. Comments are public records and are posted on the Internet as received, and can be retrieved by most internet search engines.

FOR FURTHER INFORMATION CONTACT: Janet Song, Office of Regulations and Interpretations, Employee Benefits Security Administration, (202) 693–8500; or Jim Craig, Office of the Solicitor, Plan Benefits Security Division, (202) 693-5600. These are not toll-free numbers.

SUPPLEMENTARY INFORMATION

A. Background

Approximately 68 million US employees do not have access to a retirement savings plan through their employers.[1] For older Americans, inadequate retirement savings can mean sacrificing or skimping on food, housing, health care, transportation, and other necessities. Inadequate retirement savings place greater stress on state and federal social welfare programs as guaranteed sources of income and economic security for older Americans. Accordingly, states have a substantial governmental interest in taking steps to address the problem and protect the economic security of their residents.[2] Concerned over the low rate of saving among American workers, some state governments have already sought to expand access to savings programs for their residents and other individuals employed in their jurisdictions by creating their own programs and requiring employer participation.[3]

1. *State Payroll Deduction Savings Initiatives*

One approach some states have taken is to establish state payroll deduction savings initiatives. Such programs encourage employees to establish tax-favored individual retirement plans (IRAs) funded by payroll deductions. Oregon, Illinois, and California, for example, have adopted laws along these lines.[4] These initiatives generally require specified employers that do not offer workplace savings arrangements to deduct amounts from their employees' paychecks in

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[1] Copeland, Craig, Employment-Based Retirement Plan Participation: Geographic Differences and Trends, 2013, Employee Benefit Research Institute, Issue Brief No. 405 (October 2014) (available at www.ebri.org).

[2] See Christian E. Weller, PhD, Nari Rhee, PhD, and Carolyn Arcand, Financial Security Scorecard: A State-by-State Analysis of Economic Pressures Facing Future Retirees, National Institute on Retirement Security (March 2014) (www.nirsonline.org/index.php?option=com_content&task=view&id=830&Itemid=48).

[3] See, for example, Report of the Governor's Task Force to Ensure Retirement Security for All Marylanders, Kathleen Kennedy Townsend, Chair, 1,000,000 of Our Neighbors at Risk: Improving Retirement Security for Marylanders (2015). The Georgetown University Center for Retirement Initiatives (CRI) of the McCourt School of Public Policy has compiled a "50 state survey" providing information on state legislation that would establish state-sponsored retirement savings plans at http://cri.georgetown.edu/states/. The stated mission of the CRI is "[to] strengthen the retirement security of American families by developing and promoting the bipartisan adoption of innovative state policies, legislation and administrative models, such as pooled and professionally managed funds, which will expand the availability and effectiveness of retirement solutions."

[4] Illinois Secure Choice Savings Program Act, 2014 Ill. Legis. Serv. P.A. 98-1150 (S.B. 2758) (West); California Secure Choice Retirement Savings Act, 2012 Cal. Legis. Serv. Ch. 734 (S.B. 1234) (West); Oregon 2015 Session Laws, Ch. 557 (H.B. 2960) (June 2015).

order that those amounts may be remitted to state-administered IRAs for the employees. Typically, with automatic enrollment, the states would require that the employer deduct specified amounts on behalf of the employee, unless the employee affirmatively elects not to participate. As a rule, employees can stop the payroll deductions at any time. The programs, as currently designed, do not require, provide for or permit employers to make matching or other contributions of their own into the employees' accounts. In addition, the state initiatives typically require that employers act as a conduit for information regarding the program, including disclosure of employees' rights and various program features, often based on state-prepared materials.

2. *ERISA's Regulation of Employee Benefit Plans*

ERISA defines the terms "employee pension benefit plan" and "pension plan" broadly to mean, in relevant part:

- any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program-
    - provides retirement income to employees, or
    - results in a deferral of income by employees for periods extending to the termination of covered employment or beyond, regardless of the method of calculating the contributions made to the plan, the method of calculating the benefits under the plan or the method of distributing benefits from the plan.

29 U.S.C. 1002(2)(A). The provisions of Title I of ERISA, "shall apply to any employee benefit plan if it is established or maintained . . . by any employer engaged in commerce or in any industry or activity affecting commerce."[5] 29 U.S.C. 1003(a).

[5] ERISA includes several express exemptions in section 4(b) from coverage under Title I, for example, for pension plans established or maintained by governmental entities or churches for their employees, certain foreign plans, unfunded excess benefit plans, and plans maintained solely to comply with applicable state laws regarding workers compensation, unemployment, or disability. 29 U.S.C. 1003(b).

Despite the express intent of the drafters of those state statutes not to have such a result, some have expressed concern that payroll deduction programs, such as those enacted in Oregon, California and Illinois, may cause employers to establish ERISA-covered plans inadvertently. The Department and the courts have interpreted the term "established or maintained" as requiring minimal involvement by the employer or employee organization to trigger the protections of ERISA coverage. For example, an employer may establish a benefit plan by purchasing insurance products for individual employees.[6] Moreover, retirement savings programs involving IRAs also fall within the broad definition of pension plan when those programs are established or maintained by an employer or employee organization.[7]

Pension plans covered by ERISA are subject to various statutory and regulatory requirements to protect the interests of the plan participants. These include reporting and disclosure rules and stringent conduct standards derived from trust law for plan fiduciaries. In addition, ERISA expressly prohibits certain transactions involving plans unless a statutory or administrative exemption applies.

Moreover, in order to assure nationwide uniformity of treatment, ERISA places the regulation of private-sector employee benefit plans (including employment-based pension plans) under federal jurisdiction. Section 514(a) of ERISA, 29 U.S.C. 1144(a), provides that the Act "shall supersede any and all State laws insofar as they . . . relate to any employee benefit plan" covered by the statute. The U.S. Supreme Court has long held that "[a] law 'relates to' an employee benefit plan, in the normal sense of the phrase, if it has a connection with or reference

[6] Donovan v. Dillingham, 688 F.2d 1367 (11th Cir. 1982); Harding v. Provident Life and Accident Ins. Co., 809 F. Supp. 2d 403, 415-419 (W.D. Pa. 2011); DOL Adv. Op. 94-22A (July 1, 1994).
[7] ERISA section 404(c)(2) (simple retirement accounts); 29 CFR 2510.3-2(d) (safe harbor for certain payroll deduction individual retirement accounts); 29 CFR 2509-99-1 (interpretive bulletin on payroll deduction IRAs); Cline v. The Industrial Maintenance Engineering & Contracting Co., 200 F.3d 1223, 1230-31 (9th Cir. 2000).

to such a plan." Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 96-97 (1983) (footnote omitted). In various decisions, the Court has concluded that ERISA preempts state laws that: (1) mandate employee benefit structures or their administration; (2) provide alternative enforcement mechanisms; or (3) bind employers or plan fiduciaries to particular choices or preclude uniform administrative practice, thereby functioning as a regulation of an ERISA plan itself.[8]

IRAs generally are not established or maintained by employers or employee organizations, and ERISA coverage is contingent on an employer (or employee organization) establishing or maintaining the arrangement. 29 USC 1002(1) - (2). The Internal Revenue Code is the principal federal law that governs such IRAs. The Code includes prohibited transaction provisions (very similar to those in ERISA), which are primarily enforced through imposition of excise taxes against IRA fiduciaries by the Internal Revenue Service. 26 U.S.C. 4975.

In other contexts, the Department has provided guidance to help employers determine whether their involvement in voluntary payroll deduction arrangements for sending employee retirement savings contributions to IRAs would amount to establishing or maintaining ERISA-covered plans. For example, in 1975, the Department promulgated a safe harbor regulation to clarify the circumstances under which IRAs funded by payroll deductions would not be treated as ERISA plans. 29 CFR 2510.3-2(d); 40 FR 34,526 (Aug. 15, 1975). This safe harbor is part of a more general regulation that "clarifies the limits of the defined terms 'employee pension benefit plan' and 'pension plan' for purposes of title I of the Act . . . by identifying specific plans, funds and programs which do not constitute employee pension benefit plans for those purposes." 29

[8] New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co., 514 U.S. 645, 658 (1995); Ingersoll-Rand Co. v. McClendon, 498 U.S. 133, 142 (1990); Egelhoff v. Egelhoff, 532 U.S. 141, 148 (2001); Fort Halifax Packing Co. v. Coyne, 482 U.S. 1, 14 (1987).

CFR 2510.3-2(a). Other similar safe harbors were published in the same Federal Register notice.[9]

The 1975 regulation provides that ERISA does not cover a payroll deduction IRA arrangement so long as four conditions are met: the employer makes no contributions, employee participation is "completely voluntary," the employer does not endorse the program and acts as a mere facilitator of a relationship between the IRA vendor and employees, and the employer receives no consideration except for its own expenses.[10] In essence, if the employer merely allows a vendor to provide employees with information about an IRA product and then facilitates payroll deduction for employees who voluntarily initiate action to sign up for the vendor's IRA, the arrangement is not an ERISA pension plan.

In 1999, the Department published additional guidance on this safe harbor in the form of Interpretive Bulletin 99-1. 29 CFR 2509.99-1. This guidance explains that employers may, consistent with the third condition in the regulation, furnish materials from IRA vendors to the employees, answer employee inquiries about the program, and encourage retirement savings through IRAs generally, as long as the employer makes clear to employees its neutrality concerning the program and that its involvement is limited to collecting the deducted amounts and remitting them promptly to the IRA sponsor, just as it remits other payroll deductions to taxing authorities and other third parties. 29 CFR 2510.99-1(c).[11]

The Department’s publication of the 1975 payroll deduction IRA safe harbor was prompted by comments on an earlier proposal indicating “considerable uncertainty concerning

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[9] 29 CFR 2510.3-1(j), Certain group or group-type insurance arrangements; 29 CFR 2510.3-2(f), Tax sheltered annuities. 40 FR 34530 (Aug. 15, 1975).

[10] 29 CFR 2510.3-2(d), Individual Retirement Accounts.

[11] The Department has also issued advisory opinions discussing the application of the safe harbor regulation to particular facts. See, e.g., Advisory Opinion 82-67A (Dec. 21, 1982), 1982 WL 21250; DOL Adv. Op. 84-25A (June 18, 1984), 1984 WL 23439.

Title I coverage of individual retirement programs . . . ." 40 FR 34528. When it promulgated the safe harbor regulation, the Department did not consider payroll deduction savings arrangements for private-sector employees with terms required by state laws. Instead, the payroll deduction IRA safe harbor and the group insurance safe harbor published that day focused on employers acting in coordination with IRA and other vendors, without state involvement. Under those circumstances, it was important for both safe harbors to contain conditions to limit employer involvement, both to avoid establishing or maintaining an employee benefit plan and to prevent undue employer influence in arrangements that would not be subject to ERISA's protective provisions. When a program meets the conditions of the safe harbor, employer involvement in the arrangement is minimal and employees' control of their participation in the program is nearly complete. In such circumstances, it is fair to say that each employee, rather than the employer, individually establishes and maintains the program.

One of the 1975 payroll deduction IRA safe harbor's conditions is that an employee's participation must be "completely voluntary." The Department intended this term to mean considerably more than that employees are free to opt out of participation in the program. Instead, the employee's enrollment must be self-initiated. In various contexts, courts have held that opt-out arrangements are not consistent with a requirement for a "completely voluntary" arrangement.[12] This condition is important because where the employer is acting on his or her

[12] See Doe v. Wood Co. Bd. Of Educ., 888 F.Supp.2d 771, 775-77 (S.D. W. Va. 2012) (Education Department regulations requiring "completely voluntary" choice of single-gender education not satisfied by opt-out provision); Schear v. Food Scope America, Inc., 297 F.R.D. 114, 125 (S.D.N.Y. 2014) ("For a voluntary 'tip pooling' arrangement to exist, it must be 'undertaken by employees on a completely voluntary basis and may not be mandated or initiated by employers' and an employer can take 'no part in the organization or the conduct of [the] tip-pool.'") (quoting N.Y. Dept. of Labor Opinion Letter RO–08–0049). See also Carter v. Guardian Life Ins. Co., Civil No. 11–3–ART, 2011 WL 1884625, *1 (W.D. Ky. May 18, 2011) ("Courts have held that employees' participation is not 'completely voluntary' if their enrollment in the plan is 'automatic.'"); Thompson v. Unum Life Ins. Co., No. Civ.A.3:03-CV-0277-B, 2005 WL 722717, *6 (N.D. Tex. Mar. 29, 2005) (analyzing group welfare plan safe harbor, "Thompson's participation in the plan was automatic rather than voluntary"); cf. The Meadows v.

own volition to provide the benefit program, the employer's actions –e.g., requiring an automatic enrollment arrangement – would constitute its "establishment" of a plan within the meaning of ERISA's text, and trigger ERISA's protections for the employees whose money is deposited into an IRA. As a result, state payroll deduction savings initiatives with automatic enrollment do not meet the 1975 safe harbor's "completely voluntary" requirement.

However, when a state government sets the terms for and administers a payroll deduction savings arrangement, the situation is far different than when the employer sets the terms and administers the program – the 1975 safe harbor was not written with such state laws in mind. Therefore, the Department is promulgating this new safe harbor that does permit automatic enrollment in such state payroll deduction savings arrangements. Where states require employers to offer savings arrangements, undue employer influence or pressure to enroll is far less of a concern. Moreover, the state's active involvement and the limitations on the employers' role removes the employer from the equation such that the payroll deduction arrangements are not established or maintained by an employer or employee organization within the meaning of

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Employers Health Ins., 826 F. Supp. 1225, 1229 (D. Ariz. 1993) (enrollment not "completely voluntary" where health insurance contract required 75 percent of employees to participate); Davis v. Liberty Mut. Ins. Co., Civ. A. No. 87–2851, 1987 WL 16837, *2 (D.D.C. Aug. 31, 1987) (health insurance enrollment not completely voluntary because employee would receive no alternative compensation for refusing coverage, therefore making refusal comparable to a cut in pay). See generally Advisory Council On Employee Welfare And Pension Benefit Plans, Current Challenges And Best Practices For ERISA Compliance For 403(b) Plan Sponsors (2011) (available at www.dol.gov/ebsa/publications/2011ACreport1.html) ("The Council also considered, but is not recommending, that DOL permit the inclusion of an automatic enrollment feature within the context of an ERISA safe harbor 403(b) plan. The majority of Council members concluded that automatic enrollment would require actions typically performed by a plan sponsor/fiduciary (e.g., designation of a default investment alternative), and consequently, an automatic enrollment option in the plan may not be viewed as voluntary even in light of the participant's right to opt out of the automatic contributions."). DOL Field Assistance Bulletin (FAB) 2004-1 stated that an employer could open a health savings account (HSA) and deposit employer funds into it without the employee's affirmative consent so long as, among other things, the arrangement was "completely voluntary on the part of the employees" and also that employees exercised control over the account with the power to withdraw or transfer the employer money. FAB 2004-1 was focused on the effect of employer contributions, so there was no specific discussion of what was meant by "completely voluntary" in the context of an HSA. Field Assistance Bulletin 2006-2 clarified that the completely voluntary requirement in FAB 2004-1 related to employee contributions to an HSA and confirms that completely voluntary employee contributions to the HSA must be self-initiated. The only "opt out" considered in FAB 2004-1 was the employees' power to move employer contributions out of the HSA. Neither FAB suggested that employee contributions to an HSA could be completely voluntary under an opt out arrangement.

ERISA section 3(2). Accordingly, the safe harbor proposed today permits automatic enrollment with an opt-out provision in the context of state required and administered programs that meet the terms of the proposal. The safe harbor should remove uncertainty about Title I coverage of such state payroll deduction savings arrangements by promulgating a “voluntary” standard that permits automatic enrollment arrangements with employee opt-out features. By removing this uncertainty, the objective of the proposed safe harbor is to diminish the chances that, if the issue were ultimately litigated, the courts would conclude that state payroll deduction savings arrangements are preempted by ERISA.

3. *Purpose and Scope of Proposed Regulation*

Section 505 of ERISA gives the Secretary of Labor broad authority to prescribe such regulations as he finds necessary and appropriate to carry out the provisions of Title I of the Act. The Department believes that regulatory guidance in this area is necessary to ensure that governmental bodies, employers, and others in the regulated community have guidelines concerning whether state efforts to encourage savings implicate Title I of ERISA by requiring the establishment or maintenance of ERISA-covered employee pension benefit plans.

The 1975 payroll deduction IRA safe harbor sets forth standards for judging whether employer conduct crosses the line between permitted ministerial activities with respect to non-plan IRAs and activities that involve the establishment or maintenance of an ERISA-covered plan. State payroll deduction savings initiatives are similar to arrangements covered under the 1975 safe harbor if the employer's involvement is limited to withholding and forwarding payroll deductions and performing other related ministerial duties and the state has sole authority to determine the terms and administration of the state savings arrangement. The 1975 safe harbor, however, does not envision state involvement in the IRA programs nor does it envision use of automatic enrollment and related provisions.

The proposed regulation thus would provide a new and additional “safe harbor” for state savings arrangements that conform to the proposed regulation’s provisions. The proposed regulation departs from the 1975 safe harbor for payroll deduction IRA programs by adopting a standard that enrollment be “voluntary” rather than “completely voluntary.” The new safe harbor’s voluntary standard will allow employees’ participation in state required programs to be initiated by automatic enrollment with an opt-out provision. The Department is also proposing to add other provisions to assure that employer involvement remains minimal.

The proposed regulation, however, as a “safe harbor,” does not purport to define every possible program that could fall outside of Title I of ERISA because it was not “established or maintained” by an employer. The Department also is not expressing any view regarding the application of provisions of the Internal Revenue Code (Code).

B. Description of the Proposed Regulation

The proposed regulation § 2510.3-2(h) provides that for purposes of Title I of ERISA, the terms “employee pension benefit plan” and “pension plan” do not include an individual retirement plan (as defined in 26 U.S.C. section 7701(a)(37)) established and maintained pursuant to a state payroll deduction savings program if the program satisfies all of the conditions set forth in paragraphs (h)(1)(i) through (xii) of the proposed regulation. In the Department’s view, compliance with these conditions will assure that the employer's involvement in the state program is limited to the ministerial acts necessary to implement the payroll deduction program as required by state law. In addition, the proposed conditions would give employees sufficient freedom not to enroll or to discontinue their enrollment, as well as meaningful control over their IRAs.

The term “individual retirement plan” means an individual retirement account described in section 408(a) and an individual retirement annuity described in section 408(b) of the Code.[13] Thus, by limiting the safe harbor to programs that use such individual retirement plans (which would include both traditional and Roth IRAs), the proposal incorporates the applicable protections under the Code, including the prohibited transaction provisions.

The safe harbor conditions under the proposed regulations require that the program be established by a state government pursuant to state law. As discussed above, if an employer's activities are limited to those ministerial functions required by the state law, the arrangement is not established or maintained by the employer. The term “State” in the proposed regulation has the same meaning as in Title I of ERISA generally. As in section 3(10) of ERISA, a “State” includes any “State of the United States, the District of Columbia,” and certain territories.[14] 29 U.S.C. 1002(10). The state must also administer the program either directly or through a governmental agency or other instrumentality. The safe harbor also contemplates that a state or the governmental agency or instrumentality could contract with commercial service providers, such as investment managers and recordkeepers, to operate and administer its program.

The proposal does not address whether the employees that participate in the program must be employed within the state that establishes the program, or alternatively whether the covered employees must be residents of the state or employed by employers doing business

[13] Whether a state program meets the statutory requirements under the Code is a question within the jurisdiction of the Internal Revenue Service.

[14] The term “State” in the proposed regulation has the same meaning as in section 3(10) of ERISA. This would not include Indian tribes, tribal subdivisions, or agencies or instrumentalities of either in coverage under the regulation. To date, the Department is unaware of any tribal initiatives similar to the state initiatives described elsewhere in this preamble. Comments are welcome on whether, on what basis, and under what circumstances, payroll deduction programs required by Indian tribes might be covered under the safe harbor.

within the state. The extent to which a state can regulate employers is already established under existing legal principles. The proposal simply requires that the program be established by a state pursuant to state law. The Department solicits comments on whether the safe harbor should be limited to require some connection between the employers and employees covered by the program and the state that establishes the program, and if so, what kind of connection.

The proposed regulation requires that participation in the program be voluntary for employees. As discussed above, this requirement is different from the current payroll deduction IRA safe harbor in 29 CFR 2510.3-2(d), which requires that participation be "completely voluntary." The proposed regulation expressly permits opt-out programs and, accordingly, does not require that participation be "completely voluntary." By using only the term "voluntary," the Department intends to make clear that the proposed regulation, unlike the existing safe harbor, would allow the state to require employers to automatically enroll employees, unless they affirmatively elect not to participate in the program.[15]

The proposed regulation also includes conditions to assure that control of the payroll deduction program and the savings accounts lies with the state and the employees, and not the employer. These include requirements that (1) the program does not require that an employee or beneficiary retain any portion of contributions or earnings in his or her IRA and does not otherwise impose any restrictions on withdrawals or impose any cost or penalty on transfers or rollovers permitted under the Internal Revenue Code; (2) all rights of the employee, former employee, or beneficiary under the program are enforceable only by the employee, former

[15] If a program requires automatic enrollment, adequate notice of their right to opt out must be furnished to employees in order for the program to meet the safe harbor's voluntariness condition. The proposal does not define the manner and content of "adequate notice" for this purpose. The Department expects that states and their vendors would look to analogous notice requirements contained in federal laws pertaining to automatic enrollment provisions. See, e.g., 26 U.S.C. 401(k)(13)(E) and 414(w); 29 U.S.C 1144(e)(3); and 29 CFR 2550.404c-5(d). The Department solicits comments on this issue.

employee, or beneficiary, an authorized representative of such person, or by the state (or the designated agency or instrumentality); and (3) the state adopts measures to ensure that employees are notified of their rights under the program and creates a mechanism for enforcement of those rights. In addition, the proposal requires the state to assume responsibility for the security of payroll deductions and employee savings. These conditions assure that the employees will have meaningful control over their retirement savings, that the state will enforce the employer's payroll deduction obligations and oversee the security of retirement savings, and that the employer will have no role in enforcing employee rights under the program.

Limited employer involvement in the program is the key to a determination that a state savings program is not an employee pension benefit program. Thus, the employer's facilitation must be required by state law – if it is voluntary, the safe harbor does not apply. Further, the proposal does not permit the employer to contribute to the program.[16] All contributions under the program must be made voluntarily by the employees. When employers make contributions to fund benefits of the type enumerated in Section 3(2) of ERISA, they effectively sponsor an ERISA-covered plan. Similarly, the employer may not have discretionary authority, control, or responsibility under the program and may not receive any direct or indirect compensation in the form of cash or otherwise in connection with the program, other than the reimbursement of the actual costs of the program to the employer. Finally, the proposal specifies that employer involvement must be limited to all or some of the following: (1) collecting employee contributions through payroll deductions and remitting them to the program; (2) providing notice to the employees and maintaining records regarding the employer's collection and remittance of payments under the program; (3) providing information to the state necessary to facilitate the

[16] This provision, of course, would not prohibit an employer from allowing employees to review program materials on company time or to use an employer's computer to make elections under the program.

operation of the program; and (4) distributing program information to employees from the state and permitting the state to publicize the program to employees.

A program could fit within the safe harbor and include terms that require employers to certify facts within the employer's knowledge as employer, such as employee census information (*e.g.*, status of a full time employee, employee addresses, attendance records, compensation levels, etc.). The employer could also conduct reviews to ensure it was complying with program eligibility requirements and limitations established by the state. The Department requests comments on whether the final regulation should provide more clarity and specificity on the types of functions that could be permitted consistent with the requirements of the safe harbor. [17]

A state program that meets all of the foregoing conditions will not fail to qualify for the safe harbor merely because the program is directed toward employees who are not already eligible for some other workplace savings arrangement. Nor will it fail merely because it requires automatic enrollment subject to employees having a right to opt out. Similarly, if the state program offers employees a choice of multiple IRA sponsors to which employees may make payroll deduction contributions, the state program can create a default option, i.e., designate the IRA provider to which the employer must remit the payroll withholding contributions in the absence of an affirmative election by the employee.

ERISA's expansive plan definition is critical to its protective purposes. When employers establish or maintain ERISA-covered plans, the plan's participants are protected by trust-law obligations of fiduciary conduct, reporting requirements, and a regulatory regime designed to

[17] In previous guidance issued by the Department under other safe harbors involving private parties, the Department concluded that employers could take certain corrective actions to stay within the safe harbor and that such actions, in and of themselves, did not lead to the establishment of an employee benefit plan. See DOL Information Letter to Siegel Benefit Consultants (Feb. 27, 1996) and Field Assistance Bulletin 2007-02 on the safe harbor for tax sheltered annuity programs under 29 CFR 2510.3-2(f).

ensure the security of promised benefits. In the circumstances specified by the proposed regulation, however, the employer does not "establish or maintain" the plan. Instead, the program is created and administered by the state for the benefit of those employees who voluntarily participate with minimal employer involvement. State administration of the voluntary program does not give rise to ERISA coverage, and presumably ensures that the program will be administered in accordance with the interests of the state's citizens.[18]

As noted above, ERISA generally preempts state laws that relate to employee benefit plans. The U.S. Supreme Court has long held that "[a] law 'relates to' an employee benefit plan, in the normal sense of the phrase, if it has a connection with or reference to such a plan." Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 96-97 (1983) (footnote omitted); see, e.g., New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co., 514 U.S. 645, 656 (1995). This proposed regulation would provide that certain state savings programs would not create employee benefit plans. However, the fact that state programs do not create ERISA covered plans does not necessarily mean that, if the issue were litigated, the state laws would not be preempted by ERISA. The courts' determinations would depend on the precise details of the statute at issue, including whether that state's program successfully met the requirements of the safe harbor.

Moreover, states should be advised that a program may be preempted by other Federal laws apart from ERISA. A state law that alters, amends, modifies, invalidates, impairs or supersedes a Federal law would risk being preempted by the Federal law so affected. Such

[18] To the extent that the state program allows employees not subject to the automatic enrollment requirement to voluntarily choose to participate, the employee's voluntarily participation would not result in the employer establishing an ERISA-covered plan or the state program including an ERISA-covered plan if the employer and the state program satisfy the conditions in the Department's existing safe harbor for payroll deduction IRAs at 29 CFR 2510.3-2(d). Of course, as described above, automatic enrollment of employees is not permitted under the existing payroll deduction IRA safe harbor.

preemption issues are beyond the scope of this proposed rule, however, which addresses only the question of whether particular programs involve the establishment of one or more ERISA covered employee benefit plans.

Finally, some states are considering approaches that differ from state payroll deduction savings initiatives. In 2012, Massachusetts, for example, enacted a law providing for a state-sponsored plan for non-profit employers with 20 or fewer employees.[19] Washington enacted a law to establish a small business retirement market place to assist small employers by making available a number of approved savings plans, some of which may be covered by ERISA, even though the marketplace arrangement itself is not. [20] This proposal does not address such state initiatives.

C. Effective Date

The Department proposes to make this regulation effective 60 days after the date of publication of the final rule in the FEDERAL REGISTER.

D. Regulatory Impact Analysis

1. *Executive Order 12866 Statement*

Under Executive Order 12866, the Office of Management and Budget (OMB) must determine whether a regulatory action is "significant" and therefore subject to the requirements of the Executive Order and subject to review by the OMB. Section 3(f) of the Executive Order defines a "significant regulatory action" as an action that is likely to result in a rule (1) having an annual effect on the economy of $100 million or more, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or state, local or tribal governments or communities (also referred to as an "economically

[19] Mass. Gen. Laws ch.29, sec. 64E (2014)
[20] 2015 Wash. Sess. Laws chap. 296 (SB 5826)

significant" action); (2) creating serious inconsistency or otherwise interfering with an action taken or planned by another agency; (3) materially altering the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (4) raising novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order.

OMB has tentatively determined that this regulatory action is not economically significant within the meaning of section 3(f)(1) of the Executive Order. However, it has been determined that the action is significant within the meaning of section 3(f)(4) of the Executive Order and the Department accordingly provides the following assessment of its potential benefits and costs.

a. Direct Benefits

As stated earlier in this preamble, some state governments have passed laws designed to expand workers' access to workplace savings programs. Some states are looking at ways to encourage employers to provide coverage under state-administered 401(k)-type plans, while others have adopted or are considering approaches that combine several retirement alternatives including IRAs, ERISA-covered plans and the Department of the Treasury's new starter savings program, *my*RA.

One of the challenges states face in expanding retirement savings opportunities for private sector employees is uncertainty about ERISA preemption of such efforts. ERISA generally would preempt a state law that required employers to establish and maintain ERISA-covered employee benefit pension plans. The Department therefore believes that states and other stakeholders would benefit from clear guidelines to determine whether state saving initiatives would effectively require employers to create ERISA-covered plans. The proposed rule would provide a new “safe harbor” from coverage under Title I of ERISA for state savings arrangements that conform to certain requirements. State initiatives within the safe harbor would not result in the establishment of employee benefit plans under ERISA. The Department expects that the proposed rule would reduce legal costs, including litigation costs, by (1) removing uncertainty about whether such state savings arrangements are covered by title I of ERISA, and (2) creating efficiencies by eliminating the need for multiple states to incur the same costs to determine their non-plan status.

The Department notes that the proposal would not prevent states from identifying and pursuing alternative policies, outside the safe harbor, that also would not require employers to establish or maintain ERISA-covered plans. Thus, while the proposal would reduce uncertainty about state activity within the safe harbor, it would not impair state activity outside it.

b. Direct Costs

The proposed rule does not require any new action by employers or the states. It merely clarifies that certain state initiatives that encourage workplace savings would not result in the creation of employee benefit plans covered by Title I of ERISA.

States may incur legal costs to analyze the rule and determine whether their laws fall within the proposed rule’s safe harbor. However, the Department expects that these costs will be less than the savings that will be generated. Moreover, states will avoid incurring the greater costs that might be incurred to determine their programs’ non-plan status without benefit of this proposed rule.

States that design their payroll deduction programs to conform to the safe harbor may incur costs to develop notices to be provided to participants and beneficiaries covered by the program and enter into contracts with investment managers and other service providers to operationalize and administer the programs. The Department's review of existing state payroll deduction legislation indicates that these requirements are customarily part of most state programs, and the initiatives generally could not operate without such requirements. Therefore, to the extent that state programs would exist even in the absence of this rule, only the relatively minor costs of revisions for conformity to the safe harbor are attributable to the rule, because other cost-generating activities are necessary and essential to operate and administer the programs. On the other hand, if state programs are adopted more widely in the rule's presence than in its absence, there would be more general state operational and administrative costs that are attributable to the rule. The Department does not have sufficient data to estimate the number of systems that would need to be updated; therefore, the Department invites comments and any relevant data that would allow it to make a more thorough assessment.

c. Uncertainty

The Department is confident that the proposed regulation, by clarifying that certain state programs do not require employers to establish ERISA-covered plans, will benefit states and many other stakeholders otherwise beset by greater uncertainty. However, the Department is unsure as to the magnitude of these benefits. The magnitude of the proposed regulation's benefits, costs and transfer impacts will depend on the states' independent decisions on whether and how best to take advantage of the safe harbor, and on the cost that otherwise would have attached to uncertainty about the legal status of the states' actions. The Department cannot predict what actions states will take, stakeholders' propensity to challenge such actions' legal status, either absent or pursuant to the proposed regulation, or courts' resultant decisions, and therefore the Department invites data submission or other comment that would allow for more thorough assessment of these issues.

d. *Impact of State Initiatives*

There are a number of cases in which this rulemaking could increase the prevalence of state workplace savings initiatives, thus bringing the effects of these initiatives within the scope of this regulatory impact analysis. For instance, if this issue were ultimately resolved in the courts, the courts could make a different preemption decision in the rule's presence than in its absence. Furthermore, even if a potential court decision would be the same with or without the rulemaking, the potential reduction in states' uncertainty-related costs could induce more states to pursue these workplace savings initiatives. An additional possibility is that the rule would not change the prevalence of state retirement savings programs, but would accelerate the implementation of programs that would exist anyway. With any of these possibilities, there would be benefits, costs and transfer impacts that are indirectly attributable to this rule, via the increased or accelerated creation of state-level workplace savings programs.

Employers may incur costs to update their payroll systems to transmit payroll deductions to the state or its agent and develop recordkeeping systems to document their collection and remittance of payments under the program. As with states' operational and administrative costs (discussed in section D.1.b, above), some portion of these employer costs would be attributable to the rule if more state workplace savings programs are implemented in the rule's presence than in its absence. Because employers' role in the programs must be minimal in order to satisfy the safe harbor, they will incur little cost beyond the costs associated with updating payroll systems. However, the costs that are incurred could fall most heavily on small and start-up companies, which tend to be least likely to offer pensions. Most state payroll deduction programs do exempt the smallest companies, which could significantly mitigate such costs. The Department does not have sufficient data to estimate the number of payroll systems that would have to be updated.

Therefore, the Department invites the public to provide comments and relevant data that would allow it to make a more thorough assessment.

The Department believes that well-designed state-level initiatives have the potential to effectively reduce gaps in retirement security. Relevant variables such as pension coverage,[21] labor market conditions,[22] population demographics,[23] and elderly poverty,[24] vary widely across the states, suggesting a potential opportunity for progress at the state level. For example, payroll deduction savings statutes in California and Illinois could extend savings opportunities for 7.8 million workers in California and 1.7 million workers in Illinois who currently do not have access to employment-based savings arrangements.[25] The Department offers the following policy discussion for consideration, and invites public input on the issues raised, on the potential for state initiatives to foster retirement security, and on the potential for this proposal or other Departmental action to facilitate effective state activity.

Effective state initiatives will advance retirement security. Some workers currently may save less than would be optimal because of behavioral biases (such as myopia or inertia) or labor market frictions that prevent them from accessing plans at work. Effective state initiatives would help such workers save more. Such workers will have traded some consumption today for more in retirement, potentially reaping some net gain in overall lifetime well-being. Their additional saving may also reduce fiscal pressure on publicly financed retirement programs and other public

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[21] See for example Craig Copeland, "Employment-Based Retirement Plan Participation: Geographic Differences and Trends, 2013," Employee Benefit Research Institute, Issue Brief No. 405 (October 2014) (available at www.ebri.org).
[22] See for example US Bureau of Labor Statistics, "Regional and State Employment and Unemployment—JUNE 2015," USDL-15-1430, July 21, 2015.
[23] See for example Lindsay M. Howden and Julie A. Meyer, "Age and Sex Composition: 2010," US Bureau of the Census, 2010 Census Briefs C2010BR-03, May 2011.
[24] Constantijn W. A. Panis & Michael Brien, August 28, 2015, "Target Populations of State-Level Automatic IRA Initiatives."
[25] Id.

assistance programs, such as the Supplemental Nutritional Assistance Program, that support low-income Americans, including older Americans.

The Department believes that well-designed state initiatives can achieve their intended, positive effects of fostering retirement security. However, the initiatives might have some unintended consequences as well. Those workers least equipped to make good retirement savings decisions arguably stand to benefit most from state initiatives, but also arguably are most at risk of suffering adverse unintended effects. Workers who would not benefit from increased retirement savings could opt out, but some might fail to do so. Such workers might increase their savings too much, unduly sacrificing current economic needs. Consequently they might be more likely to cash out early and suffer tax losses, and/or to take on more expensive debt. Similarly, state initiatives directed at workers who do not currently participate in workplace savings arrangements may be imperfectly targeted to address gaps in retirement security. For example, a college student might be better advised to take less in student loans rather than open an IRA, and a young family might do well to save more first for their children's education and later for their own retirement.

Employers that wish to provide retirement benefits are likely to find that ERISA-covered programs, such as 401(k) plans, have advantages for them and their employees over participation in state programs. Potential advantages include: greater tax preferences, greater flexibility in plan selection and design, opportunity for employers to contribute, ERISA protections, and larger positive recruitment and retention effects. Therefore it seems unlikely that state initiatives will "crowd-out" many ERISA-covered plans. However, if they do, some workers might lose ERISA-protected benefits that would have been more generous and more secure than state-based (or IRA) benefits, unless states adopt consumer protections similar to those Congress provided under ERISA. Some workers who would otherwise have saved more might reduce their savings to the low, default levels associated with some state programs. States can address this last concern by incorporating into their programs “auto-escalation” features that increase default contribution rates over time and/or as pay increases.

2. *Paperwork Reduction Act*

As part of its continuing effort to reduce paperwork and respondent burden, the Department of Labor conducts a preclearance consultation program to provide the general public and Federal agencies with an opportunity to comment on proposed and continuing collections of information in accordance with the Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3506(c)(2)(A)). This helps to ensure that the public understands the Department’s collection instructions, respondents can provide the requested data in the desired format, reporting burden (time and financial resources) is minimized, collection instruments are clearly understood, and the Department can properly assess the impact of collection requirements on respondents.

The Department has determined this proposed rule is not subject to the requirements of the PRA, because it does not contain a collection of information as defined in 44 U.S.C. 3502(3). The rule does not require any action by or impose any requirements on employers or the states. It merely clarifies that certain state payroll deduction programs that encourage retirement savings would not result in the creation of employee benefit plans covered by Title I of ERISA.

Moreover, the PRA definition of burden excludes time, effort, and financial resources necessary to comply with a collection of information that would be incurred by respondents in the normal course of their activities. See 5 CFR 1320.3(b)(2). The definition of burden also excludes burdens imposed by a state, local, or tribal government independent of a Federal requirement. See 5 CFR 1320.3(b)(3). The Department’s review of existing state payroll deduction programs indicates that they customarily have notification and recordkeeping requirements and that the initiatives could not operate without such requirements, especially programs that include automatic enrollment. Therefore, the proposed rule imposes no burden, because states customarily include notice and recordkeeping requirements that are an essential and routine part of administering state payroll deduction programs. In addition, employers are responding to state, not Federal, requirements when providing notices to individuals covered under state payroll deduction programs and maintaining records regarding the employers' collection and remittance of payments under the program.

Although the Department has determined that the proposed rule does not contain a collection of information, when rules contain information collections the Department invites comments that:

- Evaluate whether the collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;
- Evaluate the burden of the collection of information, including the validity of the methodology and assumptions used;
- Enhance the quality, utility, and clarity of the information to be collected; and
- Minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology, e.g., permitting electronic submission of responses.

In addition to having an opportunity to file comments with the Department, comments may also be sent to the Office of Information and Regulatory Affairs, Office of Management and

Budget, Room 10235, New Executive Office Building, Washington, DC 20503; Attention: Desk Officer for the Employee Benefits Security Administration. OMB requests that comments be received within 30 days of publication of the proposed rule to ensure their consideration.

3. *Regulatory Flexibility Act*

The Regulatory Flexibility Act (5 U.S.C. 601 et seq.) (RFA) imposes certain requirements with respect to Federal rules that are subject to the notice and comment requirements of section 553(b) of the Administrative Procedure Act (5 U.S.C. 551 et seq.) and which are likely to have a significant economic impact on a substantial number of small entities. Unless an agency certifies that a rule will not have a significant economic impact on a substantial number of small entities, section 603 of the RFA requires the agency to present an initial regulatory flexibility analysis at the time of the publication of the notice of proposed rulemaking describing the impact of the rule on small entities. Small entities include small businesses, organizations and governmental jurisdictions.

Because the proposed rule imposes no requirements or costs on employers, the Department believes that it would not have a significant economic impact on a substantial number of small entities. Accordingly, pursuant to section 605(b) of the RFA, the Assistant Secretary of the Employee Benefits Security Administration hereby certifies that the proposed rule, if promulgated, will not have a significant economic impact on a substantial number of small entities.

4. *Unfunded Mandates Reform Act*

For purposes of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1501 et seq.), as well as Executive Order 12875, this rule does not include any federal mandate that may result in expenditures by state, local, or tribal governments, or the private sector, which may impose an annual burden of $100 million.

5. *Congressional Review Act*

The proposed rule is subject to the Congressional Review Act provisions of the Small Business Regulatory Enforcement Fairness Act of 1996 (5 U.S.C. 801 et seq.) and, if finalized, would be transmitted to Congress and the Comptroller General for review.

6. *Federalism Statement*

Executive Order 13132 outlines fundamental principles of federalism. It also requires adherence to specific criteria by federal agencies in formulating and implementing policies that have `substantial direct effects'' on the states, the relationship between the national government and states, or on the distribution of power and responsibilities among the various levels of government. Federal agencies promulgating regulations that have these federalism implications must consult with state and local officials, and describe the extent of their consultation and the nature of the concerns of state and local officials in the preamble to the final regulation.

In the Department's view, the proposed regulations, by clarifying that certain workplace savings arrangements under consideration or adopted by certain states will not result in the establishment or maintenance by employers or employee organizations of employee benefit plans under ERISA, would provide more latitude and certainty to state governments and employers regarding the treatment of such arrangements under ERISA. The Department will affirmatively engage in outreach with officials of states, and with employers and other stakeholders, regarding the proposed rule and seek their input on the proposed rule and any federalism implications that they believe may be presented by it.

List of Subjects in 29 CFR Part 2510

Accounting, Employee benefit plans, Employee Retirement Income Security Act, Pensions, Reporting, Coverage

For the reasons stated in the preamble, the Department of Labor proposes to amend 29 CFR 2510 as set forth below:

PART 2510--DEFINITIONS OF TERMS USED IN SUBCHAPTERS C, D, E, F, AND G OF THIS CHAPTER

1. The authority citation for part 2510 is revised to read as follows:

Authority: 29 U.S.C. 1002(2), 1002(21), 1002(37), 1002(38), 1002(40), 1031, and 1135; Secretary of Labor's Order No. 1-2011, 77 FR 1088 (Jan. 9, 2012); Sec. 2510.3-101 also issued under sec. 102 of Reorganization Plan No. 4 of 1978, 43 FR 47713 (Oct. 17, 1978), E.O. 12108, 44 FR 1065 (Jan. 3, 1979) and 29 U.S.C. 1135 note. Sec. 2510.3-38 is also issued under sec. 1, Pub. L. 105-72, 111 Stat. 1457 (1997).

2. Section 2510.3-2 is amended by adding paragraph (h) to read as follows:

§ 2510.3-2 Employee pension benefit plans.

*** * * * ***

(h) <u>Certain State Savings Programs</u>. (1) For the purpose of Title I of the Act and this chapter, the terms “employee pension benefit plan” and “pension plan” shall not include an individual retirement plan (as defined in 26 U.S.C. section 7701(a)(37)) established and maintained pursuant to a State payroll deduction savings program, provided that:

(i) The program is established by a State pursuant to State law;

(ii) The program is administered by the State establishing the program, or by a governmental agency or instrumentality of the State, which is responsible for investing the employee savings or for selecting investment alternatives for employees to choose;

(iii) The State assumes responsibility for the security of payroll deductions and employee savings;

(iv) The State adopts measures to ensure that employees are notified of their rights under the program, and creates a mechanism for enforcement of those rights;

(v) Participation in the program is voluntary for employees;

(vi) The program does not require that an employee or beneficiary retain any portion of contributions or earnings in his or her IRA and does not otherwise impose any restrictions on withdrawals or impose any cost or penalty on transfers or rollovers permitted under the Internal Revenue Code;

(vii) All rights of the employee, former employee, or beneficiary under the program are enforceable only by the employee, former employee, or beneficiary, an authorized representative of such a person, or by the State (or the designated governmental agency or instrumentality described in paragraph (h)(1)(ii) of this section);

(viii) The involvement of the employer is limited to the following:

(A) Collecting employee contributions through payroll deductions and remitting them to the program;

(B) Providing notice to the employees and maintaining records regarding the employer's collection and remittance of payments under the program;

(C) Providing information to the State (or the designated governmental agency or instrumentality described in paragraph (h)(1)(ii) of this section) necessary to facilitate the operation of the program; and

(D) Distributing program information to employees from the State (or the designated governmental agency or instrumentality described in paragraph (h)(1)(ii) of this section) and permitting the State or such entity to publicize the program to employees;

(ix) The employer contributes no funds to the program and provides no bonus or other monetary incentive to employees to participate in the program;

(x) The employer's participation in the program is required by State law;

(xi) The employer has no discretionary authority, control, or responsibility under the program; and

(xii) The employer receives no direct or indirect consideration in the form of cash or otherwise, other than the reimbursement of the actual costs of the program to the employer of the activities referred to in paragraph (h)(1)(viii) of this section.

(2) A State savings program will not fail to satisfy the provisions of paragraph (h)(1) of this section merely because the program—

(i) Is directed toward those employees who are not already eligible for some other workplace savings arrangement;

(ii) Utilizes one or more service or investment providers to operate and administer the program, provided that the State (or the designated governmental agency or instrumentality described in paragraph (h)(1)(ii) of this section) retains full responsibility for the operation and administration of the program; or

(iii) Treats employees as having automatically elected payroll deductions in an amount or percentage of compensation, including any automatic increases in such amount or percentage, specified under State law until the employee specifically elects not to have such deductions made (or specifically elects to have the deductions made in a different amount or percentage of compensation allowed by the program), provided that the employee is given adequate notice of the right to make such elections; provided, further, that a program may also satisfy this paragraph (h) without requiring or otherwise providing for the automatic elections described in this paragraph (h)(2)(iii).

(3) For purposes of this section, the term State shall have the same meaning as defined in section 3(10) of ERISA.

Phyllis C. Borzi,
Assistant Secretary, Employee Benefits Security Administration
U.S. Department of Labor

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