STATE OF CONNECTICUT

RETIREMENT SECURITY BOARD

CO-CHAIRS: STATE COMPTROLLER KEVIN LEMBO & STATE TREASURER DENISE NAPPIER

January 7, 2016

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

Re: Proposed Rule on Savings Arrangements Established by States for Non-Governmental Employees, RIN 1210-AB71

Dear Assistant Secretary Borzi:

We write to provide comments on the proposed rule (80 Fed. Reg. 72006 (Nov. 18, 2015), the "Proposed Rule") setting forth a safe harbor describing circumstances in which a payroll deduction savings program, including one with automatic enrollment, would not be considered an employee pension benefit plan under the Employee Retirement Income Security Act of 1974, as amended ("ERISA").

The Connecticut Retirement Security Board ("CRSB") was created by statute to study the feasibility of, and to develop a proposal for, the implementation of a state workplace savings initiative in Connecticut. The CRSB's goals include studying the feasibility of, and designing, a proposal for a state-run program that would increase access to enrollment to a quality retirement program.

The CRSB is strongly supportive of the Department's efforts to facilitate state-based retirement initiatives to increase private-sector employees' access to retirement savings programs. The proposed rule provides much needed clarity and should be finalized expeditiously. We further urge the Department to ensure the final rule provides state governments with flexibility to design programs that best match the needs of their citizens. Below, we provide general comments on the Proposed Rule and specific recommendations.

I. General Comments

A. Support for the Proposed Rule

Approximately 41% of the Connecticut workforce – almost 600,000 working people – lack access to a retirement plan at the workplace.[1] People without access to a plan are considerably less likely to save for retirement, raising the risk that they will not have a nest egg to support them when they are no longer able to work. The lack of retirement preparedness will have significant costs for families and the state programs providing assistance to poor or near-poor retirees.

The Connecticut legislature created the CRSB to develop a proposal for a state-sponsored workplace savings initiative to expand retirement program coverage and improve retirement preparedness.[2] The proposal and the recommendations of the CRSB will be the basis for subsequent legislation implementing such a program. The CRSB's mandate contemplates a proposal that does not result in liability for the State and is not pre-empted by ERISA.

In developing its proposal, the CRSB heard from experts about the perceived lack of clarity regarding the interaction of state and federal law. In particular, experts told the Connecticut General Assembly and the CRSB that there is a potential for a state law expanding coverage along the lines contemplated by the CRSB's mandate to be preempted by ERISA.[3]

The CRSB applauds the Department for clarifying the legal status of state payroll deduction savings programs under ERISA. The Proposed Rule provides certainty and guidance for both the CRSB and the Connecticut legislature in crafting and implementing a program, and will greatly reduce the risk that any state payroll deduction savings program established by Connecticut will be preempted.

B. Need for Flexibility

Connecticut has a unique workforce with unique needs. Consequently, the CRSB is developing a proposal for a state payroll deduction savings program that is specifically tailored to the needs of the citizens of Connecticut, which may be different from the needs of citizens of other states. In particular, the program will be set against the backdrop of existing workplace payroll regulation (*e.g.*, regulatory oversight and monitoring of payroll deductions and the constitutional, statutory, regulatory and administrative structures in place that bear on such a program). In addition, the State is sensitive to overburdening employers, particularly small employers, with statutory mandates. Thus, we urge the Department to recognize the advantages of state-specific approaches and not unduly limit the states' flexibility in designing and implementing state workplace savings initiatives.

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[1] Schwartz Center for Economic Policy Analysis, *Are Connecticut Workers Ready for Retirement?*, 5 (Apr. 2013).
[2] Public Act 14-217.
[3] Meeting of CRSB (Feb. 4, 2015) (testimony of Brian Graff, on behalf of American Society of Pension Professionals and Actuaries); Hearing on S.B. 249 Before the Labor and Public Employees Committee (Ct. 2014) (statement of Insurance Association of Connecticut).

In that regard, the CRSB believes that some of the conditions of the Proposed Rule are not necessary to determine whether a program is covered by ERISA.[4] (We discuss these conditions in part II of this letter.) The CRSB recognizes that many of the conditions in the Proposed Rule are well intentioned and designed to encourage robust consumer protections. However, Connecticut and other states have a unique and pre-existing representational interest in the health and welfare of their citizens, so it is unnecessary for the Department to include such conditions. In fact, including extraneous conditions may actually undermine the Department's policy objectives by hampering states' ability to design flexible and custom-tailored programs.

C. Timing of Rule Finalization

The Department should finalize the Proposed Rule as soon as possible. The CRSB is currently preparing an implementation plan for consideration by the Connecticut legislature by the statutorily required deadline of April 1, 2016. It is hoped that enabling legislation can be adopted before the legislature adjourns in May 2016. Connecticut has been in the vanguard in advancing improvements in meeting the health and welfare needs of its population (*e.g.*, state-sponsored health insurance exchanges, Medicaid expansion, and 529 plans) and may well show a path forward in this area as well. Consequently, the CRSB and, we understand, state legislatures all over the country, have a pressing need for final rules. That need is exacerbated by the fact that, in issuing the Proposed Rule, the Department significantly limited the ability of states to rely on the existing payroll deduction IRA safe harbor.

II. Comments Relating to the Proposed Rule's Conditions

A. Allow Voluntary Automatic Enrollment in Payroll Deduction Savings Programs

The CRSB believes that the Proposed Rule should be amended to provide that all employers may automatically enroll their employees in a state payroll deduction savings program, regardless of whether they are required to do so or not.

One of the conditions of the Proposed Rule is that "the employer's participation in the program is required by state law."[5] Thus, the safe harbor would not apply to an employer who voluntarily participates in state- payroll deduction savings program with automatic enrollment.[6] The Department's rationale is that the employer's act of automatically enrolling its employees is sufficient to trigger ERISA because it makes the program no longer "voluntary" for employees.

The CRSB disagrees with the Department's position that an employer's decision to participate in a state payroll deduction savings program providing for automatic enrollment would make the program subject to ERISA for two reasons. First, all of the programs being

[4] For example, the Proposed Rule would prohibit a state from imposing limits on employees' withdrawals of funds beyond those imposed by the Internal Revenue Code and may limit the states' ability to delegate administrative authority. 80 Fed. Reg. at 72014.
[5] 80 Fed. Reg. at 72014.
[6] *Id.*

considered by states, including Connecticut, would, in actuality, be voluntary for employees. Employees would have the absolute right to opt out at any time. In fact, the Proposed Rule requires that right be protected.[7] Second, states are simply making a design choice to include automatic enrollment in their programs. Employers electing to make the programs available would do so on an as-is basis, would not have control over the programs' design, and would not be running a "plan" of any kind. The employer's role would be entirely ministerial, regardless of whether the program provides for automatic enrollment, and as the Department has routinely recognized, employers are permitted to take ministerial actions with respect to savings programs without triggering ERISA.[8]

The Department cites case law for the proposition that participation in a plan is not "voluntary" if the participant is automatically enrolled in the plan. However, none of the cases cited are relevant to payroll deduction IRAs with automatic enrollment. Some of these cases do not concern coverage under Title I of ERISA,[9] and others deal solely with the Department's welfare plan safe harbor.[10]

The limitation on an employer's voluntary participation in a state payroll deduction savings program with automatic enrollment raises a host of administrative concerns. Whether or not an employer is mandated to participate in a state-sponsored payroll deduction savings program could vary based on factors largely outside of the employer's control. For example, the CRSB is considering recommending that only employers of a certain size or with a minimum number of employees be required to participate in the State's program. It is also considering who should be considered an "employee," how best to count "employees," and whether some exemptions should be available. That means whether or not an employer is required to participate could change if a single employee decides to quit. After the employee's separation from service, would the program and/or the employer suddenly be subject to ERISA? And would the employer need to un-enroll its employees? The CRSB is concerned that such technically challenging questions will derail establishment of a program.

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[7] The Proposed Rule would require a program providing for automatic enrollment to operate similar to provisions in federal law, including 26 U.S.C. § 401(k)(13)(E) (Qualified Automatic Contribution Arrangement under the Internal Revenue Code ("Code")) and 29 C.F.R. § 2550.404c–5(d) (Qualified Default Investment Alternatives under ERISA). 80 Fed. Reg. at 72010 n. 15.

[8] *See, e.g.*, 29 C.F.R. § 25109.99-1 (employers may select IRA sponsors to which employees direct payroll contributions, provide educational material, and answer questions); DOL Advisory Opinion 2001-03A (Feb. 2001) (employers may approve a plan for allocation of demutualization proceeds among IRA participants from group annuity contracts); DOL Advisory Opinion 90-20A (June 15, 1990) (employer may act as trustee to IRA); DOL Advisory Opinion 85-53A (Oct. 4, 1985) (employers may expend funds to educate staff on implementation of the IRA); DOL Advisory Opinion 83-10A (Feb. 9, 1983) (employers may establish escrow account to receive employee payroll deductions). *See also* DOL Field Assistance Bulletin 2006-2 (Oct. 27, 2006); DOL FAB 2004-1 (Apr. 7, 2004) (an employer's automatic enrollment of its employees into a Health Savings Account does not make the account involuntary and subject to ERISA).

[9] 80 Fed. Reg. at 72008 n. 12 (citing *Doe* v. *Wood Co. Bd. Of Educ.*, 888 F.Supp.2d 771, 775–77 (S.D. W. Va. 2012); *Schear* v. *Food Scope America, Inc.*, 297 F.R.D. 114, 125 (S.D.N.Y. 2014).

[10] 80 Fed. Reg. at 72008 n. 12 (citing *Thompson* v. *Unum Life Ins. Co.*, No. Civ.A. 3:03–CV–0277–B, 2005 WL 722717, *6 (N.D. Tex. Mar. 29, 2005); *The Meadows* v. *Employers Health Ins.*, 826 F. Supp. 1225, 1229 (D. Ariz. 1993); *Davis* v. *Liberty Mut. Ins. Co.*, Civ. A. No. 87–2851, 1987 WL 16837, *2 (D.D.C. Aug. 31, 1987).

Not allowing employers to voluntarily choose to participate in a state payroll deduction savings program with automatic enrollment undercuts the states', and the Department's, objective of expanding access to a workplace retirement savings programs. Although some states may decide not to require certain employers to participate in their programs, it is in the best interest of working people to allow those employers the option of participating and using automatic enrollment. There is no question that automatic enrollment significantly increases retirement savings rates.[11] And given that states have a unique representational interest in the health and welfare of their citizens, there is no reason to think that the consumer protections provided under state law would be any less robust than those provided under ERISA.

Lastly, while the CRSB sees a state interest in ensuring that employers that are required to participate do participate, it does not see a state interest in ensuring that *only* employers required to participate do participate. The CRSB is not currently contemplating an enforcement regime that would exclude employers from participating.

B. Withdrawal Limitations

The Department should amend the Proposed Rule to provide that certain reasonable limitations or restrictions on the ability of employees to withdraw from a state payroll deduction savings program are permissible. The Proposed Rule would prevent states from requiring any employee or beneficiary covered by a program to retain any portion of contributions or earnings in his or her IRA and would prevent the state from providing for any restrictions on withdrawals beyond those already imposed by federal law applicable to IRAs.[12]

At the outset, the CRSB notes that this condition of the Proposed Rule is not relevant to the determination of whether the program would be subject to ERISA and the Department's stated goal of crafting conditions that would limit employer involvement. There is simply no nexus between these lockups and employer behavior.

To the extent the Department believes that the condition is necessary, the CRSB urges the Department to permit reasonable withdrawal limitations, provided they benefit participants by creating efficiencies in program operations. For example, reasonable restrictions may be advisable to prevent frequent and repeated withdrawals, which may increase the administrative costs borne by participants, including those that do not make such withdrawals. The Department has already recognized the utility of withdrawal restrictions in its regulations under section 404(c) of ERISA, which allow reasonable restrictions on the frequency with which participants and beneficiaries may give investment instructions.[13]

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[11] Employee Benefit Research Institute, *The Impact of Automatic Enrollment in 401(k) Plans on Future Retirement Accumulations: A Simulation Study Based on Plan Design Modifications of Large Plan Sponsors* (Apr. 2010), *available at* https://www.ebri.org/pdf/briefspdf/EBRI_IB_04-2010_No341_Auto-Enroll1.pdf; Defined Contribution Institutional Investment Association, *DCIIA Plan Sponsor Survey 2014: Focus on Automatic Plan Features* (June 2015), *available at* https://www.transamericacenter.org/docs/default-source/resources/tcrs2015_wp_dciia_plan_sponsor_survey.pdf.

[12] 80 Fed. Reg. at 72014.

[13] 29 C.F.R. § 2550.404c-1(b)(ii)(C).

The prohibition on withdrawal restrictions may also decrease states' flexibility to offer beneficial investment options. The programs are intended to be long-term savings vehicles, and for most participants, there will not be a need for immediate liquidity. Consequently, states may wish to consider strategies that improve returns by utilizing assets and vehicles that perform best and at lowest cost when reasonable liquidity limitations are permitted. States may also wish to offer investment vehicles that require such liquidity limitations for lower costs and better results, in the way that many funds impose load charges for rapid in-and-out movements.

The Proposed Rule may also limit the states' ability to include lifetime income distribution options. The CRSB is required by law to include in its proposal for a state workplace savings program the provision of annuitized benefits.[14] The CRSB is concerned that the Proposed Rule could unduly limit Connecticut's ability to purchase guarantees or annuities that impose withdrawal restrictions or penalties on early cash outs. As the Department has recognized, lifetime income options such as annuities may ensure employees' "savings last throughout their retirement years."[15]

C. Delegation of Responsibilities

The Department should clarify the meaning of the condition that the states retain "full responsibility" for the operation and administration of the program upon a delegation of their authority. The Proposed Rule would allow states to utilize one or more service providers to operate and administer their programs, provided that the state or designated agency or instrumentality "retains full responsibility for the operation and administration of the program."[16] We understand that the Department intended to allow states to delegate portions of the management and administration to third parties. However, we are concerned that the requirement that the state retain "full responsibility" may be interpreted as prohibiting states from delegating legal responsibility for program investments and/or administration. Such a result would be unnecessarily burdensome to states and is inconsistent with ERISA, which expressly permits the delegation of legal authority.[17] It may be that a state's program is managed and administered by a state agency, in a manner similar to a state employee retirement system, in which case the state would assume responsibility. But it may also be that a state designs its program to be managed and administered by an established third party, such as any of the existing IRA providers, to take advantage of economies of scale and save on start-up costs.

In addition, many states will be concerned that retaining "full responsibility" will make them a guarantor of the fidelity of third party providers and employers. The CRSB respectively submits that any such risk has the potential to derail establishment of the programs being contemplated.

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[14] 2014 Conn. Pub. Acts. 14-217 § 185(8).
[15] Request for Information Regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans, 75 Fed. Reg. 5253, 5254 (Feb. 2, 2010).
[16] 80 Fed. Reg. at 72014.
[17] *See, e.g.*, ERISA §405(d).

The approach taken by the Internal Revenue Service ("IRS") with regard to governmental plans qualified under section 457(b) of the Code is instructive. The IRS has stated that a plan may be considered "established and maintained" by a government employer under section 457(b) so long as the governmental employer adopts the plan for the benefit of the employees it will cover, despite the fact that a union is responsible for the administration of the plan.[18] Thus, the IRS has expressed a view that the government need not retain "full responsibility" for the administration of a plan it has established and maintained.

For these reasons, the CRSB submits that this language be modified to require state oversight but not state responsibility, unless the state assumes responsibility for the management and administration of the program directly.

D. Connection Between States and Covered Employers and Employees

The Department solicited comments on whether the safe harbor that would be provided by the Proposed Rule should require some connection between a state and employees covered by a state payroll deduction savings program, and if so, what kind of connection.[19] The CRSB believes that the Department's final rule should not provide such a requirement. States should be given the flexibility to design programs, including the flexibility to decide the extent to which employees of the state and employees employed within the state will be covered. To allow states to design their own coverage rules could engender helpful competition among the states, which would increase the quality of services. In addition, if a prescriptive rule is avoided, states could enter into regional relationships, which may allow the delivery of more efficient services, to drive down the expenses of the programs charged to employees. Further, the Department need not establish its own limitations, as the United States Constitution already places limits on the ability of states to regulate extraterritorial conduct.[20]

E. Timing of Employers' Compliance

The Department should clarify that providing an employer with discretion to delay participation in a state payroll deduction savings program, for example, to allow staggered participation into the program or to allow employers time to integrate their payroll systems into the program will not be an impermissible act of discretion causing the program to be subject to ERISA. Employers using ADP, for example, may have compliance capability at a time that is different than employers using an FSET provider.

The conditions set out in the Proposed Rule would limit employers to several discrete activities, such as collecting and remitting employee contributions.[21] The Department explains in the Preamble to the Proposed Rule that limited employer involvement is the "key" to the

[18] Rev. Rul. 2004-57 (2004).
[19] 80 Fed. Reg. at 72009.
[20] *Healy v. Beer Inst., Inc.*, 491 U.S. 324, 336 (1989); *Allstate Ins. Co. v. Hague*, 449 U.S. 302, 310 (1981).
[21] 80 Fed. Reg. at 72014.

determination that the program is not subject to ERISA, and thus, employers may not have any discretion or control with regard to the program.[22]

The CRSB and, we understand, certain other states are considering offering employers a choice with regard to the timing of implementation of their programs. Depending on the employers' size, current payroll infrastructure and operational processes, or for other reasons, the speed at which employers will be able to bring the state-run program online may vary. Thus, employers may be permitted to elect their compliance date. The CRSB believes that offering employers a choice in this regard is not the type of discretion that would cause a state-run program to become subject to ERISA.

F. Employer Involvement in Information Collection Relevant to Enforcement

The Department should confirm that a state's requirement that employers participate in the state's information collection and enforcement activities should not be an impermissible act of discretion causing the state payroll deduction savings program to be subject to ERISA. The Proposed Rule provides that a state-run program will not become covered by ERISA if the employer's involvement is limited to, among other things, providing information to the state or designated governmental agency or instrumentality necessary to facilitate the operation of the program.[23] We interpret this provision as extending to allow employers to provide information necessary for a state's enforcement activities. For example, a state may require employers to affirm that they have enrolled all employees who are required to be enrolled in the program. Employers may also be required to provide information to the state, or a designated agency, upon an audit. The CRSB believes that these activities should not cause a state-run program to be subject to ERISA. We note that states typically have an established information gathering and auditing function to review compliance with existing payroll deduction, tax collection and workplace insurance requirements.

G. State Responsibility for Security of Payroll

The Department should clarify the meaning of the requirement that states assume responsibility for the security of payroll deductions and employee savings. As noted above with respect to retaining responsibility for management and administration of the program, states may be concerned about the meaning of this requirement and the potential for indirectly guaranteeing the fidelity of providers and employers. In particular, the Connecticut legislature required that the payroll deduction savings program not result in the state incurring debts or liabilities. Would "responsibility" for security of payroll deductions and employee savings imply liability to the state?

The CRSB respectfully submits that the Department limit this responsibility to plans where the state has assumed responsibility to handle payroll deductions and employee savings, or, in the alternative, provide an alternative if (i) the payroll deduction, wage theft and similar laws that apply to payroll deductions in general apply to the same extent to payroll deductions

[22] 80 Fed. Reg. at 72010.
[23] 80 Fed. Reg. at 72014.

under the state's payroll savings program and (ii) the state's laws that protect savings in IRAs in general also apply to the employee accounts under the state's payroll savings program.

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The CRSB appreciates the opportunity to comment on the Proposed Rule and again commends the Department on its work to improve access to the retirement system. We would be happy to discuss any questions relating to this comment letter or any issues relating to the Proposed Rule further.

Very truly yours,

Kevin Lembo
Co-Chair, CRSB

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