AMERICAN BENEFITS COUNCIL

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Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N–5655
U.S. Department of Labor
200 Constitution Avenue N.W.
Washington, D.C. 20210

Re: RIN 1210-AB71 and RIN 1210-AB74

Comments on Proposed Rule Regarding Savings Arrangements Established by States for Non-Governmental Employees and Related Interpretive Bulletin

Dear Sir or Madam:

The American Benefits Council ("Council") appreciates the opportunity to provide comments on the Department of Labor's ("Department") proposed rule regarding IRA savings arrangements established by states for non-governmental employees ("state-run arrangements").[1] In addition, we offer brief comments on Interpretive Bulletin 2015-02 ("IB 2015-02"),[2] which addresses state savings programs that sponsor or facilitate plans covered by the Employee Retirement Income Security Act of 1974 ("ERISA") and was published on the same day as the proposed rule.

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either directly sponsor or provide services to retirement and health plans that cover more than 100 million Americans.

[1] 80 Fed. Reg. 72,006 (Nov. 18, 2015).
[2] 80 Fed. Reg. 71,936 (Nov. 18, 2015).

The Council and its members have long supported the Department's work to expand access to retirement saving opportunities for workers. Given the voluntary nature of our employment-based retirement system, the Department's past efforts to reduce the administrative burdens and costs of sponsoring a pension plan have been especially important in encouraging employers to offer (and to continue to offer) retirement plans for their employees. In this regard, the Council is deeply concerned that the Department's proposal for a new safe harbor to accommodate state-run arrangements will, as currently designed, take a significant step backward by undermining the current retirement system and increasing the costs and complexity for employers that maintain retirement plans.

One of the fundamental reasons that Congress had for passing ERISA was its determination that employers who choose to offer a pension plan to employees should only be subject to a single statutory and regulatory regime under federal law – not a multitude of regimes under state laws that would inevitably vary from state to state. As illustrated in more detail below, the Department's proposed safe harbor for state-run arrangements runs contrary to this fundamental purpose of ERISA. The Council respectfully urges the Department to reconsider the proposal's effect in this regard and take steps, such as those we suggest below, to ensure that this important aspect of our retirement system is upheld.

Although we understand the concerns that have led states to explore developing state-run arrangements and similar programs for private-sector workers, great care must be taken so that any accommodations made by the Department for these savings programs – which are generally intended to target small businesses – not adversely affect the savings opportunities for employees of existing plan sponsors, or serve to discourage growing employers from ever offering plans. We strongly support the Department's acknowledgment that ERISA-covered programs have several advantages over the state-run arrangements, including the opportunity for employer contributions and higher contribution limits.[3] While expanding access to retirement savings arrangements is a worthy goal, an effort that does so at the expense of employees who are currently covered under a more robust ERISA-covered plan should not be an acceptable outcome. Yet, this would be the result under the current proposal.

As described below, we believe that certain modifications to the proposed safe harbor would allow the Department to help facilitate the state-run arrangements while also protecting current plan sponsors from onerous state regulations and protecting current plan participants from losing the benefits of their ERISA-covered plan.

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[3] 80 Fed. Reg. 72,012.

SUMMARY OF THE COUNCIL'S COMMENTS ON THE PROPOSED RULE AND IB 2015-02

As explained in more detail below, the Council has the following comments on the proposed rule and IB 2015-02.

1. As drafted, the proposal will result in significant new burdens on plan sponsors by allowing states to subject them to employer mandates despite that fact that they already offer a retirement plan. Moreover, the proposal will subject plan sponsors and other employers to multiple – and even conflicting – state-run arrangement regimes. In order to better ensure that the Department's facilitation of state-run arrangements does not undermine the current retirement system, we recommend that the Department add three additional conditions to the safe harbor that would (1) protect current plan sponsors from additional burdens and expense; (2) give employers an option to avoid being subject to multiple state regimes; and (3) help eliminate situations where an employer could be subject to conflicting state regimes with respect to the same employee. Our suggestions for these additional conditions are described below.

2. If a state engages a service provider to administer all or part of its state-run arrangement, it is unclear whether the state could be liable under the Internal Revenue Code's ("Code") prohibited transaction excise tax regime. Due to states' concern with understanding and mitigating their potential liabilities under federal law (through, for example, conditioning the implementation of a program on the avoidance of such liabilities), states should be aware that the Department's proposed safe harbor, while providing an exemption from ERISA coverage, does not address potential related liabilities under the Code. Guidance from the Treasury Department is required in this regard.

3. Availability of the safe harbor should not be conditioned on a state mandating employer participation. Given the numerous other proposed conditions aimed at minimizing employer involvement, an employer mandate should not be considered necessary to avoid ERISA's application with respect to a state-run arrangement. If the Department retains the condition that employer involvement be required, the safe harbor will result in states inappropriately broadening the scope of employers that fall within the mandate. It will also eliminate a state's ability to use a flexible program design that would allow certain employers that fall outside the mandate to choose to participate.

4. I.B. 2015-02 creates an unfair playing field between the private sector and states acting as market participants by providing that a state-sponsored "open" multiple employer plan ("MEP") will be treated as a single ERISA plan without affording the same treatment for private-sector open MEPs. We request that the Department provide equal treatment for both state-sponsored and private-sector open MEPs.

5. The Department should provide a formal opportunity for notice and comment on IB 2015-02 because the guidance will have a significant impact on many stakeholders.

DETAILED COMMENTS

1. Additional safe harbor conditions are necessary to prevent state-run arrangements from undermining the current retirement system by subjecting plan sponsors to significant burdens and multiple and conflicting state regimes.

Under the proposed rule, a state-run arrangement[4] would not be considered an "employee pension benefit plan" or "pension plan" under ERISA if multiple conditions designed to ensure minimal employer involvement with respect to the arrangement are met. The Council is very concerned that the Department has not taken steps through its drafting of the safe harbor's proposed conditions to ensure that, while providing states with their desired ERISA relief, the state-run arrangements do not interfere with the workings of the existing retirement system that is currently providing benefits to millions of Americans.

Many commenters assume that medium and large employers will continue to maintain 401(k) plans regardless of the regulatory environment. This is not accurate in our view, just as the same assumption regarding defined benefit plans from many years ago has proved to be incorrect. Companies are extremely focused on managing risks and costs. At the same time, the costs and potential liabilities associated with 401(k) plans are increasing rapidly. In the last several years, we have, for the first time, heard some large companies discuss interest in finding a way to deliver retirement benefits without the costs and fiduciary risks of the current system; if there was an alternative to maintaining a plan, they might well use it.

The proposal needs to be viewed in this context. As discussed below, if the proposal were adopted in its current form, large multi-state companies could be facing a nightmare of different and possibly conflicting state laws. If maintaining a plan were to exempt the employer from such a nightmare, that would be a powerful incentive to retain their plan. If maintaining a plan does not provide an exemption, then the cost and risks of retirement benefits for large companies would skyrocket, leaving cost-conscious companies with a very attractive alternative. Since they are subject to state mandates to participate in state-run arrangements regardless, why not reduce costs by just using the state plans?

The states that have considered or passed legislation to establish state-run arrangements (or similar programs) are generally prohibiting such arrangements from

[4] The proposal generally describes a state-run arrangement in part as consisting of an individual retirement plan established and maintained by a state pursuant to a payroll deduction savings program.

being implemented unless and until certain assurances are received that such arrangements will not be subject to ERISA. While the Department is in a position to provide some assurance in this regard (through, for example, the creation of the proposed safe harbor), the Department is also in a position to require that such relief only be made available to state-run arrangements that do not unnecessarily interfere with and burden existing plan sponsors and plan participants. The Council respectfully urges the Department to use its position with this latter goal in mind, too.

Concerns with the Proposed Safe Harbor

As illustrated in the points below, the proposed safe harbor fails to protect current plan sponsors from additional costly burdens and fails to protect all employers (whether a current plan sponsor or not) that have employees who work and/or reside in multiple states from multiple and even conflicting state-run arrangement regimes. Consider, for example, the state-run programs that have passed in California,[5] Illinois,[6] and Oregon.[7] With minimal changes, each of these state programs could likely meet the conditions of the Department's proposed safe harbor. Yet, in the absence of additional state guidance, the following issues are very likely to arise depending on how each state ultimately decides to interpret and implement its own statute:

- **Current plan sponsors could be subject to state-run arrangement employer mandates**. The California, Illinois, and Oregon statutes would each mandate participation by certain employers. Although the mandates may not apply to employers that already offer an employer-sponsored retirement plan, this point is unclear. The Council's plan sponsor members are very concerned that the statutes could be interpreted by states as applying the mandate to employers that do not currently cover 100% of their employees under the plan. In fact, the treasurer of Illinois stated at a Council meeting that this point is unclear in the Illinois statute and that it would be up to the Illinois program's board to determine the precise scope of the employer mandate.

  It goes without saying that an employer that offers a 401(k) plan to 95% of its employees (but excludes, for example, the 5% of its employees who are temporary employees or are not yet eligible for participation) would be burdened by an additional requirement that the employer enroll the remaining 5% of its employee population in a state-run arrangement. For example, not only would the employer be responsible for understanding and carrying out its responsibilities under the state-run arrangement (on top of its many duties with respect to the 401(k) plan), but the employer would also be forced to constantly monitor and switch employees between the state-run arrangement and 401(k)

[5] S.B. 1234. *See also* S.B. 923, which requires a subsequent authorizing statute before the California program may be fully implemented.
[6] S.B. 2758.
[7] H.B. 2960.

program as employee eligibility for the 401(k) plan changes. In addition, some state proposals may be interpreted such that even an employer that offers a 401(k) plan to 100% of its employees, 95% of whom are participating, could be subjected to a requirement to enroll the remaining 5%, even though those individuals may have previously opted out of the plan. At some point, those additional burdens will inevitably discourage employers from continuing to offer an ERISA-covered plan.

An additional concern raised by the California, Illinois, and Oregon statutes is that current plan sponsors may be exempted from mandatory employer participation only if they offer a certain type of plan, a certain level of benefits, or certain features (e.g., automatic enrollment, or automatic enrollment at a certain default contribution level). In these states, for example, the plan offered by the employer must be tax-qualified under specific Internal Revenue Code sections to avoid the mandate. Similarly, the Oregon statute mandates employer involvement unless the employer "obtain[s] an exemption" because it offers a qualified plan. The fact that the employer exemption for offering a qualified plan is not automatic highlights plan sponsors' concerns that there is nothing stopping Oregon (or any other state) from further conditioning the exemption based on plan particulars. As drafted, the proposed safe harbor does nothing to prevent such interference by a state in the plan design choices that are afforded plan sponsors under federal law.

- **Employers will be subject to *multiple* state-run arrangement regimes**. Another issue that the state-run arrangements present for employers is that employers with operations and employees in multiple states will inevitably be subject to multiple state regimes. This concern will disproportionately affect large employers and current plan sponsors, who are much more likely to operate across state lines than the generally smaller employers who do not sponsor an ERISA-covered plan. At worst – though certainly not inconceivable – the Department's proposal could subject a large plan sponsor with stores and employees in every state to just as many state-run arrangement regimes. This would be an extraordinary burden for plan sponsors, whose only option to reduce their burden would be to terminate their ERISA-covered plan. It should be noted that in effect this places a plan sponsor in the position of choosing between an optimal, higher savings allowance for its employees such as that afforded in a 401(k) plan, and an arrangement with a lower savings maximum that provides the employer with assurance of no fiduciary responsibility or liability under ERISA.

- **Employers will likely be subject to *conflicting* state-run arrangement regimes**. Even worse than our concern that plan sponsors will be required to participate in multiple state-run arrangements is the very real likelihood that employers could be subject to *conflicting* state-run arrangement regimes *with respect to the same* *employee*. In this regard, the Department appears to have recognized this potential for conflict by acknowledging that the proposal does not address whether the employees that participate in the state-run arrangement must be employed within the state that establishes the program or must be residents or employed by employers doing business within the state.[8] The Department requested comments specifically on whether the safe harbor should be limited to require some connection between the employers and employees covered by the state-run arrangement.

Our response to the Department's question is yes, the safe harbor should be conditioned on the state-run arrangement limiting its applicability to certain employees. Consider the implications of a situation where Employee A resides in State X and works for Employer B in State Y. Employer B has operations in both State X and State Y. State X requires that all employers with operations in State X automatically enroll employees who *reside* in State X in State X's state-run arrangement at a 3% contribution rate in a target date fund. State Y requires that all employers with operations in State Y automatically enroll employees who *work* in State Y in State Y's state-run arrangement at a 4% contribution rate in a balanced fund. Consequently, Employer B faces conflicting requirements with respect to the same Employee A. The proposed rule must prevent this result.

Suggestions for Additional Conditions to Improve the Proposed Safe Harbor

In light of the above concerns we have with the Department's proposed rule, we urge the Department to add the following conditions to the proposed safe harbor:

- The program specifically exempts from mandated participation, with respect to all of an employer's employees, employers that offer a qualified plan to employees (i.e., the exemption would apply even if less than 100% of the employer's employees participate or are eligible to participate in the plan, as long as any applicable nondiscrimination rules in the Internal Revenue Code are met);

- If the Department does not adopt this first suggestion, meaning states could mandate participation with respect to employers that offer a qualified plan that does not cover 100% of employees at all times (a course we strongly believe will severely undermine the employment-based retirement system), then at a minimum the mandate should not apply to any employee offered any alternative savings vehicle, including a payroll deduction IRA (whether or not automatic enrollment is involved and whether or not the arrangement is subject to ERISA);

[8] 80 Fed. Reg. 72,009.

- The program allows employers that are subject to multiple state-run arrangement participation requirements (due to operations/employees in multiple states) to select a single state-run arrangement in which it will enroll all employees subject to any state's mandate.[9] [For example, Employer C has 10 employees that work in State V and 30 employees that work in State W. Both states require that Employer C automatically enroll employees that work in their state in their respective state-run arrangements. Employer C chooses to enroll all 40 employees in State W's state-run arrangement, which satisfies the participation requirement for both State V and State W.]; and

- The program's mandatory employer participation only applies to employees who are residents of the state, and an employer should be allowed to rely for this purpose on the employee's most recent communication to the employer regarding state residence.

By adding the above conditions to the proposed safe harbor, the Department would be taking a significant step toward ensuring that its facilitation of state-run arrangements does not undermine the current retirement system and lead to a reduction in ERISA-covered plans.

In addition to making the changes suggested above, the Council asks that the Department coordinate with the Treasury Department to ensure that employers subject to a state-run arrangement have no liability with respect to ensuring that employees do not exceed the IRA contribution limits. Employers should not be expected to monitor whether, for example, an employee has other employment where the other employer is also required to remit IRA contributions on behalf of the same individual (regardless of whether the same or different state-run arrangements are involved). Similarly, for state-run arrangements that utilize a Roth IRA, employers should have no liability with respect to monitoring whether an employee is eligible to contribute to a Roth IRA.

2. Uncertain state liability with respect to the Internal Revenue Code's prohibited transaction excise tax regime must be addressed.

A common concern among states as they move forward with proposals to implement retirement solutions for the private sector (including state-run arrangements that may qualify for the Department's proposed safe harbor) is securing an understanding of and mitigating a state's potential liabilities under ERISA and the

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[9] The conditions currently proposed for the safe harbor (as well as the state proposals we have reviewed to date) are expected to produce state-run arrangements that generally provide similar savings opportunities from the perspective of the employee (e.g., the use of IRAs as the funding vehicle). As a result, the outcome for employees should not vary significantly if an employer with employees in multiple states is allowed to satisfy the employer mandate of multiple states by enrolling all employees subject to a mandate in a single state's program.

Code. A potential source of liability that we have not seen specifically identified by states is whether and how the prohibited transaction excise tax regime described in Code Section 4975 could apply to *states* that sponsor a state-run arrangement, even where such arrangements are exempt from ERISA. This issue is particularly relevant for states that engage the help of service providers, which we expect might be a common practice as states implement their proposals.

Code Section 4975 imposes a two-tiered excise tax on "any disqualified person who participates in the prohibited transaction (other than a fiduciary acting only as such)." Generally, the Code's prohibited transaction rules prohibit "disqualified persons" from using plan assets in transactions that involve a disqualified person or otherwise benefit a disqualified person, unless a specific exemption applies. If a prohibited transaction occurs, as just noted, Section 4975 provides that the excise tax will be paid by "*any disqualified person who participates in the prohibited transaction*" (emphasis added). For this purpose, disqualified persons include plan fiduciaries, who, for purposes of Code Section 4975, are defined in part as any person who exercises any discretionary responsibility in the administration of the plan.

Although the issue of whether a prohibited transaction has occurred falls under the jurisdiction of the Department, the issue of what it means for a disqualified person to "participate" in a prohibited transaction for purposes of the Code Section 4975 excise tax falls exclusively under the jurisdiction of the Treasury Department.[10] We raise this latter issue here to bring attention to the fact that, although a state may avoid ERISA-related liabilities with respect to its state-run arrangement by meeting the conditions of the Department's proposed safe harbor, states should not be led to believe that the Department's guidance addresses all potentially applicable fiduciary-related liabilities under federal law.

If a state oversees and approves – either by action or inaction – service provider activities that constitute a prohibited transaction, it is unclear whether the state's approval would constitute "participation" in the prohibited transaction. We believe the answer would be yes, but clarification from the Treasury Department is needed in order for states to be properly informed as to what their potential liability could be under the Code if they engage service providers to administer a state-run arrangement.

3. The safe harbor condition that employer involvement is mandatory should be eliminated.

The proposal would require, as a condition of using the safe harbor, that employer participation in the state-run arrangement be required by state law. The Department states that an employer mandate is necessary in order to limit employer involvement so as to avoid the state-run arrangement becoming an ERISA-covered plan. We ask that

[10] See Reorganization Plan No. 4 of 1978.

the Department reconsider its conclusion that employer participation must be required in light of the numerous other conditions of the proposed safe harbor that are designed to limit employer involvement. Under the 1975 payroll deduction IRA safe harbor, an employer – who is otherwise substantially limited in what activities he may engage in with respect to a payroll deduction IRA – may still choose whether to offer the arrangement or not. This result should not vary based on whether the arrangement permits automatic enrollment. That characteristic properly goes to whether a plan is "completely voluntary" or "voluntary" for an employee and should not be used as a material measure of how limited an employer's involvement is, especially in this case where the employer has no say in whether automatic enrollment is provided for under the state-run arrangement.

We ask that the Department reconsider the condition of mandatory employer participation for the following reasons. As an initial point, states that have considered state-run retirement programs have contemplated making employer participation both mandatory and voluntary. Some states may decide that making a program voluntary for all employers makes more sense. But in order for a state to take advantage of the Department's proposed safe harbor (which, for all practical purposes, will be necessary if the state provides for automatic enrollment), the Department's proposal will force the state to make employer participation mandatory. Alternatively, a state could avoid ERISA and keep its program voluntary for employers by meeting the terms of the 1975 payroll deduction IRA safe harbor, but then it would be forced to give up a provision for automatic enrollment.

As an additional matter, we are concerned that conditioning the safe harbor on mandatory employer participation will severely limit the ability of states to utilize helpful and more flexible designs with respect to a state-run arrangement. Several state proposals have contemplated mandatory participation for *certain* employers (e.g., employers with 25 or more employees who do not offer a retirement plan to any employees), but would make the program available on a voluntary basis for *other* employers (e.g., employers with fewer than 25 employees or employers that sponsor an ERISA-covered plan but would like to offer the state-run arrangement to employees not covered by the plan). If the safe harbor does not allow *any* employers to voluntarily participate, we are concerned that states will be forced to choose between (1) inappropriately expanding the employer mandate (e.g., requiring participation by all employers regardless of size or current plan sponsorship), and (2) denying employers not subject to the mandate the option to offer a state-run arrangement to their employees.

4. The Department should provide parity for state-run and private-sector "open" MEPs.

Under ERISA, a "pension plan" is defined in part as a plan that is established or maintained by an employer or an employee organization (or by both). Absent the involvement of an employee organization, the Department's long-held view has been that a plan to which more than one employer contributes (i.e., a "multiple employer plan" or "MEP") is treated as a single plan only when an employment-based common nexus exists among the employers that is unrelated to the provision of benefits. Absent that nexus, the Department views such a plan – commonly referred to as an "open" MEP – as a series of separate plans established and maintained by each participating employer. Due to the administrative efficiencies and cost-savings offered by MEPs (which benefit in particular smaller employers and their participants), employers have repeatedly asked Congress and the Department to treat open MEPs as a single plan for purposes of ERISA.

In IB 2015-02, the Department sets forth three approaches that states could use to expand retirement savings opportunities for workers through ERISA-covered plans without concern that such approaches would – in the Department's view – be preempted by ERISA. One approach would entail a state establishing a "'multiple employer' 401(k)-type plan, defined benefit plan, or other tax-favored retirement savings program" ("state open MEP"). The state would be the plan sponsor, named fiduciary, and plan administrator. The Department notes in IB 2015-02 that such an arrangement could reduce administrative costs for participating employers "in large part" because the Department would treat the state open MEP as a single ERISA plan (unlike its treatment of private-sector open MEPs).

The Department justifies its disparate treatment of private-sector open MEPs and state open MEPs by stating that a state has a "unique representational interest in the health and welfare of its citizens that connects it to the in-state employers that choose to participate in the state [open] MEP and their employees."[11] As a result, the Department reasons that the state should be "considered to act indirectly in the interest of participating employers" because of the unique nexus that distinguishes the state open MEP from a private-sector open MEP.[12]

The Council welcomes guidance from the Department that treats an open MEP as a single ERISA plan. However, we strongly object to the Department creating an unequal playing field by treating state open MEPs as a single ERISA plan without affording private-sector open MEPs the same treatment. The Department emphasizes in IB 2015-02 that the three approaches addressed in the guidance should not be preempted by ERISA in part because they contemplate a state acting as a market participant rather than as a regulator. When a state acts as a market participant, it should not receive preferential treatment that disadvantages the private sector. Yet this is precisely the result when the Department provides that state open MEPs – but not private-sector open MEPs – will be treated as a single ERISA plan. In this regard, we urge the Department to modify its previous position and allow private-sector open MEPs to be treated as a single plan. If the Department chooses not to take such action, then we ask

[11] 80 Fed. Reg. 71,939.
[12] *Id.*

that the Department retract the portion of IB 2015-02 that would permit state open MEPs due to the unfair competition that will result.

5. The Department should provide an opportunity for notice and comment with respect to IB 2015-02.

The Council appreciates the Department's use of notice and comment rulemaking with respect to its proposal for a new safe harbor for state-run arrangements. The proposal has significant implications for employers, employees, service providers, states, and other stakeholders, and an opportunity to provide input to help shape the final rule is a crucial part of the regulatory process.

In this regard, we are extremely concerned about the lack of both economic analysis and prior notice and opportunity for comment with respect to IB 2015-02. In particular, by allowing open MEPs only for state programs and thereby giving states a competitive advantage over private sector service providers, the Department is making a major policy change without the opportunity for public notice and comment by stakeholders. The avoidance of notice and comment in this manner appears to be clearly contrary to the Administrative Procedure Act and the Executive Orders governing regulatory actions. We ask that the Department withdraw IB 2015-02 and issue a proposed regulation with an economic analysis and the opportunity for public comment.

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Again, we appreciate the opportunity to provide comments on the Department's proposed rule and hope that the Department will consider our comments on IB 2015-02. If you have any questions or would like to discuss these comments further, please contact me at 202-289-6700.

Sincerely,

Jan Jacobson
Senior Counsel, Retirement Policy
American Benefits Council