ELIZABETH A. PEARCE
STATE TREASURER

RETIREMENT DIVISION
TEL: (802) 828-2305
FAX: (802) 828-5182

UNCLAIMED PROPERTY DIVISION
TEL: (802) 828-2407

ACCOUNTING DIVISION
TEL: (802) 828-2301
FAX: (802) 828-2884

STATE OF VERMONT
OFFICE OF THE STATE TREASURER

To: General Assembly

From: Beth Pearce, State Treasurer

Date: January 6, 2017

Re: Interim Study of the Feasibility of Establishing a Public Retirement Plan Required by Act 157 of the 2016 Legislative Session

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This report reviews findings and recommendations pursuant to Act 157 of the 2016 Legislative Session.[1] The State Treasurer, the Commissioner of the Department of Labor, the Commissioner of the Department of Disabilities, Aging & Independent Living, two appointees from the Committee on Committees, two appointees from the Speaker of the House, and one appointee by the State Treasurer formed the Public Retirement Study Committee (the Committee) to evaluate the feasibility of establishing a public retirement plan in Vermont.

The Committee has an overarching goal of increasing retirement security for all Vermonters.

The Committee recommends implementation of a "Voluntary open multiple employer plan (MEP)" supplemented by an open retirement marketplace for employees not covered by the "Voluntary open multiple employer plan (MEP)" or other existing retirement options. The Committee also recommends a three-year check-in (after the start-date of the program) where an analysis of participation and potential strategies to increase participation would take place.

Please note that the attached report, the "Review of Potential Public Retirement Plan Options for Private Sector Employees/Employers in the State of Vermont," (CRI Report)[2] was drafted for the purposes of the Public Retirement Study Committee by the Center for Retirement Initiatives (CRI) at Georgetown University and was authored by Angela M. Antonelli, Executive Director, and CRI's legal subject matter expert for this project, David Morse, Partner at K&L Gates. This report serves as a manual and guide to assist the Committee and the State in understanding the different options available.

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[1] Please note that Act 58 of 2015 amended Act 179 of 2014 and that Act 157 of 2016 amended both of those prior Acts, http://www.vermonttreasurer.gov/sites/treasurer/files/pdf/misc/ACT157%20As%20Enacted.pdf

[2] The Center for Retirement Initiatives (CRI), McCourt School of Public Policy, Georgetown University: "Review of Potential Public Retirement Plan Options for Private Sector Employees/Employers in the State of Vermont", (CRI Report) Available on CRI Webpage: http://cri.georgetown.edu/wp-content/uploads/2017/01/GeorgetownCRI_VermontPRSCReport.pdf

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Prior Work of the Committee

During 2014 and 2015 the Committee met on six occasions and collected resources regarding retirement security from a variety of sources including the Center for Retirement Initiatives (CRI) at McCourt School of Public Policy of Georgetown University, AARP, Vermont Main Street Alliance, Vermont Businesses for Social Responsibility (VBSR), Central Vermont Chamber of Commerce, American Council for Life Insurers (ACLI), National Institute on Retirement Security (NIRS), Vermont Bankers Association (VBA), Vermont State Employees' Association (VSEA), VSEA Retirees-Chapter, Vermont-National Education Association (VT-NEA), Assets & Opportunity Scorecard, Vermont Business owners, the U.S. Department of Labor (DOL), and other stakeholders.

For a detailed state-by-state comparison matrix of states that have enacted legislation, please see the attached Georgetown CRI matrix and presentation (linked online here: http://cri.georgetown.edu/state-briefs/).[3]

Existing Retirement Security Challenge

For a comprehensive summary of the retirement security challenge nationally and in Vermont please see section I of the attached CRI report.[4]

The Committee reviewed data from a variety of sources[5] and found that retirement savings for members of the public in Vermont are insufficient and that serious contemplation of a solution or measures to combat the problem of retirement security need to be taken.

An AARP study found that "about 45 percent of Vermont's private sector employees—roughly 104,000—work for an employer that does not offer a retirement plan. Significant numbers of workers at all levels of earnings and education do not have the ability to use payroll deductions to save for retirement."[6]

The U.S. Department of Labor (DOL) found that nationally: "approximately 68 million US employees do not have access to a retirement savings plan through their employers."[7]

It was identified that some barriers do exist for Vermont businesses, especially small businesses, in providing retirement plans to their employees. It was noted that some small businesses often do not have the time or capacity to provide retirement plans or guidance to their employees, of which some are part-time. It was also noted to the Committee that existing plans are available to individuals who do not have access to a plan through their employment.[8] Further it was noted to the Committee that many Vermont businesses do offer plans to their employees.

[3] Georgetown University, McCourt School of Public Policy, Center for Retirement Initiatives, *Comparison of Retirement Plan Design Features, By State: California, Illinois, Massachusetts, Oregon, and Washington.* http://cri.georgetown.edu/state-briefs/
[4] CRI Report, http://cri.georgetown.edu/wp-content/uploads/2017/01/GeorgetownCRI_VermontPRSCReport.pdf
[5] For full list of resources please see the resources page of this report.
[6] AARP, *Factsheet: Vermont, August 2015.* http://www.aarp.org/content/dam/aarp/ppi/2015-08/aarp-vermont-fact-sheet.pdf
[7] U.S. Department of Labor, *Fact Sheet: State Savings Programs for Non-Governmental Employees, November 16, 2015.* http://www.dol.gov/ebsa/newsroom/fsstatesavingsprogramsfornongovernmentemployees.html
[8] The American Council of Life Insurers, *State Initiatives Regarding Retirement Plans for Private Sector Workers,* http://www.vermonttreasurer.gov/retirement/Public-Retirement-Study-Committee*)*

The Committee noted that the increase of individuals who are retirement age and who have inadequate or no retirement plan would force states to dedicate higher percentages of their state budgets to social services. Moreover, with higher percentages of seniors with inadequate retirement savings, states will have smaller tax bases from which to draw to pay for services.[9]

The Committee reviewed a study that focused on retirement savings in Utah. That study, done by Notalys LLC, "shows that modest increases in net worth among those who save the least for retirement would greatly improve retirement readiness and reduce government expenditures on public assistance programs."[10] Further, the "research show[ed] dramatic reduction in government outlays with a minimal increase in a worker's savings: Increasing net worth among the bottom one-third of retirees by just 10 percent over the worker's career would decrease government outlays by more than $194 million over the next 15 years."[11]

The Committee agreed that reliable and adequate income in retirement is not just good for the individual, but also has a positive impact on economic development. In 2012, the National Institute on Retirement Security (NIRS) published an economic analysis study on pension benefit expenditures. The study analyzed the impact of the millions of dollars in pension checks that are spent by retirees within their local community and state. Based on fiscal year 2009 data for Vermont, researchers determined that the $206.1 million in pension benefits paid to 13,935 retirees and their beneficiaries accounted for $299.8 million in total economic output. The study calculated that pension expenditures supported some 2,459 jobs in Vermont that paid $96.2 million in income. These expenditures also supported some $61.2 million in tax revenue at the local, state and federal levels.[12]

[9] GovBeat, The Washington Post, Sept. 12, 2013, *The Northeast is getting older, and it's going to cost them.* https://www.washingtonpost.com/blogs/govbeat/wp/2013/09/12/the-northeast-is-getting-older-and-its-going-to-cost-them/

[10] *AARP Utah Commissions Study on Cost of Retiring Poor in the State,* http://states.aarp.org/aarp-utah-commissions-study-on-cost-of-retiring-poor-in-the-state/

[11] *AARP Utah Commissions Study on Cost of Retiring Poor in the State,* "http://states.aarp.org/aarp-utah-commissions-study-on-cost-of-retiring-poor-in-the-state/

[12] http://www.vermonttreasurer.gov/sites/treasurer/files/pdf/retireState/newsletters/Web%20VSERS%20July%202012.pdf

Guiding Principles

The Committee adopted the following guiding principles in 2014 and 2015 and agreed that these principles would provide a framework for a potential plan in Vermont:

a. Simplicity—a plan should be easy for participants to understand
b. Affordable—a plan should be administered to maximize cost-effectiveness and efficiency
c. Ease of Access—the plan should be easy to join
d. Trustworthy Oversight—the plan should be administered by an organization with unimpeachable credentials
e. Protection from Exploitation—the plan should protect its participants, particularly the elderly, from unscrupulous business practices or individuals
f. Portability—the plan should not depend upon employment with a specific firm or organization
g. Choice—the plan should provide sufficient investment alternatives to be suitable for individuals with distinct goals, but not too many options to induce "analysis paralysis"
h. Voluntary—the plan should not be mandatory; however, auto-enrollment may increase participation
i. Financial Education and Financial Literacy—the plan should assist the individual in understanding their financial situation
j. Sufficient Savings—encourage adequate savings in retirement combined with existing pension savings and social security
k. Additive not Duplicative—the plan should not compete with existing private sector solutions
l. Able to use pre-tax dollars

2016 Committee Work and Legislative Recommendations

During 2016, the Committee met on eight occasions. Based on a legislative change[13], an additional member was added to the Committee to be appointed by the State Treasurer. The Treasurer appointed Lindsay DesLauriers, Director of Main Street Alliance of Vermont to that opening.

Recommendations:

The Committee recommends to the General Assembly that a "Voluntary open multiple employer plan (MEP)" model be adopted[14], supplemented by a marketplace for those employees for employees not covered by the "Voluntary open multiple employer plan (MEP)" or other existing retirement options. The Committee would be pleased to work with the General Assembly to develop appropriate language to pursue such a model.

[13] Act 157, http://www.vermonttreasurer.gov/sites/treasurer/files/pdf/misc/ACT157%20As%20Enacted.pdf
[14] For a full description of the MEP please see the CRI report (pages 26-27), http://cri.georgetown.edu/wp-content/uploads/2017/01/GeorgetownCRI_VermontPRSCReport.pdf

With concurrence of the General Assembly, the Office of the State Treasurer and the Public Retirement Study Committee will work to implement this model. The Treasurer's Office believes the attached report[15], authored by the Center for Retirement Initiatives at Georgetown University provides a framework on which the MEP and marketplace model can be developed.

Proposed Program Model and Essential Elements:

1. Employers with 50 employees or less would be eligible;

2. Employers who already offer an employer-sponsored retirement plan would not be eligible (as of the effective date or start date of a potential program);

3. The program would be voluntary;

4. If the employer opts into the program, auto-enrollment of employees will occur, but employees will have an opt-out option;

5. The Committee recommends beginning with employee contributions but would consider options for voluntary employer contributions, taking into consideration the impact on implementation and plan complexity;

6. The MEP would require a sponsor and enabling legislation that should require the creation of an oversight board[16], however the current "Public Retirement Study Committee" would continue its work by providing the implementation plan and give way to a successor board, should the program go forward; the board (using preliminary data provided by the Committee) would then set program terms, prepare and design plan documents, and be authorized to appoint an administrator to assist in the selection of investments, managers, custodians, and other support services;

7. As contemplated, it is expected that fees would support the program, beyond any de minimis ministerial support provided by the Treasurer's Office and would be paid by program participants. Until sufficient assets have been accumulated, program costs will exceed revenues during the startup phase. The Treasurer's Office will pursue options to have financial service providers subsidize the startup cost in exchange for a longer-term contract, essentially loaning its own capital to the program;[17]

8. If the Committee determines that additional financial support is necessary for start-up and/or ongoing costs, the Treasurer's Office shall inform the General Assembly prior to any decision on implementation. Further, no plan documents or obligations will be entered into until such time as it is determined that the program (and implementation of

[15] CRI Report, http://cri.georgetown.edu/wp-content/uploads/2017/01/GeorgetownCRI_VermontPRSCReport.pdf
[16] CRI Report: *Plan Design Features: Delegate to Board,* http://cri.georgetown.edu/wp-content/uploads/2017/01/GeorgetownCRI_VermontPRSCReport.pdf

[17] CRI Report: *Program Management, Participation, and Financial Feasibility,* http://cri.georgetown.edu/wp-content/uploads/2017/01/GeorgetownCRI_VermontPRSCReport.pdf

the program) will not create financial obligations to the State or that the General Assembly has considered such costs and appropriated sufficient dollars;

9. For employees of employers who do not adopt the MEP (or who do not already have access to an employer-sponsored plan), a range of retirement options including myRAs, 401(k) style-plans, Simple IRAs and other vetted products deemed sufficient by the "successor" board would be provided through a marketplace.

The Committee also recommends that, if after 3 years from the start of the "Voluntary open multiple employer plan (MEP)", there is not a significant/sufficient increase in the number of Vermonters who are covered by a retirement plan, that methods to increase participation be further explored and analyzed.

The Committee also noted that while all members unanimously voted to adopt this model, some members felt that a third tier, using an auto-IRA model with mandatory employer participation, was needed when the prior two options were not adopted by the employer. A description of that configuration is included as an addendum to the report.

Next Steps:

The Committee will continue to map out implementation pursuant to any directive of the General Assembly and work to answer key questions. The Committee will submit an update to the implementation plan in 2018.

1. Public Retirement Study Committee continue its work until 2018 sunset;

2. Creation of the Plan Design (Employee and Employer Contribution limits, withdrawal policies, tax and other incentives, default contribution rate policy, auto-enrollment/auto-escalation);

3. Create legislative recommendation;

4. Recommend make-up of the board (upon completion of the work of the Public Retirement Study Committee);

5. Outline implementation steps;

6. Give way to successor board.

The State Treasurer would like to thank the efforts of the members of the Public Retirement Study Committee for their work:

- Monica Hutt, Commissioner, Vermont Department of Disabilities, Aging and Independent Living
- Annie Noonan, Commissioner, Vermont Department of Labor
- Dan Boardman, Owner, Hickok & Boardman Retirement Solutions—Appointed by the Speaker

- Russ Bennett, founder and owner of NorthLand Visual Design & Construction Inc.—Appointed by the Speaker
- Rebecca Towne, Vermont Gas—Appointed by the Committee on Committees
- Bob Hooper, Trustee and Board Member at Vermont Pension Investment Committee—Appointed by the Committee on Committees
- Lindsay DesLauriers, State Director of Mainstreet Alliance of Vermont—Appointed by the State Treasurer

The State Treasurer would also like to thank the efforts of Angela M. Antonelli, Executive Director, at the Center for Retirement Initiatives, at Georgetown University and her project team, including David Morse, Partner at K&L Gates for their work in drafting the "Review of Potential Public Retirement Plan Options for Private Sector Employees/Employers in the State of Vermont."

Resources

The Center for Retirement Initiatives (CRI), McCourt School of Public Policy, Georgetown University: "Review of Potential Public Retirement Plan Options for Private Sector Employees/Employers in the State of Vermont", Available on CRI Webpage:

- http://cri.georgetown.edu/wp-content/uploads/2017/01/GeorgetownCRI_VermontPRSCReport.pdf
- http://cri.georgetown.edu/

The Center for Retirement Initiatives, McCourt School of Public Policy, Georgetown University: Comparison of Retirement Plan Design Features, By State: California, Illinois, Massachusetts, Oregon, and Washington. http://cri.georgetown.edu/state-briefs/

The Center for Retirement Initiatives, McCourt School of Public Policy, Georgetown University: State Level Data and Rankings: http://cri.georgetown.edu/states/state-level-data-rankings/

National Institute on Retirement Security, Financial Security for Future Retirees: Vermont Scores 5 out of 10. http://www.nirsonline.org/storage/nirs/documents/Factsheets/VT_FSS.pdf (attached)

AARP, Factsheet: Vermont, August 2015. http://www.aarp.org/content/dam/aarp/ppi/2015-08/aarp-vermont-fact-sheet.pdf

The American Council of Life Insurers:

- ACLI: Statement for the Record, U.S. Senate, Health, Education, Labor and Pensions Committee
- ACLI: Role of Life Insurers

Assets & Opportunity Scorecard, State Profile: Vermont. http://scorecard.assetsandopportunity.org/latest/report/state-profile (available online)

U.S. Department of Labor, Fact Sheet: State Savings Programs for Non-Governmental Employees, November 16, 2015. http://www.dol.gov/ebsa/newsroom/fsstatesavingsprogramsfornongovernmentemployees.html (attached)

Information concerning U.S. Department of Labor Rules:

- http://cri.georgetown.edu/news/dol-releases-regulation-and-guidance-for-state-administered-retirement-plans/
- http://www.dol.gov/ebsa/newsroom/fsstatesavingsprogramsfornongovernmentemployees.html
- https://www.gpo.gov/fdsys/pkg/FR-2015-11-18/html/2015-29427.htm
- https://www.gpo.gov/fdsys/pkg/FR-2015-11-18/html/2015-29426.htm

U.S. Census Bureau, 2014 SUSB Annual Data Tables by Establishment Industry, http://www.census.gov/data/tables/2014/econ/susb/2014-susb-annual.html

The Pew Charitable Trusts, Employer-based Retirement Plan Access and Participation across the 50 States, http://www.pewtrusts.org/en/multimedia/data-visualizations/2016/employer-based-retirement-plan-access-and-participation-across-the-50-states

Employee Benefit Research Institute, Employment-Based Retirement Plan Participation: Geographic Differences and Trends, 2013, https://www.ebri.org/pdf/EBRI_IB_405_Oct14.RetPart.pdf

Bureau of Labor Statistics, Employee Benefits Survey, https://www.bls.gov/ncs/ebs/benefits/2016/benefits_retirement.htm

January 5, 2017
Addendum to the Public Retirement Study Committee Report

The undersigned members of the study committee are of the opinion that, two years after implementation of the Multiple Employer Plan (MEP) as recommended in the committee's report, the state should also establish a publicly-enabled IRA as an automatic default program for employers who do not offer a private retirement product and who have chosen not to participate in the state administered MEP, in order to maximize retirement savings across the state and ensure the long-term financial viability of the public retirement program.

Recent DOL regulations create a "safe harbor" for states that require employers who otherwise do not provide access to a retirement product to automatically enroll their employees in a payroll deduction IRA plan administered by the state. Under these plans, employee participation is voluntary and employees may opt-out, if they choose.

Studies have shown that workers - particularly low- and moderate- income workers are more likely to save for retirement if they have access to a retirement plan through their employer. According to a recent White House announcement, "fewer than 10 percent of workers without access to a workplace plan contribute to a retirement savings account on their own."[1]

Implementing a default IRA would also allow for auto-enrollment of all working Vermonters, maximizing participation. Auto-enrollment in retirement plans has been shown to substantially boost participation and savings.

It is the opinion of the following members of the committee that the proposal described above will balance employer choice by providing a two-year window to set up a private retirement plan or join the MEP if they wish to do so, improve retirement savings across the state for all working Vermonters by ensuring the link between one's workplace and access to a retirement product, maximize participation by enabling auto-enrollment, and ensure the long-term viability of the program while offering the greatest protection to the existing private financial services industry.

Signed:
Russ Bennett
Dan Boardman
Lindsay DesLauriers

[1] https://www.whitehouse.gov/the-press-office/2016/01/26/fact-sheet-building-21st-century-retirement-system-0

GEORGETOWN UNIVERSITY
McCourt School *of* Public Policy
Center for Retirement Initiatives

Review of Potential Public Retirement Plan Options for Private Sector Employees/Employers in the State of Vermont

Submitted to:

Office of the Vermont State Treasurer
Public Retirement Study Committee

Prepared by:

The Center for Retirement Initiatives
McCourt School of Public Policy
Georgetown University

January 4, 2017

Center for Retirement Initiatives
McCourt School of Public Policy
Georgetown University
3300 Whitehaven Street, 5th Floor
Washington, DC 20007
Phone: 202-687-4901
Website: cri.georgetown.edu

ACKNOWLEDGEMENTS

This report was prepared by the Center for Retirement Initiatives (CRI) at Georgetown University's McCourt School of Public Policy and authored by Angela M. Antonelli, Executive Director, and CRI's legal subject matter expert for this project, David M. Morse, Partner, K&L Gates LLP. The Center also would like to acknowledge CRI Research Assistants, Laura Kim and Jiaoying Jiang, for their contributions to this report.

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Executive Summary

The retirement security challenge in Vermont is already real. Vermont's retirees rank only average nationally on a scale of overall retirement financial readiness. For some measures, such as average retirement account balance, Vermont ranks well below average. The state also has the fifth largest proportion of its population aged 65 and older, projected to grow to one out of every five residents between now and 2032. The mean retirement income for seniors in Vermont is $21,299. A single retiree in Vermont is conservatively estimated to require a retirement income between $24,756 and $33,060 to meet basic needs. In Vermont, 40 percent of older households spend 30 percent or more of income on housing costs, a benchmark for housing affordability.

Approximately 45 percent of private wage and salaried workers in Vermont—104,000 workers—are not covered by an employer-sponsored retirement plan. Small businesses, which represent 94 percent of all employers and employ 43 percent of Vermont's private sector labor force, are among the least likely to provide workers with access to a retirement savings plan. Employer-provided retirement plans are the most effective way to help workers save for retirement.

There are significant budgetary and economic consequences of a growing number of retirees with limited financial resources. Left unaddressed, Vermont will face the possibility of more of its seniors living at or below the poverty line and increasingly pressed to deal with the dramatic increases in the cost of social service programs, including healthcare, housing, and food and energy assistance.

States are leading innovation and evolution in the design of retirement savings programs for private sector workers. States are leading the way, working collaboratively with the federal government, to develop retirement plans to help private sector employees save for retirement. No plan design option is without some policy uncertainty, and the differences in features among the options should be carefully considered. These plans are designed to be simple, accessible and affordable to small businesses, help workers save automatically, and provide low-cost ways to invest those savings.

More than 30 states have introduced legislation to either establish a state-sponsored retirement plan or study the feasibility of establishing one for private sector workers. Eight states—California, Connecticut, Illinois, Maryland, Massachusetts, New Jersey, Oregon and Washington State—already have enacted legislation to expand the accessibility and effectiveness of retirement savings for private sector workers and are beginning to implement their programs.

Vermont's leadership will make a difference not just in Vermont but across the nation. The Vermont Legislature directed the Vermont Public Retirement Study Committee (PRSC or the "Committee") to report by January 15, 2017 on the feasibility of establishing a retirement program for private sector workers. The Committee's work will contribute to states leading the way to develop innovative approaches to address the retirement savings coverage gap. Vermont can design a program that will abide by the guiding principles it established in January 2016, including simplicity, affordability, ease of access, and portability.

To inform the work of the PRSC, this report provides an overview of the retirement security challenges facing the nation and Vermont. Second, it outlines several potential policy strategies that may help improve retirement security for the residents of Vermont, including legal, regulatory, and plan design considerations. Finally, the report provides some early lessons learned from other states that are in various stages of implementing new programs.

Introduction

Americans are facing a retirement crisis. The foundation for building a secure retirement—Social Security, employer-provided pensions, and personal savings—has been weakened because most private companies no longer provide pension plans for their employees[1] and employees have not saved much on their own for their retirement.[2] The U.S. personal savings rate has declined dramatically over the past several decades and is currently very low by historical standards.[3] Today, the confidence of many Americans to have a secure retirement is at an all-time low.[4]

Americans should be able to work, have easy access to simple, low-cost ways to save, and look forward to a level of financial security in their retirement. Millennials are concerned about their financial future and 74 percent of Americans recently surveyed expressed concern about their ability to achieve that secure retirement.[5] The ability of more workers to improve their retirement readiness is made challenging today because more than one-half of all private sector workers—approximately 68 million Americans—do not have access to retirement savings programs through their employer.[6]

Employer-provided retirement plans are often more effective for encouraging retirement savings. Workers are 15 times more likely to save for their retirement if they have a way to save through an employer-based plan.[7] Many small businesses do not provide retirement programs either because the cost is too high or the resource burden is perceived as too great for a small company.[8] Thus, many private sector employees are left without access to the simplest ways to save for retirement and do not take any steps to begin saving on their own.

The deterioration of the foundation for retirement security is one of the greatest economic and financial challenges facing our nation today. Between now and 2030, 10,000 baby boomers will retire every day. The population age 65 and over in 2030 is projected to be more than 74 million, representing more than 20 percent of the total population.[9] In 2013, almost one-third of households age 55 and older lacked retirement savings in a defined benefit (DB) plan or defined contribution (DC) savings plan, leaving Social Security as the main or only source of retirement income.[10]

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[1] King, Peter. "The Vanishing Pension: If Your Company Still Offers a Guaranteed Retirement Plan You're Fortunate These Days. But How Safe Is It?" *Newsday*, August 6, 2005. http://www.pensionresearchcouncil.org/news/?id=22.

[2] According to the EBRI's 2014 Retirement Confidence Survey, 80 percent of workers between 25-34 years of age and 48 percent of workers 45 years of age and older have saved less than $25,000 in total savings and investments. See: Helman, Ruth, Adams, N., Copeland, C. & VanDerhei, J. (2014), "The 2014 Retirement Confidence Survey: Confidence Rebounds---for Those with Retirement Plans." Employee Benefit Research Institute, Issue Brief No. 397, p. 17. http://www.ebri.org/pdf/surveys/rcs/2014/EBRI_IB_397_Mar14.RCS.pdf.

[3] See Brookings Institution (2013), Chart, "U.S. Personal Saving Rate, 1970-2012." http://www.hamiltonproject.org/multimedia/charts/u.s._personal_saving_rate_1970-2012/.

[4] Helman, Ruth, Adams, N., Copeland, C. & VanDerhei, J. (2014), op. cit.

[5] Oakley, Diane and Kenneally, Kelly (2015), "Retirement Security 2015: Roadmap for Policy Makers Americans' Views of the Retirement Crisis," National Institute on Retirement Security, p.1. http://www.nirsonline.org/storage/nirs/documents/2015%20Opinion%20Research/final_opinion_research_2015.pdf.

[6] U.S. Department of Labor, Employee Benefits Security Administration (2015), "Fact Sheet: State Savings Programs for Non-Government Employees." https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/state-savings-programs-for-non-government-employees.pdf.

[7] AARP, Letter to the U.S. Department of Labor regarding the Proposed Rule on Savings Arrangements Established by States for Non-Governmental Employees, January 19, 2016. https://www.dol.gov/sites/default/files/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB71/00039.pdf.

[8] U.S. Government Accountability Office (2013), "Retirement Security: Challenges and Prospects for Employees of Small Businesses (GAO 13-748T)," p.9. http://www.gao.gov/assets/660/655889.pdf.

[9] U.S. Government Accountability Office (2015), "Retirement Security: Most Households Approaching Retirement Savings Have Low Savings (GAO-15-419)," p.1. http://www.gao.gov/assets/680/670153.pdf.

[10] U.S. Government Accountability Office (2016), "Retirement Security: Low Defined Contribution Savings May Pose Challenges (GAO-16-408)," p.11. http://www.gao.gov/assets/680/676942.pdf.

Social Security was never meant to be the sole source of income for retirees. Yet Social Security accounts for at least half of total retirement income for over 60 percent of recipients and over 90 percent of income for more than a third of recipients.[11] As of June 2016, the average monthly Social Security benefit for a retired worker is $1,348,[12] enough to place them only about 30 percent over the poverty level.[13]

There are significant budgetary and economic consequences if more Americans enter retirement with limited financial resources. For seniors living at or below the poverty line, states will be increasingly pressed to deal with the dramatic increases in the cost of social service programs, including healthcare, housing, and food and energy assistance. As income falls, there is less consumer spending and the available tax base is reduced. By way of contrast, if retirees have greater levels of savings and income to spend, they can contribute to the strength of local and national economies. One recent study suggests that for every 100 retirees that move into a community, as many as 55 new jobs can be created.[14]

For several years, the White House and Congress have failed to act on legislative proposals to establish new retirement savings programs to close the access gap among private sector workers. Because of this federal gridlock and because of the potential budgetary and economic consequences of this failure to address the deterioration of retirement savings for millions of American workers and their families, states have begun to establish publicly sponsored retirement plans for private sector employees.

In response to this state leadership, the federal government has worked collaboratively with states and cities (referred to also as "state political subdivisions") to clear a pathway by removing regulatory uncertainty to allow for innovation. The federal government has now provided states with a range of plan design options with varying features to create programs that fit their different political and economic environments. These DC savings programs include, but are not limited to, individual retirement accounts (IRAs) using auto-enrollment, 401(k) open multiple employer plans (MEPs), 401(k) prototype plans, and a marketplace.[15] (Appendix A)

Over the last two years, at least 30 states have introduced legislation to either establish a state-sponsored retirement plan or study the feasibility of establishing one (Chart 1). Eight states—California, Connecticut, Illinois, Maryland, Massachusetts, New Jersey, Oregon and Washington State—have enacted legislation to expand the accessibility and effectiveness of retirement savings for private sector workers.[16] (Appendices B & C) For convenience, this paper generally refers to "states" and "state-sponsored retirement savings programs," even though the same federal rules apply to certain "large" cities and other state political subdivisions.

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[11] Ruffing, Kathy and Van De Water, Paul, N. (2016), "Social Security Benefits Are Modest," Center for Budget and Policy Priorities. http://www.cbpp.org/research/social-security/social-security-benefits-are-modest.

[12] Social Security Administration (2016), "Snapshot of a Month: June 2016 Beneficiary Data." https://www.ssa.gov/news/press/factsheets/basicfact-alt.pdf.

[13] Ruffing, Kathy and Van De Water, Paul, N. (2016), op. cit.

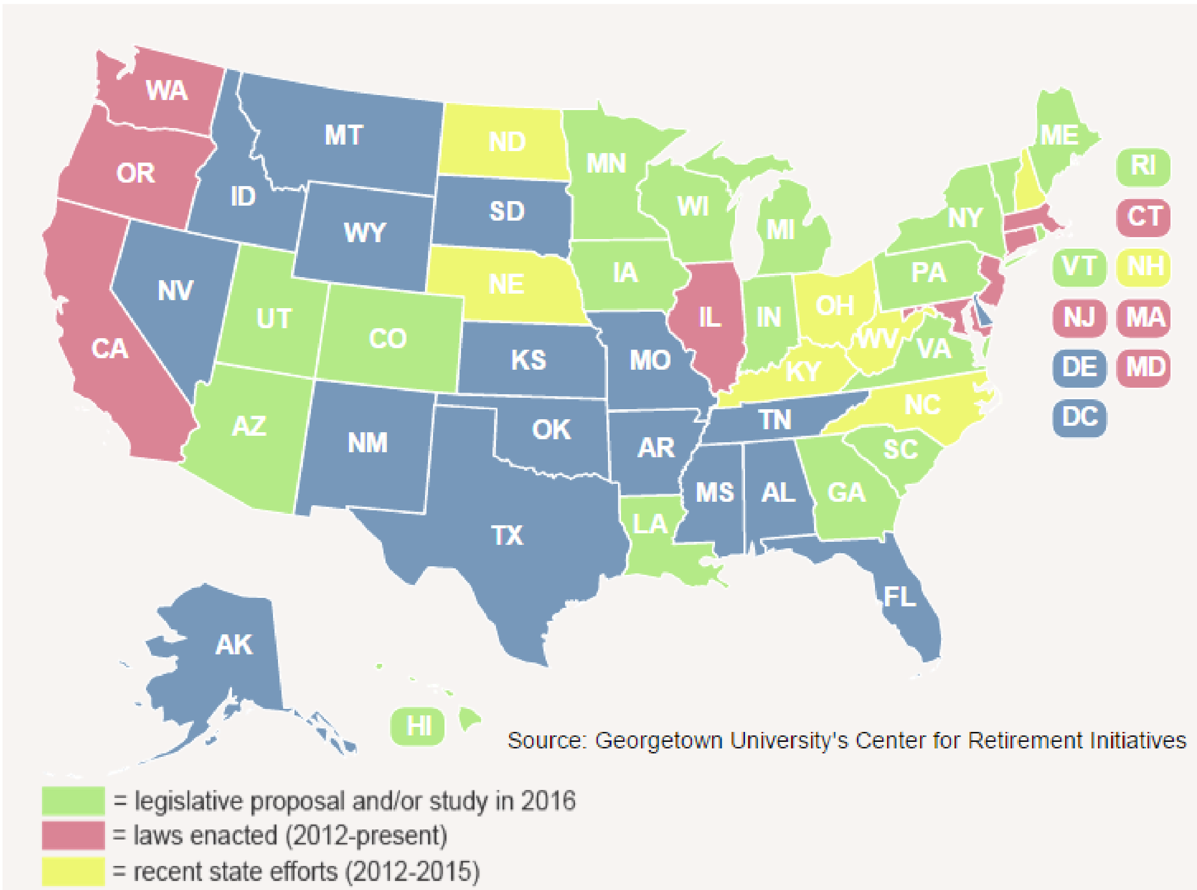
[14] Selig Center for Economic Growth, Terry College of Business, University of Georgia (2013), "Evaluating Retiree-based Economic Development in Georgia: Golden Rules," p. 11. https://www.terry.uga.edu/media/documents/selig/golden-rules-2013.pdf.

[15] For more information on the types of programs and their legal and regulatory framework, please see the Georgetown Center for Retirement Initiatives website at http://cri.georgetown.edu/states/.

[16] For more detailed information about state programs and legislative proposals, see the Georgetown Center for Retirement Initiatives website at http://cri.georgetown.edu/states/.

CHART 1

More Than 30 States Acted in 2016 to Consider Private Sector Retirement Savings Programs



Source: Georgetown University Center for Retirement Initiatives

The Vermont Legislature directed the PRSC to report by January 15, 2017 on the feasibility of establishing a retirement program for private sector workers.[17]

To inform the work of the PRSC, this report provides an overview of the retirement security challenges facing the nation and Vermont. Second, it outlines several potential policy strategies that may help improve retirement security for the residents of Vermont, including legal, regulatory, and plan design considerations. Finally, the report provides some early lessons learned from other states that are in various stages of implementing new programs.

[17] VT H. 868, No. 157, Sec. F. 1 (2016). http://legislature.vermont.gov/assets/Documents/2016/Docs/ACTS/ACT157/ACT157%20As%20Enacted.pdf.

I. The Retirement Security Challenge

A lack of retirement readiness has consistently been a top financial concern for American families for more than a decade.[18] Most Americans report a lack of confidence in their ability to prepare adequately for their own retirement.[19] If they can put money away for retirement, they often do not take the time to understand how much they will need to save and, even if they do, they are fearful they will never be able to save enough to last a lifetime. [20] This fear only grows as life expectancy in the United States continues to increase, posing new challenges for future generations of retirees.[21]

Most Americans agree that the country's retirement system is under stress and in need of reform.[22] Many support state efforts to set up retirement plans, consistently expressing that government leaders eliminate the barriers that keep employers from offering retirement savings plans. In fact, participants consider retirement benefits to be almost as important a job feature as salary and would be willing to forgo salary raises for future guaranteed retirement income.[23]

The Shift in How Americans Save and How Much They Have Saved for Retirement

Over the past 30 years, the traditional DB pension plan has gradually been replaced by a DC system of individual retirement accounts as the primary type of private sector employer-sponsored plan and the primary way workers save for retirement. A traditional DB plan provides an employee a guaranteed income (monthly, lump sum, or some combination) at retirement based on the employee's earnings history and length of service. A DC plan establishes an individual retirement savings account for the employee and gives the employee information to make decisions about whether and how much to save and how to invest those savings without any guarantee or promise of the benefit or payout that will be available at the time of retirement.

Today, most workers whose employers provide a retirement plan are offered a DC plan, most commonly a 401(k) plan. Traditional DB plans are still offered to public sector workers and some private sector workers. However, the number of DB plans has dropped significantly**.** In 2013, DC plans comprised 94 percent of all employer-sponsored plans and active DC participants outnumbered those in DB plans 76.7 million to 15.2 million.[24]

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[18] McCarthy, Justin (2016), "Americans' Financial Worries Edge Up in 2016," Gallup. http://www.gallup.com/poll/191174/americans-financial-worries-edge-2016.aspx.

[19] Financial Industry Regulatory Authority (FINRA) Investor Education Foundation (2016), "Financial Capability in the United States 2016," p. 16. http://www.usfinancialcapability.org/downloads/NFCS_2015_Report_Natl_Findings.pdf.

[20] The Associated Press-NORC Center for Public Affairs Research (2016), "Working Longer: The Disappearing Divide Between Work Life and Retirement." http://www.apnorc.org/projects/Pages/HTML%20Reports/working-longer-the-disappearing-divide-between-work-life-and-retirement-issue-brief.aspx.

[21] In 2014, the average life expectancy at birth in the United States was almost 79 years; 81 years for women and 76 years for men. See Center for Disease Control (2016), "Changes in Life Expectancy by Race and Hispanic Origin in the United States, 2013-2014." http://www.cdc.gov/nchs/products/databriefs/db244.htm.

[22] Oakley, Diane and Kenneally, Kelly (2015), "Retirement Security 2015: Roadmap for Policy Makers Americans' Views of the Retirement Crisis," National Institute on Retirement Security, p.1. http://www.nirsonline.org/storage/nirs/documents/2015%20Opinion%20Research/final_opinion_research_2015.pdf.

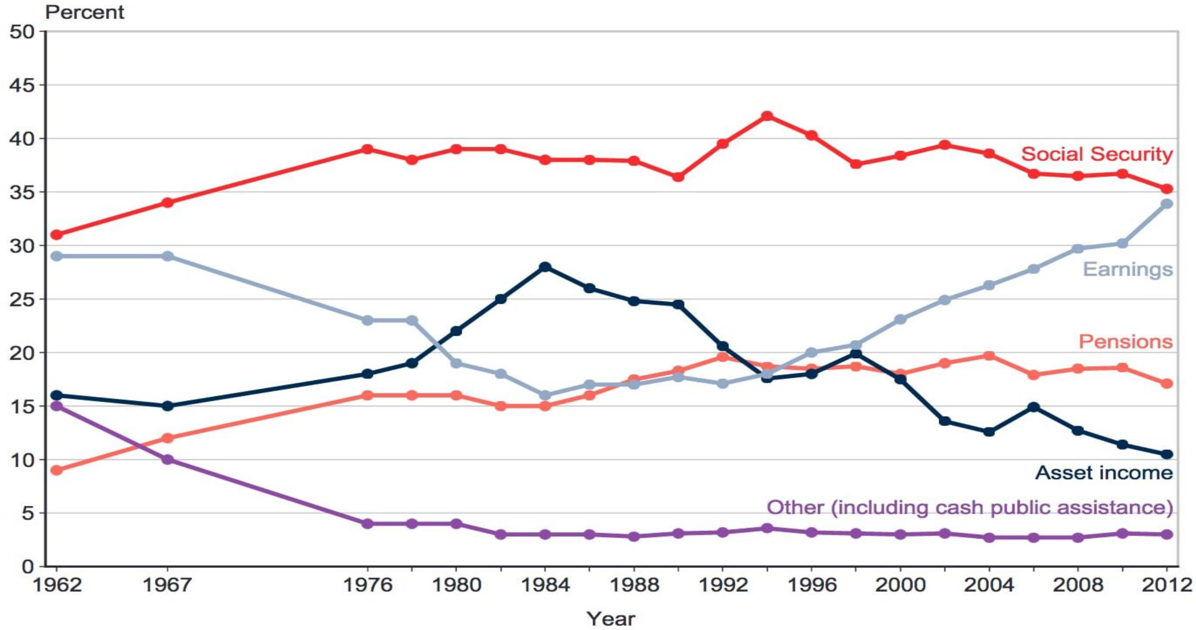
[23] Ibid., p. 2

[24] U.S. Department of Labor, Employee Benefits Security Administration (2016), "Private Pension Plan Bulletin Historical Tables and Graphs." https://www.dol.gov/sites/default/files/ebsa/researchers/statistics/retirement-bulletins/private-pension-plan-

As shown in Chart 2, since the mid-1990s, for households age 65 and older, Social Security benefits and personal retirement savings have declined while the share of income from earnings from work has almost doubled. While Social Security remains an important source of income, there is a need to help workers save more to replace more of their pre-retirement income.

CHART 2

Share of Aggregate Income for Households 65 and Older, By Source, Selected Years



Source: Social Security Administration, Income of the Aged Chartbook, 2012

Although workers may assume that they will be able to work well past age 65, the reality is that many workers often retire earlier than they expect due to illness and job loss. Almost one-half (44 percent) of workers age 58 and older have physically demanding jobs or difficult working conditions, which will prohibit many from working longer. These are mostly low-wage workers with lower educational attainment.[25] In 2015, the Retirement Confidence Survey found that 36 percent of workers expected to retire after 65, compared to just 11 percent in 1991.[26] In 2015, 50 percent of retirees left the workforce earlier than planned and of those, 60 percent reported doing so because of a hardship such as a health problem or disability.[27] In fact, there may be a sizable gap between workers' expectations and retirees'

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bulletin-historical-tables-and-graphs.pdf. See also U.S. Government Accountability Office (2016), "Retirement Security: Low Defined Contribution Savings May Pose Challenges (GAO-16-408)," p.5. http://www.gao.gov/assets/680/676942.pdf.

[25] Center for Economic and Policy Research, "Still Working Hard: An Update on the Share of Older Workers in Physically Demanding Jobs," http://cepr.net/publications/reports/still-working-hard

[26] Employee Benefit Research Institute and Greenwald & Associates, "2015 RCS Fact Sheet #2: Expectations About Retirement," p.1. https://www.ebri.org/pdf/surveys/rcs/2015/RCS15.FS-2.Expects.pdf.

[27] Ibid., p.2.

experience—while 8 percent of workers plan to retire before 60, 36 percent of retirees report retiring that early and 26 percent of workers plan to wait until at least age 70 to retire, but only 6 percent of retirees actually did so.[28]

The shift away from the traditional DB system and the rise of voluntary DC plans have weakened the retirement security of millions of American workers. In 2013, according to the U.S. Government Accountability Office (GAO):[29]

- 60 percent of all households had no savings in a DC plan from a current or former job;
- 34 percent of working households did not have a DC or a DB plan from a current or former job;
- 29 percent of households age 55 and older had neither DB nor DC retirement savings, leaving Social Security as their main or only source of retirement income.

An analysis of the 2013 Survey of Consumer Finance data shows that the median working-age household had $5,000 saved in retirement accounts.[30] According to the GAO's analysis of the same data, the overall median balance of DC savings for all working, prime-age (25-64) households was just $3,000 and the overall median balance for working, prime-age households with a DC account in 2013 was $41,900.[31] Among households age 55 and older, 48 percent had some retirement savings, with the median of approximately $109,000, which is commensurate to an inflation-protected annuity of $405 per month for a 65 year old, according to GAO calculations.[32]

Retirement Savings Varies by Income, Race and Gender

Income. A 2015 study by the National Institute on Retirement Security (NIRS) found that retirement account ownership was closely correlated with income; households with accounts had over 2.4 times the annual income of those that did not.[33] The GAO reports that only 25 percent of working, low-income households had any DC savings, compared to 81 percent of working, high-income households.[34] Among households with DC savings, the median account balance was $201,500 for high-income households, while it was just $10,400 for low-income working households. (Chart 3) In fact, GAO's DC savings projections, which incorporates a set of assumptions based on current law, investment, and other trends and applies them to a cohort born in 1997 through retirement, saw the lowest earning group with an average annuity of about $560 a month (in 2015 dollars) in retirement, with 35 percent of the group with no DC savings.[35]

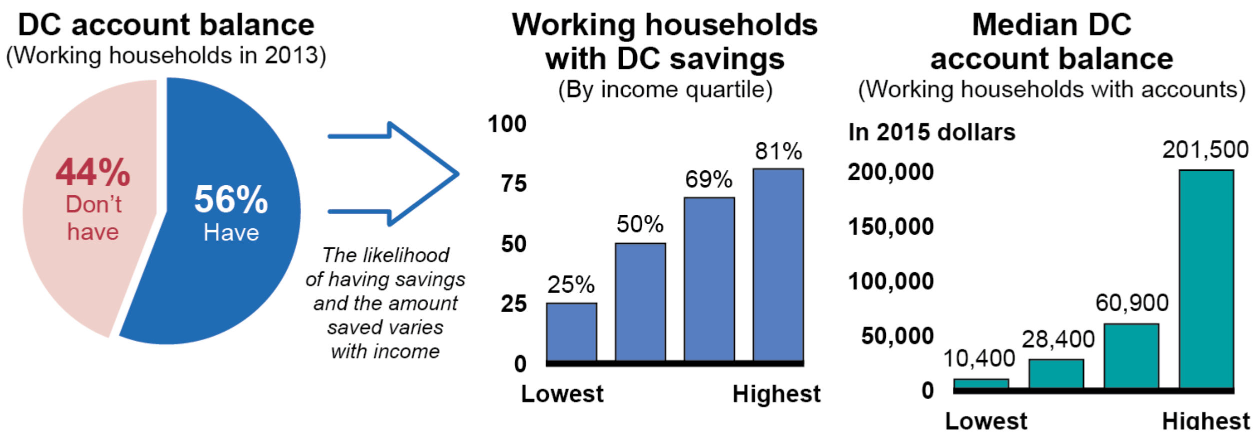
Race. Nearly two-thirds of minority households do not have any savings in a retirement account like a 401(k) or IRA, compared to a little over one-third of white households. Non-white workers are

[28] Ibid.
[29] U.S. Government Accountability Office (2016), "Retirement Security: Low Defined Contribution Savings May Pose Challenges (GAO-16-408)," p.11. http://www.gao.gov/assets/680/676942.pdf.
[30] Morrissey, Monique, "The State of American Retirement," Economic Policy Institute, p. 14. http://www.epi.org/files/2016/state-of-american-retirement-final.pdf.
[31] U.S. Government Accountability Office (2016), "Retirement Security: Low Defined Contribution Savings May Pose Challenges (GAO 16-408)," p. 13, footnote 30. http://www.gao.gov/assets/680/676942.pdf.
[32] U.S. Government Accountability Office (2015), "Retirement Security: Most Households Approaching Retirement Have Low Savings (GAO 15-419)," p. 7. http://www.gao.gov/assets/680/670153.pdf.
[33] Rhee, Nari and Boivie, Ilana (2015), "The Continuing Retirement Savings Crisis," National Institute on Retirement Security, p. 9. http://laborcenter.berkeley.edu/pdf/2015/RetirementSavingsCrisis.pdf.
[34] U.S. Government Accountability Office (2016), "Retirement Security: Low Defined Contribution Savings May Pose Challenges (GAO 16-408)," p. 13. http://www.gao.gov/assets/680/676942.pdf.
[35] Ibid., p. 25.

significantly less likely to be covered under an employer-sponsored retirement plan, compared to white workers. In a 2013 report, NIRS reported that 54 percent of Black and Asian employees and 38 percent of Latino employees between the ages of 25-64 worked for an employer with such a plan, compared to 62 percent of white employees.[36] The median balance for working households with DC savings was $58,800 for white households, compared to $16,400 for Black households and $18,900 for Hispanic households.[37] How workers treated their accounts when leaving an employer also differed by race—a study by Ariel/Aon Hewitt in 2010, cited by the GAO, found that 63 percent of Black, 57 percent of Hispanic, and 39 percent of white workers cashed out rather than rolled over their DC savings to another retirement account such as an IRA when they left their employers.[38]

CHART 3

Defined Contribution (DC) Plan Savings by Household Income Among Working Households, 2013



Source: GAO analysis of 2013 Survey of Consumer Finances; GAO 16-408

Gender. Gender disparities in retirement income can be attributed to the differing experiences that men and women have across their working years. Women on average earn less than men, have longer life expectancies and more chronic health conditions.[39] Women are more likely to work in part-time jobs, which makes it less likely they are eligible for employer sponsored retirement plans.[40] Women are 80 percent more likely than men to live in poverty at age 65 and older, and women between the ages of 75 to 79 are three times more likely than men to live in poverty.[41] This gap widens when race is added in: a 2013 study by the Institute for Women's Policy Research found that on average, white men's annual

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[36] Rhee, Nari (2013), "Race and Retirement Insecurity in the United States," National Institute on Retirement Security, p. 3. http://www.giaging.org/documents/NIRS_Report_12-10-13.pdf.
[37] U.S. Government Accountability Office (2016), "Retirement Security: Low Defined Contribution Savings May Pose Challenges (GAO 16-408)," p. 18. http://www.gao.gov/assets/680/676942.pdf.
[38] Ibid., p. 22.
[39] Hartmann, Heidi and A. English (2009), "Older Women's Retirement Security: A Primer," Journal of Women, Politics & Policy, 30(2), p. 109-140. http://www.tandfonline.com/doi/full/10.1080/15544770902901932?scroll=top&needAccess=true.
[40] U.S. Department of Labor, Employee Benefits Security Administration (2015), "Women and Retirement Savings." https://www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/publications/women.pdf.
[41] Brown, Jennifer E., Rhee, N., Saad-Lessler, J. & Oakley, D. (2016), "Shortchanged in Retirement: Continuing Challenges to Women's Financial Future," National Institute on Retirement Security, p.18. http://www.nirsonline.org/storage/nirs/documents/Shortchanged/final_shortchanged_retirement_report_2016.pdf.

pension income ($10,600) was over twice that of white ($4,300) and Black women ($4,000) and five times of Latinas ($1,900).[42]

Retirement Income in Vermont

The retirement security challenge in Vermont is already real. Vermont only scores an average five out of ten on the NIRS's Financial Security Scorecard.[43] There are several reasons why Vermont's rank is only average relative to other states:

- **Workers in Vermont who contributed to DC accounts have an average balance of $19,768, the lowest in the nation**.[44] This is just over one-third of the state's average annual earnings of $57,175 and far below financial experts' recommendation of two to three times the salary for workers in their 40s.[45] The state's average is also only about two-thirds of the national average for retirement savings of $30,345.[46]
- **Many seniors in Vermont are poor.** The senior population accounts for about 11 percent of the state's total population below the poverty line in 2015.[47] As of 2015, about 17.3 percent of the 65 and older population is below 150 percent of the poverty line.[48]
- **Vermont's 65+ population is growing more rapidly than other age groups, expected to increase by over 70 percent between 2012 and 2032 and account for almost one-quarter of the state's population.**[49] At the national level, the projected senior population is expected to be about 20 percent of the population by 2032. As of 2015, the senior population accounts for 18 percent of the total population in Vermont.[50] In addition, 98 percent of the seniors identify as white and 54 percent of the senior population is female while 46 percent is male.[51] The median age of Vermont's 65+ population is 72.7 years.[52]
- **The average Social Security income for seniors in Vermont was $20,130 in 2015 and the average retirement income for seniors in Vermont was $21,299.**[53] An estimated 91 percent of Vermont's

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[42] Fischer, Jocelyn and Hayes, Jeff (2013), "The Importance of Social Security in the Incomes of Older Americas: Differences by Gender, Age, Race/Ethnicity, and Martial Status," The Institute of Women's Policy Research, p.6. http://www.iwpr.org/publications/pubs/the-importance-of-social-security-in-the-incomes-of-older-americans-differences-by-gender-age-race-ethnicity-and-marital-status/.

[43] National Institute on Retirement Security, "Financial Security for Future Retirees: Vermont Scores 5 out of 10," http://www.nirsonline.org/storage/nirs/documents/Factsheets/VT_FSS.pdf. States were ranked by NIRS based on eight measures of financial security for future retirees including: percentage of private sector workers participating in a retirement plan at work; average defined contribution account balance; marginal tax rate on pension income; average out of pocket expenditures for Medicare patients; average Medicaid spending per elderly patient; percent of older households spending 30 percent or more of income on housing costs; unemployment rate of people 55 and older; and media hourly earnings of workers 55 and older.

[44] Ibid.

[45] Ibid.

[46] Ibid.

[47] U.S. Census Bureau, 2015 American Community Survey 1-Year Estimates, "Population 65 Years and Over in the United States." https://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=ACS_15_1YR_S0103&prodType=table

[48] Ibid. Based the population of seniors for whom poverty status is known.

[49] Houser, Ari, Fox-Grage, W.& Ujvari, K., "Across the States: Profiles of Long-term Services and Supports: Vermont," AARP, p.3. http://www.aarp.org/content/dam/aarp/research/public_policy_institute/ltc/2012/across-the-states-2012-vermont-AARP-ppi-ltc.pdf.

[50] U.S. Census Bureau, 2015 American Community Survey 1-Year Estimates, "Population 65 Years and Over in the United States." https://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=ACS_15_1YR_S0103&prodType=table.

[51] Ibid.

[52] Ibid.

[53] Ibid.

seniors live in households that receive Social Security.[54] Almost one-half of senior households in Vermont receive some sort of other retirement income. This figure is inadequate to cover costs of living, as determined by the Elder Economic Security Standard Index (Elder Index), which provides a conservative estimate of the income a retiree would need to meet his or her basic needs (which excludes extra expenses such as vacations and dining out). A single retiree in Vermont would need anywhere between $24,756 and $33,060 (the figure varies on whether the individual had a mortgage or was renting).[55] Furthermore, 40 percent of older households in Vermont spend 30 percent or more of income on housing costs, a benchmark of housing affordability.[56]

There are significant budgetary and economic consequences if more Americans enter retirement with limited financial resources. For seniors living at or below the poverty line, states will be increasingly pressed to deal with the dramatic increases in the cost of social service programs for seniors, including healthcare, housing, and food and energy assistance. As income falls, there is less consumer spending and the available tax base is reduced. Although little data currently exists estimating the budgetary consequences of an increasingly poor elderly population, one recent Utah study[57] estimated the total cost to taxpayers for new retirees in that state alone will top $3.7 billion over the next 15 years. In addition, just a 10 percent increase in net worth of the bottom third of the least prepared workers for retirement could save Utah taxpayers $194 million through 2030. [58]

Lack of Access to Employer Sponsored Plans and Participation Barriers

There is wide variation across states and regions in the level of access and participation to employer based pension or retirement savings plans.[59] There are several factors contributing to whether an employer provides access to retirement plans and, if they do, why workers may not participate in those plans.

Complexity and Costs Prevent Small Businesses from Offering Retirement Options to Workers

Small businesses play a significant role in America's economy: 98.2 percent of all firms in the United States employ fewer than 100 workers and small firms employ 34.3 percent of all employees.[60] Small businesses account for approximately two-thirds of workers that lack access to a retirement plans.[61] Small employers recognize that a lack of retirement security hurts business and the overall economy; however, many of them are overwhelmed by the number of plan options, plan administration requirements and paperwork, and fiduciary responsibilities, such as selecting investment funds and managing plan assets.[62] Moreover, small business owners indicate that cost is the biggest barrier to offering a retirement savings plan.[63]

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[54] Ibid.

[55] The Economic Security Database, The Elder Economic Security Standard Index, http://www.basiceconomicsecurity.org/gateway.aspx.

[56] National Institute on Retirement Security, "Financial Security for Future Retirees: Vermont Scores 5 out of 10," http://www.nirsonline.org/storage/nirs/documents/Factsheets/VT_FSS.pdf.

[57] Goodliffe, Jay, Krisle, E., Peterson, S. & Wilson, S. (2015), "The Cost of Retiring Poor: Cost to Taxpayers of Utahns Retiring Poor," Notalys, LLC, p.1. http://www.aarp.org/content/dam/aarp/ppi/2016-03/cost-to-taxpayers-of-utahns-retiring-poor.pdf.

[58] Ibid, p. 10.

[59] The Pew Charitable Trusts (2016), "Who's In, Who's Out: A look at access to employer-based retirement plans and participation in the states." http://www.pewtrusts.org/~/media/assets/2016/01/retirement_savings_report_jan16.pdf.

[60] U.S. Census Bureau, 2012 Statistics of U.S. Businesses, "Data by Enterprise Employment Size: U.S. & State Totals". http://www.census.gov/data/datasets/2012/econ/susb/2012-susb.html.

[61] Rhee, Nari and Boivie, Ilana (2015), op. cit., p. 4.

[62] U.S. Government Accountability Office (2013), "Retirement Security: Challenges and Prospects for Employees of Small Businesses (GAO 13-748T)". http://www.gao.gov/assets/660/655889.pdf.

[63] American Sustainable Business Council and Main Street Alliance (2013), "Poll Report: Small Business Owners' Views on Retirement Security," p. 2. http://asbcouncil.org/sites/default/files/library/docs/asbc_retirement_poll_report_june2013.pdf.

The "Gig" Economy and the Changing Nature of Work Present Additional Challenges

While the advancement of technology has seen a rise in the "gig" economy, nontraditional workers have existed for several decades.[64] Millions of workers fall under nonstandard (temporary or contract) employment arrangements. This is a significant proportion of the workforce that potentially lacks access to workplace benefits such as health insurance and retirement plans, and coverage under workforce protection laws.[65] According to the GAO, the exact number of such workers depends on the definition of contingent work, and the broadest definition which covers agency temps, independent contractors, day laborers and self-employed workers is estimated to make up more than 40 percent of employed workers in the 2010 General Social Survey (GSS) data. [66]

Contingent workers were found to have different demographic and employment experiences than full-time workers. On average, they are younger, more likely to be Hispanic, more likely to have no high school diploma, and have low family income.[67] These workers earned on average 12.9 percent less per year than standard workers, controlling for the effects of part-time work.[68] In addition, the probability of contingent workers participating in a workplace retirement plan was 67.6 percent lower than for standard workers. [69]

Rising Household Debt

Overall, 80 percent of Americans hold some form of debt such as mortgages, car loans, unpaid credit card balances, medical bills, student loans, or a combination of these.[70] Older Americans are carrying more debt into retirement than in previous decades. Eight in ten baby boomers have some form of debt, and about 47 percent are still paying on their homes. For the oldest Americans who were born between 1920 and 1945, 56 percent of these retirees have debt. [71] While the rate of homeownership has remained constant over the last decade, the number of older homeowners holding mortgages has increased. [72] Mortgage debt is the largest debt that seniors carry. The median amount of older homeowners' mortgage debt increased 82 percent, from approximately $43,400 to $79,000 during the period from 2001 to 2011.[73]

Financial Challenges of Millennials

Millennials are better educated than their predecessors but also confront greater challenges, including economic uncertainty and student debt.[74] A survey of over 5,500 millennials found that only 24 percent demonstrated basic financial literacy and 8 percent showed high financial literacy.[75] Despite this, results

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[64] Gale, W. G., Holmes, S.E., & John, D.C. (2016), "Retirement Plans for Contingent Workers: Issues and Options," The Brookings Institution, p.1. https://www.brookings.edu/wp-content/uploads/2016/09/rsp923paper1-1.pdf.
[65] Ibid.
[66] U.S. Government Accountability Office (2015), "Contingent Workforce: Size, Characteristics, Earnings, and Benefits (GAO 15-168R)," p. 12. http://www.gao.gov/assets/670/669766.pdf.
[67] Ibid., p.5.
[68]Ibid., p.6.
[69] Ibid., p. 29.
[70] The Pew Charitable Trusts (2015), "The Complex Story of American Debt: Liabilities in family balance sheets," p.2. http://www.pewtrusts.org/~/media/assets/2015/07/reach-of-debt-report_artfinal.pdf.
[71] Ibid.
[72] Consumer Financial Protection Bureau, Office for Older Americans (2014), "Snapshot of older consumers and mortgage debt," p.6. http://files.consumerfinance.gov/f/201405_cfpb_snapshot_older-consumers-mortgage-debt.pdf.
[73] Ibid., p.8.
[74] George Washington Global Financial Literacy Excellence Center and PwC (2015), "Millennials & Financial Literacy – The Struggle with Personal Finance," p. 5. https://www.pwc.com/us/en/about-us/corporate-responsibility/assets/pwc-millennials-and-financial-literacy.pdf.
[75] Ibid., p. 7

from the 2012 National Financial Capability Study (NFCS) showed that most millennials were confident about their ability to make financial decisions, with nearly 70 percent of respondents rating themselves as having a high level of financial knowledge.[76]

Two-thirds of all millennials and 80 percent of college-educated millennials carry at least one source of outstanding long-term debt, and 31 percent of all millennials and 44 percent of college-educated millennials carry more than one source of outstanding long-term debt.[77] Results from the 2012 NFCS showed that 42 percent of millennials used alternative financial services such as auto title loans, payday loans, pawnshops, rent-to-own loans, and tax refund advance loans, at least once during the five years prior to the survey.[78] While 51 percent of respondents report having a retirement account (whether employer based or independent),[79] 22 percent of account owners reported taking loans or hardship withdrawals in the past 12 months.[80] According to the more recent 2016 NFCS findings, 22 percent of millennials spent more than the income they earned, and 36 percent had "medical cost difficulties" causing them to avoid medical service because of cost concerns.[81]

Financial Education and Literacy

Empowering people to make good financial decisions is important. While setting up a structure that makes it easy for employees to save is essential, so is providing them with the skills and tools needed to make the best decisions to achieve financial security.[82] Data from FINRA's National Financial Capability Study reveal that most people have very low levels of financial literacy as defined by how well people know the ABCs of finance. According to FINRA's survey, only 31 percent of respondents report having been offered financial education at school, college, or the workplace, and 21 percent say they participated.[83] Moreover, only 14 percent of respondents can answer all five financial knowledge questions including interest rate, inflation, bond price, mortgage, and risk correctly, and 37 percent can answer at least four questions correctly.[84] With the shift from DB plans to DC plans, employees are forced to make more complex investment decisions in terms of managing their own retirement accounts. The lack of financial education and knowledge among American workers makes these decisions even more difficult.

States can do more to improve the accessibility and quality of financial education. The National Association of State Treasurers has launched an initiative to offer state treasurers a comprehensive set of materials to help them create financial literacy programs. For example, a survey of the states by the Council for Economic Education found that the topic of personal finance was included in K-12 education standards in 45 states, including Vermont, but Vermont does not require districts to implement the standard.[85] In addition, 28 states, including Vermont, did not require a high school course on the

[76] De Bassa Scheresberg, Carlos and Lusardi, A. (2014), "Gen Y Personal Finances: A Crisis of Confidence and Capability," Global Financial Literacy Excellence Center, George Washington University School of Business, p. 15. http://gflec.org/wp-content/uploads/2015/01/a738b9_b453bb8368e248f1bc546bb257ad0d2e.pdf.

[77] George Washington Global Financial Literacy Excellence Center and PwC (2015), op. cit., p. 10.

[78] De Bassa Scheresberg, Carlos and Lusardi, A. (2014), op. cit., p. 14.

[79]Ibid., p. 11.

[80] Ibid., p. 14.

[81] FINRA, "A Millennial's Guide to Financial Capability." http://www.finra.org/investors/highlights/millennials-guide-financial-capability.

[82] Lusardi, Annamaria, "Employees Financial Wellness: New Strategies for State-Sponsored Retirement Plans (Blog Post)," Georgetown University Center for Retirement Initiatives. http://cri.georgetown.edu/employees-financial-wellness-new-strategies-for-state-sponsored-retirement-plans/.

[83] FINRA Investor Education Foundation (2016), "Financial Capability in the United States," p. 32. http://www.usfinancialcapability.org/downloads/NFCS_2015_Report_Natl_Findings.pdf.

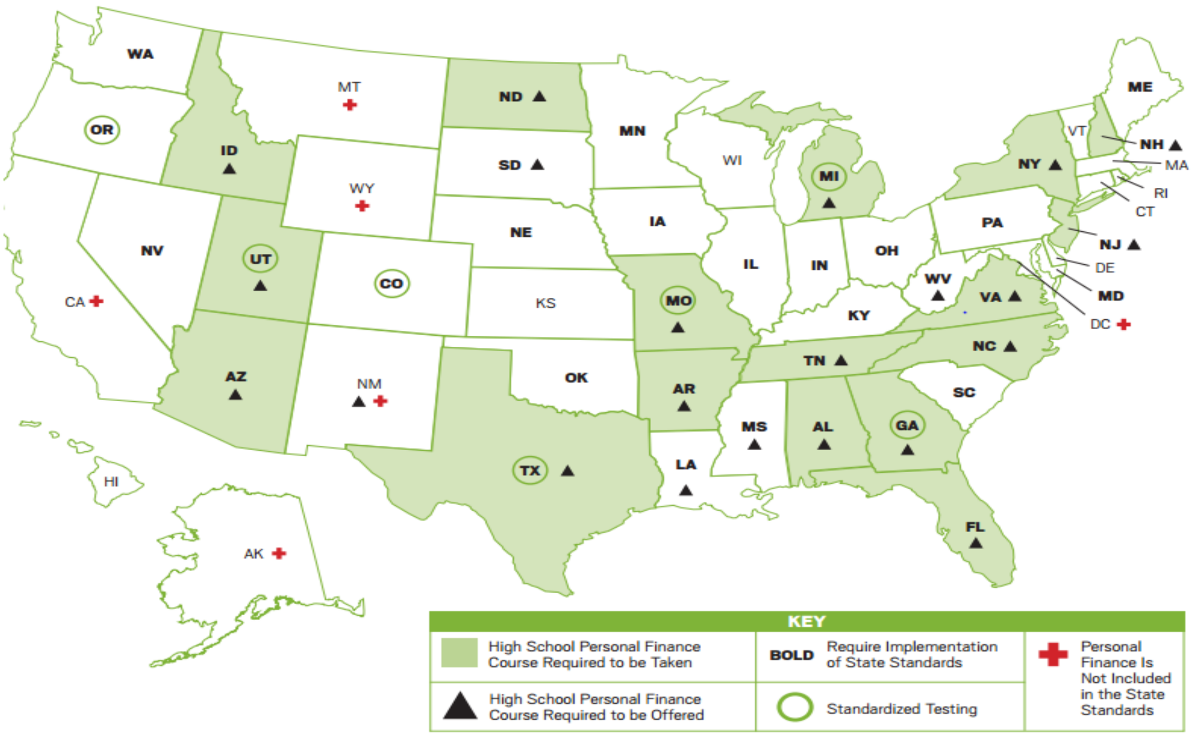
[84] Ibid. p.28.

[85] Council for Economic Education (2016), "Survey of the States: Economic and Personal Finance Education in our Nation's Schools 2016", p. 8. http://www.councilforeconed.org/wp/wp-content/uploads/2016/01/2016-Survey-of-the-States-Final.pdf.

subject to be offered, and only seven states included it in standardized tests.[86] (Chart 4)

CHART 4

Personal Financial Education in School Curricula Across the Nation



Source: Council for Economic Education.

Strategic Behavioral "Nudges" Overcome Saving Barriers

While people often fail to save for retirement, behavioral economics offers explanations and solutions on why individuals do not act in their best interests when it comes to retirement saving. [87] In his book "Misbehaving – The Making of Behavioral Economics," economist Richard Thaler outlines three reasons why people often fail to save for retirement: (1) inertia or failure to act, which explains why people do not begin to start saving even when they have the opportunity; (2) loss aversion, which explains why people avoid taking actions perceived as reducing their paycheck; and (3) the lack of self-control that contributes to choosing actions that provide immediate gratification rather than planning for the future.[88] In addition, behavioral nudges have been discussed in both public and private sectors in terms of improving retirement programs' effectiveness in policy design.

The behavioral nudges that policymakers need to consider include auto-enrollment and auto-escalation. Behavioral studies tell us when faced with overly complex choices people are more likely to use

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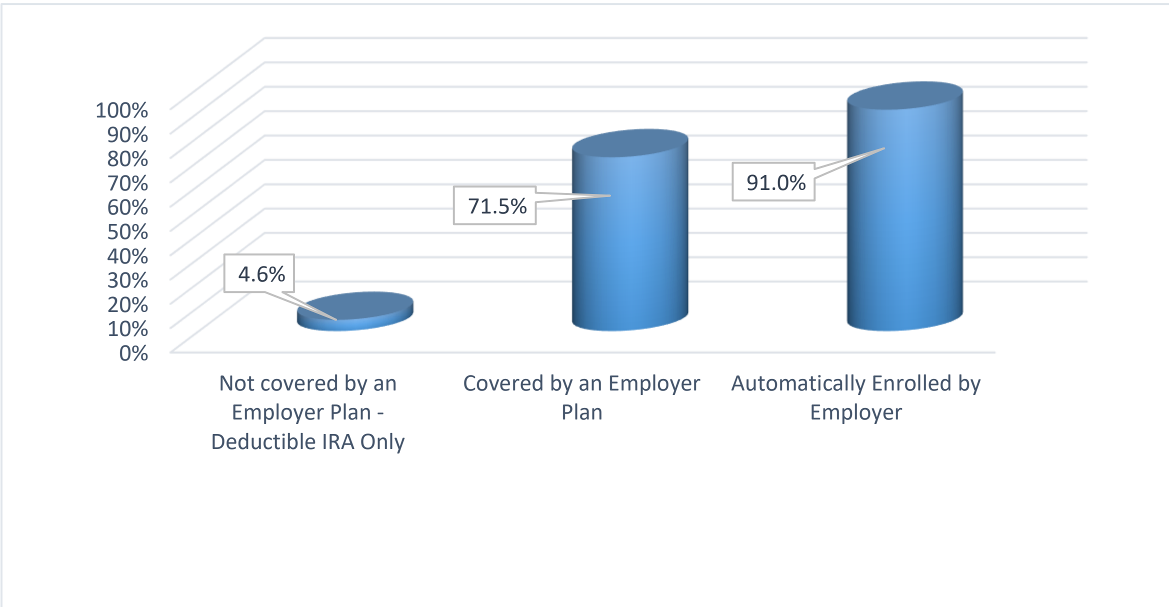
[86] Ibid.
[87] This section is drawn from Antonelli, A. and Yin, Y. (2016), "What We Know About Retirement Savings: Why Strategic Behavioral "Nudges" Make Sense (Blog Post)," Georgetown Center for Retirement Initiatives. http://cri.georgetown.edu/what-we-know-about-retirement-savings-why-strategic-behavioral-nudges-make-sense/.
[88] Ibid.

strategies that require the least effort. The use of automatic enrollment in employer-sponsored retirement plans have been shown to increase employee participation in DC plans in numerous studies. Research has shown when employees are offered a plan, about 70 percent voluntarily participate; when workers are automatically enrolled in a plan, with an option to opt out, participation jumps to about 90 percent.[89] (Chart 5)

Chart 5

Participation Rates Significantly Increase with the Power of Auto-Enrollment



Source: Data compiled by AARP's Public Policy Institute from unpublished estimates from the Employee Benefit Research Institute of the 2004 Survey of income and Program Participation Wave 7 Topical Module (2006 data). See also Brookings' Retirement Security Project and WhiteHouse.gov. Auto-Enrollment Data provided by Vanguard.

A Vanguard study of over 500,000 new hires across 460 plans found the participation rate with automatic enrollment to be 91 percent compared to 42 percent with voluntary enrollment. Participation rates rose most for young and low-income workers, with 87 percent of employees earning less than $30,000 participating when automatically enrolled, compared to only 22 percent with voluntary enrollment. Participation for employers younger than 25 was 90 percent with automatic enrollment compared to just one-quarter with voluntary enrollment.[90] Participation in plans with Prudential Retirement with automatic enrollment had a 90 percent participation rate, compared 62 percent for those without automatic enrollment. [91] This high level of participation with automatic enrollment remained constant and was not subject to significant opt-out rates over time.[92]

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[89] Ibid.

[90] Clark, Jeffrey W., Stephen P. Utkus & Jean A. Young. (2015). "Automatic Enrollment: The Power of Default," Vanguard Center for Retirement Research, p.5. https://institutional.vanguard.com/VGApp/iip/site/institutional/researchcommentary/article/InvResAutoEnrollDefault.

[91] Prudential Financial (2015), "Overcoming Participant Inertia," p. 6. http://www.prudential.com/media/managed/overcoming-participant-inertia.pdf.

[92] Ibid.

In 2008, the United Kingdom (UK) enacted the Pensions Act which introduced a new set of pension reforms including requiring employers to automatically enroll eligible workers into qualifying workplace pension programs.[93] The new employer responsibilities began implementation in October 2012 starting with the largest employers and will continue through 2018.[94] A survey conducted by the UK Department of Work and Pensions between May and September of 2015 found that across all employer sizes, the average opt-out rate was 10 percent, with rates slightly higher for small and medium employers than for large employers.[95]

Retirement Plan Access and Participation in Vermont

AARP's analysis of the number of uncovered workers by state estimates that approximately 45 percent of private wage and salaried workers in Vermont—104,000 workers—are not covered by an employer sponsored retirement plan. Of this group, more than one-half of Hispanic and Black private sector workers are uncovered.[96]

Among full-time private sector workers,[97] one-third lack access to a workplace retirement plan from their employer.[98] For workers who do have access to an employer-sponsored plan, participation is 85 percent.[99] Retirement plan access is the lowest for firms with fewer than 10 employees, for the youngest workers (between the ages of 18 to 29), and for workers earning less than $25,000. [100]

Small Businesses Less Likely to Provide Plan Access

The share of private sector workers who are not covered by an employer-sponsored plan increases as firm size decreases. At firms with more than 1000 employees, 26.2 percent of workers are uncovered, while 77.7 percent of workers at the smallest firms with under 10 employees are uncovered (Chart 6). This is especially noteworthy for Vermont because small businesses play a significant role in the state's economy. Firms with fewer than 100 employees account for 94 percent of the state's businesses[101] and employ about 43 percent of the state's private sector workforce. [102]

Lower-Income and Part-time Workers are More Likely to Lack Access

Private sector workers at the lowest income quintile are more than three times likely to be uncovered by a workplace retirement plan than those at the highest quintile. [103] The percentage of workers earning

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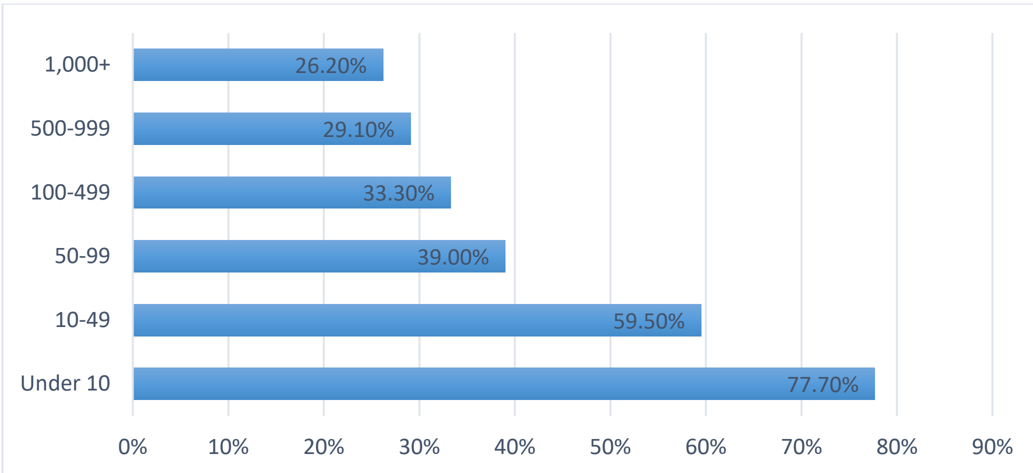
[93] UK National Employment Savings Trust (NEST), "New pension rules." http://www.nestpensions.org.uk/schemeweb/NestWeb/public/pensions/contents/new-pension-rules.html
[94] Ibid.
[95] UK Department for Work and Pensions (2015), "Automatic Enrolment evaluation report 2015," p. 60. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/477176/rr909-automatic-enrolment-evaluation-2015.pdf.
[96] AARP (2015), "Fact Sheet: Vermont - Workplace Retirement Plans Will Help Workers Build Economic Security." http://www.aarp.org/content/dam/aarp/ppi/2015-08/aarp-vermont-fact-sheet.pdf.
[97] Most estimates of uncovered workers either count only full-time, full year workers or also add in hourly wage worker, part-time part year workers. These differences account for some of the differences in the estimates of uncovered workers.
[98] The Pew Charitable Trusts (2016), "Employer-based Retirement Plan Access and Participation across the 50 States: Vermont." http://www.pewtrusts.org/en/multimedia/data-visualizations/2016/employer-based-retirement-plan-access-and-participation-across-the-50-states.
[99] Ibid.
[100] Ibid.
[101] U.S. Census Bureau (2016), 2014 Statistics of U.S. Businesses, "Data by Enterprise Employment Size: U.S. & States." http://www.census.gov/data/tables/2014/econ/susb/2014-susb-annual.html.
[102] U.S. Small Business Administration, Office of Advocacy (2016), "Small Business Profile: Vermont." https://www.sba.gov/sites/default/files/advocacy/Vermont.pdf.
[103] AARP (2015), "Fact Sheet: Vermont - Workplace Retirement Plans Will Help Workers Build Economic Security." http://www.aarp.org/content/dam/aarp/ppi/2015-08/aarp-vermont-fact-sheet.pdf.

$14,000 or less—the lowest quintile—who are uncovered is 70.7 percent, while the percentage of workers earning over $63,500—the highest quintile—who are uncovered is 19.5 percent (Chart 7).

CHART 6

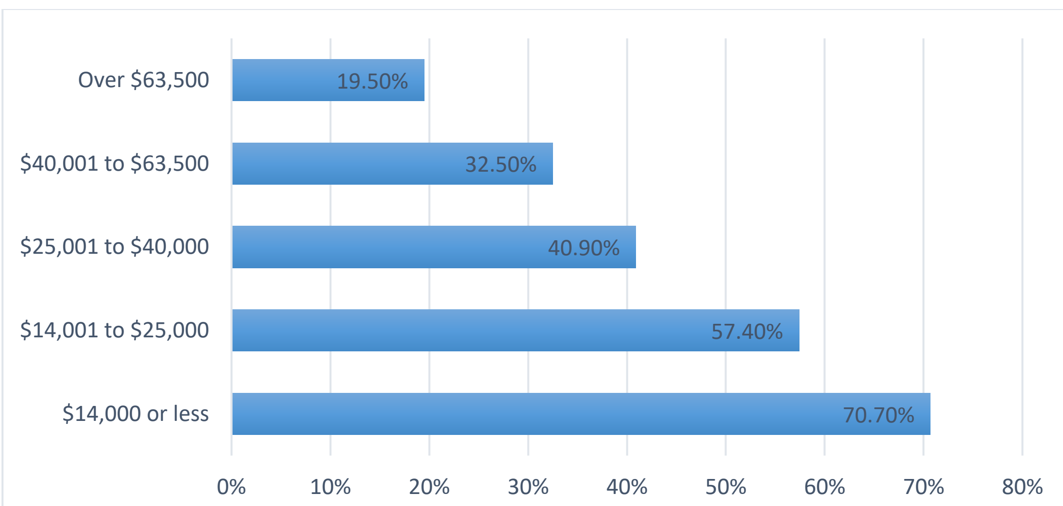
Percent of Uncovered Private Sector Workers by Employer Size in Vermont



Source: AARP's analysis from the U.S. Census Bureau's Current Population Survey, March Supplements, 2012-2014; AARP (2015), Fact Sheet: Vermont-Workplace Retirement Plans Will Help Workers Build Economic Security

CHART 7

Percent of Uncovered Private Sector Workers by Earning Quintile in Vermont



Source: AARP's analysis from the U.S. Census Bureau's Current Population Survey, March Supplements, 2012-2014; AARP (2015), Fact Sheet: Vermont-Workplace Retirement Plans Will Help Workers Build Economic Security

Among part-time workers in Vermont, 39 percent lack access to employer-sponsored retirement plans.[104] For those who do have access to such plans through their employers, only 22 percent

[104] The Pew Charitable Trusts (2016), "Who's In, Who's Out: A look at access to employer-based retirement plans and participation in the states," p.27. http://www.pewtrusts.org/~/media/assets/2016/01/retirement_savings_report_jan16.pdf.

participate in those plans.[105] As noted previously, the rise of the "gig" economy and expansion of the contingent workforce poses new challenges for estimating the size of the uncovered workforce.

Number of Uncovered Workers May Be Underestimated – Lesson from Oregon

These data on access and participation for Vermont are likely to be low-end estimates. When Oregon began to study the size of its uncovered population, data sources suggested that roughly 45 percent, or approximately 600,000 workers were uncovered.[106] Once they hired a firm to do a market analysis, the state soon discovered the number of uncovered workers potentially eligible for its state-sponsored retirement plan was over 1 million workers or approximately 60 percent of the workforce.[107] The population can be broken down into three categories: the original estimate of workers whose employers do not offer any retirement plan (590,000) and then adding to this the workers who are ineligible for the plans offered by their employers (259,000) and the self-employed (201,000).[108] The Oregon Retirement Savings Plan (ORSP) is planning to automatically enroll the first two categories of workers, and the state has expressed interest in allowing the self-employed to opt in.[109]

Implications for Policy

States are leading the way to develop innovative approaches to address the retirement plan coverage gap. Working collaboratively with the federal government, states and cities are exploring several plan design options. Each of these options needs careful consideration to determine what will work best for the residents of Vermont.

Vermont's population is aging and will become a larger portion of the state's population between now and 2032. Today, its retirees already rank only average nationally on a scale of retirement financial readiness and their income levels in retirement are below what is considered necessary to meet basic needs. Small businesses, which make up a larger proportion of Vermont's business community, are among the least likely to provide workers with access to a retirement savings plan.

The retirement security challenge in Vermont is as real, if not more so, than it is for the rest of the nation. Workers are much more likely to save if they have a simple, low-cost, easily accessible way to save. Vermont can be a leader by exploring new public-private partnerships to create a retirement plan for its uncovered private sector workers. This report will outline some of the policy design options and features being implemented and considered by states.

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[105] Ibid.

[106] Oregon State Treasury (2016), "Oregon Retirement Savings Plan: Helping Oregonians Invest for a More Secure Future," p. 5. https://www.oregon.gov/retire/SiteAssets/Pages/Newsroom/Overview%20-%20Oregon%20Retirement%20Savings%20Plan.pdf.

[107] Center for Retirement Research at Boston College (2016), "Oregon Market Research Report," p. 1. http://www.oregon.gov/treasury/ORSP/Documents/ORSP%20Market%20Analysis%2013JULY2016.pdf.

[108] Ibid.

[109] Ibid.

II. Plan Design Options for State-Sponsored Retirement Programs

There is a range of DC options available for states interested in expanding the availability and effectiveness of retirement plans for their private sector employers and employees. These design options fall into three categories:

1. Defined Contribution Plans (IRAs, MEPs, Prototypes)
2. Marketplace
3. Combination or Multi-Tiered Programs (combinations of the first two options)

Each of these programs can be designed to define the role of employers, employees, plan administration and asset management. There has been confusion regarding how federal law would affect the design and operation of a state-sponsored retirement plan, for example:

- Is the plan covered by the federal Employee Retirement Income Security Act (ERISA); and
- What are the basic federal income tax, securities laws, and other legal or regulatory considerations with which any program (ERISA-regulated or not) must comply?

Because this is a new area for states, most are not familiar with how federal laws would apply. State public employee pension plans have always been exempt from ERISA, which was enacted in 1974 to protect private sector employee benefit plans, including retirement plans.[110] As states now contemplate ways to help expand the availability and effectiveness of private sector retirement plan options, they must understand how ERISA and other federal laws would apply to any new program for the private sector.

States are already familiar with public pension plans. They primarily manage DB plans, in which states are their own fiduciaries, have responsibility for the returns on investments, and promise retirees a certain benefit. The pension plan's funds are often pooled and professionally managed. Because of their fiduciary responsibilities, state public employee pension plans are keenly aware of the risks of their portfolio in down markets and the importance of recruiting and retaining high-quality employees and advisors to manage those investments. Because states are already familiar with fiduciary duty and sound investment policy, federal requirements under ERISA and other laws, which have similar provisions, should not be unfamiliar.

Why ERISA Matters

ERISA exempts federal, state, or local governmental plans;[111] however, a plan created and/or operated by a government for private sector employees would not be considered a governmental plan. A state could not escape ERISA regulation simply by bringing private sector workers into its own retirement system.

ERISA can affect a state's retirement initiative in one of two ways.[112] First, a retirement program that is considered an ERISA "pension plan" must comply with ERISA, including its framework for establishing and running the plan, fiduciary duties of prudence and acting in the best interest of participants and beneficiaries, participant disclosure and government reporting requirements, dispute resolution, and

[110] 29 U.S.C. Sec. 1001 *et seq.*
[111] ERISA Sec 3(32), 4(b)(1).
[112] This paper follows the common usage that the term "ERISA" only refers to the fiduciary, participant safeguards, reporting and disclosure, and enforcement rules found in Title I of ERISA. Technically, the Internal Revenue Code (Tax Code) rules that govern the favorable income tax treatment afforded to qualified retirement plans also are found in ERISA, in Title II. With a few exceptions, the Department of Labor (DOL) regulates Title I and the Internal Revenue Service (IRS) regulates Title II.

prohibited transactions rules. Second, regardless of whether the plan is an ERISA plan, ERISA preempts any state law that relates to an "employee benefit plan." ERISA preemption is of concern for states wishing to require that employers provide some form of savings vehicle to employees. As will be discussed in greater detail below, a state "auto-IRA" program that is not considered to be an ERISA-regulated retirement plan under a recent U.S. Department of Labor (DOL) safe harbor is much more likely to win a preemption challenge even with an employer mandate. On the other hand, ERISA regulated DC plans have advantages over IRAs.

While much of the policy discussion to date has been focused on auto-IRAs designed to be exempt from ERISA, there also are state plan design options covered by ERISA. Policymakers can and should determine which plan design option is most suitable to achieve their desired policy goals.

Defined Contribution Retirement Savings Plans

There are several types of DC plan design options available for states to consider. Some options are not considered subject to ERISA, while other options would be considered ERISA-based plans.

The ***ERISA-exempt*** defined contribution options available to states:

1) Voluntary payroll deduction individual retirement accounts (IRAs);
2) Mandatory state-sponsored payroll deduction IRAs using automatic enrollment (auto-IRAs); and
3) Voluntary federal myRA program.

The ***ERISA-based*** defined contribution options available to states:

1) Voluntary open multiple employer plans (MEPs);
2) Voluntary master and prototype plans; and
3) Voluntary marketplace (ERISA applies only to the products, not the marketplace itself)

A Marketplace can allow employers to shop for both non-ERISA payroll deduction IRAs and more robust ERISA employer retirement programs.

It is important to note that most of the options above are voluntary participation for the employer and always voluntary for employees. There is only one option – mandatory auto-IRAs - where employer participation is mandated by the state and automatically enrolls employees and even then, employees have the right to opt out of participation.

To date, five of the eight states that have adopted programs (California, Connecticut, Illinois, Maryland, and Oregon) have enacted some form of a mandatory payroll deduction IRAs utilizing auto-enrollment. (Appendix B) Washington and New Jersey have enacted marketplace models, and Massachusetts has a small master and prototype program for nonprofits. (Appendix C)

ERISA-Exempt IRA Programs

This section describes the basic features of IRA programs that are exempt from ERISA.

State-Sponsored Payroll Deduction IRAs

The plan design option that ordinarily would not be subject to ERISA would be IRAs.[113] Any employee or self-employed person can set up an IRA by signing up and depositing money with a bank, insurance company, mutual fund, or custodian. IRAs are typically set up, controlled, and funded by an individual,

[113] See ERISA Sec. 4(a) (requiring that a plan be established or maintained by an employer or union (or both) to be covered by ERISA). Technically, under the Tax Code an IRA may be either an individual retirement account or an annuity.

not his or her employer. The individual controls the account and may invest in just about anything, including mutual funds, stocks, bonds, and annuities, but not art, jewelry, and other "collectables."

For most individuals, the contributions are tax-deductible and tax penalties apply to "early" withdrawals. In addition to a traditional IRA, most earners can contribute to a Roth IRA for which contributions are not deductible, but withdrawals, including accumulated investment income, can be 100 percent tax-free. Special limits on traditional IRA tax deductions and eligibility to make Roth contributions apply to high-income individuals.

IRAs can be a simple, low-cost alternative for retirement savings. As discussed in the next section, employers can offer payroll deduction IRAs to their employees, process employee contribution elections, and transmit the contributions to the IRA vendor without triggering ERISA regulation if the level of employer involvement is kept to a minimum.

Federal Legal and Regulatory Issues: DOL Rule and ERISA Exemption

The DOL issued rules that guide the use of payroll deduction IRAs for both employers and more recently for state-sponsored retirement savings programs.

DOL's Original 1975 ERISA Safe Harbor for Payroll Deduction IRAs. The original DOL safe harbor[114] outlines conditions under which payroll deduction IRAs offered by employers would not be treated as ERISA plans. The DOL has ruled that an employer IRA payroll deduction program is not an ERISA plan if: [115]

- It is employee-pay-all (the employer does not make any contributions);
- Employee participation is completely voluntary;
- Employer involvement is limited to making the program known to employees, without endorsement, processing payroll withholding elections, and answering questions; and
- The employer is not paid for offering the program.

This original safe harbor addressed only voluntary payroll deduction programs and did not consider automatic employee enrollment with an opt-out that we now know helps boost participation in employer-sponsored plans. For states interested in addressing the retirement savings challenge, the question of whether and how federal laws would apply to their new mandatory "auto-IRA" programs, especially if there was an employer mandate, became a source of uncertainty and made some states hesitant to advance their own programs. More specifically, would such state plans be exempt from ERISA?

New Additional DOL ERISA Safe Harbor for Auto-Enroll IRAs. In response to the large number of states with new programs (e.g., California, Connecticut, Illinois, Maryland, Massachusetts, New Jersey, Oregon and Washington) or considering legislative proposals, the Obama Administration moved quickly to address these concerns with the issuance of a new DOL safe harbor, effective October 31, 2016, exempting certain state-sponsored IRA programs from ERISA. The DOL noted that the safe harbor is just that, and a state program that does not follow the new regulation could still be determined to be exempt.

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[114] See 29 CFR 2510.3-2(d); 40 FR 34526 (Aug. 15, 1975)

[115] DOL Reg. Sec. 2510.3-2(d)

The new safe harbor's conditions focus largely on three key areas.[116]

The state's role in the program:

- The program must be established pursuant to state law;
- The program is implemented and administered by the state that established the program, though the state may implement and administer the program through a governmental agency or instrumentality;
- The state must be responsible for the security of payroll deductions and employee savings;
- The state must adopt measures to ensure that employees are notified of their rights under the program and create mechanisms for enforcing those rights;
- Allow state law to delegate a wide array of implementation and administrative authority; and
- Allow states to decide which employers and employees, if any, should be covered by a state mandate (for example, employers that do not offer other workplace savings arrangements).

The employer's role in the program:

- The employer's role must be limited to ministerial activities (collecting payroll deductions and remitting them to the program). Such duties include: maintaining records of the payroll deductions and remittance of payments, providing information to the state necessary for the operation of the program, and distributing program information from the state program to employees;
- Employers cannot contribute employer funds to the IRAs; and
- To the extent employees will be auto-enrolled, employer participation in the program must be required by state law.

Employee rights:

- Employee participation in the program must be voluntary;
- If the program requires automatic enrollment, employees must be given adequate notice and have the right to opt out; and
- Employees must be notified of their rights under the program, including the mechanism for enforcement of those rights.

In addition, the new safe harbor provides some guidance about other aspects of program design, including:[117]

- *Withdrawals and leakage*: The final rule allows state discretion regarding restrictions on employee withdrawals from a state program.[118] Some states wanted the ability to discourage pre-retirement spending (leakage) or to offer certain diversified, low-cost annuity, insured and other investment strategies that would be hampered if employees could make unrestricted withdrawals. [119]

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[116] 29 CFR Part 2510.3-2(h). See also the summary of the DOL rulemaking prepared by the Groom Law Group (2016), "DOL Finalizes Regulation on State Automatic IRAs and Proposes Extension to Cities and Other Political Subdivisions." http://www.groom.com/media/publication/1744_DOL%20Finalizes%20Regulation%20on%20State%20Automatic%20IRAs%20and%20Proposes%20Extension%20to%20Cities%20and%20Other%20Political%20Subdivisions.pdf.

[117] Ibid.

[118] 81 Fed. Reg. 59,467 (August 30, 2016)

[119]See public comments submitted to DOL at https://www.dol.gov/agencies/ebsa/laws-and-regulations/rules-and-regulations/public-comments/1210-AB71.

- *Use tax incentives or credits*: States may provide tax incentives for employers to participate in the state programs if they reflect a reasonable approximation of the employer's costs under the program.[120] This caveat is important because the DOL does not believe states should provide tax credits or incentives in a way that provides the states with an unfair advantage over the private sector market to provide such products to employers.

- *Voluntary participation for firms below a mandated threshold:* States, such as Illinois, mandate employer participation for firms with 25 or more employees. The state also would like firms with fewer than 25 employees who lack a retirement plan for its workers who want to participate in the state's program to be able to do so. In the case that a state allows, but does not require, an exempted employer to enroll employees in the program, the employer could still enroll employees in the state program if the employer does not make payroll deductions for employees without their affirmative consent (opt-in needed).[121]

- *Employers and state boundaries*. Auto-enrollment is limited to employees affected by the employer mandate. If the U.S. Constitution's prohibition against states unduly interfering in interstate commerce would prevent a state from imposing a mandate on a local employer's out-of-state employees, those employees could not be auto-enrolled under the safe harbor. However, two or more states could establish a joint auto-IRA program if auto enrollment was limited to employees covered by one of the respective state's mandates.

The DOL views an employer that voluntarily chooses to automatically enroll its employees in a state payroll deduction savings program as establishing an employee benefits plan under ERISA because employee participation is not completely voluntary per the original 1975 safe harbor. [122] The distinction drawn by DOL in the new safe harbor is that the use of auto-enrollment by the employer when mandated by the state to do so is simply complying with a state requirement; limited employer involvement is the key to a determination that the employer has not established or maintained an employee pension benefit plan. Although a new incoming White House has created some uncertainty with respect to whether the new DOL safe harbor will remain in place, the incoming Administration has not yet made any public statements to date to suggest the rule will be reversed.[123]

To summarize, DOL's safe harbors provide states with two options for the use of payroll deduction IRAs: (1) a payroll deduction IRA program with voluntary employer participation but employers cannot use auto-enrollment; and (2) a payroll deduction IRA in which employer participation is mandatory and because the state mandates employer participation, the state also can mandate the use of auto-enrollment (the primary distinction is that the state and not the employer is making the decision to auto-enroll employees).

State Action: California, Connecticut, Illinois, Maryland, and Oregon Laws (Appendix B)

Five states have enacted laws establishing mandatory IRA programs. These states—California, Connecticut, Illinois, Maryland, and Oregon—have some program design differences, such as what types

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[120] 81 Fed. Reg. 59,467 (August 30, 2016)
[121] 81 Fed. Reg. 59,471 (August 30, 2016)
[122] 81 Fed. Reg. 59,465 (August 30, 2016)
[123] At the same time it issued the final state rule on August 30, 2016, DOL also issued a proposed rule that would allow the same conditions to apply to state political subdivisions (e.g., cities and counties). The final rule for state political subdivisions was published on December 20, 2016 (81 Fed. Reg. 92639).

of employers are mandated to participate, the employer threshold for mandatory participation in the state program, default contribution levels, account structures (traditional vs. Roth IRA), use of auto-escalation, administrative fee limits, and the use of tax and other incentives. Appendix B presents an overview of the plan design features for each of these five states. These design features will be discussed in greater detail in Sections IV, V and VI of this report. Oregon is expected to be the first state to launch its mandatory auto-enroll IRA program and accept participants in a phased rollout beginning in the summer of 2017.

Federal myRA Program (Roth IRA)

Beginning in November 2015, the U.S. Treasury Department launched the myRA retirement savings program.[124] The myRA program may be of interest to policymakers as either a program that could be offered in a marketplace or as a "starter" vehicle for an auto-IRA that would allow participants in the state program to accumulate funds in a safe, low-cost investment before being switched to a diversified investment platform. Participants save using a Roth IRA invested in a specially created Treasury instrument, with no risk of principal loss. Contribution, income and tax rules for Roth IRAs apply (Appendix A). Participation in the program is voluntary. There are no costs to opening an account or other fees and employers are not permitted to administer, contribute to or match employee contributions. Participants cannot be automatically enrolled in this program through their employer, but would have to affirmatively elect to contribute. Employers would share myRA information with employees and can set up payroll deduction for their employees or inform them of other ways that they can fund their accounts. Once a participant's account reaches $15,000 or has been held for 30 years, it must roll over into a private Roth IRA. In a December 2014 letter from the DOL to the U.S. Treasury Department, DOL concluded that the federal myRA program is not subject to ERISA.[125]

State Action: California, Washington State, and New Jersey (Appendices B & C)

As noted, states may consider whether and how they want to include the myRA accounts in their programs. California's new law specifies that it will invest in Treasury bonds, myRAs or similar investments for up to the first three years of program implementation. Considered a very safe investment as the program launches, California's Board will then determine what its investment policy will be after the initial three-year period.

Washington State and New Jersey's marketplace laws allow for the federal myRA program to be among the offerings in the marketplace. Washington State is currently working closely with the U.S. Treasury Department to integrate the federal myRA program into its marketplace, which is scheduled to launch in a phased rollout beginning in mid-to-late January 2017.

ERISA-based DC Plans

This section reviews the two ERISA-based plan design options: state-sponsored Multiple Employer Plans (MEPs) and prototype plans. A MEP allows small and mid-sized employers to band together to create economies of scale in a turnkey DC plan. A prototype and similar arrangements involve a user-friendly means for employers to establish their own separate plans. While a prototype program could include an established investment and recordkeeping platform, each employer would have its own plan. Both

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[124] U.S. Department of the Treasury, myRA. https://myra.gov/.
[125] Canary, John J., Information Letter to the U.S. Department of the Treasury on December 15, 2014. https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/information-letters/12-15-2014.

MEPs and prototypes are covered by the ERISA, tax, and other federal laws that are discussed in detail later in Section III.

As a practical matter, whether through a MEP or prototype, the plan itself would be a 401(k)—a specialized employer DC retirement plan to which employees may make tax-deductible contributions from their wages. A 401(k) is an ERISA-covered retirement plan. Contributions are typically invested by the employees from a menu of investments selected by the employer. Employers also may make contributions into employees' accounts. The employee contribution limits are much higher for a 401(k) than an IRA. If the plan permits, participants may make Roth 401(k) contributions. The plan also may allow employees to borrow from their account. As with IRAs, penalties apply on "early" withdrawals.

State Sponsored Multiple-Employer Plans (MEPs)

What is a MEP? A MEP is a "pension plan" covered by the full scope of ERISA and the Tax Code "qualified" plan rules. As a single plan, all MEP assets are pooled to pay the benefits and cover costs.[126] In other words, all participants "eat from the same pot." MEPs predate ERISA and the current Tax Code. In the early days, most MEPs were DBs. Since 1989, when the funding rules changed to essentially make each employer responsible for the underfunding of the other participating employers, virtually all MEPs have been 401(k) and other DC plans.[127] The IRS and DOL appear to have different views on what it takes to be a MEP. The IRS has ruled that the combined plan of unrelated employers is a MEP if the program's assets are combined in one pool, without any employer-by-employer segregation.[128]

Technically, because the MEP is considered a single plan, all plan assets are available to pay plan creditors. With a 401(k) or other DC plan where each participant's benefits is held in an individual account and, unlike a DB plan, there is no possibility of unfunded liabilities. Pooling of all assets should not put any participant's account at additional risk from fraud, mismanagement, or other incompetent or nefarious behavior by other employers or participants. Importantly, pooling the assets of numerous small and mid-sized employer 401(k) programs should allow the MEP to accumulate sufficient assets to negotiate low investment, recordkeeping, and other fees.

However, the DOL has had an extra requirement for MEPs: unrelated employers can maintain a single plan only if they "are tied together" by "a genuine economic or representational interests." [129] Whether a group of employers is sufficiently tied in an "affinity group" is not mentioned in ERISA as a MEP requirement.

Federal Legal and Regulatory Issues: DOL Guidance for MEPs

On November 18, 2015, the DOL released an Interpretive Bulletin[130] relating to state savings programs that sponsor or facilitate savings options for private sector workers through ERISA-covered retirement plans covering MEPs, master and prototype plans, and marketplaces. The benefits of ERISA-covered plans include higher contribution limits, the ability of both employers and employees to contribute, and numerous service providers experienced in administrating ERISA 401(k) plans. However, ERISA does require participation by employers and employees to be voluntary.[131]

Open vs. Closed MEPs. Because of DOL's recent Interpretive Bulletin 2015-12, a government-sponsored MEP enjoys greater operational freedom than one sponsored by a private sector entity. Specifically, a

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126 Sec. 1.413-3(a)(2)(i); Sec. 1.414(l)-1(b)(1)
127 IRC Sec. 413(c)(4).
128 IRC Sec. 413; Treas. Reg. Secs. 1.413-2 and 414(l).
129 DOL Advisory Opinion 2012-04A, May 25, 2012.
130 80 Fed. Reg. Summary. (November 18, 2015)
131 See, 80 Fed. Reg. 71,938 (November 18, 2015)

MEP sponsored by a state or local government may allow any business employing state residents to join the program. These so-called "open" MEPs would allow, for example, a state to create a unified program available to all employers. This discussion assumes that any state-sponsored MEP would be open.

A separate trust would hold contributions made by participating employers, employer's employees, or both. The state, or designee, would be the plan sponsor and named fiduciary and plan administrator for administering the plan and could contract out to private sector providers to do so. Under a state MEP, each employer that participates would not be considered to have established its own ERISA plan, rather DOL would consider this arrangement a single ERISA plan.[132] Therefore, the state would have economies of scale in lowering administrative and other costs.

The state MEP would be distinguishable from other business enterprises that underwrite benefits or provide administrative services to several unrelated employers because the DOL views a state as having a unique representational interest in the well-being of its citizens that connects it to the in-state employers that choose to participate in the plan. Therefore, the state would be acting indirectly in the interest of the participating employers, which is in line with the requirement under Title I of ERISA relating to a person, other than an employee organization, who wishes to sponsor an employee benefit plan.

Although participation in a state open-MEP must be voluntary, its plan design features can include the use of auto-enrollment and auto-escalation, features that are not available to payroll deduction IRAs unless the state mandates employer participation.

While DOL's guidance allows for state open-MEPs, it did not extend the guidance to "open" MEPs for privately established plans and this has been subject of several congressional proposals in recent years.[133]

Establishing a State MEP. A MEP must have a plan sponsor, which could be the state itself, but more likely a board, committee or other entity appointed or created by the state through enabling legislation. For convenience, this discussion will use the term "board" to refer to all government-appointed administrators. The board would set the program's terms, prepare plan documents and select investments, hire trustees, custodians, recordkeepers and other service providers. Employers would voluntarily join the MEP by signing an adoption agreement.

DOL rules allow cities, counties and other state political subdivisions to sponsor MEPs. For convenience, this discussion refers to "states," although the same federal rules apply to state political subdivisions.

Why MEPs? A MEP offers several advantages for employers, especially smaller to mid-sized employers, and their employees. First, by commingling assets a MEP may achieve the economic heft to obtain lower investment and administrative fees, more sophisticated investment opportunities, top-shelf service providers and add-ons like financial education and advice. Second, a MEP offers employers a simplified, turnkey process for obtaining a plan document, selecting and monitoring the investment platform and the recordkeeper, IRS reporting, obtaining an independent audit, and similar chores.

Finally, by outsourcing most of the heavy lifting to the sponsor and its team of outside experts, employers can significantly minimize their exposure to possible ERISA liability. Today, small businesses

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[132] 80 Fed. Reg. 71,938 (November 18, 2015)

[133] For example, the Retirement Enhancement and Savings Act of 2016 (S. 3471) was introduced by Senator Orrin G. Hatch (R-UT) on November 16, 2016. This bill includes retirement savings reform which would make multiple employer plans more attractive by eliminating barriers and improving the quality of MEP service providers. For more information about other private sector MEP related proposals, please see http://cri.georgetown.edu/federal-legislative-proposals/.

tend to avoid offering retirement benefits because they are too expensive and too time-consuming to manage, and they expose the company to liability if something goes wrong. On the other hand, the economies of scale generated by numerous businesses joining in a single plan should make a state-sponsored program less expensive and the board with its selected cadre of investment managers, advisors and service providers make the plan more attractive to employers.

Participating employers in a state-sponsored program that is a MEP also should have minimal ERISA fiduciary responsibility (basically whether to join, remain in, or leave the plan) and thus, minimal liability exposure. In a non-MEP collection of single plans, each employer may be viewed as having greater fiduciary responsibility for plan functions and thus, greater potential liability. Also, as discussed in Section III, MEPs enjoy exemption from the federal securities laws that could otherwise treat the program as a "security" or "regulated investment company."

There are several regulatory and cost advantages to being treated as a MEP. As a MEP, one IRS Form 5500 Annual Report is filed, one ERISA fidelity bond purchased, and a single annual audit by an independent accountant conducted for the entire plan.

State Action

To date, no state has proposed a program that is solely a state-sponsored MEP. However, the New York City Comptroller's Office and Massachusetts have explored combining a MEP option with other options. These combination or multi-tiered approaches are discussed more in the subsection "State Sponsored Combination or Multi-Tiered Models."

Master and Prototype Plans

To establish a prototype plan, a provider would develop standard form 401(k) or other tax-favored retirement plans (i.e., SIMPLE-IRA plans) and obtain IRS approval. Each employer, in adopting the prototype, would sponsor an ERISA plan for its employees. Banks, insurance companies and other regulated financial institutions commonly market prototype plans to employers as simple means for them to establish and administer employee benefit plans. Each employer that adopts the prototype sponsors an ERISA plan for its employees and they can choose features such as contribution rates that meet their needs. The individual employers would assume the same fiduciary obligations associated with sponsorship of any ERISA-covered plans. For example, the prototype plan documents often specify that the employer is the plan's "named fiduciary'' and "plan administrator'' responsible for complying with ERISA, but they may allow the employer to delegate most of these responsibilities to others.[134]

Federal Legal and Regulatory Issues: DOL Guidance for Prototype Plans

Based on DOL Interpretive Bulletin, under a state-administered prototype plan, the state could allow employers to delegate many of its ERISA fiduciary and administrative responsibilities to the state or state designee, which would leave the state or a third party selected by the state to assume responsibility for most administrative and asset management functions of the plan.

As is the case with state open-MEPs, employer participation in a prototype plan must be voluntary, but can use features such as auto-enrollment with an opt-out and auto-escalation, features that are not available to payroll deduction IRAs, unless the state mandates employer participation.

[134] See IRS Online Publication, "Types of Pre-Approved Retirement Plans." www.irs.gov/Retirement-Plans/Types-of-Pre-Approved-Retirement-Plans.

State Action: Massachusetts' ERISA 401(k) Plan for Nonprofits[135] *(Appendix C)*

On March 22, 2012, Massachusetts enacted a 401(k)-type plan for certain nonprofits known as the Massachusetts Connecting Organizations to Retirement (CORE) Plan.[136] This law authorizes the state treasurer to set up a state-sponsored tax-deferred plan for nonprofits with no more than 20 employees.[137] Participation by nonprofits is voluntary. To minimize investment and administrative costs, the statute expects that the plan will be a prototype plan or similar user-friendly document and that participant accounts will be invested in the same options as are available under the existing deferred compensation plan for state employees. Participating employers will automatically deduct (with an opt-out) pre-tax earnings from participants' paychecks into individual employee accounts. Withdrawals from these accounts will be taxed at retirement.

Massachusetts' plan is covered by ERISA with small employers subject to reporting and disclosure requirements and the other ERISA and Tax Code rules. The state will provide participating employers with information regarding their obligations.

CORE Plan design includes portability, auto-enrollment, retirement income planning resources, and restricted early withdrawal options. Individuals will have their own account that is portable from one nonprofit employer to another nonprofit employer. While many people cash out their 401(k) when leaving an employer, the CORE plan hopes to discourage this "leakage" so individuals leave their account and allow it to grow. Employees of participating nonprofits generally will be automatically enrolled in the program at a default contribution rate of six percent of income. The contribution rate would be programmed to increase up to ten percent of income with no additional effort from the employer or employee. Benefit statements will include a projection of the participant's retirement income. Another retirement planning resource to be provided is a web-based tool, the Retirement Income Control Panel, which will provide account access as well as plan tools such as savings projections based on an assumed rate of return. Lastly, pre-retirement withdrawals due to hardships will be allowed.

State-Sponsored Marketplaces

In establishing a marketplace, the state would either build and maintain or contract with the private sector to provide a web-based portal or other mechanism to connect eligible employers with qualifying retirement savings programs. The state would determine which products are offered through the marketplace by determining their suitability to small and perhaps mid-sized employers (i.e., high quality, low-cost).

Federal Legal and Regulatory Issues: DOL Guidance for Marketplaces

DOL's Interpretive Bulletin 2015-12 does not consider the marketplace itself to be an ERISA-covered plan, although it could include ERISA-covered plans and other non-ERISA savings arrangements.[138] The state is not establishing or sponsoring any savings arrangement. Rather, the employer using the state marketplace would select the savings arrangement, whether it is an ERISA-covered employee benefit plan or a non-ERISA savings program. ERISA's reporting and disclosure requirements, protective

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[135] Unless otherwise noted, all information was retrieved from a presentation by David Lynch, Executive Director, Deferred Compensation, Office of the State Treasurer, State of Massachusetts, "Massachusetts CORE Plan," during the Georgetown Center for Retirement Initiative's webinar, "Private Sector Retirement Security Initiatives in the States," October 16, 2014, at http://cri.georgetown.edu/events/.

[136] Carlisle, Jon, "Grossman and Jakious Announce Major Step Forward in Creation of Non-Profit Retirement Plan," Governor Steven Grossman Press Release, June 9, 2014.

[137] See bill language MA H. 3754, No. 60 (2012). https://malegislature.gov/Laws/SessionLaws/Acts/2012/Chapter60

[138] 80 Fed. Reg. 71,937 (November 18, 2015)

standards and remedies would apply to the ERISA plans established by employers using the marketplace.[139] On the other hand, if the plan or arrangement is of a type that would otherwise be exempt from ERISA (such as a payroll deduction IRA arrangement that satisfies the conditions of the original 1975 safe harbor), the state's involvement as organizer or facilitator of the marketplace would not by itself cause that arrangement to be covered by ERISA.[140] Similarly, if, as in Washington State, a marketplace includes a type of plan that is subject to special rules under ERISA and the Tax Code, such as a SIMPLE-IRA, the state's involvement as organizer or facilitator of the marketplace would not by itself affect the application of the special rules.[141]

State Action: Washington State and New Jersey (Appendix C)

Washington State and New Jersey have new laws to create marketplace programs. One state approach is reflected in the 2015 Washington State Small Business Retirement Savings Marketplace Act. This law requires the state to contract with a private sector entity to establish a program that connects eligible employers with qualifying retirement savings plans. Only products that the state determines are suited to small employers, provide good quality, and charge low fees would be included in the state's marketplace. Products to be offered in the marketplace may include a SIMPLE-IRA as well as the federal myRA and other payroll deduction IRAs (however, without an employer mandate, the use of auto-enrollment would trigger ERISA). Washington State employers would be free to use the marketplace or not and would not be required to establish any retirement savings plans for their employees. Washington State would merely set standards for arrangements marketed through the marketplace. Sole proprietors and the self-employed can participate in the marketplace. New Jersey's program is very closely modeled on the Washington State program, although little progress to date has been made to implement the program in New Jersey. Washington State will be the first state to open its program, with a launch scheduled for mid-to-late January 2017.

State-Sponsored Combination or Multi-Tiered Programs

With the range of options now available under recent DOL rulemaking and guidance, states also have begun to consider combination or multi-tiered approaches to designing retirement savings programs. To date, there are a few types of combination models that have emerged:

1) A mandatory auto-enroll IRA program plus a voluntary state-sponsored open MEP. If employers without their own retirement plans choose not to participate in the voluntary, ERISA-based MEP or another plan of their choosing, then they would default into the mandatory auto-enroll IRA program *(MA proposal);*
2) A mandatory auto-enroll IRA program facilitated by a marketplace (*CT Law*); and
3) A mandatory auto-IRA plus a voluntary 401(k) Marketplace that includes a voluntary state-sponsored open MEP *(NYC Comptroller's Proposal, in which case it would be city-sponsored).*

In addition to these, there are other potential options, for example, a voluntary state-sponsored open MEP plus a voluntary payroll deduction IRA (auto-enroll could be used in the MEP, but not the voluntary IRA per DOL's new safe harbor).

State Action: New York City and Massachusetts MEP-IRA Proposals

***New York City Comptroller's Office**.* On October 6, 2016, New York City Comptroller Scott M. Stringer released two reports outlining the scope of the retirement security challenges facing his city's private

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[139] Ibid.
[140] Ibid.
[141] Ibid.

sector workers, the range of options for consideration and a proposed plan to address them. These reports represent 18 months of work by the Retirement Security Study Group established by the Comptroller in 2015. The study group recommended the following approach to the Comptroller[142]:

1. Employers that currently offer a workplace retirement plan would be free to continue doing so.

2. Employers that do not offer a retirement plan but would like to would be able to shop for plans through a curated marketplace overseen by an independent board. To help further assist employers the Marketplace would include prototype 401(k) plans, a new publicly sponsored Empire City 401(k) Multiple Employer Plan, and potentially SEP-IRA and SIMPLE-IRA plans. The 401(k) prototypes, MEP and other plans would provide ERISA protections to employees and allow the employer to automatically enroll employees.

3. Employers that want to offer a 401(k) plan but are concerned about ERISA fiduciary responsibilities and paperwork associated with individually sponsoring a plan would be able to select a voluntary publicly sponsored "turnkey" product in the new NYC 401(k) Marketplace, the Empire City 401(k) MEP.

4. Employers that do not select a plan on their own or through the NYC 401(k) Marketplace would default into the new NYC Roth auto-IRA. Employees would be free to opt out at any time.

Massachusetts. A bill was introduced in March 2015[143] to establish a Board to administer two retirement savings program options: a MEP plus an IRA program. The MEP Plan would be a profit sharing DC plan offering individual accounts. The IRA plan accepts individual contributions through payroll deduction and direct payment into IRAs. Assets would be pooled and professionally managed and the state or employer will not be responsible for any liabilities.

In the proposal, unless otherwise specified by the employer or directed by the employee, a participating employer would contribute three percent of the employee's annual salary or wages to the Plan. Employers would satisfy their requirements under the bill by either choosing their own plan, participating in the MEP or the IRA. The program would apply to all employers with 10 or more employees. If an eligible employer does not offer the plan, they would face a penalty. The Board and the Plan administrator and staff would act as fiduciaries under ERISA for the MEP. Employers would have minimal ERISA fiduciary responsibility under the MEP and would not be considered fiduciaries of the IRA.

State Action: Connecticut Law – Mandatory Auto-enroll IRA Facilitated by a Marketplace (Appendix B)

Connecticut's recently enacted program is a mandatory state-sponsored payroll deduction Roth IRA for private sector workers at employers with five or more employees that do not currently offer a retirement plan. An automatic default three percent payroll deduction would be made into individual retirement accounts unless an employee chooses another amount or opts out of the program at any time. The program must offer qualified retirement investment choices offered by multiple vendors and

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[142] Office of the New York City Comptroller, Bureau of Policy and Research, Bureau of Asset Management (2016), "The New York City Nest Egg: A Plan for Addressing Retirement Security in New York City." http://comptroller.nyc.gov/wp-content/uploads/documents/The-New-York-City-Nest-Egg_October_2016.pdf.
See also The New York City Retirement Security Study Group (2016), "An Analysis of Options to Increase Retirement Security for New York City Private Sector Workers." http://comptroller.nyc.gov/wp-content/uploads/documents/An-Analysis-of-Options-to-Increase-Retirement-Security-for-New-York-City-Private-Sector-Workers_October_2016.pdf.
[143] HB 924 was introduced by Representative James O'Day on January 15, 2015.

provides participants a website for information about the vendor and products available through the program.

Tax Code: IRAs and Qualified Retirement Plans

IRAs. For a worker not covered by a company retirement plan, the contribution to an IRA is tax-deductible up to the Tax Code limits—for 2017, $5,500 for someone under age 50 and $6,500 for those who will be at least 50 by year-end.[144] (Dollar limits are indexed annually for inflation.) Rules like the prohibited transaction requirements discussed in Section III also apply to an IRA. So, for example, an individual could not invest his or her IRA to fund in his or her own business. Investment income accumulates tax-deferred. Federal tax is due only on distribution (plus an excise tax for certain "early" pre-59-1/2 withdrawals). An individual may also establish a Roth IRA in which contributions are made after-tax but distributions, including investment earnings, are completely tax-free.

401(k)s and other Qualified Retirement Plans. 401(k) and other qualified DC plans are more complex than IRAs, but offer far greater savings potential and flexibility.[145] Employee 401(k) contributions are tax-deferred up to the Tax Code's limits—for 2017, $18,000 for those under 50 and $24,000 for those who will be at least 50 by year-end. (Dollar limits are indexed annually for inflation.) Alternatively, an employee can contribute up to these same limits as post-tax Roth 401(k) contributions. Employers also can contribute using "matching" or discretionary contributions. (An employer also may contribute to an employee's IRA, but that would trigger ERISA regulation.)

[144] Individuals who earn above certain amounts and who participate in an employer retirement plan, may only make post-tax contributions to an IRA. IRC Sec. 408(o)(4). Since the state programs are targeting employees without any form of retirement benefit, this limit is unlikely to affect many participants.
[145] A much-relaxed version of the Tax Code qualification rules applies to retirement plans for government employees.

SUMMARY OF PLAN DESIGN OPTIONS FOR STATE-SPONSORED DC RETIREMENT PROGRAMS

ERISA-Exempt[1]	ERISA-Based[2]
1) Payroll Deduction IRA (1975) ➢ Employer: Voluntary ➢ Employee: Voluntary *Proposals: IN, UT, ND, WV* **2) Payroll Deduction IRA with auto-enroll (2016)** ➢ Employer: Mandatory ➢ Employee: Voluntary (opt-out) *Laws: CA, CT, IL, OR, and MD* **3) Federal MyRA (Roth IRA)** ➢ Employer: Voluntary ➢ Employee: Voluntary *Laws: CA, WA*	**1) Multiple Employer Plan (MEP)*** ➢ Employer: Voluntary ➢ Employee: Voluntary** *Proposals: NYC, MA* **2) Master and Prototype Plans** ➢ Employer: Voluntary ➢ Employee: Voluntary ** *Laws: MA (Nonprofits only)* **3) Marketplace (ERISA & non-ERISA products permitted)** ➢ Employer: Voluntary ➢ Employee: Voluntary *Laws: WA, NJ*

Combination or Multi-Tiered Options***
1) Mandatory Auto-IRA + Voluntary State Open MEP *Proposal: MA* **2) Mandatory Auto-IRA facilitated by a Marketplace** *Law: CT* **3) Mandatory Auto-IRA + Voluntary 401(k) Marketplace + Voluntary State Open MEP****** *Proposal: NYC Comptroller's Office*

[1] 29 CFR 2510.3-2(d); 40 FR 34526 (Aug. 15, 1975); 29 CFR Part 2510 (August 30, 2016)

[2] 29 CFR Part 2509 (November 18, 2015)

*DOL's Interpretive Bulletin allows for publicly sponsored open MEPs; the issue of private sector open MEPs remains under consideration in Congress.

**Plan can provide that employees will be auto-enrolled with an opt-out.

***These are not intended to be the only options, but a review of options considered by states and cities to date.

****Refers to "state" even though the same federal rules apply to certain "large" cities and other state political subdivisions.

ROLES AND RESPONSIBILITIES – STATE, EMPLOYERS AND EMPLOYEES
DC PLAN DESIGN OPTIONS
(Appendix A)

	Auto-IRAs*	MEP	Master and Prototype	Marketplace
State	-Program must be established pursuant to state law. -May delegate implementation and administrative authority to instrumentality. -Must notify employees of their rights and create mechanisms to enforce those rights. -States have the control to establish restrictions on withdrawals from IRAs to limit leakage.	-The state or its designee would be the plan sponsor under ERISA and the named fiduciary and plan administrator responsible for administering the plan (either directly or through contracted agents), selecting service providers and providing other plan services. -Fiduciary responsibilities would be assigned to the parties responsible for the administration and management of the MEP.	-The state or state designee assumes many responsibilities for ERISA compliance. -Degree of state involvement would be less than a MEP (e.g., adopting employers would be plan sponsors and named fiduciaries). -The state or designated third party could assume responsibility for most administrative or asset management functions.	-The state would contract with a third party to establish a program to connect eligible employers with qualifying savings plan vendors. -The state would set standards to determine whether products are suited for small employers. -The marketplace is not subject to ERISA, only those ERISA products as offered.
Employer	-Mandatory participation. -Role must be limited to ministerial activities (e.g., setting up payroll deduction; and forwarding contributions). -Employers that are not mandated by law to participate may not automatically enroll employees. -Employers may not make contributions to an IRA.	-Voluntary participation. -Employers would be required to execute a participation agreement. -Each employer that chooses to participate would not be considered to have established its own ERISA plan. -Streamlined compliance with ERISA as one plan. -Employer contributions are permitted.	-Voluntary participation. -Each employer that adopts the prototype sponsors an ERISA plan. -Serve as plan sponsor and assume fiduciary responsibilities, although the state can perform many of these functions. -Employer contributions are permitted.	-Voluntary participation. -Employer contributions are permitted for ERISA plans.
Employee	-Voluntary participation. With auto-enrollment, employees must be given adequate notice and have the right to opt out.	- Voluntary participation. With auto-enrollment, employees must be given adequate notice and have the right to opt out.	- Voluntary participation. With auto-enrollment, employees must be given adequate notice and have the right to opt out.	- Voluntary participation. With auto-enrollment, employees must be given adequate notice and have the right to opt out.

* This refers to the 2016 DOL safe harbor conditions. If a state wants to establish a voluntary payroll deduction IRA program pursuant to the 1975 safe harbor, it can do so, but cannot use auto-enrollment (i.e., would not be an auto-IRA program).

III. Legal and Regulatory Considerations: How ERISA and Other Laws Apply to Plan Design Options

To some, "ERISA" coverage conjures up visions of onerous fiduciary obligations and unlimited liability. ERISA does have a lot of rules, but it also provides workable standards for running a retirement program; a sound set of participant protections; and a well-established system for resolving disputes over benefit claims.

This section provides an overview of how ERISA as well as other laws, such as tax and securities laws, would apply to plan design options. Essentially the same rules apply to a retirement plan whether it is a state-sponsored MEP, a prototype or other retirement plan. This discussion focuses on the additional considerations applicable to a state-sponsored MEP arising because the state, or its delegate, will assume many responsibilities on behalf of all participants.[146]

ERISA BASICS

What follows is a summary of the ERISA rules on establishing and maintaining a plan; fiduciary duties; federal government reporting and participant disclosure; and when, where, and how a participant or fiduciary can sue for unpaid benefits or harm to the plan.

Establishing and Running a Plan

An ERISA retirement plan is established by a "plan sponsor" and operated under the terms of a written plan document.[147] Besides setting how benefits are determined and when they vest and are paid, an ERISA plan must designate one or more individuals, committee or entity as the "named fiduciary"—the point person responsible for the other fiduciaries. The document also describes who may amend the plan and may provide for the delegation of authority by the fiduciaries to others. With a state-sponsored MEP, the board, committee or other special purpose entity designated by the legislature likely would serve as sponsor and named fiduciary and be authorized via enabling legislation to make certain plan amendments. All plan assets (employee and employer contributions and investment earnings) must be held in a trust or in an insurance company annuity.[148] Plan assets are sacred and bullet proof—they may only be used to pay benefits or to cover legitimate plan expenses. Each plan must maintain a fidelity bond.[149]

Fiduciaries and their Duties

Besides the plan sponsor, named fiduciary and trustee, anyone with control over plan assets is a fiduciary. This includes a money manager or anyone with responsibility to appoint or fire a money manager.[150] A person who is performing ministerial duties is not a fiduciary.[151] Examples include most recordkeepers, lawyers and other advisors. A person can wear two hats, serving in both a fiduciary and

[146] In a state-sponsored MEP, the state or its delegate would typically be the named fiduciary and have amendment, investment and administrative authority. With a prototype plan, the employer would likely retain named fiduciary status and amendment authority (although amending a prototype could cause the employer to forfeit the prototype's IRS preapproval). The state or its delegate would be expected to control plan investment options even in a prototype.
[147] ERISA Sec. 402.
[148] ERISA Sec. 403.
[149] ERISA Sec. 412(a).
[150] ERISA Sec. 3(21)(A).
[151] DOL Reg. Sec. 2509.75-5.

non-fiduciary role. For example, when a plan sponsor establishes or amends a plan, this generally is a "settlor" decision outside of the fiduciary rules.

Fiduciaries are expected to be experts and to act prudently for the exclusive benefit of participants.[152] ERISA recognizes that not every fiduciary will be an expert, so a fiduciary may instead hire experts to advise them or delegate certain duties to an expert. Hiring or delegating to an expert is itself a fiduciary act. Neither perfection nor clairvoyance is expected of ERISA fiduciaries, just prudent and well-thought out, reasonable decision making. In the words of a famous judicial opinion, "prudence not prescience" is required.[153]

The plan sponsor and named fiduciary sit at the top and are ultimately accountable for what goes wrong. Under the ERISA concept of prudence, if these fiduciaries are diligent in hiring and monitoring consultants, money managers, trustees and the like, then they will not have violated their ERISA fiduciary duties even if one of their delegates acts imprudently.

Special Investment Consideration. A large portion of fiduciary efforts concern the investment of plan assets, especially for 401(k) and other DC plans. ERISA allows fiduciaries to side-step much of their fiduciary responsibilities by allowing participants to invest their own plan accounts.[154] For this to happen, participants must be given a choice of at least three diversified investments funds—say an S&P 500 fund, an international fund and a fixed income fund—the opportunity to switch investments at least quarterly and, of course, proper disclosure to participants. With daily valuation and a dozen or more funds, it is relatively easy for most plans to meet this so-called 404(c) exception. For participants who do not make any investment election, most likely those who were auto enrolled in the plan, the participant may be "defaulted" into a diversified lifecycle, assets allocation or similar all-in-one fund.[155] Importantly, although the participant can be made legally responsible for his or her own investment choices, the plan fiduciaries remain responsible for selecting and monitoring the investments offered on the fund lineup and ensuring that the fees paid by participants are reasonable. Another advantage of a state-sponsored 401(k) plan (most likely a MEP, but also could include a prototype) is that by combining many small and mid-sized employer plans the program will achieve significant economies of scale, thus lowering participant fees and expanding the available universe of money managers and advisors. These advantages will assist state and employer fiduciaries in fulfilling their obligations.

Reporting and Disclosure Requirements.

Each plan must file an annual report (Form 5500, 5500-SF or 5500EZ) with the Internal Revenue Service (IRS) each year that includes: a financial statement and other investment information; and a representation that the plan did nothing illegal. Plans with fewer than 100 participants may file simplified annual reports and are not required to have an outside audit. One advantage of a state-sponsored MEP is that a single Form 5500 and annual audit covers the entire program; adopting employers are spared filing their own reports.

The ERISA disclosure obligations include giving participants a readable "plain English" summary plan description (SPD), a notice of plan amendments (SMM) and information on plan fees, investments and payroll withholding.[156] Participants also must be given a quarterly benefit statement. The good news is that most recordkeepers have fully automated the process and it should not present an undue burden

[152] ERISA Sec. 404.
[153] *DeBruyne v. Equitable Life Assurance Soc'y of the United States*, 920 F.2d 457, 465 (7th Cir. 1990).
[154] ERISA Sec. 404(c); DOL Reg. Sec. 2550.404c-1.
[155] ERISA Sec. 404(c)(5); DOL Reg. Sec. 2550.404c-5.
[156] ERISA Sec. 105.

for state-sponsored plans. Many plans now add simple one- or two-page readable information sheets to the ERISA disclosure so participants have accessible information.

Benefit Disputes and Litigation

ERISA offers a well-developed system for resolving participant disputes. Before suing, a participant must make a benefit claim, have the claim denied by the plan, appeal the denial and have the appeal also denied.[157] Only then may the participant sue and only in federal court.[158] The appeal/denial process must be in writing and the participant must be given notice of his or her rights and an explanation of the denial and what other information might be needed to prove the claim. The participant has a right to all relevant plan documents that relate to the claim. The plan may specify a reasonable statute of limitations for making a claim and bringing a lawsuit, otherwise the analogous state statute governs. A court may award legal fees to either party, but absent outrageous conduct by the participant or his or her counsel, the employer or plan is unlikely to be awarded fees. However, a court may award fees to a losing participant, if he or she had “some degree of success on the merits.”[159] A plan may provide that all disputes be litigated in a particular jurisdiction, for example, a Vermont-based plan could limit litigation to the courts in Vermont.

If the plan suffers a loss, for example, due to fraud or negligent action by a money manager, the fiduciaries may sue on the plan’s behalf. Again, the suit must be in federal court. Courts generally have not required participants to exhaust administrative remedies before suing for breach of fiduciary duty.

Prohibited Transactions

ERISA (and the Tax Code) penalize certain “prohibited transactions” between a plan and a related party.[160] These transactions include the direct or indirect sale or exchange, leasing of any property, lending of money or supplying goods and services between the plan and party in interest. Fiduciaries are obligated to make sure the plan avoids these transactions. Fiduciaries also must avoid self-dealing or taking actions that are averse to the plan. (There are numerous statutory and DOL-issued exemptions to these prohibited transactions.) Illegal transactions must be reversed, the plan made whole and a penalty paid by the related parties.[161]

Special ERISA rules cover a plan’s investment in employer stock.[162] In virtually all cases the employers joining a state-sponsored MEP or prototype would be privately held, so it is unlikely that these rules would ever be implicated. Nevertheless, the program should screen its employers and have appropriate notification and other investment procedures in place in case an employer is or goes public.

State-Sponsored Retirement Plans and the Tax Code

All retirement plans enjoy various federal income tax benefits and must follow numerous federal Tax Code rules and regulations. As with ERISA, the rules are mostly the same whether the plan is a MEP, prototype or other retirement plan. As the discussion will note, with MEPs the Tax Code sometimes applies to the plan as a whole and sometimes on an employer-by-employer basis.

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[157] *See Amato v. Bernard*, 618 F.2d 559, 566-67, 569 (9th Cir.1980)(noting that although ERISA does not require the exhaustion of administrative remedies, the legislative history and the text of ERISA make it clear that Congress intended for such a requirement to apply.)
[158] Technically, a participant may contest a claim denial in state court. However, the federal Rules of Civil Procedure give the plan the right (which is almost always exercised) to remove the case to federal court.
[159] *Hardt v. Reliance Standard Life Ins. Co.*, 560 U.S. 242, 245 (2010)(quoting *Ruckelshaus v. Sierra Club*, 463 U.S. 680, 694 (1983)).
[160] ERISA Secs. 406-408. Similar rules are imposed by the Tax Code.
[161] ERISA Secs. 406, 408.
[162] ERISA Sec. 407.

Employer contributions are deductible when made, the plan does not pay income taxes on its investment income and participants defer any taxation until they receive payment. Also, on leaving a job a participant may be able to rollover his or her benefit tax-deferred into an IRA or new employer plan. To achieve these tax advantages, the plan must be "qualified" by meeting numerous Tax Code requirements that boil down to a series of rules, mathematical formulas and limits that are intended to keep the plan from favoring highly compensated employees (HCEs) too heavily, limiting pre-retirement access to funds or delaying distributions too long. What follows is a brief synopsis of these rules. The IRS is responsible for interpretation and enforcement of the Tax Code.

1. Nondiscriminatory (Highly Compensated Employees (HCE)) Eligibility. Basically, an HCE is any employee who is (or was in the prior year) a 5 percent owner or was paid $120,000 (indexed for post-2017 inflation) in the prior year.[163] Whether an individual is an HCE and the plan discriminates is determined employer-by-employer.[164] All employees who are not high-paid are considered non-highly compensated employees (NHCEs). The plan must cover a reasonable percentage of NHCEs; for example, a plan benefiting 70 percent of NHCEs would pass "coverage."[165] Certain employees, such as those with less than one year of employment, part-timers who never work 1,000 hours in any year, individuals under age 21; and unionized employees (if the bargaining agreement doesn't require participation in the plan), may be excluded in coverage testing. Other categories of employees must be counted in coverage testing but may be excluded from the plan--say based on job function or location, as long the plan still meets the 70 percent or similar test. Presumably, most state-sponsored MEPs would require that each employer cover all employees, perhaps after a short waiting period. Thus, passing the coverage test should be simple. Only employees and owners working for the business may participate in the employer's plan. While a business' non-employee consultants and other independent contractors cannot participate in that business' plan, they could set up their own retirement plan as a self-employed worker.

2. Service with any participating employer counts. Employment with any employer participating in a MEP must be counted in determining if an employee satisfies the plan's age, service and vesting requirements.[166] This rule would help workers who job-hop between participating employers from forfeiting non-vested benefits or having to meet multiple waiting periods. It should be relatively simple to track employees through their Social Security numbers.

3. Non-discriminatory benefits and features. The Tax Code limits the amount of an employee's compensation that may be considered in figuring his or her 401(k) and employer contributions to $270,000 in 2017 (indexed for inflation). The annual contribution added to an employee's account (both 401(k) and employer) in 2017 may not exceed $54,000 or 100 percent of compensation, whichever is lower.[167] Besides coverage, the plan's benefit structure and other important features generally must treat all participants the same. It is possible for a plan to offer different benefits to various categories of employees, for example higher employer contributions for workers with at least ten years of employment. However, the more generous provisions must be able to pass coverage as if it were a distinct plan. Oddly, compensation limits are applied employer-by-employer while the contribution limits are applied plan-wide. For example, if someone is employed by two participating employers, his or her contributions by both employers are added together.[168] Again, as practical matter, most state-

[163] IRC Sec. 414(q).
[164] IRC Sec. 413(c)(6).
[165] Sec. 410(b); 413 MM.
[166] IRC Secs. 413(c)(1) & (3). Certain service before the employer joins the plan may be ignored.
[167] IRC Sec. 402(g); Sec. 415(b).
[168] Treas. Reg. 1.415(a)-1(e); see Treas Reg. 1.413-6(b)(1)(i)

sponsored MEPs would require that each employer offer the same benefits to all its participants, the plan should automatically be non-discriminatory.

4. Contributions. Employers may contribute to each participant's account under a stated "allocation formula" and within the limits discussed. Employer contributions can be discretionary—employer decides at year-end whether and how much to contribute—or hard-wired into the plan document. Even hard-wired contributions can be changed or eliminated prospectively. It is also possible for an employer to contribute disproportionally more for employees earning above the Social Security wage base ($127,000 in 2017). The rules for "integrating" a plan with Social Security are complex. For these reasons, states should use caution in considering an integration option. Finally, a plan may permit employees to make after-tax contributions to the plan. As discussed below, given the advantages and relatively high limits of traditional and Roth 401(k) contributions, most state-sponsored MEPs probably would not allow after-tax contributions.

5. Exclusive Benefit Rule. Every plan must be established and maintained by an employer for the exclusive benefit of its employees and their beneficiaries.[169] The IRS interprets the exclusive benefit rule as generally requiring that all covered employees must be employed by the employer or employers maintaining the plan. The exclusive benefit rule applies to the entire plan.[170] While the state sponsor will not have any employees participating, the requirement should be satisfied because all employers will adopt the plan and delegate to the board responsibility for running the plan. An analogous issue arose some twenty years ago, regarding whether leased employees could participate in the leasing company (sometimes called a professional employee organization or PEO 401(k) plan). The PEO typically treated the leased workers as its employees and not the company they were being leased to. But labor law can be unclear as to who employs them. To allow the PEO plan to cover these employees no matter whom was considered their employer, the IRS ruled[171] that a PEO plan should be converted into a MEP covering all leased employees, with the recipient businesses adopting the MEP. Thus, the exclusive benefit question will be solved even if the workers were determined not to be employees of the PEO. Similar logic should prevail regarding a state-sponsored MEP since each employer would adopt the plan as a condition of joining.[172] Nevertheless, before proceeding a more cautious state may wish to obtain guidance from the IRS.

6. General operations. Every plan must be operated in accordance with its written terms, unless the terms themselves are illegal. Both employee and employer contributions must be made on time, accurately and as specified in the employee elections and plan document. Noncompliance with either of these rules also would be an ERISA violation.

7. Top Heavy Rules. The Tax Code imposes an extra layer of requirements on mostly small employers with plans that are stacked too heavily in favor of "key" employees, defined as 5 percent or greater business owners, 1 percent owners earning at least $150,000 (indexed) and certain officers and other "high-paid" employees.[173] If over 60 percent of the account balances are held by key employees[174], the plan is "top-heavy" and must either provide minimum benefit to non-key employees or contribute at the

[169] IRC Sec. 401(a)(2).
[170] IRC Sec. 413(c)(2).
[171] Rev. Proc. 2002-21.
[172] Further, IRS instructions for completing Form 5500 annual reports and Form 5300 requests for a determination on qualification, suggest that the IRS would support this view.
[173] IRC Sec. 416.
[174] IRC Sec. 416(g).

same rate for all employees. Top-heavy plans also must use a slightly faster schedule.[175] The top-heavy rules apply employer-by-employer.[176]

While a MEP would have to test each employer for top heaviness, most state-sponsored plans would have uniform contribution rates and fast or immediate vesting that would automatically satisfy this rule. Also, a plan meeting the special 401(k) testing rules (the so-called ADP/ACP safe harbor) would satisfy the top-heavy rules.

8. Vesting. Participants always are 100 percent vested in their 401(k) and after tax contributions.[177] The plan may impose one of two vesting requirements on employer contributions: either contributions are 100 percent vested once the employee has three years of service with the employer or vest gradually—20 percent per year for each year of service starting with the second year so that the employee is 100 percent vested after six years.[178] Generally, all service with any employer participating in the MEP counts for vesting purposes.[179] Employees also vest upon reaching the plan's stated retirement age (generally age 65) while employed.[180] If an employee leaves before full vesting, he or she will forfeit the non-vested benefits. Forfeitures may be used by the employer to reduce future contributions, pay plan expenses or as an additional contribution for the remaining participants.[181] How forfeitures will be used should be clearly specified.

9. Spousal Rights. A DC plan participant must designate his or her spouse as sole beneficiary unless the spouse consents in a notarized writing to waive this right.[182] Upon divorce or legal separation, a court may issue a domestic relations order to the plan ordering it to transfer a specified portion (or even all) of the participant's benefit to a plan account set up for the spouse. While these spousal rights can get rather complicated, many recordkeepers have well-established systems to take charge.

10. Loans, Withdrawals and Distributions. The Tax Code permits a plan to allow participants to borrow from their account. The maximum loan is the lesser of $50,000 or 50 percent of the vested account. Loans may extend up to five years (longer if used to purchase a primary residence) and must charge a "commercially reasonable" interest rate. Interest and principal payments (typically through payroll withholding) are returned to the participant's account. While better than credit card, payday and some other forms of consumer credit, loans are not a particularly good deal for participants. Generally, the interest on the loan is not tax deductible but will be taxed upon distribution. Thus, loan interest is paid with after-tax dollars but is taxed (again) on retirement. More importantly, a significant minority of participants default on their loans, causing the balance of principal and accrued interest to be immediately taxed and possibly triggering a 10 percent IRS early withdrawal penalty as well.

A plan may allow participants to withdraw money from their vested account while employed. Typically, these withdrawals are limited to an IRS list of financial hardship. Examples of hardship include purchase of a home, college and other post-high school educational costs, to prevent foreclosure or eviction, and funeral expenses. The rules on withdrawal are considerably stricter for 401(k) than most employer

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[175] IRC Sec. 416(c)(2).
[176] Treas. Reg. 1.416-1, G-2.
[177] IRC Sec. 401(k); Sec. 411(a)(1).
[178] IRC Sec. 411(a)(2)(B).
[179] IRC Sec. 413MM.
[180] IRC Sec. 411(a)(8).
[181] Note, that the Tax Code is silent on the application of forfeitures in a MEP. However, the only sensible rule would be that forfeitures should be applied only with respect to the employer whose employees generated the forfeiture.
[182] IRC Sec. 401(a) (11); IRC Sec. 417. Plans that include annuity payment options also must allow the spouse a right to a 50% survivor annuity.

contributions.[183] Withdrawals are taxable and generally hit with the 10 percent early withdrawal tax. Earnings on 401(k) contributions may not be withdrawn for hardship. A plan may allow withdrawals from employer contributions, with or without hardship and from all contributions once the participant reaches age 59 1/2.

While most plans allow loans and hardship withdrawals, these features can be problematic. Number one is that easier access to 401k) funds can cause "leakage"—spending money earmarked for retirement on day-to-day expenses. Also, while recordkeepers have largely automated the process, they still add to expenses and headaches and are error-prone. Conversely, the availability of loans and withdrawals may lead some folks to contribute (or contribute more) knowing that they'll have access to the money just in case. A plan may impose a reasonable fee on participants taking a loan or hardship distribution. States should give serious thought to limiting employees' access to money before retirement.

When an employee retires or otherwise leaves employment, he or she may choose when and how to take payment within the alternatives allowed by the plan. While a plan could only offer lump sums, most states would want to allow installment and annuity payouts and give participants the ability to defer distribution if the Tax Code allows.[184] The state may determine to nudge participants into taking at least a portion of their benefit as a lifetime annuity.

An employee leaving one employer participating in a MEP for another MEP employer probably would not be considered to have terminated employment.[185] The plan must begin distributions to a participant when he reaches age 70 1/2. However, an employee, other than someone with a 5 percent or greater interest in the business, may delay these minimum distributions until actual retirement. As discussed below, the age 70 1/2 rule also does not apply to amounts held in a Roth 401(k) account.

State-Sponsored MEPs: Mistakes, Violations and Liability

All plan sponsors should have procedures in place to avoid, catch and remedy mistakes and violations and allocate financial responsibility to the guilty. This is an issue for a MEP where the state, as sponsor, will need to take the lead. Thus, this section focuses on MEPs. While state legislatures should have their eyes open to these issues, it should not dissuade them from establishing MEPs. For participating employers, an important advantage of joining a MEP will be significantly reduced liability exposure compared with operating its own single employer plan. By following well-worn ERISA governance procedures and principles of transparency employers and outsourcing most functions to vendors, states and employers can, as a practical matter, avoid most liability.

Late 401(k) contributions. Employers have a duty under both ERISA and the Tax Code to properly withhold and transmit 401(k) contributions. The DOL has a focus on late 401(k) contributions, viewing them as, in effect, interest free loans to the employer. While there is no statutory standard for when a contribution is late, the DOL has established a deadline rule that 401(k) contributions must be delivered as soon as they reasonably can be segregated, but no later than the 15th business day of the month immediately following the month in which the paycheck was issued. (The DOL gives an automatic pass to plans with fewer than 100 participants if contributions are made within seven business days after issuing the paycheck. It is not clear whether this small plan exception would apply to small employers in

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[183] IRC Sec. 401(k)(2)(B).
[184] To reduce costs and avoid missing participant problems, many plans automatically cash-out employees with small balances ($5,000) on leaving.
[185] See IRS Notice 2002-4, 2002-1 C.B. 298.

a state-sponsored MEP where the plan, but not the employer, had over 100 participants.) One way to judge how fast an employer could reasonably segregate its 401(k) contributions is to look at how quickly an employer can forward tax withholdings to the IRS. The contribution timing rule also applies to loan repayments made through payroll.

Smaller employers, perhaps using an outside service but still relying on a multi-tasking employee to manage payroll, can find this rule challenging. Recognizing the difficulty, the DOL has created a correction program that allows offending employers to add an interest factor (calculated on the DOL website) to each employee's late contribution. An employer's occasional violation can be self-corrected, while more frequent problems should be reported using the DOL voluntary correction program. Of course, chronic lateness or fraud are serious violations that could lead to penalties and other sanctions.

Late contributions should be viewed as an employer issue that the state sponsor is neither able to police nor remediate. The MEP plan documents should make this clear. As open 401(k) MEPs coverage grows, states, employers, the DOL and IRS will likely develop additional solutions.

ERISA Fiduciary Concerns. The state board can, and should, hire investment advisors and recordkeepers to accept responsibility for the heavy lifting of investing and operating the plan and agree to indemnify the board if something goes amiss. Of course, the board still would retain its ERISA duty to locate, hire, monitor and replace (if necessary) those vendors. The board should retain expert consultants and attorneys to help with these duties. Recall that ERISA does not impose a duty of perfection and, by using having and following proper procedures and governance, a board would generally be absolved from liability if one of those vendors turned out to be a loser. Indeed, most states already have in place detailed request for proposal and contracting rules to manage the process.

A board could purchase fiduciary insurance to further mitigate its exposure. That insurance should be purchased with outside (and not plan) funds. Otherwise, any insurance recovery would belong to the plan. Everything considered, the combination of outsourcing, indemnification, sound governance, outside experts and fiduciary insurance should allow even the most nervous board member to sleep at night.

One exposure for ERISA liability that cannot be simply outsourced or insured away is for the board's own fraud, malfeasance or complete abdication of duties. But there should be plenty of checks, balances, outside auditors and procedures to prevent this type of abuse.

From the employers' side, joining and remaining in a MEP are considered fiduciary decisions. The potential ERISA liability from an employer's participating in a state-sponsored MEP, backed by a team of experts and seasoned providers, would seem almost illusory.

Mistakes, Corrections & Bad Apples. Violation of any of the Tax Code requirements could, in theory, cause any plan, including a MEP, to be "disqualified." Disqualification is the IRS's nuclear option, causing the plan to retroactively lose all favorable tax benefits, immediately taxing participants on their vested benefits, even if not paid out, and the plan to pay income tax on its investment earnings; and the employer to lose some of its tax deduction on contributions; plus interest and tax penalties imposed on everyone.

Under the controversial "bad apple" rule, the IRS treats one employer's violation—say of the top-heavy or 415 benefit limitations—as infecting the entire plan.[186] Because of the draconian consequences, the IRS is loath to disqualify a plan. Instead, it has created a series of procedures where an employer can

[186] Treas. Reg. 1.413-2(a)(3)(iv).

correct a qualification defect.[187] Depending on the relative size and nature of the error, and how it was caught (by the employer and self-corrected and/or reported or by the IRS on audit), almost all errors may be fixed by undoing the mistake, making all participants whole and perhaps, by the employer paying an IRS user fee or penalty.

In a MEP the plan administrator (not the employer which messed up) must orchestrate the correction and apply for IRS relief.[188] The administrator may allocate any IRS compliance fee or penalty to the offending employer[s], rather all employers. A well-designed MEP would include procedures for identifying and correcting mistakes and allocating the costs of correction and authorizing the administrator to compel the employer[s] to fully cooperate and assume financial responsibility for its non-compliance.

Even with the correction procedures and the important policy goals of a state-sponsored MEP, some states and employers may not feel entirely comfortable relying on the common sense and good graces of the IRS in correcting errors. While careful plan design can reduce the likelihood of a qualification error and make the offending employer pay for its own mistakes, the bad apple rule may be the most troubling aspect of joining a MEP. It also does not serve any regulatory purpose to punish the innocent along with the guilty. Either the IRS will decide to revise its policy or Congress should pass legislation repealing the bad apple rule. Until then, the bad apple rule could be a factor in a state's decision to take a prototype plan approach; avoiding one problem at the possible cost of forgoing the many advantages of a MEP.

State or Employer Termination of MEP Participation

<u>Can a state exit its MEP</u>? A state may determine that it no longer wishes to sponsor a MEP, for example because the retirement plan market has expanded to offer many strong private sector alternatives. In that case, a state would have two alternatives. First, it could find a qualified private sector provider to take over and transfer sponsorship. Of course, this is a fiduciary action and the state would want to obtain airtight indemnification from the new sponsor. Second, the state could terminate the MEP. This process would involve giving employers the opportunity to set up their own replacement plans and, for the remainder of the MEP, fully vesting all participants, applying to the IRS for a determination letter that the termination comports with the tax qualification rules and distributing benefits to all participants. While a termination would be a cumbersome process, states should be comforted in knowing they have an "out."

<u>Can employers withdraw from a MEP</u>? A MEP can (and should) allow an employer to withdraw by "spinning off" the employer's slice of assets and benefit obligations into its newly established plan and trust. Participants' vested and non-vested benefits must be preserved in the new plan. The MEP's administrator would likely have an ERISA fiduciary duty to obtain assurances from the employer that the new plan appropriately treats participant benefits.

It also would be possible for an employer with an existing plan to transfer that plan into a MEP. However, under the existing ERISA and tax rules any defect in employer's plan could port over to the MEP, potentially infecting the entire program. It is doubtful that an administrator would want to put in the time and expense of due diligence of the employer plan and, absent a change in law, it would be inadvisable for most MEPs to accept a transfer from existing plan.

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[187] Rev. Proc. 2016-51.

[188] Rev. Proc. 2016-51; section 11.03.11.

Federal Legislative Efforts Related to MEPs. There has been general bipartisan support in Congress to make MEPs more user-friendly.[189] Numerous bills would eliminate the bad apple rule for any employer error, either by directing the IRS to revise its rules or by revising the text of the Code. Note even with the change, a Tax Code violation by the state sponsor could infect the entire program. There also are several proposals to allow private sector vendors the same flexibility as states to sponsor open MEPs the commonality rule discussed above. Finally, some are urging Congress to direct the DOL and IRS to allow single Form 5500 to be filed by non-MEPs. States interested in sponsoring a MEP could encourage Congress to legislatively remove the bad apple rule and the commonality requirement and generally direct the IRS, DOL and the Securities and Exchange Commission (SEC) to take a pro-MEP approach.

Other Legal and Regulatory Considerations for Plan Design Options: Federal Securities Laws and the Patriot Act

This section answers some questions about how federal securities laws might apply to DC plan design options and identifies another federal law—the Patriot Act—that also must be considered.

Federal Securities Laws[190]

A primary aim of securities laws is to protect investors—particularly small "retail" investors—by requiring, among other things, full and fair disclosure of information on investments, fees, advisors and the like. While several federal securities laws could be relevant to auto-IRAs, two key statutes are the Investment Company Act of 1940 (40 Act) and the Securities Act of 1933 (33 Act). The 40 Act regulates mutual funds and other "investment companies." The 33 Act regulates the offer and sale of "securities," defined broadly as ordinary stocks and bonds and mutual fund shares and certain "investment contracts."

Federal securities laws raise two basic questions: are state-sponsored mandatory auto-IRA programs *themselves* exempt; and can a state retirement savings program offer the type of investments available to 401(k) and other savings plans but not regular IRAs? The answers to both questions should be yes.

Are State or Other Government Plans Exempt?

Federal securities laws generally exempt states and their agencies or instrumentalities (state instrumentalities) from regulation as investment companies under the 40 Act and any securities issued by a state instrumentality are similarly exempt from registration under the 33 Act. If state-sponsored retirement plans for private sector workers are viewed as state instrumentalities, it follows logically that an auto-IRA program should be exempt from federal securities law regulation. This makes perfect sense both legally (the programs are created by state law, intended to benefit state citizens and operated under state supervision) and as a policy matter because program participants will be well-protected by state boards and trustees, who will in turn be advised by a team of experts. In fact, auto-IRA participants would not be your typical IRA owners in the market place because the state boards and their advisors will be vetting and monitoring service providers and products.

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[189] The President's Fiscal Year 2017 Budget provides open creation for open MEP plans. https://www.whitehouse.gov/sites/default/files/omb/budget/fy2017/assets/opportunity.pdf.

[190] This discussion draws heavily from Morse, David (2016), "Beyond ERISA: Other Regulatory Considerations for State-Sponsored Retirement Plans (Blog Post)," Georgetown Center for Retirement Initiatives. http://cri.georgetown.edu/beyond-erisa-other-regulatory-considerations-for-state-sponsored-retirement-plans/.

The pre-paid college tuition savings programs—or "529 savings programs"—which states began establishing more than twenty years ago, are good examples of state-run programs treated as state instrumentalities for securities law purposes.[191] Most 529 programs include state-established investments for program participants. The SEC staff issued several no-action letters confirming that these arrangements were exempt from federal securities law regulation under the exemptions for state instrumentalities. By taking such action, the SEC staff interpreted the term state instrumentality to include the concept of prepaid tuition programs being offered and sold to the public (students and their families). Once a state-sponsored and managed program is viewed as an instrumentality of the state, it fits logically within the pertinent securities laws exemptions.

Can State Retirement Plans for Private Sector Workers Offer the Same Types of Investments as 401(k) and Other Defined Contribution Plans?

If auto-IRA programs themselves are exempt, what about their underlying investments? Because the typical IRA owner is a retail investor, he/she is generally restricted to 40 Act registered mutual funds and certain registered insurance company annuity products; with limited exceptions, IRAs are not eligible to invest in unregistered pooled funds and other privately offered vehicles. The difference is not merely semantic. While functionally like "retail" mutual funds, unregistered funds enjoy more regulatory freedom and correspondingly lower expenses and afford sponsors flexibility to create "private label" investments customized to participants. A state not wishing to offer only registered mutual funds in its program has two choices. First, it could establish and register its own bespoke mutual funds. The registration process with its attendant disclosure, paperwork, and audit requirements could drive up expenses, without offsetting benefits to program participants. Another, more attractive, choice is to create—with the assistance of experienced financial firms—private label investment accounts within and exclusively for a state auto-IRA program. These accounts could be customized to program participants and offer advantages like those available to 401(k) and 457 plans investing in unregistered vehicles.

State boards preferring private label investment options can point to a favorable distinction between, on the one hand, traditional IRAs, which typically are owned and managed by individuals acting for themselves and, on the other hand, employer-sponsored 401(k) and similar employee savings programs. The securities laws generally take a "hands off" approach to employer-sponsored plans because employer sponsors (as well as plan trustees and investment professionals retained by the employer) are on the front lines protecting the individual plan participants. Similarly, auto-IRA plan participants will have state-appointed boards, trustees, custodians, professional managers and advisors to protect their interests. Thus, auto-IRA programs will not need or be helped by the securities regulations intended to protect a regular retail IRA investor. Financial firms sponsoring unregistered investment vehicles for 401(k) plans can assist boards in developing low-cost private label programs tailored to auto-IRA program participants, furthering the overall mission of helping workers save for their own retirement.

Patriot Act Requirements

The Patriot Act requires record keepers, trustees, and others to "know their customers" before setting up an account. That means having a full name, address, date of birth and a Social Security number that match and do not raise any red flags. When opening an IRA, the individual directly supplies the needed information to the vendor but for a 401(k), the employer supplies the information. The 401(k) approach should work equally as well for auto-IRA programs, with any discrepancies being resolved by the

[191] Feirstein, Andrea (2016), "529 College Savings Plan: Lessons for Publicly Sponsored Private Retirement Plans," Georgetown Center for Retirement Initiatives. http://cri.georgetown.edu/wp-content/uploads/2016/11/Policy-Brief-16-2.pdf.

participant dealing directly with the record keeper and without employer involvement. Withholding would not start until the problem is resolved. States should make the handling of the Patriot Act part of the requirements for record keepers and make sure to incorporate this need into any competitive bids, so potential vendors clearly understand and can deliver what is expected.

The Regulatory Path Forward

ERISA is not the only regulatory consideration for state-enabled retirement programs for private sector workers. The SEC staff has been receptive to applying the state instrumentality exemptions to other novel state programs created to help fill a pressing need, such as college 529 savings programs, so there is reason for optimism for state-sponsored retirement savings programs. States therefore should continue to move forward to help more workers save for their retirement. History suggests that federal-state collaboration can produce better outcomes. States can work closely with federal regulators to constructively resolve issues, preserve important consumer protections, while allowing workers to benefit from a wider array of savings options.

IV. Program Design Features (Appendix A)

Auto-enrollment/Auto-escalation

As summarized in Appendix A, the availability of tools such as auto-enrollment and auto-escalation are available to ERISA-based plan design options, such as 401(k) MEPs. For payroll deduction IRAs, auto-enrollment and auto-escalation can be used only if employer participation in the savings arrangement is mandated by the state.

Using auto-enrollment, a new participant would contribute at a specified default rate unless he or she affirmatively opts out or chooses a different rate. With auto-escalation, a participant's contribution rate is periodically increased by a set percentage, again with ability to opt out or choose a different rate. For example, a plan could auto enroll participants at 5 percent of pay, and increase the contribution rate by 1 percent each December 31st after the first year, until the participants reach 15 percent.

IRAs. Payroll deduction IRAs did not have access to automatic enrollment and automatic escalation until DOL issued its new safe harbor rule for state sponsored retirement plans in 2016. As previously noted, state-sponsored retirement plans must be established by the state and mandate employer participation to be able to use auto-enrollment and auto-escalation. A voluntary payroll deduction IRA program and the federal myRA program would not be able to use these tools without being considered an employee benefit plan subject to ERISA.

401(k)s. Since the enactment of the Pension Protection Act of 2006, automatic enrollment and automatic escalation have been design features available to 401(k) plans.[192]

Section V and Appendix B compare the different default contribution levels and use of auto-enrollment and auto-escalation in the five states that have enacted mandatory IRA programs. The contribution levels generally range from 3 to 5 percent.

As highlighted in Section I of this report, auto-enrollment and auto-escalation have been very successful in getting employees, even lower-paid employees, to contribute to a retirement savings plan. Behavioral economists claim these tools help to address the twin forces of inertia and "framing." However, as will be discussed in Section V, states should carefully consider where to set the bar and how much flexibility to give participants to adjust their contribution levels. Any state program would not want to unwittingly discourage workers from saving more than they would do on their own, and at the same time must also factor in long-term program costs and the need for the program to become self-sustaining within a reasonable amount of time.

Employer Participation

There are two major decisions to be made with respect to employer participation: (1) will the program be mandatory or voluntary; and (2) if there is a mandate, which employers would be subject to it?

IRAs. A state would need to decide whether it wanted employer participation to be mandatory or voluntary. If employer participation would be mandated, under DOL's new safe harbor, the state could also require employers to auto-enroll workers into the state program. If employer participation in a payroll deduction IRA program is voluntary, the state program would not be able to use auto-enrollment.

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[192] ERISA 514(e)

401(k)s. ERISA requires that employer and employee participation in any plan be voluntary.[193]

As summarized in Appendices B & C, states that have enacted mandatory auto-IRA programs have set different employer participation thresholds. California and Connecticut set their employer threshold for participation at five or more employees, Illinois sets it at twenty-five or more employees, Oregon requires all employers who do not offer a qualifying retirement plan to participate, and Maryland requires all employers to participate who do not have a qualifying retirement plan and who pay their employees through a payroll system or service.

Because the DOL new safe harbor requires mandatory employer participation for employees to be auto-enrolled, it creates an administrative challenge in the states that established employer thresholds. While states like Illinois want to allow employers below the mandated threshold to voluntarily join the program if they so choose, those small employers would not be able to use auto-enrollment for their workers; workers would need to opt in to state program.

Employer Contributions

A major difference between ERISA-exempt payroll deduction IRAs and ERISA-based 401(k) programs is the ability of employers to make contributions to an employee's account.

IRAs. Employers are not permitted to make contributions to any payroll deduction IRA. Doing so would establish an employee benefit plan subject to ERISA.

401(k)s. Employers can contribute to employees' accounts. An employer also may choose to "match" a portion of each employee's 401(k) contributions. For example, an employer could match participant's 401(k) contributions up to the first 6 percent. A plan may, but most do not, match age 50 catch-up contributions. Matching contributions may be automatic (e.g., hard wired into the plan but amendable prospectively) or discretionary (employer decides year-by-year). For administrative ease, most states would likely want to limit employer discretion, say by specifying the matching formula but allowing employers some discretion to make additional contributions at year-end.

Employee Participation

In all the plan design options reviewed, employee participation is always voluntary. If auto-enrollment is used, the employee always has the choice to opt out of participating in the program and the state would have to determine how much time a worker would have to opt out of the program. A state program also would have to make decisions about how to enroll employees, what information to provide, and the frequency of open-enrollment periods that allow workers to make changes to whether and how much they contribute to their accounts. States now implementing programs are just beginning to make these decisions.

[193] 81 Fed. Reg. 59,467 (August 30, 2016)

Employee Contribution Limits

If a program uses auto-enrollment, another important question is should a default contribution level be set and, if so, at what level. Section V discusses in greater detail the role default employee contribution levels play in the financial feasibility of state programs, specifically, California, Connecticut and Oregon.

A major difference between ERISA-exempt payroll deduction IRAs and ERISA-based 401(k) programs is the annual contribution limits for workers.

IRAs. Traditional and Roth IRAs: Cannot be more than $5,500 per year ($6,500 for individuals age 50 and older) or the taxable compensation for the year.[194]

- Traditional IRA: Contributions may be fully or partly deductible and generally amounts in the account (including earnings and gains) are not taxed until distributed.[195] Required minimum distribution begins on April 1 of the year following the calendar year in which the account holder reaches age 70 1/2.[196]

- Roth IRA: Contributions are not deductible and qualified distributions are tax-free. Contributions are permitted after the age of 70 1/2 and minimum distributions do not apply to employee.[197]

401(k)s. Employee 401(k) contributions are tax-deferred up to the Tax Code's limits—for 2017, $18,000 for those under 50 and $24,000 for those who will be at least 50 by year-end. (Dollar limits are indexed annually for inflation.) Alternatively, an employee can contribute up to these same limits as post-tax Roth 401(k) contributions. If the Roth contributions are held in the plan for at least five years, then all distributions (Roth plus investment income) are 100 percent tax-free. A plan can give participants a choice between making Roth or traditional 401(k) contributions.

It would take a crystal ball to know for certain whether a participant should make a Roth or traditional 401(k) contribution. Roth 401(k)s are advantageous if the person will be in a higher tax bracket when he or she retires or otherwise withdraws the money; traditional is better if the person will be in a lower bracket at retirement; if the person's tax bracket remains the same, then traditional and Roth 401(k)s are generally identical. Given that many participants in a state-sponsored MEP may be relatively low-paid, offering both with Roth as default may be preferable.

Withdrawals

Both ERISA-exempt payroll deduction IRAs and ERISA-based 401(k) programs allow for withdrawals from accounts. DOL rules allow states to have control to establish restrictions on withdrawals to limit leakage.[198] The tax code does not prohibit early withdrawals, it just imposes a penalty. The states are free to add their own early withdrawal limitations, such as a hardship requirement.

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194 IRS (2016), "COLA Increases for Dollar Limitations on Benefits and Contributions." https://www.irs.gov/retirement-plans/cola-increases-for-dollar-limitations-on-benefits-and-contributions.

195 IRS (2016), "Traditional IRAs." https://www.irs.gov/retirement-plans/traditional-iras.

196 IRS (2016), "Retirement Topics – Required Minimum Distributions (RMDs)." https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-required-minimum-distributions-rmds.

197 IRS (2016), "Roth IRAs." https://www.irs.gov/retirement-plans/roth-iras.

198 Leakage is a term to refer to plan fund withdrawals made by participants from IRAs or 401(k)/defined contribution plans. Data from HelloWallet, for example, suggests that 75 percent of 401(k) plan participants breached their savings because of basic money management problems, and 26 percent of 401(k) participants used their 401(k) savings for non-retirement needs. Fellowes, Matt and Willemin, Katy (2013), "The Retirement Breach in Defined Contribution Plans: Size, Causes, and Solutions,"

IRAs. Withdrawals for IRAs vary depending on whether it is a traditional or Roth IRA.

- Traditional IRA: Any deductible contributions and earnings that are withdrawn or distributed are taxable. An individual under age 59 1/2 may have to pay an additional 10 percent tax unless the withdrawal qualifies for exceptions. [199]

- Roth IRA: No penalties or taxes for a qualified distribution (payment or distribution made 5 years after the first contribution and after age 59 1/2 or due to disability, made to a beneficiary after death, or to meet the requirement of a first home purchase). All withdrawals of contributions are tax-free. An individual before age 59 1/2 may have to pay an additional 10 percent tax on withdrawal of accumulated income unless the withdrawal qualifies for exceptions. [200]

401(k)s. Hardship withdrawals are allowed, including for:

- Medical expenses for an individual, spouse, or dependents
- Purchasing principal residence
- Postsecondary education expenses for an individual, spouse, or dependents
- Payments to prevent eviction or foreclosure on residence
- Funeral expenses
- Certain expenses relating to repair to principal residence

Generally, withdrawals made before age 59 1/2 are taxed at 10 percent, unless they fall under exceptions.[201]

Tax and Other Incentives

Several states are considering whether and how to use tax incentives to encourage participation in state-sponsored plans. As previously noted, per DOL's recent safe harbor, states may use tax incentives but they must reasonably align with program costs out of concern that such incentives would competitively disadvantage private sector products.[202]

State laws have included the authority to examine ways to reduce costs using incentives, tax credits and other means. For example, Maryland's new law waives the annual corporate $300 filing fee for companies that participate in the state program (at the same time Maryland does not have penalties for noncompliance with its mandate requirement). However, for auto-IRA programs, states will need to make sure they remain within the DOL stricture against any employer incentives. The DOL safe harbor only allows states to provide offsets/tax credits against actual or estimated employer costs of participation.

HelloWallet. http://info.hellowallet.com/rs/hellowallet/images/HelloWallet_The%20RetirementBreachInDefinedContributionPlans.pdf?mkt_tok=3RkMMJWWfF9wsRonvqTMZKXonjHpfsX56O0sWaOwlMI/0ER3fOvrPUfGjI4ASMZjI%2BSLDwEYGJlv6SgFSLDDMbJn0LgNUhc%3D.

[199] IRS (2015), Roth IRAs in "Publication 590-B, Distributions from Individual Retirement Arrangements (IRAs)." https://www.irs.gov/publications/p590b/ch02.html#en_US_2015_publink1000231061

[200] IRS (2016), "Traditional and Roth IRAs." https://www.irs.gov/retirement-plans/traditional-and-roth-iras.

[201] IRS (2016), "401(k) Resource Guide – Plan Participants – General Distribution Rules." https://www.irs.gov/retirement-plans/plan-participant-employee/401k-resource-guide-plan-participants-general-distribution-rules.

[202] 81 Fed. Reg. 59,467-8 (August 30, 2016)

For workers, states are considering how the existing federal Saver's Tax Credit currently available but little known could be more effectively used to help increase participation in state-sponsored programs.[203] The recommendations focus on ways to highlight and more effectively provide information about the Saver's Credit to workers as part of the implementation of a state-sponsored retirement program.

Lifetime Income

A lifetime income distribution option would guarantee that participants receive a continuous income stream in retirement.[204] The GAO recently issued a report outlining some steps that could be taken to improve the use of retirement income options for plan participants. In its report, GAO surveyed 11 401(k) plan record keepers that accounted for approximately 42 percent of the 401(k) market and found that three-quarters of plans did not offer an income annuity.[205] Some of the reasons for the lack of take up include: the risk of poor investment returns leading to lower than expected savings, the timing of retirement reducing savings if there are poor investment returns just before or at the time of retirement or the risk of outliving savings. [206]

The GAO reports that industry stakeholders and Treasury officials tell them that many plans lack partial annuitization options. The result is that many participants only have the choice to annuitize their entire account balance or none of it. [207] When faced with an "all-or-nothing" choice, most participants will bypass the annuity options and opt for a lump sum. Participants are concerned about full annuitization because it does not allow them to set aside or access savings for emergencies.[208]

Connecticut is the first state to show leadership on the issue of lifetime income. Its legislation directs that once the participant reaches normal retirement age, 50 percent of the account will be invested in the lifetime income investment. The Connecticut Retirement Security Authority will designate a lifetime income investment option intended to provide a source of retirement income for life. There are different annuity options states could consider, including: an immediate annuity at retirement where participants would purchase an annuity that begins payments within twelve months of purchase; a longevity annuity which would make payments later, typically when the participant is age 80 or older; or a target date fund which includes the purchase of an annuity over a participant's working life.[209]

The GAO made several recommendations for steps that can be taken at the federal level to improve retirement income options, including clarifying the criteria to be used by plan sponsors to select an annuity provider and potentially providing limited liability relief for offering an appropriate mix of lifetime income options.[210] Thought leaders and policymakers have much work to do to assess what can

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[203] National Institute on Retirement Security and The Aspen Institute Financial Security Program (2016), "How States Can Utilize the Saver's Tax Credit to Boost Retirement Savings." http://www.nirsonline.org/storage/nirs/documents/savers_tax_credit_factsheet_2016.pdf.

[204] Kahn, Melissa and Strakosch, J. (2015), "Making State Retirement Plans Work for Private Employers: Including Lifetime Income Options," AARP Public Policy Institute. http://www.aarp.org/content/dam/aarp/ppi/2015/making-state-retirement-plans-work-for-private-employers-spotlight.pdf.

[205] U.S. Government Accountability Office (2016), "401(k) Plans: DOL Could Take Steps to Improve Retirement Income Options for Plan Participants (16-433)," p. 2. http://www.gao.gov/assets/680/678924.pdf.

[206] Ibid., p. 6.

[207] Ibid., p. 23.

[208] Ibid., p. 24.

[209] Kahn, Melissa and Strakosch, J. (2015), op. cit.

[210] U.S. Government Accountability Office (2016), "401(k) Plans: DOL Could Take Steps to Improve Retirement Income Options for Plan Participants (16-433." http://www.gao.gov/products/GAO-16-433. See highlights page.

and should be done with both legal and regulatory reforms to encourage the development and accessibility of lifetime income options.

Plan Design Features: Delegate to Board

In drafting legislation to establish a state-sponsored retirement savings program, a state would be wise to avoid locking itself into too many of the program design details in legislation. An early lesson learned by some of the more recent states (California, Connecticut) that have enacted legislation is to leave more discretion and flexibility to the state and its designated program board to determine the program features that would work best. After a law is enacted, a state board may be informed by market and financial feasibility studies, and this information will help to make better decisions about program design features. A Board must balance employer preferences against administrative costs and complexity. A state needs to determine what will work best for design details such as the default contribution level and the use of auto-escalation features, as well as how to structure the accounts and manage investments. Section V will review in greater detail some of the lessons learned from states that studied different plan features and the projected impact on a plan's financial feasibility.

V. Program Management, Participation, and Financial Feasibility: Lessons from the States[211]

Administration

Under the DOL safe harbor for state auto-IRA programs, a state can delegate administrative authority of the auto-IRA program to an instrumentality of the state.[212] Each of the five states that have enacted such programs have appointed a board.[213] The number of board members ranges from seven each in Illinois and Oregon, to fifteen in Connecticut.

As shown in Appendices B & C, each board has the authority to enter contracts with professional service providers (such as financial advisors, consultants, and third-party administrators) for the purpose of implementing and administering the program. Boards have the authority to employ staff as necessary. Boards are also responsible for ensuring that the programs meet the criteria for federal tax-deferral or tax-exemption benefits.

States that have enacted voluntary programs have formed agencies to make the programs available. In Massachusetts, which has enacted a prototype plan for non-profits with 20 or fewer employees, the agency exists in the office of the Treasurer with a five-member DC committee. The Treasurer may require the non-profit employer to sign a service agreement and use forms and procedures as arranged by the Treasurer.

In the case of states which have enacted a marketplace model, these programs exist under the Department of Commerce for Washington and the Treasurer for New Jersey. The Director and the Treasurer (or designee) in these states, respectively, will contract with private sector entities in operating the marketplace. They will also consult with outside organizations representing a wide range of groups, from eligible employers and qualified employees to retirement plan administrators and private sector financial services firms, in implementing the marketplace.

Program Participation and Costs

State-Sponsored Auto-IRA Programs

As a growing number of states move toward establishing retirement savings plans for private sector workers who lack access to an employer-sponsored plan, policymakers and stakeholders are very interested in plan cost. Will the program be self-sustaining? Can it charge fees that are low enough to be attractive to participants? What happens if enrollment falls short of assumptions?

States should be encouraged by findings from the financial feasibility studies conducted on state-sponsored retirement plans in California, Connecticut, and Oregon.[214] These states are pursuing an

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[211] This section is draw heavily from Rhee, N. (2016), "Lessons from California, Connecticut, and Oregon: How Plan Design Considerations Shaper the Financial Feasibility of State Auto-IRAs," Georgetown Center for Retirement Initiatives, November 2016 at http://cri.georgetown.edu/wp-content/uploads/2016/12/Policy-Brief-16-3.pdf.

[212] 29 CFR 2510.3-2(h)(1)(ii)

[213] See Georgetown Center for Retirement Initiatives, "State Brief 16-01: Comparison of Retirement Plan Design Features, By State: Illinois, Oregon, Maryland, Connecticut and California." http://cri.georgetown.edu/state-briefs/.

[214] Overture Financial (2016), "Final Report to the California Secure Choice Retirement Savings Investment Board." http://www.treasurer.ca.gov/scib/report.pdf.; Center for Retirement Research (2016), "Oregon Feasibility Study Report (Draft)." http://www.oregon.gov/treasury/ORSP/Documents/DRAFT%20Feasibility%20Study%2013JULY2016.pdf.; State of Connecticut Retirement Security Board (2016), "Report to Legislature: Connecticut Retirement Security Board," http://www.osc.ct.gov/crsb/docs/finalreport/CRSB_January_1_Report.pdf.

auto-IRA model in which most private employers that do not sponsor their own retirement plan must auto-enroll their employees in a payroll deduction IRA managed by the state. Each state hired consultants to study market demand for the plan, estimate likely participation rates, advise on plan design, and determine whether the plan could achieve financial self-sufficiency based solely on participant fees. All three studies indicate state auto-IRAs can be self-sufficient while charging attractive participant fees over the long run. Based on conservative assumptions, they project programs will break even in 3 to 5 years, depending on the study, and fully pay off any startup financing in 6 to 7 years.[215]

At the same time, policymakers need to understand which factors drive program finances, which ones surprisingly do not, and the potential pitfalls that can undermine program sustainability. The studies offer key lessons on both the cost and revenue sides of the equation:

1. **Recordkeeping services, which entail recording and tracking account transactions, make up the biggest and most challenging cost component.** Recordkeeping costs need to be carefully managed through program design that minimizes complexity. The larger the number of potential decision points and exceptions the recordkeeper must implement, the larger the potential cost. In addition, paper and phone transactions are also much more costly than electronic transactions.

2. **To minimize investment management costs, programs need to take full advantage of their scale by choosing institutional rather than retail investment products and services.** In particular, custom funds (in trade parlance, Collective Investment Trusts or "white label" funds)—have significantly lower expense ratios than off-the-shelf mutual funds and can be tailored to the needs of plan participants.

3. **On the revenue side, the program's default contribution rate policy—that is, the percentage of an employee's pay that will be deposited into their accounts unless he or she chooses otherwise—ultimately determines the horizon for the program becoming financially self-sufficient.** The three financial feasibility studies recommend default contribution rates of 5-6 percent, which will allow states to recoup startup costs within a reasonable timeframe without sacrificing employee participation rates.

Understanding Plan Cost Fundamentals

Each of the three key components of state auto-IRA program cost—recordkeeping, investment management, and program administration—has its own dynamic:

- ***Recordkeeping*.** Recordkeeping includes signing up new employers, tracking enrollments and opt-outs, conducting due diligence, establishing employee accounts, processing contributions and withdrawals, recording and implementing employee choices regarding contribution rates and investments, generating reports and tax documents, and providing customer service related to these activities. Recordkeeping costs are dominated by unit costs per each employer and each employee account, and constitute by far the largest cost center during program startup.

- ***Investment.*** While the Board of Trustees of the state auto-IRA program will set investment policy and exercise oversight, day-to-day management of investment portfolios will be contracted out.

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[215] States have a number of options for financing startup costs and initial operating deficits: startup funding (generically defined as any type of funding whether it be public or private), a line of credit, a subsidy from the recordkeeper in exchange for a longer-term contract, and/or a temporary increase in fees. For purpose of this paper, "startup financing" refers to any of these options.

Investment management fees are typically charged as a percentage of assets. State auto-IRAs can expect to command low investment management fees if they take advantage of their scale. Because it does not cost much more to manage a $10 billion fund than a $1 billion fund, the program's investment expense ratio—the percentage of assets spent on investment management—can be expected to drop as the plan's asset base grows.

- ***Program administration costs.*** The cost for a state to administer an auto-IRA is generally fixed. This can be defrayed with program revenues and spread across a large participant and asset base. Administration costs include program staff salaries, board expenses, consultant and legal expenses, and fiduciary liability insurance premiums. One-time program startup cost estimates in the three studies range between $.5 million and $1.1 million. Ongoing annual program administration costs are estimated to be up to $1 million in Connecticut, $1.3 million in Oregon, and $6.6 million in California, averaging just a few dollars per participant.

Until sufficient assets have been accumulated, program costs will exceed revenues during the startup phase. Because states are reluctant to levy high participant fees, all three studies identify two other options for financing the initial operating deficit. One option is for the state to provide startup funding and/or a line of credit to be paid back with interest once the program achieves positive cash flow. The other option is to have financial service providers subsidize the startup cost in exchange for a longer-term contract, essentially loaning its own capital to the program. States may choose either or a combination of both.

Simplicity and Scale Drive Cost Efficiency

Cost containment is critical for state auto-IRAs because they will start out with many accounts to service, but low average balances on which to charge fees. To minimize total program expenses as a percentage of assets, states must minimize program complexity and effectively leverage economies of scale.

- ***Plans must minimize complexity to contain cost.*** The above studies assume relatively low operating costs based on a few critical factors. First, state auto-IRAs bundle a large retirement savings market, dramatically lowering the marketing costs vendors normally must recover. Second, the studies assume a simplified retirement savings program in which participants have a limited choice of investments; if-then decisions on the part of recordkeepers and employers are minimized; and electronic communications are maximized in lieu of phone and paper. This is a departure from "rich" 401(k) service models that feature a high level of employee choice and embed significant marketing costs.

- ***Plans must effectively leverage economies of scale to minimize investment and recordkeeping expenses.*** The studies use relatively low expense ratios for investment management—ranging between 17 and 20 basis points—because state auto-IRAs can command low fees from institutional investment managers, just like large 401(k)s and public pensions. These are much lower than typical mutual fund fees, which average 67 basis points.

  The California study emphasized a corollary mechanism for cost savings, in which investment management contracts are "unbundled" from recordkeeping. That is, a state auto-IRA need not be tied to using a single firm to provide both recordkeeping and investment management expenses. Rather, it can seek out the best provider for each element. This is a model used in many large 401(k) plans to lower costs and maintain flexibility.

The studies also assume contributions would be spread across a minimal number of funds—e.g., a Target Date Fund series and a principle preservation option. Concentrating assets in a limited number of institutionally managed funds minimizes investment expenses.

In addition, states can also expect to benefit from de facto “bulk discounts” for recordkeeping, as well as simplify administration, by relying on a single recordkeeper.

The Importance of Default Contribution Rate Policy

For a program cost budget, the biggest factor driving the bottom line is the default contribution rate policy. Behavioral finance research and empirical evidence from auto-enrollment 401(k) plans indicate workers tend to stay with the default contribution rate.[216] This means a state auto-IRA’s default contribution rate policy will determine how much workers contribute to the plan each year, and therefore the size of the asset base on which fees are charged. Because of this, all three states found the default contribution rate would have a much bigger impact than any other factor related to deposits and withdrawals—including opt-out rates, account closures, and leakage—on how long their respective programs will take to achieve positive cash flow and pay off any startup financing.

The table below summarizes projections from the financial feasibility studies in California, Connecticut, and Oregon. While the study methodologies differ somewhat across the states, as do participant demographics and the total wage base, they generate roughly similar findings.

To begin, the baseline scenarios using default contribution rates of 5-6 percent indicate a relatively short horizon for self-sufficiency. In Connecticut, a 6 percent default leads to breaking even between years 2 and 3 and paying off the startup financing in year 6. In California, a 5 percent default leads to the program breaking even between years 3 and 4 and paying off the startup financing in year 7. In Oregon, a 6 percent default with auto-escalation leads to the program breaking even between years 4 and 5 and paying off the startup financing in year 7.

States can expect to be able to dramatically lower program fees after initial deficits have been repaid. All three states project expense ratios will drop quickly over time, to under 50 basis points in the 10th year of program operation, and continue to decline thereafter.

The studies also demonstrate program finances are highly sensitive to the default contribution rate. A 3 percent fixed contribution rate extends the break-even horizon by 2 years in the California and Connecticut studies. In the Oregon study, a 3 percent fixed default extends the startup financing payoff horizon by a longer time span—5 years—because the baseline model assumed both a higher default and auto-escalation. With longer timelines, it is possible that states may need to take on a greater share of the financing burden because private vendors will be less likely to tolerate losses for an extended period.

[216] Choi, James, Laibson, D., Madrian, B. C. & Metrick, A (2004) “Saving for Retirement on the Path of Least Resistance,” National Bureau of Economic Research. http://www.nber.org/programs/ag/rrc/04-08LaibsonFinal.pdf.; Robinson, Mark (2010), “Success of Auto Enrollment and Auto Increase: Using Behavioral Finance to Improve Retirement Planning,” Presented at EBRI Policy Forum, May 13, 2010. https://www.ebri.org/pdf/programs/policyforums/Robinson0510PF.pdf.; Clark, Jeffrey W., Utkus, Stephen P. & Young, Jean A. (2015), “Automatic Enrollment: The Power of the Default,” Vanguard Research. https://pressroom.vanguard.com/content/nonindexed/Automatic_enrollment_power_of_default_1.15.2015.pdf.

State Auto-IRA Financial Feasibility Study Results

	California	Connecticut	Oregon
Baseline Scenario			
Default contribution rate	5%, no auto-escalation	6%, no auto-escalation	5%, auto-escalation to 10%
Fee assumption	1%	0.5%	1.2%
Break-even horizon	Years 3-4	Years 2-3	Years 4-5
Startup financing payoff	Year 7	Year 6	Year 7
Long-term expense ratio	45 bp (0.45%) in year 10	47 bp in year 10	47 bp in year 10
Alternative Scenario			
Default contribution rate	3%, no auto-escalation	3%, no auto-escalation	3%, no auto-escalation
Break-even horizon	Year 6	Year 4	Year 8
Startup financing payoff	Year 9	Year 8	Year 12

Sources: Overture Financial 2016, Connecticut Retirement Security Board 2016, Center for Retirement Research 2016.

Opt-Out Rates, Account Closures, and Early Withdrawals Are Not Critical

Contrary to what many believe, program sustainability is not particularly sensitive to significant increases in opt-out rates, account closures, and early withdrawals. This is because state auto-IRA plan costs will be dominated by *variable* costs tied to the number of employers, number of employees, and plan assets. During the startup phase, recordkeeper costs for servicing employers and employees will make up the largest cost center. Conversely, fixed costs make up a minority of program costs. [217] In most states, an auto-IRA with an employer mandate can expect to achieve an adequately large base of participants and assets across which to spread fixed costs, even with opt-out rates that are significantly higher than expected.

California. As the largest state in the US, California has an extraordinarily wide margin of error when it comes to employee opt-out. About 6.8 million workers are potentially eligible for the California Secure Choice Retirement Savings Program.[218] Likely participation rates (70-90 percent) are sufficiently high to enable the program to achieve broad coverage well above the minimum threshold for financial sustainability.[219] The upper bound of the opt-out rate (30 percent) applies to an active-choice model in which each employee needs to actively confirm their enrollment.[220] The lower bound (10 percent) applies to a passive-choice model in which each employee is given an opportunity to opt out, and is then enrolled if they take no action.[221]

[217] Connecticut's study identified $1B in assets at the feasibility threshold, entailing an estimated $.5-1 million in fixed program costs and $4-$4.5 million in variable costs (Connecticut Retirement Security Board, op cit, p. 38). Immediately after full program rollout, variable costs will make up over 70% of total costs in California (author's calculations based on California financial feasibility model) and 64% in Oregon (calculation provided by Geoffrey Sanzenbacher, Center for Retirement Research).
[218] Overture Financial (2016), "Final Report to the California Secure Choice Retirement Savings Investment Board," p.6. http://www.treasurer.ca.gov/scib/report.pdf.
[219] Ibid.
[220] Ibid., p.19.
[221] Ibid.

The baseline financial feasibility model for California Secure Choice, which assumes 25 percent opt-out, shows that 70 percent of ongoing costs—after all eligible employers have registered and auto-enrolled their employees—will consist of variable costs related to servicing employer and employee accounts.[222] Furthermore, investment expenses are also variable, based on assets under management. Consequently, even if 50 percent of employees opt out, the program could still pay back its startup financing by year 7 in the baseline scenario. Its expense ratio would decline to just 50 basis points in year 10. The program could pay back the startup financing by year 10 even with a 70 percent opt-out rate.

Oregon. Smaller states also have a comfortable margin for acceptable opt-out rates. Approximately 1.05 million workers in Oregon are estimated to lack access to a retirement plan through their employer.[223] Oregon's market analysis report estimates employee participation to be roughly 70-80 percent of workers who are automatically enrolled into ORSP. Only 20-30 percent of workers who are automatically enrolled are likely to opt out of the program.[224] The opt-out rate is expected to be low for any contribution rate between 3 and 6 percent of pay and regardless of the choice of a before-tax or after-tax savings vehicle, the number of investment choices, and the presence of a default annuity withdrawal option upon retirement.[225]

Participation rates for workers not automatically enrolled but eligible for the ORSP (the opt-in group) are likely to be much lower, in the range of 20 to 30 percent. Participation in this group is likely to be influenced by ease of enrollment, user interface, plan design and advertising.[226]

Oregon's feasibility study found a 50 percent opt-out rate and a 50 percent account closure rate among employees switching jobs will increase the startup loan payoff horizon by one year, but also lead to a smaller program deficit during startup.[227]

Finally, the Oregon and California financial feasibility models show assets lost through account closures and early withdrawals will be dwarfed by incoming contributions and existing assets, blunting their impact on program finances.

Mind the Program Design

The financial feasibility studies for auto-IRA programs in California, Connecticut, and Oregon demonstrate that over the long term (and in some cases, the short term), they can afford to charge low fees and remain self-funding. This requires states to be vigilant about program design to minimize cost, and to be aware of the ways in which default contribution policy affects the horizon for program self-sufficiency.

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[222] The California study integrates other conservative model assumptions so that a 25% employee opt-out rate translates to an effective opt-out rate in excess of 40% in relation to the total universe of eligible workers. Mohammad Baki and Nari Rhee, "Response to Selected Public Comments Regarding the Financial Feasibility and Market Analysis Studies Conducted for California Secure Choice," March 23, 2016. http://www.treasurer.ca.gov/scib/comments/overture_responses.pdf.
[223] Center for Retirement Research (2016), "Oregon Market Research Report," p.1. http://www.oregon.gov/treasury/ORSP/Documents/ORSP%20Market%20Analysis%2013JULY2016.pdf.
[224] Ibid., p.3.
[225] Ibid.
[226] Ibid.
[227] Center for Retirement Research (2016), "Oregon Feasibility Study Report (Draft)," p. 17. http://www.oregon.gov/treasury/ORSP/Documents/DRAFT%20Feasibility%20Study%2013JULY2016.pdf. The alternative scenario also included a higher account closure rate.

States should keep plans simple and maximize electronic transactions in lieu of paper and phone transactions. They should also take full advantage of low-cost institutional investment management options available to large plan sponsors, for instance by building custom funds that can offer lower costs than off-the-shelf products while meeting the specific needs of plan participants. Finally, states should be aware a default contribution rate of 5-6 percent will yield the same participation rates as a 3 percent default, but allows the program to become self-sufficient in a shorter timeframe.

With careful design, states can offer an attractive retirement savings plan to employees who lack access to a 401(k) or pension, and to small businesses that are hard-pressed to negotiate the cost and complexity of employer-sponsored plans.

State-Sponsored MEPs

For small employers, MEPs would allow small businesses to participate in a single, professionally administered plan that provides them with economies of scale and minimal fiduciary responsibility.[228] MEPs designed for the small business community will reduce costs and administrative burdens by providing centralized plan administration and management and reduce fiduciary responsibilities for small employers sponsoring retirement plans by discharging fiduciary and administrative responsibilities to plan and investment professionals. In this way MEPs may offer an attractive and cost-efficient alternative for small (and even mid-size) businesses over stand-alone plans by utilizing economies of scale and cost efficiencies.[229] If run properly, MEPs are seen to have the potential to increase plan sponsorship, lower fees paid by participants and result in overall better services with fewer conflicts.[230] According to the Transamerica Center for Retirement Studies 16th Annual Transamerica Retirement Survey, 22 percent of employers who are not likely to offer a plan indicated that they would consider joining a MEP offered by a vendor who would handle much of the fiduciary and administrative duties.[231]

Most, if not all, states will want the MEP to cover the cost of its own operations. This would include not only recordkeeping and investment fees, but also expenses for outside lawyers, consultants, auditors and employee education and communication. Each employer could be charged for its share of some of these expenses, but DC plans typically impose these costs on participating employees. Employee payments can be handled through fees embedded in mutual fund and/or investment management fees or by a separate charge (percentage or flat fee) deducted from each employee's account. The trend among larger, more sophisticated plans is to only embed investment related fees and separately charge for all other expenses. To avoid undue hardship and the chilling effect of a flat dollar fee on new and low-paid employees but without penalizing long-tenured, high savers, a plan could charge a percentage fee up to a stated cap.

State-sponsored MEPs raise two additional fee questions: who pays the startup costs and can participants be charged for so-called "settlor-type" expenses. First, to the extent that startup costs are not picked up by taxpayers or outside donations, they would have to be covered, as a practical matter, by employees. Obviously, it would be unfair and a likely deal killer to charge newly enrolled employees for their "share" of the startup costs through higher investment and accounts fees, until these expenses

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228 Kalamarides, John J., R.J. Doyle, B. Kleinberg, "Multiple Employer Plans: Expanding Retirement Savings Opportunities," Prudential, p. 3. http://research.prudential.com/documents/rp/mep_paper_final_2015.pdf.
229 Advisory council on Employee Welfare and Pension Benefit Plans (2014), "Outsourcing Employee Benefit Plan Services," p. 19. https://www.dol.gov/sites/default/files/ebsa/about-ebsa/about-us/erisa-advisory-council/2014ACreport3.pdf.
230 Ibid.
231 Transamerica Center for Retirement Studies (2015), "16th Annual Retirement Survey: A Compendium of Findings About American Workers," p. 22. https://www.transamericacenter.org/docs/default-source/resources/center-research/16th-annual/tcrs2015_sr_16th_compendium_of_workers.pdf.

are recovered. And, ERISA requires that all charges paid by the plan and participants must be reasonable for the services provided.[232] Thus, the practical solution would be for the money managers and recordkeeper to initially absorb these costs as an investment to be recovered gradually through its profit margin. No doubt, each state will take its own approach to this issue.

The second question concerns whether ERISA limits the types of state or board expenses that may be imposed on participants. Under ERISA, participants may not be charged for “settlor” expenses. For typical employer-sponsored plans, settlor expenses involve employer activity for its own (and not the plan’s) benefit.[233] Examples include costs of a design study on whether to add a new feature to the plan. With a state-sponsored MEP the startup and other settlor-type costs are incurred by the state not the employer. Logic dictates that these state expenses are not the type of settlor charges proscribed by the DOL, since the expenses incurred by the state or board should be to benefit the plan. After all the state will not have any employees covered by the plan and will be acting solely to promote retirement savings by private sector workers. (Of course, this would not be the case if the board abused their authority, say by holding meetings at exotic luxury resorts.) Thus, all expenses should be considered as payable by the plan under ERISA. Given the DOL’s stated goal of encouraging states’ efforts to promote retirement security, all reasonable board expenses should be payable from the plan. However, states may wish to seek informal or formal guidance from the DOL on this point.

State-Sponsored Marketplaces

The Washington State legislature appropriated $524,000 to the Department of Commerce for the two-year budget cycle beginning on July 1, 2015 for the development of the Small Business Retirement Marketplace. In addition, the Director may use private funding sources including private foundations grants to pay for Marketplace expenses. The Department of Commerce is authorized to seek and accept federal and private grants for use in the Marketplace. The costs to the state of establishing and administering a marketplace should be modest, with much of the costs expected to be borne by plan providers. Administrative fees paid by investors are capped at 1 percent.

Appendices B & C review the range of appropriated dollars for the startup costs of different state programs.

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[232] There have been dozens of class action suits against sponsors and vendors seeking return of too high fees. See e.g., Abbott v. Lockheed Martin Corp. 3:06-cv-00701 (S.D. Ill.); Nos. 12-8037, 12-3736 (7th Cir.)

[233] See Letters to Carl J. Stoney, Jr. from Robert J. Doyle (Advisory Opinion 01-01A, January 18, 2001); Samuel Israel from Robert J. Doyle (Advisory Opinion 97-03A, January 23, 1997); Kirk Maldonado from Elliott I. Daniel (March 2, 1987); John Erlenborn from Dennis M. Kass (March 13, 1986).

VI. Summary of Key Issues to Consider in Structuring a State-Sponsored Plan

The key issues that a state legislature must consider in setting the general specifications for a state-sponsored retirement program include the following:

Program/Feature	**Payroll Deduction IRA**	**401(k) MEP & Prototype Plans**
ERISA Regulation	ERISA-exempt	ERISA-covered
Administrative Simplicity	Yes	Yes, but MEPs more than Prototype Plan
Employer Mandate	Yes, for use of auto-enroll features. Otherwise, states can use 1975 safe harbor for voluntary payroll deduction IRAs.	Not permitted
Auto-enrollment with Employee Opt Out	Available, but only if state mandates employer participation	Available
Contributions	• Employee – yes. Both traditional pre-tax and Roth. • Employer - no	• Employee – yes. Both traditional pre-tax and Roth. • Employer - yes
Investments	Employee chooses from plan “menu”, including a state-pooled and professionally managed option and/or private sector (third-party) options; or state could choose to direct investments.	Employee chooses from plan “menu”, including a state-pooled and professionally managed option and/or private sector (third-party) options; or state could choose to direct investments.
Withdrawals	Permitted, but tax penalties would apply. States can have discretion to limit withdrawals to reduce leakage.	Permitted, but tax penalties would apply. States can have discretion to limit withdrawals to reduce leakage.
Pros	• Simple • Low-cost • Easier to establish • Can mandate employer participation (and thus use auto-enrollment)	• ERISA protections • Some complexity but flexible design • Employees may contribute more up to $18,000 ($24,000≥ *age 50);* • Allows employer contributions • No mandate needed to use auto-enrollment
Cons	• No ERISA protections • Must mandate employer participation to use auto-enrollment • Relatively low contribution levels of $5,500 ($6,500≥ age 50) • No employer contribution • Some participant leakage depending on plan design • Investment risk on participant	• Employer participation must be voluntary • Some participant leakage depending on plan design • Investment risk on participant

Of course, this summary chart leaves off the many, many nuances that must be analyzed before a program can be designed and enabling legislation crafted. Yet, if the basic parameters can be set—simplicity vs. stronger retirement vehicle, ERISA or no-ERISA regulation—the actual task of designing the program will be significantly streamlined.

Conclusion

Too many Americans are finding it increasingly difficult to save for their retirement. The implications for government programs could be significant in the future as the population continues to age and live longer than ever before with little or no retirement savings. More state governments are recognizing the need to get ahead of this trend and look for innovative ways to expand the availability and effectiveness of retirement plans for private sector employers and employees.

States are leading the way in developing simple, easy-to-use retirement plans to help private sector employees save for retirement. State innovation should be encouraged because every state has unique demographic, economic, and retirement needs. No plan design option is without some uncertainty regarding how federal employee benefit, tax and/or securities laws apply.

Although simpler, lower cost and easier to establish, IRAs are limited by low contribution levels and no possibility of employer contributions by participants. A state has the option to make its programs mandatory or voluntary, although the use of auto-enrollment would be conditional on the state establishing an employer mandate. The state would also have to assume responsibilities for establishing a fiduciary and consumer protection regulatory framework because it would not be subject to ERISA.

To permit larger employee contributions, employer contributions, and generally greater flexibility, a 401(k) DC approach would be needed. Although the plan would be covered by ERISA, this need not be viewed as an obstacle, although employer participation would have to be voluntary and may reduce overall participation. An ERISA plan can be structured to minimize the possibility of ERISA liability to the state and the program governing board, be user-friendly to adopting employers, and offer employees the added protections that ERISA provides.

By choosing to implement a retirement plan for private sector workers, Vermont would be taking an important and much-needed step in helping its residents save for a more secure retirement.

APPENDICES

A. **Publicly Sponsored Private Retirement Plans: Comparison of Plan Design Options and Features**

B. **Comparison of Plan Design Features, by State: Illinois, Oregon, Maryland, Connecticut, and California**

C. **Comparison of Plan Design Features, by State: Massachusetts, Washington, and New Jersey**

APPENDIX A

GEORGETOWN UNIVERSITY
McCourt School *of* Public Policy
Center for Retirement Initiatives

Publicly Sponsored Private Retirement Programs: Comparison of Plan Design Options and Features

Policy Brief 16-01

November 30, 2016

The Federal Government Clears the Path for States to Innovate – A Review of the Options and Features

This chart summarizes the range of plan design options and their features available to states to expand access to simple, low cost retirement savings options for private sector workers. The federal government took action in 2016 to "clear the pathway" and expand the options available to states. These actions include:

1) **Creating a New Employee Retirement Income Security Act of 1974 (ERISA) Safe Harbor for Publicly Sponsored Auto-Enroll Individual Retirement Accounts (IRAs)**. On August 30, 2016, the U.S. Department of Labor (DOL) published a final rule related to Savings Arrangements Established by States for Non-Governmental Employees establishing a new safe harbor for state savings arrangements that allow qualifying state payroll deduction IRA programs using auto-enrollment to be exempt from ERISA. Also on August 30, 2016, DOL published a proposed rule for public comment that would allow certain state political subdivisions, such as cities, to establish similar types of plans.

2) **Issuing Guidance Regarding Publicly Sponsored ERISA Plans**. On November 18, 2015, DOL issued Interpretive Bulletin 2015-02 regarding certain state laws designed to expand the retirement savings options available to their private sector workers through ERISA-covered retirement plans. The guidance outlined three specific approaches states may choose to take including marketplaces, open multiple-employer plans (MEPs) and master and prototype plans.

3) **Launching the Federal myRA program.** Beginning in November 2015, this program has made available to workers a voluntary Roth IRA without fees and the ability set up automatic contributions of any amount desired by the worker.

These programs and policies expand the options available to states to beyond what already existed, which was a **1975 original safe harbor for payroll deduction IRAs** (See 29 CFR 2510.3-2(d); 40 FR 34526 (Aug. 15, 1975)).

This chart compares the features of all of these plan design options. The original 1975 safe harbor outlines conditions under which payroll deduction IRAs offered by employers would not be treated as ERISA plans. The conditions include requirements that: the employer make no contributions; the employer does not endorse the plan; and the employee's participation is "completely voluntary." This original safe harbor remains available to employers and now to states that wish to sponsor payroll deduction IRA plans. The new, second safe harbor was determined to be needed because a program using automatic enrollment ("auto-enroll") was determined by DOL to not meet the conditions of "completely voluntary" as outlined in the 1975 safe harbor.

States Are Leading the Way. The options outlined in this chart do not restrict options that states could take to promote retirement security for private-sector workers. As the DOL has noted, states have the ability to experiment (29 CFR 2510.3-2(a)) and may take "additional or different action…with other programs or arrangements" (80 Fed. Reg. 59466 (August 30, 2016)). States have begun to look at hybrid options combining different plan options and features. For example, the Retirement Security Study Group of the New York City's Office of the Comptroller recommended offering a voluntary retirement program NYC Marketplace including a new publicly sponsored Empire City 401(k) Multiple Employer Plan (MEP) and a new default Roth IRA for those employers who do not already have or provide a retirement plan either on their own or through the publicly sponsored marketplace.

What is important to note in this overview of plan design options is the number of options available to states and *most of the options are voluntary participation for both the employer and employee*, most notably for ERISA-covered plans **(shown as "Voluntary" in the chart)**. Of the six options presented in this chart, *there is only one option where employer participation must be mandated by a state (and employee participation remains voluntary through use of the opt-out option)* and that is if the payroll deduction IRA program uses auto-enrollment as outlined in the new safe harbor established by the U.S. Department of Labor **(shown as "Mandatory" in the chart)**.

Consistent with the history of 529 college savings plans, the federal government has taken action to support policies encouraging innovation at the state level. The federal government took such action to allow states to move forward with programs they had *already established*, primarily mandatory auto-IRA programs (more commonly referred to as "Secure Choice"). The federal government stepped out of the way of these states. The federal government must continue to work collaboratively with states and cities to develop *and implement* innovative and successful programs that will strengthen the retirement security for the millions of American workers today who lack access to simple, low-cost ways to save.

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
ERISA Applicability	Yes ERISA provides a well-established uniform regulatory structure with important consumer protections, including fiduciary obligations, automatic enrollment rules, recordkeeping and disclosure requirements, legal accountability provisions, and spousal protections.	Yes	The marketplace is itself not a plan and would not be ERISA-regulated. The plans and other arrangements available to employers through the marketplace could include ERISA-covered plans and other non-ERISA savings arrangements.[1]	No[2]	No The DOL established a 1975 safe harbor (See 29 CFR 2510.3-2(d); 40 FR 34526 (Aug. 15, 1975)) outlining conditions under which payroll deduction IRAs would not be treated as ERISA plans if provided voluntarily by employers. The conditions set out that employee participation is "completely voluntary" (meaning decision regarding an employee's enrollment in the program is made by the employee not the employer) and highlight that limited employer involvement as key to determining whether the employer has not established or maintained an employee benefit plan.	Not subject to ERISA

[1] 80 Fed. Reg. 71,937 (November 18, 2015) -Interpretive Bulletin Relating to State Savings Programs That Sponsor or Facilitate Plans Covered by the Employee Retirement Income Security Act of 1974,

[2] DOL responded to the Treasury Department on December 15, 2014 regarding ERISA's applicability to President Obama's myRA program. In the letter, DOL wrote that, given the absence of any employer funding or role in myRA's administration or design, it was the DOL's view that an employer would not be establishing or maintaining an "employee pension benefit plan" under ERISA.

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
State Role	The state, or designated governmental agency or instrumentality would be the plan sponsor under ERISA and the named fiduciary and plan administrator responsible (either directly or through contracted agents) for administering the plan, selecting service providers, communicating with employees, paying benefits, and providing other plan services. Fiduciary responsibilities would be assigned to the parties responsible for administration and management of the state MEP.	In a state administered prototype plan the state or state designee assumes responsibility for ERISA compliance. The degree of state involvement would depend on the program's structure, but would be less than under MEP approach (e.g., adopting employers would be plan sponsors and named fiduciary). Thus, the state or a designated third-party could assume responsibility for most administrative and asset management functions of an employer's prototype plan. The state could also designate low-cost investment options and a third-party administrative service provider for its prototype plans.[3]	The state would contract with the private sector to establish a program that connects eligible employers with qualifying savings plans available in the private sector market. The state would set standards to determine whether products are suited for small employers, provide good quality, and charge low fees to be included in the marketplace.[4]	No action from the state is required. However, states may consider whether and how they may want to incorporate myRA accounts into their programs.	The state may establish a voluntary payroll deduction IRA, but only may use the auto-enrollment feature and be exempt from ERISA if the program is mandatory (see Mandatory Auto-IRAs).	- The program must be specifically established pursuant to state law.[5] - The state may delegate implementation and administrative authority (rulemaking, contracting with third-party vendors, and investing, etc.) to a board, committee, or other similar governmental agency or instrumentality of the state.[6] - The state must adopt measures to ensure that employees are notified of their rights under the program and create mechanisms for enforcing those rights.[7] - States are not made guarantors or held strictly liable for employers' failures to transmit payroll deductions safely, appropriately, and in a timely fashion. - States are permitted to adopt timing and enforcement provisions specific to their respective programs.

[3] 80 Fed. Reg. 71,938 (November 18, 2015)
[4] 80 Fed. Reg. 71,937 (November 18, 2015)
[5] 29 CFR 2510.3-2(h)(1)(i)
[6] 29 CFR 2510.3-2(h)(1)(ii)
[7] 29 CFR 2510.3-2(h)(1)(iv)

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Employer Participation/ Availability to Other Employers	Voluntary. Employers meeting the specified eligibility criteria would be permitted to join the plan.[8]	Voluntary. Employers meeting the specified eligibility criteria would be permitted to adopt the plan.	Voluntary. Employers would be free to use the marketplace and are not required to establish any savings plans for their employees.[9]	Voluntary	Voluntary	Mandatory. Any employer not mandated by law to participate that voluntarily chooses to automatically enroll its employees in a state payroll deduction savings program has likely established an employee benefit plan under ERISA and would not be eligible for the ERISA safe harbor unless employees can only voluntarily contribute (no auto enrollment).[10]

[8] 80 Fed. Reg. 71,938 (November 18, 2015)
[9] 80 Fed. Reg. 71,937 (November 18, 2015)
[10] 80 Fed. Reg. 59,470 (August 30, 2016)

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Employer Role	Employers would be required to execute a participation agreement. Each employer that chose to participate would not be considered to have established its own "single employer" ERISA plan. Participating employers would not act as a plan administrator or named fiduciary. Although employers would have a duty to prudently select the arrangement and to monitor its operation, it would generally be limited to enrolling employees in the state plan and forwarding voluntary employee and employer contributions to the plan. Only a single Form 5500 Annual Return/Report would be filed. A MEP may allow participating employers to specify employer and employee contributions and maintain unique plan benefit formulas.[11]	Each employer that adopts the prototype sponsors an ERISA plan for its employees and would assume the same fiduciary obligations associated with sponsorship of any ERISA-covered plan, but the plan documents for a state-administered prototype plan would designate the state or a state designee to perform many of the functions of a plan's named fiduciary and plan administrator responsible for complying with ERISA. Employers would be able to choose certain features of the plan such as contribution rates.[12]	The employer would establish the savings arrangement, whether it is an ERISA-covered employee benefit plan or a non-ERISA savings arrangement.[13]	Employers would share myRA information with employees, and set up payroll deduction for employees or inform them of other ways that they can fund their accounts. There is no cost to opening an account and employers would not administer, contribute to, or match employee contributions.[14]	Employers would not endorse the program and would act only as a facilitator of information between the IRA provider and their employees.	The employer's role must be limited to ministerial activities (collecting payroll deductions and remitting them to the program). Such duties include maintaining records of the payroll deductions and remittance of payments, providing information to the state necessary for the operation of the program and distributing program information from the state program to employees.[15]

[11] 80 Fed. Reg. 71,938 (November 18, 2015)
[12] 80 Fed. Reg. 71,938 (November 18, 2015)
[13] 80 Fed. Reg. 71,937 (November 18, 2015)
[14] https://myra.gov/employers/
[15] 29 CFR 2510.3-2(h)(1)(vii)

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Employer Contribution	Permitted	Permitted	Permitted	Not permitted	Not permitted	Not permitted[16]
Structure of Accounts	401(k), defined benefit plan or other tax qualified retirement savings program.	401(k) or other tax-favored retirement plans such as a SIMPLE IRA plan.	ERISA and non-ERISA covered plans, such as SIMPLE IRAs, payroll deduction IRAs, Roth IRAs, 401(k)s, etc.	Roth IRA	Payroll deduction IRAs (options include traditional and Roth IRAs)	Payroll deduction IRAs (options include traditional and Roth IRAs)

[16] 29 CFR 2510.3-2(h)(1)(viii)

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Contribution Limits[17]	401(k): $18,000 ($24,000 for individuals age 50 and over). Annual additions paid to an individual's account cannot exceed $54,000 (or $60,000 including catch-up contributions) or 100 percent of an individual's compensation, whichever is less.[18] Required minimum distribution begins generally on April 1 following the later of the calendar year in which the account holder either reaches age 70.5 or retires.	SIMPLE IRA: No more than $12,500 a year ($15,500 for individuals age 50 and older)[19] Required minimum distribution for a SIMPLE IRA begins on April 1 of the year following the calendar year in which the account holder reaches age 70.5.[20]	Dependent on product – as noted for 401(k)s, SIMPLE IRAs, payroll deduction IRAs, etc.	Once account reaches $15,000 or has been held for 30 years, it must roll over into a private-sector Roth IRA. Contribution rules for Roth IRAs apply: Cannot be more than $5,500 per year ($6,500 for individuals age 50 and older) or the taxable compensation for the year.[21]	Traditional and Roth IRAs: Cannot be more than $5,500 per year ($6,500 for individuals age 50 and older) or the taxable compensation for the year.[22] Traditional IRA: Contributions may be fully or partly deductible and generally amounts in the account (including earnings and gains) are not taxed until distributed.[23] Required minimum distribution begins on April 1 of the year following the calendar year in which the account holder reaches age 70.5.[24] Roth IRA: Contributions are not deductible and qualified distributions are tax-free. Contributions are permitted after the age of 70.5. and minimum distributions do not apply to employee.[25]	Traditional and Roth IRAs: Cannot be more than $5,500 per year ($6,500 for individuals age 50 and older) or the taxable compensation for the year.[26] Traditional IRA: Contributions may be fully or partly deductible and generally amounts in the account (including earnings and gains) are not taxed until distributed.[27] Required minimum distribution begins on April 1 of the year following the calendar year in which the account holder reaches age 70.5.[28] Roth IRA: Contributions are not deductible and qualified distributions are tax-free. Contributions are permitted after the age of 70.5. and minimum distributions do not apply to employee.[29]

[17] Figures are for tax year 2017.
[18] https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-401k-and-profit-sharing-plan-contribution-limits
[19] https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-simple-ira-contribution-limits
[20] https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-required-minimum-distributions-rmds
[21] https://myra.gov/how-it-works/
[22] https://www.irs.gov/retirement-plans/cola-increases-for-dollar-limitations-on-benefits-and-contributions
[23] https://www.irs.gov/retirement-plans/traditional-iras
[24] https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-required-minimum-distributions-rmds
[25] https://www.irs.gov/retirement-plans/roth-iras
[26] https://www.irs.gov/retirement-plans/cola-increases-for-dollar-limitations-on-benefits-and-contributions
[27] https://www.irs.gov/retirement-plans/traditional-iras
[28] https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-required-minimum-distributions-rmds
[29] https://www.irs.gov/retirement-plans/roth-iras

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Income Limits for Contribution[30]	401(k): None. However, there is a compensation limit which determines how much of an individual's compensation can be accounted for when determining contribution limits. This figure is $270,000 for 2017.[31]	See MEPs for 401(k)s. SIMPLE IRAs have an income limit of $270,000.[32]	Dependent on product	Rules for Roth IRA would apply: Contributions are not allowed for adjusted gross income greater than $196,000 a year for those who are married and filing jointly and $133,000 a year for those filing as single.[33]	Roth IRA: Contributions are not allowed for adjusted gross income greater than $196,000 a year for those who are married and filing jointly and $133,000 a year for those filing as single.[34] Traditional IRA: There is no income limit. However, if individual also is eligible to participate in a 401(k) or other employer plan, tax deductions received on contributions are phased based on income. Participants receive no deductions if earning $119,000 or more for those filing jointly and $72,000 or more for those filing as single.[35]	Roth IRA: Contributions are not allowed for adjusted gross income greater than $196,000 a year for those who are married and filing jointly and $133,000 a year for those filing as single.[36] Traditional IRA: There is no income limit. However, if individual also is eligible to participate in a 401(k) or other employer plan, tax deductions received on contributions are phased based on income. Participants receive no deductions if earning $119,000 or more for those filing jointly and $72,000 or more for those filing as single.[37]

[30] Figures are for tax year 2017.
[31] https://www.irs.gov/retirement-plans/401k-plans-deferrals-and-matching-when-compensation-exceeds-the-annual-limit
[32] https://www.irs.gov/retirement-plans/retirement-plans-faqs-regarding-seps-contributions
[33] https://www.irs.gov/uac/newsroom/irs-announces-2017-pension-plan-limitations-401k-contribution-limit-remains-unchanged-at-18000-for-2017
[34] Ibid.
[35] Ibid.
[36] Ibid.
[37] Ibid.

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Automatic Enrollment	Permitted. The Pension Protection Act of 2006 made it clear that automatic enrollment is not prohibited by state wage withholding laws. It also incentivized employers to use automatic enrollment by creating a safe harbor from (i) fiduciary responsibility for the selection of certain default investments (*e.g.*, target date funds) and (ii) tax non-discrimination testing, provided the employer automatically enrolls employees at a certain rate (starting at 3% and escalating to at least 6%) and makes certain matching or non-matching contributions. Employers are not required to comply with the safe harbors.	Permitted. The Pension Protection Act of 2006 made it clear that automatic enrollment is not prohibited by state wage withholding laws. It also incentivized employers to use automatic enrollment by creating a safe harbor from (i) fiduciary responsibility for the selection of certain default investments (*e.g.*, target date funds) and (ii) tax non-discrimination testing, provided the employer automatically enrolls employees at a certain rate (starting at 3% and escalating to at least 6%) and makes certain matching or non-matching contributions. Employers are not required to comply with the safe harbors.	Permitted as noted for 401(k) plans pursuant to the Pension Protection Act of 2006 (as described for MEPs and Prototype Plan). However, if an employer chooses to use an IRA plan, it could not use auto-enrollment without being considered an employee benefit plan subject to ERISA.	Not permitted	Not permitted	Permitted[38]

[38] 29 CFR 2510.3-2(h)(2)(iii)

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Employee Opt-out	Permitted under a plan which allows for automatic enrollment. Employees must be given adequate advance notice and have the right to opt out.	Permitted under a plan which allows for automatic enrollment. Employees must be given adequate advance notice and have the right to opt out.	Permitted under a plan which allows for automatic enrollment. Employees must be given adequate advance notice and have the right to opt out.	Not applicable	Not applicable	Permitted. Employees must be given adequate advance notice and have the right to opt out.[39]
Tax & Other Incentives	Tax credits are permissible to allow small employers to offset part of the costs of starting certain types of retirement plans.[40]	Tax credits are permissible to allow small employers to offset part of the costs of starting certain types of retirement plans.[41]	Tax credits are permissible to allow small employers to offset part of the costs of starting certain types of retirement plans.[42]	Availability of federal Retirement Savings Contribution Credit (Saver's Credit).	Availability of federal Retirement Savings Contribution Credit (Saver's Credit).	States may use tax incentives or credits, as long as they ensure that economic incentives are narrowly tailored to reimbursing employers for their costs under the payroll deduction savings programs. States may not provide rewards for employers that incentivizes participation in state programs instead of establishing employee pension benefit plans.[43] Allowable incentives may include disseminating information about the federal Retirement Savings Contributions Credit (Saver's Credit).[44]

[39] Ibid.
[40] 80 Fed. Reg. 71,937 (November 18, 2015)
[41] Ibid.
[42] Ibid.
[43] 80 Fed. Reg. 59,467 (August 30, 2016)
[44] The Saver's Credit is available for individuals making eligible contributions to an IRA or employer-sponsored retirement plan. It is available to those aged 18 or older, not a full-time student and not claimed as a dependent on another person's return who earn less than $31,000 a year as a single or $62,000 as married filing jointly. Although the Saver's Credit is non-refundable (and so does not provide a refund), it can be combined with another refundable tax credit, such as the Earned Income Tax Credit, to allow a filer to receive a refund.

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Investment Options	Determination is left to the state, or a designated governmental agency of instrumentality, either directly or through one or more contract agents.[45]	The state could designate low-cost investment options and a third-party administrative service provider for its prototype plans.[46]	Dependent on product	Invests solely in a Treasury retirement savings bond.[47]	Responsibility left to IRA providers.	Determination is left to the state[48] or a designated governmental agency of instrumentality, either directly or through one or more contract agents.

[45] 80 Fed. Reg. 71,938 (November 18, 2015)
[46] Ibid.
[47] https://myra.gov/how-it-works/
[48] 80 Fed. Reg. 59,467 (August 30, 2016)

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Withdrawal Options	401(k): Hardship withdrawals are allowed, including for: • Medical expenses for an individual, spouse, or dependents • Purchasing principal residence • Postsecondary education expenses for an individual, spouse, or dependents • Payments to prevent eviction or foreclosure on residence • Funeral expenses • Certain expenses relating to repair to principal residence Generally, withdrawals made before age 59.5 are taxed at 10 percent, unless they fall under exceptions.[49] Plan also may allow hardship withdrawals of employer contributions.	Early withdrawals from IRAs (including SIMPLE-IRA) are permissible at any time without a need to show hardship. Early withdrawals will be included in taxable income and may be subject to a 10 percent additional tax for those under the age of 59.5. Exceptions to the 10 percent tax are made for disability, higher education expenses, first time homebuyers, and medical expenses. There is an additional tax of 25 percent if withdrawals are made from a SIMPLE IRA plan within the first two years of participation.[50] 401(k) prototypes are covered by the same rules discussed under MEPs.	Dependent on product	Roth IRA: No penalties or taxes for a qualified distribution (payment or distribution made 5 years after the first contribution and after age 59.5 or made due to disability, made to a beneficiary after death, or to meet the requirement of a first home purchase). All withdrawals of contributions are tax free. An individual under age 59.5 may have to pay an additional 10 percent tax on withdrawal of accumulated investment income unless the withdrawal qualifies for exceptions.[51]	Traditional IRA: Any deductible contributions and earnings that are withdrawn or distributed are taxable. An individual under age 59.5 may have to pay an additional 10 percent tax unless the withdrawal qualifies for exceptions.[52] Roth IRA: No penalties or taxes for a qualified distribution (payment or distribution made 5 years after the first contribution and after age 59.5 or due to disability, made to a beneficiary after death, or to meet the requirement of a first home purchase).[53] All withdrawals of contributions are tax free. An individual before age 59.5 may have to pay an additional 10 percent tax on withdrawal of accumulated investment income unless the withdrawal qualifies for exceptions. [54]	States have the control to establish restrictions on withdrawals from IRAs to limit leakage.[55] Traditional IRA: Any deductible contributions and earnings that are withdrawn or distributed are taxable. An individual under age 59.5 may have to pay an additional 10 percent tax unless the withdrawal qualifies for exceptions. [56] Roth IRA: No penalties or taxes for a qualified distribution (payment or distribution made 5 years after the first contribution and after age 59.5 or due to disability, made to a beneficiary after death, or to meet the requirement of a first home purchase). All withdrawals of contributions are tax free. An individual before age 59.5 may have to pay an additional 10 percent tax on withdrawal of accumulated income unless the withdrawal qualifies for exceptions. [57]

[49] https://www.irs.gov/retirement-plans/plan-participant-employee/401k-resource-guide-plan-participants-general-distribution-rules
[50] https://www.irs.gov/retirement-plans/retirement-plans-faqs-regarding-iras-distributions-withdrawals
[51] https://www.irs.gov/publications/p590b/ch02.html#en_US_2015_publink1000231061
[52] Ibid.
[53] Ibid.
[54] https://www.irs.gov/retirement-plans/traditional-and-roth-iras
[55] 80 Fed. Reg. 59,467 (August 30, 2016)
[56] https://www.irs.gov/publications/p590b/ch02.html#en_US_2015_publink1000231061
[57] https://www.irs.gov/retirement-plans/traditional-and-roth-iras

	Voluntary					Mandatory
	Multiple Employer Plan ("MEP")/ 401(k)	**Master and Prototype ("Prototype")**	**Marketplace**	**myRA**	**Payroll Deduction IRAs**	**Auto-IRAs**
Disclosures and Consumer Protection	ERISA's reporting and disclosure requirements, protective standards and remedies would apply.	ERISA's reporting and disclosure requirements, protective standards and remedies would apply.[58]	ERISA's reporting and disclosure requirements, protective standards and remedies would apply to the ERISA plans used by employers through the marketplace.[59]	The program is underwritten by the federal government. Assets are invested in government bonds, so there is no risk of principal loss.[60] See previous information regarding Employer Role for myRAs.	Does not have the fiduciary consumer protection of ERISA. However, IRS prohibited transaction rules that address conduct between plans and related parties still apply. States can establish their own regulatory framework for effective disclosures, oversight and risk management.[61]	Does not have the fiduciary consumer protection of ERISA. However, IRS prohibited transaction rules that address conduct between plans and related parties still apply. States can establish their own regulatory framework for effective disclosures, oversight and risk management.[62]

58 80 Fed. Reg. 71,938 (November 18, 2015)
59 80 Fed. Reg. 71,937 (November 18, 2015)
60 https://myra.gov/how-it-works/
61 80 Fed. Reg. 59,469 (August 30, 2016)
62 Ibid.

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APPENDIX B

GEORGETOWN UNIVERSITY
McCourt School of Public Policy
Center for Retirement Initiatives

Comparison of Retirement Plan Design Features[1], By State:
Illinois, Oregon, Maryland, Connecticut and California

State Brief 16-01

November 30, 2016
UPDATE

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[1] On August 30, 2016, the U.S. Department of Labor (DOL) published a final rule related to Savings Arrangements Established by States for Non-Governmental Employees proposing a new safe harbor for state IRA retirement savings arrangements that would allow for qualifying state programs to be exempt from ERISA. The state plans in this document are assumed to be covered under the new rule.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Bill Sponsor	Sen. Daniel Biss	Rep. Tobias Read, Rep. Jennifer Williamson and Sen. Lee Beyer	Del. William Frick and Sen. Douglas Peters	Rep. Joe Aresimowicz and Sen. Martin Looney	Sen. Kevin de León
Bill Number	SB 2758: Public Act 098-1150 (2015); Refer to 820 Illinois Compiled Statute 80 for subsequent amendments	HB 2960: Chapter 557 (2015)	HB 1378: Chapter 324 (2016) SB 1007: Chapter 323 (2016)	HB 5591: Public Act 16-29 (2016)	SB 1234: Chapter 804 (2016)
Bill Status	Enacted January 5, 2015, as amended by SB 2420 in 2016	Enacted June 25, 2015	Enacted May 10, 2016	Enacted May 27, 2016, as amended by Public Act 16-3	Enacted September 29, 2016
Implement if ERISA Applies[2]	No. The Board shall not implement the program if it is determined that the program is an employee benefit plan under the federal Employee Retirement Income Security Act (ERISA).	No. The Board shall not establish the plan if it determines that the plan would qualify as an employee benefit plan under ERISA and/or applies to employers.	No. The Board shall take any action necessary to ensure that the program is not preempted by federal law.	No. The Authority will ensure that the Program meets all criteria for federal tax-deferral or tax-exempt benefits, and to prevent the program from being treated as an employee benefit plan under ERISA.	No. The Board shall not implement the program if it is determined that the program is an employee benefit plan under ERISA.

[2] As previously noted, on August 30, 2016, the U.S. Department of Labor (DOL) published a final rule related to Savings Arrangements Established by States for Non-Governmental Employees proposing a new safe harbor for state IRA retirement savings arrangements that would allow for qualifying state programs to be exempt from ERISA. The state plans in this document are assumed to be covered under the new rule. Should there be a future determination that such savings arrangements are subject to ERISA, state laws have provisions about ERISA applicability.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Market, Feasibility and/or Legal Analysis Required	Not required by law; however, the Board is conducting a market analysis as a part of its pre-implementation planning.	Yes. The Board shall conduct market analysis to determine the feasibility of the plan and to what extent similar plans exist in the market; to obtain legal advice regarding the applicability of ERISA to plan design; and to study aspects of employer and employee participation in the plan.	Not required by law; however, the Board may conduct market and financial feasibility studies before the program becomes operational.	Yes. The Board shall conduct a study of the interest of participants and potential participants of the program in investing in a traditional IRA option. The study will include, but is not limited to: the number of participants whose incomes exceed federal limits for contributing to a Roth IRA, and the percentage of current participants that would prefer a tax-deferred savings option. The Board will submit a report not later than January 1, 2019 to the joint standing committee of the General Assembly. The Authority also may study the feasibility of making available through the state or the Authority a multiple-employer 401(k) plan or other tax-favored savings vehicle.	As required by the 2012 law Chapter 734, the market analysis was completed and submitted to the California Legislature on March 28, 2016.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Administrative Entity	The Illinois Secure Choice Savings Board. Board with seven (7) members: Treasurer (serving as chair); State Comptroller; Director of the Governor's Office of Management and Budget; two public representatives with expertise in retirement savings plan administration or investment appointed by Governor; a representative of participating employers appointed by Governor; and a representative of enrollees appointed by Governor. The Board is appointed and meets regularly.	The Oregon Retirement Savings Board with seven (7) members: Treasurer (serving as chair); and the Governor shall appoint: a representative of employers; a representative with experience in the field of investments; a representative of an association representing employees; and a public member who is retired. A member of the Senate is appointed by the President of the Senate; and a member of the House of Representatives is appointed by the Speaker of the House. The Board is appointed and meets regularly.	The Maryland Small Business Retirement Savings Board with eleven (11) members who will elect a chair from among the members: The State Treasurer, or the Treasurer's Designee; the Secretary of Labor, Licensing and Regulation, or the Secretary's Designee; nine members with expertise in retirement programs - three appointed by the Governor, three appointed by the President of the Senate, and three appointed by the Speaker of the House of Delegates. The Board is appointed and held its first meeting on November 17, 2016.	The Connecticut Retirement Security Authority Board with fifteen (15) members and the chair to be selected by the Governor from among the members: Treasurer; Comptroller; Secretary of the Office of Policy and Management; Banking Commissioner; and Labor Commissioner all serving as ex officio voting members; one appointed by the Speaker of the House of Representatives; one appointed by the Majority leader of the House of Representatives; one appointed by the Minority leader of the House of Representatives; one appointed by the president pro tempore of the Senate; one appointed by the Majority leader of the Senate; one appointed by the Minority leader of the Senate; and four appointed by the Governor. All appointments shall be made not later than January 1, 2017.	The California Secure Choice Retirement Savings Investment Board with nine (9) members: Treasurer (serving as chair); Director of Finance; the Controller; an individual with retirement savings and investment expertise appointed by Senate Committee on Rules; an employee representative appointed by Speaker of the Assembly; a small business representative appointed by the Governor; a public member appointed by the Governor; two additional members appointed by the Governor. The Board, subject to its authority and fiduciary duty, shall design and implement the Program. The Board is appointed and meets regularly.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Employer Participation	Mandatory for certain employers, with 2-year delay for new businesses. Employers retain the option of providing a qualified plan available on the open market.	Mandatory. Employers must establish alternative qualified retirement plans for some or all of their employees if they choose not to facilitate.	Mandatory for all employers that pay employees through a payroll system or service. There is a 2-year deferral for new businesses. Employers retain the option of providing a plan available on the open market.	Mandatory. Employers retain the option of providing a plan available on the open market.	Mandatory. Employers retain the option at all times to set up a tax-qualified retirement plan instead of the state arrangement.
Employers Affected	Employers with 25 or more employees that have not offered a qualifying retirement plan in the preceding 2 years.	Employers that do not currently offer qualified plans.	All qualifying employers that do not currently offer plans.	Qualified employers with 5 or more employees that do not currently offer a plan.	Employers with 5 or more employees that do not already provide a qualified employer-sponsored retirement plan and satisfy the requirements to establish or participate in a payroll deposit retirement savings arrangement. Also, an employer of a provider of in-home supportive services, if determined to be eligible.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Penalties for Employer Non-Compliance	Yes. $250 per eligible employee to start.	Not Specified	Yes. If a covered employer is not in compliance, the covered employer may not receive a waiver of the State's $300 business filing fee. Applies only after program is open for enrollment.	Yes. The employee, or the Labor Commissioner, may bring a civil action to require the employer to enroll the covered employee and shall recover attorneys' fees.	Each eligible employer that, without good cause, fails to allow its eligible employees to participate in the program shall pay a penalty of $250 per eligible employee on or before 90 days after service of notice by the Director of the Employment Development Department. If found to be noncompliant 180 days or more after the notice, an additional penalty of $500 per eligible employee shall be paid by the employer.
Structure of Accounts	Roth IRA	Roth IRA – per proposed rule, with a Traditional IRA potentially offered in the future as an electable participant choice.	One or more payroll deposit IRA arrangements to be determined by the Board.	Roth IRA	One or more payroll deduction IRA arrangements to be determined by the Board.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Automatic Enrollment[3]	Yes	Yes	Yes	Yes	The Board will design and disseminate to employers an employee information packet which includes information on the program and appropriate disclosures including the mechanics of how to make contributions to the program. Employees must acknowledge that they have read all of the disclosures and understand their content.
Employee Opt-Out	Yes	Yes	Yes	Yes	Yes
Employee Re-Enrollment after Opt-Out	Yes, but only during designated open re-enrollment period which will be held at least once every year.	Not Specified	Yes, in accordance with procedures established by the Board.	Not Specified	Yes, but only during the designated open re-enrollment period which will be held at least once every two years.

[3]The DOL final rule allows the use of auto-enrollment only by those employers mandated to participate in a state-sponsored savings arrangement. For those employers below the employee threshold, the final rule would not allow employers to use auto-enrollment. For states such as Illinois, Oregon and Connecticut, utilization of automatic enrollment by small employers and individuals may be allowed if it does not create liability under ERISA. See section "Availability to Other Employers."

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Default Contribution Rate	3%	The Board has the administrative discretion to set the minimum, maximum and default contribution levels. By proposed rule, set at 5% standard, 1% minimum, and no maximum except for IRS limits.	The Board has the administrative discretion to set default, minimum and maximum employee contribution levels.	3%	3% (with Board discretion to adjust in the range of 2% to 5%). The Board may implement auto-escalation and, if so, auto-escalation cannot increase more than 1% per year and is capped at 8% of salary. An employee may opt out of auto-escalation and may set his or her own contribution rate.
Employer Contribution	Not permitted	Not permitted	Not specified	Not permitted	Permitted only if would not trigger ERISA.
Availability to Other Employers[4]	Yes. Employers with fewer than 25 employees may be allowed to participate. The Board will establish a process by which an individual may voluntarily enroll in and make contributions to the program.	To facilitate, employers must be covered by the state's mandate.	Yes, the Board may evaluate and establish the process by which an employee of a non-participating employer may participate.	Yes. A private employer with 4 employees or fewer may make the program available to its employees. No employer shall require any employee to enroll in the program.	Yes. Employees of non-participating employers and the self-employed may be allowed to contribute, with method and timing to be determined by the Board.

[4] See Footnote 3

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Tax & Other Incentives	Not specified and not currently planned.	Board can examine ways to reduce costs through incentives, tax credits or other means.	The state will waive the annual business filing fee of $300 per year for those qualifying employers who participate in the state program or otherwise provides auto-enroll IRA or annuity or an employer offered savings arrangement that is in compliance with federal law.	The Board shall disseminate information concerning the tax credits that may be available to small business owners for establishing new retirement plans.	Yes. Disseminate information about tax credits available to small businesses for allowing their employees to participate in the program and the use of federal Retirement Savings Contributions Credit (Saver's Credit) available to low- and moderate-income households to encourage retirement savings.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Investment of Assets	The Board shall establish investment options for enrollees to include: default life-cycle target date fund and any or all of the following: a conservative principal protection fund; a growth fund; a secure return fund; and an annuity fund. The Board has created a set of [Investment Principles]() to guide future investment decisions.	By rule, investment of contributions in target date funds as a standard. Capital preservation likely to be offered as a participant election.	The Board shall evaluate and establish a range of investment options including a default investment selection for employees' payroll deposit IRAs. The Board may not offer options that could result in liability to the state or its taxpayers. When selecting investment options, the Board will consider methods to minimize the risk of significant investment losses at the time of a participating employee's retirement. The Board will consider investment options that minimize administrative expenses, and may provide an investment option that provides an assured lifetime income.	The Authority shall provide for each participant's account to be invested in an age-appropriate target date fund with the vendor selected by the participant (or the program default option applies) or other investment vehicles as deemed feasible and cost effective by the Authority. The program will offer qualified retirement investment choices offered by multiple vendors. The assets must be held in trust or custodial accounts meeting the federal requirements for IRAs. Once the participant reaches normal retirement age, 50% of the participant's account will be invested in the lifetime income investment. Participants may elect to invest a higher percentage of account balances in the lifetime income investment. The Authority will designate a lifetime income investment option intended to provide participants with a source of retirement income for life.	For up to three years following initial implementation, the Board shall establish managed accounts invested in U.S. Treasuries, myRAs, or similar investments. During this period, the Board will develop and implement an investment policy that defines the program's investment objectives. Investment options may encompass a range of risk and return opportunities and allow for a rate of return commensurate with an appropriate level of risk to meet the investment objectives. Investment option recommendations may include, but are not limited to, the creation of a reserve fund or establishment of customized investment products, and may also address risk-sharing and smoothing of market losses and gains. After the initial three-year period described above, the Board will annually prepare and adopt a written statement of investment policy that includes a risk management and oversight program.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Investment Management and Liability	The Program Fund is established with the Board as its Trustee and moneys in the fund from enrollees and participating employers will be held as pooled investments to achieve cost savings through efficiencies and economies of scale. The Board will engage outside investment firms, as needed, and select investment options that do not incur debt or liabilities to the state. The Fund will maintain individual accounts for enrollees. The Fund is the not the property of the State and cannot be commingled with State funds. The Board also must establish effective risk management and oversight programs.	Pooled accounts established under the plan for investment; accounts will be professionally managed. Plan must maintain separate records and accounting for each plan account. May not guarantee any rate of return or interest rate on any contribution. The plan, the Board, each Board member and the State of Oregon may not be liable for any loss incurred by any person as a result of participating in the plan.	The Trust is established with contributions paid by employees and the Board shall delegate administration of the Trust to a third party. Assets of the Trust must remain in the Trust and cannot be transferred out. The Board may arrange for collective, common, and pooled investment of assets of the program, with a goal of saving costs through efficiencies and economies of scale. The Board will also explore and establish investment options that offer employees returns on contributions and the conversion of individual retirement savings account balances to secure retirement income without incurring debt or liabilities to the state. The Board must adopt an investment policy that includes a risk management and oversight program. The Program Fund may be privately insured and is not guaranteed by the state.	The Authority may contract with financial institutions or other organizations offering or servicing retirement programs. The State will not be liable for the payment of any benefit to any participant or beneficiary of any participant and shall not be liable for any liability or obligation of the Authority. Any employer who provides automatic enrollment shall be relieved of liability for investment decisions made by the employer or the Authority as long as employees are given open notice and ability to select investments as required by law. Liability relief also extends to any plan official who makes investment decisions on behalf of participating employees.	The moneys in the Program Fund may be invested by the Treasurer or may be invested in whole or in part under contract with the board of a California public retirement system, with private money managers, or in myRAs, or a combination as determined by the Board. The Board will use one or more investment management entities. The Trust's Program Fund is to be invested as determined by the Board as its Trustee which will arrange for the collective, common and pooled investment of assets. There must be a mechanism in place to hold the state harmless against any liability. The state shall not have any liability for the payment of retirement savings benefits earned by program participants. The Board must establish effective risk management and oversight programs.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Fees	Total expenses cannot exceed .75% of the total trust balance.	Must keep administrative fees low.	Administrative expenses may not exceed 0.5% of assets under management in the program.	Not specified, but the Authority shall minimize total annual fees, and after the completion of the fourth calendar year following the date that the program becomes effective, the total annual fees associated with the program shall not exceed three-quarters of one percent (.75%) of the total value of the program assets. Fees are defined as investment management charges, administrative charges, investment advice charges, trading fees, marketing and sales fees, revenue sharing, broker fees and other costs necessary to administer the program.	On or after six years from the date the program is implemented, on an annual basis, expenditures from the Administrative Fund shall not exceed more than 1% of the total Program Fund.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Program Funding	The Illinois Secure Choice Administrative Fund is created as a non-appropriated separate and apart trust fund in the State Treasury. The Administrative Fund is to be used by the Board to pay for administrative expenses it incurs. The Administrative Fund may receive any grants or other moneys designated for administrative purposes from the State, or any unit of federal or local government, or any other person, firm, partnership, or corporation. The Illinois General Assembly appropriated $2.1 million for fiscal year 2017 to assist with start-up costs. These funds will need to be paid back when the program becomes operational.	The Oregon Retirement Administrative Savings Plan Fund must be self-sustaining and is established from funds to be continuously appropriated to the Board. It is separate and distinct from the General Fund. The Plan Fund consists of moneys appropriated by the Legislative Assembly; moneys transferred from the federal government, other state agencies or local governments; moneys from payment of fees; any gifts or donations; and earnings on moneys in the fund. The Legislature appropriated $250,000, which may be used only for reimbursing other state agencies for providing outreach or technical assistance services; and $743,541, which may be used only for the operating expenses of the Board. The appropriation is a General Fund loan.	The Maryland Small Business Retirement Board, consistent with its fiduciary duties, may enter into an agreement to borrow funds from the state or any other entity to provide funding for the operation of the program until the program can generate sufficient funding for operations through fees assessed on program accounts. All expenses incurred to implement, maintain, and administer the Program and Trust will be paid from money collected by the Program or Trust.	The Connecticut Retirement Security Authority may borrow working capital funds and other funds as may be necessary for the start-up and continuing operation of the program, as long as such funds are borrowed in the name of the Authority only. Such borrowings shall be payable solely from revenues of the Authority.	The California Secure Choice Retirement Savings Trust is established as a self-sustaining trust. The Board shall segregate moneys received into two funds – the Program Fund and the Administrative Fund. Moneys from the Program Fund are transferred to the Administrative Fund to cover the operating costs of the program. The State can accept any grants, gifts, legislative appropriation, and other moneys from the state, any unit of the federal, state or local government or any other person, firm, partnership or corporation for deposit to the Program or Administrative Fund. The Budget Act of 2016 appropriates up to $1.9 million from the General Fund as a loan to support the administrative costs of the program. The loan shall be repaid by June 30, 2022, with interest calculated at the rate earned by the Pooled Money Investment Account at the time of the transfer.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Program Administration	The Board shall make and enter into contracts necessary for the administration of the program and Fund, including, but not limited to, retaining and contracting with investment managers, private financial institutions, other financial and service providers, third-party administrators, and other professionals as necessary. The Board shall determine the number and duties of staff members needed to administer the program including assembling and employing staff as needed, appointing a program administrator, and entering into contracts with the Treasurer to make employees of the Treasurer's office available to administer the program.	The Board shall make and enter into contracts, agreements or arrangements, and to retain, employ and contract for following: services including those of private and public financial institutions, depositories, consultants, investment advisers, investment administrators and third-party plans; research, technical and other services; services to other state agencies to assist the Board; to evaluate the need for and procure pooled private insurance of the plan.	The Board may hire consultants, administrators, and other professionals as necessary to help implement, maintain, and administer the Program and the Trust. The Board shall appoint a program administrator and determine the duties of the program administrator; employ staff as necessary and set the compensation of the staff; procure insurance against any loss of the Trust; and adopt regulations to ensure that the program meets all criteria for federal tax-deferral or tax-exempt benefits, or both.	The Board may contract with financial institutions or other organizations offering or servicing retirement programs; make and enter into contracts or agreements with professional service providers, including, but not limited to, financial consultants and lawyers, as may be necessary. The Board may appoint an executive director and assistant executive director, who shall not be members of the Board and who shall serve at the pleasure of the Board. The Board shall adopt written procedures for making modifications to the program to be consistent with federal rules and regulations in order to ensure that the program meets all criteria for federal tax-deferral or tax-exempt benefits.	The Treasurer shall, on behalf of the Board, appoint an executive director, who shall not be a member of the Board and who shall serve at the pleasure of the Board. The Treasurer shall determine the duties of the executive director and other staff as appropriate and set his or her compensation. The Board may authorize the executive director to enter into contracts on behalf of the Board or conduct any business necessary for the efficient operation of the Board. The Board has the authority to employ staff and make and enter into contracts necessary for the administration of the Trust; to contract with and determine the duties of the program administrator; to collaborate with, and evaluate the role of, licensed insurance agents and financial advisors in assisting and providing guidance for eligible

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Program Administration (continued)	The Board shall evaluate the need for, and procure as needed, insurance against any and all loss in connection with the program; facilitate compliance by the program with all applicable requirements for the program under the Internal Revenue Code, including tax qualification requirements or any other applicable law and accounting requirements.				employees; to procure insurance against any loss of the Trust; to set minimum and maximum investment levels in accordance with contribution limits set for IRAs by the Internal Revenue Code; to facilitate compliance by the arrangements under the program with all applicable requirements for the program under the Internal Revenue Code of 1986; and to adopt regulations to ensure that the program meets all criteria for federal tax-deferral or tax-exempt benefits, or both.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Marketing & Outreach	The Board shall facilitate education and outreach to employers and employees.	The Board shall have the power to develop and implement an outreach plan to gain input and disseminate information regarding the plan and retirement savings in general. The Board may collaborate with state agencies as necessary to provide outreach services for the plan.	Not specified.	The Board shall distribute information as the Board may deem necessary or advisable to provide to participants, potential participants and qualified employers in the state.	The Board shall collaborate and cooperate with the board of a California public retirement system, private financial institutions, service providers, and business, financial, trade, membership, and other organizations to the extent necessary or desirable for effective and efficient design, implementation, and administration of the program and to maximize outreach to eligible employers and eligible employees. The Board shall also include comprehensive worker education and outreach in the program, and may collaborate with state and local government agencies, community-based and nonprofit organizations, foundations, vendors, and other entities deemed appropriate to develop and secure ongoing resources for education and outreach that reflect the cultures

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Marketing & Outreach (continued)					and languages of the state's diverse workforce population. The Board shall include comprehensive employer education and outreach in the program, with an emphasis on employers with fewer than 100 employees, developed in consultation with employer representatives, with the integration of a program Internet Web site to assist the employers of participating employees.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Establish Website	Yes. The Board shall establish and maintain an Internet website designed to assist employers in identifying private sector providers of retirement arrangements that can be set up by the employer rather than allowing employee participation in the program under this Act, if there is sufficient interest in a site by private sector providers and if the private sector provides the funds necessary to build and maintain the site.	Not Specified	Not Specified	Yes. The Authority shall establish and maintain a secure Internet website to provide Exchange participants with information regarding approved vendors that offer individual retirement accounts through the program and the various investment options, including the historical investment performance of such options that may be available for such individual retirement accounts.	Yes. The creation of a Retirement Investments Clearinghouse, but only if there is sufficient interest in a site by private sector providers and if the private sector provides the funds to build and maintain the site. The website would contain information on the vendor registration process, retirement plans, and statements from participating vendors. Vendors must offer an appropriate array of accumulation funding options, including, but not limited to, investment options that offer guaranteed returns and the conversion of retirement savings account balances to secure retirement income, a diversified mix of value, growth, growth and income, hybrid and index funds or accounts across large, medium and small capitalization asset classes.

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Implementation Timeline	Enrollment of participants must be possible within 24 months after the effective date of the Act (by June 1, 2017). Employers then have 9 months after that date to set up their automatic payroll deposits for their employees. If the Board does not have adequate funds to implement the program within the specified timeframe, the Board may delay implementation. The Board intends to use a phased enrollment approach, beginning with a pilot program. It will seek legislative authority to change the rollout date from June 2017 to 2018.	By December 31, 2016, the Board must provide a report to the Legislative Assembly including, but not limited to, the market analysis, ways to increase financial literacy, analysis of cost to employers, and a timeline for program implementation so individuals may begin making contributions no later than July 1, 2017.	The Act will take effect July 1, 2016.	Not later than January 1, 2018, qualified employers need to provide covered employees with the informational materials prepared by the Authority. Not later than 60 days after a qualified employer provides informational materials to a covered employee, such qualified employer shall automatically enroll each of its covered employees in the program. The Authority may defer the effective date of the program, in whole or in part, as deemed necessary.	The California Secure Choice Retirement Savings Program is approved by the Legislature and effective as of January 1, 2017. - Within 12 months after the Board opens the program for enrollment, eligible employers with more than 100 eligible employees shall allow employee participation. - Within 24 months eligible employers with more than 50 eligible employees shall allow employee participation. - Within 36 months all other eligible employers shall allow employee participation. Prior to opening the program for enrollment, the Board shall report to the Governor and Legislature: - The specific date on which the program will start to enroll participants. - The program is structured to meet the criteria of the DOL's safe harbor. - The payroll deduction IRA arrangements offered by

	Illinois Secure Choice Savings Program	Oregon Retirement Savings Plan	Maryland Small Business Retirement Savings Program and Trust	Connecticut Retirement Security Exchange	California Secure Choice Retirement Savings Program
Implementation Timeline (continued)					the program qualify for favorable federal income tax treatment under the Internal Revenue Code. - The Board has adopted a third-party administrator operational model that limits employer interaction and transactions with the employee to the extent feasible.

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APPENDIX C

GEORGETOWN UNIVERSITY
McCourt School of Public Policy
Center for Retirement Initiatives

Comparison of Retirement Plan Design Features[1], By State:
Massachusetts, Washington and New Jersey

State Brief 16-02

November 30, 2016
UPDATE

[1] On November 18, 2015, the U.S. Department of Labor issued a final Interpretive Bulletin Relating to State Savings Programs That Sponsor or Facilitate Plans Covered by the Employee Retirement Income Security Act (ERISA) of 1974. The Bulletin outlines those state-sponsored retirement savings programs that would include ERISA-covered retirement plans. These options include a marketplace, prototype plans, and state-sponsored "open" multiple employer plans (MEPs). The state plans in this document are plans covered by the Interpretive Bulletin.

	Massachusetts Retirement Plan for Non-Profits ("Prototype Plan")	Washington Small Business Retirement Marketplace	New Jersey Small Business Retirement Marketplace
Bill Sponsor	Rep. Garrett Bradley	Sen. Mark Mullet and Sen. Don Benton	Rep. Vincent Prieto
Bill Number	Chapter 60 (2012)	ESSB 5826 (2015)	Chapter 298 (2016)
Bill Status	Enacted March 22, 2012	Enacted May 18, 2015	Enacted January 19, 2016
ERISA Applicability	Yes	ERISA cannot apply to the state for operating the marketplace, but ERISA plans are allowed in the marketplace and normal ERISA requirements would apply to participating employers.	ERISA cannot apply to the state for operating the marketplace, but ERISA plans are allowed in the marketplace and normal ERISA requirements would apply to participating employers.
Market, Feasibility and/or Legal Analysis Required	No	No	No
Administrative Entity	Agency - Office of the State Treasurer. There shall be in the Office of the State Treasurer a not-for-profit defined contribution committee. The committee shall consist of the Treasurer or a designee, who shall serve as chairperson, and additional members appointed by the Treasurer, two of whom shall have practical experience in the non-profit community and two of whom shall be currently employed by not-for profit corporations.	Agency - State Department of Commerce. The Director shall consult with the Washington State Department of Retirement Systems, the Washington State Investment Board, the Office of the Insurance Commissioner and the Department of Financial Institutions in designing and managing the marketplace. Prior to approving a plan to be offered on the marketplace, the Department of Commerce must receive verification from the Department of Financial Institutions and Office of the Insurance Commissioner that the financial services firm offering the plan meets requirements set forth in statute and that the plan meets the requirements set forth in statute.	Agency - The State Treasurer, or the Treasurer's designee, shall consult with the Director of Investment of the Department of the Treasury, or the Director's designee; the Commissioner of Banking and Insurance, or the Commissioner's designee; the Commissioner of Labor and Workforce Development, or the Commissioner's designee; the Chairperson of the State Investment Council, or the Chairperson's designee; the Director of the Division of Pensions and Benefits, or the Director's designee; and the Chief Executive Officer (CEO) of the New Jersey Economic Development Authority, or the CEO's designee, in designing and managing the marketplace.

	Massachusetts Retirement Plan for Non-Profits ("Prototype Plan")	Washington Small Business Retirement Marketplace	New Jersey Small Business Retirement Marketplace
Employer Participation	Voluntary	Voluntary	Voluntary
Employers Affected	Non-profits only with 20 or fewer employees	Fewer than 100 employees	Fewer than 100 employees
Penalties for Employer Non-Compliance	Not Applicable	Not Applicable	Not Applicable
Structure of Accounts	Defined contribution 401(k) plan	SIMPLE IRA; myRA (Roth IRA); payroll deduction IRA and ERISA plans can be added. May also offer "life insurance plans designed for retirement purposes."	SIMPLE IRA; myRA (Roth IRA); payroll deduction IRA and others can be added. Shall also offer "life insurance plans designed for retirement purposes."
Automatic Enrollment	Permissible	Business owners may auto enroll as IRS rules allow - no state requirement.	Business owners may auto enroll as IRS rules allow - no state requirement.
Employee Opt-Out	Voluntary employee participation.	Voluntary employee participation.	Voluntary employee participation.
Employee Re-Enrollment after Opt-Out	Not Specified	Not Applicable	Not Applicable
Default Contribution Rate	6% or can choose 4% with auto-escalation up to 10%	Not Specified	Not Specified
Employer Contribution	Permitted	Permitted if an ERISA plan option.	Permitted if an ERISA plan option.

	Massachusetts Retirement Plan for Non-Profits (“Prototype Plan”)	Washington Small Business Retirement Marketplace	New Jersey Small Business Retirement Marketplace
Availability to Other Employers	No	Yes. The self-employed and sole proprietors are eligible to participate in the marketplace.	Yes. The self-employed and sole proprietors are eligible to participate in the marketplace.
Tax & Other Incentives	Not Specified	Yes. The Director shall contract with a private sector entity to identify and promote existing federal or state tax credits and other benefits to encourage retirement savings or participation in retirement plans. Using funds specifically appropriated for this purpose, and funds provided by private foundations or other private sector entities, the Director may provide incentive payments to participating employers that enroll in the marketplace.	Yes. The State Treasurer or designee shall contract with private sector entities to identify and promote existing federal and state tax credits and benefits to encourage retirement savings or participation in retirement plans. The State Treasurer, or designee, shall approve incentive payments to participating employers that enroll in the marketplace if there are sufficient funds provided by private foundations or other private sector entities, or with State funds specifically appropriated for this purpose.
Investment of Assets	13 custom target date funds; 4 objective base funds: growth fund; income fund; capital preservation fund; and an inflation protection fund.	Firms participating must offer a minimum of two product options: a target date fund or other similar fund and a balanced fund.	Firms participating in the marketplace shall offer a minimum of two product options, including a target date or other similar fund and a balanced fund.

	Massachusetts Retirement Plan for Non-Profits ("Prototype Plan")	Washington Small Business Retirement Marketplace	New Jersey Small Business Retirement Marketplace
Investment Management	The Treasurer may contract with practitioners, administrators, investment managers and other entities, including the pension reserves investment management board, in order to design, administer and provide investment options under the plan. The plan provides for a qualified trust, with contributions made to the trust by the not-for-profit employer, the employer's employees, or both.	Not Specified	Not Specified
Fees	Custom Target Date Funds: 22-86 bps Growth: 60 bps Income: 40 bps Capital Preservation: 40 bps Inflation Protected: 86 bps	No more than 1% in total annual fees to investors; participating employers may not be charged an administrative fee.	No more than 1% in total annual fees to investors; participating employers may not be charged an administrative fee.

	Massachusetts Retirement Plan for Non-Profits ("Prototype Plan")	Washington Small Business Retirement Marketplace	New Jersey Small Business Retirement Marketplace
Program Funding	Under the trust instrument, any part of the corpus or income shall not be used for, or diverted to, purposes other than the exclusive benefit of employees or their beneficiaries at any time prior to the satisfaction of all liabilities with respect to employees and their beneficiaries.	The Legislature appropriated $524,000 for the Department of Commerce for the two year budget cycle beginning July 1, 2015. In addition to any appropriated funds, the Director may use private funding sources, including private foundation grants, to pay for marketplace expenses. On behalf of the marketplace, the Department shall seek federal and private grants and is authorized to accept any funds awarded to the department for use in the marketplace.	In addition to any funds appropriated for the purposes of this act, the State Treasurer, or the Treasurer's designee, shall approve the use of private funding sources, including private foundation grants, to pay for marketplace expenses. On behalf of the marketplace, the Department of Treasury shall seek federal and private grants and is authorized to accept any funds awarded to the State Treasurer, or the Treasurer's designee, for use in designing, implementing, and operating the marketplace. The State Treasurer, or designee, may establish a fee system that charges participating marketplace firms in order to cover the startup and annual administrative expenses.

	Massachusetts Retirement Plan for Non-Profits ("Prototype Plan")	Washington Small Business Retirement Marketplace	New Jersey Small Business Retirement Marketplace
Program Administration	In order to participate in the plan, a not-for-profit employer shall execute a participation agreement, agree to the terms of the plan and operate the plan in compliance with the Internal Revenue Code and ERISA. The Treasurer may require the not-for-profit employer sign a service agreement and use forms and procedures prescribed by the Treasurer. The Treasurer may also require that certain employers seek approval of their plans from the IRS.	The Director will contract with a private entity to establish protocols for reviewing financial services firms interested in selling products and operating the marketplace website. The Director shall adopt rules necessary to allow the marketplace to operate as authorized by this legislation. As part of the rule development process, the Director shall consult with organizations representing eligible employers, qualified employees, private and nonprofit sector retirement plan administrators and providers, organizations representing private sector financial services firms, and any other individuals or entities that the Director determines relevant to the development of an effective and efficient method for operating the marketplace.	The State Treasurer, or designee, shall contract with one or more private sector entities to establish a protocol of reviewing and approving the qualifications of all financial services firms that meet the requirement to participate in the marketplace. The State Treasurer, or designee, shall consult with organizations representing eligible employers, qualified employees, private and nonprofit sector retirement plan administrators and providers, private sector financial services firms, and any other individuals or entities that the State Treasurer, or designee, determines relevant to the effective and efficient method of effectuating the purposes of this act.
Marketing & Outreach	Not Specified	The Director may contract with a private sector entity to develop marketing materials about the marketplace that can be distributed electronically or posted on public sector maintained websites and promote the benefits of retirement savings and other information that promotes financial literacy.	The State Treasurer, or designee, shall contract with one or more private sector entities to develop marketing materials about the marketplace that can be distributed electronically or posted on both public and private sector maintained websites and promote the benefits of retirement savings and other information that promotes financial literacy.

	Massachusetts Retirement Plan for Non-Profits ("Prototype Plan")	Washington Small Business Retirement Marketplace	New Jersey Small Business Retirement Marketplace
Establish Website	Yes. Retirement Income Control Panel – web-based tool to allow participants to view hypothetical projections of retirement income based on assumptions on account balances, savings and rate of return.	Yes. The website would include information on how eligible employers can voluntarily participate in the marketplace.	Yes. The website would include information on how eligible employers can voluntarily participate in the marketplace.
Implementation Timeline	Not Specified	Rules to implement the program must be presented by January 1st of the year to be adopted and cannot be adopted until the end of the legislative session that year.	Not Specified

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