

DEPARTMENT OF LABOR

Employee Benefits Security Administration

29 CFR Part 2510

RIN 1210-AB71

Savings Arrangements Established by States for Non-Governmental Employees

AGENCY: Employee Benefits Security Administration, Department of Labor.

ACTION: Final rule.

SUMMARY: This document describes circumstances in which state payroll deduction savings programs with automatic enrollment would not give rise to the establishment of employee pension benefit plans under the Employee Retirement Income Security Act of 1974, as amended (ERISA). This document provides guidance for states in designing such programs so as to reduce the risk of ERISA preemption of the relevant state laws. This document also provides guidance to private-sector employers that may be covered by such state laws. This rule affects individuals and employers subject to such state laws.

DATES: This rule is effective [INSERT DATE 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER].

FOR FURTHER INFORMATION CONTACT: Janet Song, Office of Regulations and Interpretations, Employee Benefits Security Administration, (202) 693-8500. This is not a toll-free number.

SUPPLEMENTARY INFORMATION:

I. BACKGROUND

Approximately 39 million employees in the United States do not have access to a retirement savings plan through their employers.¹ Even though such employees could set up and contribute to their own individual retirement accounts or annuities (IRAs), the great majority do not save for retirement. In fact, less than 10 percent of all workers contribute to a plan outside of work.²

For older Americans, inadequate retirement savings can mean sacrificing or skimping on food, housing, health care, transportation, and other necessities. In addition, inadequate retirement savings places greater stress on state and federal social welfare programs as guaranteed sources of income and economic security for older Americans. Accordingly, states have a substantial governmental interest to encourage retirement savings in order to protect the economic security of their residents.³ Concern over the low rate of saving among American workers and the lack of access to workplace plans for many of those workers has led some state governments to expand access to savings programs for their residents and other individuals employed in their jurisdictions by creating their own programs and requiring employer participation.⁴

A. State Payroll Deduction Savings Initiatives

¹ National Compensation Survey, Bureau of Labor Statistics (July 2016), Employee Benefits in the United States – March 2016 (<http://www.bls.gov/news.release/pdf/ebs2.pdf>). These data show that 66 percent of 114 million private-sector workers have access to a retirement plan through work. Therefore, 34 percent of 114 million private-sector workers (39 million) do not have access to a retirement plan through work.

² See The Pew Charitable Trust, “How States Are Working to Address The Retirement Savings Challenge,” (June 2016) (<http://www.pewtrusts.org/~media/assets/2016/06/howstatesareworkingtoaddresstheretirementsavingschallenge.pdf>).

³ See Christian E. Weller, PhD, Nari Rhee, PhD, and Carolyn Arcand, “Financial Security Scorecard: A State-by-State Analysis of Economic Pressures Facing Future Retirees,” National Institute on Retirement Security (March 2014) (www.nirsonline.org/index.php?option=com_content&task=view&id=830&Itemid=48).

⁴ See, e.g., Kathleen Kennedy Townsend, Chair, Report of the Governor’s Task Force to Ensure Retirement Security for All Marylanders, “1,000,000 of Our Neighbors at Risk: Improving Retirement Security for Marylanders” (2015).

One approach some states have taken is to establish state payroll deduction savings programs. Through automatic enrollment such programs encourage employees to establish tax-favored IRAs funded by payroll deductions.⁵ California, Connecticut, Illinois, Maryland, and Oregon, for example, have adopted laws along these lines.⁶ These initiatives generally require certain employers that do not offer workplace savings arrangements to automatically deduct a specified amount of wages from their employees' paychecks unless the employee affirmatively chooses not to participate in the program.⁷ The employers are also required to remit the payroll deductions to state-administered IRAs established for the employees. These programs also allow employees to stop the payroll deductions at any time. The programs, as currently designed, do not require, provide for or permit employers to make matching or other contributions of their own into the employees' accounts. In addition, the state initiatives typically require that employers provide employees with information prepared or assembled by the program, including information on employees' rights and various program features.

B. ERISA's Regulation of Employee Benefit Plans

Section 3(2) of ERISA defines the terms "employee pension benefit plan" and "pension plan" broadly to mean, in relevant part "[A]ny plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an

⁵ These could include individual retirement accounts described in 26 U.S.C. 408(a), individual retirement annuities described in 26 U.S.C. 408(b), and Roth IRAs described in 26 U.S.C. 408A.

⁶ California Secure Choice Retirement Savings Trust Act, Cal. Gov't Code §§ 100000-100044 (2012); Connecticut Retirement Security Program Act, P.A. 16-29 (2016); Illinois Secure Choice Savings Program Act, 820 Ill. Comp. Stat. 80/1-95 (2015); Maryland Small Business Retirement Savings Program Act, Ch. 324 (H.B. 1378)(2016); Oregon Retirement Savings Board Act, Ch. 557 (H.B. 2960)(2015).

⁷ Workplace savings arrangements may include plans such as those qualified under or described in 26 U.S.C. 401(a), 401(k), 403(a), 403(b), 408(k) or 408(p), and may constitute either ERISA or non-ERISA arrangements.

employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program provides retirement income to employees....”⁸ The Department and the courts have broadly interpreted “established or maintained” to require only minimal involvement by an employer or employee organization.⁹ An employer could, for example, establish an employee benefit plan simply by purchasing insurance products for individual employees. These expansive definitions are essential to ERISA’s purpose of protecting plan participants by ensuring the security of promised benefits.

Due to the broad scope of ERISA coverage, some stakeholders have expressed concern that state payroll deduction savings programs, such as those enacted in California, Connecticut, Illinois, Maryland, and Oregon may cause covered employers to inadvertently establish ERISA-covered plans, despite the express intent of the states to avoid such a result. This uncertainty, together with ERISA’s broad preemption of state laws that “relate to” private-sector employee pension benefit plans has created a serious impediment to wider adoption of state payroll deduction savings programs.¹⁰

⁸ 29 U.S.C. 1002(2)(A). ERISA’s Title I provisions “shall apply to any employee benefit plan if it is established or maintained . . . by any employer engaged in commerce or in any industry or activity affecting commerce.” 29 U.S.C. 1003(a). Section 4(b) of ERISA includes express exemption from coverage under Title I for governmental plans, church plans, plans maintained solely to comply with applicable state laws regarding workers compensation, unemployment, or disability, certain foreign plans, and unfunded excess benefit plans. 29 U.S.C. 1003(b).

⁹ Donovan v. Dillingham, 688 F.2d 1367 (11th Cir. 1982); Harding v. Provident Life and Accident Ins. Co., 809 F. Supp. 2d 403, 415-419 (W.D. Pa. 2011); DOL Adv. Op. 94-22A (July 1, 1994).

¹⁰ ERISA’s preemption provision, section 514(a) of ERISA, 29 U.S.C. 1144(a), provides that the Act “shall supersede any and all State laws insofar as they . . . relate to any employee benefit plan” covered by the statute. The U.S. Supreme Court has long held that “[a] law ‘relates to’ an employee benefit plan, in the normal sense of the phrase, if it has a connection with or reference to such a plan.” Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 96-97 (1983) (footnote omitted). In various decisions, the Court has concluded that ERISA preempts state laws that: (1) mandate employee benefit structures or their administration; (2)

C. 1975 IRA Payroll Deduction Safe Harbor

Although IRAs generally are not set up by employers or employee organizations, ERISA coverage may be triggered if an employer (or employee organization) does, in fact, “establish or maintain” an IRA arrangement for its employees. 29 U.S.C. 1002(2)(A).¹¹ In contexts not involving state payroll deduction savings programs, the Department has previously issued guidance to help employers determine whether their involvement in certain voluntary payroll deduction savings arrangements involving IRAs would result in the employers having established or maintained ERISA-covered plans. That guidance included a 1975 “safe harbor” regulation under 29 CFR 2510.3-2(d) setting forth circumstances under which IRAs funded by payroll deductions would not be treated as ERISA plans, and a 1999 Interpretive Bulletin clarifying that certain ministerial activities will not cause an employer to have established an ERISA plan simply by facilitating such payroll deduction savings arrangements.¹²

The 1975 regulation provides that certain IRA payroll deduction arrangements are not subject to ERISA if four conditions are met: (1) the employer makes no contributions; (2) employee participation is "completely voluntary"; (3) the employer does not endorse the program and acts as a mere facilitator of a relationship between the IRA vendor and employees; and (4) the employer receives no consideration except for its

provide alternative enforcement mechanisms; or (3) bind employers or plan fiduciaries to particular choices or preclude uniform administrative practice, thereby functioning as a regulation of an ERISA plan itself.

¹¹ ERISA section 404(c)(2) (simple retirement accounts); 29 CFR 2510.3-2(d) (1975 IRA payroll deduction safe harbor); 29 CFR 2509.99-1 (interpretive bulletin on payroll deduction IRAs); Cline v. The Industrial Maintenance Engineering & Contracting Co., 200 F.3d 1223, 1230-31 (9th Cir. 2000).

¹² See 29 CFR 2510.3-2(d); 40 FR 34526 (Aug. 15, 1975); 29 CFR 2509.99-1. The Department has also issued advisory opinions discussing the application of the safe harbor regulation to particular facts. See, e.g., DOL Adv. Op. 82-67A (Dec. 21, 1982); DOL Adv. Op. 84-25A (June 18, 1984).

own expenses.¹³ In essence, if the employer merely allows a vendor to provide employees with information about an IRA product and then facilitates payroll deduction for employees who voluntarily initiate action to sign up for the vendor's IRA, the employer will not have established, and the arrangement will not be, an ERISA pension plan.

With regard to the 1975 IRA Payroll Deduction Safe Harbor's condition requiring that an employee's participation be "completely voluntary," the Department intended this term to mean that the employee's enrollment in the program must be self-initiated. In other words, under the safe harbor, the decision to enroll in the program must be made by the employee, not the employer. If the employer automatically enrolls employees in a benefit program, the employees' participation would not be "completely voluntary" and the employer's actions would constitute the "establishment" of a pension plan, within the meaning of ERISA section 3(2). This is true even if the employee can affirmatively opt out of the program.¹⁴ Thus, arrangements that allow employers to automatically enroll employees—as do all existing state payroll deduction savings programs—do not satisfy the condition in the safe harbor that the employees' participation be "completely voluntary," even if the employees are permitted to "opt out" of the program. Consequently, such programs would fall outside the 1975 safe harbor and could be subject to ERISA.

¹³ 29 CFR 2510.3-2(d) (1975 IRA Payroll Deduction Safe Harbor).

¹⁴ See generally Proposed rule on Savings Arrangements Established by States for Non-Governmental Employees, 80 FR 72006, 72008 (November 18, 2015) (The completely voluntary condition in the 1975 safe harbor is "important because where the employer is acting on his or her own volition to provide the benefit program, the employer's actions—e.g., requiring an automatic enrollment arrangement—would constitute its 'establishment' of a plan within the meaning of ERISA's text, and trigger ERISA's protections for the employees whose money is deposited into an IRA.").

D. 2015 Proposed Regulation

At the 2015 White House Conference on Aging, the President directed the Department to publish guidance to support state efforts to promote broader access to workplace retirement savings opportunities for employees. On November 18, 2015, the Department published in the Federal Register a proposed regulation providing that for purposes of Title I of ERISA the terms “employee pension benefit plan” and “pension plan” do not include an IRA established and maintained pursuant to a state payroll deduction savings program if that program satisfies all of the conditions set forth in the proposed rule.¹⁵ By articulating the types of state payroll deduction savings programs that would be exempt from ERISA, the proposal sought to create a safe harbor for the states and employers and thus remove uncertainty regarding Title I coverage of such state payroll deduction savings programs and the IRAs established and maintained pursuant to them. In the Department’s view, courts would be less likely to find that statutes creating state programs in compliance with the proposed safe harbor are preempted by ERISA.

The proposal parallels the 1975 IRA Payroll Deduction Safe Harbor in that it requires the employer’s involvement to be no more than ministerial. 29 CFR 2510.3-2(d).¹⁶ In both contexts, limited employer involvement in the arrangement is the key to finding that the employer has not established or maintained an employee pension benefit

¹⁵ 80 FR 72006 (November 18, 2015). On the same day that the NPRM was published, the Department also published an interpretive bulletin (IB) explaining the Department’s views concerning the application of ERISA to certain state laws designed to expand retirement savings options for private-sector workers through ERISA-covered retirement plans. 80 FR 71936 (codified at 29 CFR 2509.2015-02). A number of commenters on the NPRM discussed ERISA preemption and other issues that the commenters perceived as raised by the analysis and conclusions in the IB. Comments on the IB are beyond the scope of this regulation and are not discussed in this document.

¹⁶ The Department has issued similar safe harbor regulations for group and group-type insurance arrangements, 29 CFR 2510.3-1(j) and for tax sheltered annuities, 29 CFR 2510.3-2(f).

plan. The proposal added the conditions that employer involvement must be required under state law, and that the state must establish and administer the program pursuant to state law. Significantly, and in recognition of the fact that several state initiatives provide for automatic enrollment and therefore would not satisfy the Department's 1975 IRA Payroll Deduction Safe Harbor condition that employee participation in such programs be "completely voluntary," the proposal also adopted a new condition that employee participation be "voluntary." Because the new safe harbor requires that the employer's involvement in the program be required and circumscribed by state law, the 1975 safe harbor's condition that employee participation be "completely voluntary" has been modified to permit state-required automatic employee enrollment procedures.

The Department received and analyzed approximately 70 public comments in response to the proposed rule. The Department is issuing a final rule that contains some changes and clarifications in response to questions raised in the public comments. Those changes are described herein.

II. OVERVIEW OF FINAL RULE

The final rule largely adopts the proposal's general structure. Thus, new paragraph (h) of § 2510.3-2 continues to provide in the final rule that, for purposes of Title I of ERISA, the terms "employee pension benefit plan" and "pension plan" do not include an individual retirement plan (as defined in 26 U.S.C. 7701(a)(37))¹⁷ established and maintained pursuant to a state payroll deduction savings program if the program satisfies all of the conditions set forth in paragraphs (h)(1)(i) through (xi) of the

¹⁷ The term "individual retirement plan" includes both traditional IRAs (individual retirement accounts described in section 408(a) and individual retirement annuities described in section 408(b) of the Code) and Roth IRAs under section 408A of the Code.

regulation. Thus, if these conditions are satisfied, neither the state nor the employer is establishing or maintaining a pension plan subject to Title I of ERISA.

Most of the new safe harbor's conditions focus on the state's role in the program. The program must be specifically established pursuant to state law. 29 CFR 2510.3-2(h)(1)(i). The program is implemented and administered by the state that established the program. 29 CFR 2510.3-2(h)(1)(ii). The state must be responsible for investing the employee savings or for selecting investment alternatives from which employees may choose. Id. The state must be responsible for the security of payroll deductions and employee savings. 29 CFR 2510.3-2(h)(1)(iii). The state must adopt measures to ensure that employees are notified of their rights under the program, and must create a mechanism for enforcing those rights. 29 CFR 2510.3-2(h)(1)(iv). The state may implement and administer the program through its governmental agency or instrumentality. 29 CFR 2510.3-2(h)(1)(ii). The state or its governmental agency or instrumentality may also contract with others to operate and administer the program. 29 CFR 2510.3-2(h)(2)(ii).

Many of the rule's conditions limit the employer's role in the program. The employer's activities must be limited to ministerial activities such as collecting payroll deductions and remitting them to the program. 29 CFR 2510.3-2(h)(1)(vii)(A). The employer may provide notice to the employees and maintain records of the payroll deductions and remittance of payments. 29 CFR 2510.3-2(h)(1)(vii)(B). The employer may provide information to the state necessary for the operation of the program. 29 CFR 2510.3-2(h)(1)(vii)(C). The employer may distribute program information from the state program to employees. 29 CFR 2510.3-2(h)(1)(vii)(D). Employers cannot contribute

employer funds to the IRAs. 29 CFR 2510.3-2(h)(1)(viii). Employer participation in the program must be required by state law. 29 CFR 2510.3-2(h)(1)(ix).

Other critical conditions focus on employee rights. For example, employee participation in the program must be voluntary. 29 CFR 2510.3-2(h)(1)(v). Thus, if the program requires automatic enrollment, employees must be given adequate advance notice and have the right to opt out. 29 CFR 2510.3-2(h)(2)(iii). In addition, employees must be notified of their rights under the program, including the mechanism for enforcement of those rights. 29 CFR 2510.3-2(h)(1)(iv).

III. CHANGES TO PROPOSAL BASED ON PUBLIC COMMENT

A. Ability to Experiment

The final rule contains new regulatory text in paragraph (a) of § 2510.3-2 making it clear that the rule's conditions on state payroll deduction savings programs simply create a safe harbor. A safe harbor approach to these arrangements provides to states clear guide posts and certainty, yet does not by its terms prohibit states from taking additional or different action or from experimenting with other programs or arrangements. Although the Department expressed this view in the proposal's preamble, commenters requested that this safe harbor position be explicitly incorporated into the operative text, just as the Department did previously under § 2510.3-1 with respect to certain practices excluded from the definition of "welfare plan."¹⁸ The Department

¹⁸ See Comment Letter # 58 (Joint Submission from Service Employee International Union, National Education Association, American Federation of Teachers, American Federation of State County and Municipal Employees, and National Conference on Public Employee Retirement Systems) ("Although the preamble to the Proposed Rule clearly states that it is providing an additional 'safe harbor' that defined an arrangement that is not subject to ERISA coverage, that statement does not appear within the body of the regulation itself. It would be helpful to those states that may wish to experiment by adopting programs that

agrees that the final regulation would be improved by adding regulatory text explicitly recognizing that the regulation is a safe harbor. Adding such regulatory text clarifies the Department's intent and conforms this section with § 2510.3-1 (relating to welfare plans).

Accordingly, the final rule revises paragraph (a) of § 2510.3-2 by deleting some outdated text and adding the following sentence: "The safe harbors in this section should not be read as implicitly indicating the Department's views on the possible scope of section 3(2)." By adding this sentence to paragraph (a) of § 2510.3-2, the sentence then modifies all plans, funds and programs subsequently listed and discussed in paragraphs (b) through (h) of § 2510.3-2.¹⁹ In different contexts in the past, the Department has stated its view that various of the programs listed in paragraphs (b) through (g) of § 2510.3-2 are safe harbors and do not preclude the possibility that plans, funds, and programs not meeting the relevant conditions in the regulation might also not be pension plans within the meaning of ERISA. Thus, this revision to paragraph (a) merely clarifies this view in operative text for these other programs.

B. Ability to Choose Investments and Control Leakage

The final rule removes the condition from paragraph (h)(1)(vi) of the proposal that would have prohibited states from imposing any restrictions, direct or indirect, on employee withdrawals from their IRAs. The proposal provided that a state program must not "require that an employee or beneficiary retain any portion of contributions or

are not specifically and clearly covered by the safe harbor but that are consistent with its meaning and intent if the [final rule] were to include such a statement.").

¹⁹ The plans, funds, and programs described in 29 CFR 2510.3-2 are severance pay plans (see paragraph (b)), bonus programs (see paragraph (c)), 1975 IRA payroll deduction (see paragraph (d)), gratuitous payments to pre-ERISA retirees (see paragraph (e)), tax sheltered annuities (see paragraph (f)), supplemental payment plans (see paragraph (g)) and certain state savings programs (see new paragraph (h)).

earnings in his or her IRA and does not otherwise impose any restrictions on withdrawals or impose any cost or penalty on transfers or rollovers permitted under the Internal Revenue Code.” The purpose of this prohibition, as explained in the proposal’s preamble, was to make sure that employees would have meaningful control over the assets in their IRAs.²⁰

The first reason commenters gave for removing this condition was that it would interfere with the states’ ability to guard against “leakage” (*i.e.*, the use of long-term savings for short-term purposes). Absent such prohibition, states might seek to prevent leakage by, for example, requiring workers to wait until a specified age (*e.g.*, age 55 or 60) before they have access to their money, subject to an exception for “hardship withdrawals.” Since the states deal directly with the effects of geriatric poverty, they have a substantial interest in controlling leakage, and the proposal’s prohibition against withdrawal restrictions could undermine that interest.²¹

The commenters’ second reason for removal was that the proposal’s prohibition would interfere with the states’ ability to design programs with diversified investment strategies, including investment options where immediate liquidity is not possible, but where participants may see better performance with lower costs. For instance, some state payroll deduction savings programs may wish to use default or alternative investment options that include partially or fully guaranteed returns but do not provide immediate liquidity. In addition, some state payroll deduction savings programs may wish to pool

²⁰ 80 FR 72006, 72010 (Nov. 18, 2015).

²¹ See Comment Letter # 39 (AARP) (“Increasingly, states are realizing that if retired individuals do not have adequate income, they are likely to be a burden on state resources for housing, food, and medical care. For example, according to a recent Utah study, the total cost to taxpayers for new retirees in that state will top \$3.7 billion over the next 15 years.”).

and manage default investments using strategies and investments similar to those for defined benefit plans covering state employees, which typically include lock ups and restrictions ranging from months to years. The commenters assert that these long-term investments tend to provide greater returns than similar investments with complete liquidity (such as daily-valued mutual or bank funds), but would not have been permitted under the proposal's prohibition.

The third reason given by commenters was that the proposal's prohibition would interfere with the states' ability to offer lifetime income options, such as annuities. One consumer organization commented, for instance, that the proposed prohibition "may have the effect of preventing states from requiring an annuity payout (or even permitting an annuity payout option)..."²² Another commenter stated, "as drafted, the withdrawal restriction can be read to apply at the investment-product level, which could impede an arrangement's ability to offer an investment that includes lifetime income features. Absence of immediate liquidity is an actuarially necessary element for many products that guarantee income for life, and there is no policy basis for excluding investment options that incorporate such features."²³

The fourth reason given for removal was that the proposal's prohibition was not relevant to determining under ERISA section 3(2) whether the state program, including employer behavior thereunder, constitutes "establishment or maintenance" of an employee benefit plan; or the Department's stated goal of crafting conditions that would limit employer involvement.

²² Comment Letter # 65 (Pension Rights Center).

²³ Comment Letter # 44 (TIAA-CREF).

The Department agrees in many respects with these arguments and has removed this prohibition from the final regulation. Although the Department included this prohibition in the proposal to make sure that employees would have meaningful control over the assets in their IRAs, the Department has concluded that determinations regarding the necessity for such a prohibition are better left to the states. Based on established principles of federalism, it is more appropriately the role of the states, and not the Department, to determine what constitutes meaningful control of IRA assets in this non-ERISA context, subject to any federal law under the Department’s jurisdiction – in this case, the prohibited transaction provisions in section 4975 of the Internal Revenue Code (Code) – applicable to IRAs.

C. Ability to Use Tax Incentives or Credits

The final rule modifies the condition in the proposal that would have prohibited employers from receiving more than their actual costs of complying with state payroll deduction savings programs. The proposal provided that employers may not receive any “direct or indirect consideration in the form of cash or otherwise, other than the reimbursement of actual costs of the program to the employer” The purpose of this provision was to allow employers to recoup actual costs of complying with the state law, but nothing in excess of that amount, in order to avoid economic incentives that might effectively discourage sponsorship of ERISA plans in the future.

Several commenters urged the Department to moderate that proposal’s prohibition and grant the states more flexibility to determine the most effective ways to compensate employers for their role in the state program. The majority of commenters on this issue indicated that states should be able to reward employer behavior with tax incentives or

credits.²⁴ The states themselves who commented believe it should be within their discretion whether to provide support to employers that participate in the state program, and to determine the type and amount of that support, particularly where participation in the state program is required by the state.²⁵ Many commenters also pointed out that it would be very difficult if, as the proposal required, the state had to determine actual cost for every individual employer before providing a reimbursement.²⁶ One commenter, for example, stated “it may be exceedingly difficult if not impossible for states to accurately calculate the 'actual cost' accrued by each participating employer, and it may be impractical for the amount of each tax credit to vary by employer.”²⁷ The commenters generally recommended that the rule clearly establish that states are able to use tax incentives or credits, whether or not such incentives or credits vary in amount by employer or represent actual costs.

The Department does not intend that cost reimbursement be difficult or impractical for states to implement. Accordingly, paragraph (h)(1)(xi) of the final rule does not require employers’ actual costs to be calculated. Instead, it provides that the maximum consideration the state may provide to an employer is limited to a reasonable approximation of the employer’s costs (or a typical employer’s costs) under the program. This would allow the state to provide consideration in a flat amount based on a typical employer's costs or in different amounts based on an estimate of an employer’s expenses. This standard accommodates the commenters’ request for flexibility and confirms that

²⁴ See, e.g., Comment Letter # 65 (Pension Rights Center).

²⁵ See, e.g., Comment Letter # 54 (Oregon Retirement Savings Board). See also Comment Letter #37 (Maryland Commission on Retirement Security and Savings).

²⁶ See, e.g., Comment Letter # 63 (Tax Alliance for Economic Mobility).

²⁷ Comment Letter # 56 (Aspen Institute Financial Security Program).

states may use tax incentives or credits, without regard to whether such incentives or credits equal the actual costs of the program to the employer. In order to remain within the safe harbor under this approach, however, states must ensure that their 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 incentivize them to participate in state programs in lieu of establishing employee pension benefit plans.

D. Ability to Focus on Employers That Do Not Offer Savings Arrangements

The final rule modifies paragraph (h)(2)(i) of the proposal, which stated that a state program meeting the regulation's conditions would not fail to qualify for the safe harbor merely because the program is “directed toward those employees who are not already eligible for some other workplace savings arrangement.” Even though this refers to a provision (directing the program toward such employees) that is not a requirement or condition of the safe harbor but is only an example of a feature that states may incorporate when designing their automatic IRA programs, some commenters maintained that this language in paragraph (h)(2)(i) could encourage states to focus on whether particular employees of an employer are eligible to participate in a workplace savings arrangement. They maintained that such a focus could be overly burdensome for certain employers because they may have to monitor their obligations on an employee-by-employee basis, with some employees being enrolled in the state program, some in the workplace savings arrangement, and others migrating between the two arrangements. Such burden, they maintained, could also give employers an incentive not to offer a

retirement plan for their employees. The Department sees merit in these comments and also understands that the relevant laws enacted thus far by the states have been directed toward those employers that do not offer any workplace savings arrangement, rather than focusing on employees who are not eligible for such programs. Thus, the final rule provides that such a program would not fail to qualify for the safe harbor merely because it is “directed toward those employers that do not offer some other workplace savings arrangement.” This language will reduce employer involvement in determining employee eligibility for the state program, and it accurately reflects current state laws.

E. Ability of Governmental Agencies and Instrumentalities to Implement and Administer State Programs

The final rule clarifies the role of governmental agencies and instrumentalities in implementing and administering state programs. Some conditions in the proposal referred to “State” while other conditions referred to “State ... or ...governmental agency or instrumentality of the State.” This confused some commenters who wondered whether the Department intended to limit who could satisfy particular conditions by use of these different terms. The commenters pointed out that state legislation creating payroll deduction savings programs typically also creates boards to design, implement and administer such programs on a day-to-day basis and grants to these boards administrative rulemaking authority over the program. The commenters requested clarification on whether the state laws establishing the programs would have to specifically address every condition in the safe harbor, or whether such boards would be able to address any condition not expressly addressed in the legislation through their administrative rulemaking authority.

In response to these comments, the final regulation uses the phrase “State (or governmental agency or instrumentality of the State)” throughout to clarify that, so long as the program is specifically established pursuant to state law, a state program is eligible for the safe harbor even if the state law delegates a wide array of implementation and administrative authority (such as authority for rulemaking, contracting with third-party vendors, and investing) to a board, committee, department, authority, State Treasurer, office (such as Office of the Treasurer), or other similar governmental agency or instrumentality of the state. See, e.g., § 2510.3-2(h)(1) (iii), (iv), (vi), (vii), (xi), and (h)(2)(ii). In addition, the phrase “by a State” was removed from paragraph (h)(1)(i) and the word “implement” was added to paragraph (h)(1)(ii) for further clarification. A conforming amendment also was made to paragraph (h)(2)(iii) to reflect the fact that state legislatures may delegate authority to set or change the state program’s automatic contribution and escalation rates to a governmental agency or instrumentality of the state as noted above.

IV. COMMENTS NOT REQUIRING CHANGES TO PROPOSAL

A. Applicability of Prohibited Transaction Protections – Code § 4975

A number of commenters sought clarification on whether, and to what extent, the protections in the prohibited transaction provisions in section 4975 of the Code would apply to the state programs covered by the safe harbor. These commenters expressed concern regarding a perceived lack of federal consumer protections under the proposed safe harbor for state payroll deduction savings programs, because such safe harbor

arrangements would be exempt from ERISA coverage (including all of ERISA's protective conditions).²⁸

The safe harbor in the final rule is expressly conditioned on the states' use of IRAs, as defined in section 7701(a)(37) of the Code. 29 CFR 2510.3-2(h)(1). Such IRAs are subject to applicable provisions of the Code, including Code section 4975. Section 4975 of the Code includes prohibited transaction provisions very similar to those in ERISA, which protect participants and beneficiaries in ERISA plans by identifying and disallowing categories of conduct between plans and disqualified persons, as well as conduct involving fiduciary self-dealing. These prohibited transaction provisions are primarily enforced through imposition of excise taxes by the Internal Revenue Service.

Consequently, the final regulation protects employees from an array of transactions involving disqualified persons that could be harmful to employees' savings. For instance, absent an available prohibited transaction exemption,²⁹ the safe harbor effectively prohibits a sale or exchange, or leasing, of any property between an IRA and a disqualified person; the lending of money or other extension of credit between an IRA and a disqualified person; the furnishing of goods, services, or facilities between an IRA and a disqualified person; a transfer to, or use by or for the benefit of, a disqualified person of the income or assets of an IRA; any act by a disqualified person who is a fiduciary whereby he or she deals with the income or assets of an IRA in his or her own

²⁸ Comment Letter # 29 (Securities Industry Financial Management Association); Comment Letter # 55 (U.S. Chamber of Commerce); Comment Letter # 62 (Investment Company Institute).

²⁹ See Code section 4975(d) (enumerating several statutory prohibited transaction exemptions); Code section 4975(c)(2) (authorizing Secretary of the Treasury to grant exemptions from the prohibited transaction provisions in Code section 4975) and Reorganization Plan No. 4 of 1978 (5 U.S.C. App. at 237 (2012) (generally transferring the authority of the Secretary of the Treasury to grant administrative exemptions under Code section 4975 to the Secretary of Labor).

interest or for his or her own account; and any consideration for his or her own personal account by any disqualified person who is a fiduciary from any party dealing with the IRA in connection with a transaction involving the income or assets of the IRA. 26 U.S.C. 4975(c)(1)(A)-(F).

Section 4975 imposes a tax on each prohibited transaction to be paid by any disqualified person who participates in the prohibited transaction (other than a fiduciary acting only as such). 26 U.S.C. 4975(a). The rate of the tax is equal to 15 percent of the amount involved for each prohibited transaction for each year in the taxable period. Id. If the transaction is not corrected within the taxable period, the rate of the tax may be equal to 100 percent of the amount involved. 26 U.S.C. 4975(b). The term “disqualified person” includes, among others, a fiduciary and a person providing services to an IRA.

With regard to commenters who asked how the prohibited transaction provisions in section 4975 of the Code would apply to the state programs covered by the safe harbor, the final rule does not adopt any special provisions for, or accord any special treatment or exemptions to, IRAs established and maintained pursuant to state payroll deduction savings programs. The prohibited transaction rules in section 4975 of the Code apply to, and protect, the assets of these IRAs in the same fashion, and to the same extent, that they apply to and protect the assets of any traditional IRA or tax-qualified retirement plan under Code section 401(a). To the extent persons operating and maintaining these programs are fiduciaries within the meaning of Code section 4975(e)(3), or provide services to an IRA, such persons are “disqualified persons” within the meaning of Code section 4975(e)(2)(A) and (B), respectively. Their status under these sections of the Code is controlling for prohibited transaction purposes, not their status or title under state

law. Accordingly, section 4975 of the Code prohibits them from, among other things, dealing with assets of IRAs in a manner that benefits themselves or any persons in whom they have an interest that may affect their best judgment as fiduciaries. Thus, persons with authority to manage or administer these programs under state law should exercise caution when carrying out their duties, including for example selecting a program administrator or making investments or selecting an investment manager or managers, to avoid prohibited transactions. Whether any particular transaction would be prohibited is an inherently factual inquiry and would depend on the facts and circumstances of the particular situation.

State programs concerned about prohibited transactions may submit an individual exemption request to the Department. Any such request should be made in accordance with the Department's Prohibited Transaction Exemption Procedures (29 CFR Part 2570). The Department may grant an exemption request if it finds that the exemption is administratively feasible, in the interests of plans and of their participants and beneficiaries (and/or IRAs and of their owners), and protective of the rights of the participants and beneficiaries of such plans (and/or the owners of such IRAs).

B. Prescribing a Further Connection Between the State, Employers, and Employees

A number of commenters provided comments on whether the safe harbor should require some connection between the employers and employees covered by a state payroll deduction savings program and the state that establishes the program, and if so, what kind of connection. Some commenters favor limiting the safe harbor to state programs that cover only employees who are residents of the state and employed by an

employer whose principal place of business also is within that state.³⁰ These commenters were focused primarily on burdens on small employers, particularly those operating near state lines with employees in multiple jurisdictions. Other commenters reject the idea that the Department’s safe harbor should interfere with what is essentially a question of state law and prerogative. These commenters maintain that the extent to which a state can regulate employers is already established under existing legal principles.³¹ The Department agrees with the latter commenters. The states are in the best position to determine the appropriate connection between employers and employees covered under the program and the states that establish such programs, and to know the limits on their ability to regulate extraterritorial conduct. Inasmuch as existing legal principles establish the extent to which the states can regulate employers, the final rule simply requires that the program be specifically established pursuant to state law and that the employer’s participation be required by state law. 29 CFR 2510.3-2(h)(1)(i) and (ix). These two conditions define and limit the safe harbor to be coextensive with the state’s authority to regulate employers.

C. Assuming Responsibility for the Security of Payroll Deductions

A number of commenters provided comments on paragraph (h)(1)(iii) of the proposal, which in relevant part provides that a state must “assume[] responsibility for the security of payroll deductions” Many commenters representing states were

³⁰ See, e.g., Comment Letter #16 (Empower Retirement) and Comment Letter #31 (American Benefits Council).

³¹ Comment Letter #11 (Connecticut Retirement Security Board) (“[T]he Department need not establish its own limitations, as the United States Constitution already places limits on the ability of states to regulate extraterritorial conduct.” Citing Healy v. Beer Inst., Inc., 491 U.S. 324, 336 (1989); Allstate Ins. Co. v. Hague, 449 U.S. 302, 310 (1981)).

concerned that this condition might be construed to hold states strictly liable for payroll deductions, even in extreme cases such as, for example, fraud or theft by employers.

This condition does not make states guarantors or hold them strictly liable for any and all employers' failures to transmit payroll deductions. Rather, this condition would be satisfied if the state established and followed a process to ensure that employers transmit payroll deductions safely, appropriately and in a timely fashion.

Nor does this condition contemplate only a single approach to satisfy the safe harbor. For instance, some states have freestanding wage withholding and theft laws, as well as enforcement programs (such as audits) to protect employees from wage theft and similar problems. Such laws and programs ordinarily would satisfy this condition of the safe harbor if they are applicable to the payroll deductions under the state payroll deduction savings program and enforced by state agents. Other states, however, have adopted, or are considering adopting, timing and enforcement provisions specific to their payroll deduction savings programs.³² In the Department's view, the safe harbor would permit this approach as well.

Some commenters requested that the Department expand paragraph (h)(1)(iii) by adding several conditions to require states to adopt various consumer protections, such as conditions requiring deposits to be made to IRAs within a maximum number of days, civil and criminal penalties for deposit failures, and education programs for employees regarding how to identify employer misuse of payroll deductions. The Department encourages the states to adopt consumer protections along these lines, as necessary or

³² Connecticut Retirement Security Program, P.A. 16-29, §§ 7(e) and 10(b) (2016).

appropriate. The Department declines the commenters' suggestion to make them explicit conditions of the safe harbor, however, as each state is best positioned to calibrate the type of consumer protections needed to secure payroll deductions. Accordingly, the final rule adopts the proposal's provision without change.

D. Requiring Employer's Participation to be "Required by State Law"

1. In General

A number of commenters raised concerns with paragraph (h)(1)(x) of the proposal, which in relevant part states that the employer's participation in the program must be "required by State law[.]" Several commenters representing states and financial service providers requested that the Department not include this condition in the final rule. These commenters believe the safe harbor should extend to employers that choose whether or not to participate in a state payroll deduction savings program with automatic enrollment, as long as the state – and not the employer – thereafter controls and administers the program. Another commenter asserted that automatic enrollment "goes to whether a plan is 'completely voluntary' or 'voluntary' for an employee and should not be used as a material measure of how limited an employer's involvement is, especially in this case where the employer has no say in whether automatic enrollment is provided for under the state-run arrangement."

It is the Department's view that an employer that voluntarily chooses to automatically enroll its employees in a state payroll deduction savings program has established a pension plan under ERISA and should not be eligible for a safe harbor exclusion from ERISA. ERISA broadly defines "pension plan" to encompass any "plan, fund, or program" that is "established or maintained" by an employer to provide

retirement income to its employees. Under ERISA's expansive test, when an employer voluntarily chooses to provide retirement income to its employees through a particular benefit arrangement, it effectively establishes or maintains a plan. This is no less true when the employer chooses to provide the benefits through a voluntary arrangement offered by a state than when it chooses to provide the benefits through the purchase of an insurance policy or some other contractual arrangement. In either case, the employer made a voluntary decision to provide retirement benefits to its employees as part of a particular plan, fund, or program that it chose to the exclusion of other possible benefit arrangements.

In such circumstances, the employer, by choosing to participate in the state program, is effectively making plan design decisions that have direct consequences to its employees. Decisions subsumed in the employer's choice include, for example, the intended benefits, source of funding, funding medium, investment strategy, contribution amounts and limits, procedures to apply for and collect benefits, and form of distribution. By contrast, an employer that is simply complying with a state law requirement is not making any of these decisions and therefore reasonably can be viewed as complying with the safe harbor and not establishing or maintaining a pension plan under section 3(2) of ERISA.³³ The state has required the employer to participate and automatically enroll its

³³ One commenter asserted that the proposal contrasted with the Department's prior positions on ERISA preemption, and cited the Department's amicus brief in Golden Gate Rest. Ass'n v. San Francisco, 546 F.3d 639 (9th Cir. 2008). Because arrangements that comply with the safe harbor are being determined by regulation not to be ERISA plans, the Department sees its position in the Golden Gate case as distinguishable from its position here. The commenter also argued that the Supreme Court opinion in Fort Halifax Packing Co. v. Coyne, 482 U.S. 1 (1987), where the court found that a state law requiring employers to make severance payments to employees under certain circumstance was not preempted by ERISA because it did not require establishment of an ongoing administrative scheme, was not support for the Department's proposal. Although such an ongoing scheme may be a necessary element of a plan, it is not, as evidenced by the Department's earlier safe harbors, sufficient to establish an employee benefit plan

employees; the employer neither voluntarily elects to do this nor significantly controls the program. Limited employer involvement in the program is the key to a determination that the employer has not established or maintained an employee pension benefit plan. The employer's participation must be required by state law – if it is voluntary, the safe harbor does not apply.

The 1975 IRA Payroll Deduction Safe Harbor is still available, however, to interested parties who voluntarily choose to facilitate employees' participation in a state program, if the conditions of that safe harbor are met and if permitted under the state payroll deduction savings program. As discussed above, the 1975 IRA Payroll Deduction Safe Harbor has terms and conditions substantially similar to those in the safe harbor being adopted today, but it does not permit automatic enrollment, even if accompanied by an option to opt out. Thus, if a state payroll deduction savings program permits employees of employers that are not subject to the state's automatic enrollment requirement to affirmatively choose to participate in the program, neither such participation nor the employer's facilitation of that participation would result in the employer having established an ERISA-covered plan, as long as the employer and state program satisfy the conditions in the 1975 IRA Payroll Deduction Safe Harbor.

Some commenters asserted that the Department was arbitrary in interpreting the 1975 safe harbor to prohibit automatic enrollment. However, as discussed at greater length in the NPRM, the Department's interpretation of the "completely voluntary" provision in the safe harbor is a reasonable reading of the safe harbor condition supported

under ERISA where other conditions – such as being established or maintained by an employer or employee organization, or both – are absent.

by legal authorities interpreting the concept of “completely voluntary” in other contexts. The interpretation of the safe harbor is also consistent with a legitimate policy concern about employers implementing “opt-out” provisions in employer-endorsed IRA arrangements without having to comply with ERISA duties and consumer protection provisions. That concern is not present with respect to state programs that require employers to auto-enroll employees in a state sponsored IRA program.

One commenter asserted that the Department’s analysis in the proposal of whether an automatic payroll deduction savings program operated by a state is an ERISA plan conflicts with the analysis in the interpretive bulletin relating to whether a state can sponsor a multiple employer plan. This comment misapprehends the Department’s position in this rulemaking. If the state and the employer comply with the safe harbor conditions, the Department’s view is that no ERISA plan is established. Although the interpretive bulletin indicates that a state may under some circumstances act for (in the interest of) a group of voluntarily participating employers in establishing an ERISA-covered multiple employer plan, the bulletin does not mean a state would be similarly acting for employers when it requires that they participate in a program requiring the offering of a savings arrangement that is not an ERISA plan.

2. Special Treatment for Reduction in Size of Employer

Several commenters raised the issue whether the final rule could or should address situations in which an employer that was once required to participate in a state program ceases to be subject to the state requirement due to a change in its size. These commenters noted that most state payroll deduction IRA laws contain an exemption for small employers. In California and Connecticut, for instance, employers with fewer than

5 employees are not subject to the state law requirement.³⁴ In Illinois, the exemption is available to employers with fewer than 25 employees.³⁵ Thus, as the commenters noted, an employer that is subject to the requirement could subsequently drop below a state's threshold number of employees, and into the exemption, simply by having one employee resign. The commenters asked whether an employer that falls below the minimum number of employees could continue to make payroll deductions for existing employees (or automatically enroll new employees) under the program and still meet the conditions of the Department's safe harbor.

The situation identified by the commenters results from the operation of the particular state law and is properly a matter for the states to address. For example, a state law with the type of small employer exemption discussed above could require that an employer, once subject to the participation requirement, remains subject to it (either permanently or at least for the balance of the year or some other specified period of time), without regard to future fluctuations in workforce size. A state might also require an employer to maintain payroll deductions for employees who were enrolled when the employer was subject to the requirement, but not require the employer to make deductions for new employees until after its work force has regained the minimum number of employees. An employer that ceases to be subject to a state participation requirement, but that continues the payroll deductions or automatically enrolls new employees into the state program, would be acting outside the boundaries of the new safe harbor. However, its continued participation in the program would reflect its voluntary

³⁴ Cal. Gov't Code §100000(d) (2012); Conn. P.A. 16-29, § 1(7) (2016).

³⁵ 820 Ill. Comp. Stat. 80/5 (2015).

decision to provide retirement benefits pursuant to a particular plan, fund, or program. Accordingly, it would thereby establish or maintain an ERISA-covered plan.

Nevertheless, if the state allows but does not require an exempted small employer to enroll employees in the program, the employer may be able to do so without establishing an ERISA plan if the employer complies with the conditions of the Department's 1975 IRA Payroll Deduction Safe Harbor, which ensure minimal employer involvement in the employees' completely voluntary decision to participate in particular IRAs. To comply with these conditions, the employer would not be able to make payroll deductions for employees without their affirmative consent.

In the event that an employer establishes its own ERISA-covered plan under a state program, that plan would be subject to ERISA's reporting, disclosure, and fiduciary standards. In such circumstances, the employer generally would be considered the "plan sponsor" and "administrator" of its plan, as defined in section 3(16) of ERISA.³⁶ The Department would not, however, view the establishment of an ERISA plan by an employer participating in the state program as affecting the availability of the safe harbor for other participating employers.

E. Extending the Safe Harbor to Political Subdivisions

A number of commenters urged the Department to expand the safe harbor to cover payroll deduction savings programs established by political subdivisions of states.

³⁶ Commenters requested that this regulation provide a method for employers or states that inadvertently take actions causing an arrangement or program to fail to satisfy the safe harbor to cure that failure and qualify for the safe harbor. Commenters also requested that this regulation allow employers to cure ERISA failures that might result from the creation of an ERISA plan. Although these issues are beyond the scope of this regulation, if problems arise relating to these topics for particular state programs, the Department invites states and other interested persons to ask the Department to consider whether some additional guidance or relief would be appropriate.

The proposal was limited to payroll deduction savings programs established by “States.” For this purpose, the proposal defined the term “State” by reference to section 3(10) of ERISA. Section 3(10) of ERISA, in relevant part, defines the term “State” as including “any State of the United States, the District of Columbia, Puerto Rico, the Virgin Islands, American Samoa, Guam, [and] Wake Island.” Thus, the proposed safe harbor was not available to payroll deduction savings programs established by political subdivisions of states, such as cities and counties.

These commenters argued that the proposal would be of little or no use for employees of employers in political subdivisions in states that choose not to have a state-wide program, even though there is strong interest in a payroll deduction savings program at a political subdivision level, such as New York City, for example.³⁷ These commenters asked the Department to consider extending the safe harbor in the proposal essentially to large political subdivisions (in terms of population) with authority and capacity to maintain such programs.³⁸ Others, however, are concerned that such an expansion might lead to overlapping and possibly conflicting requirements on employers, both within and across states.

³⁷ See, e.g., Comment Letter #57 (The Public Advocate for the City of New York) (“The United States Department of Labor’s proposed rule reflects the Department’s clear understanding of the dire need for policymakers to develop retirement security solutions for millions of Americans. However, we are concerned that by not including cities in its proposed rule, in particular those with populations over a certain size – such as one million residents – the Department could significantly thwart the positive objectives of the proposed rule.”).

³⁸ See, e.g., Comment Letter #36 (AFL-CIO) (“With respect to political subdivisions of a state, we suggest the Department establish minimum eligibility requirements to ensure that the political entity has the administrative capacity and sophistication necessary to administer a retirement savings arrangement, protect the rights of participating workers, and ensure the security of workers’ payroll deductions and retirement savings. The Department could use easily measured proxies for administrative capacity and sophistication. For example, total population of a political subdivision as measured by the most recent decennial census or an interim population estimate published by the U.S. Census Bureau would be an appropriate proxy. The eligibility threshold could be set at or near the total population of the smallest of the 50 states, such as 500,000.”).

The Department agrees with commenters that there may be good reasons for expanding the safe harbor, but believes its analysis of the issue would benefit from additional public comments. Accordingly, in the Proposed Rules section of today's Federal Register, the Department published a notice of proposed rulemaking seeking to amend paragraph (h) of § 2510.3-2 to cover certain state political subdivision programs that otherwise comply with the conditions in the final rule. The proposal seeks public comment on not only whether, but also how to amend paragraph (h) of § 2510.3-2 to include political subdivisions of states. Commenters are encouraged to focus on how broadly or narrowly an amended safe harbor might define the term "qualified political subdivision" taking into account the impact of such an expansion on employers, employees, political subdivisions, and states themselves.³⁹

V. REGULATORY IMPACT ANALYSIS

A. Executive Order 12866 Statement

Under Executive Order 12866, the Office of Management and Budget (OMB) must determine whether a regulatory action is "significant" and therefore subject to the requirements of the Executive Order and subject to review by the OMB. Section 3(f) of the Executive Order defines a "significant regulatory action" as an action that is likely to result in a rule (1) having an annual effect on the economy of \$100 million or more, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or state, local or tribal governments or communities (also referred to as an "economically significant" action); (2) creating

³⁹ Some commenters asked whether states could join together in multi-state programs. Nothing in the safe harbor precludes states from agreeing to coordinate state programs or to act in unison with respect to a program.

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

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

Several states have adopted or are considering adopting state payroll deduction savings programs to increase access to retirement savings for individuals employed or residing in their jurisdictions. As stated above, this document amends existing Department regulations by adding a new safe harbor describing the circumstances under which such payroll deduction savings programs, including programs featuring automatic enrollment, would not give rise to the establishment or maintenance of ERISA-covered employee pension benefit plans. State payroll deduction savings programs that meet the requirements of the safe harbor would be established by states, and state law would require certain private-sector employers to participate in such programs. By making clear that state payroll deduction savings programs with automatic enrollment that conform to the safe harbor in the final rule do not give rise to the establishment of ERISA-covered plans, the objective of the safe harbor is to reduce the risk of such state programs being preempted if they were challenged.

In analyzing benefits and costs associated with this final rule, the Department focuses on the direct effects, which include both benefits and costs directly attributable to the rule. These benefits and costs are limited, because as stated above, the final rule merely establishes a safe harbor describing the circumstances under which such state payroll deduction savings programs would not give rise to ERISA-covered employee pension benefit plans. It does not require states to take any actions nor employers to provide any retirement savings programs to their employees.

The Department also addresses indirect effects associated with the rule, which include potential benefits and costs directly associated with the scope and provisions of the state laws creating the programs, and include the potential increase in retirement savings and potential cost burden imposed on covered employers to comply with the requirements of the state programs. Indirect effects vary by state depending on the scope and provisions of the state law, and by the degree to which the rule might influence state actions.

1. Direct Benefits

As discussed earlier in this preamble, some state legislatures have passed laws designed to expand workers' access to workplace savings arrangements, including states that have established state payroll deduction savings programs. Through automatic enrollment such programs encourage employees to establish IRAs funded by payroll deductions. As noted, California, Connecticut, Illinois, Maryland, and Oregon, for example, have adopted laws along these lines. In addition, some states are looking at ways to encourage employers to provide coverage under state-administered 401(k)-type

plans, while others have adopted or are considering approaches that combine several retirement alternatives including IRAs and ERISA-covered plans.

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

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

Some comments expressed concern about whether the safe harbor rule requires employers to participate in states’ savings arrangements, and whether it implicitly

indicates the Department's views on arrangements that do not fully conform to the conditions of the safe harbor. To address these concerns, the Department added regulatory text in the final rule explicitly recognizing that the regulation is a safe harbor and as such, does not require employers to participate in state payroll deduction savings programs or arrangements nor does it purport to define every possible program that could fall outside of Title I of ERISA.

2. *Direct Costs*

The final rule does not require any new action by employers or the states. It merely establishes a safe harbor describing certain circumstances under which state-required payroll deduction savings programs would not give rise to an ERISA-covered employee pension benefit plan. States may incur legal costs to analyze the rule and determine whether their laws fall within the final rule's safe harbor. However, the Department expects that these costs will be less than the costs that would be incurred in the absence of the final rule.

3. *Uncertainty*

The Department is confident that the final safe harbor rule, by clarifying that certain state payroll deduction savings programs do not require employers to establish ERISA-covered plans, will benefit states and many other stakeholders otherwise beset by greater uncertainty. However, the Department is unsure as to the magnitude of these benefits. The magnitude of the final rule's benefits, costs and transfer impacts will depend on the states' independent decisions on whether and how best to take advantage of the safe harbor and on the cost that otherwise would have attached to uncertainty about the legal status of the states' actions. The Department cannot predict what actions states

will take, stakeholders' propensity to challenge such actions' legal status, either absent or pursuant to the final rule, or courts' resultant decisions.

4. Indirect Effects of Safe Harbor Rule: Impact of State Initiatives

As discussed above, the impact of state payroll deduction saving programs is directly attributable to the state legislation that creates such programs. As discussed below, however, under certain circumstances, these effects could be indirectly attributable to the final rule. For example, it is conceivable that more states could create payroll deduction savings programs due to the guidelines provided in the final rule and the reduced risk of an ERISA preemption challenge, and therefore, the increased prevalence of such programs would be indirectly attributable to the final rule. If this issue were ultimately resolved in the courts, the courts could make a different preemption decision in the rule's presence than in its absence. Furthermore, even if a potential court decision would be the same with or without the rulemaking, the potential reduction in states' uncertainty-related costs could induce more states to pursue these workplace savings initiatives. An additional possibility is that the rule would not change the prevalence of state payroll deduction savings programs, but would accelerate the implementation of programs that would exist anyway. With any of these possibilities, there would be benefits, costs and transfer impacts that are indirectly attributable to this rule, via the increased or accelerated creation of state programs.

Commenters expressed concern that states will incur substantial costs to implement their payroll deduction savings programs. One state estimates that it will

incur \$1.2 million in administrative and operating costs during the initial start-up years.⁴⁰ To administer its opt-out process, the same state estimates it will incur \$465,000 in one-time mailing and form production costs.⁴¹ Another state estimated that it will take several years before its savings arrangement becomes self-sufficient and it would require a subsidy of between \$300,000 and \$500,000 a year for five to seven years.⁴² Commenters also raised concerns about the states' potential fiduciary liability associated with establishing state payroll deduction savings programs.

The Department is aware of these potential costs, and although the commenters raise valid concerns, the costs are not directly attributable to the final rule; they are attributable to the state legislation creating the payroll deduction savings program. In enacting their programs, states are responsible for estimating the associated costs during the legislative process and determining whether the arrangement is self-sustainable and whether the state has sufficient resources to bear the associated costs and financial risk. States can design their programs to address these concerns, and presumably, will enact state payroll deduction legislation only after determining that the benefits of such programs justify their costs.

Employers may incur costs to update their payroll systems to transmit payroll deductions to the state or its agent, develop recordkeeping systems to document their collection and remittance of payments under the program, and provide information to employees regarding the state savings arrangement. As with states' operational and administrative costs, some portion of these employer costs would be indirectly

⁴⁰ Department of Finance Bill Analysis, California Department of Finance (May 2, 2012).

⁴¹ Id.

⁴² Voluntary Employee Accounts Program Study, Maryland Supplemental Requirement Plans (2008).

attributable to the rule if more state payroll deduction savings programs are implemented in the rule's presence than would be in its absence. Because the employers' administrative burden to participate in the state program is generally limited to withholding the required contribution from employees' wages, remitting contributions to the state program, and providing information about the program to employees in order to satisfy the safe harbor, most associated costs for employers would be minimal.

Although such costs would be limited for employers, several commenters expressed concern that these costs would be incurred disproportionately by small employers and start-up companies, which tend to be least likely to offer pensions. According to one survey submitted with a comment, about 60% of small employers do not use a payroll service.⁴³ The commenters assert that these small employers may incur additional costs to use external payroll companies to comply with their states' payroll deduction savings programs. However, some small employers may decide to use a payroll service to withhold and remit payroll taxes independent of their state's program requirements. Therefore, the extent to which these costs can be attributable to states' initiatives could be smaller than what commenters estimated. Moreover, most state payroll deduction savings programs exempt the smallest companies,⁴⁴ which could mitigate such costs.

⁴³ National Small Business Association, April 11, 2013, "2013 Small Business Taxation Survey." This survey says 23% of small employers that handle payroll taxes internally have no employee. Therefore, only about 46%, not 60%, of small employers are in fact affected by state initiatives, based on this survey. The survey does not include small employers that use payroll software or on-line payroll programs, which provide a cost effective means for such employers to comply with payroll deduction savings programs.

⁴⁴ For example, California Secure Choice would affect employers with 5 or more employees, Illinois Secure Choice would affect employers with 25 or more employees, and Connecticut Retirement Security would affect employers with 5 or more employees. Cal. Gov.t Code §100000(d) (2012); 820 Ill. Comp. Stat. 80/5 (2015); Conn. P.A. 16-29 § 1(7) (2016).

Additional cost-related comments addressed penalties that employers are subject to pay if they fail to comply with the requirements of their states' programs.⁴⁵ The commenter argued that those penalties would be more detrimental to small employers because profit margins of small employers are often very thin. However, the costs associated with those penalties are due to a failure to comply with state law. In addition, the final rule accommodates commenters and allows states to use tax incentives or credits as long as their economic incentives are narrowly tailored to reimbursing the costs of states' payroll deduction savings programs. If states reimburse employers for costs incurred to comply with their payroll deduction savings programs, the employers' cost burden can be substantially reduced.

While several comments focused on the cost burden imposed on small employers, an organization representing small employers expressed support for state efforts to establish state payroll deduction savings arrangements, because such arrangements provide a convenient and affordable option for small businesses and their employees to save for retirement. This commenter further states that small business owners want to offer the benefit of retirement savings to their employees because it would help them attract and retain talented employees.

The Department believes that well-designed state-level initiatives have the potential to effectively reduce gaps in retirement security. Relevant variables such as

⁴⁵ For example, according to a comment letter, the Illinois Secure Choice Savings Program allows for a penalty for noncompliance in the first year of \$250 per employee per year, which then increases to \$500 for noncompliance per employee for each subsequent year.

pension coverage,⁴⁶ labor market conditions,⁴⁷ population demographics,⁴⁸ and elderly poverty,⁴⁹ vary widely across the states, suggesting a potential opportunity for progress at the state level. Many workers throughout these states currently may save less than would be optimal because of (1) behavioral biases (such as myopia or inertia), (2) labor market conditions that prevent them from accessing plans at work, or (3) they work for employers that simply do not offer retirement plans.⁵⁰ Some research suggests that automatic contribution policies are effective in increasing retirement savings and wealth in general by overcoming behavioral biases or inertia.⁵¹ Well-designed state initiatives could help many savers who otherwise might not be saving enough or at all to begin to save earlier than they might have otherwise. Such workers will have traded some consumption today for more in retirement, potentially reaping net gains in overall lifetime well-being. Their additional savings may also reduce fiscal pressure on publicly financed retirement programs and other public assistance programs, such as the Supplemental Nutritional Assistance Program, that support low-income Americans, including older Americans.

⁴⁶ See, e.g., Craig Copeland, “Employment-Based Retirement Plan Participation: Geographic Differences and Trends, 2013,” Employee Benefit Research Institute, Issue Brief No. 405 (October 2014) (available at www.ebri.org). See also a report from the Pew Charitable Trusts, “How States Are Working to Address The Retirement Savings Challenge,” (June 2016).

⁴⁷ See, e.g., US Bureau of Labor Statistics, “Regional and State Employment and Unemployment—JUNE 2015,” USDL–15–1430 (July 21, 2015).

⁴⁸ See, e.g., Lindsay M. Howden and Julie A. Meyer, “Age and Sex Composition: 2010,” US Bureau of the Census, 2010 Census Briefs C2010BR–03 (May 2011).

⁴⁹ Constantijn W. A. Panis & Michael Brien, “Target Populations of State-Level Automatic IRA Initiatives,” (August 28, 2015).

⁵⁰ According to National Compensation Survey, March 2015, about 69% of private-sector workers have access to retirement benefits – including Defined Benefit and Defined Contribution plans - at work.

⁵¹ See Chetty, Friedman, Leth-Petresen, Nielsen & Olsen, “Active vs. Passive Decisions and Crowd-out in Retirement Savings Accounts: Evidence from Denmark,” 129 *Quarterly Journal of Economics* 1141-1219 (2014); See also Madrian and Shea, “The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior,” 116 *Quarterly Journal of Economics* 1149-1187 (2001).

However, several commenters were skeptical about potential benefits of state payroll deduction savings arrangements. These commenters believe the potential benefits – primarily increases in retirement savings – would be limited because the proposed safe harbor rule does not allow employer contributions to state payroll deduction programs.

The Department believes that well-designed state initiatives can achieve their intended, positive effects of fostering retirement security. However, the initiatives might have some unintended consequences as well. Those workers least equipped to make good retirement savings decisions arguably stand to benefit most from state initiatives, but also arguably could be at greater risk of suffering adverse unintended effects. Workers who would not benefit from increased retirement savings could opt out, but some might fail to do so. Such workers might increase their savings too much, unduly sacrificing current economic needs. Consequently they might be more likely to cash out early and suffer tax losses (unless they receive a non-taxable Roth IRA distribution), and/or to take on more expensive debt to pay necessary bills. Similarly, state initiatives directed at workers who do not currently participate in workplace savings arrangements may be imperfectly targeted to address gaps in retirement security. For example, some college students might be better advised to take less in student loans rather than open an IRA, and some young families might do well to save more first for their children's education and later for their own retirement. This concern was shared by some commenters who stated that workers without retirement plan coverage tend to be younger, lower-income or less attached to the workforce, which implies that these workers are often financially stressed or have other savings goals. These comments imply that the benefits of state payroll deduction savings arrangements could be limited

and in some cases potentially harmful for certain workers. The Department notes that the states are responsible for designing effective programs that minimize these types of harm and maximize benefits to participants.

Some commenters also raised the concern that state initiatives may “crowd-out” ERISA-covered plans. According to one comment, the proposed rule could inadvertently encourage large employers operating in multiple states to switch from ERISA-covered plans to state-run arrangements in order to reduce costs, especially if they are required to cover employees currently ineligible to participate in ERISA-covered plans under state-run arrangements. Some commenters were concerned about employers’ burden to monitor their obligations under the state laws particularly when employers operate in multiple states. These commenters raised the possibility that large employers would incur substantial costs to monitor the participation status of ineligible workers, such as part-time or seasonal workers. The final rule clarifies that state payroll deduction savings programs directed toward employers that do not offer other retirement plans fall within this safe harbor rule. However, employers that wish to provide retirement benefits are likely to find that ERISA-covered programs, such as 401(k) plans, have advantages for them and their employees over participation in state programs. Potential advantages include significantly greater tax preferences, greater flexibility in plan selection and design, opportunity for employers to contribute, ERISA protections, and larger positive recruitment and retention effects. Therefore it seems unlikely that state initiatives will “crowd-out” many ERISA-covered plans, although, if they do, some workers might lose ERISA-protected benefits that could have been more generous and more secure than

state-based (IRA) benefits if states do not adopt consumer protections similar to those Congress provided under ERISA.

There is also the possibility that some workers who would otherwise have saved more might reduce their savings to the low, default levels associated with some state programs. States can address this concern by incorporating into their programs participant education or “auto-escalation” features that increase default contribution rates over time and/or as pay increases.

Some commenters were concerned that state payroll deduction savings arrangements would in general provide participants with less consumer protection than ERISA-covered plans. Another commenter pointed out that one particular state’s payroll deduction savings program would require employees to pay higher fees than those charged to private plans.⁵² However, a careful review of the report cited in this comment suggests that fees set by this particular state’s arrangement are not inconsistent with the average fees in the mutual fund industry.⁵³ Moreover, the Department reiterates that states enacting savings arrangements can take actions to augment consumer protections.

B. Paperwork Reduction Act

In accordance with the requirements of the Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3506(c)(2)), the Department solicited comments regarding its determination that the proposed rule is not subject to the requirements of the PRA,

⁵² According to a comment letter, Illinois’ Secure Choice Savings Program stated that the costs of fees paid by employees will be charged up to 0.75 percent of the overall balances, which is higher than those charged to 401(k) plan participants who invested in equity mutual funds (0.58 percent).

⁵³ According to the ICI Research Perspective, “The Economics of Providing 401(k) Plans: Services, Fees, and Expenses, 2014,” the mutual fund industry average expense ratio was 0.74 percent in 2013 and in 0.70 percent in 2014, which are in the comparable range to the Illinois Secure Choice Savings Program’s ceiling in fees, 0.75 percent.

because it does not contain a “collection of information” as defined in 44 U.S.C. 3502(3). The Department's conclusion was based on the premise that the proposed rule did not require any action by or impose any requirements on employers or states. It merely clarified that certain state payroll deduction savings programs that encourage retirement savings would not result in the creation of ERISA- covered employee benefit plans if the conditions of the safe harbor were met.

The Department did not receive any comments regarding this assessment. Therefore, the Department has determined that the final rule is not subject to the PRA, because it does not contain a collection of information. The PRA definition of “burden” excludes time, effort, and financial resources necessary to comply with a collection of information that would be incurred by respondents in the normal course of their activities. See 5 CFR 1320.3(b)(2). The definition of “burden” also excludes burdens imposed by a state, local, or tribal government independent of a Federal requirement. See 5 CFR 1320.3(b)(3). The final rule imposes no burden on employers because states customarily include notice and recordkeeping requirements when enacting their payroll deduction savings programs. Thus, employers participating in such programs are responding to state, not Federal, requirements.

C. Regulatory Flexibility Act

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) (RFA) imposes certain requirements with respect to Federal rules that are subject to the notice and comment requirements of section 553(b) of the Administrative Procedure Act (5 U.S.C. 551 *et seq.*) and which are likely to have a significant economic impact on a substantial number of small entities. Unless an agency certifies that a rule will not have a significant

economic impact on a substantial number of small entities, section 603 of the RFA requires the agency to present an initial regulatory flexibility analysis at the time of the publication of the notice of proposed rulemaking describing the impact of the rule on small entities. Small entities include small businesses, organizations and governmental jurisdictions.

Although several commenters maintained that the proposed rule would impose significant costs on small employers, similar to the proposal, the final rule merely establishes a new safe harbor describing circumstances in which state payroll deduction savings programs would not give rise to ERISA-covered employee pension benefit plans. Therefore, the final rule imposes no requirements or costs on small employers, and the Department believes that it will not have a significant economic impact on a substantial number of small entities. Accordingly, pursuant to section 605(b) of the RFA, the Assistant Secretary of the Employee Benefits Security Administration hereby certifies that the final rule will not have a significant economic impact on a substantial number of small entities.

D. Unfunded Mandates Reform Act

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

E. Congressional Review Act

The final rule is subject to the Congressional Review Act provisions of the Small Business Regulatory Enforcement Fairness Act of 1996 (5 U.S.C. 801 *et seq.*) and will be transmitted to Congress and the Comptroller General for review. The final rule is not a "major rule" as that term is defined in 5 U.S.C. 804, because it is not likely to result in (1) an annual effect on the economy of \$100 million or more; (2) a major increase in costs or prices for consumers, individual industries, or Federal, State, or local government agencies, or geographic regions; or (3) significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of United States-based enterprises to compete with foreign-based enterprises in domestic and export markets.

F. Federalism Statement

Executive Order 13132 outlines fundamental principles of federalism. It also requires adherence to specific criteria and requirements, such as consultation with state and local officials, in the case of policies that have federalism implications, defined as “regulations, legislative comments or proposed legislation, and other policy statements or actions that have substantial direct effects on the states, on the relationship between the national government and states, or on the distribution of power and responsibilities among the various levels of government.”

The final rule describes circumstances under which a state payroll deduction savings program would not constitute the establishment or maintenance of an ERISA-covered plan by specified actors. Such guidance may therefore be helpful to states that have taken or might take action, but the safe harbor does not limit the actions that states could take. The safe harbor does not require states to do anything or preempt state law.

Nor does it act directly on a state, or cause any state to do anything the state had not already decided or is inclined to do on its own. For example, as described elsewhere in this final rule, a state program that fell outside the terms of the safe harbor would not necessarily result in the creation of ERISA plans. The regulation itself is devoid of consequences to the state or states that decide not to follow its terms. In other words, the regulation may indirectly influence how states design their payroll deduction savings programs, but its existence is unlikely to be dispositive on whether states adopt programs in the first instance, as evidenced by some states that already enacted legislation. Therefore, the final rule does not contain policies with federalism implications within the meaning of the Order.

Nonetheless, in respect for the fundamental federalism principles set forth in the Order, the Department affirmatively engaged in outreach with officials of states, and with employers and other stakeholders, regarding the proposed rule and sought their input on any federalism implications that they believe may be presented by the safe harbor. Departmental staff engaged in numerous meetings, conference calls, and outreach events with interested stakeholders on the proposed rule and on various state legislative proposals. The Department also received numerous comment letters from states and local governments and their representatives. Many of the changes in the final rule stem from suggestions contained in these comment letters. Indeed, the notice of proposed rulemaking on political subdivisions discussed earlier in this preamble also stems from comments and concerns raised by state or local governments.

List of Subjects in 29 CFR Part 2510

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

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

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

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

AUTHORITY: 29 U.S.C. 1002(2), 1002(21), 1002(37), 1002(38), 1002(40), 1031, and 1135; Secretary of Labor's Order No. 1-2011, 77 FR 1088 (Jan. 9, 2012); Sec. 2510.3-101 also issued under sec. 102 of Reorganization Plan No. 4 of 1978, 5 U.S.C. App. at 237 (2012), E.O. 12108, 44 FR 1065 (Jan. 3, 1979) and 29 U.S.C. 1135 note. Sec. 2510.3-38 is also issued under sec. 1, Pub. L. 105-72, 111 Stat. 1457 (1997).

2. Revise § 2510.3-2 (a) to read as follows:

§ 2510.3-2 Employee pension benefit plans

(a) General. This section clarifies the terms “employee pension benefit plan” and “pension plan” for purposes of title I of the Act and this chapter by setting forth safe harbors under which certain specific plans, funds and programs would not constitute employee pension benefit plans when the conditions of this section are satisfied. The safe harbors in this section should not be read as implicitly indicating the Department’s views on the possible scope of section 3(2). To the extent that these plans, funds and programs constitute employee welfare benefit plans within the meaning of section 3(1) of

the Act and §2510.3-1 of this part, they will be covered under title I; however, they will not be subject to parts 2 and 3 of title I of the Act.

3. In § 2510.3-2, add new paragraph (h) to read as follows:

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

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

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

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

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

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

(vi) All rights of the employee, former employee, or beneficiary under the program are enforceable only by the employee, former employee, or beneficiary, an authorized representative of such a person, or by the State (or governmental agency or instrumentality of the State);

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

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

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

(C) Providing information to the State (or governmental agency or instrumentality of the State) necessary to facilitate the operation of the program; and

(D) Distributing program information to employees from the State (or governmental agency or instrumentality of the State) and permitting the State (or governmental agency or instrumentality of the State) to publicize the program to employees;

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

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

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

(xi) The employer receives no direct or indirect consideration in the form of cash or otherwise, other than consideration (including tax incentives and credits) received directly from the State (or governmental agency or instrumentality of the State) that does not exceed an amount that reasonably approximates the employer's (or a typical employer's) costs under the program.

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

(i) Is directed toward those employers that do not offer some other workplace savings arrangement;

(ii) Utilizes one or more service or investment providers to operate and administer the program, provided that the State (or governmental agency or instrumentality of the State) retains full responsibility for the operation and administration of the program; or

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

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

Signed at Washington, DC, this 24th day of August, 2016.

Phyllis C. Borzi,

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

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