March 10, 2016

California Secure Choice Investment Board
915 Capitol Mall, Room 110
Sacramento, CA 95814

SUBJECT: Public comment on final Report to the Secure Choice Retirement Program prepared by Overture Financial LLC

Dear Chairman Chiang and Board members.

During the legislative process of Senate Bill 1234 (Chapter 734, 2012), the authorizing statute enacting the California Secure Choice Retirement Savings Program, the employer community expressed significant concerns with the proposed plan. Although we ultimately removed our opposition, we did so to allow a feasibility study to be conducted to fully explore our concerns regarding the implementation and operation of the program. This study has been completed by Overture, and this letter both represents our comments on the findings contained in their report (report) and expresses our coalition's remaining concerns with the recommendations for implementing the program.

The Secure Choice program must be easy for employees and employers to understand, easy to implement and easy to comply with its requirements. Employers must not be exposed to risks for employee assets or investment choices and must not face traps that could cause inadvertent liability. The coalition finds that the report oversimplifies the processes and procedures that employers will be required to complete, makes assumptions that may or may not materialize regarding the recordkeeper function under the direct service model, and fails to adequately and completely identify and address risks and liabilities for employers.

Furthermore, the coalition must note that our requests to Overture to discuss our concerns directly with them went unanswered, and the concerns that were communicated to the board through public comment and letters were neither adequately raised nor addressed in the report. For example, employer groups assert that the statement on page 102 indicating input was sought from stakeholders is not fully accurate. While one phone call from the consultant was had with two employer group representatives that are members of this coalition, broader input was not sought from equally impacted business groups.

Following are a number of concerns raised by our employer community coalition regarding risk and program administration that we urge the board to address, and reflect in the final program design.

Federal Law Impact

ERISA Applicability. Because one of the employer community's primary concerns during the legislative process was with the application of ERISA both to the plan and employers, SB 1234 explicitly acknowledges these risks and was amended to reflect that further study and assurance were required. The law states as follows:

100043. The board shall not implement the program if the IRA arrangements offered fail to qualify for the favorable federal income tax treatment ordinarily accorded to IRAs under the Internal Revenue Code, or if it is determined that the program is an employee benefit plan under the federal Employee Retirement Income Security Act.

The coalition has significant concerns with the inadequate attention given by the report to ERISA and to program compliance with the DOL regulations, as proposed or otherwise. Given that the enabling legislation prohibited the implementation of the program if ERISA applies, the analysis is incomplete.

Further, the report states on page 49 that only two organizations were concerned about potential liabilities to employers related to ERISA and asserts that employers have merely four concerns, not one of which is the concern regarding ERISA liability. We are concerned that the ERISA risks were not accurately attributed to employer stakeholders perhaps because Overture has assumed that the DOL will provide airtight protection on this matter to employers. Therefore, we find it disingenuous to say that because only two employer organizations were acknowledged as having concerns, since all employers will share the risk, and conclude that this concern was not given its due significance and attention, especially in light of DOL's admission that their safe harbor may in fact not provide complete security from risk and liability, as discussed above. The report merely acknowledges this as an "other issue" for the board to consider (page 50), but the report does not provide any guidance or recommendations regarding the issue.

Proposed DOL Regulation. While the program has not been determined to be "…*an employee benefit plan under the federal Employee Retirement Income Security Act,"* it also has not been determined that the program is not nor will not be subject to ERISA. Although the federal Department of Labor (DOL) has proposed draft regulation to "reduce the risk of state programs being preempted," the DOL admits that the ultimate determination rests with the courts.

In fact, there is a risk of increased legal liability for employers that the guidance does not address. An employee or class action suit could challenge the safe harbor definition under this proposal and claim that the employers are subject to ERISA. If a violation of ERISA is found, the employers will have been unwittingly subjected to this increased liability without any recourse against the state or the DOL. Furthermore, it is unclear that if a determination of ERISA pre-emption is found if it would be applicable to the entire program or to the specified employer(s).

Additionally, what would happen if some ineligible employers intentionally or inadvertently "sneak" into the program and auto-enroll their employees, or if legitimate employers maintain enrollment when their employee count drops below the mandated threshold. While we understand this may be a desirable outcome for the board, the proposed safe harbor suggests that such non-mandated employers could cause an entire program to fail the safe harbor and become an ERISA plan, with potentially disastrous consequences for the thousands of participating employers and millions of employees. the state cannot fully vet all participating employers for eligibility and continue to keep operating costs to a minimum.

Importantly, the proposed regulation does not include clear detail that specifies what the "ministerial duties" are on the part of employers in order to make sure employers clearly understand their limited duties and do not inadvertently become subject to ERISA and the requirements there under. Our coalition is very concerned that if the state follows the guidance but an employer inadvertently provides

more than ministerial duties, it could put all employers in the position of being covered under ERISA and at risk of legal liability.

Employer Outreach and Education

Key to the success of the program is the full participation by eligible employers, which will require extensive outreach and education in advance of implementation. Furthermore, employer understanding of the all the nuances of the program and the role of the employer is essential in order to facilitate a satisfactory experience for the employee. This program component is not given adequate attention in the report, while employee outreach and employee protections are given significant weight.

Integral to the success of the program is employers' ability to adequately understand the program rules and procedures, including a complete understanding of their "*ministerial*" responsibilities. Success also depends on employers' ability to understand and prevent exposure to ERISA and other liabilities, including how to safely interact with employees in accordance with DOL's guidance (which has not yet been provided in the proposed DOL regulation or in the report recommendations). Given the potential for significant risk to employers and the program, the coalition urges the board to require extensive, immediate and ongoing comprehensive education and training for employers prior to any program activities on the part of the employer, including prior to beginning employee enrollment.

For the protection of the employer and the employee, as well as to facilitate enrollment and satisfaction with the program experience, it is essential that employers have a website and hotline available 24/7 for customer service. Ready access to information will decrease employer's chance of mistakes. Keep in mind that small businesses in particular tend to work long hours, handling administrative duties after normal working hours. To minimize business disruption, access to specialists must be available during extended hours.

The coalition recommends that the board be clear about the specific dynamics used in calculating the cost of employer outreach, and on how this expense will be covered. Materials must be designed, printed, distributed, posted to websites and updated regularly. The diversity of industries and employer size may require differing approaches and materials. The coalition strongly encourages officials to make in person as well as webcast presentations to employer groups. Consequently, there will be significant costs involved. In reviewing the report, we do not see how this cost is addressed, and leaves us with questions. Have these costs been included in program start up estimates? Is it part of the administrative costs? Will employers and employer associations be expected to bear any costs of outreach? Have the associations indicated in the report been contacted to discuss this outreach as recommended in the report? If EDD is to assume costs, is that included in the administrative costs of the program – the 1 percent charged directly to the program? If it is not, where will the money come from – General Fund, employers, investors, vendors?

Employee Outreach

The report recommends a concerted, aggressive public education campaign focused on workers and small businesses. We agree this outreach and education of employees is very important. Employee access to information is also critical to the success of the program. The more education and access the employees have, the greater the chance to eliminate the provision of information, counsel and advice by the employer. In order to protect employers – employees must be completely informed.

Given the lack of investment sophistication of the program's targeted population as identified by the study, employees must have easily understandable and readily accessible information that covers all

aspects of the program including the fundamentals of process, procedure and investment risk and reward. Information must be easily and consistently accessible, especially in-person – either face to face or via telephone access. Key recommendations of the report omit (or downplay) the key financial education that employees will require, and instead focuses on granting employees with enforcement and compliance powers targeted at the employer.

Rules and Procedures

Regardless of how simple the report insists the process will be for employers, there are many steps and rules the employers must understand and follow. The rules and procedures recommendations fail to acknowledge and address the complexities of the employer duties, responsibilities, and risks. Furthermore, the report fails to specify what the employer's "ministerial duties" are limited to, leaving employers at risk of ERISA pre-emption. Below are just a few of the many concerns the coalition has regarding rules and procedures that are not enumerated.

- **Employer Eligibility**. The terms "firm" and "establishment" that are proposed for determining employer eligibility requires more specific definition in order to avoid confusion and liability.

- **Employment Intermediaries**. The report suggests that these intermediaries be responsible for compliance. This recommendation requires more detail and a discussion of its underlying assumptions, for example, in the context of professional employer associations.

- **Employer/Employee Interaction**. Interaction about the program must be limited between employers and employees in order for employers to prevent risk and liability under ERISA, and any other laws that may pertain. Employers need specific instructions. The report fails to acknowledge and address these rules.

- **Enrollment Process**. The report fails to adequately address the issue of ineligible employers (as defined in the proposed DOL rules for the safe harbor from ERISA) participating in the program.

- **Signature Requirement**. The report recommends a signature from the employee acknowledging receipt of program information and then retention of those records. Will the employer be required to collect these signatures and maintain the documentation? What happens if an employee does not sign?

- **Employer Customer Service**. Employers must have access to not only online assistance, but readily accessible in person assistance by telephone.

- **Hidden Burdens and Costs**. The operational model in the report (page 92) states "processing volumes should be spread evenly over the period (e.g. no month-end, quarter-end spikes). The report does not consider that most employers process at month-end and quarter-end. Changing their process calendar could be a major administrative burden. If in fact the recommended model requires employers to add administrative processing at a different time than other administrative processes, this needs to be considered and thoroughly addressed from a feasibility and cost perspective. Adding a payroll processing function each month could also trigger new costs in addition to the administrative burden.

- **Employer Audit**. Operational model features (page 99) show that EDD will audit employer eligibility. What does this mean? How is this paid for?

Enforcement against employers

The coalition has serious concerns regarding the enforcement component. This provision has not been made clear enough. It is our understanding that discussions have occurred with the Department of Industrial Relations (DIR) and their ability to address enforcement against employers. A primary concern for California employers is that additional enforcement functions for DIR will require an increase in assessments on employers since the Department is supported by a fee on employers.

Further, it is imperative that enforcement policies differentiate between employers who make technical, inadvertent mistakes due to a misunderstanding or lack of awareness, and those who have not enrolled employees, and those who purposefully violate the program rules and engage in practices such as wage theft. Those employers that do make procedural mistakes should be given time to correct those errors prior to any enforcement action. We also urge the board to consider delaying any enforcement against employers until such time that all eligible employers have transitioned into the program and have been fully educated about their role and responsibility under the program.

Roth IRA vs. Traditional IRA

While the report insists that the number of participants potentially ineligible for a Roth IRA is "small," based on the report's projections, that number exceeds a half a million participants (8 percent of participants) – not an insignificant population. The recommendations require participants to be responsible for tracking contribution limits to a Roth IRA in relation to their income. We point to this target population as significant and the implications to them and their employers deserve more attention.

The coalition is concerned that the employee has a tremendous responsibility to track their eligibility for the proper investment vehicle. It is imperative that the employee be informed of how to determine and maintain their eligibility for a Roth IRA, and how to switch to a traditional IRA. In such a circumstance, the employee will almost certainly approach the employer (if they even know there is a potential for ineligibility) to help them figure out their eligibility. It will not only be those employees that are possibly ineligible, but other employees who seek to know if they are or are not eligible. The report recommends that the employee be responsible for identifying which IRA they are eligible for, and then to track their contributions. All operational aspects of this uncertainty must be specific and eliminate risk and liability for the employer particularly under ERISA.

The feasibility study indicates that the target population for the program has limited financial literacy which adds to the complexity of this feature. The eligibility requirements for one IRA versus another are complex. The assertion that a target participant will be financially literate enough to know if they are eligible or not for a Roth IRA is absurd. The understanding of eligibility and the selection of the appropriate investment vehicle by participants is severely under –rated by the report.

Recordkeeper concerns

Throughout the report, the recordkeeper is assumed or hoped to be capable of a variety of operations, excerpt below:

"Recordkeeping is the central operational function of a retirement plan and as such represents the largest administrative cost component. The recordkeeper is responsible for managing the day-to-day

operations of the plan including the maintenance of individual accounts and keeping track of transactions and assets at the individual participant account level. A recordkeeper is also responsible for enrolling participants, tracking participant contribution rates and investment selections, providing account statements, maintaining the plan website and providing general support to participants and plan sponsors/employers."

The coalition prefers an operational model that provides as much separation as possible between the employer and the participation and investment decisions of the employee, and that limits the employer's role to distributing program marketing materials to employees and processing their payroll contributions. However, the coalition is concerned that the recordkeeper role described in the report with the capability to process the anticipated number of participants may not exist or materialize, and that the cost of the record keeper function may be under-estimated. In the absence of a recordkeeper performing these functions, the employer functions are not enumerated and analyzed. It is important to understand the risks and implications in the event that one or more of these functions are not available from a recordkeeper.

Overture themselves state (page 92) "…new technology solutions coming to market" are needed to make their recordkeeping scheme work.

Furthermore, the recordkeeper verification of employee social security numbers and identity after receiving it from the employer, then having to contact the employee directly in the event of errors has potentially significant privacy implications, and potential Patriot Act implications.

Multiple statements in the report assume the recordkeeper will manage auto-escalation. What specifically does this mean? Is it anticipated that the recordkeeper will notify the employer or the payroll service when to increase contributions? The employer still would need to track and account for changes in payroll deductions. This is an administrative burden not adequately addressed by the report.

The report further recommends the direct service model with a recordkeeper and that the program hire a consultant to draft the RFP, run the RFP process and oversee the implementation of the operational model. How have these costs been accounted for in the start up costs?

Risk and Liability

An analysis of any risks to the program and their potential consequences, and how to minimize or prevent them is not part of the report. Many questions remain unanswered regarding potential risks and threats, and how potential problems could be addressed, such as:

- In the event of lost contribution and late contributions, who is responsible for any lost income by the participant? Who owes the money to the participant? What happens if year-end reconciliations are not accurate-if deductions do not equal contributions, either to the positive or negative?

- Are there legal requirements regarding the time lapse between the payroll deduction and the deposit into the investment account? Can these time lines be met? If not, what are the consequences? Who is responsible?

- Are there security and investment laws – state or federal - that govern the program that employers and the board are subject to and need to be aware of?

- Are there any privacy rules that employers need to be aware of and comply with?
- In the event the program is not self sustaining as anticipated, who is responsible for any shortfall?
- What are the risks to the General Fund, to the program, to the board and to the investors? What if the program is not self-sustaining?
- Should ERISA-like protections be afforded participants in this program? If so, which ones should be adopted into or eliminated from this program?
- What recourse do employers have if the "safe harbor" guideline are struck down by the courts or overruled by legislation from Congress? Will they be held harmless? What will happen to participants' contributions?
- If one employer, or a group of employers, are found to be preempted by ERISA as a result of doing what they were told was required for compliance and acceptable under this program, is the entire statewide program preempted? For example, if one or more employers fail to remit some contributions, or fail to maintain adequate records, does such noncompliance result in the state program becoming an ERISA-covered plan? Or, would that result in the non-compliant employer(s) having established an ERISA-covered plan? What is the liability of the board or the state under this scenario?
- Do any other options for retirement saving exist in the marketplace that would be less risky, less costly and would provide greater protections and better retirement security for employees?

Cost to Employers

In contrast to simplistic model portrayed in the report, the coalition has identified many decision and tracking points for employers, all of which not only create cost, but also potential liability for mistakes and lawsuits. Many of these concerns have been previously communicated to the board in written comments (September 21, 2015). Some of those concerns are repeated here, as they are not addressed in the report and we urge the board to consider them in their recommendations to the Legislature.

Employers will be tasked with calculating and verifying payroll deduction amounts that will be different for most employees. Some are likely to be fixed amounts, others based on various percentages of wages. As we understand it, the report recommends that the employee be able to revise their contribution amount to any amount, at any time. If there is a recordkeeper that acts as intermediary as proposed between employer and employee, the recordkeeper will be transmitting information to the employer on a regular basis that the employer must document and act upon, such as changes to contributions, opting in and opting out. This could be quite an administrative burden for employers, even employers with few employees. The coalition is concerned that the many moving parts of tracking and remitting payroll contributions could result in mistakes, and that those mistakes could wind up being costly for employers in terms of enforcement penalties, and could potentially result in exposure to legal liabilities.

The report states that several employers noted that the cost of compliance would be absorbed by employers as a normal cost of doing business. However, the cost of compliance was not disclosed and is still not known so this statement has no basis. We urge the board not to assume that this cost to employers is absorbable.

Conclusion

In conclusion, the coalition thanks the board for the opportunity to share our comments regarding the Secure Choice report prepared by Overture. While we appreciate Overture's insights and work to establish feasibility and to conduct the market analysis, we respectfully suggest that more study and analysis must be completed before any action should move forward. We have enumerated some of the points where the report falls short of providing the complete information the coalition believes the board needs to make informed decisions regarding the risk, liability and administrative functions required by employers in order to implement the program.

The coalition also notes that simple, cost effective private market solutions may be available and yet have not been explored. Perhaps there is a better path to addressing the "retirement crisis."

To discuss our comments in further detail, please contact Marti Fisher, California Chamber of Commerce (916)444-6670, or Nicole Rice, California Manufacturers and Technology Association, (916) 498-3322.

Respectfully,

California Chamber of Commerce
California Manufacturers & Technology Association
Allied Managed Care and Acclamation Insurance Management Services
Associated Builders and Contractors of California
California Building Industry Association
California Business Roundtable
California Chapter American Fence Contractors
California Construction and Industrial Materials Association
California Farm Bureau Federation
California Fence Contractors
California Framing Contractors Association
California Professional Association of Specialty Contractors
California Retailers Association
California Restaurant Association
Conejo Valley Chamber of Commerce
Flasher Barricade
National Association of Independent Business
National Association of Professional Employer Organizations
North Orange County Chamber of Commerce
United Chambers of Commerce
Western Manufactured Housing Communities Association

C: Christina Elliott, Executive Officer