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California State Senate

SENATOR
KEVIN DE LEÓN
TWENTY-SECOND SENATE DISTRICT

SB 1234 (De León-Steinberg) California Secure Choice Retirement Savings Program

PURPOSE:

Create a supplemental retirement savings program for California's private sector workers that do not have access to retirement plans through their jobs. The California Secure Choice Retirement Savings Program would provide a reliable, affordable, and completely portable retirement savings opportunity for the millions of Californians without a workplace retirement plan.

BACKGROUND:

<u>Retirement Insecurity: Californians at Risk</u>

Across the United States, millions of workers will retire into poverty because they will not have enough in assets to meet their basic needs in their senior years. Here in California, nearly one-half of workers will face significant economic hardship in retirement, with incomes below 200% of the federal poverty threshold. The most at-risk groups are young workers age 25-44 and low-income workers, but even middle-income workers will be at substantial risk of not having enough retirement income to be self-sufficient.

Since the nation's personal savings rate is extremely low and retirement planning is now largely controlled by private for-profit Wall Street investment firms, the United States is staring at an economic time bomb that left unaddressed will overwhelm taxpayer-funded entitlement and other safety net programs. The lack of retirement savings affects all Californians, as seniors without sufficient retirement savings will more likely need to rely on government assistance for housing, health care and other basic necessities.

According to a recent report by the UC Berkeley Center for Labor Research and Education, *Meeting California's Retirement Security Challenge* (October 2011), **62% of private sector workers in California do not participate in an employer-sponsored retirement plan,** compared to 57% in the United States as a whole. Also, workers in small- and medium-sized firms are disadvantaged in their access to employer-sponsored retirement plans—in California, 84% of people working for employers with 25 or fewer workers do not participate in a retirement plan at work.

Social Security is the foundation of retirement income for the vast majority of retirees in California, but these payments alone, averaging $1,181 per month, are not enough to sustain workers in retirement. Although Social Security has reduced the poverty rate among retirees in general, women and minorities are disproportionately represented among retirees living in poverty and among low-income retirees. In California, approximately 2/3 of the retirees living in poverty are women.

PROPOSAL:

California workers in the private sector need a lifelong retirement savings system that provides them with the opportunity to build their assets and achieve financial stability in retirement. The California Secure Choice Retirement Savings Program would provide a vital supplement to Social Security income by offering participants a low-risk, low-cost, and completely portable individual retirement accounts and/or individual retirement annuities (IRAs) that will offer a rate of return on their retirement savings.

Employers that want to offer their employees a retirement savings plan also need a way to help their employees save for retirement. Private sector employers often face significant barriers in setting up their own workplace retirement plans—in addition to the costs of hiring service providers and paying service fees, plans such as 401(k)s can be complex to maintain and administer, employers must accept fiduciary responsibility, and they are subject to an array of rules and regulations.

Under the California Secure Choice Retirement Savings Program, voluntary contributions from employees would be deposited into a professionally-managed retirement fund that leverages economies of scale and longer investment horizons to offer every California worker the chance to enroll in a retirement savings program.

Here in California, over 6.3 million private sector workers do not have access to a retirement plan at their place of employment. If these workers contributed 3% of their earnings towards a retirement fund, the fund would have over $6 billion to invest in the first year alone.

This legislation seeks to accomplish all of the following:

<u>California Secure Choice Retirement Savings Investment Board</u>

- Create the California Secure Choice Retirement Savings Trust, administered by the California Secure Choice Retirement Savings Investment Board. This governing and oversight board would be chaired by the State Treasurer and modeled after ScholarShare, California's 529 College Savings Plan.

- In addition to the State Treasurer, the nine-member Board would include the State Controller, Director of Finance, an individual with retirement savings and investment experience appointed by the Senate Rules Committee, a small business representative and a public member each appointed by the Governor, two additional gubernatorial appointees, and an employee representative appointed by the Speaker of the Assembly.

- In establishing the California Secure Choice Retirement Savings Program, the Board would hire private firms to manage the investment portfolio and the individual retirement savings accounts, and also secure underwriting through private insurers. CalPERS would be eligible to bid on the contract to manage the investment portfolio provided it could form a partnership with private vendors to handle the day-to-day account management and obtain the necessary private insurer underwriting.

- Trust funds could only be used exclusively for the purpose of paying benefits to program participants, for program administration costs, and for investments made for the benefit of the program.

<u>Taxpayer Protections</u>

- Prior to the development of the California Secure Choice Retirement Savings Program, direct the Board to conduct a market analysis to determine the viability of implementation, including the assessment of likely participation rates, contribution levels, and the feasibility of investment vehicles.

The market analysis would only be conducted if sufficient funds are made available through a non-profit or private entity, or federal funding for this purpose.

- Following the market analysis, forward the Board's findings to the Chairs of the Senate Public Employment and Retirement Committee and the Assembly Public Employees, Retirement and Social Security Committee, and the Chairs of the Senate Labor and Industrial Relations Committee and the Assembly Labor and Employment Committee.

- The implementation of the California Secure Choice Retirement Savings Program would only move forward if based on the market analysis the Board determines that the program is feasible and will be completely self-sustaining.

- Before studying, developing and obtaining the necessary approvals to fully implement the California Secure Choice Retirement Savings Program, the Board would have to receive sufficient funding to cover these start-up costs through a non-profit, private entity, federal funding, or an annual Budget Act appropriation.

- Once fully implemented, the California Secure Choice Retirement Savings Trust would be self-sustaining and extremely low-risk due to the modest rate of return (likely tied to the 30-year Treasury-bond rate) and long investment horizon. In setting the rate of return for the retirement savings program, ensure zero-liability to the state by requiring the Board to secure private underwriting and reinsurance to protect the returns earned by program participants.

- There would be no state liability for the retirement savings benefit to program participants. Any financial liability for the payment of benefits that exceeds the funds available in the program would be borne by the private underwriters pursuant to the contract entered into with the Board on behalf of program participants.

<u>Disclosures for Employees and Employer Liability Protections</u>

- Employees would receive a program information packet with a disclosure form that includes the benefits and risks of making retirement contributions, the mechanics of how to participate in or opt out of the program, the process for the withdrawal of retirement savings, and how to obtain additional information about the program.

- The disclosure form would clearly inform employees that employers are not liable for their decisions whether to participate in or opt out of the program, or for employee investment decisions, and state that their employer is not a fiduciary of the California Secure Choice Retirement Savings Trust or program, the employer does not bear responsibility for how the program is administered, and the employer is not liable with regard to investment returns and benefits paid to program participants.

- In addition, the disclosure form would notify employees that the program is not an employer-sponsored retirement plan, their employers are not in a position to provide financial advice, and that they should contact financial advisors if they want to seek financial advice.

- To notify employees that the state is not liable for the retirement savings benefit, the disclosure form would also specify that the program fund is privately insured and is not guaranteed by the State of California.

- Employees would be required to sign and date the disclosure form acknowledging that they have read all of the disclosures and understand their content.

Employee Participation in the California Secure Choice Retirement Savings Program

- When the Board officially opens the California Secure Choice Retirement Savings Program for enrollment, allow employers to voluntarily offer the program to their employees and use their payroll system to remit employee contributions into the retirement savings plan.

- Phase-in employee participation into the California Secure Choice Retirement Savings Program—only employers that do not offer their own employer-sponsored retirement plan (such as a 401(k), SEP, or SIMPLE plan) or payroll deduction IRA would have to perform the ministerial duty of supplying the information packet with disclosure form, and allowing employees to remit contributions through payroll deduction:
  - Employers with 100+ employees: allow employee participation within 3 months of the Board opening the program for enrollment;
  - Employers with 50+ employees: within 6 months;
  - Employers with 5+ employees: within 9 months.

- Set the employee default savings amount at 3%, and authorize the Board to adjust the amount between 2%-4% and vary the amount according to the length of time the employee has contributed to the California Secure Choice Retirement Savings Program.

- Voluntary employee participation—employees that do not want to enroll and make contributions to the California Secure Choice Retirement Savings Program can opt-out at any time.

- At least once every two years, employers would designate an "open enrollment period" during which employees that previously opted-out would be given the opportunity to enroll or opt-out again. Employees that decide to opt-out of the program would only be able to enroll or restart their participation during the employer-designated open enrollment period.

- Employees that already have access to a workplace retirement plan can also voluntarily participate in the California Secure Choice Retirement Savings Program. However, their employer would not be obligated to allow them to use their payroll system to make automatic payroll deductions to the program.

Role of Employers

- Unlike employer-sponsored retirement plans such as 401(k)s, employers participating in the California Secure Choice Retirement Savings Program would not bear any fiduciary responsibility and would not be required to pay administrative fees or comply with federal quarterly-reporting mandates.

- Employers that opt to make the California Secure Choice Retirement Savings Program available to their employees would have the limited obligation of allowing their employees to access their payroll system to make reliable, systematic, automatic payroll deductions to the program.

- Limitation on voluntary employer contributions—employers with employees participating in the California Secure Choice Retirement Savings Program would only be allowed to use the program to make their own contributions to their employees' individual retirement accounts if permitted under the federal Internal Revenue Code and it would not cause the program to be treated as an employee benefit plan under the Employee Retirement Income Security Act (ERISA).

- Employers would retain the option at all times to set up and offer their own retirement plans or a payroll deduction IRA instead of permitting their employees' access to the California Secure Choice Retirement Savings Program.

- <u>If it is determined that the payroll deduction IRA arrangements offered by the California Secure Choice Retirement Savings Program constitute an employee benefit plan under ERISA, the Board would be prohibited from implementing the program.</u>

<u>Role of the Employment Development Department</u>

- The Employment Development Department (EDD) would provide outreach and marketing to the employer community, and also facilitate the dissemination of the employee information packet designed by the board.

- If EDD finds through its routine investigation and audit function that an employer is out of compliance, the employer would be given notice and allowed a 90-day grace period to comply without penalty. Employers that are out of compliance after 90 days would be required to pay a penalty of $250 per employee, and if an employer is found to still be noncompliant 180 days or more after the notice, there would be an additional penalty of $500 per employee.

<u>Retirement Investments Clearinghouse</u>

- Prior to implementation of the California Secure Choice Retirement Savings Program, if there is sufficient interest by financial services providers to participate and provide the necessary funding, the board would set up a Retirement Investments Clearinghouse on its web site and establish a vendor registration process.

- The Retirement Investments Clearinghouse would contain information about employer-sponsored retirement plans and payroll deduction IRAs and annuities offered by private providers, and eligible employers would receive a notification from EDD that this resource is available to explore alternatives to allowing employee participation in the California Secure Choice Retirement Savings Program.

<u>Implementation of the California Secure Choice Retirement Savings Program</u>

- **The Board is prohibited from implementing the program if the IRA arrangements offered fail to qualify for favorable tax treatment for IRAs under the Internal Revenue Code, or if it is determined that the program is an employee benefit plan under ERISA.**

- **Pursuant to companion measure SB 923 (De León), the Board cannot open the program for enrollment until a subsequent authorizing statute is enacted that expresses the approval of the Legislature for the program to be fully implemented.**