March 28, 2016

Name
Office
Address
Sacramento, CA 95814

Subject: California Secure Choice Retirement Savings Investment Board Recommendations for Legislation Implementing the California Secure Choice Retirement Savings Program

To Whom It May Concern:

In accordance with Government Code Section 100040, the California Secure Choice Retirement Savings Investment Board (Board) finds the Secure Choice Retirement Savings Program (Secure Choice or Program) to be a feasible, sustainable, and legally permissible program that could help 6.8 million workers start saving for their future.

Since inception in 2012, the Board raised private money from various groups and hired consultants to conduct a market analysis and feasibility study with corresponding program design features. With the private funding, the Board also hired outside legal counsel to provide legal analysis to ensure the Program and all impacted employers would not be considered an employee benefit plan subject to the Employee Retirement Income Security Act of 1974 (ERISA). The legal analysis also focused on the legal viability of the Program as the market research was being conducted.

President Obama directed Secretary of Labor, Thomas E. Perez, to issue regulations that would clarify how states could move forward with retirement plans for private sector workers without being preempted by the Employee Retirement Income Security Act (ERISA). In the fall of 2015, the U.S. Department of Labor released proposed rules which created a safe harbor from ERISA for savings arrangements established by states for non-governmental employees. The proposed rule allows programs like Secure Choice to move forward without ERISA preemption. The catalyst for this safe harbor is the employer mandate. Employers acting pursuant to a state mandate to enroll their employees into Secure Choice would have no liability or fiduciary duty for the plan. This was an exciting win for the Program and for other states interested in Secure
Choice-type programs as we have been given the green light to auto-enroll workers into an Individual Retirement Account (IRA).

The key findings of the market analysis and feasibility study are:

- About 6.8 million workers are potentially eligible for the California Secure Choice Retirement Savings Program
- Likely participation rates are sufficient to enable the Program to achieve broad coverage well above the minimum threshold for financial sustainability
- Eligible participants in California are equally comfortable with a 3% or 5% default contribution rate. The vast majority of likely participants are also comfortable with auto-escalation in 1% increments up to 10%
- Given its inherent portability, the Program should have a lower incidence of rollovers and cash-outs than employer-sponsored 401(k) plans, which often force workers with low balances to close their accounts

The findings of the market analysis as well as the corresponding legal analysis are attached to this memo. Based on the findings of the final report, stakeholder feedback, and public comment, the Board recommends that Senate Bill 1234 allow the Board to:

- Establish managed accounts that would be invested in U.S. Treasuries for the first three years of the program
  
  o Recognizing there are legal and practical hurdles to overcome before the various investment options could be implemented. After three years, the Board should begin to develop investment options that address risk-sharing and smoothing of market losses and gains. Options could include but not be limited to custom pooled, professionally managed funds that minimize management costs and fees, the creation of a reserve fund, or the establishment of investment products

- The Board will conduct an annual peer review to compare California Secure Choice funds with similar funds on performance and fees

- The Board will be required to seek to minimize participant fees

- Implement program features that provide maximum possible income replacement in an IRA based environment
  
  o The Board will establish an initial automatic contribution rate of between 2% and 5% of salary
The Board may implement automatic escalation of participants’ contribution rates up to 10% of salary with the option for participants to stop automatic escalation and change their contribution rates.

The Board and its contracted administrators and consultants shall have a fiduciary duty to the participants of the Program. Investment policy decisions, including asset allocation and investment options, will be entrusted with the Board subject to fiduciary duties.

- Include quasi-private workers to be enrolled if found legally permissible

- Develop an intensive communication and education campaign for both employers and employees both at launch and continually that includes information about the inherent risk in investments

- Determine the default payout method to retirees

- Clearly define “ministerial duties” expected of employers in the implementation of the program and limit liability for all employers if an employer inadvertently provides more than ministerial duties

The board acknowledges the concerns raised by business associations and will partner with employer representatives as it creates the administrative structure to ensure their concerns are addressed. The business community is a vital stakeholder in this work and we will ensure they are partners with us as we form the outreach and education to California businesses. The education campaign to California’s employers will be a top priority as we understand that employers must not hold any liability. Additionally, it must be clear both in statute and as part of the education campaign that the State of California has no liability for the program or its investments.

Legislative language consistent with these principles will provide the Board with sufficient flexibility to shape the program as it develops and react to changes in the market, while protecting workers’ contributions and limiting employer burdens. Your support is paramount to the Board’s ability to lay the groundwork for the Program.

We encourage the Legislature and the Governor to move forward with Secure Choice. While the preliminary work for this endeavor has come to a close, there is much more to do. We must continue to collaborate with members of the Legislature, workers, businesses and other stakeholders to improve the Program as it develops. There are some outstanding legal questions with respect to how this fund would be treated by the Securities and Exchange Commission. However, these issues will not thwart the ability of the Board to implement the Program. We also acknowledge the need to further evaluate costs with respect to customer service needs and record keeping. California continues to be a thought leader on this front and believes that every worker deserves the option to retire with dignity. I hope you join in supporting this great endeavor.
Respectfully submitted,

The California Secure Choice Retirement Savings Investment Board

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CC: Chair of the Senate Committee on Labor and Industrial Relations  
Chair of the Assembly Committee on Labor and Employment  
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Chair of the Assembly Committee on Public Employees, Retirement and Social Security