



GEORGETOWN UNIVERSITY
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Center for Retirement Initiatives

NAST 2014 Issues Conference

State Initiatives to Expand the Availability and Effectiveness of
Private Sector Retirement Plans
How Federal Laws Apply to Plan Design Options

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America's Retirement Crisis

- Most Americans rank having not enough money for retirement as one of their top concerns (Gallop, 2014).
- A sizeable portion of workers report virtually having no savings or investments (EBRI, 2014).
- Traditional pension plans are becoming rare in private sector.
- Employees much more likely to save through company 401(k) plan than on their own via IRA or taxable account.
- Approximately one-half of private sector workers are not covered by an employer plan.

Why Some Employers Don't Provide Retirement Plans?

- Expense
- Management Time
- Fear



States Can Take Action to Address

- Pass enabling legislation.
- State-appointed Board creates/runs turn-key retirement program.
- Low-cost; low-risk; and user-friendly.
- Allowing meaningful amounts to be saved for retirement.
- While leaving room for the private sector to craft other solutions.

But...Challenge for States

- Familiar with managing traditional defined benefit pension plans for public sector.
- Already aware of fiduciary responsibilities, pooled and professionally managed funds and risk management.
- State pension plans have been exempt from ERISA.
- How would ERISA and other laws apply to state actions to address need in private sector?



Federal Law: ERISA

- Covers all:
 - 401(k), traditional pensions, and other employer plans deferring payments until retirement;
 - Regulates plan operation and imposes strict duties on fiduciaries; but
 - Typical IRA is not an ERISA plan.
- ERISA has lots of rules, but also provides workable standards, sound protections and a system for resolving benefit claims.

Fiduciary Details

- Includes:
 - Plan sponsor;
 - Administrative Board and trustees;
 - Anyone with control over plan money; and
 - Anyone with power to hire/fire another fiduciary.
- Duties:
 - Prudent expert, but can outsource to professionals;
 - Act in best interest of participants;
 - Perfection is *not* required, just reasonable decision-making.

ERISA Preemption

- ERISA trumps state law that “relates to a benefit plan.”
- Shifting legal standard.
- Is state law that requires employers to offer a no-cost benefit preempted?

State Can Decide –ERISA or Exempt?

- There are 3 plan options:
 - Individual Retirement Account (IRA);
 - 401(k)/defined contribution (DC);
 - Traditional pension; AKA defined benefit (DB);
- ERISA exempt or ERISA coverage – states have enacted both models (California and Massachusetts).
- Legal questions about ERISA remain.



IRA

- Employee contributions via payroll withholding.
- No employer contributions or “endorsement.”
- Employee invests from menu of available funds selected by state board.
- **Pros**
 - Simple
 - Portable
- **Cons**
 - Low contributions (\$5,500/year)
 - Leakage
- Can state require auto-enrollment with opt out without triggering ERISA?

401(k)/DC

- Employee contributions via payroll withholding.
- Employer matching and non-matching contributions allowed.
- Employee invests from menu of available funds selected by board.
- **Pros**
 - Flexible
 - Auto-enrollment allowed
 - Higher contributions (\$18,000/year)
 - Portable
 - Less leakage than IRA
- **Cons**
 - More complex than IRA
- Single plan (MEP) or many separate plans?

Pension Plan/DB

- Employees receive lifetime annuity.
- Employers and employees may contribute.
- Board, or its delegates, invests plan funds.
- **Pros**
 - Ideal for providing retirement income
 - Less leakage
- **Cons**
 - Employer has risk of underfunding (can reduce via design and hybrids)
 - More complex and costly to administer

State-Sponsored Plans Can

- Avoid risk and cost to taxpayers.
- Be self-supporting.
- Offer options for fund investment.



Investments

- IRAs and 401(k)s can have “default” investment of professionally managed, diversified low-cost fund.
- Also offer “menu” of other professionally managed funds.
- Pension plans invested by Board or delegate, would not have minimum return “bogey.”



Bottom Line

- States can help workers to save for retirement.
- No “correct solution.”
 - IRA, 401(k), and pension each have pros and cons
- Don’t fear ERISA!
 - ERISA should not be made the bogeyman to stop states from taking action to address the retirement crisis.

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