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IN FOCUS

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State-Administered IRA Programs: Overview and Considerations for Congress

Overview of State-Administered Retirement Plans

While Congress addresses retirement security at the national level and establishes federal pension law and savings incentives, several states have enacted or implemented state-administered retirement savings programs to increase retirement plan access and savings among private-sector workers. Because retirement plans, such as 401(k)s or defined benefit plans, are optional for employers to adopt, some workers may not have access to employment-based retirement benefits. In March 2019, 33% of private-sector workers did not have access to a workplace retirement plan. State-administered retirement programs are intended to provide savings options for workers whose employer does not offer a workplace plan.

States are taking a variety of approaches to these programs, including the following: retirement marketplaces, in which employers and individuals can purchase a savings plan through different state-approved providers; multiple-employer plans, in which unrelated businesses may jointly sponsor a 401(k) plan; and payroll deduction Individual Retirement Accounts (IRAs), in which employers deduct a portion of pay from an employee's paycheck and deposit it into the employee's own IRA (a tax-advantaged retirement savings account regulated at the federal level). This In Focus describes the most common state-administered program—the payroll deduction IRA.

Table 1. State- and City-Administered Retirement Savings Program Approaches
(enacted programs as of July 2020)

Program Approach	States
Retirement Marketplace	NM, WA
Multiple-Employer Plan	MA, VT
Payroll Deduction IRA	CA, CO,[a] CT, IL, MD, NJ, NM,[a] NY,[a] OR, WA (Seattle only)

Source: Congressional Research Service (CRS).
Notes: New Mexico (NM) enacted a combination of approaches.

a. New Mexico and New York have payroll deduction Individual Retirement Account (IRA) programs that are optional for employers to adopt; other states' programs are mandatory for employers. Both program types allow employees to opt out once enrolled. Colorado program details are not yet available.

In some state programs, employer participation is mandatory (with some exceptions). In other state programs, employer participation is voluntary. Typically, eligible employees of participating employers are automatically enrolled in a state program but can opt out at any time. Because of the automatic enrollment feature, these plans are sometimes referred to as automatic, or auto, IRAs. As of July 2020, six states have enacted auto IRA programs (Maryland, Colorado, Connecticut, New Jersey, New Mexico, and New York), and three states have implemented auto IRAs (California, Oregon, and Illinois). Employer participation in New Mexico and New York is optional (see **Table 1**). One city—Seattle, WA—has also enacted an auto IRA program.

State-Administered Automatic IRAs

State-administered auto IRA programs share many features. A state retirement board oversees each program and is responsible for making program decisions, such as contracting with an IRA provider. Some programs are optional for employers to adopt; other programs are mandatory for nonexempt employers. Generally, exempt employers (1) are under a certain size or (2) already offer an employer-sponsored pension plan. The programs in place also allow self-employed workers and those who do not work for a participating employer to self-enroll.

Among the programs in place as of July 2020, the default accounts are Roth IRAs. Contributions to Roth IRAs are made with after-tax income, and withdrawals in retirement are generally tax-free. The programs also offer a traditional IRA option. Contributions to traditional IRAs may be tax deductible for individuals who do not have access to an employer-sponsored retirement plan. Because individuals with income over a certain threshold cannot contribute to Roth IRAs (e.g., a single filer with income of $139,000 or higher in 2020), some employees may have to opt out or choose the traditional IRA option.

State-administered IRA programs are subject to federal IRA contribution limits, which in 2020 generally are $6,000 ($7,000 for individuals aged 50 and over). The programs in place do not allow for employer contributions. They each have a 5% default contribution rate, which means that 5% of an employee's pay is deducted when an employee is automatically enrolled but does not choose a contribution rate. The state-administered programs in place also have an auto-escalation feature, which is a gradual increase in the worker's contribution rate over a specified number of years. Contributions from individuals with income under certain thresholds may be eligible for the federal Retirement Savings Contribution Credit.

Employees can withdraw original contributions from Roth IRAs at any point. Any earnings withdrawn prior to age 59½ from accounts that are not at least five years old are included in taxable income and generally subject to a 10%

penalty. Employees who change employers or move out of state can keep the same IRA or transfer savings to a different IRA.

State-Administered IRA Programs and ERISA

Whether federal pension law applies to state-administered IRAs is subject to debate. Congress passed the Employee Retirement Income Security Act of 1974 (ERISA; P.L. 93-406) to protect the benefits of participants in private-sector pension plans. Among other things, ERISA sets standards for participation and fiduciary duties and outlines reporting requirements for these plans. Private-sector employers that establish or maintain plans that fall within ERISA's scope must comply with these requirements. In mandating private-sector employers to participate in payroll deduction savings programs, some stakeholders question whether states are unintentionally compelling employers to establish ERISA plans, subject to the act's comprehensive requirements.

If state-administered IRA programs are considered ERISA plans, this may create challenges for the programs. The issue is one of federal preemption. Section 514 of ERISA broadly preempts "any and all" state laws that "relate to" ERISA-covered employee benefit plans. Accordingly, if a state-administered IRA program establishes an ERISA plan (or the state program is an ERISA plan itself), it is possible that state laws underlying the program may be superseded by ERISA and judicially invalidated. A legal challenge to California's IRA program on such grounds is currently pending before the U.S. Court of Appeals for the Ninth Circuit (*Howard Jarvis Taxpayers Assoc. v. Cal. Secure Choice Ret. Sav. Program*, No. 20-15591 (9th Cir. 2020)).

The Department of Labor (DOL) has issued regulations addressing ERISA's relationship to private-sector payroll deduction IRAs. A 1975 regulation (29 C.F.R. §2510.3-2(d)) outlined four conditions for a payroll deduction IRA to *not* be considered an ERISA plan: (1) the employer makes no contributions, (2) employee participation is completely voluntary, (3) the employer does not endorse the program and merely facilitates it, and (4) the employer receives no consideration except for its own expenses. In August 2016, DOL issued a safe harbor regulation that established criteria for designing state-administered payroll deduction IRAs "as to reduce the risk of ERISA preemption" (29 C.F.R. §2510.3-2(h) (2016)). Under this regulation, state programs were required to be (1) authorized in state law and (2) administered by the state that established the program. The regulations specified that employer participation must be required by state law and limited the employer role to activities such as collecting payroll deductions and distributing program information. In December 2016, DOL issued another rule that expanded the applicability of the safe harbor to qualified state political subdivisions, which applied to cities that established payroll deduction IRA programs.

In April 2017 and May 2017, Congress used the procedures in the Congressional Review Act (CRA, enacted as part of the Small Business Regulatory Enforcement Fairness Act of 1996; P.L. 104-121) to nullify DOL's regulations creating safe harbors for savings arrangements established by qualified state political subdivisions and by states (P.L. 115-24 and P.L. 115-35, respectively). Senator Mitch McConnell contended that state-administered auto IRA programs would free states and cities from federal consumer protections and would create a competitive advantage for the programs compared to private-sector plans. Following Congress's actions under the CRA, the issue of ERISA preemption remains uncertain. Despite this uncertainty, some states have indicated that they are continuing with program implementation. Congressional action could resolve the uncertainty legislatively.

Considerations for Congress

The goal of state-administered auto IRA programs is to increase retirement savings for individuals without access to employer plans. Although all individuals with wage income can establish and contribute to an IRA on their own, many do not. Advocates for the state-administered programs cite research that employees are more likely to save for retirement if they are offered a plan through their workplace. If these programs were to increase individuals' savings above what they would have otherwise saved given the lack of access to an employer plan, states and the federal government could see reductions in demand for social services when workers retire.

Some stakeholders have expressed concern that state-administered auto IRA programs may replace existing employer-sponsored plans. State-administered payroll deduction plans differ from employer-sponsored defined contribution plans, such as 401(k) plans, in multiple ways. For example, IRA contribution limits are lower than those for 401(k) plans, and IRAs generally lack employer contributions. In 2020, the annual IRA contribution limit is $6,000; the 401(k) plan limit is $17,500 (and the combined employer and employee 401(k) contribution limit is $57,000). Compared with participants in a 401(k) plan, those enrolled in a payroll deduction IRA may not accumulate savings at the same rate. Stakeholders have also expressed concern that state-administered plans lack adequate measures to protect participants' benefits (e.g., whether deposits would be made in a timely manner, fees would be reasonable, investment choices prudent, and decisionmakers held to a standard high enough). Existing state law or provisions in authorizing state legislation might alleviate some of these concerns. In addition, employers that operate in multiple states could be required to participate in several programs, which could be administratively challenging. For example, employers might have to monitor employee eligibility for different state programs based on residence or office location.

Further Information

CRS Report RL34397, *Traditional and Roth Individual Retirement Accounts (IRAs): A Primer*.

"Proceedings and Debates of the 115th Congress, First Session," *Congressional Record*, vol. 163, part 55 (March 29, 2017), p. S2055.

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