WILLKIE FARR & GALLAGHER LLP

CLIENT ALERT

Small Employers in Illinois, California and New York: Preparing for State-Mandated Automatic IRA Programs in 2022

May 20, 2022

AUTHORS

Alexander P. Ryan | Sarah Haddy

I. Background

A number of states have passed, or are considering, laws requiring private employers that do not offer a workplace retirement plan to enroll employees in a state-run plan. Although some of these programs have been effective for a number of years, 2022 represents a pivotal time for three states in particular. In Illinois and California, certain employers who do not offer a retirement plan have already been required to start participation. In 2022, the laws will apply to increasingly smaller-sized employers, including those who traditionally have not offered a retirement plan to their employees. In New York, a new law has been implemented requiring participation for the first time from small employers. This alert focuses on these three states.[1]

Upcoming 2022 Deadlines: The deadline for California employers with 5 – 50 employees to register for, or opt out of, its program is June 30. The deadlines for Illinois employers with 16 – 24 employees to register for, or opt out of, its program is November 1.

[1] Although not discussed here, similar laws have been enacted or are in effect in Colorado, Connecticut, Maine, Maryland, New Jersey, New Mexico, Oregon, and Virginia, as well as New York City and Seattle.

II. Overview

a. Illinois: Illinois was the first state to enact a state-run retirement savings plan. Enacted January 4, 2015 and effective as of June 1, 2015, the Illinois Secure Choice Savings Program ("Illinois Secure Choice") originally applied to employers with 25 employees who did not offer a retirement plan. In 2021, the state expanded Illinois Secure Choice to apply to employers with at least five employees. Under the mandatory program, covered employers are required to enroll employees in Illinois Secure Choice, which is an automatic Roth individual retirement account ("IRA") program. Illinois Secure Choice has rolled out in various waves, in accordance with the following schedule:

Number of employees	Deadline
Over 500 employees	November 1, 2018
100 – 499 employees	July 1, 2019
25 – 99 employees	November 1, 2019
16 – 24 employees	**November 1, 2022**
5 – 15 employees	November 1, 2023

b. California: In September 2019, then-Governor Jerry Brown signed legislation requiring private employers with five or more employees who do not sponsor a retirement plan to automatically enroll their employees into a new state retirement savings program. Similar to Illinois Secure Choice, the CalSavers Retirement Savings Program ("CalSavers") is an automatic Roth IRA program funded with employee payroll contributions. CalSavers opened for enrollment on July 1, 2019, and employers in California are required to register their business in accordance with the following schedule:

Number of employees	Deadline
Over 100 employees	September 30, 2020
Over 50 employees	June 30, 2021
5 or more employees	**June 30, 2022**

c. New York: In October 2021, Governor Hochul signed legislation requiring private employers who employ 10 or more employees and do not sponsor a retirement plan to automatically enroll their employees into the New York State Secure Choice Savings Program (the "New York Program"). Like Illinois and California, New York utilizes an automatic Roth IRA program funded with employee payroll contributions. Although the statute provided that the New York Program implementation and enrollment of employees was to begin no later than December 31, 2021, New York has only recently started implementation.

III. Eligible Employees; Participation in the Program

In each of the three states, the law applies to employees who are eighteen years of age or older, who are employed by an employer that is subject to the mandate (as defined below), and who have wages allocable to that state during a calendar year. Under the different arrangements, eligible employees are automatically enrolled at a certain rate, unless the employee elects to opt out. Like traditional IRAs, employees that participate in the state-run automatic IRAs may generally make contributions up to the maximum deductible IRA limit under Section 219 of the Internal Revenue Code of 1986. As these accounts are IRAs, they are "portable," allowing participating employees to continue to contribute or roll over their accounts into other retirement savings plans.

Employee participation in each state is subject to the following rules:

a. Illinois: Individuals employed by a covered employer will be automatically enrolled in Illinois Secure Choice by the employer's facilitation of a 5% payroll deduction, which will automatically increase by 1% each year until it reaches 10%. The opt-out period for employees is 30 days. Multiple investment options are available to participating employees. Employees that fail to elect an investment will be invested in the Illinois Secure Choice Target Retirement Fund.

b. California: Individuals employed by a covered employer will be automatically enrolled in CalSavers by the employer's facilitation of a 5% payroll deduction, which will automatically increase by 1% each year until it reaches 8%. Unless employees choose an alternate investment option, initial contributions will be invested in the CalSavers Money Market Fund. Following the first 30 days, funds and future contributions are automatically allocated to a target-date fund based on age or expected year of retirement, or to a fund of the participant's choice.

c. New York: Individuals employed by a covered employer will be automatically enrolled in the New York Program by the employer's facilitation of a 3% payroll deduction. Employees may select from the investment options offered under the New York Program, and the New York Secure Choice Savings Program Board will designate a default investment option for employees that fail to make an election.

IV. Covered Employers; Employer Responsibilities

In each of the three states, the law generally applies to an employer that has a minimum number of employees and does not offer a traditional employer-sponsored retirement plan (*e.g.*, an ERISA-governed 401(k) plan). None of the laws specify that the foregoing employer-sponsored plan must cover each employee in the state in order to be exempt from mandatory participation. Thus, there does not appear to be any requirement that the employer-sponsored plan cover all employees in order to exempt the employer from the state program.

a. Illinois: Under Illinois Secure Choice, an employer is any person or entity engaged in a business, industry, profession, trade, or other enterprise in Illinois, whether for profit or not for profit that (i) has employed at least five employees in Illinois during every quarter of the previous calendar year, (ii) has been in business at least two years, and (iii) has not offered a qualified retirement plan, including, but not limited to, a plan qualified under Section 401(a), Section 401(k), Section 403(a), Section 403(b), Section 408(k), Section 408(p) or Section 457(b) of the Internal Revenue Code of 1986 in the preceding two years.

b. California: For purposes of CalSavers, an employer is any person or entity (other than the federal government, the State of California or any county, municipal corporation or any units or instrumentalities of the state), whether for profit or not (i) that is engaged in a business, industry, profession, trade or other enterprise in California, (ii) that employs at least five California employees, with at least one of the five employees being an eligible employee, and (iii) that does not sponsor a plan qualified under Section 401(a), Section 401(k), Section 403(a), Section 403(b), Section 408(k), or Section 408(p).

c. New York: For purposes of the New York Program, an employer is any person or entity engaged in a business, industry, profession, trade, or other enterprise in New York state, whether for profit or not for profit that has (i) at all times during the previous calendar year employed at least 10 employees in the state, (ii) been in business for at least two years, and (iii) not offered a qualified retirement plan under Section 401(a), Section 401(k), Section 403(a), Section 403(b), Section 408(k), Section 408(p) or Section 457(b) of the Internal Revenue Code of 1986 in the preceding two years. Employers are prohibited from terminating their own retirement plans in order to join the New York Program.

Covered employers are required to perform certain administrative tasks in each state, including facilitating automatic enrollment of employees, withholding and remitting payroll deductions for employees that do not opt out, and providing certain employee demographic information to the state's program. In each state, the program will furnish informational materials that must be or may be, depending on the state, provided to employees. Thus, the compliance requirements in each state may require employers to establish and maintain new procedures and practices with respect to new and ongoing employees, at the employer's own cost, and employers will need to ensure these are in place prior to applicable deadlines.

Although employers will have some administrative responsibilities, employers will not have many of the responsibilities that come with sponsoring a private retirement plan, such as non-discrimination testing, Form 5500 reporting, and ERISA disclosure obligations. Employers are not required to contribute to any of the state programs. And unlike in traditional ERISA-governed plans, employers are insulated from any fiduciary responsibilities with respect to these programs.

V. Implementation and Registration

The Illinois and California programs have been implemented and in effect for a number of years. In both states, registration is open to eligible employers, including employers that are not yet required to comply. In New York, although the statute provided that implementation and enrollment of employees was to begin no later than December 31, 2021, New York has only recently started implementation.

a. Illinois: As an established program, Illinois Secure Choice provides a website containing various pieces of information for employers and registration is available through an employer portal. Covered employers may have received (or should expect to receive) a registration notification from the Illinois Secure Choice account administrator, notifying employers of the date they may begin registration and start enrolling their employees, and when that process must be complete. Employers are required to access the online portal to register for the program before the applicable deadline. During the registration process, an employer is required to provide information about its business to determine if it is subject to mandatory participation. An employer that is exempt from Illinois Secure Choice, but that receives a registration notification, is required to notify the account administrator through the online portal or by contacting the account administrator that it is not required to participate. Illinois Secure Choice is overseen by the Illinois Secure Choice Savings Board.

b. California: Like Illinois Secure Choice, CalSavers has been up and running for a few years and maintains a website with employer program information and enrollment. Covered employers are required to proactively register for CalSavers by the effective deadline. Unlike Illinois, California employers are not required to notify the state that they are exempt. However, CalSavers encourages employers to inform its administrator if they are exempt. CalSavers is overseen by the CalSavers Retirement Savings Board.

c. New York: Implementation of the New York Program is underway, but registration is not yet available. The New York Secure Choice Savings Program Board is responsible for the New York Program and held its first meeting on January 26, 2022. During the meeting, the New York Secure Choice Savings Program Board directed the Department of Taxation and Finance to undertake the implementation of the program and directed it to release a request for proposal to select a consultant to assist with program design and the development of future procurements for program administration and investment management. The statute requires that covered employees must have a payroll deposit arrangement in place within nine months after the New York Secure Choice Savings Program Board opens the New York Program for enrollment.

VI. Penalties for NonCompliance

Each state's program has a unique penalty structure for noncompliance.

a. Illinois: An employer who fails to timely enroll an employee, without reasonable cause, in Illinois Secure Choice will be subject to a penalty of (i) $250 per employee for the first calendar year the employer is noncompliant, and (ii) $500 per employee for each subsequent calendar year the employer is noncompliant. Noncompliance does not need to be consecutive to incur the $500 penalty. The Illinois Secure Choice website indicates that enforcement for non-compliant employers with 25 or more employees will begin in 2022.

b. California: Noncompliant employers will receive a notice of noncompliance in California. Employers that, without good cause, fail to enroll their employees in CalSavers upon receiving the notice of noncompliance may be subject to a penalty of $250 per eligible employee if noncompliance extends 90 days or more after receipt of such notice. If noncompliance continues for 180 days or more after the notice, an additional $500 per eligible employee penalty applies (for a total per eligible employee penalty of $750). CalSavers has begun notifying employers with more than 100 employees and more than 50 employees that did not register by the applicable deadline.

c. New York: The New York Program does not provide for any penalties in the statute.

VII. Impressions

Until recently, there was some question as to whether automatic IRA programs like those mandated by Illinois, California and New York would be preempted by ERISA. CalSavers was challenged in the U.S. District Court for the Eastern District of California, where the court held that CalSavers is not an ERISA plan and that ERISA does not preempt the state law. This view was upheld by the Ninth Circuit, and the United States Supreme Court recently declined to review the challenge based on ERISA preemption grounds, thereby allowing the program to go forward.

Given the ruling in the Ninth Circuit and the Supreme Court's decision not to review the CalSavers case, more states are likely to consider automatic IRA programs. Employers that do not offer retirement plans to employees should monitor the changing laws in states in which they do business. Employers that become subject to state programs should be prepared to facilitate payroll deductions and payments to those state plans in accordance with the regimes mandated in those states.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

Alexander P. Ryan
202 303 1129
aryan@willkie.com

Sarah Haddy
312 728 9058
shaddy@willkie.com