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**THE NEXT GENERATION OF PREEMPTION  
CASES:  
STATE REGULATION OF 401(K) PLANS**

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INTRODUCTION

The Employee Retirement Income Security Act of 1974,<sup>1</sup> as amended (“ERISA”) was written to provide the exclusive rules with respect to retirement plans.<sup>2</sup> ERISA explicitly preempts state laws that relate to employee benefit plans.<sup>3</sup> Although the phrase “relate to” appears relatively straightforward,<sup>4</sup> the U.S. Supreme Court’s interpretations of its meaning have varied.<sup>5</sup> As a consequence, not all state laws that have an impact on employee benefit plans have been held

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1. 29 U.S.C. §§ 1001-1461 (2006).

2. See generally James A. Wooten, *A Legislative and Political History of ERISA Preemption, Part 3*, 15 J. OF PENSION BENEFITS 15 (2008) (“The desire for uniformity required preemption language that went considerably beyond the Disclosure Act and previous legislative proposals.”).

3. ERISA § 514, 29 U.S.C. § 1144(a).

4. The American Heritage Dictionary defines the term “relate to” in the way I think people commonly think of this phrase. That is, it includes the following as possible definitions for “relate to”: “[1] to bring into logical or natural association. [2] to establish or demonstrate a connection between. [3] to have a connection, relation, or reference.” Thus, interpreting the words in accordance with how they are normally used, ERISA preempts state laws that have a demonstrable connection with employee benefit plans. AMERICAN HERITAGE DICTIONARY 705-06 (4th ed. 2001).

5. Compare *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 98 (1983) (interpreting ERISA’s preemption provisions broadly based on Congressional intent), with *N.Y. State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 668 (1995) (stating that in areas of traditional state concern limitations on “relate to” will apply).

to be preempted by ERISA.<sup>6</sup>

States have considerable motivations for regulating 401(k) plans. In addition to the significant amount of attention placed on these types of plans by the media, state politicians' constituents will suffer the consequences that result from inadequate retirement savings and will place substantial burdens on state governments to provide for them in retirement.<sup>7</sup> As the Baby Boomers retire, these issues will become more pronounced.<sup>8</sup> Concerns regarding 401(k) plans have been primarily focused on the amount of workers covered by these plans, the fees charged to the plans, and the adequacy of the retirement savings of workers who participate in the plans (known as participants).<sup>9</sup> States have proposed legislation to address some of these issues.<sup>10</sup> The

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6. See, e.g., *Travelers*, 514 U.S. at 668 (indicating that a state law imposing surcharges was not preempted because it only had an indirect economic effect on an ERISA plan); *Cal. Div. of Labor Standards Enforcement v. Dillingham Constr. N.A., Inc.*, 519 U.S. 316, 330 (1997) (holding that a prevailing wage law was not preempted because it was "quite remote from the areas with which ERISA is expressly concerned"); *Mackey v. Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825, 831-32 (1988) (finding that a state's garnishment statute's general provisions were not preempted because it was a law of general applicability).

7. Individuals who are not adequately prepared for retirement are more likely to qualify for benefits provided by states as well as to use other resources that are not income-based. EBRI indicated that the median (midpoint) annual income for the elderly population was \$16,770 in 2006. Ken McDonnell, *Income of the Elderly Population Age 65 and Over, 2006*, 28 EBRI NOTES 1, 10 (2007).

8. Stephanie L. Freid, *U.S. Seniors Face Increased Poverty Budget Woes Hit Women, Minorities Hardest*, NEWSDESK.ORG, Sept. 19, 2003, <http://www.newsdesk.org/archives/003208.html> (stating that "Projected Census Bureau figures show that as Baby Boomers (those born between 1946 and 1964) reach their golden years, the overall senior population will increase dramatically—as much as sixfold by 2040. Advocates for seniors fear this will place greater pressure on state and federal governments for subsidized healthcare and adult care programs.").

9. See, e.g., David Pratt, *Retirement in a Defined Contribution Era: Making the Money Last*, 41 J. MARSHALL L. REV. 1091, 1120 (2008) (discussing risks relating to coverage and benefit adequacy in defined contribution plans); Debra A. Davis, *How Much is Enough? Giving Fiduciaries and Participants Adequate Information About Plan Expenses*, 41 J. MARSHALL L. REV. 1005, 1021-22 (2008); (discussing the information needed by fiduciaries of and participants in 401(k) plans about the fees charged to their plans); Susan J. Stabile, *Is it Time to Admit the Failure of an Employer-Based Pension System*, 11 LEWIS & CLARK L. REV. 305, 310-16 (2007) (discussing the problems with 401(k) plans, including issues relating to participation, the contribution of sufficient assets by participants, the selection among the plan's investment options by participants, the lack of a guaranteed benefit, and the limited opportunity for redress against plan fiduciaries); Adam Carasso & Jonathan Barry Forman, *Tax Considerations in a Universal Pension System (UPS): Discussion Paper No. 28* (Urban-Brookings Tax Policy Ctr.), Dec. 20, 2007, at ii (discussing the need for a universal compulsory pension system).

10. Several states have considered universal retirement plans for their residents, including California, Connecticut, Illinois, Indiana, Maryland, Massachusetts, Michigan, Pennsylvania, Rhode Island, Tennessee, Virginia, Washington, and West Virginia. Albert B. Crenshaw, *Not Saving Enough at Work? How About a Boost From Your State?*, AARP BULLETIN TODAY, July 2, 2008,

solutions currently considered by states have been voluntary. However, as states face overwhelming costs related to retirees they may approach these issues as they have with health care, that is, to require employer action.

This Article argues that the federal government is optimally suited to address coverage, cost, and benefit adequacy issues related to 401(k) plans. Part I discusses the interest of states in legislating 401(k) plans, previously introduced legislation, and likely future legislation. Part II of the Article analyzes ERISA's preemption provisions, the Supreme Court's interpretation of them, and challenges states would face in enacting laws that impact 401(k) plans. Part III explains the benefits of a uniform system for plan design and administration, for workers to be able to transfer among their companies' locations, and for interested parties and organizations to effectively participate in the political and regulatory processes. Part IV analyzes the likelihood of preemption of state laws that address 401(k) plans. Part V concludes that the regulation of retirement plans is best handled by the federal government in order to provide for a uniform system.

## I. STATE ACTION

In the area of employee benefits, states have acted in response to significant financial pressures by passing laws to require employer action. When national health care reform failed in the mid-90s, states began to consider and adopt "fair share" laws, designed to have employers help to ensure that workers had adequate health care by

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[http://bulletin.aarp.org/yourmoney/retirement/articles/state\\_savings\\_plans.html](http://bulletin.aarp.org/yourmoney/retirement/articles/state_savings_plans.html); ECONOMIC OPPORTUNITY INSTITUTE, UVRA UPDATE, STATE UPDATES, 1 UVRA UPDATE 4 (Mar. 2008), <https://www.policyarchive.org/bitstream/handle/10207/11145/UVRAUpdate-Mar08.pdf?sequence=1> [hereinafter UVRA UPDATE, STATE UPDATES]; ECONOMIC OPPORTUNITY INSTITUTE, UVRA UPDATE, UNIVERSAL VOLUNTARY RETIREMENT ACCOUNTS: STATE UPDATES (Apr. 2009), [http://www.eoionline.org/retirement\\_security/uvra\\_update/UVRAUpdate-Apr09.pdf](http://www.eoionline.org/retirement_security/uvra_update/UVRAUpdate-Apr09.pdf) [hereinafter UVRA UPDATE, UNIVERSAL VOLUNTARY RETIREMENT ACCOUNTS]. Connecticut was the first state to pass legislation to create a state-administered 401(k) plan. Press Release, State Sen. Donald Williams, Democratic Senate Makes History—Passes 1st in the Nation Universal 401(k) Plan (Apr. 24, 2008), *available at* <http://www.senatedems.ct.gov/pr/williams-080424b.html>. Although Connecticut's Senate passed the bill, it was not enacted into law. The Connecticut General Assembly's Web site describes the status of SB-652 as passed by Connecticut's Senate, but that no action was taken by Connecticut's House of Representatives. AN ACT CONCERNING SMALL BUSINESS RETIREMENT PLANS, BILL STATUS REPORT FOR SUBSTITUTE FOR RAISED S.B. NO. 652 (Conn. 2008), *available at* [http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=House+Cal%23&bill\\_num=459&which\\_year=2008&SUBMIT1.x=12&SUBMIT1.y=6&SUBMIT1=Normal](http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=House+Cal%23&bill_num=459&which_year=2008&SUBMIT1.x=12&SUBMIT1.y=6&SUBMIT1=Normal) [hereinafter BILL STATUS REPORT S.B. NO. 852].

requiring employers to spend a greater amount of money on health care or alternatively pay the states.<sup>11</sup> Similarly, states will look to employers to help ensure that workers have adequate retirement benefits.

In order to make sure that workers have sufficient benefits at retirement, workers need to be able to participate in plans, have the assets in the plans grow (and not be unreasonably reduced by fees) and be able to accumulate sufficient assets within their plans. States have already begun to consider legislation to address these issues and at least one state has commissioned a study to look into 401(k) issues further.<sup>12</sup>

### A. States' Approaches to Health Care Coverage

States' approaches to health care reform are strong indicators of their future responses to addressing inadequate retirement benefits of their constituents. In response to rising health care costs, particularly for the uninsured, several states and local governments passed laws that required employers to provide a minimum level of benefits to their workers or alternatively, make payments to the government (known as "pay or play laws").<sup>13</sup>

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11. William Pierron & Paul Fronstin, *ERISA Pre-emption: Implications for Health Reform and Coverage*, EBRI NOTES, Feb. 2008, at 12, [http://www.ebri.org/pdf/briefspdf/EBRI\\_IB\\_02a-20082.pdf](http://www.ebri.org/pdf/briefspdf/EBRI_IB_02a-20082.pdf).

12. COMMERCE COMMITTEE JOINT FAVORABLE REPORT, THE STATE OF CONNECTICUT'S PROPOSED "AN ACT CONCERNING SMALL BUSINESS RETIREMENT PLANS, BILL NO. SB-652 (Conn. 2008) <http://www.cga.ct.gov/2008/JFR/S/2008SB-00652-R00CE-JFR.htm>. The State of Connecticut's proposed bill, entitled "An Act Concerning Small Business Retirement Plans," (SB-652), would have required the comptroller to establish a defined contribution plan to be available to self-employed individuals, small employers, and non-profit organizations. *Id.* The Commerce Committee of the Connecticut General Assembly stated that the "program this bill seeks to establish must seek (1) to minimize costs by helping small employers and individuals, (2) arrangements and investments through economies of scale, and (3) standardization and other measures." *Id.* Although the bill was passed by Connecticut's Senate, it was not enacted into law. Connecticut's Senate has re-introduced the bill as SB-971. The Connecticut General Assembly's Web site describes the status of SB-652 as passed by Connecticut's Senate, but that no action was taken by Connecticut's House of Representatives. *See* BILL STATUS REPORT S.B. NO. 852 (Conn. 2008). The Connecticut General Assembly's Web site also reflects the status of SB-971. *See* AN ACT CONCERNING SMALL BUSINESS RETIREMENT PLANS, BILL STATUS REPORT FOR SUBSTITUTE FOR RAISED S.B. NO. 971 (Conn. 2009), *available at* [http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill\\_num=971&which\\_year=2009&SUBMIT1.x=10&SUBMIT1.y=13&SUBMIT1=Normal](http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill_num=971&which_year=2009&SUBMIT1.x=10&SUBMIT1.y=13&SUBMIT1=Normal). Other states that have considered retirement savings plans for private-sector employees include California, Illinois, Indiana, Maryland, Massachusetts, Michigan, Pennsylvania, Rhode Island, Tennessee, Virginia, Washington, and West Virginia. *Creshaw, supra* note 10; UVRA UPDATE, UNIVERSAL VOLUNTARY RETIREMENT ACCOUNTS, *supra* note 10, at 1-3.

13. A number of state and local governments have enacted this type of legislation, including Massachusetts, Maryland, Suffolk County, and the City of San Francisco. They have also been

States have been largely undeterred by ERISA's preemption provisions. Even though courts have held that several laws by state and local governments were preempted, states continue to consider legislating in this area.<sup>14</sup> For example, the California Assembly passed a pay or play law after the Fourth Circuit Court of Appeals found that Maryland's pay or play law was preempted by ERISA.<sup>15</sup>

Similarly, states that want to increase the amount of benefits provided to their constituents through 401(k) plans will pass legislation regardless of ERISA's preemption provisions. Although states will be cognizant of ERISA's provisions and attempt to draft laws in such a way as to avoid preemption, ERISA does not serve as a complete deterrent for this type of legislation.

### *B. Motivations for State Action*

States have considerable reasons for wanting to legislate in this area. Numerous concerns have been expressed in recent years about 401(k) plans.<sup>16</sup> These concerns have predominantly focused on coverage, fees, and benefit adequacy.<sup>17</sup> In this Article, "coverage" refers to the amount of workers who have access to and elect to participate in 401(k) plans. The term "fees" is used in this Article to refer to the amount and reasonableness of the fees charged to 401(k) plans as well as the disclosure of those fees to fiduciaries of and participants in the plans. "Benefit adequacy" refers to the amount of benefits that participants have at retirement and the ability of participants to have sufficient funds during retirement on which to live. Benefit adequacy includes coverage

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considered by several other states. See NATIONAL CONFERENCE OF STATE LEGISLATURES, 2006 "PAY OR PLAY" BILLS (2006), <http://www.ncsl.org/default.aspx?tabid=13873>. See generally Amy B. Monahan, *Pay or Play Laws, ERISA Preemption, and Potential Lessons from Massachusetts*, 55 U. KAN. L. REV. 1203 (2007) (analyzing the creativity of new "pay or play" laws by states attempting to avoid ERISA preemption).

14. See Edward A. Zelinsky, *The New Massachusetts Health Law: Preemption and Experimentation*, 49 WM. & MARY L. REV. 229 (2007).

15. The California Assembly passed ABX1 1 on December 17, 2007. *Fielder* was decided on January 17, 2007. Rest. Indus. Leaders Ass'n v. *Fielder*, 536 F.3d 639 (9th Cir. 2007).

16. See, e.g., Pratt, *supra* note 9; Davis, *supra* note 9. Several professors have also suggested completely eliminating 401(k) plans. Professor Teresa Ghilarducci suggests that 401(k) plans be replaced with a mandatory, universal savings plan. TERESA GHILARDUCCI, *WHEN I'M SIXTY-FOUR: THE PLOT AGAINST PENSIONS AND THE PLAN TO SAVE THEM* 24 (Princeton Univ. Press 2008). Professor Susan Stabile suggests replacing our employer-based system with a government pension or alternatively, creating a mandatory employer-based system. Stabile, *supra* note 9, at 325-29. Professor Jonathan Forman has also suggested replacing our current system with a uniform pension system. Carasso & Forman, *supra* note 9, 2-3.

17. See *supra* note 9 and accompanying text.

issues, in that workers need to participate in order to have sufficient retirement savings.

### 1. Coverage

401(k) plans have garnered national attention as they have become the primary means of saving for retirement for most American workers.<sup>18</sup> Abstracts of the 2006 Form 5500 Annual Reports, the most recent year that data is available, reflect that 401(k) plans have been rapidly increasing since legislation was passed creating 401(k) plans in 1978.<sup>19</sup> In 2006, there were 466,000 401(k) plans that had 58.4 million active participants.<sup>20</sup> For almost 94% of participants, a 401(k) plan was the only type of retirement plan offered by their employer in 2006.<sup>21</sup>

Despite the large number of 401(k) plans, many companies do not offer 401(k) plans and for those companies that sponsor plans, not all workers participate in the plans.<sup>22</sup> The Congressional Research Service reports that for 2007, only 55% of employees worked for a private-sector company that sponsored a defined contribution plan, such as a 401(k) plan.<sup>23</sup> For workers whose employers sponsored a defined contribution plan, 78% of employees participated in the plan.<sup>24</sup> However, the overall participation rate for private-sector workers in defined contributions plans was only 43%.<sup>25</sup>

These issues are more pronounced with employees of small companies, that is, employers with fewer than 100 workers. In 2007, only approximately 42% of workers at small companies were offered the ability to participate in a defined contribution plan and only around 33%

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18. Pratt, *supra* note 9, at 1102.

19. EMPLOYEE BENEFITS SECURITY ADMIN., U.S. DEP'T OF LABOR, PRIVATE PENSION PLAN BULLETIN: ABSTRACT OF 2006 FORM 5500 ANNUAL REPORTS 1 (Dec. 2008).

20. *Id.*

21. *Id.* at 42.

22. PATRICK PURCELL, RETIREMENT PLAN PARTICIPATION AND CONTRIBUTIONS: TRENDS FROM 1998 TO 2006, CRS REPORT FOR CONGRESS 1 (2009), [http://assets.opencrs.com/rpts/RL33116\\_20090130.pdf](http://assets.opencrs.com/rpts/RL33116_20090130.pdf) (More specifically, “[a]ccording to the data collected by the Census Bureau, there were 99.2 million workers aged and 21 older with a paid job in the private sector in an average month in the first half of 2006. Of this number, 61.7 million (62.2%) worked for employers that sponsored retirement plans—either pensions or 401(k)-type plans—and 44.7 million workers (45.1%) participated in employer-sponsored retirement plans.”).

23. Patrick Purcell & John T. Topoleski, *401(k) Plans and Retirement Savings: Issues for Congress*, CONGRESSIONAL RES. SERV. (CRS Washington, D.C.), July 14, 2009, at 3.

24. *Id.*

25. *Id.*

elected to participate in the plan.<sup>26</sup>

In order to encourage employee participation, Congress included automatic enrollment provisions in the Pension Protection Act of 2006.<sup>27</sup> Automatic enrollment provides that an employee will become a participant and a pre-determined percentage will be deferred on a pre-tax basis from the employee's pay unless the employee elects a different percentage or opts out of participation.<sup>28</sup> According to a study by Hewitt Associates of approximately 150 mid- to large-sized employers, 51% of the employers surveyed offer automatic enrollment in 2009, compared to 44% in 2008.<sup>29</sup> However, among the companies that do not offer automatic enrollment, only 25% are somewhat or very likely to add it for new hires in 2009, compared to 57% in 2008, and only 15% are likely to adopt it for existing employees in 2009, compared to 27% in 2008.<sup>30</sup>

In 2007, Congress proposed legislation that would mandate automatic IRAs, which would include an automatic enrollment feature.<sup>31</sup> The Automatic IRA Bill of 2007<sup>32</sup> would have required companies to make payroll deposits into IRAs for employees who were not eligible to participate in a retirement plan during the prior year and who have not satisfied a plan's eligibility requirements for the current year.<sup>33</sup>

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26. *Id.*

27. ERISA section 514(e) was added by section 902(f)(1) of the Pension Protection Act of 2006, P.L. No. 109-280, 8/17/2006 120 Stat. 780 (2006). Section 514(e)(1) provides that all state laws are preempted to the extent that they would "directly or indirectly prohibit or restrict the inclusion in any plan of an automatic contribution arrangement . . ." ERISA § 514(e)(1), 29 U.S.C. § 1144(e)(1) (2006). The DOL indicated in the Preamble to 29 C.F.R. § 2550 (2008) that:

Analyses of automatic enrollment programs demonstrate that such programs increase participation. The increase is most pronounced among employees whose participation rates otherwise tend to be lowest, namely lower-paid, younger and shorter-tenure employees . . . Plans implementing automatic enrollment programs may increase their participation rates on average from approximately 70 percent to perhaps 90 percent. Consequently, the Department estimates that this regulation will increase overall 401(k) participation rates from 73 percent to between 77 percent and 80 percent.

Default Investment Alternatives Under Participant Directed Individual Account Plans, 72 Fed. Reg. 60,451, 60,470 (Oct. 24, 2007) (codified 29 C.F.R. pt 2550) (footnotes omitted).

28. ERISA section 514(e)(2) uses the term "automatic contribution arrangement" and describes it as an arrangement, "[U]nder which a participant is treated as having elected to have the plan sponsor make such contributions in an amount equal to a uniform percentage of compensation provided under the plan until the participant specifically elects not to have such contributions made (or specifically elects to have such contributions made at a different percentage) . . ." ERISA § 514(e)(2), 29 U.S.C. § 144(e)(2)(B).

29. Rebecca Moore, *Economy Slows Auto Enrollment Trend*, PLANSPONSOR.COM, Feb. 2, 2009, [http://www.plansponsor.com/pi\\_type11/?RECORD\\_ID=44850&page=3](http://www.plansponsor.com/pi_type11/?RECORD_ID=44850&page=3).

30. *Id.*

31. Automatic IRA Bill of 2007, H.R. 2167, S. 1141, 110th Cong. § 408B(a) (2007).

32. *Id.*

33. *Id.* at § 408B(b)-(c).

Although the Automatic IRA Bill of 2007 was never enacted, states may try to find ways to increase participation using similar methods.

Given the low percentage of workers who participate in 401(k) plans, states are likely to pass laws designed to increase participation. For small companies in particular, states will want to make it easier, if not mandatory, for employers to adopt and operate 401(k) plans. States may also want to encourage or require companies that have 401(k) plans to cover all employees, include automatic enrollment provisions in their plans or alternatively, mandate that employers without 401(k) plans implement automatic IRAs. However, as discussed below, these types of state laws should be preempted by ERISA.

## 2. Fees

Fees can have a considerable impact on the amount of money workers will have in their 401(k) plans at retirement.<sup>34</sup> The U.S. Department of Labor's ("DOL") publication on plan fees includes an example where a 1% increase in fees results in a 28% decrease in the value of the participant's account balance at retirement.<sup>35</sup>

The DOL has issued proposed regulations to increase fee disclosures, but these have not been finalized at the time this Article went to publication.<sup>36</sup> The DOL issued proposed regulations to require

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34. Davis, *supra*, note 9, at 1006 (discussing the information needed by fiduciaries of and participants in 401(k) plans about the fees charged to their plans); Jonathan Barry Forman, *The Future of 401 (k) Plan Fees*, in NEW YORK UNIVERSITY REVIEW OF EMPLOYEE BENEFITS AND COMPENSATION 9-1, 9-3 (Alvin D. Lurie ed., 2007); Colleen E. Medill, *Challenging the Four "Truths" of Personal Social Security Accounts: Evidence from the World of 401(k) Plans*, 81 N.C. L. REV. 901, 907-08, 937-46 (2003) (discussing the effect of fees on employees' account balances at retirement).

35. The DOL publication provides the following example:

Assume that you are an employee with 35 years until retirement and a current 401(k) account balance of \$25,000. If returns on investments in your account over the next 35 years average 7 percent and fees and expenses reduce your average returns by 0.5 percent, your account balance will grow to \$227,000 at retirement, even if there are no further contributions to your account. If fees and expenses are 1.5 percent, however, your account balance will grow to only \$163,000. The 1 percent difference in fees and expenses would reduce your account balance at retirement by 28 percent.

A Look at 401(k) Plan Fees, U.S. DEP'T OF LABOR (Employee Benefits Security Admin., Washington, D.C.), available at [http://www.dol.gov/ebsa/publications/401k\\_employee.html](http://www.dol.gov/ebsa/publications/401k_employee.html) (last visited Oct. 24, 2009).

36. A Memorandum for the Heads of Executive Departments and Agencies from Rahm Emanuel, Assistant to the President and Chief of Staff was published in the Federal Register on January 26, 2009 and stated that all proposed and final regulations that have not been published in the Federal Register should be withdrawn to give the new administration a chance to review them. Memorandum for the Heads of Executive Departments and Agencies, Notices, 74 Fed. Reg. 4435

service providers to disclose the direct and indirect compensation they receive to plan fiduciaries<sup>37</sup> as well as proposed regulations to increase the disclosures that fiduciaries must make to participants in 401(k) plans about certain fees paid by the plan.<sup>38</sup>

The DOL's efforts have been met with opposition. In response to the proposed regulations on the disclosure of compensation received by and potential conflict of interest for service providers,<sup>39</sup> the DOL received over eighty written comments, many of which criticized the proposed regulations, as well as nearly thirty requests to testify on the issue.<sup>40</sup> The DOL also received nearly one hundred comments on its proposed regulations requiring fiduciaries to disclose fees to participants in 401(k) plans.<sup>41</sup> Additionally, Rep. George Miller has expressed that he does not believe that the proposed regulations are adequate and has stated that “[w]hile a step in the right direction, the Department of Labor’s proposal would still allow financial firms to hide many fees that they take from 401(k) plan participants’ accounts.”<sup>42</sup>

(Jan. 26, 2009).

37. Proposed DOL Reg. § 2550.408b-2 would require certain types of service providers to disclose the types of services that they will provide to plans, their compensation for those services, and potential conflicts of interest. These written disclosures would be required before a service provider entered into, extended, or renewed an arrangement with a plan. The DOL defined compensation very broadly for this purpose and included “money or any other thing of monetary value . . . received, or to be received, directly from the plan or plan sponsor or indirectly . . . in connection with the services to be provided . . . .” Reasonable Contract or Arrangement Under Section 408(b)(2)-Fee Disclosure, 72 Fed. Reg. 70,988, 71,004 (Dec. 13, 2007) (codified 29 C.F.R. pt. 2550).

38. Proposed DOL Reg. § 2550.404a-5 would require investment information, including fee and expense information to be provided to participants in participant-directed individual plans, such as 401(k) plans. Fiduciaries would be required to make these disclosures in order to satisfy their fiduciary obligations. Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans, 73 Fed. Reg. 43,014, 43,015 (July 23, 2008) (codified at 29 C.F.R. pt. 2550).

39. Reasonable Contract or Arrangement Under Section 408(b)(2)-Fee Disclosure, 72 Fed. Reg. 70,988, 70,989 (Dec. 13, 2007) (codified at 29 C.F.R. pt. 2550).

40. Employee Benefits Security Administration of the U.S. Department of Labor, Reasonable Contract Or Arrangement Under Section 408(b)(2) Fee Disclosure, [http://www.dol.gov/ebsa/regs/cmt-408\(b\)\(2\)-combined.html](http://www.dol.gov/ebsa/regs/cmt-408(b)(2)-combined.html) (displaying written responses and requests to testify to its proposed regulation under ERISA § 408(b)(2), 29 U.S.C. § 1108(b)(2) (2006)) (last visited Nov. 1, 2009) [hereinafter Fee Disclosure].

41. Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans, 73 Fed. Reg. at 43,015; *see also* Employee Benefits Security Administration of the U.S. Department of Labor, Fiduciary Requirements for Disclosure in participant-Directed Individual Account Plans, <http://www.dol.gov/ebsa/regs/cmt-fiduciaryrequirements.html> (displaying written responses it received to its participant fee disclosure proposed regulation) (last visited Nov. 1, 2009).

42. Doug Halonen, *Fee Disclosure Timetable Met with Some Skepticism*, PENSION & INVESTMENTS ONLINE, Aug. 4, 2008, <http://www.pionline.com/apps/pbcs.dll/article?AID=/20080804/PRINTSUB/892842826/1005> (last

Some states' views of the proposed regulations are likely to differ from the views of the DOL as well. States may disagree with the approaches taken by the federal government and/or have alternative ideas that they would like to implement to address these issues. Given the significance of plan fees on retirement assets and the attention that has been given this issue, states are likely to want to enact laws that regulate in this area. Potential approaches could include negotiating with service providers on behalf of plans or facilitating the aggregation of plans. They could also attempt to require plans offered by employers in their states to include low cost investments or mandate that the employers pay a percentage of the fees.

### 3. Benefit Adequacy

Doubt has been raised concerning the ability of 401(k) plans to provide participants with adequate retirement benefits.<sup>43</sup> The Government Accountability Office ("GAO") commented in its report on savings in defined contribution plans that "workers may receive limited or no contributions from their employers, spend accumulated savings prior to retirement, or choose not to participate in a pension plan at all, ultimately arriving at retirement with insufficient savings to support themselves."<sup>44</sup> The DOL commented in the Preamble to the proposed default investment regulation that:

It is well established that many of America's workers are not adequately saving for retirement. Part of the retirement savings problem is attributable to employees who, for a wide variety of

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visited Oct. 24, 2009).

43. See, e.g., Alicia H. Munnell & Annika E. Sundén, *401(k) Plans are Still Coming up Short*, 43 CENTER FOR RETIREMENT RES. AT B.C. 1, 7 (2006), available at [http://crr.bc.edu/images/stories/Briefs/ib\\_43.pdf?phpMyAdmin=43ac483c4de9t51d9eb41](http://crr.bc.edu/images/stories/Briefs/ib_43.pdf?phpMyAdmin=43ac483c4de9t51d9eb41) (concluding that 401(k) plans must be made easier and more automatic in order to effectively enable participants to save for retirement). Alternatively, Peter J. Brady argues that "moderate 401(k) contribution rates can lead to adequate income replacement rates in retirement for many workers; that adequate asset accumulation can be achieved using only a 401(k) plan; and that these results do not rely on earning an investment premium on risky assets." Peter J. Brady, *Can 401(k) Plans Provide Adequate Retirement Resources*, (Pension Research Council Working Paper WP2009-01 Jan. 2009), available at <http://www.pensionresearchcouncil.org/publications/document.php?file=709>.

44. UNITED STATES GOVERNMENT ACCOUNTABILITY OFFICE ACCOUNTING OFFICE, REPORT TO THE CHAIRMAN, COMMITTEE ON EDUCATION AND LABOR, HOUSE OF REPRESENTATIVES, PRIVATE PENSIONS: LOW DEFINED CONTRIBUTIONS PLAN SAVINGS MAY POSE CHALLENGES TO RETIREMENT SECURITY, ESPECIALLY FOR MANY LOW-INCOME WORKERS 1 (Nov. 2007).

reasons, do not take advantage of the opportunity to participate in their employer's defined contribution pension plan (such as a 401(k) plan).<sup>45</sup>

States may attempt to increase the amount of benefits that their residents will have at retirement by regulating 401(k) plans. For example, states may attempt to require plans to include automatic enrollment provisions. They could also take an approach similar to the "pay or play" laws, where employers would be required to pay a tax if their contributions to their retirement plans did not reach a certain threshold.

### C. Actions Taken By State Governments

Numerous states have considered ways in which to provide accessibility to retirement savings programs to their residents. States have primarily considered setting up programs to encourage individual retirement accounts ("IRAs") or voluntary defined contribution plans.

Connecticut has considered legislation to establish a defined contribution plan to be available to self-employed individuals, small employers and non-profit organizations.<sup>46</sup> The Commerce Committee of the Connecticut General Assembly stated that the "program this bill seeks to establish must seek (1) to minimize costs by helping small employers, and individuals, (2) arrangements and investments through economies of scale, and (3) standardization and other measures."<sup>47</sup> This was the first state-administered 401(k) plan approved by a state legislature.<sup>48</sup> Although the bill was passed by Connecticut's Senate in 2008, it was not enacted into law.<sup>49</sup> Connecticut's Senate re-introduced the bill in February 2009.<sup>50</sup>

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45. Default Investment Alternatives Under Participant Directed Individual Account Plans, 71 Fed. Reg. 56,806 (Sept. 27, 2006) (codified at 29 C.F.R. pt. 2550).

46. COMMERCE COMMITTEE JOINT FAVORABLE REPORT, *supra* note 12.

47. *Id.*

48. Press Release, State Sen. Donald Williams, Democratic Senate Makes History—Passes 1st in the Nation Universal 401(k) Plan (Apr. 24, 2008), *available at* <http://www.senatedems.ct.gov/pr/williams-080424b.html>.

49. CONN. GEN. ASSEMBLY, 2008 REGULAR SESSION BILL INFORMATION: AN ACT CONCERNING SMALL BUSINESS RETIREMENT PLANS, S.B. NO. 652 (Conn. 2008), *available at* [http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill\\_num=652&which\\_year=2008&SUBMIT1.x=9&SUBMIT1.y=12&SUBMIT1=Normal](http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill_num=652&which_year=2008&SUBMIT1.x=9&SUBMIT1.y=12&SUBMIT1=Normal) (last visited Oct. 24, 2009).

50. CONN. GEN. ASSEMBLY, 2009 REGULAR SESSION BILL INFORMATION: AN ACT CONCERNING SMALL BUSINESS RETIREMENT PLANS, S.B. NO. 971 (Conn. 2009), *available at* [http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill\\_num=971&which\\_year=2009&SUBMIT1.x=7&SUBMIT1.y=10&SUBMIT1=Normal](http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill_num=971&which_year=2009&SUBMIT1.x=7&SUBMIT1.y=10&SUBMIT1=Normal) (last visited Oct. 24, 2009).

The Washington state legislature directed the Department of Retirement Systems to investigate and design a voluntary retirement accounts program, such as a defined contribution plan, to be made available to workers in the state.<sup>51</sup> The report identified two types of payroll deduction or IRAs and a state administered 401(k) as options.<sup>52</sup> Although the Department of Retirement Systems recommended that the state start with one of the payroll deduction or IRA options, bills were introduced in both the state Senate and House of Representatives for both employer sponsored plans and IRAs.<sup>53</sup> As of the date this Article went to publication, the bills have not been enacted.

In Maryland, legislation was introduced to create voluntary employee accounts.<sup>54</sup> The legislation would have required the State Board of Trustees of the Maryland Teachers and State Employees Supplemental Retirement Plans to “implement, maintain, and administer the Program and specified retirement plans for specified employees . . . .”<sup>55</sup> The Program is defined in the House Bill as “Maryland Voluntary Employee Accounts Program established under this title offering retirement plans to participating employers and, if the board determines, IRAs to the residents of Maryland.”<sup>56</sup> The bill was not enacted.<sup>57</sup>

In Michigan, Governor Jennifer Granholm advocated the adoption of a state sponsored retirement plan. In her 2006 State of the State Address, she explained, “My administration will design and open a 401(k) plan, like the state’s plan, for those workers of small companies who don’t offer a pension plan. At minimal expense to state government, we will help tens of thousands of Michigan workers save for their retirement and achieve economic security.”<sup>58</sup> She reiterated her

51. Crenshaw, *supra* note 10, at 3-4; UVRA UPDATE, STATES UPDATES, *supra* note 10, at 4.

52. WASHINGTON VOLUNTARY ACCOUNTS REPORT TO THE LEGISLATURE 1 (2009), *available at* <http://www.spectrumension.com/media/4359/wa%20st%20vol%20ret%20acct%20report%20final%202009%20feb%206.pdf> (last visited July 22, 2009).

53. S.B. 5791, 61st Leg., Reg. Sess. (Wash. 2009); H.B. 1893, 61st Leg., Reg. Sess. (Wash. 2009).

54. UVRA UPDATE, STATES UPDATES, *supra* note 10, at 3.

55. MD. GEN. ASSEMBLY, 2008 REGULAR SESSION BILL INFORMATION: HOUSE BILL 1228 (2008), <http://mlis.state.md.us/2008rs/billfile/hb1228.htm>; *see also* MD. GEN. ASSEMBLY, 2008 REGULAR SESSION BILL INFORMATION: SENATE BILL 728 (2008), *available at* <http://mlis.state.md.us/2008rs/billfile/sb0728.htm>.

56. H.B. 1228, 2008 Leg., Gen. Assem. Sess. (Md. 2008).

57. *See* MD. GEN. ASSEMBLY, SENATE CURRENT STATUS REPORT, 425TH SESS., at 43 (2008), *available at* <http://www.mlis.state.md.us/2008rs/CurrentStatusReport/SenateCurrentStatusReport.pdf>.

58. Governor Jennifer Granholm, 2006 State of the State Address, Working Our Plan, Securing Our Future 15 (Jan. 25, 2006), *available at*

plan in her 2007 State of the State Address when she said “I also urge you to finally pass the small business retirement plan I introduced at this podium last year . . . Rep. Bieda and Sen. Thomas have introduced bills to turn this good idea into law. I urge you to pass them now.”<sup>59</sup> The bills were not enacted into law.<sup>60</sup>

Other states that have considered retirement savings programs for private-sector employees include California, Illinois, Indiana, Massachusetts, Pennsylvania, Rhode Island, Tennessee, Virginia, and West Virginia.<sup>61</sup>

#### *D. Potential Future Legislation By State Governments*

Given the significant attention placed on 401(k) plans, states are likely to look for ways to improve them. This is particularly true, given the challenges faced by 401(k) plans with respect to covering a significant portion of workers, keeping the fees paid by the plan at a prudent level, and helping participants to attain adequate benefits at retirement. Even though retirement plans are heavily regulated, states are likely to believe that they can improve upon the current system.

Furthermore, there are considerable incentives for states to intervene. Residents that lack adequate retirement savings are likely to turn to their states’ resources to assist them during retirement if they do not have sufficient retirement assets, regardless of whether the shortage results from excessive fees being paid by their 401(k) plans or their failure to participate, to contribute enough, or to properly invest their assets. A report issued by the Washington Department of Retirement Systems commented that:

The growing realization is that a significant portion of the population

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[http://www.michigan.gov/documents/SOS\\_2006\\_148708\\_7.pdf](http://www.michigan.gov/documents/SOS_2006_148708_7.pdf).

59. Governor Jennifer Granholm, 2007 State of the State Address, *Our Moment, Our Choice: Investing in Michigan’s People* 5 (Feb. 6, 2007), available at [http://www.michigan.gov/documents/gov/2007\\_SOS\\_186092\\_7.pdf](http://www.michigan.gov/documents/gov/2007_SOS_186092_7.pdf).

60. Senator Samuel Thomas introduced SB 0024 and Representative Steve Bieda introduced HB 4135. S. 0024, 94th Leg., Reg. Sess. (Mich. 2007); H.R. 4135, 94th Leg., Reg. Sess. (Mich. 2007).

61. See, e.g., A.B. 2940, Cal. Leg., 2007-08 Reg. Sess., at 1-4 (Cal. 2008); S.B. 25, 79th Leg., 1st Reg. Sess. (W. Va. 2009); S.B. 5791, 61st Leg., 2009 Reg. Sess. (Wash. 2009); S.J. Res. 1075, 105th Gen. Assem., Reg. Sess. (Tenn. 2008); H.B. 1669, 2007 Gen. Assem., 2007 Reg. Sess. (Pa. 2007); H.B. 2026, 2009 Gen. Assem., 2009 Gen. Assem., 2009 Reg. Sess. (Va. 2009). See generally Crenshaw, *supra* note 10; UVRA UPDATE, STATES UPDATES, *supra* note 10; Dory Rand, *Illinois Voluntary Accounts*, SARGENT SHRIVER NATIONAL CENTER ON POVERTY LAW, Jan. 18, 2007, <http://www.mobilityagenda.org/illinois.pdf>.

may not be saving for retirement is emerging as a national social concern. The Washington State Legislature, with the support of stakeholders such as the Economic Opportunity Institute (EOI), has recognized the potential impact inadequate retirement preparedness may have on many of the state's citizens and the state's economy.<sup>62</sup>

Consequently, states are likely to consider ways in which they can improve 401(k) plans, especially with respect to coverage, fees, and benefit adequacy, without being preempted by ERISA. As the Economic Opportunity Institute noted when discussing Washington's consideration of universal retirement accounts, "As this is the first program of its kind in the nation, there are numerous IRS, Employee Retirement Income Security Act (ERISA), and legal issues to consider."<sup>63</sup>

## II. ERISA PREEMPTION

ERISA's preemption provisions initially appear fairly straightforward. They generally provide that ERISA "shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan . . . ."<sup>64</sup> State laws are defined as "all laws, decisions, rules, regulations, or other State action having the effect of law, of any State."<sup>65</sup> ERISA also indicates that a law of the United States that is only applicable to the District of Columbia is also considered to be a state law for this purpose.<sup>66</sup> ERISA contains several explicit exceptions to its preemption rule, which implies that these are the only exemptions from the preemption provisions.<sup>67</sup>

ERISA's legislative history indicates that ERISA's preemption provisions were intended to be interpreted broadly.<sup>68</sup> Although the U.S.

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62. SANDRA J. MATHESON, WASHINGTON STATE DEPT. OF RETIREMENT SYSTEMS, WASHINGTON VOLUNTARY ACCOUNTS REPORT TO THE LEGISLATURE 3 (2009), <http://www.spectrumension.com/media/4359/wa%20st%20vol%20ret%20acct%20report%20final%202009%20feb%206.pdf> (last visited Oct. 24, 2009).

63. UVRA UPDATE, STATES UPDATES, *supra* note 10, at 4.

64. Employment Retirement Income Security Act (ERISA) of 1974 § 514(a), 29 U.S.C. § 1144(a) (2006).

65. ERISA § 514(c)(1), 29 U.S.C. § 1144(c)(1). ERISA section 514(c)(2) indicates that "The term 'State' includes a State, any political subdivisions thereof, or any agency or instrumentality of either, which purports to regulate, directly or indirectly, the terms and conditions of employee benefit plans covered by this subchapter." ERISA § 514(c)(2), 29 U.S.C. § 1144(c)(2).

66. ERISA § 514(c)(1), 29 U.S.C. § 1144(c)(1).

67. *See* ERISA § 514(b), 29 U.S.C. § 1144(b).

68. *See* Alessi v. Raybestos-Manhattan, Inc., 451 U.S. 504, 522-23 (1981).

Supreme Court initially interpreted ERISA's language broadly, the Court has since limited the circumstances under which state laws will be preempted.<sup>69</sup> As discussed below, the Court should interpret ERISA's preemption provisions broadly with respect to 401(k) plans in order to promote uniform administration, which results in economies of scale and reduced costs for plans. Additionally, workers at companies that operate in multiple states should be able to transfer among the company's locations without having to worry about different plan provisions applying in other locations. Finally, organizations that represent varying interested parties with respect to ERISA plans should be able to work with the U.S. Congress and the variety of federal agencies that oversee ERISA plans to facilitate workable rules for ERISA plans and should not have to deal with state agencies and legislators as well.

#### A. Legislative Background

The legislative history for ERISA's preemption provisions indicates that Congress intended for retirement plans to be exclusively within the jurisdiction of the federal government.<sup>70</sup> The U.S. Supreme Court in *Shaw v. Delta Air Lines, Inc.*<sup>71</sup> explains "[C]ongress used the words 'relate to' in [section] 514(a) in their broad sense. . . . The bill that became ERISA originally contained a limited pre-emption clause, applicable only to state laws relating to the specific subjects covered by ERISA."<sup>72</sup>

For example, statements by ERISA's sponsors such as Representative Dent indicated that they intended for ERISA's preemption provisions to be broad.<sup>73</sup> Representative Dent stated:

Finally, I wish to make note of what is, to many, the crowning

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69. See *District of Columbia v. Greater Wash. Bd. of Trade*, 506 U.S. 125, 129-30 & n.1 (1992).

70. See generally *Alessi*, 451 U.S. at 522 (noting that 29 U.S.C. § 1144(a) aids the courts as an "explicit congressional statement about the pre-emptive effect of its action"); James A. Wooten, *A Legislative and Political History of ERISA Preemption, Part 1*, 14 J. OF PENSION BENEFITS 31, 32 (2006) (noting that "[t]he desire for federal preemption was a key factor—perhaps, the key factor—in creating the coalition that pushed ERISA through Congress"); James A. Wooten, *A Legislative and Political History of ERISA Preemption, Part 2*, 14 J. OF PENSION BENEFITS 5, 10 (2007) ("[T]he politics of preemption led Congress to pass a more ambitious slate of reforms than it might otherwise have done."); Wooten, *supra* note 2 at 15.

71. 463 U.S. 85 (1983).

72. *Id.* at 98.

73. *Id.* at 98-99.

achievement of this legislation, the reservation to Federal authority the sole power to regulate the field of employee benefit plans. With the preemption of the field, we round out the protection afforded participants by eliminating the threat of conflicting and inconsistent State and local regulation.<sup>74</sup>

Senator Williams also expressed his view that ERISA's preemption provisions were intended to apply broadly.<sup>75</sup> He stated:

It should be stressed that with the narrow exceptions specified in the bill, the substantive and enforcement provisions of the conference substitute are intended to preempt the field for Federal regulations, thus eliminating the threat of conflicting or inconsistent State and local regulation of employee benefit plans. This principle is intended to apply in its broadest sense to all actions of State or local governments, or any instrumentality thereof, which have the force or effect of law.<sup>76</sup>

The U.S. Supreme Court also stated in *FMC Corp. v. Holliday*<sup>77</sup> that "Congress intended by ERISA to 'establish pension plan regulation as exclusively a federal concern.'"<sup>78</sup> The Court also described Congress' desire to avoid "endless litigation over the validity of State action . . ."<sup>79</sup>

Thus, the legislative history for ERISA indicates that ERISA was intended to replace current and future state laws that relate to employee benefit plans. Congress' objectives in enacting ERISA's preemption provisions were to avoid the potential for conflicting or inconsistent state and federal laws and avoid entangling plans in legislation regarding the validity of state laws.<sup>80</sup> Despite this, the U.S. Supreme Court's narrowing interpretation of ERISA's preemption provisions and of the circumstances under which state laws are preempted will likely encourage states to attempt to pass laws that regulate ERISA plans.<sup>81</sup>

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74. *Id.* at 99 (citing 120 CONG. REC. 29,197 (1974)).

75. *Id.*

76. *Id.* (citing 120 CONG. REC. 29,933 (1974)).

77. 498 U.S. 52 (1990).

78. *Id.* at 64 (1990) (citing *Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504, 523 (1981)).

79. *Id.* at 65 (citing 120 CONG. REC. 29,942 (1974) (remarks of Sen. Javits)).

80. *Id.* at 65; *see also Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 98-99 (1983).

81. *See discussion supra* Part II.B-C (discussing the emergence of State laws regulating 401(k) plans).

### B. Supreme Court's Interpretation of "Relate To"

The U.S. Supreme Court's interpretation of ERISA's preemption provisions was initially very broad, but has narrowed significantly in recent years.<sup>82</sup> The Court in *Shaw v. Delta Air Lines, Inc.* stated that "[i]n fact, however, Congress used the words 'relate to' in [section] 514(a) in their broad sense. To interpret [section] 514(a) to preempt only state laws specifically designed to affect employee benefit plans would be to ignore the remainder of [section] 514."<sup>83</sup> However, the Court narrowed its approach beginning with *N.Y. State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*<sup>84</sup> In *Travelers*, the

82. Compare *Shaw*, 463 U.S. at 96 ("The breadth of [section] 514(a)'s pre-emptive reach is apparent from that section's language."), with *N.Y. State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 662 (1995) (holding that the state law at issue did not "bear the requisite 'connection with' ERISA plans to trigger pre-emption").

83. *Shaw*, 463 U.S. at 98. *Shaw* involved a New York law that prohibited discrimination in employee benefit plans due to pregnancy and a New York law that required companies to pay sick leave benefits to workers who could not work as a result of pregnancy or other non-occupational disabilities. *Id.* at 88. The Court framed its role for preemption purposes as determining Congress' intent in enacting ERISA. *Id.* at 88-89, 95. The Court found that the New York laws were clearly preempted and stated:

We have no difficulty in concluding that the Human Rights Law and Disability Benefits Law "relate to" employee benefit plans. The breadth of [section] 514(a)'s pre-emptive reach is apparent from that section's language. A law "relates to" an employee benefit plan, in the normal sense of the phrase, if it has a connection with or reference to such a plan . . . . We must give effect to this plain language unless there is good reason to believe Congress intended the language to have some more restrictive meaning . . . . In fact, however, Congress used the words "relate to" in [section] 514(a) in their broad sense.

*Id.* at 96-98 (citing *Consumer Product Safety Comm'n v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980)).

84. 514 U.S. 645 (1995). In *Travelers*, the U.S. Supreme Court restricted the scope of ERISA's preemption provisions. See *id.* at 662. In *Travelers*, New York subjected health maintenance organizations ("HMOs") to surcharges and required hospitals to collect surcharges from patients covered by a commercial insurer. *Id.* at 649. Hospitals were not required to collect surcharges for patients insured by Blue Cross/Blue Shield plans. *Id.* Several commercial insurers who served as fiduciaries of ERISA plans sued New York state officials, arguing that the state laws were preempted by ERISA. *Id.* at 649. The U.S. Supreme Court acknowledged its prior cases, including *Shaw v. Delta Air Lines, Inc.* and implied that the *Travelers* case merely clarified the breadth of ERISA's preemption provisions. *Id.* at 655. The Court stated:

The governing text of ERISA is clearly expansive. Section 514(a) marks for pre-emption "all state laws insofar as they . . . relate to any employee benefit plan" covered by ERISA, and one might be excused for wondering, at first blush, whether the words of limitation ("insofar as they . . . relate") do much limiting. If "relate to" were taken to extend to the furthest stretch of its indeterminacy, then for all practical purposes pre-emption would never run its course, for "[r]eally, universally, relations stop nowhere . . . ." But that, of course, would be to read Congress's words of limitation as mere sham, and to read the presumption against pre-emption out of the law whenever Congress

Court stated that the phrase “relate to” could continue indefinitely and would thereby lack meaning.<sup>85</sup> The Court did not delineate any specific parameters, but indicated that there is a presumption that state laws are not preempted and held that a law that only has an indirect economic effect on an ERISA plan is not preempted.<sup>86</sup>

The Court has set forth several principles regarding the determination of whether a state law is preempted by ERISA. In *Shaw v. Delta Air Lines, Inc.*, the Court stated that a state law relates to an employee benefit plan if it refers to an ERISA plan or has a connection with an ERISA plan.<sup>87</sup> The Court has held that state laws are preempted where they act on an ERISA plan, an ERISA plan is essential to the law’s operation, or the state law requires a particular plan design, mandates the manner in which plans are administered, or conflicts with ERISA.<sup>88</sup> The Court has held that state laws are not preempted where they only have an indirect economic impact on ERISA plans or are laws of general applicability.<sup>89</sup>

#### 1. Act on ERISA Plans or Where ERISA Plans Are Essential

The U.S. Supreme Court has held that a state law refers to an ERISA plan if the law acts immediately and exclusively on an ERISA plan or an ERISA plan is essential to the law’s operation.<sup>90</sup> The Court has held that a state law was preempted as the existence of an ERISA plan was critical to the law’s existence where the law allowed plaintiffs to recover in a wrongful discharge action if they could establish that the employer’s principal reason for terminating their employment was to avoid contributing to its retirement plan for them or paying retirement benefits to them was preempted.<sup>91</sup> The Court stated that “the existence

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speaks to the matter with generality. That said, we have to recognize that our prior attempt [in *Shaw*] to construe the phrase “relate to” does not give us much help drawing the line here.

*Id.* (quoting HENRY JAMES, RODERICK HUDSON at xv (Scribner 1977) (1907)).

85. *Id.* (quoting, HENRY JAMES, RODERICK HUDSON at xv (Scribner 1977) (1907)).

86. *Id.* at 654, 668.

87. *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 96-97 (1983).

88. *See, e.g., Ingersoll Rand Co. v. McClendon*, 498 U.S. 133, 139-40 (1990); *FMC Corp. v. Holliday*, 498 U.S. 52, 60 (1990); *Boggs v. Boggs*, 520 U.S. 833, 841 (1997).

89. *See, e.g., Shaw*, 463 U.S. at 100 n.21; *Mackey v. Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825, 830-38 & n.12 (1998).

90. *Cal. Div. of Labor Standards Enforcement v. Dillingham Constr., N.A., Inc.*, 519 U.S. 316, 325 (1997).

91. *Ingersoll-Rand*, 498 U.S. at 139-40 (1990). The Texas statute that allowed plaintiffs to recover in a wrongful discharge action if they could establish that the employer’s principal reason

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of a pension plan is a critical factor in establishing liability under the State's wrongful discharge law. As a result, this cause of action relates not merely to pension benefits, but to the existence of the *plan* itself."<sup>92</sup>

The Court also held that a state law was preempted because it referenced ERISA plans.<sup>93</sup> A state law was preempted where it required employers who provided health insurance to provide continuation coverage that was not required under federal law.<sup>94</sup> The state law would have had no substance without an ERISA plan.<sup>95</sup>

Thus, the Court held that the state laws in these cases were preempted due to the significant involvement of ERISA plans. The state laws lacked meaning without the existence of ERISA plans. Therefore, state laws that rely on ERISA plans for their meaning or that substantially involve ERISA plans will be preempted.

## 2. Mandatory Design or Administration

The U.S. Supreme Court has also held that state laws are preempted if they require plans to be designed or administered in a particular manner. The Court found that a state law that prevented employee benefit plans from exercising their subrogation rights was preempted.<sup>96</sup> The Court stated that requiring companies "to design their programs in an environment of differing State regulations would complicate the administration of nationwide plans . . . ."<sup>97</sup> The Court held that this would create "considerable inefficiencies in benefit program operation . .

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for terminating their employment was to avoid contributing to its retirement plan for them or paying retirement benefits to them. *See id.* at 135. The Court held that the statute was preempted because it related to ERISA plans. *Id.* at 140.

92. *Id.* at 139-40.

93. *District of Columbia v. Greater Wash. Bd. of Trade*, 506 U.S. 125, 130-31 (1992). In *Greater Washington Board of Trade*, a law of the District of Columbia required employers who provided health insurance to continue to cover employees while they were receiving or eligible to receive workers' compensation benefits. *Id.* at 126-27. The Court held that "[s]uch employer-sponsored health insurance programs are subject to ERISA regulation . . . any state law imposing requirements by reference to such covered programs must yield to ERISA." *Id.* at 130-31.

94. *Id.* at 127-28.

95. *Id.* at 132-33.

96. *FMC Corp. v. Holliday*, 498 U.S. 52, 54, 65 (1990). *FMC Corp.* involved a Pennsylvania law that prevented employee benefit plans from exercising their subrogation rights. *Id.* at 54. The law, in effect, prohibited companies from designing their ERISA plans with subrogation provisions for participants in Pennsylvania as these provisions would not be enforceable. *Id.* at 59-60. The Court held that the use of subrogation provisions was a plan design feature. *Id.* at 60-61. The Court emphasized that the state's regulation of a plan design feature was preempted by ERISA because it would subject a plan to potentially conflicting state regulations. *Id.* at 65.

97. *Id.* at 60 (citing *Fort Halifax Packing Co. v. Coyne*, 482 U.S. 1, 10 (1987)).

..<sup>98</sup>

The U.S. Supreme Court also held that a state law that automatically revoked a designation of beneficiary upon divorce was preempted because it interfered with plan administration.<sup>99</sup> The Court explained that the statute had “an impermissible connection with ERISA plans” because it “binds ERISA plan administrators to a particular choice of rules for determining beneficiary status.”<sup>100</sup>

Thus, the Court has held that state laws are preempted if they have a substantial impact on a plan’s design or interfere with the administration of a plan.<sup>101</sup> The Court emphasized the importance of uniformity in the administration of plans, which would not be possible with state laws that mandated actions by or features in ERISA plans that could potentially conflict with the plans’ provisions or other state laws.<sup>102</sup> State laws that attempt to regulate 401(k) plans will therefore be preempted if they interfere with plan design or administration.

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98. *Id.* (quoting *Coyne*, 482 U.S. at 11).

99. *Egelhoff v. Egelhoff*, 532 U.S. 141, 147 (2001). In *Egelhoff*, a Washington statute automatically revoked a spousal beneficiary designation upon the participant’s divorce. *Id.* at 143. The state law would require plans to continuously monitor state laws to determine their impact on the plan’s administration. *See id.* at 147-48. The Court explained the importance of uniformity when administering ERISA plans. It stated:

The Washington statute also has a prohibited connection with ERISA plans because it interferes with nationally uniform plan administration. One of the principal goals of ERISA is to enable employers “to establish a uniform administrative scheme, which provides a set of standard procedures to guide processing of claims and disbursement of benefits.” Uniformity is impossible, however, if plans are subject to different legal obligations in different States.

*Id.* at 148 (citing *Coyne*, 482 U.S. at 9).

The Court also explained its reasoning as to why the state law created a risk for plan administration. It stated:

The Washington statute at issue here poses precisely that threat. Plan administrators cannot make payments simply by identifying the beneficiary specified by the plan documents. Instead they must familiarize themselves with state statutes so that they can determine whether the named beneficiary’s status has been “revoked” by operation of law. And in this context the burden is exacerbated by the choice-of-law problems that may confront an administrator when the employer is located in one State, the plan participant lives in another, and the participant’s former spouse lives in a third. In such a situation, administrators might find that plan payments are subject to conflicting legal obligations.

*Id.* at 148-49 (footnote omitted). Consequently, the Court found that the state law was preempted. *Id.* at 150.

100. *Id.* at 147.

101. *Id.* at 147-48.

102. *Id.* at 148.

### 3. Conflicting Requirements

The U.S. Supreme Court has also held that state laws are preempted if they would subject plan administrators to conflicting requirements.<sup>103</sup> The Court found that a state law was preempted because it subjected the plan to conflicting rules regarding the determination of the participant's beneficiary.<sup>104</sup> The Court stated that the state law conflicted with the plan documents.<sup>105</sup> The law would have required the fiduciaries to violate ERISA, as ERISA requires fiduciaries to comply with the terms of the plan documents.<sup>106</sup>

Similarly, the Court held that a state law that allowed a non-participant spouse to transfer her interest in retirement benefits was preempted because it could result in conflicting requirements.<sup>107</sup>

### 4. Limitations to Preemption

The U.S. Supreme Court stated that ERISA's preemption provisions are not without limitation.<sup>108</sup> The Court has held that state laws that only have an indirect economic impact on ERISA plans and state laws of general applicability are not preempted.<sup>109</sup>

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103. *Id.* at 148-50.

104. *Id.* at 147.

105. *Id.* at 150.

106. *Id.* In *Egelhoff*, the Court emphasized the impact of conflicting laws as well as the affect of the Washington statute on plan administration. *Id.* at 149-50. The statute automatically revoked a spousal beneficiary designation upon the participant's divorce. *Id.* at 143. The plan's terms conflicted with the statute. *Id.* at 149-150. ERISA requires fiduciaries to act in accordance with their plan's terms. Employment Retirement Income Security Act (ERISA) of 1974 § 404(a)(1)(D), 29 U.S.C. § 1104(a)(1)(D) (2006). Thus, a state law that differs from the plan's terms would cause a fiduciary to violate ERISA. *Egelhoff*, 532 U.S. at 149-50. The Court explained that "[t]he statute binds ERISA plan administrators to a particular choice of rules for determining beneficiary status. The administrators must pay benefits to the beneficiaries chosen by state law, rather than to those identified in the plan documents . . . . In particular, it runs counter to ERISA's commands . . . ." *Id.* at 147.

107. *Boggs v. Boggs*, 520 U.S. 833, 835-36, 841 (1997). In *Boggs*, the participant's children with his first wife claimed an interest in his retirement benefits as a result of amounts bequeathed them in their mother's will. *Id.* at 836-37. The participant's second wife also claimed an interest under the terms of the plan. *Id.* The Court held that "[i]n the face of this direct clash between state law and the provisions and objectives of ERISA, the state law cannot stand." *Id.* at 844.

108. *N.Y. State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 661 (1995) (finding that although Congress intended ERISA's pre-emption to be broad, "nothing in the language of the Act or the context of its passage indicates that Congress chose to displace general health care regulation, which historically has been a matter of local concern.") (internal citations omitted).

109. *Id.* at 662.

The Court held that a state law that imposed surcharges was not preempted because it only had an indirect economic impact on ERISA plans.<sup>110</sup> The Court held that the law did not regulate ERISA plans.<sup>111</sup> It stated that “[a]n indirect economic influence, however, does not bind plan administrators to any particular choice and thus function as a regulation of an ERISA plan itself . . . .”<sup>112</sup> The Court also stated that the law did not impact plan administration.<sup>113</sup> The Court stated, “[n]or does the indirect influence of the surcharges preclude uniform administrative practice or the provision of a uniform interstate benefit package if a plan wishes to provide one. It simply bears on the costs of benefits and the relative costs of competing insurance to provide them.”<sup>114</sup>

Similarly, the Court held that a prevailing wage law was not preempted because it only had an indirect economic influence on ERISA plans.<sup>115</sup> Although the law had an impact on ERISA plans, the Court held that its relationship to ERISA plans was too tenuous.<sup>116</sup> The Court stated that the state law was similar to the New York law in *Travelers* in that “[t]he prevailing wage statute alters the incentives, but does not dictate the choices, facing ERISA plans.”<sup>117</sup>

The Court has also found that a tax on hospitals only had an indirect economic effect on plans and, therefore, was not preempted.<sup>118</sup>

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110. *Id.* at 668. In *Travelers*, New York imposed surcharges with respect to HMOs. *Id.* at 649. Hospitals were also required to collect surcharges from patients covered by a commercial insurer, but not for patients insured by Blue Cross/Blue Shield plans. *Id.* The Court held that the surcharge may have changed the cost of providing benefits, but did not relate to ERISA plans. *Id.* at 662.

111. *Id.* at 659.

112. *Id.*

113. *Id.* at 659-60.

114. *Id.* at 660.

115. *Cal. Div. of Labor Standards Enforcement v. Dillingham Constr. N.A., Inc.*, 519 U.S. 316, 329, 334 (1997). In *Dillingham*, the Court held that a California prevailing wage law was not preempted because it only had an indirect economic influence on ERISA plans. *Id.* The state law provided that a lower prevailing wage applied to apprenticeship plans, which may or may not be covered by ERISA, if they were approved. *Id.* at 319-20. However, the Court held that the law’s relationship to ERISA plans was too tenuous, as apprenticeship plans do not need to be ERISA plans and the law did not dictate ERISA plans’ choices. *Id.* at 334.

116. *Id.*

117. *Id.*

118. *DeBuono v. NYSA-ILA Medical & Clinical Servs. Fund*, 520 U.S. 806, 816 (1997). In *DeBuono*, the Court considered whether New York could impose a gross receipts tax on the income of hospitals operated by ERISA plans as well as other hospitals. *Id.* at 809. The Court held that the state law was not preempted and explained that “[a]ny state tax, or other law, that increases the cost of providing benefits to covered employees will have some effect on the administration of ERISA plans, but that simply cannot mean that every state law with such an effect is pre-empted by the federal statute.” *Id.* at 816.

The Court noted that the hospitals were not predominantly owned or operated by ERISA plans.<sup>119</sup> As a result, the Court considered the state law's impact to be indirect and stated that it would merely increase the cost of providing benefits.<sup>120</sup>

The Court has also held that state laws of general applicability are not preempted.<sup>121</sup> The Court held that a garnishment statute's general provisions were not preempted because it was a law of general applicability.<sup>122</sup> However, the statute's exception for ERISA plans was preempted because it related to employee benefit plans.<sup>123</sup>

Thus, the U.S. Supreme Court has taken the position that state laws that only impose an indirect economic impact on ERISA plans and state laws of general applicability do not relate to employee benefit plans. States that want to regulate 401(k) plans will likely try to characterize their laws in this way. That is, states will attempt to argue that their laws are taxes<sup>124</sup> that only impose an indirect economic impact on ERISA plans and state laws of general applicability.

States are likely to have difficulty attempting to impact coverage, fees or benefit adequacy through laws that only impose an indirect economic impact on 401(k) plans or laws of general applicability. However, states may be able to indirectly influence 401(k) plans by regulating service providers to 401(k) plans.

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119. *Id.*

120. *Id.*

121. *See* Mackey v. Lanier Collection Agency & Serv., Inc., 486 U.S. 825, 831 (1988).

122. *See id.* In *Mackey*, Georgia had a general garnishment statute and an anti-garnishment statute that specifically exempted ERISA welfare plans from the general statute. *Id.* The general statute would have required plans to garnish amounts otherwise payable to participants and beneficiaries. *Id.* The Court held that "ERISA does not forbid garnishment of an ERISA welfare benefit plan, even where the purpose is to collect judgments against plan participants." *Id.* at 841. However, the Court held that the anti-garnishment statute was preempted because it "expressly refers to—indeed, solely applies to—ERISA employee benefit plans." *Id.* at 828 n.2, 829.

123. *Id.* at 830.

124. For example, in *RILA v. Fielder*, the Maryland Secretary of Labor, Licensing, and Regulation argued that the Maryland's law was a tax on employers. *Retail Indus. Leaders Ass'n v. Fielder*, 475 F.3d 180, 188 (4th Cir. 2007). The Fourth Circuit Court of Appeals rejected this argument, stating "[t]here is overriding evidence that the Fair Share Act's primary purpose is to regulate employers' healthcare spending, not to raise revenue." *Id.* at 189. Maryland's Fair Share Health Care Fund Act looked less like a tax given the few employers who were subject to the tax and the fact that the tax could be avoided completely by providing health benefits to employees. *Id.* Given that Maryland's Fair Share Health Care Fund Act was preempted by ERISA, other states will be more likely to avoid these problems.

### C. Statutory Exceptions to Preemption

ERISA includes several exceptions to preemption.<sup>125</sup> That is, certain types of state laws are not preempted, even if they relate to employee benefit plans. ERISA's most significant exceptions are for state laws that regulate insurance, banking or securities (known as the "saving clause"), and generally applicable criminal laws of a state.<sup>126</sup> ERISA prevents states from deeming ERISA plans to be insurance companies and thus, using that type of recharacterization as a means to regulate them.<sup>127</sup>

At the crux of the saving clause is what it means to regulate insurance. The U.S. Supreme Court set forth a three-part test in *Metropolitan Life Insurance Co. v. Massachusetts*<sup>128</sup> for determining whether a state law relates to the business of insurance.<sup>129</sup> The Court looked to cases that interpreted the scope of the McCarran-Ferguson Act when determining whether the state law related to the business of insurance.<sup>130</sup> As a result, the three-part test considered "first, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry."<sup>131</sup>

The U.S. Supreme Court adopted a new approach to determining whether a state law regulated insurance in *Kentucky Association of Health Plans v. Miller*.<sup>132</sup> The Court stated:

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125. Employment Retirement Income Security Act (ERISA) of 1974 § 514(b), 29 U.S.C. § 1144(b) (2006).

126. *Id.* at ERISA § 514(b)(2)(B)-(4).

127. *Id.* at ERISA § 514(b)(2)(B).

128. 471 U.S. 724 (1985).

129. *Id.* at 743. *Metropolitan Life* involved a Massachusetts statute that required a minimum level of mental health benefits to be provided to residents who were insured under certain insurance policies and health plans. *Id.* at 727. The U.S. Supreme Court held that the statute related to employee benefit plans and "[bore] indirectly but substantially on all insured benefit plans, for it require[d] them to purchase the mental-health benefits specified in the statute when they purchase[d] a certain kind of common insurance policy." *Id.* at 739.

130. *See id.* at 735-37 (citing *Attorney General v. Travelers Ins. Co.*, 433 N.E.2d 1223, 1232 (Mass. 1982)).

131. *Id.* at 743 (citing *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 129 (1982) (emphasis omitted)). Using this three-part test, the Court held that the Massachusetts statute was saved from preemption as it regulated insurance. *See id.* at 746. The Court stated that the statute regulated the spreading of risk, regulated "an integral part of the relationship between the insurer and the policyholder by limiting the type of insurance that an insurer may sell to the policyholder" and only regulated insurers. *Id.* at 743.

132. 538 U.S. 329 (2003). *Miller* involved Kentucky's "any willing provider" law, whereby

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Today we make a clean break from the McCarran-Ferguson factors and hold that for a state law to be deemed a ‘law which regulates insurance’ under [section] 1144(b)(2)(A), it must satisfy two requirements. First, the state law must be specifically directed toward entities engaged in insurance. Second, as explained above, the state law must substantially affect the risk pooling arrangement between the insurer and the insured.<sup>133</sup>

Thus, state laws can avoid preemption if they regulate insurance, banking or securities, or are generally applicable criminal laws. States that want to regulate 401(k) plans may try to characterize their laws as regulating insurance, banking, or securities. They may also impact 401(k) plans through the regulation of service providers to 401(k) plans, particularly those in the business of insurance, banking, and/or securities.

### III. NEED FOR PREEMPTION OF STATE LAWS THAT IMPACT 401(K) PLANS

As the U.S. Supreme Court acknowledged in *Shaw v. Delta Air Lines, Inc.*, ERISA was intended to preempt state laws that relate to ERISA plans.<sup>134</sup> The phrase “relate to” should be interpreted broadly in order to facilitate the uniform design and administration of ERISA plans, transfer of workers of companies that operate in multiple states, and interaction between organizations that represent varying interested parties with respect to ERISA plans should be able to work with the U.S. Congress and the variety of federal agencies that oversee ERISA plans.

#### *A. Uniform Plan Design and Administration*

The Court should interpret ERISA’s preemption provisions broadly with respect to 401(k) plans in order to promote uniform administration, which results in economies of scale and reduced costs for plans. As the U.S. Supreme Court noted in *Egelhoff*:

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health insurers were not permitted to discriminate against providers who were willing to accept their terms and conditions and every health benefit plan that offered chiropractic services was required to permit any licensed chiropractor who agreed to their terms and conditions to serve as a participating primary chiropractor for the plan’s participants. *Id.* at 331-32. The U.S. Supreme Court held that the law was subject to ERISA, but was not preempted as a result of the saving clause. *Id.* at 334-36. 133. *Id.* at 341-42 (citations omitted).

134. 463 U.S. 85, 91 (1983). In *Shaw*, the Court stated “[i]n fact, however, Congress used the words ‘relate to’ in [section] 514(a) in their broad sense.” *Id.* at 98.

One of the principal goals of ERISA is to enable employers “to establish a uniform administrative scheme, which provides a set of standard procedures to guide processing of claims and disbursement of benefits.” Uniformity is impossible, however, if plans are subject to different legal obligations in different States.<sup>135</sup>

As the ERISA Industry Committee (“ERIC”) noted in its discussion of health care reform proposals, “[w]ithout ERISA’s nationally uniform standards, the most creative, innovative and cost-effective employer-sponsored health benefit plans could not exist because of the burden of complying with overlapping and inconsistent state laws.”<sup>136</sup> Although ERIC was discussing health care reform proposals, similar issues apply with respect to 401(k) plans. Additionally, as ERIC noted, “[d]isparate state approaches will cause employers and providers to flee from states with more burdensome requirements to states with less burdensome requirements.”<sup>137</sup>

In order to allow 401(k) plans to operate as efficiently and effectively as possible, they must be free from potentially conflicting regulation by states.<sup>138</sup> Additionally, plans should not have to expend considerable resources monitoring state laws and guidance in order to operate.<sup>139</sup>

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135. 532 U.S. 141, 148 (2001) (quoting *Fort Halifax Packing Co. v. Coyne*, 482 U.S. 1, 9 (1987)).

136. Health Policy Issue Brief, The ERISA Industry Committee, *Successful Employer-Provided Health Plans Depend on Nationally Uniform Standards*, HEALTH POLICY ISSUE BRIEF, Oct. 15, 2007, [http://www.eric.org/forms/uploadFiles/e5f6000000f.filename.ERIC\\_-\\_Employers\\_Depend\\_on\\_National\\_Uniformity.pdf](http://www.eric.org/forms/uploadFiles/e5f6000000f.filename.ERIC_-_Employers_Depend_on_National_Uniformity.pdf).

137. *Id.*

138. *Navigating the ACA, EACA, QACA, and QDIA Rules*, EXECUTIVE COMPENSATION, BENEFITS & EMP. L. FOCUS (White & Case LLP, New York, N.Y.), Aug. 2008, at 5, available at [http://www.whitecase.com/files/Publication/739a5dbd-41ee-451e-81f0-e259428806a3/Presentation/PublicationAttachment/d98bcd53-6cf1-43c2-8d93-e95d00f24801/ECBEL\\_August\\_2008\\_5.pdf](http://www.whitecase.com/files/Publication/739a5dbd-41ee-451e-81f0-e259428806a3/Presentation/PublicationAttachment/d98bcd53-6cf1-43c2-8d93-e95d00f24801/ECBEL_August_2008_5.pdf) (discussing ERISA § 514(e)).

139. In 401(k) plans, these costs could be borne by participants. In defined contribution plans, a participant’s benefit is primarily based on the contributions that are made to his account and any earnings on those contributions. A participant in a 401(k) plan is entitled to the amount of money in his account, which is equal to the amount of deferrals made by the participant, any employer contributions, and other income such as forfeitures that are allocated to the account and the investment earnings. 29 U.S.C. § 1002(34). The value of the account is reduced by expenses that are charged to the plan. *Id.* §§ 1002(23)(B); 1002(34) (2006). Proper expenses may be paid using plan assets as long as the plan document does not prohibit it. U.S. Dep’t of Labor Advisory Opinion 2001-01A (Jan. 18, 2001), U.S. Dep’t of Labor, Employee Benefits Sec. Admin., available at <http://www.dol.gov/ebsa/regs/aos/ao2001-01a.html>.

### *B. Transfer of Employees Among Locations*

Employees at companies with locations in more than one state should be able to transfer to another location without changing benefits. It is not uncommon for companies to operate in more than one state. Even small employers may have more than one location, particularly where they are located near the border of a state.

If 401(k) plans were subject to state law, they could be required to include different features in the plan based on where the employee was a resident. As a result, a worker who was transferred (or requested a transfer) to a location in another state could have his 401(k) plan features changed as a result. Consequently, participants in addition to plan sponsors would need to understand the different rules associated with each state when making plan decisions.

Workers at companies that operate in multiple states should be able to transfer among the company's locations without having to worry about different plan provisions applying in other locations. As a result, the same rules should apply to all workers, regardless of where they are located.

### *C. Involvement By Interested Parties*

Organizations that represent varying interested parties with respect to ERISA plans as well as interested individuals currently work with the U.S. Congress, the DOL, U.S. Department of Treasury ("Treasury"), and the Pension Benefit Guaranty Corporation ("PBGC") to facilitate workable rules for ERISA plans.<sup>140</sup> For example, when the DOL issued a Request for Information with respect to Fee Disclosures to 401(k) Plan Participants,<sup>141</sup> it received over eighty written comments in response.<sup>142</sup> Additionally, the DOL received over eighty written comments in response to its proposed regulations on the requirements for a reasonable

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140. Organizations that focus on employee benefit issues include AARP, American Benefits Council, American Institute of Certified Public Accountants (AICPA), American Society of Pension Professionals & Actuaries (ASPPA), Council of Independent 401(k) Recordkeepers (CIKR), ERISA Industry Committee (ERIC), Investment Company Institute (ICI), National Association of Independent Retirement Plan Advisors (NAIRPA), Pension Rights Center, and Society of Actuaries.

141. Reasonable Contract or Arrangement Under Section 408(b)(2)-Fee Disclosure, 72 Fed. Reg. 20,423, 20,457 (Apr. 25, 2007) (codified at 29 C.F.R. pt. 2550).

142. Employee Benefits Security Administration of the U.S. Department of Labor, Fee Disclosures to 401(k) Plan Participants—RFI, <http://www.dol.gov/ebsa/regs/cmt-feedisclosures.html> (click on each link to view the written responses the Department of Labor received to its request for information) (last visited Nov. 1, 2009).

contract or arrangement under ERISA section 408(b)(2),<sup>143</sup> as well as nearly thirty requests to testify on the issue.<sup>144</sup>

The DOL, Treasury and PBGC published considerable guidance with respect to ERISA plans that interested persons and organizations typically review, analyze, and frequently provide comments on. In 2008, the DOL published over sixty documents in the Federal Register, most of which required review by interested persons and organizations.<sup>145</sup> During this time, Treasury also published over forty items of guidance relating to retirement plans in addition to Treasury guidance that impacted health and welfare plans.<sup>146</sup> The PBGC also published over forty documents in the Federal Register in 2008.<sup>147</sup> Although 401(k) plans are typically not subject to regulation by the PBGC, most interested individuals and organizations monitor all types of employee benefit issues, not just those relating to 401(k) plans.

If ERISA's preemption provisions are interpreted more narrowly so that fewer state laws that impact 401(k) plans were preempted, interested persons and organizations would need to devote considerably more time, energy, and resources working with state legislatures and agencies to help them understand the practical impacts of state legislation on 401(k) plans. Thus, in order to keep the system as efficient and effective as possible, ERISA's preemption provisions should be interpreted broadly.

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143. Reasonable Contract or Arrangement Under Section 408(b)(2)-Fee Disclosure, 72 Fed. Reg. 70,987, 70,994 (Dec. 13, 2007) (codified at 29 C.F.R. pt. 2550).

144. Fee Disclosure, *supra* note 40 (displaying written responses and requests to testify to its proposed regulation under ERISA § 408(b)(2)).

145. *See generally* Employee Benefits Security Administration of the U.S. Department of Labor, Federal Register Documents for EBSA, <http://www.dol.gov/federalregister/DocumentList.aspx?AgencyID=8> (displaying 2009 documents published by the Department of Labor in the Federal Register) (last visited Nov. 1, 2009).

146. *See generally* DEPARTMENT OF THE TREASURY, FIRST PERIODIC UPDATE OF THE 2007-2008 PRIORITY GUIDANCE PLAN (2008), <http://www.irs.gov/pub/irs-utl/2007-2008pgp.pdf> (showing a list of guidance that the Treasury Department published on the topic of retirement benefits). The guidance included regulations, revenue rulings, revenue procedures, notices, and announcements. *See id.*

147. *See generally* Pension Benefit Guarantee Corporation, PBGC's Federal Register Documents, <http://www.pbgc.gov/practitioners/law-regulations-informal-guidance/content/page13189.html> (providing hyperlinks to all PBGC content published in the Federal Register since 1996) (last visited Nov. 1, 2009). Although 401(k) plans are typically not subject to regulation by the PBGC, it appears that most interested individuals and organizations monitor all types of employee benefit issues, not just those relating to 401(k) plans. *See generally* Pension Benefit Guarantee Corporation, General FAQs About PBGC, <http://www.pbgc.gov/about/wrfaqs.html> what types (discussing that "PBGC does not insure retirement plans that do not promise specific benefit amounts") (last visited Nov. 1, 2009).

#### IV. PREEMPTION OF STATE LAWS THAT IMPACT 401(K) PLANS

States are likely to encounter preemption difficulties if they attempt to address coverage, fee or benefit adequacy issues with respect to 401(k) plans.

ERISA defines the term “employee benefit plan” broadly to include pension and welfare plans.<sup>148</sup> Pension plans are defined as:

[A]ny plan, fund, or program . . . established or maintained by an employer . . . to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program (i) provides retirement income to employees, or (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond . . .<sup>149</sup>

An arrangement maintained by an employer that results in the deferral of income would be considered an employee benefit plan for purposes of ERISA preemption. As a result, state-required arrangements may still be considered ERISA plans as a result of the broad definition of employee benefit plan.

##### *A. Coverage Issues*

In order to increase the amount of workers covered by 401(k) plans, states have several options. They can offer voluntary retirement accounts, which numerous states have considered.<sup>150</sup> Alternatively, states can pass legislation that would require employers to sponsor 401(k) plan or for employers who already sponsor 401(k) plans, to allow more employees to defer.<sup>151</sup>

State laws that require employers to adopt a program that results in the deferral of income would be preempted by ERISA as ERISA plans are essential to its existence. As the U.S. Supreme Court indicated in *Greater Washington Board of Trade*, “[A]ny state law imposing requirements by reference to [ERISA plans] . . . must yield to

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148. Employment Retirement Income Security Act (ERISA) of 1974 § 3(3); 29 U.S.C. § 1002(3).

149. *Id.* at § 1002(2)(A).

150. Crenshaw, *supra* note 10.

151. Employers can currently design 401(k) plans to exclude categories of workers if the plans can satisfy the Internal Revenue Code’s (“Code”) nondiscrimination requirements. 26 U.S.C. §§ 401(a)(4), 401(k), 410(b).

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ERISA.”<sup>152</sup>

Additionally, state laws that require employers to allow all or certain categories of employees to participate in their 401(k) plans would also be preempted. The U.S. Supreme Court indicated in *FMC Corp.* that state laws are preempted if they require plans to be designed in a particular manner.<sup>153</sup>

### *B. Fee Issues*

States that want to reduce plan fees also have several options. They can negotiate with the service providers to the state plans to offer similar rates to plans in their states. They could also help plans to present themselves to service providers on an aggregated basis in order to negotiate lower rates. Alternatively, states could attempt to require 401(k) plans to include investments that they consider low cost or require employers to pay a portion of their plans' fees.

State laws that provide for negotiation of fees by the state on behalf of plans and laws that would aggregate plans may be preempted even though they treat plans more favorably. The U.S. Supreme Court held in *Mackey* that an anti-garnishment statute that specifically exempted ERISA welfare plans from the general statute was preempted.<sup>154</sup> The Court held that the anti-garnishment statute was preempted because it “expressly refers to—indeed, solely applies to—ERISA employee benefit plans.”<sup>155</sup>

State laws that require plans to include investments that they consider low cost or require employers to pay a portion of their plans' fees would also be preempted. The U.S. Supreme Court stated in *Egelhoff* that a state law that requires plans to be administered in a particular manner is preempted by ERISA.<sup>156</sup>

### *C. Benefit Adequacy Issues*

States that want to increase the amount of benefits by requiring plans to include automatic enrollment provisions or mandating that employers contribute to 401(k) plans using a “pay or play” approach. Automatic enrollment refers to a plan design whereby amounts are

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152. *District of Columbia v. Greater Wash. Bd. of Trade*, 506 U.S. 125, 130-31 (1992).

153. *FMC Corp. v. Holliday*, 498 U.S. 52, 59-60 (1990).

154. *Mackey v. Lanier Collection Agency Serv., Inc.*, 486 U.S. 825, 830 (1988).

155. *Id.* at 829.

156. *Egelhoff v. Egelhoff*, 532 U.S. 141, 147 (2001).

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automatically deferred into the plan from participants' pay checks unless the participants opt out of participating in the plan or elect a different deferral percentage.<sup>157</sup>

It is unclear whether a "pay or play" approach would be preempted under current law as the Federal Circuit Courts of Appeal are split on this issue.<sup>158</sup> However, mandatory automatic enrollment would likely be preempted by ERISA because, as discussed above, state laws cannot require plans to be designed in a particular way.

## V. CONCLUSION

As more workers reach retirement age without adequate assets to live on during retirement, states are going to increasingly look for opportunities to improve the 401(k) system. However, ideas to improve retirement plans are best channeled through Congress, where the changes can benefit all Americans.

Congress created a preemption system that works effectively for 401(k) plans when its provisions are interpreted broadly. In order to enable plans to attempt to minimize their costs and explore new methods of helping participants to prepare for retirement, a uniform system of rules must apply. As a result, ERISA's preemption provisions must be interpreted broadly by courts in order to discourage states from attempting to regulate 401(k) plans.

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157. See Employment Retirement Income Security Act (ERISA) of 1974 § 514(e), 29 U.S.C. § 1144(e) (which uses the term "automatic contribution arrangement" to describe automatic enrollment arrangements).

158. *Golden Gate Rest. Ass'n v. City & County of San Francisco*, 546 F.3d 639 (9th Cir. 2008). The San Francisco Health Care Security Ordinance currently requires employers that engage in business in San Francisco to make minimum required health care expenditures for their workers based on the amount of time those employees work in San Francisco. *Id.* at 642-43. The Golden Gate Restaurant Association ("GGRA") sued the City of San Francisco, claiming that the ordinance was preempted by ERISA. *Id.* at 642. The Ninth Circuit Court of Appeals ruled that the ordinance was not preempted by ERISA. *Id.* The GGRA filed petition for a writ of certiorari with the U.S. Supreme Court on June 6, 2009. The U.S. Supreme Court asked the opinion of the Solicitor General as to whether it should hear the case on October 5, 2009. As of the date this Article went to publication, the Solicitor General's office has not responded. However, in *Fielder*, the Fourth Circuit Court of Appeals held that Maryland's "pay or play" law was preempted by ERISA. *Retail Indus. Leaders Ass'n v. Fielder*, 475 F.3d 180, 183 (4th Cir. 2007).