CALSAVERS RETIREMENT SAVINGS BOARD

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October 21, 2022

Ms. Somjita Mitra
Chief Economist, California Department of Finance
915 Capitol Mall
Sacramento, CA 95814

Re: Response to Department of Finance Comments on Standardized Regulatory Impact Assessment

Dear Ms. Mitra,

Thank you for providing your comments on the standardized regulatory impact assessment (SRIA) developed for proposed regulations amendments to Sections 10000, 10001, 10002, and 10004 of Title 10, Chapter 15, of the California Code of Regulations. We have responded to each comment in the materials attached to this letter.

If you have any questions, please contact me at (916) 653-1744 or by email at kselenski@sto.ca.gov.

Sincerely,

K.C. Selenski

Kathleen Selenski
Executive Director, CalSavers Retirement Savings Board

Attachment: Response to Department of Finance Comments on SRIA

Cc: Ms. Dee Dee Myers, Director, Governor's Office of Business and Economic Development
Mr. Kenneth J. Pogue, Director, Office of Administrative Law

The CalSavers Retirement Savings Program

Overseen by the

CalSavers Retirement Savings Board

Response to Department of Finance Comments on Standardized Regulatory Impact Assessment (SRIA)

Date of Release: October 24, 2022

CalSavers Retirement Savings Board
915 Capitol Mall, Suite 105
Sacramento, California 95814

SUMMARY

The CalSavers Retirement Savings Board (Board) proposed to complete the regular rulemaking process to make permanent emergency regulations amendments that took effect in March 2022. In accordance with California Code of Regulations, title 1, section 2002(a)(1), the Board submitted a Standardized Regulatory Impact Assessment (SRIA) to the Department of Finance September 2, 2022. The Department of Finance (DOF) provided comments on the SRIA September 30, 2022. This document includes DOF's comments and the Board's responses to the comments.

DEPARTMENT OF FINANCE COMMENTS

On September 30, 2022, DOF provided the following comments in response to the SRIA:

"Thank you for submitting the standardized regulatory impact assessment (SRIA) and summary for the Amendments to the CalSavers Retirement Savings Program proposed regulations, as required in the California Code of Regulations, title 1, section (a)(1). Proposed text of the regulations were not submitted, therefore comments are based solely upon the SRIA and other publicly available information.

The proposed regulations amend current program criteria by adjusting and clarifying the definition of an eligible employer to include businesses that employ five employees, rather than more than five employees, allow businesses to register without a full calendar year of employee data if they meet the definition of an eligible employer, accelerate the deadline for newly eligible employers to December 31 of the employers' first year, as opposed to December 31 of the second year, and removal of the required data field and extension to the timeframe of the employee receiving the program information packet. The SRIA assumes these amendments will primarily impact the 30,800 newly mandated employers in 2023, of which only around 6,200 are expected to facilitate the CalSavers program for a total of 149,000 newly eligible employees. Each facilitating employer is expected to incur a compliance cost of $179 in the first year for a total cost of $1.1 million in 2023 from staff time necessary to administer the program. Ongoing costs to each employer are expected to be around $150 annually. The SRIA assumes that in the first twelve months following employer registration, newly eligible employees will make contributions only in the last nine months of the that year. At the assumed default rate of 5 percent of the average employee income ($39,252), total contributions or new savings are assumed to total nearly $83 million in 2023. As a result of the increased savings, the regulation assumes a short-term loss of consumption for participating employees, as they will contribute some portion of their income to their CalSavers account, resulting in over a $1.6 million reduction in sales and use tax revenue in California in 2023 (assuming a sales tax rate of 8.2 percent).

Finance generally concurs with the methodology, with the following exceptions. First, the SRIA currently states that the economic baseline is the environment prior to the emergency regulations amendments evaluated in this analysis. The SRIA should include a baseline description of the number and types of businesses and individuals impacted, which would also support the CalSavers Retirement Savings Board's assessment that the regulations will benefit small businesses and lower-income individuals. The proposed regulatory alternatives should then be compared to the defined baseline and include quantified cost impacts. The SRIA currently only discusses the qualitative impacts of the alternatives; however, it must also disclose the quantitative impacts of each proposed alternative.

Second, the SRIA must include comprehensive estimates of expected fiscal impacts. Although the SRIA broadly and qualitatively discusses potential impacts to other state programs that will be impacted by the proposed regulation, the SRIA states that the impacts are estimated to be "*de minimis*." However all fiscal impacts must be quantified regardless of their magnitude. Finally, the SRIA assumes that future program participation will be in line with the actual program data through the first half of 2022, and does not discuss the potential for a higher number of eligible employers to decide to facilitate the program or that a smaller number of eligible employees might choose to not opt-out of the program. Since increased participation in the program would lead to higher total contributions and a larger reduction of total sales tax revenue, the SRIA should explain why the current assumptions are the most representative or, alternatively, include a sensitivity analysis to show how impacts may vary under different rates of program participation.

These comments are intended to provide sufficient guidance outlining revisions to the impact assessment if a SRIA is required. The SRIA, a summary of Finance comments, and any responses must be included in the rulemaking file that is available for public comment. If any significant changes to the proposed regulations during the rulemaking process result in economic impacts not discussed in the SRIA, please note that the revised economic impacts must be reflected on the Standard Form 399 for the rulemaking file submittal to the Office of Administrative Law. Please let us know if you have any questions regarding our comments."

CALSAVERS RETIREMENT SAVINGS BOARD COMMENTS

The CalSavers Retirement Savings Board appreciates the careful review of the Department of Finance. This section includes a response to each of the comments submitted by DOF, including qualitative and quantitative analyses and a description of the methodology used. Additional detail on the range of macroeconomic impact resulting from the proposed amendments are included in the appendices.

Economic Baseline

In the SRIA, the authors stated the economic baseline as being the environment prior to the emergency regulations that were analyzed in the SRIA. In the SRIA, the authors calculated the estimated number of businesses, individuals, and industries impacted by the regulations. The SRIA reports on the expected economic impacts due to reduced consumption resulting from the amendments and details the macroeconomic impacts on those industries. The SRIA also includes estimates of expected economic benefits to California companies due to increased investments and details the macroeconomic impacts.

DOF noted the authors must include a baseline description of the number and types of businesses and individuals impacted by the amendments. While the authors specified in the SRIA that the economic baseline was "the environment prior to the emergency regulations," the SRIA established an economic baseline that describes the number and types of businesses impacted by the regulations.

The regulations will impact a few different categories of businesses in different ways. The regulations will impact some employers directly by imposing a more sudden registration deadline than prescribed in the previous regulations. Those employers include any employer with five or more employees that does not sponsor a retirement plan that has become subject to the mandate within the past couple of years, either due to the establishment of a new business, the termination of a qualified retirement plan, or growth in their number of employees to more than five.

Those impacts will be spread relatively evenly across industries and employer sizes, predominating in industries that are typically less likely to sponsor a retirement plan:

- Accommodation and Food Services (17%)
- Health Care and Social Assistance (12%)

- Construction (10%)
- Retail (10%)
- Manufacturing (7%)
- Agriculture (3%)
- Recreation (2%)
- Other (39%)

The authors estimated those impacts to total $1,112,709 in 2023 through indirect impacts caused by the opportunity costs incurred due to the administrative steps necessary for employers to facilitate the program.

Because the amendments will lead to more savings, some businesses will be impacted due to reduced consumption. Those impacts are expected to concentrate in the food sector (48% of expected impacts), entertainment (14% of expected impacts), apparel (12% of expected impacts), and miscellaneous sectors impacted by consumer discretionary spending (26% of expected impacts). In total, the authors estimate $61,951,373 in economic impacts related to reduced consumption from the amendments in 2023.

Finally, the amendments are expected to bring economic benefits due to increased investment in California companies.

Quantification of Alternatives

The authors evaluated the following alternatives in the SRIA:

Proposed Regulations	**Alternative**
Establish December 31 registration deadline for newly mandated employers	Maintain requirement that newly mandated employers register no later than 24 months from their date of eligibility or by the specific dates established in Section 10002(a)
Allow employers to register if they have at least one quarter of employment data – and otherwise meet criteria for eligibility	Maintain requirement that employers have at least one full calendar year of data to be eligible for the program

DOF requested the authors to quantify cost impacts of each alternative. While the authors had implicitly quantified impacts of the alternatives through the quantification of the employer, economic, and fiscal impacts, as they represented variance from the baseline, those quantifications were not explicitly reported in the alternatives section of the SRIA.

The following table quantifies the differences between the baseline and each alternative considered:

Regulation	**Benefit**	**Cost**
Baseline	$15,703,748	$46,639,553
Alternative 1	$46,639,553	$15,703,748
Alternative 2	$0	$0

The benefits reported for the baseline include benefits related to increased investment in the state, due to expected increases in new savings that are partially invested in California-based companies. The costs reported for the baseline are both economic and fiscal impacts due to reductions in consumption caused by new savings by Californians.

Alternative 1 would maintain the requirement that newly mandated employers register no later than 24 months after their date of eligibility, rather than the 12-month deadline established through the regulations amendments. Because alternative 1 would result in less new savings than the baseline, the benefits of the alternative would be due to reduced consumption loss compared to the baseline. Costs for alternative 1 include reduced investment in California-based companies, as the alternative would be expected to result in less new savings by Californians compared to the baseline.

While the baseline has greater economic and fiscal cost than benefits in the near term, the authors expect there to be greater economic and fiscal benefits in the long term, as participating employees will mostly not realize the financial benefits of the program until several years and, for the youngest participants, decades, in the future.

The macroeconomic impacts related to the increased investment and decreased consumption are reported in Appendices 3-6 in the SRIA.

Alternative 2 is not expected to have any costs or benefits, as it places no restrictions or requirements on the regulated community, but rather allows some employers to join the program earlier than they had previously been allowed.

*Quantification of Fiscal Impacts Determined to be "*de minimis"

DOF requested the authors to quantify all fiscal impacts resulting from these regulations amendments, including those determined to be "*de minimis.*" In the SRIA, the authors described how the amendments would result in fiscal impacts, quantifying the impacts related to reduced sales and use tax and describing how, if at all, the amendments would impact income tax, claims of the California Earned Income Tax Credit (CalEITC), the Franchise Tax Board, Medi-Cal, and the Federal Saver's Credit. To be more precise, the authors should have instead stated there will be no fiscal impacts aside from the impacts to sales and use tax revenue. Below, the authors have described why the amendments will not have fiscal impacts.

Income Tax

CalSavers accounts are Roth Individual Retirement Accounts (Roth IRAs). Any contributions to a Roth IRA are subject to normal income tax in the year in which the contributions are made. When a saver reaches retirement age, their contributions and any investment interest earned on those contributions, can be withdrawn tax-free[1].

Contributions to a Traditional IRA may be tax deductible in the year in which they are made. Unlike a Roth IRA, withdrawals from a Traditional IRA, which may include the amount of the contributions and any investment earnings, are subject to income tax.

[1] Specifically, individuals can withdraw funds from an IRA without taxes or penalties if they are age 59 ½ or older, or if they use it for a qualified expense, qualified educational expenses, first time home purchase, or other reasons allowed under federal law.

In general, Roth IRAs tend to be favorable to individuals who are younger and who have relatively less income, as the tax advantage can be more favorable for those who build long term savings and any tax deduction may be negligible for those with less income – and, therefore, less of a tax liability.

CalSavers allows savers to recharacterize contributions from a Roth IRA to a Traditional IRA. To date, only 0.01% of savers have recharacterized their contributions to Traditional. Based on that rate of recharacterization, the authors estimate between six to seventeen employees will recharacterize to a Traditional IRA out of the population of employees who will be impacted by the amendments.

Savers may have a variety of reasons to recharacterize, but the most likely reasons are that either the saver is near retirement age and would most benefit from an immediate tax deduction, or the individual is simply ineligible to save in a Roth IRA, as individuals are phased out of eligibility to save in a Roth IRA if their modified adjusted gross income exceeds $144,000 annually for single filers or $204,000 for married joint filers[2].

Assuming the maximum expected recharacterizations of seventeen employees receive the maximum possible tax deduction due to saving the maximum allowable annual contributions ($7,000 for those age 50 and above), the amendments would only have an impact of $119,000 in 2023.

<u>CalEITC</u>
The SRIA describes potential fiscal impacts resulting from an increase in CalEITC claims that could be caused by the amendments. Any increase in CalEITC claims would be due to a corresponding increase in tax filings, as some individuals may be more motivated to file their taxes, and therefore claim the CalEITC, due to seeking a tax deduction for contributions to a Traditional IRA. As described above, few savers recharacterize to Traditional IRAs. Additionally, the CalEITC is limited to individuals with income below $30,000 annually[3]. Because lower income individuals have little to no incentive to recharacterize to a Traditional IRA, the authors do not expect there to be any fiscal impacts due to increased CalEITC claims.

<u>Franchise Tax Board</u>
As noted in the SRIA, the Franchise Tax Board (FTB) is designated as the entity responsible for issuing final notices of penalty application to noncompliant employers – and for conducting appeals of employer penalties. Any costs incurred by FTB due to fulfilling either role would be reimbursed by the program, as required by the statute under Government Code Section 100033(d)(2).

The authors expect no fiscal impact to FTB resulting from these regulations. While the amendments subject some employers to a more sudden registration deadline, the amendments do not substantially change the number of employers subject to a deadline. FTB would be required to aid CalSavers in enforcing employer compliance from this same population of employers under either the former or current regulations.

Furthermore, the vast majority of FTB's costs for enforcement activities are related to the development of a database to manage enforcement activities. This activity will occur regardless of the deadlines established for newly mandated employers.

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[2] https://www.irs.gov/retirement-plans/plan-participant-employee/amount-of-roth-ira-contributions-that-you-can-make-for-2022
[3] https://www.ftb.ca.gov/file/personal/credits/california-earned-income-tax-credit.html

Medi-Cal Savings

The SRIA describes potential long-term fiscal benefits due to state savings on Medi-Cal expenses. Those savings would be realized due to more Californians having retirement savings that will allow them to avoid relying on Medi-Cal for health care services. Any fiscal impacts would be by nature long term and not included in 2023, the year in which impacts from these amendments were analyzed for the SRIA.

Sensitivity Analysis

Economic and fiscal impacts are highly sensitive to a range of factors that are difficult to predict, specifically employer participation rates and employee participation rates, which are impacted by both opt-out rates and identity verification failures. To provide a range of potential impact, staff conducted a sensitivity analysis to evaluate economic and fiscal impacts under the following assumptions:

Table 1. – Assumptions Used for Scenario Analysis

Scenario	Wave 1 Facilitation	Wave 2 Facilitation	Wave 3 Facilitation	CID Fails	Employee Participation Rate
1. SRIA Assumptions	24.32%	26.41%	20.00%	40%	63%
2. Moderately High Employer Facilitation	50.00%	41.00%	30.00%	40%	63%
3. High Employer Facilitation	75.00%	56.00%	40.00%	40%	63%
4. High Employee Participation	24.32%	26.41%	20.00%	30%	70%
5. High Employer and Employee Participation	75.00%	56.00%	40.00%	30%	70%

The differences in economic and fiscal impacts under each scenario are reported in the table below:

Table 2. – Economic and Fiscal Impacts in Scenario Analyses

Scenario	Employer Impact	Saver Contributions	Consumption Impact	Sales and Use Tax Impact
1. SRIA Assumptions	$1,112,709	$69,658,150	$61,125,027	$1,654,043
2. Moderately High Employer Facilitation	$1,682,450	$117,939,204	$103,491,651	$2,800,484
3. High Employer Facilitation	$2,251,880	$165,610,255	$145,322,999	$3,932,440
4. High Employee Participation	$1,112,709	$90,297,602	$79,236,146	$2,144,130
5. High Employer and Employee Participation	$2,251,880	$214,679,961	$188,381,666	$5,097,608