

## **EMPTY PROMISES: CAN THE WELFARE BENEFITS OF CURRENT RETIREES BE SAVED?**

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*The current economic climate has placed many retirees who depend on former employers for important welfare benefits, most notably health insurance, in a particularly precarious situation. Faced with the prospect of layoffs and bankruptcy, many large companies are choosing to restructure or slash benefit packages, leaving retirees with little recourse. There are currently three legal theories available to retirees under ERISA (Employee Retirement Income Security Act) that can be used to challenge a denial of benefits: arguing that the benefits contractually vested, alleging breach of fiduciary duty by a benefit administrator, and demonstrating estoppel through reliance on material misrepresentations. However, in practice none of these remedies gives retirees meaningful protection. This Note suggests that several changes are desperately needed in order to ensure that retirees have a voice and a reasonable degree of protection in place for their welfare benefits. The proposals include giving retirees representation at union negotiations when their benefits are being discussed, taking a more realistic assessment of retirees' reasonable expectations in cases where the duration of welfare benefits is ambiguous, requiring that employer-created VEBA's (Voluntary Employee Benefit Associations) are sufficiently diversified to shield retirees from market risks, and looking at ways to control the rising costs of health care in the United States.*

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## I. Introduction

Thousands of retirees who rely on welfare benefits provided by their former employers are finding themselves caught between a rock and a hard place. Faced with skyrocketing medical costs and inadequate income from social security and investments, many are experiencing a less comfortable retirement than they had anticipated.<sup>1</sup> Many retirees of once prominent and powerful American industries face benefit cuts as their formerly profitable employers find themselves facing harsh economic realities.<sup>2</sup>

New proposals and changes in employer practices should help protect future retirees by reducing the impact of economic dependence that currently makes benefits volatile. However, preserving the current benefits of existing retirees presents a different and more daunting problem. These retirees considered their former employers' representations about pension and welfare benefits in determining when to retire and how much to save.<sup>3</sup> Unfortunately, many of these employers encountered financial difficulties, including the prospect of bankruptcy, and simply lacked the resources to maintain these benefits at promised levels.<sup>4</sup> Relying on federal programs to replace these benefits could be a risky endeavor, as several existing support systems for the elderly are nearly insolvent, and large budget deficits are producing historic levels of national debt.<sup>5</sup>

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1. See Stephen F. Befort, *The Perfect Storm of Retirement Insecurity: Fixing the Three-Legged Stool of Social Security, Pensions, and Personal Savings*, 91 MINN. L. REV. 938, 939 (2007) (noting that a growing portion of American workers are financially unprepared for retirement); see also Emily Brandon, *Your Retirement Calculations May Be Way Off*, U.S. NEWS & WORLD REP., Sept. 15, 2006, <http://www.usnews.com/usnews/biztech/articles/060915/15buildingblocks.htm> (last visited Nov. 10, 2009).

2. See John Thacher McNeil, *The Failure of Free Contract in the Context of Employer-Sponsored Retiree Welfare Benefits: Moving Toward a Solution*, 25 HARV. J. ON LEGIS. 213, 214 (1988) (explaining that many companies in the manufacturing and mining industries have modified retiree welfare benefits due to long-term economic declines).

3. See Richard L. Kaplan et al., *Retirees at Risk: The Precarious Promise of Post-Employment Health Benefits*, 9 YALE J. HEALTH POL'Y L. & ETHICS 287, 289 (2009) [hereinafter Kaplan, *Retirees at Risk*] (finding that the presence of retiree health insurance is one of the most significant factors in determining when people leave the workforce).

4. See Daniel Keating, *Harsh Realities and Silver Linings for Retirees*, 15 AM. BANKR. INST. L. REV. 437, 447 (2007) [hereinafter Keating, *Harsh Realities*].

5. Amy Goldstein, *Alarm Sounded on Social Security*, WASH. POST, May 13, 2009, at A01, available at <http://www.washingtonpost.com/wp-dyn/content/article/2009/05/12/AR2009051200252.html>. "[T]he White House is predicting a 10-year federal deficit of \$9 trillion—more than the sum of all previous deficits

This Note discusses the shaky state of welfare benefits for current retirees who were promised specific benefits under defined benefit retirement plans. It begins by explaining the reasons that these benefits are in jeopardy and why the problems facing welfare benefits are more serious than those facing pension benefits. Next, this Note discusses possible negotiation and litigation remedies available to retirees facing benefit cuts, protections for welfare benefits when former employers enter bankruptcy, and relevant emerging trends in the provision of welfare benefits. Ultimately, this Note concludes that while current practices that separate retirement benefits from the future economic status of the employer may provide stability for future retirees, they cannot fully protect the welfare benefits of current retirees who detrimentally relied on explicit and implicit promises of life-long benefits. Accordingly, new legislation and judicial standards are needed to protect retirees in negotiations over plan modifications, to ease the burden retirees face in court proceedings, to encourage employers to shift their welfare obligations to more secure vehicles that are insured and can survive apart from the fortunes of the employers, and to provide more efficient federal welfare programs that can maintain benefits while controlling costs.

## II. Background

A variety of different benefits are broadly considered “welfare benefits,” including such categories as health care, accident, disability, death, unemployment, vacation, training, child care, scholarship funds, and prepaid legal services.<sup>6</sup> Welfare benefits first became prevalent during the World War II era, when employers began offering benefits to compete for scarce labor because wage controls prevented them from increasing salaries.<sup>7</sup> Newly powerful labor unions often sought these popular benefits in collective bargaining negotiations.<sup>8</sup> Although welfare benefits were initially viewed as inexpensive perks, they did not remain inexpensive for long.<sup>9</sup> Medical costs surged dra-

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since America’s founding.” Jim Kuhnhenh, *Analysts: U.S. Deficit Will Surge*, HERALD (Rock Hill, S.C.), Aug. 26, 2009, at 1A.

6. 29 U.S.C. § 1002(1) (2006).

7. David A. Pratt, *The Past, Present, and Future of Retiree Health Benefits*, 3 J. HEALTH & BIOMEDICAL L. 103, 105 (2007).

8. Douglas Sondgeroth, *High Hopes: Why Courts Should Fulfill Expectations of Lifetime Retiree Health Benefits in Ambiguous Collective Bargaining Agreements*, 42 B.C. L. REV. 1215, 1219 (2001).

9. McNeil, *supra* note 2, at 220.

matically, and simultaneous increases in life expectancy meant that former employees could enjoy these increasingly costly benefits for longer periods.<sup>10</sup> Many employers promised these benefits while looking at the future through rosy lenses, and the influx of fierce global competition and changes in the relative economic power of different industries have produced a far different present situation than those employers anticipated.<sup>11</sup>

Employers were forced to expose their substantially expensive retiree obligations after the accounting rules were changed in 1993.<sup>12</sup> Before those changes, employers were only required to report these expenses when they were incurred.<sup>13</sup> Statement of Financial Accounting Standards No. 106 mandated that employers account for the value of these benefits as employees earned them.<sup>14</sup> To comply with this rule, employers had to report their accumulated obligations to present and future retirees as either a one-time nonrecurring charge, or spread out through annual charges over a period of up to twenty years.<sup>15</sup> Many companies elected to make astronomical one-time write-offs: "GE's was \$1.8 billion[;] AT&T's \$6.6 billion. The Big Three automakers booked \$33.2 billion in charges . . . eliminat[ing] three fourths of the net worth of GM."<sup>16</sup>

In light of these huge obligations, employers have been increasingly reluctant to promise specific retirement benefits: from 1974 through 2007, the percentage of employees covered by defined benefit pension plans declined from 44% to 17%.<sup>17</sup> Instead, many employers offer defined contribution plans, where employees and employers

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10. *Id.* at 219–20.

11. See Larry Grudzien, *The Great Vanishing Benefit, Employer Provided Retiree Medical Benefits: The Problem and Possible Solutions*, 39 J. MARSHALL L. REV. 785, 786 (2006) (attributing the decline in employer-sponsored retiree medical coverage to accounting issues, increased costs, international competition, age discrimination issues, and lack of viable and flexible funding vehicles).

12. FIN. ACCOUNTING STANDARDS BD., STATEMENT OF FINANCIAL ACCOUNTING STANDARDS NO. 106, EMPLOYER'S ACCOUNTING FOR POSTRETIREMENT BENEFITS OTHER THAN PENSIONS 5 (1990), available at <http://www.fasb.org/pdf/fas106.pdf> [hereinafter FAS 106]; Pratt, *supra* note 7, at 121.

13. Marilyn J. Ward Ford, *Broken Promises: Implementation of Financial Accounting Standards Board Rule 106, ERISA, and Legal Challenges to Modification and Termination of Postretirement Health Care Benefit Plans*, 68 ST. JOHN'S L. REV. 427, 436 (1994).

14. FAS 106, *supra* note 12, at 5.

15. Pratt, *supra* note 7, at 121.

16. *Id.* (citing JOHN H. LANGBEIN & BRUCE A. WOLK, PENSION AND EMPLOYEE BENEFIT LAW 211 (3d ed. 2000)).

17. Keating, *Harsh Realities*, *supra* note 4, at 445.

make contributions to investment vehicles that provide income for employees in retirement.<sup>18</sup> These plans are popular because they do not create specific obligations that employers owe their retirees, and shift the risk of underperforming investments to the retirees.<sup>19</sup>

Of all the categories that the Employee Retirement Income Security Act (ERISA) defines as “welfare benefits,” health care is generally the most costly and most important to retirees.<sup>20</sup> These benefits in particular face a precarious situation. Health care costs continue to increase for all persons at a rate substantially faster than the cost of living.<sup>21</sup> These costs are typically borne by employers because the United States, unlike most other industrialized countries, lacks a comprehensive national health care program.<sup>22</sup> Examining the substantial impact these costs have on American automakers shows just how much they can affect employers’ competitiveness. Before their bankruptcies, GM had amassed \$64 billion in retiree health care obligations, and Chrysler incurred \$16.5 billion in retiree pension and health care costs.<sup>23</sup> National Public Radio calculated in December 2005 that, although assembly line workers at GM and Toyota were paid similar hourly wages (\$31.35 at GM versus \$27 at Toyota), the average labor cost per hour was over \$25 higher at GM compared to Toyota (\$73.73 versus \$48).<sup>24</sup> By 2007, health care costs alone added \$1525 to each vehicle produced by GM and \$1100 to each vehicle produced by Ford; in contrast, their Japanese competitors spent an average of \$450 per vehicle to cover health care obligations.<sup>25</sup> As health care costs continue to rise, American companies that promised to provide health insurance for retirees are increasingly disadvantaged relative to foreign competitors

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18. Susan J. Stabile, *Paternalism Isn't Always a Dirty Word: Can the Law Better Protect Defined Contribution Plan Participants?*, 5 EMP. RTS. & EMP. POL'Y J. 491, 495–96 (2001).

19. *See id.* at 497–98.

20. Sondgeroth, *supra* note 8, at 1217–18, 1222.

21. Milt Freudenheim, *Health Care Costs Rise Twice as Much as Inflation*, N.Y. TIMES, Sept. 27, 2006, at C1, available at <http://www.nytimes.com/2006/09/27/business/27insure.html>.

22. *See* William T. Payne & Pamina Ewing, *Union-Negotiated Lifetime Retiree Health Benefits: Promise or Illusion*, 9 MARQ. ELDER'S ADVISOR 319, 320 (2008).

23. Pratt, *supra* note 7, at 118.

24. Diane Geng, *GM vs. Toyota: By the Numbers*, NPR, Dec. 19, 2005, <http://www.npr.org/news/specials/gmvstoyota/>.

25. *UAW v. Gen. Motors Corp.*, 497 F.3d 615, 620 (6th Cir. 2007).

that support fewer retirees and receive government subsidies to offset some of their health care expenses.<sup>26</sup>

Many retirees who relied on promised pension and welfare benefits when planning the timing and financing of retirement are finding themselves victims of this reliance.<sup>27</sup> It is unlikely that they will find more security in the near future, as current burdens posed by retiree obligations will likely continue increasing.<sup>28</sup> The American workforce is aging, and the ratio of retirees to active workers keeps getting higher.<sup>29</sup> GM, for example, had a workforce of 142,000 white-collar and production workers supporting 460,000 retirees in 2005, and this ratio of current to retired workers is increasing further as GM cuts its workforce in efforts to return to profitability.<sup>30</sup> Additionally, retirees face difficulties in asserting their interests against those of current employees. Their contributions to employers were made in the past, and they have no votes in labor contracts that may sacrifice their benefits to protect the interests of current workers.<sup>31</sup> Retirees often trace their benefits to contracts negotiated by their former unions, and these same unions have no statutory duty to represent the interests of retirees when renegotiating labor contracts.<sup>32</sup> As pieces of the labor pie continually get smaller, retirees will likely find themselves increasingly forced to compete with current workers in order to maintain their benefits, and the unions representing them will face divided loyalties.<sup>33</sup>

Existing government programs cannot fully replace the loss of employer-provided welfare benefits. The Employee Benefit Research Institute found that Medicare covered only around 60% of health care

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26. See Grudzien, *supra* note 11, at 793 (noting that health care costs are one-third higher in manufacturing than in the service sector).

27. Kaplan, *Retirees at Risk*, *supra* note 3, at 289.

28. Medicare's shortfall is projected to be \$32.4 trillion over the next seventy-five years; if Medicare spending continues to grow at current rates (2.5% faster than the per capita GDP), it will consume nearly the entire federal budget by 2082. ANDREW J. RETTENMAIER & THOMAS R. SAVING, *MEDICARE: PAST, PRESENT AND FUTURE* 6-7 (2007), <http://www.ncpa.org/pdfs/st299.pdf>.

29. Keating, *Harsh Realities*, *supra* note 4, at 437.

30. Geng, *supra* note 24. For comparison, Toyota's American workforce of 38,000 white-collar and production workers was supporting only 1600 retirees as of December 2005. *Id.*

31. Keating, *Harsh Realities*, *supra* note 4, at 437-38.

32. Robert S. Bates, Jr., *Benefits of Retirees: Negotiations and the Duty of Fair Representation*, 21 J. MARSHALL L. REV. 513, 516 (1988).

33. See Keating, *Harsh Realities*, *supra* note 4, at 456. Because unions have a statutory duty to represent active employees, not retirees, they might increasingly favor active employees as resources decline. See Bates, *supra* note 32, at 513, 516.

expenses for beneficiaries over sixty-five in 2006.<sup>34</sup> Furthermore, the expenses Medicare covers are generally limited in duration and often require that recipients pay substantial deductibles.<sup>35</sup> According to one estimate, the average senior retiring at age sixty-five in 2009 will need \$240,000 to pay the out-of-pocket lifetime costs of health care.<sup>36</sup> When Congress finally tackles Medicare's significant financial problems, the burden on retirees will likely increase.<sup>37</sup> Other government programs for retirees also face funding problems and cannot equal the employer-promised benefits retirees expected.<sup>38</sup> ERISA established the Pension Benefit Guarantee Corporation (PBGC) to insure pension benefits by requiring employers to contribute monthly premiums, but that program quickly became insolvent and forced Congress to formulate another, the Pension Protection Plan of 2006, to rescue it.<sup>39</sup> Additionally, PBGC-insured pension plans often do not protect the entire amount of the employer obligation and do not cover any welfare benefits such as health care.<sup>40</sup> Welfare benefits are even more vulnerable than these pension benefits because ERISA does not require that they vest, so retirees must demonstrate that parties intended to create vested benefits in order for the courts to treat welfare benefits as more than mere gratuitous promises.<sup>41</sup>

Faced with this distasteful situation, many retirees have been forced to accept reduced benefits from their former employers with-

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34. Paul Fronstin et al., *Savings Needed for Health Expenses in Retirement: An Examination of Persons Ages 55 and 65 in 2009*, EMP. BENEFIT RES. INST. NOTES, June 2009, at 2, [http://www.ebri.org/pdf/notespdf/EBRI\\_Notes\\_06-June09.HlthSvg-RetFndg1.pdf](http://www.ebri.org/pdf/notespdf/EBRI_Notes_06-June09.HlthSvg-RetFndg1.pdf).

35. See, e.g., LAWRENCE A. FROLIK & RICHARD L. KAPLAN, *ELDER LAW* 66–67 (4th ed. 2006) (detailing how Medicare Part A pays for hospitalizations up to ninety days, with an initial deductible that was \$952 in 2006 and an additional deductible of one-fourth the initial deductible for days 61–90). An additional sixty days are available over the patient's lifetime. *Id.* at 67–68.

36. PAMELA VILLAREAL & DEVON HERRICK, NAT'L CTR. FOR POLICY ANALYSIS, *HEALTH CARE COSTS DURING RETIREMENT 1* (2009), <http://www.ncpa.org/pdfs/ba660.pdf>.

37. See 2009 BDS. OF TRS., FED. HOSP. INS. & FED. SUPPLEMENTARY MED. INS. TRUST FUNDS ANN. REP. 4, available at <http://www.cms.hhs.gov/ReportsTrustFunds/downloads/tr2009.pdf>.

38. See, e.g., 29 U.S.C. § 1321(a)–(b) (2006); Keating, *Harsh Realities*, *supra* note 4, at 447.

39. 29 U.S.C. § 4022 (2006); Keating, *Harsh Realities*, *supra* note 4, at 444.

40. 29 U.S.C. § 1321(a)–(b). The PBGC covers a percentage of pension obligations, with a cap on the amount covered and does not apply to welfare benefits. *Id.*

41. Nathanael R. Berneking, Comment, *Don't Mow Over the Yard-Man Inference: Guarding Against Improper Modification of Welfare Benefits Provided in a Collective Bargaining Agreement*, 45 ST. LOUIS U. L.J. 261, 277 (2001).

out any corresponding increases in aid from the government.<sup>42</sup> These reductions often come from renegotiated contracts between retirees' former unions and their former employers.<sup>43</sup> When these negotiations produce agreements that are unacceptable to retirees, or former employers cut benefits without approval and take away more than retirees believe is necessary, many turn to the courts for relief.<sup>44</sup>

### III. Analysis: The Current State of Retirees' Protections Against Benefit Cuts

Although many retirement plans guarantee specific welfare benefits for retirees, their former employers are generally free to terminate those benefits at will.<sup>45</sup> Employees gain an unalterable right to their benefits once they vest: after that point, employers can no longer alter or rescind benefits without employees' consent.<sup>46</sup> While ERISA requires that pension benefits vest when the retiree reaches sixty-five, Congress did not include welfare benefit plans when it established ERISA's vesting requirements.<sup>47</sup> Consequently, welfare benefits are generally subject to modification or elimination on the whim of the employer unless both the employer and employees intended to create vested benefits.<sup>48</sup>

Retirees facing cuts to their welfare benefits have several possible remedies. Some recognize the realities of their former employers' economic situations and agree to accept health care plans with higher co-pays and deductibles in an effort to make those benefits more affordable for their former employers.<sup>49</sup> Others seek redress in court

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42. See, e.g., Amy Joyce, *GM's UAW Retirees Face Health Care Costs*, WASH. POST, Oct. 21, 2005, at D01, available at <http://www.washingtonpost.com/wp-dyn/content/article/2005/10/20/AR2005102002078.html>; see also Keith L. Alexander, *Delta Pilots Vote to Approve Cuts in Pay, Benefits*, WASH. POST, Nov. 12, 2004, at E01, available at <http://www.washingtonpost.com/wp-dyn/articles/A43171-2004Nov11.html> (detailing how that airline pilots' union agreed by nearly seventy-nine percent to reduced benefits and to replace their defined benefit pension plan with a defined contribution plan).

43. See Joyce, *supra* note 42, at D01.

44. See Michael I. Richardson, *Employee Benefits Law: Securing Employee Welfare Benefits Through ERISA*, 61 NOTRE DAME L. REV. 551, 559-67 (1986).

45. *Curtiss-Wright Corp. v. Schoonejongen*, 514 U.S. 73, 78 (1995) ("Employers or other plan sponsors are generally free under ERISA, for any reason at any time, to adopt, modify, or terminate welfare plans.")

46. McNeil, *supra* note 2, at 223.

47. 29 U.S.C. § 1053 (2006).

48. Payne & Ewing, *supra* note 22, at 321-22.

49. See, e.g., Joyce, *supra* note 42, at D01.



when their former employers insist on reducing benefits beyond what they are willing to accept or simply eliminate retiree welfare benefits altogether.<sup>50</sup> These retirees can argue that the parties had intended to create vested benefits, that their employers breached fiduciary duties by misrepresenting their retirement plans, or that they detrimentally relied on their employers' misrepresentations about benefits.<sup>51</sup> When retirees' welfare benefits are threatened by Chapter 11 bankruptcy, the bankruptcy code provides specific protections.<sup>52</sup> Through negotiations, settlements, and bankruptcy proceedings, retirees are increasingly relieving their former employers of their obligations to provide specific benefits and allowing them to instead make defined contributions to investment vehicles that will pay for retiree health care.<sup>53</sup>

#### A. Negotiated Benefit Reductions

When former employers are financially unable to continue fully providing promised benefits, retirees might agree to accept reduced benefits in order to ensure that at least some can continue. These retirees agree to bear some costs themselves, often by accepting monthly premiums and co-pays in health insurance, to reduce the risk that cost-conscious employers will eliminate benefits entirely.<sup>54</sup> For example, GM's retirees agreed in 2005 to end their previously free health insurance and accept monthly premiums and increased deductibles, paying yearly costs of up to \$370 for individuals and \$752 for families in addition to continued co-payments for prescription drugs.<sup>55</sup> While these amounts are relatively modest in comparison to the average cost of health care, GM anticipated that they would result in significant savings for the company—around \$1 billion per year.<sup>56</sup>

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50. Payne & Ewing, *supra* note 22, at 319.

51. Vallone v. CNA Fin. Corp., 375 F.3d 623, 626–27, 632, 639 (7th Cir. 2004).

52. See Dan Keating, *Good Intentions, Bad Economics: Retiree Insurance Benefits in Bankruptcy*, 43 VAND. L. REV. 161, 174 (1991) [hereinafter Keating, *Good Intentions*].

53. PHYLLIS C. BORZI, KAISER FAMILY FOUND., RETIREE HEALTH VEBAS: A NEW TWIST ON AN OLD PARADIGM: IMPLICATIONS FOR RETIREES, UNIONS, AND EMPLOYERS 3–6 (2009), available at <http://www.kff.org/medicare/upload/7865.pdf>.

54. Joyce, *supra* note 42, at D01.

55. *Cuts in Benefits for G.M. Retirees Approved*, N.Y. TIMES, Apr. 1, 2006, at C1; Joyce, *supra* note 42, at D01.

56. *Cuts in Benefits for G.M. Retirees Approved*, *supra* note 55, at C1; Joyce, *supra* note 42, at D01.

Negotiated benefit reductions often occur in largely unionized industries and come out of negotiations between the retirees' former labor unions and their former employers.<sup>57</sup> Many employers currently facing economic hardships, including those in the automotive and manufacturing industries, are unionized and owe their retirees welfare benefits under collective bargaining agreements.<sup>58</sup> Although labor unions often agree to reduce benefits for current retirees in contract negotiations, they have no duty to represent the interests of retirees when doing so because retirees are not considered members of the collective bargaining unit.<sup>59</sup> Accordingly, retirees currently have no recourse against their former unions when those unions fail to represent retirees or their interests during contract negotiations.<sup>60</sup>

## B. Litigation Remedies

Since the Supreme Court's landmark decision in *Curtiss-Wright v. Schoonejongen* established that ERISA does not bar employers from altering their welfare benefit plans, retirees have had a difficult time fighting benefit cuts in court.<sup>61</sup> While retirees are not entitled to have these benefits continue, ERISA does provide retirees who wish to challenge benefit cuts in court with three potential legal theories.<sup>62</sup> Although ERISA explicitly exempts welfare benefits from its vesting requirements, retirees can argue that the parties intended to contractually create vested benefits.<sup>63</sup> Retirees also have recourse against former employers that breached their fiduciary duties as benefit plan administrators by materially misleading employees about their retirement benefits.<sup>64</sup> And finally, retirees can bring successful estoppel claims by proving that they justifiably relied to their detriment on their employ-

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57. See, e.g., Peter Whoriskey & Kendra Marr, *In Auto Talks, No Cure-All for Health Care Costs: Promised Benefits Weighed Against Survival of Industry*, WASH. POST, Feb. 27, 2009, at D01 ("As General Motors, Chrysler, the autoworkers union and the Obama administration enter negotiations . . . one of the most delicate issues they face is what to do about the health benefits of an estimated 800,000 retirees.").

58. See *id.*

59. *Allied Chem. & Alkali Workers, Local Union No. 1 v. Pittsburgh Plate Glass Co.*, 404 U.S. 157, 166 (1971).

60. See Keating, *Harsh Realities*, *supra* note 4, at 456.

61. 514 U.S. 73, 78 (1995); Bates, *supra* note 32, at 516, 528.

62. Kaplan, *Retirees at Risk*, *supra* note 3, at 301.

63. Henry H. Rossbacher et al., *ERISA's Dark Side: Retiree Health Benefits, False Employer Promises and the Protective Judiciary*, 9 DEPAUL BUS. L.J. 305, 309 (1997).

64. *Id.* at 333.

ers' material misrepresentations under circumstances that warrant relief.<sup>65</sup>

#### 1. VESTING

ERISA sections 1132(a)(1)(B) and (a)(3) give retiree-plaintiffs the ability to enforce the rights provided by their benefits plans and to recover any benefits that are due under those plans.<sup>66</sup> In order to prevail under these sections, plaintiffs must demonstrate that they have a contractual right to their welfare benefits.<sup>67</sup> Thus, the inquiry turns on whether employment contracts created retirement benefits that were alterable at the employer's will, or whether the employer and its employee intended to expressly create vested welfare benefits.<sup>68</sup> Unless such intent is present, courts have treated welfare benefits as revocable, gratuitous promises.<sup>69</sup>

In deciding whether the parties intended to create vested benefits, courts may consider a variety of controlling documents, such as collectively bargained pension agreements and summary plan descriptions.<sup>70</sup> When these documents are ambiguous about the parties' intent, courts may also consider other extrinsic evidence, such as oral representations by the company and its officials concerning whether the benefits were guaranteed upon retirement.<sup>71</sup> A key issue here is whether the documents governing the benefit plan had "reservation of rights" clauses, where the employer reserved the right to unilaterally alter or terminate benefits.<sup>72</sup> When a reservation of rights clause is present, it defeats the claim that the parties intended to create vested welfare benefits and gives the employer the power to unilaterally change welfare benefits.<sup>73</sup>

When the plaintiffs trace their welfare benefits to union-negotiated collective bargaining agreements, the federal circuits have adopted different approaches in determining whether benefits are vested due to the circuit split that emerged after the *UAW v. Yard-*

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65. *Id.* at 329–30.

66. 29 U.S.C. § 1132(a)(1)(B) (2006); § 1132(a)(3).

67. See Richardson, *supra* note 44, at 559.

68. Payne & Ewing, *supra* note 22, at 321.

69. *Id.* at 322.

70. Collective bargaining agreements govern benefit plans for unionized workers; summary plan descriptions inform employees of their coverage, as required by statute. Kaplan, *Retirees at Risk*, *supra* note 3, at 306.

71. Pratt, *supra* note 7, at 139.

72. Payne & Ewing, *supra* note 22, at 322.

73. *Id.*

*Man, Inc.* decision.<sup>74</sup> In *Yard-Man*, the Sixth Circuit created an inference that, absent explicit language in the governing documents, the parties intended to create vested benefits.<sup>75</sup> The *Yard-Man* case arose from a 1974 collective bargaining agreement between Yard-Man, Inc. and the United Automobile Workers (UAW) that was to last three years and provided that once a retired employee reached sixty-five, the company would pay insurance benefits equal to those received by active employees.<sup>76</sup> As it turned out, this promise was short-lived: Yard-Man closed its plant in 1975, and two years later it notified its retirees that their benefits would not continue once the agreement expired.<sup>77</sup> In response, the UAW filed a claim under LMRA § 301, alleging that the termination was a breach of the collective bargaining agreement.<sup>78</sup> The court found that the language in the agreement was unclear as to whether the benefits would last for the lifetime of the retirees or would be subject to renegotiation upon the current contract's expiration, so it looked to factors outside the contract.<sup>79</sup> Retirees had continued receiving benefits even as active employees' benefits had terminated with the plant closing.<sup>80</sup> Additionally, the Sixth Circuit reasoned that a promise to provide early retirees with health insurance when they reached retirement age would be illusory for early retirees under sixty-two if it expired at the end of the collective bargaining agreement's three-year term.<sup>81</sup> Finally, the court reasoned that because retirement benefits are "typically understood as a form of delayed . . . compensation for past services," reasonable parties would not leave them contingent on future negotiations.<sup>82</sup> Considering these factors and contending that reasonable parties would not leave retiree benefits contingent on future negotiations, the court held that retiree benefits had a special "status," and unless there was explicit language to the contrary in the plan documents, the court created an inference that the parties intended to create vested benefits.<sup>83</sup>

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74. Julie Vanneman, *Procedural Fencing in Retiree Benefits Disputes: Applications of the First-Filed Rule in Federal Courts*, 69 U. PITT. L. REV. 123, 146 (2007).

75. *UAW v. Yard-Man, Inc.*, 716 F.2d 1476, 1482 (6th Cir. 1983); Berneking, *supra* note 41, at 271.

76. Berneking, *supra* note 41, at 268.

77. *Id.*

78. *Id.*

79. *Yard-Man*, 716 F.2d at 1480.

80. *Id.* at 1481.

81. *Id.*

82. *Id.* at 1482.

83. *Id.*

Because *Yard-Man* created an inference of vested benefits rather than a presumption, retirees still have the burden of demonstrating that the parties most likely intended to create vested benefits.<sup>84</sup> In subsequent cases, the Sixth Circuit acknowledged that the *Yard-Man* inference applied only if the context and other available evidence indicated an intent to vest.<sup>85</sup> Nevertheless, some federal circuits declined to follow the Sixth Circuit's *Yard-Man* inference.<sup>86</sup> In *International Union v. Skinner Engine Co.*, the Third Circuit reasoned that current employees have the burden of lobbying the union for vested benefits, and therefore benefits should not be considered vested if the language is unclear.<sup>87</sup> The Third Circuit read *Yard-Man* as creating a presumption of vested benefits, a legal rule it found contrary to ERISA's explicit exemption of welfare benefits from its vesting requirements.<sup>88</sup> Similarly, the Seventh Circuit places the burden on plaintiffs when the collective bargaining agreement is silent.<sup>89</sup> The court pointed out in *Bidlack v. Wheelabrator Corp.* that unions have conflicting motivations—there is no reason for them to bargain for vested benefits for retirees who no longer contribute to the union, but those current workers who will retire under a collective bargaining agreement would want vested benefits.<sup>90</sup> Ultimately, the Seventh Circuit has reasoned that because unions are aware of the risks of leaving issues ambiguous when they negotiate collective bargaining agreements, their silence should not give rise to an inference of vested benefits.<sup>91</sup>

While courts are thus divided over whether unionized retirees should have an inference of vested benefits when governing materials lack language to the contrary, no court recognizes such an inference for nonunionized retirees.<sup>92</sup> Both unionized and nonunionized retirees face the same pressure to settle in order to restore their benefits more quickly, but nonunionized retirees are further disadvantaged because they are unorganized in their efforts to maintain benefits.<sup>93</sup> Moreover,

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84. Berneking, *supra* note 41, at 271–72.

85. See, e.g., *Cole v. ArvinMeritor, Inc.*, 549 F.3d 1064, 1069 (6th Cir. 2008); *Yolton v. El Paso Tenn. Pipeline Co.*, 435 F.3d 571, 579 (6th Cir. 2006).

86. Vanneman, *supra* note 74, at 146.

87. 188 F.3d 130, 141 (3d Cir. 1999).

88. *Id.* at 140–41.

89. See, e.g., *Bidlack v. Wheelabrator Corp.*, 993 F.2d 603, 609 (7th Cir. 1993).

90. *Id.*

91. See *Rossetto v. Pabst Brewing Co.*, 217 F.3d 539, 544 (7th Cir. 2000).

92. Kaplan, *Retirees at Risk*, *supra* note 3, at 315.

93. See McNeil, *supra* note 2, at 234.

the documentation they have is generally less thorough than the documentation that most unions maintain.<sup>94</sup>

Regardless of whether retiree-plaintiffs received their benefits pursuant to union-negotiated agreements, they are rarely successful in their claims that welfare benefits were meant to be vested.<sup>95</sup> Even when plan materials promise retirees that they will receive welfare benefits for their lifetimes, the presence of a reservation of rights clause in any controlling document is generally sufficient to overcome retirees' claims of vested benefits.<sup>96</sup> The Seventh Circuit recently confronted such a case in *Cherry v. Auburn Gear, Inc.* and acknowledged the difficult situation faced by retirees while upholding the employer's termination of retiree benefits.<sup>97</sup> Although the court recognized that the legal distinction between lifetime benefits and vested benefits "understandably escaped" the retirees and that few people without legal training would be able to fully comprehend how courts would interpret a reservation of rights clause, it found itself constrained by principles of contract interpretation.<sup>98</sup>

Retirees have not been entirely unsuccessful in claiming that their welfare benefits are vested by contractual agreement. The Sixth Circuit, creator of the *Yard-Man* inference, found in *McCoy v. Meridian Automotive Systems, Inc.* that employees were entitled to vested benefits even though their summary plan descriptions included reservation of rights clauses.<sup>99</sup> The decision found that an agreement tying together eligibility for health and pension benefits, incorporated by reference into the collective bargaining agreement, was convincing intrinsic evidence that the parties intended to create vested benefits.<sup>100</sup> Accordingly, it interpreted the reservation of rights clause as merely informing employees who had not retired before the agreement's end that the company might discontinue their benefits.<sup>101</sup> Additionally, the Seventh Circuit reversed a summary judgment against nonunionized retirees in a case where plan documents contained language about "life-time" benefits and lacked any reservation of rights clauses.<sup>102</sup>

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94. *See id.*

95. Kaplan, *Retirees at Risk*, *supra* note 3, at 305.

96. Payne & Ewing, *supra* note 22, at 322.

97. 441 F.3d 476, 486 (7th Cir. 2006).

98. *Id.* (citing *Vallone v. CAN Fin. Corp.*, 375 F.3d 623, 642 (7th Cir. 2004)).

99. 390 F.3d 417, 421 (6th Cir. 2004).

100. Kaplan, *Retirees at Risk*, *supra* note 3, at 312–13.

101. *McCoy*, 390 F.3d at 425.

102. Kaplan, *Retirees at Risk*, *supra* note 3, at 319.

Overall, cases where retirees successfully argued that they were contractually entitled to vested benefits are increasingly few and far between.<sup>103</sup> As employers continue to vigilantly include reservation of rights clauses in plan-governing documents, those clauses will continue to defeat most claims of vested benefits.<sup>104</sup>

## 2. BREACH OF FIDUCIARY DUTIES

ERISA imposes fiduciary duties of disclosure, care, and loyalty on employers who act as benefit plan administrators.<sup>105</sup> Employers are considered fiduciaries when they have discretionary control over or manage pension plan assets, and such employers must not violate their fiduciary duties when they discuss benefits with their employees.<sup>106</sup> If the employer-administrator materially misled its retirees about retiree welfare benefits when they were employees, those retirees have a cause of action for breach of fiduciary duties under section 404(a)(1) of ERISA.<sup>107</sup> To succeed on such a claim, retiree-plaintiffs must show that the misrepresentation was material and that it was made with scienter.<sup>108</sup> What retirees must prove to satisfy the scienter requirement varies depending on the circuit, and can range from intentional fraud to mere negligence.<sup>109</sup>

The Supreme Court first recognized that ERISA provides employees and former employees with a cause of action when their employer breached its fiduciary duties in *Varity Corp. v. Howe*.<sup>110</sup> In *Varity Corp.*, the Court found that a company had violated its fiduciary duties by intentionally leading its employees to transfer their benefit plans to an insolvent subsidiary in a cost-cutting scheme.<sup>111</sup> *Varity Corp.* was a clear case of an employer engaging in intentionally fraudulent conduct, and while it confirmed that an employer's breach of fiduciary duties was actionable, it left open the issues of when a misrepresentation is material and what level of intent plaintiffs must prove.<sup>112</sup>

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103. *Id.* at 309.

104. *Id.* at 309–15.

105. 29 U.S.C. § 1104(a)(1) (2006).

106. Kaplan, *Retirees at Risk*, *supra* note 3, at 320–21.

107. 29 U.S.C. § 1104(a)(1).

108. Kaplan, *Retirees at Risk*, *supra* note 3, at 321.

109. *Id.*

110. 516 U.S. 489, 490 (1996).

111. *Id.* at 494.

112. Kaplan, *Retirees at Risk*, *supra* note 3, at 321.

Federal circuits have adopted different approaches in resolving these issues. Regarding materiality, most circuits follow the Serious Consideration Doctrine, which holds that potential changes to benefits are material and must be disclosed when they are being discussed for purposes of implementation by senior management with authority to implement the changes.<sup>113</sup> Before this point, any potential changes to employee benefits are speculative, not material, so employers are not liable for misrepresenting them.<sup>114</sup> The Second and Fifth Circuits find the Serious Consideration Doctrine flawed because it could allow a plan administrator to knowingly deny or mislead employees simply because plan changes had not achieved sufficient internal ratification.<sup>115</sup> Those circuits have instead found changes material when an employer's misrepresentation was substantially likely to mislead a reasonable employee in making an adequately informed retirement decision.<sup>116</sup>

Plaintiffs' burdens in proving scienter also vary depending on the circuit.<sup>117</sup> The Seventh Circuit requires that a successful breach of fiduciary duty claim demonstrate intentional misconduct on the part of the employer.<sup>118</sup> In contrast, the Second, Third, and Sixth Circuits find employers liable when they recklessly give misinformation.<sup>119</sup> These circuits find even unintentional misrepresentations actionable because ERISA imposes fiduciary duties that are higher than those at common law, and it focuses on the effect disclosures have on the listener rather than on the subjective intent of the discloser.<sup>120</sup>

In practice, plaintiffs have significant evidentiary burdens in proving the materiality and scienter requirements of a breach of fiduciary duties claim. If plaintiffs are unable to prove either contractually vested benefits or a breach of fiduciary duties, estoppel provides them with a third legal challenge to benefit reductions.

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113. *Id.* at 322.

114. *Beach v. Commonwealth Edison Co.*, 382 F.3d 656, 659 (7th Cir. 2004).

115. Kaplan, *Retirees at Risk*, *supra* note 3, at 323 (citing *Martinez v. Schlumberger, Ltd.*, 338 F.3d 407, 428 (5th Cir. 2003)).

116. *See, e.g.*, *Ballone v. Eastman Kodak Co.*, 109 F.3d 117, 122–23 (2d Cir. 1997).

117. Kaplan, *Retirees at Risk*, *supra* note 3, at 324–25.

118. *Vallone v. CNA Fin. Corp.*, 375 F.3d 623, 642 (7th Cir. 2004).

119. Kaplan, *Retirees at Risk*, *supra* note 3, at 324–25.

120. *Id.*



### 3. ESTOPPEL

Retirees can bring a final challenge to their former employers' alterations of benefits under the doctrine of estoppel.<sup>121</sup> This claim posits that an employer made false statements about the unalterable or lifetime nature of welfare benefits, and its retirees took reasonable actions in reliance on those statements that proved detrimental to their interests.<sup>122</sup> To succeed on an estoppel claim, plaintiffs must establish three elements: (1) a material misrepresentation, (2) reasonable and detrimental reliance upon the representation, and (3) extraordinary and extreme circumstances.<sup>123</sup>

Each of these requirements imposes a high burden for plaintiffs to overcome. Plaintiffs must generally prove that the employer knowingly provided false information in order for a misrepresentation to be material.<sup>124</sup> As the Seventh Circuit posited in *Vallone v. CNA Financial Corp.*, this requirement means that an employer's representations about plans cannot be considered false unless the speaker actually had a different intention when the representation was made.<sup>125</sup> Furthermore, courts have found that retirees' reliance on any alleged statements of lifetime benefits is unreasonable where reservation of rights clauses in plan documents give the employer a right to change or eliminate benefits.<sup>126</sup> Employees must also prove that the detrimental reliance came after the employer made the alleged misstatement. For instance, the Seventh Circuit held in *UAW v. Rockford Powertrain, Inc.* that plaintiffs had not demonstrated reliance when the alleged misstatements were made during exit interviews after they had already decided to retire.<sup>127</sup> Even if retirees meet these burdens, they must still prove that extraordinary circumstances justify estoppel.<sup>128</sup> Courts evaluate the facts in each particular case to determine whether such circumstances are present but generally require proof that the employer

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121. Payne & Ewing, *supra* note 22, at 348.

122. *Id.* at 349.

123. Kaplan, *Retirees at Risk*, *supra* note 3, at 327.

124. *Id.*

125. 375 F.3d 623, 639 (7th Cir. 2004).

126. See, e.g., *In re Unisys Corp. Retiree Med. Benefit "ERISA" Litig.*, 58 F.3d 896, 907-08 (3d Cir. 1995).

127. 350 F.3d 698, 705-06 (7th Cir. 2003).

128. Kaplan, *Retirees at Risk*, *supra* note 3, at 327.

intentionally used false statements about benefits to induce employees' actions.<sup>129</sup>

Because of this high evidentiary burden, estoppel claims, like claims of vested benefits and breach of fiduciary duties, are difficult to prove. Considering the difficulties that plaintiffs face in bringing any of these causes of action, it is no surprise that retirees rarely succeed when challenging cutbacks of their welfare benefits in court.

### C. Protection of Welfare Benefits in Bankruptcy

Retiree benefits are protected when companies enter Chapter 11 bankruptcy under section 1114 of the Bankruptcy Code.<sup>130</sup> Congress' goal in enacting § 1114 was to mandate that companies in Chapter 11 continue providing as many of the promised health care benefits as possible while reorganizing.<sup>131</sup> Because of § 1114, employers are obligated to continue providing medical benefits unless there are extenuating circumstances.<sup>132</sup>

Under § 1114(g)(3), modification is permitted if "such modification is necessary to permit the reorganization of the debtor and assures that all creditors, the debtor, and all of the affected parties are treated fairly and equitably, and is clearly favored by the balance of the equities."<sup>133</sup> Alternately, modification is allowed if the trustees of the bankrupt entity reach an agreement with the representative of the recipient retirees.<sup>134</sup> A recent amendment to § 1114 further protects health care benefits by providing that if a debtor modifies benefits within 180 days before filing bankruptcy, and the debtor was insolvent at the time of modification, the court will reinstate the premodifi-

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129. *Id.* at 330–31 (citing *Devlin v. Empire Blue Cross & Blue Shield*, 274 F.3d 76, 86–87 (2d Cir. 2001); *Abbruscato v. Empire Blue Cross & Blue Shield*, 274 F.3d 90, 101–02 (2d Cir. 2001)).

130. Keating, *Good Intentions*, *supra* note 52, at 174.

131. Keating, *Harsh Realities*, *supra* note 4, at 447.

132. *See, e.g.*, Daniel Keating, *Bankruptcy Code § 1114: Congress' Empty Response to the Retiree Plight*, 67 AM. BANKR. L.J. 17, 18 (1993) [hereinafter Keating, *Empty Response*] (explaining that section 1114 of the Bankruptcy Code forced LTV Corporation to, "absent extenuating circumstances, continue to honor promises of medical benefits made to retirees even if the company was in chapter 11"). The courts do allow modification if necessary to allow a debtor to reorganize successfully. *See, e.g.*, *In re Horizon Natural Res. Co.*, 316 B.R. 268, 272–74 (Bankr. E.D. Ky. 2004) (where the termination of a collective bargaining agreement in bankruptcy caused nearly 3800 coal workers and their dependents to lose health insurance).

133. 11 U.S.C. § 1114(g)(3) (2006).

134. § 1114(e)(1)(B).

cation benefits unless the balance of equities favors modification.<sup>135</sup> Section 1114 applies while the Chapter 11 case is pending, but § 1129(a)(13) continues these protections through the plan confirmation process, mandating that the debtor continue all retiree benefits at levels established under § 1114 until the bankruptcy court confirms the reorganization plan.<sup>136</sup> Thus, retirees might have three claims in bankruptcy: an unsecured claim for the amount by which their benefits are reduced while the Chapter 11 case is pending, a claim for the amount they are reduced in the confirmed plan, and a right to the continued payment of benefits as established by the Chapter 11 plan.<sup>137</sup> Section 1129 also conditions court approval on the plan's feasibility, which assures retirees that the former employer's promise to continue payments is "more than just wishful thinking."<sup>138</sup>

The protections of § 1114 are not as strong in practice as they might initially seem because courts routinely allow modifications to retiree benefits that they deem necessary to allow companies in Chapter 11 to reorganize.<sup>139</sup> The legislative history behind § 1114 suggests that the "necessary to permit reorganization of the debtor" language should be construed in favor of retirees, but the vagueness of the standard has led to diverse interpretations by the courts.<sup>140</sup> In one recent case involving the Horizon Natural Resources Company, the debtor company had a clause stipulating that the various obligations to current union workers and retirees would "run with the company."<sup>141</sup> The bankruptcy plans sought to sell the company's assets free of all encumbrances, including those retiree obligations.<sup>142</sup> The court found that those obligations were preventing the debtor from selling its assets and refused to enforce the clause in order to allow the company to sell the assets together and for a higher price than it could have received with the clause intact.<sup>143</sup>

Thus, while Congress did give health care benefits in bankruptcies some protection with § 1114, the broad judicial discretion it gives

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135. § 1114(l); Keating, *Harsh Realities*, *supra* note 4, at 447.

136. § 1129(a)(13); Keating, *Empty Response*, *supra* note 132, at 45.

137. Keating, *Empty Response*, *supra* note 132, at 45.

138. *Id.* at 46.

139. See Steven Kropp, *Collective Bargaining in Bankruptcy: Toward an Analytical Framework for Section 1113*, 66 TEMP. L. REV. 697, 709-12 (1993).

140. Keating, *Empty Response*, *supra* note 132, at 40.

141. Keating, *Harsh Realities*, *supra* note 4, at 449 (citing *In re Horizon Natural Res. Co.*, 316 B.R. 268, 271 (Bankr. E.D. Ky. 2004)).

142. *Id.* (citing *Horizon Natural Res.*, 316 B.R. at 271-72, 274).

143. *Id.* at 450 (citing *Horizon Natural Res.*, 316 B.R. at 279).

courts means that continuation of benefits in Chapter 11 is far from guaranteed. Additionally, § 1114 applies only in Chapter 11 bankruptcies; retirees whose former employers have filed for Chapter 7 bankruptcy remain unprotected.<sup>144</sup> Consequently, many companies seeking bankruptcy protection file Chapter 7 in order to shed their retiree obligations.<sup>145</sup>

#### D. Shifting from Defined Benefit Plans to Defined Contribution Plans

Employers' widespread shift from promising defined retirement benefits to offering defined contribution plans is perhaps the most dramatic current trend affecting retiree benefits.<sup>146</sup> Alongside this trend, several employers have recently dealt with the problems posed by their increasingly expensive defined welfare benefit obligations by transferring these obligations to investment vehicles and promising defined contributions to these vehicles.<sup>147</sup> As replacements for employer-provided welfare benefits, these vehicles place many of the risks formerly borne by employers on the shoulders of retirees,<sup>148</sup> but could nevertheless potentially provide more stability for retirees hoping to maintain their welfare benefits.

Under defined contribution plans, the employers promise to make predetermined contributions to investment vehicles that supplement contributions made by the employees themselves.<sup>149</sup> The employee's income in retirement depends on the investment success of these vehicles.<sup>150</sup> These plans give the employee the ability to direct how the funds will be invested, within the parameters determined by the plan.<sup>151</sup> Many employers create incentives to stimulate employee contributions to these funds, often by offering to match employee contributions to 401(k) plans and similar investment vehicles.<sup>152</sup> In con-

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144. Keating, *Empty Response*, *supra* note 132, at 30–31.

145. Nicholas J. Brannick, *At the Crossroads of Three Codes: How Employers Are Using ERISA, the Tax Code, and Bankruptcy to Evade Their Pension Obligations*, 65 OHIO ST. L.J. 1577, 1599–1600 (2004).

146. Stabile, *supra* note 18, at 495.

147. See BORZI, *supra* note 53, at i.

148. See Richard L. Kaplan, *Enron, Pension Policy, and Social Security Privatization*, 46 ARIZ. L. REV. 53, 59 (2004) [hereinafter Kaplan, *Enron*].

149. See Befort, *supra* note 1, at 946.

150. Kaplan, *Enron*, *supra* note 148, at 59–60.

151. *Id.* at 59.

152. Michael Barbanell Landres, *Smoke, Mirrors, and ERISA: The False Illusion of Retirement Income Security*, 40 LOY. L.A. L. REV. 1169, 1176 (2007). While 401(k)

trast, traditional defined benefit plans promise specific retirement benefits that are typically funded solely by the sponsoring employer.<sup>153</sup>

As noted earlier, many employers are modifying the way in which they fund the welfare benefits of current retirees by creating investment vehicles to absorb their current obligations to provide specific benefits.<sup>154</sup> These employers most commonly do so by creating Voluntary Employee Benefits Associations (VEBAs).<sup>155</sup> VEBAs are tax-exempt organizations that collect funds from employers and use the investment income from these funds to provide benefits in retirement.<sup>156</sup> Unlike 401(k) plans and similar individual investment accounts, investment professionals manage the funds in VEBAs.<sup>157</sup>

Defined contribution systems are attractive for employers because they shift the risks of investment performance to employees.<sup>158</sup> The risk of future increases in health care costs is consequently also borne by retirees, and the employer's potential liability is capped because its only obligation is to make its agreed-on contributions to vehicles that pay the retiree benefits.<sup>159</sup> This means that if the investments do not provide enough income to cover retirement benefits, the employee has no recourse against the employer.<sup>160</sup> While these plans are understandably attractive for employers, they have significant drawbacks for employees. Besides bearing the risks of investment performance, employees are often provided with investment vehicles that rely heavily on investments in the employing company, making those vehicles riskier investments than more diversified portfolios.<sup>161</sup>

In contrast, employees might find defined benefit plans appealing because they place the risk of investment performance with the

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plans are often provided in place of defined benefit plans, they are not true pension plans because they generally involve the employee's funds alone. Kaplan, *Enron*, *supra* note 148, at 65.

153. Befort, *supra* note 1, at 946.

154. See ELLEN O'BRIEN, AARP PUB. POLICY INST., RETIREE HEALTH CARE: WHAT DO THE NEW AUTO INDUSTRY VEBAS MEAN FOR CURRENT AND FUTURE RETIREES? 4 (2008), [http://assets.aarp.org/rgcenter/econ/i4\\_veba.pdf](http://assets.aarp.org/rgcenter/econ/i4_veba.pdf).

155. See *id.* at 4–5, 9 (detailing nine VEBAs recently established to cover employers' welfare benefit obligations).

156. McNeil, *supra* note 2, at 257.

157. *Id.* at 258.

158. Stabile, *supra* note 18, at 497–98.

159. BORZI, *supra* note 53, at 8; Befort, *supra* note 1, at 946, 949.

160. See Befort, *supra* note 1, at 946, 949.

161. Defined contribution plans often heavily invest assets in the company stock of participants' employers against the widely lauded investment strategy of diversification. *Id.* at 955, 958. The Enron scandal illustrates the dangers of this prevalent approach. *Id.* at 955–56.

employer by creating specific obligations that it must fulfill.<sup>162</sup> Defined benefit plans make retirement planning easier because they let employees know exactly what level of welfare benefits they can expect in retirement, provided that the employer carries out its promises.<sup>163</sup> However, as many current retirees are experiencing, these traditional pension plans have significant downsides in practice. First, these plans depend entirely on the former employer's financial ability to fulfill its promises.<sup>164</sup> Second, as retirees' difficulties in maintaining their welfare benefits through litigation illustrate, these obligations are illusory when employers often unambiguously reserve the right to unilaterally terminate or modify welfare benefits.<sup>165</sup>

While their current shortcomings should raise some concerns, VEBAs are not without benefits for retirees. Benefits provided out of income from these investment vehicles are not subject to cutbacks from former employers after retirement, except to the extent that those employers fail to make promised contributions.<sup>166</sup> If VEBAs are properly diversified so their financial success is placed apart from that of the beneficiaries' former employer, they could become a more reliable source of welfare benefits than gratuitous promises from financially challenged employers.

Putting aside the relative advantages and disadvantages of defined contribution-funded plans, they are becoming an increasingly important source of welfare benefits for current retirees. Employers have often developed VEBAs to take over defined welfare benefit obligations after collective bargaining negotiations, to settle lawsuits against their modification or termination of welfare benefits, or to resolve outstanding liabilities in bankruptcy.<sup>167</sup> During the previously mentioned 2005 negotiations with the UAW, Ford and General Motors agreed to create VEBAs in exchange for reduced retiree health care obligations.<sup>168</sup> The new health care plans either provided retirees with substantial benefits in exchange for monthly premiums paid by reti-

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162. Kaplan, *Enron*, *supra* note 148, at 57.

163. See Timothy A. Steadman, *Fighting Windfalls: The PBGC's Battle for Workers' Pension Benefits (and Its Own Financial Health)*, 61 ARK. L. REV. 509, 511 (2008).

164. Henry H. Drummonds, *The Aging of the Boomers and the Coming Crisis in America's Changing Retirement and Elder Care Systems*, 11 LEWIS & CLARK L. REV. 267, 271 (2007) (noting that employees of defined benefit plans bear the risk that the employer will become insolvent).

165. Payne & Ewing, *supra* note 22, at 322.

166. See BORZI, *supra* note 53, at 8-9.

167. *Id.* at i.

168. Keating, *Harsh Realities*, *supra* note 4, at 453.

rees, or provided catastrophic coverage with no premiums but higher deductibles and co-pays.<sup>169</sup> In exchange for these cost-reducing concessions, the companies agreed to make contributions to VEBAs: GM agreed to contribute \$3 billion in cash through 2011, along with at least \$30 million per year in profit-sharing payments through 2012 and additional payments based on stock price.<sup>170</sup> Defined contribution vehicles also have been used in bankruptcy cases to ensure that benefits continue for existing retirees.<sup>171</sup> For example, a bankruptcy court resolving the case of Tower Automotive upheld a bankruptcy plan that created a VEBA that would receive cash payments of at least twenty percent of the \$150 million value of future retiree medical benefits.<sup>172</sup>

This recent use of VEBAs to provide retiree benefits that were previously guaranteed by defined benefit pension plans means that the current shift toward defined contribution plans is potentially relevant for current retirees who receive guaranteed benefits pursuant to defined benefit plans.<sup>173</sup> Considering the volatile nature of defined welfare benefits, which depend on the fortunes of the providing employer and are generally terminable at will, this shift may prove to be a blessing for many retirees.

## E. Conclusions

In most cases, current remedies leave retirees with little recourse when their former employers are determined to cut or eliminate their welfare benefits.<sup>174</sup> The remedies available to retirees have significant flaws and do not provide adequate protection. Retirees have little bargaining power with their former employers and are not represented in union negotiations that affect their benefits.<sup>175</sup> Legal challenges when benefits are reduced or eliminated impose high evidentiary burdens on plaintiffs, and they almost always fail when employers have unambiguously reserved the right to modify or terminate welfare benefits.<sup>176</sup> While retirees' welfare benefits receive some

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169. *Id.*

170. *Id.*

171. *Id.* at 454.

172. *In re Tower Auto. Inc.*, 241 F.R.D. 162 (S.D.N.Y. 2006); Keating, *Harsh Realities*, *supra* note 4, at 454.

173. Keating, *Harsh Realities*, *supra* note 4, at 440, 452-56.

174. *Id.* at 460-61, 440-42.

175. *Id.* at 437-38.

176. Kaplan, *Retirees at Risk*, *supra* note 3, at 301-06.

protections during Chapter 11 bankruptcy proceedings, they are unprotected when employers' troubles lead to Chapter 7 bankruptcy.<sup>177</sup> Finally, the defined contribution vehicles employers are developing to provide retirees' welfare benefits often depend too heavily on investments in the employer.<sup>178</sup>

#### **IV. Proposal: Retirees' Reasonable Expectations of Welfare Benefits Need Additional Protections**

Preserving welfare benefits at the levels employees had expected in retirement will remain impossible in many cases where the former employer's economic situation necessitates reductions.<sup>179</sup> Although legal changes could help current retirees by making excessive benefit cuts more difficult and encouraging employers to develop sustainable welfare benefit plans, they cannot create sufficient financial resources for employers to satisfy their promises to retirees where resources are lacking. Given this constraint, government can most effectively protect retirees from economically motivated cutbacks by controlling the costs that these benefits impose on their former employers.

Current retirees need additional protections on several fronts to ensure that their reliance-backed expectations of welfare benefits can be met without jeopardizing the financial health of former employers. Formerly unionized retirees should be represented in negotiations that affect their benefits and should have some recourse against their former unions when those negotiations result in unreasonable benefit cuts. The *Yard-Man* inference should be adopted in all circuits, and courts should account for the relative naïveté of employees by more fully considering whether reasonable persons would infer lifelong benefits from plan documents and employer representations. Finally, the law should address the concerns raised by funding welfare benefits with defined employer contributions by imposing diversification

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177. See U.S. DEP'T OF LABOR, FACT SHEET: YOUR EMPLOYER'S BANKRUPTCY: HOW WILL IT AFFECT YOUR EMPLOYEE BENEFITS? 1 (2008), <http://www.dol.gov/ebsa/pdf/bankruptcy.pdf>.

178. See Arleen Jacobius, *More Employers Making Contributions in Stock; Percentage of Plan Sponsors Offering Employer Stock Jumps, Despite Enron Fallout*, BUS. INS., Sept. 23, 2002, at 15.

179. See, e.g., Drummonds, *supra* note 164, at 277-78 (discussing the underfunding of United Airlines pilots' pension fund, as well as those of Delta and Northwest, as they underwent bankruptcy reorganization); Keating, *Good Intentions*, *supra* note 52, at 168 ("Without adequate prefunding, an unambiguously vested retiree insurance program remains a promise whose worth is a function of the financial health of the company that has made it.").



requirements on VEBAs and other employer-independent investment vehicles.

Unfortunately, these reforms will likely prove ineffective or economically untenable for former employers if the cost of providing health care for retirees continues escalating at its current pace.<sup>180</sup> While Americans are continually bombarded with fears that Social Security will soon face funding shortfalls, Medicare faces an even more dire future outlook.<sup>181</sup> Social Security costs were equal to 4.4% of the national gross domestic product (GDP) in 2008 and are projected to increase to 6.2% of GDP by 2034 before falling to around 5.8% by 2050 and remaining at that level.<sup>182</sup> Medicare spending, on the other hand, currently represents around 3.2% of GDP and is projected to surpass Social Security spending by 2028 and reach 11.4% of GDP in 2083.<sup>183</sup> According to one recent projection, health care costs will top \$8000 per person for the first time in 2009.<sup>184</sup> By 2018, health care costs are projected to reach \$13,100 per person, comprising “\$1 out of every \$5 spent on the economy.”<sup>185</sup> The impact of these costs is being heightened as a consequence of the current economic downturn; because less tax revenue is available to cover these costs, Medicare’s hospital trust fund could become insolvent as early as 2016, three years sooner than previously projected.<sup>186</sup> These problems are especially acute for retirees, as annual health costs for those over sixty-five are more than three times those of the general population.<sup>187</sup> Retirees’ health care costs are increasing at an alarming rate that employers could not reasonably have anticipated and cannot reasonably afford. Accordingly, the federal government must find a permanent solution that addresses these skyrocketing costs if employer-provided retiree health care benefits are to continue.

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180. See Freudenheim, *supra* note 21, at C1.

181. See PAMELA VILLAREAL, NAT’L CTR. FOR POLICY ANALYSIS, SOCIAL SECURITY AND MEDICARE PROJECTIONS: 2009, at 1 (2009), <http://www.ncpa.org/pdfs/ba662.pdf>.

182. Soc. Sec. & Medicare Bds. of Trs., Soc. Sec. Admin., A Summary of the 2009 Annual Reports, <http://www.ssa.gov/OACT/TRSUM/index.html> (last visited Nov. 12, 2009).

183. *Id.*

184. Associated Press, *Health Care Costs to Top \$8,000 per Person*, PRESS OF ATLANTIC CITY, Feb. 24, 2009, at A6 [hereinafter *Health Care Costs*].

185. *Id.*

186. *Id.*

187. Brent R. Trame, Note, *Going Dutch: Can Holland Solve the U.S. Insurance Problem?*, 16 ELDER L.J. 445, 454 (2009).

### A. Give Retirees Representation in Union Negotiations That Affect Their Benefits

Labor unions currently owe retirees no duty of fair representation because retirees are not considered “employees” under the National Labor Relations Act and, therefore, are not members of the collective bargaining unit.<sup>188</sup> Accordingly, courts have held that retiree benefits are a permissive, rather than mandatory, subject of bargaining.<sup>189</sup> Historically, active workers in the union have safeguarded the interests of retirees.<sup>190</sup> Union members often feel a sense of loyalty to retirees as friends and family members and recognize that they will someday as retirees be subject to agreements they bargain for as workers.<sup>191</sup> However, as pieces of the proverbial pie become smaller, it is inevitable that the interests of retirees will increasingly clash with those of current workers. Recently, many retirees have found that their former unions were not adequately representing their interests.<sup>192</sup> In *Nelson v. Stewart*, the Seventh Circuit acknowledged this conflict of interest between the union and retirees, and asserted that section 1114 of the Bankruptcy Code mandated that when such a conflict is present, the court should appoint a retiree committee if the debtor seeks to modify or terminate retiree medical benefits.<sup>193</sup>

Retirees are particularly vulnerable in collective bargaining negotiations. Not only do they have no votes in labor contracts that affect their interests, they also lack leverage with both their former unions and former employers because their contributions occurred in the past.<sup>194</sup> Furthermore, retirees have already detrimentally relied on the employer and union representations about welfare benefits and often require more resources than active workers because they increasingly outnumber those active workers.<sup>195</sup> These factors heighten the union’s temptation to favor active workers over retirees in contract negotiations, a temptation that is likely to increase as the ratio of retirees to current workers continues to rise.<sup>196</sup>

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188. Bates, *supra* note 32, at 516.

189. *Allied Chem. & Alkali Workers, Local Union No. 1 v. Pittsburgh Plate Glass Co.*, 404 U.S. 157, 187–88 (1971).

190. Keating, *Harsh Realities*, *supra* note 4, at 456.

191. *Id.*

192. *Id.*

193. 11 U.S.C. § 1114(c)(2) (2006); 422 F.3d 463, 471 (7th Cir. 2005).

194. Keating, *Harsh Realities*, *supra* note 4, at 437–38.

195. *Id.* at 438–39.

196. *See id.* at 437.

Retirees deserve a voice in negotiations that directly affect their benefits. Their former unions usually represent their interests in collective bargaining negotiations and often represent them well.<sup>197</sup> However, as cases such as *Nelson* make clear, the union must bargain over a finite amount of resources and has incentives that may lead it to favor the interests of active workers over those of retirees.<sup>198</sup> To counter this temptation, unions should have a duty to represent the interests of retirees when entering into negotiations that affect retiree benefits, and retirees should have legal recourse against their former unions if they approve unreasonable cuts. This would be a duty of fair representation similar to that already imposed on unions when they represent members of the collective bargaining unit, and it would forbid treating retirees' interests in a way that is arbitrary, discriminatory, or in bad faith.<sup>199</sup> Such a duty would not unduly constrain unions in collective bargaining negotiations, as courts recognize that they have a "wide range of reasonableness" in representing their collective bargaining unit, and therefore do not breach their duty simply by supporting the interests of one group over those of another.<sup>200</sup> Rather, holding unions accountable for agreements they make that affect the rights of existing retirees would protect the interests of those retirees and ensure that unions do not treat those interests lightly as they seek compromises that ensure optimal benefits for active workers.

**B. Courts Should Find Welfare Benefits Vested Where Plan Documents Are Ambiguous and Retirees Reasonably Believed in Lifelong Benefits**

Retirees who choose to challenge employer modifications of benefits in court are rarely successful, as they must overcome high evidentiary burdens to prevail under existing legal remedies. The *Yard-Man* inference relaxes this burden when plan documents are ambiguous about whether benefits are vested and retirees provide other evidence supporting their belief in vested benefits.<sup>201</sup> This approach properly balances the interests of retirees with the interests of employers by protecting the reasonable expectations of retirees without

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197. *Id.* at 456.

198. Sondgeroth, *supra* note 8, at 1225.

199. Bates, *supra* note 32, at 513 (citing *Vaca v. Sipes*, 386 U.S. 171, 190 (1967)).

200. *Id.* at 513–14.

201. Berneking, *supra* note 41, at 271–72.

violating the contractual agreements of employers who legitimately and unambiguously reserved the right to alter or eliminate benefits. Accordingly, it should be adopted across the federal courts.

Those circuits that have declined to follow the *Yard-Man* approach have primarily cited concerns about its compatibility with ERISA, which explicitly exempts welfare benefits from its vesting requirements.<sup>202</sup> Although ERISA does exempt welfare benefits from its vesting requirements, it does not prohibit parties from contractually creating vested benefits. Moreover, there was a rationale behind ERISA's exclusion of welfare benefits: when ERISA was enacted, pension benefits were far more widespread and costly than welfare benefits.<sup>203</sup> Congress did not require that welfare benefits vest and did not provide insurance for those benefits because it determined that the cost of doing so was unjustifiable and reasoned that the court system could develop the law as needed to protect these benefits.<sup>204</sup> The fact that welfare benefits are exempted from ERISA's vesting requirements may preclude a presumption of vesting, but given the context of that exclusion, it should not prevent courts from giving retirees a favorable inference where they provide evidence justifying their expectations of lifelong benefits.

When plan documents are ambiguous, courts also should realistically evaluate retirees' expectations of retirement benefits based on their employers' representations. As the Seventh Circuit acknowledged, individuals who are unfamiliar with the intricacies of legal terminology would not likely recognize a distinction between vested and lifelong benefits.<sup>205</sup> When plan documents do not unequivocally state that the welfare benefits of retiree-plaintiffs are alterable or terminable at will, and their employer's representations gave them reasonable foundation for their belief that these benefits were guaranteed for life, courts should enforce these promises. Employers should bear the burden when they neglect to clearly inform employees that their benefits are subject to alteration or termination and instead represent them as lifelong benefits.

Realistically, these changes may provide increasingly little help to retirees challenging benefit modifications. Employers have gotten

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202. See, e.g., *Int'l Union v. Skinner Engine Co.*, 188 F.3d 130, 141 (3d Cir. 1999); *Anderson v. Alpha Portland Indus., Inc.*, 836 F.2d 1512, 1517 (8th Cir. 1988).

203. Sondgeroth, *supra* note 8, at 1259.

204. *Id.*

205. *Cherry v. Auburn Gear, Inc.*, 441 F.3d 476, 486 (7th Cir. 2006).

much better at clearly reserving the right to modify or terminate benefits.<sup>206</sup> Even when retirees prevail on their legal challenges, courts can only order employers to continue providing benefits when they can afford to do so.<sup>207</sup> Most employers that decide to reduce or terminate benefits do so because of economic difficulties and have insufficient financial resources to satisfy defined welfare benefit obligations.<sup>208</sup> However, fully extending the *Yard-Man* inference and realistically assessing employees' retirement benefit expectations would recognize the legitimacy of plaintiffs' expectations and provide relief when employers have sufficient resources to honor judgments. Perhaps more importantly, the increased likelihood that retirees may succeed in litigation could make employers more willing to bargain over welfare benefit modifications, rather than simply cutting benefits with knowledge that legal challenges will likely be unsuccessful.

### C. Require Diversification When VEBAs Provide Welfare Benefits

The federal government currently spends an enormous amount of money on providing Medicare to older Americans. Medicare spent an average of \$8304 per enrollee in 2006, an amount that grew an average of 3.5% each year between 1992 and 2006.<sup>209</sup> Considering these costs, the federal government avoids substantial burdens by encouraging the private funding of retiree welfare benefits.<sup>210</sup> As such, it should encourage practices that will help employer-provided welfare benefits continue.

Welfare benefits are not sufficiently protected when they are provided in defined benefit pension plans.<sup>211</sup> They impose prohibitive costs on employers, and employers usually are able to alter or rescind these benefits at will.<sup>212</sup> Furthermore, because the defined benefit scheme imposes no vesting requirements on welfare benefits, employ-

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206. See Kaplan, *Retirees at Risk*, *supra* note 3, at 309.

207. See McNeil, *supra* note 2, at 230.

208. See Grudzien, *supra* note 11, at 786.

209. Richard Pizzi, *Study: Variations Hinder Medicare Reform*, HEALTHCARE FIN. NEWS, Apr. 3, 2009, <http://www.healthcarefinancenews.com/news/study-variations-hinder-medicare-reform>.

210. Lorraine Schmall, *Defined Contribution Plans After Enron*, 41 BRANDEIS L.J. 891, 935 (2003).

211. See, e.g., *Lockheed Corp. v. Spink*, 517 U.S. 582, 890 (1996) ("Employers or other plan sponsors are generally free under ERISA, for any reason at any time, to adopt, modify, or terminate welfare plans.")

212. *Curtiss-Wright Corp. v. Schoonejongen*, 514 U.S. 73, 78 (1995).

ers have largely been unwilling to guarantee them.<sup>213</sup> Employers included in the Standard & Poor 500 had funded only 22% of their expected welfare benefit costs as of December 2005, compared to 90% of their expected pension costs.<sup>214</sup> While many employers have continued providing welfare benefits on a pay-as-you-go basis, they are unwilling to pre-fund these benefits under the current scheme because they view them as uncertain and conditional liabilities that they are not eager to guarantee.<sup>215</sup> As employer modification or termination of benefits is becoming increasingly routine, promises of specific welfare benefits in retirement seem especially illusory when employers are unwilling to set aside money to fund them.

Conversely, employers are more willing to fund welfare benefits through VEBAs because they impose much more predictable funding requirements and place the risk of uncertain health care costs on retirees.<sup>216</sup> For example, the automakers agreed to fund their health care VEBAs at a much higher level than Standard & Poor 500 companies have generally funded anticipated welfare benefit costs: 68% for GM, 57% for Ford, and 60% for Chrysler.<sup>217</sup> Aside from inducing employers to better fund their welfare benefit obligations, VEBAs benefit retirees by placing the investment vehicles that fund these benefits in the hands of an independent trustee, removing the risk that the employer will be able to modify or eliminate welfare benefits when its financial status is threatened.<sup>218</sup>

Employers have been eager to shed their uncertain welfare benefit liabilities and are routinely using negotiations, legal settlements, and bankruptcy reorganizations to transfer these benefits to VEBAs.<sup>219</sup> However, many legal commentators have expressed concerns for retirees about funding vehicles that make their benefits dependent on volatile financial markets and extensively rely on investments in their former employers.<sup>220</sup>

To address these concerns, and to make VEBAs' independence from their beneficiaries' former employers a meaningful advantage,

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213. O'BRIEN, *supra* note 154, at 3.

214. *Id.*

215. *Id.*

216. *Id.*

217. *Id.* at 7 tbl.1.

218. BORZI, *supra* note 53, at 2, 8–9.

219. *Id.* at i; *see also* O'BRIEN, *supra* note 154, at 4–5 Box 1 (providing several examples of VEBAs that have recently been established to fund employers' health care liabilities).

220. Stabile, *supra* note 18, at 499–500.

the government should impose minimum diversification requirements on VEBAs. The government could ensure adequate diversification by adopting a model similar to those already imposed on mutual funds.<sup>221</sup> As a similar proposal suggested, an insurance program for VEBAs could adopt a diversification formula that sets a range of acceptable investment levels across a range of investment categories with different risk classifications.<sup>222</sup> Requiring investments in relatively secure bonds and other stable instruments along with more volatile stocks would keep investment vehicles equipped to weather some market fluctuations.<sup>223</sup> Additionally, the federal insurance program should cap the amount investment vehicles can have in a single company. This would ensure that retirees' investment success can continue apart from the fortunes of their former employer.<sup>224</sup>

Meeting these diversification requirements could prove very difficult for current defined contribution funds that are highly dependent on investments in retirees' former employers. For example, GM's UAW retiree health care trust received a 17.5% stake in the new company after GM emerged from Chapter 11 bankruptcy.<sup>225</sup> Because diversifying trusts such as these will take time, any diversification requirement should be phased in gradually. The government could also help VEBAs meet diversification requirements while remaining adequately capitalized by setting aside federal funds for assistance. So long as the award it gives to struggling VEBAs is less than the costs the VEBA-covered retirees would impose on Medicare and Medicaid if the VEBAs would have failed without government assistance, this should result in net savings.

While this proposal would necessarily require that the government invest resources to monitor VEBAs' investment activities, it could create substantial savings for the government by keeping retiree

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221. Regina T. Jefferson, *Rethinking the Risk of Defined Contribution Plans*, 4 FLA. TAX REV. 607, 654 (2000).

222. *Id.* at 653.

223. *See id.*

224. Several similar proposals were debated before Congress enacted the Pension Protection Act of 2006. One proposal from Senators Boxer and Corzine would have capped company stock holdings at twenty percent of an individual's 401(k) holdings; another proposal from Senator Kennedy would have given employers the option of contributing stock to 401(k) plans or offering it as an investment option to plan participants, but not both. Befort, *supra* note 1, at 979–80.

225. Peter Whoriskey, *GM Emerges from Bankruptcy After Landmark Government Bailout*, WASH. POST, July 10, 2009, at A10, available at <http://www.washingtonpost.com/wp-dyn/content/article/2009/07/10/AR2009071001473.html>.

welfare benefits funding within more stable, secure VEBA's and out of federal programs.

#### D. Control the Escalating Costs of Health Care

The United States arguably has one of the most inefficient health care systems of any industrialized country. While America has the world's highest per capita spending on health care, its system produces objective results inferior to systems that spend half as much.<sup>226</sup> As Medicare rapidly approaches insolvency, health care reform is urgently needed.<sup>227</sup> Congress is currently debating several comprehensive proposals for health care reform, but the proposals are primarily aimed at extending health insurance to the uninsured, rather than at reducing the costs of employer-provided health care.<sup>228</sup> Unless the government acts to temper the rapidly increasing costs of health care, it is unrealistic to expect employers already in difficult financial straits to generate enough resources to fulfill retirees' expectations of lifetime health care benefits.

Among the numerous proposals for health care reform are many which suggest that the United States model potential reforms on the health care systems of other countries.<sup>229</sup> Some proposals argue that there should be universal catastrophic health insurance, with noncatastrophic coverage left to the free market.<sup>230</sup> Others advocate adopting a system where the government intervenes to lower health care costs and to better spread those costs among society.<sup>231</sup> One such proposal suggests using the Dutch health care system as a model because it provides universal health care with lower per capita costs and better

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226. See Uwe E. Reinhardt, *Reforming the Health Care System: The Universal Dilemma*, 19 AM. J.L. & MED. 21, 29-30 (1993) (explaining that although the United States spends nearly twice as much of its GDP on health care as Japan and the United Kingdom, a large portion of the population remains uninsured); Press Release, World Health Organization, World Health Organization Assesses the World's Health Systems (June 21, 2000), available at <http://www.who.int/inf-pr-2000/en/pr2000-44.html> (ranking U.S. health care 37th out of 191 countries).

227. *Health Care Costs*, supra note 184, at A6.

228. Ross Douthat, Op-Ed., *The Catastrophic Option*, N.Y. TIMES, Oct. 18, 2009, <http://www.nytimes.com/2009/10/19/opinion/19douthat.html>; see Sheryl Gay Stolberg, *Missing in Health Bills: Solutions for Rising Costs*, N.Y. TIMES, Nov. 10, 2009, at A1.

229. See, e.g., Trame, supra note 187, at 472-75.

230. See, e.g., Douthat, supra note 228.

231. See Trame, supra note 187, at 460-61.



measures of success and is structured in a way that avoids many concerns commonly raised by critics of nationalized health care.<sup>232</sup>

Before the Netherlands enacted the New Health Insurance Act in January 2006, its health care system faced problems similar to those currently faced in America—rising costs and individual difficulties in securing coverage.<sup>233</sup> The reformed system requires individuals to pay annual premiums directly to insurers (the average person paid €028 in 2006) and contribute a portion of their salary (up to €2000) to a central fund, and in return the entire population receives a standard health plan, regardless of age or health.<sup>234</sup> Employers must also support the system by reimbursing the employees' salary contributions.<sup>235</sup> Additionally, insurance companies are required to offer basic coverage to any individual, regardless of age or health, and in return, the central fund compensates insurers when they accept individuals with greater health risks.<sup>236</sup> Finally, the government contributes to the plan's success by providing subsidies for those with low incomes, performing administrative functions regarding the plans, and negotiating with prescription drug makers to obtain a reduction in prices.<sup>237</sup> This system spreads the burden of caring for those with expensive medical conditions across society, which reduces health care costs for elderly retirees.<sup>238</sup> Additionally, individuals receive information about all the various insurers from the government and cannot be rejected by any of them, so insurers have an incentive to negotiate with health care providers for reduced costs.<sup>239</sup>

Regardless of the path the United States follows, it must combat the escalating costs of employer-provided health care if it expects employers to continue providing health care for their retirees. The impending insolvency of Medicare, perhaps now as early as 2016, shows that in the near future, taxpayers will bear huge burdens in providing

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232. *Id.* at 473.

233. *Id.* at 458.

234. *Id.* at 459. In 2006, the average annual premium paid was approximately \$1300.

235. *Id.*

236. *Id.* at 459–60. The companies can still set premium levels for their plans, and the entire population has the option of purchasing additional coverage. *Id.*

237. *Id.* at 460.

238. *Id.* at 461. “[F]ormal subsidies, as well as the informal subsidies of the risk equalization pool, allow senior citizens with low and fixed incomes to pay for quality coverage at lower rates.” *Id.* at 462.

239. *See id.* at 461–62.

health coverage to America's elderly.<sup>240</sup> As elderly retirees are far more likely to have expensive medical conditions than the general population, reforms that can allocate these burdens across a wider spectrum of society and provide incentives for insurers and providers to lower health care costs will be necessary so retirees and their former employers can continue to afford medical coverage.<sup>241</sup>

## V. Conclusion

It is unrealistic to expect retirees' former employers to continue providing welfare benefits when it is financially untenable for them to do so. Giving retirees effective representation in negotiations that affect their benefits and honoring their justified expectations in court could ensure that cutbacks are made only in cases of financial necessity, and encouraging the use of more stable welfare benefit funding vehicles could help insulate these benefits from economic fluctuations. Even with these reforms, the cost of retirement benefits will continue to burden employers, taxpayers will soon have to deal with huge deficits in Medicare funding, and retirees will continue to lose their employer-provided welfare benefits. Although it is too late to entirely eliminate the problems and insecurities facing the welfare benefits of current retirees, the federal government can ease the burdens on all who shoulder them by passing meaningful health care reform that transforms the system into one with manageable costs.

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240. *Health Care Costs*, *supra* note 184, at A6. This insolvency is projected to occur three years earlier than previously anticipated due to the current economic downturn. *See id.*

241. Trame, *supra* note 187, at 454.