HARSH REALITIES AND SILVER LININGS FOR RETIREES

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INTRODUCTION

When contemplating the future of labor law through the lens of bankruptcy, I cannot help but focus on the plight of the retiree. Granted, American workers today have plenty of problems of their own: stagnant wages for much of the middle class, increased outsourcing to cheaper foreign sources of labor, and a mounting pressure for greater productivity at any cost.

Yet I would contend that despite the myriad problems and stresses faced by today's American workers, the typical retiree is in an even more vulnerable position. There are several reasons why this is so. First, retirees lack the leverage that current workers have, since all of the retirees' contributions to their employer occurred in the past. At least if you are a current employee, you can use the threat of not working as a way to bargain for better terms or to try to maintain the level of benefits that you already have. Retirees, by contrast, must rely solely on promises that were made to them at a time when they had the leverage of their labor to protect their interests.

Second, many retirees are effectively prisoners of their own detrimental reliance on the promises of their employers. For these retirees, their decision about precisely when they retired was a function of the various pension and health insurance promises made to them. If after their retirement begins, the retirees' former employer reneges on these promises and makes retirement financially untenable, it is not as if the retirees' old jobs are still there waiting for them to fill.

Third, the overall aging of the American work force means that the ratio of retirees to active workers just keeps getting higher.[1] As this ratio climbs, there are relatively fewer active workers to create the profits necessary in a firm to support the firm's earlier commitments of pensions and medical benefits for an increasingly large pool of retirees. The effects of this trend are only magnified further by the general decline in union membership, thereby reducing the economic leverage of organized labor in the negotiation process.

Finally, I see the position of retirees as uniquely vulnerable in the years to come because they typically have no vote in labor contracts that often adversely affect

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1 *See* UAW v. Gen. Motors Corp., 497 F.3d 615, 621 (6th Cir. 2007) (noting "growing ratio of retirees to active employees (four to one at GM in 2006 and two to one at Ford in 2005) . . . ."); Kimberly Blanton, *Facing a Fund Gap—Lucent Seeking to Shift Part of Soaring Health Costs of Retirees*, BOSTON GLOBE, Oct. 20, 2004, at C1 ("Lucent Technologies' population of retired workers has grown so large over the years, there are four retirees for every active employee on its payroll."); *cf.* Justin Fox, *Good Riddance to Corp's Pension: The Real Shame is that Workers Put Such Faith in Unstable System*, CHI. SUN TIMES, Jan. 16, 2006 (noting that "[w]hen succeeding generations are bigger and wealthier than the ones whose retirements they must help fund . . . [there] isn't much of a problem. But [this is] no longer the case at GM.").

their interests. In recent years, the most pressing issue in many important labor agreements has been how to control the legacy costs associated with various retiree benefits.

As I look to the future of labor law, I see trouble on the horizon for retirees – or, perhaps more accurately, I see *more* trouble for retirees, since the past decade or so has not exactly been a bed of roses for retirees in this country.[2] As my title would suggest, I anticipate some hard times in the coming years for retirees. My predicted "harsh realities" fall into three general categories.

First, I believe that the defined-benefit pension crisis is far from over, despite the enactment by Congress in 2006 of the most sweeping pension reform bill since ERISA. Courts continue to allow pension plan terminations, typically as part of a business reorganization strategy, and the affected retirees are left to collect the often-reduced pension benefits that the federal pension insurance program provides. As for the new pension reform bill, probably its chief impact will be to accelerate the already growing trend of employers to move from defined-benefit plans to defined-contribution plans.

The second harsh reality for retirees of the future is that the status of retiree medical benefits is shakier than ever these days. Despite a special section of the Bankruptcy Code intended to help protect those benefits,[3] and despite an amendment to that Bankruptcy Code section as part of the 2005 bankruptcy reform bill,[4] retirees continue to lose promised medical benefits in many chapter 11 cases.[5] Indeed, some large companies today have been able to negotiate significant reductions in retiree medical benefits without filing bankruptcy at all.[6] What was once an open-ended promise by the employer to provide health benefits for life is now being transformed in many instances to a set payment by the employer to a trust fund which retirees must rely on to fund their health benefits. In short, the risk of future health-care cost increases is being shifted from the employer to its retirees.

The third harsh reality I see for retirees is that as the overall labor pie gets smaller, retirees can no longer count on their active union brethren to protect the

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[2] *See generally* Daniel Keating, *Why the Bankruptcy Reform Act Left Labor Legacy Costs Alone*, 71 MO. L. REV. 985 (2006) (describing difficulties faced by retirees during past several years); c*f.* Marilyn Geewax, *Airline Pension Help in Bill; House, Senate Continue Negotiations*, ATLANTA J.-CONST., June 17, 2006, at 1F (observing trend of major airlines terminating "pension plans while under the protection of bankruptcy laws"); Blanton, *supra* note 1, at C1 ("Corporations nationwide are trimming or eliminating retiree benefits.").

[3] 11 U.S.C. § 1114 (2006) (outlining special protections in chapter 11 cases for retiree medical benefits).

[4] 11 U.S.C. § 1114(l) (providing retiree medical benefits modified within 180 days before a company files bankruptcy be reinstated unless the equities clearly favor modification).

[5] *See* United Steelworkers of Am. v. Ormet Corp. (*In re* Ormet), 355 B.R. 37, 39 (S.D. Ohio 2006) (allowing retiree medical benefits to be modified post-confirmation); Pension Guar. Benefit Corp. v. Falcon Prods., Inc. (*In re* Falcon Prods., Inc.), 497 F.3d 838, 842–43 (8th Cir. 2006) (affirming bankruptcy court's approval of chapter 11 debtor's proposed termination of pension plans); Blanton, *supra* note 1, at C1 (observing that "[a]fter declaring bankruptcy, Bethlehem Steel ended retiree health benefits altogether.").

[6] *See, e.g.*, UAW v. Gen. Motors Corp., 497 F.3d 615, 636–37 (6th Cir. 2007) (upholding retiree medical benefits reduction outside of bankruptcy); Maurer v. Joy Techs., Inc. 212 F.3d 907, 919 (6th Cir. 2000) (approving modification of retiree medical benefits).

retirees' interest. This is not to suggest that union workers have completely abandoned the concerns of those who came before them. Rather, I believe that there will simply be more cases in which retirees will be disappointed at the representation given to them by the active union workers. In a number of recent cases, groups of retirees have either sued or are planning to sue their union for its failure to adequately represent their interests.[7]

In the face of all these harsh realities, is there any hope for good news regarding the plight of the retiree in the future? I believe that there are indeed some silver linings for future retirees in this fast-approaching new world of labor. For one thing, most retirees in the future will not need to rely on the solvency of their former employer in order for their retirement promises to be kept. Instead, the retirees will be able to look to separate funds that will not be available to other creditors of their employer, such as 401(k) plans for pensions and Voluntary Employee Benefit Associations (VEBAs) for medical benefits. Furthermore, as a result of the separate-fund nature of future retiree benefits, retirees will be able to plan for their retirements with a lot more certainty about exactly what will be there for them when they stop working. For the retiree of the future, the promises of retirement benefits won't be nearly as grandiose as they once were, but neither will there be as many sad tales of bait-and-switch that are so common for today's retirees.

The balance of this essay proceeds in four parts. Part I considers the continuing pension crisis and summarizes the impact of the Pension Protection Act of 2006. Part II discusses the ways in which retiree health benefits remain susceptible to reduction or termination. Part III explores the increasing instances of conflicts between retirees and the unions who represent them. Part IV concludes with some thoughts on the potential positive effects of the shift under way in the realm of retirement benefits.

I. THE FUTURE OF PENSIONS

It has been clear for a fairly long time now that defined-benefit pension plans are on their way out, and that eventually defined-contribution plans will be the only private employer-sponsored pension plans that workers can look to in order to supplement their social security checks.[8] At some level this is bad news for

[7] *See, e.g.*, Nelson v. Stewart, 422 F.3d 463, 465, 474–75 (7th Cir. 2005) (upholding retirees' right to sue union for state-law causes of action following union's agreement with chapter 11 debtor to reduce retiree medical benefits); Mansfield v. Air Line Pilots Ass'n Int'l, No. 06 C 6869, 2007 U.S. Dist. LEXIS 73515, at *11–12 (N.D. Ill. Oct. 1, 2007) (denying union's motion to exclude retirees from class as those retirees were presumably owed a duty of representation); Baker v. Bd. of Educ., 770 N.Y.S.2d 782, 785–86 (N.Y. App. Div. 2004) (stating that while unions do not generally have a duty to represent former members, the defendant union "had a continuing duty to represent [plaintiff retirees] in negotiations . . . .").

[8] Christopher E. Condeluci, *The New Single-Employer Defined Benefit Plan Funding Rules: What's in Store for Defined Benefit Plan Sponsors and Participants?*, 48 TAX MGM'T MEMORANDUM 59, 59 (2007) (noting that from 1974 until today, percentage of private-sector employees covered by defined-benefit plans has decreased from 44% to 17%); C. Scott Pryor, *"May it Please the Court": If I had Been at Oral Argument*

workers, since the beauty of the defined-benefit plan is that in theory it gives retirees more certainty and security about their retirement income than the defined-contribution alternative.[9] It also puts the risk of figuring out how to fund the retiree's pension at predetermined levels squarely on the shoulders of the employer. The defined-contribution plan, by contrast, puts the risk of generating an adequate annual return with the employee, not the employer. The defined-contribution plan is not a promise, but a pot of money, and it is up to the employee to manage that pot of money upon retirement in a way that ensures sufficient annual income for life.[10]

Despite the clear trend away from defined-benefit pension plans, those plans are still very much a part of our current labor landscape. We are now in the midst of a painful transition period, and the legacy of defined-benefit pension promises continues to haunt some of this nation's largest industries, such as steel, coal, airline and automobile manufacturing. A number of companies that have traditionally offered such plans are freezing benefit levels and substituting defined-contribution plan features for what would otherwise have been increases in promised benefit levels under the old-style plans.[11]

Courts, for their part, have not hesitated to allow plan terminations in cases

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in Rousey v. Jacoway Part II, 24 AM. BANKR. INST. J. 18, 18 (March 2005) ("Defined-benefit plans are the traditional sort of pension plans, but defined-contribution plans (frequently profit-sharing plans) have become more common . . . ."); Robert M. Sade, *Complementary and Alternative Medicine: Foundations, Ethics, and Law*, 31 J.L. MED. & ETHICS 183, 187 (2003) ("Funding of employees' health insurance by employers is shifting from defined benefits to defined contributions.").

[9] *See* Michael J. Borden, *PSLRA, SLUSA, and Variable Annuities: Overlooked Side Effects of a Potent Legislative Medicine*, 55 MERCER L. REV. 681, 709 (2004) (pointing out that "[i]n a defined benefit plan, the employee is assured of a certain benefit upon retirement," whereas same is not true of defined contribution plans); Daniel Keating, *Chapter 11's New Ten-Ton Monster: The PBGC and Bankruptcy*, 77 MINN. L. REV. 803, 805–06 (1993) (describing differences between defined benefit and defined contribution pension plans); Pryor, *supra* note 8, at 18 (noting "[p]ension plans come in two basic types: defined-benefit plans and defined-contribution (also known as individual account) plans" and describing their differences).

[10] Borden, *supra* note 9, at 709.

> The alternative to a defined benefit plan is a defined contribution pension plan, in which the employer contributes to the employee's account via a payroll deduction. The employer maintains control of the aggregated funds invested by all of its plan participants but must provide a range of investment options for each employee . . . . The employer administers the account, but the employee owns it and carries it with him as he moves from job to job or stops working. Ultimately the employee must be responsible for making decisions about how to invest the funds in a defined contribution plan, and employees often do so on their own without the guidance of a plan administrator.

Id.

[11] Condeluci, *supra* note 8, at 59 (noting survey of chief investment officers which indicated plans by companies to freeze some or all benefits under defined-benefit plans and to start defined-contribution plans in place of those foregone benefit increases). *See generally* Borden, *supra* note 9, at 710, 713 (outlining factors that have "contributed to the shift away from defined benefit to defined contribution plans"); Allen Michel & Israel Shaked, *Fiduciary Responsibility in the Case of Defined Contribution Plans*, 23 AM. BANKR. INST. J. 46, 46 (December 2005) ("Firms have been increasingly switching their retirement plans offered to employees from defined benefit plans to defined contribution plans.").

where the court believes that termination of the plan is necessary to allow the debtor-company to reorganize successfully. In the chapter 11 case of *In re Kaiser Aluminum Corp.*,[12] the debtor sought to terminate all six of its pension plans under ERISA's reorganization test.[13] That test requires a debtor to show that without the requested plan termination, the company could not reorganize.[14]

The PBGC argued that the appropriate question was not whether the debtor could continue to fund all six of its plans and still reorganize; rather, the PBGC contended that ERISA required a plan-by-plan approach to termination instead of necessarily considering all of the plans in the aggregate.[15] The Third Circuit disagreed with the PBGC, and said that the plan-by-plan approach that the federal pension insurance agency advocated would be unworkable.[16] The court noted that ERISA provides no guidance whatsoever on how a court would apply such a test, including, for example, in what order the plans would need to be terminated.[17]

The Third Circuit also said that the PBGC's suggested approach would be unfair to workers. The court pointed out that the PBGC's approach could mean that some workers in the same union would get full pension benefits while others in their union would get the reduced PBGC-guaranteed benefits.[18] In a case heard shortly after *Kaiser*, the Eighth Circuit agreed with the Third Circuit on this issue and affirmed the decision of the Bankruptcy Court for the Eastern District of Missouri that allowed plan termination using an aggregate test.[19]

Probably the most noteworthy plan termination over the last couple of years was allowed by the bankruptcy court for the Northern District of Illinois in the *United Airlines* case[20], where the debtor-airline was able to dump a defined-benefit plan onto the PBGC that was underfunded by $6.6 billion.[21] The bankruptcy judge in the *United* case certainly understood the magnitude of what he was allowing, but as he noted, the very nature of bankruptcy is often to present a series of unattractive

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[12] 456 F.3d 328 (3d Cir. 2006).

[13] *Id.* at 330.

[14] *See* 29 U.S.C. § 1341(c)(2)(B)(ii) (2006) ("The requirements of this clause are met by a person if— . . . (IV) the bankruptcy court . . . determines that, unless the plan is terminated, such person will be unable . . . to continue in business outside the chapter 11 reorganization process"); *Kaiser Aluminum Corp.*, 456 F.3d at 335 ("The reorganization test is satisfied when a bankruptcy court determines that a plan sponsor will be unable to continue business outside of Chapter 11 'unless the *plan* is terminated.'") (citation omitted) (emphasis in original); Pension Guar. Benefit Corp. v. Falcon Prods., Inc. (*In re* Falcon Prods., Inc.), 354 B.R. 889, 893 (E.D. Mo. 2006), *aff'd*, 497 F.3d 838 (8th Cir. 2006) (describing reorganization test by quoting language of § 1341(c)(2)(B)(ii)(IV)).

[15] *In re Kaiser Aluminum Corp.*, 456 F.3d at 332–33.

[16] *Id.* at 337.

[17] *Id.*

[18] *Id.* at 341.

[19] *See In re* Falcon Prods., 497 F.3d at 841–42.

[20] *In re* U.A.L. Corp., No. 02 B 48191, 2005 WL 2840266, at *5 (Bankr. N.D. Ill. Oct. 25, 2005) (terminating Pilot Plan pursuant to motion by PBGC based on "unreasonable increase in the liability of [PBGC's] fund" if plan continued).

[21] Mary Wisniewski, *Judge Allows United to Drop Pension Plan; Calls it "Least Bad of a Number of Unfortunate Choices"*, CHI. SUN-TIMES, May 11, 2005 at 77 (stating Pension Benefit Guaranty Corp. is taking over $6.6 billion in funding for United workers' pension plans).

alternatives: "Bankruptcy generally involves choosing the least bad of a number of unfortunate choices. The least bad choice keeps the airline functioning, keeps people employed, and is an alternative to the worst choice, which is a shutdown of the company."[22]

One might think that in a world with federal pension insurance, retirees would be more or less indifferent to terminations of defined-benefit plans. After all, that's what the insurance is there for, right? Unfortunately, the reality of pension-insurance is more nuanced and ultimately a lot more modest than the ideal. There are a number of exceptions to the PBGC's insurance coverage, including an overall monthly cap on payments, as well as a failure to cover certain kinds of pension benefits, such as early-retirement incentives.[23] In any event, the bitterness expressed by the United retirees in the wake of the court's termination ruling in that case left little doubt that the affected retirees had become well aware of the many holes in the PBGC's insurance coverage.[24]

The Pension Protection Act of 2006[25] (PPA) tried to effect a number of changes to shore up the nation's pension system, and one of its main goals was to improve the solvency of both the PBGC and the many defined-benefit plans that this federal corporation insures.[26] There are a whole host of problems with the PPA, and I outline some of them below. In fairness to the drafters of the PPA, I do want to emphasize at the outset that they were truly faced with an impossible task. By the time of this legislation, the damage to the nation's defined-benefit pension system had already been done by decades of statutory loopholes and shoddy enforcement that had left many plans significantly, yet legally, underfunded.

Certainly the greatest tension faced by the PPA drafters was this: On the one hand, pension laws needed to get tougher on employer funding rules and needed to insist that plan underfunding no longer be tolerated. On the other hand, if the new law got too tough too quickly, the net result would simply be additional terminations of pension plans that were already woefully underfunded. When you

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[22] *Id.*

[23] *See* Keating, *supra* note 2, at 989–90 (noting limits of PBGC coverage).

[24] *See U.A.L. Corp.*, 2005 WL 2840266, at *1 (terminating Pilot Plan pursuant to motion by PBGC based on "unreasonable increase in the liability of [PBGC's] fund" if plan continued); Michelle Maynard, *The Basics: If an Airline Fails, Who Would Care?*, N.Y. TIMES, May 15, 2005, at 42 (stating workers suffer from United Airlines failure); Wisniewski, *supra* note 21, at 77 (describing a flight attendant with 27 years' experience who bemoaned PBGC takeover of pensions and claimed she will lose almost half her pension benefits as result of takeover).

[25] Pub. L. No. 109-280, 120 Stat. 780 (2006) (demonstrating how scattered sections of 26 U.S.C. and 29 U.S.C. were amended and later codified).

[26] *See* Adam E. Cearley, *The PBGC: Why the Retiree's Traditional Life Raft is Sinking and How to Bail It Out*, 23 EMORY BANKR. DEV. J. 181, 187 (2006) (stating Pension Protection Act of 2006 addressed problem of underfunded pension plans in large corporations); Condeluci, *supra* note 8 (noting enactment of PPA was motivated by concerns that plan underfunding and resulting plan terminations were pushing PBGC to brink of insolvency); A GUIDE TO UNDERSTANDING THE PENSION BENEFIT GUARANTY CORPORATION, CONG. BUDGET OFFICE, at 1 (2005), *available at* http:// www.cbo.gov/ftpdocs/66xx/doc6657/09-23-GuideToPBGC.pdf ("The recent spate of corporate bankruptcies has caused workers to shoulder many of the burdens of corporate mismanagement [and] ineffective government regulation . . . one of the few silver linings for workers . . . [is] the Pension Benefit Guaranty Corporation.").

inherit a system that already includes a number of underfunded plans, you discover that the plans which are most underfunded are those sponsored by companies that are least in a position to rectify that. Typically, it is the plan sponsor's poor cash flow that caused the plan to become so underfunded in the first place.

There is no question that the PBGC's overall deficit of roughly $23 billion was a major impetus for the passage of the PPA, and therefore a chief focus of the bill was how to strengthen what had obviously been ineffective pension-funding rules. Nevertheless, many members of the business community complained that the defined-benefit plan underfunding problems were partly due to a statutory discount rate for valuing plan liabilities that was artificially low. This, they said, created a future-liability figure for the plans that was artificially high, thereby overstating the extent of plan underfunding in many cases.[27]

Another complaint from the business community about the pre-PPA funding rules was that the employer's contribution obligations varied too much from year to year based on swings in interest rates.[28] As a result, there were some years when the employer would be required to contribute a lot to their plans, and other years in which the employer would not be allowed to contribute at all to their plans. Unfortunately, the PPA did not fix the contribution volatility problem, although it does force certain underfunded plans to reduce benefits and benefit options for participants.[29]

The gist of the new funding requirements under the PPA is that an employer's annual contribution to a defined-benefit pension plan must equal 100% of new obligations for that year.[30] As for plan underfunding already in place from past years, the PPA allows a seven-year amortization period in which the employer can pay that back.[31] The seven-year amortization period for past underfunding is a good example of the delicate balancing act faced by the PPA drafters. That period is generally shorter than previous amortization periods for correcting underfunding,

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[27] *See* Norman Stein, *Far-Reaching Changes are Bundled into the Pension Protection Act*, 78 PRAC. TAX STRATEGIES 281, 282 (2007) (describing problem of statutory discount rate).

[28] *See* Debra L. Raskin, *Recent Legislative Developments in Employment Law*, in 36th Annual Institute on Employment Law, at 65, 68–69 (Practicing Law Institute, Litig. & Admin. Prac. Course Handbook, PLI ORDER NO. 11091, October 2007) (discussing how Pension Protection Act was enacted to cure inadequacies of pre-PPA funding rules). *See generally* Cearley, *supra* note 26, at 183–84 (discussing PBGC's overall deficit).

[29] *See* Harold J. Ashner, *Update on PBGC Legislative and Regulatory Activity*, ALI-ABA COURSE OF STUDY, at 1759 (March 2006) (discussing how PPA amendments set out criteria that must be met before an underfunded plan could be voluntarily terminated); Raskin, *supra* note 28, at 68–69 (stating PPA makes it more difficult for employers to underfund plans); Stein, *supra* note 27 (noting that net result of these deficiencies in PPA may push more employers toward defined-contribution plans).

[30] *See* Pension Protection Act of 2006, Pub. L. No. 109-280, § 112(a) (providing funding rules for single-employer defined benefit pension plans); I.R.C. § 412(b)(2)(A) (2006) (providing text for liability for contribution section of I.R.C.); I.R.C. § 430(a)(1)(A) (2006) (requiring annual contributions to underfunded plans equal portion of liabilities attributable to current year).

[31] *See* Pension Protection Act of 2006 § 112(a) (providing funding rules for single-employer defined benefit pension plans); I.R.C. § 430(c)(2) (2006) (stating seven-year amortization period); Nell Hennessey, *Bankruptcy-Related Provisions of the Pension Protection Act of 2006*, 25 AM. BANKR. INST. J. 10, 64 (November 2006) (discussing seven-year amortization period).

which could be as long as 30 years.[32] But the PPA still allows the underfunding to exist for seven years rather than requiring employers to rectify it immediately. Given that the underfunding in most cases took years to accumulate, it probably would have been folly for Congress to think that such underfunding could be immediately corrected without precipitating a number of corporate bankruptcies and plan terminations.

Perhaps the thorniest problem that the PPA had to face was the airline industry. At the very same time that the PPA was being drafted in an attempt to stave off the insolvency of the PBGC, airline executives were lobbying Congress for relief from their obligation to repay underfunding under existing pension law. The PPA compromise for airlines is that they are given an additional three years beyond the standard seven years to amortize their past underfunding.[33] Alternatively, the PPA allows an airline to amortize a funding shortfall over 17 years, but only if benefit levels are frozen and certain benefits are eliminated altogether.[34]

The PPA contains other provisions on funding that make for a paradoxical mix of full-funding acceleration provisions on the one hand, and full-funding waivers or exceptions on the other hand. On the full-funding side, "at risk" plans (those funded at a level of 80% or less) have a faster-than-normal schedule of minimum required contributions.[35] The hope is that the plan will thereby transition out of its at-risk position sooner than the typical amortization of plan funding shortfalls would dictate. On the waiver side, the IRS can still grant waivers of the minimum required funding contributions to companies that cannot afford to pay them.[36]

Recognizing the reality that many of the new stricter funding rules would drive some employers away from defined-benefit plans, the drafters of the PPA also included provisions that would make it easier for employers to encourage their workers to participate in defined-contribution plans.[37] The PPA preempts any state law that would otherwise make illegal (under local payroll withholding laws, for example) an automatic enrollment feature of an employer-sponsored 401(k) plan.[38] Thus, an employer could create a default rule under which an employee's pay is

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[32] *See* Hennessey, *supra* note 31 (discussing amortization period). *Compare* I.R.C. § 412(b)(2)(B) (2006) (requiring amortization periods of between five and 30 years under pre-PPA law) *with* I.R.C. § 430(c)(2) (stating seven-year amortization period).

[33] *See* Pension Protection Act of 2006 § 402 (describing special rules for airlines).

[34] *Id.*

[35] *See* Pension Protection Act of 2006 § 112(a) (describing for significantly underfunded plans).

[36] *See* I.R.C. § 412(d)(1) (2006) (stating IRS waiver procedures and requirements).

[37] *See* Pension Protection Act of 2006 § 902 (describing special incentives for defined-contribution plans); *see also* 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, 977–78 (2007) (noting Pension Protection Act of 2006 removes potential obstacles to default enrollment of employees in defined contribution plans); Susan J. Stabile, *Is It Time to Admit the Failure of an Employer-Based Pension System?*, 11 LEWIS & CLARK L. REV. 305, 317–18 (2007) (noting study showing automatic enrollment increases 401(k) participation by new hires and Pension Protection Act of 2006 encourages adoption of automatic enrollment of plan participants).

[38] *See* Pension Protection Act of 2006 § 902(f)(1) ("Notwithstanding any other provision of this section, this title shall supersede any law of a State which would directly or indirectly prohibit or restrict the inclusion in any plan of an automatic contribution arrangement.").

automatically taken out and put into a 401(k) plan unless and until the employee specifically opts out of the plan.

From 1974 until today, the percentage of private-sector employees covered by defined-benefit pension plans has decreased from 44% to 17%.[39] Many commentators believe that the PPA will simply accelerate the trend away from defined-benefit pension plans.[40] In a survey of chief investment officers of many of the nation's largest corporate pension plans, 60% said that the PPA would cause them to freeze some or all benefits under their defined-benefit plan and to substitute defined-contribution plans going forward.[41] Some experts predict that the only defined-benefit plans remaining over the next decade will be public-sector defined-benefit plans.[42]

The shift from defined-benefit to defined-contribution plans as the primary source of a retiree's social security supplement raises a host of concerns. As noted above, the key difference between the two types of plans is which party, the employer or employee, bears the risk of ensuring that there is enough money to fund the retiree's living expenses for the duration of retirement. Historically, employees have not been known to participate fully in 401(k) plans or to contribute adequately to such plans even if they do participate.[43]

Employees are also not known to be the wisest investors of the money that is in

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[39] Condeluci, *supra* note 8, at 59 (citing statistics on decline of defined-benefit programs). *See generally* Befort, *supra* note 37, at 948 (discussing decline in defined benefit pension plans); Stabile, *supra* note 37, at 307–08 ("The number of defined benefit plans declined substantially between 1985 and 2004, from 114,000 in 1985 to 31,200 in 2004, and the number of employees covered by defined benefit plans fell from 30.1 million in 1980 to 22.2 million in 2000.").

[40] *See, e.g.*, Stein, *supra* note 27, at 290–291 (calling new funding rules "death spiral for large defined benefit plans"); *see also* Befort, *supra* note 37, at 975–76 (expressing concern over Pension Protection Act's combination of more rigorous defined benefit funding rules along with loosened cash balance conversion standards hastening demise of traditional defined benefit plans); Condeluci, *supra* note 8 at 59 (noting "shift away from defined benefit plans").

[41] Cearley, *supra* note 26, at 211 ("[The Pension Protection Act of 2006] could have the consequence of forcing companies to freeze their plans or to get out of the defined benefit system altogether."); Condeluci, *supra* note 8, at 68 (reporting results of survey); *see also* Befort, *supra* note 37, at 976 (opining changes made by Pension Protection Act will act as incentives for still more employers to terminate or freeze defined benefit plans).

[42] *See* Stein, *supra* note 22, at 291 (predicting that public-sector defined-benefit programs will be last ones to fall, but "fall they eventually will"); *see also* 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, 283 (2007) ("[C]ertainly with the defined contribution/individual account model increasingly entrenched in the private sector, support for the defined benefit structural model in the public sector can also be expected to decline."); Karen Eilers Lahey & T. Leigh Anenson, *Public Pension Liability: Why Reform Is Necessary to Save the Retirement of State Employees*, 21 NOTRE DAME J.L. ETHICS & PUB. POL'Y 307, 332 (2007) (noting nine out of ten largest pension funds in United States are public pensions).

[43] *See* Stabile, *supra* note 37, at 311 (stating upwards of one quarter of eligible employees do not participate in 401(k) plan and "[m]ost workers who do participate in 401(k) plans fail to contribute enough to accumulate sufficient retirement savings."); *see also* Karen C. Burke & Grayson M.P. McCouch, *Social Security Reform: Lessons from Private Pensions*, 92 CORNELL L. REV. 297, 308 (2007) ("Given the option to participate in a 401(k) plan, more than a quarter of all eligible employees do not do so at all, and less than 10% of participants contribute the maximum allowable amount."). *See generally* Dorothy A. Brown, *Pensions and Risk Aversion: The Influence of Race, Ethnicity and Class on Investor Behavior*, 11 LEWIS & CLARK L. REV. 385, 390 (2007) (describing empirical data on low participation rates).

their accounts. Too many employees fail to diversify their holdings adequately, oftentimes holding too much stock in their own employer.[44] Some employees are too conservative in their investment strategy, especially considering that the money is going to be in the account for a long period of time.[45] In short, the benefit of employee autonomy with defined-contribution plans can also be the biggest drawback of that type of pension.

II. RETIREE MEDICAL BENEFITS: SHAKIER THAN EVER

As poorly designed as the defined-benefit pension insurance program has proven to be, it nevertheless sparkles in comparison to the protections available to retirees for their employer-promised medical benefits. The only vesting rules that exist with retiree medical benefits are the common-law rules of vesting, which are subject to a lot of uncertainty and are sometimes a function of the jurisdiction where the promises were made.[46] But even if you can get beyond the vesting hurdle, the central problem with retiree medical benefits is that the employer has no obligation to pre-fund them. Ultimately, then, because the obligation is not funded until it comes due, the promise ends up being only as strong as the company that makes it.

Until the Financial Accounting Standards Board (FASB) tightened up its accounting rules with respect to retiree medical benefits several years ago, things were even worse. Companies could make grandiose promises about retiree medical benefits and take steps to cause them to vest without putting a penny aside for the future liability and without needing to reveal that hidden but real liability on its balance sheet. The lack of a pre-funding requirement still has not changed, but thanks to FASB amendments, at least businesses now must show these liabilities on their books.[47]

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[44] *See* Brown, *supra* note 43, at 392 (noting lower-income employees are particularly likely to over-invest in employer stock); *see also* Burke, *supra* note 43, at 308 (stating many employees make missteps with 401(k) plans including investing substantial portion of accounts in employer stock when allowed to do so); Stabile, *supra* note 37, at 319 (stating many 401(k) plan participants continue to remain heavily invested in employer stock).

[45] *See* Brown, *supra* note 43, at 392 (describing how employees "over-invest in conservative fixed-income options"); *see also* Burke, *supra* note 43, at 308 ("Many employees are prone to inertia and procrastination; to avoid the laborious process of comparing alternative options and making affirmative choices, they simply follow default rules."); Stabile, *supra* note 37, at 315 (noting women especially tend to invest assets more conservatively leading to lower plan accumulations).

[46] *See* Keating, *supra* note 2, at 987–88 ("While ERISA's disclosure provisions apply to retiree health benefits, its mandatory vesting and pre-funding requirements do not."); Helen M. Kemp, *The Employer Giveth and Taketh Away*, 34 THE BRIEF 16, 18 (American Bar Association, Tort Trial & Ins. Practice Section, Spring 2005) (stating retiree health insurance benefit plans are not subject to mandatory vesting under ERISA and generally are not vested); *see also* 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, 1228 (2001) ("ERISA, however, neither mandates that welfare benefits vest, nor expressly prohibits the vesting of welfare benefits or authorizes unilateral termination of welfare benefits.").

[47] *See* Len Boselovic, *Accounting Rule Shift on Pensions Could Accelerate Huge Revisions*, PITTSBURGH POST-GAZETTE, Apr. 23, 2006, at D1 (reporting planned FASB regulations would require companies to reflect funded status of pension plans on balance sheets); Adam Geller, *New Accounting Rules Could Retire*

Just like with defined-benefit pension plans, the problem with retiree medical benefits in our transitional period we face today is not so much that employers are promising more of them. Rather, it's that employers have realized that there is no feasible way to honor the promises that they made some time ago. Having accepted that reality, employers then must face the challenge of how to give their retirees some type of coverage in this arena that still enables the employer to survive as an ongoing entity.

Section 1114 of the Bankruptcy Code, which is now about 20 years old, was better than nothing at helping retirees protect their benefits, but not a whole lot better.[48] Most fundamentally, section 1114 is flawed in that it does nothing to address the lack of a pre-funding requirement. Given that it is part of the Bankruptcy Code, section 1114 is really not suited to address the nonbankruptcy problem of a failure to require pre-funding.

Congress made one small change to try to strengthen the protections of section 1114 of the Bankruptcy Code as part of the recently enacted bankruptcy reform bill.[49] Newly enacted section 1114(l) says that if a debtor causes a pre-bankruptcy modification of retiree benefits within 180 days before filing bankruptcy and at a time when the debtor is insolvent, the court shall reinstate those benefits at their pre-modification level "unless the court finds that the balance of the equities clearly favors such modification."[50] The aim here was to make sure that a company which knew that it was headed for chapter 11 could not circumvents the retiree protections of section 1114 simply by effecting the reduction in benefits immediately prior to filing its bankruptcy.[51] Of course, this new provision would do nothing to help retirees post-confirmation in a case where the original retiree benefit promise included a right by the employer to terminate the benefits at any time.

Congress' basic message in section 1114 is that companies in chapter 11 should continue to give retirees as much of their promised health benefits as is possible while still reorganizing the company.[52] But therein lies the rub. When retirement

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Pensions, ST. LOUIS POST-DISPATCH, Jan. 17, 2006, at B1 (describing impact of change in FASB standards); Ellen Simon, *Pension Crisis Is Double Trouble: Besides Underfunding, Firms Face Specter of Accounting Changes*, CHARLOTTE OBSERVER, Jan. 7, 2006, at 1D (observing FASB will require companies to add net pension and retiree health care costs to balance sheets).

[48] *See* 11 U.S.C. § 1114 (2006); Steven L. Willborn, *Workers in Troubled Firms: When Are (Should) They Be Protected?*, 7 U. PA. J. LAB. & EMP. L. 35, 52 (2004) ("Section 1114 provides special, heightened protections for the health insurance benefits of retirees.").

[49] *See* Keating, *supra* note 2, at 991 (observing under new section 1114(l) court shall reinstate retiree benefits if modified prior to petition while company was insolvent).

[50] 11 U.S.C. § 1114(l).

[51] *See* Keating, *supra* note 2, at 991 ("Presumably, this new provision was inserted in anticipation of a contingency in which a corporate employer contemplating bankruptcy modifies retiree benefits on the ever of bankruptcy to avoid the special protections given to those benefits after the employer files Chapter 11.").

[52] *See* 11 U.S.C. § 1114(l); Richard Levin & Alesia Ranney-Marinelli, *The Creeping Repeal of Chapter 11: The Significant Business Provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 603, 611 (2005) ("Thus, in addition to potentially increasing a debtor's retiree benefit burden by authorizing the rescission of lawful modifications made within 180 days of the petition date, BAPCPA could well be found to abrogate a debtor-in-possession's right to reduce such benefits postpetition based upon a unilateral modification clause.").

health-benefit obligations run in the millions or even billions of dollars, how is a struggling company supposed to devise a plan of reorganization that gets the support of other creditors while still paying any significant portion of its retiree medical benefits?

Not surprisingly, then, despite the existence of section 1114 of the Bankruptcy Code, retirees have continued to see their medical benefits reduced or lost altogether during the last several years. Between 1998 and 2003, about 250,000 union steelworker retirees lost their medical benefits due to steel industry bankruptcies.[53] Those retirees either had to buy replacement medical coverage on the open market, or to pay for their retiree medical benefits under COBRA if their company was still in operation. Many of these retirees have struggled to buy health benefits on the open market because of pre-existing conditions that might not even be covered if they had to buy their own policies.

In the Delta Airlines bankruptcy, Delta and its retirees reached an agreement during the airline's chapter 11 case in which Delta retirees would for the first time have to pay some portion of their retiree medical benefits.[54] Even municipal retirees may soon see their health benefits reduced. A relatively new Governmental Accounting Standards Board Statement, No. 45, requires cities, counties, public utilities, school districts, and public colleges and universities to disclose the extent of the their retiree medical benefit obligations.[55] These newly disclosed liabilities could have the effect of hurting these public employers' bond ratings and thereby making it more expensive for them to borrow. That, in turn, might cause the public employers to think long and hard before offering or enhancing such benefits in the future.

Probably one of the ugliest and most high-profile cases in the last few years

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[53] *See* Pamela A. MacLean, *Promises To Retirees Depend on What 'Lifetime' Means*, THE CONN. L. TRIB., Aug. 2007, at S10 (quoting steelworker union official stating 250,000 retirees and spouses lost benefits during chapter 11 bankruptcies); Kimberly Peterson, *Unions resisting Dana's cuts; Retiree health benefits, worker wages in judge's hands*, THE FORT WAYNE J. GAZETTE, Apr. 30, 2007, at 1C (citing statistics on lost retiree benefits). *See generally* Peter Krouse, *Bearing the Burden of Yesterday's Promises Legacy Costs of Pensions, Health Care Leave LTV in a Bind*, CLEVELAND PLAIN DEALER, Sept. 9, 2001, at G1 (discussing history of large integrated mills creating legacy of retirees for steel mills).

[54] *See* Harry R. Weber, *Delta, Retirees Reach a Deal*, CINCINNATI POST, Oct. 6, 2006, at A17 (reporting conclusion of deal to change medical benefits for Delta employees and retirees); *Delta Reaches Deal on Retiree Health-Care Benefits*, CFO.com, October 6, 2006, http://www.cfo.com/article.cfm/8017758 (describing Delta's modification of retiree medical benefits, which will save Delta $50 million annually); *see also* Corey Dade, *Buckle Up Possible Turbulence*, CINCINNATI POST, Oct. 10, 2007, at A (mentioning retiring Delta chief executive negotiated reduction in health benefits with employees to cut costs during bankruptcy).

[55] *See* Dean Gloster, *Seasons of Change*, AMERICAN CITY & COUNTY, Nov. 1, 2006, at 2B (noting effects of new municipal accounting standards); Ronald Kramer & Mark Casciari, *Governmental Accounting Standards Board (GASB) Statement No. 45 Makes Public Employers Revisit Retiree Health Insurance*, 37 URB. LAW. 427, 429–30 (2005) (outlining requirements of GASB Statement No. 45); Bruce Murphy, *Devastating Health Costs Loom for Milwaukee*, MILWAUKEE J. SENTINEL, Nov. 18, 2003 ("By 2007, the Governmental Accounting Standards Board, which issues guidelines for state and local governments, is expected to begin requiring governments to account for the expense of retiree health insurance just as it does for pensions.").

involving the loss of retiree benefits was the case involving Horizon Natural Resources Company.[56] What made the *Horizon* case so noteworthy is that it demonstrated that even in the absence of a piecemeal liquidation of a company's assets, retirees could nevertheless lose all of their promised and vested retiree benefits.[57]

In *Horizon*, the ten debtors in bankruptcy, all unionized coal companies, had successorship clauses in their collective bargaining agreements.[58] Under these clauses, the debtors were not supposed to sell their operation without getting the new owners to agree to assume the old employer's obligations under the collective bargaining agreement.[59] The idea here was that all of the various obligations to current union workers and retirees would have to "run with the company," as it were. About 800 of the 2,500 total debtor employees were union-represented.[60]

The debtors filed chapter 11 with the thought of reorganizing, but ultimately they reached a point where they decided to simply liquidate most of their assets.[61] The debtors filed two chapter 11 plans that provided for the sale of the debtor's assets, with the buyers of the assets assuming obligations to reclaim the mine sites.[62] The proceeds of these proposed sales of the debtors' assets would pay off post-petition lenders, secured creditors, administrative claims and other unsecured creditors.[63]

The plans sought to conduct the sale as a section 363 sale, free and clear of all liens, claims, encumbrances and other interests, including the successor liability clauses under the collective bargaining agreements.[64] The debtors had earlier

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[56] *In re* Horizon Natural Resources Co., 316 B.R. 268 (Bankr. E.D. Ky. 2004). *See* James Dao, *Miners' Benefits Vanish With Bankruptcy Ruling*, N.Y. TIMES, Oct. 24, 2004, at N20 (recognizing termination of collective bargaining agreement caused nearly 3,800 coal workers and their dependents to lose health insurance).

[57] *Horizon*, 316 B.R. at 282 (holding "absent the rejection of collective bargaining agreements and the proposed modifications of the retiree benefits, conversion of these cases to chapter 7 and piecemeal liquidation would ensue."); *see Employee Distress—What About My Retirement?*, 11th Annual Southeast Bankruptcy Workshop, American Bankruptcy Institute (July 26-29, 2006), *available at* Westlaw 060726 ABI-CLE 163 (observing that if a company is forced to liquidate under chapter 7, as opposed to reorganize under chapter 11, debtors' retirees could suffer "reduced retirement income"); *cf. In re* Sai Holdings Ltd., No. 06-33227, 2007 WL 927936, at *1,*4 (Bankr. N.D. Ohio March 26, 2007) (stating section 1114 of Bankruptcy Code applies to chapter 11 liquidation plans, but denying debtors' request for order authorizing termination of retiree benefits).

[58] *Horizon*, 316 B.R. at 271.

[59] *Id.* ("Each of the collective bargaining agreements includes a 'successorship clause,' whereby the employer agreed not to sell its operation without obtaining the agreement of the purchaser to assume the employer's obligations under the agreement."). *See generally In re* Chateaugay, 155 B.R. 636, 654–55 (Bankr. S.D.N.Y. 1993) (noting union's successorship clause required partial purchaser of debtor's business to assume all of the obligations of collective bargaining agreement to both current and former employees); John D. Ayer et al., *The Intersection of Chapter 11 and Labor Law*, 26 AM. BANKR. INST. J. 22, 56 (May 2007) (defining successorship clauses).

[60] *Horizon*, 316 B.R. at 271.

[61] *Id.*

[62] *Id.*

[63] *Id.*

[64] *Id.* at 278 n.7; *see* 11 U.S.C. § 363(f)(5) (2006) (stating trustee may sell property free and clear of any vested or contingent right only if "such entity could be compelled, in a legal or equitable proceeding, to

attempted to negotiate with the unions to modify the collective bargaining agreements and the retiree medical benefits within those agreements, but the unions insisted that the successorship clauses in the collective bargaining agreements could not even be on the table for negotiation.[65]

The debtors' experts testified that they tried diligently to market their businesses with the successorship clauses in place, but that no one wanted to buy the assets with the union and retiree obligations still attached to them.[66] There was also evidence that without the section 363 nature of the sale, the assets would not even generate enough proceeds to pay off post-petition lenders and administrative priority claims.[67] Some potential buyers specifically pointed to the legacy costs and the successorship clauses as deal-breakers for them.[68]

In holding for the debtors and allowing the sale to go forward free and clear of the retiree benefit obligations, the *Horizon* court pointed to a similar case where a court also allowed a section 363 sale.[69] In the analogous case, the debtor's assets were worth about $1.9 million free and clear of liabilities, but the debtor's accrued Coal Act obligations were valued at about $7 million.[70] The court in that case found that absent a section 363 "free and clear" order, the assets would have to be sold piecemeal for fewer dollars than could be realized if they could be sold as a unit without the Coal Act obligations.[71]

Turning to the case at bar, the court in *Horizon* noted, "It is in the best interests of the Coal Act Plan and Fund and their beneficiaries and creditors generally that the debtors' assets be sold for the best possible price, not on a piecemeal basis. If the modification of the Coal Act retiree benefits is necessary to accomplish that goal and the other requirements of 1114 are satisfied, modification must be permitted."[72]

Horizon is not the only recent case to take an expansive view of a chapter 11 company's ability to modify its retiree benefits. In the case of *In re Ormet*,[73] the court allowed a modification of retiree medical benefits to take place under section

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accept a money satisfaction of such interest."); *cf. In re* Netfax, Inc., 335 B.R. 85, 87 (D.Md. 2005) (affirming bankruptcy court's order authorizing Chapter 7 Trustee to sell intellectual property free and clear of all liens, claims, and encumbrances pursuant to 11 U.S.C. § 363(f)(3)).

[65] *Horizon*, 316 B.R. at 272.

[66] *Id.* at 274.

[67] *Id.*

[68] *Id.*

[69] *Id.* at 279 (citing United Mine Workers of Am. 1992 Benefit Plan v. Leckie Smokeless Coal Co. (*In re* Leckie Smokeless Coal Co.), 99 F.3d 573 (4th Cir. 1996)).

[70] United Mine Workers of Am. 1992 Benefit Plan v. Leckie Smokeless Coal Co. (*In re* Leckie Smokeless Coal Co.), 99 F.3d 573, 586 (4th Cir. 1996) ("[T]he Bankruptcy Court found that $1.9 million represented a fair and reasonable price for the debtors' assets; the debtors' accrued Coal Act obligations, though, stand at about $7 million.").

[71] *Id.* at 586–87 ("If a free and clear order could not be issued, the assets would almost inevitably have to be sold piecemeal, thereby generating fewer funds with which to satisfy the claims of the Fund, the Plan, and the debtors' other creditors.").

[72] *Horizon*, 316 B.R. at 279.

[73] 355 B.R. 37 (D. Ohio 2006).

1114 even after the debtor's chapter 11 plan had been confirmed.[74]

A month and a half after confirmation, the debtor made a section 1114 proposal to the United Steelworkers union, offering to create a retiree medical benefits trust that would save the company $5 million per year.[75] The two sides negotiated but could not agree, so the bankruptcy court granted the debtor's section 1114 modification proposal three months following the plan's confirmation.[76] The union appealed to the district court after the bankruptcy court allowed the post-confirmation modifications of retiree benefit obligations.[77] The union argued that section 1114 relief is simply not available post-confirmation.[78] The district court disagreed, holding that "[t]here is no temporal limitation stated in 1114 as to when relief is available."[79]

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[74] *See Ormet*, 355 B.R. at 43 ("Section 1114 authorizes a bankruptcy court to enter an order modifying retiree benefits if certain procedural and substantive conditions are satisfied."); *see also* J. Keith Bryan, *Expiration of Retiree Benefit Plans During Reorganization: A Bitter Pill for Employees*, 9 BANKR. DEV. J. 539, 544–45 (1993) ("The purpose of section 1114 is to avoid unilateral changes in retiree benefit plans by companies undergoing reorganization.").

[75] *Ormet*, 355 B.R. at 40 ("On January 28, 2005, the Debtors made a § 1114 proposal to the USW. The proposal called for the creation of a voluntary employee beneficiary association that would be in charge of providing benefits to retirees."); *see* Brief of Appellee of Unsecured Creditors of Ormet Corp., et al., in Opposition to the Appellant United Steelworkers' Appeal from the Bankruptcy Court's Order Granting Relief Under 11 U.S.C. § 1114(4), *In re* Ormet, 355 B.R. 37 (D. Ohio 2006) (No. 2:05-cv-571), 2005 WL 2669931 ("The required remaining savings, approximately $5.1 million annually, needed to be achieved through the relief sought in the Section 1114 Application.").

[76] *See Ormet*, 355 B.R. at 40 ("On December 15, 2004, the bankruptcy court confirmed the reorganization plan."); *see also* Brief of Respondent-Appellant United Steelworkers at 7, *In re* Ormet, 355 B.R. 37 (D. Ohio 2006) (No. 2:05-cv-571), 2005 WL 2268102 ("The bankruptcy court erred as a matter of law in holding that a Chapter 11 debtor can modify retiree benefits pursuant to 11 U.S.C. § 1114 after confirmation of its reorganization plan."); Brief of Appellee of Unsecured Creditors of Ormet Corporation, et al., in Opposition to the Appellant United Steelworkers' Appeal from the Bankruptcy Court's Order Granting Relief Under 11 U.S.C. § 1114, *supra* note 75, at 9 ("The Bankruptcy Court correctly held that the Debtors could seek relief under Section 1114 after confirmation of the plan of reorganization.").

[77] *See Ormet*, 355 B.R. at 39 ("The United Steelworkers of America (the "USW") brings this appeal of the bankruptcy court's March 24, 2005 order granting relief under 11 U.S.C. § 1114 to modify retiree benefits."); *see also* Brief of Appellee of Unsecured Creditors of Ormet Corporation, et al., in Opposition to the Appellant United Steelworkers' Appeal from the Bankruptcy Court's Order Granting Relief Under 11 U.S.C. § 1114, *supra* note 75, at 6 (noting USW entered this appeal on April 4, 2005); Appellees–Reorganized Debtors' Opposition to Appellant United Steelworkers' Appeal from the Bankruptcy Court's Order Granting Relief Under 11 U.S.C. § 1114 at 6 n.2, *In re* Ormet, 355 B.R. 37 (D. Ohio 2006) (No. 2:05-cv-571), 2005 WL 2669928 (noting "[o]n August 19, 2005, this Court (Graham, J.) dismissed the USW's appeal from the Bankruptcy Court's Section 1113 Order as moot.").

[78] *See Ormet*, 355 B.R. at 42 ("The USW argues that the bankruptcy court erred in granting § 1114 relief after the Plan had been confirmed. The USW does not argue that the bankruptcy court was without jurisdiction to consider the Debtors' application for § 1114 relief."); *see also* Brief of Respondent-Appellant United Steelworkers, *supra* note 76, at 7 (arguing the bankruptcy court erred in holding modification under 1114 is available post-confirmation); Reply Brief of Respondent-Appellant United Steelworkers at 8, *In re* Ormet, 355 B.R. 37 (D. Ohio 2006) (No. 2:05-cv-571), 2005 WL 2872911 (arguing "[t]he Bankruptcy Code is thus clear that relief pursuant to Section 1114 cannot be obtained post confirmation.").

[79] *Ormet*, 355 B.R. at 423. *See In re* Federated Dep't Stores, Inc., 132 B.R. 572, 575 (Bankr. S.D. Ohio 1991) (emphasizing "the present posture of this case, however, by no means enables the Debtor to unilaterally embark on a course to 'wipeout' the pre-petition retirees the day after a confirmation hearing."); *In re* Farmland Indus. Inc., 294 B.R. 903, 921 n.19 (Bankr. W.D. Mo. 2003) (noting debtor could still terminate the life insurance benefits after plan confirmation).

If the *Ormet* case broke new ground in the case of post-confirmation retiree medical benefit modifications, an even bigger trend that is happening lately is section 1114-like modifications to retiree medical benefits without the need for an employer to file bankruptcy at all. The most common modifications under these scenarios involve a shift in retiree benefits from a promise owed by the employer for the future to a present fixed payment by the employer into a Voluntary Employee Benefit Association (VEBA)[80] from which retirees will need to cover their benefit costs down the road. The basic idea here is to shift the risk of future increases in health-care costs from the employer to the retiree, and also to cap the total liability of the employer for its retiree health-care promises.[81]

In many ways, this arrangement is analogous to how the legal system dealt with companies' mass-tort liabilities during the 1980s and 1990s.[82] In those cases, the companies would admit that they had future liabilities that were significant. The problem was, these companies could not successfully operate as ongoing entities with the size and scope of those liabilities still unknown. If these giant uncertain future liabilities would force a company to liquidate in the short-term, then everyone would lose, including future victims. The solution was to shift a portion of the company's assets into a separate financial entity that would be solely responsible for that category of liability. In that way, future victims would have some source of funds from which to recover, and the companies could continue to operate without the specter of unlimited future liability holding them back.

A prominent example of this recent trend is the arrangement that was forged,

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[80] *See* 26 U.S.C. § 501(c)(9) (2006) (describing a VEBA as a tax exempt organization providing for the payment of life, sick, accident or other benefits (including retiree medical benefits) for both active and retired employees, their dependents, and beneficiaries); *see also* John J. Koresko, V & Jennifer S. Martin, *VEBAs, Welfare Plans, and Sec. 419A(F)(6): Is the IRS Trying to Regulate or Spread Propaganda?*, 32 SW. U. L. REV. 1, 7–8 (2003) ("Although there are socially useful reasons for having VEBAs and protecting the ability of small businesses using VEBAs to provide the much needed welfare benefits to both business owners and their employees, there is the potential for misuse and schemes by those seeking only to evade taxes."); John McNeil, *The Failure of Free Contract in the Context of Employer-Sponsored Retiree Welfare Benefits: Moving Towards a Solution*, 25 HARV. J. ON LEGIS. 213, 257 (1988) ("VEBAs do not speak to governance of the employer-employee relationship. They do not address the creation of a retiree welfare benefit plan, nor do they address the conditions under which an employer can stop contributing to the VEBA.").

[81] *See* Anne P. Birge, *The Pending Crisis in Employer-Provided Health Benefits for Retirees: Are Tax Breaks for Employers the Answer?*, 19 N.Y.U. REV. L. & SOC. CHANGE 797, 809 (1992) ("VEBAs also limit an employer's ability to terminate its retiree medical plan, a benefit security concern for employees."); Andrew W. Stumpff, *The Unimportance of Being a VEBA: Tax Attributes of Nonexempt Welfare Benefit Trusts*, 47 TAX LAW. 113, 130 (1993) ("When a welfare benefit trust is wholly funded by a single employer's contributions, it is more difficult to demonstrate that the employer (the insured) has shifted risk to the trust (the insurer).").

[82] *See* Kathy L. Yeatter, *Fumbling Towards Consistency*: *Valuation of Future Asbestos Personal Injury Claims in Bankruptcy*, 25 AM. BANKR. INST. J. 50, 52 (November 2006) (noting the *Manville* asbestos crisis demonstrates "historical claims data cannot be taken for granted when developing a workable estimate of future asbestos personal-injury claims"); *see also* Scott S. Evans, *Dynamic Incentives: Improving the Safety, Effectivity, and Availability of Medical Products Through Progressively Increasing Damage Caps for Manufacturers*, 2007 U. ILL. L. REV. 1069, 1088 (2007) (stating in order to avoid future liability, potential mass-tort defendants withdrew their product from the market).

without the need for bankruptcy, between General Motors (GM), Ford and their unions. In 2005 the United Auto Workers (UAW) filed a declaratory-judgment class action regarding GM's and Ford's legal ability to unilaterally modify retiree medical benefits outside of bankruptcy when those benefits were arguably vested.[83] Ultimately, the two companies, the UAW, and the class which filed the class action ended up settling the matter, but "a small percentage of the retirees from each company (less than one half of one percent) objected to . . . the settlements."[84]

The settlements replaced premium-free and deductible-free plans that retirees had in place with two options: modified plans with some monthly premiums and substantial benefits, or catastrophic plans with no premiums but higher deductibles and co-pays.[85] GM expected to reduce its accumulated retiree medical benefit liability by $15 billion with the settlement and Ford by $5 billion.[86] Under the terms of the settlement, even the new costs required to be paid by the retirees will be offset by a defined-contribution VEBA trust.[87] GM will contribute $3 billion in cash to that trust through 2011 along with at least $30 million per year in profit-sharing payments through 2012, plus additional payments based on increases in GM's stock

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[83] *See* UAW v. Gen. Motors Corp., 497 F.3d 615, 620 (6th Cir. 2007) (discussing the two settlements and the declaratory judgment action).

[84] *See Gen. Motors Corp.*, 497 F.3d at 620 (noting less than one half of one percent objected to the proposed settlements); *see also* Brief of Movants–Appellants at 47, UAW v. Gen. Motors Corp., 497 F.3d 615 (No. 05-73991), 2006 WL 4588292 ("In approving the settlement, the district court noted that approximately 1,250 class members objected, a small percentage of the 476,000 class members estimated to be effected."); Brief of Defendant–Appellee General Motors Corporation at 26, UAW v. Gen. Motors Corp., 497 F.3d 615 (No. 05-73991), 2006 WL 4588289 ("In response, fewer than 1,250 of the 476,676 Class Members (less than three-tenths of one percent) submitted an objection to the Settlement Agreement.").

[85] *See Gen. Motors Corp.*, 497 F.3d at 623–24 (explaining the two options available to retirees); *see also* Brief of Defendant–Appellee General Motors Corporation, *supra* note 85, at 26 ("As the district court found, with mitigation provided by the DC-VEBA, new charges for retirees under the Modified Plan will initially cost a single retiree a maximum of $370 per year (about $1 per day) for comprehensive medical, vision and dental health care; family coverage will cost a maximum of $752 per year ($2.06 per day)."); Brief of Movants–Appellants, *supra* note 85, at 34 (arguing "[t]he settlement also treats members of the Class differently based upon their age.").

[86] *See Gen. Motors Corp.*, 497 F.3d at 624 ("In the long run, GM expects to reduce its annual healthcare expenditures by $3 billion and shed some $15 billion of its accumulated retiree healthcare obligations; Ford expects to shave more than $5 billion from its accumulated retiree healthcare obligations."); *see also Judge OKs GM Health-Care Deal; Retirees Claimed Settlement Violated Their Contracts*, GRAND RAPID PRESS (Michigan), Apr. 1, 2006, at B1 ("GM has said the agreement would save it $1 billion after taxes each year and would shave $15 billion off its $70 billion in long-term retiree health-care liabilities."); David Shepardson, *Ford Retirees Fight Cuts; Group Wants Judge to Block Changes to Health Care Benefits Because Automaker Plats to Invest in Mexico*, THE DETROIT NEWS, July 7, 2006, at 1C ("The deal is expected to translate into an annual pretax savings to Ford of $650 million, for cash savings of about $200 million annually. It also will reduce Ford's overall retirement obligations by $5 billion.").

[87] *See Gen. Motors Corp*., 497 F.3d at 624 ("[T]he retirees who must pay these new costs will not be required to pay all of them. Under the agreements, a substantial percentage of these costs will be paid for through a trust set up for that purpose-what the parties call a defined contribution 'Voluntary Employees' Beneficiary Association trust . . . .'"); *see also* Jim Leute, *Health Care Slows Auto Talks*, THE JANESVILLE GAZETTE (Wisconsin), Sept. 19, 2007 (explaining the VEBA trust); Todd Seibt, *Deal; UAW: 'We Feel Very Good'*, THE FLINT JOURNAL (Michigan), Sept. 26, 2007, at A01 (suggesting GM was content with establishing a VEBA trust).

price.[88] Ford will make comparable contributions. For its part, the UAW agreed to defer negotiated wages and COLA adjustments and contribute those to the trusts, with the foregone wages adding about $4 billion to the trust over the next 20 years.[89]

Goodyear is another prominent example of a retiree medical benefit reduction negotiated while the employer was not yet in chapter 11. Goodyear shed all of its retiree medical benefits outside of bankruptcy in exchange for a $1 billion investment in a VEBA that would be controlled by the union.[90] Goodyear was happy because it shed this uncertain liability that was projected to cost it $1.2 billion, and the union was happy because now if Goodyear files for bankruptcy, there is no way that any other creditors can get at the retiree benefit money since it will be separate and independent from Goodyear's bankruptcy estate. Goodyear's total contributions to the VEBA will consist of $700 million in cash and $300 million in either cash or stock at Goodyear's option.[91]

The substitution of VEBAs for an employer's health-care promises is also happening inside of bankruptcy in the context of section 1114 court-sanctioned modifications of retiree medical benefits. Dana Corporation agreed this summer to create a retiree medical benefits VEBA in its chapter 11 bankruptcy case.[92] As a result, it expects to save about $100 million per year, even though its one-time payment to the VEBA includes $703 million in cash and $80 million in stock.[93] There was a lot of consternation among Dana retirees as to exactly how much this would reduce their current levels of retiree medical benefits, but most retirees believed after learning more that the VEBA would keep their benefit costs fairly close to their historical levels.[94]

In re Tower Automotive[95] involved a fairly contentious creation of a retiree medical benefit VEBA in the context of a chapter 11 case. Tower initially offered to make a one-time $5 million contribution to a VEBA on behalf of existing retirees

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[88] *See Gen. Motors Corp.*, 497 F.3d at 624 (discussing GM's contributions); *see also* Brief of Movants–Appellants, *supra* note 84, at 11 ("The Settlement Agreement provides for the VEBA to be funded from several sources. First, GM will make three payments of $1 billion each in the first and second years and again in 2011."); *Judge OKs GM Health-Care Deal; Retirees Claimed Settlement Violated Their Contracts*, *supra* note 86 ("The agreement requires active GM hourly workers to contribute part of their future pay increases to a new fund to help pay for retirees' coverage. GM would contribute $3 billion to that fund through 2011.").

[89] *See Gen. Motors Corp.*, 497 F.3d at 624 (discussing Ford's contributions and the deferred wage and cost-of-living adjustments); Shepardson, *supra* note 86 (explaining Ford's various contributions pursuant to the settlement agreements). *See generally* John K. Teahen Jr., *The Big 3 Gave Away the Store*, AUTOMOTIVE NEWS, Sept. 10, 2007, at 14 (suggesting Ford, GM, and Chrysler gave away too much in the settlement agreements).

[90] *See* Sharon Silke Carty, *Big 3, UAW Tackle Health Care; Goodyear Could Be Model For Union-Run Fund*, USA TODAY, July 10, 2007, at 3B (describing Goodyear arrangement).

[91] *Id*.

[92] *See* Jon Chavez, *Dana, 2 Unions Cut Deal to Save $100M Annually*, THE BLADE (Toledo, Ohio), July 7, 2007 (explaining arrangement in Dana case).

[93] *Id.*

[94] *Id.*

[95] 241 F.R.D. 162 (S.D.N.Y. 2006).

in lieu of honoring its outstanding retiree medical benefit obligations.[96] The final settlement included, rather than the one-time payment, Tower's promise to make a series of cash payments to a retiree health-benefits VEBA.[97] In addition, Tower promised that a $150 million unsecured claim representing the value of retirees' future medical benefits would receive at least a 20% recovery to be paid into the VEBA (after subtracting the separate cash payments that were scheduled to be made to the VEBA).[98]

The settlement specifically provided that the guarantee of at least a 20% recovery on the $150 million unsecured claim would be honored even if other general unsecured creditors ended up receiving something less than 20% on their claims.[99] The creditors' committee argued that this kind of a floor guarantee was impermissible under the Code.[100]

Specifically, the creditors' committee contended that the settlements were illegal because they treated similarly situated creditors differently.[101] In other words, the argument was that the debtor could not provide a minimum guarantee to only one group of general unsecured creditors (the retirees) but not to another group of general unsecured creditors. The court in *Tower Automotive* disagreed, pointing out that section 1114 by its nature gives the retiree medical benefit claim, even though it is unsecured, a special status that is greater than that of the general unsecured creditor.[102] This settlement, the court believed, was not inconsistent with the statutorily elevated status that the retiree claim otherwise enjoyed.[103]

There are a number of obvious downsides for retirees as a result of a shift of their retiree benefits to employer-funded VEBAs. When the VEBA is funded in whole or in part with stock rather than cash, the extent of the retirees' benefits under the VEBA will be a function of the company's share price. For example, when Wheeling-Pittsburgh's share value declined by 27 percent in one week, the retirees of Wheeling-Pittsburgh took a big hit since their retiree medical benefit VEBA holds about four million shares of Wheeling-Pittsburgh stock.[104] The VEBA was created as part of Wheeling-Pittsburgh's chapter 11 reorganization.

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[96] *Id.* at 164.
[97] *Id.* at 165.
[98] *Id.*
[99] *Id.*
[100] *Id.* at 165–66.
[101] *Id.* at 166. *But cf. In re* U.S. Truck Co., Inc., 800 F.2d 581, 585 (6th Cir. 1986) ("'It does not require that similar claims *must* be grouped together, but merely that any group created must be homogenous'" (quoting Barnes v. Whelan, 689 F.2d 193, 201 (D.C. Cir. 1982))); *In re Graphic Commc'ns, Inc*., 200 B.R. 143, 146 (Bankr. E.D. Mich. 1996) ("Plainly read, § 1122(a) does not require that similar claims be placed in the same class.").
[102] *See Tower Auto.*, 241 F.R.D. at 167; *see also* 11 U.S.C. § 1114 (2006); *In re* Ionosphere Clubs, Inc., 134 B.R. 515, 517 n.1 (Bankr. S.D.N.Y. 1991) (indicating status of claims for retirees' benefits is elevated during chapter 11 case).
[103] *See Tower Auto.*, 241 F.R.D. at 167; *see also* 11 U.S.C. § 1114 (2006); Dan Keating, *Good Intentions, Bad Economics: Retiree Insurance Benefits in Bankruptcy*, 43 VAND. L. REV. 161, 183 (1990) (noting Congress elevated retirees' status in Bankruptcy Code).
[104] *See* Len Boselovic, *Steelmaker's Ill Health Has Retirees Feeling Queasy*, PITTSBURGH POST-GAZETTE, Nov. 13, 2005, at D1 (describing plight of retirees from Wheeling-Pittsburgh).

That share-value reduction translated into a $13 million loss in value for the Wheeling-Pittsburgh VEBA, and there has been a $139 million drop in value for the VEBA when measured from the stock's all-time high following the creation of the VEBA.[105] To make matters worse for the Wheeling-Pittsburgh retirees, the VEBA also has significant restrictions in its ability to sell the Wheeling-Pittsburgh stock.[106] The extent of each Wheeling-Pittsburgh retiree's medical coverage is ultimately a function of the value of the VEBA, which in turn depends on the value of the Wheeling-Pittsburgh stock.

III. UNION/RETIREE DIVERGENCE OF INTERESTS

Retirees have historically relied on their unions to represents their interests in labor contracts and labor disputes. For the most part, this has worked out well for retirees. Active union workers, who are the ones that have the votes, have a number of good reasons to look out for the interests of retirees. First, there is the general sense of loyalty to the retirees for the labor that the retirees have contributed to the company through the years. This reason we might think of as purely altruistic. Second, and perhaps a little more self-interested, is that many retirees are relatives or close friends of the active union workers, and so it only makes sense that the workers would want to make certain they are adequately taking care of their own. Finally, the active workers, particularly the older ones, realize that they will one day be retirees themselves and thus have to live with whatever arrangements the union has bargained for retirees.

It would be an exaggeration to assert that this alignment of interests has completely broken down over the last few years. Nevertheless, there have been an increasing number of situations, some of them fairly high-profile, in which retirees believe that their interests are not being properly represented by their union. Part of this, I suspect, is the reality that when the overall pie gets smaller, as it certainly has in the labor arena as of late, it is naturally harder for current workers to be generous to retirees.[107]

Following GM's establishment of the VEBA for retiree medical benefits that was described above, some GM retirees sued in federal district court, arguing that

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[105] *Id.*

[106] *Id*.

[107] *See* Jeff Green, *GM Retirees May Fight Reductions in Benefits; Michigan Lawsuit Challenges UAW*, BUFF. NEWS, Jan. 2, 2006, at B7 (noting that "[h]istorically, active UAW workers have been reluctant to cut retiree benefits because many are near retirement age or have parents and other relatives who are already union retirees," but that "[l]osses at GM and Ford have forced a change."); *see also* Turner v. Local Union No. 302, Int'l Bhd. of Teamsters, 604 F.2d 1219, 1223, 1226 (9th Cir. 1979) (holding retirement benefits were not vested rights, but contractual rights and so reductions approved by active union members were permitted in response to changes in working to retired employees ratio); Joan Vogel, *Until Death Do Us Part: Vesting of Retiree Insurance*, 9 INDUS. REL. L. J. 183, 204 n.130 (1987) ("Retirees are an easier target for cost-cutting than active employees because cutting their benefits will not necessarily damage the morale of active employees, as retirees are not present in the workplace.").

their union should not have been allowed to negotiate this deal on their behalf.[108] The retirees argued unsuccessfully that the shifting of retiree medical benefit liabilities from the company to the VEBA was a matter on which the retirees deserved a more formal say.[109]

Another recent case that is illustrative of this increasing tension between unions and retirees is *Nelson v. Stewart*.[110] The Indiana Steel & Wire company had filed for chapter 11 bankruptcy in March of 1998.[111] The company and its union began renegotiating its collective bargaining agreement in bankruptcy. During these negotiations, the union assured the retirees that the retirees' medical insurance in the collective bargaining agreement was not even a subject for negotiation and that therefore the retirees did not need separate representation.[112]

However, in August of the same year, the company filed a motion to reject the collective bargaining agreement and to amend the retiree medical benefits under sections 1113 and 1114. Then, a few weeks later, a prospective buyer for the company emerged and the union negotiated the collective bargaining agreement with that prospective buyer, including termination of retiree medical benefits. In September, the local union ratified both the modification of the collective bargaining agreement and the purchase itself. In October, the bankruptcy court approved both the collective bargaining agreement modification and the sale. When the retirees learned after the fact that they had lost their retiree medical benefits, they sued their union, arguing negligence, misrepresentation and promissory estoppel.[113]

The Seventh Circuit noted that section 1114 is designed to account for the inherent conflict of interest that exists between the interests of the union's current workers and its retirees, particularly as that conflict affects retiree medical benefits.[114] The union is the presumptive representative of the retirees' interests under section 1114.[115] However, if the union elects not to serve, or the court decides

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[108] *See* UAW v. Ford Motor Co., No. 05-74730, 2006 WL 1984363, at *28–29 (E.D. Mich. July 13, 2006) (rejecting argument that union lacked authority to negotiate on retirees' behalf) (*aff'd*, 497 F.3d 615 (6th Cir. 2007)).

[109] *See* UAW v. General Motors Corp., 497 F.3d 615, 626 (6th Cir. 2007) (holding retirees were adequately represented in declaratory judgment class action to determine if collective bargaining agreements vested former union workers with their health care benefits on retirement).

[110] 422 F.3d 463 (7th Cir. 2005).

[111] *Nelson*, 422 F.3d at 464.

[112] *Id*.

[113] *Id*.

[114] *See Nelson*, 422 F.3d at 471; *see also In re* Tower Auto. Inc., 241 F.R.D. 162, 166 (S.D.N.Y. 2006) (noting Congress' purpose in enacting section 1114 was "to ensure that the debtors did not seek to effect reorganization 'on the back of retirees' for the benefit of other parties in interest." (quoting *In re* Ionosphere Clubs, Inc., 134 B.R. 515, 523 (Bankr. S.D.N.Y. 1991))); *In re* Farmland Indus., Inc., 294 B.R. 903, 918 (Bankr. W.D. Mo. 2003) (stating that "Congress knowingly acted to provide special protections for retiree benefits when it enacted section 1114.").

[115] *See* 11 U.S.C. § 1114(c) (2006) ("A labor organization shall be . . . the authorized representative of those persons receiving any retiree benefits covered by any collective bargaining agreement to which that labor organization is signatory" unless organization refuses or court determines different representation appropriate).

that the union should not serve, or a party in interest makes a motion, then under section 1114 the court should appoint a retiree committee whenever the debtor seeks to modify or terminate retiree medical benefits.[116] Ultimately, the Seventh Circuit concluded that section 1114 was not intended to preempt state-law causes of action such as the retirees were bringing here for the union's alleged misrepresentation, and thus the retirees were allowed to proceed with their state-law causes of action against the union.[117]

The retiree-union conflict of interest has also been rearing its head in the public sector. A couple of years ago in Chicago, city retirees, mostly from the city's building trade unions, were threatening to sue their union.[118] The city workers' union had just entered into a new four-year union contract with the city of Chicago that provided for two years' worth of back pay to 8,000 active workers, but not to the city's 1,000 retirees.[119] The exclusion of the retirees from the back-pay part of the deal saved the city about $4 million. In response, one disgruntled city retiree was quoted as saying, "[The unions] took our money when we were on the job, and then they did not represent us."[120]

A few states to the east, the Ohio Education Association, a labor union for education employees of the state, terminated retiree medical benefits for all of its retirees over 65 even though those benefits were arguably vested. Following this move by the union, one retiree noted: "If a union can do this to its own retirees, no one is safe."[121]

One union-retiree rift that has gotten a lot of play in the popular press over the last year or so has been the battle between the NFL players' union and its retirees. NFL retirees, particularly those suffering from debilitating injuries, have argued that the union has not taken care of their needs. Gene Upshaw, head of the NFL players' union, has responded by noting that he has increased retiree benefits in each of his years as union chief, and that current players are now contributing almost $100

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[116] 11 U.S.C. § 1114(c)(2).

[117] *Nelson*, 422 F.3d at 475.

[118] *See* Todd Lighty, *Retirees May Sue City Hall Over Union Deal, Back Pay*, CHI. TRIB., Dec. 28, 2005, at 1 [hereinafter *Retirees May Sue City Hall*] (detailing events surrounding tension between union and its retirees); *see also* Marcatante v. City of Chicago, No. 06 C 328, 2006 WL 2331100, at *1 (N.D. Ill. Aug. 10, 2006) (describing how suit was brought by retirees against City for excluding them from retroactive pay increase); Todd Lighty, *City Retirees File Class-Action Suit Over Lost Back Pay*, CHI. TRIB., Jan. 23, 2006, at 3 [hereinafter *City Retirees File Class-Action*] (reporting commencement of suit by retired worker, contesting City's contract settlements with unions denying back pay to retirees).

[119] *Retirees May Sue City Hall, supra* note 118, at 1; *see also* Marcatante v. City of Chicago, No. 06 C 328, 2006 WL 2331100, at *1, *3 (N.D.Ill. Aug. 10, 2006) (laying out retirees' allegations of being treated differently than similarly situated active employees with respect to back pay, having been denied back pay because of retirement); *City Retirees File Class-Action, supra* note 118, at 3 (discussing terms of labor contract that benefit 8,000 active union members and exclude retired ones).

[120] *Retirees May Sue City Hall, supra* note 118, at 1.

[121] *See* John L. Wardell, *Retirees Challenge OEA for Slashing Benefits*, COLUMBUS DISPATCH, Jan.12, 2005, at 10A (describing benefit-reduction scenario for retirees); *see also* Prater v. Ohio Educ. Ass'n, No. 06-4393, 2007 WL 2849555, at * 2 (6th Cir. Oct. 3, 2007) (discussing how OEA's termination of post-65 supplemental insurance gave rise to dispute).

million per year to fund the pensions of retired NFL players.[122] Despite Upshaw's positive-spin figures, a July 2007 meeting between the union and some retiree representatives was described as taking place "amid a growing wave of protest from former football stars who allege that the pension and disability programs for older NFL retirees are broken and that the league and the players union are not doing enough."[123]

In the increasing number of situations where the interests of active workers and retirees diverge, it becomes especially irritating to retirees to accept the reality that on most union matters, they simply do not have a vote or even a seat at the table. A few years ago when Denver-area union supermarket workers prepared to vote on a new contract, it became distressingly clear to the retirees of that union that they were depending on the kindness of the active workers to protect the retirees' interests.[124] The retirees had no vote on this contract, even though the employer contribution to retiree medical benefits had not increased for 11 years. Given that freeze, an individual retiree's monthly medical premium had climbed from $119 per month to $556 per month in just five years because of the increasing cost of health care and the lack of any increase in the employer contribution to retiree health benefits.

Some retirees have tried to change the system that refuses to give them a vote on union contracts, even in matters that directly affect their interests. A little over a year ago, there was a proposal before the United Auto Worker delegates that would have allowed retirees to vote on those parts of labor contracts that affect retiree medical benefits.[125] The proposal was voted down 207-9.

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[122] *See* Tim Lemke, *Bitter, Broken Affair in NFL: Union, Retirees Are Still at Odds*, WASH. TIMES, June 14, 2007, at C1 (describing current state of "rift between retired football players and the NFL Players Association"); *see also* Chris Colston, *NFL Retirees Feel Forgotten as Fight for Benefits Rages*, USA TODAY, July 8, 2007, *available at* http://www.usatoday.com/sports/football/nfl/2007-07-08-sw-retirees_N.htm (recounting Upshaw's contributions to improve retired player's pensions, including annual pension increases and $88,000 annually for institutional care f ex-players with dementia); Mike Freeman, *Pro Football: Inside the N.F.L.; Pension Pay Raised for Pre-1977 Players*, N.Y. TIMES, May 19, 2002, *available at* http://query.nytimes.com/gst/fullpage.html?res= 9401E1D71738F93AA25756C0A9649C8B63 ("[P]ension-rights experts maintain what the N.F.L. did in doubling pension payments to the older players is almost without precedent.").

[123] *See* Greg Johnson, *Goodell, Upshaw Meet With Retirees: New Assistance Program Is Set Up to Help Former NFL Players With Critical Health, Financial Issues*, L.A. TIMES, July 25, 2007, at 10 (discussing events leading to meeting between former football players and union representatives). *See generally* Chris Colston, *supra* note 122 (describing the financial difficulties and physical disabilities of N.F.L. retirees); Mike Freeman, *supra* note 122 ("There has been only one glaring gap in the N.F.L.'s shiny armor, and that is the sad physical, and sometimes poor financial, shape of many of its older, retired players.").

[124] *See* Kimberly S. Johnson, *Grocery Retirees' Benefits at Risk; Health Care Funding is Fading*, DENVER POST, November 3, 2004, at C1 (outlining history of dispute). Janet Forgrieve, *Grocery Workers Fund May Go Bust No Proposal On Table To Raise Payments Into Trust for Retirees*, Rocky Mountain News, November 4, 2004, at 5B (pointing out how union supermarket retirees in Denver have "[n]o standing in contract negotiations between the stores and the current workers"); World Socialist Web Site, *Workers Struggles: The Americas*, http://www.wsws.org/articles/2004/nov2004/wkrs-n09.shtml (last visited October 17, 2007) (highlighting the 2006 events that took place with Denver supermarket union workers).

[125] *See* Jason Roberson, *UAW Dissenters Speak Out: Activists Battle the Odds in Challenging Union Hierarchy*, DETROIT FREE PRESS, June 18, 2006 (giving details surrounding vote); *see also* Dina El

IV. SILVER LININGS AND MORE DARK CLOUDS

With all of the harsh realities for retirees that are outlined above, one might think that the future of benefits is necessarily a bleak one for retirees. But I don't believe that would be completely accurate. For buried away in the midst of otherwise disturbing labor trends are at least some silver linings for retirees. In this final part of the essay, I describe just a few of them.

Let me start by comparing the old world of retiree medical benefits with the current trend. Under the old-world approach, a company would make unlimited and grandiose promises of retiree medical benefits for life, with no premiums or deductibles for covered retirees. With this approach, the employer would not put aside any money today to cover the promises to which it was binding itself for the future. The new approach to retiree medical benefits is that a company makes a predetermined contribution of cash, stock, or some combination of the two to a VEBA that then becomes the sole source of a retiree's entitlement to health benefits beyond whatever Medicare would give the retiree. The VEBA-covered medical benefits are almost invariably a lot more modest than the unfunded promises the employer would be making under the old approach.

Given the more modest coverage, what is the advantage to the new health-benefits paradigm for retirees? Probably the main benefit to the new approach is that it separates for retirees their employer's health-benefits commitment from the fortunes of the company that is making the commitment. In some ways, the traditional retiree-benefit promises were akin to a worker having a 401(k) plan full of Enron stock. All of the eggs were in one basket, and when the company would fall, so too would fall the promises made of lifetime health benefits. The beauty of the VEBA arrangements that are becoming increasingly common for providing retiree health benefits is that even if the company later files for bankruptcy, none of the company's creditors can attach the funds that are in the retiree health-care VEBA.

A similar observation could be made about the trend toward defined-contribution plans instead of defined-benefit plans. Even though defined-benefit pension plans are technically insured by the PBGC, the reality is that for many retirees a termination of the plan precipitated by the employer's financial distress will lead to significantly reduced pension benefits under the PBGC's replacement coverage. So just like in the realm of retiree-benefit promises, those who are counting on receiving their entire defined-benefit pension entitlements are effectively counting on the continued financial health of their employer. Defined-contribution plans, by contrast, create a separately funded account, the viability of

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Boghdady, *UAW Chief Warns Workers of Tough Changes Ahead*, WASHINGTON POST, June 13, 2006, DO1, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2006/06/12/AR2006061201157 (reporting on challenges faced by members of UAW); Roberta Wood, *Autoworkers Want Traction on Job, Health Care*, PEOPLE'S WEEKLY WORLD, June 19, 2006 (discussing how national health care was an important issue on the minds of retirees at the June, 2006 United Auto Workers convention in Las Vegas).

which does not depend on the overall fortunes of the company that created it. All else being equal, retirees are certainly better off with a dedicated and separate fund than they are with a mere promise.

Another silver lining to the evolving approach to pensions and retiree medical benefits relates to the power of expectations and, in particular, the bitterness felt when clear expectations have been disappointed. The new paradigm of retiree benefits has the distinct advantage of not setting up for retirees extravagant promises of lifetime benefits that ultimately cannot be fulfilled. While the scope of promises being made to retirees in the future will largely be limited to whatever funds are in their health-care VEBA or their defined-contribution plan, we should no longer see the tragic bait-and-switch scenarios being discussed in union halls across the country.

In the *GM* case involving proposed cutbacks of retiree medical benefits, for example, frustrated retirees came to federal court to complain about the impending modifications, noting specifically that they had promises in writing from their former employer that guaranteed them health benefits for life. The retirees before the court argued that the company should stop wasting money on bad strategic moves so that they would not have to take money away from retirees.[126]

In the similar case involving proposed modifications in Ford's retiree medical benefits, one retiree noted that he even took classes on financial management that were offered by Ford before he decided that he could indeed afford to retire at the age he did.[127] With Ford reneging on its promise of lifetime health care, this retiree argued, Ford should be required to allow him to come back to work.[128] "They gave us the tools to make our choice," this retiree said, "and now they've taken those tools away."[129]

Perhaps the most bitter retirees of all are those from the *Horizon* case affected by the bankruptcy sale of the coal mine assets that stripped away all of their retiree medical benefits. "I feel let down and cheated," said one affected mine worker.[130] "We were productive for these people. We lived with what we signed. They should have to. But these lawyers, these corporations, they see the loopholes and they can take our benefits."[131]

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[126] UAW v. General Motors Corp., 497 F.3d 615, 619–120 (6th Cir. 2007) (holding that retirees challenge to modification of retirement benefits without consent was permissible in light of the settlement agreement); *see* Michael Ellis, *Automaker, Union Under Fire: Retirees Blast UAW Deal with GM: Proposal Calls for Shifting Portion of Health Care Costs*, DETROIT FREE PRESS, March 7, 2006 (detailing frustration of some UAW retirees for cut backs in their health care benefits).

[127] *See Retirees Blast Ford Health Care Deal; Tell Judge Union and Car Maker Can't Alter Benefits*, BELLEVILLE NEWS DEMOCRAT (Associated Press) June 1, 2006, at B5 (outlining complaints of retirees) [hereinafter *Retirees Blast Ford Health Care Deal*]; *see also* John Welbes, *At Ford, Families in Limbo*, ST. PAUL PIONEER PRESS, December 31, 2005, at 1A (discussing the devastating effect Ford's downturn has had on families of Ford workers and retirees).

[128] *Retirees Blast Ford Health Care Deal*, *supra* note 127, at B5 (outlining complaints of retirees).

[129] *Id.*

[130] *See* Sharon Cohen, *Health Benefits Vanish in Bankruptcy Court*, L.A. TIMES, December 19, 2004, at 23 (describing stories of individual retirees affected by *Horizon* case).

[131] *Id*.

There is a final silver lining to the new-world order of retirement benefits, although this is a silver lining only for future retirees rather than current ones. This silver lining is about a company's future viability in light of the promises that it makes today concerning pensions and retiree medical benefits that will come due in the future. With the benefit of hindsight, one could argue that the generous pension and medical packages offered to union retirees in certain industries were destined to make those companies unable to compete in the global market. At the time those promises were made, perhaps neither the pervasiveness of the global market nor the staggering increases in health-care costs could have been predicted by anyone. But now that we know what we do, it simply is not realistic any longer to think that employers can make these kind of open-ended promises surrounding pensions and health benefits and still compete effectively as an ongoing firm.

Consider the untenable position that such legacy costs have placed some of our nation's largest employers. Delphi, a car-parts manufacturer that ended up in chapter 11 bankruptcy, had such generous pension and health benefits for its retirees that an active worker who made $25 per hour ended up costing the company $65 an hour once he or she retired.[132] Noting these figures, one commentator opined, "The first [lesson] is that unions gain nothing in the long run by extracting promises their employers cannot keep."[133]

The GM and Ford cases are tales along similar lines. Testimony in the GM case indicated that GM provides health care to 1.1 million people at a cost (in 2005) of $5.4 billion, of which $3.7 billion is for retiree medical benefits.[134] Ford's numbers are about half of GM's figures. Health care costs added on average $1,525 to the price of a GM car and $1,100 to the price of a Ford car. Their Japanese rivals spend about $450 per car for the combined health-care costs of active workers and retirees.[135]

GM's accumulated retiree medical benefit obligations increased from $42 billion in 2000 to $67.6 billion at the close of 2004; from 2000 to 2005, Ford's accumulated retiree health obligations went from $21 billion to $35 billion.[136] By the close of 2004, GM's total retiree medical benefit promises equaled about seven times the company's market value, and Ford's retiree health benefits totaled about three times its market value. At GM in 2006, there were four retirees for each

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[132] *See Delphi May be the World's Largest Maker of Car Parts, but that's Just a Hobby*, 57 NAT'L. REV. (Special Issue) 20 (November 7, 2005) (outlining statistics on legacy costs at Delphi); Henry H. Drummonds, *The Aging of The Boomers And the Coming Crisis In America's Changing Retirement and Elder Care Systems*, 11 LEWIS AND CLARK L. REV. 267, 279 (2007) (stating that "[D]elphi runs a pension deficit it estimates at $5.1 billion (by PBGC calculation $10.8 billion), and carries obligations for retiree medical expenses estimated at $9.6 billion."); Gretchen Morgenson, *Oohs and Ahs At Delphi's Circus*, N.Y. TIMES, November 13, 2005 ("Workers at Delphi earn good money—$26 to $30 an hour in many cases . . . . [and the] company jettisons a pension that is underfunded by $11 billion . . . and proposes cuts of up to two thirds in worker's pay and deep reductions in retiree benefits . . . .").

[133] *See Delphi May be the World's Largest Maker of Car Parts, but that's Just a Hobby, supra* note 132 (outlining statistics on legacy costs at Delphi).

[134] UAW v. General Motors Corp., 497 F.3d 615, 620 (6th Cir. 2007).

[135] *Id.*

[136] *Id*. at 621.

active worker, and at Ford in 2005 there were two retirees for each active worker.[137] Absent the benefit-modification settlement before the court, GM expected its accumulated obligations to increase 22% between 2005 and 2009.[138]

The court in the GM/Ford case pointed out that even if the plaintiffs were correct in their assertion that the retirees' medical benefits were legally vested under the case law, "any such victory would run the risk of being a Pyrrhic one because the cost of insisting on irreversible healthcare benefits might well be—and indeed almost certainly would be—the continuing downward spiral of the companies' financial position . . . While we need not embellish the point by raising the prospect of bankruptcy, it is well to remember that the Federal Government's Pension Benefit Guaranty Corporation, which provides *pension* guarantees for the employees and retirees of financially distressed companies, has no sister agency that provides the same guarantees for retiree *healthcare* benefits."[139] (emphasis in original)

CONCLUSION

Now that I've outlined what I see as three silver linings to the evolving approach to pensions and retiree medical benefits—financial separation of the funds from the company, more realistic expectations about the future, and a greater ability of the employer to compete effectively in the long-term—I feel that I must circle back to the dark clouds on the horizon that were mentioned earlier in this essay.

The real danger of the fast-approaching new system for retirement benefits is whether individual workers can and will do all of the right things to enable the new system to work for them. The "right things" in this case include a number of components, each of which is fraught with peril.

First, employees need to choose to participate in defined-contribution pension plans offered by their employers. Perhaps more employers will take advantage of the default opt-in approach that has been made easier by the PPA, but even that approach means that employees can still choose to opt out.

Second, those employees who do opt in need to put enough money into their defined-contribution plans to make retirement possible at a reasonable age. This invariably presents a challenge to the typical employee who is living paycheck to paycheck and cannot imagine having much money at the margin to put aside for the future. The sad irony is that at the time in employees' career when extra dollars would mean the most to the long-term growth of their pension funds, employees are at an age when they feel least able to put the money aside. It takes a discipline and a long-term view that many, if not most, young workers simply have not developed.

Third, employees need to make the right investment choices with the money that they do put into their pension accounts. What is the "right" choice depends in part on each individual's taste for risk, but there are certainly universal truths that

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[137] *Id.*
[138] *Id.*
[139] *Id.* at 632.

can sometimes be lost on the individual investor. Every worker, for example, should diversify their retirement portfolio against risks that can be diversified away. This means that you would not want to have a 401(k) that consists primarily or exclusively of your company's own stock, or any single stock, for that matter. Similarly, if you know that the money in your account won't be touched for at least 30 years, it makes little sense based on historical returns to invest in risk-free short-term vehicles rather than in the stock market.

Perhaps the darkest cloud on this new horizon, however, is the one that future retirees cannot fully plan around, no matter how wise or disciplined they are in their preparations. Here I refer to the risk of an overall bad market that affects the value of their defined-contribution plan, or the risk that health-care costs will increase at a greater rate than is anticipated. Under the old world, the employers bore those risks with their defined-benefit plans and blanket health-care promises for retirees; under the (brave?) new world, the individual retirees bear those risks.

Neither risk-bearer is ideal. When the employer bore all those risks, the end result was crippling legacy costs and broken promises. When the individual retiree bears those risks, the end result, one might imagine, will be either delayed retirements or retirees who have a lot less income or health care during their retirement than they ever imagined.

Is there a magic bullet here that can take the risk away from both sides? In a country with unlimited resources, I guess that's where a beefed-up social security and Medicare system could come in and save the day. But the truth is that we don't have unlimited resources, and far from expanding benefits, social security and Medicare have been struggling to maintain the levels of benefits that they have historically given.

In light of all those realities, perhaps the only safe advice for future retirees is to fasten your seatbelts and get ready for what promises to be an interesting, if somewhat bumpy, ride.