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ERISA@40: A Time for Reflection and a Time for Action



By JAMES A. KLEIN

Even for those who do not experience a full-fledged “mid-life crisis” at or around age 40, it is often a time when people take stock of where they are personally and professionally. Have they been successful? What changes are needed to meet their life’s objectives? In that same vein, the 40th anniversary of the Employee Retirement Income Security Act (ERISA) is an appropriate time to reflect on how the employee benefits system has evolved, and what changes may be appropriate.

With the Baby Boom generation recently entering or nearing retirement, the public is focused on retirement income adequacy as never before. This 40th anniversary also coincides with the effective date of the principal elements of the Patient Protection and Affordable Care Act (PPACA); and the employer-sponsored health coverage system is undeniably at a crossroads.

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In light of those realities, the American Benefits Council’s Policy Board of Directors embarked on a year-long endeavor to develop a blueprint for the future employee benefits system. We are unveiling it in conjunction with ERISA’s 40th anniversary and have called it “A 2020 Vision” since it sets the year 2020 as the date by when we must be clearly on a path to achieve certain goals.

The strategic policy is more than just a vision statement, however. It also contains 46 specific legislative and regulatory recommendations to help reach these goals.

It has been said that in hindsight, everyone has 20/20 vision. Looking back and reflecting on ERISA@40, may be helpful in placing a better future clearly in our sights.

A 2020 Vision. The four over-arching visions of the employee benefits system in 2020 are:

Personal Health and Financial Well-Being Will Be Benefit Plans’ Primary Objective. Health and retirement benefits will no longer be considered in separate silos. One manifestation of this will be a transition from “wellness,” focusing specifically on physical and mental health, to “well-being” which includes a health component as well as financial security both when actively employed and in retirement. It also embraces benefits

such as life, disability and long-term care, which are important to ensure personal financial security. Employer-sponsored plans will continue to be positioned to provide an efficient path to personal health and financial well-being, which maximizes employee productivity.

Global Competitiveness Will Dictate Benefit Design. Increasingly, employers will face global competitiveness and a mobile workforce in providing or facilitating employees' personal health and financial well-being. To maintain fidelity to their core business goals, employers will need to accommodate varying needs of their international workforce, navigate myriad laws that govern benefits and make benefit plan funding and administration more cost-effective.

Employers Will Have the Flexibility to Pursue a Range of Employee-Benefit Approaches. The benefits system will continue to be predicated on the principle that employers are best equipped to design, fund and implement benefit strategies to suit their workforces. Some strategies will involve a traditional approach in which employers closely manage plan funding and administration; others may empower individuals to take direct ownership of their benefits. This requires a legal and regulatory framework accommodating the continuum from traditional sponsor to facilitator.

Benefits Administration and Participation Will be Simple and Predictable. Since benefits are significant long-term investments, a stable environment is essential for efficient plan administration. Predictable tax and regulatory policy, simplified administrative compliance and reasonable protection from liability will uphold a vibrant future benefits structure. Large multi-state employers will need ERISA's federal framework to avoid or manage conflicting state and local laws. Since many people will need to plan for their personal health and financial well-being, public policy will foster transparent plan designs that leverage available technology while protecting privacy.

As I reflect on ERISA's first 40 years in the context of meeting the vision set forth above I believe there are six themes to consider as we contemplate a future employee benefits system that achieves ERISA's original objectives. These are:

- acknowledging the application of ERISA to health benefits;
- accommodating the changing role of individuals and employers;
- adopting a new paradigm for regulation of benefit plans;
- embracing new technology;
- balancing the "revenue" and "health and financial well-being" aspects of employee benefits policy; and
- cultivating employee benefits policy champions.

Application of ERISA to Health Benefits. Four decades after ERISA's enactment some still believe ERISA only applies to retirement policy. Perhaps that is understandable since the word "retirement" is included in the law's name and the word "health" is not.

While ERISA's application to health plans was never an afterthought, unquestionably it was various failures in the retirement system that provided the impetus for the law.

Even among those who are aware of ERISA's applicability to health benefits, the practice of interchangeably using the term "self-insured plan" and "ERISA plan" contributes to the false impression that ERISA has no relevance to insured health plans purchased in the marketplace.

If the steady development of laws, regulations and litigation regarding employer-sponsored health plans chipped away at incorrect assumptions about the law's scope, enactment in 2010 of the Patient Protection and Affordable Care Act should leave no doubt. As we embark on a new era in employer-sponsored health coverage, it is important to recognize how PPACA could set the stage for big tests for ERISA yet to come.

When ERISA was debated by Congress in the 1970s the provision prescribing federal preemption of state laws was deemed by some of its authors to be "the crown jewel" of the law. And for 40 years it has been essential for enabling employers to provide uniform benefits to employees wherever they live or work.

Also, because self-insuring relieves plan sponsors of certain legal requirements, some companies are considering self-insurance where they would not have before PPACA. This has caused some state legislators to pursue proposals restricting the ability of certain-size employers to purchase stop-loss reinsurance. This is an area where ERISA preemption will likely be challenged for the foreseeable future.

Other PPACA features appear destined to give rise to "proxy battles" over preemption. Tucked into the law is a little-noticed provision giving states, starting in 2017, the opportunity to seek State Innovation Waivers from the federal government so they can have greater flexibility in implementing the health care reform law. Potentially broad interpretations by the Secretaries of Treasury and Health and Human Services as the waiver program gets underway could result in states effectively eroding federal preemption without directly amending ERISA.

However, even if the waiver program does not have these negative consequences, PPACA presents potentially separate risks to preemption. The health reform law requires states to make important decisions (e.g., Medicaid expansion, establishing insurance marketplaces, rather than relying on a federal exchange, etc.). States might ask Congress for expanded authority (i.e., changes to ERISA preemption) as the *quid pro quo* for assuming more responsibility. It could prove attractive to members of Congress of both political parties to accommodate such requests; with corresponding challenges for plan sponsors and participants if that happens. Notwithstanding ERISA's origins as principally a pension law, some of the most significant future debates will likely arise in the health benefits context.

Individuals and Employers. ERISA put more definition on the responsibilities of the benefit system's stakeholders—most notably employers. Now at the 40-year mark and looking forward, it is clear that individuals and employers will remain the principal players in the system; although their roles are continually evolving.

Most noteworthy is the transition from defined benefit pensions to defined contribution retirement savings plans. While we know this intuitively, the actual statistics tell the story without need for further embellishment.

For plans with more than 100 participants, the number of defined benefit plans plunged from 20,035 in 1975 to 9,839 in 2011; while defined contribution plans over the same period leapt from 8,587 to 75,320. For plans with fewer than 100 participants, defined benefit plans dropped from 83,111 in 1975 to 35,418 in 2011, while the number of defined contribution plans rose from 199,161 to 563,070¹

The inexorable movement towards defined contribution plans changes the respective roles of employers and employees. To accommodate this trend, policy makers will need to accelerate their consideration of bold strategies that empower individuals to better prepare for retirement.

The Council's 2020 Vision calls for lowering the eligibility age to 45 for so-called "catch-up" contributions and increasing contribution limits as individuals assume a more prominent role in ensuring retirement income security.

Additionally, permitting advisers affiliated with plan investment offerings to provide advice (with appropriate conflicts of interest provisions to protect employees and fiduciary liability protections for employers) is another 2020 Vision recommendation reflecting the changed role of employers and individuals resulting from the continued trend from defined benefit to defined contribution plans.

This shift has been mirrored in the health-care arena as well. Health Savings Accounts (HSAs) first became available in 2004 and in 2014, 17.4 million people are enrolled in HSA-eligible High Deductible Health Plans (HDHPs)²

This trend underscores the imperative for greater transparency of specific data about the quality and costs of certain health services.

Apart from the defined benefit to defined contribution shift is PPACA's possible impact on employer-sponsorship of any type of coverage. Will exchanges create a marketplace where small employers that previously were not able to obtain coverage for their workers now will be able to do so? Will myriad PPACA requirements cause employers that currently sponsor a plan to drop them and pay the "employer responsibility" penalty? If exchanges create a more robust individual insurance marketplace, will employers cease offering coverage and direct workers to exchanges thereby transforming a largely employer-based health coverage system into an individually-based one? Inevitably, to some extent *all* of these results will occur within the health system and require significantly accommodating changed roles for individuals and employers.

One of the recommendations of the "2020 Vision" is to allow employers to contribute to Health Reimbursement Arrangements, or similar accounts, that employees could use to purchase coverage in public insurance exchanges. This could represent an approach that lies between the current predominant defined benefit model of employer-sponsored health coverage and a scenario whereby employers feel compelled to exit the system altogether.

One thing is clear: the defined benefit system that described the employer-sponsored pension and health

plan systems when ERISA was enacted has given way to an ever-expanding defined contribution model. But ERISA has not kept pace to enable employers to fully empower workers to discharge responsibilities they are increasingly called upon to assume.

Regulation of Benefit Plans. One of ERISA's successes is demonstrated each time workers and employers transfer large sums of money to a third party confident that it will be responsibly managed, prudently invested and will pay retirees benefits many decades into the future. That trust is based on the knowledge that if those to whom the funds are given are negligent or dishonest, a system exists to hold them accountable.

It is not a linguistic coincidence that the vehicle into which retirement assets are placed is called a "trust." That this system is largely self-policing is a tribute to how well it works the vast majority of the time. In that spirit, I propose that we consider adopting a new regulatory paradigm that involves even greater *trust* between regulators and the regulated community.

Plan sponsors and benefits practitioners have long decried ERISA's complexity. Even those who believe the rules are warranted, acknowledge it. In some respects the regulatory scheme is a by-product of the breakdown in trust between government and plan sponsors. This was perhaps most clearly evidenced in the 1986 pension nondiscrimination regulations that went from a relatively flexible "facts and circumstances" standard to more precise mechanical rules.

On one level, the rejection of the "facts and circumstances" approach was a response to complaints from plan sponsors themselves that interpretation and enforcement of those standards was inconsistent and arbitrary.³ On the other hand, more rigid standards represented regulators' lack of confidence that employers were designing plans fairly for participants of different income levels.

While it would be easy to attribute the pension system's structure to a breakdown in trust between the "regulators" and the "regulated," that, too, would be an oversimplification. The late Michael S. Gordon, one of the true fathers of ERISA, summed up the essential paradox of ERISA when he wrote about the law's "mandatory imposition of substantial regulatory standards on a totally voluntary system."⁴

The fact that many employers who are not required to sponsor a retirement or health plan (at least until the employer responsibility penalties of PPACA go into effect) continue to do so, *despite* costly and complex regulatory requirements, demonstrates the system's underlying strength. It also evidences employers' belief that benefit plans are important, despite the difficulty of maintaining them.

¹ U.S. Department of Labor "Private Pension Plan Bulletin Historical Tables and Graphs," (2013) pp. 7-8.

² America's Health Insurance Plans, Center for Policy and Research (2012). "Health Plans: Research Highlights."

³ "ERISA After 25 Years: A Framework for Evaluating Pension Reform," William G. Gale, John B. Shoven and Mark J. Warshawsky, *Benefits Quarterly*, Volume Fifteen, Number Four (1999) p. 78.

⁴ "Twenty-Fifth Anniversary Reflections on ERISA," Michael S. Gordon, *Benefits Quarterly*, Volume Fifteen, Number Four (1999) p. 6.

“It is not a linguistic coincidence that the vehicle into which retirement assets are placed is called a “trust.” That this system is largely self-policing is a tribute to how well it works the vast majority of the time.”

On the other hand, to the extent regulatory burdens are a principal reason employers choose not to sponsor a plan, the challenge is to forge a regulatory system that does not undermine their willingness to initiate or continue a plan.

How will this be accomplished? At the margins, legislative and regulatory relief could strip away some of the unnecessary layers of regulations. But to make meaningful progress toward a framework based less on meeting precise measurements, and more on basic concepts of fairness and equity, will require restored trust between regulators and the regulated community.

From the regulators’ perspective, this may require rules giving sponsors more flexibility in operating plans.

From the perspective of sponsors and service providers this may involve a willingness to accept greater penalties for failure to meet the more flexible standards that would be established.

In other words, the regulated community will be accorded more trust that they are designing and operating plans for the benefit of participants and beneficiaries within a broader framework of the enunciated public policy.

In return, regulators will be accorded more trust that they will enforce the law consistently and fairly within that more flexible framework; and they may be empowered to impose greater sanctions when actions taken are clearly inconsistent with the objectives of the underlying rule (i.e., abuse cases).

The “2020 Vision” spells out how a new paradigm might be achieved. One idea would be to develop an “exceptions-based” regulatory framework that targets sponsors with poor performance, rather than imposing burdens on all sponsors. A related approach would be adoption of “large business” exceptions to certain rules, rather than “small business” exceptions, since many rules are aimed at addressing real or perceived concerns related to small plan sponsors. Yet another specific example of a new paradigm would include eliminating retroactive adverse tax and ERISA consequences when the IRS or a court determines that the employer’s classification of a worker as “contingent” was incorrect but the employer made that determination in good faith.

The kind of flexible system described above would represent a significant departure from the status quo. But there are reasons for optimism that it could happen. More than a decade ago the IRS and Labor Department initiated programs in which pension plan sponsors are accorded more protections from sanctions if they volun-

tarily disclose various violations.⁵ Updates to that voluntary corrections framework were made as recently as 2013.⁶

One mechanism is the Self-Correction Program whereby plans may be corrected without formally requesting IRS approval. This program can be used to fix significant errors within two years and minor errors any time. Yet more could be done. For instance, the “2020 Vision” calls for greater ability to self-correct retirement plan loan errors. And compliance would be enhanced by eliminating the punitive nature of many correction rules, such as those applicable to pension automatic enrollment rule violations.

One possible confidence-building measure to develop a better regulatory paradigm might be to more fully engage parties with a legitimate stake in the outcome of regulations with one another in the development of regulations. Most rulemaking since ERISA’s enactment has involved the agencies’ inviting parties with an interest in the rules to provide written comments, to testify at public hearings and to directly discuss concerns with regulators. While the level of communication between the regulators and interested parties is excellent—one of ERISA’s true successes—the many disparate segments of the benefits system rarely engage in *simultaneous* discussions with one another and the regulators.

The Negotiated Rulemaking Act⁷ authorizes a process in which the views of multiple interested parties and regulators can be discussed together in developing regulations. Apart from some Pension Benefit Guaranty Corporation rulemaking, the negotiated rulemaking process has been rarely employed. Perhaps it should be tried on more occasions to see if an improved regulatory framework emerges. At a minimum, it might help interested parties more fully understand and accept the outcome of the rulemaking process. This approach, by itself, would not represent the reinvention of the regulatory paradigm; but could offer one possible tool for building it.

Embracing New Technology. Like the rest of us, ERISA’s authors may be forgiven for not anticipating today’s technology back in 1974.

But given ERISA’s numerous reporting and disclosure requirements, it certainly would serve the interests of participants and beneficiaries, plan sponsors and the regulatory agencies themselves, if ERISA’s regulations more fully embraced evolving communications technology.

While it may not be plan sponsors’ most significant ERISA compliance concern, certainly a very frequent complaint relates to the wasted time, effort and expense devoted to preparing printed and mailed materials that have little, if any, value for participants and beneficiaries.

To their credit, the Treasury and Labor departments have adopted policies to permit electronic notices in certain circumstances.

Unfortunately, those agencies have inconsistent policies for electronic notices. For example, Treasury regu-

⁵ Employee Plans Compliance Resolution System, Revenue Procedure 2003-44; Voluntary Fiduciary Correction Program, RIN 1210-AA76, March 28, 2002.

⁶ Revenue Procedure 2013-12 on Updates to Employee Plans Compliance Resolution System (03 PBD, 1/4/13).

⁷ 5 U.S.C. Sections 561-570.

lations allow electronic delivery if a participant has the “effective ability to access” electronic media. However, Labor rules allow a method whereby plan sponsors may use a secure website for posting benefit statements, if individuals are told how to access it, and that they may opt-out and receive paper statements at no cost.

Because procedures that may be adequate today will become outdated, the 2020 Vision calls upon the regulatory agencies to adopt standards to accommodate evolving technology. These include a “presumption of good faith” standard allowing employers to use technology as it becomes available, rather than waiting for regulatory approval.

We also urge adoption of a “least burdensome compliance” standard establishing that before promulgating new administration or reporting requirements, agencies would have to verify they are unable to achieve the objective in a manner that imposes fewer burdens on regulated parties, taking into account available technology.

The 2020 Vision also directs agencies to explore leveraging technology to obtain information from one another rather than requiring sponsors to report the same information to multiple agencies. The 2020 Vision provides that all of these expanded uses of technology be engaged with appropriate privacy safeguards.

If taken seriously by Congress and agencies, ERISA compliance can become more cost-effective and better serve participants and beneficiaries.

Balancing Different Aspects of Benefits Policy. Oversight and regulation of ERISA falls within the domain of the Senate and House of Representatives’ tax-writing and the labor committees and, correspondingly, the departments of Treasury and Labor. This dual structure reflects the fact that benefits policy is genuinely an amalgam of labor and tax policy. It is hard to envision a legal framework that would not include both dimensions. That said, were there a somewhat higher level of collaboration among the congressional committees of jurisdiction, oversight would be simpler and more consistent.

The agencies with enforcement responsibilities have generally avoided directly conflicting activities since the adoption of Reorganization Plan No. 4 in 1978;⁸ but multiple agency oversight has often created unnecessary duplication.

But the “tax” versus “labor” tension is not simply one of financial concerns versus fiduciary concerns. The more serious conflict over much of the past 40 years has been the tension between legislation enacted for revenue raising purposes, versus legislation enacted to advance benefits policy purposes.

Particularly throughout the 1980s and early 1990’s, many changes to pension law were enacted to address substantial federal budget deficits. Because these were principally revenue-driven efforts, there was not necessarily a strong underlying retirement income policy basis.

Moreover, much legislation designed to curtail the tax revenue loss attributable to pensions (e.g., TEFRA (1982), DEFRA (1984), TRA (1986), OBRA (1993))⁹ was

enacted intermittently between other legislation designed to shore up the funded status of pensions (e.g., SEPPA (1986), OBRA (1987)).¹⁰

This somewhat schizophrenic pattern exposed the absence of any coherent retirement income policy. But it also made evident the clash between tax policy that curtails the loss of revenue (by limiting pension contribution and benefit levels) and tax policy that protects benefits (by requiring stronger funding).

The problem was mitigated somewhat in the mid to late 1990s as the (temporary) transformation of budget deficits into surpluses eased efforts to enact frequent measures that curtailed the pension tax expenditure. In addition, the stronger economy in those years naturally led to better funded plans and less need for stricter funding standards.

Between 2012 and 2014, Congress enacted two highway trust fund reauthorization measures and the Bipartisan Budget Act, which either raised Pension Benefit Guaranty Corporation premiums or made changes to funding rules, or did both. Although Congress cited compelling policy reasons for doing so, unquestionably the combined \$43.6 billion in tax revenue raised was a significant reason those provisions were included in legislation that fundamentally did not relate to pension matters.

In fairness, the tax revenue versus benefits policy schism reaches beyond Congress.

Some have observed that different functions within plan sponsor organizations do not always work in harmony. The corporate model has been analogized to a car in which (1) the head of human resources is the driver, pressing the accelerator to provide generous benefits, (2) the chief financial officer is in the front passenger seat leaning over to apply the brakes and control costs, and (3) the company actuary is in the back seat, looking out the rear window giving directions.

Clearly, the development of corporate benefits policy often parallels how it is done within the legislative arena!

The tax expenditures associated with employer-sponsored health and retirement plans (\$1.1 trillion and \$649 billion, respectively, for Fiscal Year 2015)¹¹ are scored as the two largest in the federal budget.

Looking toward the future, continued large federal budget deficits and possible bipartisan interest in comprehensive tax reform could pose challenges for the tax-favored treatment of employer-sponsored benefits if lawmakers view the tax expenditure principally as a means to pay for other priorities. There is a risk they might focus on the *cost* of benefits rather than their *value* in ensuring Americans’ health and financial well-being.

⁸ 43 Fed. Reg. 47,713 (Oct. 17, 1978).

⁹ Tax Equity and Fiscal Responsibility Act of 1982; Deficit Reduction Act of 1984; Tax Reform Act of 1986; Omnibus Budget Reconciliation Act of 1993.

¹⁰ Single-Employer Pension Plan Amendments Act, which was part of the Consolidated Omnibus Budget Reconciliation Act of 1986; Omnibus Budget Reconciliation Act of 1997.

¹¹ U.S. Office of Management and Budget, Fiscal Year 2015 Analytical Perspectives, Table 14-3, p. 216.

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If policy makers from all the Congressional committees with jurisdiction over ERISA seize the opportunity to work in harmony, some important questions about future health and financial security can be asked and answered.

Cultivating Champions. Virtually every history of ERISA portrays the bipartisan statesmanship of the legislative leaders who crafted the law. They not only possessed vision about the need for a comprehensive law to regulate the benefits system but they also immersed themselves in the technical knowledge necessary to write the law.

Remarkably, despite the prominent role retirement plans play in our economy, the past 40 years has produced just a handful of members of Congress who could genuinely be called pension system champions.

And although health policy has been *the* single most debated domestic policy issue for at least the past five years—and about which virtually every elected official has strong opinions—we do not have enough of them who are fully conversant with much of the legal and legislative foundation of health policy.

This situation may be due to the difficulty of mastering what obviously is extremely complex subject matter. Another contributing factor may be the aforementioned focus on raising revenue, rather than benefits policy itself.

Whatever the reasons for the insufficient number of ERISA champions, it is hard to imagine that much positive policy will develop without more members of Congress willing to make understanding the issues their personal priority.

Four years after the enactment of PPACA national health policy is still unsettled. Although the next steps are difficult to predict, hopefully the continued debate will, at a minimum, lead more lawmakers to dedicate the time and effort required to understand the intersection of ERISA and health policy.

The dynamics in the pension context are different (and somewhat more encouraging), perhaps because there is less partisanship around retirement policy.

However, the shortage of pension legislative champions has resulted in the lack of a coherent national retirement income policy, nor even the articulation of the virtue of trying to have one. Developing a policy would be difficult even if there were widespread agreement that it should be done.

Whether the country should embark on the development of a national retirement income policy 40 years after the passage of ERISA deserves greater discussion. But I mention it only to make a different point. Congress’s willingness to frequently consider retirement legislation in the absence of a national policy against which such legislation might be measured, demonstrates that we in the benefits community have not yet done a sufficiently good job cultivating retirement policy champions.

The challenge ahead is for all who support a robust employer-sponsored benefits system to engage in a thoughtful dialogue with members of Congress from both parties. To enlist a larger group of policy champions who will be effective—regardless of the particular agenda they may wish to advocate—will require convincing future political leaders that it is worthwhile to learn the intricacies of ERISA.

In doing so, they will earn the respect of their congressional colleagues who will rely upon their judgment as retirement and health policy is crafted. It is a tall order but one that is definitely worth pursuing.