

# Introduction: The Significance and Complexity of ERISA

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## SYMPOSIUM

### THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974: LABOR LAW CONSIDERATIONS

#### INTRODUCTION: THE SIGNIFICANCE AND COMPLEXITY OF ERISA

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When the Employee Retirement Income Security Act of 1974 (ERISA)<sup>1</sup> was signed into law on Labor Day, 1974, only members of and staff assistants for congressional committees that had worked on the bill,<sup>2</sup> the representatives of federal agencies that had assisted in its passage, and those few professionals in the field who had watched closely the legislative process could have had a full understanding of the complexity of the bill being enacted or could have imagined its far-reaching implications. Full consideration of the complicated pension system existing in the private sector required more time to be expended on the legislation than had been expected. Congress was obliged to examine single-employer plans, multiemployer plans, defined-contribution plans, defined-benefit plans, and complicated systems designed to determine the reserves necessary to guarantee payments as pension benefits become due. To pass a workable bill, it became necessary to divide the administration of the Act between the Department of Labor and the Department of the Treasury,<sup>3</sup> to give a great amount of regulatory authority to the federal agencies chosen to administer the law,<sup>4</sup> to provide a myriad of special

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1. Pub. L. No. 93-406, 88 Stat. 829 [hereinafter cited as ERISA].

2. The four congressional committees involved were the House Education and Labor Committee, the House Ways and Means Committee, the Senate Labor and Public Welfare Committee, and the Senate Finance Committee.

3. See H.R. REP. No. 1280, 93d Cong., 2d Sess. 356 (1974).

4. *Id.* at 356-63.

provisions for special problem areas,<sup>5</sup> and to set several different effective dates.<sup>6</sup>

ERISA was enacted to protect individuals who failed to receive an anticipated pension because terms of the pension plan denied benefits to workers no longer employed by the company issuing the plan or because the company ended operations with inadequate funds set aside to pay promised benefits.<sup>7</sup> Congress also was concerned that large amounts of money in the hands of plan managers created a temptation for self-dealing and improper handling of these funds.<sup>8</sup> Among the provisions designed to achieve the purposes of the Act are expanded current reporting and disclosure provisions for all employee benefit plans covered by the Act,<sup>9</sup> standards of diligence and honesty applicable to those managing employee benefit plans,<sup>10</sup> minimum standards prohibiting the denial of certain earned pension benefits,<sup>11</sup> increased financing requirements for pension plans,<sup>12</sup> the establishment of an insurance program for the protection of guaranteed pension benefits in the event of a plan termination,<sup>13</sup> and a retirement scheme for employees who are not covered by a company plan.<sup>14</sup>

Although usually referred to as the Pension Reform Act because much of its content is exclusively concerned with pensions, the Act incorporates many provisions, including sections concerning fiduciary responsibility, reporting, and disclosure, that cover other types of employee benefit plans, such as welfare, vacation, and apprenticeship programs.<sup>15</sup> The practitioner in this field not only must acquaint himself with all the provisions of the Act, but also must patiently await regulations that are being promulgated as government agencies become adequately staffed and able to address the many subjects not considered completely in the Act. Naturally, such regulations will be subject to periodic change. Al-

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5. See H.R. REP. No. 807, 93d Cong., 2d Sess. (1974), in 1974 U.S. CODE CONG. & AD. NEWS 4672-76.

6. ERISA §§ 111, 211, 306, 414, 29 U.S.C.A. §§ 1031, 1061, 1086, 1114 (1975); ERISA §§ 1017, 1024, 1034 (codified in scattered sections of INT. REV. CODE OF 1954).

7. ERISA § 2(a), 29 U.S.C.A. § 1001(a) (1975).

8. See H.R. REP. No. 533, 93d Cong., 1st Sess. 4 (1973); S. REP. No. 127, 93d Cong., 1st Sess. (1973), in 1974 U.S. CODE CONG. & AD. NEWS 4864-71.

9. ERISA §§ 101-11, 29 U.S.C.A. §§ 1021-31 (1975).

10. *Id.* §§ 401-14, 29 U.S.C.A. §§ 1101-14.

11. *Id.* §§ 201-11, 29 U.S.C.A. §§ 1051-61.

12. *Id.* §§ 301-06, 29 U.S.C.A. §§ 1081-86.

13. *Id.* §§ 4001-82, 29 U.S.C.A. §§ 1301-81.

14. ERISA §§ 2001-08 (codified in scattered sections of INT. REV. CODE OF 1954).

15. ERISA §§ 3(1), 103(b)(1), 401, 29 U.S.C.A. §§ 1002, 1023(b)(1), 1101 (1975).

ready, reporting dates and forms originally established have been changed in the interest of making a rather complex law workable for the practitioner and helpful to the participant, the intended beneficiary of the new legislation.<sup>16</sup> Because of the broad scope of ERISA, the Act and regulations pursuant to it will effect repercussions throughout the field of labor law.<sup>17</sup>

### REPORTING AND DISCLOSURE

The reporting and disclosure provisions are an extension of the Welfare and Pension Plans Disclosure Act,<sup>18</sup> which required the filing of reports with the Department of Labor and the disclosure of certain information to plan participants.<sup>19</sup> The new law gives broad regulatory powers over reporting and disclosure to the Secretary of Labor. These powers have been exercised by altering reporting dates and forms, by exempting certain benefit funds from reporting and disclosure requirements, and by providing modified reports for certain classes of benefit funds.<sup>20</sup>

The right of an employee to know the status of his benefits lies behind reporting and disclosure. The original Welfare and Pension Plans Disclosure Act was adopted with this purpose in mind, but proved ineffective; unrealistic filing deadlines were missed with no repercussions and the Department of Labor was inadequately staffed to review the reports filed. For these reasons, ERISA effectuates substantial changes in filing dates and in the nature of the reports. The general thrust of the Act, with all its changes, indicates congressional intent that the reporting and disclosure provisions of the Act are to be followed to make these provisions effective devices to inform the employee of the benefits to which he is entitled and the condition of his benefit program.<sup>21</sup>

Included among the required reports are a description of the plan<sup>22</sup> and an annual report<sup>23</sup> to be filed with the Secretary of Labor,<sup>24</sup> who

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16. See Proposed Dept. of Labor Reg. §§ 2550.1-9, 39 Fed. Reg. 40853 (1974); 40 Fed. Reg. 19469, 20628, 21084 (1975).

17. See Fillion & Trebilcock, *The Duty To Bargain Under ERISA*, 17 WM. & MARY L. REV. 251 (1975).

18. Pub. L. No. 85-836, 72 Stat. 997 (1958).

19. *Id.* § 7.

20. See Proposed Dept. of Labor Reg. §§ 2520-23, 39 Fed. Reg. 42235-42 (1974).

21. H.R. REP. NO. 533, 93d Cong., 1st Sess. 8 (1973).

22. ERISA § 102, 29 U.S.C.A. § 1022 (1975).

23. *Id.* § 103, 29 U.S.C.A. § 1023.

24. *Id.* § 104(a) (1), 29 U.S.C.A. § 1024(a) (1).

has the authority to reject reports and to seek information in addition to that provided in the reports as filed.<sup>25</sup> In addition, the plan managers must make a summary plan description,<sup>26</sup> an annual report, and other materials available to participants and beneficiaries.<sup>27</sup> Disclosure requirements necessitate providing some of these reports directly and periodically<sup>28</sup> to the participants upon request,<sup>29</sup> as well as making these reports and other documents available at the plan office and other convenient locations.<sup>30</sup>

Of particular significance is the report informing employees of their pension rights, which must be delivered upon specific request.<sup>31</sup> This requirement obliges plan administrators to keep their records substantially current rather than rely upon a detailed verification of the work history of individual employees at the time benefits are requested. This latter practice has been particularly prevalent in multiemployer plans because of the complexities of securing detailed employment records, particularly for periods prior to the time that employers contributed into the fund on behalf of the employee.

#### FIDUCIARY RESPONSIBILITIES

Although trustees of trust funds are considered fiduciaries under the common law, the Act spells out this responsibility in much detail. Some of the specific features of the fiduciary standards of the Act are set forth below.

1. A fiduciary must discharge his duties for the exclusive purpose of providing benefits and defraying reasonable administrative expenses.<sup>32</sup>
2. Fiduciaries must perform in accordance with a federal prudent man standard, which requires the fiduciary to discharge his duties "with the care, skill, prudence, and diligence under the circum-

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25. *Id.* §§ 104(a)(2)(B), (a)(4), 29 U.S.C.A. §§ 1024(a)(2)(B), (a)(4).

26. *Id.* § 102, 29 U.S.C.A. § 1022.

27. *Id.* §§ 102(a), 103(a)(1)(A), 104(b), 29 U.S.C.A. §§ 1022(a), 1023(a)(1)(A), 1024(b).

28. *Id.* § 104(b), 29 U.S.C.A. § 1024(b).

29. *Id.* § 104(b)(4), 29 U.S.C.A. § 1024(b)(4).

30. *Id.* § 104(b)(2), 29 U.S.C.A. § 1024(b)(2). Further, the Department of Labor must make available reports filed with it at its exhibit room. *Id.* § 106, 29 U.S.C.A. § 1026.

31. *Id.* § 105(a), 29 U.S.C.A. § 1025(a).

32. *Id.* § 404(a)(1), 29 U.S.C.A. § 1104(a)(1).

stances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims . . . .”<sup>33</sup>

3. Fiduciaries must diversify their investments unless it is clearly prudent not to do so.<sup>34</sup>
4. Fiduciaries may delegate certain of their functions, including the investment of funds, to certain stipulated persons.<sup>35</sup>
5. Trustees are liable for breaches by cofiduciaries of which they had, or should have had, knowledge, unless a reasonable effort under the circumstances is made to remedy the breach.<sup>36</sup>
6. Fiduciaries are prohibited from self-dealing or participating in transactions with parties whose interests are adverse to the interests of the plan<sup>37</sup> except under the specific circumstances authorized in the Act.<sup>38</sup>
7. Although exculpatory clauses in plan documents are void, fiduciary responsibility insurance may be purchased from private carriers to cover trustee liability. Premiums to cover individual liability may be paid by the trustee or through the union, the appointing employer, or an employers' association.<sup>39</sup>
8. Fund documents must be amended to comply with specific provisions of this part of the Act. Upon application, exemptions to December 31, 1975, were granted for this process.<sup>40</sup>
9. Fiduciaries employed by participating employers or a participating union may not be compensated for their services but may be reimbursed for expenses actually incurred.<sup>41</sup> Regulations authorize per diem payments and the advancement of reasonable expense money.<sup>42</sup>

### VESTING

Vesting is required to insure that benefits will not be lost following a change of employment by an employee who has a reasonable employ-

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33. *Id.* § 404(a) (1) (B), 29 U.S.C.A. § 1104(a) (1) (B).

34. *Id.* § 404(a) (1) (C), 29 U.S.C.A. § 1104(a) (1) (C).

35. *Id.* § 405(c), 29 U.S.C.A. § 1105(c).

36. *Id.* § 405(a), 29 U.S.C.A. § 1105(a).

37. *Id.* § 406(b), 29 U.S.C.A. § 1106(b).

38. *Id.* § 408, 29 U.S.C.A. § 1108.

39. *Id.* § 410, 29 U.S.C.A. § 1110. See Gertner, *Trustee Liability Insurance Under ERISA*, 17 WM. & MARY L. REV. 233 (1975).

40. 29 C.F.R. § 2550.414b-1 (1975).

41. ERISA § 408(c) (2), 29 U.S.C.A. § 1108(c) (2) (1975).

42. Department of Labor ERISA Interp. Bull. 75-6, 40 FED. REG. 31755 (1975).

ment relationship with an employer.<sup>43</sup> Because the parties in Congress could not agree upon a single system of minimum vesting requirements, there is a choice of three:<sup>44</sup> 10-year vesting;<sup>45</sup> 15-year graded vesting;<sup>46</sup> and the rule of 45.<sup>47</sup> The vesting provisions of a particular plan can be more liberal than those provided.<sup>48</sup> Under the Act, a participant will receive a one year credit for 1,000 hours of employment in a year,<sup>49</sup> but he may suffer a break in service if he has less than 500 hours of credit in a year.<sup>50</sup> The Secretary of Labor has the task of defining the hours for which the participant will receive credit in order to satisfy these provisions.<sup>51</sup> The break-in-service rule is quite liberal: after an employee has suffered a break in service, if he subsequently accumulates 1,000 hours for another year of credit toward vesting, this may be added to his credited service prior to the break unless the employee has had consecutive years of break exceeding, or equal to, the credited years prior to the break.<sup>52</sup>

Of major significance is the provision that allows an employee to count all of his employment history with an employer, even if it is employment not covered by a particular plan.<sup>53</sup> An employer, for example, might have contributed to a multiemployer plan for a carpenter, who had worked several years as a carpenter and subsequently became part of management. For purposes of satisfying the adopted vesting rules of the carpenter's plan, his subsequent employment by the same employer will add years of accumulation for purposes of vesting even though it will not add years for the accumulation of benefits.

Under the Act, if pension benefits are to be paid in the form of an annuity, the plan must have the effect of a joint and survivor annuity, providing the surviving spouse with an annuity of at least 50 percent of the value of the annuity payable for the joint lives of the participant and his spouse,<sup>54</sup> unless the employee specifically declines this option.<sup>55</sup>

43. See H.R. REP. NO. 533, 93d Cong., 1st Sess. 5-6 (1973).

44. See H.R. REP. NO. 1280, 93d Cong., 2d Sess. 267-82 (1974).

45. ERISA § 203(a)(2)(A), 29 U.S.C.A. § 1053(a)(2)(A) (1975).

46. *Id.* § 203(a)(2)(B), 29 U.S.C.A. § 1053(a)(2)(B).

47. *Id.* § 203(a)(2)(C), 29 U.S.C.A. § 1053(a)(2)(C).

48. *Id.* § 203(d), 29 U.S.C.A. § 1053(d).

49. *Id.* § 203(b)(2)(A), 29 U.S.C.A. § 1053(b)(2)(A).

50. *Id.* § 203(b)(3), 29 U.S.C.A. § 1053(b)(3).

51. *Id.* § 202(a)(3), 29 U.S.C.A. § 1052(a)(3).

52. *Id.* § 203(b)(3), 29 U.S.C.A. § 1053(b)(3)..

53. *Id.* § 203(b)(1), 29 U.S.C.A. § 1053(b)(1).

54. *Id.* §§ 205(a), (g)(3), 29 U.S.C.A. §§ 1055(a), (g)(3).

55. *Id.* § 205(e), 29 U.S.C.A. § 1055(e).

There is also a provision requiring an employee to be given a reasonable period to elect a qualified joint and survivor annuity when he becomes eligible for early retirement.<sup>56</sup>

The Act also limits the circumstances under which payment of pension benefits, once started, may be suspended. Under a single-employer plan, payment may be suspended only if the employee returns to work with the same employer.<sup>57</sup> In a multiemployer plan, payment may be suspended only if the employee returns to work in the same industry, trade, or craft, within the same geographic area covered by the plan.<sup>58</sup>

### FUNDING

Before ERISA was passed it was necessary to fund a pension plan by setting aside the costs attributable to the current year plus the amount of interest due on any unfunded liability of the plan.<sup>59</sup> The new Act requires the unfunded liability of all plans in effect on January 1, 1974, to be amortized over a maximum period of 40 years.<sup>60</sup> Plans that come into existence after January 1, 1974, must be amortized over a maximum period of 30 years, although multiemployer plans are allowed 40 years.<sup>61</sup> Experience losses are to be amortized over 15 years in single employer plans and 20 years in multiemployer plans.<sup>62</sup>

In order to insure that funds will be available to pay vested benefits in the event of plan termination, the Act establishes the Pension Benefit Guaranty Corporation, a federal agency, to provide for the uninterrupted payment of pension benefits through maintenance of low-cost insurance for private plans.<sup>63</sup> The Act renders the employer liable to the Corporation for losses beyond the amount of the employer's regular contributions into the plan. In the event of a plan termination requiring the Pension Benefit Guaranty Corporation to pay out funds over and above the assets that are available in a pension plan, the Corporation will proceed against the employer or employers contributing to the plan, who will be required to contribute up to 30 percent of their net worth to re-

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56. *Id.* § 205(c)(1), 29 U.S.C.A. § 1055(c)(1).

57. *Id.* § 203(a)(3)(B)(i), 29 U.S.C.A. § 1053(a)(3)(B)(i).

58. *Id.* § 203(a)(3)(B)(ii), 29 U.S.C.A. § 1053(a)(3)(B)(ii).

59. See H.R. REP. NO. 533, 93d Cong., 1st Sess. 7 (1973).

60. ERISA § 302(b)(2)(B)(i), 29 U.S.C.A. § 1082(b)(2)(B)(i) (1975).

61. *Id.* § 302(b)(2)(B)(ii), 29 U.S.C.A. § 1082(b)(2)(B)(ii).

62. *Id.* § 302(b)(2)(B)(iv), 29 U.S.C.A. § 1082(b)(2)(B)(iv).

63. See H.R. REP. NO. 533, 93d Cong., 1st Sess. 14-15 (1973); ERISA § 4002(a), 29 U.S.C.A. § 1302(a) (1975).



imburse the Corporation for funds it has expended.<sup>64</sup> The Corporation is to create a program for employers who desire to purchase insurance to protect themselves against this contingent liability.<sup>65</sup> When this insurance program is established by the Corporation or through private carriers, premiums may be retroactive to the effective date of the Act; this feature may be desirable, however, inasmuch as the insurance coverage will not be effective until payments of premiums have been made by the employer for 60 months.<sup>66</sup>

Further extensions of contingent employer liability are present in the Act. An employer who is responsible for more than 10 percent of the contributions into a pension plan in two consecutive of the preceeding three years and who withdraws from the plan is required to ascertain whether there will be any amount due from the employer in the event the plan terminates. If such liability is determined, the withdrawing employer must place in escrow his proportionate share of the amount due, or furnish a bond equal to 150 percent of his share. These funds must remain available to insure payment of the employer's liability for five years before they will be released.<sup>67</sup>

Another significant innovation in the Act permits individuals to contribute tax-free funds to a pension plan. This contribution is limited to \$1,500 annually, and is applicable only if no pension plan is available to the employee through his employer.<sup>68</sup> This provision very well may portend a change of principle with respect to the source of pension funds; already there have been requests by employer representatives and others to make the concept of tax-free contributions by employees applicable to pension plans already established by companies.

#### MISCELLANEOUS PROVISIONS

A limitation is placed on benefits that may be provided by fixed-benefit plans and on contributions that may be made for fixed-contribution plans. In a defined-benefit plan the benefit must be the lesser of an annual benefit of \$75,000 or 100 percent of the individual's average compensation for the highest three years of pay.<sup>69</sup> In a defined-contribution plan,

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64. ERISA § 4062, 29 U.S.C.A. § 1362 (1975).

65. *Id.* § 4023(a), 29 U.S.C.A. § 1323(a).

66. *Id.* § 4023(d), 29 U.S.C.A. § 1323(d).

67. *Id.* § 4063, 29 U.S.C.A. § 1363.

68. *Id.* § 2002, INT. REV. CODE OF 1954, § 219.

69. *Id.* § 2004, INT. REV. CODE OF 1954, § 415(b)(1).

the maximum annual contribution is the lesser of \$25,000 or 25 percent of the employee's compensation.<sup>70</sup>

Under the principle of federal preemption, the Act supersedes state laws governing employee benefit plans.<sup>71</sup> The Act further specifically provides that a trust fund will not be considered an insurance company subject to state insurance regulations.<sup>72</sup> This is important to funds that self-insure health benefits, for attempts have been made to require that such benefits be provided through an insurance contract or that the trust itself be declared an insurance company.

The Act spells out a system of litigation by private parties using the federal court structure.<sup>73</sup> Because the courts are given discretion to award either party the costs of such actions, including attorney's fees,<sup>74</sup> litigation may be encouraged. Additionally, the Secretary of Labor may bring an action upon his own motion and has general authority to establish periodic investigations of benefit plans.<sup>75</sup> This provision resembles systems that some states have utilized in recent years.

#### CONCLUSION

ERISA is a long and complex Act, is very confusing in many instances, and is sometimes contradictory. The Secretary of Labor and the Secretary of the Treasury are granted broad powers under the Act; some parts of the Act, for example, are not operative until regulations are issued. Regulations needed to complete the legislation are being issued piecemeal and will continue to appear for some time. Further delays will be introduced by the requirement that many regulations be jointly approved by the Department of Labor and the Department of the Treasury. Early attempts at regulation have demonstrated the difficulty of the task and it is to be expected that regulations will be undergoing constant change.

Actions of the Secretary of Labor to police pension benefit plans will take two forms. First, the Secretary will undertake to investigate and control those aggravated situations that are brought to his attention. In time this likely will be followed by a national network of routine in-

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70. *Id.* § 2004, INT. REV. CODE OF 1954, § 415 (c) (1).

71. *Id.* § 514(a), 29 U.S.C.A. § 1144(a) (1975).

72. *Id.* §§ 514(b) (2) (A)-(B), 29 U.S.C.A. §§ 1144(b) (2) (A)-(B).

73. *Id.* § 502, 29 U.S.C.A. § 1132. See Donaldson, *The Use of Arbitration To Avoid Litigation Under ERISA*, 17 WM. & MARY L. REV. 215 (1975).

74. ERISA § 502(g), 29 U.S.C.A. § 1132(g) (1975).

75. *Id.* §§ 502(a), 504, 29 U.S.C.A. §§ 1132(a), 1134.

vestigations of all plans of significant size or character. Augmenting this administrative supervision will be suits brought by private litigants seeking redress, encouraged by eased litigation procedures and potential awards of attorney's fees.

The Act will have a major impact on trustee responsibilities, potentially reaching beyond the pension field. The establishment of a federal prudent man rule for employee benefit plan fiduciaries should set a national standard for the behavior of fiduciaries, although it will be some time before litigation will formulate a body of law that will control fiduciary activities. The power to delegate fiduciary responsibilities is clarified by the law and may relieve trustees of burdensome duties, particularly in the area of investment responsibilities. The treatment of prohibited transactions by fiduciaries and parties in interest will remain troublesome, however, until actions prohibited as detrimental to beneficiaries are clearly defined so that other transactions, favorable to beneficiaries, may continue.

ERISA is a new law, basic in its objectives, but complicated by its application to an extremely complex field. One result is the inclusion of lengthy and often confusing provisions that will be subjects of much regulation and will be potential targets for litigation. In the effort to acquire the knowledge and understanding of the Act essential for all practitioners, there is no substitute for careful reading of the Act in all its detail. Well-considered Articles like those included in this Symposium, however, can provide significant aid to the practitioner who finds himself in an old field with a new set of regulations.