

WORKERS IN TROUBLED FIRMS: WHEN ARE (SHOULD) THEY BE PROTECTED?

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I. INTRODUCTION

Workers are at special risk during corporate reorganizations, especially when a reorganization takes place during bankruptcy proceedings. The United States provides varying levels of legal protection against these risks. For example, workers tend to bear job and wage-related risks without much legal protection, while a relatively comprehensive government-sponsored insurance scheme absorbs much of the risk related to defined benefit pension plans. Compared to other industrialized countries, the protections in the United States tend to be fewer and less comprehensive.¹ Both of these general observations lead to interesting questions that will be addressed later in this Article. First, why are different types of worker interests protected differently in the United States? Second, what explains the different, and generally lower, levels of protection in the United States compared to other industrialized countries?

In the first section of this Article, I will describe the types of protections available to workers during corporate reorganizations in the United States. I will then discuss the two more general policy questions.

II. WORKER PROTECTIONS

In this section, I will explore the full range of protections available to workers during corporate reorganizations with respect to jobs, wages, unemployment compensation, health insurance, and pension benefits.

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1. See Richard N. Block et al., *Comparing and Quantifying Labor Standards in the United States and the European Union*, 19 INT'L J. COMP. LAB. L. & INDUS. REL. 441, 447 (2003), http://www.fu-berlin.de/iira2003/papers/track_3/Plenary_track_3_Block.pdf (comparing the level of governmental regulation of the workplace in the United States with the level of regulation in the European Union); Charles B. Craver, *The American Worker: Junior Partner in Success and Senior Partner in Failure*, 37 U.S.F. L. REV. 587, 595-603 (2003) (contrasting worker participation models in the United States with those in four other developed countries).

Sometimes, especially for troubled firms, these reorganizations occur as a part of bankruptcy proceedings. In the United States, however, the available protections for workers against the risks of corporate reorganizations rarely turn on whether the company is in bankruptcy. Thus, I will not limit my discussion to worker protections during bankruptcy. When bankruptcy affects the protections workers receive, that will be noted. This structure will provide a broader context within which to consider the American response to this issue.

Despite this broader focus, some basic information on American bankruptcy law seems appropriate. American bankruptcy law provides for two basic types of reorganizations for troubled firms. A Chapter 7 bankruptcy contemplates dissolution of the firm. When a firm files for bankruptcy under Chapter 7, all actions against the firm are consolidated before the bankruptcy court, the court appoints a trustee, and the trustee, under the court's supervision, manages the liquidation of all firm assets and the distribution of the proceeds to the firm's creditors.² A Chapter 11 bankruptcy contemplates relief from the immediate pressure of creditors and a court-supervised corporate reorganization, which permits the firm to emerge from the bankruptcy as a going concern.³

A. *Jobs*

American workers have few protections against job loss during corporate reorganizations. This is not surprising given that they have relatively few protections against job loss in any context.

Protection against job loss is roughly the same for non-union and union workers. For non-union workers, "employment at-will," a legal doctrine which permits discharge for any reason or no reason at all, has steadily eroded over the past thirty years.⁴ Congress has engrafted many limitations on the doctrine, most conspicuously through a variety of non-discrimination laws.⁵ In addition, courts in almost every state have adopted other limitations.⁶ These range from an increased willingness to enforce

2. See 11 U.S.C. §§ 701-784 (2000).

3. See 11 U.S.C. §§ 1101-1129 (2000).

4. See MARK A. ROTHSTEIN & LANCE LEIBMAN, *EMPLOYMENT LAW: CASES AND MATERIALS* 989-1090 (5th ed. 2003) (discussing the evolution of the "employment at-will" doctrine).

5. *E.g.*, Title VII of the Civil Rights Act of 1964 § 703, 42 U.S.C. § 2000e-2 (2000) (prohibiting discharge on the basis of race, color, religion, sex or national origin); Age Discrimination in Employment Act of 1967 (ADEA) § 4, 29 U.S.C. § 623 (2000) (prohibiting discharge on the basis of age for employees forty years of age and older); Americans with Disabilities Act of 1990 (ADA) § 102, 42 U.S.C. § 12112 (2000) (prohibiting discharge because of an individual's disability).

6. ROTHSTEIN & LEIBMAN, *supra* note 4, at 989-1090.

employment contracts to the recognition that tort law may prohibit certain types of discharges, such as a discharge because an employee refuses to commit perjury for the employer.⁷ Despite this, however, no court has held that job losses because of corporate restructuring fall within any of these general limitations on employment at-will. Therefore, with respect to corporate reorganizations, non-unionized American employees are still very much employees at-will.

For union workers, although collective bargaining contracts almost uniformly require employers to have “just cause” to discharge employees,⁸ those clauses are uniformly interpreted to permit discharges in response to economic circumstances.⁹ Economic circumstances are “just cause” to discharge an employee.¹⁰ As a general matter, then, since corporate reorganizations are responses to economic circumstances, collective bargaining agreements do not protect the jobs of unionized workers during corporate reorganizations.

In some circumstances, however, unionized workers may have bargained for stronger protections. In addition to a “just cause” discharge clause, a collective bargaining agreement may contain more specific job protections, such as notice provisions, limits on subcontracting, or even limits on plant closings or sales.¹¹ Explicit limits on major corporate reorganizations, however, are quite rare because they are normally outside the scope of subjects on which the parties must bargain.¹² It is not illegal

7. See STEVEN L. WILLBORN ET AL., *EMPLOYMENT LAW: CASES AND MATERIALS* 95-216 (3d ed. 2002) (discussing various contract, tort and good faith limitations on the employment at-will doctrine).

8. BUREAU OF NAT'L AFFAIRS, *BASIC PATTERNS IN UNION CONTRACTS* 7 (14th ed. 1995) (noting that ninety-seven percent of union contracts require cause or just cause for discharge).

9. See, e.g., *Losacco v. F.D. Rich Constr. Co.*, 992 F.2d 382, 384 (1st Cir. 1993) (holding that under Massachusetts law an employer has just cause to discharge an employee if the discharge is reasonably related to the economic needs of the business); *McCart v. J. Walter Thompson USA, Inc.*, 469 N.W.2d 284, 287 (Mich. 1991) (“bona fide economic reasons for discharge constitute ‘just cause’”).

10. See generally Roger I. Abrams & Dennis R. Nolan, *Toward a Theory of “Just Cause” in Employee Discipline Cases*, 1985 DUKE L.J. 594 (1985) (discussing the meaning of “just cause” in collective bargaining agreements).

11. See *UAW Leader Seeks to Ward Off Co-Pays, Auto Plant Closings in Detailing Goals*, 112 Daily Lab. Rep. (BNA) A-5 (June 11, 2002) (discussing UAW bargaining goal to renew moratorium on plant closings or sales contained in its current contract with the Big Three automakers); *UAW Members Ratify National Contract at American Axle, Mirroring Big Three Deals*, 47 Daily Lab. Rep. (BNA) A-9 (March 9, 2000) (discussing UAW ratification of a three-year collective bargaining agreement with limits on plant closings and sales).

12. Seventy-seven percent of union contracts contain no explicit limitations on the ability of employers to shutdown or relocate plants. *BASIC PATTERNS IN UNION CONTRACTS*, *supra* note 8, at 81. Even these clauses, however, seldom cover major reorganizations such as liquidations or sales of major divisions. Instead, they tend to be limited to issues such as

for a firm simply to refuse to discuss limits on major corporate restructuring during bargaining; it would be illegal for a union to insist on such limits, for example, to strike because a firm refuses to discuss or agree to a clause limiting major corporate restructuring.¹³ Even if a union overcomes this hurdle and succeeds in inserting limits on corporate reorganizations in a collective bargaining agreement, these limits could be overridden if the firm enters into bankruptcy.

Finally, both unionized and non-unionized workers have indirect job protections through the Worker Adjustment and Retraining Notification (WARN) Act,¹⁴ which requires employers with one hundred or more employees to give at least sixty days advance notice before a plant closing or mass layoff.¹⁵ The Act defines a plant closing as “the permanent or temporary shutdown of a single site of employment . . . [that] results in an employment loss . . . during any 30-day period for 50 or more employees”¹⁶ A “mass layoff” is defined as a reduction in force, other than a plant closing, that causes five hundred employees to lose their jobs or, if the employer has less than 1,500 employees, causes one-third of the workforce and at least fifty employees to lose their jobs.¹⁷ Several points about the WARN Act in the context of corporate restructurings are worth mentioning. First, corporate restructurings that involve lower wages and benefits, but job losses below the WARN Act thresholds, are not covered. For example, if a company sells its business to another business which continues to employ virtually all the workers, but at significantly lower wages and benefits, the WARN Act is not implicated.¹⁸ Second, if a

notice and transfer rights. *Id.*

13. *Cf.* *First Nat'l Maint. Corp. v. NLRB*, 452 U.S. 666, 686 (1981) (holding that bargaining over management decisions of whether to shut down for purely economic reasons is not mandatory). *But cf.* *United Food & Commercial Workers Int'l Union, Local No. 150-A v. NLRB*, 1 F.3d 24, 33 (D.C. Cir. 1993) (holding that relocation may be a mandatory subject of bargaining). The exception here is that limits on restructuring that turn on labor costs are within the scope of subjects on which the parties must bargain. In *First Nat'l*, the Court carefully limited its holding to the facts of the case, specifically distinguishing the case from *Fibreboard Paper Products Corp. v. NLRB*, 379 U.S. 203 (1964). *First Nat'l Maint. Corp.*, 452 U.S. at 687-88. In *Fibreboard*, the Court held that the employer's decision to restructure by subcontracting for maintenance work previously done by union employees was a subject of mandatory bargaining. 379 U.S. at 215. Thus, although the dividing line is not entirely clear, the parties must bargain about limits on restructuring when the restructuring is driven by labor costs, but not on restructuring caused by other factors, such as changes in product markets or the firm's capital investment strategies.

14. 29 U.S.C. §§ 2101-2109 (2000).

15. 29 U.S.C. § 2102.

16. 29 U.S.C. § 2101(a)(2).

17. 29 U.S.C. § 2101(a)(3).

18. *Int'l Alliance of Theatrical & Stage Employees v. Compact Video Servs., Inc.*, 50 F.3d 1464, 1469 (9th Cir. 1995) (holding that the sale of a business is not an action covered

restructuring involves a Chapter 7 dissolution without proper notice, the Act provides no effective remedies. Courts are not authorized by the Act to enjoin plant closings or mass layoffs. Instead, they only have authority to award backpay, benefits, and attorneys' fees.¹⁹ Under Chapter 7, the priority for such an award means that a violating firm would almost never have to pay such a judgment.²⁰ Finally, and most significantly, the WARN Act provides no job protections. It only requires that employers give notice of likely job losses. Thus, the Act is fully within the principal American approach to job loss: the best solution to job loss is to facilitate smooth, easy, and quick re-employment with another employer, rather than to impose inflexible obligations on the former employer.

B. Wages

On wages, we used to think about two distinct worker interests. First, there is the interest in payment for work already performed. Second, there is the interest in not having one's future wages reduced. American workers have some protection for the former interest but only very limited protection for the latter interest.

Wage payment statutes in every state provide some protection for the workers' interests in payment for work already performed. In general, these statutes require employers to pay for labor within a relatively short period of time after the work is performed, usually within thirty days.²¹ Thus, the general exposure of workers to this type of risk is limited because the amount of unpaid wages is kept relatively low.

A corporate reorganization usually will not affect a firm's liability for unpaid wages. Even after a reorganization, the firm will continue to be liable under wage payment statutes for the entire amount of any unpaid wages.²² However, the situation may be different when a firm enters bankruptcy. Wages earned prior to the filing of bankruptcy are unsecured claims entitled only to third priority under American bankruptcy law.²³

by the WARN Act).

19. 29 U.S.C. § 2104(a).

20. See *In re Trans World Airlines, Inc.*, 322 F.3d 283, 292 (3d Cir. 2003) (noting that "in the context of a bankruptcy, [employee suits] are, by their nature, general unsecured claims and, as such, are accorded low priority").

21. See, e.g., STEVEN L. WILLBORN ET AL., *EMPLOYMENT LAW: SELECTED FEDERAL AND STATE STATUTES* 146-61 (2002) (providing examples of several state wage payment statutes).

22. See generally Emmanuel S. Tipon, Annotation, *Validity, Construction, and Effect of State Laws Requiring Payment of Wages on Resignation of Employee Immediately or Within Specified Period*, 11 A.L.R. 5TH 715, 743-809 (1993) (discussing the construction and application of state wage payment statutes, including circumstances affecting the right of former employees to recover under such statutes).

23. 11 U.S.C. § 507(a)(3) (2000).

This may, and generally does, mean that the company will first run out of money. Even if it does not, each employee is only entitled to a maximum of \$4,925²⁴ and only for work performed within ninety days before the filing of the bankruptcy petition.²⁵ Thus, workers may suffer some losses in the form of non-payment for services already rendered when a firm enters bankruptcy. However, the wage payment statutes, which generally require wages to be paid soon after they are earned, tend to limit these losses.²⁶

The second worker interest is in not having future wages reduced because of corporate restructuring. With respect to this interest there are considerable differences between union and non-union workers and, for union workers, between bankruptcy and non-bankruptcy restructuring.

For non-union workers, the legal protections against wage reductions during corporate restructuring, or at any time for that matter, are very limited. The only protection is provided by the minimum wage laws. An employer cannot reduce wages to a level below the minimum wage laws. But this protection is minimal because American minimum wage laws govern wages at such a low level that they affect few workers.²⁷ As with employment status for at-will employees, employers can simply reduce wages for any reason or no reason. There are, however, very strong customs against wage reductions.²⁸ Nevertheless, a reorganization, including one under Chapter 11 of the bankruptcy laws, may provide license to violate these strong customs and reduce wages.

For unionized workers governed by a collective bargaining agreement, firms are required to pay the promised wage for as long as the agreement remains in force. However, for corporate reorganizations outside of bankruptcy the collective bargaining agreement generally does not survive

24. This amount became effective April 1, 2004, and was the amount in effect at the time of publication. The amount is subject to change by the Judicial Conference of the United States.

25. 11 U.S.C. § 507(a)(3)(B) (2000). Wages earned after the bankruptcy filing are allowed to be paid as administrative expenses. 11 U.S.C. § 503(b)(1)(A) (2000).

26. See WILLBORN ET AL., *supra* note 21, at 146-61 (listing state wage payment statutes, all of which require wages to be paid within a short period after they are earned).

27. For most workers, the minimum wage in the United States is \$5.15 per hour. Fair Labor Standards Act (FLSA) of 1938 § 6(a)(1), 29 U.S.C. § 206(a)(1) (2000). However, some states and localities provide higher minimum wages. Cf. NAT'L ECON. COUNCIL, *THE MINIMUM WAGE: INCREASING THE REWARD FOR WORK* 5, 6 (2000), at <http://clinton4.nara.gov/media/pdf/minwagereport000208.pdf> (last visited Nov. 21, 2004) (stating that in 1999, fewer than five percent of all workers were paid at or below the minimum wage).

28. See Edward B. Rock & Michael L. Wachter, *The Enforceability of Norms and the Employment Relationship*, 144 U. PA. L. REV. 1913, 1925 (1996) (noting that firms are more likely to lay off employees than to lower wage rates).

the reorganization.²⁹ For example, if a plant is sold as a sale of assets from Corporation A to Corporation B and continues to operate as it did before the sale with the same equipment and most of the same employees, Corporation B is not bound by any provisions of the collective bargaining agreement entered into between Corporation A and its workers, including the wage provisions.³⁰

Bankruptcy exposes workers to an even greater risk that their contractually promised wages will be reduced. Outside of bankruptcy, it is clear that the contracting firm itself (as opposed to any successor through corporate reorganization) must continue to pay the wages it has promised in a collective bargaining agreement for the duration of the agreement.³¹ If a firm enters bankruptcy, however, it can apply to the court for relief from any of the terms of a collective bargaining agreement, including wage provisions.

To escape a collective bargaining agreement, the firm must satisfy both procedural and substantive requirements. Procedurally, the firm must make a proposal to the union to modify the agreement, provide the union with sufficient information to evaluate the proposal, and meet with the union in good faith and at reasonable times to attempt to reach agreement on the modifications.³² If an agreement cannot be reached the firm may apply to the court for rejection of the collective bargaining agreement. The court should approve the application if the union has refused to accept the proposals without good cause and the balance of equities clearly favors rejecting the agreement.³³ Absent bankruptcy, the union could reject any attempts by the firm to modify the agreement during its term.³⁴

29. *NLRB v. Burns Int'l Sec. Servs. Inc.*, 406 U.S. 272, 281-82 (1972). For a more general discussion of a successor's labor obligations and liabilities, see Paul E. Starkman, *Mergers & Acquisitions: A Checklist of Employment Issues*, 13 DEPAUL BUS. L.J. 47 (2000-2001).

30. *See Fall River Dyeing & Finishing Corp. v. NLRB*, 482 U.S. 27, 42 (1987) (holding, under similar facts, that the successor company was not bound by the terms of the collective bargaining agreement entered into by the predecessor company and its employees). The rules governing whether the collective bargaining agreement continues to apply are different and more stringent than the rules governing whether the union continues to represent the workers after a corporate reorganization. *Fall River* held that the successor employer had to bargain with the union, even though it was not bound by the terms of the predecessor's contract. *Id.*

31. *See* National Labor Relations Act (NLRA) § 8(d), 29 U.S.C. § 158(d) (2000) (declaring absent union agreement, it is a violation of the Act to change the terms or conditions of a labor agreement prior to its expiration date). *See also* *NLRB v. Katz*, 369 U.S. 736, 747 (1962) (upholding a finding by the National Labor Relations Board that an employer violated the National Labor Relations Act by making unilateral changes to the terms and conditions of employment during negotiations with the union).

32. 29 U.S.C. § 1113(b) (2000).

33. 11 U.S.C. § 1113(c) (2000).

34. *See* NLRA § 8(d), 29 U.S.C. § 158(d) (pronouncing that if an employer proposes to

This ability to reduce wage rates is sometimes a major reason firms enter bankruptcy. For example, in the 2002 United Airlines filing, the firm attempted to negotiate with unions to reduce wage rates to avoid a bankruptcy filing.³⁵ When it was unable to do so, it filed for bankruptcy. A primary goal of its bankruptcy filing was to obtain judicial relief from its labor contracts, and it was able to persuade the bankruptcy court that that was necessary.³⁶

In sum, workers have only limited protection for their wages. In bankruptcy, workers may lose some of their wages for work already performed. Moreover, their interest in not having their wages reduced is also in jeopardy. Non-union workers have almost no protection of this interest, while bankruptcy law explicitly permits firms to override protections of this interest that unionized workers have won through collective bargaining.

C. *Unemployment Compensation*

Every state provides unemployment compensation for workers who lose their jobs.³⁷ This is not a “job” protection because it does not directly limit an employer’s ability to dismiss employees.³⁸ Nor is it a “wage” protection because these statutes protect neither of the employee interests in wages discussed in the preceding section. Nevertheless, as will be discussed in Part III *infra*, this is the primary protection in the United States for job and wage losses during corporate reorganizations.

Unemployment compensation requires employers to pay benefits to workers who lose their jobs because of corporate reorganizations.³⁹ The benefits are generally equal to about half the worker’s salary and are

modify the agreement, the union is not required to “discuss or agree to any modification of the terms and conditions contained in a contract for a fixed period, if such modification is to become effective before such terms and conditions can be reopened under the provisions of the contract”).

35. Michael Bologna, Judge Grants United Airlines’ Motion to Cut Wages of IAM-Represented Employees, *Bankr. L. Daily (BNA)* (Jan. 13, 2003).

36. *Id.*

37. For a general discussion of the state-based unemployment compensation systems, see WILLBORN ET AL., *supra* note 7, at 685-723.

38. Unemployment compensation sometimes protects jobs indirectly by limiting the benefits employers receive from layoffs. When large, economically viable firms dismiss workers who are entitled to unemployment compensation, they immediately lose all of the workers’ labor. However, they only avoid a portion of their wages because they are often responsible for contributing to the dismissed worker’s unemployment compensation.

39. See generally Gillian Lester, *Unemployment Insurance and Wealth Redistribution*, 49 *UCLA L. REV.* 335, 344-58 (2001) (describing eligibility requirements and disqualification standards for state unemployment compensation programs).

available for about six months.⁴⁰ Unemployment benefits are highly targeted to active members of the labor force. In general, to be eligible for benefits workers must have demonstrated substantial prior commitment to the labor force, they must continue to seek employment, and they must not have left their prior job on their own volition or lost it because of misconduct.⁴¹

The payment system for these benefits means that workers will generally receive them even if their employer goes bankrupt. The payments are made by the state from a pool created by unemployment taxes imposed on employers. Thus, even if an employer goes bankrupt and cannot contribute to the pool anymore, its workers would be entitled to receive unemployment compensation benefits.⁴²

D. Health Insurance

Most non-elderly people in the United States obtain their health insurance through their employers. Of those with private health insurance, approximately ninety-one percent receive their coverage through an employment-based health plan.⁴³ Viewed another way, sixty-six percent of all non-elderly Americans receive health insurance through their employer, eighteen percent are uninsured, and the remainder are insured under government programs or non-employer private plans.⁴⁴ The elderly receive health insurance through Medicare, a government program.⁴⁵ Thus, an important interest at stake in corporate reorganizations is continued health insurance coverage.

There are two important federal laws protecting employee interests in continued health insurance coverage. The Consolidated Omnibus Budget Reconciliation Act of 1986 (COBRA)⁴⁶ requires employers who offer health insurance to continue to provide coverage for eighteen to thirty-six

40. WILLBORN ET AL., *supra* note 7, at 690. Benefits are capped at amounts that vary by state. As a result, some high-income workers receive benefits equal to less than half of their wages. Because of this cap on benefits, average unemployment benefits replace only about one-third of prior wages. *Id.*

41. *Id.* at 705-07.

42. For a general description of the system for financing unemployment benefits, see *id.* at 688-91.

43. PAUL FRONSTIN, EMPLOYMENT-BASED HEALTH BENEFITS: TRENDS AND OUTLOOK 4 (Employee Benefit Research Inst., Issue Brief No. 233, 2001) (citing statistics for 1999).

44. *Id.*

45. 42 U.S.C. §§ 1395 *et seq.*

46. Pub. L. No. 99-272, 100 Stat. 82 (codified as amended in scattered titles of U.S.C.). The portions of COBRA relevant for the purposes of this Article are contained within a broader section of the federal statutes designed to protect worker interests in pensions and health insurance, the Employee Retirement Income Security Act (ERISA), 29 U.S.C. §§ 1001-1461 (2000).

months from the time of an event (such as a job termination) that results in a loss of coverage.⁴⁷ Even though COBRA requires employers to offer this continuation coverage, it requires the employee to pay for it.⁴⁸ Thus, COBRA looks to the “old” employer to provide continued coverage in order to give the employee time to find new coverage either with another employer or in the individual insurance market.

The Health Insurance Portability and Accountability Act of 1996 (HIPAA)⁴⁹ provides another type of protection by looking forward to a new employer instead of backward to the old employer. One of the problems with continued health insurance coverage prior to HIPAA was that new employers required waiting periods before health insurance would become effective and preexisting conditions would often be excluded from coverage. Thus, workers between jobs would often have a temporary gap in coverage for all health insurance needs and a permanent gap in coverage for specific, high-need problems.⁵⁰ For workers who have had jobs previously, HIPAA generally prohibits new employers from imposing waiting periods or limits on coverage for pre-existing conditions.⁵¹

Let’s consider how these laws apply to firms in financial distress. First, consider a non-union firm. The firm can discontinue its health insurance any time it wants to. No law requires an employer to provide health insurance or to continue it.⁵² Neither COBRA nor HIPAA provides any protection for employees of a firm in this situation. COBRA only requires employers who offer health insurance to provide COBRA continuation coverage.⁵³ Thus, once the employer no longer offers health insurance, it does not have to make the offer of COBRA continuation coverage. Further, HIPAA does not provide any protection to workers who stay with the firm after health coverage is discontinued. If a worker leaves the firm to work at another firm, the second firm would be required to provide immediate and full coverage under HIPAA, assuming the new firm

47. 29 U.S.C. § 1162(2)(A).

48. Employees are required to pay roughly the full average cost of the insurance for other employees. 29 U.S.C. § 1164(1). This usually seems high to the terminated employee, because employers typically cover most of this cost while the employee is working. As a result, COBRA suffers from a relatively severe adverse selection problem, because healthy workers turn down the coverage while sicker ones accept it.

49. Pub. L. No. 104-191, 110 Stat. 1936 (codified as amended in scattered titles of U.S.C.). The portions of HIPAA relevant for the purposes of this Article are contained within ERISA. 29 U.S.C. §§ 1181-1182.

50. See WILLBORN ET AL., *supra* note 7, at 843-45.

51. 29 U.S.C. § 1181.

52. A non-union firm can bind itself contractually to provide health insurance for a certain period of time. As a general matter, however, firms are very careful to avoid these types of promises. Workers generally lose lawsuits in which they claim that non-union firms are contractually required to continue health insurance coverage.

53. 29 U.S.C. § 1161 (2000).

offered health insurance to its employees.⁵⁴ However, HIPAA does not look back and require any coverage by the old firm.

On the other hand, consider a situation where a financially distressed firm decides to divest an unprofitable division. In this situation, if either the old firm or the new firm offers health insurance, workers of the divested division will have at least some continued health insurance coverage. If the old firm continues to offer health insurance, but the new firm does not, workers would be entitled to COBRA continuation coverage with the old firm.⁵⁵ If the old firm terminates its coverage, but the new firm offers coverage, the workers would be entitled to immediate, full enrollment in the new firm's health insurance plan under HIPAA.⁵⁶

If the financially distressed firm is unionized, it is likely to have a collective bargaining agreement that requires it to continue to provide health insurance for the duration of the agreement.⁵⁷ Thus, unionized employees are better off than non-unionized employees because their health insurance plan is generally part of an enforceable collective bargaining agreement. However, bankruptcy provides a route for a financially distressed firm to avoid that promise. In this instance, the same rules as discussed in Part B *supra* would apply for the firm to be able to abandon this promise. That is the firm must apply to the court for relief and satisfy both the procedural and substantive requirements embodied in the statute.

A very interesting provision of the bankruptcy code provides special protections for the health benefits of retired employees. Outside of bankruptcy, employers have been quite successful at terminating programs providing health benefits for retired employees, albeit not without some struggles.⁵⁸ However, once a firm has filed for bankruptcy under Chapter 11 it can terminate its retiree health plan only if it meets the standards for rejecting a collective bargaining agreement.⁵⁹ This is true even if the firm could have freely terminated the plan outside of bankruptcy.⁶⁰ Moreover,

54. 29 U.S.C. § 1181.

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56. 29 U.S.C. § 1181.

57. Seventy percent of collective bargaining agreements provide comprehensive medical insurance. BASIC PATTERNS IN UNION CONTRACTS, *supra* note 8, at 13.

58. *Compare Sprague v. Gen. Motors Corp.*, 133 F.3d 388, 404 (6th Cir. 1998) (en banc) (holding that the employer had the right to terminate its retiree health program despite any bilateral agreements to the contrary made between the company's officers and individual employees), *with Stearns v. NCR Corp.*, 97 F. Supp. 2d 954, 965 (D. Minn. 2000) (holding that bilateral contracts entered into at retirement were enforceable and provided lifetime benefits).

59. 11 U.S.C. § 1114.

60. See generally Susan J. Stabile, *Protecting Retiree Medical Benefits in Bankruptcy: The Scope of Section 1114 of the Bankruptcy Code*, 14 CARDOZO L. REV. 1911, 1912-14, 1926-29 (1993) (discussing the statutory barriers faced by bankrupt firms seeking to

meeting these requirements is more difficult than meeting the requirements for rejecting a collective bargaining agreement, even though the procedural and substantive standards are the same. With a collective bargaining agreement, the firm at least knows with whom it must bargain. For retiree health insurance, a difficult first step is often finding the right representative for the group of retirees.⁶¹

E. Pensions

Employer-sponsored pensions fall into two broad groups: defined contribution plans and defined benefit plans. Defined benefit plans present more problems when firms become financially distressed, but also provide more flexibility when implementing corporate reorganization strategies. However, recent events in the United States have shown that there are also flaws in protections for participants in defined contribution plans.

Defined contribution plans, in essence, are simple promises by the firm to each employee to pay a certain amount into individual accounts, to be held and invested for retirement.⁶² The plans are relatively straightforward: the firm's principal promise is to put the money into a worker's individual account at roughly the same time as the work is performed (so few risks arise from delayed payments),⁶³ and the firm bears no responsibility for ensuring that the amount in the account will be sufficient when the worker retires.⁶⁴ The worker absorbs the risk that the investments held in the account may not be favorable and that there might not be enough in the account to support a decent living at the time of retirement.

As a general matter, worker interests in defined contribution plans are not affected by corporate reorganizations or bankruptcy. If the corporation reorganizes or goes bankrupt, the firm may cease to make contributions to

terminate retiree medical benefit plans).

61. *Cf.* *Allied Chem. & Alkali Workers, Local Union No. 1 v. Pittsburgh Plate Glass Co.*, 404 U.S. 157, 172 (1971) (upholding a determination that a union representing active employees was not the proper representative of retired employees).

62. 29 U.S.C. § 1002(34). *See generally* JOHN H. LANGBEIN & BRUCE A. WOLK, *PENSION AND EMPLOYEE BENEFIT LAW* 47-55 (3d ed. 2000) (discussing the varieties of defined contribution plans).

63. 29 C.F.R. § 2510.3-102(a)-(b) (2004) (employers must deposit amounts from salary deferrals into employee 401(k) accounts within fifteen days of end of month, thirty days for SIMPLE IRA accounts).

64. Normally, one would expect workers to prefer to be paid cash rather than to have the same amount put into an account which they cannot easily access until years later in retirement. Tax advantages are the principal reason for utilizing a defined contribution retirement account. *See* WILLBORN, ET AL., *supra* note 7, at 736-39 (explaining the tax advantages and other benefits of employing a defined contribution retirement account).

the plan (just as it may stop making wage payments),⁶⁵ but the money already in the accounts would be unaffected.⁶⁶

However, the recent highly publicized Enron bankruptcy exposed some exceptions to this general rule.⁶⁷ There were two problems with the defined contribution plans set up for Enron employees. First, the plans were heavily invested in Enron stock.⁶⁸ This is not uncommon,⁶⁹ even though it is a very bad idea for workers.⁷⁰ Second, at the precise time Enron stock was falling steeply, workers were unable to sell the stock in their pension portfolios.⁷¹ Pension law permits plans to suspend transactions during administrative changeovers, and Enron fit into that exception during the period when its stock was rapidly declining in value.⁷² As a formal matter, workers' pension accounts were not hurt by the Enron bankruptcy. All they were promised was that Enron would make contributions to their pension accounts, which the company did. Everyone knew that the risk of investment gains and losses in the accounts fell on the workers. Thus, workers were not "hurt" by the losses: instead, they merely suffered loss from a risk to which they always knew they were exposed. However, as a practical matter, because of the nature of the investments in the accounts and the limits on transactions, workers suffered significant

65. Sometimes a collective bargaining agreement requires the firm to continue to make payments into the defined contribution plan for some period of time. Such a promise can be avoided only if the firm goes through the steps discussed in Section B *supra* for relief from the terms of a collective bargaining agreement.

66. Cf. 29 U.S.C. § 1104 (listing fiduciary duties of fiduciaries of pension funds); *Donovan v. Bierwirth*, 680 F.2d 263, 271 (2d Cir. 1982) (noting that trustees of pension funds must make all decisions with "an eye single to the interests of the participants and beneficiaries").

67. See Sharon Reece, *Enron: The Final Straw & How to Build Pensions of Brick*, 41 DUQ. L. REV. 69, 89-115 (2002) (describing the implications of the Enron bankruptcy for the company's pension plans).

68. See *id.* at 92 (noting that sixty-seven percent of the plans' assets were invested in Enron stock).

69. Employer stock comprises nineteen percent of all 401(K) plan assets and, obviously, a much larger proportion in some major plans. John H. Langbein, *What's Wrong with Employer Stock Pension Plans*, in ENRON: CORPORATE FIASCOS AND THEIR IMPLICATIONS 487, 491 (Nancy B. Rapoport & Bala G. Dharan, eds., 2004). For example, in January 2000, Proctor & Gamble had a defined contribution plan with ninety-six percent of the plan assets invested in employer stock, Pfizer had one with eighty-eight percent invested in employer stock, and Abbot Laboratories had one with eighty-seven percent so invested. *Id.*

70. *Id.* at 491 ("A pension fund portfolio holding a massive part of its assets in any one stock is bad; but holding such a concentration in the stock of the employer is worse. . . . The simple reason is that the employee is already horribly underdiversified by having his or her human capital tied up with the employer.").

71. See Reece, *supra* note 67, at 95-96 (discussing the transaction lockout period during which no participant transactions are allowed).

72. The value of Enron's stock plummeted thirty-five percent during the ten (trading) day period when Enron employees were unable to sell the stock in their portfolios. *Id.* at 96.

losses.⁷³

Defined benefit plans expose workers to much greater risks during reorganizations and bankruptcies. In these plans, employers offer workers a “defined benefit” at retirement. The amount of the benefit is determined by a formula specified in the plan.⁷⁴ Employees do not have individual accounts established for them in defined benefit plans. Instead, the employer is responsible for making contributions into a trust account sufficient to ensure that the promised benefits can be paid.⁷⁵ The amount of contributions required depends on a complex actuarial analysis; which takes into consideration factors such as the age and length of service of employees, projections of future salary increases, and the rate of return on plan investments.⁷⁶

For a number of reasons, defined benefit pension plans can become underfunded.⁷⁷ In fact, most plans begin underfunded because ERISA permits plans to offer benefits immediately and to amortize towards full funding over a thirty-year period.⁷⁸ Plans may be underfunded at times after their inception as well because of factors such as actuarial mistakes and unexpectedly bad investment experiences.⁷⁹

To protect against the risk of underfunding and failed plans, ERISA provides an insurance scheme for defined benefit plans administered by the Pension Benefit Guaranty Corporation (PBGC), a government-created corporation.⁸⁰ Every plan must make a premium payment to cover the cost of the insurance.⁸¹ The basic premium is currently nineteen dollars per participant.⁸² If a plan fails, the insurance covers some, but not all, of the losses. A primary limit on coverage is a cap on the maximum benefits the PBGC will pay.⁸³

73. See *id.* at 99 (detailing the losses suffered by Enron employees).

74. For example, a formula might promise a pension at retirement equal to .02 (the generosity factor) times years of service with the firm (say thirty years) times final salary (say \$50,000). Thus, in our example, the worker would be entitled to a pension at retirement of \$30,000 (.02 x 30 x \$50,000).

75. See LANGBEIN & WOLK, *supra* note 62, at 45-47 (describing the features of defined benefit plans).

76. *Id.* at 356-57.

77. See *id.* at 917-23 (discussing various ways in which defined benefit plans can become underfunded).

78. 26 U.S.C. § 412(b)(2)(B)(ii) (2000). For plans in existence on or before January 1, 1974, the amortization period for initial pension liabilities is forty years. 26 U.S.C. § 412(b)(2)(B)(i) (2000). If a plan is amended to provide greater benefits based on past service with the employer, the cost of those increases can also be amortized over a thirty-year period. 26 U.S.C. § 412(b)(2)(B)(iii) (2000).

79. LANGBEIN & WOLK, *supra* note 62, at 920-22.

80. 29 U.S.C. § 1302 (2000).

81. 29 U.S.C. § 1307 (2000).

82. 29 U.S.C. § 1306(a)(3)(A)(i) (2000).

83. See 29 U.S.C. §§ 1322, 1322b (2000) (providing a formula for determining the cap

Defined benefit pension plans and the PBGC insurance scheme are often major factors in corporate reorganizations and Chapter 11 bankruptcies.⁸⁴ In *Pension Benefit Guaranty Corp. v. LTV Corp.*,⁸⁵ the LTV Corporation filed for Chapter 11 bankruptcy primarily to relieve itself of \$2.1 billion in liabilities from underfunded defined benefit pension plans.⁸⁶ After the PBGC terminated the plans and began to pay benefits under the insurance scheme, LTV established new “follow-on” plans designed to wrap around benefits and place workers in the same position they were in before the original plans were terminated.⁸⁷ LTV’s plan was designed to replace benefits where the PBGC insurance failed to provide coverage. This left LTV in a much better position. Instead of paying for all the benefits it had promised, the PBGC was paying for most of them (up to the limits of the insurance provided) and LTV was only paying for benefits beyond the insurance limits. This precise strategy was discouraged by the Supreme Court.⁸⁸ The Court held that the wrap-around plan was sufficient reason for the PBGC to cease making payments and to restore responsibility for the plans to LTV.⁸⁹

Nevertheless, the general strategy of using bankruptcy law to limit or avoid defined benefit pension plan liabilities is still common and viable.⁹⁰ For example, this was a major factor in the recent US Airways bankruptcy filing. Through the filing US Airways is seeking to shed \$1.6 billion in underfunded defined benefit pension liabilities in favor of a new plan that would pay \$850 million in benefits over the same time period.⁹¹

on benefits the PBGC will pay to a particular employee).

84. See generally LANGBEIN & WOLK, *supra* note 62, at 898-923, 939-46 (discussing the termination of defined benefit plans and the subsequent intervention of PBGC in the context of corporate reorganizations and Chapter 11 bankruptcies).

85. 496 U.S. 633 (1990).

86. *Id.* at 640.

87. *Id.* at 641-42.

88. *Id.* at 651. The Court cited several reasons for its disapproval of follow-on plans. It noted that “[t]he availability of a follow-on plan . . . would remove a significant check—employee resistance—against termination of a pension plan.” *Id.* The Court also found that follow-on plans “may tend to frustrate one of the objectives of ERISA that the PBGC is supposed to accomplish” and that such plans “have a tendency to increase the PBGC’s deficit and increase the insurance premiums all employers must pay.” *Id.*

89. *Id.* at 656.

90. See Press Release, Pension Benefit Guaranty Corporation, PBGC Calls for Pension Protections: Actions of US Airways and UAL Underscore Need for Fix (Sept. 14, 2004), at http://www.pbgc.gov/news/press_releases/2004/pr04_65.htm. (last visited Nov. 5, 2004) (outlining the PBGC’s recommendation to Congress, made at least partly in response to the establishment of follow-on plans by US Airways and United Air Lines, that it be allowed to perfect a lien in favor of a pension plan when a company in bankruptcy fails to make its required contributions to the plan).

91. Micheline Maynard & Mary Williams Walsh, *Judge Rules US Airways Can End Pilots’ Pension*, N.Y. TIMES, March 3, 2003, at C2.

III. WHY ARE DIFFERENT INTERESTS PROTECTED DIFFERENTLY?

As discussed to this point, workers in the United States have different levels of protection for different interests. Their interests in jobs and wages are largely unprotected by the law. In contrast, there are stronger protections for their interests in continued health insurance coverage and pensions. What explains these differing levels of protection within the United States?

In thinking about the United States, it is seldom misleading to begin by thinking about markets. In this Article the primary focus is on the level of legal protections workers receive when the markets go bad, when they lose their jobs or when their firms go bankrupt. However, in its laws (and absence of laws) the United States also exhibits a deep faith in the ability of the markets themselves, rather than the law, to protect workers. Indeed, although I am jumping ahead a bit, it may not be an overstatement to say that a major explanation for the different and lesser levels of legal protection for workers in the United States than elsewhere is that the United States entertains legal protections only after it gives the market ample opportunity to solve the problem first.

In general, markets will work as a protection for workers to the extent that they can quickly and easily find a replacement for the lost good in the market. If a worker loses a job because a firm becomes financially distressed, there is no loss if an equivalent job can be found in the market the next day. In that situation there is no need for any legal protection. On the other hand, if the worker cannot replace the job in the market very easily, the need for legal protection may arise.

First consider the limited legal protection for the jobs and wages of workers during corporate reorganizations and bankruptcies. Why might that be? In a dynamic market, the best option for workers who lose their jobs is to find another equivalent job. Thus, in the United States, the principal governmental programs on jobs and wages are state unemployment compensation programs. These programs do not protect jobs or wages directly, nor are they designed primarily as welfare programs to ease poverty caused by job losses.⁹² Instead, these programs provide resources to help workers find better replacement jobs, which is the favored type of protection against these kinds of losses.⁹³ In the United States, this

92. See *supra* notes 37-42 and accompanying text.

93. Unemployment insurance programs all contain a number of details that emphasize their role as mechanisms to aid job match and job replacement. See generally Joseph M. Becker, *The Location of Financial Responsibility in Unemployment Insurance*, 59 U. DET. J. URB. L. 509, 510-18 (1982) (illustrating that cost sharing between states might result in better unemployment insurance programs).

form of market protection tends to operate fairly well. In 1997-1998, the most recent year for which data are available, the median long-tenured displaced worker found a new job paying almost exactly the same wage within about five weeks.⁹⁴

Compare this to the situation with health insurance benefits. Prior to HIPAA, most employers imposed limits on their health insurance coverage, making it difficult for displaced workers to replace lost coverage.⁹⁵ For example, most employers imposed waiting periods before health insurance coverage would begin and excluded from coverage certain preexisting medical conditions.⁹⁶ Thus, once a worker lost her health insurance coverage, the market did not work very well to enable the worker to replace it easily and quickly, even if the worker did find a new job quickly.

On this issue, laws were enacted precisely to remove these barriers to the ability of displaced workers to replace the lost good. HIPAA does not require health insurance coverage or prohibit employers from removing employees from coverage (e.g., by firing them). But it does prohibit employers who hire displaced workers from limiting their access to health insurance. In most cases, HIPAA requires employers offering health insurance to offer it to displaced workers without a waiting period and without excluding pre-existing conditions from coverage. Here, once again, the United States relies on the ability of the market to provide protection for workers who lose this type of good. Here, however, laws are required to ensure reasonable access to that market protection.

Section 1114 of the Bankruptcy Code can also be viewed as a response to the challenges in finding a replacement for lost health

94. Ryan T. Helwig, *Worker Displacement in a Strong Labor Market*, MONTHLY LAB. REV., June 2001, at 13, 18, 22-23. During this time period the economy was strong. When the economy is not as strong, these numbers are less favorable. Generally, this type of market protection will work well so long as another job can be found quickly and there are not large returns to seniority (which will be lost when the initial job is lost). There has been considerable debate on these issues in the United States over the past decade, but the latest evidence tends to indicate that the losses caused by job matching and returns to seniority are relatively modest. See JOSEPH G. ALTONJI & NICOLAS WILLIAMS, *DO WAGES RISE WITH JOB SENIORITY? A REASSESSMENT* 29-31 (Nat'l Bureau of Econ. Research, Working Paper No. 6010, 1997) (concluding that returns to seniority are modest); see also Joseph G. Altonji & Robert A. Shakotko, *Do Wages Rise with Job Seniority?*, 54 REV. ECON. STUD. 437, 438 (1987) (proposing that the effect of seniority on wages is small). But see Robert Topel, *Specific Capital, Mobility, and Wages: Wages Rise with Job Seniority*, 99 J. POL. ECON. 145, 147 (1991) (finding that the average returns to seniority are significant).

95. See S. REP. NO. 104-156, at 3-4 (1996) ("Because of the prevalence of participation requirements, preexisting condition clauses, and discriminatory enrollment practices, many workers have had to limit their employment choices to hold on to their health coverage while others live with the fear of knowing that a job layoff could mean a total loss of health coverage").

96. See *id.* at 8 ("More than half of all workers are enrolled in employment-based plans that impose some form of preexisting condition exclusion or limitation").

insurance, but in an even more difficult circumstance.⁹⁷ Section 1114 provides special, heightened protections for the health insurance benefits of retirees. Retirees are especially likely to have difficulty replacing lost health insurance because the primary mechanism of replacement—finding another job which offers health insurance as a benefit—is not available. Once again, then, this general rationale seems to work well to explain the heightened legal protections of Section 1114 for retiree health benefits.

Finally, for defined benefit pension plans, the federal government has established perhaps the highest level of protection—a mandatory insurance scheme, the PBGC.⁹⁸ Pension plans are especially difficult to replace because the benefits accrue over an extended period of time. For example, if a worker earns a \$40,000 per year pension after forty years of employment based on a standard pension formula (.02 x 40 years x \$50,000 final salary) and then the pension is forfeited, the worker can likely replace it only by working another forty years for another employer. That is, unless descended from Methuselah, he simply cannot replace it. Thus, since the market cannot provide a reasonable replacement for the lost benefit, the law steps in.

IV. CONCLUSION

Conventional wisdom about the United States is that it provides relatively few protections for workers against employment risks.⁹⁹ This Article provides a slightly different and, perhaps, more nuanced view. The United States provides few legal protections for some types of employment risks, such as job and wage losses, but relatively robust legal protections against other types of risks, such as loss of health insurance (especially for retirees) and pension benefits.

Viewed through this alternative lens, the issue becomes why legal protections are provided for some types of employment risks but not for others. This Article suggests that the explanation is that the United States relies on direct legal protections only as a second-best response. If market forces can be harnessed to provide protection, that is the first (and last) response. Especially in the context of financially distressed firms, these types of market protections are viewed as preferable to legal protections for a number of reasons. First, market protections create a proper set of

97. 11 U.S.C. § 1114 (2000).

98. 29 U.S.C. §§ 1301-1461 (2000).

99. See, e.g., Clyde W. Summers, *Employment At Will in the United States: The Divine Right of Employers*, 3 U. PA. J. LAB. & EMP. L. 65, 65 (2000) (noting that “[t]he United States, unlike almost every other industrialized country and many developing countries, has neither adopted through the common law or by statute a general protection against unfair dismissal or discharge without just cause, nor even any period of notice”).

incentives for workers by encouraging them to focus their attention on other firms that may be able to better accommodate them, rather than backward to the distressed firms. Second, market protections avoid a drag on firm formation. With legal protection of jobs, firms may be reluctant to form or expand by creating more jobs because when they create a job, they also create a legal claim to that job by its current occupant.¹⁰⁰ Thus, the lack of legal protections contributes to the ability of workers to find replacement jobs by expanding, at least in theory, the number of replacement jobs available. Third, market protections encourage the socially productive movement of workers from distressed and troubled firms to more successful firms. The first option for workers in financially distressed firms, and maybe their only option, is to search for a more successful firm rather than maintaining their connection to the old, troubled firm.

Having said all this, relying on market protections will leave some workers in a bad situation. Some will not be able to find alternative jobs quickly and easily, or at all. By assumption, they will have no legal alternative. The treatment of health insurance and pensions in this country illustrates that the United States is not blind to these types of costs. When finding replacement goods becomes too difficult for workers, the United States can and does provide legal protections.

Thus, the difference between the United States and other countries is not that the United States is unwilling to provide legal protections while other countries are. Instead, the difference is that the United States is much more willing to rely on market forces to provide protection against employment risks because of the benefits it sees in a less constrained labor market.¹⁰¹ But once again, that willingness to rely on market forces is not unlimited. Even in the United States, the risks can become unacceptable. When that occurs, legal protections are provided.

100. See Katharine G. Abraham & Susan N. Houseman, *Does Employment Protection Inhibit Labor Market Flexibility? Lessons from Germany, France, and Belgium*, in *SOCIAL PROTECTION VERSUS ECONOMIC FLEXIBILITY* 59, 59 (Rebecca M. Blank ed., 1994) (recognizing the claims of critics of job-security regulations that that strong job rights "prevent employers from adjusting to economic fluctuations and secular changes in demand").

101. In this Article, my focus is on the bias in the United States toward harnessing market forces to address employment risks, in contrast to the bias in some other countries toward using government regulation to address the same risks. These different biases may reflect and reinforce other types of differences between the United States and other countries, such as different and competing visions of the interests requiring protection and different evaluations of the empirical effects of the types of protections provided.