Governing by Fiduciary: How the Employee Retirement Income Security Act of 1974 Delegated Control over Pension Policy to Private Actors

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ABSTRACT

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Approximately one-half of Americans participate in a pension plan offered by their employers and subject to the Employee Retirement Income Security Act of 1974 (ERISA) (Howard 2007, 76). Yet ERISA is frequently ignored by social scientists researching retirement income because of its complexity. Given the enormous amount of foregone tax revenues that support private pensions, the motivating question of my dissertation is: How did the American state change as Congress delegated power over American pension plans to private employers? I argue that a weak system of bureaucratic oversight and the federal courts' deference to pension administrators allowed fiduciaries to control policy implementation and assume a role traditionally reserved for the state – blurring the line between public and private.

My purpose here is to provide an analytical history of ERISA that explores its methods of delegating both policymaking control over and the detailed nuances of administration of private pension plans to private actors. I explore the concept of fiduciary status as a safeguard when government outsources the implementation of policy to private actors. Regardless of whether fiduciary standards have ensured sufficient accountability in the ERISA context – and I find that they have not – I argue that the potential is there and analyze where ERISA went wrong.

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DEDICATION

For Josh, whose intellectual curiosity resulted in many lengthy discussions that helped shape this dissertation. As always, your love and support is what allows me to do what I do and be happy doing it.

For Jake, who reminded me frequently that my dissertation is not the most important thing in his world and therefore is not the most important thing in my world either.

INTRODUCTION

We have all heard the lament about the decline of defined benefit pension plans. Traditional pension plans have withered, and most Americans – especially those with lower incomes – save little for retirement and rely mainly on Social Security for retirement income. But the vast majority of employees covered by employer-sponsored retirement savings plans such as 401(k)'s do participate, and few without the option to participate in employer-sponsored plans save through alternate vehicles like individual retirement accounts.[1] President Obama is working to expand access to and participation in retirement savings plans outside the employment relationship, but the importance of employer-sponsored plans to the American safety net remains.

The American welfare state depends heavily on employers to provide their employees with social welfare benefits (*e.g.*, health insurance and pensions). A long emphasis on self-reliance and small government resulted in years of tax subsidies encouraging the connection of welfare benefits to work and a uniquely American path to social security (Hacker 2002).[2] Management consultant Peter Drucker called the growth of private pensions an "unseen revolution" and "an

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[1] Seventy-two percent of those with annual salaries from $30,000 to $50,000 who were covered by an employer plan participated, while only five percent of those not covered by an employer plan saved through an individual retirement account (IRA). Dorning, Mike, and Margaret Collins. "Obama Offering Retirement Savings Plan for Workers," Bloomberg, January 1, 2014, http://www.bloomberg.com/news/2014-01-28/obama-seen-offering-retirement-savings-plans-for-workers.html.

[2] Early research on the importance of public-private linkages in the welfare state showed that private welfare benefits are shaped and subsidized by the government through tools such as tax incentives (Howard 2007; Stevens 1988). These incentives empowered many private actors (*i.e.*, employers, insurance companies, and unions) who now play a key role in the state itself (Hacker 2002).

outstanding example of the efficacy of using the existing private, nongovernmental institutions of our 'society of organizations' for the formulation and achievement of social goals and the satisfaction of social needs" (quoted in Hacker 2002, 82). Political scientist Jacob Hacker (2002, 82-83), however, sees danger when welfare policy control is located outside government and the path of welfare policy can be changed "through stealth": "[T]he politics of private pensions is subterranean politics, only occasionally involving a broad circle of participants and resisting the scrutiny that public programs typically invite – even when sizable public resources and recognized national policy goals hang in the balance."

The Employee Retirement Income Security Act of 1974 (ERISA) formalized nearly a century of public-private relationships by regulating systematically for the first time pension promises made by employers to employees (Stevens 1988; Klein 2003).[3] ERISA was designed to protect workers from the insecurities of a private pension system while simultaneously encouraging the growth of that private system (Hacker 2002).[4] After all, protecting employee expectations of receiving pensions would be meaningless if employers stopped offering pension plans because of onerous regulations.

"Based on the sheer number of lives touched, the passage of ERISA is arguably the third 'big bang' of the American welfare state" after Social Security and Medicare/Medicaid (Howard 2007). By 1974, nearly 31 million Americans were covered by a private pension plan, and

[3] Historian Stuart D. Brandes (1976, 5-6) defines welfare capitalism as "any service provided [by employers] for the comfort or improvement of employees which was neither a necessity of the industry nor required by law."

[4] For a discussion of the 1964 collapse of the Studebaker pension plan for 11,000 of its current and former auto workers, commonly considered the event that sparked the press for pension reform, see Wooten (2001).

today, roughly one-half of private workers participate in an employer-sponsored retirement plan (Thompson 2005, 1; Dushi and Iams 2013, 46). A significantly larger proportion of the population receives Social Security benefits. In 2011, 87% of married couples and 85% of non-married individuals aged 65 or older received Social Security benefits.[5] Many Americans, however, and particularly the wealthiest, hold the majority of their retirement assets in the form of private pension benefits. While Social Security benefits constituted the major source of total income (at least 50%) for 74% of non-married individual beneficiaries in 2011, they were the major source for only 52% of married beneficiaries, who tend to be wealthier than non-married beneficiaries.[6]

ERISA governs the enactment and maintenance of private pension plans, including both traditional defined benefit (*i.e.*, employer pays retiree a fixed sum per month) and defined contribution (*i.e.*, employer and/or employee contributes to an account tax-free and employee receives the money in the account after investment gains and losses at retirement) pension plans. Although in 1974, 87% of participants in private pension plans had defined benefit plans, by 1995 participation in defined contribution plans exceeded participation in defined benefit plans – and the gap has subsequently widened (Thompson 2005, 1; Bureau of Labor Statistics 2004). Employers have full discretion to provide or not provide pension benefits and need not act in the

[5] The proportion of Americans covered by Social Security will rise because government workers now have nearly universal participation in Social Security during employment while many former government workers are not covered by Social Security.

[6] "Fast Facts & Figures About Social Security, 2013." Social Security Administration: 8. Available at http://www.ssa.gov/policy/docs/chartbooks/fast_facts/2013/fast_facts13.pdf. Total income did not include withdrawals from savings, non-annuitized IRAs, or 401(k) plans, resulting in an overemphasis on the extent to which the wealthy rely on Social Security benefits for their income.

best interests of employees when deciding what form of pension benefits to offer. However, once an employer decides to provide its employees with a pension plan, ERISA plays a central role.

Those who manage an ERISA pension plan or its assets, which may include executives at the employer or third parties, are considered fiduciaries. Fiduciaries are "caretakers" who must act in the best interests of employees and stand in a position of power over plan participants (employees and former employees).[7] An industry of third party service providers who serve employers and fiduciaries by administering pension plans and providing investment or legal advice, and therefore take on a fiduciary role themselves, has developed. These third party service providers profit from fees generated by pension plans. ERISA, in addition to corresponding Department of Labor and Internal Revenue Service regulations and federal case law, sets forth the rules that govern the relationships between these private parties. Besides providing a framework for pension administrators, ERISA also permits plan participants and their beneficiaries to bring lawsuits in federal court to challenge a denial of their claims to benefits or the manner in which the plan is run.[8]

[7] ERISA § 404(a), 29 U.S.C. § 1104(a) ("[A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and – (A) for the exclusive purpose of : (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan; (B) with the care, skill, prudence, and diligence under the circumstances 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; (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and (D) in accordance with the documents and instruments governing the plan insofar as such documents are consistent with the provisions of this subchapter and subchapter III of this chapter.").

[8] ERISA § 502(a), 29 U.S.C. § 1132(a) ("A civil action may be brought – (1) by a participant or beneficiary . . . (B) to recover benefits due him under the terms of his plan . . . [or] (3)(A) to enjoin any act or practice which violates

In spite of the number of Americans that are participants in or beneficiaries of an ERISA-covered pension plan, the enormous value of the assets managed under the plans, and the importance of the decade-long struggle to pass the statute to the country's political history,[9] there is little analysis of the statute within political science literature.[10] Every day, private actors affiliated with employers make decisions about whether to grant one participant's claim for benefits or change one rule about how one pension plan will be administered. ERISA sanctions their right to make these decisions. In the aggregate, these decisions make pension policy. The questions that my dissertation explores are how did we get here and who is watching.

The first question of how we got here, to the current state of pension policy, implicates not just the historical path but a conscious decision made at the time of ERISA's passage that it was acceptable to place this power in private hands. Once Congress and the President acknowledged the need to overhaul regulation of private pensions, regulation could have reasonably followed several different paths. The resulting scheme gave private employers substantial leeway to implement Congress' desired policy objectives and delegated quasi-public power to private actors, both of which demonstrate a blurring of the line between public and private actors.

any provision of this subchapter or the terms of the plan . . ."). ERISA prohibits litigation of these claims in state courts. ERISA § 514, 29 U.S.C. § 1144.

[9] It took over a decade – spanning the tenures of four Presidents – to secure the passage of reforms, from President Kennedy's establishment of the President's Committee on Corporate Pension Funds in 1962 to President Ford's Labor Day ceremony signing ERISA into law in 1974. Much of that time was spent wrangling with powerful interest groups and congressional infighting over the jurisdiction of committees responsible for labor and tax legislation. See Wooten (2004).

[10] One notable exception is the work of Jacob Hacker (2002) in *The Divided Welfare State: The Battle Over Public and Private Social Benefits in the United States*. While Hacker is one of the only political scientists to examine ERISA, he does not take on a detailed analysis of the regulatory framework and private litigation remedy.

ERISA can thus add to the literature on delegation of legislative powers and its current exploration of delegation to private actors instead of or in addition to the bureaucracy. The question of how and why Congress sanctioned such extensive delegation and the design of this particular delegation should inform future decisions about whether and how to delegate to private actors.

The second question of who is watching these employer representatives that control trillions in U.S. assets asks whether these private actors are behaving in accordance with legislative intent (although that is a notoriously murky concept), statutory design, and the best interests of plan participants (as ERISA explicitly requires). The issue is essentially accountability – who determines whether these private actors are behaving as desired; how is compliance measured, meaning what are the standards to which they are supposed to adhere and how is deviation determined; and what are the consequences if the private actors fail to behave as desired.

ERISA's framework assigns to multiple government institutions and plan participants (given the private litigation remedy) the task of supervising pension administrators and asset managers and holding them accountable. Governmental actors include: (1) Congress, which designed the ERISA system and continues to make legislative adjustments; (2) the bureaucracy, including both the Department of Labor and the Internal Revenue Service, which share administrative

responsibility over ERISA pension plans;[11] and (3) the federal courts, which interpret the statute by adjudicating pension claims. ERISA can therefore contribute to administrative law and political science scholarship on accountability because there are multiple pressure points to help evaluate which methods have worked well and should be applied in the future and which have gone awry.

ERISA demonstrates how historic public-private partnerships shift and change over time by circumstance and by design. The nature of delegation research currently is to determine how best to manage the delegation of increasing power and control to the private sector. ERISA was designed to protect promises made by employers to employees – to regulate private behavior that is beneficial to society. The extent to which government is able to order private relations and enforce promises goes to the very justification for its existence.

Who Governs?: Structuring Delegation to Private Actors[12]

If bureaucratic structure and oversight is heavily debated when Congress delegates to government actors, then structuring delegations to private actors deserves at least as much attention. My goal here is not to debate the wisdom of delegation in general or in the case of ERISA specifically (Lowi 1979), but instead to focus on the importance of legislative tools to

[11] The Pension Benefit Guaranty Corporation, which guarantees defined benefit pension plans up to a statutory maximum through insurance premiums, is another government actor with jurisdiction over ERISA but not relevant for my discussion here.
[12] Dahl (2005).

control private actors used by Congress to achieve public goals (Moe 1989). The extent to which Congress is willing to delegate to private actors depends on the success of those tools.

An exploration of ERISA's design provides insight into ways Congress can craft statutes to ensure accountability when it transfers extensive policymaking authority to private actors. ERISA uses fiduciary duties to hold private actors accountable. The bureaucracy and the courts have enforcement roles designed to ensure compliance. The result of a decade of congressional work on pension reform deserves a prominent place in the delegation literature. A review of that literature demonstrates where ERISA can add value.

Before I address the delegation literature, however, I need to address why ERISA is a case of delegation at all. Traditionally, delegation occurred when Congress drafted broad legislation and then directed government agencies to establish more detailed standards to regulate the private sector. Research focused on whether bureaucrats stayed true to congressional goals or caused policy to drift in an undesired direction. Outsourcing instead occurred when the government paid a private supplier directly for the provision of goods or services set forth in a contract governing the relationship.[13] Because the task was more clearly defined by the contract, the main concern of government and researchers alike was ensuring that the quality of the goods or services provided was high and met expectations.[14]

[13] The United States has a long history of public and private interaction. "[W]hile the language of 'outsourcing,' 'contracting,' and 'deregulation' is certainly contemporary, the history of U.S. government reliance on intersecting public-private partnerships runs much deeper" Novak (2009, 27).

[14] Many thanks to Professor Michael Ting for his thoughts on this subject and helping to clarify mine.

At first glance, ERISA may seem more like outsourcing because the government directs tax subsidies to employers in exchange for providing pension plans under the terms of the statute and employers are not asked to ignore their own interests when deciding whether or not to offer such plans. Two aspects of ERISA, however, make this instead a case of delegation: (1) the extent of the discretion left to employers and their representatives, and (2) the lack of a contract between the government and employers.

As explained further below, Congress drafted ERISA as a broad statute that included many gaps to avoid overly burdening employers voluntarily offering pension benefits and because political battles made it impossible to pass more detailed legislation. Employers' latitude therefore includes both decisions about what type (if any) of pension benefits to offer and, to a large extent, how to administer those benefits. Congress was concerned with not only the typical outsourcing concern that employers provide the expected services (*i.e.*, provide pensions that meet ERISA's accrual, funding, and vesting standards) but also with employers pursuing the public good by protecting employees from themselves. ERISA's exclusive benefit rule demands that employers and their representatives set aside their own self-interest when administering pension plans.[15] In typical contractual relationships, each party acts in its own self-interest according to clearly specified terms. This is not the case with ERISA.

[15] "[A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—(A) for the exclusive purpose of: (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan." ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1).

The lack of a contract between the government and employers to provide pensions for employees (third party beneficiaries in the language of contract law) also makes ERISA an example of delegation instead of outsourcing. This may seem overly simplistic given that the statute sets forth what the government wants employers to do and they can accept the offer of tax subsidies in exchange by creating and maintaining pension plans. The lack of contractual privity, however, is indicative of a different relationship between the parties. Here, Congress can at any time change the terms under which employers provide pensions – there is no duration for which they are fixed, and employers have no ability to negotiate those changes directly with the government. Employers can also choose to exit the relationship at any point. There is no term during which they must continue to offer pension benefits as long as they honor past benefits promised and vested. This uncertainty and lack of a binding relationship between the parties is what takes ERISA out of the contracting realm and into the realm of delegation, particularly in conjunction with the discretion accorded to employers to motivate them to continue the voluntary relationship.

Although some scholars have also distinguished situations where funding is provided through grants or tax subsidies from outsourcing because there is no direct payment, I do not believe this difference is dispositive.[16] ERISA's tax subsidies may not be offered only to one or a small number of private firms competing for government (and therefore the people's) business as in direct fee-for-service arrangements, but the individual citizen (or consumer) can evaluate the

[16] Although Freeman and Minow (2009, 7) argue that encouraging private actors to advance public goals through "subsidies" is not the same as direct payments to particular firms, they offer no empirical evidence to support this argument and do not explain how it differs.

firms providing pensions and select among them. Assuming competition among employers for employees exists and employees have knowledge of the pension benefits offered by different employers, employees who value a better pension plan will switch employers as necessary to gain that benefit. Assuming that there is little to no competition among employers for employees or knowledge of employers' pension benefits or that the transaction costs for switching employers are high, this is a problem faced under either the delegation or contract label.

Although I argue that ERISA constitutes delegation instead of outsourcing, the boundary between the two methods of private implementation of government goals is fuzzy. Where the outsourcing literature adds to the story told here, particularly on the quandary of holding private actors accountable, I will discuss it below. My overarching framework, however, is within the sphere of delegation, of private actors treated as public actors and the complications that arise.

Congressional delegation occurs for many reasons, including time constraints, the desire to benefit from the accumulated knowledge of specialists (Moe 1984, 756), and electoral advantages (Kiewiet and McCubbins 1991, 2) such as credit claiming for constituent service (Mayhew 1974) and blame avoidance in controversial areas (Fiorina 1982). Political scientists spent years debating how and whether Congress holds bureaucrats accountable when it delegates authority to implement legislation and cedes control over its policy goals. This research is consumed by the classic principal-agent problem. The principal-agent dilemma addresses the difficulties an individual or entity (the principal) has motivating another party (an agent) to

complete one or more tasks delegated by the principal exactly as the principal would if the principal had the time and/or expertise to complete the task himself in an efficient manner.

Delegation involves risks. As Kiewiet and McCubbins (1991, 5) aptly summarized:

> The opportunism that generates agency losses is a ubiquitous feature of the human experience. It crops up whenever workers are hired, committees are appointed, property is rented, or money is loaned. The message that we are all feckless agents of a Divine Principal is at the very heart of Judeo-Christian theology.

In addition to outright theft or self-dealing, delegation can result in shirking and slippage. While an agent pays the cost for hard work in time (if not money), the reward goes mainly to the principal. An agent may therefore "shirk" – or exert less effort – to complete the delegated task, resulting in slippage – or the gap between what the principal wants done and how the agent completes the task. Because monitoring involves costs, a principal must weigh the benefits of monitoring (reduced shirking and slippage) against these costs (Moe 1984, 750-51). Some amount of slippage is inevitable at each point of delegation and oversight (*e.g.*, when citizens delegate to government, when the legislature delegates to the bureaucracy or private actors, and when the courts or Congress hold hearings regarding complaints about the agent's behavior) (Moe 1990, 231).

Ways of controlling the agent once the decision to delegate has been made can be divided into ex-ante and ex-post methods. While interest groups can raise "fire alarms" to alert Congress when agents act in undesirable ways (McCubbins and Schwartz 1984), Congress largely uses procedures and rules to keep agents in line (McCubbins, Noll, and Weingast ("McNollGast")

1987, 1989). These procedures allow interest groups to participate in the agent's work and help force the agent to disclose information necessary for other parties (and the principal(s)) to understand and participate in its decisions at key points. Thus, principals can "stack the deck" for ex-ante control.[17]

Principals can also seek to hold agents responsible with oversight or ex-post control. Decisions about whether to use ex-ante or ex-post mechanisms and how much to use are "separate" but "not independent" (Bawn 1997). Although costs of ex-ante oversight are generally higher, congressional committees with greater information and credit claiming opportunities frequently have lower costs and prefer higher amounts of oversight (or "police patrol" oversight as per McCubbins and Schwartz) (Aberbach 1990; Bawn 1997).

Recently, political scientists have recognized that government[18] faces the same basic principal-agent problem when delegating to private actors. But government delegation to private actors instead of the bureaucracy presents unique difficulties for policy implementation.[19] Beyond the classic notion that firms are motivated by maximizing profits and that makes it difficult to align

[17] For a discussion of the effectiveness of ex-ante structural mechanisms in controlling delegation, see Spence (1999), finding that procedures that increase the costs of specific agency decisions (instead of agency decision making more generally) are more successful.

[18] Although the political science literature largely models Congress as the principal in delegation studies, I take no position on whether Congress or the executive or both is the principal. When discussing congressional negotiations over ERISA's statutory design, I refer to Congress as the principal for expediency. I also refer to the bureaucracy and the courts as principals in redelegating additional authority to the private actors under discussion or attempting to control their behavior.

[19] "A central characteristic of much government privatization is that private delegates are granted powers not simply for their own advantage, but rather to enable them to act—and more specifically, to interact with third parties—on the government's behalf" (Metzger 2003, 1463). These private actors have additional power based on the importance of the services they provide and the imprimatur of the government (Metzger 2003, 1463-64).

their goals with those of Congress, political scientist Jessica Green (2007) has focused on how the voluntary nature of the relationship between principal and agent in this case affects Congress' ability to control its agents. The literature is now moving toward an exploration of how Congress can control private actors (or hold them accountable at least) when it decides to delegate to them. This is the natural progression of previous work on controlling the bureaucracy. Accountability is "'the most difficult issue' when governance is provided by private actors." (Mattli and Buthe 2005, 227).

Congressional efforts to force employers to behave exactly as Congress or employees want when offering pension benefits were doomed from the start. And legislators knew it. Employer representatives faced an inherent conflict between employee interests in receiving the greatest amount of benefits possible and employer interests in containing costs. A voluntary private pension system required Congress to give employers significant discretion and incentives to maintain pension plans – such as the ability to have their own executives and contractors run the plans. All the political fighting over the balance between protecting employees and growing the private pension system came down to this basic fact. Recognizing that Congress could never have complete control over the regulation of voluntary, private pensions then, my analysis focuses on how to design a system of sufficient accountability. How political compromise was reached under ERISA and the results should inform any discussion of the risks of delegation and whether different structures mitigate those risks to an extent necessary to achieve the benefits of delegation to private actors.

Who Has the Final Say: Managing Delegation to Private Actors

The first step when exploring a method of holding private actors with delegated powers accountable is to define accountability. Many of the administrative law scholars researching the topic, usually in the outsourcing context, skip this initial step and end up with a circular argument that following the suggested procedures or enforcement mechanisms *is* accountability. Law professor Jerry Mashaw, however, supplies a framework:

> [W]e should be able to specify at least six important things: *who* is liable or accountable to *whom*; *what* they are liable to be called to account for: *through what processes* accountability is to be assured; *by what standards* the putatively accountable behavior is to be judged; and, what the potential *effects* are of finding those standards have been breached.

(Mashaw 2006, 118, quoted in Freeman and Minow 2009, 16). I use Mashaw's framework here because it is both general enough to apply to all delegations to private actors and comprehensive enough to evaluate existing and proposed accountability mechanisms (including those under ERISA).

Before evaluating accountability mechanisms, I want to say more about the particular risks of delegation to private actors that make this exercise so important. The first risk is that there will be increased slippage away from government's goals because delegation is made to a private actor instead of a more traditional public actor. The second risk is that the very act of delegation diminishes government's capacity to supervise a private actor, particularly when combined with a vast increase in delegation and outsourcing more broadly.

Increased slippage from delegation to private actors occurs as a result of the multiple principals problem (which, among other things, drives firms to focus on profits), increased agent autonomy because of outside revenue sources, and the voluntary nature of the principal-agent relationship (Mattli and Buthe 2005, 232; Green 2007, 19; Green 2014, 46). On the first point, political scientists Walter Mattli and Tim Buthe (2005, 232) argue that "[t]he key difference between delegation to public agents and delegation to private agents is that delegation to private agents creates a multiple-principals problem." Private agents are largely collective actors (firms or organizations) with one or more owners or patrons who are the prior and more direct principals of the private agents. At a minimum, each of these private agents "has at least two principals, one public and one private" (232). Private agents with conflicts of interest therefore abound.

One result of the multiple-principals problem is that private actors that are for profit entities face pressure from their private principals to maximize profits. The desire to maximize profits can result in cutting costs for goods or services provided through the delegation relationship even if it means reducing the amount of goods or services provided (assuming that the amount is not specified in legislation or contract) or the quality of the goods or services provided. Although economist Andrei Shleifer (1998, 139) argues that the potential harm from the profit motivation of firms is not a reason for government to instead provide the services itself since terms can be spelled out in detail ex-ante and competition among firms and reputational incentives motivate the firm to maintain high quality services, there are some areas of delegation (particularly outside the domain of government contracts on which he writes) where there is little or no competition and reputational incentives are muted. I will discuss that further below.

On the second reason for increased slippage from delegation to private actors, firms are not reliant on their principals within government because of outside funding sources and are also insulated from oversight (Green 2007, 19; Green 2014, 46). Principals within government lack the same budgetary control over firms that they have over agencies. Bureaucrats know at all times that if they stray too far from congressional intent, they are likely to be punished fiscally. Firms are more autonomous, and the place of firms outside the traditional government organizational structure makes it difficult to reign in that autonomy. Principals have less knowledge of how the delegation is being managed, and their ability to enforce their goals informally is limited.

Finally, at the heart of the problem with slippage when delegating to private actors is the voluntary nature of the relationship. "When states delegate to public actors, the relationship is 'involuntary', in the sense that state agencies (on the domestic level) . . . are not in a position to refuse any task delegated to them. This logic does not hold for private actors, who can simply refuse to enter into any arrangement that they do not find beneficial" (Green 2007, 19). The fact that these relationships are voluntary changes the power structure in the relationship. While firms may like the revenue or tax subsidies provided by the government as part of the delegation, if the burdens associated become too onerous, they can exit the relationship.[20] That may not be a problem for the public principal(s) if there are many other firms willing to supply the services, but it is a big problem if there is not another firm ready and able to step in. Knowledge of firms'

[20] The transaction costs associated with exiting the relationship, however, depends on the exact circumstances of the relationship.

ability to break off the relationship can lead to fewer requirements for and oversight of private actors.

After addressing the increased risk of slippage as a result of delegation to private actors, the next risk of government delegation to private actors to discuss is that of diminished capacity within the government after delegation. As administrative law scholars Jody Freeman and Martha Minow discuss in their book on government contracting, all three branches of government may lack the knowledge and information to properly supervise delegations in an era of increased outsourcing. Thus, there may be no one left to ensure that implementation by private actors meets "democratic norms" (Verkuil 2006, 418; Freeman and Minow 2009, 2-5).[21] This is of particular concern where the services provided by the private actor are complex and the principals must have expertise in the subject area to evaluate the quality of the services provided.

For these reasons, delegation to private actors is fraught with risk that those actors will behave in a way not desired by government or the people who themselves have delegated powers to the government to act on their behalf. The success or failure of the government's attempt to hold private actors accountable under ERISA – to force them to comply with government will or to correct their behavior where they fail – is therefore the second motivating question behind my dissertation.

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[21] "More broadly, widespread contracting out could wreak havoc with the balance of power among the branches of government: weakening the legislative and executive branches through fragmentation and delegation, and overburdening the judiciary with challenges to contractual schemes" (Freeman 2000, 156-57).

Accountability Mechanisms

The tools available to public principals seeking to hold private actors accountable are extensive. Freeman and Minow (2009, 3) identify "three accountability regimes of law, markets, and politics" to structure oversight of private actors. These categories are useful for exploring existing and potential oversight of delegation outside of the formal contract scenario as well. I am concerned here with the failure of market accountability and a proposal for improved legal and political accountability in its place.

I will not discuss market accountability in depth because the situations in which it fails like ERISA are the ones that motivate my research. "With perfect contracting and regulation, there is no difference between state and private provision of goods and services. . . . the pursuit of 'social goals' does not, on its own, make the case for government ownership" (Shleifer 1998, 135). In fact, Shleifer (1998, 139-40) argues that government provision of services only makes sense where: (1) there are opportunities for cost cutting by private firms that reduce quality of services provided; (2) innovation by firms is not a big factor; (3) consumer choice is impeded by a lack of competition; and (4) firms are not concerned about harming their reputation by failing to provide high quality goods and services in the area. Since ERISA is precisely one such situation – where firms are motivated to reduce amount or quality of services and those details are not (or cannot be properly) specified in a contract, innovation is not a big factor, there is little competition or high transaction costs make switching suppliers difficult, and reputation concerns for firms are muted – market accountability is insufficient. Relying on "customer satisfaction" is not proper

where consumers have difficulty learning about the quality of the services supplied and difficulty switching suppliers even if they do gain such information (Freeman and Minow 2009, 16).

Government accountability usually entails a mix of political and legal measures (*e.g.*, elections and enforcement in courts, respectively). Insufficient investment in government oversight is made because one purpose of delegation is to save money (Freeman and Minow 2009, 16-17). Costly oversight in the form of expanded bureaucratic capacity for supervision or a new venue for adjudication of disputes negates the value of privatization and can hold the failings of private delegates up for public inspection and outrage – resulting in political consequences. For this reason, altering political accountability is more difficult than altering legal accountability.

Improving legal accountability can also help motivate and improve political accountability.[22] Administrative law scholars do not view lawsuits in isolation as providing comprehensive security when supervising private actors. "Ideally, legal reforms should prompt agencies to . . . monitor government contractors more thoroughly. Agencies likely will have superior access to information [about consumer needs and the services provided]" (Mendelson 2009, 243). Even if procedures applied to executive agencies under the Administrative Procedure Act (APA) and Freedom of Information Act (FOIA) are applied to private actors through the legal system, oversight by Congress, the executive, and the public is necessary (Mendelson 2009, 244).[23]

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[22] The same values that pervade political accountability mechanisms are important when focusing on legal accountability. "Public participation" and "rights of review" are key (Green 2007, 13). Transparency is necessary for the public to participate and to ensure a full review (13).

[23] Providing for APA and FOIA-like transparency and rights of comment involve the public in "implementation and monitoring" and help ensure the legitimacy of service provision by private actors (Aman 2009, 264-65).

In many ways, legal accountability under ERISA has failed. And its domination of political accountability has multiplied the effects of that failure. The ascendancy of the private litigation remedy in ERISA and the failure of the courts to sufficiently protect plan participants as intended by Congress adds to the debate about how and whether private litigation remedies are a useful accountability tool. The interaction of the political and legal accountability mechanisms under ERISA also informs whether redundancy is beneficial or causes coordination problems. In the end, a delicate political compromise and the inability to adjust and remake political bargains when accountability proved insufficient hindered the achievement of ERISA's core goal.

Fiduciary Obligations as a Control Mechanism

Although political and legal accountability under ERISA has been imperfect, one success is ERISA's use of fiduciary duties to control the behavior of employers and their representatives and force them to elevate the interests of employees. Pension administrators and asset managers still face an inherent conflict of interest, but fiduciary obligations force them to tread lightly when making decisions. A fear of liability (not to mention pressure from regulators) influences the administration of pension plans. Had more effective political and legal enforcement existed, fiduciary standards could have been the answer to the need to delegate broad authority to private, self-interested actors under ERISA.

When the policy space is very complex, as with pension regulation, grants of power are necessarily broad and provide private actors with great discretion. "Certain public problems . . . lend themselves to neither specific behavioral commands nor measurable outcomes." (Bamberger 2006, 389). Congress typically sacrifices control to realize the benefits of bureaucratic expertise, and the same may be said for delegation to private actors. Facing a lack of access to information possessed by private actors, this delegation is at times an expedient and necessary strategy.[24] Congress has used the strategy of delegation in areas of complex legislation and difficult political compromise for many years. In fact, leaving significant discretion to the private sector instead of burdening it with cumbersome regulation is frequently part of the political compromise.

Acknowledging that Congress may not have the ability to set forth detailed instructions when delegating to private actors in a complex area, or may not want to do so because curtailing discretion results in sacrificing the benefits of agents' expertise, the question remains how to ensure accountability and thereby "tame complex risk" (Bamberger 2006, 380). "[D]iscretion in the interpretation and implementation of regulatory directives may compromise three related governance values: *rationality* in choosing between solutions; *responsiveness* to public interests; and *reviewability* by others" (Bamberger 2006, 403). Therefore, any proposed method of

[24] Agencies delegate to the private firms they regulate in these complex areas to obtain the benefits of their expertise. As legal scholar Kenneth Bambeger (2006, 392) has written in this area, agencies and the private actors they regulate "are partners in regulation, implicitly and explicitly enlisted to fill out the substance of legal norms and develop the means for implementing those broader principles locally." The political science literature too explores the give and take between agencies and the private actors they regulate, seeing influence and coercion flowing in both directions. See Gordon and Hafer (2007); Lieberman (2010).

improving accountability of private actors to whom authority has been delegated by legislators (and agencies) should be evaluated to determine whether it meets these important criteria.

The common law has been handling complex delegation issues under the classic principal-agent scenario for many years. The law of agency addresses the problems that arise when an agent enters into a fiduciary relationship with a principal – when the relationship triggers a higher level of protection because of the special vulnerability of the principal in the relationship. A conflict of interest exists here because the agent is tasked with ignoring his own interests in favor of those of another (Metzger 2003, 1463). It is necessary to address, then, whether common law or codified fiduciary standards are a sufficient means of holding private actors accountable.

My dissertation explores the ability of fiduciary duties to maintain or help maintain accountability over private actors to whom the government delegates substantial discretionary authority in a complex area. ERISA is an example where Congress delegated substantial authority to private actors in a complex policy space and utilized fiduciary standards developed by courts under the common law and enforced by both the bureaucracy and those courts to hold actors accountable. It is not the only example where fiduciary standards are used to hold private actors accountable. For example, the foster care system holds foster parents accountable for meeting their fiduciary duties under state common law. ERISA, however, has the benefit of greater transparency for research purposes since it was a significant federal statute where common law fiduciary standards were codified (showing intent to use fiduciary duties as part of

an accountability regime) and copious legislative history exists. There are also several decades of evidence showing the effects of ERISA's design, including significant case law.

Plan for Dissertation

My dissertation provides an analytical history of ERISA that explores its methods of delegating both policymaking control over and the detailed nuances of administration of private pension plans to private actors. Regardless of whether fiduciary standards have ensured sufficient accountability in the ERISA context – and I find that they have not – I argue that the potential is there and offer some observations on where ERISA went wrong.

Chapter 1 explores what it means to be a fiduciary. The nature and responsibilities of this role are instructive when evaluating its success in holding private actors accountable.

Chapter 2 chronicles the lengthy battle to pass ERISA, focusing on how common law fiduciary standards became a central part of the statute.

Chapter 3 addresses why Congress decided to delegate such extensive responsibility over pensions to private actors.

Chapter 4 discusses the triumph of legal accountability over political accountability in ERISA's implementation through an absence of strong bureaucratic enforcement.

Chapter 5 explains the failure of legal accountability under ERISA – in essence, what went wrong and why the private litigation remedy failed to properly enforce ERISA's fiduciary protections, resulting in a lack of accountability.

The Conclusion examines how fiduciary obligations as enforced by the bureaucracy and the courts failed to hold private actors accountable under ERISA based on the criteria set forth in the Introduction. I argue that there is still hope for fiduciary protections to play a vital role in accountability mechanisms where the government delegates extensive authority to private actors in a complex area.

CHAPTER 1

CRAFTING FIDUCIARY RELATIONSHIPS: POWERS AND DUTIES

To evaluate fiduciary status and duties as a mechanism for holding private actors with delegated powers accountable, it is necessary to first explore what it means to be a fiduciary. Although ERISA has codified common law fiduciary standards, the courts continue to inform our understanding of fiduciary powers and duties through interpretation and enforcement of this statute. The common law is therefore at the center of any discussion about who fiduciaries are and how they can and should behave. This chapter traces the delicate balance back and forth between power and duty, discretion and restriction. Special risks inherent to all or some fiduciary relationships are addressed. Finally, the traditional theory that public officials are constrained by fiduciary obligations to those they govern connects the courts' historical attempts to reign in private fiduciaries with historical attempts to reign in public fiduciaries. The country has long used fiduciary protections to hold both public and private actors with significant power over others accountable.

Defining a Fiduciary Based on His Powers

A clear definition of the fiduciary role in American society is difficult given the many different responsibilities and powers that fiduciaries possess.[25] As Justice William Brennan of the United

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[25] The word "fiduciary" developed in nineteenth century English courts to describe relationships of trust existing outside the formal legal meaning of that word as modern trust law developed to encompass specific agency relationships. See Sealy (1962, 70-71, 74-79), seeking to narrow the typically broad definition of fiduciary

States Supreme Court wrote:

> [T]o say that a man is a fiduciary only begins the analysis; it gives direction to further inquiry. To whom is he a fiduciary? What obligations does he owe as a fiduciary? In what respect has he failed to discharge these obligations? And what are the consequences of his deviation from duty?

(quoted in Frankel 2011a, 2). Thus, the heart of the fiduciary concept is the relationship between the fiduciary and the person who places his trust in that fiduciary (a "beneficiary"[26]) to accomplish a task. Generally, a fiduciary relationship forms when one party acts on behalf of another "while exercising discretion with respect to a critical resource belonging to the beneficiary" (Smith 2002, 1402). For example, fiduciary relationships arise because service providers, such as lawyers, doctors, and investment advisers, offer an expertise that is not common or easily obtained.[27] The parties to a fiduciary relationship set the initial terms and conditions under which the property or power will be shared by one with another. The law then enforces these terms or sets limits on what the terms may be (Frankel 2011a, 8).

The difficulty of creating a unified theory of fiduciary law based on legal history is evident in the repeated attempts by Professor Tamar Frankel to do so and the responses of other legal scholars

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relationships by classifying such relationships into four overlapping categories: (1) where a person has control of the property of another; (2) where a person is given a job by another; (3) where a person has limited or partial rights to property; and (4) where one person has undue influence over the other.

[26] There are various terms used to refer to the person who places his trust in a fiduciary, such as a "principal" under agency law, a "beneficiary" under trust law, and a "participant" or "beneficiary" under pension law. Professor Tamar Frankel coins the term "entrustor" for use in her articles and book exploring a unified concept of fiduciary law. In this section, I use the term "beneficiary" since I discuss fiduciary law in general and the roots of ERISA in trust law. The use of the term "beneficiary" instead of "principal" also has appropriate connotations regarding the power imbalance in the fiduciary relationship between pension provider and participant.

[27] These traditional relationships, including trustee/beneficiary, director/shareholder, and attorney/client, have been described as "formal", while many "informal" relationships of trust have been defined as fiduciary without a clear explanation for when a relationship based on trust should rightly be called such (Smith 2002, 1412 *et seq.*).

to her work. Attempting to provide concrete guidance, Frankel (2011a, 4) identifies three common characteristics of all fiduciary relationships: (1) "entrustment of property or power," (2) trust of fiduciaries by those beneficiaries who provide them with property or power, and (3) risk to those beneficiaries. This last element, which can also be called the "potential for opportunism" (Smith 2002, 1444), is the key to the creation of laws regulating fiduciary relationships because when the risk (or potential costs) of trusting fiduciaries becomes too high, these important relationships will not take place.[28] Laws are imposed to mitigate the risk involved with trusting another person and prevent harm to those who give their trust, and Frankel argues in favor of broad fiduciary protections.

Some legal scholars who view fiduciary law as merely a species of contract law, however, seek to narrow the range of relations brought within the protective orbit of fiduciary law and to narrow the protections themselves. Professor Larry Ribstein (2011, 901) favors a definition of fiduciary relationships that does not encompass broadly such relationships as those between doctor and patient or spouses. Ribstein instead defines a fiduciary as one who has "open-ended management power over property without corresponding economic rights." Under this definition, a fiduciary possesses unwavering discretion to act through power delegated by the property owner.

As the discussion above illustrates, there is great debate over the proper definition of a fiduciary and the proper reach of fiduciary duties. When regulating different relationships of trust,

[28] Without an information asymmetry, there is no incentive to hire the fiduciary for his advice and services, but this very asymmetry requires regulation (Cummings and Finke 2010).

lawmakers and courts choose who will fall into this fiduciary category. Lawmakers and courts also decide whether strict fiduciary protections are required or if the parties can be left to bargain among themselves.

The Role of Discretion in the Fiduciary Relationship

Fiduciaries are hired for their expertise and require discretion to use their skills to aid beneficiaries. Beneficiaries may not even know enough about the area of expertise to tell fiduciaries how to accomplish their tasks or closely supervise their work. In addition, a long-term relationship would be overly cumbersome and costly if a beneficiary had to set forth every possible future task for a fiduciary and would not be flexible enough to address changing conditions (such as changing stock market conditions) (Frankel 2011a, 25-35; Sitkoff 2011, 1040-41). In the past, the law sought to limit the amount of discretion accorded fiduciaries (*e.g.*, by terminating an agent's authority on the incapacity of his principal and by disabling a corporation from acting outside the limited purpose set forth in its charter), but this prevented fiduciaries from engaging in useful behavior (Sitkoff 2011, 1042). The amount of discretion accorded to the fiduciary depends on the nature of the task assigned to the fiduciary and the amount of independence accorded to the fiduciary to accomplish these tasks without directions from the beneficiary (Frankel 1983, 810). With increased discretion, however, comes an increased liability in the form of fiduciary duties (Frankel 2011a, 25-35; Sitkoff 2011, 1042).

The risk that a fiduciary will abuse his or her power can be mitigated through mechanisms other than fiduciary law. First, power will ideally be delegated to a fiduciary who does not have a conflict of interest with the beneficiary. It is unlikely to find a completely disinterested party to serve as fiduciary, however, particularly now that most fiduciaries are in the business of providing such services (Frankel 1983, 811). Second, performance based compensation helps ensure that it is in the fiduciary's interest to achieve optimal performance when managing property. Such compensation spreads the risk of a poor outcome between the beneficiary and the fiduciary (811-12). Third, the beneficiary may control the fiduciary by retaining the right to terminate the fiduciary, specifying in a detailed contract the terms of the relationship, providing direct orders instead of delegating, or setting forth detailed standards for the fiduciary's conduct. Unfortunately, these checks on fiduciary power involve high monitoring costs and undermine the very purpose for the fiduciary relationship (812-14).[29]

The amount of discretion beneficiaries are willing to allow is also dictated by the type of laws governing fiduciary behavior. General standards provide more discretion than bright-line rules that spell out in detail how a fiduciary must behave. "Fuzzy rules . . . leave a gray area that presents a risk of violating the law," although they may also help reduce enforcement costs by leaving fiduciaries uncertain of the extent of their reach and therefore unwilling to push their behavior to the boundary between legal and illegal (Frankel 2011a, 104-05). With broad standards like the duties of loyalty and care discussed below, courts seek to complete the parties'

[29] Frankel (1995, 1222-23) also mentions and discards the possibility of insuring against the risk of loss due to breach of fiduciary duty. Not only would it be difficult to decide on the proper level of coverage, but insurance companies are unlikely to insure against intentional misconduct. Finally, the cost of such insurance would be at least partially passed on to beneficiaries, decreasing the utility of fiduciary relationships.

agreement by setting the terms they would likely have agreed to had they anticipated the situation in question. This reduces transaction costs when entering into a fiduciary relationship since the parties themselves need not enter into terms that cover every possible situation that could arise. It also, however, increases "decision costs" by forcing the judiciary to more actively regulate fiduciary relationships (Sitkoff 2011, 1044).[30]

Fiduciary Duties

Most discussions of fiduciary duties focus on the duty of loyalty and the duty of care.[31] Recent research has debated whether fiduciary law is or should be a body of law distinct from contract law. This debate has implications for whether fiduciary duties offer additional safeguards in a relationship that make it more reasonable for government actors to delegate their authority to private parties.

The foundation of this debate is the economic analysis of "contractarians" Judge Frank Easterbrook and Professor Daniel Fischel (1993) that states unequivocally that fiduciary relations fall within the various types of contractual relations. As they state, the fiduciary "package" is "empty" because the parties still contract for their own gain – the basic purpose of any contract (426). According to Easterbrook and Fischel, under fiduciary law, judges use the guise of the

[30] See Chapter 5 for a discussion of how the judiciary, however, failed to actively monitor compliance with ERISA's broad fiduciary standards as expected when the statute was passed.

[31] Professor D. Gordon Smith (2002, 1409-10) asserts that fiduciaries are expected to be more careful about self-interested behavior than a party merely engaged in a contractual relationship with another because the fiduciary relationship is not limited by the four corners of the contract.

duty of loyalty to provide a "public service" by filling in the terms the parties would have agreed to if the cost was not prohibitive to specify the terms to govern all possible situations (427). "Fiduciary duties are not special duties; they have no moral footing . . ." because they are subservient to actual contracts and the parties can contract out of their obligations (429).[32] Langbein (1995-1996, 650)[33] agrees with Easterbrook and Fischel that fiduciary duties are contractual because the formation of fiduciary relationships is voluntary and fiduciary law's protections are default rules that can be circumvented by the parties.[34] However, he argues that Easterbrook and Fischel are "too dismissive" when they say that fiduciary duties "have no moral footing" because "they embody deep moral precepts about the behavior appropriate for a trustee or other fiduciary" (658).

On the other side are "anti-contractarian" arguments that there is something unique about fiduciary relationships that requires special protection and takes these relationships outside the

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[32] "Contractarians" like Ribstein argue that fiduciary protections should be narrowly construed and do not always see fiduciary rules as beneficial in society. As Justice Benjamin Cardozo famously described the standard for fiduciary behavior in *Meinhard v. Salmon*, 164 N.E. 545, 546 (N.Y. 1928):

> Joint adventurers, like copartners, owe to one another, while the enterprise continues, the duty of the finest loyalty. . . . A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior.

(quoted in Ribstein 2011, 903). According to Ribstein (2011, 913), compensation structure and enhanced disclosure of conflicts provide sufficient protection for the relationship, and broad fiduciary protections are unnecessary.

[33] Langbein (1995-1996) explores generally how the need for additional trustee discretion in the modern era of portfolio management resulted in a shift from limited trustee powers to broad discretion governed by the protections of fiduciary duties.

[34] But see Hansmann and Mattei (1998, 466-67, 471), asserting that Langbein says trust law is contractual because of his normative purpose to make trust law less restrictive on trustees who face conflicts of interest. Instead, they argue that the property-based features of trusts are central and not contractual aspects. The trust form is used as a device in American pension funds, for example, to segregate and safeguard assets from a corporation's creditors.

realm of contract law. Although scholars on this side of the debate have difficulty agreeing on what makes fiduciary relationships different from other, non-fiduciary relations, they agree that fiduciary relationships differ from contract relationships in "doctrinal structure" and "ethical basis." They believe that fiduciary relationships "facilitate the doing of justice, that they promote virtue, and that they enhance freedom in a distinctive way" (Fitzgibbon 1999, 305).

In a fiduciary relationship, unlike in contract, the beneficiary is dependent on the fiduciary. This dependence is the reason that fiduciary law is designed to protect the beneficiary. Unlike in contract law, where both parties seek self-gain and the law sanctions such conduct, fiduciary law is designed to protect the beneficiary (Frankel 1983, 800).

Anti-contractarians argue that fiduciary obligations are not merely default contract provisions. Professor Deborah DeMott (1988) argues that contractarians are "traveling light as legal theorists" by assuming that simply because fiduciary duties may at times make it unnecessary for parties to detail these obligations in a contract, fiduciary duties are default rules or implied contractual provisions. She calls on contractarians to make it clear if they are instead making a normative argument (889).[35] Frankel (1995) also argues that it is a cumbersome process for a beneficiary to waive any of the fiduciary duties (and some cannot be waived at all), and therefore courts are not merely rewriting the agreement between the parties as they would do so without

[35] In return, Easterbrook and Fischel (1993, 434, citing DeMott 1988, 909-10) take issue with DeMott because she states that fiduciary law is a tool that allows the law to respond to situations in which "one person's discretion ought to be controlled," which they argue is not a cohesive theory like that of contract law. Yet, "[n]either 'contract' nor 'fiduciary' exists in nature" (Brudney 1997, 596). The idea that contract entails a voluntary relationship between parties seeking self-gain where the parties freely set their terms without government interference is not without controversy. The state does intervene to set the rules on which the parties' bargain will be enforced, and some rules cannot be circumvented by contract (Brudney 1997, 597-98).

transaction costs. To waive fiduciary duties: "(1) [beneficiaries] must receive notice of the proposed change in the mode of the relationship; (2) [beneficiaries] must receive full information about the proposed bargain; (3) the [beneficiaries'] consent should be clear and the bargain specific; (4) the proposed bargain must be fair and reasonable" (1234). It seems unlikely that fiduciaries will be able to easily meet these requirements and transform the relationship into a true contractual relationship where both parties have freedom to bargain and define their relationship.[36]

I agree with the anti-contractarians that fiduciary law is a distinct body of law. Even if it is difficult at times to define precisely who is a fiduciary or what a fiduciary does, fiduciary obligations provide the reassurance necessary for these relationships of trust to occur. As my dissertation shows, these obligations also provided the reassurance necessary for the state to delegate an enormous amount of authority to private actors. These private actors' behavior is limited by the fiduciary standards contained in a statute or set by common law, but standards necessarily sacrifice certainty in their application for flexibility to cover a variety of circumstances and prevent having to revisit a rule each time a new set of facts arises to which it is applied (Hart 1961, 124-28). Much discretion and therefore power is placed in the hands of fiduciaries, as explained by legal theorist H. L. A. Hart (1961, 125):

> It is a feature of the human predicament (and so of the legislative one) that we labour under two connected handicaps whenever we seek to regulate unambiguously and in advance, some sphere of

[36] In addition, there is the question of why much of fiduciary law is left to the province of common law while a few, exceptional categories of fiduciary relations are governed by statute and how this affects the debate over whether fiduciary obligations are merely a species of contract. The length of the fiduciary relationship and information and power asymmetries between employers and employees may be one explanation for ERISA's exceptionalism (Romano 1993, 449).

> conduct by means of general standards to be used without further official direction on particular occasions. The first handicap is our relative ignorance of fact. The second is our relative indeterminacy of aim.

The Duty of Loyalty

The duty of loyalty requires that fiduciaries act solely in the interest of beneficiaries.[37] The duty requires that fiduciaries avoid self-interested behavior when "exercising discretion with respect to the beneficiary's critical resources" (Smith 2002, 1407). The duty of loyalty also requires that the fiduciary adhere to instructions provided by the beneficiary, act in good faith, and account to the beneficiary (disclose information) (Frankel 2011a, 108, 122, 129).[38]

Disloyalty typically occurs when there is a conflict between the fiduciary's interests and the beneficiary's interests but may also involve representing multiple beneficiaries with conflicting interests. Disloyalty can occur in three scenarios. First, the fiduciary uses his position (without the beneficiary's consent) to direct business opportunities to himself ("self-dealing"). For example, the fiduciary passes himself off as the owner of the trust property and uses it as collateral to purchase additional property. Second, the fiduciary transacts with the beneficiary

[37] "Unless otherwise agreed, an agent is subject to a duty not to act or to agree to act during the period of his agency for persons whose interests conflict with those of the principal in matters in which the agent is employed." Restatement (Second) of Agency § 394 (1958). According to Ribstein (2011, 208-10), this is the only true fiduciary duty. Other related "non-fiduciary" duties, such as the duty of care, are implied in contract. Law Professor D. Gordon Smith (2002, 1406-07, 1409) similarly argues that fiduciary duty refers only to the duty of loyalty because "the duty of care is 'not distinctively fiduciary.'" As will be discussed below, regardless of how one may define the concept of fiduciary duty using legal history, Congress defined fiduciary duty to include the duty of care under ERISA. In doing so, Congress relied on its own interpretation of fiduciary duties as mediated by legal scholars and judges.

[38] Although these duties are related to the duty of loyalty, they are frequently cited as distinct duties.

with his or the court's consent but that consent is based on inadequate disclosure. For example, the fiduciary invests the beneficiary's assets with the beneficiary's consent but does not tell the beneficiary that the company he is investing in is owned by the fiduciary's brother. Third, the fiduciary transacts with a third party in a way that implicates the beneficiary's interests, such as misappropriating an opportunity and pursuing "secret profits" (Cooter and Freedman 1990, 305-06). For example, a buyer of real estate purchases a house from a seller through the seller's real estate agent. The agent, a fiduciary, knows that the price offered is above the seller's minimum sales price but pockets the difference without informing the seller (DeMott 2007, 1053).

Since delegating discretion to a fiduciary necessarily involves ceding control, the difficulty with penalizing breaches of the duty of loyalty is discovering them. A poor outcome (such as a negative return on investment) does not necessarily mean that the fiduciary has engaged in a self-interested act (such as misappropriating all or part of the value of property entrusted to the fiduciary). While the beneficiary can observe the outcome, because the outcome is based both on the fiduciary's act and chance it is difficult to tell whether the fiduciary's act or chance caused the poor outcome (Cooter and Freedman 1990, 330-31). In addition, the more effort the beneficiary must expend in monitoring a fiduciary to prevent a breach of this duty, the less reason there is for the existence of the fiduciary relationship at all since the costs may begin to exceed the benefits.

Penalties for breach of the fiduciary duty of loyalty seek to rectify this situation. The duty of loyalty under common law carries remedies taken from the law of contracts, torts, restitution,

and unjust enrichment (DeMott 2007, 1049). If the only remedy were disgorgement of ill-gotten gains, given imperfect enforcement, there would still be a large incentive for the fiduciary to breach his duty. More is needed to deter improper conduct (Cooter and Freedman 1990, 304). The aggrieved party need only demonstrate that the fiduciary's actions were a substantial factor in a loss to the beneficiary – a low threshold. Once this burden is met, the beneficiary may be entitled to punitive damages in addition to requiring the fiduciary to disgorge any gains received through improper use of the beneficiary's property (even if the beneficiary was not harmed at all by the breach) (DeMott 2007, 1056-57). The deterrent value of these remedies demonstrates the importance at law of preventing breaches of the fiduciary duty of loyalty.

The prohibitions on self-interested behavior by fiduciaries do not seek to prevent all self-dealing, however. Rather, they promote advance disclosure to the beneficiary so that he can make an informed decision on whether to consent to the transaction (Sitkoff 2011, 1043). The fiduciary's ability to obtain advance consent and his ability to terminate the relationship soften the harshness of remedies for breach of the duty of loyalty (DeMott 2007, 1052-53).[39] The high cost of penalties for fiduciary breaches has not deterred many from entering the field, and providing

[39] But see Langevoort (2011, fn 30), discussing how disclosure may give fiduciaries "greater moral wiggle room" and result in greater acceptance of their advice among beneficiaries. Even when aware of a conflict of interest, beneficiaries rarely have full information about how that conflict has affected a fiduciary's advice, frequently discounting possible bias or at least exhibiting an increased tendency to accept the advice based on the existing relationship of trust (citing Cain 2005 and Sah 2011). Although an experiment by Church (2009) finds that disclosure and the threat of sanctions in the financial adviser/advisee context resulted in less biased advice by the adviser and better evaluation of that advice by advisee, their experiment models sanctions as costly for the beneficiaries but certain to result in punishment where the fiduciary engages in bad behavior. The experiment also assumes the advisee has complete freedom regarding whether to invest or not and that the relationship is a one-time interaction – an unrealistic scenario because pension plan participants, for example, do not choose the plan's financial adviser(s) and most adviser/advisee relationships involve repeated interaction (see Langevoort 2011, fn 30).

fiduciary services has become a big business with big profits. As a result, there is frequently a culture at these companies that serve as fiduciaries that motivates greed and self-dealing instead of ethical behavior (Langevoort 2011).[40]

The Duty of Care

The duty of care requires fiduciaries to act "with prudence, attention, and proficiency" in providing their services (Frankel 2011a, 169).[41] Fiduciaries must have or obtain the information required to competently perform their tasks and act on such information after engaging in a reasonable deliberative process (Cooter and Freedman 1991, 1062). Fiduciaries are required to use the specialized training and skills that caused the beneficiary to hire them and to react appropriately to unfavorable circumstances (Frankel 2011a, 172-73). The performance of a fiduciary with specialized training and skills is measured by the standard of what a "reasonable or prudent person" with those skills would have done in the same circumstances (Sitkoff 2011, 1044). This standard does not hold fiduciaries liable for mistakes or unfavorable outcomes but instead for failing to complete their duties in a professional manner (Frankel 2011a, 170-74).

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[40] "It is thus worth thinking hard about what the favored traits are in the fiduciary business and how they interact with – and easily frustrate – the law's efforts to insist on fiduciary responsibility from those who are, in heart and soul, salespeople" (Langevoort 2011, 995).

[41] Like Ribstein and Smith, Professor William A. Gregory (2005, 183) argues that the duty of care is not a fiduciary duty at all but instead a negligence concept that has been conflated with the fiduciary duty of loyalty by courts and legal scholars. He argues that "[t]o describe negligent acts as being breaches of fiduciary duty is misleading, because a breach of fiduciary duty 'connotes disloyalty or infidelity. Mere incompetence is not enough.'" Gregory's point is that only duties that are unique to the fiduciary role are fiduciary duties. Instead, he argues that the duty of care always falls under tort law (188).

Measuring performance, however, is difficult. Even courts must rely on other experts to judge fiduciaries' performance (Frankel 2011a, 170-74). As with the duty of loyalty, it is difficult to determine whether the fiduciary has used "reasonable" effort based on outcome since, in the absence of disloyalty, a poor outcome can result from either poor effort or chance (Cooter and Freedman 1991, 1056-57).[42] Courts typically evaluate the "process" used by the fiduciary to fulfill his role (Laby 2004, 117). Unscrupulous intent is not required to find a breach of this duty (Laby 2004, 109).[43]

Special Risks Associated with Many Beneficiaries and a Large Amount of Assets

Typically, as the number of beneficiaries increases, the total amount of property (*e.g.*, money) that the fiduciary is responsible for increases. As is often the case, with more money comes more power for the fiduciary. Among other responsibilities, fiduciaries select service providers to help manage assets, such as lawyers and investment advisers, and these third parties compete to please the fiduciaries that hire them – not the beneficiaries who own the assets. Two consequences are: (1) externally, it becomes difficult for those doing business with a fiduciary to distinguish whether he manages the assets or owns the assets and (2) internally, each

[42] "Whether the trustee is prudent in the doing of an act depends upon the circumstances as they reasonably appear to him at the time when he does the act and not at some subsequent time when his conduct is called in question" (Laby 2004, 119, quoting Restatement (Second) of Trusts 174 cmt b (2004)).

[43] Professor Arthur Laby (2004, 141-45) argues that the negative duty of loyalty trumps the positive duty of care. This emphasizes the importance of trust in the relationship between fiduciary and beneficiary rather than the quality of services provided. One example of how the two duties can conflict in the ERISA context was faced by Enron directors who also served as administrators of the company's ERISA plans that invested in company stock. The court found that the plaintiffs stated a claim for breach of the fiduciary duty of loyalty to ERISA plan participants even though any disclosure of the company's precarious financial condition by the directors would arguably have violated their fiduciary duty of care to the company.

beneficiary’s control over the fiduciary is weakened because of the small share of his ownership (Frankel 2011a, 11). The first consequence leads to greater temptation to breach the duty of loyalty, as discussed above, and the greater ability to do so since because of apparent ownership of the assets managed. My focus in this section, however, is the distinct difficulty in controlling the fiduciary as the number of beneficiaries increases.

Acting as a fiduciary to a large number of beneficiaries is a public service role even when performed by supposedly private actors. In a 1995 article, Frankel defines “public fiduciaries” as those engaged in “commercial relationships, that is, mass-produced, non-personal relationships with numerous public [beneficiaries]” and private fiduciaries as only those in relationships with few beneficiaries (1251-52). She identifies two categories of public fiduciaries: (1) fiduciaries who manage large pools of assets for efficiency (*e.g.*, pension fund managers) and (2) fiduciaries to entities owned by many beneficiaries (*e.g.*, directors of public corporations). The first category, which I focus on in this section, is typically regulated by law as private fiduciaries (Frankel 1995, fn 117). I define public fiduciaries to include only government actors (*e.g.*, congressmen or employees of government agencies) and not fiduciaries to mass amounts of beneficiaries to tease out the differences between private parties supplying services to the mass public and government actors doing the same. Frankel’s terminology, however, indicates the easy comparison between her “public fiduciaries” and government actors, as discussed further in the section below.

Frankel (1995, 1252-53) recognizes that fiduciaries who provide services to a large number of beneficiaries have significant power because the beneficiaries are “rationally passive”, meaning that the cost for an individual beneficiary to monitor a fiduciary exceeds the small benefit to the beneficiary that results because of his small share of ownership. A fiduciary managing property for many beneficiaries cannot be subject to the direction of each beneficiary on a daily basis – that would make managing the property impractical and defeat the purpose of centralizing management to increase efficiency. With a large number of beneficiaries, it is more likely that each has a small financial interest and will not rationally expend the large amount of time, effort, and money necessary to monitor and/or remove the fiduciary for the entire group and will instead “free ride” on the effort of any active investors (1256). As Frankel states, “A fiduciary managing $500 million for one [beneficiary] has far less power than a fiduciary managing the same amount for 50,000 [beneficiaries]” (1257). Fiduciaries controlling the property of a large number of beneficiaries also have more power to affect the economy and financial order of our society. If beneficiaries feel powerless to control bad behavior among fiduciaries, if for example strong legal standards do not restrict fiduciary malfeasance, they may withdraw their assets from the system entirely (1259-60).

In addition to the general risk to all beneficiaries where a fiduciary has greatly increased power, there is a risk to beneficiaries that the fiduciary will prefer the interests of some beneficiaries over others. The fiduciary has many different principals to respond to – and it is often an impossible task to give all the beneficiaries, who will often have conflicting goals and desired strategies, what they want. As a result, under trust law, fiduciaries have a duty of impartiality

when dealing with various beneficiaries of a pool of assets managed by the fiduciary.[44] This duty falls within the duty of loyalty discussed above (Fischel and Langbein 1988, 1109; DeMott 2007, 1054).[45] At its most basic level, any payment from the pool of assets harms the interest of the other beneficiaries by reducing the pool of assets, and the fiduciary must decide who has the right to payment in different circumstances (Fischel and Langbein 1988, 1128-29).

When beneficiaries' control over fiduciaries is weakened for the reasons discussed above, the law seeks to protect their interests (Frankel 2011a, 39). Frankel argues that the more beneficiaries, the more strict regulation of fiduciaries and remedies for breaches of these rules should be (Frankel 2011b, 1297). However, the costs of regulation are high.[46]

[44] Although the duty of impartiality traditionally referred to the fiduciary's duty to consider both life and remainder interests in trust property (Langbein 2007, 1075), the duty is equally applicable for trusts that manage assets owned by large numbers of beneficiaries. See Restatement (Third of Trusts) § 79 (2007): "A trustee has a duty to administer the trust in a manner that is impartial with respect to the various beneficiaries of the trust."

[45] ERISA ignores impartiality and instead emphasizes that pension fiduciaries must act in the best interest of employees – implicitly assuming that those employees share common interests. The Revenue Act of 1921 first introduced the exclusive benefit rule, or the idea that an employer creating a pension plan had to set up a trust for the exclusive benefit of employees, into the American private pension system. ERISA continues this same rule (Fischel and Langbein 1988, 1109). Fischel and Langbein (1988, 1120-21, 1159-60), however, show that it is foolish to assume all pension plan participants have common interests. They detail typical conflicts, such as that between older and younger workers over the extent to which employers should provide compensation in the form of pension benefits at all and the conflict between active employees and retirees. ERISA's exclusive benefit rule does not sufficiently explain how to balance these competing interests, and, over a decade after the passage of ERISA, Fischel and Langbein argue for the incorporation of the trust law duty of impartiality into pension law.

[46] See Cummings and Finke (2010), arguing that all professionals providing financial advice should be subject to fiduciary standards instead of regulated by self-regulating organizations (*e.g.*, FINRA) or government to ensure that they act in the best interests of their clients. This would decrease agency costs.

Similarity of Public and Private Fiduciaries

Similarities between public and private fiduciaries make it easier for Congress to delegate authority to private actors subject to many of the same constraints they face when engaged in a relationship of trust with large numbers of people. Elected officials, whom I will call here public fiduciaries, and private fiduciaries are similar in that both face checks on their discretion (including the Constitution in the former case) to prevent mishandling of the trust placed in these officials and to ensure the use of due care in the performance of their services (Frankel 2011a, 279). The Founding Fathers were acquainted with fiduciary law (Ponet and Leib 2011, fn 34). They therefore set forth the terms governing public fiduciaries' performance of their duties just as the parties to a private fiduciary relationship agree on basic terms to govern their relationship (Frankel 2011a, 281-82). At the federal constitutional convention in 1787, many delegates espoused "ideals of fiduciary government," drawing on concepts already contained within state constitutions (Natelson 2004, 1083).[47] This comparison of public officials and private fiduciaries

[47] Federalist No. 49 ("The members of the legislative department, on the other hand, are numberous. They are distributed and dwell among the people at large. Their connections of blood, of friendship, and of acquaintance embrace a great proportion of the most influential part of the society. The nature of their *public trust* implies a personal influence among the people, and that they are more immediately the confidential guardians of the rights and liberties of the people."); Federalist No. 55 ("I am equally unable to conceive that there are at this time, or can be in any short time, in the United States, any sixty-five or a hundred men capable of recommending themselves to the choice of the people at large, who would either desire or dare, within the short space of two years, *to betray the solemn trust committed to them*."); Federalist No. 57 ("The aim of every political constitution is, or ought to be, first to obtain for rulers men who possess most wisdom to discern, and most virtue to pursue, the common good of the society; and in the next place, to take the most effectual precautions for keeping them virtuous whilst they *continue to hold their public trust*."); Federalist No. 63 ("Yet however requisite a sense of national character may be, it is evident that it can never be sufficiently possessed by a numerous and changeable body. It can only be found in a number so small that a sensible degree of the praise and blame of public measures may be the portion of each individual; or in an assembly [*i.e.*, the Senate] so durably invested *with public trust*, that the pride and consequence of its members may be sensibly incorporated with the reputation and prosperity of the community.") (papers cited in Natelson 2004, fn 19) (emphasis added).

is known as the public trust doctrine (Natelson 2004, 1087). As Grover Cleveland said, "We are the trustees and agents of our fellow citizens" (quoted in Natelson 2001, 192).

The public trust doctrine, as set forth by Professor Robert G. Natelson (2004, 1088, 1091) but nowhere formally required of elected officials, includes: (1) a duty to follow instructions, such as those outlined in the Constitution; (2) a duty of reasonable care; (3) a duty of loyalty; (4) a duty of impartiality, which requires that public officials not favor one group of citizens over another; and (5) a duty to account for their actions, including remedying harm (although this is limited in the case of public officials). The parallels between the duties owed by a private fiduciary, as discussed above, and the duties owed by a public fiduciary are clear.

The fiduciary duty of loyalty suggests (but does not require) that elected officials engage with the governed regularly to address any potential conflicts of interest (Ponet and Lieb 2011, 1258). The duty of care requires public fiduciaries to have the knowledge to execute their jobs and avoid "indiscretions" (Frankel 2011, 283). This duty also includes consulting the governed regularly to ascertain their wishes, although the public fiduciary must then use his own judgment and skills to translate those wishes into legislative action (Ponet and Lieb 2011, 1259).

Logic suggests that the fiduciary demands on public officials should be higher because it is so difficult for citizens to exit the relationship if they are dissatisfied with the officials' performance (Natelson 2004, 1088). Exit, even from a small, local jurisdiction, is inconvenient at best and

impossible at worst, and removing public officials is nearly impossible because the costs to organize such a campaign are high (Natelson 2001, 199).[48]

Yet there is no general fiduciary duty imposed on public officials, and they are instead subject to varying checks and balances designed to control their behavior indirectly (Natelson 2001, 193). Not only does an individual dissatisfied with an official's performance have far less legal rights vis-à-vis the official than he would against a private fiduciary, the official is rarely even subject to an accounting:

> The private fiduciary must be prepared to justify his decisions by showing reasonable investigation and disinterested analysis; if he cannot, he may see his decisions invalidated and be subject to liability. Yet outside a few instances in which the courts apply 'strict scrutiny' or 'intermediate scrutiny,' government officials may proceed on slender or no empirical basis and in circumstances of clear conflict of interest, and the courts will sustain the decisions and protect from liability those who made them.[49]

(Natelson 2001, 201-02). Natelson argues that the same fiduciary protections that apply to private fiduciaries should also apply to public officials because they help protect the vulnerable beneficiaries in this relationship of trust.[50]

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[48] It may, however, be similarly difficult for a single beneficiary to exit a relationship with a fiduciary that involves a large number of beneficiaries (see Frankel 1995, 1254, 1256-58). While the market may offer alternatives to the fiduciary, a single beneficiary lacks the power to make a change among service providers. In the context of employer-sponsored and tax-subsidized pension plans, exit by terminating the relationship (*i.e.*, quitting one's job) is costly.

[49] This of course assumes that private fiduciaries are frequently called to account, a proposition in doubt where they report to many beneficiaries who are rationally passive, as discussed above.

[50] To refute arguments that the application of fiduciary duties to public officials is not possible, Natelson (2001, 194) uses as an example the government of the Roman Emperor Trajan from 98-117 AD.

Just as Natelson recognizes the utility of an extra check on the power held by those who regulate the affairs of a large number of (frequently uninformed) beneficiaries, the traditional checks and balances established in the state have conditioned legislators to find solace in fiduciary law as a check on the behavior of private actors. This tool allowed Congress to delegate authority over the property of millions of employees to more well-informed employers that it acknowledged would always be tempted to act in their own self-interest. Congress believed that this tool of fiduciary protections could hold back the self-interested behavior of employers and their agents when acting for the beneficiaries.

There is an inverse relationship between private and public fiduciary power once Congress decides to regulate a particular field. An increase in private power comes at the expense of public control, and Congress ceded significant control over retirement income to private actors. The excesses of private fiduciary power in a time of limited regulation, as we have seen recently, frequently result in increased government control (Frankel 2011a, 285). For example, the well-known corporate governance failures in the Enron scandal resulted in the passage of the Sarbanes-Oxley Act in 2002. Therefore, the pendulum may swing back in the future, and Congress can retake some of the power over retirement income. The area of regulating private fiduciary power is still in its infancy compared to society's experience with regulating public fiduciary power – despite trust law's centuries-old legacy (Frankel 2011a, 286). The importance of Congress' willingness to utilize fiduciary law to protect the public and allow it to delegate substantial authority to private actors has not received the attention it deserves.

In Chapter 2, I will discuss how Congress delegated substantial authority to private actors under ERISA and whether fiduciary protections written into the law motivated the delegation. My focus here is to show Congress' intent to use fiduciary duties to hold private actors accountable, rather than simply continuing their role in protecting pension participants at common law.

CHAPTER 2

HOLDING EMPLOYERS ACCOUNTABLE: CONGRESS USES FIDUCIARY DUTIES TO PROTECT EMPLOYEES UNDER ERISA

Advocates of full codification of the common law – or law made by judges through court decisions – argue that there should be no gaps in the law, or instances where "the code does not provide a rule to solve the case" (Weiss 2000, 458). In fact, executive and legislative bodies that instituted legal codes "liked the idea of reducing judges to legal calculating machines, because it secured their own power over the law and it protected citizens from arbitrary standards in judging" (459). In practice, it has been impossible to codify the law without leaving gaps (459-62).

ERISA is not an example of a statute that left a few gaps open for regulatory agencies and the courts to fill. Instead, ERISA's framers acknowledged that they were leaving many details to be determined and, as discussed above, delegation in a complex area such as pension management typically involves leaving significant discretion to the agent. This chapter examines the role of fiduciary standards in Congress' decision to cede primary power over the many vagaries and gaps remaining in pension regulation after the passage of ERISA to private actors.

Why Codification of Common Law Fiduciary Standards Was Necessary

The most basic question to address when discussing ERISA's fiduciary rules is why they were enacted at all. As explained below, stricter minimum vesting standards (*i.e.*, rules regarding the

time it takes for pension participants to qualify irrevocably for their benefits and not risk forfeiting those benefits upon job loss, for example) and funding standards were needed because they did not previously exist – the government had allowed employers and employees to make their own pension bargains without setting any minimum terms. Judges had used state common law of trusts, however, to enforce fiduciary obligations against trustees for many years. ERISA required that all pension plans be in the form of trusts but need not have preempted state trust law's application to pension plans, so why was codification of the fiduciary rules necessary at all? And how, if at all, did ERISA change trust law?

In answer to the first question, codification was necessary because trust law was designed originally to respond to interfamilial gifts to a small number of people managed by neutral trustees. Codification was therefore necessary not to set in place an entirely new legal regime but instead to adapt trust law to the employee benefit context. In answer to the second question, ERISA expanded the fiduciary duties of trust law and made them mandatory for all involved in the administration of a pension plan – refusing to let fiduciaries opt out of the expansive new duties for pension plan administrators.

There has long been a debate among legal scholars regarding whether the common law should be codified in all areas of the law. "Codification refers to the legislative pronouncement of previously fluid judge-made law in an organized and authoritative form" (Rosen 1994, 1127). Although the debate was at its height from the 1830s to the early 1900s, with those against codification carrying the day, significant codification occurred starting in the middle of the

twentieth century.[51] Opponents of codification have traditionally argued that the common law adds needed "flexibility" that allows the law to adapt to changing facts and times, while proponents assert that unelected judges should not be making law (Rosen 1994, 1122-23). With respect to fiduciary standards, Congress incorporated these standards from trust law into ERISA, which is why agencies and courts look to trust law for answers when ERISA is silent or ambiguous (Langbein 1997, 168).[52]

Professor Langbein (2003, 1319) argues that "the reach of trust-law principles in ERISA is far deeper and more controlling" than the courts often recognize but that ERISA adapted trust law to the employee benefit context. ERISA codified the duties of loyalty and prudence from trust law but otherwise did not write existing trust law into the statute wholesale. Instead, Congress intentionally relied on the courts to look to trust law to fill in its "skeletal" outline and adapt trust law to the employee benefits context (1325-26). Unable to compromise on thorny political issues, Congress punted to the courts to make resolving these issues unnecessary. Refusing to spell out each detail of the legal framework that would govern employee benefit plans also gave Congress flexibility when regulating a complex field that few understood and whose response to such regulations fewer could predict (1329). Adopting much of the trust law framework saved

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[51] For a general discussion of the history of codification in American legal history, see Rosen (1994) and Weiss (2000).

[52] See *Varity Corp. v. Howe*, 516 U.S. 489, 496 (1996) ("In doing so, we recognize that these fiduciary duties draw much of their content from the common law of trusts, the law that governed most benefit plans before ERISA's enactment.") (internal citations omitted); *Firestone Rubber v. Bruch*, 489 U.S. 101, 110 (1989) ("ERISA's legislative history confirms that the Act's fiduciary responsibility provisions 'codif[y] and mak[e] applicable to [ERISA] fiduciaries certain principles developed in the evolution of the law of trusts.' Given this language and history, we have held that courts are to develop a 'federal common law of rights and obligations under ERISA-regulated plans.'") (internal citations omitted).

Congress the time of having to generate and agree on a new regime while also providing the legitimacy associated with a well-established body of law (1328).

Remarks by ERISA architect Senator Jacob Javits explain why codification of trust law was necessary and what fundamental changes were made to existing law. When introducing a comprehensive pension reform bill to the Senate on March 13, 1970 (over four years before ERISA was enacted), Javits cited three reasons why the existing framework of fiduciary protections under state trust law was not sufficient in the pension context. All of these reasons relate to conflicts between employer (or the employer's agents) and employees and conflicts among employees. First, he argued, "there is a very serious problem arising from the fact that at common law the definition of 'trustee' is quite narrow in scope, while in pension and welfare trust administration, the number of persons who handle and exercise control of the funds is much broader." Javits first goal was thus to protect beneficiaries by subjecting more of the service providers administering pension plans to fiduciary rules. Second, he noted that trust law developed to deal with relationships involving a small number of beneficiaries. He recognized the problems inherent in the pension context where each benefit fund might have thousands of participants and beneficiaries. Simple issues such as regular communication regarding trust matters become complicated because of the sheer number of plan participants and the distance between fiduciary and beneficiary.[53] Finally, Javits stated that trust law permitted exculpatory

[53] Javits stated that at common law, "[t]hese trusts usually involve but a single settler and, at most, a relatively small, well defined class of beneficiaries. . . . Clearly, this body of traditional trust law, vast as it is, must be applied quite differently to employee benefit plans which are the product of collective bargaining and may cover thousands of employees of many different employers." S. 3589–Introduction to Employee Benefits Protection Act–Administration Bill to Amend the Welfare and Pension Plans Disclosure Act, 91st Cong., Cong. Rec. 7278-79 (March 13, 1970).

clauses that helped fiduciaries avoid responsibility for breaching their duties, and this did not provide the security needed for pension plan participants.[54]

Court decisions permitting employee benefit plan administrators to opt out of their fiduciary obligations prior to ERISA show the need for codification of trust law in relation to pension plans. Exculpatory provisions in trust documents were allowed by courts even where the trustee had duties to numerous people and a collective action problem made it difficult to argue that the provision was duly bargained for by all parties (Coffee 1989, fn 138). In *Collins v. Storer Broadcasting Co.*,[55] the court found that even if the defendant committee members were trustees administering the profit-sharing plan at issue, the exculpatory clause exempted them from liability except for "wilful misconduct" because the creator of a trust has the legal right to create such a provision in the trust documents. Thus, trustees operating under a trust agreement with an exculpatory clause can be held liable only for an act "more than involuntary, inadvertent, negligent, mistaken, careless or accidental default . . . an intentional failure to do or not to do something required – an affirmative wrong."[56] Generally, exculpatory provisions in trust agreements limiting a fiduciary's liability for negligence were upheld under common law unless they violated clearly stated public policy.[57]

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[54] Id. at 7278-79, 7285-86. Ignoring the likelihood that savvy trustees could take advantage of those creating trusts, trust law historically permitted exculpatory clauses in trust formation documents that exempted trustees from liability for anything other than egregious conduct. *Collins v. Storer Broadcasting Co.*, 120 S.E. 2d 764, 769 (Ga 1961).

[55] 120 S.E. 2d 764, 769-70 (Ga 1961).

[56] Id. at 770 (internal citations omitted).

[57] *Kelley v. Astor Investors, Inc.*, 462 N.E.2d 996, 999-1000 (Ill. App. Ct. 1984), *aff'd* 478 N.E.2d 1346 (Ill. 1985); see Restatement (Second) of Trusts (1959) § 222.

Prior to ERISA, exculpatory clauses had even been permitted for fiduciaries managing pension funds. Specifically, in *Morrissey v. Curran*, 483 F.2d 480 (2d Cir. 1973), the court refused to hold two defendant trustees of the National Maritime Union of America's pension plan for its officers liable for improper payments from the plan. The trust agreement stated:

> 4. The trustee shall not be liable for . . . any loss to, or diminution of the Fund, *except due to their own wilful misconduct*. 5. The Trustees . . . shall be protected in relying and acting upon the opinion of legal counsel (including opinion of legal counsel who is or may be a trustee hereunder) in connection with any matter pertaining to the administration or execution of this Trust Fund. *No Trustee shall be liable for any action taken or omitted by him unless such act or omission is the result of wilful misconduct, nor for the acts of any agent, employee, or attorney selected by the Trustees with reasonable care, nor for any act or omission of any other Trustee*.[58]

While another trustee's "'reckless indifference' to his duty as a trustee" permitted liability against him, the exculpatory clause operated to release the two negligent fiduciaries from liability.[59]

Javits and other pension reformers sought to prohibit fiduciaries from striking bargains relieving them of their traditional obligations under trust law. As Javits explained, "Whatever the validity such provisions might have with respect to testamentary trusts, they are inappropriate in the case

[58] *Morrissey v. Curran*, 483 F.2d 480, 483-84 (2d Cir. 1973).

[59] Id. Section 501(a) of the Labor-Management Reporting and Disclosure Act of 1959 provides, "A general exculpatory provision in the constitution and bylaws of such a labor organization or a general exculpatory resolution of a governing body purporting to relieve any such person of liability for breach of the duties declared by this section shall be void as against public policy." However, the court held that this language did not apply to a "standard trustee exculpatory clause of a trust agreement." Id. at 484.

of employee benefit plans. The large numbers of people and enormous amounts of money involved in such plans coupled with the public interest in their financial soundness, as expressed in the Act, require that no such exculpatory provision be permitted."[60] The idea that the parties should not be able to contract around fiduciary protections implicates the debate of the contractarians and the non-contractarians. The mandatory nature of fiduciary protections under ERISA arguably removed this fiduciary law from the contract realm – if it was ever there at all. Fiduciary obligations were no longer merely default rules but instead became "universal mandatory minimum standards" (Coffee 1989, 1652).[61]

Changes to existing trust law, including those discussed by Javits, were necessary to solve a few problems with the strict application of trust law to employee benefit plans.[62] A tougher problem with the application of state trust law to large-scale pension plans was the conflict of interest between employers and employees, plan sponsors and participants. Although all fiduciary

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[60] S. 3589–Introduction to Employee Benefits Protection Act–Administration Bill to Amend the Welfare and Pension Plans Disclosure Act, 91st Cong., Cong. Rec. 7285 (March 13, 1970).

[61] See Langbein 1997, 183 (ERISA turned the default rules of trust law into mandatory fiduciary obligations).

[62] See *Varity*, 516 U.S. 489, 496-97 (1996) (internal citations omitted):

> We also recognize, however, that trust law does not tell the entire story. After all, ERISA's standards and procedural protections partly reflect a congressional determination that the common law of trusts did not offer completely satisfactory protection. . . . Consequently, we believe that the law of trusts often will inform, but will not necessarily determine the outcome of, an effort to interpret ERISA's fiduciary duties. In some instances, trust law will offer only a starting point, after which courts must go on to ask whether, or to what extent, the language of the statute, its structure, or its purposes require departing from common-law trust requirements. And, in doing so, courts may have to take account of competing congressional purposes, such as Congress' desire to offer employees enhanced protection for their benefits, on the one hand, and, on the other, its desire not to create a system that is so complex that administrative costs, or litigation expenses, unduly discourage employers from offering welfare benefit plans in the first place.

relationships involve some conflict of interest because a trustee must act for the interests of beneficiaries even where they directly oppose the trustee's interests, the trustee typically has not contributed any of the assets in the trust from his own pocket, nor is he paying to administer the trust. This is the issue that makes Congress' delegation risky and – according to some – requires that the government administer all pension funds. Congress, including Senator Javits, believed that alterations to common law fiduciary protections at the time of codification could reduce the risk sufficiently to make delegation to these conflicted fiduciaries advisable, particularly since Congress had to balance the need to protect beneficiaries already participating in pension plans with the goal of encouraging the maintenance and growth of private pensions by employers.

ERISA's drafters sought to prevent fiduciary disloyalty and poor management because pension plan sponsors frequently created and administered plans for their own benefit instead of participants'. Employers created benefit plans to shelter money from taxes or to invest in employer securities. Sponsors rarely had rank-and-file employees' well-being as their sole focus. Sponsors traditionally had the ability to control plan documents and make investments that served their business interests. For example, sponsors could amend plans at any time to cut or eliminate benefits, and they frequently invested pension funds in real estate the company wanted to purchase or in loans to the company that carried low interest rates. Since sponsors were not required to disclose the plan's investments, forcing disclosure of "prohibited transactions" required timely and costly litigation by plan participants who were often uninformed and certainly less powerful than those running the plans (Sass 1997, 205-07).

ERISA departs from trust law by allowing executives of the employer to serve as fiduciaries, even though trustees were traditionally professionals without any inherent conflicts of interest and employer representatives face inherent conflicts (Langbein 2003, 1327-28).[63] The plan may also be administered by an insurance company hired by the employer to run the plan, resulting in another conflict of interest as the third party has an interest in pleasing the plan sponsor to retain the contract to administer the plan rather than pleasing the participants who have no say in the selection of the plan administrator (Langbein 2007, 1326). Congress recognized that allowing the plan sponsor to retain control over plan administration was necessary to encourage plan formation by helping an employer keep costs down through its hiring or retention of lower cost parties to help administer the funds.

But Congress believed that mandatory fiduciary obligations would prevent employers from acting in their own interest and force them all – everyone involved in running the pension plans – to act in the interests of plan participants. Indeed, "ERISA's fiduciary regime, which governs benefit denial cases, is also profoundly paternalistic. Precisely because ERISA subjects every employee benefit plan to ERISA's duties of loyalty, prudent administration, and 'full and fair' internal review of benefit denials, we can be certain that Congress preferred these protective principles of ERISA fiduciary law [to freedom of contract]" (Langbein 2007, 1329-30).[64]

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[63] "Nothing in section 1006 of this title shall be construed to prohibit any fiduciary from . . . (3) serving as a fiduciary in addition to being an officer, employee, agent, or other representative of a party in interest." ERISA § 1108(c)(3), 29 U.S.C. § 408(c)(3).

[64] Langbein (2007) takes issue with cases decided by Judge Posner that fail to acknowledge the inherent conflict of interest held by most ERISA plan administrators and instead argue that the relationship between administrator and participants is similar to that of any contractual parties standing on opposite sides of the table. Instead, Langbein asserts that ERISA's fiduciary protections do not permit the type of self-interested behavior allowed among

Congress thus explicitly incorporated fiduciary standards in ERISA to hold those who administer private pension plans accountable.

The Lengthy Battle Over ERISA

President Gerald Ford signed ERISA into law on Labor Day, September 2, 1974 after over a decade of study and debate regarding how to safeguard private pensions. Senator Jacob Javits, a key proponent of the legislation, said of the occasion, “[T]he pension reform bill is the greatest development in the life of the American worker since social security” (quoted in Wooten 2004, 1).

The question that is the focus of Professor James A. Wooten’s (2004) work on the political history of ERISA is how this legislation passed given the opposition of both employers and, frequently, organized labor. Employers opposed increased regulation because of costs. Many unions opposed legislation because they wanted the role of policing pensions and did not trust the federal government to provide for workers’ retirement income security (7-8). Wooten argues that a new framework for pension policymaking (the “worker-security theory”) caused Congress to take on this historic legislation protecting retirement income and thereby increasing the cost to employers of providing pensions instead of ratifying the traditional view that private pensions were merely tools of employers to manage retention of their employees and alter at their will (the

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contractual parties and instead protect participants from the clear conflict of interest of plan administrators who work directly or indirectly for the plan sponsor (1329-30).

"personnel theory") (4). Legislators risked the wrath of key interest groups and passed ERISA "because they believed it was the *right* thing to do" (8).

One missing piece to the puzzle of ERISA's passage, however, is why it took the form it did. Path dependence is one part of the answer. Path dependence indicates that "timing matters" since policy decisions made early in the path, to provide tax incentives to spur the growth of private pensions for example, have a larger influence than those made later. The conditions that resulted in the formation of initial policies may no longer exist, but the policies remain. Path dependence assumes a significant amount of "institutional inertia" that continues policies put in place at an earlier time because of increasing returns – the concept that returns for remaining on a pre-existing path increase as time goes by, making it difficult to change course (Pierson 2000a, 2000b; Hacker 2002, 52-55).[65]

Even assuming that path dependence played a large role in the prominence of private pensions and the failure to expand Social Security to fill the gap in worker security identified, though, there were many different forms that the legislation could have taken. The path that Congress took to hold administrators of private pensions accountable had many possible branches,

[65] In part, ERISA took the form it did because Congress expected that only by permitting employers to manage private pensions would reform legislation pass. As Professor Paul A. David writes in his 1985 article explaining the dominance of the QWERTY keyboard, "Intuition suggests that if choices were made in a forward-looking way, rather than myopically on the basis of comparisons among the currently prevailing costs of different systems, the final outcome could be influenced strongly by expectations. A particular system could triumph over rivals merely because the purchasers of the [system] expected that it would do so" (335). Just as these expectations caused users of typewriters to rally around "the wrong system," expectations about the shape of successful legislation caused Congress to rally around a private pension system controlled by employers (336). See also discussion of self-reinforcing sequences in Mahoney (2000).

including greater oversight of fiduciaries by a single, active and knowledgeable agency.[66] Path dependence does not imply that the role of private fiduciaries could not have changed more significantly under ERISA or that Congress cannot use fiduciary standards to hold private actors accountable in many different ways.

It would have taken a critical juncture to break with the past entirely, though, and separate employers from the administration of pension plans they sponsored, however, because they had been administering those plans for over half a century. The concept of critical junctures elevates certain time periods above others in the historical path and shifts the focus from the more common policy inertia to how periods of dramatic change or potential change arise. "In social policy development, critical junctures represent moments of political opportunity when significant new policy departures may be put in place or when the forces for change are strong enough to cut into the ongoing path-dependent development of an existing policy and alter its trajectory." Some sort of crisis can act as an "exogenous" shock to realign political players and develop a new path (Hacker 2002, 59-60, 303-11). It took the collapse of pensions for thousands of Studebaker employees to pass a reform bill for private pensions at all – even one that left control in the hands of employers and arguably failed to hold them adequately accountable – and it would doubtless have taken a crisis affecting many more people to shift the public/private pension balance.

[66] Many thanks to Professor Wooten for his help with this idea.

Congress then sought a device to make workers secure by controlling the behavior of the private actors to whom it was delegating responsibility for supervising workers' retirement income security – while making a conscious decision to place control over worker pensions in employers' hands. The revised fiduciary regime it codified under ERISA was Congress' attempt to hold employers accountable for the workers' expectations.

Prior to ERISA, employees had little recourse if employers reneged on those promises, and their reliance on those promises was frequently misplaced because employers changed or eliminated pension benefits.[67] Employees lost all or a portion of their expected pensions when: (1) plan managers "misuse[d] or [stole] assets" ("agency risk"); (2) the employees quit or were fired from employment ("forfeiture risk"); or (3) an employer failed to properly fund the benefit plan and faced hardship itself ("default risk") (Wooten 2004, 3).[68] My focus in the remainder of this chapter is on how Congress responded to agency risk under ERISA.[69] Agency risk includes the possibilities that those who administer a pension plan will do a poor job of managing their obligations, use funds for self-interested purposes, or decline to pay benefits to which

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[67] Initially, courts viewed pension promises as "gratuitious, free-will gifts" and not contracts. They permitted employers to alter or eliminate benefits even without specific reservations of rights in the plan documents. Faced with increasing arguments that pensions were contractual promises to employees secured by years of service, employers began reserving their rights to amend plan benefits and limiting any legal claims to assets already contributed to the pension fund – not allowing employees to touch an employer's separate assets. Lengthy vesting provisions that were poorly understood by employees also caused many to lose pensions even after decades of service (Sass 1997, 187-89).

[68] Employers and some unions argued that different vesting and funding rules would make pension plans more expensive and force employers to provide less generous benefits or to eliminate the plans entirely. Many legislators, however, argued that private pension funds needed to meet the government's goals of worker security instead of employers' goals (Wooten 2004, 9-10).

[69] Agency risk is also referred to as "administration risk" by Professor John H. Langbein (2003, 1322).

participants are entitled. While default and forfeiture risks typically relate to defined benefit plans, agency risk "is common to all employee benefit plans" – including 401(k) plans and welfare plans (Langbein 2003, 1323). Much of ERISA prescribes specific funding, accrual, and vesting rules that are applicable to defined benefit plans – which have declined significantly in importance since the passage of ERISA. ERISA's fiduciary duties, however, remain of great import to today's pension and welfare plans. The legislative history of ERISA below emphasizes the incorporation of fiduciary standards under ERISA.

Pre-ERISA Pension Regulation

Private pensions developed beginning in 1875 to serve the interest of railroads in removing aging employees from the payroll by giving them income sufficient to retire (Gordon 1984, 2; Wooten 2004, 20-21). The problem of worker security in old age was first recognized when the move from the farm to the factory (and beyond the factory in the case of railroads) dislocated families that normally cared for their aging members (Wooten 2004, 20-21). Few employers beyond the railroads and even few welfare capitalists in the 1800s, however, focused on pension plans because the attenuated promises of a distant pension did not reduce turnover or decrease unionization significantly (Sass 1997, 14-17). With these early pension plans, employers "reserved the right to terminate the plan as a whole or any individual employee's pension at any time" (Wooten 2004, 20-21).

Tax incentives made pension contributions increasingly attractive for employers, particularly as key executives sought to shelter their earnings from taxes. In 1919, the Bureau of Internal Revenue decided that a firm could deduct pension contributions made to a trust if the trust met certain indicia of independence from the employer (Wooten 2004, 25). After 1921, employees who participated in defined benefit or defined contribution pension plans and those who were paid from an annuity that the employer purchased with an insurance company were all taxed only at the time they received the payments instead of when the initial contributions were made (25). Finally, in 1926, the tax on pension trusts themselves was eliminated, which removed the bias that resulted when the trusts paid higher taxes on the pension money than the employees would have paid had they received the contributions directly as regular income (26).

The Social Security Act of 1935 created a basic public pension program for workers based on years of service and wage rate, allowing private pension plans to cater to the highly compensated.[70] Employers were left to fill the gap between Social Security payments (initially under the Old-Age, Survivors Insurance Program and later under the renamed Old-Age, Survivors, and Disability Insurance Program) and the amount employees wanted and needed for retirement. Since higher wage earners expected larger pensions, private plans focused mainly on the highly paid by integrating Social Security benefits into their pension calculations (*i.e.*, either excluding from participation or paying a reduced benefit to those who earned less than the

[70] In reality, pension plans at the time of the Social Security Act did not provide pensions for many workers, and the Act affirmed the notion that private companies were not responsible for the retirement income of workers and need not sponsor pension plans that provided benefits to many outside the highest earning group of executives. In addition to being poorly funded and actuarially unsound, lengthy age and service provisions meant that private pension plans at the time covered only a little over ten percent of wage workers and only five to ten percent of those covered ever received a pension (Gordon 1984, 2-3).

maximum wages taxable under Social Security) (Wooten 2004, 27, 29).[71] Because Social Security left employers to sponsor pensions mainly to retain key employees, focusing on the highly compensated served this interest (Sass 1997, 99-100). Pension plans did not cover all employees (Wooten 2004, 30).[72]

The growth of private pensions increased dramatically during World War II. Substantial tax increases for individuals during World War II made pension plans the perfect tax shelter for highly compensated employees, who could defer income until retirement when their marginal tax rates were likely to be lower. Corporations also used pension plans as a tax shelter after their corporate taxes increased and a tax was created for money retained by corporations from profits and not paid out as dividends (Wooten 2004, 29-31). Finally, wage freezes during the war caused an explosion in the payment of "fringe benefits" such as pensions to compensate workers adequately (Javits 1981, 378).[73] Up to 60 percent of plans in existence at the end of 1941 were created in the previous two years. As top marginal tax rates reached 94 percent for individuals and 85.5 percent for corporations, this process accelerated (Wooten 2004, 32).

[71] See generally Slusher (1998).

[72] Social Security also helped increase the number of outside consultants used by employers to manage pension plans. To focus on highly paid employees, pension plans had to "integrate" their plans with Social Security benefits – offsetting benefits under their plans by the amount provided by the federal government. Because calculating Social Security benefits was complicated, employers turned to outside experts for assistance (Sass 1997, 100). See *infra* Chapter 3 for further discussion of who has historically helped administer pension plans.

[73] Wage controls designed to prevent wartime inflation due to shortages excluded fringe benefits such as pensions and allowed the demand for higher wages to be satiated in part by new and expanded pension plans (Gordon 1984, 3).

Pension coverage increased further to 11 million workers in 1960 (Wooten 2004, 34), largely due to the efforts of unions (Gordon 1984, 3-4). Older workers were encouraged to remain with employers to support the war effort during World War II. In addition, inflation during the war diminished the value of Social Security benefits, keeping these older workers in the labor force after the war (Wooten 2004, 34-35). A Republican Congress hostile to public social welfare programs took control in 1947, making substantial increases to Social Security benefits that would motivate these older workers to retire unlikely. Private pensions were the only tool available to move older workers out of the workforce.

Michael Gordon, pension counsel to Senator Jacob Javits during the passage of ERISA, argued in his retrospective on the ten-year anniversary of the legislation that pension plan gains during World War II merely made up ground lost during the Great Depression. Instead, union interest in negotiating pension benefits for their members with employers resulted in the greatest expansion of coverage (1984, 3-4). The mineworkers' push for an employer-financed fund to provide welfare and pension benefits resulted in Section 302 of the Taft-Hartley Act requiring joint administration of such funds by employer and union representatives and creating a system for the administration of large pension funds that received contributions from multiple employers ("multiemployer pension funds") (4). When the National Labor Relations Board announced that the Inland Steel Company should have bargained with the steelworkers' union about a pension plan because it was a mandatory topic of bargaining[74] and a federal appeals court agreed in

[74] *Inland Steel Co. v. United Steelworkers of America, CIO*, 77 NLRB 4 (1948).

September 1948,[75] newly empowered unions were encouraged to take worker retirement security into their own hands (Gordon 1984, 4; Wooten 2004, 35-36). The expansion of pensions to collective bargaining agreements changed the political players in the game of pension regulation and the size of large private pension plans as the Congress of Industrial Organizations (CIO) and American Federation of Labor (AFL) union affiliates moved to obtain pensions for their members (Wooten 2004, 36-37).[76]

Scandals Bring Calls for Reform

The effort for pension reform began in the 1950s in response to high profile investigations into mismanagement by union officials (Sass 1997, 192). Investigations were conducted at this time by subcommittees of the House Committee on Education and Labor, the House Committee on Government Operations, and a special committee of the Senate Committee on Labor and Public Welfare. Abuses found included embezzlement, excessive fees, and "ineptness" (Gordon 1984, 6). Pension funds were also frequently invested in assets of the employer – placing the employer's needs above those of the workers (Wooten 2004, 44). As a result of increasing reports of such self-dealing, in 1954, Congress enacted prohibited-transaction rules that

[75] *Inland Steel Co. v. NLRB*, 170 F.2d 251 (7th Cir. 1949).

[76] Unlike the CIO, the AFL affiliates focused on creating multiemployer pension plans covering thousands of workers to allow seasonal or other short-term employees to accrue pension credits and vest based on service to different employers in the same industry. Unions frequently helped administer these plans. Another difference with traditional single-employer pension plans was that with multiemployer plans, employers generally contributed a fixed amount and then administrators set the benefit level promised to workers – a less stable arrangement than paying the contributions necessary to fund a set benefit level as in single-employer plans (Wooten 2004, 38-39).

attempted to ensure that such transactions would at least be on terms as favorable as the employer would enter into with an unrelated entity (45).

The federal government moved to protect workers from pension misdeeds, but it moved slowly and continued to focus on increased reporting and disclosure to plan participants as the best method of oversight. In January 1954, President Eisenhower called for a study of these issues, but it was not until January 1956 that he submitted legislation requiring benefit plans to report to the Department of Labor. In May 1956, Senators Paul Douglas (D, Ill.), Irving Ives (R, N.Y.), and James Murray (D, Mont.) proposed a bill to have plans file annual reports with the Securities and Exchange Commission (SEC) (Wooten 2004, 45-46).[77] All proposals faced opposition from employers arguing that single-employer plans had not demonstrated a need for such restrictions and that agency jurisdiction should not lie with the Department of Labor (typically thought to be biased in favor of employees) but instead with the Securities and Exchange Commission (SEC) or the IRS (47).[78]

The McClellan hearings in the Senate further ignited public outrage over inappropriate (but frequently not illegal) behavior by pension plan administrators. Starting in February 1957, the Senate Select Committee on Improper Activities in the Labor or Management Field chaired by John McClellan (D, Ark.) heard 270 days of testimony over two and a half years on the misdeeds

[77] I use here the convention of Wooten (2004) to provide the political party and state of each congressman discussed given the long and tangled legislative history of ERISA.

[78] Six states also moved to regulate welfare and pension plans (Wooten 2004, 45-46). As the narrative later discusses, in the early 1970s, the potential for conflicting state laws regulating pensions was again a powerful force for national action in this area.

of labor unions and employers. The misdeeds of union officials received the brunt of public outrage (Wooten 2004, 47-48).

Congress moved for new legislation – not to set forth specific rules for the administration of pension plans, but to require greater disclosure to participants of plan information so that participants could monitor plans for themselves.[79] The Senate Labor Committee reported a bill in 1958 that placed jurisdiction for employee benefit plan monitoring with the Department of Labor and covered both single and multiemployer plans. The legislation, however, dropped the idea of requiring plans to send information directly to participants in favor of requiring disclosure upon employee request (Wooten 2004, 47-48). Still, the conservative Chair of the House Committee on Education and Labor, Graham Barden (D, N.C.), rejected the authority granted to the Department of Labor to monitor plans and punish anything but "willful noncompliance" with filing requirements. Thus, the Welfare and Pension Plans Disclosure Act of 1958 ("Disclosure Act") was toothless from the start (48-49).

The President's Committee

On March 28, 1962, after earlier leading the failed charge in the Senate to amend the Disclosure Act to allow the Labor Department to monitor compliance with the law, dictate the required filings from plans, and penalize theft and false disclosures criminally, John F. Kennedy created the President's Committee on Corporate Pension Funds ("President's Committee") (Gordon

[79] Although it is unclear what they were supposed to do with this information once they had it.

1984, 7-8; Wooten 2004, 77, 82, 84). This cabinet-level committee was tasked with making recommendations on both public and private pensions (Wooten 2004, 84). The committee was created in part to respond to two pages on pensions in a lengthy report issued in 1961 by the private, non-governmental Commission on Money and Credit created by the Committee for Economic Development in 1958.[80] *Money and Credit's* brief discussion of private pensions expressed concern about the agency risk associated with conflicts of interests and resulting poor investments by pension funds. The report recommended that the federal government set forth standards for those administering pension funds along with stronger enforcement and increased disclosure (85).

The President's Committee included all of the powerful players in a new game of pension regulation – the Secretaries of Labor, Treasury, and Health, Education and Welfare, the Director of the Bureau of the Budget, and the Chairmen of the Securities and Exchange Commission and the Federal Reserve Board (Wooten 2004, 86). Treasury officials sought to use the committee to create rules that forced pension plans to cover more low and moderate income workers and provide them with more generous pensions to qualify for the generous tax deduction.[81] Minimum vesting standards appealed to the committee's sense of fairness because participants

[80] The report was the result of a $1.5 million project by this organization. Although President Kennedy favored the report and a summary of it was read into the Congressional Record by a New York congressman, it was not produced by the government. "More on the Money-Credit Report." *Research Reports*. September 18, 1961. American Institute for Economic Research. Great Barrington, Mass. Accessed March 20, 2013, http://www.aier.org/sites/default/files/publications/RR19610918.pdf.

[81] Forcing employers to cover non-salaried workers, providing for quicker coverage under pension plans and speedier vesting of benefits (vesting at the time did not have to occur before an employee was eligible to retire under the pension plan), and capping pension contributions on behalf of any particular individual would allow Treasury to meet these goals. The President's Committee largely adopted these recommendations (Wooten 2004, 87-91, 93).

promised a pension were frequently denied one as a result of lengthy vesting provisions (93). Similarly, the President's Committee recommended new minimum funding standards that required pension plans to fund at least all benefits accrued during the year and amortize new benefits for past service within a period not to exceed 25 years.[82] This helped allay the default risk that resulted when a plan terminated with insufficient funds to pay promised benefits (94-96).

But the President's Committee skirted the issue of reforming fiduciary rules. Although the report by the Commission on Money and Credit had fiduciary obligations as its focus for pension reform, the committee worried about appearing to target unions given the recent investigations. The committee even considered more lax fiduciary standards so that pension plans could be "flexible" when investing pension funds (Sass 1997, 198-99). Investments were governed by state common law of trusts (as discussed above), the prohibited-transaction rules of the Internal Revenue Code, and the Disclosure Act. Treasury argued that state trust law was insufficient because many pension trust agreements permitted investments that flouted state rules and enforcement of fiduciary standards was forgiving (Wooten 2004, 97-99). In the end, the President's Committee recommended only stricter self-dealing provisions in the tax code but no new fiduciary regulations otherwise. Focusing on enforcement problems instead, the committee called for more disclosure of specific investments (99).

[82] Collective bargaining agreements frequently negotiated benefit increases that included higher pensions for previously accrued, or earned, pension credits. This sudden increase in pension liability for past service resulted in significant underfunding of these plans in most cases.

Initially tentative about their proposals, especially given President Kennedy's contentious relationship with the business community, the President's Committee issued an interim report in November 1962. Kennedy then asked his Advisory Committee on Labor-Management Policy ("Advisory Committee") to review it (Wooten 2004, 80, 101). The Advisory Committee's response in December 1963 (after Kennedy's death) opposed the vesting and funding provisions recommended by the President's Committee and argued that employers would not sponsor pension plans under these terms – hurting employees more in the long run than the current absence of regulation (80-81). Unconvinced, the President's Committee sent the report to President Johnson with only minor changes. The controversial report languished until after the election despite the urging of Labor Secretary and President's Committee Chair Willard Wirtz, and when the President released the report in January 1965, he did not support its suggestions (81). Yet the committee's final report, issued in January 1965, "became 'the 'bible' in this field" (quoted in Wooten 2004, 80).[83]

In the January 1965 report ("Wirtz Report"),[84] the committee argued that agency risk for retirement funds was not an issue of a lack of "appropriate standards of prudence" but instead was a lack of proper enforcement mechanisms for the current fiduciary standards already established by trust law (73-74). The committee emphasized the importance of disclosure, arguing that no one could seek to correct injuries done to plan participants if they were unaware

[83] Another event increasing calls for pension reform around this time was the 1964 publication of *The Future of Private Pensions* by Merton Bernstein, which thoroughly catalogued the failures of private pensions to provide reliable retirement income to workers and recommended the expansion of Social Security (Gordon 1984, 8-9).

[84] President's Committee on Corporate Pension Funds and Other Private Retirement and Welfare Programs. 1965. *Public Policy and Private Pension Programs: A Report to the President on Private Employee Retirement Plans*. U.S. Government Printing Office.

of those injuries. The report called for amendments to the Disclosure Act to disclose plan investments in greater detail but recognized that "[d]isclosure is not necessarily sufficient in itself" (78). Although recommending only further study of proper enforcement mechanisms, the committee did state that "it might be necessary to empower a regulatory agency to act as guardian for the collective interests of employees and their beneficiaries and, if necessary, to bring suit in [sic] behalf of the plan participants" (78-79).

In August 1965, President Johnson created the Task Force on Labor and Related Legislation ("Task Force") with Willard Wirtz as chair to craft legislative suggestions based on the committee's report (Wooten 2004, 117). The White House Task Force proposed broad legislative action, including on fiduciary protections (119). One explanation for the sudden push for tighter fiduciary rules in spite of the committee's refusal to address that topic in depth was the return of Senator McClellan to the scene with the Senate Permanent Subcommittee on Investigations under the auspices of the Government Operations Committee. McClellan's investigation into the actions of union officials administering pension plans demonstrated the inability of disclosure to sufficiently protect pension participants from fiduciary abuses (Gordon 1984, 10-11).[85] When the President's Committee met again in April 1966, now with representatives from the Commerce and Justice Departments to take account of business

[85] McClellan investigated the Allied Trade Council and Local 815 of the International Brotherhood of Teamsters, New Jersey unions. His investigation found that George Barash, founder of the two unions, created a consulting organization that charged the pension funds excessive fees. Barash then attempted to transfer millions from the funds to charitable organizations off shore that he had established (Gordon 1984, 10-11).

opposition, Senator McClellan's efforts resulted in immediate pressure to address fiduciary and disclosure rules (Wooten 2004, 120-21).[86]

An interagency group of staffers assigned to move pension reform legislation forward addressed fiduciary obligations first. The staffers used Senator McClellan's bill (proposed in October 1965 and crafted with the help of the Labor Department) as a model. That bill employed the common law of trusts to codify fiduciary standards by amending the Disclosure Act, calling for fiduciaries to act "for the sole and exclusive" purpose of providing pensions to participants and to prevent conflicts of interest. Individuals convicted of crimes could not be fiduciaries. To enforce its mandates, the McClellan bill allowed participants and the Labor Department to sue to enforce rights and recover money, and it also created criminal sanctions for intentional violations of fiduciary obligations (Gordon 1984, 11; Wooten 2004, 121-22). "This bill became the forerunner of the fiduciary provisions that ultimately were enacted in ERISA, even though it did not represent official policy of the Johnson administration at the time of its introduction" (Gordon 1984, 11). Wirtz circulated a draft bill in August 1966 that cut back cumbersome agency oversight of individual plan actions and deleted some criminal sanctions but incorporated the basic idea that pension plans are trusts and administrators must adhere to specified fiduciary standards (Wooten 2004, 122-23).

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[86] Distraught that the abuses discovered by McClellan were not adequately dealt with by present laws, Senator Jacob Javits on the Government Operations Committee quickly introduced legislation to amend the Taft-Hartley Act to tighten fiduciary obligations for union-negotiated pension plans. Participants and the Secretary of Labor would have enforcement rights in the federal courts. The Labor Department worried about placing too much emphasis on abuses in union-run plans and wanted to focus more broadly on all plans, however, and the bill did not pass (Gordon 1984, 11).

After approval by the President's Committee, Johnson submitted the Welfare and Pension Protection Act of 1967 to Congress. The legislation was introduced by Ralph Yarborough (D, Tex), chair of the Labor Subcommittee of the Senate Labor and Public Welfare Committee (Wooten 2004, 127-28). Emphasizing the administration's focus on fiduciary issues, Yarborough stated on the occasion:

> In order to assure ordinary care and prudence in handling the welfare and pension funds, persons managing the funds must be responsible as fiduciaries to the funds and the participants and their beneficiaries. While the tax-exempt status of a fund may presently be lost by the trustees making prohibited transactions, no penalty either criminal or civil is imposed on the trustees.
>
> The extremely rapid growth of welfare and pension plans, coupled with uncertainty about the rights of the employees participating in them, have afforded opportunities for abuse. Legal protection against such abuse has been dependent on State laws. However, under many of these laws the extent to which persons handling such funds are bound by the responsibilities and standards of 'trustees' is uncertain. . . .

(quoted in Gordon 1984, 11, citing 113 Cong. Rec. 3924 (Feb. 20, 1967)).

Javits Pushes Reform Ahead

Stepping out front in the movement for pension reform, on February 28, 1967, Jacob Javits proposed the first comprehensive pension reform bill. The Pension and Employee Benefit Act of 1967 (S. 1103) included not just fiduciary standards and disclosure but also vesting, funding, and termination insurance that would protect participants from default risk (Gordon 1984, 12; Wooten 2004, 127, 129). Javits was the highest ranked Republican on the Senate Committee on Labor and Public Welfare and considered pension reform to be "necessary because the nation's

private pension system was deceptive, unsafe, and unjust" (Javits 1981, 378; Wooten 2004, 129). One important component of Javits' bill was a commission that would monitor compliance with the legislation and monitor employee benefit plans more generally. The bill would place its mandates within the labor laws and was therefore referred to the Committee on Labor and Public Welfare. This was a sharp change from previous proposals and allowed Javits to avoid the rules requiring tax legislation to begin in the House of Representatives that empowered the House Ways and Means Committee (Wooten 2004, 130-31).[87]

On January 11, 1968, the President's Committee pushed Johnson for comprehensive pension reform after finally finishing its work, with neither big business nor unions firmly on board. The key change to the committee's recommendations was to put vesting, funding, and termination insurance within the purview of the labor laws instead of the tax code as Javits had done. This would allow less busy congressional labor committees to take up the legislation and avoid the chair of the House Ways and Means Committee, Wilbur Mills, who opposed pension legislation (Wooten 2004, 144-45).

Fearful of business and union opposition, Johnson delayed. Congress continued to push pension reform, however. John Dent (D, Penn.), chair of the House General Labor Subcommittee and a representative of many Pennsylvania steelworkers, scheduled hearings on the administration's fiduciary and disclosure legislation (which later died when Congress adjourned) and the bills by Javits and Senator Hartke (a Democratic Senator from Indiana, where the Studebaker pension

[87] Javits' comprehensive 1967 bill owed much to legislation in Ontario, Canada, that covered funding, vesting, and fiduciary standards (Sass 1997, 211).

plan defaulted, who proposed termination insurance) (Wooten 2004, 145). President Johnson remained cautious, though, and he had Willard Wirtz send the Pension Benefit Security Act (S. 3421) to Congress on behalf of the Labor Department only (although many viewed it as an administration bill and business groups were outraged that they were not consulted).

Richard Nixon's election brought a more pro-business administration in 1969, and the impetus behind pension legislation came from Congress (Wooten 2004, 150). In congressional hearings in 1968, members of the business community continued to oppose vesting and funding changes, termination insurance, and portability proposals, but they were more flexible on fiduciary standards and increased disclosure (152). In September 1968, the House Education and Labor Committee reported a fiduciary and disclosure bill that compromised with the desires of big business. Suddenly, reforms in this area seemed less threatening. As Robert Lane of Mobil Oil stated in a letter to Commerce, "[M]ost of the shortcomings and problems which the Labor Department and some of our congressional friends have focused on are due substantially to a lack of understanding on the part of employees, and many times on the part of employers and unions, of the exact nature of the benefits and the conditions under which they can be paid under private welfare and pension plans" (quoted in Wooten 2004, 153-54).

The Nixon administration thus focused on disclosure and sent the Employee Benefits Protection Act of 1970 to Congress on March 13, 1970 with labor jurisdiction as continued congressional hearings made the issue of pension reform popular (Wooten 2004, 155). Widely publicized events increased public pressure for comprehensive reform instead of merely increased

disclosure, however. The shutdown of the Studebaker auto plant in South Bend, Indiana was the "focusing event" needed to bring about the passage of ERISA, with the large number of forfeitures helping to publicize shortcomings in pension promises made to employees (Wooten 2001).[88] Indeed, Javits himself called the Studebaker episode, where roughly 4500 workers lost the vast majority of their pension benefits, "[t]he most notorious and tragic examples of pension failure" (Javits 1981, 379).[89]

Nevertheless, it took a publicity campaign by Javits to push legislators into action. As the media publicized stories of pensions promised and lost after many years of hard work, leaving workers in dire straits, pressure for reform mounted. In March 1971, Javits and Senate Labor Subcommittee Chairman Harrison Williams (D, N.J.) held sensational hearings (Wooten 2004, 150-51). "By packaging pension reform as comprehensive legislation, reformers could link 'sexy' issues like fiduciary standards to measures like vesting and funding standards, which drew considerable opposition but not much support" (158). Williams investigated United Mine Workers President Anthony Boyle's abuse of his position as trustee for the union's benefit fund

[88] As noted above, the importance of time in the development of the welfare state, including the concepts of critical junctures and path dependence is discussed extensively by Hacker (2002), drawing on Pierson (2000a, 2000b). Lieberman (2002) adds the importance of examining ideas at these key moments in time to examine political change such as the enactment of ERISA. Explaining ideational change, in combination with examining institutions, helps explain policy change.

[89] The explanation for how so many lost their promised pension benefits when Studebaker's business declined is the underfunding of its pension plans. Large firms like GM, Ford, and Chrysler (and the smaller firms like Studebaker that followed their lead) used pension underfunding to prevent labor unrest. Unions recognized that significant benefit or wage increases had to be balanced against pension funding. Any risk to the business interests of the company could bring about the collapse of the pension plan, and therefore pension funding was a bargaining chip (Sass 1997, 186). IRS rules required vesting upon plan termination, but vesting was irrelevant without proper funding to pay for vested benefits (Sass 1997, 184-85). Because regular benefit increases for past service were amortized over thirty years but retirees had first claim to benefits in the event of termination, unfunded benefit increases for this group left less of the pot available to pay benefits to less senior groups of employees (Sass 1997, 185-86).

as well as pension funds more generally.[90] As Gordon said, "[F]iduciary abuses . . . are relatively easy to grasp and lend themselves to graphic portrayal" (quoted in Wooten 2004, 158-59). Agency risk caught the public's attention because it was easier to understand than forfeiture and default risks (Wooten 2004, 159).

Javits and Williams also used dire statistics warning that few received their promised pensions to grab public attention. Javits' staff, including Michael Gordon (previously of the Labor Department) created a questionnaire on pension plans to gather information. Williams' subcommittee sent the questionnaire to 1500 pension plans in May 1970 (Wooten 2004, 159). Javits and Williams went public with the results of the questionnaire in March 1971, and the press publicized their questionable statistics indicating that most employees failed to receive their promised pensions (Wooten 2004, 161-67). "The study found that in the sample of plans studied, which had lengthy service requirements, only 5 percent of the millions of employees covered since 1950 had ever received benefits, only 8 percent had qualified for benefits, and while most of these employees had only worked a very short period of time (less than 5 years), there were substantial numbers of workers who had longer periods of service and failed to qualify for benefits" (Gordon 1984, 15).

The public attention brought President Nixon back into the arena of pension reform. Administration proposals in December 1970, however, focused on a vesting provision that

[90] Javits and Williams used the circumstances surrounding the murder of Joseph Yablonski, Sr., unsuccessful candidate for the presidency of the UMWA to investigate President W.A. Boyle's misuse of pension funds in connection with the union election. Javits and Williams pushed for the Labor Subcommittee's authority to include a broader investigation of pension funds, and they used this as a springboard for their very public pension campaign (Gordon 1984, 15).

helped only older workers with at least a combined 50 years of age and service -- a small percentage of those who forfeited pension credit before vesting – and individual retirement accounts (IRAs). The press protested that the proposals did little to ensure that pension promises were kept (Wooten 2004, 176).

The Senate Labor Subcommittee worked hard next to draft legislation. Its draft bill, finalized in February 1972, courted the AFL-CIO (still not on board with broad pension reform) by giving jurisdiction over plan compliance to an "independent agency . . . housed at the Department of Labor" (quoted in Wooten 2004, 178). The AFL-CIO was dissatisfied, however, and did not want an agency supervising union actions, particularly if it was independent of the traditionally favorable Labor Department. As staffers negotiated, the subcommittee continued to draw attention to the need for pension reform. On May 1, it held hearings on plan terminations, traveling to cities around the country to hear stories with the press following (Wooten 2004, 178-79).

The House also focused on pension reform. On May 8, John Dent's subcommittee released an interim report, and the Ways and Means Committee focused on IRA legislation. Although business representatives were feeling the public pressure for reform and coming around to the administration's proposed vesting rule, opposition in the House required action in the Senate (Wooten 2004, 179).

On May 11, 1972, Williams and Javits introduced the Retirement Income Security for Employees Act, S. 3598. The new bill placed jurisdiction for pensions within the Labor Department instead of an independent body and attempted to address the needs of multiemployer plans. Javits and Williams now settled down to the task of negotiating legislation instead of public rhetoric. Ralph Nader's decision to take up the pension cause for the left allowed the Senators to move to the center and appear ready for reasonable compromise (Wooten 2004, 180-81).[91] On September 13, the day after NBC broadcast "Pensions: The Broken Promise", the subcommittee reported the bill with amendments that included shortened transition periods. On September 15, the committee reported the bill with few changes (183-84).

With administrative backing, however, Senate Finance Committee Chair Russell Long took up the jurisdictional fight. The bill was referred to the Finance Committee, and Long prepared to delete all but the fiduciary and disclosure provisions before reporting the bill. Although Javits and the press decried Long's action, the bill died as the legislative session closed. Long responded that the stricken provisions dealt with matters traditionally within the jurisdiction of the tax committees and needed to start in the House Ways and Means Committee (Wooten 2004, 186-87).[92] The public reacted swiftly and sent letters to Congress to express their outrage over

[91] Ralph Nader's plan, modeled after TIAA-CREF retirement plans for professors, advocated turning all pension plans into SEC-licensed mutual funds that invested contributions and provided retirement annuities to retirees, allowing for immediate vesting and portability. Nader said the bill proposed by Williams and Javits, on the other hand, was merely the result of a "curious pension coalition of industry and organized labor" (quoted in Gordon 1984, 21).

[92] Javits, however, argued that the jurisdiction issues were simply an excuse because Long favored employers and his brand of "populism demanded that government, rather than private pension plans, assume prime responsibility for retirement." Indignant, Javits spoke on the floor of the Senate, saying, "It will take a magician to demonstrate how the action of the Finance Committee is a service to our country and the American workingman. . . . What has

Long's actions. "[A] broad consensus had formed behind the comprehensive reforms adopted by the Committee on Labor and Public Welfare" (Gordon 1984, 24).

Legislation Finally Gains Momentum

Moving quickly on its legislative priorities in 1973, the Democratic leadership in Congress attempted to control wayward committee members like Long (Wooten 2004, 192). Williams and Javits immediately introduced S. 4, which was identical to S. 3598 as reported by the Labor Committee the previous year. Javits discussed the connection between Congress' institutional competence and its need to pass pension reform. Williams held brief hearings starting on February 15, and he and Javits had fifty consponsors for the bill. The subcommittee reported the bill on March 5.

Knowing that he had to act quickly or labor jurisdiction of pension reform would go forward without his input, Senator Long established a Subcommittee on Private Pension Plans and named as chair a sponsor of S. 4 and Labor Committee member. On March 13, Lloyd Bentsen introduced the Finance Committee's own draft bill, S. 1179, and accepted the idea of tighter vesting and funding standards as well as termination insurance (Wooten 2004, 194). The Finance Committee bill placed these provisions within the Internal Revenue Code as requirements for tax qualification of pension plans. The bill did not address disclosure, which the committee left to the Labor Committee (196).

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happened is not unusual. It has happened before in American history, where a rather myopic point of view on what is best for this country has dictated some reactionary opposition to a given measure" (Javits 1981, 383).

In the House, John Dent introduced two bills and planned hearings. The divide among unions about pension legislation put Dent in a bad position, though. Ways and Means Committee Chair Wilbur Mills held hearings on tax reform, including pension issues, but pension reform was not at the top of his committee's agenda (Wooten 2004, 196-97).

The Senate also dawdled as jurisdictional conflicts continued. On May 21, the Senate Finance Committee's Subcommittee on Private Pensions began hearings. Areas of conflict involved termination insurance and which agency would have oversight. Concerns focused on expertise and whether tax penalties or a court order after a lawsuit by the Labor Department would be more effective to enforce the legislation (Wooten 2004, 201-02).

As the federal government wrangled over details, the states took up pension reform. Wisconsin, California, Connecticut, Illinois, New Hampshire, New Jersey, New York, and Pennsylvania considered measures, and New Jersey enacted the Private Nonvested Pension Benefits Protection Tax Act. When a plant closed, the statute taxed an employer in the amount of pension accruals forfeited by unvested employees with at least fifteen years of service. However, this did not solve the problem of forfeitures since the plans lacked funding and still might not be able to pay vested participants their benefits. The potential for a patchwork of different state regulations of pension plans finally brought business to support federal regulation.[93] Yet it appeared that the

[93] According to Wooten (2006, 1-2), "The desire for federal preemption was a key factor—perhaps, the key factor—in creating the coalition that pushed ERISA through Congress." The desire to avoid the involvement of the states in pension regulation pushed the business community and the AFL-CIO to support federal legislation. Legislation

Finance Committee's proposals as part of the tax code would not preempt state regulation, and – in an ironic twist – only the Labor Committee could help the business community (Wooten 2004, 204-05).

After the Senate Finance Committee agreed to general principles in executive session, it moved to draft a revised bill, and consideration of the Labor Committee's S. 4 on the floor was postponed until September. Finance agreed to substantially similar proposals on participation, vesting, and funding, but placed jurisdiction over termination insurance in a new body administered by Labor, Treasury, and Commerce (Wooten 2004, 206). In addition, the Finance Committee sought to keep jurisdiction over fiduciary self-dealing in the tax domain with an excise tax. Reporting S. 1179 presented again the issue that revenue measures had to originate in the House, and it was proposed that the pension bill be attached to H.R. 4200, a two page bill on military pensions. But which bill to attach? If compromise meant revisions to the Finance bill, the Finance Committee would choose representatives for the conference committee, and Javits and Williams would lose control of the legislation. Regardless, any bill attached to H.R. 4200

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passed in New Jersey in May 1973 was of particular concern. Drafted in response to the closure of the Raybestos-Manhattan Company plant in Passaic, New Jersey, the bill taxed companies closing factories and used that tax to pay pension benefits to those who worked long years but had not yet vested in their pensions prior to the shutdown. "Cahill Signs Pension-Safety Bill For Those Whose Plants Close," *New York Times*, May 11, 1973, 84. The tax was:

> equal to the total amount of nonvested pension benefits of such employees of the employer who have completed 15 years of covered service under the pension plan of the employer and whose employment was or will be terminated because of the employer's ceasing to operate a place of employment within this State and whose nonvested pension benefits have been or will be forfeited because of such termination of employment . . .

"The Private Nonvested Pension Benefits Protection Tax Act." Sec. 3, Ch. 124, Laws of 1973. Approved May 9, 1973. Although even Governor Cahill recognized that private pension reform was "a subject which can best be treated properly at the Federal level," he "intend[ed] to do all within my power to help solve this perplexing problem." "Cahill Signs Pension-Safety Bill For Those Whose Plants Close," *New York Times*, May 11, 1973, 84.

would head to Wilbur Mills and the Ways and Means Committee – and an uncertain fate (207-09).

On August 21, 1973, the Senate Finance Committee reported S. 1179, a 240-page bill. On September 18, the Senate committees had reached a compromise. Gaylord Nelson, head of the Finance Committee's Subcommittee on Private Pensions and also a member of the Labor Committee proposed two amendments – amendment 496 on vesting, funding, fiduciary obligations, portability, termination insurance, and enforcement and amendment 497 on tax issues not discussed in the Labor bill. Vesting and funding were placed in the tax code, but insurance would be under the Department of Labor in a body called the Pension Benefit Guaranty Corporation. The amendment gave the Department of Labor enforcement authority in spite of dual codification in Treasury and Labor (Wooten 2004, 212-13). To enforce fiduciary rules on self-dealing, the IRS could use excise taxes and the Labor Department could pursue the fiduciaries in court. After years of reform efforts, Senators debated only for two days on the compromise. It was then passed unanimously as a 300-page addition to revenue bill H.R. 4200.

The action then shifted to the House. Under the House rules, H.R. 4200 had to be referred back to the Ways and Means Committee. Worried about losing labor jurisdiction, Dent's subcommittee revised and reported H.R. 2 on September 20, only one day after the Senate passed H.R. 4200. On October 2, the Education and Labor Committee reported H.R. 2. Among other differences between H.R. 2 and H.R. 4200, H.R. 2 gave jurisdiction to the Labor Department instead of dividing responsibilities (Wooten 2004, 218).

Bogged down in trade legislation and with Wilbur Mills absent for health reasons, Ways and Means under Chairman Al Ullman (D, Ore.) nevertheless moved quickly to pass pension reform in the war for jurisdiction in the House. Ullman asked for written comments instead of holding hearings and planned for executive sessions. Although House rules allowed committees to combine two bills on the floor, Ullman delayed any compromise and instead went to work on a bill identical to H.R. 4200 without the military pensions, while the Speaker held H.R. 4200. Congressmen criticized the quick schedule on such a lengthy and complicated bill (Wooten 2004, 223-25). Although Ullman signaled areas of compromise, the Labor Committee pushed to send H.R. 2 to the floor before Ways and Means finished its work, and tempers flared.

As Ways and Means worked on a bill, the House postponed working on H.R. 2 until December and then until January 1974 when the fight over jurisdiction continued (Wooten 2004, 227-28, 231). Finally, after the AFL-CIO agreed to joint tax and labor jurisdiction over participation, vesting, and funding standards, Dent and Ullman reached a deal that gave both Treasury and Labor enforcement powers (232-33).

On February 4, 1974, Ullman introduced the Ways and Means bill, and on February 14, 1974, Dent introduced a new bill that tracked the Ways and Means bill more closely. Dent's new bill included sweeping language to preempt states from regulating employee benefit plans and termination insurance (Wooten 2004, 234). Under the rule created, the Labor Committee's bill would become Title I of H.R. 2, and the Ways and Means bill would become Title II of H.R. 2

(237). H.R. 2 passed 376 to 4, and the Senate substituted its previously passed bill, H.R. 4200, for H.R. 2 as the legislation moved to conference (240).

Amidst the fallout from the Watergate scandal, the conference committee set to work creating legislation from two bills that reached nearly 650 pages with members of four committees bitter after the long fight to reach this point (Wooten 2004, 242). In fact, the House would only allow its labor conferees to address topics in Title I of its H.R. 2 and Ways and Means conferees to address topics in Title II of its version of H.R. 2 – attempting to force Senate conferees to the House model (243). As the work of committee staffers proceeded into May without any official committee meetings, House Labor Committee staff Russell Mueller explained the problem this way: "[T] he House's objectives were to set up minimum standards to make pension reform technically sound, while the Senate wanted to draft 'the perfect plan' for everyone" (quoted in Wooten 2004, 245).

On May 15, the conference committee had its first official meeting (Wooten 2004, 246). During nineteen meetings, the committee settled all major differences (249). The Labor Department and IRS would have joint jurisdiction over many aspects of participation, vesting, and funding, including the prohibited transaction rules (250-51). The main difference between the House and Senate bills on fiduciary standards related to the definition of "fiduciary." The House definition included not only those who managed plan assets but anyone who had discretionary authority over plan administration. The staffers recommended the broader House definition, and the conferees agreed on June 18 (257-58).

After a dramatic expansion of the proposed preemption clause left states with the inability to pass laws that even "relate to" employee benefit plans, the committee and staff's work was nearing an end (Wooten 2004, 265, 267). The House passed the revised legislation unanimously on August 20, 1974, and the Senate followed on August 22 (269). At the behest of Senator Javits, President Ford signed the Employee Retirement Income Security Act on Labor Day, September 2, 1974 (269-70).

At the time of ERISA's enactment, "there was great uncertainty about how the legislation would play out in practice" (Wooten 2004, 242). Or, as one newspaper article stated prior to passage, the legislation "is not as good as it could be and should be. But it is probably the best piece of legislation that can, as a practical matter, be enacted now."[94] After years of opposition by big business and unions, the passage of any legislation was miraculous, but that legislation was a compromise. ERISA attempted to balance security for workers with freedom for employers to decide the terms of compensation – including pension benefits – for their employees.[95] Even the legislators who enacted ERISA recognized its limitations. Immediately following enactment, Senator Javits stated, "Congress has made an auspicious beginning with the enactment of the pension reform bill but there still remains a great deal to do if we are to promote a more

[94] "Pension Bill Can Be Improved—Later," Los Angeles Times, July 9, 1974, B6 ("Ralph Nader, for one, has called the final version a 'terrible disappointment.'"). Commentators criticized the legislation for succumbing to pressure from both business and labor and not mandating more stringent protections of workers, such as stricter vesting terms and funding of past service liabilities.

[95] As Michael Gordon (1984, 23) said, "In short, the bill . . . represented middle-of-the-road reforms, doing just what was thought germane and necessary to get the job done."

satisfactory private retirement system—one that will enable every American, after his or her productive years, to look forward to a retirement with freedom from anxiety and economic want (Gordon 1984, 25).[96] In the end, Congress delegated significant discretion over private pensions to employers and their representatives and relied on ERISA's fiduciary standards and judicial enforcement of those standards to reign in the inevitable slippage between its pension reform goals and the behavior of these private actors.

ERISA's Fiduciary Rules

ERISA requires every covered plan to "provide for one or more named fiduciaries who jointly or severally shall have authority to control and manage the operation and administration of the plan."[97] In addition, ERISA states:

> a person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. . . .[98]

[96] Quoting from Address by Senator Jacob K. Javits, Briefing Conference on Pension and Employee Benefits, New York State School of Industrial and Labor Relations, Cornell University and Federal Bar Association, Washington DC (Sept. 19, 1974).

[97] ERISA § 402(a)(1), 29 U.S.C. § 1102(a)(1).

[98] ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A). As the conference committee explained, "Under this definition, fiduciaries include officers and directors of a plan, members of a plan's investment committee and persons who select these individuals. Consequently, the definition includes persons who have authority and responsibility with respect to the matter in question, regardless of their formal title. The term 'fiduciary' also includes any person who renders investment advice for a fee and includes persons to whom 'discretionary' duties have been delegated by named fiduciaries.

Fiduciaries are subject to ERISA's fiduciary duties, which provide that:

> a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—(A) for the exclusive purpose of: (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan; (B) with the care, skill, prudence, and diligence under the circumstances 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; (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and (D) in accordance with the documents and instruments governing the plan . . .[99]

ERISA's test of who is a fiduciary is a "functional" one – the work done for a plan by the person determines whether he or she is a fiduciary rather than the title or lack of title assigned to the party. An example given by the Department of Labor is illustrative. A plan may employ a person as a "benefit supervisor." If that benefit supervisor only calculates how large of a benefit to pay a participant based on the formulas set forth in plan documents and a superior has final authorization to confirm the benefit, then the benefit supervisor is not a fiduciary. If the person with the title "benefit supervisor" instead has final approval to determine the benefit amount of a participant when there is a disagreement as to how much the participant is entitled to under the

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While the ordinary functions of consultants and advisers to employee benefit plans (other than investment advisers) may not be considered as fiduciary functions, it must be recognized that there will be situations where such consultants and advisers may because of their special expertise, in effect, be exercising discretionary authority or control with respect to the management or administration of such plan or some authority or control regarding its assets. In such cases, they are to be regarded as having assumed fiduciary obligations within the meaning of the applicable definition." *Highlights of the New Pension Reform Law*, Text of Joint Explanatory Statement of Conference Committee, at 124-25 (1974).

[99] ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1).

plan documents, the person is a fiduciary.[100] Courts have found a member of a company's board of directors and insurance agents with authority to amend plan documents or manage fund investments to be fiduciaries (Sacher 2000, 625-26).[101] Persons who merely perform administrative functions for the pension plan and have no discretion regarding management of the plan are not fiduciaries.[102]

ERISA's broad definition of fiduciary allows for the "fractionalization of trusteeship" (Langbein, Stabile, and Wolk 2006, 516). While the commonly accepted definition of "trustee" is "the person holding property in trust," reflecting the notion of one person or entity managing the trust, ERISA's more complex definition allows management of the pension trust to be dispersed to numerous individuals and entities. With the vast sums of money involved in large pension plans, they frequently outsource management to the actuaries, consultants, or insurance companies who design the plan; several financial services companies who manage the investment of plan funds; a bank who safeguards the funds; third party administrators who decide claims and make payments; and lawyers, accountants, and actuaries who handle other daily administrative needs of the plan (Langbein Stabile, and Wolk 2006, 516-17). Langbein, Stabile, and Wolk's well-known pension law text book explains that "[b]y defining fiduciary status so broadly, ERISA

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[100] 29 C.F.R. § 2509.75-8, D-3 Q.

[101] Citing *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 262 (1993): "ERISA, however, defines 'fiduciary' not in terms of formal trusteeship, but in functional terms of control and authority over the plan." See also Langbein, Stabile, and Wolk (2006, 511).

[102] 29 C.F.R. § 2509.75-8, D-2 Q (explaining that "a person who performs purely ministerial functions such as the types described above for an employee benefit plan [which include determining eligibility to participate in the plan, calculating benefits, and making recommendations to others regarding plan administration] within a framework of policies, interpretations, rules, practices and procedures made by other persons is not a fiduciary").

allows plan designers to have considerable flexibility in allocating plan functions, while still preserving the protective principle that persons exercising material discretion must be responsible as fiduciaries for their conduct" (2006, 511).

To enforce ERISA's fiduciary provisions, Congress authorized both criminal and civil penalties. The statute provides for civil action by both plan participants and beneficiaries or the Secretary of Labor. ERISA created a private right of action as follows:

> A civil action may be brought – (1) by a participant or beneficiary – . . . (B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan. . . . (3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this subchapter or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provisions of this subchapter or the terms of the plan.[103]

This private litigation remedy was another protection of participants' rights through a review of fiduciary actions in the federal courts.

Of course these fiduciary protections would not have been necessary without Congress' act of delegation to private actors. In Chapter 3, now that the reader understands the course of pension regulation and reform, I will focus more narrowly on Congress' basic decision to delegate to private actors and affirm that it was a conscious decision instead of merely the continuance of past practices.

[103] ERISA § 502(a), 29 U.S.C. § 1132(a).

CHAPTER 3

THE NEED FOR ACCOUNTABILITY: DECISION TO DELEGATE TO PRIVATE ACTORS

After addressing above how Congress delegated to private fiduciaries under ERISA, questions remain about who those fiduciaries are and why Congress was willing to give them extensive power. Regardless of the private fiduciary's previous *de facto* dominance and control over employee pensions, with ERISA Congress formally recognized and approved of the fiduciary's power over private pensions.[104] This legislative anointment is the focus of my dissertation, and there is great import to Congress' formal approval of private fiduciaries – even if Congress at the same time enacted protections to control the behavior of fiduciaries and monitor their compliance with fiduciary duties.

Employers had not only inertia on their side when pressuring Congress to delegate power to private actors but also great expertise acquired over decades in the complex field of pension management. Executives and consultants understood not only the details of accrual, vesting, and funding, but also the idiosyncrasies of private plans amended regularly in response to a changing economy and worker demands. Unless Congress intended to demand uniformity and simplify private plans, it would be difficult for the government to more closely supervise such diverse plan terms. Reformers were unable to authorize the resources necessary to compete with the insider knowledge and substantial apparatuses already built by employers.

[104] Many thanks to Professor Wooten for raising this point in correspondence dated August 14, 2012.

Who Administers Pension Plans

Employers have relied on third parties to administer pension plans since their inception. Many early pension plans were administered by insurance companies. Because pension plans managed by insurance companies held up well during the Great Depression, insurance companies saw their market share of total pension coverage rise from 3.6 percent in 1930 to 16.3 percent in 1940, encompassing 700,000 plan participants (Sass 1997, 146). This growing business was less profitable than expected, however, due to lower than expected mortality and interest rates. Insurance companies, therefore, curtailed new business just as the tax increases of World War II increased the demand for private pensions (147).

After the war, interest rates rose and once again made group annuity pension plans profitable, but other players had arrived. The insurance carriers managed to repeal the tax on pension investments made by insurance companies instead of trust companies by 1961 (Sass 1997, 162-63). However, "[t]he inability to invest in equities thus came to be a central barrier to insurance company success in the pension field" because they could not offer sufficient rates of return on employer funds (166). By January 1963, insurance companies gained the right to create separate pension accounts that invested in equities and were now able to compete with trust companies (167), but insurance companies had lost their dominance and insured less than ten percent of single-employer plans and almost no multiemployer plans by the 1960s (150).

Changing risk preferences and economic conditions directed pension plans away from insurance companies as more plans self-insured. With basic retirement pay guaranteed by Social Security, participants were willing to tolerate more risk in their supplemental private pension plans (Sass 1997, 150-51). The additional cost of pension insurance and its inability to adjust to changed economic circumstances, such as increasing interest rates and thus inflation, also pushed employers away from insurers and towards the stock market. Nor did annuity contracts allow employers to alter their pension funding obligations depending on tax provisions or the company's cash flow needs (151-53). Finally, the Revenue Act of 1942 eliminated the advantage insurers had by no longer allowing companies to deduct the full cost of insurance premiums.

Most large corporations were already administering their own pension plans in trust form during the Depression and World War I. They were helped by, at a minimum, an actuary, a bank trustee, and often an investment advisor. During the war, banks aggressively grew their pension business, advertising record-keeping and plan payment services. Banks referred their plans to outside firms for plan design and actuarial consulting (Sass 1997, 154-55).[105]

Because self-insured pension plans needed to know the price of future benefit obligations, they often turned to insurance brokers (who later became pension consultants). These brokers began designing plans and offering actuarial services instead of merely connecting plan sponsors with the services of insurance companies. Many firms that formed in this manner, such as Towers,

[105] The availability of actuarial services was limited, however, in the middle of the century since there were few actuaries and most worked for insurance companies (Sass 1997 154-55).

Perrin, Forster & Crosby, the Wyatt Company, and the Martin E. Segal Companies, are still the main players today (Sass 1997, 156-58).

Pension consultants helped plan sponsors design pension plans to suit their needs. They made it possible to direct most of the funds to the highly compensated -- adjusting benefit accruals, using final salary in benefit calculations, and integrating plans with Social Security. Flexible vesting and funding schedules were developed as well to adjust to employers' cash flow needs. And none of these plan features needed to be actuarially sound since the federal government had yet to regulate the security of pension promises. Consultants frequently fiddled with actuarial assumptions such as mortality rates, retirements, future wages, and interest rates to justify increased or decreased pension contributions desired by sponsors (Sass 1997, 160-61). Pension consultants decried:

> Any course of action which leads to a stronger company, better able to weather occasional financial reverses, and to meet competition, may enhance the security of the employees as a whole, regardless of the current effect on the level of pension contributions . . .

(quoted in Sass 1997, 162).

By the early 1960s, most mid to large-sized companies sponsoring pensions already self-insured – leaving the pension industry to provide the remaining investment and actuarial services. While insurance companies provided both of these services "under one roof", trust companies and actuarial consultants provided only their respective services (Sass 1997, 168). As the complexity of benefits and related IRS regulations increased, outside providers became more important

(169). Sponsors also began to prefer the "unbundling" of services to make switching investment managers easier and to prevent the conflict of interest that resulted when an asset manager was paid based on the amount of assets controlled while that same institution designed the plan and therefore the amount of assets it would control (171). In addition, customized pension plans arose as the sizeable liabilities of pension plans were integrated more broadly into companies' financial planning and senior executives instead of human resources personnel took over management of pension plans within the corporations (172-73).

The decline of the insurance company as an integrated pension manager left employees less secure in their pensions at a time when pensions assumed greater importance due to increases in life expectancy and earlier retirements. Prior to ERISA, the numerous and decentralized provision of pension services through separate actuarial and legal consultants and investment managers left employees far less secure, particularly if these service providers lacked responsibility and accountability for the plan decisions they made (Sass 1997, 177-78).

Why Congress Delegated to Private Actors In Spite of Pension Scandals

As discussed above, pension reform advocates like Senators Javits and Williams used salacious tales of misdeeds by pension managers to garner press coverage for their crusade and create widespread public support for pension reform – rather than focusing on the more complex and less attention-getting details of pension accrual, vesting, and funding rules. After years spent describing horrific mismanagement and outright embezzlement by pension fiduciaries, why then

did they approve of the delegation of such vast authority over private pensions to these same fiduciaries? In truth, Javits and Williams (and other congressmen who passed ERISA) believed that fiduciary breaches were few and far between and that most pension plans were managed responsibly. Once the momentum for pension reform had virtually ensured legislation, Javits and Williams were able to strike a conciliatory tone and make clear that their earlier focus on the harm done by fiduciaries was merely a strategy designed to provoke public outrage. These later comments help explain why Congress was willing to delegate authority to these private figures after years of hearings and public statements regarding fiduciaries behaving badly.

Although pension reform advocates discussed complex issues like accrual, vesting, funding, and even termination insurance, they focused on publicizing the misdeeds of fiduciaries to avoid discussing individual stories of woe that seemed less broadly applicable and to dramatize the story about private pensions by creating a villain. Benefit forfeiture by individuals because of accrual and vesting rules was less appealing to the public than stories of fiduciary incompetence and graft that affected entire pension plans. Accrual and vesting rules applied to all pension plan participants, but the harshness of their application differed depending on the number of years worked before the forfeiture and the age of the employee at the time of forfeiture. Most workers who forfeited pension credits were young and would go on to earn pensions elsewhere, complicating the expectation of public outrage at tails of forfeiture. In addition, because the employment history of each worker forfeiting pension credit was different and records were sparse, it was difficult to determine the overall impact of such rules (Sass 1997, 187).

When discussing the need for fiduciary reform at hearings of the Subcommittee on Labor of the Senate Committee on Labor and Public Welfare held in July 1968, Senator Javits "refer[red] to a horror case" investigated by the Government Operations Committee, Permanent Subcommittee on Investigations and asked that their report dated June 30, 1966 be included in the records of these hearings on pension reform. That report examined the impropriety of George Barasch, founder of two New York/New Jersey unions, the Allied Trades Council (related to the AFL-CIO) and Local 815 of the International Brotherhood of Teamsters. As a lifetime trustee of the employee benefit funds of these unions, Barasch maintained the ability to harm plan participants even though he was no longer in power at the unions. He used roughly $4 million in benefit funds to create "research foundations" in Puerto Rico and Liberia. In another example of Barasch's malfeasance, the primary pension plan for the two unions paid pension benefits of $120,030 from 1960 to 1964 but paid $338,427 in administrative expenses during this time period to a not-for-profit corporation run by Barasch and his brother-in-law. Barasch and his associates also borrowed substantial sums from the benefit funds and offshore entities and made a substantial profit from investing those sums.[106]

Jimmy Hoffa is another prime example of the ability to make pension malfeasance sensational and bring the public into the quest for reform. President of the International Brotherhood of Teamsters, he ran the Central and Southern States Pension Fund (CSPF) with threats of strikes if he did not get his way. The result was that 75 percent of the fund's assets were lent to

[106] Employee Retirement Income Security Act: Hearings on S. 3421, S. 1024, S. 1103, S. 1255, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 90th Cong. 167-209 (1968) (statement of Senator Jacob Javits). Evidence showed that any management trustees helping to administer the benefit funds acted as merely a "rubber stamp" for Barasch's actions and that employers contributing to the benefit funds were unconcerned with the behavior of union officials as long as there was no labor unrest.

commercial enterprises run by friends and colleagues of Hoffa and other trustees at reduced rates, and some of these loans were risky. In addition, loan fees may have been kicked back to Hoffa, and loan proceeds may have been used to purchase political and legal influence (Sass 1997, 180-83).[107]

Javits and Williams went one step further and engaged in a campaign to rally the public behind pension reform – even if it meant rallying the public behind the fiduciary straw man. They publicized fiduciary breaches by holding hearings around the country in New York, Philadelphia, Cleveland, and Minneapolis. The stories they heard from those who came to discuss their own pension failures focused on the mundane issues of accrual and vesting. As Javits said, "It was heart-rending to hear these men and women recount how they had depended on their pensions, had worked hard to earn a comfortable retirement, had lived for that day in many cases – only to find the pension snatched away almost at the last minute of the last hour, for some reason that most of them really did not understand" (Javits 1981, 381). Yet the stories the Senators fed back to the public through the press focused on pension fund theft and unsavory pension plan administrators.

Given the comparative scarcity of pension participants harmed by fiduciary breaches compared to participants who forfeited benefits due to lengthy vesting provisions, discussion of fiduciary

[107] See Gordon (1984, fn 39); *US v. Hoffa*, 367 F.2d 698 (7th Cir. 1966), vacated and remanded, 394 U.S. 310 (1969) (upholding conviction of Hoffa for mail fraud).

mismanagement is vastly overrepresented in news coverage of the time period.[108] Many examples of the investment of pension funds in employer securities to benefit employers and not participants are cited.[109] Other examples include conflicted decision makers[110] and excessive management fees.[111] In one case, officers of a holding company used pension funds to purchase stock in the holding company to prop up its value – while simultaneously selling their own stock in the company. The fund eventually lost $1.6 million on the stock.[112] The media also overemphasized the problem of fiduciary mismanagement by union officials,[113] particularly

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[108] Even some newspaper articles admitted that most pension plans were being appropriately managed. See "Urged: Tighter Rules on Pension Funds," U.S. News & World Report, April 12, 1971 ("Private studies in recent years have indicated that most funds are soundly based and adequately financed."); Kessler, Ronald, "Lapses by Huge Pension Funds Bring Huge Cries for Greater Control," Washington Post, November 24, 1970 ("The majority of pension funds are run fairly and prudently.").

[109] See Kessler, Ronald, "Lapses by Huge Pension Funds Bring Huge Cries for Greater Control," Washington Post, Nov. 24, 1970 ("Many bankers and pension administrators believe pension funds that invest heavily in the stock of the fund's own company present opportunities for conflict-of-interest and place employees in double jeopardy: if the company becomes bankrupt, the pension assets are worthless."); Lardner, Jr., George, "Pension Plan Study Reveals Big Majority Gets No Benefits," Washington Post, April 1, 1971 (citing examples from the Senate pension study initiated by Javits and Williams including a "Midwestern cable corporation with $900,000 or 5 [sic] percent of its $1.7 million in pension fund assets invested in securities of the company"); Strong, James, and Ronald Koziol, "Retirement Dreams Become Tragedies in 'Pension Hoaxes'," Chicago Tribune, March 21, 1971 (citing examples from fiduciary breaches in Labor Department records, including a Chicago trustee who invested $250,000 – 69 percent of the pension fund's assets – in the company's preferred stock, an investment that declined in value to $13,500).

[110] See Lardner, Jr., George, "Pension Plan Study Reveals Big Majority Gets No Benefits," Washington Post, April 1, 1971 (citing examples from the Senate pension study initiated by Javits and Williams including a "major oil company in Oklahoma whose president is both trustee of its $62.2 million pension plan and a director of the bank where the funds are deposited").

[111] See Shabecoff, Philip, "Pension Plan Plans Scored by Study—Panel in Study Finds Few Workers Get Any Benefits," N.Y. Times, April 1, 1971 (citing examples from the Senate pension study initiated by Javits and Williams including a cable company in the Midwest noted above as being over-invested in employer securities which "also spent a third more on costs to operate the plan than it did on benefits"); "What You Should Know About Your Pension," excerpt from Harvest Years, Apr. 1971 (citing example where one corporation had five trustees run its 16 pension and profit-sharing plans, and they were paid $300,000 in fees in addition to the $130,000 paid to an outside company for investments and plan administration services).

[112] "What You Should Know About Your Pension," excerpt from Harvest Years, April 1971.

[113] Kessler, Ronald, "Lapses by Huge Pension Funds Bring Huge Cries for Greater Control," Washington Post, November 24, 1970 (citing inappropriate loans by union officials running pension funds and kickbacks from those

given that only approximately seven percent of retirement plans were administered jointly by unions and only one percent solely by unions.[114]

In response, the public bombarded their Congressmen with letters demanding reform. Javits (1981, 381) explained that "with business groups opposed, and organized labor divided, the most important support came from the people and the press. We received thousands of letters from victims who volunteered to testify [at upcoming hearings by the Senate Labor Committee]. In one two-week period in 1972 my office received twenty thousand letters of support for pension reform."

Without rallying the public around the broadly applicable and easy to understand issue of fiduciary mismanagement, there would have been no mass public support for pension reform. Only by stoking public outrage on this "narrow problem" could Javits and Williams insist on pension reform on their terms to satisfy the public. The fact that those terms included vesting and funding reform was always the plan. They needed the ammunition to insist on comprehensive reform and found it in the overwhelming response of the public to their publicity campaign.

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loans which the article claims occurs too often because "[i]t's disloyal for a union member to question his officers about pension money). In perhaps one of the best examples of sensational coverage, a newspaper article touted how "loose control of pension funds" resulted in murder. Strong, James, and Ronald Koziol, "Retirement Dreams Become Tragedies in 'Pension Hoaxes'," Chicago Tribune, March 21, 1971 ("Two members of a painters' union local in San Francisco, Dow Wilson and Lloyd Green, were killed by trustees to cover thefts from union pension funds.").

[114] Employee Retirement Income Security Act: Hearings on S. 3421, S. 1024, S. 1103, S. 1255, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 90th Cong. 268 (1968) (statement of Thomas R. Donahue, Assistant Secretary of Labor).

The hearings that Javits and Williams held via the Subcommittee on Labor of the Senate Committee on Labor and Public Welfare in July and October of 1971 followed a similar path to their hearings around the country – listening to tales of forfeiture due to strict plan rules on accrual and vesting and then focusing disproportionately on tales of mismanagement, conflict of interest, and outright theft. The July hearings allowed pension participants to convey their stories of hardship, and they focused mainly on those who lost their expected pensions through strict accrual and vesting rules. In October, however, the hearings focused on pension plan administrators who used pension funds for their own purposes instead of acting in the best interests of employees. Testimony repeatedly returned to the issue of trustees investing pension funds in employer securities and real estate connected to the employer's business.[115] The focus on conflicts of interest included a discussion regarding how overvaluation of the pension fund's real estate investments allowed a company to reduce its required contributions to the fund to pay for pension benefits.[116] When questioned whether these investments resulted in conflicts of interest for the pension plan trustees, some executives/trustees denied the existence of any conflicts. At one point, Javits' pension counsel, Michael Gordon, asked Robert G. Zimmerman of F.W. Woolworth Company, "Do you see any possible conflict of loyalty which might arise by virtue of the fact that the retirement committee, which consists of members of the board of

[115] See, *e.g.*, Employee Retirement Income Security Act: Hearings on Private Welfare and Pension Plan Study, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 92nd Cong. 521-22 (Oct. 1971) (questioning J. Godfrey Butler, Senior Vice President of D.C. Transit System, Inc. regarding why the company's pension fund has a $2.3 million mortgage on property owned by the company).

[116] See Employee Retirement Income Security Act: Hearings on Private Welfare and Pension Plan Study, Day 2, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 92nd Cong. 707 (Oct. 1971) (questioning William L. Bland, Assistant Secretary at Genesco regarding the company pension fund's investment of one-third of its assets in Genesco securities or property of a related company).

directors of the Woolworth Co., would be responsible ultimately for making a decision about unloading Woolworth's properties if that necessity should ever arise?" Mr. Zimmerman responded, "I don't see any conflict at all."[117]

Yet examples like Hoffa were few and far between. Most pension funds were run conservatively to maximize the funds available for participants (Sass 1997, 183). In fact, the United Auto Workers, who negotiated the failed Studebaker pension plan, helped run the plans they negotiated with integrity. They even liberalized vesting procedures in contracts with Ford and struck Chrysler over pension plan funding. Studebaker thus represented more systemic issues with the pension system than occasional fiduciary breaches (Sass 1997, 183-84).

At the 1971 Senate Labor Committee hearings, Javits himself acknowledged that the true problem with the pension system was not fiduciary malfeasance. As Javits stated on July 27, 1971:

> It would be comforting, in a way, to find that the widespread disappointments in the pension field are simply the products of fraud, theft and criminal activity, because then all we have to do to solve the problem is 'catch the thieves' – not provide for a system which would really deliver on the sound and highly desirable pension plan idea. Not that there are no thieves in the pension business – we all know there are some, though I think there are very few.[118]

[117] Employee Retirement Income Security Act: Hearings on Private Welfare and Pension Plan Study, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 92nd Cong. 773 (Oct. 1971).

[118] Employee Retirement Income Security Act: Hearings on Private Welfare and Pension Plan Study, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 92nd Cong. 12 (July1971).

Continuing his efforts to move pension reform beyond fiduciary protections to pass comprehensive legislation, Javits added later that day:

> [T]here are all too many who believe that the inequities in the private pension system are caused by dishonest and corrupt individuals and that all that is necessary is to establish strong federal standards of fiduciary responsibility. I yield to no one in my concern over assuring the honest, loyal and prudent management of welfare and pension plans, but I can guarantee to this Committee that the vast majority of these funds are run honestly and faithfully, and that enactment of fiduciary standards alone would barely touch on the really serious and pervasive deficiencies in the private pension system.[119]

Javits even went so far as to reassure the fiduciaries questioned heatedly in October 1971 that the Committee was concerned with the lack of regulation of pension plans and not with painting all fiduciaries as unethical -- at least at this point in the process. To Jack F. Whitaker, President of Whitaker Cable Company, whose pension fund invested over $1.2 million in the company's own building, Javits explained:

> My only point is that, in the absence of any regulation in this field – this is all I am pointing out – it is possible for an employer contributed pension fund to buy a building of the employer himself for a big piece of assets of the pension fund, and I do not think this is desirable, in the interests of the workers or in the interests of the pension funds. It does not mean that there is anything that is immoral or culpable about you. I want to make that very clear. I am just pointing out that this is the end result. . . . I just want you to understand that there is no accusation, no question of moral fault, or anything else.[120]

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[119] Employee Retirement Income Security Act: Hearings on Private Welfare and Pension Plan Study, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 92nd Cong. 86 (July1971) (Testimony of Senator Javits, Ranking Republican Member of the Senate Labor and Public Welfare Committee, Prepared for delivery to The House General Subcommittee on Labor Hearing on Private Welfare and Pension Plan Legislation, Wednesday, April 28, 1971).

[120] Employee Retirement Income Security Act: Hearings on Private Welfare and Pension Plan Study, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 92nd Cong. 441 (Oct. 1971).

Javits goes on to again repeat how there is no "moral fault" here – although the pension fund's tax exempt status was revoked by the IRS and the executive was also a director of the bank that administered the pension plan.

Senator Javits' closing statement to the 1971 Senate Labor hearings makes clear that he was not looking to alter the traditional framework that allowed company executives to serve as pension fund trustees. Instead, he wanted only to add regulation to constrain fiduciary actions. Javits claims, "As every first year law student knows, it is a time-honored legal principal that 'no man can serve two masters.' . . . The massive use of tax-free funds set aside for employees as if they were an adjunct to the corporate treasury or to serve the interests of company officers is incompatible with a fiduciary's obligation. It is deplorable to assert before this committee that this sort of thing is in the employees' interests because the investment is sound." Yet Javits believed that additional regulations would allow fiduciaries to no longer "serve two masters" and presumably think entirely of the interests of participants when making decisions for the pension fund. He was "confident that this subcommittee will take the action that is necessary to see to it that the level of conduct for pension trustees is 'kept at a level higher than that trodden by the crowd.'"[121]

[121] Employee Retirement Income Security Act: Hearings on Private Welfare and Pension Plan Study, Day 2, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 92nd Cong. 878, 880 (Oct. 1971) (quoting *Meinhard v. Salmon*, 164 N.E. 545 (N.Y. 1928)).

Why Congress Delegated to Private Fiduciaries Instead of the Bureaucracy

As discussed in my Introduction, many scholars have examined why Congress delegates authority at all. Epstein and O'Halloran (1999), however, examine the question of when Congress decides to delegate authority to the executive branch and when it instead drafts detailed legislation itself and leaves little discretion for other policymakers. Using a "transaction cost politics" approach, they find that legislators make policy when "political benefits" to themselves exceed "political costs"; where costs exceed benefits, legislators delegate.

My argument here, however, is that the framework for analysis is not merely whether legislators make policy or delegate to the executive.[122] Instead, legislators can also choose to delegate to private actors and use administrative procedures and the courts to supervise those actors just as they use those methods to supervise executive agencies. Thus, while Congress may delegate less to the executive during divided government (Epstein and O'Halloran 1999, 135), as during Nixon's second term when ERISA passed, there are competing concerns.[123] Epstein and O'Halloran theorize that Congress will delegate more to the executive in a highly technical, complicated area such as pension regulation with few particularized benefits to claim credit for providing through legislation (230-31). Given the competing tendencies to delegate less to the executive under divided government and more given the complexity of private pensions, the

[122] Epstein and O'Halloran (1999) do include in their models the federalist concept of delegation to the states, local governmental entities, and the courts as a way to avoid delegating to the executive (153-54, 156-67). This is a small part of their analysis, however, and their focus is on whether the locus of policymaking remains in Congress or is delegated to the executive branch.

[123] See Krent (1990) for an argument that congressional delegations outside of the federal government, which may include private litigation remedies to enforce federal statutes, run afoul of the separation of powers doctrine.

question needs to be answered if this is precisely the type of situation in which legislators delegate more to private actors. After all:

> Structural choices have importance consequences for the content and direction of policy, and political actors know it. When they make choices about structure, they are implicitly making choices about policy. And precisely because this is so, issues of structure are inevitably caught up in the larger political struggle. Any notion that political actors might confine their attention to policymaking and turn organizational design over to neutral criteria or efficiency experts denies the realities of politics.

(Epstein and O'Halloran 1999, 153, quoting Moe 1998, 268).

When debating pension reform, Congress faced overwhelming pressure to delegate to private actors. In fact, the above legislative history indicates that the only way comprehensive pension legislation could pass was through delegation to private actors. Not only did congressional democrats (and indeed all congressmen) want to avoid giving President Nixon the type of power that he would gain if the bureaucracy more closely supervised private pensions and perhaps adjudicated any disputes regarding those pensions, but Congress had to contend with the status quo.

Employers had spent decades running their pension plans as they saw fit. Leaving substantial authority in their hands was the only way to avoid outright rebellion. In addition, employers had another important advantage: expertise. Their accumulated experience in administering private pensions meant that they understood the funding, accrual, and vesting issues better than Congress and had the loyalty of an industry of actuaries and investment managers. This made congressional deference to employers understandable and efficient. Congress was mainly

content to allow employers significant discretion, then, while at the same time attempting to reign in the outlandish abuses that had been well-publicized.

As the next chapters evaluate enforcement of these fiduciary protections and resulting accountability, it is important to recognize that the design of the accountability regime for ERISA plan administrators incorporates not only fiduciary duties but enforcement of those duties by agencies and courts. Any failure of fiduciary standards to hold employers accountable for supervising private pension plans then can be attributed either to the failure of fiduciary duties as an accountability mechanism when the government delegates to private actors or to the failure of the bureaucracy and/or the courts to enforce those fiduciary provisions as intended.

CHAPTER 4

THE FAILURE OF POLITICAL ACCOUNTABILITY UNDER ERISA

In 1922, Roscoe Pound wrote that "[w]ealth in a commercial age is made up largely of promises" (Langbein 2004, 53, quoting Pound 1922, 236). The primary impetus behind ERISA was to ensure that employers honored their promises to pay pension benefits to employees, and any evaluation of enforcement and accountability must incorporate this goal. ERISA permits executives and agents of the employer to serve as fiduciaries[124] but includes a broad definition of fiduciary to ensure that they act in the best interests of participants and beneficiaries instead of the employer. Anyone who has discretion to manage the plan or its assets or "has any discretionary authority or discretionary responsibility in the administration of such plan" is a fiduciary and subject to ERISA's enforcement provisions.[125]

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[124] ERISA § 408(c), 29 U.S.C. 1108(c) ("Nothing in section 1106 of this title shall be construed to prohibit any fiduciary from— . . . (3) serving as a fiduciary in addition to being an officer, employee, agent, or other representative of a party in interest.").

[125] ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A). As the conference committee explained:

> Under this definition, fiduciaries include officers and directors of a plan, members of a plan's investment committee and persons who select these individuals. Consequently, the definition includes persons who have authority and responsibility with respect to the matter in question, regardless of their formal title. The term 'fiduciary' also includes any person who renders investment advice for a fee and includes persons to whom 'discretionary' duties have been delegated by named fiduciaries.
>
> While the ordinary functions of consultants and advisers to employee benefit plans (other than investment advisers) may not be considered as fiduciary functions, it must be recognized that there will be situations where such consultants and advisers may because of their special expertise, in effect, be exercising discretionary authority or control with respect to the management or administration of such plan or some authority or control regarding its assets. In such cases, they are to be regarded as having assumed fiduciary obligations within the meaning of the applicable definition.

James Q. Wilson (1989, 25-26) wrote that successful bureaucracies, or organizations, focus on tasks and not on goals. Goals can be hard to pin down, and there is frequently disagreement about what the goals are from the start. In the case of government bureaucracies, there is disagreement about goals within Congress and between Congress and the President. Focusing on tasks thus allows bureaucracies to move forward and take decisive action, but it may not lead directly to a clear "end" even if the goal or goals as understood are taken into account when performing tasks.

ERISA complicates the achievement of the goal of protecting promises to workers further because of a contradictory (at times) goal and an overwhelming complexity. Encouraging employers to voluntarily offer pension benefits to their employees means protecting workers without overly burdening employers with regulations. Incentivizing employers to create and maintain pension plans is therefore a competing goal. And the complexity of pension regulation and enforcement because of both the expertise required to plot a course towards the goal and the coordination required by the overlapping jurisdiction of two government agencies makes meeting the goal of worker protection more difficult. Complexity makes it harder to predict that the tasks performed are in fact a means to achieve the end and that there is a united path towards the goal, even if the effort to protect workers is made.

Taking the competing goal of encouraging employers to offer pension benefits as a given, this chapter focuses on how the added complexity of concurrent and overlapping bureaucratic

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Highlights of the New Pension Reform Law, Text of Joint Explanatory Statement of Conference Committee, at 124-25 (1974).

jurisdiction under ERISA and insufficient resources for enforcement made it impossible for the bureaucracy to achieve the goal of protecting workers. The bureaucratic agencies with enforcement responsibilities failed to ensure political accountability for meeting the goal of worker protection (which even critics agree was at a minimum one main purpose of the legislation). This chapter and the next serve as a reminder that the execution of laws can undo congressional bargains.

The Triumph of ERISA's Private Litigation Remedy

With respect to enforcement of pension reform legislation, Senator Javits wrote:

> I think a single agency is required for the purpose and it will be a very difficult task to regulate the operation of the employee benefit plans sufficiently to assure legitimate expectations of employee participation while avoiding undue and unnecessary interference in the operation of these plans. Overregulation or unnecessary regulation would be worse than none for it would defer the installation and improvement of these much-needed programs. We have to steer between frustrated expectations for pension plan members growing out of no regulation and frustrations caused by overregulation which will deter the employer from instituting a pension plan.[126]

Despite the consensus among most pension reform advocates that a single bureaucratic agency was preferable to fragmented bureaucratic jurisdiction, Congress (for the reasons discussed below) placed principal responsibility for enforcing the statute with two existing bureaucratic

[126] Employee Retirement Income Security Act: Hearings on S. 3421, S. 1024, S. 1103, S. 1255, Day 1, Before the Subcommittee on Labor of the Committee on Labor and Public Welfare, 90th Cong. 210 (1968) (statement of Senator Jacob Javits).

agencies rather than creating a single agency to regulate pensions and perhaps even adjudicate disputes.[127]

Given the extent of the authority Congress was delegating to employers as fiduciaries, Congress faced an important question when deciding who would enforce the bargain reached to better protect workers against abuses: (1) the bureaucracy – and if so, which agency, (2) the courts, or (3) both. In the end, Congress split regulatory authority between the Department of Labor and the Internal Revenue Service to resolve conflict between congressional committees, bureaucratic agencies, and interest groups. The result was that neither agency became a policy leader – leaving the bulk of the ERISA enforcement responsibilities to the courts and to the participants themselves who would initiate lawsuits in the absence of bureaucratic enforcement. Before turning to an account of why redundancy failed under ERISA, I will review the literature's recent focus on the benefits of redundancy to show why it was not effective in this case.

Redundancy – Friend or Foe?

Beginning in 1969 with Martin Landau's article, the literature on redundancy in government has fought back against the notion that redundancy is wasteful and inefficient. To counter the modern movement to reduce "duplication and overlap" (349) in government as was being done in private firms, Landau theorized that such efforts would instead harm public administration.

[127] As discussed further below, participants and beneficiaries were authorized under ERISA to file lawsuits to enforce their rights under the statute, and the courts have sole adjudicative power under ERISA to resolve disputes between plan administrators and participants and beneficiaries.

While touting the redundancy built into our government's system of checks and balances, Landau argues, "If there is no duplication, if there is no overlap, if there is no ambiguity, an organization will neither be able to suppress error nor generate alternate routes of action. In short, it will be most unreliable and least flexible, sluggish, as we now say" (356).

In the context of service delivery, duplication signifies that two agencies "both provide the same services through identical systems" (Miranda and Lerner 1995, 196, citing Lerner 1986, 336). Duplication, while costly, reduces the probability of a system failure as long as the redundant parts function independently (so that if one fails the other will not fail as a result) (Lerner 1986, 350). While more important to the reliability of mechanical or security systems, for example, duplication and its corresponding increase in reliability can help ensure sufficient social service delivery.

Overlap means that the agencies "have a different core set of activities, but also produce some of the same services" (Lerner 1986, 336). This latter category fits the example of the relationship between the Department of Labor (DOL) and Internal Revenue Service (IRS) under ERISA. Laundau's discussion of overlap and precisely how it results in increased reliability in biological organisms is considerably more nebulous (350-51).

In addition to reliability and flexibility, scholars argued that competition among government agencies has efficiency benefits just as it does in the private sector (Bendor 1985, 33; Miranda and Lerner 1995, 194). Niskanen (1971) argued that inter-agency competition may reduce the

effects of an agency's monopoly jurisdiction because bureaucrats have greater information about the cost to produce the required services and supposedly seek to maximize their budgets instead of providing services more efficiently. Competition can also improve the quality of services provided (Miranda and Lerner 1995, 198).

The primary criticisms of redundancy are that it is inefficient, may result in regulatory gaps assuming a zero-sum budget game, and that it makes assigning responsibility for an error or problem difficult (Bendor 1985, 28-30). The most relevant concern for my work is that redundancy decreases accountability in organizations. "Overlapping jurisdictions make it difficult to place blame when things go wrong" (Streeter 1992, 106-07). As Wilson (1989, 274) has said regarding redundancy in bureaucracy, while redundancies are not necessarily bad, "[t]he problem, of course, is to choose between good and bad redundancies."

Law professor Michael Doran (2011, 1858) argues that redundancy in retirement-security programs enacted by Congress (including ERISA) is a reflection of "the distributive costs and informational benefits associated with administrative redundancy." Instead of having one program for older Americans under the jurisdiction of one congressional committee and one bureaucratic agency, Social Security, Medicare, and the other tax expenditure and regulatory programs were enacted and are monitored by different committees and different agencies. Responsibility for ERISA is divided among four congressional committees and two agencies (three if you include the insurance program run by the Pension Benefit Guaranty Corporation) (1860). Doran argues that while it is possible that this redundancy is designed to ensure that

older Americans are very well taken care of (that reliability factor discussed above), it is more likely that congressional committees with ties to different agencies are simply trying to gain power over an issue of great importance to many of their constituents. ERISA allows the Senate Finance and Health, Education, Labor, and Pensions Committees and the House Ways and Means and Education and Workforce Committees to control over $6.3 trillion in private pension money.[128] But by fragmenting authority over retirement-security programs, Congress is able to take advantage of the specialized knowledge of the different committees and agencies (1861-62). The balance of distributive costs and informational benefits is difficult to quantify, but my dissertation measures instead the accountability costs.

My argument is that the overlapping jurisdiction of the DOL and IRS over private pension plans prevented the DOL (or a new agency with sole jurisdiction over private pensions) from assuming the leadership role it would otherwise have assumed over protecting promises made to workers using ERISA's fiduciary provisions. To give an analogy, two Black Hawk helicopters were shot down over Iraq in a friendly fire incident because each F-15 pilot patrolling the area did not confirm the identity of the helicopters but instead thought the other pilot had done so (Carroll 2004, 955, citing Sagan 2004). The overlapping jurisdiction over private pension regulation left each agency regulating ERISA assuming the other would step up. The leadership failure left the courts to establish a unified pension policy through private litigation to which the agencies were not a party, and it did not further the goal of protecting workers.

[128] Private Pension Plan Bulletin Historical Tables and Graphs. U.S. Department of Labor Employee Benefits Security Administration. June 2013. Table E1. Number of Pension Plans *by type of plan, 1975-2011*. Available at http://www.dol.gov/ebsa/pdf/historicaltables.pdf.

The Death of the Single Agency Proposal

Because pension rights were litigated rarely prior to ERISA as a result of the large costs involved and the small potential recovery, reform advocates argued that "you need an agency to enforce these private rights, or a union." But which agency?[129] The Department of Commerce was viewed as favorable to business, while the DOL supposedly sided with workers. The IRS already helped regulate the tax qualification of pension plans.

The debate over where to place enforcement authority within the bureaucracy embroiled congressmen, their committees, and their business and labor constituencies for years. Their inability to agree on where to locate enforcement duties doomed the proposal of a single, powerful agency regulating private pensions and consequently enhanced the significance of the private litigation remedy.[130]

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[129] Private Pension Plan Reform: Hearings Before the Senate Committee on Finance, Subcommittee on Private Pension Plans, 93d Cong. 992-95 (1974) (statement of Frank Cummings). Cummings asserted that the Internal Revenue Service could not be an enforcement agency because:

> [i]t isn't equipped to enforce private rights. Only the Labor Department is, which, after all, enforces private rights all the time. For example, if you don't pay time and one-half for overtime, you go to the Labor Department and the Labor Department says "do it" and it goes into the court and the judge says "do it." So, if you want to protect private rights, you have to create private rights and you have to create an agency that will enforce those private rights.

Id. at 848. While unions and the Democrats who traditionally represented them favored enforcement by the Department of Labor, employers favored the Securities and Exchange Commission or Internal Revenue Service since the Department of Commerce lacked expertise in the area. See Wooten (2004, 47).

[130] Controversy over which part of the bureaucracy should have oversight of pension regulation began in the decades prior to ERISA's enactment as momentum for pension reform built. Legislation to force increased and more accurate disclosure from plans was gutted prior to passage because of disagreement over the location and extent of enforcement powers. An Eisenhower bill from January 1956 required pension plans to report to the DOL, the traditional regulator of the employment relationship. The Douglas-Ives-Murray bill introduced in May 1956 in the

When Senator Javits introduced the first comprehensive bill for pension reform, the Pension and Employee Benefit Act of 1967, he proposed a single agency with oversight – "an independent commission that would have jurisdiction over the new regulations as well as most existing federal oversight of employee benefit plans."[131] Drawing on recent pension legislation in Ontario,[132] Javits' "United States Pension and Employee Benefit Plan Commission" would have included five members appointed by the President with the advice and counsel of the Senate.[133] Among the duties of the Commission were "to promote the establishment, extension, and improvement" of pension plans and to register or decline to register plans.[134] As part of those duties, the Commission had the power to inspect the books and records of pension plans and broadly "to require any such administrator, employer, insurer, trustee, or other person to furnish,

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Senate, however, provided that pension plans would register and file reports with the SEC. Employees would receive summaries of plan terms, and the SEC could penalize incomplete or inaccurate disclosure with fines or imprisonment. In the end, the Welfare and Pension Plans Disclosure Act of 1958 placed oversight within the DOL but denied automatic disclosure to employees and eliminated penalties for false statements, omissions, and even embezzlement. Thus, the legislation denied the DOL "the investigative and enforcement authority it would need to implement the law" (Wooten 2004, 45-49, 121-22).

[131] Wooten (2004, 129-30, 177) (Senator Williams called in February 1972 for "the centralization in one agency of all existing as well as prospective regulation of private pension plans."). The President's Committee's report also introduced the possibility of a central pension agency. "As suggested by the Commission on Money and Credit, it might be necessary to empower a regulatory agency to act as guardian for the collective interests of employees and their beneficiaries and, if necessary, to bring suit in [sic] behalf of the plan participants." President's Committee on Corporate Pension Funds and Other Private Retirement and Welfare Programs. 1965. *Public Policy and Private Pension Programs: A Report to the President on Private Employee Retirement Plans*, at 78. U.S. Government Printing Office.

[132] See copy of Ontario legislation, *The Pension Benefits Act of 1965*; correspondence from Allen E. Kaye to Frank Cummings, Mar. 7, 1966; correspondence from R. M. Gaby to Allen E. Kaye. Mar. 21, 1966; correspondence from Laurence E. Coward to Allen E. Kaye, Mar. 24, 1966, Box 92, Folder Pension Reform – Pension Background – 1965-1970, Series 4, Subseries 3, Senator Jacob K. Javits Collection, Special Collections. Department, Frank Melville, Jr. Memorial Library, Stony Brook University, Stony Brook, N.Y. ("Javits Collection").

[133] S. 1103 § 3(a), 90th Cong., Cong. Rec. 4654 (Feb. 28, 1967).

[134] Id. at § 4(a).

in a form acceptable to the Commission, such information as the Commission deems necessary for the purpose of ascertaining whether this Act and regulations of the Commission hereunder have been or are being complied with."[135]

As Javits himself stated, "My [1967] bill also would have established a U.S. Pension Commission, analogous to the Securities and Exchange Commission, to supervise the complex and technical aspects of pension plans" (Javits 1981, 380).[136] Javits' 1967 bill envisioned a single regulatory body because he thought it necessary to "respond effectively to the inevitable shocks in its economic environment and shifts in the power, and interests, of its various constituents." He wanted to take power over pensions from its jurisdiction in the IRS, DOL, SEC, and Social Security Administration, and give it to a unified commission, as well as adding domain over a new portability program (Sass 1997, 211). Indeed Javits was "convinced that a single agency is required" to manage the delicate task of safeguarding employee pensions while promoting the maintenance and growth of private pensions by employers (Gordon 1984, 13-14, citing 113 Cong. Rec. 4650-4653 (Feb. 28, 1967)).

Although those working on pension reform had assumed that all vesting, funding, and termination insurance proposals would amend the tax code, Javits and his staff placed all elements of his bill under the labor laws to avoid the powerful and hostile House Ways and

[135] Id. at § 4(b).

[136] See Gordon (1984, 13-14). Javits' proposal also called for this independent pension agency to supervise a new portability program in which participants could accumulate small pension credits from various employers into a single pension. Difficulties in administering this portability program such as how to deal with inflation while not making these government-backed pensions more generous or secure than private pensions caused the proposal to fail both in the United States and when considered in Canada and England (Sass 1997, 196-97, 211-12).

Means Committee and instead give jurisdiction to the Senate Labor Committee (Wooten 2004, 129-30). Thus began a lengthy battle between congressional committees with jurisdiction over labor matters and those supervising taxation. The single agency proposal fell victim to the jurisdictional dispute.

As soon as Javits proposed a single agency to administer pension reform, opposition to the idea arose. A memorandum from the Bureau of the Budget ("BOB Memo") dated September 8, 1967 explains that even without "thorough study" of current and prospective pension regulation, "[i]t does not appear feasible to vest all functions relating to pension plans in a single agency" and "[i]t does not appear feasible to vest the new functions, or the existing functions which may be separable, in a new agency."[137] The BOB Memo argued that a single agency was unworkable because pension functions already performed by existing agencies were tied to their core missions. For example, the IRS determination of qualification for tax deductions was related to basic tax administration. "Similarly, Labor's functions with respect to bargaining rights and overtime rate computations with respect to pension plans do not appear separable from its broader role in those areas."[138] No explanation of why these tasks could not be performed by a different agency is given.

The BOB Memo finds problems with creating an independent agency to administer and enforce pension regulation – or as much as can be separated from existing agencies:

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[137] Memorandum from the Executive Office of the President, Bureau of the Budget, Howard Schnoor to Mr. March, *Organization for private pension plan program*, Sept. 8, 1967, at 2, Box 119, Folder Pension Reform: Inter-Agency Task Force on Private Pension Plans – 1966-1969, Javits Collection.

[138] Id.

> Such an agency, even with the broadest possible program now envisioned, would be small and isolated from the major policy-making agencies of Government. It would have little chance of access to the President, and problems could develop in trying to develop its programs in the context of related programs affecting the labor force and income maintenance in other agencies.[139]

The Johnson administration task force considering pension reform opposed bureaucratic consolidation for practical reasons. Representative Wilbur Mills, chairman of the House Ways and Means Committee, opposed many of the reforms proposed. Focusing on substantive reforms in areas such as vesting and funding, the task force wanted to avoid Mills by drafting a bill under the jurisdiction of labor committees in Congress and enforced by the DOL. This made consolidation of the IRS' current pension duties impossible at the time (although Mills and congressional tax committees later become involved in pension reform) (Sass 1997, 212).

For the next several years, Javits continued to push for a single agency to enforce ERISA within the bureaucracy. On May 14, 1969, he again introduced legislation that sought to "establish an SEC-style agency" that would have oversight of new pension standards and "any existing regulatory standards dealing with pension and welfare plans that now rest in other Federal agencies."[140] Recognizing the deep divisions even among those involved within the pension reform movement, Javits hedged: "I do not, however, claim that this bill represents the only way

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[139] Id.

[140] *Javits Seeks SEC-Type Agency to Oversee $100-Billion Private Pension Plans; Bill Protects Against Last-Minute Pension Forfeiture After Long Service*, May 14, 1969, Box 121, Folder Pension Reform: Pension Legislation – 1968-69, Javits Collection.

of dealing with problems in the pension field; there are other approaches which can and should be explored."[141]

Further study of the structure of pension regulation emphasized the political difficulties of consolidating enforcement within a single agency while acknowledging its benefits. The Secretaries of Labor and Commerce on April 14, 1969 charged a Joint Task Force with reviewing the "'security' issues of vesting, funding, insurance and portability." The Task Force included in its resulting report a chapter that examined potential routes of administration and enforcement for pension reform legislation. Specifically, it looked at the questions: (1) "Should all pension plan activities of the Federal government be vested in a single agency?" and (2) "Assuming that pension regulatory functions should be consolidated in a single agency, should that agency constitute a new independent regulatory agency?"[142]

The Task Force concluded that a single agency should administer and enforce all pension regulation. Among the benefits of the single agency concept noted were easing the burden on employers administering pension plans, reducing duplication, and achieving coordinated pension policy to safeguard pensions while also encouraging the expansion of private pension plans. "A single agency, possessed of all the expertise and experience available, would be able to focus in

[141] Quoted in id.

[142] Written Report from Joint Labor/Commerce Task Force review of pension security, Preface and Table of Contents to Administration & Enforcement chapter, Box 137, Folder Pension Reform: Pension Benefit Security Issues and Options 1969, Javits Collection.

the most efficient and flexible way on the complex and dynamic aspects of the private pension system."[143]

The Task Force acknowledged that the real question was not whether the federal government's regulation of pensions *should* be consolidated in a single agency but instead whether such an action was "feasible." Jurisdiction over pension issues was already fragmented because it involved the IRS, DOL, SEC, National Labor Relations Board, Department of Justice, and assorted other agencies applying their rules to pension plans.[144] It might not be possible to avoid IRS and SEC interaction with pension plans, for example, because their missions touched on the conduct of plans (as the BOB Memo had noted). If all pension matters could not be brought under one roof, the benefits of consolidation could not be fully achieved.[145]

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[143] Id. at 3.

[144] Id. at Administration & Enforcement chapter, 2-3. The report notes that current jurisdiction included: (1) the IRS management of tax qualification of plans and employer deductions; (2) the DOL enforcement of wage and hour laws that are affected by pension credits and gathering of labor statistics; (3) the SEC's application of rules to plan investments and information gathering on the same; (4) the NLRB's oversight of the Taft Hartley's provisions on whether pension plans penalize union members and are fairly bargained; (5) the enforcement by the DOJ of a section of the Taft Hartley Act dealing with improper use of benefit funds for purposes not benefiting employees; and (6) the application of EEOC, HUD, and DOD regulations to benefit plans. Id. at 2-3, 5-27.

[145] Id. at 3-4. The report cites Javits' seeming concern over the difficulties of implementing a single agency proposal:

> It may be that the entire scope of Treasury operations affecting pension plans should be transferred to the Commission. And yet, such determinations as the manner of integrating pension benefits with social security benefits and the determination of reasonable levels of compensation obviously have an important impact on Federal revenue considerations. Similarly, the extent to which regulations of pension plan investments is now performed by the Securities and Exchange Commission warrants careful consideration as to what functions, if any, should be transferred to the proposed Commission.

Id. at 4 (quoting 113 Cong. Rec. 4653 (1967) (statement of Sen. Javits)).

Most of the DOL's pension functions, such as enforcement of disclosure standards, were found capable of transfer and consolidation, but it was more difficult to transfer all IRS duties to another agency. Functions such as determinations that plans met qualification standards and the gathering of data on pension plans could be consolidated, but concerns of tax evasion, discrimination by pension plans in favor of highly compensated employees, and allowable deductions by employers and exclusions of trust income from taxation by pension plans related to the IRS' tax policy mission.[146] The report concluded that "centralization to the maximum feasible extent"[147] was still worthwhile given the benefits that would result.

The Task Force then considered which agency should administer and enforce pension regulation – an existing agency and, if so, which one, or a new, independent agency. Although the IRS was perhaps the best qualified to handle complex pension matters, "the public interest factor [of pension reform] transcends revenue considerations."[148] At the SEC, the mission to regulate securities might force labor and pension issues to a subsidiary role despite the SEC's experience handling disclosure, investments, and fiduciary law. While pension regulation did not clash with any preexisting core agency mission at the DOL, the report noted that a decision to consolidate regulation at the DOL would result in backlash from employers.[149]

[146] Id. at 5-14, 17-20, 27-28. The need for the Secretary of Labor to use the value of employee benefits as a component in the prevailing wage rates used to set the minimum wages was not readily subject to consolidation, though. Id.

[147] Id. at 28.

[148] Id.

[149] Id. at 29-30.

Uncertain which existing agency should have primary responsibility for pensions, the Task Force addressed the advantages and disadvantages of creating a new, independent body. Although independent agencies are typically thought to have greater political independence from the President (and thus have greater continuity of staffing at high levels), be more bipartisan, and be more efficient since they are focused on the statute they administer, the Task Force found no clear support for these supposed advantages. Similarly, the evidence was inconclusive on the supposed disadvantages of independent agencies, including that the President cannot control them or coordinate their policies, they are more readily subject to capture by the industries they regulate, and they have trouble juggling administration and enforcement with long-term policy coordination. The Task Force concluded by refusing to take a position on whether consolidation within an existing agency or the creation of a new agency was preferable, noting that political factors should influence the choice.[150] The fact that this group agreed that consolidation within a single agency was best but could not agree on which agency should have primary power to administer and enforce pension laws indicates how sensitive the issue was and how difficult the task of consolidation would be.

Ironically, however, labor put the final nail in the coffin of Javits' proposal for an independent agency with oversight of pension regulation. Javits attempted to gain the support of labor by placing that independent agency within the DOL in a draft bill proposed in February 1972 (Wooten 2004, 178). He did this in spite of arguing earlier that his U.S. Pension and Employee Benefit Commission, should have jurisdiction over pension regulation (including tax

[150] Id. at 31-36.

qualification) instead of the Department of Labor.[151] The AFL-CIO, however, rejected his proposal. After years of government scrutiny of labor actions, including hearings focusing on pension misdeeds by union leaders, the organization did not want to empower another government agency to investigate unions. If any agency was such power, it would need to be the DOL – the traditional friend of labor – not an independent and unknown power within that agency (Wooten 2004, 178).[152]

Javits was forced to advocate instead for consolidation of pension regulation within the DOL instead of an independent agency. The congressional testimony of Frank Cummings, Javits' Chief of Staff, is illustrative of Javits' position that an independent commission was best but given the lack of support for that idea, the DOL should manage as much ERISA enforcement as possible.[153] Cummings argued that an independent, SEC-like commission was the best answer for pension reform (as he helped Javits argue for years) because it could consolidate pension expertise and place all regulation under one agency for "one-stop service."[154] His key point here

[151] See *Hearing on S. 3421, S. 1024, S.1103, and S. 1255 Before S. Subcomm. on Labor and Pub. Welfare*, 90th Cong. 210 (1968) (statement of Sen. Jacob Javits) ("I think that the question of whether the Commission should run it or the Secretary of Labor should run it is a substantive difference, perhaps of a major character.").

[152] As Wooten (2004, 178) writes, "Labor leaders 'feel they must have 'their man' in the Cabinet to protect them against the possibilities of extreme action . . . .' The same concern led the AFL-CIO to demand Labor Department oversight of pension regulation. An 'independent agency . . . housed at the Department of Labor' would not do. The idea had to go and did."

[153] *Private Pension Plan Reform: Hearings Before the S. Comm. on Fin., Subcomm. on Private Pension Plans*, 93d Cong. 87-154 (1974) (statement of Frank Cummings).

[154] Written Report from Joint Labor/Commerce Task Force review of pension security, Administration & Enforcement chapter at 28, Box 137, Folder Pension Reform: Pension Benefit Security Issues and Options 1969, Javits Collection.

is the importance of consolidating all pension expertise in one agency to strengthen bureaucratic regulation:

> If the pension thrust of the IRS really has such extensive expertise, there is no reason why the personnel of that branch could not be transferred, en masse, to such a commission. If there is expertise in the Bureau of the Labor Department which now administers the Disclosure Act, the personnel of that branch could be transferred there, to such a Commission. With a corps of personnel like that, drawn from the IRS, the Labor Department, and perhaps also from the SEC, the Justice Department and from State Agencies preempted by federal law, I would doubt very much that any great additional bureaucracy would be needed.[155]

The same results could not be achieved merely by consolidating such expertise within an existing agency such as the IRS or DOL because they were already devoted to their core missions and would not give the same attention and resources to pension regulation.[156]

Yet, given that "no one seemed interested" during the years Javits pushed for the independent commission and there was "no evidence of increasing interest in it now," any consolidation of pension regulation needed to take place within the IRS or DOL.[157] Only the DOL was qualified to respond to employee complaints since the IRS – not used to responding to complaints from workers – offered merely the remedy of tax penalties or disqualification for the pension plan. This would present the employee the equivalent remedy of cutting off one's nose to spite one's face since the plan would then be less able to pay the employee pension benefits because its

[155] Id. at 28-29.

[156] Id. at 29.

[157] Id.

assets would be diminished by increased taxes on earnings and tax penalties.[158] This left the DOL as the best of the "half-loaf" options.[159]

Congressional hearings held immediately prior to the passage of ERISA indicate the ongoing dispute over regulatory jurisdiction. While Javits and other reform advocates affiliated with congressional labor committees as well as unions[160] thought the DOL should have as large a role

[158] Id. at 25-29. "The IRS is not essentially an investigating and enforcing agency. . . . Indeed, if a pension participant were to go to the IRS and complain . . . he would only be cutting his own throat. The most he could accomplish would be to disqualify the plan, and if he did so, he would be, in effect, reducing his own pension." Id. at 25.

[159] Influential pension scholar Merton Bernstein argued against "half-loaf" pension reform as "legislation that is inadequate and less than can be attained." Rebutting the argument that the legislation could be enhanced in the future, he asserted, "Pension reform factors are approaching a critical mass. Once legislation results, that mass will be dissipated." *Second Panel Discussion on Private Pension Plan Reform, Vesting and Funding Provisions; Termination Insurance; Portability; and Fiduciary Standards: Hearing Before the S. Comm. on Fin., Subcomm. on Private Pension Plans*, 93d Cong. 33 (1973) (statement of Merton Bernstein).

[160] Testimony by union representatives for the United Steelworkers of America and the United Auto Workers shows that they preferred jurisdiction within the DOL to the IRS. Similarly, a summary of AFL-CIO testimony provides that it:

> Urges that the Department of Labor administer the pension plan requirements, as in S. 4. Considers pension plans to be an integral part of the collective bargaining process. Suggests that placing the administration in an agency whose primary interest is in collection of taxes may place the agency in a conflict-of-interest situation in relation to policing any funding standard because the more rapidly a pension plan funds, the less it pays in taxes. Maintains that regulatory supervision under the IRS hinges on an employer's self interest in obtaining tax deductions. Feels that this is a very weak enforcement mechanism from the viewpoint of the beneficiaries. Considers possible IRS solutions to noncompliance to not really protect the interests of beneficiaries because if the plan's tax exemption is removed or the plan terminated, this does not help the beneficiaries.
>
> Asserts that better administration would occur if a single agency were to be responsible for both enforcement and reporting.

Digest of Testimony on Proposals for Private Pension Plan Reform Before the S Comm. on Fin., Subcomm. on Private Pension Plans, 93d Cong. 35-36 (1973); see Hearings before S. Comm. on Fin., Subcomm. on Private Pension Plans, 93d Cong. 384-85 (1973).

as possible, employers, their interest groups,[161] and members of congressional tax committees favored primary IRS jurisdiction because they viewed the DOL as biased in favor of employees.

The testimony of Senators Javits and Williams before the Senate Finance Committee's Subcommittee on Private Pension Plans shows not only the ongoing jurisdictional dispute over pension regulation within the Senate but also how Javits and Williams hedged and left the door open for significant IRS involvement because it was politically expedient.[162] Senator Javits stated that employers' primary motivation for maintaining pension plans is to improve employee morale and "employee relations", elements of the DOL's mission.[163] Among the other reasons cited why IRS administration was inappropriate was that half of pension plans were collectively bargained, tax penalties were insufficient, only the DOL jurisdiction would provide the necessary preemption of state law to ensure coordinated policy, and – most importantly – that the primary

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[161] A summary of testimony on the proper administering agency and enforcement for pension legislation shows that the American Bankers Association and the Chamber of Commerce believed that the IRS should have jurisdiction because of its expertise and impartiality. Interestingly, the National Association of Manufacturers (NAM) felt that "regulatory functions in the pension area performed by the various departments and agencies of government should continue under their respective jurisdictions and should not be centralized in one agency, thus preserving the technical expertise required." *Digest of Testimony on Proposals for Private Pension Plan Reform Before the S Comm. on Fin., Subcomm. on Private Pension Plans*, 93d Cong. 35-36 (1973). Perhaps not incidentally, the NAM's position was also likely to (and did in fact) continue the existing inefficiency and uncoordinated regulation of pension promises.

[162] See Hearings before S. Comm. on Fin., Subcomm. on Private Pension Plans, 93d Cong. 1075-1108 (1973) (remarks of Sen. Javits and Sen. Williams).

[163] Id. at 1084. Senator Williams added, "Now it just seems to me that we have reached a point where pension legislation most clearly falls within the stated purpose in the law of the Department of Labor as a Department 'to foster, promote, and develop the welfare of the wage earners of the United States and to improve their working conditions and to advance their opportunities for profitable employment.' This is intimately part of the job of benefit protection and, historically, that part of the workers' arrangement with his employer has been watched over under law and regulation by the Department of Labor." Id. at 1091-92.

mission of the IRS is collecting revenue through taxes and pension regulation would suffer from the IRS' need to focus on its core mission.[164]

When members of the Senate Finance Committee questioned whether Javits and Williams believed that there was any role for the IRS in pension regulation, they relented and agreed to some form of IRS involvement. As Javits said:

> Again . . . this doesn't denigrate the interests of the tax authorities nor their interest in the deductions which are taken for payment to pension plans. They have a vital interest. We don't challenge that at all.[165]

When trying to define exactly the ongoing role that they foresaw for the IRS in pension regulation, however, Senators Javits and Williams ran into trouble. As Senator Williams admitted, "this is not finally formed in my mind" – even after many years of work on the issue.[166] Senator Javits added that the IRS would have a role in determining reasonableness of compensation for purposes of discrimination in favor of highly compensated employees as well as enforcing eligibility and vesting standards "for tax purposes only."[167]

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[164] Id. at 1085, 1091 ("Senator, we believe very strongly that the weight of administrative judgment is for administration in the Labor Department because, while you are absolutely right about the fact that IRS is doing more than they did, the fact is that it is still their primary jurisdiction to collect taxes and punish evasion and define people who evade. This represents such an enormous range in which they must operate, that pension plan supervision would only be one item."); see Wooten (2004, 205), explaining that it was uncertain whether the IRS' implementation of the power to tax could include preemption of state pension regulation while the DOL's control of the employment relationship through Congress' power to regulate interstate commerce allowed for such preemption.

[165] Hearings before S. Comm. on Fin., Subcomm. on Private Pension Plans, 93d Cong. 1087 (1973) (remarks of Sen. Javits and Sen. Williams).

[166] Id. at 1094-95.

[167] Id. at 1095.

Having conceded a necessary role for the IRS in areas like eligibility, vesting, and funding, Senators Javits and Williams then faced questions about the problem of dual – and potentially conflicting – jurisdiction in these areas if the DOL also regulated here.[168] This is the question not fully resolved as the parties fought over jurisdiction and reached a compromise that involved duplication, overlap, and conflict.

Yet more complex institutional issues beyond multiple committee jurisdiction were also at play in the decision of legislators to delegate broad discretion to private fiduciaries with weak, fragmented supervisory authority in the executive instead of a powerful superagency. Late 1972, the period prior to the passage of ERISA, was a time where congressional power was at an all-time low. After Congress adjourned, President Nixon impounded funds to reduce government expenditures – refusing to spend the money. On December 18, 1972, Nixon ordered bombing in North Vietnam without consulting Congress (Wooten 2004, 191). Without the fall of Nixon to the Watergate scandal and the decline in power and prestige of the presidency, Congress may not have had the ability to finally pass pension legislation that delegated authority to private fiduciaries instead of the executive branch. Negotiations over the final bill might have taken a different turn.

[168] Id. at 1099.

The Inability of the Bureaucracy to Enforce ERISA

The administration and enforcement regime put in place under ERISA divides responsibility between the DOL and the Department of Treasury (mainly the IRS).[169] Pensions historically fell within the purview of the IRS because plans needed to be qualified for favorable tax treatment. They also related to the DOL's mission of worker protection and compensation as pensions are considered deferred wages.

Turf battles within Congress and the bureaucracy resulted in the political compromise of overlapping – and frequently conflicting – jurisdiction (Klimkowsky 1984, 83).[170] Indeed, even while the Conference Committee was resolving the final details of dual administration of ERISA by the DOL and IRS, many doubted that the statute could be effectively enforced in the planned manner. As staff members noted, "While recognizing the staffs have made a valiant effort to resolve the jurisdictional problem, some staff members believe the proposed solution falls short of eliminating the inevitable complexities, costs and inequities which will result from dual jurisdiction and enforcement."[171]

[169] A newly created agency – the Pension Benefit Guaranty Corporation – also administered the statute's insurance program, but its involvement is not relevant to this discussion. See Langbein, Stabile, and Wolk (2006, 90).

[170] "When President Ford signed ERISA into law on Labor Day 1974, the administrative apparatus charged with implementing the new law reflected the ambiguity concerning the proper jurisdictional sphere for the law and continued congressional rivalry over turf" (Klimkowsky 1984, 83).

[171] Staff Comments Relating to Jurisdictional Matters, undated, Box 128, Folder Pension Reform Leg. House/Senate Conference on HR 2 - 1974, Javits Collection.

After the passage of ERISA, it quickly became clear that dual jurisdiction needed to be sorted out for the agencies to implement ERISA. The impracticalities of the IRS and DOL issuing regulations together slowed the process of implementation (Klimkowsky 1984, 84). By executive order, President Carter issued Reorganization Plan No. 4 of 1978.[172] The IRS gained exclusive control over participation, vesting, and funding (among other areas), while the DOL governs fiduciary management and disclosure and prohibited transactions. The DOL and IRS also share control over decisions regarding whether a plan meets the exclusive benefit rule (Klimkowsky 1984, 95; Langbein, Stabile, and Wolk 2006, 91). This plan completed the transition away from the previous notion that the DOL would have primary control of pension regulation.

Early conflicts within the DOL after ERISA's passage also prevented effective administration and enforcement of fiduciary obligations. DOL leaders could not even agree on an internal structure for pension regulation. For three years and under five different administrators, the agency struggled with whether to house ERISA responsibilities under a new Assistant Secretary or under the existing Labor Management Services Administration that administered the Welfare and Pension Plan Disclosure Act but had other primary responsibilities. After three years, the DOL finally decided upon the Office of Pension Benefit Welfare Programs reporting to the Assistant Secretary for Labor Management Relations – at least for the moment (Klimkowsky 1984, 86-87).

[172] Exec. Order No. 12,108, 44 Fed. Reg. 1065 (Jan. 3, 1979), available at http://www.dol.gov/ebsa/regs/exec_order_no4.html.

Effective administration and enforcement of fiduciary responsibilities at the DOL was also hampered by the complexity of ERISA and the agency's lack of resources. Policy analyst Beverly Klimkowsky (1984, 88) noted in a paper prepared for the Senate Special Committee on Aging on the tenth anniversary of ERISA:

> As one of the most complex laws Congress ever passed, ERISA suffers from having an unclear mandate. Multiple jurisdiction is a major example of congressional indecision being papered over and left to the administrators to sort out. Some of ERISA's provisions (e.g., paperwork) are too specific, leaving administrators with little flexibility. Many other provisions were so vague that over 100 regulations needed to be issued.

The DOL lacked financial and manpower resources initially to administer this complex statute. The IRS had many pension experts on staff already because of its previous work in the area, but the DOL lacked expertise and experienced higher turnover (Klimkowsky 1984, 88-89, 93).

Although the Reorganization Plan allocated tasks more efficiently between the IRS and DOL and aided administration greatly, enforcement was still an issue of concern.[173] The IRS and DOL maintained control over enforcement in their respective areas of ERISA, making coordinated pension policy difficult to achieve (Klimkowsky 1984, 96). The Secretary Labor has the power to file or intervene (in most circumstances) in civil lawsuits related to its areas of administration and also assess civil penalties.[174] The Secretary of Labor can also investigate conduct that may constitute a violation of ERISA's title I by reviewing books and records and interviewing the relevant people where "reasonable cause" to believe there has been a violation exists or where

[173] See Klimkowsky (1984, 84, 98), stating, "ERISA enforcement constitutes the weakest link in implementation . . ."

[174] ERISA § 502, 29 U.S.C. § 1132; see Lewis, Rumeld, and LeBeau (2012, § 3-14).

the plan gives consent.[175] No plan, however, can be forced to provide its books and records to the DOL more than once in a 12 month period unless such "reasonable cause" to believe there has been a violation exists.[176] The DOL engaged in few enforcement activities until a lengthy and involved matter with the Central State Teamsters Plan, and the DOL's problems with internal organization left overall enforcement inadequate.

After a critical report by the General Accounting Office ("GAO") in 1977, the DOL announced that it would use the significant case theory to guide its enforcement efforts – requiring regional audits of large pension plans. The significant case theory was controversial, however. What constituted a large plan in one region might not in another. In addition, the strategy left the many participants in small plans unprotected. The Solicitor's Office was also overwhelmed and unable to respond to all proposed cases. When Reagan took office, however, personnel at the DOL changed and the significant case strategy ended. Other strategies of emphasizing criminal cases and more centralized enforcement were attempted (Klimkowsky 1984, 97).

Since that time, reports on DOL enforcement of ERISA's fiduciary provisions have routinely been critical. The GAO's January 1989 report to the House Ways and Means Committee's Subcommittee on Oversight found that the DOL's enforcement efforts had a limited reach.[177] By

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[175] ERISA § 504(a), 29 U.S.C. § 1134(a); see Lewis, Rumeld, and LeBeau (2012, § 3-13).

[176] ERISA § 504(b), 29 U.S.C. § 1134(b); see Lewis, Rumeld, and LeBeau (2012, § 3-13).

[177] U.S. Gen. Accounting Office, GAO/HRD-89-32, Pension Plans: Labor and IRS Enforcement of the Employee Retirement Income Security Act 3-4 (1989). During the period examined, fiscal years 1985 to 1987, the DOL only closed roughly 1,300 pension plan investigations per year, though in 1987 there were an estimated 870,350 private

1994, the GAO noted improvements made by the DOL in enforcement but still had substantial recommendations for change in its report entitled *Pension Plans: Strong Labor ERISA Enforcement Should Better Protect Plan Participants*.[178] Of the 117 cases referred to the DOL Solicitor's Office for civil litigation or to the Department of Justice for criminal litigation, only 38 lawsuits were filed.[179]

Recent problems found with DOL ERISA enforcement include a lack of plan audits and resources for proper enforcement. After once again noting significant problems in 2002, the GAO (which now stood for the Government Accountability Office) issued another report in January 2007 finding protection of participants still inadequate.[180] The DOL still did not have an accurate picture of ERISA noncompliance and therefore could not properly target its enforcement efforts. The DOL did not conduct routine plan audits or risk assessments like other agencies and was focused on problems identified by plan sponsors, participants, or other agencies. Finally, although it had recruited more skilled personnel needed to administer the

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pension plans. Only one in four plans investigated were cited for ERISA violations, and the number was one in five for the first eight months of fiscal year 1988. The DOL found 574 fiduciary violations in 1987. Id.

[178] U.S. Gen. Accounting Office, GAO/HEHS-94-157, Pension Plans: Stronger Labor ERISA Enforcement Should Better Protect Plan Participants (1994). Area office enforcement staff had grown from 266 to 365 from 1986 to 1993. By program year 1993, the number of investigations closed was 2,998 (although 1,480 of these cases had been opened to test computer targeting programs that were still in the exploration stage). While the DOL managed to recover $183 million for plans and "impact" 72,199 plans and 21 million participants in 1993 with its focus on "significant issue" cases, only 303 cases resulted in a monetary recovery, only 125 had fiduciary results (fiduciaries were removed, fiduciaries were forced to diversify plan investments or discontinue a particular investment, or other administrative practices were altered) and only 187 cases had nonfiduciary results (changes were made to comply with reporting and disclosure or bonding requirements). Id. at 5-6.

[179] Id. at 5-6. The report recommended reviewing the amount of resources focused on the "significant issue" strategy, focusing more on targeted computer programs, and increasing the use of penalties. Id. at 14-15.

[180] U.S. Gov't Accountability Office, GAO-07-22, Employee Benefits Security Administration: Enforcement Improvements Made but Additional Actions Could Further Enhance Pension Plan Oversight (2007).

complex statute, the DOL had a high attrition rate for related personnel.[181] By fiscal year 2005, the DOL's Office of the Solicitor litigated only 178 of the 258 ERISA civil cases referred by the DOL's Employee Benefit Security Administration ("EBSA").[182] As the report summarized:

> EBSA is a relatively small agency facing the daunting challenge of safeguarding the retirement assets of millions of American workers, retirees, and their families. . . . EBSA's ability to protect plan participants against the misuse of pension plan assets is still limited, because its enforcement approach is not as comprehensive as those of other federal agencies, and generally focuses only on what it derives from its investigations.[183]

The importance of enforcing ERISA's fiduciary provisions is clear from ERISA's legislative history. Yet Congress has never provided funding or authorization sufficient for the DOL to audit plans on a regular basis as the SEC and banking agencies do to enforce regulations in their sectors (Klimkowsky and Lanoff 1985, 96-97). Given the current economic climate and push for deficit reduction, it is highly unlikely that the executive agencies will soon be given the resources necessary for proper enforcement.[184]

Data from EBSA show how anemic current levels of enforcement are within the bureaucracy. The data relate only to penalties assessed from 2000 to present in closed cases where pension

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[181] Id. at 2-4. The DOL's Employee Benefits Security Administration ("EBSA") had a ratio of personnel to regulated plans/entities of 1:8,000 as compared to 1:3,000 for the IRS and 1:9 for the SEC. Id. at 10.

[182] Formerly called the Pension and Welfare Benefits Administration. Id. at 11.

[183] Id. at 28.

[184] See Getman (1994, 476), arguing, "Complex statutes are inevitably difficult to enforce. Enforcement of a statute of this magnitude and complexity requires a major bureaucracy. The need for this type of bureaucracy, however, is arising at a time when public opinion is strongly opposed to governmental expansion. . . . It would be difficult to reconcile today's hostility toward increasing bureaucracy with the need for the expanded bureaucracy required to enforce ERISA. Enforcing the statute selectively would create more complexity, confusion, and political resentment."

plan responses to ERISA's annual form 5500 filing requirement were late, insufficient, or nonexistent.[185] In 2011, there were 683,647 pension plans according to 5500 filings (including single employer and multiemployer, defined benefit and defined contribution).[186] Yet there were only 401 penalties assessed for filing deficiencies with respect to the annual form 5500. (See Table 4.1.) As Table 4.1 at the end of this chapter indicates, there are few actions overall even to enforce the basic filing requirement.

And when penalties are assessed for filing deficiencies, they are the financial equivalent of a slap on the wrist. In 2011, pension plan assets totaled over $6.3 trillion, but 88% of penalties assessed were below $50,000.[187] (See Table 4.1.)

Years after the passage of ERISA, there are still calls for a single agency to administer the statute and its amendments. As one article noted, "A review of fiduciary enforcement, in particular, indicates that the Department of Labor cannot enforce ERISA; the IRS does not enforce ERISA; and coordination in this area does not function well" (Klimkowsky and Lanoff 1985, 90).[188] Its

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[185] "The dataset consists of closed cases that resulted in penalty assessments by EBSA since 2000. This data provides information on EBSA's enforcement programs to enforce ERISA's Form 5500 Annual Return/Report filing requirement focusing on deficient filers, late filers and non-filers." U.S. Department of Labor Data Enforcement. Data Catalog. Available at http://ogesdw.dol.gov/views/data_summary.php.

[186] Private Pension Plan Bulletin Historical Tables and Graphs. U.S. Department of Labor Employee Benefits Security Administration. June 2013. Table E1. Number of Pension Plans *by type of plan, 1975-2011*. Available at http://www.dol.gov/ebsa/pdf/historicaltables.pdf.

[187] Id.

[188] Klimkowsky and Lanoff (1985, 90) blame problems with enforcing the statute on Congress for setting an "impossible task" of joint administration for the DOL and IRS.

authors argued that the only hope for proper enforcement of the statute and coordinated policymaking is a single agency with jurisdiction over private pension regulation (91, 94).[189]

The current insufficient bureaucratic enforcement of ERISA has left private litigation as the main enforcement mechanism. Policy analyst Beverly Klimkowsky (1984, 84) wrote on the tenth anniversary of ERISA that "ERISA implementation has not reached the mature stage of implementation in which the administering agencies act as powerful players in the policy process."[190] The same remains true today, and the courts have picked up the policymaking mantle.

Because of the lack of procedural safeguards and the conflicted nature of ERISA fiduciaries, the courts are not supposed to be policymakers when deciding claims under ERISA but instead merely "interpreters of contractual entitlements."[191] As discussed in Chapter 5, however, they

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[189] Klimkowsky acknowledges the difficulties of bureaucratic consolidation under ERISA while still arguing in favor. On the one hand, Klimkowsky and Lanoff (1985, 91, 94) write, "As ERISA was written, DOL and the IRS shared responsibilities jointly, as opposed to having divided responsibilities, necessitating intensive coordination between the two agencies if the law was to be implemented. Because political compromise rather than ease of administration dictated the administrative structure of ERISA, severe management problems surfaced as soon as managers attempted to implement the new law." But Klimskowky (1984, 101) notes the problems facing the idea of consolidation after ERISA's enactment (many of which helped doom the idea initially):

> The structure and leadership of a new agency would be open to much debate and possible disagreement which could kill the idea entirely. It might not be possible to wrestle pensions away from the IRS entirely, since the issue remains very much a tax issue. Also, it is critical that interest be aroused on the Hill before anything can be accomplished. Few if any legislators have appeared to accept the mantle of leadership from ERISA's founding fathers.

[190] Klimkowsky notes that pension policy was largely being influenced by groups that do not regard "the fulfillment of the promise for a private pension as [their] sole or primary concern" (1984, 84).

[191] *Van Boxel v. The Journal Co. Employees' Pension Trust*, 836 F.2d 1048, 1050 (7th Cir. 1987).

have in practice made pension policy to an extent not predicted by Congress at the time of

ERISA's enactment.

TABLE 4.1[192]

Closed cases that resulted in penalty assessments under EBSA's programs to enforce ERISA's Form 5500 Annual Return/Report filing requirement.

	Number of Cases with Penalty				
Year Case Closed	$0-10,000	$10,001-50,000	$50,001-100,000	Over $100,000	Total
2000	91	26	4	5	126
2001	127	85	15	3	230
2002	57	37	4	12	110
2003	73	18	5	7	103
2004	202	58	27	11	298
2005	218	93	45	15	371
2006	259	164	89	14	526
2007	303	123	103	6	535
2008	203	98	48	5	354
2009	284	138	62	6	490
2010	146	90	19	0	255
2011	221	173	5	2	401
2012	198	164	3	4	369
2013	133	88	8	3	232
Total	2515	1355	437	93	

[192] "The dataset consists of closed cases that resulted in penalty assessments by EBSA since 2000. This data provides information on EBSA's enforcement programs to enforce ERISA's Form 5500 Annual Return/Report filing requirement focusing on deficient filers, late filers and non-filers." U.S. Department of Labor Data Enforcement. Data Catalog. Available at http://ogesdw.dol.gov/views/data_summary.php.

CHAPTER 5

THE FAILURE OF LEGAL ACCOUNTABILITY UNDER ERISA

ERISA provides for civil action by both plan participants and beneficiaries in addition to the Secretary of Labor. The statute created a private right of action as follows:

> A civil action may be brought – (1) by a participant or beneficiary – . . . (B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan. . . . (3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this subchapter or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provisions of this subchapter or the terms of the plan.[193]

For the 12-month period ending March 31, 2013, there were 7,946 ERISA cases filed in the federal district courts according to a report from the Administrative Office of the U.S. Courts on the composition of the courts' caseload. In only 110 of those cases was the federal government the plaintiff.[194]

When creating private litigation remedies, Congress is aware that the courts may not always enforce the legislation as expected or desired. "It is in the nature of statutory interpretation that the interpreter, whether judicial or administrative, will frequently be called upon to make policy" (Farhang 2008, 821-23). In the absence of strong bureaucratic enforcement of ERISA, however, the judiciary has become the central pension policymaking institution in the United States.

[193] ERISA § 502(a), 29 U.S.C. § 1132(a).

[194] Federal Judicial Caseload Statistics. Caseload Statistics 2013. Table C-2, Cases Commenced, by Basis of Jurisdiction and Nature of Suit. Available at http://www.uscourts.gov/Statistics/FederalJudicialCaseloadStatistics/caseload-statistics-2013.aspx.

Many legal scholars have argued that the courts have used this position in ways not intended by "ERISA's language, legislative history, or purposes" (Conison 1992, 4-5).

When examining congressional delegation to bureaucratic agents, political scientist Mathew McCubbins (1999, 30) noted conditions under which delegation fails and becomes abdication:

> Principals may lack an effective check because their agent has expertise that the principals do not possess *or* because of conflicting interests among the principals. Where delegation occurs under such conditions, agents may be free to take any action that suits them, regardless of the consequences for the principals. Delegation then becomes abdication.

In the case of pension regulation, Congress delegated authority over the administration of private pensions to fiduciaries. The courts were supposed to supervise that delegation through a private right of action made increasingly important after bureaucratic failings, but they both lack the expertise necessary to control fiduciary administration and have conflicting interests in judicial efficiency. While Congress intended for the courts to fill gaps in the statute and create common law to implement ERISA, many legal scholars argue that federal common law regarding ERISA benefit claims directly contradicts congressional intent (Conison 1992, 7).[195] The result is judicial abdication in the enforcement of ERISA's mission to safeguard benefit promises made to workers and the failure of legal accountability under ERISA.

[195] Conison (1992, 7) also discusses legislative history that suggests Congress preempted state law on benefit claims as too restrictive because state courts "strictly interpret the plan indenture and are reluctant to apply concepts of equitable relief or to disregard technical document wording."

Private Litigation Remedies: "The American Way?"

In correspondence with the author, law professor John Langbein wrote, "I do not accept the implication that had there been a single agency, it would have substituted for the private cause of action. . . . Private causes of action are the American way, our default preference for structuring enforcement."[196] He refers to the work of legal historian John Witt (2004), who traces the "experimentation in accident law" that resulted in our workers' compensation system. Witt argues that "powerful traditions in American law limit the ability of our legal institutions to develop innovative solutions to new problems" (209). One of the traditions he cites is the "deep-rooted historic tradition that everyone should have his own day in court" (209).

And yet Witt's tale of accident law is precisely one in which, at a critical juncture, workers gave up their freedom to pursue their own day in court in favor of an administrative remedy to better protect themselves from harm. The parallels between this critical moment for accident law and the development of ERISA are clear. What is not clear is whether this was a moment where experimentation and a solution other than the traditional private litigation remedy could have won out or if the pull of traditions was too strong. This question has implications for the future of private pensions as well. Those who believe that the moment for change in the private pension system has passed need wait only until the issue comes to the forefront again as retirement incomes stagnate or decline.

[196] Email dated August 8, 2013 from Professor John Langbein to the author.

Political scientist Sean Farhang studies the decision by Congress to develop private litigation remedies that effectively call on private individuals to enforce the statute passed through the courts. He shows that the presence of divided government – a Republican president and majority-Democrat Congress – during the passage of ERISA likely influenced Congress' decision to enact a private litigation remedy.[197] Over 90% of litigation enforcing statutes is litigated by a diverse group of private individuals acting in their own interests but also carrying out a larger public service by enforcing the statute for all those affected.[198]

Farhang argues that Congress consciously uses a statute's "private enforcement regime" to regulate in addition to, or instead of, typical regulation by the bureaucracy. Congress can alter the amount of litigation that will be brought under the statute – manipulating burdens of proof, liability standards, and other factors to reach its desired level of enforcement through private litigation (Farhang 2009, 3-4).[199] Using the Civil Rights Act of 1991 as a case study,[200] Farhang

[197] Farhang (2008, 821) finds that divided government, typically measured by a president of one political party in office with a Congress dominated by the other political party, results in increased "incentives to mobilize private litigants." A majority Democratic Congress and interest group lobbying in the area of legislation, conditions associated with the passage of ERISA, are also associated with the inclusion of private litigation remedies in legislation.

[198] Farhang (2008, 822-23) uses the model of rational behavior from the law and economics literature that specifies that a litigant will file a lawsuit whenever her expected monetary value (EV) is positive, where EV is equivalent to the litigant's expected monetary benefit in the event of victory (EB) multiplied by the probability that the litigant wins her case minus the costs to the litigant of bringing her case (EC). In other words, a litigant brings a lawsuit where $EV = EB(p) - EC$, and EV is positive. Congress can alter incentives with tools such as damage caps or multipliers, shifting attorney's fees and court costs to the losing side, and setting the burdens of proof for the plaintiff.

[199] Farhang (2009, 7-8) addresses arguments that the decision to litigate is also based on noneconomic concerns such as a desire to be heard or a wish to avoid conflict. His model also assumes that potential litigants have perfect

argues that Congress attempted to manipulate incentives to bring private litigation to address a problem noted in a study by the Federal Courts Study Committee that "the monetary stakes in [employment discrimination] cases may be so small . . . that, even with the potential to recover attorneys' fees, claimants sometimes find it difficult to litigate in Federal court because they cannot find counsel to take their cases."[201] This is the same quandary that existed for pension plan participants immediately prior to the passage of ERISA.

Although Congress is aware that judges' ideology influences their decisions in these cases, it controls the rules of the litigation game as noted, though courts have control over rule articulation. Regardless of the risks involved when trying to institutionalize the legislative bargain struck, divided government frequently makes the courts a better avenue of enforcement than the bureaucracy when Congress seeks to circumvent a president of the opposing party (825-26).[202]

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information to assess the value of litigation under the statute. He acknowledges that these additional variables may dilute Congress' ability to manipulate the amount of litigation to enforce a statute.

[200] As Farhang (2009, 9-12) notes, the Civil Rights Act of 1991 is an excellent case study on the point of whether and how Congress manipulates the private enforcement regime to enforce a statute through private litigation because it took an existing right and altered its enforcement through the courts in clear rebuke to the Supreme Court's efforts to make it more difficult for plaintiffs to succeed in court.

[201] In the legislative history for the Civil Rights Act of 1991, the House Report spoke of "encouraging citizens to act as private attorneys general," while the Senate report again spoke of the need to provide additional incentives for attorneys to bring discrimination cases. Id. at 12-13.

[202] Indeed, beginning in the 1960s and 1970s, courts began to operate more frequently to "handle a problem unsatisfactorily resolved by another branch of government" and make policy "independent of Congress and the bureaucracy" (Horowitz 1977, 6). As divided government took over and hyperpartisanship increased, it paved the way for judicial policymaking – and not only in areas where Congress and the bureaucracy remained silent.

As Congress has tinkered with incentives for private litigation and viewed plaintiffs as a cohesive group to be manipulated based on Congress' desired behavior for a larger population, the facts and circumstances of each individual plaintiff have taken a lesser role for courts as well.[203] This has allowed judges to focus not on the misery of an individual who has worked hard and been denied some contemplated pension benefit, but instead on the effect that the decision might have on the maintenance of a pension system managed by private employers who are still viewed as bestowing some sort of extra benefit on employees by maintaining a pension plan – the last vestiges of an outdated and overruled turn of the common law.

Pension Lawsuits Prior to ERISA

Prior to ERISA, employees faced many obstacles when challenging the pension decisions of employers in the courts. Consider the testimony of Frank Cummings, Chief of Staff to Senator Javits during the passage of ERISA, before the Senate Finance Committee on June 4, 1973 regarding the problems faced by a participant seeking to litigate against a pension plan.[204]

Cummings started his discussion at the point when a hypothetical participant tells a potential lawyer that "they owe him a pension" or "they are misusing the money in the pension fund." The first of several problems facing the lawyer was to figure out who "they" are – what

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[203] See Horowitz (1977, 7): "The individual litigant, though still necessary, has tended to fade a bit into the background. Courts sometimes take off from the individual cases before them to the more general problem the cases call up, and indeed they may assume—dubiously—that the litigants before them typify the problem."

[204] *Private Pension Plan Reform: Hearings Before the S. Comm. on Fin., Subcomm. on Private Pension Plans, Part II*, 93d Cong. 992-95 (1974) (statement of Frank Cummings).

corporate entity employs the participant, who are the trustees, which bank holds the money, which insurance company (perhaps) funds the plan, and which unions and officers are involved.

The next question is what jurisdiction's law to apply and whether a single court has jurisdiction over all of the relevant parties. The individuals and entities that make up the less than cohesive "they" in question may be located in several different states, and the plan documents may not have a choice of law provision.

The final question is what legal claim the participant will assert and whether participants and their lawyers will have an adequate incentive to litigate. If the lawyer argues misuse of funds by the plan, the recovery will go to the pension fund and not the individual plaintiff. The plaintiff gets nothing except a more well-funded pension fund. If the plaintiff sues to recover his pension, the value of the lawsuit is the net present value of one pension. In either case, the benefit recovered, if any, will likely be too small to motivate most lawyers to tackle the complexities of pension law. Only in the event of a class action lawsuit, which is typically organized and financed by a larger entity (such as a union), does the potential recovery justify the costs and uncertainties of litigation for prospective lawyers.

With great foresight, Cummings concluded:

> In short, private lawsuits, under existing law, do not provide a meaningful remedy for the employee in most pension cases. What is needed is a national law, with a national agency to enforce it,

> which will get this whole matter out of the area of ordinary, garden variety, litigation, which simply does not work.[205]

As Cummings made clear, private litigation remedies did not sufficiently protect employees prior to ERISA.

Pension Promises as Gratuities

Beginning in the late nineteenth century and lasting until the middle of the twentieth century, courts viewed pensions as gratuities (*i.e.*, gifts) to be altered or withdrawn freely by employers.[206] Plan documents for pensions also limited an employer's legal liability to employees, and courts found that offering pensions to employees created no judiciable rights (Heinsz 1972, 282; Stein 1986, 138).[207] For example, in *McNevin v. Solvay Process Co.*,[208] the plaintiff sued to recover $52.54 from a pension fund established by his employer. The court found that the amount credited to his "account" under the plan by his employer was a gift completed only upon "actual payment" and that the employee had no vested right to the money until payment. In the governing documents, the employer had reserved the right to determine whether its employees were entitled to the "gift", and the court refused to review that decision:

[205] Id. at 995; see id. at 847 ("You can't sue for a pension today. Even if the plan owes it to you, you can't sue unless someone is backing you or unless you have a class action. The legal fee for the first day of the lawsuit would exceed the amount of recovery.").

[206] The gratuity theory was followed in cases until the 1950s. See Langbein, Stabile, and Wolk (2006, 134): "Because the plan authorized the employer to revoke promised pension benefits at will, those promises were treated like a promise to make a gift in the future, which is unenforceable until the gift is actually completed. (Notice the similarity to the common law doctrine of employment at will.)"

[207] See Stein (1986, 138), stating that the majority rule for early pension promises was that they were "more akin to charity than to earned wages" and reviewing representative cases and relevant treatises.

[208] 53 N.Y.S. 90 (N.Y. App. Div. 1898), *aff'd mem.*, 80 N.E. 1115 (N.Y. 1901).

> It seems to me that the scheme by which this fund is created is simply a promise on the part of the defendant to give to its employees a certain sum in the future with an absolute reservation that it may at any time determine not to complete the gift, and if it does so determine, an employee has no right of action to recover the sum standing to his credit on the books of the pension fund.[209]

Courts that denied participants their pensions emphasized the voluntary, non-contributory (*i.e.*, entirely employer funded) nature of the plans.[210] The gratuitous nature of these plans and the reservations of the employer's right to amend or cancel the terms at any time meant that employees' and retirees' pension benefits never vested.[211] Even in cases where the employer and the court acknowledged that the employer's pension promises benefited the employer through improved employee morale and increased tenure based on the promise of a pension, courts

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[209] Id. at 8. See, *e.g.*, *Menke v. Thompson*, 140 F.2d 786, 790-91 (8th Cir. 1944) ("The company was within its rights in providing that the pensions awarded under the plan were gratuities. . . . By the rules and regulations promulgated by the company and administered by the Board of Pensions [an entity set up and controller by the employer], the company only obligated itself to pension such employees as the Board of Pensions, in the fair exercise of the power conferred upon it, determined to be eligible to receive the benefits of the plan.); *Fickling v. Pollard*, 179 S.E. 582, 583 (Ga. Ct. App. 1935) (Although the plaintiff argued the existence of an implied contract, the cessation of his disability pension payments was not actionable because the payments "amounted to no more than a gratuitous arrangement by the company for the payment, at its option, of pensions to old employees. . . . [and] was 'expressly' made subject to denial, suspension, or permanent discontinuance by the company at any time.").

[210] See *Neuffer v. Bakery & Confectionery Workers Union*, 307 F.2d 671, 672 (D.C. Cir. 1962) ("Here, the Pension Plan voluntarily established by the appellee Union required no contribution from Neuffer or any other participant, and none was made. The Union could properly prescribe, as it did here, conditions on payment of pension benefits reasonably related to the Union's welfare."); *Hughes v. Encyclopaedia Britannica, Inc.*, 117 N.E.2d 880, 882 (Ill. App. Ct. 1954) ("These provisions say that the defendant is paying the entire cost of the plan; that the payments are voluntary; that no contractual relationship is intended or created between the defendant and its employees."); *Umshler v. Umshler*, 76 N.E.2d 231, 233 (Ill. App. Ct. 1947) ("The uncontroverted evidence shows that the pension plan of defendant railroad company is wholly voluntary. All the benefits are paid out of the corporate treasury. No pension fund is provided, nor were any contributions required of or made by defendant Umshler or any other employee and, so far as the record shows, all the expense of the administration of the plan is borne by defendant railroad company.").

[211] See *Dolan v. Heller Bros. Co.*, 104 A.2d 860, 861 (N.J. Super. Ct. Ch. Div. 1954) ("[I]t seems well settled in other jurisdictions that a pension plan which is purely voluntary on the part of the employer and to which the employee makes no contribution, is not an enforceable contract, but a mere gratuity, in which the employee has no vested right until he begins to receive benefits thereunder."); *Kravitz v. Twentieth Century-Fox Film Corp.*, 160 N.Y.S.2d 716, 719 (N.Y. Sup. Ct. 1957) ("The donor of a gift has the right to fix the terms and the objects of his bounty. The terms of the Retirement Plan give no vested rights to others than those specifically provided for. . . . The most that may be said for plaintiffs is that each enjoyed an inchoate gift. This never ripened into a vested one.").

refused to find that pension promises constituted a binding contract.[212] Some courts even recognized that pension promises were a form of deferred compensation but still denied claims. As the New York Court of Appeals stated when denying former employees access to funds set aside in a retirement and profit sharing plan:

> There were some references in the testimony that a portion of the funds would otherwise have been distributed as bonuses, and in that sense the members were contributors. However, bonuses were gratuities which might or might not be distributed at the pleasure of the Board of Directors of the Company. It cannot be gainsaid, we think, that the benefits conferred on the Members of the Plan were tantamount to gifts, and the Company had the right, as the donor, to fix the terms and limitations of the gifts.[213]

As a federal appeals court noted in denying pension benefits: "No statute then in force required of the company the assumption of the burden which it took upon itself in providing for pensions for its employees. It therefore had the right . . . to condition its bounty in such manner as it saw fit."[214]

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[212] See *Hughes*, 117 N.E.2d at 883 ("Defendant concedes that an employer receives a benefit from instituting a pension plan by way of increased stability of employment and in the greater security and contentment of its employees and that it is largely for this reason it instituted and presently maintains such a program. It does not follow, however, that where a pension plan is placed into effect the employee thereby acquires a vested right to have the plan kept in effect.").

[213] *Fernekes v. CMP Indus., Inc.*, 195 N.E.2d 884, 887 (N.Y. 1963). But *cf. Schofield v. Zion's Coop. Mercantile Inst.*, 39 P.2d 342 (Utah 1934). In *Schofield*, the court found that a contract did exist providing the retirees with a vested pension that could not be reduced. The terms of the pension plan stated that the purpose of the plan was to "encourage long and faithful service" and that after such service an employee would be entitled to a pension in the amount stated in the plan. Id. at 344-45. The court held that this the pension acted as an inducement for the plaintiffs to continue their employment, and after their long service and the determination that they had met the terms required for the pension, no modification of the contract was possible by the employer. Id. at 345. The lack of equivocation and plan language carefully stating that the pension promised was a gift that could be modified or withdrawn at any point distinguishes this case from the bulk of pension claims during this era, however.

[214] *Menke*, 140 F.2d at 790.

While pension law subsequently advanced beyond viewing pension promises as gratuities, the voluntary nature of our private pension system remains.

Pension Promises as Contracts

Although in the decades prior to ERISA's enactment most courts ruled that pension rights were contractual and not gratuities,[215] "employees fare[d] no better under this theory than they did under the gratuity theory" (Heinsz 1972, 283-84).[216] Most judges believed that they had no choice but to strictly construe the terms of pension plans that were drafted by and to favor employers.[217]

Neuffer v. Bakery & Confectionery Workers Union,[218] highlights the evolution of pension jurisprudence from viewing pensions as gratuities to contracts. The district court initially approved the defendant union's actions forfeiting a retiree's pension and terminating payments.

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[215] See *Heinz v. Nat'l Bank of Commerce,* 237 F. 942, 949-50 (8th Cir. 1916), for an early example of the recognition of contractual rights to a pension.

[216] See Stein (1986, 138-39), finding trend in case law towards recognition of unilateral contract rights through pension plans by the 1930s and stating that "some courts, faced with the argument that employees who were promised pensions just might have given some consideration—namely, their labor—found more satisfactory legal doctrines to deny many dissatisfied employees their pensions *most* of the time." One dissenting judge protested a circuit court decision upholding an employer's termination of a retiree's pension, writing, "I am unwilling to endorse the employer's brutal treatment of a pensioner who served it for most of his mature life. We open ourselves to the charge that judicial concern for individual rights in this jurisdiction is confined arbitrarily and capriciously to criminal cases." *Neuffer v. Bakery & Confectionery Workers Union*, 307 F.2d 671, 675 (D.C. Cir. 1962) (Burger, dissenting).

[217] See *Wallace v. Northern OhioTraction & Light Co.*, 13 N.E. 2d 139, 143 (Ohio Ct. App. 1937) ("To hold otherwise, is to become involved in a discussion of purely ethical questions with no pertinent rule of law or related principle in equity to form a standard for our conclusion.").

[218] 193 F. Supp. 699 (D.D.C. 1961), *aff'd*, 307 F.2d 671 (D.C. Cir. 1962).

It held that there were "none of the essential elements of a contract" and it would not construe the terms of a "voluntary, non-contributory plan strictly against an employer." Since the employer reserved its rights to modify the plan and to determine eligibility and forfeiture under the terms of the plan, the union was within its rights to suspend payments.[219] The appellate court, while still siding with the employer, found that the terms of the pension plan did create a valid contract between the employee and the union. Any vested rights created by the plan were subject to reasonable conditions placed on the continued receipt of a pension, however, and the court "nevertheless enforces reasonable contracts."[220] The strongly worded dissent, on the other hand, affirms that a pension is now considered a contractual form of deferred compensation and not a gratuity but disagrees with the result reached by the majority. Since the employer drafted the contract, it should have been strictly construed against the union.[221]

Under the "unilateral contract theory", a pension contract was created when the employer offered a pension plan and the employee accepted employment or remained on the job based in part on that pension – relying on the promise of a future pension and presumably accepting some decrease in current wages.[222] To qualify for a pension, the employee had to satisfy the terms set

[219] Id. at 700.

[220] *Neuffer v. Bakery & Confectionery Workers Union*, 307 F.2d 671, 673 (D.C. Cir. 1962).

[221] Id. at 674-75.

[222] See Heinsz (1972, 283-85); Stein (1986, 138-40); see also *In re Schenectady R.R.*, 93 F. Supp. 67, 70 (N.D.N.Y. 1950) (holding that promised pensions were a part of the consideration for employees' labor under the collective bargaining agreement and that, like wages, vacation pay, and other benefits, pensions were "a part of the reward for his effort"); *Hunter v. Sparling*, 197 P.2d 807, 814 (Cal. Ct. App. 1948) ("[W]here the employer has a pension plan and the employee knows of it, continued employment constitutes consideration for the promise to pay the pension. The pension is considered to be deferred compensation."); *Gearns v. Commercial Cable Co.*, 32 N.Y.S.2d 856, 858, *aff'd*, 56 N.E.2d 67 (N.Y. Civ. Ct. 1947) (denying plaintiff's pension claims on other grounds but confirming that "it

forth in the pension plan's governing documents – none of which he had any say in. Then, he had to hope he was not laid off from his job and that the employer remained financially sound.[223]

In *Texas N. O. R. Co. v. Jones*,[224] for example, a Texas appellate court found that the defendant employer could not terminate the plaintiff's pension because he had been committed to a state-run mental facility. Quoting the trial court decision, the appellate court found:

> That the offer made under said pension system was an inducement to the company's employees to remain in its service and render to it the long continued faithful service, giving their entire time to its service, as required, in order to reap the benefits offered under said pension system, and that the rendering of the long continued faithful service of its employees as required by it, was a benefit to

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is doubtful if defendant arbitrarily could have refused payment as the plan was not merely a benefaction but a contract supported by plaintiff's consideration of continued services under the plan and his acceptance of other obligations under it."). Compare *Sigman v. Rudolph Wurlitzer Co.*, 11 N.E. 2d 878, 880 (Ohio Ct. App. 1937) ("During these years [the employee] was led to believe that two per cent of his earnings would be paid him when the company considered him more favorably in the position of a pensioner than as an employee receiving a full salary or wage. The appellant has made its election. It has concluded that he has reached the point of industrial old age. . . . He, however, cannot be in good faith and justice denied the alternative held out by the employer as an inducement, for more than a quarter of a century, to continue service with the appellant.") and *Wilson v. Rudolph Wurlitzer Co.*, 194 N.E. 441 (Ohio Ct. App. 1934) (refusing to allow the company to avoid its contractual pension obligation by firing an employee arbitrarily at age 65 because its pension promises were "a daily inducement to continuation of service and to exertion to satisfy"), with *Bos v. U.S. Rubber Co.*, 224 P.2d 386 (Cal. Ct. App. 1958) (rejecting plaintiff's claim that his discharge at age 60 violated his pension contract because he had no right to retire under the plan at age 60 and receive a pension).

[223] See Heinsz (1972, 283), noting that even if an employee was able to "survive the hazards of job changes, layoffs, mergers, or business failures, and . . . meet all of the conditions of the employer's pension plan, the insurance contract or trust indenture, or the collective bargaining agreement, he may still be denied his pension." In *Gallo v. Howard Stores Corp.*, 145 F. Supp. 909 (E. D. Pa.), *aff'd per curiam*, 250 F.2d 37 (3d Cir. 1956), the plaintiff sued to receive early retirement pension benefits after relying on a booklet issued by the company which failed to mention that the employee needed the company's consent to retire early and receive the pension to which he had contributed for years. Setting aside a jury verdict that ruled that the plaintiff's reliance on the booklet was reasonable, the court held that the booklet could not replace the tripartite contract between the employee, the employer, and the insurance company guaranteeing the pension benefits – a contract the plaintiff had never seen. Id. at 912.

[224] 103 S.W. 2d 1043 (Tex. Civ. App. 1937).

> the railroad company, and that the offer and acceptance by performance constituted a mutual consideration.[225]

The court was careful to note, however, that the pension promise only became a "binding contract" *after* the employee had continued his employment with the employer until retirement and officially been awarded a pension.

Finally, in a mistake not likely to be repeated by savvy employers following the case, the company failed to include an unconditional reservation of its right to terminate pension payments at any time in the plan documents, instead only reserving the right to cancel payments due to gross misconduct by the former employee.[226] Thus, many employees who forfeited their pensions still remained unprotected by the contractual framework.

Even if an employee remained with his employer until retirement, an employee could still be denied his pension based on decisions by those administering the pension plan. Employers created boards composed of their executives to administer pension plans, including the power to decide whether an employee qualified for a pension.[227] Their decisions sometimes had harsh consequences for employees.[228] For example, in *Menke v. Thompson*,[229] a federal appellate court

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[225] Id. at 1046.

[226] Id.

[227] Outside of pension plans for unionized employees under collective bargaining agreements (which make up a small percentage of all pension funds today), employees are typically not represented on these boards.

[228] See *Wallace v. Northern OhioTraction & Light Co.*, 13 N.E. 2d 139, 143 (Ohio Ct. App. 1937) (company could abandon its pension plan and any employees or former employees who had not yet qualified for a pension were not entitled to any benefits – no matter how close they were to qualifying for a pension); Heinsz (1972, 283-84) ("For example, boards have been allowed to disqualify employees whom they concluded did not meet physical disability requirements in a pension plan, despite medical evidence to the contrary.").

affirmed the denial of a pension to an employee of the Missouri Pacific Railroad Company from 1886 to 1932. Any person who voluntarily left employment, even for a day, was denied a pension under the terms of the plan, and Menke went on strike in July 1922 and did not return until October 1922.[230] Although the company argued that the pensions were gratuities, the court found that even under the unilateral contract theory, Menke was not entitled to his pension. The terms of the plan gave the Board of Pensions nearly unbridled discretion to interpret (and amend) the rules of the plan and decide eligibility for a pension.[231] The Board's decision was final "'in the absence of fraud or such gross mistakes as imply bad faith or a failure to exercise an honest judgment.' The burden of proof . . . was upon the appellant here, and, to sustain such a showing, the evidence 'must be more than a mere preponderance, it must be overwhelming.'"[232]

Courts occasionally achieved equity in individual cases of hardship through other legal theories while leaving the general practice of deference to employers in place. Courts relied on the quasi-contractual theories of promissory estoppel and unjust enrichment to temper the worst injustices

[229] 140 F.2d 786 (8th Cir. 1944).

[230] Id. at 787-88.

[231] Id. at 790-91 ("[T]he company only obligated itself to pension such employees as the Board of Pensions, in the fair exercise of the power conferred upon it, determined to be eligible to receive the benefits of the plan.").

[232] Id. at 791 (internal citations omitted); see *Dowling v. Texas & N.O.R.R.*, 80 S.W.2d 456 (Tex. Civ. App. 1935) (denying appellant a pension after he worked for his railroad employer for approximately 34 years because his voluntary separation of less than a year in the middle of his employment violated the plan's eligibility terms even though he "never had a copy of the rules and regulations with reference to the pension").

visited upon individual pension claimants. Those theories were, however, applied narrowly and infrequently.[233] Section 90 of the Restatement of the Law of Contracts provides:

> A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.[234]

Even when courts utilized quasi-contractual theories to protect workers' rights, the holdings were limited and did not affect the overwhelming legal bias in favor of employers. In *Lucas v. Seagrave Corp.*,[235] the court used unjust enrichment and quantum meruit to reject a harsh enforcement of the pension contract. *Lucas* involved the purchase by Seagrave of another company's assets and an assumption of its liabilities under a non-contributory pension plan. After consummating that transaction, Seagrave terminated 30 of the 65 employees of the

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[233] Compare *West v. Hunt Foods, Inc.*, 225 P. 2d 978, 982-83 (Cal. Ct. App. 1951) (holding that repeated promises made by management to the plaintiff that confirmed he would receive a pension according to the company's customary policy as he understood it may state a claim for promissory estoppel where they induced him to remain on the job – even though the plaintiff's understanding of the company's policy was incorrect) and *Hunter v. Sparling*, 197 P. 2d 807, 815-16 (Cal. Ct. App. 1948) (finding in plaintiff's favor where he retired and received roughly half of his promised pension because even if a contract had not existed, the gift would be enforceable under the doctrine of promissory estoppel since the plaintiff knew about the pension promise and rejected other offers of employment in reliance on the promise of a future pension), with *Sbrogna v. Worcester Stamped Metal Co.*, 234 N.E.2d 749 (Mass. 1968) (denying claim of unjust enrichment where all of the plaintiffs' previously-purchased retirement annuities were cancelled by the defendant employer when they went on strike after the expiration of their union's collective bargaining agreement with the employer) *and Hughes v. Encyclopaedia Britannica, Inc.*, 117 N.E.2d 880, 883 (Ill. App. Ct. 1954) (holding that the employer's pension plan constituted an unenforceable gratuity and rejecting plaintiff's theory of promissory estoppel because "there is no fraud, no intent to deceive and no detrimental change of position" by the employee).

[234] An example that the Restatement gives of the concept is:

> *A* promises *B* to pay him an annuity during *B*'s life. *B* thereupon resigns a profitable employment, as *A* expected that he might. *B* receives the annuity for some years, in the meantime becoming disqualified from again obtaining good employment. *A*'s promise is binding.

Restatement (Second) of Contracts § 90 (1981).

[235] 277 F. Supp. 338 (D. Minn. 1967).

company it acquired. The plaintiffs (terminated employees) contended that Seagrave terminated them to avoid making future contributions to the pension plan since forfeited pension credits could be used to cover those obligations.[236]

The plaintiffs in *Lucas* alleged that the accrued pension contributions were compensation for services already rendered, and they were therefore entitled to recover the value even if they did not meet the terms of the pension contract. Although the court discussed how participants generally did not have vested pension rights unless they had strictly met the terms of the plan, the court "found no decision which has ruled directly on the assertion of a quasicontractual right of recovery of pension benefits on the basis that such benefits are essentially a form of compensation."[237] Instead, relying on cases about collective bargaining agreements where pensions were held to be a component of wages, the court found that as an employee approaches retirement age, pension accruals "may even overshadow his cash wages as consideration for his services."[238] Although noting that "present decisions apparently give no weight or recognition to the existing and accepted characteristic of pension plans as a mode of employee compensation," the court found theory rooted in quasi-contract for protecting these workers who left employment involuntarily when terminated by an employer allegedly attempting to avoid its obligations while retaining the value of the unpaid services of the workers terminated.[239]

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[236] Id. at 340.

[237] Id. at 343.

[238] Id.

[239] Id. at 344-45.

While the *Lucas* case may seem to be an example of judicial activism at its best, the procedural posture of the case is a motion for summary judgment. Thus, in the end, all the court does is to deny defendant's motion and allow that plaintiffs in such an egregious set of circumstances may have a claim in quasi-contract if they can develop the facts to support their theories – a difficult endeavor.[240] More importantly, the plaintiffs must prove that the employer acted in bad faith by terminating the employees because simply dismissing an employee nearing retirement who had not yet vested in his pension rights would not be actionable under this theory since the employee was found to have assumed such a risk. As the court stated:

> [I]t seems harsh to assert that employees assume knowingly the risk of all contingencies which might prevent their recovery of benefits; as if the plan were a negotiated contract agreed upon through arm's length bargaining. It hardly seems equitable to apply the literal contract language, which may not have been inserted to cover such a situation, to uncritically rule that employees bear the risk of a group termination which may not have been contemplated by the contract or the actuarial expectations upon which the plan is funded. Such a literal enforcement of plan provisions may defeat rather than foster plan purposes. This approach seems particularly unjustifiable where there may be indications of bad faith or where the doctrine of unjust enrichment is invoked.[241]

Thus, even after courts acknowledged that employees had contractual rights with respect to pension promises, few courts were willing to deviate from enforcing strictly contracts written

[240] Id. at 346 ("At this stage of the record it is not clear whether the facts of the instant case justify such a recovery.")

[241] Id.; Coleman and Herlands (1973, 477-78).

and enforced by employers to meet their needs – leaving workers with little recourse.[242] As two law students presciently wrote in a journal article on the eve of ERISA's passage:

> In view of the many possible ways employees can lose their benefits, it would seem logical and desirable as a matter of public policy for the courts to strive to safeguard the rights of pension plan participants. . . . [T]he courts have not attempted to achieve this aim. . . . [T]he courts' strict interpretation of pension plans, the paucity of available legal theories to support recoveries by employees, and the hesitancy of the courts to utilize those few theories that have been accepted, have vitiated the potential of the judiciary to champion workers' rights and institute reform.[243]

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[242] Some advocates for pension reform in the years in the years leading up to the passage of ERISA argued that courts should use a theory of deferred wages to adjudicate pension disputes. The germs of the theory can be seen in the *Lucas* case discussed above but are fundamentally derived from cases holding that pensions are considered wages for the purpose of collective bargaining. See *Inland Steel Co. v. NLRB*, 170 F.2d 247 (7th Cir. 1948), *cert. denied*, 336 U.S. 960 ("While, as the Company has demonstrated, a reasonable argument can be made that the benefits flowing from such a plan are not 'wages,' we think the better and more logical argument is on the other side, and certainly there is, in our opinion, no sound basis for an argument that such a plan is not clearly included in the phrase, 'other conditions of employment.'"); "Consideration for the Employer's Promise of a Voluntary Pension Plan" (102-03). This theory holds that when an employer contributes to a pension plan on an employee's behalf, these contributions are wages withheld and the employee's property. As a result, the employee's right to the funds vests immediately when they are withheld, and he does not forfeit this property even if terminated for cause. Coleman and Herlands (1973, 478-79) (quoting Senator Williams: "Pensions are not gratuities, but earnings saved and deferred to retirement. They represent compensation which the employee would have received in his paycheck had he not belonged to a pension plan."). While many argue that a theory of deferred wages presents itself in the cases under the contractual framework because deferred wages form a basis for finding the consideration necessary for contract formation, this theory takes a leap to immediate vesting not found in the case law.

The theory of deferred wages does have its problems, although it at least respects the importance of pension promises. First, when focusing on the defined benefit plans more prevalent at this time, pension benefits are based on a formula that emphasizes earnings late in a career and years of service – reducing the value of pension benefits accrued for much of an employee's earlier service and stacking the deck for work in later years. Second, the goal of private pensions is to help workers maintain quality of life during retirement. Treating pension accruals as wages may result in a feeling that employees should have the right to spend the money now instead of engaging in the always difficult process of delayed gratification. Pension portability would help solve the temptation to treat deferred wages as current wages, however. Id. at 467, 479.

[243] Id. at 465, 474.

Conflating Delegation to Private Actors with Delegation to Bureaucratic Actors

The analogy of private fiduciaries to agency bureaucrats by federal courts reviewing the decisions of fiduciaries under ERISA demonstrates the blurring of the line between delegation to government officials and delegation to private actors.[244] The "vast majority of ERISA cases are simple benefit claim disputes in which a federal judge is reviewing the decision of a plan fiduciary."[245] Under ERISA, making determinations of a participant or beneficiary's benefits is a fiduciary function because "a person is a fiduciary with respect to the plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets."[246] The courts are authorized to review such determinations because ERISA provides that a participant or beneficiary may sue "to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan."[247] Most pension participants or beneficiaries therefore seek the assistance of the courts to resolve benefit claims and are mainly concerned about fiduciary decisions that deny them all or part of the benefits to which they believe they are entitled. Because of this point, I

[244] See Langbein (2007, 1331-33) for a discussion of this analogy and a review of key cases.

[245] Langbein, Stabile, and Wolk (2006, 649).

[246] ERISA § 3(21)(A)(iii), 29 U.S.C. § 1002(21)(A)(iii).

[247] ERISA § 502(a)(1)(B), 29 U.S.C. § 1132(a)(1)(B).

will focus on how the courts have abdicated their role to supervise fiduciaries in deciding benefit claims, although the same can be said of many other ERISA claims decided by the courts.[248]

In the landmark case of *Firestone Tire & Rubber Co. v. Bruch*,[249] the Supreme Court ruled that the standard of review for courts reviewing an ERISA fiduciary's administrative decision is *de novo*, meaning that the court should review all evidence without giving any deference to the fiduciary's decision. However, the Court then created an enormous legal loophole that ERISA fiduciaries drove right through by holding that if the plan documents reserved the fiduciary's right to exercise its discretion to determine benefit claims, then the fiduciary's decision would be reviewed under the deferential "arbitrary and capricious" standard. This standard provides that unless the fiduciary's decision was clearly arbitrary and capricious, then the court cannot overturn the original decision – even if the judge believes that another decision is proper. *Bruch* permits the exception to eat the rule since nearly all plans now contain reservations of rights that lead to the more lax standard of review. This arbitrary and capricious standard grants the same deference to ERISA fiduciaries as to decision makers in executive agencies.[250]

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[248] Law Professor Jay Conison (1992, 32-33) notes the importance of ERISA benefit claims and calls them the "bottom-line" of ERISA. In his view, benefit claims are first in ERISA's hierarchy because "[u]nder ERISA, there is nothing else to protect." Vesting, accrual, and funding standards, as well as remedial provisions for fiduciary breaches are all designed solely to ensure that participants and beneficiaries receive the benefits to which they are entitled.

[249] 489 U.S. 101 (1989).

[250] Discussing the cases prior to *Bruch* that mandated an arbitrary and capricious standard of review, Conison (1992, 48) writes that "courts in ERISA cases appreciated the irony of applying an approach whose main effect was to facilitate defeat of benefit expectations. Because the approach was perceived as well established, however, courts were reluctant to make any substantial changes." He then systematically undermines the Court's attempt to justify deferential review through assumptions that benefit claims are a form of judicial review and that trust law governs such claims. The focus, he argues, should instead be on whether benefit claims are decided correctly (51-60). See

Some courts have compared ERISA fiduciaries to executive branch administrators without fully acknowledging the implications of such an analogy. Judge Easterbrook, for example, compared administrators at a company that manages a large portion of disability benefit plans covered by ERISA (which applies to most disability and health benefit plans in addition to pension plans) to administrative law judges at the Social Security Administration who determine eligibility for Social Security disability benefits.[251] In considering whether to apply the arbitrary and capricious standard of review to UNUM Life Insurance Company in light of its interest in keeping costs down, Easterbrook noted that each benefit claim has little impact on a large company's balance sheet, its employees do not necessarily share its self-interest, and its clients want to maintain good relationships with their employees and would not want benefit claims summarily denied.[252] Adding to these factors that UNUM passes along the costs of benefit claims to employers (though imperfectly) through experience rating (*i.e.*, increased employer costs to reimburse third parties administering benefit plans for retrospective benefit payments), Easterbrook concluded, "Thus we have no reason to think that the actual decision makers at

also Bogan (2009, 147), arguing that contract law and not trust law should govern ERISA benefit claims, making summary deferential judicial proceedings inappropriate.

[251] See *Perlman v. Swiss Bank Comprehensive Disability Prot. Plan*, 195 F.3d 975, 978 (7th Cir. 1999) ("[W]e have held that courts may treat welfare benefit plans just like administrative law judges implementing the Social Security disability-benefits program.") (citations omitted); Langbein (2007b, 1330-33).

[252] See *Perlman*, 195 F.3d at 981 ("We have no reason to think that UNUM's benefits staff is any more 'partial' against applicants than are federal judges deciding income-tax cases.").

UNUM approached their task any differently than do the decision makers at the Social Security Administration, and ordinarily deferential review is the order of the day."[253]

As Judge Diane Wood noted in her dissent, however, the analogy between decision making by ERISA fiduciaries and that of the Social Security Administration is improper because of a lack of safeguards to protect those whose benefits are in question. She argued:

> Most importantly, the SSA is a public agency, whose decisions are subject to the strictures of the Administrative Procedure Act, while ERISA plan administrators are private sector actors subject to regulation under the ERISA statute. A host of federal constitutional rights and statutory rights combine to assure procedural regularity in the case of public agencies that are not available to those who attack private action.[254]

The absence of these procedural safeguards for ERISA fiduciaries deciding benefit claims makes the analogy of ERISA fiduciaries to agency decision makers inappropriate.[255]

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[253] Id.; see *Berry v. Ciba-Geigy Corp.*, 761 F.2d 1003, 1006 (4th Cir. 1985) ("While the [arbitrary and capricious] standard is perhaps more commonly associated with appellate court review of administrative findings, deference is likewise due when a district court reviews the action of a private plan trustee. Here, as in other contexts, the standard exists to ensure that administrative responsibility rests with those whose experience is daily and continual, not with judges whose exposure is episodic and occasional."). For an argument that Judge Easterbrook inappropriately combines "rulemaking" and "administrative adjudication" under a category of judicial deference to agencies that he terms "delegation", see Bogan (2004, 21). Bogan argues that because Congress did not delegate the adjudicative function under ERISA to any executive agency, the function belongs with the federal courts and not private fiduciaries.

[254] See *Perlman v. Swiss Bank Comprehensive Disability Prot. Plan*, 195 F.3d 975, 985 (7th Cir. 1999) (Wood, D., dissenting).

[255] *Herzberger v. Standard Ins. Co.*, 205 F.3d 327, 332 (7th Cir. 2000) ("The Social Security Administration is a public agency that denies benefits only after giving the applicant an opportunity for a full adjudicative hearing before a judicial officer, the administrative law judge. The procedural safeguards thus accorded, designed to assure a full and fair hearing, are missing from determinations by plan administrators."); DeBofsky (2004, 738-43); Langbein (2003, 1332-33).

ERISA's required claims procedures, discussed further below, are insufficient in several ways when compared with the procedural safeguards available under the Administrative Procedure Act ("APA") and to Social Security claimants, for example. Within the Social Security Administration, an Administrative Law Judge presides over an administrative trial where the claimant can present evidence and subpoena and cross-examine witnesses. When federal courts hear an appeal, the claimant has already had an opportunity to be heard in the trial.[256] Yet courts use the same arbitrary and capricious standard to review the ERISA benefit claims even though participants have not been heard by a neutral decision maker, been permitted discovery or had the chance to cross-examine witnesses at trial.[257]

Nor do ERISA fiduciaries necessarily have the expertise that agency administrators possess to justify greater deference. Fiduciaries, particularly executives of the employer appointed to help administer the plans and contain costs, frequently lack basic ERISA knowledge or legal or accounting training to prepare them for their duties. They may have no knowledge of legal rules of evidence or other procedures to make sure they have investigated benefit claims sufficiently (DeBofsky 2004, 739).

Under the APA, agency decisions made without the hallmarks of substantive or procedural due process are subject to *de novo* review by courts (DeBofsky 2004, 739-40). Yet decisions by

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[256] Bogan (2004, 26-27); DeBofsky (2004, 738).

[257] Bogan, (2004, 28); DeBofsky (2004, 738-39) ("Although the ERISA claim regulations provide many of these guarantees, the most crucial protections are denied ERISA claimants. . . . Such claims are not presented to an unbiased tribunal; and claimants lack any opportunity to challenge adverse evidence through cross-examination.").

ERISA fiduciaries that lack such safeguards receive the same deferential arbitrary and capricious standard of review.

Other federal courts have also cautioned against the analogy between ERISA fiduciaries and executive agencies because of the conflict of interest that fiduciaries face between acting for the exclusive benefit of participants and to preserve the assets of employers funding pension plans or third parties insuring ERISA welfare plans. In *Bruch*, the Court acknowledged that "if a benefit plan gives discretion to an administrator or fiduciary who is operating under a conflict of interest, that conflict must be weighed as a "factor[] in determining whether there is an abuse of discretion."[258] Courts have been unsure how exactly conflicts should alter their review of benefit claims, and in *Metropolitan Life Insurance Co. v. Glenn*, the Supreme Court did not clarify its answer substantially.[259] Instead, the Court reiterated that the arbitrary and capricious standard of review applies when an employer or insurer that decides benefit eligibility must also pay approved claims out of its own pocket. As a circuit court wrote regarding the problem of applying administrative law in the ERISA context:

> Use of the administrative agency analogy may, ironically, give too much deference to ERISA fiduciaries. Decisions in the ERISA context involve the interpretation of contractual entitlements; they 'are not discretionary in the sense, familiar from administrative law, of decisions that make policy under a broad grant of delegated powers.' Moreover, the individuals who occupy the position of

[258] *Bruch*, 489 U.S. at 115 (quoting Restatement (Second) of Trusts § 187, cmt. d (1959)).

[259] *Metropolitan Life Ins. Co. v. Glenn*, 554 U.S. 105 (2008) (confirming that courts need to weigh different factors when reviewing benefit claims, and conflict of interest is only one, although it carries more weight "where circumstances suggest a higher likelihood that it affected the benefits decision" and less weight "where the administrator has taken active steps to reduce potential bias and to promote accuracy"); *see* Kennedy (2001); Langbein, Stabile, and Wolk (2006, 665-669).

> ERISA fiduciaries are less well-insulated from outside pressures than are decisionmakers at government agencies.[260]

This conflict of interest is one not typically faced by decision makers at executive agencies.[261]

Because of the lack of procedural safeguards and the conflicted nature of ERISA fiduciaries, they are supposed to me mere "interpreters of contractual entitlements."[262] Continuing to treat fiduciaries as bureaucrats, courts have instead required that participants and beneficiaries first pursue their claims through the ERISA plan's internal grievance procedures (referred to as the exhaustion requirement) prior to seeking review in the federal courts.

Section 503 of ERISA provides:

> In accordance with regulations of the Secretary, every employee benefit plan shall – (1) provide adequate notice in writing to any participant or beneficiary whose claim for benefits under the plan has been denied, setting forth the specific reasons for such denial, written in a manner calculated to be understood by the participant, and (2) afford a reasonable opportunity to any participant whose

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[260] *Brown v. Blue Cross & Blue Shield of Ala., Inc.*, 898 F.2d 1556, 1564 n. 7 (11th Cir. 1990) (internal citations omitted).

[261] When it sponsors a defined benefit pension plan, to take a classic ERISA example, an employer assumes the risk of paying a stated amount to workers and their beneficiaries in the future. If, for example, the stock market underperforms and the money set aside by the employer is insufficient to pay the required pension, the employer will need to contribute more money. If, on the other hand, the employer can find a way to deny a claim for pension benefits, then it will not have to contribute as much to the pension plan. Benefit claims therefore directly affect the employer's finances, and because high-level employees or third parties hired by the employer administer pension plans and owe their employment to the plan sponsor, they have a conflict of interest when deciding benefit claims. See Langbein, Stabile, and Wolk (2006, 652-53) (noting that "because ERISA § 408(c)(3) allows management officers to serve as plan fiduciaries, ERISA all but invites conflicts of interest in plan administration").

[262] *Van Boxel v. The Journal Co. Employees' Pension Trust*, 836 F.2d 1048, 1050 (7th Cir. 1987) (noting that ERISA sought to limit freedom of contract to protect pension participants, and they deserve a fair judicial hearing to determine their rights).

> claim for benefits has been denied for a full and fair review by the appropriate named fiduciary of the decision denying the claim.[263]

The text above does not require that a claimant exhaust the plan's review process prior to seeking review of the benefit determination in the courts. Yet courts have held exhaustion of a plan's internal administrative remedies to be mandatory with very limited exceptions.[264] In effect, the courts have required that claimants petition the very administrator(s) who initially rejected their claims prior to seeking any assistance from the courts.

Courts have relied on ERISA's text and legislative history to justify requiring exhaustion of internal remedies prior to seeking recourse in the courts. In ERISA's requirement that benefit plans have internal claims procedures for participants who want to petition the plan to review its decision to deny benefits, the courts have found that Congress intended them to be used for all benefits claims.[265] Courts relied on Congress' supposed concern with efficient resolution of ERISA claims – favoring efficiency over correcting flawed decisions.[266] According to one

[263] ERISA § 503, 29 U.S.C. § 1133.

[264] DeBofsky (2004, 732); Conison (1992, 21-22); Langbein, Stabile, and Wolk (2006, 754-56).

[265] *Amato v. Bernard*, 618 F.2d 559, 567 (9th Cir. 1980) ("It would certainly be anomalous if the same good reasons that presumably led Congress and the Secretary to require covered plans to provide administrative remedies for aggrieved claimants did not lead the courts to see that those remedies are regularly used.").

[266] *Makar v. Health Care Corp. of Mid-Atlantic*, 872 F.2d 80, 83 (4th Cir. 1989) (internal citations omitted) ("Congress' *apparent* intent in mandating these internal claims procedures was to minimize the number of frivolous ERISA lawsuits; promote the consistent treatment of benefit claims; provide a nonadversarial dispute resolution process; and decrease the cost and time of claims settlement.") (emphasis added); *Taylor v. Bakery and Confectionary Workers*, 455 F. Supp. 816, 820 (E.D.N.C. 1978) (internal citations omitted) ("Tied to these inter-fund claims procedures was Congress' awareness of the potential costs of pension reform, and it sought to 'strike a balance between providing meaningful reform and keeping costs within reasonable limits.' Congress was particularly concerned with outlining a private insurance system that would operate efficiently, thereby increasing its acceptance and institution among American business.").

district court, it is in the best interests of both employers and employees that costs of administering benefit claims be minimized:

> If claimants were allowed to litigate the validity of their claims before a final trustee decision was rendered, the costs of dispute settlement would increase markedly for employers. Employees would also suffer financially because, rather than utilize a simple procedure which allows them to deal directly with their employer, they would have to employ an attorney and bear the costs of adversary litigation in the courts.[267]

The courts even justified the exhaustion requirement as a burden that Congress had placed on fiduciaries to review their actions and efficiently enforce the plan's provisions.[268] "In short, Congress intended plan fiduciaries, not the federal courts, to have primary responsibility for claims processing."[269]

Contrary to the rule adopted by the courts, the legislative history indicates that requiring claims procedures was merely to provide another avenue to address grievances. The House labor bill did not require an internal claims review procedure. While the Senate labor bill did include a version of ERISA Section 503, the bill that went to the conference committee provided for

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[267] *Taylor*, 455 F. Supp. at 820.

[268] *Makar*, 872 F.2d at 83 (internal citations omitted) ("By preventing premature interference with an employee benefit plan's remedial provisions, the exhaustion requirement enables plan fiduciaries to efficiently manage their funds; correct their errors; interpret plan provisions; and assemble a factual record which will assist a court in reviewing the fiduciaries' actions."); *Denton v. First Nat'l Bank*, 765 F.2d 1295, 1303 n.13 (5th Cir. 1985) ("Another important facet of the exhaustion requirement is that it prevents fiduciaries from avoiding their duties under the Plan by insulating all benefit decisions in the protective mantel of federal judicial review. If fiduciaries were to find their decisions more closely supervised by an intervening federal judiciary, it is likely that they would go to court to seek instruction by declaratory relief on questions involving claims for benefits, rather than deciding those questions themselves as Congress intended."); *Amato*, 618 F.2d at 567 ("[I]mplementation of the exhaustion requirement will enhance their ability to expertly and efficiently manage their funds by preventing premature judicial intervention in their decision-making processes.").

[269] *Makar*, 872 F.2d at 83 (4th Cir. 1989) (internal citations omitted).

voluntary arbitration instead. The main concern was protecting participants and giving them easy, cheap ways to recover their benefits. As Senator Williams stated, a participant or beneficiary "would have the right" to know why his or her claims was denied and "would be entitled to a full and fair review." This language focuses on the participant or beneficiary's rights – not the employer's rights. The adoption of an exhaustion requirement actually represented a step backwards from state law pre-ERISA (Conison 1992, 22-25).[270]

"Congress unquestionably intended courts to develop *some* set of rules to govern actions for benefits under section 502(a)(1)(B). But the rules developed must be consistent with the purposes of ERISA. The current law pays little attention to ERISA's central purpose of safeguarding benefit expectations. Indeed, it often seems perversely designed to thwart benefit expectations, for no better reason than judicial force of habit" (Conison 1992, 3).

While Frank Cummings worried about the dollar amounts of pension claims being too small to motivate lawyers to take the cases as necessary to pursue a participant's rights, perhaps he should instead have worried about whether the courts would be willing to review pension cases. As Law Professor Jay Conison (1992, 61) argues, "the main policy argument advanced for deference has been that it reduces judicial caseload," but this was not the concern of ERISA. Courts are hostile to benefit claims because they are fact-intensive and usually involve small value claims, even though there is no evidence that a less deferential standard of review would

[270] "Thus, the legislative history provides no support for the view that a suit for benefits was intended to be the second, appellate stage of a process beginning with the plan claims procedures" (Conison 1992, 22-25).

overwhelm court dockets. Regardless, Congress mandated that courts decide benefit claims, and the judicial thwarting of its role has allowed control over retirement security to flow unhindered to the private sector.

Impact of Delegation on Healthcare

While the legislative history of ERISA focuses on pension reform, ERISA dramatically altered healthcare in the United States with few outside the industry aware of the changes. ERISA did not impose detailed rules for the provision of health benefits by employers other than reporting and disclosure requirements and fiduciary protections. Yet the courts' use of the arbitrary and capricious standard to review benefit claims applied to health plans as well, and ERISA's broad preemption clause effectively allowed employers and health insurance companies to opt in to the generous deference provided by courts to ERISA-covered benefit plans through self-insurance (Wooten 2004, 281).

ERISA's preemption clause allowed employers to avoid state regulation of healthcare and deny benefits to an increasing number of participants. The clause mandates that ERISA "supercede[s] any and all State laws insofar as they may now or hereafter relate to any employee benefit plan" with an exception for any law that "regulates insurance, banking, or securities."[271] The "deemer clause" then prevents the application of these state insurance, banking, and securities laws to employee benefit plans. In the case of health plans, the "deemer clause" provides that an

[271] ERISA § 514(a), (b)(2)(A), 29 U.S.C. § 1144(a), (b)(2)(A).

employee benefit plan will not be "deemed to be an insurance company or other insurer . . . or to be engaged in the business of insurance" for the purpose of state insurance laws.[272]

To take advantage of the pre-emption of state laws and the favorable standard of review for benefit claims, particularly when healthcare costs started to skyrocket in the 1980s, many additional employers began to self-insure. Although at the time of ERISA large health plans had begun to self-insure, the trend now included many smaller plans. The development of utilization review brought employers administering health plans and their third party administrators (often insurance companies) into diagnostic decisions. The plans now frequently had to approve healthcare decisions before the services could be provided – in effect deciding what type of care an employee or relative could receive (Wooten 2004, 281-83).

Self-insurance benefited employers with little risk of significant liability. They purchased "stop-loss" policies to prevent unanticipated liability if benefit payments exceeded estimated costs. And they increasingly denied benefit claims through utilization review, while plan participants faced an uphill battle appealing denials in court. At worst, the plan would have to pay the claim and attorneys' fees after a lawsuit because courts also interpreted ERISA's remedies narrowly (Wooten 2004, 281-83). Scandals over bad faith denials of benefit claims were exposed slowly and called into question the involvement of ERISA fiduciaries in healthcare decisions.[273]

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[272] ERISA § 514(b)(2)(B), 29 U.S.C. § 1144(b)(2)(B).

[273] See Langbein (2007b, 1317-21) discussing scandal over the UNUM/Provident Corporation's long-term policy of denying valid disability benefit claims to increase profits.

Courts downplayed the conflict of interest faced by these fiduciaries deciding benefit claims. They argued that "small" benefit claims did not make an administrator at a company with billions of dollars in annual revenue conflicted. Yet the pattern of denial of small benefit claims added up to significant additional revenue. Courts also found comfort in employers' reputational concerns, arguing that if their health plans unfairly denied benefit claims employees would go elsewhere. Given the opaque process of deciding benefit claims, however, employees had little chance to compare employers based on their administration of health plans. Employers and third party administrators also had significant financial incentives to deny claims that overrode reputational concerns. Finally, courts argued that benefit costs were passed on to employers through experience rating later. In the competitive insurance market, insurance companies needed to absorb much of the unexpected costs, though (Langbein 2007b, 1327-31).

While there is hope that the Affordable Care Act's provisions requiring external review will provide an opportunity to increase the fairness of decisions by administrators of health plans (Goldin 2011), the political pressure applied by employers and insurance companies to contain costs and increase profits will be difficult to resist.

The crisis caused by denying pension benefit claims attracts little attention. Perhaps the decline in defined benefit pensions has ameliorated the effects of these benefit denials. Or maybe the economic recession made salary the primary concern of the workforce. Employees also notoriously discount the value of pension benefits when they are younger. Pensioners may have

to rely on welfare plan participants to finally secure the protections they were promised under ERISA.

The United States is not the only country whose judiciary has failed to adequately protect pension beneficiaries when available tools made it possible. Law Professor Elizabeth Shilton (2011, 83) declared, “For employee pension rights [in Canada], the promise of trust law has proved to be a false one.” Recognizing that courts “share a responsibility with legislatures for distributive outcomes within employment pension plans,” she takes issue with the abdication of Canadian courts in their role as protectors of employee pension rights (84). In the end, Shilton finds that the need to facilitate voluntary pensions overcomes the moral aspect of the fiduciary duties inherent in trust law. “If employers can over-ride the most ‘fundamental’ characteristics of a trust simply by inserting explicit wording, then it is employers, rather than the courts, who will ultimately define the scope and content of trust commitments” (98-99).

Refusing to absolve judges of their responsibility for the turn that pension law has taken in Canada, Shilton notes, “The analysis of the case law in this paper has identified numerous analytic nodes where courts applying the common law have made choices—choices not dictated by ‘the law,’ but by predispositions and values, and the weighing of those policy factors they identify as relevant and important” (112). While acknowledging the need for additional legislation to safeguard employee pension rights and the hesitancy of the legislature to act on this

sensitive issue, Shilton sees an important role for the courts in shifting the common law and finding a stronger role for fiduciary protections (114).

Similarly, I argue here that the failure to create a single, expert bureaucratic agency to supervise Congress' delegation of authority to private fiduciaries has left the courts as the only government institution capable of properly supervising fiduciaries and finally creating a coherent body of pension policy that focuses on protecting workers' expectations. The courts have made choices, as Shilton says, and these choices were not mandated by ERISA but instead based on factors important to the judges and fear of involvement in this unwieldy statute. It is time for the courts to reexamine ERISA's legislative history and focus on its underlying goals. Congress did not mandate a highly deferential standard of review for benefit claims or a restriction on the types of evidence that courts will hear. The courts did that, and they can therefore find a way to better enforce pension promises.

CONCLUSION

The years leading up to the passage of ERISA were a moment when inertia gave way to reform, when a traditional *laissez faire* attitude towards employee benefits yielded to concerns of worker protection. John Witt writes of the passage of workers' compensation laws that "the dialects of free labor gave way to the languages of security and social insurance" (207). The notion of free labor that dominated after the end of slavery and the Civil War gave way because it ignored risk and failed to insure against or shift the costs of such risk away from those least able to bear them (14-16). Similarly, ERISA came to fruition because the risks associated with pension loss – the default, forfeiture, and agency risks discussed above[274] – were too much for workers to bear, and the public took notice. After ERISA, employers systematically shifted those risks back to workers.

Employers avoided default and forfeiture risks by shifting their defined benefit pension plans to defined contribution plans. ERISA's funding requirements forced employers to fund future benefits now instead of making grand promises that it would fund later or renege on as business allowed. This increased the cost and decreased the flexibility of promising generous pensions. Strict vesting standards designed to protect employees from forfeiting pensions if they quit or were fired from employment (the forfeiture risk) meant increased pension costs for employers. Employers were counting on many short-term employees to forfeit their pensions when

[274] As a reminder, employees lost all or a portion of their expected pensions when: (1) plan managers "misuse[d] or [stole] assets" ("agency risk"); (2) the employees quit or were fired from employment ("forfeiture risk"); or (3) an employer failed to properly fund the benefit plan and faced hardship itself ("default risk") (Wooten 2004, 3).

considering the cost of providing long-term employees with guaranteed retirement income for years. When pension costs went up because employers had to maintain a higher level of funding and many employees no longer forfeited their benefits, employers reacted by paying small sums (if any) now into tax-deferred plans with no commitment to continue paying past the termination of employment. Actuarial uncertainties regarding mortality were also eliminated.

My dissertation, however, has focused on how employers shifted the agency risk of poor fiduciary behavior with respect to plan assets back to workers. Although Wooten's discussion of agency risk centers on fiduciary theft and misappropriation of assets for the fiduciary's own benefit, I write here of discretion. As any student of contract law knows, even when relationships are governed by a legal document (in the case of ERISA, the plan document and summary plan description provided to the worker), endless disputes can arise about how to interpret that document. The discretion left to ERISA's fiduciaries and the refusal of either the bureaucracy or the courts to review the fiduciaries' use of that discretion without great deference, has allowed fiduciaries to decide nearly all close calls in their favor (and their employer's favor). This is also an agency risk that ERISA was designed to protect against. If ERISA's fiduciaries can circumvent the statute's goals and risk shifting in this manner, then its system of accountability has failed.

To determine the effectiveness of the political and legal accountability regimes under ERISA designed to supervise the delegation of authority over private pensions to fiduciaries, we need to recall Mashaw's criteria:

> [W]e should be able to specify at least six important things: *who* is liable or accountable to *whom*; *what* they are liable to be called to account for: *through what processes* accountability is to be assured; *by what standards* the putatively accountable behavior is to be judged; and, what the potential *effects* are of finding those standards have been breached.

(Mashaw 2006, 118, quoted in Freeman and Minow 2009, 16). ERISA seeks to hold fiduciaries accountable (while acknowledging that the agents of the employer who serve as fiduciaries are conflicted and need to be closely watched). Yet the statute's answers to the other criteria are less clear.

To whom are ERISA fiduciaries liable? Ultimately, the employees who will receive pension (and other) benefits are supposed to be the masters to whom fiduciaries answer. Yet Congress, influenced also by those employers, is the more powerful party to whom employers answer. The threat of legislation placing additional burdens on employers is a powerful lever that Congress has, while employees under ERISA can only file lawsuits that typically involve small claims and present little threat to the overall well-being of employers. Employers also answer to the IRS and DOL, with whom they have ongoing relationships, and the courts. Given that employers must serve various masters and these institutional parties do not have the same goals as employees and their beneficiaries, it becomes far more difficult to hold fiduciaries accountable.

Also unclear is what fiduciaries are liable to be called to account for. Is it acceptable that fiduciaries use their discretion to decide all cases where the statute or the plan documents are vague or ambiguous in the employer's favor? Courts have decided that it is acceptable for

conflicted decision makers to keep their thumbs on the scale. Only grave abuses of their powers result in a searching judicial review.

After the tangle that Congress wove under ERISA, the courts have assured that the main processes through which fiduciaries are held accountable are lawsuits filed by employees or beneficiaries against the pension plan and its fiduciaries, and they determined the standards by which fiduciaries will be judged. Continuing their tradition of deference to employers when deciding pension claims, the courts moved actively to shift pension policy once the bureaucracy was unable to act decisively. In the end, fiduciaries are subject to little scrutiny. The locus of adjudication in the courts instead of another administrative mechanism means that a body with little expertise in the subject matter and concerns of scarce resources was the death of accountability under ERISA.

Congress intended for courts to enforce ERISA's primary mission of safeguarding pension promises. As was the case before ERISA (when plan participants relied on trust theories and breach of contract to seek redress in court), however, the courts gave sustained deference to the decisions made by employer representatives. Faced with fiduciaries who had more experience and expertise in the administration of benefit plans and their own conflicting objective of judicial efficiency, courts abdicated the role Congress intended for them to play in the regulation of private pensions after ERISA and expanded the delegation of authority to fiduciaries. This left fiduciaries the power to decide all benefit claims essentially without supervision by an outside,

disinterested party. And it left participants with little more protection than they had prior to ERISA.

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