

## COMMENT

### The OPEB Tsunami: Riding the Wave of Public Sector Postemployment Health Benefits

JENNA AMATO MORAN†

#### INTRODUCTION

There is a tsunami coming.<sup>1</sup> Not convinced? You may have missed the 800-pound gorilla<sup>2</sup> or the elephant in the room, but there's no way around the trillion-dollar pothole.<sup>3</sup> What does this ominous language signify?<sup>4</sup> Our nation is drowning in the midst of an amassed unfunded liability of public sector “other postemployment benefits” (OPEB). Though the OPEB category covers medical, dental, vision, life insurance, and legal services, it is most often used in reference to retirement health benefits.<sup>5</sup> While the funding

---

† J.D. Candidate, Concentration in Labor & Employment Law, Class of 2010, University at Buffalo Law School, State University of New York; B.A., 2004, College of the Holy Cross.

1. Wayne Tompkins, *New Accounting Rule Gives Cities Credit Concerns*, MIAMI DAILY BUS. REV., Jun. 26, 2008, at 1.

2. Cathie G. Eitelberg, *GASB Issues and Solutions for Government Plans*, A.L.I., Sept. 2008, at 540.

3. See DAVID ZION & AMIT VARSHNEY, CREDIT SUISSE, YOU DROPPED A BOMB ON ME, GASB 8 (2007), <http://online.wsj.com/public/resources/document/s/DroppedB.pdf>.

4. See *id.*

5. The OPEB category includes the following benefits: medical, dental, vision, prescription drugs, life insurance, and legal services. This Comment will focus only on medical benefits, since it is the largest percentage—and the most volatile—of all the OPEB costs. See GOVERNMENTAL ACCOUNTING STANDARDS

of these benefits has long been swept under the rug by employers in the public sector, new accounting standards have mandated governmental recognition of this liability.<sup>6</sup> If this predicament sounds familiar, it is because the private sector was forced into recognizing its own liability nearly twenty years ago.<sup>7</sup> Shortly after being confronted with the intimidating financial reality of promises made, private employers began a determined course of reducing the liabilities they owed by cutting retiree health benefits.<sup>8</sup> Now, fast forward twenty years: if government employers follow the same course as the private sector, our nation is likely to see major changes in the retirement health benefits provided to public sector workers and retirees, as governments attempt to control their unfunded liabilities. These changes will surely result in legal challenges. While there are few definitive rules governing public sector retiree benefits across the nation, several important lessons can be learned by studying the private sector's reduction in benefits.

## I. BACKGROUND

Jobs in the public sector have often been plagued by the stereotype that the wages are less desirable than positions

---

BOARD, OTHER POSTEMPLOYMENT BENEFITS: A PLAIN-LANGUAGE SUMMARY OF GASB STATEMENTS NO. 43 AND NO. 45 1 [hereinafter PLAIN-LANGUAGE SUMMARY], available at [http://www.gasb.org/project\\_pages/oepb\\_summary.pdf](http://www.gasb.org/project_pages/oepb_summary.pdf); THE PEW CTR. ON THE STATES, PROMISES WITH A PRICE: PUBLIC SECTOR RETIREMENT BENEFITS 41 [hereinafter PROMISES WITH A PRICE], available at [http://www.pewtrusts.org/uploadedfiles/wwwpewtrustsorg/reports/state\\_policy/pension\\_report.pdf](http://www.pewtrusts.org/uploadedfiles/wwwpewtrustsorg/reports/state_policy/pension_report.pdf).

6. See ACCOUNTING AND FINANCIAL REPORTING BY EMPLOYERS FOR POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS, Statement of Gov't Accounting Standards Bd. No. 45 (Gov't Accounting Standards Bd. 2004) [hereinafter GASB No. 45].

7. See EMPLOYERS' ACCOUNTING FOR POSTRETIREMENT BENEFITS OTHER THAN PENSIONS, Statement of Financial Accounting Standards Bd. No. 106 (Fin. Accounting Standards Bd. 1990) [hereinafter FASB No. 106]. The private sector standards were issued in 1990. See Ronald Kramer & Mark Casciari, *Government Accounting Standards Board (GASB) Statement No. 45 Makes Public Employers Revisit Retiree Health Insurance*, 37 URB. LAW. 427, 428 (2005).

8. See David A. Pratt, *The Past, Present and Future of Retiree Health Benefits*, 3 J. HEALTH & BIOMEDICAL L. 103, 104 (2007).

in the private sector.<sup>9</sup> The advantage of public sector employment is that the benefit packages are considered stronger than what is provided by many private companies. Benefits are not only provided for active workers during their term of employment, but also for former employees after retirement age. In fact, state and local government personnel managers perceive that the offer of retiree health benefits is very helpful in both recruiting and retaining workers for public sector jobs.<sup>10</sup> In a 2008 survey, ninety-two percent of states and sixty-one percent of local governments reported offering retiree health benefits to their workers.<sup>11</sup> The largest groups receiving postemployment health benefits in the current era are high-level executives, union workers, and civil servants.<sup>12</sup>

Employers generally offer one of two types of plans for other postemployment benefits: the defined contribution plan or the defined benefit plan.<sup>13</sup> The most popular plan is the defined benefit plan, to which employers contribute enough to cover specific amounts of benefits during the employee's retirement years.<sup>14</sup> Under this plan, the postretirement benefits that employees are entitled to are clearly specified, and the employer is responsible for contributing a sufficient amount of money to fund those benefits.<sup>15</sup> This is also the typical instrument for paying out pension funds.<sup>16</sup> In the case of retiree health benefits, the

---

9. In this Comment, the "public sector" refers to employment by state and local governments. The federal government is not included in this discussion because the accounting standards at issue are directed at state and local governments. *See* GASB No. 45, *supra* note 6, at 2.

10. RICHARD C. KEARNEY ET AL., CTR. FOR STATE & LOCAL GOV'T EXCELLENCE, AT A CROSSROADS: THE FINANCING AND FUTURE OF HEALTH BENEFITS FOR STATE AND LOCAL GOVERNMENT RETIREES 52, 61 (2009), <http://www.slge.org/vertical/Sites/%7BA260E1DF-5AEE-459D-84C4876EFE1E4032%7D/uploads/%7BCB148BE9-7325-4A7E-B17D-72AEDD246914%7D.PDF>.

11. *Id.* at 62.

12. *See id.* at 115.

13. *See* GASB No. 45, *supra* note 6, at 2; *see also* PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 1.

14. *See* GASB No. 45, *supra* note 6, at 2; PROMISES WITH A PRICE, *supra* note 5, at 14.

15. *See* PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 1-2; PROMISES WITH A PRICE, *supra* note 5, at 14.

16. *See* PROMISES WITH A PRICE, *supra* note 5, at 14.

employer generally promises to pay medical insurance premiums.<sup>17</sup> In a defined benefit plan, the employee could reasonably expect his or her benefit to be covered in full by the employer, though this expectation may very well be changing in the public sector.

Less popular are the defined contribution plans, where employers pay a specific amount of money per year of active service.<sup>18</sup> Generally, this is a set percentage of the employee's salary.<sup>19</sup> The employer will not necessarily specify that it is providing for the payment of a medical insurance premium, as in the defined benefit plan. Instead, employees retire with a set amount of money to put towards their OPEB expenses, which they can utilize until the employer's contribution is exhausted.<sup>20</sup> Under this type of plan, there is less certainty that the employee's OPEB needs will be covered during retirement, based on a number of factors including degree of sickness, cost of health care, and life expectancy. However, this type of plan allows the employer to calculate how much it will need to set aside for each employee.

In the public sector, the world of retirement health benefits is generally regulated on the state level by constitutions or statutes, or by the particular provisions of a collective bargaining agreement between an employer and a union.<sup>21</sup> When the regulation of retirement benefits is discussed, it is logical to wonder about the regulatory role of the Employee Retirement Income Security Act of 1974 (ERISA).<sup>22</sup> ERISA governs both pension funds and welfare benefits; but only for the private sector.<sup>23</sup> ERISA does not

---

17. *See id.*

18. *See* PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 2; PROMISES WITH A PRICE, *supra* note 5, at 14.

19. *See* PROMISES WITH A PRICE, *supra* note 5, at 14.

20. *See* PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 2; PROMISES WITH A PRICE, *supra* note 5, at 14.

21. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, REPORT TO THE COMMITTEE ON FINANCE, U.S. SENATE, STATE AND LOCAL GOVERNMENT RETIREE BENEFITS: CURRENT STATUS OF BENEFIT STRUCTURES, PROTECTIONS, AND FISCAL OUTLOOK FOR FUNDING FUTURE COSTS 25 (2007) [hereinafter GAO REPORT 2007].

22. 29 U.S.C. §§ 1001-1461 (2006).

23. *Id.* § 1003; *see also* JONES DAY COMMENTARY, EVERYTHING YOU ALWAYS WANTED TO KNOW ABOUT A PUBLIC EMPLOYER'S ABILITY TO MODIFY RETIREE

contain any vesting, funding, or reporting rules for the public sector.<sup>24</sup> So while ERISA is a popularly referenced piece of legislation in the private sector, it is not directly relevant in the case of public sector postemployment health benefits. As we will see, however, courts deciding public sector cases have often borrowed legal reasoning from private sector ERISA cases in making their determinations.<sup>25</sup>

## II. NEW ACCOUNTING STANDARDS CALL FOR RECOGNITION OF UNFUNDED LIABILITIES

Funding of pension plans has, for the most part, kept pace with demand in the United States.<sup>26</sup> This is mostly due to the fact that funding is largely regulated by ERISA in the private sector and by state constitutions or statutes in the public sector.<sup>27</sup> The imposing of strict requirements has kept employers on schedule with pension fund obligations.<sup>28</sup> Other postemployment benefits rarely enjoy the same protection from constitutional or statutory provisions.<sup>29</sup> This includes retiree health benefits, which are generally unfunded liabilities. In fact, most state and local government employers fund their OPEB liabilities on a “pay-as-you-go” basis.<sup>30</sup> Under this method, an employer regularly contributes an amount equal to the amount due for the present cost of benefits at that moment.<sup>31</sup> Imagine a

---

BENEFITS BUT WERE TOO AFRAID TO ASK 2 (2008), [http://jonesday.com/pubs/pubs\\_detail.aspx?pubID=S5394](http://jonesday.com/pubs/pubs_detail.aspx?pubID=S5394) [hereinafter JONES DAY] (citing §1003(b)(1)).

24. UNITED STATES GOVERNMENT ACCOUNTABILITY OFFICE, REPORT TO THE COMMITTEE ON FINANCE, U.S. SENATE, STATE AND LOCAL GOVERNMENT RETIREE BENEFITS: CURRENT FUNDED STATUS OF PENSION AND HEALTH BENEFITS 6 n.8 (2008) [hereinafter GAO REPORT 2008].

25. See, *infra*, text accompanying notes 227-231, discussing *Davis v. Wilson County*, 70 S.W.3d 724 (Tenn. 2002). In *Davis*, the court used ERISA principles to decide a public sector retiree benefits case. *Id.*

26. See PROMISES WITH A PRICE, *supra* note 5, at 19.

27. See GAO Report 2007, *supra* note 21, at 18-20.

28. See *id.*

29. See *id.* at 6-7.

30. See *id.* at 6.

31. PROMISES WITH A PRICE, *supra* note 5, at 15.

situation where, instead of paying a semester's worth of tuition up front, a student paid for each credit hour when entering the classroom door. This "pay-as-you-go" system may work well for one student, especially one who has budgeted wisely and always has the money to pay for that credit hour. But imagine a parent with four college-aged children attempting to cope with this type of system. Add in factors such as a family's tight budget and the ever-increasing cost of tuition, and this situation would quickly breed inefficiency, translating into a shaky future for the younger children. These are the concerns that go along with government funding on a "pay-as-you-go" basis. The impending retirement of a large number of workers in the public sector is causing concern that governments will not be able to keep up with their current "pay-as-you-go" funding strategy.<sup>32</sup>

The Governmental Accounting Standards Board (GASB) recently introduced new accounting standards in the hopes of influencing government employers to alter their OPEB funding strategy. The GASB is an independent "professional standard-setting body which serves as the primary source of Generally Accepted Accounting Practices (GAAP) for some 80,000 state and local government entities in the United States."<sup>33</sup> Established in 1984 by the Financial Accounting Foundation, a private, not-for-profit foundation,<sup>34</sup> the GASB's mission is to establish and improve the standards by which state and local governments account for their financial health.<sup>35</sup> This can be a tough mandate because the GASB is not an official government organization and

---

32. See UNITED STATES GOV'T ACCOUNTABILITY OFFICE, REPORT TO THE CHAIRMAN, SPECIAL COMMITTEE ON AGING, U.S. SENATE, STATE AND LOCAL GOVERNMENT RETIREE HEALTH BENEFITS: LIABILITIES ARE LARGELY UNFUNDED, BUT SOME GOVERNMENT ARE TAKING ACTION 24-25 (2009) [hereinafter GAO REPORT 2009].

33. Terry A. M. Mumford, *GASB for Lawyers: What You Need to Know About the New Accounting Standards for Postemployment and Termination Benefits Provided by Government Employers*, 2005 A.L.I.-A.B.A., RETIREMENT, DEFERRED COMPENSATION, & WELFARE PLANS OF TAX-EXEMPT AND GOVERNMENT EMPLOYERS 471; see GAO REPORT 2008, *supra* note 24, at 7.

34. See *id.*

35. See Kenneth W. Bond, *GASB 45: What it Means to Local Governments*, 39 URB. LAW. 723, 723 (2007).

therefore has no enforcement authority.<sup>36</sup> However, most state and local governments adhere to the GASB standards either because of state law requirements or because GASB standards are recognized by the American Institute of Certified Public Accountants (AICPA).<sup>37</sup> The code of the AICPA requires that auditors who are preparing financial statements for government entities look for departures from the GASB standards and note those departures on financial reports.<sup>38</sup> Therefore, it is highly unlikely that a government entity would eschew the financial reporting and accounting standards set forth by the GASB.

A. *From “Pay-As-You-Go” to Prefunding*

In 2004, GASB simultaneously promulgated two rules that forever changed the face of financial reporting and accounting for other postemployment benefits. GASB Statement No. 43, entitled *Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans*, establishes “uniform financial reporting standards” for OPEB plans.<sup>39</sup> GASB Statement No. 45, entitled *Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions*, requires governmental entities to “recognize the cost of these benefits when they are earned by employees, provide information on their financial statements with respect to whether these OPEB are funded, and provide information regarding the impact that the cost of providing OPEB will have on the employer’s future cash flow.”<sup>40</sup> Because of its specific directions for the way in which state and local governments must handle their future financial reporting, GASB No. 45 will have a more foreseeable impact on public sector employment than GASB No. 43.<sup>41</sup>

---

36. See GAO REPORT 2008, *supra* note 24, at 7; Kramer & Casciari, *supra* note 7, at 428.

37. See GAO REPORT 2008, *supra* note 24, at 7; Bond, *supra* note 35, at 723; Kramer & Casciari, *supra* note 7, at 428.

38. See Mumford, *supra* note 33, at 471-72.

39. Melissa A. Fingar, *GASB 43 and GASB 45: The End of Public Sector Retirement Benefits As We Know Them?*, J. COMP. & BENEFITS, Nov.-Dec. 2006, at 18, 20.

40. *Id.* at 21.

41. See Kramer & Casciari, *supra* note 7, at 427 n.1.

Specifically, GASB No. 45 calls for governments to change the way they view other postemployment benefits. Up until now, governments have funded their OPEB liabilities on a "pay-as-you-go" basis. Government employers have derived their payment strategy (or lack thereof) from the fact that employees are not eligible to receive OPEB benefits until they have retired. Meanwhile, employees have long counted on the promise of these benefits because, as mentioned previously, the promise of retirement health benefits is often used in recruiting workers for public sector employment.<sup>42</sup> For many employers, this lag time between the hiring of a worker (and the promise of benefits made) and the eventual retirement of the worker (when benefits begin to be collected) can create an unfortunate temptation to delay funding.<sup>43</sup> When the payment on this liability is so far in the future, the employer is not under any pressure to develop an adequate funding strategy.<sup>44</sup>

The GASB mandate, in sum, means that the government employer must calculate the present amount it expects to pay out for OPEB for its current retirees and employees. The employer must then take this number and determine what annual contribution is required in order to adequately fund its OPEB liability over thirty years. As long as the annual contribution is met each year, at a minimum, the government employer should have sufficient funds to meet the needs of its OPEB plan.<sup>45</sup> Although the new GASB rules do not mandate the implementation of an adequate funding strategy, they certainly encourage a change of perspective regarding this financial liability. Even though employees cannot gain control over them until retirement, these funds represent benefits that are being earned each year. GASB likens OPEB to any other benefit that is earned with each year of service. Active workers who have health insurance benefits earn them and utilize them simultaneously in the same year. Regardless of the fact that retirement health benefits are not utilized until the future, they are also earned presently. This fact should be reflected

---

42. See *supra* text accompanying note 10.

43. See Pratt, *supra* note 8, at 124.

44. There is also an expectation among employers that a certain percentage of employees may retire or choose to leave public sector employment before satisfying the eligibility requirements to obtain retiree health benefits.

45. PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 4.



in the way that the government funds its OPEB liability. The earning of OPEB benefits is part of an “exchange transaction . . . model” where “benefits are ‘earned,’” as part of the “compensation for services.”<sup>46</sup> GASB No. 45 mandates that OPEB be *recognized* on an accrual basis in order to appropriately account for this compensation transaction.<sup>47</sup>

It does not mandate, however, that the benefits be *funded* on an accrual basis. This is an important distinction to be made, one which has caused some criticism of the limitations of GASB No. 45.<sup>48</sup> The Governmental Accounting Standards Board has mandated that governments recognize their unfunded OPEB liability in their annual financial accounting. However, there is no mandate that governments must begin to *fund* this liability. To counter this limitation, it is important to understand that GASB’s authority over the AICPA renders consequences for those governments who leave large liabilities unfunded. As previously mentioned, AICPA members must note any departures or irregularities on the financial accounting reports they prepare.<sup>49</sup> Governments who do not begin to fund their OPEB liabilities will begin to feel pressure from banks and credit companies when the large amount of their unfunded liability becomes public knowledge and sharply drags down their credit ratings.<sup>50</sup> There is some degree of understanding from credit rating agencies, who know that it will take time to lessen the burden of the amassed OPEB liabilities that states and local governments have accumulated.<sup>51</sup> General wisdom from actuaries and consultants is that these credit agencies are also in line with the GASB viewpoint that the governments must at least *start* the funding process, rather than continue to ignore it completely.<sup>52</sup>

---

46. Pratt, *supra* note 8, at 124.

47. *Id.*

48. See Fingar, *supra* note 39, at 21.

49. See *supra* text accompanying notes 34-36.

50. Tompkins, *supra* note 1, at 1. “You don’t have to set up a trust and put money in it. But if you do, it brings all of the numbers down and the rating agencies will treat you much more kindly.” *Id.*

51. It is important to note, however, that after recent economic events credit agencies may no longer have the luxury of being lenient and understanding. Their procedures must now be much more objective.

52. See Tompkins, *supra* note 1, at 1.

To help transition governments who have a long history of ignoring their OPEB liabilities, GASB No. 45 calls for a graduated timeline for implementation of the rule. The three-tiered phase-in calls for larger governments to proceed first. For employers with annual revenue that exceeds \$100 million, the rules went into effect in the first fiscal year beginning after December 15, 2006.<sup>53</sup> For medium-sized governments with annual revenue between \$10 million and \$100 million, the rules went into effect in the first fiscal year beginning after December 15, 2007.<sup>54</sup> And finally, for the smallest governments, with annual revenue less than \$10 million, the deadline was the first fiscal year after December 15, 2008.<sup>55</sup> As of 2009, all governments should be incorporating the GASB No. 45 mandate into their annual accounting methods. Smaller governments not only benefit from a later deadline, but are also permitted to estimate their OPEB cost using “simplified methods and assumptions” if they employ less than 100 workers.<sup>56</sup> This has been done in the hopes of sparing smaller governments the cost of hiring consultants and actuaries to perform the valuation calculations.<sup>57</sup>

#### B. *Factors Affecting GASB No. 45 Calculations*

An employer responding to the mandates of GASB No. 45 will have to heed many factors when calculating the amount needed to adequately fund OPEB. Even with the assistance of skilled actuaries, this will be a challenging task. GASB staff members have acknowledged five factors that employers should consider.<sup>58</sup> The list includes (1) the number of employees eligible to receive benefits, (2) the number of years that employees will work, (3) the expected lifespan of the employees, (4) the cost of healthcare, including the amount of expected increase, and (5) the

---

53. GASB No. 45, *supra* note 6, at 35; PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 11.

54. GASB No. 45, *supra* note 6, at 35.

55. *Id.*

56. PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 6; *see* GASB No. 45, *supra* note 6, at 22-25.

57. *See* PLAIN-LANGUAGE SUMMARY, *supra* note 5, at 6.

58. *Id.* at 3.

amount of money that the government is expected to make off of its investments.<sup>59</sup> This is a daunting list of factors that must be considered when calculating the OPEB liability that remains unfunded.

Rising health care costs, the impending retirement of baby-boomers, and increased life expectancy will cause major increases in the amount of money necessary to fund OPEB plans.<sup>60</sup> Now that the baby-boom generation is reaching retirement, there will be many more retirees needing health care.<sup>61</sup> In 2006, the state of Illinois reported that sixty-five percent of its public employees were between the ages of 40 and 59.<sup>62</sup> In 1986, this amount was only forty-one percent.<sup>63</sup> In the near future, aging in the workforce will affect the public sector much more than the private sector, due to the fact that public employees are generally older than those in the private sector.<sup>64</sup> Another factor is the upward trend in life expectancy, with an estimated average life span of 79.2 years in the year 2015.<sup>65</sup> This is due to both a decrease in infant mortality rates, as well as improvements in medical technology and healthcare.<sup>66</sup> It will result in a larger number of retirees requiring health care for a longer number of years post-retirement.

To further complicate the issue, health care costs are rising exponentially, making it difficult to calculate the increasing rate of growth.<sup>67</sup> Estimates of retirement medical costs vary greatly depending on the source. Some reports state that a couple will need between \$215,000 and \$295,000 to cover their medical expenses in retirement, while other reports run the gamut from \$760,000 to \$2.26

---

59. *Id.* This last factor is perhaps more daunting after the recent collapse of the financial markets.

60. See EMPLOYEE BENEFIT RESEARCH INSTITUTE, FUNDAMENTALS OF EMPLOYEE BENEFIT PROGRAMS 7-10 (5th ed. 1997); see also PROMISES WITH A PRICE, *supra* note 5, at 6.

61. See PROMISES WITH A PRICE, *supra* note 5, at 11.

62. *Id.*

63. *Id.*

64. See *id.*

65. *Id.* at 12.

66. See *id.*

67. See GAO REPORT 2009, *supra* note 32, at 21-25.

million.<sup>68</sup> The fact that prominent research institutes in the area of employee benefits cannot come up with a consistent average proves that this is a very difficult calculation to make, and that regardless of the actual number, the costs will be extremely high, and will only continue to increase.

### C. *Current Status of Funding*

A 2009 Government Accountability Office (GAO) report calculates the combined OPEB liability of all fifty states and thirty-nine local governments at \$530 billion.<sup>69</sup> The fifty states alone account for \$405 billion.<sup>70</sup> Though the local governments selected for the GAO report are the largest thirty-nine cities and counties in the nation, the \$129 billion they owe is surely just the tip of the iceberg for local government liabilities in general.<sup>71</sup> Only a small minority of the fifty states had made some prefunding contribution to their liability before the introduction of GASB No. 45.<sup>72</sup> The majority of states have approached their OPEB liability on a pay-as-you-go basis. As of 2006, only six states were on schedule to completely fund their liability within the next thirty years.<sup>73</sup> These states were Arizona, North Dakota, Ohio, Oregon, Utah, and Wisconsin.<sup>74</sup> However, the largest states in the nation had not made any contributions towards prefunding their OPEB liability before 2006.<sup>75</sup> Those states include California, Florida, Illinois, New York, and Texas.<sup>76</sup> Since it is logical to assume that the largest

---

68. Pratt, *supra* note 8, at 117-18 (citing reports from Fidelity Investments, the Employee Benefit Research Institute, Oxford University Press, and the Center for Retirement Research at Boston College). Some of the variation in these numbers is caused by the approximation of how much of the OPEB liability would be funded by employers, versus how much the employee would need to cover on his or her own.

69. GAO REPORT 2009, *supra* note 32, at 9.

70. *Id.*

71. *Id.* To qualify for inclusion in the GAO Report, each local government must have a total revenue of over \$2 billion. *Id.* at 2.

72. See Pratt, *supra* note 8, at 133. Approximately thirteen states had made an OPEB contribution prior to 2004. *Id.*

73. PROMISES WITH A PRICE, *supra* note 5, at 43.

74. *Id.*; see also Pratt, *supra* note 8, at 133.

75. See PROMISES WITH A PRICE, *supra* note 5, at 43.

76. *Id.*

states will have the largest amount of retirees, and therefore the highest OPEB costs, this statistic is quite daunting. The total cost of OPEB will more than likely be in the billions of dollars for each state.<sup>77</sup> Ohio, for example, has calculated its OPEB obligation at nearly \$30 billion.<sup>78</sup>

Because the GASB standards in Statement No. 45 mandate reporting of this liability, the situation is becoming more visible to taxpayers, credit rating agencies, and others. Whereas governments could previously hide this cost off-the-books, it is now mandatory that they make it public knowledge. The situation has improved transparency, but these large amassed liabilities will come as a shock to many taxpayers. Governments are even more aware of keeping their budgets and credit ratings afloat in the current state of the economy.<sup>79</sup> Fiscal pressure on state and local governments is growing rapidly, as federal funding is being cut and the cost of providing social services is increasing.<sup>80</sup> In short, this is a difficult time to be introducing new fiscal responsibilities into the budget.<sup>81</sup> Two major recession-related developments are contributing to the difficulty of controlling OPEB obligations.

First, states and municipal governments are bringing in less income because federal contributions to their budgets are being cut, and it is becoming more expensive to provide for the needs of governmental activities.<sup>82</sup> The immediate effect on employment is often in the form of hiring freezes, salary freezes, or even salary reductions.<sup>83</sup> In many cases,

---

77. *Id.*

78. Pratt, *supra* note 8, at 133.

79. See Tom Petrino, *Recession Hits All 50 States, a First in at Least 30 Years*, L.A. TIMES, Jan. 29, 2009, [http://latimesblogs.latimes.com/money\\_co/2009/01/recession-state.html](http://latimesblogs.latimes.com/money_co/2009/01/recession-state.html).

80. See Tom Ryan, *Recession Hits States' Ability to Pay Jobless Benefits*, REUTERS, Feb. 11, 2009, <http://uk.reuters.com/article/marketsNewsUS/idUKN1026199720090211>.

81. See Tompkins, *supra* note 1, at 1 (quoting John Pryor, Director of the Broward County Accounting Division, Broward Fla.).

82. See, e.g., Jennifer Steinhauer, *As Aid Vote Nears, Cash-Pressed Governors Are Dialing for Dollars*, N.Y. TIMES, Feb. 10, 2009, at A14.

83. The federal government recently announced an impending freeze on discretionary spending for the next three years on many domestic programs. See Jackie Calmes, *Obama to Seek Spending Freeze to Trim Deficits*, N.Y. TIMES, Jan. 26, 2010, at A1.

government employers may have compensated for reduced salaries by offering increased postemployment benefits to recruit and retain potential employees.<sup>84</sup> Since these costs have previously been off-the-books, employers could make such promises without having to recognize them immediately. With GASB No. 45, however, employers will begin to feel the pressure of these large unfunded liabilities on their balance sheets. No longer can they delay these bills in good conscience. In light of our current economic recession, benefits promised to employees may be coming back to haunt employers. If government employers have not yet realized the circular effect of making these promises, they may still be increasing benefits in lieu of salary increases. These types of actions will lead to ever-growing increases in OPEB liability.

Second, the recession has been laden with layoffs and terminations, leaving many active workers without jobs, while collecting unemployment benefits and possibly even welfare benefits.<sup>85</sup> The number of participants in these government-provided social services is rising dramatically.<sup>86</sup> The cost of providing these benefits to help individuals and families is an increasing drain on government financial resources. Because there is not enough money to go around, and the money may be needed more immediately to provide social services, it may be taken from other parts of the budget, including the funding of retiree health benefits.

One positive effect of the economic recession on OPEB funding is that workers who are unsure of their financial future are reportedly putting off retirement. This is due as much to the uncertainty in the economic climate as it is to the crash in the financial sector that damaged many investment portfolios.<sup>87</sup> Public sector personnel managers acknowledge that many employees who will be eligible for

---

84. See PROMISES WITH A PRICE, *supra* note 5, at 3.

85. See Press Release, Bureau of Labor Statistics, Employment Situation Summary for January 2010 (Feb. 5, 2010), available at <http://www.bls.gov/news.release/pdf/empstat.pdf>.

86. See Associated Press, *Filings for Jobless Claims Rise Unexpectedly*, N.Y. TIMES, Feb. 5, 2010, at B8 (reporting on Press Release, U.S. Department of Labor, Unemployment Insurance Weekly Claims Report (Feb. 4, 2010), available at <http://www.dol.gov/opa/media/press/eta/ui/eta20100138.htm>).

87. See Kelly Greene, *Baby Boomers Delay Retirement*, WALL ST. J., Sept. 22, 2008, at A4.

retirement within the next five years are postponing their retirement because of the “slumping economy.”<sup>88</sup> When workers stay actively employed, the state or local government employer profits from delaying the funding of retiree health care for those workers. The workers’ decision to stay active also results in fewer years of retiree health care that must be provided by the employer, which will help decrease the government’s overall OPEB liability.<sup>89</sup> Despite this one positive sign that may help delay the call for retiree health benefits, it is unlikely to make a significant reduction in OPEB liability. State and local governments must soon face the impending financial reality of the promises made to its workers in the form of retiree health benefits.

### III. LESSONS FROM THE PRIVATE SECTOR

Once public sector employers adjust to the mandates of GASB Statement No. 45, it may seem that an insurmountable task is in front of them. If, in the light of the economic recession, they are unable to implement an adequate funding strategy, then they may be pressured to modify the level of health benefits currently provided to retirees. In both situations, it is helpful for public sector employers to know that there are lessons that can be learned from a similar situation that began in the private sector almost twenty years ago.

#### A. *The Implications of FASB No. 106*

Changes to OPEB funding in the private sector originated at the Financial Accounting Standards Board (FASB), a sister organization to GASB also run by the Financial Accounting Foundation.<sup>90</sup> Much like GASB, it sets

---

88. CENTER FOR STATE & LOCAL GOVERNMENT EXCELLENCE, A TIDAL WAVE POSTPONED: THE ECONOMY AND PUBLIC SECTOR RETIREMENTS 2 (2009), available at <http://www.slge.org> (follow the “A Tidal Wave Postponed” hyperlink under “Workforce”; then download the article). Approximately 80% of personnel managers report that the slumping economy is affecting the timing of retirements. *Id.*

89. The flip side to this “benefit” is that while the employee keeps working, the government employer remains responsible for wages and any employee benefits currently being provided to active workers and their dependents.

90. See Mumford, *supra* note 33, at 471.

“financial accounting and reporting standards,” but for the private sector as well as not-for-profit organizations.<sup>91</sup> FASB Statement Number 106 went into effect in 1993, mandating that all private sector employers report their unfunded OPEB liabilities. These new accounting mandates were referred to as “FASB-forced recognition” of the employer’s accumulated obligation to provide postemployment benefits.<sup>92</sup> In essence, GASB No. 45 is analogous to FASB No. 106.<sup>93</sup> At the introduction of FASB No. 106, private sector employment was plagued with the same unfunded liabilities attributable to retiree healthcare. Studies estimated that implementing the first phase of FASB No. 106 would “decrease the equity of the S&P 500 by \$248 billion or 6 percent.”<sup>94</sup> This enormous liability was due to the fact that private employers had been operating under the “pay-as-you-go” method for many years. Under this approach, the average employer contribution to its unfunded liability totaled only one percent of its payroll costs.<sup>95</sup>

After FASB No. 106 was implemented in 1993, OPEB contributions increased to between five and ten percent.<sup>96</sup> This dramatic increase in costs caused private sector employers to “serious[ly] reconsider . . . whether and how to provide for retiree health insurance” after 1993.<sup>97</sup> In fact, the percentage of large private employers providing retiree health benefits decreased sharply, from sixty-six percent pre-FASB No. 106 to thirty-six percent post-FASB No. 106.<sup>98</sup> When faced with mandated accounting for their retiree health care obligation, employers chose to cut costs and control spending by decreasing or eliminating benefits. It is foreseeable that GASB No. 45 will likely have the same effect on public sector employers, causing them to dramatically decrease or eliminate benefits as well.

---

91. Bond, *supra* note 35, at 723.

92. Pratt, *supra* note 8, at 121-22.

93. See Kramer & Casciari, *supra* note 7, at 428.

94. Pratt, *supra* note 8, at 122.

95. Kramer & Casciari, *supra* note 7, at 431.

96. *Id.*

97. *Id.*

98. *Id.* The sixty-six percent measurement is from 1988, while the thirty-six percent measurement is from 2004. *Id.*



Can employers cut retiree health benefits? Many lawsuits in the private sector have asked this very question. Public sector employers contemplating cuts in retirement benefits in order to control OPEB liabilities may be able to take important lessons from previous litigation, despite the fact that the majority of lawsuits in the private sector have been brought under ERISA.<sup>99</sup> ERISA regulates employers' compliance with the terms of employee benefit plans.<sup>100</sup> Private sector employees and unions often attempt to bring their suit under ERISA, claiming "violation of a 'plan,'" "estoppel," or "breach of fiduciary duty."<sup>101</sup> Other lawsuits have been brought under the auspices of the Labor Management Relations Act (LMRA) or the National Labor Relations Act (NLRA).<sup>102</sup> It is critical to understand that these federal pieces of legislation are not applicable to the public sector. Parties to public sector employment cases should be careful about how closely they interpret private sector litigation that involves these types of claims. Private sector rulings can still be helpful, however, when "interpreting the federal statutes . . . [and] deciding whether . . . a public employer is somehow prohibited from changing benefits."<sup>103</sup> For this reason, it is important to be knowledgeable about previous private sector litigation.

#### B. *Case Study*: General Motors

General Motors, an American automobile manufacturer and one of the country's largest employers, has publicly struggled with the costly burden of its retiree health benefits.<sup>104</sup> Its retiree health care cost is reportedly equal to \$1525 per GM car manufactured.<sup>105</sup> The implementation of

---

99. See *supra* text accompanying notes 22-24.

100. See William T. Payne & Pamina Ewing, *Union-Negotiated Lifetime Retiree Health Benefits: Promise or Illusion*, 9 MARQ. ELDER'S ADVISOR 319, 322 (2008) (citing 29 U.S.C. §§1132(a)(1)(B), (a)(3) (2006)).

101. *Id.* at 322-23 (citing § 1132(a)(1)(B), (a)(3)).

102. See Kramer & Casciari, *supra* note 7, at 436.

103. *Id.*

104. See *Int'l Union, United Auto., Aerospace, and Agric. Implement Workers of America v. Gen. Motors Corp.*, No. 07-CV-14074-DT, 2008 WL 2968408, at \*6 (E.D. Mich. July 31, 2008) [hereinafter *General Motors Case*].

105. See *id.* at \*5 (stating that the labor cost is higher than steel cost); Fingar, *supra* note 39, at 19 (discussing the high labor cost per car).

FASB No. 106 and the consequential accounting of its OPEB liability “eliminated three fourths of the net worth of GM” on paper.<sup>106</sup> GM’s unfunded liability was measured then at \$20.8 billion.<sup>107</sup> Reporting this liability on its books, along with other factors feeding soaring labor costs, put GM in a precarious financial situation where it was unable to control the costs associated with maintaining its business.<sup>108</sup> In 2005, twelve years after the implementation of FASB No. 106, GM’s unfunded liability had actually *increased* to \$81 billion.<sup>109</sup> Skyrocketing costs, along with the impact of having such a large outstanding obligation, caused GM to announce in 2005 that it would make unilateral cutbacks in retiree health benefits.<sup>110</sup> Retirees immediately sued to stop these cutbacks, and the two sides came to a settlement agreement in *UAW v. General Motors Corp.*,<sup>111</sup> nicknamed “*Henry I*” after the lead plaintiff. The settlement preserved health benefits through 2011 in the form of a trust funded by GM.<sup>112</sup>

After the 2005 agreement, GM’s operations continued to suffer financially, and this downward trend translated into a significant deterioration of its credit rating.<sup>113</sup> Because its unfunded retiree health benefit obligation “adversely affect[ed] lending institutions’ assessment of the company’s creditworthiness . . . [it] limit[ed] GM’s access to capital for business operations.”<sup>114</sup> In 2007, GM announced it would have no choice but to “unilaterally reduce” retiree health benefits when the terms of the settlement ended in 2011.<sup>115</sup> Further negotiations between GM and the UAW resulted in an agreement that a new, independent trust would assume

---

106. Pratt, *supra* note 8, at 121.

107. *Id.*

108. See generally Bill Vlasic, *G.M., Teetering on Bankruptcy, Pleads for a Federal Bailout*, N.Y. TIMES, Nov. 12, 2008, at B1.

109. Pratt, *supra* note 8, at 131.

110. See *General Motors Case*, *supra* note 104, at \*3.

111. *UAW v. Gen. Motors Corp.*, No. 05-CV-73991-DT, 2006 WL 891151, at \*6 (E.D. Mich. Mar. 31, 2006).

112. *General Motors Case*, *supra* note 104, at \*3-4.

113. *Id.* at \*4-5.

114. *Id.* at \*5.

115. *Id.* at \*7.

responsibility for OPEB in 2010.<sup>116</sup> The plaintiffs from *Henry I* sued again, claiming that GM and the UAW could not bargain away their retirement benefits.<sup>117</sup> Eventually, the plaintiffs were convinced to join in the settlement. In essence, they were agreeing to settle for less than the full value of their promised benefits. Counsel for the class convinced them to do so in order to avoid a portending situation where “achieved victories . . . later became ‘hollow’ because the losing company then filed for bankruptcy.”<sup>118</sup> The settlement agreement between the parties was deemed “reasonable, fair and adequate,” and was approved by Judge Robert H. Cleland, United States District Court, Eastern District of Michigan, on July 31, 2008.<sup>119</sup> It was decided that the new trust would have “both a fiduciary responsibility and the authority to manage assets and to adjust future benefits after 2011 as necessary for the purpose of continuing to provide substantial lifetime benefits.”<sup>120</sup> The settlement agreement mandated that GM would continue its current contributions through 2011,<sup>121</sup> at which point the new trust would take control via an eleven-member independent committee.<sup>122</sup> This committee would be free to reduce or extend health benefits as necessary.<sup>123</sup> GM assumed responsibility for contributing a fixed amount of \$33 billion to this new trust.<sup>124</sup> Beyond that, the settlement agreement stated that GM bears no responsibility for further funding.<sup>125</sup>

---

116. *Id.*

117. *Id.*

118. *Id.* at \*11.

119. *Id.* at \*35. This settlement agreement is only for hourly GM workers. Different negotiations have been in play over the years for salaried GM employees. This Comment focuses only on the negotiations of hourly employees because the majority of GM employees are hourly workers.

120. *Id.* at \*14.

121. *Id.* This pre-2011 contribution is estimated to be approximately \$5.4 billion. *Id.* at \*15.

122. *Id.* at \*13-14.

123. *Id.* at \*15.

124. *Id.*

125. *Id.*

The settlement agreement was made on the premises that the trust should last approximately eighty years, in order to provide the *Henry I* class of retirees and many current workers with their promised level of retiree health benefits.<sup>126</sup> With the current state of the economy, as well as the rising cost of health care, there are growing concerns over whether this fund can last the planned eighty years.<sup>127</sup> In terms of controlling the potentially devastating impact of GM's OPEB obligation, the court certifying the settlement agreement stated that "[t]he 2008 Settlement will substantially improve GM's opportunity for success by converting GM's OPEB health care obligation from an uncertain defined benefit plan to one that is fixed and capped."<sup>128</sup> This will "free . . . up capital for GM to invest in its core business . . ."<sup>129</sup> This was truly the main focus of the settlement agreement: cost-containment and getting the unfunded liability off of GM's books. Without the mandating of FASB No. 106, this downward trend in GM's business may or may not have occurred, but it is definite that *because* of FASB No. 106, the economic devastation to the company has been much worse.

Despite GM's efforts at relinquishing its postemployment benefit liabilities, it continued to suffer economically after the settlement agreement. In early 2009, GM requested federal aid in order to stave off bankruptcy.<sup>130</sup> It received billions of dollars, along with an executive order to determine a viable strategy for getting out of economic trouble.<sup>131</sup> During the next sixty days, GM, the UAW, and the federal government negotiated to lower GM's costs, especially those concerning the funding of retirement benefits.<sup>132</sup> Even though *Henry I* had developed a strategy for shedding GM's unfunded liability, GM and the UAW had yet to agree on how the obligation would actually be funded.

---

126. *Id.* at \*15-16.

127. *Id.*

128. *Id.* at \*16.

129. *Id.*

130. Bill Vlastic & Nick Bunkley, *Automakers Seek \$14 Billion More, Vowing Deep Cuts*, N.Y. TIMES, Feb. 18, 2009, at A1.

131. Bill Vlastic & Nick Bunkley, *Obama is Upbeat for G.M.'s Future on a Day of Pain*, N.Y. TIMES, June 2, 2009, at A2.

132. *Id.*

During this crisis, GM maintained its proposal of providing part of the trust contribution in the form of company stock, instead of cash. The UAW, in an effort to protect its members' benefits, stringently rejected this proposal, calling it a "non-starter."<sup>133</sup> GM's fiscal situation continued to deteriorate throughout the spring. Just days before declaring bankruptcy, the parties announced the UAW's acceptance of GM's stock funding proposal, making the union a 17.5% shareholder in the auto manufacturer.<sup>134</sup> The agreement also ushered in several enumerated reductions in health benefits, including less prescription drug coverage for retirees.<sup>135</sup> GM emerged quickly from bankruptcy with a restructuring plan aimed at making it a leaner and stronger company.<sup>136</sup> Analysts still predict that in order to stretch the retiree health trust to cover benefits for the projected eighty years, benefit levels will have to be cut even further.<sup>137</sup> Unfortunately, both GM and its retirees are already well aware of the tough decisions and sacrifices that come along with the implementation of a funding strategy for OPEB liabilities.

#### IV. PUBLIC SECTOR REACTION

General Motors's fight to contain the cost of retiree benefits may seem extreme, especially with the intervention of the federal government, a billion-dollar bailout, a speedy bankruptcy, and a subsequent restructuring that conveyed majority stock ownership to the federal government and the union. The automaker's story, however, highlights many issues that private sector employers have been struggling with for the past two decades. With the fiscal pressure

---

133. See Justin Hyde, *Labor Negotiations: UAW Rejects Chrysler, GM Retiree Trust Plans*, DETROIT FREE PRESS, Feb. 14, 2009, at A11.

134. John D. Stoll et al., *GM-Union Deal Raises U.S. Stake*, WALL ST J., May 27, 2009, at A1; see also *GM, Union Agree to Cut Retiree Health Benefits In Exchange for Stock*, KAISER HEALTH NEWS, May 27, 2009, available at <http://www.kaiserhealthnews.org/Daily-Reports/2009/May/27/GM-Union-agree.aspx>.

135. *GM, Union Agree to Cut Retiree Health Benefits In Exchange for Stock*, *supra* note 134.

136. See Bill Vlasic & Nick Bunkley, *supra* note 131.

137. See Joseph Szczesny, *Managing Trusts Will Be Huge Challenge for UAW*, OAKLAND PRESS, Jan. 10, 2010, at F6.

resulting from GASB No. 45, these issues are now beginning to crop up in the public sector. Upon calculating their unfunded liabilities, government employers may begin to get nervous about how they will pay up when the bill comes due. It took twelve years after the implementation of FASB No. 106 for GM to take action to cut its unfunded OPEB liability. In today's economic recession, armed with knowledge of the private sector's prior venture into this territory, it is likely that the public sector will act much more quickly in attempting to resolve its unfunded liabilities.

A. *The State of the Union*

Governments have, in fact, started reacting to these large unfunded liabilities becoming public. Some have had small initial reactions, such as enacting requirements to only reward employees who have a significant number of years of service with the employer.<sup>138</sup> Others have attempted to negotiate lower premium costs with health insurance companies, so that the overall cost burden to the government is reduced.<sup>139</sup> But some reactions have been more dramatic, such as the state of Oregon's decision to discontinue retirement health benefits to all employees hired after 2003.<sup>140</sup> This will cut its overall OPEB obligation, while also enabling it to catch up on funding the liability, since the state will not be amassing any more future benefit costs. However, the state of Oregon may be on the extreme side of initial reactions. As of 2006, only five percent of government employers claimed they may cut benefits to retirees as a result of GASB No. 45.<sup>141</sup>

On the other hand, a higher percentage of employers stated that they were taking *no action* to deal with this impending obligation.<sup>142</sup> Most government employers are still calculating and verifying the cost of funding their

---

138. See GAO REPORT 2007, *supra* note 21, at 38.

139. See *id.*

140. See *id.*

141. *Id.*

142. See *id.* Nine percent of public employers indicated they were "likely" or "very likely" to "take no action" in response to GASB No. 45. Compare this to five percent of employers who said they would cut benefits. *Id.*

OPEB liability and will be doing so for the next few years.<sup>143</sup> Until the employers are more confident that they have correctly estimated their obligation, there may not be many dramatic modifications to the level of benefits provided. Furthermore, the providing of benefits in the public sector is often guaranteed through collective bargaining agreements, and employers may have their hands tied until the next scheduled bargaining.<sup>144</sup> In the meantime, government employers' biggest worry is the impact that this ever-increasing unfunded liability will have on their credit ratings.

### B. *Proposed Strategies*

When dealing with this type of economic environment, employers must consider the best strategy for meeting the GASB No. 45 mandates. One scholar encourages governments to focus on the "three R's of cost containment."<sup>145</sup> First, *redefining* their OPEB plan.<sup>146</sup> This may mean small changes such as enacting eligibility requirements or negotiating lower premium costs with insurance companies. It may also involve larger changes, such as Oregon's decision to freeze retirement benefits for current active workers. These changes allow governments to contain their OPEB liability by making needed cuts in their annual costs. Second, *rethinking* the idea of cost sharing.<sup>147</sup> Government employers may be able to save money, and keep providing the same benefits, by changing the proportion of the government's contribution versus the employee's contribution. Another way to increase cost sharing is to implement a defined contribution plan.<sup>148</sup> In

---

143. *See id.* at 39.

144. *See id.*

145. *See Eitelberg, supra* note 2, at 521.

146. *See id.*

147. *See id.*

148. The federal government has considered switching its own retiree health benefits to something similar to a defined contribution plan. In the new plan, the federal government would pay for a defined portion of the insurance premium (\$3,600 for an individual, \$8,400 for a family). The Congressional Budget Office has calculated that restricting the government's expenditures to this defined contribution would save approximately \$9.7 billion in five years. *See Pratt, supra* note 8, at 137.

this type of plan, the employer contributes a set percentage of the employee's salary each year.<sup>149</sup> When the employee retires, he has a defined amount of money that he is free to spend on health care costs.<sup>150</sup> When the money is used up, the employer has no further liability towards the employee.<sup>151</sup> This type of arrangement could make the employer's costs more manageable, which is the ultimate goal of cost containment. Third, governments will want to think about *restructuring* their benefits scheme.<sup>152</sup> This includes reviewing how their employer-provided plan works in conjunction with Medicare benefits. Employers can leverage the support of Medicare to decrease benefits for retirees age 65 and over. The Medicare-coordination strategy has only recently become authorized by the federal government.

Employer-provided benefits often duplicate the benefits that retirees are eligible to receive under Medicare. Many employers have opted to save on retiree health care by cutting benefits for ages 65 and over. In both the public and private sector combined, more than ninety percent of large employers offer health benefits to retirees under the age of 65.<sup>153</sup> This number drops to seventy-seven percent for retirees over the age of 65.<sup>154</sup> Presumably, this is due to employer coordination with Medicare benefits. The employer is able to cut back on his obligation once the retiree becomes Medicare-eligible. However, employers who imposed this change before 2001 ran into trouble with the Equal Employment Opportunity Commission (EEOC). The EEOC claimed "that coordinating retiree health insurance benefits with the eligibility for Medicare (a condition solely based on age) was discriminatory and was prohibited under the Age Discrimination in Employment Act."<sup>155</sup> The discrimination claim was based on the fact that retirees were treated distinctly differently based on their age, with one group of retirees earning more benefits than the other.

---

149. *See supra* text accompanying notes 19-21.

150. *See id.*

151. *See id.*

152. *See Eitelberg, supra* note 2, at 521.

153. Pratt, *supra* note 8, at 115.

154. *Id.*

155. Fingar, *supra* note 39, at 19.



Or in some cases, the younger retirees received benefits while the older retirees received nothing.

Following EEOC guidance and providing equal retiree health coverage to Medicare-eligible retirees caused duplication of benefits, which was a waste of financial resources. Also, when employers were not allowed to pare down benefits to these older retirees, they often solved the problem by cutting benefits across the board, which started unfairly affecting retirees under the age of sixty-five. Seeing the impact of its decision, the EEOC rescinded its discrimination claim in 2001.<sup>156</sup> Employers are now permitted to apply different benefits packages to retirees below the age of sixty-five, and retirees aged sixty-five and above. The employer must now ensure that the coordination of benefits with Medicare still provides sufficient benefits for the over-65 retiree.<sup>157</sup>

#### V. LEGAL ISSUES IN THE PUBLIC SECTOR

The legal issues surrounding public sector retiree health benefits have been examined in several state courts, but with many different outcomes. This is partly due to the fact that there is no firm authority for resolving public sector cases. The subject area is instead governed by various state statutes and constitutions, as well as by case-specific collective bargaining agreements that provide a contractual framework for the issues in dispute. Because of the differences among states, it is difficult to gather a national consensus on legal issues such as duration of benefits and the employer's ability to make modifications. Further, some state courts have yet to adjudicate on these issues. This part will examine the general legal trends and offer several state-specific examples in order to highlight the legal issues that are likely to arise during the implementation of post-GASB No. 45 retiree health benefit changes.

---

156. *See id.*

157. *See* 29 C.F.R. § 1625.32 (2007). The federal government has a similar procedure for providing retiree health benefits. For Medicare-eligible retirees, the government's Federal Employees Health Benefits (FEHB) program pays for amounts that are not covered by Medicare. This amount is limited, however; FEHB will not pay "more than what it would have paid in the absence of Medicare." CONGRESSIONAL BUDGET OFFICE, BUDGET OPTIONS 162 (2007), <http://www.cbo.gov/ftpdocs/78xx/doc7821/02-23-BudgetOptions.pdf>.

A. *Constitutions, Statutes, and Ordinances*

When deciding public sector employment disputes, courts often look to employees' constitutional rights. A federal or state constitutional claim is one way to sue in order to regain retirement health benefits. In consideration of Federal Constitutional rights, protection may be granted by the Fifth or the Fourteenth Amendments. The Fifth Amendment protects against takings by the government.<sup>158</sup> Retirees may argue that a downward modification in their benefits constitutes a "taking" or an impairment of their contract rights in violation of the Constitution.<sup>159</sup> The Fourteenth Amendment protects property rights by mandating due process before modification.<sup>160</sup> Retirees argue that their health benefits should be included in the property rights that cannot be modified without due process.<sup>161</sup>

One Constitutional issue that has received more attention among the judiciary is the Contract Clause, which asserts that "[n]o State shall . . . pass any . . . Law impairing the Obligation of Contracts."<sup>162</sup> If a state contracted with its employees to provide a specified level of benefits, it may not impair this contract. In cases where the Contract Clause—or a similar state constitutional provision—has arisen, courts first ask whether the modification of benefits truly "impairs" the contract.<sup>163</sup> If it is a mere change in plan provider or a small increase in retiree contribution, then state courts have generally decided the modification is not an impairment.<sup>164</sup> If the modification rises to the level of being an impairment, the state may not carry out that modification to the contract unless it falls into the public policy exception.<sup>165</sup> States

---

158. U.S. CONST. amend. V.

159. See Kramer & Casciari, *supra* note 7, at 446-47.

160. U.S. CONST. amend. XIV.

161. See Kramer & Casciari, *supra* note 7, at 447.

162. U.S. CONST. art. 1, § 10.

163. See, e.g., *U.S. Trust Co. v. New Jersey*, 431 U.S. 1, 17 (1977).

164. See John Sanchez, *The Vesting, Modification, and Financing of Public Retiree Health Benefits in Light of New Accounting Rules*, 41 J. MARSHALL L. REV. 1147, 1181-82 (2008).

165. See, e.g., *U.S. Trust Co.*, 431 U.S. at 22.

reserve the power to modify a contract if the modification is reasonable and necessary to serve an important public purpose.<sup>166</sup> The Contract Clause limits the power of a state to alter its own contracts; however, it cannot be an absolute bar to modification because that would destroy state sovereignty.<sup>167</sup> In theory, the public purpose behind a government employer's modification of benefits would be to save money during a time of tight state and municipal budgets. Under the Contract Clause, however, this rationale is generally not considered reasonable and necessary. "If a State could reduce its financial obligations whenever it wanted to spend the money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all."<sup>168</sup> State employers that use the Contract Clause in their defense strategy will want to assert a more substantial public purpose than the budgetary rationale.

A number of state constitutions include similar contracts protection for employee and retiree benefits.<sup>169</sup> Here, the court must often reach an additional level of analysis to determine if a contract for retiree health benefits is protected from modification. This analysis frequently focuses on the language in the state constitution. In Alaska, for example, Article XII Section 7 states:

Retirement Systems. Membership in employee retirement systems of the State of its political subdivisions shall constitute a contractual relationship. Accrued benefits of these systems shall not be diminished or impaired.<sup>170</sup>

The court in *Duncan v. Retired Public Employees of Alaska* held that "accrued benefits" included retiree health benefits, based on the intent of the drafters.<sup>171</sup> Even though retiree health benefits were not in existence at the time the

---

166. This exception is "necessarily reserved by the States to safeguard the welfare of their citizens." *Id.* at 21.

167. "In short, the Contract Clause does not require a State to adhere to a contract that surrenders an essential attribute of its sovereignty." *Id.* at 23.

168. *Id.* at 26.

169. See Kramer & Casciari, *supra* note 7, at 443. These states include: Alaska, New York, Illinois, Michigan, and Louisiana. *Id.*

170. ALASKA CONST. art. XII, §7.

171. 71 P.3d 882, 886-87 (Alaska 2003).

state constitution was developed, the court held that the drafters intended that accrued benefits would encompass the entire package of benefits given to the retired worker.<sup>172</sup> Health benefits should not be separated out, but should instead be afforded the same protection as pension benefits.<sup>173</sup>

State courts remain divided on interpretations of these constitutional provisions. The Supreme Court of Michigan held that health benefits are not included in the following constitutional provision, which contains very similar language:

The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby.<sup>174</sup>

The court's interpretation in Michigan was based on the descriptive phrase "accrued financial benefits."<sup>175</sup> The court held that retiree health benefits were neither accrued nor financial.<sup>176</sup> The court interpreted the term "accrued" as invoking a benefit that grows over time with the number of years of service, such as a pension that accumulates its worth.<sup>177</sup> Benefits promised to an employee do not generally "grow" in the same sense of the term. Likewise, the court found health care benefits are not considered to be "financial" benefits because health care is generally provided as a service, not in monetary form.<sup>178</sup> The court found further evidence by looking to the next section of the constitution, which discusses annual funding of the accrued financial benefits.<sup>179</sup> Since the state did not have a practice

---

172. *Id.* at 887.

173. The court also noted that there was no express limitation placed on the benefits, as there is in ERISA's separation of health benefits from the protection given to pension benefits. *Id.*

174. *Studier v. Mich. Pub. Sch. Employees' Ret. Bd.*, 698 N.W.2d. 350, 355 (Mich. 2005) (citing MICH. CONST. art. 9, § 24).

175. *Id.* at 357.

176. *Id.* at 357-58.

177. *Id.* at 357.

178. *Id.* at 358.

179. *Id.*

of prefunding retiree health benefits, this was further proof that health benefits were not intended to be constitutionally protected.<sup>180</sup> The constitutional provision was instead intended to protect pension benefits, which accrue financially and are prefunded.

Besides federal and state constitutions, it is important to examine any relevant statutes. As previously discussed, federal statutes that may govern private sector benefits are not applicable in the public sector, and therefore there is less certainty in how courts will determine the outcome of a modification of benefits case. In public, non-union settings, without the existence of federal statutes or collective bargaining agreements, there is little evidence of statutory contractual rights. “Changes [in benefits] . . . are almost always contested [by retirees], and the outcome usually depends on the court’s interpretation of the ordinance or statute giving rise to the retirement coverage.”<sup>181</sup> Because there is a lack of strong statutory authority, the main focus of the court’s analysis is whether any existing governing statutes are “‘plain and susceptible of no other reasonable construction’ than that the legislature intended to be bound to a contract.”<sup>182</sup> There must be adequate evidence that the state intended to be bound. The reason for the court’s hesitation is because it does not want to infer a private contract where a state or local government is one of the contracting parties.<sup>183</sup> The Supreme Court of Colorado found that, despite the following City of Colorado Springs municipal ordinance, the city was not obligated to provide full retirement health benefits to its workers:

Upon retirement of an employee the City will pay the cost of continuing his Blue Cross-Blue Shield program . . . . [T]he City will pay the entire monthly premium cost . . . .<sup>184</sup>

---

180. *Id.*

181. JONES DAY, *supra* note 23, at 1.

182. *Id.* at 10 (citing Stanislaus County v. San Joaquin & King’s River Canal & Irrigation Co., 192 U.S. 201, 208 (1904)).

183. *See* JONES DAY, *supra* note 23, at 10.

184. Colo. Springs Fire Fighters Ass’n, Local 5 v. City of Colo. Springs, 784 P.2d 766, 768 n.2 (Colo. 1989) (citing Colorado Springs, Colo., Ordinance No. 3256 (Jan. 25, 1966)).

When the city decided to cap the amount of its contribution to \$91.40 per month per retiree, the court held that the employees could not rely on the above ordinance as evidence of contractual vesting.<sup>185</sup> This decision was based in part on the city's charter, which stated that the city council did not have the authority to promise indefinite financial expenditures.<sup>186</sup> Holding the city responsible for paying an indefinite cost would violate the charter and burden the city council with a large financial obligation for years to come.<sup>187</sup> The ordinance's use of the phrase "entire monthly premium cost" was not sufficiently definite to make the ordinance valid in the eyes of the court to infer contractual obligations between the two parties.<sup>188</sup>

There is no clear path for the courts to take on these issues where there is a constitutional provision, state statute, or municipal ordinance at issue. Courts often examine the intent at the drafting or ratification of the constitution, as well as the actual language of the provision. This examination frequently involves a comparison between health benefits and pension benefits. Although the exact approach varies state-by-state, most courts' decisions attempt to balance the intent of the legislature with the public policy of protecting the financial interests of the state.

### B. *Identifying and Analyzing the Relevant Documents*

Retiree health benefits cases require the examination of several different types of documents. With all of these documents gathered, courts are able to do a complete analysis of the intent of the parties, to decide the questions of contract rights and vesting. Under private sector ERISA claims, the court looks first and foremost to the "governing document."<sup>189</sup> Even though public sector cases are not ruled by ERISA, it is probable that courts will turn to a similar examination to study the expectations of employer and employee, as well as the parties' consensus. The test of

---

185. *Id.*

186. *Id.* at 773.

187. *Id.*

188. *Id.* at 773-74.

189. Payne & Ewing, *supra* note 100, at 323.

which document governs is “not what a document calls itself but whether it in fact governs a plan.”<sup>190</sup> Possible governing documents include a collective bargaining agreement (CBA), summary plan description (SPD), merger agreement, letter from the employer, or other employment contract.<sup>191</sup> Once the governing documents are uncovered, courts will study them for evidence of contract rights and vesting.<sup>192</sup>

More specifically, courts will look for two specific clauses. The first being the general duration clause, which states how long the benefits are provided for.<sup>193</sup> Oftentimes, this is ambiguous in the language of the governing document. However, if the document happens to tie vesting of retiree health benefits into the vesting of pension benefits, then the court assumes the health benefits are meant to extend throughout the retiree’s lifetime.<sup>194</sup> This is known as the “tying principle” and often works in the retiree’s favor to protect his health benefits from employer diminishment.<sup>195</sup>

Second, courts looks for a reservation of rights clause, in which the employer categorically states his right to amend the agreement in the future.<sup>196</sup> Some courts discount this type of clause, because of its unilateral nature.<sup>197</sup> Other courts see the reservation of rights as providing the employer with necessary control over the employment relationship.<sup>198</sup> A reservation of rights clause puts the employees and retirees on notice that changes can be made at any time and for any reason. If the employee knew the employer had the right to make modifications in the future, he could not have reasonably relied upon the conditions as originally agreed. The reservation of rights clause can be used to challenge an employee’s estoppel or reliance claim.<sup>199</sup>

---

190. *Id.*

191. *See id.* at 323-27.

192. *See id.* at 328.

193. *See id.* at 346.

194. *See id.* at 347-48.

195. *Id.*

196. *See id.* at 340.

197. *See id.* at 340-41.

198. *See id.* at 341.

199. *Id.* at 349.

If a retiree can show that reliance caused him a detriment, he may be able to bring a claim of estoppel.<sup>200</sup> In general, estoppel is applicable when the employer has made a "material misrepresentation" to the employee or retiree.<sup>201</sup> However, a claim of estoppel can be countered by the employer with the unambiguous existence of a reservation of rights clause in the contract, plan documents, or collective bargaining agreement.<sup>202</sup> If a reservation of rights clause does not exist and the employee is able to prove reliance, he has a stronger chance of winning on a claim of contractual rights. For example, if the employer required a certain number of years of service in order to be eligible for benefits, an employee who put in that much time could be successful in his or her claim.<sup>203</sup> The reliance proves the construction of a unilateral contract, thereby granting contractual rights to the employee.<sup>204</sup>

After examination of the governing document, courts will analyze the remaining documents brought forth by either party. This may include all documents that were not deemed to be the governing document, as well as any oral or written statements made to employees or retirees.<sup>205</sup> Additionally, the analysis can include documentation of contract or collective bargaining negotiations, including proposals and counterproposals.<sup>206</sup> Finally, courts will gather extrinsic evidence that is not expressly documented, but is much more anecdotal. This includes factors such as whether the employer continued retiree health benefits during worker strikes, any analysis of benefit cost containment done by the employer, and the history of prior modifications to retiree benefits.<sup>207</sup> In most cases, however, courts must decide that the contract language in the governing document is ambiguous before examining any

---

200. *Id.*

201. *Id.*

202. *See id.*

203. *See Kramer & Casciari, supra* note 7, at 440.

204. *See id.*

205. *See Payne & Ewing, supra* note 100, at 334-35.

206. *See id.*

207. *See id.* at 335-36.



extrinsic evidence.<sup>208</sup> As with many issues in retiree health benefits cases, the decision of courts to look at certain documents is a state-specific choice often made on a case-by-case basis.

### C. *The Vesting Question*

When reviewing all of the aforementioned documents, the courts examine them for any evidence of vesting. An employee vests when he “gains a legal claim to an eventual benefit.”<sup>209</sup> That claim means he has “attained an unalterable right” to that benefit.<sup>210</sup> Pension benefits vest to the employee, but there is much disagreement over whether retiree health benefits are vested benefits as well.<sup>211</sup> If they are not considered to be vested, it means they are merely gratuitous, and therefore are subject to unilateral reduction by the employer.<sup>212</sup> When courts examine the issue of vesting, they must look for evidence of how long the promised benefits last and whether the employer is free to modify or terminate the benefits without the employee’s consent.<sup>213</sup> Many courts have determined that the key to deciding the vesting issue is looking at the employer’s intent.<sup>214</sup> Much like analyzing the intent of controlling constitutional or statutory language, determining whether the employer intended for benefits to be vested tells a court whether the employer can make subsequent modifications.

---

208. See generally *Poole v. Waterbury*, 831 A.2d 211, 229-30 (Conn. 2003), where ambiguous language in the collective bargaining agreement led the court to decide based on extrinsic evidence that the city had a long-standing practice of continuing to provide health care benefits to retired workers.

209. Olivia S. Mitchell with Erica L. Dykes, *New Trends in Pension Benefit and Retirement Provisions*, in *BENEFITS FOR THE WORKPLACE OF THE FUTURE* 110, 112 (Olivia S. Mitchell et al. eds., 2003).

210. Richard L. Kaplan et al., *Retirees at Risk: The Precarious Promise of Post-Employment Health Benefits*, 9 *YALE J. HEALTH POL’Y L. & ETHICS* 287, 303 (2009).

211. See *id.* “[T]he vesting of health care benefits has spawned extensive litigation and nuanced jurisprudential hopscotch over whether vesting of welfare benefits can occur.” *Id.*

212. See Payne & Ewing, *supra* note 100, at 321-22.

213. See Sanchez, *supra* note 164, at 1164-65.

214. See Payne & Ewing, *supra* note 100, at 322.

Courts have had varied opinions on whether changes to retiree health care infringes upon vested benefits.<sup>215</sup>

Without existing authority on vesting in the public sector, courts deciding these cases have looked to private sector rulings.<sup>216</sup> Case law in the world of private sector employer-union relationships does not provide any definite rules, however, because of an existing circuit split. The most well-known case is the Sixth Circuit's *UAW v. Yard-Man, Inc.*<sup>217</sup> In *Yard-Man*, the court examined whether the employer and the union had contracted in the collective bargaining agreement to provide vested benefits. The court determined that its decision must be based on a strict interpretation of the intent that can be read only from the terms of the contract alone.<sup>218</sup> The so-called "*Yard-Man* inference" stands for the interpretation that as long as a person remains classified as a "retiree," it should be inferred that his retirement benefits will continue without modification.<sup>219</sup> This interpretation has been rejected by other circuit courts. The Seventh Circuit's holding in *Bidlack v. Wheelabrator Corp.* ruled in favor of the presumption that retiree benefits only last as long as the agreement under which they began.<sup>220</sup> The Third, Fifth, and Eighth Circuits have also rejected *Yard-Man* to varying degrees, but have not made any solid presumptions of their own to replace the "*Yard-Man* inference" or "*Wheelabrator* presumption."<sup>221</sup> Until the Supreme Court addresses this private sector issue, it remains contested, and it will not provide much help to state courts that often look to the private sector for guidance.

A frequently cited public sector case is *Roth v. City of Glendale*, where the Supreme Court of Wisconsin held that health benefits will vest unless there is express contractual language stating otherwise.<sup>222</sup> Here, the court took into

---

215. *See id.* at 343.

216. *See, e.g.,* Davis v. Wilson County, 70 S.W.3d 724 (Tenn. 2002).

217. *UAW v. Yard-Man, Inc.*, 716 F.2d 1476 (6th Cir. 1983).

218. *See* Kramer & Casciari, *supra* note 7, at 438; Payne & Ewing, *supra* note 100, at 329-30.

219. *See* Kramer & Casciari, *supra* note 7, at 438.

220. *Bidlack v. Wheelabrator Corp.*, 993 F.2d 603, 608 (7th Cir. 1993).

221. *See* Kramer & Casciari, *supra* note 7, at 438-39.

222. 614 N.W.2d 467, 474 (Wis. 2000).

account the retired worker's expectation that he will receive the health care benefits promised by his employer: "Bargained for benefits are not gratuities handed to the employee, but rather deferred compensation for past services rendered."<sup>223</sup> The *Roth* court called for a presumption in favor of vesting in order to protect promises made and compensation owed.<sup>224</sup> The opinion relied on the concurrence in *Wheelabrator*, allowing for the consideration of extrinsic evidence: "When the agreement is ambiguous, extrinsic evidence may be consulted to rebut the [vesting] presumption and to demonstrate that the parties did not intend the benefits to vest."<sup>225</sup> The vesting presumption, therefore, can only be rebutted if there is express language or extrinsic evidence that clearly runs contrary to vesting.<sup>226</sup>

On the other hand, the Supreme Court of Tennessee has held that retiree health benefits will not vest unless there is express language stating the intent to do so.<sup>227</sup> The opinion in *Davis v. Wilson County* was largely based on a comparison to the private sector where pensions vest under ERISA but health care benefits do not.<sup>228</sup> Private sector employers are not legally required to provide health care benefits, much less to vest them.<sup>229</sup> From this perspective, the court took into account the unnecessary burden that would be placed on the employer if public sector health benefits automatically vested.<sup>230</sup> Because "vested benefits are forever unalterable," it may prove to be overly burdensome to require employers who voluntarily provide the benefits to be unable to unilaterally make modifications.<sup>231</sup>

---

223. *Id.* at 472.

224. *Id.* at 472-73.

225. *Id.*

226. *Id.* at 472-73.

227. *Davis v. Wilson County*, 70 S.W.3d 724, 728 (Tenn. 2002).

228. *Id.* at 727.

229. *Id.* at 727-28.

230. *Id.*

231. *Id.* (citation omitted).

#### D. *Collective Bargaining*

In private and public sector union settings, courts will focus on collective bargaining agreements, in which the parties have created rules for the distribution and modification of benefits. When discussing public sector employment, it is crucial to understand the issues that are specific to collective bargaining agreements, since a large number of public employees are union workers. “[I]t is estimated that 37.2% of the (public sector) workforce are members of a union versus only 8.2% for the private sector.”<sup>232</sup> It is general wisdom that the more unionized the workers, the more difficult it is for employers to modify retiree benefits.<sup>233</sup> This was certainly the case for General Motors.<sup>234</sup> Unions and labor advocacy groups are strongly opposed to GASB No. 45.<sup>235</sup> The largest public employee union, the American Federation of State, County and Municipal Employees (AFSCME), has been a vocal critic of the new accounting standards.<sup>236</sup> According to AFSCME, mandating that government employers report their unfunded OPEB liability will unnecessarily provoke “excessively alarmist predictions” about how these liabilities will be the source of economic crisis.<sup>237</sup> AFSCME also believes that implementation of GASB No. 45 will lead to a “taxpayer backlash” and a “contraction of public-sector benefits” that will force their members to relinquish long-held retirement benefits.<sup>238</sup> Union members’ strong criticism of the GASB standards will complicate the implementation among government employers. Therefore, public employers who hold union contracts must understand the issues that are specific to unions and their collective bargaining agreements.

---

232. Pratt, *supra* note 8, at 104 n.8 (citing ZION & VARSHNEY, *supra* note 3, at 18).

233. *See id.*

234. *See supra* text accompanying notes 104-137.

235. *See* Kramer & Casciari, *supra* note 7, at 428.

236. *See* Marie Gottschalk, *Back to the Future? Health Benefits, Organized Labor, and Universal Health Care*, 32 J. HEALTH POL. POL’Y & L. 923, 934 (2007).

237. *Id.*

238. *Id.*

When examining the contractual rights of the parties in a union setting, the strongest piece of evidence is the collective bargaining agreement. “[T]o the extent retiree health benefits are legally protected, it is generally because they have been collectively bargained . . . .”<sup>239</sup> A collective bargaining agreement is often the governing document in an employer-union relationship. Because both sides take part in the creation of the document, it sends a much clearer signal of both parties’ intent. Courts very often “draw inferences or make presumptions” on the basis of the collective bargaining agreement alone.<sup>240</sup> But do courts regard the document as granting contractual rights? In *Poole v. City of Waterbury*,<sup>241</sup> the Superior Court of Connecticut held that the agreement was a contract “between two parties of relatively equal bargaining power” that could “effectuate the intent of the parties, which is determined from the language used interpreted in the light of the situation of the parties and the circumstances connected with the transaction.” The agreement was deemed to be the governing document and the court instructed that “[w]here the language of the contract is clear and unambiguous, [it] is to be given effect according to its terms.”<sup>242</sup> In general, courts are divided over whether to follow similar reasoning when adjudicating public sector benefits.<sup>243</sup>

During the collective bargaining process, some employment issues are mandatory subjects of bargaining. The private sector employer, governed by the National Labor Relations Act, must bargain with the union on these subjects.<sup>244</sup> Although the NLRA does not cover the public sector, courts are likely to apply similar rules towards collective bargaining to provide guidelines for their

---

239. GAO REPORT 2008, *supra* note 24, at 7.

240. Payne & Ewing, *supra* note 100, at 342 (citing *In re White Farm Equipment Co.*, 788 F.2d 1186, 1193 (6th Cir. 1986)).

241. 831 A.2d 211, 224 (Conn. 2003).

242. *Id.*; see also Kramer & Casciari, *supra* note 7, at 441.

243. See Kramer & Casciari, *supra* note 7, at 440.

244. See generally ARCHIBALD COX, DEREK CURTIS BOK, ROBERT A. GORMAN & MATTHEW W. FINKIN, LABOR LAW: CASES AND MATERIALS 442-43, 458-59 (14th ed. 2006).

examination of the issues.<sup>245</sup> Subjects that are considered mandatory under the NLRA are generally those that “vitally affect[] the ‘terms and conditions’ of their employment.”<sup>246</sup> If the employer refuses to bargain about a mandatory subject of bargaining, or does not bargain in good faith, the employer commits an unfair labor practice in violation of NLRA § 8(a)(5).<sup>247</sup> Active worker health benefits are a mandatory subject of bargaining because they vitally affect the terms and conditions of employment.<sup>248</sup> A private employer has a duty to bargain on the subject and may not make unilateral changes.<sup>249</sup> The Supreme Court in *Allied Chemical & Alkali Workers v. Pittsburgh Plate Glass*<sup>250</sup> distinguished retiree health benefits from the general rule governing active worker health benefits. The employer is not obligated to bargain about modifying provisions in the contract that govern vesting of retiree health benefits, as these benefits are not vital to the relationship between employer and employee.<sup>251</sup>

The Supreme Court in *Allied Chemical* also held that retirees did not have a place in the bargaining negotiations between employees and their employer.<sup>252</sup> Retirees and active workers “do not share a community of interests broad enough to justify inclusion” of retirees in the bargaining unit.<sup>253</sup> While retirees are interested in the protection of their pensions and benefits, employees’ concerns center on wages and working conditions. Having two groups within the same bargaining unit with such different priorities could result in “severe internal conflicts that would impair the unit’s ability to function and would disrupt the processes of collective bargaining.”<sup>254</sup> The exclusion of

---

245. See Sanchez, *supra* note 164, at 1156.

246. *Allied Chemical & Alkali Workers of Am., Local Union No. 1 v. Pittsburgh Plate Glass Co.*, 404 U.S. 157, 179 (1971).

247. 29 U.S.C. § 158 (2006).

248. *Allied Chemical*, 404 U.S. at 159.

249. See COX ET AL., *supra* note 244, at 459.

250. 404 U.S. at 176-78.

251. *Id.* at 177-78.

252. *Id.* at 158; see also *General Motors Case*, *supra* note 104, at \*30.

253. *Allied Chemical*, 404 U.S. at 173.

254. *Id.*

retirees from the bargaining process factored heavily into the Supreme Court of Wisconsin's decision-making in *Roth*. The court called for a presumption in favor of vesting in order to "protect the voiceless in the subsequent negotiating process."<sup>255</sup> Because retirees were not included in the collective bargaining process, the court found they were generally entitled to the health benefits that were negotiated by the collective bargaining agreement that was in effect at the time of their retirement.<sup>256</sup> The court in *Poole* held that the retiree health benefits at issue should vest because the post-retirement "plaintiffs [would] no longer . . . be in a position to negotiate with the city over future benefits."<sup>257</sup> The decision to vest retirees with the health benefits promised at retirement best reflected the intent of the parties at the time of their agreement.<sup>258</sup>

## VI. THE FUTURE

It is difficult to ascertain whether a state court will protect retiree health benefits promised to a public sector worker or if it will allow the government employer to modify the prior-existing agreement. Litigation from the private sector can share some clues as to how the implementation of GASB No. 45 may play out in the public sector. Now that all public sector governments are required to report their unfunded OPEB liabilities on an annual basis, states and local governments may begin feeling pressure to reduce the amount owed. Governments have two options to reduce this unfunded liability: develop an adequate funding strategy, or modify existing retiree health benefits. Due to the economic recession, many state and local governments are not in a position to begin implementing a funding strategy in the current climate. It is likely then that the number of government employers considering modifications to benefit packages will increase over the next several years.

In light of the future implications this may cause for state and local governments, it is critical that labor and

---

255. *Roth v. City of Glendale*, 614 N.W.2d 467, 473 (Wis. 2000).

256. See *Payne & Ewing*, *supra* note 100, at 344-45.

257. *Poole v. City of Waterbury*, 831 A.2d 211, 228 (Conn. 2003).

258. This reflects the reasoning in *Yard-Man*, a private sector case often cited in public sector cases. See *supra* text accompanying notes 215-17.

employment lawyers are aware of the implications of the new GASB standard. They can assist their clients—both employer and employee—through the muddy waters of retiree health benefits post-GASB No. 45. And after all, “the types of claims raised by . . . retirees facing the loss or reduction of retiree health insurance benefits are limited only by the imagination of their counsel.”<sup>259</sup> If all involved are more aware of the situation and its serious implications, we may be able to lessen the impact of the approaching OPEB tsunami.

---

259. Kramer & Casciari, *supra* note 7, at 446.