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SOME IMPLICATIONS OF THE CHANGING STRUCTURE OF WORK FOR WORKER
RETIREMENT SECURITY, PENSIONS AND HEALTHCARE

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1. INTRODUCTION

In 2014, Dr. David Weil published an important book in which he discusses the “fissured workplace” and its consequences for workers:

The fissured workplace reflects competitive responses to the realities of modern capital and product markets. The boundaries of firms have been redrawn as a result of new technology and the falling costs of information. As detailed in Part II, the consequences of the fissured workplace are profound. Wage determination changes dramatically, often to the detriment of workers whose work has been shifted outward. Blurring lines of responsibility increase the risks for bad health and safety outcomes. And the pressure to cut corners and not comply with basic labor standards intensifies.¹

Anne-Marie Slaughter, among others, has written of the problems women face in the “toxic workplace”:

The problem is even more acute for the 42 million women in America on the brink of poverty. Not showing up for work because a child has an ear infection, schools close for a snow day, or an elderly parent must go to the doctor puts their jobs at risk, and losing their jobs means that they can no longer care properly for their children -- some 28 million -- and other relatives who depend on them. They are often suffering not only from too little flexibility but also too much, as many low-wage service jobs no longer have a guaranteed number of hours a week.

THE problem is with the workplace, or more precisely, with a workplace designed for the “Mad Men” era, for “Leave It to Beaver” families in which one partner does all the work of earning an income and the other partner does all the work of turning that income into care - the care that is indispensable for our children, our sick and disabled, our elderly. Our families and our responsibilities don’t look like that anymore, but our workplaces do not fit the realities of our lives.²

Add to this the continuing effects of the recession (unemployment, underemployment, stagnating wages, uncertain work schedules) and the picture for many, if not most, working families is not encouraging.

Qualified employer retirement plans have been regulated under the Internal Revenue Code (the “Code”) since the 1920s. The Social Security Act and the National Labor Relations Act were enacted in 1935. The Fair Labor Standards Act was enacted in 1938. Medicare and Medicaid were enacted in 1965. The Employee Retirement Income Security Act (“ERISA”), which regulates employee benefit plans (including both retirement plans and health and welfare plans), was enacted in 1974. These statutes were enacted at times when, by comparison to today, the

¹ David Weil *The Fissured Workplace: Why Work Became So Bad for So Many and What Can be Done to Improve It* (hereafter, “Weil”), Harvard Univ. Press, 2014, at 180.

² Anne-Marie Slaughter, *A Toxic Work World*, New York Times, Sept. 20, 2015, at SR 1.

labor market was vastly different, employers were less fixated on quarterly earnings, income inequality was less pronounced and life expectancies were generally shorter.

In contrast, the Affordable Care Act³ is only 5 years old: though it has already significantly increased access to health care, eliminated many questionable insurance practices and reduced the number of uninsured Americans, it has been subjected to incessant attacks and threats of repeal. If one looked only at statements made by our elected representatives, one could conclude that Americans do not want retirement security or access to good health care (at least, not for other people). I believe that this is incorrect, but people must make their voices heard to convince employers and politicians that these are vital issues for the survival of America as a great, prosperous and compassionate society.

2. SOCIAL SECURITY

Social Security continues to be the largest single source of income for elderly Americans. In 2012, Americans aged 65 or older received 38% of their income from Social Security, with another 18.4% coming from pensions and annuities.⁴

According to the Social Security Administration:

“Social Security is the major source of income for most of the elderly.

Nine out of ten individuals age 65 and older receive Social Security benefits.

Social Security benefits represent about 39% of the income of the elderly.

Among elderly Social Security beneficiaries, 53% of married couples and 74% of unmarried persons receive 50% or more of their income from Social Security.

Among elderly Social Security beneficiaries, 22% of married couples and about 47% of unmarried persons rely on Social Security for 90% or more of their income.”⁵

The following shows estimated Social Security benefits for workers reaching retirement age (age 66) in 2015 at different earnings levels and illustrates the downward gradation in Social Security replacement levels, that occurs as earnings levels increase. Low earnings 44.5%; medium earnings 32.9%; high earnings 27.3%. These replacement ratios will decline over the next 20 to 30 years. Reasons for this decline include the legislated increase in the “full-benefit age” for

³ The Affordable Care Act (or ACA) is a shorthand name for two separate statutes, the Patient Protection and Affordable Care Act, P.L. 111-148, signed on March 23, 2010, and the Health Care and Education Reconciliation Act, P.L. 111-152, signed on March 30, 2010.

⁴ Employee Benefit Research Institute, Databook on Employee Benefits, chapter 3, chart 3.1b, updated July 2014. For 1974, the corresponding percentages were 42% and 14%. Id., chart 3.1a. See also Social Security Administration, Income of the Population 55 or Older, 2012, available at www.ssa.gov.

⁵ Social Security Basic Facts, October 13, 2015, <https://www.socialsecurity.gov/news/press/basicfact.html>. See also Ke Bin Wu, Sources of Income for Older Americans, 2012, AARP Public Policy Institute, www.aarp.org, finding that “Social Security accounts for about four out of every five dollars of income for older people with low to moderate incomes” and that “In 2012, Social Security benefits kept about 15 million people aged 65 and older out of poverty. Without Social Security income, the poverty rate for this group would rise from 9.1 percent to 44.4 percent.”

receiving Social Security benefits, increased income taxation of Social Security benefits, and rising Medicare premiums that are deducted directly from Social Security benefits.⁶

It is clear that the financing of Social Security needs to be recalibrated, but the situation is nowhere near as dire as the alarmists suggest. And one solution advocated by many, including several Presidential candidates, raising the retirement age across the board, would affect lower income retirees drastically:

Advocates of the idea usually argue the reform makes sense because life spans are rising. If we leave the Social Security retirement age unchanged, the increase in life expectancy means payments from the program must cover more years, even though the number of years we expect workers to remain employed will remain unchanged. This argument would be more convincing if increases in life expectancy were spread evenly across the workforce. They are not. Workers who earn low wages throughout their careers have seen little or no improvement in life expectancy. It seems unfair to ask low-earners to take a benefit cut to pay for the added benefits high-earners enjoy because of longer life spans...Researchers in the Social Security Administration and elsewhere have found that men near the bottom of the earnings distribution and women with below-average schooling and in families with low incomes have seen little or none of the improvement in life expectancy that higher income groups have enjoyed.

Low income workers always had shorter life expectancies than workers with higher incomes. New research shows that the gaps in life expectancy are growing... These new estimates [from the National Academy of Sciences] indicate that life expectancies are typically higher for men and women with higher incomes, but that remaining life expectancy at age 50 has remained almost unchanged or fallen at the bottom of the distribution, whereas it has increased substantially at the top.⁷

In fact, there is a strong argument that Social Security should be expanded: it is the most efficient part of the overall retirement system, it protects beneficiaries against inflation, investment risk, longevity risk and cognitive risk, and by redistributing (to some extent) resources to lower-earning beneficiaries it can fill some of the gaps in the private retirement system.⁸

⁶ Social Security Administration, Office of the Chief Actuary, Actuarial Note Number 2014.9, July 2014, <http://www.socialsecurity.gov/OACT/NOTES/ran9/an2014-9.pdf>.

⁷ Gary Burtless, Raising everyone's retirement age undercuts a key goal of Social Security, Oct. 22, 2015, <http://www.brookings.edu/research/opinions/2015/10/22-raising-everyones-retirement-age-undercuts-key-goal-of-social-security-burtless>. See also Esmé E Deprez, Margarte Newkirk, Republican Plans to Raise Retirement Age Fall Heavily on Poor: "In wealthy Fairfax County, just outside Washington, the average woman can expect to celebrate her 84th birthday, and men their 81st. Travel 130 miles (210 kilometers) south to Petersburg, a poor, majority-black city near Richmond, and those figures plummet by 11 years for women and 14 for men. In 2010, a 50-year-old man in the poorest quintile could expect to die 13 years earlier than his counterpart in the richest, according to a report last month by the National Academies of Sciences, Engineering and Medicine. In 1980, the difference was just five years. Life expectancy for the least educated white people (education is often used as a proxy for income) has actually fallen since 1990, according to a 2012 study by the journal Health Affairs."

⁸ See, e.g., Monique Morrissey, The State of U.S. Retirement Security: Can the Middle Class Afford to Retire?, March 12, 2014, testifying before the U.S. Senate Committee on Banking, Housing and Urban Affairs Subcommittee on Economic Policy,

Why is Social Security the subject of such virulent attacks? According to Paul Krugman, “The decline of private pensions has left working Americans more reliant on Social Security than ever.... By a very wide margin, ordinary Americans want to see Social Security expanded. But by an even wider margin, Americans in the top 1 percent want to see it cut.”⁹

3. PRIVATE SECTOR RETIREMENT PLANS¹⁰

3.1 The Decline of Defined Benefit Plans

In 1974, when ERISA was enacted, the defined benefit plan still dominated the landscape. Since then, the number of defined benefit plans, and the number of participants accruing benefits under defined benefit plans, have declined sharply. According to the Employee Benefit Research Institute (EBRI), in 1974-1975 43.7% of private nonfarm wage and salary workers were participating in a defined benefit plan and there were 103,346 defined benefit plans: by 2003-2004, these numbers had declined to 16.8% and 26,000, respectively.¹¹

In 1974, it would have seemed inconceivable that iconic companies like IBM and General Electric would cease providing defined benefit plans to new employees. However, they have done so, along with other household names, including Boeing, Honda, Chrysler, General Motors, Bank of America, Disney and Anheuser Busch.¹²

As of January, 2013, the number of single employer defined benefit plans covered by the Pension Benefit Guaranty Corporation (“PBGC”) insurance program fell to 22,697, an all-time low. In 1985, PBGC insured more than 112,000 single employer plans. “Only 11 Fortune 100 companies offered traditional defined benefit plans to new employees as of June 30, down from

<http://www.epi.org/publication/morrissey-senate-panel-retirement-security/>, and stating that “Our first priority should be expanding Social Security benefits as proposed by Sen. Tom Harkin, Rep. Linda Sánchez, and others. Such measures could replace some of the benefits cut in 1983 and restore the progressivity of lifetime benefits as life expectancy grows more unequal. The Harkin-Sánchez bill would also better protect seniors and other beneficiaries from the rising cost of health care and other increases in the cost of living that erode the value of their benefits.”

⁹ Paul Krugman, *Republicans Against Retirement*, New York Times, August 17, 2015, A19.

¹⁰ This paper does not discuss public sector retirement plans or multiemployer, collectively bargained plans as, in each case, the issues are complex and an adequate discussion would take more time and space than I have available. Suffice it to say that the funding issues surrounding public sector plans, though significant, have generally been overstated. The funding problems in involving multiemployer plans have proved intractable and there is little cause for optimism that this will improve significantly in the near future.

¹¹ EBRI, *Benefit Statistics, 1974-1978-2003*, www.ebri.org. Similar declines have occurred in the U.K. and other countries. “The decline in defined benefit plans has varied considerably across countries, Defined benefit plans have declined to a greater extent in the United Kingdom and the United States than in Canada and Ireland.” John A. Turner and Gerard Hughes, *Large Declines in Defined Benefit Plans Are Not Inevitable: The Experience of Canada, Ireland, the United Kingdom, and the United States*, April, 2008, Pensions Institute Discussion Paper PI-0821, www.pensions-institute.org/.

¹² See the list of companies on the Pension Rights Center website, www.prc.org.

19 in 2009.” 19 more companies offered hybrid plans, down from 35 in 2004.¹³ In 1998, 90 percent of Fortune 100 companies offered defined benefit plans to new salaried employees.¹⁴

The percentage of workers covered by a traditional defined benefit (DB) pension plan that pays a lifetime annuity, often based on years of service and final salary, has been steadily declining over the past 25 years. From 1980 through 2008, the proportion of private wage and salary workers participating in DB pension plans fell from 38 percent to 20 percent. In contrast, the percentage of workers covered by a defined contribution (DC) pension plan—that is, an investment account established and often subsidized by employers, but owned and controlled by employees—has been increasing over time. From 1980 through 2008, the proportion of private wage and salary workers participating in only DC pension plans increased from 8 percent to 31 percent. More recently, many employers have frozen their DB plans.¹⁵

In 2011, defined benefit plans covered 67 percent of union employees but only 13 percent of nonunion workers, and covered 22 percent of full-time workers but only 8 percent of part-timers.¹⁶

Commentators have advanced many reasons for the decline of defined benefit plans. One major reason, for both large and small employers, has been the volatility and unpredictability of the required minimum contributions. Around 2000, the combination of historically low interest rates and stock market volatility caused a “perfect storm”.

Recent legislative and regulatory developments have not encouraged employers to look more kindly on defined benefit plans. The Pension Protection Act of 2006 tightened the funding requirements significantly. More recently, the budget agreement, HR 1314, signed by the President on November 2, 2015, includes the third PBGC premium hike for single employer plans since 2012. The flat rate premium increases from \$64 in 2016 to \$80 after 2018. The variable rate premium is \$30 per \$1,000 of unfunded vested benefits in 2016 and increases to \$41 in 2019.

In response to concerns that information regarding pension obligations and assets should be more useful and transparent for investors, the Financial Accounting Standards Board (FASB) changed the balance sheet rules. Under Statement of Financial Accounting Standards (SFAS) 158, “Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans,” adopted

¹³ Jerry Geisel, Number of defined benefit plans hit all-time low, *Business Insurance*, Feb. 28, 2013.

¹⁴ Jerry Geisel, Fewer Employers Offering Defined Benefit Pension Plans to New Salaried Employees, *Workplace*, October 3, 2012.

¹⁵ Barbara A. Butrica, Howard M. Iams, Karen E. Smith, and Eric J. Toder, The Disappearing Defined Benefit Pension and Its Potential Impact on the Retirement Incomes of Baby Boomers, *Social Security Bulletin*, Vol. 69, No. 3, 2009 at 1. See also William J. Wiatrowski, The last private industry pension plans: a visual essay, *Monthly Labor Review*, December 2012, pp. 3-18, stating that “In 2011, only 10 percent of all private sector establishments provided defined benefit plans, covering 18 percent of private industry employees.... 78 percent of state and local government workers had such coverage in 2011.” and noting that 35 percent of private industry workers had such coverage in the early 1990s. “Among establishments with fewer than 50 workers, 8 percent offered a defined benefit plan. In contrast, among establishments with 500 or more workers, 48 percent offered a plan.” *Id.*

¹⁶ Wiatrowski, note 15 above, at 7.

in 2006, plan sponsors must now recognize plan assets and obligations in their balance sheets. SFAS 158 made no change in the way net pension expense is included in the plan sponsor's income statement, but FASB is reviewing those rules as well.¹⁷ SFAS 158 makes balance sheets much more volatile.

3.2 Retirement Inequality

David Weil points out that

In the period from 1993 to 2010, real income grew by 13.8%. For the bottom 99% of the income distribution, the real growth rate was 6.4%, while for the top 1% the real growth rate was 58%.... Between 1979 and 2009, productivity rose by 80%. Over the same period, however, average hourly wages increased by only 7%, and average hourly compensation (wages plus benefits) increased by 8%.¹⁸

The average male worker's real earnings have declined: "The typical man with a full-time job—the one at the statistical middle of the middle—earned \$50,383 last year, the Census Bureau reported this week. The typical man with a full-time job in 1973 earned \$53,294, measured in 2014 dollars to adjust for inflation."¹⁹ According to one recent report, "Out of a total of 160.1 million full-time and part-time American workers with earnings, 115.2 million workers (72%) make less than the U.S. mean (average) income of \$54,964."²⁰

According to Harvard economist Larry Katz, "Economists differ over how much of this [wage inequality] is the result of globalization, technological change, changing social mores, and government policies, but there is no longer much dispute about the fact that inequality is increasing."²¹

Wage stagnation, unemployment, underemployment and unstable work patterns result in lower Social Security benefits and make it more difficult for individuals to save for long-term needs, such as retirement, when they are having difficulty paying their bills.²² Defined benefit plans are not inherently superior to defined contribution plans. However, they do have some characteristics that provide important safeguards to plan participants, particularly those who have lower incomes and/or are financially unsophisticated. In the private sector, defined benefit plans are almost always funded entirely by the employer and participation is automatic. Defined benefit

¹⁷ See Denise Lugo, FASB Approves Proposal on Presentation of Net Benefit Cost, BNA Pension and Benefits Reporter, Nov. 2, 2015, 42 BPR 1952.

¹⁸ Weil, note 1 above. at 281.

¹⁹ David Wessel, The typical male U.S. worker earned less in 2014 than in 1973, <http://www.brookings.edu/research/opinions/2015/09/17-male-us-worker-earned-less-in-2014-than-in-1973-wessel>.

²⁰ Chuck Vollmer, Jobonomics U.S. Unemployment Analysis, Q3 2015, Nov. 10, 2015, www.jobonomics.com.

²¹ Wessel, note 19, citing Larry Katz.

²² "Lower income employees cannot be expected to provide for the future when current income is barely adequate for a minimum standard of living." Daniel I. Halperin, Special Tax Treatment for Employer-Based Retirement Programs: Is It 'Still' Viable as a Means of Increasing Retirement Income? Should It Continue?, 49 Tax L. Rev. 1 (1993), at 14.

plans also protect individuals against investment risk, longevity risk, and cognitive risk (the risk that your assets will last longer than your wits).

Numerous studies establish that most individuals are not saving enough for retirement, including those aged 55 to 64:

Retirement savings are unequally distributed across and within income fifths. Among middle-income households, for example, only half (52 percent) had savings in these accounts in 2010. The average among all households was \$34,981, which means those with positive savings averaged around \$67,000 ($\$34,981/52$ percent). The median (50th percentile) balance in these accounts was much lower (\$23,000) than the mean, reflecting an unequal distribution of retirement savings even for middle-income households with positive balances. In 2010, households in the top income-fifth accounted for 72 percent of total savings in retirement accounts. Disparities in retirement savings, part of a larger problem of rising wealth inequality, are only partly explained by income inequality.

The trends exhibited in these figures paint a picture of increasingly inadequate savings and retirement income for successive cohorts and growing disparities by income, race, ethnicity, education, and marital status. Even women, who by some measures appear to be narrowing gaps with men (in large part because men are faring worse than they did before) are ill-served by an inefficient retirement system that shifts risk onto workers, including the risk of outliving one's retirement savings. The existence of retirement system (sic) that does not work for most workers underscores the importance of preserving and strengthening Social Security, defending defined-benefit pensions for workers who have them, and seeking solutions for those who do not.²³

In order for a 401(k) plan to provide adequate retirement savings for an employee, the employee should (1) start to contribute at the earliest possible date; (2) contribute each year, without interruption,²⁴ at least the amount required to obtain the maximum available match, and increase

²³ Natalie Sabadish and Monique Morrissey, Retirement Inequality Chartbook: How the 401(k) revolution created a few big winners and many losers, September 6, 2013, www.epi.org/publication/retirement-inequality-chartbook/. See also the studies published by, among others, the Employee Benefit Research Institute, available at www.ebri.org, and the Center for Retirement Research at Boston College, <http://crr.bc.edu/>. The Government Accountability Office found that about half of households age 55 and older have no retirement savings in a 401(k) plan or IRA. About 29 percent have neither retirement savings nor a defined benefit plan. Among the 48 percent of households with some retirement savings, the median amount is approximately \$109,000, equivalent at current rates to an inflation-protected annuity of \$405 per month for a 65-year-old. About 55 percent of households age 55-64 have less than \$25,000 in retirement savings, including 41 percent who have zero. 27 percent of this age group have neither retirement savings nor a DB plan. For the 59 percent of households age 55-64 with some retirement savings, the estimated median amount is about \$104,000. While about 15 percent of these households have retirement savings over \$500,000, 11 percent have retirement savings below \$10,000 and 24 percent have savings of less than \$25,000. GAO, Most Households Approaching Retirement Have Low Savings, GAO-15-419, May 12, 2015. For comments on the report, see Jack VanDerhei, GAO Report on Retirement Savings: Overall Gaps Identified, but the Focus of Retirement Security Reform Should be on the Uncovered Population, June 4, 2015. See also Retirement Savings Shortfalls: Evidence from EBRI's Retirement Security Projection Model, February 2015, EBRI Issue Brief #410, available at www.ebri.org, noting "the extreme importance of longevity risk and nursing home and home health care costs in simulating Retirement Savings Shortfalls."

²⁴ This is difficult for the vast majority of employees who have several jobs during their lifetimes, as each employer's plan will typically require satisfaction of a waiting period.

the rate of contributions as he or she ages; (3) consistently make good investment choices and avoid paying excessive fees;²⁵ and (4) avoid depleting the account by taking in-service distributions (e.g., for hardship) or failing to keep accumulated savings in an employer plan or IRA. After retirement, the individual must continue to manage the fund astutely for life and be able to respond to changing financial needs (e.g., for health care or long term care) and declines in cognitive ability. Where did we get the idea that this was within the capacity of every American worker?

If we assume, as we must, that 401(k) plans will continue to be the lynchpin of the private pension system in the USA for the foreseeable future, then we must increase the level of plan participation; increase the amounts contributed by employers and employees; ensure that those contributions are invested successfully; reduce the amount of pre-retirement leakage; provide more effective lifetime income options; and do all this at an acceptable cost in terms of tax incentives. In addition, simplification would help to make plans more attractive to employers and reduce the cost of compliance.

A report by the Center for Effective Government and the Institute of Policy Studies found that the 100 largest U.S. CEO retirement packages are worth \$ 4.9 billion, equal to the entire retirement savings of 41% of American families.²⁶ “In contrast, nearly half of all working age Americans do not have access to a retirement plan at work. The median 401(k) balance was \$18,433 at the end of 2013, enough to generate a \$104 monthly retirement check for life, the report said.”²⁷

Corporate executives have strong incentives to increase profits to boost stock prices (and thus the value of stock options) by reducing expenses (including workers’ wages and benefits). “And since more than half of executive compensation is tied to the company’s stock price, every dollar not spent on employee retirement security is money in the CEO’s pocket. YUM Brands former CEO David Novak is sitting on the largest retirement nest egg in the Fortune 500, with \$234 million, while hundreds of thousands of his Taco Bell, Pizza Hut, and KFC employees have no company retirement assets whatsoever.”²⁸

Past attempts to restrain executive compensation through the tax law²⁹ have not been very successful. However, there is no doubt that executives do derive substantial current economic benefits from deferring compensation, and that some attempt should be made to tax this benefit

²⁵ See, e.g., The Effects of Conflicted Investment Advice on Retirement Savings, Council of Economic Advisers, Feb. 2015; Christian E. Weller and Teresa Ghilarducci, The Inefficiencies of Existing Retirement Savings Incentives, Center for American Progress, Oct. 29, 2015; Matthew O’Brien, The Crushing Expensive Mistake Killing Your Retirement, The Atlantic, Feb. 15, 2004; John Chalmers and Jonathan Reuter, Is Conflicted Investment Advice Better Than No Advice, Sept. 24, 2015 (concluding that the answer is no).

²⁶ A Tale of Two Retirements, <http://www.foreffectivegov.org/two-retirements>.

²⁷ Meaghan Kilroy, 100 largest CEO retirement accounts equal 41% of American families' retirement savings-report, October 28, 2015, <http://www.pionline.com/article/20151028/ONLINE/151029838/100-largest-ceo-retirement-accounts-equal-41-of-american-families-retirement-savings-8212-report>.

²⁸ Kilroy, note 27 above. The percentage of executive pay represented by performance based compensation, such as stock options, has increased dramatically since the enactment of Code section 162(m), which places a \$1 million annual cap on the deductibility by public companies of compensation of “covered employees” but provides an exception for “performance-based compensation”.

²⁹ Primarily, Code sections 162(m), 280G and 409A.

currently. The basic argument for imposing special lower limits on employees of governmental and non-profit employers is that those employers do not lose a current tax deduction as the price for providing deferred compensation. Perhaps there should be annual limits on the amount deferred by an employee of any employer, even if the limit for businesses is higher than for governments and non-profits. In any event, the current regime under Code sections 409A, 457 and 457A is unnecessarily complex, and cries out for simplification.

3.3 Retirement Plan Coverage and Participation

The Bureau of Labor standards (“BLS”) found that “Retirement benefits were available to 66 percent of private industry workers in the United States in March 2015.... Employer-provided retirement benefits were available to 31 percent of private industry workers in the lowest wage category (the 10th percentile). By contrast 88 percent of workers in the highest wage category (the 90th percentile) had access to retirement benefits. In state and local government, 61 percent of workers in the lowest wage category had access to retirement benefits, compared with 98 percent of workers in the highest wage category. (See chart 1 and table 1.)”³⁰ However, because participation in 401(k) plans is voluntary, unlike most defined benefit plans, the take up rate was 74% so the actual percentage of workers who were participating was only 49%.³¹ Among full-time workers, the access and participation rates were 76% and 59%, respectively: for part-time workers, the rates were only 37% and 19%. For union workers, the access and participation rates were 92% and 82%: for non –union workers, they were only 63% and 46%.³² Firm size also had a significant effect: for firms with 1 to 99 workers, the access and participation rates were 51% and 35%: for firms with 100 or more workers they were 84% and 65%.³³

The evidence is clear: retirement plan access and participation are strongly correlated with higher incomes; full-time status; union membership; and larger employers. As discussed in section 4.1 below, the same patterns apply to employer-provided health plan access and coverage.

“Many employees who are offered a plan do not participate, generally because they do not wish to, or feel that they cannot afford to, contribute. Other workers are excluded, temporarily or permanently, by the plan’s eligibility rules: they have not completed a year of service, or are under the age of 21, work too few hours, are in an ineligible class of employees, or are classified as independent contractors. In America, we generally have a strong preference for voluntary programs rather than government mandates: however, it is unrealistic to expect that a system where employer sponsorship of a plan, employer contributions to a plan and employee contributions to a plan are all voluntary will succeed in providing adequate retirement income for most Americans, even when supplemented by Social Security.”³⁴

³⁰ BLS News Release, July 24, 2015, Employee Benefits In The United States –March 2015. www.bls.gov/ebs.

³¹ Id., Table 1.

³² Id.

³³ Id.

³⁴ David Pratt, Private Pension Reform, New York University Review of Employee Benefits and Executive Compensation, forthcoming, 2015.

Part of the problem results from unemployment and underemployment: “the low participation rates of lower-income respondents are driven primarily by weak labor force attachment and working for a firm without a pension. Only about half of the lower-income individuals are working and, among those who are working, only about 60 per-cent work for firms that offer a pension. These figures indicate serious trouble spots for participation. Eligibility and take-up rates among the lower income also help to explain their low participation, but these factors are considerably less important as both are between 85-90 percent. Of course, providing universal pension coverage in the workplace would still leave a large fraction of lower-income individuals without coverage due to their low employment rates. Thus, the only way to further expand participation would be through measures to boost employment.”³⁵

Why don't small employers offer retirement plans? According to the 2002 Small Employer Retirement Survey (SERS) (involving employers with 5 to 100 full-time workers), the most commonly cited “most important” reasons for not having a plan were: employees prefer wages and/or other benefits; revenue is too uncertain to commit to a plan; a large portion of workers are seasonal, part time or high turnover; required company contributions are too expensive; and it costs too much to set up and administer a plan.³⁶ According to a 2001 U.S. Department of Labor Working Group Report, “Significant reasons why more employers do not sponsor pension plans for any or some of their employees include: concerns over the business realities of revenues and profit; the nature of the employer’s workforce; employee preferences for cash and health insurance; the decline in unionization; the cost of setting-up and administering a plan; concerns about government regulation and liability; and a lack of information or knowledge among employers and employees.”³⁷

In February, 2012, Phyllis C. Borzi, assistant secretary of labor for the Employee Benefits Security Administration, said that unless pensions and retirement savings plans are more attractive to employers, efforts to expand coverage and participation will fall short of what is necessary.³⁸ One recent study noted that “Legal reforms now offer employers tax credits for sponsoring a plan, special plans with little or no discrimination tests like the auto-enrollment safe harbor 401(k) plan, and reduced fiduciary liability through participant investment discretion and the use of Qualified Default Investment Alternatives as investment options. Yet there has been no appreciable increase in the percentage of employers, particularly small to mid-size employers, willing to offer plans.”³⁹

Under a defined benefit (DB) plan, employees are automatically enrolled and (in the private sector) rarely have to contribute. With most DC plans, the majority of which are now 401(k)-type plans, workers are responsible for their own financial security. Barbara Butrica and her coauthors wrote that if plans don't “include automatic features, workers have to actively decide to participate, how much to contribute, which investments to put their money in, and how to

³⁵ April Yanyuan Wu, Matthew S. Rutledge, and Jacob Penglase, Why Don't Lower-Income Individuals Have Pensions?, Center for Retirement Research, April 2014.

³⁶ 2002 Small Employer Retirement Survey, Summary of Findings, www.ebri.org.

³⁷ U.S. Department of Labor, Report of the Working Group on Increasing Pension Coverage, Participation and Benefits, November 13, 2001.

³⁸ BNA Pension & Benefits Reporter, 39 BPR 396, Feb. 28, 2012.

³⁹ C. Eugene Steuerle, Benjamin H. Harris and Pamela J. Perun, Entitlement Reform and the Future of Pensions, September 2014, PRC WP2014-08, Pension Research Council.

manage their benefits through retirement.”⁴⁰ Consequently, in 2013 the participation rates of “private wage-and-salary workers who were offered an employer retirement plan were 87 percent in defined benefit pensions but only 71 percent in DC plans.” DC plans with automatic enrollment features, in which employees must opt out of participating in the plan instead of affirmatively enrolling, see higher participation rates, around 80 percent or more.⁴¹

Ideally, employees would begin to save for retirement as soon as they enter the workforce and contribute continuously throughout their working lives. The current eligibility rules impede that goal:

A plan may require the completion of a year of service before an employee is eligible. Most workers have several jobs during their lives, and thus have to satisfy several separate waiting periods during which they are not covered by a plan.

A plan may exclude permanently workers who are part time, are in an ineligible job category or are not classified as employees of the sponsoring employer.

The administration’s 2016 budget proposal would require retirement plans to allow long-term part-time workers to participate, by permitting an employee to make salary reduction contributions if the employee has worked at least 500 hours per year with the employer for at least three consecutive years. The proposal would not require them to receive any employer contributions. The proposal would also require a plan to credit, for each year in which such an employee worked at least 500 hours, a year of service for purposes of vesting. With respect to employees newly covered under the proposed change, employers would receive nondiscrimination testing relief (similar to current-law relief for plans covering otherwise excludable employees), including permission to exclude these employees from top-heavy vesting and benefit requirements.⁴²

“This proposal is a start, but it does not go far enough. The one year waiting period should be reduced to no more than 90 days (the permissible waiting period for health plan coverage under the Affordable Care Act); part-time employees should be covered; and the ability of employers to exclude classes of employees (other than union employees and non-resident aliens) should be severely curtailed, possibly by increasing the 70% coverage threshold.”⁴³

The Obama administration is monitoring the automatic enrollment strategies being adopted in other countries: “Mark Iwry, the Treasury Department’s deputy assistant secretary for retirement and health policy, recently told a conference audience that “the administration is monitoring retirement innovations around the globe and is particularly interested in the approach being developed in the U.K. In October 2012, the U.K. launched a broad retirement savings initiative, which included the creation of a low-cost savings platform known as the National Employment

⁴⁰ Barbara A. Butrica et al., “Flattening Tax Incentives for Retirement,” Urban-Brookings Tax Policy Center (June 30, 2014), available at <http://www.brookings.edu>.

⁴¹ Harris et al., “Tax Subsidies for Asset Development: An Overview and Distributional Analysis,” at 13 (the Urban Institute, 2014), available at <http://www.taxpolicycenter.org>.

⁴² General Explanations of the Administration’s Fiscal Year 2016 Revenue Proposals (the “Green Book”), pp. 140-141.

⁴³ Pratt, note 34 above; Code section 410(b).

Savings Trust (NEST). By statute, all employers in the U.K. must automatically enroll eligible employees in an approved retirement savings system, a NEST product, or a traditional pension and make annual contributions. Iwry conceded that the administration's myRA program—launched nationwide Nov. 4 (see related article in this issue)—is modest compared with the U.K. model. Unlike the U.K. model, the myRA program doesn't require employers to make contributions to the accounts.”⁴⁴

In addition to the myRA program, there is a push to enable States to enact coverage expansion laws that would not be preempted by ERISA. DOL issued a proposed rule on November 18, 2015.⁴⁵

4 HEALTH PLANS

4.1 Introduction

The patterns of health plan coverage are similar to those of retirement plan coverage: large employers are significantly more likely to offer coverage to at least some of their employees; coverage is also closely correlated with higher income, union membership and full-time rather than part-time status. There are two additional factors. First, the cost of health coverage has increased for many years at a rate significantly higher than the general inflation rate, putting increased financial strain on both employers and employees. “Health care costs at current levels override the incentives that have historically supported employer-based health insurance. Now that health costs loom so large, companies that provide generous benefits are in effect paying some of their workers much more than the going wage—or, more to the point, more than competitors pay similar workers. Inevitably, this creates pressure to reduce or eliminate health benefits. And companies that can't cut benefits enough to stay competitive—such as GM—find their very existence at risk.”⁴⁶

Second, the Affordable Care Act, while improving access and coverage generally, caused employers to question whether they should continue to offer coverage. The most recent evidence is encouraging: “While Mercer's surveys have consistently shown that large employers remain committed to offering health coverage, in the early days of the health reform debate sizable numbers of small employers thought it was likely that they would drop their plans and send employees to the public exchange. In 2013, 21% of employers with 50-499 employees said they were likely to drop their plans within the next five years; this number fell to 15% in 2014 and to

⁴⁴ Michael J. Bologna, Administration Looks to U.K. for Retirement Savings Model, *Pension & Benefits Daily* (BNA), Nov. 4, 2015.

⁴⁵ 80 Fed. Reg. 72,006, Nov. 18, 2015. See also the DOL Fact Sheet, State Savings Programs for Non-Governmental Employees, Nov. 16, 2015, available at www.dol.gov/ebsa/newsroom/.

⁴⁶ Paul Krugman & Robin Wells, *The Health Care Crisis and What To Do About It*, *The N.Y. Review of Books* 38, 39 (Mar. 23, 2006) (reviewing Henry J. Aaron et al., *Can We Say No?* (2005), Julius Richmond & Rashi Fein, *The Health Care Mess* (2006), John F. Cogan, et al., *Healthy, Wealthy, and Wise* (2005)).

just 7% this year. Among employers with 500 or more employees, just 5% say they are likely to drop their plans, essentially unchanged from 4% last year.”⁴⁷

4.2 Access and Coverage

In March, 2015, according to BLS, “For private industry, 87 percent of workers in management, professional, and related occupations had access to medical care, compared with 41 percent in service occupations. In state and local government, the corresponding figures were 89 percent and 82 percent, respectively. (See table 2.) For civilian workers, access rates to medical care ranged from 53 percent for the smallest establishments (those with fewer than 50 workers) to 90 percent for the largest establishments (those employing 500 workers or more).... Access to medical care benefits for private industry workers was 86 percent in goods-producing industries, compared with 66 percent for workers in service-providing industries.”⁴⁸

Health benefits were available to 86% of full-time private sector workers but only 21% of part-time private sector workers: the participation rates were 64% and 12%.⁴⁹ The access and participation rates for union workers were 95% and 79%, compared to 67% and 47% for non-union workers. The access rates for workers in the lowest 25% and the lowest 10% of average wages were only 34% and 23%, and the participation rates were 20% and 11%.⁵⁰ Private sector employers with fewer than 50 employees offered coverage to 53% of their workers and 38% participated. For firms with 100 or more employees, the rates were 84% and 62%.⁵¹

Most plans impose a waiting period, and in 2015 the average waiting period is 2 months. “Before eligible employees may enroll, almost three-quarters (74%) of covered workers face a waiting period, although the average length of waiting periods for covered workers with waiting periods has decreased in each of the last two years.”⁵²

These coverage patterns matter because of the large number of part-time and other contingent workers; the continuing decline in, and state level attacks on, union membership; and the large number of workers who work for small employers or other firms that are at or near the bottom of the fissured workplace pyramid described by David Weil.

⁴⁷ Mercer, *With the Excise Tax in their Sights, Employers Hold Health Benefits Cost Growth to 3.8% in 2015*, Nov. 19, 2015, available at www.mercer.com/newsroom, discussing the Mercer National Survey of Employer-Sponsored Health Plans.

⁴⁸ Bureau of Labor Standards, News Release, *Employee Benefits in the United States-March, 2015*, www.bls.gov/ebs.

⁴⁹ *Id.* See also Kaiser Family Foundation, *2015 Employer Health Benefits Survey, Section 2*: “Among firms offering health benefits, relatively few offer benefits to their part-time and temporary workers.... In 2015, 19% of all firms that offer health benefits offer them to part-time workers (Exhibit 2.6). Firms with 200 or more workers are more likely to offer health benefits to part-time employees than firms with 3 to 199 workers (35% vs. 18%) (Exhibit 2.9). Among firms offering health benefits to at least some employees, relatively few report that they stopped offering benefits to part-time workers in the last year (2%) (Exhibit 2.7). A small percentage (3%) of firms offering health benefits offer them to temporary workers (Exhibit 2.8). More large firms (200 or more workers) offering health benefits elect to offer temporary workers coverage than small firms (11% vs. 3%) (Exhibit 2.10).”

⁵⁰ BLS, note 48, Table 2.

⁵¹ *Id.*

⁵² Kaiser Family Foundation, note 49, Section 3.

4.3 Employee Costs for Health Insurance Coverage

According to BLS, “The share of premiums workers were required to pay for their medical coverage [in March, 2015] varied by bargaining status. Private industry nonunion workers were responsible for 23 percent of the total single coverage medical premium, whereas the share of premiums for union workers was 13 percent. The share of premiums for family coverage was 35 percent for nonunion workers and 16 percent for union workers. (See chart 2 and tables 3 and 4.).... The employee share of family medical premiums was 27 percent for workers in goods-producing industries and 33 percent for workers in service-providing industries. (See tables 2 and 4.)”⁵³

The share of the premium paid by the worker also varied by full-time or part-time status (21% for full-timers, 27% for part-timers) and by average wages (20% for the highest paid 10% but 30% for the lowest paid 10%).⁵⁴

For family coverage, employers paid 68% of the premium for full-time workers, and 63% for part-timers; 84% for union workers and 65% for non-union workers; 72% for the 10% of workers with the highest average wages and 57% for the 10% with the lowest wages. Firms with 500 or more workers paid 76% of the family premium; firms with fewer than 50 employees paid 62%.⁵⁵

According to the Kaiser Family Foundation 2015 Employer Health Benefits Survey,⁵⁶ “Annual premiums for employer-sponsored family health coverage reached \$17,545 this year, up 4 percent from last year, with workers paying on average \$4,955 towards the cost of their coverage. Employer-sponsored insurance covers over half of the non-elderly population, 147 million people in total. The average annual single coverage premium is \$6,251.”

With respect to responses to the ACA, “Relatively small percentages of employers with 50 or more full-time equivalent employees reported switching full-time employees to part time status (4%), changing part-time workers to full-time workers (10%), reducing the number of full-time employees they intended to hire (5%) or increasing waiting periods (2%) in response to the employer shared responsibility provision which took effect for some firms this year.”⁵⁷

Between 2005 and 2015, “total premiums for family coverage increased by 61%. The worker contribution increased by 83% and the employer contribution by 54%. As with total premiums, the share of the premium contributed by workers varies considerably.... the average annual premium contributions in 2015 are \$1,071 for single coverage and \$4,955 for family coverage.”⁵⁸

⁵³ BLS, note 48 above.

⁵⁴ Id., Table 3.

⁵⁵ Id., Table 4.

⁵⁶ Kaiser Family Foundation 2015 Employer Health Benefits Survey, Sep. 22, 2015, www.kff.org, Summary of Findings.

⁵⁷ Id.

⁵⁸ Id. See also Exhibit 1.12 Average Annual Premiums for Covered Workers with Family Coverage, by Firm Size, 1999-2005

There has been a significant increase in participation in high deductible plans. “Almost a quarter (24%) of covered workers are enrolled in HDHP/SOs in 2015; enrollment in these plans has increased over time from 13% of covered workers in 2010.”⁵⁹ This trend raises policy concerns, particularly with respect to lower income workers. “Enrollment in HDHP/SOs is higher for covered workers employed at firms with many low-wage workers (at least 35% of workers earn \$23,000 per year or less) than firms with fewer low-wage workers.”⁶⁰ This suggests that at least some workers are enrolling in high deductible plans because their share of the premium is less than it would be under another type of plan. “The average worker contribution in HDHP/SOs is lower than the overall average worker contributions for single coverage (\$868 vs. \$1,071) and family coverage (\$3,917 vs. \$4,955) (Exhibit 6.5).”⁶¹ However, these individuals may incur much higher out of pocket medical expenses. “The average annual out-of-pocket maximum for single coverage is \$3,866 for HDHP/HRAs and \$4,085 for HSA-qualified HDHPs (Exhibit 8.7).”⁶²

Not surprisingly, “The cost of health insurance remains the primary reason cited by firms for not offering health benefits. Among small firms (3-199 workers) not offering health benefits, 41% cite high cost as “the most important reason” for not doing so, followed by “employees are generally covered under another plan” (26%) (Exhibit 2.14). Relatively few employers indicate that they did not offer because they believe that employees will get a better deal on the health insurance exchanges (4%).”⁶³

4.4 Retiree Health Benefits

Retiree health benefits are an important part of retirement security in view of the substantial, and increasing, out of pocket medical costs incurred by the elderly, including Medicare premiums, deductibles and co-payments. According to EBRI, “In 2015, a 65-year-old man needs \$68,000 in savings and a 65-year-old woman needs \$89,000 if each has a goal of having a 50 percent chance of having enough money saved to cover health care expenses in retirement. If either instead wants a 90 percent chance of having enough savings, \$124,000 is needed for a man and \$140,000 is needed for a woman. This analysis does not factor in the savings needed to cover long-term care expenses. Savings targets increased between 6 percent and 21 percent between 2014 and 2015. For a married couple both with drug expenses at the 90th percentile throughout retirement who want a 90 percent chance of having enough money saved for health care

	All Small Firms (3-199 Workers)	All Large Firms (200 or More Workers)
1999	\$5,683	\$5,845
2005	\$10,587	\$11,025
2014	\$15,849	\$17,265
2015	\$16,625	\$17,938

⁵⁹ Id. See also Mercer Signal, 2015 A Milestone Year for Consumer-Directed Health Plans, Dec. 2, 2015, www.ushealthnews.mercer.com.

⁶⁰ Id., Section 5.

⁶¹ Id., Section 6.

⁶² Id., Section 8.

⁶³ Id., Section 2.

expenses in retirement by age 65, targeted savings increased from \$326,000 in 2014 to \$392,000 in 2015.”⁶⁴

According to the Kaiser Family Foundation, “Twenty-three percent of large firms that offer health benefits in 2015 also offer retiree health benefits, similar to the percentage in 2014 (25%). Among large firms that offer retiree health benefits, 92% offer health benefits to early retirees (workers retiring before age 65), 73% offer health benefits to Medicare-age retirees, and 2% offer a plan that covers only prescription drugs. Employers offering retiree benefits report interest in new ways of delivering them. Among large firms offering retiree benefits, seven percent offer them through a private exchange and 26% are considering changing the way they offer retiree coverage because of the new health insurance exchanges established by the ACA....There has been a downward trend in the percentage of firms offering retirees coverage, from 34% in 2006 and 66% in 1988 (Exhibit 11.1).... Large firms with at least some union workers are more likely to offer retiree health benefits than large firms without any union workers (37% vs. 18%) (Exhibit 11.3).”⁶⁵

4.5 The “Cadillac” Tax

Beginning in 2020, employer health plans will be assessed a non-deductible 40% excise tax on the value of the total cost of their plans, on a per-employee basis, above indexed dollar thresholds. [Note that, since this paper was written, the effective date was postponed from 2018 to 2020 by the Consolidated Appropriations Act, enacted on December 18, 2015] The total cost includes any FSA contributions made by the employee on a salary reduction basis, premium costs, and employer HRA contributions. Some employers have already begun making changes to their health benefits. “Among firms who have conducted an analysis to determine their liability under the high-cost plan tax, 12% believe their plan with the largest enrollment will exceed the thresholds in 2018 (Exhibit 14.14). Some employers have already taken action to mitigate the anticipated impacts of the high-plan excise tax; 13% of large firms (200 or more employers) and 7% of small firms have made changes to their plans’ coverage or cost sharing to avoid exceeding the limits. Eight percent of both large and small firms have switched to a lower cost plan. Looking at firms that took one of these two actions, 11% of small firms (3-199 workers) and 16% of large firms reported either changing their plan or switching carriers to reduce the cost of their plan in anticipation of the assessment. Among large firms (200 or more workers) who indicated changing their plan or switching carriers to reduce the cost of their plan, 64% have increased cost sharing, 10% have reduced the scope of covered services, 34% have moved benefit options to account-based plans such as an HRA or HSA, 18% have increased incentives to use less costly providers, and 16% have considered offering health insurance through a private exchange in anticipation of the excise tax (Exhibit 14.15).”⁶⁶

5 WHO IS AN “EMPLOYEE” OR “EMPLOYER”?

⁶⁴ EBRI Notes, Oct. 2015, Amount of Savings Needed for Health Expenses for People Eligible for Medicare: Unlike the Last Few Years, the News Is Not Good, www.ebri.org.

⁶⁵ Kaiser Family Foundation, 2015 Employer Health Benefits Survey, section 11, www.kff.org.

⁶⁶ Id. Section 14.

Amazingly, for a system that revolves around identifying employers, employees, and employee benefit plans, the fundamental definitions are woefully inadequate, and have become more so over time as workplace conditions have changed dramatically since ERISA was enacted in 1974. Under ERISA, “The term ‘employer’ means any person acting directly as an employer, or indirectly in the interest of an employer, in relation to an employee benefit plan, and includes a group or association of employers acting for an employer in such capacity.”⁶⁷ The definition of ‘employee’ is equally unilluminating: “The term ‘employee’ means any individual employed by an employer”.⁶⁸ As David Weil has written, “A positive path forward requires revisions of existing workplace laws so that they adequately recognize the far more complex nature of the modern workplace and the growing presence of multiple organizations with roles in employment decisions.”⁶⁹

In its most recent ERISA decision directly addressing this issue, which itself is more than 20 years old, the Supreme Court pointed out that the ERISA definition of employee “is completely circular and explains nothing.”⁷⁰ The Court decided unanimously to “adopt a common-law test for determining who qualifies as an ‘employee’ under [ERISA].” The Court relied on its earlier opinion in a case interpreting the term “employee” as used in the Copyright Act of 1976, identifying “the hiring party’s right to control the manner and means by which the product is accomplished” as the proper test, and listing factors that bear on whether the purported employer exercised sufficient control to make the other party an employee.⁷¹

Although the Court’s decision is supported by precedent,⁷² relying on a test that dates back to 18th century master and servant rules, intended primarily to determine when the master was

⁶⁷ ERISA section 3(5).

⁶⁸ ERISA section 3(6).

⁶⁹ Weil, note 1 above, at 289. He has also pointed out that “Defining who is the employer and who is the employee turns out to be a far less straightforward task than one might imagine. The definitions differ across federal, state, and common law. Federal workplace statutes (the focus of this discussion) do not use a single definition, but rather multiple ones, from fairly expansive definitions that acknowledge the range of relationships that may actually arise in the workplace (as in the Fair Labor Standards Act [FLSA]) to narrow descriptions built around the archetypical large employer (think General Motors) with thousands of employees (as in the National Labor Relations Act [NLRA]). . . . For many decades following passage of the FLSA and other federal statutes, subtle differences in definitions of employment were less consequential for much of the economy: it was relatively clear who the employer and the employee were, just as were the boundaries of the firm. The more the work place has fissured, the more the subtleties raised by definitions of employment matter.” Weil, note 1 above, at 184-185.

⁷⁰ *Nationwide Mutual Ins. Co. v. Darden*, 503 U.S. 318 (1992).

⁷¹ *Community for Creative Non Violence v. Reid*, 490 U.S. 730 (1989).

⁷² In *Darden*, the United States Court of Appeals for the Fourth Circuit observed that “Darden most probably would not qualify as an employee” under traditional principles of agency law but found the traditional definition inconsistent with the “declared policy and purpose” of ERISA. The Supreme Court said that “In taking its different tack, the Court of Appeals cited *NLRB v. Hearst Publications, Inc.*, 322 U.S. at 120-129, and *United States v. Silk*, 331 U.S. at 713, for the proposition that “the content of the term ‘employee’ in the context of a particular federal statute is ‘to be construed “in the light of the mischief to be corrected and the end to be attained.”’” *Darden*, 796 F.2d at 706, quoting *Silk*, *supra*, at 713, in turn quoting *Hearst*, *supra*, at 124. But *Hearst* and *Silk*, which interpreted “employee” for purposes of the National Labor Relations Act and Social Security Act, respectively, are feeble precedents for unmooring the term from the common law. In each case, the Court read “employee,” which neither statute helpfully defined, to imply something broader than the common-law definition; after each opinion, Congress amended the statute so construed to demonstrate that the usual common-law principles were the keys to meaning. See *United Ins. Co.*, *supra*, at 256 (“Congressional reaction to [*Hearst*] was adverse and Congress passed an amendment . . . the obvious purpose of [which] “as to have the . . . courts apply general agency principles in

responsible for acts of the servant, makes no sense in interpreting employment legislation in the 21st century.⁷³

Darden also involved an issue simpler than most that arise in this area: it was clear that the key relationship was between Darden and Nationwide, so the only question was whether he was an employee or an independent contractor. In today's workplace, there are often several different entities with some control over the worker. The question is which one or more of them should be responsible for complying with labor and employment laws, and the answer is not necessarily the entity that gives the worker a W 2 or 1099 tax form.

Other countries have recognized that not all service-provider/service-recipient relationships fit neatly within the traditional employee/independent contractor dichotomy by establishing a third category, a dependent contractor, who receives some of the protections afforded to employees.⁷⁴

The drafters of ERISA recognized that the minimum coverage and nondiscrimination rules for qualified retirement plans could easily be circumvented by splitting employees among a number of employers related by common ownership. ERISA and subsequent legislation broadened the employee group that must be taken into account, by enacting the controlled group, affiliated service group and leased employee rules, and giving the Treasury Department broad regulatory authority to prevent the avoidance of employee benefit requirements through the use of separate organizations, employee leasing or other arrangements.⁷⁵ It is time for these anti-avoidance concepts to be broadened, to reflect the realities of the 21st century economy in which control can be exercised without common ownership.

6 WORKER (MIS)CLASSIFICATION

distinguishing between employees and independent contractors under the Act"); Social Security Act of 1948, ch. 468, § 1(a), 62 Stat. 438 (1948) (amending statute to provide that term "employee" "does not include . . . any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an independent contractor") (emphasis added); see also *United States v. W. M. Webb, Inc.*, 397 U.S. 179, 183-188, 25 L. Ed. 2d 207, 90 S. Ct. 850 (1970) (discussing congressional reaction to *Silk*).... To be sure, Congress did not, strictly speaking, "overrule" our interpretation of those statutes, since the Constitution invests the Judiciary, not the Legislature, with the final power to construe the law. But a principle of statutory construction can endure just so many legislative revisitations, and Reid's presumption that Congress means an agency law definition for "employee" unless it clearly indicates otherwise signaled our abandonment of *Silk*'s emphasis on construing that term "in the light of the mischief to be corrected and the end to be attained." *Silk*, supra, at 713, quoting *Hearst*, supra, at 124. The definition of "employee" in the FLSA evidently derives from the child labor statutes, see *Rutherford Food*, supra, at 728, and, on its face, goes beyond its ERISA counterpart. While the FLSA, like ERISA, defines an "employee" to include "any individual employed by an employer," it defines the verb "employ" expansively to mean "suffer or permit to work." 52 Stat. 1060, § 3, codified at 29 U. S. C. §§ 203(e), (g). This latter definition, whose striking breadth we have previously noted, *Rutherford Food*, supra, at 728, stretches the meaning of "employee" to cover some parties who might not qualify as such under a strict application of traditional agency law principles. ERISA lacks any such provision, however, and the textual asymmetry between the two statutes precludes reliance on FLSA cases when construing ERISA's concept of "employee."

⁷³ Second 220 of the Restatement of the Law, Second, Agency, cited by the Court in *Darden*, is part of Chapter 7, Liability of Principal to Third Person; Torts.

⁷⁴ See also NLRB Member Wilma B. Liebman's dissent in *St. Joseph News-Press and Teamsters Union Local 460*, National Labor Relations Board, 345 N.L.R.B. 474 (2005), where she argued that the newspaper's substantial economic advantage over carriers resulted in a relationship of economic dependence on the newspaper, and was persuasive evidence that the carriers were employees, not independent contractors.

⁷⁵ Code sections 414(b), (c), (m), (n), (o) and (t). See also the separate line of business rules under section 414(r).

Subject to special rules for statutorily defined “leased employees,”⁷⁶ an employer who allows individuals other than employees or owners (e.g., partners in the employer) to participate in a qualified retirement plan would jeopardize the plan’s qualification, as a plan is required to be for the exclusive benefit of the employees or their beneficiaries.⁷⁷ This issue has two separate aspects: misclassification of workers, and whether it would be feasible to allow participation by other individuals within the present framework, which is based on the assumption that all participants will either be employees or owners of the business.

Worker misclassification has been a serious issue for many years. Employers have an incentive to classify workers as independent contractors, not only to avoid providing retirement and other benefits, but also to avoid having to pay Social Security taxes, unemployment compensation premiums and worker’s compensation premiums.⁷⁸ “It is common for employers to inaccurately and illegally declare employees to be contractors. A 2000 study by the U.S. Department of Labor, for instance, found that 10–30 percent of audited employers misclassified workers.... In many states, there is no mechanism for workers to challenge their bosses’ designation except for filing unemployment or workers’ compensation claims—meaning one must be fired or injured before there is any legal avenue for contesting one’s status.... In some industries, misclassification has become so commonplace that well-meaning employers are under pressure to wrongly classify their employees in order to not be undercut by less ethical competitors.... At the federal level, a 2009 report from the Government Accountability Office estimated that misclassification costs the federal government nearly \$3 billion per year.”⁷⁹ Françoise Carre notes that “Numerous state-level studies show that between 10 and 20 percent of employers misclassify at least one worker as an independent contractor.”⁸⁰

This results in a large loss of income and employment tax revenue. The misclassified employees typically do not pay the full self-employment taxes and are wrongly left uninsured or underinsured, without benefits and without job security.⁸¹

⁷⁶ Under IRC § 414(n), a “leased employee” who performs services for any person (the “recipient”) pursuant to an agreement between the recipient and any other person (the “leasing organization”) is treated for certain purposes, including discrimination testing, as an employee of the recipient. A “leased employee” is defined as any person who provides services to the recipient but who is not an employee of the recipient, if such services (1) have been performed on a substantially fulltime basis for a period of at least one year, and (2) are performed “under primary direction or control by the recipient.” There is a limited safe harbor exception for leased employees who are covered by a sufficiently generous money purchase pension plan of the leasing organization, provided that leased employees do not constitute more than 20 percent of the recipient’s nonhighly compensated work force. IRC § 414(n)(5).

⁷⁷ Code section 401(a).

⁷⁸ “Unfortunately, current tax, labor and employment law gives employers and employees incentives to create contingent relationships not for the sake of flexibility or efficiency but in order to evade their legal obligations. For example, an employer and a worker may see advantages wholly unrelated to efficiency or flexibility in treating the worker as an independent contractor rather than an employee. The employer will not have to make contributions to Social Security, unemployment insurance, workers’ compensation, and health insurance, will save the administrative expense of withholding, and will be relieved of responsibility to the worker under labor and employment laws. The worker will lose the protection of those laws and benefits and the employer’s contribution to Social Security, but may accept the arrangement nonetheless because it gives him or her an opportunity for immediate and even illegitimate financial gains through underpayment of taxes. Many low-wage workers have no practical choice in the matter.” DOL, Contingent Workers, www.dol.gov/_sec/media/reports/dunlop/section5.htm.

⁷⁹ Weil, note 1 above, at 212-215.

⁸⁰ Françoise Carré, (In)dependent Contractor Misclassification, June 8, 2015 <http://www.epi.org/publication/independent-contractor-misclassification/>.

IRS enforcement has been hampered by section 530 of the Revenue Act of 1978, which allows a service recipient to treat a worker as an independent contractor for employment tax purposes, even though the worker may be an employee under the common law rules, if the service recipient has a reasonable basis for so doing and certain other requirements are met. If a service recipient meets these requirements, the IRS is prohibited from reclassifying the worker as an employee. The classification may continue indefinitely, even if it is incorrect. This section also prohibits the IRS from issuing generally applicable guidance addressing worker classification.

The administration's 2016 budget proposal would allow the IRS to require prospective reclassification of workers who are misclassified.⁸² Treasury and the IRS also would be permitted to issue generally applicable guidance on the proper classification of workers under common law standards. Service recipients would be required to give notice to independent contractors, when they first begin performing services for the service recipient, that explains how they will be classified and the consequences. The IRS would be permitted to disclose to the Department of Labor information about service recipients whose workers are reclassified.

7 WHO IS THE EMPLOYER IN THE FISSURED WORKPLACE?

It is time for a detailed review of the affiliated service group and leased employee rules. Also, if the separate line of business rules are to be retained, the Treasury and the IRS should issue new, more workable regulations that take into account changes in business organization and structure over the last 30 years. The affiliated service group and leased employee rules were enacted in the early 1980s to address specific, and relatively narrow, abuses. Both provisions are far broader than is required to deal with the abuse, guidance is sparse, and the regulations do not address recent developments in the workplace. A detailed review of these rules is long overdue.

Congress enacted the separate line of business ("SLOB") rules in 1986 to provide relief for organizations that, while connected by common ownership, were in fact separate. The regulations add highly detailed and restrictive requirements that make the SLOB rules available to only very few employers. IRS should issue new, more workable regulations

A major problem today is the opposite situation: organizations that are not connected by common ownership, but are not truly separate (e.g., many franchisor-franchisee relationships).⁸³

Many of the industries in which fissured workplaces are common (e.g., as a result of franchising or supply chain management) "account for a disproportionate share of low-wage workers. For example, while food services and drinking places employed about 6.4% of the workforce, it comprised about 12.4% of all low-wage workers in 2010; retail workers comprised 10.2% of the workforce but 18.9% of low-wage workers; and the roughly 1.8 million workers in the hotel and motel industry accounted for 1.2% of employment but twice that percentage of low-wage workers."⁸⁴

⁸¹ Id.

⁸² Green Book, pp. 223 et seq.

⁸³ See Weil, note 1 above, passim.

⁸⁴ Id. at 269-270.

Weil points out that the definition of “employee” under the Fair Labor Standards Act (FLSA) is broader than under other federal statutes, such as ERISA: “The FLSA defines an employee as “any individual who is employed by an employer” and that “employer includes to suffer or permit to work.” This obscure phrase offers the broadest definition of “employee” of any federal statute. It goes beyond the definition offered by common law focus on the degree of actual control of the employee. Instead, courts have noted that the phrase “to suffer or permit” implies that even broad knowledge of work being done on an employer’s behalf is sufficient to establish a relationship. Given the wide latitude implied by this definition, courts have applied an economic realities test to evaluate the particular economic situation surrounding a worker and his or her employer or employers. The broad definition of “employer” under the FLSA (and under most state minimum wage laws) provides the potential for interpretations that capture the complexities of the fissured workplace even though courts have historically tended to hew to relatively narrow definitions of employment.”⁸⁵

As Weil argues, “Reform of existing workplace legislation and new policy initiatives could broaden the responsibility of lead organizations in the realm of employment so that it is consistent with the roles played in their other relationships with subordinate businesses. The principle here is one of parallelism: if a company exerts minute control over aspects of quality, production, and delivery of services, that control should extend more fully to the domain of employment as well those aspects of business that are directly valuable to the company.”⁸⁶

A similar argument is made by Matthew Bodie: “The critical insight is that employment is defined not by control, but by participation-participation in team production. Although the notion of control has dominated the common law test, most of the other factors in that test reflect the degree of participation in the enterprise. Within the common boundaries of the firm, employers have an obligation to pay minimum wage and overtime; provide family and medical leave; avoid discrimination; bargain with collective representatives; adhere to certain requirements as to retirement and health care benefits; and provide insurance in case of unemployment.... Employers have the responsibility to provide these things because employees are participants in the employer’s common enterprise.... Team production justifies obligations from the team to the individual Members.”⁸⁷

8 THE CONTINGENT WORKFORCE

A recent issue of *Jobonomics* reports that, as reported by the BLS, contingent workers represent 29% of the U.S. workforce and notes that “Another alarming trend involves the dramatic rise in the contingent workforce. The BLS defines the contingent workforce as the portion of the labor force that has “nonstandard work arrangements” or those without “permanent jobs with a traditional employer-employee relationship”. The contingent workforce is comprised of two general categories: core and non-core. Core contingency workers include agency temps, direct-hire temps, on-call laborers and contract workers. Core contingency workers generally represent low wage earners that have nonstandard work arrangements out of necessity. These workers are

⁸⁵ *Id.*, at 184.

⁸⁶ Weil, note 1 above, at 205.

⁸⁷ Matthew T. Bodie, *Participation as a Theory of Employment*, 89 *Notre Dame L. Rev.* 661 (2013).

often subjected to exploitation and are usually not entitled to traditional employer-provided retirement and health benefits. The non-core category includes independent contractors, self-employed workers and standard part-time workers who work fewer than 35 hours per week. Non-core workers generally seek nonstandard work agreements as a matter of choice. Jobenomics views the non-core workforce as a positive economic force that will grow significantly via the emerging digital economy. On the other hand, Jobenomics views the core contingency as a major challenge as more and more citizens work for substandard wages, become frustrated, and seek alternative ways of income.”⁸⁸

Anthony Atkinson notes that “In the twentieth century, employment in OECD countries was largely characterised by regular jobs, but the twenty-first century is witnessing a significant return to what is now regarded as nonstandard employment. Part-time work is the most common.... The McKinsey Global Institute 2012 paper *Help Wanted: The Future of Work in Advanced Economies* found that "managing employees and contract workers across the Internet, companies now have the ability to make labor more of a variable cost, rather than a fixed one, by engaging workers on an as-needed basis. Across the OECD... nations, part-time and temporary employment among prime-age workers has risen 1.5 to 2 times as fast as total employment since 1990.... In our own surveys of US employers, more than one third say they plan to increase use of contingent labor and part-time workers in the years ahead.... It is therefore increasingly misleading to talk in terms of people having, or not having, a job. Work is not simply a (0,1) activity. The twenty-first century labour market is more complex, and this has implications for how we think about employment as a route out of poverty and full employment as a means of assisting us on the way to less inequality.”⁸⁹

More than five million Americans are working part-time for economic reasons. This is down from a peak of over 9 million but is much greater than the 4 million in 2006.⁹⁰ “About 31% of workers worked in contingent employment situations in 2005, if one characterizes contingent workers as those not employed in standard, full-time settings.... The number of workers classified as independent contractors grew from 8.3 million to 10.3 million, and also increased as a percentage of total employment, from 6.7% to 7.4%.”⁹¹

In a recent report, the General Accountability Office (GAO) pointed out that “The size of the contingent workforce as a proportion of the total U.S. employed labor force can range widely, depending on how it is defined.”⁹²

GAO found that “Contingent work can be unstable, or may afford fewer worker protections than standard work, depending on a worker’s particular employment arrangement. As a result, contingent work tends to lead to lower earnings, fewer benefits (such as retirement plans and health insurance), and a greater reliance on public assistance. Accounting for other factors that

⁸⁸ Chuck Vollmer, *Jobenomics U.S. Unemployment Analysis*, Q3 2015, Nov. 10, 2015, www.jobenomics.com.

⁸⁹ Anthony B. Atkinson, *Inequality: What Can Be Done?* Harvard, 2015, at 135-137.

⁹⁰ Bureau of Labor Statistics, *Employment Level- Part-Time for Economic Reasons, All Industries (2015)*; Bureau of Labor Statistics, Table A-8, *Employed Persons by Class of Worker and Part-Time Status*, Economic News Release, March 6, 2015.

⁹¹ Weil, note 1, at 272-273.

⁹² *Contingent Workforce: Size, Characteristics, Earnings, and Benefits*, GAO-15-168R: Published: Apr 20, 2015. Publicly Released: May 20, 2015.

affect earnings, contingent workers earn less than standard workers on an hourly, weekly, and annual basis.... GAO also found that contingent workers are about two-thirds less likely than standard workers to have a work-provided retirement plan and less than half as likely to have work-provided health insurance.”⁹³

9 SHOULD EMPLOYERS CONTINUE TO BE INVOLVED IN PROVIDING RETIREMENT AND HEALTH BENEFITS?

Perhaps it is time to change the role of the employer. For retirement plans to be employer-based is logical, though not inevitable: the retirement benefits replace the wages received from the employer. For health benefits to be employer-based is a historical accident and is anomalous from an international viewpoint.

In 2007, one of the proposals made by the Conversation on Coverage was the establishment of a national clearinghouse structure to administer portable individual retirement accounts.⁹⁴ In the same year, the ERISA Industry Committee (ERIC) issued a comprehensive reform proposal.⁹⁵ ERIC proposed a new structure that would provide benefits through independent Benefit Administrators, who would compete based on quality, use of information technology, plan design and cost. Benefit Administrators, in many respects, would assume the role of today’s plan sponsors and, particularly with regard to health care, would be organized on a geographic basis.⁹⁶ Frank Cummings, one of the drafters of ERISA, viewed the proposal favorably: “The ERIC Proposal is a beacon of light for a system losing its bearings in a storm of plan cutbacks, freezes and terminations. It represents the only new upside after years of downside inventions.... At long last ERIC has propounded at least an invitation to some new thinking.”⁹⁷

Susan Stabile argues that the failures of the employer-based retirement system cannot be rectified by incremental changes and that “there are really only two possible models. The first is to jettison the employer-based system entirely and provide a government pension [providing a livable pension for all elderly Americans] for everyone. The second is to retain the employment-based system but move to a mandatory system with more stringent regulation of defined contribution plans than currently exists.”⁹⁸

Katherine Stone argues that the current system of benefits originated in the industrial era of the 20th century, when employers sought to secure a stable workforce, that this employer-centered model of benefits has largely outlived its usefulness in the new “boundaryless” workplace of the

⁹³ Id.

⁹⁴ Covering the Uncovered: Final Report of the Conversation on Coverage, www.conversationoncoverage.org.

⁹⁵ The New Benefit Platform for Life Security, available at www.eric.org. As it states on its web site, ERIC is “dedicated exclusively to representing the employee benefits and compensation interests of America’s major employers.”

⁹⁶ Id.

⁹⁷ BNA Pension & Benefits blog, <http://bnablog.bna.com/penben/2007/07/several-weeks-a.html#comments>.

⁹⁸ Stabile, *Is it Time to Admit the Failure of an Employer-based Pension System?*, 11 *Lewis & Clark L. Rev.* 305, 325 (2007). A similar argument was made by Daniel Halperin in 1993: “If, as a matter of public policy, it is important for people to be able to maintain their standard of living upon retirement, or at least maintain a minimum standard beyond what is provided by Social Security, rather than trying to encourage employer plans or individual savings, it would be more straightforward either to enhance Social Security benefits or to require employers to contribute to private plans for their employees.” Halperin, “Special Tax Treatment,” *supra* note 22, at 44.

21st century, and that it must be replaced with an alternative that is more portable and more affordable for the vast majority of workers.⁹⁹

More recently, Eugene Steuerle, Benjamin Harris and Pamela Perun have argued that “In a DC plan system where the majority of the risks and responsibilities for saving fall on workers, where independent financial services companies provide investments, and where professional administrators manage the plan, it is self-defeating to continue to insist that employers as plan sponsors remain the ultimate guarantors of the plan and all its functions. There is increasing recognition that the next bold move in the evolution of the 401(k) plan system could be to transform employers into facilitators of their employees’ saving. This merely requires activating an employer’s payroll system to transfer employee contributions to a saving plan run by an external entity. Such a system has been in place for decades in the 403(b) plan universe where employers typically make supplemental savings plans available to their employees. In such plans, employers are not fiduciaries, and their primary responsibility is to transfer elective contributions, limited in amount as in the 401(k) world, to the plan chosen by the employee.”¹⁰⁰

10 CONCLUSION

The employer-based system of providing retirement and health benefits is failing too many Americans, including disproportionate numbers of the poorer and more vulnerable members of society. The largely incremental changes made over the last 30 years have not solved the basic problems of access, coverage and adequacy. Accordingly, I suggest that it is time for a more radical approach. One approach would be to redefine the terms “employer” and “employee” to capture the realities of the 21st century workplace. However, any redefinition would be susceptible to the development of new workplace relationships that work around the redefinitions. Accordingly, the more promising approach is to provide a system in which entitlement to some level of retirement and health benefits is independent of employment or employment history, with employers remaining free to offer supplementary benefits to attract and retain talented employees.

⁹⁹ Katherine V.W. Stone, A Fatal Mismatch: Employer-centric Benefits in a Boundaryless World, 11 Lewis & Clark L. Rev. 452 (2007).

¹⁰⁰ C. Eugene Steuerle, Benjamin H. Harris and Pamela J. Perun, Entitlement Reform and the Future of Pensions, September 2014, PRC WP2014-08, Pension Research Council.