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Final Equal Employment Opportunity Commission Rules on Retiree Health Plans and the Age Discrimination in Employment Act

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Summary

Under the Age Discrimination in Employment Act (ADEA), the Equal Employment Opportunity Commission (EEOC) has authority to issue reasonable exemptions the Commission finds "necessary and proper in the public interest." 29 U.S.C. § 628. Recently, the EEOC approved a narrowly-drawn exemption, for circulation to other federal agencies, to permit the practice of coordinating employer-provided retiree health coverage with eligibility for Medicare. The proposed final rule states that it is not a violation of the ADEA to alter, reduce or eliminate health benefits for retirees when the participant becomes eligible for Medicare or comparable state health benefits. An Appendix to the final rule makes clear that the exemption is also intended to apply to dependent and/or spousal health benefits that are included as part of the health benefits provided to retirees. However, dependent and/or spousal benefits need not be identical to benefits provided to retirees, and may be altered, reduced, or eliminated, regardless of how corresponding benefits for retirees are treated. No other aspect of ADEA coverage, or other employee benefits, are affected. The ADEA exemption is intended to apply to existing and newly-created employer-provided retiree health plans from the date of publication of a final rule in the Federal Register. Meanwhile, employers within states covered by the Third Circuit – which includes Pennsylvania, New Jersey, Delaware and the Virgin Islands – remain subject to standards set forth in *Erie County Retirees Ass'n v. County of Erie*, which held that the ADEA requires employers to assure that pre- and post- Medicare eligible retirees receive health benefits of equal type and value.

Employers have frequently sought to trim the high cost of providing group health coverage for their workers by reducing retiree benefits or narrowing the group of retirees eligible for coverage. One commonly used formula is to differentiate in health plan benefits between retirees eligible for Medicare and younger retirees. But in *Erie County*

Retirees Ass'n v. County of Erie,[1] a federal appeals court ruled that the Age Discrimination in Employment Act (ADEA) applies to retirees and prohibits the practice of coordinating retiree health benefits with Medicare eligibility, an "explicitly" age-related factor. In October 2000, the Equal Employment Opportunity Commission (EEOC) adopted the court's reasoning as the agency's national enforcement policy, but later rescinded its position to further review the issue. Following two years of study, on April 22, 2004, the Commission proposed a "final rule," for circulation to other federal agencies, that would allow employer-sponsored retiree health plans to reduce or eliminate benefits for Medicare-retirees without violating the ADEA.[2]

Background.

The ADEA prohibits discrimination against workers over 40 years of age in compensation or with respect to employment "terms, conditions, or privileges."[3] The act's legislative history contained a Statement of Managers, which suggested that the practice of coordinating retiree health plans with Medicare was not prohibited.[4] In *Erie County Retirees*, however, the Third Circuit disregarded that evidence of congressional intent when it ruled that providing inferior benefits to Medicare-eligible retirees than younger retired workers may be illegal age discrimination. It remanded the case for a trial court determination of whether the plan was saved by the equal-benefit or equal-cost safe harbor provisions of the Older Workers Benefit Protection Act (OWBPA).[5]

In that case, a group of retirees who were over the age of 65 sued the County claiming that their retiree health program was inferior to the program offered to younger retirees. Designed to supplement Medicare benefits, older retirees were offered an HMO plan that coordinated all health care services through a primary care physician. The county provided former employees who were not Medicare-eligible with a "hybrid point of service program " that combined the features of an HMO with a traditional indemnity plan. The district court granted partial summary judgment for the county, holding that the

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[1] 220 F.3d 193 (3d Cir. 2000).

[2] See EEOC, Age Discrimination in Employment Act; Retiree Health Benefits (Final Rule), published at [http://www.eeoc.gov/policy/regs/retiree_benefits.html]

[3] 29 U.S.C. § 623.

[4] See Older Workers Benefit Protection Act of 1990, P.L. 101-433, 104 Stat. 9780(1990)(OWBPA), Final Substitute: Statement of Managers, 136 Cong. Rec. S25353 (Sept. 24, 1990). In addition, the Conference Report for the recently enacted Medicare Prescription Drug Improvement and Modernization Act of 2003, P.L. 108-173, 117 Stat. 2066)(2003), also provides that "the conferees reviewed the ADEA and its legislative history and believe the legislative history clearly articulates the intent of Congress that employers should not be prevented from providing voluntary benefits to retirees only until they become eligible to participate in the Medicare program." H.R. Conf. Rep. No. 108-391, at 365 (2003).

[5] Section 4(f)(2) of the ADEA provides that it is not unlawful for an employer to observe the terms of any bona fide retirement plan that is not a subterfuge to evade the purposes of the act. Under ADEA regulations, a "safe harbor" was created for employers who provide equal benefits to older and younger workers, or who incur equal costs on behalf of each. The OWBPA codified this "equal benefit or equal cost" standard. 29 U.S.C. § 623(f)(2)(B)(i).

ADEA was not intended to apply to retirees such as plaintiffs, who based their age discrimination claim on disparities in health coverage arising from Medicare eligibility. In its reversal, the Third Circuit found that age discrimination had occurred since the medical benefits for older retirees were based solely on their eligibility for Medicare, and "Medicare eligibility follow[s] ineluctably upon attaining age 65."

Reviewing the ADEA, the Third Circuit concluded that an age-based disparity in retiree health benefits is only lawful if the program falls within a "safe harbor" established by the "equal benefit/equal cost" standard. Both the legislative history of OWBPA and the "plain language" of the safe harbor provision indicated Congress' intent that the section apply when an employer reduces health benefits on the basis of Medicare eligibility. In other words, the County of Erie could only prevail if it established that the benefits offered to Medicare-eligible retirees were equal to those provided to younger retirees or that its costs for providing benefits to the two groups were equal. The Third Circuit remanded the case back to the trial court for further determination. The trial court ultimately found that the County's plan was unlawful since 1) older retirees were required to pay a greater percentage of their overall premium than were younger retirees; and 2) younger retirees were given the option between HMO coverage or indemnity coverage, while older retirees could only elect HMO coverage. For these reasons, the trial court concluded that older retirees were provided inferior benefits in violation of ADEA.

A significant aspect of the *Erie County* case was the Third Circuit finding that retirees are entitled to sue under the ADEA even though they are no longer "employees." An associated claim that retirees had been treated less favorably than active employees was withdrawn prior to appeal and went unaddressed by the Third Circuit opinion, but could arise in some future controversy. In particular, the relative legal status of the two groups could be important if an employer were to decide, for cost-saving reasons, to eliminate all medical benefits for retirees while retaining health care coverage for current employees. Emphasizing the "fair middle ground"struck by the equal cost or equal benefit standard of the OWBPA, however, the Third Circuit was able to focus on the problem as between the competing groups of retirees.

Note, also, that in *General Dynamic Land System, Inc. v. Cline*,[6] the U.S. Supreme Court confronted the obverse, but not unrelated, issue of whether an employer may treat older employees more favorably than younger protected class employees without running afoul of the ADEA. Prior to July 1, 1997, General Dynamics had been obligated by a collective bargaining agreement to provide full health benefits to employees who retired after 30 years of service. Under the terms of a new agreement, only employees who were age 50 or older on that date were eligible for retiree health benefits. A group of employees between the ages of 40 and 50 sued General Dynamics, alleging that the company had discriminated against them in violation of the ADEA. The district court dismissed the case, holding that the ADEA does not prohibit an employer from discriminating against employees in the protected class (i.e. aged 40 and over) who are younger than the favored employees. The Sixth Circuit, however, found that the ADEA prohibited discrimination against any individual in the protected class on the basis of age, not just the relatively older, and upheld younger workers right to sue for alleged denial of retiree health benefits.

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[6] 124 S.Ct 1236 (2004).

In a 6 to 3 decision, the Supreme Court reversed the Sixth Circuit. It found that the text, structure, purpose and history of the ADEA revealed that it was enacted "as a remedy for unfair preference based on relative youth," and that it does not prohibit an employer from favoring an older employee over a younger one. In the process, the Court rejected as "clearly wrong" the EEOC regulatory position that a decision between hiring two individuals within the protected class has to be made on the basis of a factor other than age. The Court thus appears to approve of "grandfathering" older workers, by treating them more favorably, when reforming benefits packages for age protected employees. It did not, however, consider the lawfulness of providing differential benefits that disadvantage relatively older workers, as addressed in the *Erie County* case and the EEOC final regulations.

The EEOC had filed an *amicus curiae* brief advocating the position adopted by the Third Circuit in *Erie County*, which the agency then incorporated in its "Compliance Manual" as part of its national enforcement policy on the ADEA. But in August 2001, after consulting various labor and employer groups, EEOC rescinded its policy regarding employer-sponsored retiree health plans, announcing that it would study the issue further. The EEOC study demonstrated a considerable decline in the number of employers providing retiree health benefits in the decade preceding, due to higher health care coverage costs, the number of employees nearing retirement age, and changes in accounting rules for retiree health benefits.[7] In addition, it found that "concern about the potential application of the ADEA to employer-sponsored retiree health benefits is adversely affecting the continued provision of this important retirement benefit." Because "it is not possible to apply the equal benefit/equal cost test, or a variant of that rule, to the rapidly changing landscape of retiree health case," the study concluded, a reversal of policy was required in the "public interest" to protect retiree health coverage as a valuable benefit to older individuals.

The EEOC Final Rule.

The proposed final rule amends EEOC regulations under the ADEA to exempt from its prohibitions the alteration, reduction or elimination of employer-sponsored retiree health benefits when retirees become eligible for Medicare or other comparable state retiree health benefits. The authority cited in the preamble is § 9 of the ADEA which permits EEOC to "establish such reasonable exemptions to and from any or all provision of [the act] as it may find necessary and proper in the public interest." EEOC notes that employers are not legally obligated to provide any retiree health benefits and argues that the safe harbor provisions of the OWBPA have become unworkable given the broad diversity of employer health plan options currently available Consequently, the exemption is deemed "necessary and proper" as an incentive to employers not to eliminate all retiree health benefits, or to reduce the benefits of younger retirees to equal those provided to their Medicare-eligible counterparts.

The final regulations also include an appendix with questions and answers that provide the following specific guidance.

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[7] See 68 Fed. Reg. 42542 - 41549 (7-14-03).

- The exemption does not mean that the ADEA does not apply to retirees, or that all forms of retiree health coverage are exempted. Only the specific practice of coordinating retiree health benefits with Medicare or a comparable state health plan is exempted from ADEA.

- Employers may offer "Medicare carve out plans" under which Medicare is primary and the employer plan secondary for retirees, but not active employees.

- The exemption also applies to dependent and/or spousal health benefits included as part of retirees' benefits, although these may be altered, reduced or eliminated even when the retirees' are not.

- Medicare eligibility (or eligibility under a similar state health plan) or the age of such eligibility may not be used as a basis for any other act, practice, or decision regarding retirees.

- The exemption does not apply to active employees over the age of Medicare (or state health plan) eligibility.

The proposed final rule will not become effective until reviewed by the Office of Management and Budget in accordance with Executive Order 12866 and published in the Federal Register.

Conclusion.

While only rarely invoked, congressional delegation of ADEA exemption authority to the EEOC would probably confer binding legal force on the retiree health benefit rule and require great deference by the courts under the *Chevron* doctrine.[8] But employers within the Third Circuit – Pennsylvania, New Jersey, Delaware, and the Virgin Islands – continue to operate under the shadow of the *Erie County* decision pending finalization of the EEOC position that altering or eliminating benefits of Medicare-eligible retirees is permissible. As noted, language inserted into the legislative record of the new Medicare prescription drug law indicates the current Congress' intent that employers should not be prevented from providing voluntary benefits only until they become eligible for Medicare. However, until such time as the ADEA is actually amended, or the Supreme Court speaks to the issue, the possibility of future litigation remains.

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[8] Chevron U.S.A., Inc. v. Natural Resources Defense Council, 467 U.S. 837 (1984)(courts must defer to a federal agency's construction of a statute that it administers unless the legislature has evidenced a contrary intent).