DowLohnes

HR ALERT

August 2007

Court Decision Affirms Employers' Ability to Coordinate Retiree Health Benefits with Medicare Benefits

On June 4, 2007, the U.S. Court of Appeals for the Third Circuit held that employers may coordinate the provision of retiree health benefits with Medicare benefits. *AARP v. EEOC*, No. 05-4594 (3rd Cir. 2007). This decision clears the way for the U.S. Equal Employment Opportunity Commission ("EEOC") to finalize the proposed rules it issued in 2003 to exempt from the prohibitions of the Age Discrimination in Employment Act ("ADEA") the practice of reducing or eliminating employer-sponsored retiree health benefits when retirees become eligible for benefits under Medicare or a state-sponsored program.

Historically, employers have coordinated retiree health benefits with other benefits that a retiree may be entitled to under a government-sponsored plan. As such, younger retirees may receive a more generous benefit package from their employer than retirees who are 65 and older. The EEOC's 2003 proposed regulation condoned this practice in an effort to stave off the movement of employers' terminating their retiree medical plans due to increased costs. Before the EEOC could finalize its proposed regulations, the American Association of Retired People ("AARP") obtained an injunction in 2004 to prevent the rules from taking effect. In 2005, a U.S. District Court in Pennsylvania upheld the injunction, finding that the regulation was contrary to the intent and language of the ADEA, and, as such, the EEOC did not have the authority to issue the regulation. Upon reconsideration, however, the same court held for the EEOC and found that the regulation did not violate the ADEA. The court maintained the injunction pending the Third Circuit's review of the decision. The Third Circuit upheld the EEOC's authority to issue the regulation and lifted the injunction, holding that the EEOC's proposed exemption is consistent with the purposes and intent of the ADEA and is necessary and proper to encourage employers to provide the greatest possible health benefits to all retirees.

On August 20, 2007, the U.S. Court of Appeals for the Third Circuit denied a request by the AARP for the full appeals court to review the court's earlier decision. The AARP has indicated it will file an appeal with the U.S. Supreme Court regarding this decision, and has asked the U.S. District Court in Pennsylvania to continue its stay on the new regulations that the EEOC wants to issue in this area while the AARP appeals the case to the U.S. Supreme Court.

COPYRIGHT © 2007 BY DOW LOHNES PLLC
ALL RIGHTS RESERVED
THIS PUBLICATION IS PREPARED BY THE LAW FIRM OF DOW LOHNES PLLC AS AN INFORMATION SOURCE FOR CLIENTS AND OTHER INTERESTED PARTIES. WE PERMIT AND ENCOURAGE PHOTOCOPYING AND DISTRIBUTION WITH ATTRIBUTION. THE CONTENT OF THIS PUBLICATION IS GENERAL LEGAL INFORMATION AND READERS SHOULD NOT ACT UPON INFORMATION PRESENTED HEREIN WITHOUT PROFESSIONAL LEGAL COUNSEL ADDRESSING THE FACTS AND CIRCUMSTANCES SPECIFIC TO THEM.

Pending the result of the appeal to the Supreme Court, this court decision eliminates a split in the circuits, as other circuits also have ruled in favor of the EEOC on this point, and allows all plan sponsors to adopt or maintain retiree health care programs that coordinate with Medicare. This decision is particularly important to employers who have the desire to coordinate prescription drug coverage for retirees with Medicare Part D. As a result of this decision, companies now may consider providing Medicare-eligible retirees with reduced health care and/or prescription drug benefit coverage.

Getting In Line After Massachusetts--More State Health Care Initiatives

In the wake of the Massachusetts Health Care Reform Act (See HR Alert-Employers Take Notice-Impact of the Massachusetts Health Care Reform Act), the Missouri, Connecticut and Rhode Island state governments have enacted legislation requiring employers to establish cafeteria plans according to Section 125 of the Internal Revenue Code to allow employees to make pre-tax contributions toward the cost of their health care coverage. California does not seem far behind, with the prospect that more states might follow.

The new legislation in these states demonstrates a trend of state governments attempting to regulate employers' provision of health care benefits to employees. As the Massachusetts Health Care Reform Act has not been challenged under ERISA, it is reasonable to expect other states to follow suit with similar legislation. A review of recent state activity is as follows:

I. Missouri

The new Missouri legislation, enacted on June 1, 2007, requires employers that offer health insurance coverage in which the employer pays some portion of the premium to establish a "premium-only" cafeteria plan. However, on its face, this law does not apply to sponsors of self-insured plans.

II. Connecticut

The new Connecticut legislation, enacted on July 10, 2007, also mandates the establishment of cafeteria plans. This law requires that any employer providing health insurance benefits paid at least partly through payroll deductions also must offer a cafeteria plan. The Connecticut law does not define the term "employee," or make clear which workers (i.e., both full and part time employees) are entitled to participate in the employer's cafeteria plan. The legislation also does not currently specify penalties for noncompliance. It is unclear on its face whether this legislation is intended to apply to self-funded plans (which could bring up some ERISA preemption issues).

III. Rhode Island

The new Rhode Island legislation, enacted on June 27, 2007, also requires employers with an average of 25 or more employees in Rhode Island for six consecutive months of the year to adopt cafeteria plans for those employees. It is unclear whether the

COPYRIGHT © 2007 BY DOW LOHNES PLLC
ALL RIGHTS RESERVED
THIS PUBLICATION IS PREPARED BY THE LAW FIRM OF DOW LOHNES PLLC AS AN INFORMATION SOURCE FOR CLIENTS AND OTHER INTERESTED PARTIES. WE PERMIT AND ENCOURAGE PHOTOCOPYING AND DISTRIBUTION WITH ATTRIBUTION. THE CONTENT OF THIS PUBLICATION IS GENERAL LEGAL INFORMATION AND READERS SHOULD NOT ACT UPON INFORMATION PRESENTED HEREIN WITHOUT PROFESSIONAL LEGAL COUNSEL ADDRESSING THE FACTS AND CIRCUMSTANCES SPECIFIC TO THEM.

legislation actually intends for employers with 25 employees or more to establish a health care plan in addition to a cafeteria plan—if they do not currently offer a health care plan. Other key details are unclear, including the definition of an "employee," as well as possible penalties for noncompliance. It is also unclear whether this legislation is intended to apply to self-funded plans.

IV. California

It appears that California is about to enact its own version of the Massachusetts health care reform initiative. Based on recent action in the state legislature, a bill being considered would become effective on January 1, 2009. Similar to Massachusetts, the bill would give California employers a choice of providing health insurance to their employees or contributing to a state purchasing pool. The bill would require employers to actually begin purchasing coverage for their employees by October 1, 2009, or to contribute to a state health care cooperative program. At this time, it is not clear which employees must be covered, so the coverage of part time employees may become an issue. The bill also would require employers to set up a cafeteria plan to allow employees to pay premiums with pre-tax money. Finally, the bill imposes penalties for the failure to adopt the cafeteria plan.

If you have any questions, please contact either Richard P. McHugh (rmchugh@dowlohnes.com), Paul R. Lang (plang@dowlohnes.com) or Michael A. Hepburn (mhepburn@dowlohnes.com).

WWW.DOWLOHNES.COM

COPYRIGHT © 2007 BY DOW LOHNES PLLC
ALL RIGHTS RESERVED
THIS PUBLICATION IS PREPARED BY THE LAW FIRM OF DOW LOHNES PLLC AS AN INFORMATION SOURCE FOR CLIENTS AND OTHER INTERESTED PARTIES. WE PERMIT AND ENCOURAGE PHOTOCOPYING AND DISTRIBUTION WITH ATTRIBUTION. THE CONTENT OF THIS PUBLICATION IS GENERAL LEGAL INFORMATION AND READERS SHOULD NOT ACT UPON INFORMATION PRESENTED HEREIN WITHOUT PROFESSIONAL LEGAL COUNSEL ADDRESSING THE FACTS AND CIRCUMSTANCES SPECIFIC TO THEM.