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STATE OF ARIZONA
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WASHINGTON, D.C.

October 10, 2004

ASSOCIATION OF U S WEST RETIREES

Re: Post-1990 Qwest Management Retirees Health Care Costs
The *Dark Side* of ERISA

In September 2003, Qwest Communications International, Inc. announced it had made dramatic changes to its employee benefit plans providing potential benefits to retirees. In particular, the company announced that it would begin requiring ***management*** retirees who retired after January 1, 1991 to pay a portion, at least 20%, of the annual costs of the premiums to provide heath care coverage. The changes caught many by surprise, as they had expectations Qwest would continue to provide free health care benefits, like historically provided by U S WEST, Mountain Bell and the former Bell System companies. **Many post-1990 management retirees** wonder whether or not a legal challenge can be made.

The short answer: ***No*.** The following is an explanation of the reason there is no viable legal challenge option.

The Employee Retirement Income Security Act ("ERISA") of 1974 was intended by Congress to protect employees, retirees and their beneficiaries in pension and employee benefit plans through a uniform body of federal law. One of Congress' main goals in ERISA was the replacement of state-by-state regulation of employee benefit plans with a comprehensive federal statute covering such programs. This intent is expressed in ERISA Section 514(a), 29 U.S.C. § 1144(a) which states, in part: "The provisions of this title . . . shall supersede any and all state laws insofar as they may now or hereafter relate to any employee benefit plan." The scope of ERISA's preemption provision has been found "deliberately expansive" and "conspicuous for its breadth." It includes state statutes, rules, regulations and common law causes of action that

"relate to" ERISA plans. ERISA "completely preempts" state law in order to create uniform federal law governing employee benefit plans. ERISA's preemption provision was not supposed to leave plan participants worse off than they had been under pre-ERISA state law.

ERISA recognizes there are two types of employee benefit plans: pension plans and welfare plans. Pension plans provide (I) retirement income to employees or (ii) result in a deferral of income by employees for periods extending to the termination of covered employment or beyond. 29 U.S.C. § 1002(2)(A). Welfare plans provide "medical, surgical or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment. . ." 29 U.S.C. § 1002(1). ERISA Provides Less Protection for Welfare (Medical) Plans. ERISA contains elaborate vesting (i.e., contractually enforced rights) for pension plans, but does not require automatic vesting of welfare benefit plans. *Alexander v. Primerica Holdings, Inc.,* 967 F.2d 90, 95 (3rd Cir. 1992). When enacting ERISA, Congress did not see fit to impose vesting requirements on welfare or health care plans because Congress recognized the need for flexibility with regard to an employer's right to change health care plans. As the Court of Appeals for the Second Circuit has observed:

> Automatic vesting [of rights to medical plan benefits] was rejected because the cost of such plans are subject to fluctuating and unpredictable variables. Actuarial decisions concerning fixed [pension] annuities are based on fairly stable data, and vesting is appropriate. In contrast, medical insurance must take account of inflation, changes in medical practice and technology, and increases in the cost of treatment independent of inflation. These unstable variables prevent accurate prediction of future needs and costs."

Moore v. Metropolitan Life Ins. Co., 856 F.2d 488, 492 (2d Cir. 1988). The Supreme Court amplified this point in the case of *Inter-Modal Rail Employees Ass'n v. Atchison, Topeka & Santa Fe Ry*, 520 U.S. 510, 515, 117 S.Ct. 1513, 1515 (1997):

> "The flexibility an employer enjoys to amend or eliminate its [health care] welfare plan is not an accident; Congress recognized that "requir[ing] the vesting of these ancillary benefits would seriously complicate the administration and increase the cost of plans." S. Rep. No. 93-383, p. 51 (1973). Giving employers this flexibility also encourages them to offer more generous benefits at the outset, since they are free to reduce benefits should economic conditions sour. If employers were locked into the [health care] plans they initially offered, "they would err initially on the side of omission." (citing *Heath v. Variety Corp*., 256, 71 F. 3d 258 (CA 7, 1995).

Soon after the enactment of ERISA, AT&T got its employee benefit plans, including its many health care plans for employees and retirees, in compliance with the federal law ERISA. AT&T distributed Summary Plan Descriptions (SPDs) to all employees and retirees. The SPDs

were the primary documents used to inform participants and beneficiaries of their rights, benefits, and obligations under the health care plans. In 1984, with the effective break-up of AT&T, its massive health care plan was divided among the newly established regional holding companies, including U S WEST, the parent company of Mountain Bell, Northwestern Bell and Pacific Northwest Bell. Between 1984 and 1990, U S WEST acted as plan sponsor for several employee medical and dental plans, including at least nine retiree health care plans, all with different terms and levels of benefits. The health and dental care plans were traditional "fee for service" or "indemnity" plans, meaning, as a general rule, employees and retirees were permitted to visit almost any health-care provider of their choosing, but they were responsible for an annual deductible, co-insurance payments for office visits, and would be reimbursed for reasonable and customary expenses.

During the late 1980's there was a major movement within corporate America to change from traditional indemnity health insurance to health maintenance organization ("HMO") type health insurance. U S WEST began providing that option to current employees. This created administrative difficulties and pressure to unite the company's many different health care plans into one umbrella plan. Therefore, the Human Resources Department began efforts to consolidate and streamline plans. The end result was the creation of the January 1, 1991 dated "U S WEST Health Care Plan."

When US WEST created the U S WEST Health Care Plan, the law department inserted in the governing plan document legal language known as a "reservation of rights clause, " stating the Company:

> "reserves the right to terminate or amend [the health and dental care plans] at any time with respect to any or all classes of current or future Participants (including Retired Employees), subject to applicable limitations of the law."

Essentially, U S WEST was saying it did not recognizing any commitment to provide anyone lifetime benefits and the company was attempting to put everyone on notice that the company could make any changes it wanted, with or without further written notice. This language in the governing plan document gave U S WEST the right, at any time, to change, reduce and terminate the medical and dental care plans. The Supreme Court has ruled that any employer plan sponsor can change, reduce or cancel health care benefits for retirees as long as the employer has reserved that right in the governing plan document. *Curtiss-Wright, Corp. v. Schoonejongen*, 514 U S 73, 115 S.Ct. 1223, 1228 (1995).

The new governing plan document for the U S WEST Health Care Plan which document was about 100 pages in length was not widely distributed to employees and retirees until many

months after its creation. Eventually, the new governing plan document caught the attention of a group of retirees, including retiree Nelson Phelps, formerly employed as an Executive Director in the Human Resources Department at Mountain Bell and U S WEST. When Mr. Phelps took retirement in 1990, representatives and employees of U S WEST made commitments and representations to him that weighed heavily in his decision to, then, take early retirement. U S WEST made representations to Mr. Phelps and thousands of others who retired in 1990 that, during their respective lifetimes, they would be entitled to receive the same level of medical and dental care coverage that they were provided as active employees during year 1990.

However, none of the commitments guaranteeing lifetime unreduced indemnity plan coverage to Mr. Phelps and others were memorialized in the new governing document for the U S WEST Health Care Plan. Moreover, during the Spring and Summer of 1995, U S WEST was engaged in a rush to enroll thousands of retirees into HMOs and get them out of the traditional indemnity health insurance coverage. U S WEST refrained from stating in the many pieces of literature and propaganda distributed to retirees that they had a right to lifetime health care coverage under the company paid indemnity health plan. Mr. Phelps was justifiably concerned that U S WEST had not formalized its commitment to provide lifetime unreduced indemnity medical and dental coverage in the new governing health care plan document, and the company was moving away from that commitment by soliciting retirees to enroll in HMO. Therefore, Mr. Phelps asked me to address the legal matter.

I informed Mr. Phelps and other retirees that the law was clear. In order for any commitment by U S WEST about providing lifetime health care coverage to be enforceable, this commitment must be specifically written in the ERISA controlling Plan documents. In order for the retirees' expectation of employee benefit rights to be protected, U S WEST's guarantee of lifetime coverage had to be "stated in clear and express language" in the governing Plan documents, including the SPDs. *In re Unisys Corp. Retiree Medical Benefit "ERISA" Litigation*, 58 F.3d 896, 902 (3d. Cir. 1995). *Alday v. Container Corp. of America*, 906 F.2d 660, 665 (11th Cir. 1990) ("[A]ny retiree's right to lifetime medical benefits at a particular cost can only be found if it is established by contract under the terms of the ERISA-governed benefit plan document"), *cert. denied*, 498 U.S. 1026, 111 S.Ct. 675, 112 L.Ed.2d 668 (1991). By then, the federal judiciary had been virtually unanimous in finding technical and policy reasons to deny "breach of contract" claims for aggrieved employees and retirees claiming their employer had reneged on agreements to provide lifetime health care coverage.

In August, 1995, I sent to U S WEST leadership a letter stating Mr. Phelps' demand that the Company memorialize its commitment to those like Mr. Phelps who retired with assurances of guaranteed lifetime health care coverage. The letter demanded that:

> "the Plan Administrator and the EBC [Employee Benefit Committee] obtain a resolution from the U S West, Inc. Board of Directors formally acknowledging the Company is contractually bound not to either reduce or eliminate medical, dental and vision care coverage for pre-1991 retirees during their respective lifetime. Further, Mr. Phelps and the class demand the Company and the EBC acknowledge this obligation by amending the Plans' respective disclaimer and reservation of rights and insert language memorializing the Company's contractual obligation. Finally, Mr. Phelps and the class of pre-1991 retirees demand the Company forthwith distribute a formal notice to all participants in the Plans."

Alas, my demand letter was not even acknowledged by U S WEST for at least ninety (90) days, all the while U S WEST intensified concerted efforts to get retirees enrolled into HMOs. Therefore, on November 1, 1995, Mr. Phelps commenced legal proceedings under ERISA to cause U S WEST to remove "reservation of rights" language appearing in the ERISA controlled medical and dental employee benefit plan documents. The case was filed in Denver Federal Court, Civil Action No. 95-Z-2759. This was a "pre-emptive strike" against U S WEST and proposed as a class action on behalf of more than 30,000 retirees. [1]

Within his lawsuit, Mr. Phelps insisted U S WEST formally recognize its prior commitments to over 30,000 persons who retired before January, 1991. He demanded U S WEST place formal language in the governing plan documents to memorialize a guarantee of lifetime unreduced indemnity medical and dental care coverage made to all pre-'91 retirees. Furthermore, he demanded U S WEST guarantee the company (and any successors in interest) would not force the pre-1991 retirees into changing from the traditional indemnity plan into Health Maintenance Organizations.

In conjunction with his lawsuit, Mr. Phelps and others formed a grass roots organization of U S WEST retirees to awaken and educate the masses about the perils of the presently worded "reservation of rights" language appearing in the governing plan document for the health care

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[1] In his lawsuit, Mr. Phelps sought declaratory and injunctive relief either requiring U S WEST to amend the then existing "reservation-of-rights" clause in the governing Plan documents or forbidding U S WEST from exercising said "rights" and detrimentally changing the coverage for the proposed class of 30,000 retirees. Mr. Phelps sought relief under ERISA § 502(a)(3)(B), 29 U.S.C. § 1132(a)(3)(B), which statutory provision gave the federal trial court subject matter jurisdiction to insure plan documents are in compliance with ERISA. Furthermore, Mr. Phelps asked the federal trial court to "clarify [Mr. Phelps' and class members'] rights to future benefits under the terms of the [P]lan." ERISA § 502(a)(1)(B), 29 U.S.C. § 1132(a)(1)(B).

plan. Thousands of retirees joined the "Association of U S WEST Retirees" and inundated U S WEST leadership with letters demanding the company formally recognize its previous commitment to provide them lifetime health care coverage.

On November 6, 1995, exactly five days after Mr. Phelps' lawsuit was commenced, U S WEST Communications, Inc. President & CEO Solomon D. Trujillo, in response to news media attention about the lawsuit, wrote to the Editor of *The Denver Post*, stating:

> "Less than 24 hours after this request was made -- in the form of an unnecessary lawsuit -- U S WEST polled the members of the Employee Benefits Committee and reached agreement to change the plan language. As we told the *Post* reporter, we will notify retirees of this change pending completion of necessary legal steps".

Thus, Mr. Phelps quickly achieved everything he demanded. In January, 1996, U S WEST adopted a plan amendment effectively nullifying the "reservation of rights" language and benefitting over 30,000 plan participants. U S WEST memorialized a guarantee to provide lifetime health care coverage to this large group of retirees. In addition, U S WEST guaranteed the company and any successor would not force pre-'91 retirees to enroll in HMOs. These ironclad guarantees appear in Appendix 11 to the U S WEST Health Care Plan. **This ironclad guarantee is binding upon every successor company!** On February 7, 1996, Mr. Phelps and U S WEST then agreed to end the litigation.

Ironically, several months later, the Tenth Circuit Court of Appeals, which has jurisdiction over federal cases filed in Colorado, announced a decision just as expected. In the case of *Chiles v. Ceridian, Corp.*, 95 F.3d 1505, 1511 (10th Cir. 1996), the Tenth Circuit Court of Appeals ruled in harmony with other federal appellate courts: "Because an employee benefit plan must be established by a 'written instrument', 29 U.S.C. § 1102(a)(1), a promise to provide vested benefits 'must be incorporated in some fashion, into a formal written ERISA plan' " (citing *Jensen v. SIPCO*, 38 F.3d 945, 949 (8th Cir. 1994), *cert. denied*, 115 S.Ct. 1428 (1995). In *Chiles*, the Tenth Circuit observed that "[T]he weight of case authority supports the [ruling] that a reservation of rights clause allows the employer to retroactively change the medical benefits of retired participants, even in the face of clear language [found elsewhere in other company publications] promising company-paid lifetime benefits." Id., 95 F.3d at 1512 n. 2. Thus, **the pre-emptive strike taken by Mr. Phelps was necessary** so as to cause U S WEST leadership to memorialize an enforceable agreement within the governing plan document.

Since, 1996, U S WEST and Qwest have honored the commitment to the pre-1991 retirees and their level of health care benefits have not been reduced. [2] However, Qwest has the following language or "reservation of rights clause" in Section 12.1 of the governing plan document for the U S WEST Health Care Plan:

> "Except to the extent limited by any applicable collective bargaining agreement and with respect to Benefits for Pre-1991 Retirees and ERO Retirees, as set forth in Appendix 11, the Company reserves the right, in its sole discretion, to amend the Plan at any time, in any manner, including without limitation, the right to amend the Plan to reduce, change, eliminate, or modify the type or amount of Benefits provided to any class of Participants. Moreover, unless otherwise explicitly provided in a Contract, no amendment shall be made to the Plan without the consent of the Company. Any such amendment of the Plan shall be effective on such date as the Plan Sponsor may determine; provided, however, that no amendment shall reduce the benefits of any Participant with respect to health care expenses incurred prior to the date such amendment is adopted."

In accordance with the aforesaid "reservation of rights clause" in the governing plan document, Qwest has steadily reduced the level of coverage for post-1990 retirees and those persons in active employment status.

Neither U S WEST nor Qwest has ever made a written guarantee of health care coverage for persons who retired after January 1, 1991 (except for about 250 nonmanagement retirees who retired in 1992 under a special Union negotiated program called "Early Retirement Offer.").

In September, 2000, Qwest Communications International Inc. announced it had made dramatic changes its employee benefit plan providing potential benefits to retirees. In particular, the company announced that it would no longer provide retiree health, dental and life insurance benefits to future management classified retirees who either did not have at least 20 years employment service as of December 31, 2000 or would not become service pension eligible by

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[2] There is also a lifetime commitment protecting a group of about 250 nonmanagement retirees who retired in 1992 under a special program called "Early Retirement Offer." Mr. Phelps' lawsuit included that group because the special retirement program included representations making a commitment on the part of U S WEST. Qwest has repeatedly proclaimed in informational literature to its employees that "the only retirees who are eligible for **free** retiree health care **for life** are those who retired before 1991 and a group of employees who left in 1992 under an enhanced retirement offer."

December 31, 2003. Also, Qwest announced that persons retiring on or after September 7, 2000, would have to start making contributions to retiree health care benefits in year 2004. [3] In short, this group of retirees would have to make premium payments in the same amount as required of active employees in year 2004. Sure enough, in late 2003, Qwest announced that post-1990 management retirees would have to begin paying at least 20% of the premiums for coverage.

There is no legal basis for challenging the situation. By judicial fiat, any complaining Qwest employee must bear the burden of proving that the proposed health care plan changes affect "vested" rights. **But, no such vested rights exist.** If any Qwest employee were to commence ERISA benefits litigation to regain company-sponsored welfare benefits which Qwest has reduced or eliminated, he or she must be able to show the employer breached an expressed commitment set forth in the governing plan document. Qwest has been quick to point out in its announcements about changes to the benefit plans that Qwest never committed to continuing to provide health care benefits and, at least since 1991, the company has expressly stated its "reservation of rights" to change, reduce or eliminate future retiree health care benefits.

In short, the only protection afforded to workers and retirees is that provided by ERISA. **The federal law ERISA is presently written and interpreted by the federal courts so as to allow Qwest the right to eliminate health care coverage altogether in the future for all present employees and retirees and future retirees**. The only group of protected persons guaranteed lifetime health care coverage are those identified as a result of the ironclad commitment memorialized as a result of the *Phelps* litigation (i.e., pre-1991 retirees and a limited group of 1992 nonmanagement retirees).

Understandably, many employees at Qwest view the changes to the benefit programs as part of a concerted effort by corporate leadership to strip employees of health care insurance. However, "ERISA does not create any substantive entitlement to employer-provided health benefits . . . . Employers . . . are generally free under ERISA, for any reason at any time, to adopt, modify, or terminate welfare plans." *Curtiss Wright, supra,* 514 U.S. at 78. Therefore, any complaint that Qwest amended its health care plan so as to deprive some group of employees of health benefits is not legally cognizable under ERISA.

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[3] For example, if the employee cost for active medical coverage is $100 per month in 2004, this group of retirees will shoulder the same cost for retiree medical coverage, i.e., $100 per month. **Qwest has already stated that after year 2004 "retiree health care contributions will be increased by 50% of the increase in the cost of retiree benefits**." (See e.g., QR2 "Questions & Answers About Qwest Benefits," as updated November 7, 2000). Yet, even that statement is not an enforceable promise, according to ERISA and interpretative case law.

The fact that Qwest is engaging in discrimination and providing better treatment (i.e., not charging any costs) to nonmanagement retirees at least until January 1996 is not a situation that can be legally challenged. **There can be no claim of discrimination, because ERISA is not your friend**. Unfortunately, ERISA, the only law that governs in this instance "does not prohibit an employer from distinguishing between groups or categories of employees, providing benefits for some but not for others." *Bronk v. Mountain States Tel. and Tel., Inc.*, 140 F.3d 1335, 1338 (10th Cir. 1998) (citing *Shaw v. Delta Air Lines, Inc*., 463 U.S. 85, 91 (1983) ("ERISA does not mandate that employers provide any particular benefits, and does not itself proscribe discrimination in the provision of employee benefits."); *Abraham v. Exxon Corp*., 85 F.3d 1126, 1130-31 (5th Cir. 1996); *Averhart v. US WEST Management Pension Plan*, 46 F.3d 1480, 1488 (10th Cir. 1994). As Department of Labor regulations recognize, "[a]n employee pension plan can provide different benefits for various classes of employees." 29 C.F.R. § 2520.201-4; see e.g., *Trenton v. Scott Paper Co.*, 832 F.2d 806, 809-10 (3d Cir. 1987), *cert. denied*, 485 U.S. 1022 (1988). As you can see, several times a group of Mountain Bell or U S WEST management employees have tried to pursue such claims without any success.

So, why has Qwest chosen to make post-1990 retirees pay part of the cost of retiree heath care. The short answer – to "remain competitive" and conserve operating expenses. [4] Qwest has reported that the changes to the employee benefit plans were those promoted by a consulting firm, Watson Wyatt, which outfit "verified that the new pay and benefit plans for employees of Qwest are very competitive." (See "Qwest Pay & Benefits, September 7, 2000 *The Q Home Announcement*). Qwest speciously argues that it made changes to the benefit plans because "we wanted plans that would allow the new Qwest to attract, retain and motivate the types of employees who can make the company successful." (Id.). Qwest leadership have repeatedly adamantly proclaimed "in the case of Qwest, our primary objective is to enhance shareholder value." Id.

During the past decade, many corporations have been eliminating or reducing retiree health benefits, restricting access to programs and ending coverage for future employees. After almost 8 years of litigation between General Motors retirees and their former employer, the federal courts final decision was that, regrettably, the corporation acted within its rights to

[4] In addition, during 1999 and 2000, a significant amount of the Qwest Health Care Plan/Trusts investments were made in Qwest securities, common stock that nose dived during the past few years. It is questionable whether that investment, which suffered hundreds of millions of dollars in market value loss, was prudent, permissible and in the best interests of Qwest Health Care Plan participants – the retirees. That matter is being investigated, because the significant investment loss may have played a big factor in the Company's September 2003 announced decision to start charging post-1990 management retirees monthly premiums.

eliminate certain retiree health care coverage and to start charging retirees monthly premiums for their remaining health care coverage. *Sprague v. General Motors Corp.*, 133 F.3d 388, 401 (6th Cir.) (en banc) (stating SPD specifically provided that General Motors, the employer/plan sponsor, "reserve[d] the right to amend, change or terminate the Plans and Programs described in this booklet"), *cert. denied*, 524 U.S. 923 (1998). This definitive ruling inspired a trend within corporate America to move towards eliminating traditionally provided retiree health care benefits.

The trend continues to play out. Several years ago, J.C. Penney Co. told employees that it's restructuring its retiree health benefits and eliminating them for future retirees. In early August, 2001, J.C. Penney sent letters to workers informing them that anyone hired after January 1, 2002 won't get health insurance when they leave the company. Penney also said it intends to raise premiums for retirees and it won't pay for dental coverage any longer. Bell Helicopter Textron Inc. made a similar change to its benefits in 1994. Sears, Roebuck and Co. did the same thing in year 2000. Other companies have cut their retiree health benefits completely. Montgomery Ward & Co. did so after it filed for bankruptcy this year. Pabst Brewing Co. dropped health coverage for retirees in 1996. Countless other businesses have reduced benefits.

Qwest adamantly maintains that its negative changes to the employee benefit programs are just "**fine**", because it is keeping up with the Joneses, meaning its economically oppressive changes are in line with what the super-rich corporate leaders have done to the active workers and retirees at such "peer" companies as America OnLine, AT&T, BellSouth, Cisco Systems, Cox Communications, Lucent Technologies, MCI WorldCom, Microsoft, Sprint and Sun Microsystems. Indeed, across America the top executives realize over 400 times the annual wage rate paid to the average worker and, no doubt, have no personal inkling of the drastic financial impact their partially selfish motivated directives have on the average worker.

I am unaware of any pending litigation between Qwest retirees and the company over any of the issues discussed herein. Yet, false rumors have spread that a class action had been filed concerning the employee benefit changes. Any challenge to Qwest's changes to the health care plan must be made under ERISA which is the only controlling law. **Qwest's decision** to change the health care benefits plan and charge post-1990 management retirees part or all of the costs of coverage **is permitted by ERISA** and, presently, there is no evidence of any other enforceable commitment by the company to continue making those benefits available.

Sincerely,
Curtis L. Kennedy