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The Effect of Firm Bankruptcy on Retiree Benefits, with Applications to the Automotive and Coal Industries

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Summary

Benefits for retired employees are of particular interest to policy makers because of the growing number of retirees and forecasts indicating that some future retirees may not have the necessary financial resources to maintain their standards of living. Part of this congressional concern is what happens when bankrupt employers are unable to provide promised pension and health benefits to their retired employees.

In chapter 11 bankruptcy reorganization, the employer receives protections against its financial commitments in the hope that it may once again become profitable. This protection could include not having to honor obligations concerning pensions and retiree health insurance. Its employees may therefore be at risk of not receiving some of their promised benefits. Unionized and non-unionized employees may be treated differently under the law because unionized workers have a legal contract governing their terms and conditions of employment.

The costs to the employers for the pension, health insurance, and other benefits promised to retired employees are known as legacy costs, and different costs are subject to different federal laws. Although employers are required to prefund their defined benefit pension trusts, the level of required funding may not be present as the employer enters bankruptcy. The Pension Benefit Guaranty Corporation (PBGC), a quasi-public agency, monitors the finances of pension plans. The PBGC becomes the trustee of and pays the benefits to participants in terminated, underfunded single-employer pension plans. PBGC benefits are subject to a statutory maximum that may be less than the retiree was promised by his or her employer. The PBGC has been running deficits for several years, and the deficit for one of its two programs is at an all-time record high. PBGC funding comes from employer premiums set by Congress, the assets of the plans it takes over, and investment returns. There is no taxpayer funding.

Some retirees receive health benefits from their former employer. Retiree health benefits, however, are not insured by any public agency, and employers are not required to prefund health benefits. On the other hand, employees (perhaps represented by their unions) can fund health benefits (for active and retired employees) through a tax-preferred trust fund known as a Voluntary Employees' Beneficiary Association (VEBA). When the employer and union agree to form a VEBA, and it is approved by the bankruptcy court, the employer generally contributes a collectively bargained level of funding to the VEBA. Providing the contribution usually fulfills the employer's total responsibility for retiree health care. All subsequent retiree health benefit decisions are transferred to the trustees of the VEBA.

After a discussion of these issues, this report provides three examples of bankruptcy proceedings where the retirees' pensions and health insurance benefits received substantial federal attention: the General Motors Corporation, the Delphi Corporation, and the Patriot Coal Corporation.

During bankruptcy proceedings for the General Motors Corporation (commonly known as Old GM or pre-bankruptcy GM) bankruptcy, retiree health benefits were central and pensions, although underfunded, were not a major issue. Old GM's main union, the United Auto Workers (UAW), accepted stock in the General Motors Company (commonly known as New GM or post-bankruptcy GM) as a partial funding source for its retiree health care VEBA. The VEBA has covered retiree health benefits since 2010. It was intended to cover retiree health benefits for 80 years, but it is unclear how long its funding will last.

Pensions were a central source of controversy during the bankruptcy of the Delphi Corporation (Delphi). Some (union and nonunion) employees had been promised a pension greater than the PBGC maximum. When the various Delphi pension plans were terminated by the PBGC, most unionized employees did not see their pensions fall because of supplemental pension coverage originally negotiated by Old GM and the UAW. The salaried Delphi workers, however, had no union, and some found themselves receiving lower pension benefits than had been promised by Delphi. Salaried workers formed a labor association, the Delphi Salaried Retirees Association (DSRA), with hopes of strengthening their position. The DSRA has been unsuccessful in its efforts to have their members' pensions increased, and the subsequent court case has not yet been settled.

The bankruptcy of the Patriot Coal Corporation (Patriot) was also complicated and contentious, even though federal law covering retired coal miners has been in place for many years. Both pension and retiree health benefits were central to the negotiations. The relevant union, the United Mine Workers of America (UMWA), is a multiemployer union where the collectively bargained contracts cover the employees of many employers. The UMWA Pension Trust was underfunded before the Patriot bankruptcy, and remains underfunded. In fact, some consider the potential insolvency of the coal employers' pension plan a threat to the overall solvency of PBGC's program on multiemployer pension plans. Because many Patriot retirees were employees of another employer, Peabody Energy, when they were actively working, the bankruptcy court ruled that Peabody, and not Patriot, was responsible for funding the VEBA newly created to cover health benefits.

Contents

Introduction ... 1
Protections for Retirees: Background Factors ... 2
Bankruptcy ... 2
Type of Labor Organization ... 4
Type of Employee ... 5
Employer Agreements with its Former Subsidiaries ... 6
Protections for Retirees' Pensions: The Pension Benefit Guaranty Corporation ... 6
Background ... 6
Single-Employer Plans ... 8
Multiemployer Plans ... 8
Protections for Retirees' Health Insurance: VEBAs ... 10
Advantages Associated with VEBAs ... 11
Risks Associated with VEBAs ... 11
Funding VEBAs ... 11
Protections for Retirees: Other Programs ... 12
Case Study 1: General Motors and the United Auto Workers ... 14
Background ... 14
Pensions ... 14
Retiree Health Insurance ... 15
Case Study 2: Delphi and the Delphi Salaried Retirees Association ... 17
Background ... 17
Pensions ... 18
Retiree Health Insurance ... 19
Case Study 3: Patriot Coal and the United Mine Workers of America ... 20
Background ... 20
Pensions ... 21
Retiree Health Insurance ... 22
Recent Legislation ... 23

Contacts

Author Contact Information ... 24

Introduction

Benefits for retired employees are of particular interest to policy makers because of the growing number of retirees and forecasts indicating that some future retirees may not have the necessary financial resources to maintain their standards of living.[1] Part of this congressional concern is what happens when bankrupt employers are unable to provide promised pension and health benefits to their retired employees.

This report explores the protections of benefits awarded retirees and future retirees of bankrupt private-sector employers under current law. Although there are many types of employee benefits, active employees, retirees, and the employers themselves are often especially concerned with post-retirement pensions and health insurance benefits, usually the two largest components of these so-called *legacy costs*. This analysis provides examples from two industries of interest to Congress where competitive pressures resulted in changes in each sector's business outlook: automobiles and coal.

Automotive Industry. The bankruptcy of the General Motors Corporation (Old GM) [2] in 2009 was the fourth-largest bankruptcy in U.S. history,[3] and was accompanied by a period of federal aid to the automotive industry. Two distinctive features of the Old GM bankruptcy were that federal financing was important to the ultimate outcome, and that the outcome was associated with a particularly strong labor union—the United Auto Workers (UAW).[4]

The report also focuses on the Delphi Corporation, an automobile parts supplier[5] where salaried retirees attempted to receive the benefits that hourly UAW retirees received.[6] The benefits to UAW hourly employees at Delphi had been contractually promised by Old GM in the pre-bankruptcy period. Salaried workers at Delphi had no such contractual promise. In order to facilitate increasing their benefits, salaried retirees formed a labor association, the Delphi Salaried Workers Association (DSRA).[7]

Coal Industry. The United Mine Workers of America (UMWA) represents over 73,000 coal miners.[8] Congress has periodically passed legislation covering retiree benefits for coal miners

[1] For more information, see Vickie Bajtelsmit, Anna Rappaport, and LeAndra Foster, *Measures of Retirement Benefit Adequacy: Which, Why, for Whom, and How Much*? Society of Actuaries, January 2013, https://www.soa.org/search.aspx?go=True&q=&page=1&pagesize=10&or=True&adv=True&with=measures+of+retirement+benefit+adequacy&within=0, and Alicia H. Munnell, Natalia Sergeyevna Orlova, and Anthony Webb, *How Important is Asset Allocation to Financial Security in Retirement?*, Center for Retirement Research at Boston College, CRR WP 2012-13, April 2012, http://crr.bc.edu/wp-content/uploads/2012/04/wp-2012-13.pdf.

[2] Old GM is a commonly used expression for GM before its bankruptcy. Details are given in a later section of this report.

[3] For more information, see http://money.cnn.com/2009/06/01/news/companies/gm_bankruptcy.

[4] The full name of the UAW is the International Union, United Automobile, Aerospace & Agricultural Implement Workers of America.

[5] Delphi was part of General Motors until 1999 when it was spun off as a separate company.

[6] It is not conventional to refer to "Old Delphi" and "New Delphi," partly because the name of the entity (Delphi Corporation) was the same before and after the bankruptcy.

[7] As will be discussed in a later section of this report, associations do not have the same collective bargaining rights as unions.

[8] For more information, see https://www.unionfacts.com/union/United_Mine_Workers.

since at least the 1940s. In October 1992, passage of the *Coal Act*[9] protected health benefits for some retired coal miners. In 2006, trust funds covering health insurance for retired miners received federal assistance.[10] Various bills dealing with pensions and health benefits provided by bankrupt coal employers were introduced in the first session of the 113th Congress. These bills were influenced by the July 2013 bankruptcy of the Patriot Coal Corporation (Patriot), an employer with coal mines in West Virginia and Kentucky.

These three case studies are not necessarily representative of all chapter 11 bankruptcy proceedings of large, unionized firms. Indeed, as case studies, they are not necessarily representative of all bankruptcy proceedings of large, unionized firms in industries in which Congress has become involved. Nevertheless, they do provide some evidence of how the federal government deals with retiree benefits in industries where competitive pressures have changed.

This report begins with a discussion of whether bankrupt firms can invalidate previous commitments covering retiree pensions and health insurance. The report next discusses the specific protections accorded to retiree pensions and health insurance benefits. Certain types of pensions are guaranteed by a quasi-public agency, while no such guarantee exists for retiree health insurance. The report concludes with brief case studies of the bankruptcies of Old GM, Delphi, and Patriot.[11]

Protections for Retirees: Background Factors

Whether retirees and future retirees receive their promised pensions and health insurance benefits depends on many factors. Four are discussed in this section: 1) the type of bankruptcy (e.g., chapter 7 or chapter 11) and the relevant provisions of the Bankruptcy Code;[12] 2) the type of labor organization (e.g., union, association, or not organized); 3) the type of employee (e.g., active employee or retired employee); and 4) the legal relationship between the bankrupt employer, any subsidiaries, and any parent company.

Bankruptcy

Employers generally file one of two forms of bankruptcy: chapter 7 (liquidation) or chapter 11 (reorganization). The bankruptcies filed by companies in the automotive and coal industries have generally been filed under chapter 11; therefore, this report will focus on chapter 11 bankruptcies after providing background information on both types.

Chapter 7

Chapter 7 of the Bankruptcy Code is designed for liquidation. For businesses, this generally involves complete cessation of the business and disposition of all assets. The employer files for chapter 7 bankruptcy when it believes that no amount of reorganization (including restructuring

[9] Title XIX, Subtitle C, Health Care of Coal Miners (P.L. 102-486, 1992).

[10] Title II, Subtitle B, Coal Industry Retiree Health Benefit Act (P.L. 109-432, 2006).

[11] This report does not cover labor organizations that have never been used at Old GM, New GM, Delphi, or Patriot. For example, Multiple Employee Welfare Associations (MEWAs) are not discussed.

[12] 11 U.S.C. § 101 *et seq.*

and financial modifications) would make the business profitable. Under chapter 7, a trustee is appointed to preside over the consolidation and ultimate distribution of the employer's assets. The assets would either be sold or transferred to the employer's creditors. In either case, the value of the assets would be used to reimburse claimholders in a prescribed manner. Those with secured claims would be paid first.[13] Remaining assets then would be used to pay select unsecured claims.[14] If the assets were sufficient to pay all the priority claims in full, the remaining assets would be used to pay the unsecured, non-priority claims on a proportional basis. Any claim for retiree health or pension benefits would be both unsecured and non-priority. In short, employers in chapter 7 bankruptcy are usually unable to fund any retiree health benefits and are only able to pay pension benefits if their pension trust fund has sufficient assets.

Chapter 11

Chapter 11 bankruptcy proceedings generally involve a plan to restructure a business so that it may become viable.[15] In other words, a debtor (often the employer) filing under chapter 11 generally expects its obligations to be reorganized so that the business can continue to exist.[16] Under chapter 11, the debtor generally remains in possession of the assets and continues to operate. The debtor here is known as the *debtor in possession*. The debtor in possession operates the business.[17] In some cases, a buyer may be found for some or all of the assets. However, no assets may be sold outside of the normal course of business without the approval of the bankruptcy court.

Retiree benefits do not automatically end when a company files under chapter 11. Two sections of the Bankruptcy Code govern the law determining retiree benefits before the debtor sells assets under chapter 11.[18] Section 1113 covers the rejection of a collective bargaining agreement (CBA) for unionized firms, and Section 1114 covers the payment of retiree health insurance in both unionized and nonunionized firms. [19]

11 U.S.C. Section 1113 – Rejection of Collective Bargaining Agreements

Section 1113 covers the conditions under which a debtor in possession may reject a CBA by either modifying or terminating it. Although the employees (through their union) can be expected

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[13] A secured claim is one where the claimant has the right to take and hold or sell certain property of the debtor in satisfaction of some or the entire claim. An unsecured claim is one where the claimant holds no special assurance of payment.

[14] More specifically, the remaining assets would be used to satisfy unsecured claims with priority under Section 507 of the Bankruptcy Code.

[15] When a firm has filed under chapter 11 and then determines that it will not be able to successfully reorganize, it may either convert the bankruptcy to chapter 7 or structure its own liquidation within chapter 11.

[16] Some chapter 11 cases, however, result in liquidation of the debtor company. Example include Circuit City, Whitehall Jewelers, and Linens'n'Things. For more information, see H. Jason Gold and Dylan G. Trache, *Liquidation of Troubled Businesses: Chapter 11 Liquidations Increasing*, Wiley Rein LLP, March 31, 2009, http://www.metrocorpcounsel.com/articles/11228/liquidation-troubled-businesses-chapter-11-liquidations-increasing.

[17] 11 U.S.C. § 1107(a).

[18] Much of this section is taken from archived CRS Report RL33138, *Employment-Related Issues in Bankruptcy*, by Robin Jeweler.

[19] A CBA is a negotiated contract governing the terms and conditions of employment. Information on the contents of a CBA is provided in the next section.

to argue that the negotiated benefits should continue to be awarded, the bankruptcy court may allow the debtor in possession to alter or terminate the CBA using the following procedure. The debtor in possession must first supply the authorized representative of the employees (usually a union officer) information justifying the need for modifying the employees' benefits and protections. The employees (through the union negotiator) and employer then engage in good faith negotiations with respect to proposals for alteration or termination of the CBA. If the parties cannot negotiate an agreement, the debtor in possession requests that the court alter or terminate the CBA. The court may take this step upon finding that the following conditions have been met:

1. The debtor in possession provided the authorized representatives of the employees with the necessary information,
2. The authorized representative has refused to accept the proposal without good cause, and
3. On balance, fairness favors voiding the CBA.

This section of the Bankruptcy Code applies only to unionized workplaces because nonunion workplaces will not have a CBA. As will be discussed, employees who have formed an association are nonunion employees.

11 U.S.C. Section 1114 – Payment of Insurance Benefits to Retired Employees

Section 1114 covers the conditions under which the debtor in possession may terminate or modify retiree health benefits, whether or not the employees are operating under a CBA. Section 1114 is modeled after Section 1113 and requires similar findings by the court to allow the debtor in possession to terminate or modify retiree health insurance benefits. The debtor in possession must first negotiate proposed modifications in benefits with an authorized representative of the retirees. If they cannot agree on changes, the court may permit modification if it finds that the proposed modification is *necessary* to permit the reorganization of the employer. In addition, all creditors, the employer, and all other affected parties must be treated fairly and equitably, and the authorized representative must have refused to accept the proposal without good cause.

Type of Labor Organization

Whether or not an employer is in bankruptcy, the benefits promised to current retirees and future retirees (i.e., active employees), and the risks assumed by the current retirees and future retirees, may depend on the type of labor union (or association) involved. The National Labor Relations Act (NLRA, P.L.74-198, as amended) recognizes the right of employees to engage in collective bargaining through representatives of their own choosing. The NLRA, however, does not recognize a right of retirees to form a union, or to engage in collective bargaining.[20]

The relationship between labor and management in bankruptcies involving collective negotiations depends on whether the union is a single-employer union (such as the UAW), a multiemployer union (such as the UMWA), or an association (such as the DSRA). A union's membership generally coalesces around a type of work done by that group of employees. Union workers in

[20] For more information on the NLRA, see CRS Report R42526, *Federal Labor Relations Statutes: An Overview*, by Gerald Mayer, Jon O. Shimabukuro, and Benjamin Collins.

U.S. firms are more likely to be paid by the hour than are many nonunion workers, who are often paid an annual salary.[21]

Most unions are *single-employer unions* where representatives of one employer's management and the union (on behalf of the employer's employees) bargain over the terms and conditions of employment. These terms and conditions generally include wages, hours of work, sick days, vacation days, health insurance, retiree benefits, and many other aspects of work.[22] The bargaining results in a contract, which is known as a *collective bargaining agreement* (CBA). Any employee who could be a member of the union, based on his or her occupation and perhaps other factors, is subject to the terms of the CBA even if the employee chooses not to join the union.[23]

Multiemployer unions represent employees of more than one employer in a single industry, and frequently negotiate the same employee benefit plan for all eligible employees of many employers. These plans are referred to as *Taft-Hartley* plans, and are relatively more likely to be found in industries where employees frequently move among different employers.[24] CBAs with Taft-Hartley plans ensure that union members can keep their pensions, health insurance, and all other benefits as they move from one employer to the next, because the union members are covered by the same CBA at their various places of employment. Unions in the trucking and construction industries often offer Taft-Hartley benefit plans.

Finally, some groups of active employees and/or retirees, sometimes known as *associations*, partly behave like unions, even though they are not officially certified as unions. In the current context, groups of retirees can form associations in order to facilitate the negotiations required by the Bankruptcy Code. It should be noted that the term association is not legally defined; there is nothing to prevent a union from calling itself an association. For example, the National Education Association is a union.[25] In addition, some representatives of the employers call themselves an association such as the coal industry's Bituminous Coal Operators Association (BCOA).

Type of Employee

When bargaining over the terms and conditions of employment, either two or three categories of workers are typically considered. Single-employer unions may bargain on behalf of *active* employees and *retired* employees. (These categories are related because active employees may someday become retired employees.) Both active and retired employees may face the loss of at least some of their retiree benefits should the single employer become insolvent or otherwise be unable to fund the promised benefits.

[21] For more information on the relationship between union status and salaried employment, see Daniel S. Hammermesh, "12 Million Salaried Workers are Missing," *Industrial and Labor Relations Review*, vol. 55, no. 4 (June 22, 2002), pp. 657-658.

[22] The NLRA specifies which terms and conditions of employment must be subject to bargaining, may be subject to bargaining, and must not be subject to bargaining.

[23] Employees do not have to join the union or pay union dues in so-called "right to work" states. For more information, see CRS Report R42575, *Right to Work Laws: Legislative Background and Empirical Research*, by Benjamin Collins.

[24] The Labor Management Relations Act of 1947 (P.L. 80-101) is commonly known as the Taft-Hartley Act. Although the majority of the Act restricted the power of unions, the Act also clarified the conditions under which unions and employers can use employer funds to provide pensions and other employee benefits to unionized employees. This part of the Taft-Hartley Act can therefore be viewed as a precursor to ERISA.

[25] For more information, see http://www.nea.org/home/18469.htm.

Multiemployer unions, however, are also associated with a third type of employee: the *orphan* retiree. An orphan retiree is a retiree who is covered by a multiemployer CBA entitling him or her to benefits from an employer that is no longer solvent. However, other employer signatories to the contract are solvent. In other words, the multiemployer CBA may specify that an employer is obligated to pay for the retiree's benefits, but the employer is unable or unwilling to do so for a variety of reasons; it may be entirely out-of-business, in bankruptcy proceedings, otherwise lacking funds, or refusing to pay the benefits. This retiree then becomes an orphan retiree. Other employers who are signatories to the CBA are expected to pay benefits for the orphan retirees. In this case, a solvent employer may find itself funding retiree benefits for individuals who were never employed by the company.

Employer Agreements with its Former Subsidiaries

Some employers entering chapter 11 bankruptcy, such as Old GM, have a long history as independent firms. Other employers, however, were recently part of a larger entity. For example, Delphi was once a division of Old GM and Patriot was once a part of Peabody Energy. The process by which Delphi and Patriot became independent employers is known as a *spin-off*, and Old GM and Peabody were the *parent* employers. The protections for retirees in bankrupt companies that were once a part of larger enterprises depend on the spin-off arrangements negotiated between the union and the parent company. In some cases, the parent company assumes responsibility for the pensions and/or retiree health benefits of the employees transferred to the new spin-off company.

The next three sections of this report discuss protections for employee pensions, protections for retiree health insurance, and other health insurance protections available for retirees.

Protections for Retirees' Pensions: The Pension Benefit Guaranty Corporation

Background

The Employee Retirement Income Security Act of 1974 (ERISA, P.L. 93-406) protects the interests of participants in certain employee benefit plans.[26] ERISA requires that benefit plans be operated solely in the interest of the participants and their beneficiaries and for the exclusive purpose of providing benefits to participants and their beneficiaries. It protects employees' pensions by establishing vesting requirements (how long an employee has to work to be entitled to benefits); funding requirements (how much the employer must set aside to pay for current and future benefit obligations); and pension insurance (which will pay retiree benefits in case of the plan sponsor's bankruptcy). Pension obligations must be prefunded by the employer, and the present value of the plan's assets must be large enough to cover the present value of the plan's liabilities.[27]

[26] CRS Report RL34443, *Summary of the Employee Retirement Income Security Act (ERISA)*, by Patrick Purcell and Jennifer A. Staman.

[27] Present value is the current worth of a future sum of money or stream of cash flows given a discount rate. The higher (continued...)

ERISA pension insurance covers private-sector *defined benefit* (DB) pension plans. A DB plan typically pays a set monthly amount after the employee's retirement. The specific amount paid is often based on a combination of the employee's salary and years of service. Some DB plans, however, offer the benefit as a fixed lump-sum payment. Under ERISA, participants in DB plans do not own the pension plan assets, but have a claim on the amount of their vested benefits. Pension plan sponsors may not reduce workers' vested pension benefits.[28] In addition, employee pension trust funds are not part of the bankruptcy estate available to satisfy creditor claims.

ERISA established the Pension Benefit Guaranty Corporation (PBGC) to insure the pension benefits of workers in private sector DB plans. The PBGC says it has "protect[ed] more than 42 million workers and retirees in private defined benefit pension plans ...by encouraging companies to keep their plans, and by paying benefits when they cannot."[29] To fund its benefit obligations, the PBGC collects insurance premiums from employers that sponsor insured pension plans, receives funds from the pension plans it takes over, and earns money from investments. The insurance premiums are set by Congress.[30] The benefits to retirees paid by the PBGC do not come from taxpayer funding, and the benefit obligations of the PBGC are not obligations of the United States.[31] Pensions disbursed by the PBGC to any retiree may not exceed a statutorily guaranteed limit.

The PBGC has a stated goal of avoiding the termination of plans in cases of bankrupt companies:

> Even after a company enters bankruptcy, we work to try and preserve its plans. We take an active role in bankruptcies to prevent unnecessary plan terminations, and to pursue claims on behalf of the plan participants, and the pension insurance program.[32]

The PBGC maintains two separate insurance programs: one for single-employer pension plans and one for multiemployer pension plans. A single-employer pension plan is maintained by one employer for its eligible employees. A multiemployer plan is maintained under a collective bargaining agreement by more than one employer for all of their eligible employees. In 2013, the PBGC single-employer plan had a deficit of $27.4 billion, while the multiemployer plan had a deficit of $8.3 billion.[33]

(...continued)

the discount rate, the lower the present value of the future cash flows. The choice of discount rate is critical to an accurate valuation of future liabilities.

28 Defined contribution (DC) plans are a second type of pension plan where the employee owns the assets as soon as the plan is vested. However, DC plans do not promise a set value at retirement. DC plans include profit-sharing and 401(k) plans.

29 Pension Benefit Guaranty Corporation, *Helping Secure Retirements*, Annual Report 2013, p. 4, https://www.pbgc.gov/Documents/2013-actuarial-report.pdf.

30 Insurance premiums are updated periodically, and depend on the risks of ongoing coverage by the PBGC. The American Academy of Actuaries argues that legacy costs should be incorporated into the premium-setting process. For more information, see American Academy of Actuaries, *Examining the PBGC Premium Support Structure*, Issue Brief, April 2012, http://actuary.org/files/publications/IB_on_PBGCPremium_120426.pdf.

31 ERISA 4002 § 1302(g)(2) and 29 U.S.C. § 1302(g)(2).

32 Pension Benefit Guaranty Corporation, *Excellence in Customer Service*, Annual Report 2012, p. 15, https://www.pbgc.gov/documents/2012-annual-report.pdf.

33 Pension Benefit Guaranty Corporation, *Helping Secure Retirements*, Annual Report 2013, p. 26, https://www.pbgc.gov/Documents/2013-actuarial-report.pdf. For more information, see CRS Report RS22624, *The Pension Benefit Guaranty Corporation and Single-Employer Plan Terminations*, by Jennifer A. Staman and Erika K. Lunder.

Single-Employer Plans

The PBGC protects the pension benefits of about 35 million active and retired employees in about 23,000 single-employer pension plans.[34] The PBGC categorizes single-employer pension plan terminations into three categories.

- A *standard termination* occurs when the employer's plan has sufficient funding to cover future benefits and distribute all plan benefits as insurance company annuities or lump sum payments.[35] In this case, the PBGC's role is solely to ensure compliance with the plan termination rules of ERISA.
- A *distress termination* occurs when the employer's plan does not have sufficient assets to pay all the promised benefits. The PBGC determines whether the employer meets at least one of four financial distress tests.[36] In this case, the PBGC becomes the plan's trustee and uses its own assets to insure that retirees and future retirees receive the benefits to which they are entitled, up to the guaranteed limit.
- An *involuntary termination* occurs when the PBGC chooses to terminate a pension plan, even if the employer has not started termination proceedings of its own accord. Involuntary plan termination occurs when the PBGC believes that the plan owners can no longer fulfill their responsibility to pay the current and future retirees their pension benefits as they become due.

The PBGC maximum guarantee for a pension plan terminated in 2014 is $4,943 per month ($59,318 per year) for retirees who begin receiving pensions at the age of 65.[37] If a participant in a terminated pension plan had been promised a pension greater than $4,943 a month from the employer, he or she would receive a reduced monthly pension from the PBGC because of the statutory maximum benefit.

Multiemployer Plans

The PBGC insures the pensions of about 10 million active and retired employees in about 1,400 multiemployer pension plans.[38] Benefit contributions for multiemployer plans are usually based on employer contributions in proportion to their current (covered) employment. The employer contributions may also be tied to some measure of employer output such as the number of items produced, tons of coal mined, or gross sales. Most multiemployer plans are governed by a board

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[34] Pension Benefit Guaranty Corporation, *Helping Secure Retirements*, Annual Report 2013, p. 4, https://www.pbgc.gov/Documents/2013-actuarial-report.pdf.

[35] In this context, an annuity is a fixed amount of money paid periodically over time to the retiree.

[36] The four conditions are listed at Pension Benefit Guaranty Corporation, *Plan Termination Fact Sheet*, p. 2, http://www.pbgc/gov/res/factsheets/page/termination.html.

[37] Amounts are reduced so that retirees receive actuarially neutral pension benefits if they begin receiving benefits before the age of 65 or in a non-standard form. One example of a non-standard form is a joint and survivor annuity, which must have at least two annuitants. Payments are continued as long as one of the annuitants is alive. Pension Benefit Guaranty Corporation, *PBGC Maximum Insurance Benefit Increases for 2014*, Press Release, November 6, 2013, http://www.pbgc.gov/news/press/releases/pr13-13.html.

[38] Pension Benefit Guaranty Corporation, *Helping Secure Retirement*, Annual Report 2013, p. 4, http://www.pbgc.gov/Documents/2013-annual-report.pdf.

of trustees, with equal representation from employers and employees. Contributions are held in a trust fund, and assets in the plan never revert back to contributing employers.

There are various categories to describe a multiemployer plan's funded status. A plan is in *critical status* if at least one of five conditions holds. For example, one condition is that the plan's ratio of assets to liabilities is less than 65% and the value of the plan's assets and contributions will be less than the value of the benefits within five years.[39] Multiemployer pension plans in critical status must adopt a rehabilitation plan (a range of options that will allow the plan to emerge from critical status during a 10-year rehabilitation period). In addition, the employers that sponsor plans in critical status may not increase pension benefits during the rehabilitation period.[40]

A plan is in *endangered status* if 1) the plan is less than 80% funded or 2) the plan is underfunded in the current year or is projected to be underfunded in one of the next six years. A plan is in *seriously endangered status* if the plan meets both criteria for endangered status. Multiemployer plans in endangered status must adopt a funding improvement plan that will reduce the plan's underfunding by 33% during a 10-year funding improvement period. Multiemployer plans in seriously endangered status must adopt a funding improvement plan that will reduce the plan's underfunding by 20% during a 15-year funding improvement period. Plans in endangered status or seriously endangered status may not increase pension benefits during the funding improvement period.[41]

An employer may leave a multiemployer pension plan for a variety of reasons, including when the employer goes out of business, negotiates a new CBA, or moves the business out of the pension plan coverage areas. An employer that withdraws from a pension plan may be assessed withdrawal liabilities.[42]

Multiemployer pension plans may become insolvent when the plan is unable to pay its benefit obligations. Unlike single-employer plans, multiemployer plans cannot be terminated as part of any employer's bankruptcy proceedings. When a multiemployer plan becomes insolvent, the PBGC provides a loan to the trustees of the pension plan, and the pension plan uses the loan to pay benefits. The PBGC never becomes the trustee of a multiemployer plan. Because many multiemployer pension plans face financial difficulties, the PBGC calls itself "flexible when plans propose new rules governing employer liability."[43] Among other innovations, the PBGC has attracted new employers by limiting their legacy liabilities.

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[39] For a complete description of the conditions, see Department of Labor, The Department of the Treasury, and the Pension Benefit Guaranty Corporation, *Multiemployer Pension Plans: Report to Congress Required by the Pension Protection Act of 2006*, January 2013, p. 37, http://www.pbgc.gov/documents/pbgc-report-multiemployer-pension-plans.pdf.

[40] For more information, see CRS Report R43305, *Multiemployer Defined Benefit (DB) Pension Plans: A Primer and Analysis of Policy Options*, by John J. Topoleski, p. 7.

[41] For more information, see CRS Report R43305, *Multiemployer Defined Benefit (DB) Pension Plans: A Primer and Analysis of Policy Options*, by John J. Topoleski, p. 8.

[42] Pension Benefit Guaranty Corporation, *Helping Secure Retirements*, Annual Report 2013, p. 6, http://www.pbgc.gov/documents/2013-annual-report.pdf.

[43] Pension Benefit Guaranty Corporation, *Excellence in Customer Service*, Annual Report 2012, p. 8, http://www.pbgc.gov/documents/2012-annual-report.pdf.

The PBGC maximum guarantee for an insolvent multiemployer pension in 2013 is $1,073 per month ($12,870 per year) for those who retire with 30 years of work at age 65.[44] This maximum benefit level from the PBGC may be less than the retiree would have received under the original CBA.

The overall financial health of the PBGC multiemployer pension trust is in some doubt.[45] For example, the multiemployer trust reported a net loss of $3.02 billion in fiscal year (FY) 2012, up from a net loss of $2.47 billion in FY 2011. In addition, the PBGC's projections indicate that there is a 50% chance that the multiemployer insurance program will be insolvent by the end of FY 2022 and a 90% chance of insolvency by the end of FY 2025.[46] Two multiemployer pension plans are thought to be a particular threat to the multiemployer trust's overall solvency. Although the PBGC does not name the plans, one is in the "agriculture, mining, and construction" industry category.[47]

Protections for Retirees' Health Insurance: VEBAs

ERISA does not require retiree health insurance benefits to be prefunded. In practical terms, even if a retiree was contractually promised $400 a month in health insurance benefits, the employer is not required to have $400 a month available. In addition, retiree health insurance claims are neither secured nor priority in bankruptcy. Therefore retirees have no guarantee that they will actually receive any of the benefits they were promised in a CBA. One way to guarantee at least some funding for health insurance benefits is for the (active and/or retired) employees to form a Voluntary Employees' Beneficiary Association (VEBA). VEBAs are tax-advantaged trust funds, first created by the Revenue Act of 1928. VEBAs can finance many types of employee benefits, including retiree health insurance benefits (but not pensions).[48]

VEBAs historically were owned by a single employer. More recently, however, many newly-created VEBAs are structured as a trust independent of the employer. These trusts are sometimes termed independent VEBAs, new VEBAs, or stand-alone VEBAs. An independent VEBA must be controlled by its membership, by independent trustees, or by other fiduciaries designated by the membership. Trustees chosen by a CBA are considered designated by the membership. VEBAs have been created or modified both as part of bankruptcy proceedings and as part of the normal course of business in healthier entities. In all cases, the trust acts in the fiduciary interest of the employees. Nevertheless, the creation of a VEBA cannot be characterized as a victory for

[44] For details on this calculation, see the worksheets at http://www.pbgc.gov/prac/multiemployer/multiemployer-benefit-guarantees.html#2. This is the most recent year for which data are available.

[45] For more information, see CRS Report R43305, *Multiemployer Defined Benefit (DB) Pension Plans: A Primer and Analysis of Policy Options*, by John J. Topoleski.

[46] Pension Benefit Guaranty Corporation, *FY 2013 PBGC Projections Report*, p. 1, http://www.pbgc.gov/documents/Projections-report-2013.pdf.

[47] Pension Benefit Guaranty Corporation, *Excellence in Customer Service*, Annual Report 2012, p. 35, http://www.pbgc.gov/documents/2012-annual-report.pdf.

[48] Rules for VEBAs are found in IRC § 501(c)(9). This section covers VEBAs used for health insurance in a workplace with a union, association, or other group of workers sharing a common bond. The regulations concerning the tax deductibility of VEBA income depend on the union status of the workplace, the particular employee benefits the VEBA funds, and other factors. VEBAs provide tax savings when they cover health insurance in an organized workplace. Much of the information in this section is drawn from archived CRS Report R41387, *Voluntary Employees' Beneficiary Associations (VEBAs) and Retiree Health Insurance in Unionized Firms*, by Carol Rapaport.

either the employer or the employees; each individual VEBA differs with respect to funding levels and other terms, and the funding levels and other terms themselves depend on the relative bargaining power of the employer and employees.

Advantages Associated with VEBAs

VEBAs, as tax-exempt instruments, provide the employer incentives to prefund health benefits.[49] More specifically, contributions to some VEBAs are tax deductible, and the investment income sometimes grows tax-free. In addition to these tax advantages, VEBAs can improve an employer's financial position. Employers are required by the Financial Accounting Standards Board (FASB), which establishes financial and reporting standards for private-sector U.S. firms, to use accrual accounting when calculating liabilities for retiree health benefits; in other words, the employer's liability increases as the number of employees eligible for benefits, along with the expected amount of these benefits, increases. This liability must be reported on the firm's balance sheet, where a particularly large liability value can depress the firm's market value. Removing the firm's liability for current and future benefits by transferring the benefits to a VEBA (independent of the employer) can sometimes increase the market value of the employer. This increase in market value is a primary advantage of a VEBA for the employer.

A primary advantage of a VEBA for the employee is a reduction in the risk associated with actually receiving promised retiree benefits. If the employer has already deposited funds into a dedicated retiree health VEBA, these funds must go to their intended recipients. They may never revert back to the employer. In many instances, without a VEBA, the employees have no recourse if an employer lacks the funds to pay for promised retiree health benefits. If an employer falls short, or simply decides to place its money elsewhere, no law or regulation compels the firm to honor past promises.

Risks Associated with VEBAs

The presence of a VEBA does not automatically remove all the risk to the employee, because the VEBA itself must have assets and income. For current and future retirees to receive promised benefits there must be sufficient funds in the VEBA to cover the cost of benefits. A VEBA that contains sufficient funds to cover the expected costs of the benefits over the life of the VEBA is known as a *fully funded* VEBA. Several scenarios can prevent VEBAs from being fully funded. First, the calculations of the funding needed for the VEBA to cover the expected costs of the retiree benefits may have been incorrect. Second, the employer may not have contributed the amount necessary to fully fund the VEBA. In any case, federal law does not require that VEBAs be fully funded.

Funding VEBAs

The amount of money necessary to fully fund the VEBA cannot be calculated easily.[50] For illustrative purposes, consider a firm that wants to cover retiree health insurance for the 10,000

[49] Archived CRS Report R41387, *Voluntary Employees' Beneficiary Associations (VEBAs) and Retiree Health Insurance in Unionized Firms*, by Carol Rapaport, pp. 3-4.

[50] Ellen O'Brien, *What Do the New Auto Industry VEBAs Mean for Current and Future Retirees?*, AARP Public Policy Institute, Publication #14, March 2008.

employees who were actively working on December 31, 2013, plus their surviving spouses and dependents. The calculation of the level of funding needed to meet such a guarantee typically involves forecasting the following variables:[51]

- the expected date of retirement for each employee working on December 31, 2013;
- each employee's (and his or her covered family's) life expectancy;
- each employee's (and his or her covered family's) health care utilization over time;
- the rate of medical inflation over time;
- the return on the VEBA trust's assets over time; and
- changes in the tax code affecting the value of the VEBA.

If any of these forecasts prove to be incorrect, then the amount of money needed to fully fund the VEBA over the course of its lifetime would be calculated incorrectly.[52]

The calculation becomes more complicated if *future* employees (i.e., those who are not yet hired) are eligible for retiree health benefits funded from the VEBA. The number of such employees, together with the years in which they will start work and ultimately retire, must also be estimated. Calculating the fully funded level for an employer that has terminated the availability of benefits for new hires is therefore easier than calculating the fully funded level for a financially healthy employer that intends to continue offering retiree health benefits to new hires.

Some VEBAs are created as part of the course of doing business, while others are created during chapter 11 bankruptcy proceedings. A VEBA may also be negotiated as part of a standard CBA, and then modified during bankruptcy proceedings. Financial negotiations can be contentious. A percentage of the amount needed to fully fund the VEBA is negotiated. As would be expected, the employees prefer to receive as close to 100% of the fully-funded amount as possible, while the employer prefers that the percentage be as small as possible. Additionally, the composition of the funding must be agreed upon. The employer can transfer any number of assets to the VEBA, including cash and notes. If the union accepts stock in the company as a VEBA funding source, the resulting situation becomes unusual in that a trust fund acting on behalf of the employees becomes a partial owner of the company.

Protections for Retirees: Other Programs

Apart from the PBGC, there are no federal programs that provide pension benefits to retirees whose former employer cannot meet its pension obligations. On the other hand, retirees may have a number of additional health insurance options available to them.

Retirees who no longer have access to health insurance through their former employer(s) may be able to obtain coverage through Medicare, Medicaid, health insurance offered through the

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[51] Archived CRS Report R41387, *Voluntary Employees' Beneficiary Associations (VEBAs) and Retiree Health Insurance in Unionized Firms*, by Carol Rapaport, p. 5.

[52] It is theoretically possible that two or more forecasting errors could offset each other.

exchanges established by the Patient Protection and Affordable Care Act of 2010 (ACA, P.L. 111-148 as amended by P.L. 111-152) or, in the case of some chapter 11 bankruptcies, Title X of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA, P.L. 99-272). Retired individuals who have End Stage Renal Disease as well as those who are disabled or aged 65 or older generally will be eligible for Medicare. Some lower-income individuals may become eligible for Medicaid in states that chose to expand their Medicaid program. Additionally, the health insurance exchanges established by ACA became active on January 1, 2014. Retirees can purchase health insurance policies through the exchanges; however, only those who are ineligible for Medicare and Medicaid will be eligible for premium credits and cost-sharing subsidies, provided they meet income and perhaps other requirements.

Under COBRA, employers are required to permit employees and family members to continue their group health insurance coverage at their own expense, but at group rates, if they lose coverage because of designated work or family-related events.[53] Among the "qualifying events" that trigger COBRA's continuation coverage is an employer's filing a case under the Bankruptcy Code. The retired employee is eligible for COBRA continuation coverage for life, and his or her spouse and dependents are eligible for continuation coverage for 36 months. This continuation coverage, however, is contingent upon the employer maintaining a health insurance plan for active employees.

Two additional congressionally authorized programs have provided retiree funding in the past few years, but have expired. First, Section 1102 of ACA authorized $5 billion in funding for the Early Retiree Reinsurance Program (ERRP).[54] The ERRP reimburses employers for especially high health insurance claims incurred by early retirees. The early retirees themselves do not receive any reimbursements from this program. Rather, the reimbursements are used to fund various cost-savings and other improvements to the employer's provision of health insurance. The ERRP began accepting for reimbursement claims incurred on or after June 1, 2010, and was closed to new enrollees as of May 6, 2011, because expenditure projections indicated that the $5 billion would be exhausted by the employers already enrolled. The authorization for the ERRP ended on January 1, 2014.

Second, the Health Coverage Tax Credit (HCTC), a federal income tax credit, has subsidized 72.5% of the cost (premiums) of qualified health insurance for eligible taxpayers and their family members.[55] Eligibility for the HCTC is limited to three groups of taxpayers, two of which are individuals eligible for the Trade Adjustment Assistance (TAA) program. The third group consists of individuals whose pension plans were taken over by the PBGC. This credit expired on January 1, 2014, and new enrollees must have registered before October 1, 2013.[56]

The remainder of this report provides three examples of bankruptcy proceedings in unionized entities where the retirees' pensions and health insurance benefits received substantial federal attention. The first example is Old General Motors and the United Auto Workers, the second

[53] This paragraph is taken from archived CRS Report RL33138, *Employment-Related Issues in Bankruptcy*, by Robin Jeweler, pp. 8-9.

[54] The information in the paragraph is from CRS Report R43048, *Overview of Private Health Insurance Provisions in the Patient Protection and Affordable Care Act (ACA)*, by Annie L. Mach, p. 21.

[55] The information in this paragraph is from archived CRS Report RL32620, *Health Coverage Tax Credit*, by Bernadette Fernandez.

[56] The information in this paragraph is from Internal Revenue Service, http://www.irs.gov/Individuals/The-Health-Coverage-Tax-Credit-%28HCTC%29-Program.

example is Delphi and the Delphi Salaried Retirees Association, and the final example is Patriot and the United Mine Workers of America.

Case Study 1: General Motors and the United Auto Workers

Background

On June 1, 2009, the *General Motors Corporation* filed a chapter 11 bankruptcy petition. On July 5, 2009, the bankruptcy court approved the sale of the company's "good" assets in a "section 363 sale."[57] The sale closed on July 10, 2009.[58] The buyer was a newly formed corporation that, after the sale was completed, changed its name to *General Motors Company*.[59] In this report, "Old GM" is used to refer to General Motors Corporation, and "New GM" is used to refer to General Motors Company.

Funding supplied by the Troubled Asset Relief Program (TARP) was instrumental in the restructuring of Old GM. TARP was a part of the Emergency Economic Stabilization Act of 2008 (EESA, P.L. 110-343).[60] EESA was originally intended to purchase assets and equity from financial institutions, but was extended to the automobile industry by President George W. Bush in 2008 and further financial assistance was granted by President Barack Obama in 2009. In total, Old GM and New GM together received $50.2 billion in financial support from the Department of the Treasury.[61]

Pensions

Old GM maintained separate pension trusts for hourly and salaried workers. Unionized employees hired prior to October 15, 2007, are eligible for DB pensions.[62] The amount of the pension was negotiated and depends on the number of years of service, with a supplemental

[57] In re: General Motors Corp., "Decision On Debtors' Motion For Approval Of (1) Sale Of Assets To Vehicle Acquisition Holdings LLC; (2) Assumption And Assignment Of Related Executory Contracts; And (3) Entry Into UAW Retiree Settlement Agreement," http://www.motorsliquidationdocket.com/pdflib/2967_50026.pdf.

[58] Motors Liquidation Company, Court Documents and Claims Register, General Information, http://www.motorsliquidationdocket.com/.

[59] Media reports at the time widely reported the event as GM emerging from bankruptcy; however, the company that entered bankruptcy in June remained in bankruptcy after the sale, although its name was changed to "Motors Liquidation Company." General Motors Company was a completely new company. See e.g., David Bailey, "GM Emerges from Chapter 11 Bankruptcy," Reuters, July 13, 2009, http://blogs.reuters.com/great-debate-uk/2009/07/13/gm-emerges-from-chapter-11-bankruptcy/; "A Leaner GM Zooms Out of Bankruptcy," Associated Press, July 10, 2009, http://www.nbcnews.com/id/31826205/ns/business-autos/t/leaner-gm-zooms-out-bankruptcy/#.UzmZwoVxD3U; "A 'New' GM Emerges From Bankruptcy," National Public Radio, July 10, 2009, http://www.npr.org/templates/story/story.php?storyId=106459662.

[60] *Special Inspector General for the Troubled Asset Relief Program*, SIGTARP 13-003, August 15, 2013, p.1.

[61] For a full description of the GM assistance under TARP, see CRS Report R41978, *The Role of TARP Assistance in the Restructuring of General Motors*, by Bill Canis and Baird Webel.

[62] Those hired on or after this date may participate in defined contribution pension plans.

amount for early retirees with at least 30 years of service.[63] Taken together (that is, including New GM employees represented by any of its unions plus nonunionized employees) New GM pensions were underfunded by $17.1 billion at the end 2009.[64] Despite this underfunding, pensions were not a central bargaining issue in the late 2000s. There was virtually no debate over UAW pensions during the bankruptcy process, and no changes were made to the pension plans.[65]

Pension controversies did emerge after the bankruptcy. Concerned about possible large increases in their required pension contributions, New GM offered some *salaried* workers a buy-out in 2012; these workers could accept a lump-sum payment in exchange for giving up all rights to any other kind of pension support. About 30% of 44,000 eligible, salaried workers accepted this offer.[66] Additionally, New GM has spoken of giving the UAW workers the option of trading their promised DB pensions for a lump-sum payment.

Retiree Health Insurance

Old GM has historically provided generous health insurance coverage. In 2005, the then-Chairman and CEO of Delphi remarked, “Some have said GM is actually a giant HMO that happens to make cars!”[67] Over time, however, the cost of providing this insurance proved to be high. For example, it was reported that health care costs were the single largest component of the growing disparity in labor costs between the domestic and foreign automakers.[68] A 2007 memorandum of understanding covering post-retirement medical care states that UAW and Old GM have “discussed that the current cost of providing post-retirement medical care is one of the most critical issues facing the Company’s ability to compete in the North American marketplace.”[69]

During the 2007 contract negotiations, Old GM agreed to contribute a percentage of its projected retiree health liabilities to an independent VEBA intended to fund retiree health benefits for 80 years. Following their initial VEBA contributions in 2007, Old GM would also make additional contributions to the VEBA beginning in 2008. According to one analyst, Old GM contributions were projected to fund about 68% of their future retiree health obligations over the life of the VEBA (in present value terms).[70] The 2007 contract stipulated that GM was responsible for funding retiree health until January 1, 2010. On that date, the VEBA (officially known as the *UAW Retiree Medical Benefits Trust)* took over all funding responsibilities for retiree health insurance from GM. Only those retirees (and their eligible spouses, surviving spouses, and

[63] General Motors, Annual Report, 2012, p. 123.

[64] General Motors, Annual Report, 2010, p. 89.

[65] CRS analysis of contractual documents.

[66] Deepa Seetharaman, "GM spends $3.6 billion on lump-sum pension buyouts," *Reuters*, October 31, 2012.

[67] The Associated Press,"Remarks by Delphi Corp. Chairman and CEO Robert "Steve" Miller on Friday," *The Associated Press State and Local Wire*, October 28, 2005, http://www.wallstreet-online.de/discussion/1016181-421-430/super-meldung-bei-delphi, BC cycle.

[68] Bill Vlasic, "Seeking the right balance; Carmakers need cuts; union fights to preserve what it has," The Detroit News, July 17, 2007, p. 1A.

[69] Form 8-K, Ex. 10-1, Memorandum of Understanding, Post-Retirement Medical Care, September 26, 2007, http://online.wsj.com/public/resources/documents/gmfiling20071015.pdf.

[70] Ellen O'Brien, *What Do the New Auto Industry VEBAs Mean for Current and Future Retirees?*, AARP Public Policy Institute, Insight on the Issues, March 2008, p. 7, http://assets.aarp.org/rgcenter/econ/i4_veba.pdf.

dependents) eligible for retiree medical benefits from Old GM as of October 15, 2007, can participate in the VEBA.[71]

The VEBA is one trust with three separate accounts, one each for New GM, Ford, and Chrysler. The assets in each account are separate, and one automaker's account cannot be used to fund benefits for another automaker. Nevertheless, the VEBA files a single tax return. The VEBA is managed by an independent board of 11 trustees appointed by the UAW and the bankruptcy court as part of the bankruptcy settlement agreements with New GM and Chrysler.[72]

Because Old GM had a large debt load and no cash flow when it entered bankruptcy, the UAW accepted a contribution of stock in New GM. The restructuring agreement made the UAW a partial owner of New GM. Such an ownership structure is not typical of bankruptcy decisions. When the VEBA became the source for retiree health benefits on January 1, 2010, the VEBA held $14.5 billion in investment assets, 17.5% of New GM's common stock, New GM's preferred stock with a face value of $6.5 billion, and a note with a face value of $2.5 billion.[73] Because New GM's common stock was not publically traded at that time, there was great uncertainty associated with the ultimate value of owning 17.5% of the common stock.[74] The VEBA ownership in New GM fell from 17.5% in 2009 to 9.2% in 2014 as the VEBA sold stock.[75]

It is difficult to evaluate the performance of a trust fund designed to last 80 years after the passage of only five years. Nevertheless, the VEBA officers have emphasized the investment risks when communicating with the membership. In particular, they have mentioned the "market meltdown" of 2008 and early 2009, and the uncertainty associated with projections of future medical costs.[76] In fact, the 2011 contract negotiations covered the possibility of diverting up to 10% of profit sharing to the VEBA.[77]

The most recent legislation concerning the Old GM bankruptcy was introduced in the 111th Congress, and concerned the use of TARP funding in the bankruptcy proceedings. The bills were **H.R. 4118**, **H.R. 6046**, and **S. 3526**.

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[71] UAW, *UAW Retiree Medical Benefits Trust*, no date, p. 49. In addition, some Delphi retirees are eligible to participate.

[72] Ford never filed for bankruptcy.

[73] Letter from UAW Retiree Medical Benefit Trust to UAW GM Retiree or Surviving Spouse, May 17, 2010, http://www.uawtrust.org/AdminCenter/Library.Files/Media/501/Trust%20Communications/GM/GM%202010%20letter.pdf.

[74] When the U.S. Treasury sold a block of New GM stock through an initial public offering in fall 2010, it was priced at $33 per share. It later fell to a low of about $19 per share, climbed to more than $41 per share, and traded just over $33 a share on August 5, 2014.

[75] CRS Report R41978, *The Role of TARP Assistance in the Restructuring of General Motors*, by Bill Canis and Baird Webel.

[76] Letter from UAW Retiree Medical Benefits Trust to UAW GM Retiree or Surviving Spouse, May 17, 2010, http://www.uawtrust.org/AdminCenter/Library.Files/Media/501/Trust%20Communications/GM/GM%202010%20letter.pdf.

[77] Kristin Dziczek, *An Analysis of the 2011 UAW-Detroit Three Contracts, and a Look Ahead to 2015 Talks*, Center for Automotive Research (CAR), Nineteenth Annual Automotive Outlook Symposium, Federal Reserve Bank of Chicago, June 1, 2012, http://www.chicagofed.org/digital_assets/others/events/2012/aos/dziczek.pdf.

Case Study 2: Delphi and the Delphi Salaried Retirees Association

Background

The Delphi Corporation supplies parts and components directly to vehicle manufacturers. Delphi was originally a part of Old GM, was spun off into its own public company in 1999, and continues to have New GM as its primary customer.[78] As part of the spin-off agreement, Old GM and the UAW negotiated the benefits of union employees who were being moved from Old GM employment to Delphi employment. Old GM agreed to cover the pension benefits for Delphi employees (former Old GM employees) who retired prior to October 1, 2000. The pension benefits of employees who retired on or after October 1, 2000, became the obligations of the various Delphi pension plans.[79]

In addition, Old GM entered into a benefit guarantee agreement with the UAW covering employees whose pensions might be taken over by the PBGC in the future. In the event of a termination of the Delphi pension plans for hourly workers, the guarantee agreement obligated GM to supplement the benefits for workers who received the statutory maximum benefit from the PBGC. In other words, GM agreed to a "top-up" for each covered UAW retiree. A top-up is a payment of the difference between the benefit received from the PBGC and the benefit that would have been received had the plan not been terminated. Salaried employees were not UAW members and were not covered by this top-up guarantee.

In October 2005, Delphi entered chapter 11 bankruptcy. Delphi emerged from bankruptcy in October 2009 after a group of Delphi's lenders purchased most of Delphi's assets; New GM also assumed some of the Delphi assets.

The PBGC assumed responsibility for Delphi's DB pension plans in July 2009. In total, the pension plans had almost 70,000 participants and were underfunded by about $7.2 billion, according to the PBGC.[80]

This case study focuses on a group of Delphi salaried retirees who did not have the protections of a CBA. These retirees did not receive the same pension and retiree health benefits as the unionized retirees. On one hand, the salaried workers never had contractual rights to the benefits that the union workers had. On the other hand, the salaried workers argued that it was only fair that they receive the same benefits as their unionized coworkers. To pursue this matter, many of the Delphi salaried workers formed the Delphi Salaried Retirees Association (DSRA). The DSRA was recognized as an authorized representative of the retired employees by the bankruptcy court.

[78] The entire world-wide entity, including all subsidiaries, is named Delphi Automotive PLC. This report covers the American subsidiary, which is named The Delphi Corporation; see Exhibit 21.1 of the SEC Form 10-K available at http://investor.delphi.com/phoenix.zhtml?c=245477&p=irol-sec.

[79] CRS Report R42076, *Delphi Corporation: Pension Plans and Bankruptcy*, by John J. Topoleski.

[80] A Delphi retirees group, however, has stated that its "plan was very adequately funded when it was terminated." Delphi Salaried Retirees Association, "What Are We Fighting For?" press release, August 12, 2013, https://www.delphisalariedretirees.org/delphi/index.php/what-we-are-fighting-for.

Pensions

Both Old GM and New GM might have been able to invalidate the top-up agreement with Delphi during the bankruptcy proceedings. Nevertheless, New GM said that it honored its top-up agreement with the UAW for commercial reasons.[81] One reason cited was that these union members needed to give their consent to finalize the sale of assets in Delphi's bankruptcy and the top-up would speed bankruptcy proceedings.[82] In addition, New GM topped-up pensions for members of two other unions that comprised large shares of its workforce: the International Union of Electricians-Communication Workers of America (IUE-CWA); and the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers Union (USW). New GM maintained that it was not contractually obligated to give retired members of these two unions top-ups. Once the PBGC assumed responsibility for the remaining Delphi pensions, some Delphi salaried retirees (who were not union members) saw their pension benefits reduced because their monthly benefit (as previously promised by Delphi) was larger than the statutory maximum benefit. New GM did not top-up these salaried workers' pensions. New GM argued that it had no contractual obligation to do so.[83]

When the Delphi plans were terminated in 2009, the maximum benefit from the PBGC was $54,000 per year for an individual who retired at age 65 with no survivor benefit. As of June 2011, the PBGC estimated that 18% of the total number of salaried retirees would see their pension benefits reduced to this amount, while 1% of the total number of hourly workers would see their total pension benefits reduced to this amount.[84]

The DSRA argued that all parties, including the federal government, were treating salaried workers less well than hourly workers. In particular, the DSRA argued that the top-up funding came from TARP as part of the Old GM restructuring.

On September 14, 2009, the DSRA filed a lawsuit against the PBGC, the U.S. Treasury Department, and the Presidential Task Force on the Auto Industry. One of the DSRA's claims was that the agreement between New GM and the unions representing hourly employees to top-up the hourly employees' pensions was a violation of the Equal Protection Clause of the Fifth Amendment to the U.S. Constitution. The DSRA argued that New GM, acting as a government agent because of TARP's role in the Old GM bankruptcy, unfairly discriminated against the salaried employees "solely on the basis of their choice not to associate with a union."[85] The DSRA argued that Old GM's bankruptcy in June 2009 voided the 1999 top-up agreements and that New GM renegotiated and provided the top-up to the unions' pension plans for political

[81] A. Nicole Clowers, *Statement of A. Nicole Clowers, Director of Financial Markets and Community Investment Issues*, Government Accountability Office, July 10, 2012, Opposite the Cover Page, http://gao.gov/assets/600/592225.pdf.

[82] U.S. Congress, House Oversight and Government Reform Committee, Subcommittee on Government Operations, *Statement of Steven Rattner*, 113th Cong., 1st sess., September 11, 2013, p. 2.

[83] CRS is not aware of any other top-up agreements beyond those discussed in this paragraph.

[84] Delphi employed a small number of hourly workers who were members of "splinter unions;" these unionized retirees did not receive top-up pension benefits. See U.S. Government Accountability Office, *Delphi Pension Plans: GM Agreements with Unions Give Rise to Unique Differences in Participant Benefits*, GAO-12-168, December 2011, pp. 34-35, http://www.gao.gov/products/GAO-12-168.

[85] Black et. al. v. Pension Benefit Guaranty Corporation et. al, Second Amended Complaint, paragraph 37, https://www.delphisalariedretirees.org.

reasons. On September 9, 2011, the U.S. district court dismissed the claims against the U.S. Department of the Treasury. The PBGC remains a defendant in the case.

The DSRA submitted an affidavit from a pension actuary stating that the PBGC miscalculated the benefit obligations of the Delphi pension plans and that the pension plan for salaried employees was 86.5% funded at termination.[86] It also said that it was rare for pension plans with this amount of funding to require termination. According to PBGC estimates, at the time of termination the plans for the Delphi salaried employees had $2.4 billion in assets and $5.0 billion in liabilities; the plan was therefore only 48% funded. The PBGC indicated that it expected to be responsible for about $2.2 billion of the plan's estimated $2.6 billion in underfunding. The Delphi court case remains ongoing; recently, a U.S. district judge ordered the U.S. Department of the Treasury to turn over documents related to President Barack Obama's Auto Task Force's role in the termination of the salaried pension plan.[87]

There is some difference of opinion concerning Old GM's contractual obligation to honor previous top-up commitments to the UAW Delphi hourly workers. Both the Government Accountability Office (GAO) and the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) argue that the UAW was treated with special care because it could influence the bankruptcy proceedings and/or call a strike.[88] However, the GAO writes that the "Treasury did not explicitly approve or disapprove of GM's agreement to honor previously negotiated top-up agreements."[89] On the other hand, SIGTARP quotes a Treasury official that "it is my understanding that as the buyer, we got to determine which liabilities [we would take on]."[90]

Although no top-up commitment was ever given to the Delphi salaried workers, the DSRA argues that the salaried workers should enjoy the same benefits as the hourly workers. This position rested on a notion of "fairness" without regard to contractual obligations. Nevertheless, the DSRA did not have current employees at New GM, and, therefore, could not slow down bankruptcy proceedings.

Retiree Health Insurance

The process of establishing health benefits for Delphi's current and future retirees took less time than the still-ongoing pension process. The DSRA created a VEBA committee, and the bankruptcy court accepted this committee as the Section 1114 committee.[91] The negotiations between Delphi and the Section 1114 committee proceeded according to the rules of the

[86] This paragraph is taken from CRS Report R42076, *Delphi Corporation: Pension Plans and Bankruptcy*, by John J. Topoleski, pp. 8-9.

[87] "Judge Orders Treasury to Produce Delphi Documents in Pension Suit," *The Detroit News*, June 20, 2014, http://www.detroitnews.com/article/20140620/AUTO0103/306200109.

[88] Nick Bunkley, "GM Rightly Favored Delphi UAW Pensions Over Salaried, Rattner Says," *Automotive News*, September 11, 2013.

[89] U.S. Government Accountability Office, *Delphi Bankruptcy: Termination of Delphi Pension Plans*, GAO-12-909T, July 10, 2012, Back of Title Page, http://www.gao.gov/assets/600/592225.pdf.

[90] Special Inspector General for the Troubled Asset Relief Program, *Treasury's Role in the Decision for GM To Provide Pension Payments to Delphi Employees*, Troubled Asset Relief Program, August 15, 2013, Introduction, http://www.sigtarp.gov/Audit%20Reports/SIGTARP_Delphi_Report.pdf.

[91] Details on a Section 1114 committee are provided in an earlier section of this report.

Bankruptcy Code. Delphi eventually agreed to provide $8.75 million in up front funding for the VEBA. The funding was in cash; the VEBA did not receive any Delphi stock. When the bankruptcy court accepted the agreement, only salaried workers who were retired or eligible to retire on or before April 1, 2009, were eligible to receive health insurance benefits from the VEBA. Nevertheless, the trust agreement was amended by its own trustees such that it could provide its benefit plans to hourly retirees of Delphi and their dependents and survivors. As a result, if the hourly retirees preferred the health insurance plans offered by the DSRA VEBA, they could enroll in these plans at their own expense instead of the plans offered by Delphi. The hourly retirees, however, could receive no funds from the VEBA.

The DSRA VEBA, which is formally known as the *Delphi Salaried Retirees Association Benefit Trust*, opened with the $8.75 million Delphi contribution in 2009.[92] Delphi has provided no additional contributions since that time. To date, the largest source of additional VEBA funding has been the Early Retiree Reinsurance Program. Most recently, the DSRA was advocating for an extension of the now-expired Health Coverage Tax Credit (HCTC), for which they are eligible because their pensions were taken over by the PBGC.[93] Several bills introduced in the 113th Congress would extend the HCTC for varying lengths of time. These bills are **H.R. 2783**, **S. 1446**, and S. 1859.

Case Study 3: Patriot Coal and the United Mine Workers of America

Background

Federal involvement in retiree pensions and health insurance in the coal industry has a long history in the United States. Following World War II, the United Mine Workers of America (UMWA) demanded health and retirement benefits from coal employers. When these benefits were not forthcoming, the miners staged a walkout. To avoid a shutdown of American coal production, President Harry Truman signed an executive order seizing all of the nation's bituminous coal mines.[94] The Secretary of the Interior, Julius Krug, was ordered to negotiate an agreement with the UMWA President John L. Lewis. The Krug-Lewis Agreement, signed on May 29, 1946, established the UMWA Health and Retirement Funds. Congress has been involved in the operations of coal mines ever since.[95]

The current structure of pension and retiree health benefits in the coal industry is spelled out in the most recent National Bituminous Coal Wage Agreement (NBCWA), a CBA between the UMWA (a multiemployer union) and the Bituminous Coal Operators Association (BCOA), whose

[92] The information in this paragraph is from the DSRA Benefit Trust, Quarterly Financial Report, 2012 Q4, Unaudited, Sources and Uses of Funds, available at http://www.dsrabenefittrust.net/dsrabene/index.php/document-center/DSRA-Benefit-Trust-Documents/Financials/financials-2012/DSRA-BT-2012-Q4-Financial-Report-Post.

[93] For more information, see WHIO, Channel 7, March 10, 2014, https://www.youtube.com/embed/ZwVoc9m2T-c?rel=0;autoplay=1;loop=0;wmode=opaque.

[94] Bituminous is the softest form of coal.

[95] For more information on federal involvement in the coal industry, see Memorandum Decision and Order on Motion to Reject Collective Bargaining Agreements and to Modify Retiree Benefits Pursuant to 11 U.S.C. §§ 1113 and 1114, pp. 8-12.

members represent the owners of the coal mines.[96] The most recent NBCWA was negotiated in 2011 and extends through 2016. It includes, among other terms and conditions of employment, details covering the pension plan and three retiree health funds used by signatory employers.

All plans contain an "evergreen clause" or "continuing contributions clause" to provide for the long-term financing of pensions and health benefits for retired employees and orphan retirees.[97] Thus, all employers who are (or ever were) members of the pension plan or any health plan must contribute, including employers who are not current members of the BCOA. In other words, employers who were once signatory employers to any NBCWA must continue to contribute to all pension and health insurance trust funds until the CBA is changed. Employers are therefore responsible for maintaining benefits for miners who may never have been their employees.

Patriot filed for chapter 11 bankruptcy protection in July 2012 and emerged from bankruptcy in December 2013. Patriot was formed in 2007 as a spin-off company from Peabody Energy. The following year, Patriot purchased Magnum Coal, itself a spin-off of Arch Coal. Consequently, Patriot entered bankruptcy with about three times as many retirees, inherited from Arch and Peabody, compared to active employees. The two parent employers had an improved financial picture following the spin-off; for example, the present value of Peabody's retiree health obligations was reduced by $637.6 million.[98] Patriot, however, was left with an estimated present value of over $1.6 billion in retiree health obligations, an amount the bankruptcy court called "astronomical."[99] In addition, Patriot had been receiving funding from the Early Retiree Reinsurance Program, but additional funding from this source is no longer available.

Pensions

The 1974 Pension Trust (the Trust) was established by collective bargaining and covers all employees whose employer was a signatory employer to the NBCWA one or more times. The Trust documents detail the required contributions of the employers and the benefits received by the eligible retirees under a wide variety of conditions. This Trust pre-dates the Coal Act. Patriot is now the Trust's second largest contributor.

At the time of the Patriot bankruptcy filing, the Trust was less than 73% funded and had a status of "seriously endangered."[100] As discussed above, the 2012 PBGC annual report acknowledges that were this Trust unable to meet its pension obligations, the financial position of the PBGC might be threatened.[101]

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[96] The NBCWA reflects congressional actions, including Title XIX, Subtitle C, Health Care of Coal Miners (P.L. 102-486, enacted in 1992, and commonly referred to as the Coal Act) and Title II, Subtitle B, Coal Industry Retiree Health Benefit Act (P.L. 109-432, enacted in 2006, and commonly referred to as the Amendments to the Coal Act), and the Surface Mining Control and Reclamation Act of 1977 (P.L. 95-87, SMCRA).

[97] As discussed above, an orphan retiree is a retiree who has a multiemployer CBA entitling him or her to benefits from an employer that is no longer solvent.

[98] Patriot Coal, Form 10-K, p. 20, filed with the Securities and Exchange Commission on Feb. 22, 2013.

[99] Memorandum Decision and Order on Motion to Reject Collective Bargaining Agreements and to Modify Retiree Benefits Pursuant to 11 U.S.C. §§ 1113 and 1114, p. 24.

[100] As discussed above, a plan is in *seriously endangered status* if the plan's funding ratio is less than 80% and the plan has a funding deficiency in the current year or is projected to have one in the subsequent five years.

[101] Pension Benefit Guaranty Corporation, *Excellence in Customer Service*, Annual Report 2012, p. 35, http://www.pbgc.gov/documents/2012-annual-report.pdf.

The Patriot bankruptcy negotiations ended with Patriot remaining a participant in the 1974 Pension Trust. Patriot covers current retirees, surviving spouses, and dependents under the existing terms. In addition, active employees hired before January 1, 2012, are covered. Employees hired on or after January 1, 2012, will not be eligible for the 1974 (defined benefit) Pension Trust, but will have a (defined contribution) 401(k) retirement plan.

Retiree Health Insurance

As with the automotive industry, the coal industry provides generous health benefits. The UMWA says that it sacrifices wage increases for employees in exchange for better health insurance because miners face many occupational health challenges.[102]

Coal employers usually maintain their own retiree health plans. However, some employees, especially those whose former employers are no longer mining coal or are bankrupt, have access to one of three UMWA retiree health care funds. Each fund has its own trustees, and the trustees are responsible for paying premiums and benefits and for investing the assets of their respective trust fund.

- The *Combined Benefit Fund (CBF)* is a trust fund created by the Coal Act. It provides retiree health benefits for UMWA employees (and their surviving spouses and dependents) who retired on or before July 20, 1992, and did not have another source of retiree health benefits because they were orphan retirees. The currently-proposed legislation (discussed below) does not affect the CBF.
- The ***1992*** *Benefit Trust* is a trust fund created by the Coal Act. It provides retiree health benefits to those employees (and their surviving spouses and dependents) who retired from the coal industry after July 20, 1992, but before September 30, 1994, and do not have another source of retiree health benefits. The major difference between the 1992 Benefit Trust and the CBF is that under the 1992 Benefit Trust, the premiums paid by each signatory coal company are adjusted each year to meet the expected health care costs of the beneficiaries. The 1992 Trust is therefore better able to keep pace with increases in health care costs than the CBF.
- The ***1993*** *Benefit Trust* covers employees who retired on or after October 1994. In addition, new, inexperienced miners hired after January 1, 2007, cannot receive benefits from this Trust unless they are disabled as a result of a mine accident. The 1993 Benefit Trust is therefore almost entirely closed to new enrollees.[103] The 1993 Benefit Trust was created through negotiation between the UMWA and the BCOA as part of the NBCWA of 1993. Retired miners are eligible for the 1993 Benefit Plan if their past employers either went out of business or defaulted in providing retiree health benefits. The NBCWA specifies the required contributions of the BCOA members for active employees, retired employees, and orphan employees. Note that the bargained level of funding need

[102] U.S. General Accounting Office, *Retired Coal Miners' Health Benefit Funds: Financial Challenges Continue*, GAO-02-243, April 2002, p. 21, http://www.gao.gov/assets/240/234405.html. Compensation for employees with black lung disease, however, primarily comes from its own funding source and was not an issue in the bankruptcy proceedings.

[103] See Patriot Coal, Form 10-K, p. 21, filed with the Securities and Exchange Commission on Feb. 22, 2013.

not correspond with the funding level required to maintain the contractual level of health care benefits for its members.

At the start of the chapter 11 bankruptcy proceedings, Patriot spoke of eliminating retiree health insurance benefits entirely. The UMWA's Section 1114 committee started negotiations, but the bankruptcy court ruled in favor of Patriot's Section 1113 and Section 1114 motions. Therefore Patriot no longer had to honor the existing NBCWA, and no longer had to honor previous commitments to provide retiree health insurance to UMWA retirees (or any other current or future retirees). The court's ruling was viewed unfavorably by the UMWA, and the union threatened to strike. Patriot and the UMWA then began negotiations that included contributions to a new VEBA.

These negotiations became irrelevant when the United States Bankruptcy Appellate Panel for the 8th Circuit reversed an earlier bankruptcy court decision. The original bankruptcy court would have allowed Peabody Energy to stop paying the health care benefits for certain retirees that it had agreed to at the time of the Patriot spin-off. The appellate decision requires Peabody to take responsibility for paying the health care benefits for these retirees. After another round of negotiations, the Peabody case was settled with Peabody contributing $90 million to the VEBA in 2014, $75 million in 2015, $75 million in 2016 and $70 million in 2017, in addition to other requirements.[104]

Recent Legislation

Several bills have been introduced in the 113th Congress that would change the benefits awarded to current and future retirees in the coal industry.

- **H.R. 980** and **S. 468**, Coal Accountability and Retired Employee (CARE) Act of 2013, would transfer part of the interest earned on a coal mine land reclamation fund to the 1974 UMWA Pension Trust to be used to pay pension benefits required under this plan without regard to whether Pension Trust participation is limited to individuals who retired in or after 1976. The Act would make those who would be eligible to receive benefits from the 1974 UMWA Pension Trust following an insolvency proceeding relating to a coal operator eligible for the 1992 Trust.
- **H.R. 2627**, The Caring for Coal Miners Act, would make retired miners who are not receiving benefits they are otherwise entitled to because of a bankruptcy commencing in 2012 eligible for the 1993 Benefit Trust. Benefits made available by this Act would be reduced by the amount actually paid by the VEBA on behalf of a covered beneficiary, so that no beneficiary receives a greater benefit than would have been payable before the establishment of the VEBA.
- **H.R. 2918**, The Coal Healthcare and Pensions Protection Act of 2013, would make retired miners who are not receiving benefits they are otherwise entitled to because of a bankruptcy commencing in 2012 eligible for the 1993 Benefit Trust.

[104] In re Patriot Coal Corporation et. al., Notice and Motion of the Debtors for Entry of an Order Pursuant to 11 U.S.C. §§ 105(a), 363(b), 1113 and 1114(e) and Fed. R. Bankr. P. 9019(a), Approving the Settlement With Peabody Energy Corporation, and the UMWA, On Behalf of Itself and in its Capacity as Authorized Representative of the UMWA Employees and UMWA Retirees, document 5163, http://patriotcaseinformation.com/maincase.php?start_no=4901&end_no=5000.

> Benefits made available by this Act would be reduced by the amount actually paid by the VEBA on behalf of a covered beneficiary. Any additional monies (except the amount needed to cover administrative costs) would be transferred from the VEBA to the 1993 Trust. Any remaining excess monies would be transferred to the 1974 UMWA Pension Trust.

All four bills introduced in the 113th Congress would increase the health benefits available to Patriot retirees. The CARE Act of 2013 would allow Patriot retirees to join the 1992 Benefit Trust, and thus receive the most generous benefits available to any orphan retiree. The Caring for Coal Miners Act would allow those who became orphan retirees as a result of a bankruptcy proceeding commencing in 2012 to join the 1993 Benefit Trust. However, the 1993 Benefit Fund would be prohibited from covering expenses on behalf of a beneficiary that was already covered by the VEBA. The Coal Healthcare and Pensions Protection Act of 2013 would allow those who became orphan retirees as a result of a bankruptcy proceeding commencing in 2012 to join the 1993 Benefit Trust, and would transfer all monies from the VEBA to this Trust. Any extra funding after healthcare obligations have been fully met would be transferred to the 1974 UMWA Pension Trust.

Of the four bills introduced in the 113th Congress, only two would definitely increase the funding available to the 1974 Pension Trust. The CARE Act of 2013 would move some of the interest earned on a coal mine land reclamation fund to the 1974 Pension Trust. This move, however, would reduce the funds available to two health benefit trust funds. The Coal Healthcare and Pensions Protection Act of 2013 would transfer any extra funding after healthcare obligations have been fully met to the 1974 UMWA Pension Trust.

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