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Volume 11 | Number 4 Article 1

9-1-1978

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Susan Wittenberg Liebeler

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Recommended Citation
Susan W. Liebeler, *Pensions and the Cost of Securities Law Protection: The Implications of Daniel v. International Brotherhood of Teamsters*, 11 Loy. L.A. L. Rev. 709 (1978).
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PENSIONS AND THE COST OF SECURITIES LAW PROTECTION: THE IMPLICATIONS OF *DANIEL v. INTERNATIONAL BROTHERHOOD OF TEAMSTERS*†

*by Susan Wittenberg Liebeler**

I. INTRODUCTION

Persons disappointed in a wide variety of transactions have increasingly found solace under the federal securities laws. The scope of federal securities regulation was once limited to what most reasonably knowledgeable persons would recognize in the commercial world as security instruments. Today, however, various kinds of interests in chinchillas,[1] live beavers,[2] silver foxes,[3] whiskey,[4] rare coins,[5] self-improvement programs,[6] diamonds,[7] religious cults[8] and other unusual

† 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978).

* B.A., 1963 (University of Michigan); LL.B., 1966 (U.C.L.A.). Professor of Law, Loyola Law School, Los Angeles.

1. Miller v. Central Chinchilla Group, Inc., 494 F.2d 414 (8th Cir. 1974). The court held it to be a question of fact whether the purchase of chinchillas for raising and breeding constituted an investment contract under the securities laws.

2. Continental Marketing Corp. v. SEC, 387 F.2d 466 (10th Cir. 1967), *cert. denied*, 391 U.S. 905 (1968) (purchase of interest in live beaver ranch investment contract).

3. SEC v. Payne, 35 F. Supp. 873 (S.D.N.Y. 1940) (purchase of interest in silver fox farm is an investment contract).

4. SEC v. Haffenden-Rimar Int'l, Inc., 496 F.2d 1192 (4th Cir. 1974); Glen-Arden Commodities, Inc. v. Costantino, 493 F.2d 1027 (2d Cir. 1974) (the purchase of an interest in barrels of aging whiskey constitutes an investment contract).

5. SEC v. Brigadoon Scotch Distrib., Ltd., 388 F. Supp. 1288 (S.D.N.Y. 1975) (sale of rare coin portfolios held investment contract).

6. SEC v. Glenn W. Turner Enterprises, Inc., 474 F.2d 476 (9th Cir.), *cert. denied*, 414 U.S. 821 (1973). *Turner* involved a gigantic pyramiding scheme. Purchasers of "Dare to be Great" self-motivation courses received the right to sell similar courses to other equally credulous persons. The content of the courses was minimal—their main value lay in the purchaser's ability to sell. For example, a person who purchased Adventure IV for $5,000 obtained the right to sell Adventure IV courses at $5,000 each. A $2,500 commission would be paid for any such sale. *Id.* at 478. The court, in an attempt to protect the "investors," held that the sale of the adventures was a " 'security' within the meaning of the federal securities laws." *Id. See also* SEC v. Koscot Interplanetary, Inc., 497 F.2d 473 (5th Cir. 1974).

7. In Charles Anthony Diamond Invs., Inc., [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,623 (June 15, 1978), the SEC staff refused to issue a no action letter on the

enterprises have been given the protection of the federal securities laws in spite of the semantic contortions required to justify this result.

The Securities Act of 1933 (1933 Securities Act)[9] and the Securities Exchange Act of 1934 (1934 Exchange Act)[10] provide an extensive definition of the term "security." Included in the statutory definitions are long lists of specific instruments including investment contracts and participations in any profit-sharing agreements.[11] The latter have been the focal point of administrative and judicial attention as new and unanticipated forms of economic activity have been characterized as securities and subjected to the regulatory jurisdiction of the Securities and Exchange Commission (SEC or Commission).[12]

This continued growth in the scope of securities regulation has been nurtured by the Commission which has been quite vigilant in patrolling the "investment" universe. It has come into conflict with other regulatory bodies when it has sought jurisdiction over matters traditionally regulated by other federal agencies.[13] By encouraging the expansion of the definition of a "security," the Commission has

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question of whether the sale of diamonds involved the sale of securities subject to the federal securities laws. The staff reply to the Charles Anthony inquiry stated:

> On the basis of the facts presented, particularly (a) the touting of diamonds as an investment medium appropriate for the entire investing public, (b) the offering of resale services, (c) installment sales, and (d) the repurchase feature of the proposed program, it appears that serious questions are raised as to whether a "security" requiring registration under the Act is being publicly offered and sold.

Id. at 86,564.

8. SEC v. World Radio Mission, Inc., 544 F.2d 535 (1st Cir. 1976) (defendant minister induced the faithful to invest their money in "His" economy; transaction held subject to the securities laws).

9. 15 U.S.C. §§ 77a-77aa (1976).

10. *Id.* §§ 78a-78hh.

11. *See* 1933 Securities Act § 2(1), 15 U.S.C. § 77b(1) (1976). The 1934 Exchange Act, § 3(a)(10), 15 U.S.C. § 78c(a)(10) (1976), provides a similar definition. The Supreme Court has held that the two definitions are "virtually identical." United Hous. Foundation, Inc. v. Forman, 421 U.S. 837, 847 n.12 (1975).

12. The genesis of the expansive definition of "security" can be traced to two Supreme Court cases, SEC v. C.M. Joiner Leasing Corp., 320 U.S. 344 (1943), and SEC v. W.J. Howey Co., 328 U.S. 293 (1946).

See generally Faust, *What is a Security? How Elastic Is the Definition?*, 3 SEC. REG. L.J. 219 (1975) for a discussion of problems related to the expansive definitions of "security." The result, according to Faust, has been "a dissipation of emphasis on the types of problems with which the Commission should be primarily concerned, and an inappropriate extrusion of federal securities legislation." *Id.* at 220.

13. For example, the Commission has had a continuing jurisdictional dispute with the Commodity Futures Trading Commission. *See, e.g.*, SEC v. Univest, Inc., 410 F. Supp. 1029 (N.D. Ill. 1976). The SEC has also come into conflict with the Justice Department over antitrust regulation of stock exchanges, broker dealers and other entities over which the SEC also has jurisdiction. *See* Baker, *Antitrust Law and Policy in the Securities Industry: A Tale of Two Days in June*, 31 BUS. LAW. 743, 746 (1976). *See also* Merman & Harmance, *Implica-*

significantly increased its jurisdiction and the need for additional regulations.[14] Many transactions have been "jigsawed" into the securities law[15] with little apparent regard for the financial and administrative burdens imposed upon economic activities which historically have been, and under "common sense" standards should be, regulated by tort and contract law and state or other federal statutes.[16]

To the private litigant the lure of the securities law is almost irresistible. Encouraged by the Commission's own attempts to expand the scope of federal securities law, and eager to avoid application of the

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tion of SEC's Victory Over Antitrust Regulation in the Securities Industry: Justice Department's Suit Against AT&T on the Line, 2 J. CORP. LAW 305 (1977).

The Secretary of Labor has opposed the SEC's entry into pension regulation, stating that application of the antifraud provisions of the securities laws to employee interests in mandatory, non-contributory pension plans "conflicts with the regulatory program prescribed for plans by Congress in ERISA [Employee Retirement Income Security Act, codified in substantial part at 29 U.S.C. §§ 1001-1381 (1976) and in various sections of the Internal Revenue Code of 1954]. . . wastefully duplicates ERISA disclosure [and] is inconsistent with labor law and national labor policy." Brief for Secretary of Labor as Amicus Curiae at 5, 20, Daniel v. International Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977) (*cert. granted*, 98 S. Ct. 1232 (1978)).

In part because of the opposing positions of the SEC and the Department of Labor, the Solicitor General had great difficulty formulating the position of the United States before the Supreme Court. 201 PENS. REP. (BNA) A-16, A-19 (Aug. 14, 1978). The Solicitor General eventually adopted the position of the Labor Department and moved to file an amicus curiae brief urging reversal of the court of appeals decision in *Daniel*. However, in an unusual procedure, the SEC, with the permission of the Solicitor General, has continued to oppose the position of the Secretary of Labor. The SEC has moved to file its own amicus curiae brief in the Supreme Court, urging affirmance of the court of appeals decision. 203 PENS. REP. (BNA) A-7 (Aug. 28, 1978). The Supreme Court has denied the Solicitor General's motion to file an amicus brief. However, the SEC will be allowed to argue as amicus curiae.

14. *See, e.g.*, Briefs for Securities and Exchange Commission as Amicus Curiae, United Hous. Foundation, Inc. v. Forman, 421 U.S. 837 (1975), Daniel v. International Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978). In *Forman*, the Court did not afford the SEC the deference an agency charged with administering a governing statute normally enjoys. The Court noted as its reason that the SEC brief "flatly contradicts" its previous position. 421 U.S. at 858 n.25.

15. Professor Cary, an ardent proponent of federal fiduciary standards through new legislation, has criticized this development. "It seems anomalous to jig-saw every kind of corporate dispute into the federal courts through the securities acts as they are presently written." Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663, 700 (1974) *cited in* Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 480 n.17 (1977).

16. In United Hous. Foundation, Inc. v. Forman, 421 U.S. 837 (1975), the Supreme Court restricted the increasingly expansive application of the securities law. In spite of an SEC amicus curiae brief urging the Court to apply the federal securities laws, the Court held that non-transferable shares of stock in a government subsidized non-profit housing cooperative entitling the purchaser to occupy an apartment were not securities and therefore were not subject to the federal securities laws. The Court looked at the "economic realities" and found that "the inducement to purchase [the stock] was solely to acquire subsidized low cost living space, it was not to invest for profit." *Id.* at 851. The decision reflects a more conservative attitude than the Court had previously shown toward defining securities.

Statute of Frauds or similar doctrines restricting recovery under state or other federal laws, private parties have increasingly sought relief in the federal securities law.[17] Added incentives are the liberal venue, service of process and jurisdiction provisions in the federal securities acts,[18] as well as the traditional advantages of federal procedure.[19]

Still another inducement to these plaintiffs has been the willingness of the judiciary to imply private damage actions under certain sections of the securities acts, particularly the antifraud sections.[20] These plaintiffs could seek standing under the several carefully drawn sections of the securities acts which provide explictly for private damage actions.[21] But, unlike the implied rights under the antifraud sections, these ex-

17. *See, e.g.*, Schlansky v. United Merchants & Mfrs., Inc., 443 F. Supp. 1054 (S.D.N.Y. 1977).

18. *See, e.g.*, 1933 Securities Act § 22, 15 U.S.C. § 77 v(a) (1976); 1934 Exchange Act § 27, 15 U.S.C. § 78aa (1976).

19. Several aspects of the federal judicial system are of particular relevance in securities litigation. Of primary importance is FED. R. CIV. P. 23.1 which delineates the method for bringing shareholder derivative actions in federal court.

A significant aspect of rule 23.1 is its lack of a security for expenses provision. Importantly, several states do have statutes with security for expenses provisions. For an example of one such statute, see N.Y. BUS. CORP. LAW § 627 (McKinney Supp. 1978).

Another aspect of federal procedure which may prove useful, if not essential, in securities litigation regards the rules dealing with discovery. *See* FED. R. CIV. P. 26-37. The purpose of the federal discovery rules is to bring all relevant, non-privileged facts out in the open. Hickman v. Taylor, 329 U.S. 495 (1947). Hence, the rules have "been generously construed to provide a great deal of latitude for discovery." Harris v. Nelson, 394 U.S. 286, 297 (1969).

20. 1933 Securities Act § 17(a), 15 U.S.C. § 77q(a) (1976); 1934 Exchange Act § 10(b), 15 U.S.C. § 78j(b) (1976). The implication of private damage actions under § 10(b) was approved by the Supreme Court in a footnote. Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 13 n.9 (1971). The Court has never decided whether there exists a similar implied cause of action for sellers under § 17(a). Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 733 n.6 (1975). The lower courts are divided on the issue. *Compare* Dyer v. Eastern Trust & Banking Co., 336 F. Supp. 890 (D. Me. 1971) *with* Newman v. Prior, 518 F.2d 97 (4th Cir. 1975). It has also been suggested that the issue is not important because of the availability of comparable relief in implied damage actions under § 10(b). SEC v. Texas Gulf Sulphur, 401 F.2d 833, 867, *cert. denied*, 394 U.S. 976 (1968) (Friendly, J., concurring).

The Supreme Court has recently expressed concern that broadening the class of plaintiffs with standing to bring implied damage actions under the securities laws will cause more harm than good. The Court has moved to restrict that class. *See, e.g.*, Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) (non purchasers and non sellers lack standing to bring private damage actions under § 10(b) and rule 10b-5); Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) (private damage action under § 10(b) and rule 10b-5 does not lie for defendant's negligence; plaintiff must allege scienter); Piper v. Chris-Craft Indus., Inc., 430 U.S. 1 (1977) (unsuccessful tender offeror lacks standing to bring implied private damage action under § 14(e) and rule 10b-6); Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977) (breach of fiduciary duty not actionable in private damage action under § 10(b) and rule 10b-5).

21. 1933 Securities Act § 11, 15 U.S.C. § 77k (1976) (civil damage action based on mis-

pressed rights are subject to many restrictions, including short statutes of limitation,[22] a security for expenses provision,[23] reliance requirements[24] and maximum limits on certain damage awards.[25] Largely because they avoid these restrictions, implied causes of action under the antifraud provisions have become a Mecca for the disappointed.

This judicial inference of private rights of action, together with the expansion of the notion of what is a security,[26] has created chaos in the area of civil liability under the securities acts.[27] Since regulation of securities has a significant impact upon the national economy, it is difficult to imagine an area of the law in which uncertainty could be more troublesome and inhibiting.[28]

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statements or omissions in registration statement); *id.* § 12(1), 15 U.S.C. § 77*l*(1) (1976) (purchaser may sue seller for rescission or damages based on violation of § 5 registration requirements); *id.* § 12(2), 15 U.S.C. § 77*l*(2) (1976) (purchaser may sue seller for rescission or damages based on misstatements or omissions in prospectus or oral communication); *id.* § 15, 15 U.S.C. 77*o* (1976) (joint and several liability for controlling persons). 1934 Exchange Act § 9(e), 15 U.S.C. § 78i(e) (1976) (buyers and sellers may sue any persons who willfully manipulates security prices in violation of § 9(a), (b), or (c)); *id.* § 16(b), 15 U.S.C. § 78p(b) (1976) (corporation or shareholder on its behalf may recover short swing profits from officers, directors and certain beneficial owners); *id.* § 18(a), 15 U.S.C. § 78r(a) (1976) (buyer or seller reasonably relying upon false or misleading statements in reports filed under § 15 may sue for damages); *id.* § 20, 15 U.S.C. § 78t (1976) (joint and several liability for controlling persons).

22. *E.g.*, 1933 Securities Act § 13, 15 U.S.C. § 77m (1976); 1934 Exchange Act §§ 9(e), 18(c), 15 U.S.C. §§ 78i(e), 78r(c) (1976).

23. 1933 Securities Act § 11(e), 15 U.S.C. § 77k(e) (1976) (authorizes the court in its discretion to require undertaking for payment of suit costs, including attorney's fees, in any suit brought under the 1933 Securities Act).

24. *E.g.*, 1934 Exchange Act § 18(a), 15 U.S.C. § 78r(a) (1976) (plaintiff must have relied on false or misleading statement).

25. *E.g.*, 1933 Securities Act § 11(e), 15 U.S.C. § 77k(e) (1976) (underwriter's liability limited to total offering prices of securities underwritten and distributed by him); *id.* § 11(g), 15 U.S.C. § 77g (1976) (recovery under § 11 cannot exceed price at which securities offered to public).

26. *See* notes 1-8 *supra* and accompanying text.

27. Professor Loss has expressed it thus:

> In the area of civil liability the law has become almost chaotic as a result of the judicial implication of private rights of action—a development that, however salutory, should be synchronized with the express civil liability provisions in the several statutes in a way that appropriately levels the peaks and valleys and reduces the volume of needless litigation.

Loss, *Introduction to Proposed Official Draft of Federal Securities Code*, [1978] SEC. REG. & L. REP. (BNA) E-1, at E-2 (Apr. 26, 1978).

28. In United Hous. Foundation, Inc. v. Forman, 421 U.S. 837, 849 (1975) the Court stated:

> The primary purpose of the Acts of 1933 and 1934 was to eliminate serious abuses in a largely unregulated securities market. The focus of the Acts is on the capital market of the enterprise system: the sale of securities to raise capital for profit-making purposes,

The federal courts do not appear to have given much attention to the question of whether the benefits of expanding the federal securities law are likely to exceed the costs. Nor have they been inclined to ask whether more cost-effective solutions are available and might be developed and applied by other institutions. Indeed, the courts do not appear to have considered the possibility that the costs of any remedy which could be fashioned might, of necessity, exceed the benefits thereby conferred.

No one article can hope to survey such a broad field, and the examination of one new remedy created by such expansion does not necessarily reflect upon the value of others. This article will, nevertheless, attempt to cast some light upon the general question of the costs and benefits of that expansion by examining the current attempt to apply the federal securities law to employee interests in pension plans. Discussing the probable costs and benefits of that attempt, the article concludes that this particular expansion of securities regulation is not likely to benefit society, but will, instead, impose considerable costs which can only add to the apparently significant burdens which government regulation has already imposed on the private pension system. While this conclusion may not be indicative of the value of other such expansions, it certainly suggests that the federal courts ought not to be so ready in the future to expand the scope of federal securities regulation.

An examination of the results of the decades-long judicial expansion of the federal securities laws raises with particular force the more general question of whether the courts are well-suited to perform tasks that many would characterize as legislative in nature. While there is no reason to believe that they are well-suited, if they persist in that activity, they should do so only in those cases in which a rough cost-benefit estimate indicates that their efforts would not reduce the aggregate wealth of society.

II. Securities Regulation of Pension Plans — A New Development

An example of the dubious benefits of expansion of federal securities laws may be found in recent developments applying those laws to pension plans. Historically, the securities law has not been actively used to regulate pensions. Although pension plans were enjoying increased

the exchanges on which securities are traded, and the need for regulation to prevent fraud and to protect the interest of investors.

popularity when the securities acts were initially adopted, there was no reference to pension plans in the original securities acts. Nor is there any indication in the legislative history that Congress ever considered the question of whether such plans, or employee interests in them were securities.[29] In the ensuing years the issue never became important because the SEC adopted the position that interests in pensions did not involve a sale.[30] In the absence of a sale, securities are not subject to the registration or antifraud provisions of the securities acts.[31]

Since the passage of the 1933 Securities Act, some statements may have been made suggesting that some interests in pensions plans are

29. This is not because "in the early 1930's pension plans were still a rarity" as suggested by the court of appeals in Daniel v. International Bhd. of Teamsters, 561 F.2d 1223, 1241 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978). Murray Latimer had published a monumental two volume study of domestic pension plans in 1932 (M. LATIMER, INDUSTRIAL PENSION SYSTEMS IN THE UNITED STATES AND CANADA (1932)) and the same Congress which enacted the securities acts also passed the Railroad Retirement Act of 1934, ch. 868, §§ 1-8, 48 Stat. 1283. Moreover, Congress had dealt with pension plans several years before in the context of the tax law when it provided for favorable tax treatment of pension plans in the Revenue Act of 1928, ch. 852, §§ 23(q), 165, 45 Stat. 802, 839. Subsequent studies have revealed that "[b]etween 1900 and 1933 some 800 industrial institutions adopted and installed pension plans affecting some 4,000,000 employees." S. REP. No. 610, 76th Cong., 1st Sess. 46 (1939).

The more likely explanation for the failure of Congress to consider or mention pension plans in connection with the securities acts is that no one thought pension plans bore the remotest resemblance to securities. *See* note 47 *infra*.

30. This view was formally expressed in September 1941 in an opinion of John F. Davis, then Assistant General Counsel of the SEC: "[N]o 'offer' or 'sale' is involved in the case of a noncontributory plan, where the employees are not requested to make any contributions, or in the case of a compulsory plan where there is no element of volition on the part of employees whether or not to participate and make contributions." [1978] 1 FED. SEC. L. REP. (CCH) ¶ 2105.53. The staff position was reaffirmed on August 1, 1962 in a letter to CCH from the Chief Counsel, Division of Corporation Finance, which stated that the September 1941 opinion of the Assistant General Counsel correctly outlined current policies of the Commission staff. *Id.* at ¶ 2105.52.

The Commission did not require registration of all voluntary or contributory plans stating that "no question will be raised with respect to the registration of participations in a voluntary contributory pension, profit-sharing, or similar plan that does not invest in the securities of the employer company in an amount exceeding the company's contribution." Mundheim & Henderson, *Applicability of the Federal Securities Laws to Pension and Profit-Sharing Plans*, 29 LAW & CONTEMP. PROB. 795, 809 (1964). Thus, by a "no-action" position, the SEC "exempted" from registration those voluntary and contributory plans which did not invest more than the employer's contributions in the securities of the employer.

31. Section 5 of the 1933 Securities Act requires registration of only those securities offered for sale or sold. 15 U.S.C. 77e(1976). Section 17(a) of that act prohibits misleading statements and omissions and fraudulant practices in connection with the sale or offer from sale of a security. 15 U.S.C. § 77q(a) (1976). Section 10(b) of the 1934 Exchange Act and rule 10b-5 prohibit misleading statements and omissions and fraudulant practices in connection with the purchase or sale of a security. 15 U.S.C. § 78j(b) (1976) and 17 C.F.R. § 240.10b-5 (1977).

securities.[32] However, the question of whether expectancy interests in mandatory, non-contributory pension plans were securities was never addressed on its merits because of the Commission's "no sale" policy. Indeed, the SEC had been criticized for this policy.[33] Perhaps in response to this criticism, or in an attempt to broaden its jurisdiction, the SEC has abruptly and formally abandoned its no sale position and now insists that all employee interests in non-contributory, mandatory defined benefit pension plans involve the sale of a security[34] and are

32. *See, e.g.*, Mundheim & Henderson, *Applicability of the Federal Securities Laws to Pension and Profit-Sharing Plans*, 29 LAW & CONTEMP. PROB. 795, 804-05 (1964).

33. The lower court in *Daniel* characterized the Commission's no-sale position as illogical. Daniel v. International Bhd. of Teamsters, 410 F. Supp. 541, 553 (N.D. Ill. 1976), *aff'd*, 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978).

34. Judge Kirkland was the first federal judge to consider the precise question of whether employee expectancy interests in mandatory, non-contributory pension plans are securities. Daniel v. International Bhd. of Teamsters, 410 F. Supp. 541 (N.D. Ill. 1976), *aff'd*, 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978). Several other district courts have since addressed the issue. *E.g.*, Weins v. International Bhd. of Teamsters, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,005 (C.D. Cal. 1977); Hurn v. Retirement Fund Trust of Plumbing, Heating & Piping Indus., 424 F. Supp. 80 (C.D. Cal. 1976). In *Weins* and *Hurn* the plaintiffs were disappointed former employees who, as a condition of their employment, had "participated" in mandatory non-contributory pension plans. In neither case were the plaintiff's expectations met. Plantiff Hurn's receipt of vested benefits terminated when he was elected an officer of his local union. Plaintiff Weins failed to qualify for a pension because of an involuntary break in service. In both cases it was held that plaintiffs' interests in their pension plans were not securities and, alternatively, that acquisition of their interests did not constitute a sale of a security. Although *Hurn* was decided several months after the district court opinion in *Daniel*, the *Hurn* court did not cite *Daniel*. In its brief conclusions of law the court relied instead upon United Hous. Foundation, Inc. v. Forman, 421 U.S. 837 (1975) and Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) in holding that no sale of any security had occurred. The court further held that ERISA preempted the securities law with respect to disputes over pension benefits. In *Weins*, Judge Hill specifically rejected the district court's rationale in *Daniel*, and was particularly unsympathetic toward expansion of the securities law to encompass interests in pension plans. [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,005 (C.D. Cal. 1977).

A third case, Robinson v. UMW Health & Retirement Funds, 435 F. Supp. 245 (D.D.C. 1977), was a class action brought on behalf of surviving dependents of deceased miners. The potential class members sought declaratory relief with respect to their right to health care benefits under a union-sponsored health and retirement plan. Judge Gesell considered and rejected the analysis of the lower court in *Daniel*, stating that the securities laws were not meant to regulate such plans.

A fourth case, Cinnamon v. Brooks, No. 77-204 (C.D. Cal., filed 1977) involved a cross-complaint by a former employee whose benefit expectations were not met. The cross-complaint contained several counts, including one under the antifraud provisions of the securities acts. On May 20, 1977 Judge Lydick dismissed the securities counts of the cross-complaint.

Two other district courts have accepted *Daniel's* reasoning. Schlansky v. United Merchants & Mfrs., Inc., 443 F. Supp. 1054 (S.D.N.Y. 1977) was a class action filed on behalf of present and former employees whose pension expectations were not met. Citing the therefore subject to the antifraud provisions of the securities acts.[35]

The Commission changed its position on this issue in its amicus brief before the court of appeals[36] in *Daniel v. International Brotherhood of Teamsters*.[37] The original action in *Daniel* was an individual and class action brought by a retired truckdriver who contended that, contrary to his expectations and contrary to the representations of the defendants, he had not received benefits under a mandatory, non-contributory pension plan in which his employer participated.

The defendants in *Daniel* were the pension trust fund, its trustees,

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court of appeals' decision in *Daniel*, the court found that former employees' interests in a single-employer, non-contributory, mandatory pension plan were securities and were thus subject to the antifraud provision of the 1934 Exchange Act. The court dismissed the claim for relief under § 17a of the 1933 Securities Act, 15 U.S.C. § 77q(a) (1976), on the ground that there is no private right of action thereunder. *See* note 20 *supra*.

In Assay v. Hallmark Cards, Inc., No. 76-1 (N.D. Iowa, filed 1976) the court denied a motion to dismiss the securities counts of a complaint filed on behalf of former employees who did not receive their expected benefits under a single-employer, non-contributory, mandatory pension plan. The court stated that plaintiffs' assertion of jurisdiction under the antifraud provisions of the securities laws was clearly not frivolous under the district court opinion in *Daniel*.

35. According to the Commission, however, interests in mandatory, non-contributory pension plans are exempted from the registration requirements of the 1933 Securities Act under § 3(a)(2), 15 U.S.C. § 77a(2) (1976). Brief for Securities and Exchange Commission as Amicus Curiae at 5, 31, Daniel v. International Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977)(*cert. granted*, 98 S. Ct. 1232 (1978)). The Commission has also exempted such interests from the registration requirement of the 1934 Exchange Act by promulgating rule 12h-2, 17 C.F.R. § 240.12h-2 (1976). Since pension plans do not file registration statements under the 1933 Securities Act or the 1934 Exchange Act, they are not required to file periodic reports under § 13 or § 15(d) of the 1934 Exchange Act, 15 U.S.C. §§ 78m, 78*o*(d) (1976).

36. The response to the Commission's sudden change in position has been somewhat unfavorable. Judge Tone, in his concurring opinion in *Daniel* commented:

> In reaching this conclusion, I have found little comfort in the opinion expressed by the SEC, as amicus curiae. Apparently for the first time ever, it now takes the position in its brief before us that the employee's interest or expectancy in a plan such as this is subject to the anti-fraud provisions of the securities laws. The Commission has not been as candid as we might have hoped in acknowledging and explaining its change in position.

Daniel v. International Bhd. of Teamsters, 561 F.2d at 1251 (Tone, J., concurring), *cert. granted*, 98 S. Ct. 1232 (1978).

In a case similar to *Daniel*, Judge Hill commented:

> Now, we have the interesting phenomenon that defendant points out that for forty years the SEC has said that these pension plan interests were not securities; but the SEC may have changed its mind recently as a result of the Daniel case. But there is a quick and easy answer to that supplied, I think, by the Supreme Court in Forman; and the Supreme Court, I think, teaches us in the Forman opinion that the SEC position, past or present, is of minimal importance, and especially of minimal importance when that position has suddenly shifted after a long period in the other direction.

Weins v. International Bhd. of Teamsters, [1977-1978 Transfer Binder] FED. SEC. L. REP. ¶ 96,005, at 91,519 (C.D. Cal. 1977). *See* note 14 *supra*.

37. 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978).

and the local and international unions to which Mr. Daniel belonged.[38] The complaint contained several counts, the first two of which were premised on violations of section 17(a) of the 1933 Securities Act[39] and section 10(b) of the 1934 Exchange Act[40] and rule 10b-5[41] promulgated thereunder. It also alleged breach of duty of fair representation under section 9a of the National Labor Relations Act,[42] violation of section 305(5) of the National Labor Relations Act,[43] breach of fiduciary duty, and fraud and deceit. The complaint sought reformation of the pension plan by deleting the alleged "arbitrary length and continuity requirements of all vesting provisions," judgment equal to all pension benefits unlawfully denied plaintiff and members of his class,[44] and judgment for amounts equal to pension trust funds "unlawfully diverted from their proper purposes."[45] On appeal from the denial of a

38. In addition, the complaint named three classes of defendants: "Teamster local unions with pension funds similarly situated to Local 705, trustees of such pension funds and all officers of locals with such pension funds." *Id.* at 1225.

39. 15 U.S.C. § 77q(a) (1976).

40. *Id.* § 78j(b).

41. 17 C.F.R. § 240.10b-5 (1977).

42. 29 U.S.C. § 159(a) (1976).

43. *Id.* § 186(5).

44. Mr. Daniel could not recover his expected or promised pension under the securities laws.

> Section 28 of the Securities Exchange Act permits the recovery only of "actual" damages, generally construed to mean a plaintiff's out-of-pocket loss, not the benefit of what the plaintiff bargained for. Accordingly a pension beneficiary plaintiff might well be confined to recovering the contributions to the pension, and not the pension benefit itself, if recovery were permitted.

Memorandum to Chairman Williams of the SEC from the Office of the General Counsel of the SEC (December 7, 1977), *reprinted in* 4 J. PENS. PLAN. & COMPLIANCE 11, 16 (1978).

While the memorandum is correct in stating that there can be no recovery of the pension benefit itself, it is incorrect in assuming that recovery can be had for the employer contributions. As explained in note 62 *infra*, the employer contributions are merely a funding mechanism designed to finance pension obligations. An employee has no interest whatsoever in employer contributions in a non-contributory defined benefit plan.

Mr. Daniel's out-of-pocket costs are his opportunity costs—the costs he incurred in not changing jobs. This opportunity cost could be considerably less (or more) than the amount of employer contribution or the promised pension. In Mr. Daniel's case, his opportunity costs may be zero. Mr. Daniel stated in his affidavit that had he known of the way in which the pension plan vesting requirements would be interpreted, he would have sought other employment with retirement benefits of the type he expected to receive under the Local 705 Plan. Had Mr. Daniel changed jobs in 1955, the year in which the Local 705 plan was instituted, he would have received no past service credit in his new employer's pension plan. Since prior to ERISA plans often required twenty years of employment prior to vesting, Mr. Daniel may not have been eligible for any benefits in his new employer's plan when he retired in December 1973. The relevant portions of Mr. Daniel's affidavit are discussed in note 161 *infra*.

45. The complaint alleged that there have been unlawful diversions and investments of trust funds; however, the Supreme Court has held that breaches of fiduciary duty are not

motion to dismiss the securities counts of the complaint, with the support of the SEC as amicus, the court of appeals held that plaintiff, as a purchaser of a security, had standing to maintain an action under the antifraud provisions of the federal securities acts.[46]

Daniel presents a particularly good opportunity for examination of the consequences of ad hoc judicial expansion of the securities laws, since not long before the court's decision, Congress addressed the general issue of pension reform on the assumption that employee interests in pension plans were not subject to federal securities regulation.[47] This article will contrast the results of this legislation with the results implicit in the *Daniel* decision.

To make this comparison it is first necessary to survey the growth of the private pension system and the accompanying growth of its regula-

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actionable in private damage suits under § 10(b) and rule 10b-5. Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977). *Accord,* O'Brien v. Continental Ill. Nat'l Bank & Trust Co. of Chicago, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,034 (N.D. Ill. 1977); Blackmar v. Lichtenstein, [1978] PENS. REP. (BNA) D-1 (E.D. Mo. 1977) (beneficiaries of a trust have no standing under § 10(b) to complain of breaches of fiduciary duty by the trustees). *But see* Cartano, *Rule 10b-5 and ERISA After the Daniel Case,* 4 J. PENS. PLAN. & COMPLIANCE 183, 188 (1978).

46. In 1973 when Mr. Daniel retired and was denied pension benefits, ERISA had not been enacted. Since the new legislation operates prospectively only, Mr. Daniel has no claim for relief under it. However, the *Daniel* holding is not restricted to persons whose benefits were denied prior to ERISA. The *Daniel* court viewed the antifraud sections of the securities laws as complementary to ERISA, and held that the antifraud provisions apply to interests in plans covered by ERISA. Daniel v. International Bhd. of Teamsters, 561 F.2d 1223, 1248-49 (7th Cir. 1977), *cert. granted,* 98 S. Ct. 1232 (1978).

47. Senator Williams recently stated:

> At no time during the period of ERISA's development was it ever stated to me or, to the best of my knowledge, to any other member of Congress that the Securities Acts' antifraud provisions applied to noncontributory, involuntary pension plans . . . . Parties and *amici* in *Daniel,* including the Commission, have devoted much argument to the legislative history of ERISA, its predecessor labor law, the Welfare and Pension Plans Disclosure Act, the antifraud provisons of the 1933 and 1934 Securities Acts, and the amendment to section 3(a)(2) of the 1933 Act that was contained in the Investment Company Amendments Act of 1970; and the record is devoid of any affirmative statement by the SEC of the proposition it has supported in *Daniel* . . . . The relevant legislative history demonstrates a focus on the registration provisons of the 1933 Act; the antifraud provisions are rarely mentioned and if it is true that the Commission never stated that the antifraud provisions did not apply as they have been held to apply in *Daniel,* it is also true that the Commission never stated that they did apply. In over 40 years, there was no affirmative statement and, most importantly, no action that would have put the Congress on notice.
>
> The lack of notice is very important because, given the delicate balance Congress sought to strike in ERISA, notice that the antifraud provisions were applicable to a fact situation such as that in *Daniel* certainly would have been a matter worthy of legislative consideration as, indeed, it has become a matter of legislative consideration since the 7th circuit decision.

Letter from Senator Williams to SEC Chairman Williams (Dec. 13, 1977), *reprinted in* 4 J. PENS. PLAN. & COMPLIANCE 17, 18-19 (1978).

tion by the government. In so doing note must be taken of the perceived inequities and abuses associated with the pension system and the available means for rectifying them must be examined. Only then can the implications of *Daniel* be assessed. While a comprehensive history and analysis of these abuses and the "solutions" offered by the Employee Retirement Income Security Act (ERISA)[48] are beyond the scope of this paper, it will be useful to focus briefly on funding practices, vesting and continuity of service rules, and participation and disclosure policies, all of which are relevant to the *Daniel* decision.[49]

III. THE GROWTH OF THE PENSION SYSTEM AND PENSION REGULATION

A. *The System*

While formal pension plans have been in use in the United States since 1875,[50] striking growth in their use has occurred during the past few decades. Originally pension plans offered employees annuity benefits financed by the investment of employer contributions in government bonds or similar fixed interest bearing securities.[51] The character of these investments began to change in the 1950's when General Motors instituted a new type of plan with an investment trust designed to make diversified investments, particularly in equity securities. This was a revolutionary development and within a year, 8,000 new plans were written, each copying the General Motors diversified investment trust.[52]

Today pension plans cover at least one-half of the industrial work force and represent a major source of investment capital.[53]Many factors have contributed to their rapid growth.

48. A substantial portion of ERISA's provisions has been codified at 29 U.S.C. §§ 1001-1381 (1976); the remainder has been codified in various sections of the Internal Revenue Code of 1954.

49. For a comprehensive survey of ERISA, see Comment, *The Employee Retirement Income Security Act of 1974: Policies and Problems*, 26 SYRACUSE L. REV. 539 (1975) [hereinafter cited as *ERISA: Policies and Problems*].

50. Historians generally agree that the first formal pension plan in the United States was established in 1875 by the American Express Company. W. GREENOUGH & F. KING, PENSION PLANS AND PUBLIC POLICY 26 (1976) [hereinafter cited as GREENOUGH & KING].

51. P. DRUCKER, THE UNSEEN REVOLUTION 6 (1976).

52. *Id.*

53. S. REP. No. 93-127, 93d Cong., 2d Sess. 3 (1974), *reprinted in* Daniel v. International Brotherhood Of Teamsters *A Report To The Committee On Federal Regulation Of Securities From The Study Group of 1933 Act—General Subcommitteee On Daniel, Et Al. v. International Brotherhood Of Teamsters*, 32 BUS. LAW. 1925, 1930 n.11 (1977) [hereinafter cited as *Daniel Study Group Report*].

Pension plan growth has been stimulated by the federal government. This has been accomplished primarily by the creation of certain statutory tax advantages[54] for qualifying plans. Under this system of preferential tax treatment, taxes are deferred on employer contributions and trust investment earnings, thus leaving untaxed significant accumulations of wealth. The federal judiciary contributed its encouragement to pension growth by holding that employee benefit plans were mandatory subjects for collective bargaining.[55] Additional federal nourishment was provided during World War II and the Korean Conflict with the imposition of wage controls and excess profits taxes, and with the exemption from wage controls of indirect increases in employee compensation through pension and other benefit plans.[56]

Pension plans are perceived to be useful to the various interest groups in industrial employment.[57] They provide employers with a means of encouraging long-term employment, reducing expensive employee turnover and inducing the retirement of older, highly paid employees without incurring the ill will of the labor force. For employees and unions, the pension promises retirement security.[58]

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54. The employer receives an immediate deduction for the contribution and the tax on the contributions and earnings is deferred until distribution to the recipient. I.R.C. §§ 401-404, 501(a). For a thorough review of the taxation of qualified plans, see M. CANAN, QUALIFIED RETIREMENT PLANS (1977).

55. Inland Steel Co. v. NLRB, 170 F.2d 247 (7th Cir. 1948), *cert. denied*, 336 U.S. 960 (1949).

56. M. BERNSTEIN, THE FUTURE OF PRIVATE PENSIONS 10, 197-98 (1964) [hereinafter cited as BERNSTEIN].

57. For a discussion of the objectives of unions, employers and employees in utilizing pension plans, see *id.* at 9-14. The author questions whether pension plans fulfill these objectives.

58. Some have maintained that pensions are aggregate deferred wages for each year of employment. Thus the decision to ratify a collective bargaining agreement of which a pension plan is a part becomes an investment decision by employees who must decide whether to take a part of their present wages and invest in pension benefits. Under this analysis, it is then concluded that when employees fail to qualify for pensions, they "forfeit" their employer contributions (the deferred wages). The underlying assumption is that, in the absence of a pension plan, employer contributions would go directly into the paychecks of present employees.

While this assumption and the mode of analysis described do make pension plans appear to be similar to "securities" traditionally regulated under securities law, they do not comport with the realities of non-contributory, defined benefit pension plans which typically require lengthy employment periods before any right to receive benefits vests. The Supreme Court recently had occasion to examine the nature of such plans and it specifically rejected the assumption that benefits are aggregate deferred wages for each year of employment.

In Alabama Power Co. v. Davis, 431 U.S. 581 (1977), the Court held that § 9 of the Military Selective Service Act, 50 U.S.C. App. § 459(b), subsequently recodified at 38 U.S.C. § 2021(b)(2) (1976), requires an employer to give an employee pension credit for his period

Thus pension plans have enjoyed tremendous popularity. By 1973 pension plans covered approximately thirty million employees. The total asset value of these plans was estimated at 150 billion dollars in 1973 and has been projected to exceed 250 billion dollars by 1980.[59]

Because of the wide variety of economic conditions prevailing in different industries, several types of pension plans were developed. A "multi-employer" plan, covering the employees of financially unrelated employers, is generally collectively bargained and provides for transfer of pension credits among participating employers. These plans are often industrywide in operation and may be local, regional or national in scope. Multi-employer plans are usually found in industries characterized by numerous small employers with a high rate of business failure. In such an environment, this type of plan provides employees with pension benefits not otherwise available. For small employers, the multi-employer plan provides the economies of scale associated with the administration of a large plan and the standardization of pension costs among competing employers. Some employers use "single-employer plans," which may cover a few to several hundred thousand employees. Such plans may be collectively bargained or may be instituted unilaterally by an employer. Single-employer plans account for a substantial majority of private pension plans and employees covered by such plans.[60]

The employer's obligation under multi- or single-employer plans may be to make specified contributions, or to make whatever contributions are necessary to produce specified benefits. The former is referred to as a "defined contribution" plan and the latter as a "defined benefit" plan.[61] Defined contribution plans, which include profit shar-

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of military service. In reaching this conclusion, the Court decided that the pension involved was a reward for length of service:

> Other aspects of pension plans like the one established by petitioner suggest that the "true nature" of the pension payment is a reward for length of service. The most significant factor pointing to this conclusion is the lengthy period required for pension rights to vest in the employee. *It is difficult to maintain that a pension increment is deferred compensation for a year of actual service when it is only the passage of years in the same company's employ, and not the service rendered, that entitles the employee to that increment.*

Id. at 593 (emphasis added).

59. S. REP. No. 93-127, 93d Cong., 2d Sess. 3, *discussed in Daniel Study Group Report, supra* note 53.

60. D. MCGILL, FUNDAMENTALS OF PRIVATE PENSIONS 78-79 (3d ed. 1975).

61. The defined benefit may depend upon earnings or length of service. The benefit payable is generally expressed in one of the following ways: (1) a flat amount (unrelated to earnings or service); (2) a percentage of an employee's earnings (dependent on earnings, unrelated to service); (3) a flat amount per year of service (unrelated to earnings, dependent on service); or (4) a percentage of each year's earnings (dependent on earnings and service).

ing, certain pension and other retirement plans, do not produce a predetermined level of benefits, but rather a level of benefits dependent on the value of the plan assets.[62]

The *Daniel* plan is typical of most defined benefit pension plans; employee participation occurs automatically as a conditon of employment and only employers contribute to the plan trust fund. Such plans are referred to as mandatory, non-contributory defined benefit plans. Unless otherwise indicated, this article will focus on this type of plan.

B. Pension Regulation Before ERISA

For many years the most significant, though indirect, mechanism for pension regulation has been the tax law. In order to qualify for advantageous tax treatment permitting deferment of tax on employer contributions to the trust as well as on the trust earnings,[63] a pension plan had to satisfy certain criteria. Among other things, employers were required to place their contributions in an irrevocable trust for the benefit of all employees; "qualified" plans could not discriminate in favor of shareholder-employees or management personnel; and employers were required to finance plan obligations with advance funding.[64] While

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J. MELONE & E. ALLEN, JR., PENSION PLANNING 37 (rev. ed. 1972) [hereinafter cited as MELONE & ALLEN].

62. Employees have no interest or expectancy in their employers' contributions to a non-contributory defined benefit plan fund. The amount of pension benefits payable to any employee under such a plan does not depend upon the amount contributed to the fund by any employer on the employee's behalf, nor does it depend upon the earnings on such contributions. If, upon satisfaction of the conditions for payment of a pension, the employer contributions together with accumulated earnings thereon exceed the defined benefit, the employee is entitled only to the defined benefit, and nothing more. Conversely, if the employer contributions and accumulated earnings are less than the defined benefit, an employee satisfying all the conditions for payment is entitled to the full amount of the defined benefit.

Employer contributions made over the years with respect to particular employees are merely an advance funding mechanism designed to provide for payment of future pension obligations. Absent ERISA's new funding requirements and the advantages associated with qualified pension plans, a defined benefit pension could be financed in other ways.

Thus, the court in *Daniel* seems to have erred in stating that an employee who fails to qualify for a pension has *forfeited* his interest in his employer's contributions and the earnings thereon. Since contributions are merely an advance funding mechanism, it is illogical to hold that a particular employee has an "interest" in the contributions. While the court's analysis may have merit with reference to a defined contribution plan, it has no such merit when applied to a defined benefit plan.

63. *See* note 54 *supra* and accompanying text.

64. Employer contributions were only required to be made in the amount necessary to cover current costs and interest on unfunded past service obligations. There was no requirement that employers fund these past service obligations. For a discussion of the taxation of qualified plans prior to ERISA, see *ERISA: Policies and Problems*, *supra* note 49, at 589-95.

there was no law compelling plans to become "qualified," the promise of "tax-free" earnings provided sufficient incentive for employers and unions to qualify their plans.[65]

While the National Labor Relations Act[66] and the Labor Management Reporting and Disclosure Act[67] contain some provisions relating to the operation of certain joint union and management pension plans, the first serious attempt at direct pension regulation was the Welfare and Pension Plans Disclosure Act of 1958.[68] This legislation was supposed to protect plan participants by requiring disclosure of certain financial and other information to the Secretary of Labor and, upon request, to plan participants. A later amendment attempted to deal with unlawful diversion of pension assets by making such activity a federal crime and granting the Secretary of Labor limited regulatory authority in this regard.[69]

The Welfare and Pension Plans Disclosure Act was not generally regarded as effective in protecting participating employees or pension assets.[70] What many perceived as serious inequities in the pension system continued in spite of the several federal statutes relating to pensions. Studies of private pension plans revealed that many plans required extended (and to some persons "onerous") periods of service before any vesting of benefits occurred.[71] It was also evident that many plans had serious funding problems; sometimes the assets were insufficient to meet accrued liabilities upon plan termination.[72] Funding problems were compounded by administrative and investment

65. For a discussion of non-qualified plans and the circumstances in which they may be more advantageous than qualified plans, see M. CANAN, QUALIFIED RETIREMENT PLANS 16-61 (1977).

66. 29 U.S.C. §§ 141-188 (1976).

67. *Id.* §§ 401-531.

68. Act of Aug. 28, 1958, Pub. L. No. 85-836, 72 Stat. 997 (codified at 29 U.S.C. §§ 301-309 (1970) (repealed by ERISA § 111, 29 U.S.C. § 1031 (1976)).

69. *Id.* § 308(a) (repealed by ERISA § 111, 29 U.S.C. § 1031 (1976)).

70. S. REP. No. 93-127, 93d CONG. 1ST SESS. 4 (1973), *reprinted in* SEN. COMM. ON LABOR AND PUBLIC WELFARE, 94TH CONG., 2D SESS., I LEGISLATIVE HISTORY OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974, at 1599 (Comm. Print 1976) [the Legislative History is hereinafter cited as I, II or III LEGISLATIVE HISTORY]. *See also* GREENOUGH & KING, *supra* note 50, at 66.

71. These vesting and service requirements are discussed at notes 97-98 *infra* and accompanying text.

72. A 1970 survey of plans which covered 7.1 million workers showed that one-third of the plans surveyed reported a ratio of assets to accrued liabilities of 50% or less; 7% reported a ratio of 25% or less. *ERISA: Policies and Problems*, *supra* note 49, at 548 n.61. Congressional concern with funding is shown in ERISA § 2(a), 29 U.S.C. § 1001(a) (1976) which states in pertinent part: "The Congress finds . . . that owing to the inadequacy of current minimum standards, the soundness and stability of plans with respect to adequate funds to pay promised benefits may be endangered . . . ." It has been suggested that pension plans are in worse financial condition than is generally reported. *See* note 88 *infra*.

abuses by pension trustees which further diminished plan assets.[73] Often these problems were further complicated by the lack of meaningful disclosure to plan participants who, ignorant of vesting and continuity of service requirements, placed unjustified reliance on future pension benefits which never materialized.[74]

C. ERISA

In addressing the issue of pension reform in the proceedings which eventuated in ERISA, Congress had two conflicting goals: it wanted to secure the receipt of employee pension benefits and, at the same time, conserve the private pension system. It was obviously disturbed by the high percentage of employees who would never receive any benefits under the pension plans in which they were participating.[75] Senator

73. *See, e.g.*, Blankenship v. Boyle, 329 F. Supp. 1089 (D.D.C. 1971) (involving alleged conduct of trustees of the United Mine Workers of America pension trust).

74. *See* notes 107-08 *infra* and accompanying text.

75. ERISA's legislative history abounds with parades of perceived horribles—the names and stories of persons like John Daniel who, after working many years for the same employer and after retirement or plan termination, found their pension expectations unmet. For example, Senator Williams remarked:

> While there can be no doubt that our private pension system has well served the needs of many workers, our study found that for countless others, the expectation of retirement benefits has proven to be built on sand.
>
> This was the experience, for example of Stephen Duane, who worked for 32 years at an A. & P. warehouse in Jersey City.
>
> Because his warehouse was shutdown [*sic*]when Mr. Duane was 4 years short of the company's minimum pension age, he received no retirement benefits whatever despite his long years of service.
>
> A similar experience was recounted by Murray Finkelstein, a New York shoe salesman.
>
> After 20 years in his retirement plan, he lost all his pension rights at age 60 when the Andrew Geller shoe store, at which he worked, went out of business.
>
> The system also failed for Iris Kweck whose employment by Anaconda was terminated after 30 years of service because of a shutdown of its Detroit billing office.
>
> At age 48, she lost all future pension rights.
>
> These are but a few of the numerous examples brought to the attention of our committee.

119 CONG. REC. 30003 (1973), *reprinted in* II LEGISLATIVE HISTORY, *supra* note 70, at 1599. Senator Bentsen remarked:

> We must not forget that the termination of a retirement plan is much more than a statistic compiled for Government charts. It is much more than a list of numbers or a series of percentages. As the victims of pension plan terminations can easily attest, a termination represents a great personal tragedy.
>
> It was certainly a real tragedy for the retired worker in Minnesota who learned that he might lose his vested pension because his former employer was about to discontinue the retirement plan. This retired worker said:
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> "If I get a cut in my pension, I don't know what I will do. My wife has been mentally ill for 14 years and had 45 shock treatments and I am doctoring for cancer since 1954. So you can see my health and my wife's are not too good. Her medicine for a year runs over $500 not including mine, so we need all the pension fund we can get."

Hartke remarked: "Today over 34 million working men and women are subject to great inequities in the private pension systems. These inequities cause the intolerable situation in which only one out of ten employees enrolled in pension plans will ever receive benefits."[76] Senator Jackson's concern was also evident:

> At present, there are 34 million workers participating in private pension plans. Undoubtedly, most of these workers are planning and relying on their pension plans to provide them with a substantial part of their retirement income. And yet, the facts are at present that only 22 percent of American workers receive all of the pension benefits which they have earned and which are rightfully theirs. I believe that these statistics are shocking and scandalous. It is just not right for the middle or low-income worker, who has made a productive contribution to his community all of his working life, to be cheated out of his pension and left out in the cold in his retirement.[77]

But while Congress wanted to protect pension benefits,[78] it was also concerned that federal regulation might eliminate or significantly reduce the number of private pension plans. The attempt to balance these competing objectives in ERISA is reflected in the following excerpt from a House Ways and Means Committee Report on the proposed legislation:

> [T]he committee has been mindful of the need to construct the new requirements so that they will provide meaningful improvement in the various problem areas noted under the present law. At the same time, the committee is aware that under our voluntary pension system, the cost of financing pension plans is an important factor in determining whether any particular retirement plan will be adopted and in determining the benefit levels if a plan is adopted, and that unduly large increases in costs

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> The experience of Olaf Anderson of Philadelphia provides another illustration. After working for the same company for 48 years, Mr. Anderson retired in 1970 and began to receive a pension of $100 a month. However, the company pension plan was terminated in 1971, and Mr. Anderson now receives no pension at all. It is interesting to note that this company provided its employees with a booklet describing the pension. The booklet informed the employees:
>
> "You can look forward to retirement with peace of mind knowing under the plan there will be a pension check in the mail to you from the company every month for life."
>
> In light of such occurrences, it is not difficult to understand why so many Americans look at the private retirement system as a series of broken promises.

120 CONG. REC. 29950 (1974), *reprinted in* III LEGISLATIVE HISTORY, *supra* note 70, at 4793-94.

76. SENATE COMM. ON FINANCE, REPORT ON PRIVATE PENSION PLAN REFORM, S. REP. No. 93-383, 93d Cong., 1st Sess. 151 (1973) (additional views of Mr. Hartke), *reprinted in* I LEGISLATIVE HISTORY, *supra* note 70, at 1218.

77. 119 CONG. REC. 29839 (1973), *reprinted in* I LEGISLATIVE HISTORY, *supra* note 70, at 1267.

78. *See* ERISA § 2(b)-(c), 29 U.S.C. § 1001(b)-(c) (1976).

> could impede the growth and improvement of the private retirement system. For this reason, in the case of those requirements which add to the cost of financing retirement plans, the committee has sought to adopt provisions which strike a balance between providing meaningful reform and keeping costs within reasonable limits.[79]

An understanding of these problems and the solutions attempted by ERISA is necessary in order to analyze the issues involved in *Daniel.*

1. Funding Practices

Since pension plans are a means of encouraging long-term employment and also retirement of older, highly paid workers, plans generally require employees to reach a specified retirement age and complete a long employment period before qualifying for benefits.[80] When a plan is initially adopted many older employees would never be able to complete the lengthy employment term required for pension eligibility unless they received credit for their pre-plan employment. Consequently, at adoption most plans credit present employees with their past service, and those employees thereby become eligible for full retirement benefits a relatively short time after the plan is adopted. Therefore, under any defined benefit plan the annual pension benefit payout increases rapidly for the first several years of plan operation as more employees are added to the benefit drawing group than are removed by death. Generally, it will take a substantial time period for the size of the retirement group and the annual pension benefit payout to stabilize.[81]

Since no funds have been set aside for the retirement of those older workers receiving past service credit, most defined benefit pension plans have large unfunded past service obligations. In addition, there is considerable doubt that, under many plans, present service costs are adequately funded.[82]

One of the most serious risks to the receipt of pension benefits is the termination of a pension plan before full funding is achieved. Plans typically provide that the employer is not liable if plan assets prove insufficient to pay liabilities.[83] Thus, prior to ERISA, when an un-

79. HOUSE COMM. ON WAYS AND MEANS, PRIVATE PENSION TAX REFORM, H.R. REP. No. 93-807, 93d Cong., 2d Sess. 14-15 (1974), *reprinted in* II LEGISLATIVE HISTORY, *supra* note 70, at 3134-35.

80. *See* note 58 *supra* and accompanying text.

81. MELONE & ALLEN, *supra* note 61, at 65-66.

82. For a discussion of underfunded plans and liabilities, see note 72 *supra* and note 88 *infra.*

83. BERNSTEIN, *supra* note 56, at 34. Some collectively bargained plans provide that "the employer is liable for whatever contributions were agreed upon." *Id.*

derfunded pension plan was terminated, at least some employees did not receive their full pension benefits.

A good illustration of the vulnerability of pension benefits to premature plan termination is provided by the Studebaker experience. In 1964, Studebaker closed its South Bend, Indiana plant and terminated its underfunded pension plan. While a limited number of Studebaker employees received their full pension benefits, a substantial portion of those with vested benefits received only fifteen cents on the dollar; others received nothing.[84]

Before ERISA there were no mandatory funding requirements for pension plans and a variety of mechanisms were in use. Some plans were entirely unfunded with employers making current disbursements to pay pension obligations as they became due. Partially or fully funded plans were financed by "terminal" or "advance" funding. Under terminal funding, when a retiring employee became eligible for pension benefits, the employer set aside a lump sum from which the promised monthly benefits were paid. Since plans using terminal or current disbursement financing could not obtain qualified status, these types of financing were not often used.[85] Advance funding, now required by ERISA, has always been the most common type of plan financing, since it was the only financing which permitted plan qualification prior to ERISA. The employer periodically sets aside funds prior to employee retirement. However, the funds are not necessarily earmarked for particular employees. While employer contributions may be used to purchase annuity type insurance policies, contributions are most frequently placed in a trust fund from which pension obligations are paid as they become due.[86] Even qualified plans utilizing advance funding were not required to fund past service obligations,[87] however, and many pension plans had, and still have today, huge unfunded past service obligations.[88]

84. 120 CONG. REC. 29950 (1974) (Remarks of Senator Bentsen), *reprinted in* II LEGISLATIVE HISTORY, *supra* note 70, at 4793.

85. For a discussion and comparison of the various types of financing mechanisms in use before ERISA, see MELONE & ALLEN, *supra* note 61, at 69-80.

86. *Id.* at 74.

87. *See* note 64 *supra.*

88. *See generally* Ehrbar, *Those Pension Plans are Even Weaker than You Think*, FORTUNE, Nov. 1977, at 104. Ehrbar suggests that pension liabilities are "ridiculously understated." He points out that legitimate actuarial methods produce widely differing results and suggests that even under ERISA the accounting and actuarial treatment of pension liabilities is a "masterpiece of obfuscation" particularly with respect to the latitude permitted actuaries in choosing wage and interest assumptions. In determining plan costs and liabilities and the appropriate level of employer contribution under a defined benefit plan, actua-

Congress was concerned with this underfunding and was determined to encourage and eventually to require full funding of all pension obligations.[89] It did not do so by mandating immediate funding of past service obligations. The cost to the employer of such a requirement would have been so high as to jeopardize the continuation of existing plans and to discourage the inclusion of past service credits in new plans.[90] Instead ERISA requires gradual amortization of past service obligations.[91] Additional provisions discourage underfunding of pension plans.[92]

Even under the new funding rules, however, it will be many years before most plans become fully funded. In order to protect employee benefits during this interim period, ERISA provides for termination insurance underwritten by the Pension Benefit Guaranty Corporation (PBGC).[93] Upon plan termination, this insurance guarantees, with

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ries work with employers in estimating the rate of return at which plan assets will be invested (the interest assumption) and the rate at which wages will grow (the wage assumption). *Id.* at 107. Small errors in either assumption produce substantial differences in the calculation of plan costs and liabilities. The author cites Professor Winklevoss of Wharton who states that on the average, an increase of 1% in the interest assumption will cause a 25% reduction in plan expenses and liabilities. Likewise a 1% reduction in the wage assumption will produce a 13% reduction in the calculation of expenses and liabilities. *Id.* Moreover, Ehrbar estimates that the adoption of more realistic assumptions would nearly double corporate pension liabilities and quintuple unfunded liabilities. *Id.* at 107-08.

89. ERISA § 302, 29 U.S.C. § 1082 (1976).

90. Generally, the 30-year amortization requirements initially add only moderately to an employer's funding cost under present law. This is true because under present law interest on unfunded accrued past service liabilities (which accounts for the bulk of the level amortization payments required under the bill in the early years) must be contributed to a qualified pension plan. Therefore, your committee believes that 30-year amortization will not hamper an employer in starting a new plan, or in adding plan amendments, that includes past service liabilities. Similarly, the 40-year amortization will not unduly increase present costs of an employer with an existing plan.

HOUSE COMM. ON WAYS AND MEANS, PRIVATE PENSION TAX REFORM, H.R. REP. NO. 93-779, 93d CONG., 2d SESS. 76-77 (1974), *reprinted in* II LEGISLATIVE HISTORY, *supra* note 70, at 2665-66.

91. Past service costs for existing plans and for all multi-employer plans must be amortized within 40 years. ERISA § 302(b)(2)(B), 29 U.S.C. § 1082(b)(2)(B) (1976). For certain new plans a 30 year amortization is required. *Id.* However, under certain circumstances the Secretary of the Treasury is authorized to grant employers variances or waivers from the minimum funding standards if satisfaction of the standards would result in substantial business hardship. *Id.* § 303, 29 U.S.C. § 1083 (1976).

92. *See, e.g.*, ERISA § 1013(c)(1), I.R.C. § 404(a)(1)(A) (higher maximum tax deduction permitted employers for contributions above the minimum standard); ERISA §§ 501-502, § 1013(b), I.R.C. § 4971 (penalties and taxes for funding deficiencies); ERISA §§ 3041-3042, 29 U.S.C. §§ 1241-1242 (1976) (government regulation of actuaries through establishment of Joint Board of Actuaries). For a thorough discussion of funding restrictions, see *ERISA: Policies and Problems*, *supra* note 49, at 589-606.

93. ERISA § 4002, 29 U.S.C. § 1302 (1976) establishes within the Department of Labor a corporate body known as the Pension Benefit Guaranty Corporation.

some limitations, the payment to employees of all vested benefits payable under defined benefit plans.[94] The insurance is to be paid for in part by compulsory annual fixed premiums from employers and also by payments from employers who terminate underfunded plans.[95] Such an employer is contingently liable, up to thirty percent of the employer's net worth, for any payments made by PBGC because of the termination of a plan in which the employer participated.[96]

2. Vesting and Continuity of Service Requirements

Private pension plans generally required long periods of continuous employment in order to qualify for pension benefits at normal retirement age. Some plans failed to provide for any pre-retirement vesting of benefits and employees whose employment terminated prior to normal retirement frequently lost their right to a pension.[97] Often a short

94. ERISA states that, subject to certain limitations, the PBGC shall guarantee payment of all non-forfeitable basic benefits payable under certain qualified single-employer defined benefit plans and amendments thereto which have been in effect for a 5 year period. ERISA § 4022(a), (b)(1), 29 U.S.C. § 1322 (a), (b)(1) (1976). Benefits payable under plans or amendments which have been in effect less than 5 years are partially guaranteed in proportion to the amount of time they have been in effect. *Id.* § 4022(b)(8), 29 U.S.C. § 1322(b)(8) (1976). Benefits which become nonforfeitable solely because of plan termination are not guaranteed, nor are benefits under a plan which is terminated for the purpose of obtaining the payment of benefits by the PBGC. *Id.* § 4022(a), (c), 29 U.S.C. § 1322(a), (c) (1976). While the compulsory insurance of non forfeitable benefits payable under single-employer plans is already in effect, the mandatory insurance of benefits payable under multi-employer plans is deferred until July 1, 1979. *Id.* § 4082(b), 29 U.S.C. § 1381(b) (1976). For a more detailed discussion of plan termination insurance and employers' contingent liability, see *ERISA: Policies and Problems*, *supra* note 49, at 607-21.

95. ERISA § 4005(b)(1), 29 U.S.C. § 1305(b)(1) (1976). The compulsory benefit insurance may involve a significant redistribution of wealth between the shareholders and employee beneficiaries of financially weak employers with financially troubled pension plans and the shareholders and employees of financially strong employers with fully funded pension plans. *See* Ehrbar, *Those Pension Plans are Even Weaker than You Think*, FORTUNE, Nov. 1977, at 110-11.

96. ERISA §§ 4062, 4064, 29 U.S.C. §§ 1362, 1364 (1976). The PBGC is instructed to offer employers insurance against this contingent liability. *Id.* § 4023, 29 U.S.C. § 1323 (1976). *See* note 127 *infra*.

97. Studies have revealed that in 1969 13% of the employees covered by private single-employer retirement plans and 49% of the employees covered by private multi-employer retirement plans (comprising 23% of the employees covered by private retirement plans) were under plans with no provision for pre-retirement vesting. The remaining employees were under plans which made some provision for pre-retirement vesting: (1) 1% were covered by plans providing for vesting after 5 years of service; (2) 45% were covered by plans providing for full or graded vesting after 10 years of service; (3) 39% were covered by plans providing for vesting after 15 years of service; and (4) 3% were covered by plans providing for vesting after more than 20 years of service. GREENOUGH & KING, *supra* note 50, at 165.

These studies reveal a substantial improvement over the more stringent service and vesting provisions found in plans in the 1950's when 50% of employees covered by private peninterruption in employment caused a period of employment to be excluded from consideration in determining benefit eligibility.[98]

The Local 705 International Brotherhood of Teamsters Pension Trust Fund Pension Plan (Local 705 Plan) contained many restrictions of this type. At the time Mr. Daniel applied for retirement benefits in December of 1973, the Local 705 Plan required beneficiaries to have completed twenty consecutive, uninterrupted years of employment immediately preceding retirement. Any short lay-off or break in service prior to January 1970 caused earlier employment to be disregarded in the calculation of the twenty consecutive years.[99]

Daniel highlights the effect of such rigorous eligibility requirements. Mr. Daniel was sixty-three years old when he retired with impaired vision after twenty-two and one-half years of employment with employers who participated in the Local 705 Plan. He was declared ineligible for benefits because of an involuntary four month lay-off in his ninth year of employment.

During the Congressional debates on ERISA, Senator Bentsen may well have been using the twenty-year vesting requirement of the Local 705 Plan as an example of the need for minimum vesting standards.

> Another example of unreasonable vesting requirements involves the participants of a union-administered pension plan in Chicago. Each local within this union administers its own pension plan. Under the terms of these plans a worker must remain within the same local for 20 years in order to acquire any vested rights. Sometimes a slight shift in jobs—perhaps from the loading docks to the weighing station—involves a shift in union locals and a complete loss of all pension rights for an employee with less than 20 years on the first job.
>
> These are only a few examples of the way countless numbers of American working men and women have been tragically victimized by unreasonable vesting provisions in their pension plans.
>
> Such tragic losses of pension benefits will be prevented in the future when this pension legislation goes into effect. Under this bill, the em-

sion plans were under plans with no provision for pre-retirement vesting. An excellent description of the vesting and service requirements of private retirement plans in the 1950's may be found in BERNSTEIN, *supra* note 56, at 20-32.

It should be noted that vesting statistics do not take into account the fact that under multiemployer plans an employee does not lose his prior employment credit when he changes jobs and works for another employer who participates in the plan. *Id.* at 25.

98. BERNSTEIN, *supra* note 56, at 21.

99. The Local 705 Plan has been liberalized to permit employees to undergo two involuntary breaks in service (after January 1970) under certain specified circumstances. 1973 Local 705 Pension Plan Booklet 4 (Jan. 1973). But this modification was not designed to benefit employees such as Mr. Daniel who have already received advantageous treatment under the past service credit provisions of the plan.

ployer or union running the plan has the option of meeting one of three minimum vesting formulas.[100]

ERISA includes minimum vesting standards which may be achieved under three alternate vesting schedules, all of which encourage early vesting.[101] If the Local 705 Plan had included any of these vesting schedules, Mr. Daniel's pension would have vested prior to his retirement. In addition, had the Local 705 Plan contained the type of break in service provision mandated by ERISA, Mr. Daniel's short lay-off would not have caused his long prior employment to be disregarded.[102]

3. Participation

Another problem closely associated with the prolonged vesting requirements is that of participation standards. An employee's entry or participation in a pension plan is generally governed by age and length of employment. Prior to ERISA it was common practice to exclude young employees from participation until they had completed long periods of employment.[103] The only governmental regulation of participation was a requirement that, in order to qualify for preferential tax treatment, a plan could not exclude employees who had worked for more than five years.[104]

ERISA's new participation requirements reflect an attempt to strike a balance between encouraging early employee participation and minimizing the high cost factors associated with permissive participation provisions. With minor exceptions,[105] ERISA now mandates em-

100. 120 CONG. REC. 29950 (1974), *reprinted in* III LEGISLATIVE HISTORY, *supra* note 70, at 4792.

101. ERISA § 203(a), 29 U.S.C. § 1053 (1976).

102. Under ERISA, existing plans may disregard years of service prior to ERISA which would have been disregarded under the plan's break in service rules in effect before ERISA. Subject to this and a few relatively minor exceptions, the general rule is that all employment years during the term of the pension plan in which an employee completes 1000 hours of service must be counted for purposes of vesting. *Id.* § 203(b)(1)-(2), 29 U.S.C. § 1053(b)(1)-(2) (1976). A 1 year break in service only occurs when an employee fails to complete more than 500 hours of service in any consecutive 12 month period. *Id.* § 203(b)(3)(A), 29 U.S.C. § 1053(b)(3)(A) (1976). In only a limited number of situations are plans permitted to disregard an employment year prior to a 1 year break in service. For a more detailed discussion of the break in service requirements, see *ERISA: Policies and Problems*, *supra* note 49, at 576-78.

103. Such a requirement excludes high-turnover employees from participation and thereby avoids the administrative expenses related to bringing them into a plan as participants. D. MCGILL, FUNDAMENTALS OF PRIVATE PENSIONS 82 (3d ed. 1975).

104. Int. Rev. Code of 1954, ch. 736, § 401(a)(3)(A), 68 Stat. 730 (now I.R.C. § 401(a)(3)).

105. *E.g.*, ERISA § 202(a)(2)(B), 29 U.S.C. § 1052(a)(2)(B) (1976) (permits defined benefit plans to exclude from participation older employees who begin work within 5 years of normal retirement age under the plan); *id.* § 202(a)(1)(B)(i), 29 U.S.C. § 1052(a)(2)(B)(i)

ployee participation after an employee reaches age twenty five and completes one year of employment.[106]

4. Disclosure

Before the enactment of ERISA, there was concern over possible inadequacies in the disclosure of pension plan provisions to employees.[107] A purported serious deficiency in the reporting system established by the Welfare and Pension Plans Disclosure Act was that disclosure was made only to the Secretary of Labor. Information was available to plan participants only upon request.[108]

ERISA repeals the Welfare and Pension Plans Disclosure Act[109] and substitutes a system of prescribed disclosures to plan participants. In addition, ERISA requires comprehensive reporting to the Secretary of Labor. Participants and beneficiaries must each be furnished with a comprehensive summary of the pension plan, written in a manner designed to be understood by average participants and reasonably calculated to advise them of their rights and obligations under the plan.[110] Among other things, the summary must describe the participation and vesting requirements and the circumstances likely to result in ineligibility or loss of benefits.[111] A description of the claim and redress procedures for denied claims must also be included.[112] A summary must be furnished shortly after participation or benefit payments begin. Further summaries are to be furnished after material modifications are made to the plan and at five- or ten-year intervals.[113] Each year participants and beneficiaries must also be furnished certain financial information concerning plan assets, including a balance sheet and a

(1976) (permits plans which provide for 100% vesting after not more than 3 years of service to exclude employees from participation until they are 25 years of age and have completed 3 years of service).

106. *Id.* § 202(a)(1)(A), 29 U.S.C. § 1052(a)(1)(A)(1976). For a comprehensive discussion of the participation standards, see *ERISA: Policies and Problems*, *supra* note 49, at 566-71.

107. *Id.* § 2(a), 29 U.S.C. § 1001(a) (1976) provides in pertinent part: "The Congress finds that . . . owing to the lack of employee information and adequate safeguards concerning their operation, it is desirable and in the interests of employees and their beneficiaries, . . . that disclosure be made and safeguards be provided with respect to the establishment, operation, and administration of such plans . . . ."

108. 29 U.S.C. § 307(a) (1970) (repealed by ERISA § 111(a), 29 U.S.C. § 1031(a) (1976)).

109. *Id.* However, the Welfare and Pension Plans Disclosure Act remains in effect for certain transactions occurring prior to January 1, 1975.

110. ERISA §§ 101(a), 102(a)(1), 29 U.S.C. §§ 1021(a), 1022(a)(1) (1976).

111. *Id.* § 102(b), 29 U.S.C. § 1022(b) (1976).

112. *Id.*

113. *Id.* § 104(b)(1), 29 U.S.C. § 1024(b)(1) (1976).

schedule of receipts and disbursements.[114]

In addition to the above information, a participant may request other information, including a written statement from the plan administrator of the total benefits accrued, the earliest date when vesting will occur, and the nonforfeitable amount, if any, of any monthly pension benefits available at normal retirement age.[115] Participants and beneficiaries may also demand a copy of the annual report required to be filed with the Secretary of Labor.[116] This report contains detailed information and financial data and must be certified by a public accountant and an actuary.[117]

The elaborate reporting and disclosure requirements of ERISA are intended to complement the substantive protections afforded employees by the new vesting and participation standards. The idea is that informed employees can better enforce the new rights ERISA creates for them. Equally important is the probability that meaningful communication of pension information will discourage employees from placing unjustified reliance upon receipt of future benefits.

IV. Should the Federal Securities Laws Be Applied to Pension Plans?

There are, of course, important political questions raised whenever courts, rather than legislatures, expand existing law to the extent that this was done in *Daniel*. However, the focus of this article is on the question of whether *Daniel's* expansion of the antifraud provisions of the securities laws is likely to produce benefits that exceed their costs.

A. The Costs of Pension Regulation and Congressional Concern with Them

ERISA and its legislative history show clearly that Congress was concerned with the cost of pension regulation.[118] The careful consideration of the costs imposed by the new vesting rules and the refusal to apply the new vesting and break in service requirements retroactively

114. *Id.* §§ 103(b)(3)(A)-(B), 104(b)(3), 29 U.S.C. §§ 1023(b)(3)(A)-(B), 1024(b)(3) (1976).
115. *Id.* § 105(a), 29 U.S.C. § 1025(a) (1976).
116. *Id.* § 104(a), (b)(4), 29 U.S.C. § 1024(a), (b)(4) (1976).
117. *Id.* § 103, 29 U.S.C. § 1023 (1976).
118. *E.g.*, Congress considered the study of the National Federation of Independent Business which analyzed the impact of the proposed legislation on small businesses. It was estimated that the new funding, vesting and participation requirements would impose the following additional costs on small employers if current benefit levels were not reduced:

are obvious examples.[119] ERISA also permits plans to exclude certain younger and older employees from particiption, thereby relieving em-

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New Requirements Under ERISA	Annual Increase In Employer Contribution
Vesting standards	$ 720,000,000
Funding requirements	498,000,000
Participation standards	5,000,000,000

120 Cong. Rec. 4311 (1974), *reprinted in* II Legislative History, *supra* note 70, at 3460.

A study of the cost of mandatory vesting provisions included in a report of the Senate Finance Committee estimated that the new vesting standards would increase present plan costs by 0 to 58%, depending on the liberality of the pre-ERISA vesting provisions in existing plans.

ESTIMATED RANGE OF INCREASE IN PENSION PLAN COSTS UNDER REQUIREMENT FOR MINIMUM VESTING ADOPTED BY THE COMMITTEE

	Present vesting: None	Present vesting: Moderate[1]	Present vesting: Liberal[2]	All plans
Percentage of pension plan members covered under such plans	23	56	21	100
Range of present plan cost as a percent of payroll ...	1.8-11.2	2.2-12.5	2.2-12:7	1.8-12.7
Range of increase in cost under committee vesting requirement:				
As a percent of payroll	.2-1.5	.1-.2	0-.1	0-1.5
As a percent of present plan cost	5-58	1-8	0-3	0-58

1 Plan provides some vesting, but less liberal than full vesting after 10 years of service.
2 Plan provides full vesting after 10 years service or less, with no age requirement.
Source: "Summary of Report, Study of the Cost of Mandatory Vesting Provisions Prepared for the Joint Committee on Internal Revenue Taxation," by Donald S. Grubbs, Jr., July 30, 1973.

S. Rep. No. 93-383, 93d Cong., 1st Sess. 21 (1973), *reprinted in* I Legislative History, *supra* note 70, at 1089.

119. The general rule is that plans subject to ERISA must give vesting credit for pre-ERISA employment. However plans may disregard years of service prior to ERISA which "would have been disregarded under the rules of the plan with regard to breaks in service, as in effect on the applicable date." ERISA § 203(b)(1)(F), 29 U.S.C. § 1053(b)(1)(F) (1976). Also, plans need not give vesting credit for certain pre-ERISA employment of employees who do not complete 3 years of employment after December 31, 1970. ERISA § 203(b)(1)(E), 29 U.S.C. § 1053(b)(1)(E) (1976). In commenting on the latter provision Representative Ullman stated: "The purpose of the provisions is to avoid imposing on plans very heavy costs for providing retroactive vesting for employees who have already terminated their service. This might jeopardize benefits for employees still covered under the plan and could involve very serious recordkeeping problems." 120 Cong. Rec. 29199 (1974), *reprinted in* I Legislative History, *supra* note 70, at 4675.

ployers of the high costs associated with their inclusion.[120] In addition, ERISA itself provides for waivers and variances of some requirements on the basis of cost considerations.[121] This concern with costs was premised on the belief that employers would create or maintain fewer pension plans and would reduce pension benefits as their costs increased.

Implicit in ERISA, however, is the judgment that it is socially desirable to protect some level of benefits for employees participating in the various pension plans.[122] There is obviously a trade-off between those benefits which Congress sought to assure through ERISA and the costs which Congress knowingly imposed upon the system in adopting ERISA.[123] While the exact weight accorded to various costs and benefits cannot be specified precisely, it appears that Congress was willing to accept a sharp decline in the number of extant plans as the price of increasing the welfare of the beneficiaries of the remaining plans. If Congress was not, indeed, willing to make that trade-off, then it apparently misjudged the extent and impact of the costs which ERISA entailed.

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120. *See* remarks of Representative Ullman, 120 CONG. REC. 29199 (1974), *reprinted in* III LEGISLATIVE HISTORY, *supra* note 70, at 4674.

121. *E.g.*, ERISA § 303, 29 U.S.C. § 1083 (1976) permits the Secretary of the Treasury under certain circumstances to grant variances from the new funding standards; *id.* § 207, 29 U.S.C. § 1057 (1976), discussed at note 101 *supra*, permits the Secretary of Labor under certain circumstances to grant waivers and variances from the new vesting standards; *id.* § 110, 29 U.S.C. § 1030 (1976) permits the Secretary of Labor under certain circumstances to grant variances from the new disclosure standards.

122. *See, e.g.*, ERISA § 2(b)-(c), 29 U.S.C. § 1001(b)-(c) (1976).

123. In the debate on the Conference Report which later became ERISA, Senator Nelson stated:

> In all its deliberations and decisions, Congress was acutely aware that under our voluntary pension system the cost of financing pension plans is an important factor in determining whether a pension plan will be adopted. Unduly large increases in cost can impede the progress of the private pension system. For this reason, in the case of those requirements which add to the cost of financing pension plans, Congress tried to adopt provisions which strike a balance between providing a meaningful protection for the employees and keeping costs within reasonable limits for employers.

120 CONG. REC. 29952 (1974), *reprinted in* III LEGISLATIVE HISTORY, *supra* note 70, at 4800.

Representative Ullman made the following remarks on the Conference Report:

> I want to emphasize that these new requirements have been carefully designed to provide adequate protection for employees and, at the same time, provide a favorable setting for the growth and development of private pension plans. It is axiomatic to anyone who has worked for any time in this area that pension plans cannot be expected to develop if costs are made overly burdensome, particularly for employers who generally foot most of the bill. This would be self-defeating and would be unfavorable rather than helpful to the employees for whose benefit this legislation is designed. For this reason, we have been extremely careful to keep the additional costs very moderate. The additional costs resulting from the new minimum vesting requirements in the bill, for example, for the most part is expected to range only from 0 to 1.5 percent of payroll.

Id. at 29198, *reprinted in* III LEGISLATIVE HISTORY, *supra* note 70, at 4673.

It cannot be doubted that such costs are significant: the most obvious are those associated with the new vesting, participation and funding requirements.[124] Additional costs are imposed by compliance with the new disclosure and filing requirements[125] and by premiums on mandatory benefit insurance guaranteeing the employee's receipt of vested, accrued benefits upon plan termination.[126] In addition, an em-

124. The Subcommitteee on SBA and SBIC Legislation and General Small Business Problems of the House Committee on Small Business recently surveyed all employers which had notified the PBGC during the period June 1976 through April 1977 that they intended to terminate pension plans. The questionnaires were designed to obtain information on the effect of ERISA on the decision to terminate these pension plans. Approximately 79% indicated that ERISA had an effect upon the decision to terminate. Those employers citing ERISA as a factor affecting their decision to terminate were asked to indicate the extent of cost increases imposed by ERISA's funding, participation and vesting requirements. Approximately 48% indicated that the increased "contributions required to provide benefits to employees entering the plan due to the new eligibility standards" were "very large." Approximately 30% indicated that the increased "contributions required to meet new minimum funding standards" were also "very large." Approximately 22% indicated that the cost increase for "providing benefits to terminating employees due to new vesting provisions" was "very large." STAFF OF HOUSE COMM. ON SMALL BUSINESS, 95TH CONG., 1ST SESS., ERISA QUESTIONNAIRE RESULTS (Comm. Print 1977), *reprinted in* [1977] 4 PENS. PLAN GUIDE (CCH) ¶ 25,194 [hereinafter cited as ERISA QUESTIONNAIRE].

125. In a recent survey of employers which were terminating pension plans, those citing ERISA as a factor affecting their decision to terminate were asked to quantify the cost increases imposed by certain administrative costs associated with ERISA. A large number of those businesses responding indicated that the cost increases for record keeping (approximately 27%) and reporting to employees (approximately 26%) were "very large." Over 53% responded that cost increases related to reporting to government agencies were "also very large." *Id. See* note 124 *supra*.

Senators Bentsen and Lugar have sponsored legislation which would reduce the paperwork required by ERISA. S. 3193, 95th Cong., 2d Sess. (1978), *discussed in* 195 PENS. REP. (BNA) A-6 (July 3, 1978).

126. The original annual premium rate for single-employer plans was $1.00 per employee participant. ERISA § 4006(a)(3), 29 U.S.C. § 1306(a)(3) (1976). After studying its potential liabilities arising from its guarantee of benefits to participants in single-employer plans, the PBGC found:

> As a result of the study, it is clear that the present rate of $1.00 is just not adequate to finance the claims associated with current and likely future terminations on a sound basis. By the end of September 1976, the Corporation had about a $41 million deficit. The deficit has now increased to approximately $60 million.

[1977] 4 PENS. PLAN GUIDE (CCH) ¶ 23,034 (Remarks of Matthew M. Lind, Acting Executive Director of PBGC). Congress responded by raising the annual premium rate for single-employer plans to $2.60 per participant. ERISA § 4082(e), 29 U.S.C. § 1381(e) (1976).

ERISA originally provided that the PBGC would guarantee payment of certain benefits payable under multi-employer plans terminating after January 1, 1978. ERISA § 4082(c), 29 U.S.C. § 1381(c) (1976). The annual premium for multi-employer plans was set at 50 cents per participant. ERISA § 4006(a)(3), 29 U.S.C. § 1306(a)(3) (1976).

A September 29, 1977 PBGC study revealed that,

> approximately one-eighth of all multiemployer plans, covering one-fifth of participants in such plans, are experiencing significant financial hardship which may result in plan termination.

ployer is now contingently liable, up to a maximum thirty percent of net worth, if there are insufficient assets to pay vested pension obligations upon plan termination.[127] Consideration must also be given to the costs of the relatively new and untested fiduciary duty and civil liability provisions of ERISA.[128]

The prediction that increased costs would lead to the maintenance and creation of fewer plans is not contradicted by statistics maintained by the Internal Revenue Service. These statistics compare the two years following the adoption of ERISA with previous periods and show both a significant increase in plan terminations and a decrease in the number of new plans being written.[129] Not only are fewer plans being written, but these new plans are primarily defined contribution plans,

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. . . .

> Thus, because of the magnitude of the potential liabilities of terminating multiemployer plans and its impact on the current insurance program and employers, and because of the potentially adverse impact of Title IV on the growth and continuance of multiemployer plans, it is essential that a serious and immediate reexamination be undertaken of the provisions of Title IV applicable to these plans.

H.R. REP. No. 95-706, 95th Cong., 1st Sess. 2, 3 (1977), *reprinted in* Pension Benefit Guarantee Corporation, *Potential Multiemployer Plan Liabilities Under Title IV of ERISA*, [1977] 4 PENS. PLAN GUIDE (CCH) ¶ 23,036.

Congress responded by deferring PBGC's mandatory termination insurance coverage of multi-employer plans for eighteen months, until July 1, 1979. ERISA § 4082(c), 29 U.S.C. § 1381(c) (1976).

On July 2, 1978 PBGC reported to Congress on multi-employer plan insurance. The report contains discouraging findings on the financial condition of many multi-employer plans:

> Approximately 160 multiemployer plans covering 1.3 million participants have characteristics indicating a possibility of termination during the next 10 years. If all 160 were to terminate, the total estimated present value of the gross unfunded liability for the guaranteed benefits would be $8.3 billion. An annual premium of $80 per participant could be required to finance these liabilities under the current program.

Fact Sheet on Multiemployer Plan Termination Insurance: PBGC Report to Congress, [1977] 4 PENS. PLAN GUIDE (CCH) ¶ 22,752. The report contains several proposals designed to strengthen multi-employer plans and discourage their termination. A modification of the current guarantee structure and a removal of the current net worth limitation on employer liability are among the program alternatives suggested. *Id.*

127. ERISA § 4062(b), 29 U.S.C. § 1362(b) (1976) (liability of employers under single-employer plans); ERISA § 4064(b), 29 U.S.C. § 1364(b) (1976) (liability of employer under multi-employer plans). ERISA § 4023, 29 U.S.C. § 1363 (1976) directs the PBGC to insure or arrange for others to insure employers against contingent liabilities arising from plan termination. The PBGC has recently reported to Congress that the contingent employer liability insurance program is not feasible and has recommended further study of several alternative approaches which would restructure employer liability. *Fact Sheet on Contingent Employer Liability Insurance: Status Report to the Congress*, [1977] 4 PENS. PLAN GUIDE (CCH) ¶ 22,752.

128. For a discussion of these new fiduciary standards and the liabilities of fiduciaries, see Little & Thrailkill, *Fiduciaries Under ERISA: A Narrow Path to Tread*, 30 VAND. L. REV. 1 (1977).

129. The following table sets forth annual totals of new plans and terminated plans from 1965 to 1976 and the ratio of new plans to terminated plans:

which are exempt from ERISA's costly funding and insurance requirements and often provide smaller benefits than defined benefit plans.[130]

However, it is not altogether clear that the contraction of the pension plan population is attributable entirely to ERISA. Although the new legislation is highly suspect as a principal cause of that decline,[131] several preliminary surveys of terminated plans have been made with varying results.[132] Without data on the lost pension benefits associated

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Tax-Qualified Corporate Plans

	New Plans	Terminated Plans	Ratio of New Plans to Terminated
1965	13,532	1,036	13.1
1966	18,183	1,210	15.0
1967	20,521	1,307	15.7
1968	23,782	1,443	16.5
1969	28,075	1,729	16.2
1970	32,574	2,306	14.1
1971	40,664	3,335	12.2
1972	49,335	3,520	14.0
1973	59,605	4,130	14.4
1974	59,385	4,604	12.9
1975	30,039	8,108	3.7
1976	25,820	15,859	1.6

Library of Congress, Jan. 27, 1978, *reprinted in* Scheibla, *Revamping ERISA*, Barron's, May 1, 1978, at 4, 5, cols. 2 and 3.

These statistics suggest a substantial reduction in the growth of the plan population. It must be noted, however, that these statistics reflect only the number of pension plans, and it is unknown how many employees are covered under such plans.

In addition, PBGC has stated that a large number of existing multi-employer plans are in poor financial condition and may be terminated. *See* note 126 *supra*.

130. Congressional Research Service Report on Pension Plan Terminations, *reprinted in* 129 PENS. REP. (BNA) R-23 (March 21, 1977).

131. In an attempt to estimate how many pension plan terminations would have occurred in the absence of ERISA, regression analysis was applied to control for the effects of inflation and historical and seasonal trends. It was then estimated that, absent ERISA, there would have been 9,132 plan terminations in the 24 month period following ERISA's enactment; instead 21,123 occurred. *Id.*

In a recent survey of employers which were terminating pension plans, approximately 79% of those responding indicated that ERISA affected their decision to terminate. Substantially all (93%) of those citing ERISA as a cause of termination indicated that its increased costs had some effect on the termination decision. ERISA QUESTIONNAIRE, *supra* note 124.

A survey by Senator Lugar of small Indiana businesses indicated that ERISA is the principal reason for the high rate of plan terminations and the reduced number of new plans being written by that survey's sample group. 195 PENS. REP. (BNA) A-6 (July 3, 1978).

132. A PBGC analysis of single-employer defined benefit plan terminations in 1975 revealed that in those terminations involving an ongoing employer, 35% indicated a new pension plan as the reason for termination; 12% indicated ERISA as the only reason for

with terminated and unwritten plans and any lowering of pension benefits under present and future plans, it cannot be determined if ERISA has resulted in net losses or gains to society. The benefits lost as a result of ERISA must be compared to the increased security and benefit levels of persons receiving or expecting benefit payments under ERISA.[133] Many other costs must be identified, including those imposed by ERISA's many requirements. Several cost-benefit studies of post-ERISA plan experiences are being considered by various groups, including Congress and several government agencies.[134]

It is here that we find the first cost of *Daniel*: its effects may well be intermingled with those of ERISA, making it difficult to evaluate the latter. Many plan terminations and failures to raise benefit levels or to

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termination and an additional 11% cited ERISA and other reasons for termination. Although 77% did not cite ERISA as a reason for termination, some pension experts have questioned the validity of these responses. Under preexisting IRS rules, the discontinuance of a pension plan within a few years of adoption for other than valid business reasons could result in adverse tax consequences. Congressional Research Service Report on Pension Plan Terminations, *reprinted in* 129 PENS. REP. (BNA) R-23-24 (March 21, 1977).

133. The amount of social loss does not equal the reduction in pension benefits produced by ERISA-related cancellations or failures to write new pension plans. Presumably employers will pay alternative compensation approximately equal to that which would have been contributed to the pension fund. Perhaps longevity bonuses or other fringe benefits will be substituted for pension plans. This will produce a social loss, however, because employers and employees will be forced to a less preferred position by the regulation. The fact that before the regulation they chose pensions over other forms of compensation suggests that they valued pensions more than they valued the other forms of compensation. The social loss will equal this difference in valuation.

Since the alternative compensation may not qualify for the preferential tax treatment afforded pension plans, employees may ultimately receive less than they would have received under a pension plan and the government may receive more. There will be an additional social loss measured by the difference in consumer satisfaction created when the government spends the money as compared to that created if the pensioners could have spent it themselves. Additional losses may be generated by the transaction costs of devising and implementing the substitute forms of compensation.

134. ERISA § 512, 29 U.S.C. § 1142 (1976), establishes the Advisory Council on Employee Welfare and Pension Benefit Plans which is to advise the Secretary of Labor. *Id.* § 513(a), 29 U.S.C. § 1143(a) (1976) directs the Secretary of Labor to undertake specified research studies on pension plans. *Id.* §§ 3021-3022, 29 U.S.C. 1221-1222 (1976) create the Joint Pension, Profit Sharing and Employee Stock Ownership Plan Task Force and direct it to make a study of certain aspects of pension plans. *Id.* § 3031(a), 29 U.S.C. § 1231(a) (1976) directs certain Congressional committees to undertake specified studies of retirement plans. *Id.* § 3032, 29 U.S.C. 1232 (1976), directs the Secretary of Labor to study the pension rights of personnel employed under federal procurement, construction or research contracts and grants. President Carter has appointed a Presidential Retirement Policy Commission to study the implications of the growth of private and public pension systems. As part of its work it will analyze the impact of ERISA. *Study on the Growth of Pension Systems is Urged by Carter*, Wall St. J., Jan. 24, 1978, at 5, col. 2.

The House Small Business Committee is studying the impact of ERISA on Small Business and has held hearings in this regard. 160 PENS. REP. (BNA) A-3 (Nov. 24, 1977).

write new plans may have been prompted by *Daniel's* application of the antifraud provisions of the securities acts to expectancy interests in mandatory, non-contributory pension plans. However, it would be all but impossible to separate *Daniel's* effects from those of ERISA. ERISA was enacted in September 1974. Its various requirements have different effective dates, commencing in January 1975 and continuing thereafter. Some provisions are not yet in effect. At a time when many are studying ERISA and attempting to identify and evaluate its costs and benefits, it seems ill-advised to superimpose the amorphous liabilities associated with the antifraud provisions of the securities laws. One good argument for reversing *Daniel* is that doing so will permit ERISA alone to regulate plans. At least the possibility would then exist that tolerably accurate data could be collected and informed choices could be made as to whether ERISA alone or in combination with additional regulation is, or would be, beneficial.

The difficulty that applying the federal securities laws to pension funds has created in terms of assessing the effects of ERISA, however, may be among the lesser costs of the *Daniel* decision. The likely impact of that case in terms of the vesting and break in service provisions of existing plans will be much greater. Mr. Daniel, for example, failed to satisfy the stringent vesting and break in service rules of the Local 705 Plan. Congress was aware of the plight of Mr. Daniel and others like him when it debated pension reform.[135] It decided to remedy this perceived inequity not merely by requiring adequate disclosure of plan rules to employees but also by adopting a pervasive scheme of substantive rules relating to the vesting and break in service features of pension plans.[136] It considered a great deal of data on the costs and benefits produced by these new requirements and declined to apply them retroactively.[137] Congress undoubtedly realized that the increased costs imposed by retroactive application of the vesting and break in service standards would most likely result in the wholesale dismemberment of existing pension plans.[138] Instead it opted for gradual and prospective

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135. *See* note 75 *supra*.

136. For a discussion of the new vesting and break in service requirements, see notes 97-102 *supra* and accompanying text.

137. *See* notes 102 and 119 *supra*.

138. The Supreme Court has recently indicated its reluctance to impose large, unexpected retroactive liabilities on pension funds. In Los Angeles Dep't of Water & Power v. Manhart, 98 S. Ct. 1370 (1978), the Court held that a pension plan violated Title VII of the 1964 Civil Rights Act. The Court did not require refund of excess contributions by female employees. It stated:

> The assets held in trust for these employees are vast and growing—more than $400 billion were reserved for retirement benefits at the end of 1977 and reserves are increas-

changes in the rules governing pension plans.[139]

In spite of the explicit Congressional decision to avoid the high costs of retroactive application of ERISA's vesting and break in service rules, the *Daniel* court, using the antifraud provisions of the securities laws, has provided a means for the imposition of precisely those costs;[140] dissatisfied employees may now try to obtain increased benefits under the auspices of the antifraud provisions of the securities acts. While there are various estimates of the number of employees who, prior to ERISA, would never have received any benefits under their pension plans,[141] the district court and the court of appeals in *Daniel* both cited a Senate study indicating that only eight percent of the participants in pension plans with eleven-year or longer vesting requirements would ever receive any benefits under such plans.[142] *Daniel* will enfranchise the re-

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ing by almost $50 billion a year. These plans, like other forms of insurance depend on the accumulation of large sums to cover contingencies. The amounts set aside are determined by a painstaking assessment of the insurer's likely liability. Risks that the insurer foresees will be included in the calculation of liability, and the rates or contributions charged will reflect that calculation. The occurrence of major unforeseen contingencies, however, jeopardizes the insurer's solvency and, ultimately, the insureds' benefits. Drastic changes in the legal rules governing pension and insurance funds, like other unforeseen events, can have this effect. Consequently, the rules that apply to these fund should not be applied retroactively unless the legislature has plainly commanded that result.

> .... Retroactive liability could be devastating for a pension fund. The harm would fall in large part on innocent third parties. If, as the courts below apparently contemplated, the plaintiffs' contributions are recovered from the pension fund, the administrators of the fund will be forced to meet unchanged obligations with diminished assets. If the reserve proves inadequate, either the expectations of all retired employees will be disappointed or current employees will be forced to pay not only for their own future security but also for the unanticipated reduction in the contributions of past employees.

Id. at 1382-83 (footnotes omitted). The Court noted that Congress had been careful to provide gradual and prospective changes in the rules governing pension plans in ERISA, and declined to impose immediate and huge plan costs through the judiciary. *Id.* at 1382 n.40.

139. *Id.*

140. Moreover, Congress specifically delayed application of portions of ERISA to certain existing pension plans made pursuant to collective bargaining agreements. ERISA § 211(c)(2), 29 U.S.C. § 1061(c)(2) (1976). Application of the antifraud provisions of the securities law may nullify this delayed application.

141. These estimates ranged from 10% to 33⅓%. *See, e.g.*, 119 CONG. REC. 30003 (1973) (remarks of Sen. Williams) (33%), *reprinted in* II LEGISLATIVE HISTORY, *supra* note 70, at 1599; SENATE COMM. ON FINANCE, REPORT ON PRIVATE PENSION PLAN REFORM, S. REP. No. 93-383, 93d CONG., 1st SESS. (28%), *reprinted in* I LEGISLATIVE HISTORY, *supra* note 70, at 1089; 119 CONG. REC. 29839 (1973) (remarks of Sen. Jackson) (22%), *reprinted in* I LEGISLATIVE HISTORY, *supra* note 70, at 1267; SENATE COMM. ON FINANCE, REPORT ON PRIVATE PENSION PLAN REFORM, S. REP. No. 93-383, 93d CONG., 1st SESS. 151 (1973) (additional views of Sen. Hartke) (10%), *reprinted in* I LEGISLATIVE HISTORY, *supra* note 70, at 1218.

142. Daniel v. International Bhd. of Teamsters, 410 F. Supp. at 551, *aff'd*, 561 F.2d at 1229, *cert. granted*, 98 S. Ct. 1232 (1978).

maining ninety two percent who will seek their benefits under the securities laws.

Some attempts have been made to estimate the potential liabilities imposed upon pension funds as a result of the *Daniel* holding. The Department of Labor recently released an actuarial study on the estimated potential liabilities of private pension and profit sharing plans as a result of *Daniel*. The study estimated that potential liabilities could be as high as *39.6 billion dollars*, depending upon the applicable statute of limitations. The study projected that the greater costs imposed by *Daniel* will inevitably lead to more plan terminations, reduced benefits under existing plans, larger expenditures by the PBGC, and the writing of fewer new plans.[143]

In its amicus curiae brief before the court of appeals, the ERISA Regulations Industry Committee[144] urged reversal of the district court order. The Committee conservatively assumed that only one third of

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143. The study assumes that the applicable measure of damages is the value of accrued benefits and that all plaintiffs are successful in their suits. The study estimates the following potential liabilities:

ESTIMATED RANGE OF POTENTIAL LIABILITY FOR ACCRUED BENEFITS
(All figures in $ billions)

Estimated Range of Potential Liability by Class of Plan

Statute Limitations Starts to Run	Terminated Non-Vested Employees Entitled to Damages	Collectively Bargained Multiemployer Plans	All Collectively Bargained Plans	All Private Pension Plans		
				Contributory Plans	Non-Contributory Plans	All Plans
From date of terminations	All	$ 1.7—2.8	$ 3.5—5.8	$ 1.1-1.9	$ 7.0—11.6	$ 8.1—13.5
	5 or more years service	1.4—2.3	2.9—4.8	0.9—1.5	5.7—9.5	6.6—11.0
	10 or more years service	0.8—1.3	1.6—2.6	0.5—0.8	3.0—5.0	3.5—5.8
From age 65	All	4.9—8.1	10.1—16.9	3.3—5.5	20.5—34.1	23.8—39.6
	5 or more years service	4.0—6.6	8.3—13.9	2.7—4.5	16.7—27.8	19.4—32.3
	10 or more years service	2.2—3.6	4.7—7.8	1.4—2.4	8.7—14.5	10.1—16.9

[1978] 4 PENS. PLAN GUIDE (CCH) ¶ 25,228.

144. This committeee is an ad hoc group of representatives of 80 major United States corporations engaged in a wide cross-section of American business. These corporations maintain a total of over 900 separate employee retirement plans covering nearly 7 million employees. *See* Motion for Leave to Submit Brief as Amicus Curiae of the ERISA Regulations Industry Committee (ERIC) at 2-3, Daniel v. International Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977) (*cert. granted*, 98 S. Ct. 1232 (1978)) [hereinafter cited as ERISA Regulations Industry Committee Brief].

the participants in existing plans would receive any retirement benefits.[145] The Committee then calculated that ten million participants in union-negotiated plans would not receive any benefits. If those participants sued and prevailed in *Daniel* causes of action, the Committee calculated that employers would be exposed to a potential contingent liability for collectively bargained plans alone of *300 billion dollars*.[146]

The court of appeals made no serious attempt to deal with this calculation or with its potential effect on the termination and creation of pension plans in the future. Nor did the court appear to consider effects upon the distribution of income between shareholders and employee interests if multiple antifraud actions are brought by employees. Instead it characterized the ERISA Committee calculations as a "parade of horribles" and attributed the large numbers to the zeal of advocacy.[147]

While the ERISA Regulations Committee figures may be high,[148] the march of disappointed employees to the federal court house has already begun. Prior to the filing of the *Daniel* complaint on November 3, 1974, and even prior to Judge Kirkland's March 1, 1976 opinion and order denying dismissal of the securities law counts of the *Daniel* complaint, pension benefit cases traditionally did not include claims for relief under federal securities law.[149] Not surprisingly, the *Daniel* case

145. There are varying estimates as to the number of persons who will never receive any benefits under their pension plans. The court of appeals in *Daniel* referred to an actuarial probability as low as 8% that an employee would receive any benefits under his pension plan. 561 F.2d at 1227, *cert. granted*, 98 S. Ct. 1232 (1978). Other estimates range from 10% to 33⅓%. *See* note 141 *supra*. The ERISA Committee's use of the figure of 33⅓% was thus conservative.

146. The average annual retirement benefit paid in 1973, when Mr. Daniel retired was $2,000. The Committeee thus assumed for purposes of its calculations a $2,000 annual retirement benefit and an average retirement life of 10 years. The Committee, however, did not concede that the appropriate measure of damages would be the promised pension benefits. ERISA Regulations Industry Committee Brief, *supra* note 144, at 2-3.

147. 561 F.2d at 1250, *cert. granted*, 98 S. Ct. 1232 (1978). The court of appeals further noted that plan liability would be limited by a number of factors such as the statute of limitations and the need for plaintiffs to prove justifiable reliance. *Id.*

Since the conduct proscribed by the court in *Daniel* appears to have been the omission of material facts (the statistically determinable risk that an employee would never receive any benefits), it is logical that courts following *Daniel* will adhere to the traditional securities law approach of presuming reliance. For the enunciation of the rule that reliance may be presumed in cases of material omission, see Affiliated Ute Citizens v. United States, 406 U.S. 128 (1972).

148. These calculations erroneously assume that the appropriate measure of damages is "lost profits." This is not the case; the damages should be limited to out-of-pocket costs. For a discussion of the appropriate measure of damages, see note 44 *supra*. For information on the ERISA Regulations Industry Committee, see note 144 *supra*.

149. This has caused one federal judge to comment that although the securities acts have

has received much attention. The availability of a securities cause of action has apparently captured the eye and pen of many small practitioners representing employees, or former employees, whose pension or employee benefit plan expectations have never materialized. In the district courts, at least twenty such cases have been filed.[150] Almost all the cases involve benefits under mandatory, non-contributory, multiemployer pension plans. Five of the cases were plead as class actions. A majority of the cases include the pension trusts as a defendant. While the claims for relief are often plead in the alternative and framed in generalities, most seek judgment in an amount equal to the benefits allegedly wrongfully denied.[151]

The costs of these actions will be increased because of several problems associated with implied private damage actions under the antifraud sections. First, the cause of action is an implied one and therefore lacks many of the restrictions contained in express rights of action.[152] Second, the modern commercial activities to which the antifraud sections apply are vastly different from the typical transaction covered by the common law tort of fraud and deceit in which privity requirements, forseeability and face-to-face dealing placed practical limits on recovery.[153] The development of modern telecommunication technology has created a large and impersonal commercial environment where the lack of face-to-face dealing, coupled with the lack of a privity requirement,[154] make possible "Draconian" damages and damage recovery.[155] This concern is particularly applicable to large pension plans, where there may be no direct dealings between the employee and the plan trustees, the union or the employer. Third, securities antifraud litigation is often particularly difficult to dispose of prior to trial.[156] All of these problems give an antifraud suit additional settlement value, unrelated to its merits. The threat of extensive

been around since 1933, "nobody has had the temerity to argue that this was a security until *Daniel* was decided." Weins v. International Bhd. of Teamsters, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,005 (C.D. Cal. 1977).

150. *See* Appendix A.

151. For a discussion of the appropriate measure of damages, see note 44 *supra.*

152. *See* notes 20-25 *supra* and accompanying text.

153. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 744-45 (1975).

154. *Id.* at 744-47.

155. The potential for large damage judgments in private damage actions under the antifraud provisions has concerned several courts. *See, e.g.*, SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 867 (1968), *cert. denied*, 394 U.S. 976 (1969) (Friendly, J. concurring). *See also* Fridrich v. Bradford, 542 F.2d 307, 321 (4th Cir. 1976), *cert. denied*, 429 U.S. 1053 (1977); Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 495 F.2d 228 (2d Cir. 1974).

156. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 739-42 (1975).

discovery of business records and unwarranted disruption of business activities contribute to its settlement potential.[157]

These very concerns caused the Supreme Court to check the growth of implied private damage actions under section 10(b) and rule 10b-5. In *Blue Chip Stamps v. Manor Drug Stores*,[158] the Court commented extensively on the potential abuses associated with such litigation and affirmed the twenty-year-old "*Birnbaum* rule"[159] limiting standing in implied private damage actions under section 10(b) and rule 10b-5 to actual purchasers and sellers of securities. In so doing, the Court articulated its unwillingness to risk substantial damage recovery by persons lacking objective evidence of their reliance upon the defendant's deceit. If non-purchasers and non-sellers were permitted to recover damages under the antifraud provision of the 1934 Exchange Act, the elements of their causes of action would be totally within their own subjective states of mind, unknown and unknowable by the defendant.[160]

An examination of the *Daniel* record reveals many of the characteristics of the litigation which so concerned the Supreme Court in *Blue Chip*. Subsequent to the filing of his complaint, Mr. Daniel filed an affidavit which the court of appeals treated as part of the pleadings for purposes of review. Plaintiff swore that he believed that he would receive a pension after twenty years of employment with Local 705-covered employers and that in no event would employer contributions be forfeited. Mr. Daniel further stated in his affidavit that his belief con-

157. *Id.* at 739-41.

158. 421 U.S. 723 (1975).

159. Birnbaum v. Newport Steel Corp., 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S. 956 (1952).

160. In Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 746 (1975) the Court carefully analyzed this problem:

> But in the absence of the *Birnbaum* rule, it would be sufficient for a plaintiff to prove that he had failed to purchase or sell stock by reason of a defendant's violation of Rule 10b-5. The manner in which the defendant's violation caused the plaintiff to fail to act could be as a result of the reading of a prospectus, as respondent claims here, but it could just as easily come as a result of a claimed reading of information contained in the financial pages of a local newspaper. Plaintiff's proof would not be that he purchased or sold stock, a fact which would be capable of documentary verification in most situations, but instead that he decided *not* to purchase or sell stock. Plaintiff's entire testimony could be dependent upon uncorroborated oral evidence of many of the crucial elements of his claim, and still be sufficient to go to the jury. The jury would not even have the benefit of weighing the plaintiff's version against the defendant's version, since the elements to which the plaintiff would testify would be in many cases totally unknown and unknowable to the defendant. The very real risk in permitting those in respondent's position to sue under Rule 10b-5 is that the door will be open to recovery of substantial damages on the part of one who offers only his own testimony to prove that he ever consulted aprospectus of the issuer, that he paid any attention to it, or that the representations contained in it damaged him.

Id. at 745-46 (footnotes omitted).

tinued after receipt of many communications about the plan from his union and the plan trustees. Finally, Mr. Daniel claimed that he would have changed jobs had he known how the vesting requirements would be applied.[161]

The *Daniel* case presents examples of the very type of subjective allegations which prevent settlement before trial. This would be so even if the plan brochures and communications had clearly stated that twenty years of uninterrupted, continuous employment was required for benefit eligibility.[162]

Application of the antifraud provisions to employee expectancy interests in mandatory, non-contributory pension plans is a branch of the General Sherman Tree which the Court sought to prune in *Blue Chip*.[163] Based upon the holding in *Daniel*, any employee whose pension benefits did not vest or whose benefits were less than expected, and perhaps even those employees who were not eligible for participation at all, can, on the basis of oral testimony and affidavits, plead a cause of action under the antifraud sections. Since the pension plan is mandatory and non-contributory, there will be no objective evidence of

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161. The Affidavit stated:

> 6. In 1955, I was notified by a letter . . . that Local 705 had established a pension fund for its members who worked for employers who had entered into labor contracts with Local 705. At that time, and at all times thereafter, I understood and believed that a Local 705 member would be eligible to receive a retirement benefit upon completing 20 years of employment with Local 705 covered employers. . . .
>
> 7. Because of my limited educational background and my concern for financial security in my old age, the pension plan . . . was a material factor in my continuing in employment with Local 705 covered employers. Had I known of the way in which . . . [the] trustees would interpret the eligibility requirements for a retirement benefit, I would have sought employment . . . elsewhere—with retirement benefits of the type I understood Local 705 to be offering.
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> 8. . . . I received various communications, both through the mails and otherwise, . . . pertaining to and describing the Local 705 pension plan . . . . After receiving all such communications it remained my understanding and belief that I would receive a pension were I to complete 20 years of employment with Local 705 covered employers.

Brief for Respondent in Opposition to the Petitions for Writs of Certiorari, Appendix at 2-4, Daniel v. International Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978).

162. This was precisely the situation presented in Schlansky v. United Merchants & Mfrs., Inc., 443 F. Supp. 1054 (S.D.N.Y. 1978). In that case an employee received no credit for his prior employment with the defendant employer's predecessor in interest and thus failed to qualify for pension benefits. The court, in dismissing the plaintiff's contract cause of action without leave to amend, found that the expressed terms of the written contract (the pension plan) precluded crediting of the former employment. However, the court, following *Daniel* stated that relief could be afforded through an implied cause of action under the 1934 Exchange Act.

163. "When we deal with private actions under Rule 10b-5, we deal with a judicial oak which has grown from little more than a legislative acorn." Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 737 (1975).

any employee's understanding. Compared to the costs involved in this situation, the costs of ERISA seem small indeed.

B. The Benefits of Daniel

In order to produce any economic benefit[164] to society at all in the context of ERISA regulation, the securities laws must reduce the cost of producing information, produce better information at comparable cost, or beneficially alter the timing and delivery of that information.

First, consider the possibility that the securities laws may reduce the cost of providing information. Absent ERISA, a powerful argument could be made that the most efficient way to preserve the private pension system and at the same time promote employee retirement income security would be to subject employee interests in pension plans to the federal securities laws. After existing pension plan exemptions from securities law registration and reporting provisions were removed,[165] adequate disclosures of plan provisions to employees would presumably be "insured" by the securities laws, and market forces would determine the appropriate vesting, funding and break in service plan provisions. Society might have been better off if it had used the securities laws to regulate pension plans, rather than expending resources on lengthy pension reform studies and deliberations and on the administration of and compliance with ERISA's many requirements.

But Congress did not choose to regulate the pension system through the securities acts. Instead it opted for the pervasive regulatory scheme of ERISA, under which the Internal Revenue Service, the Secretary of Labor and the Pension Benefit Guaranty Corporation share administrative responsibility.[166] The problems of coordination and conflict inherent in such an arrangement have already caused several legislators

164. An "economic benefit" is only produced when the aggregate wealth of society is increased. The fact that Mr. Daniel and others may receive judgments in lieu of unmet pension expectations does not produce any economic benefit. Since the costs of these judgments will be paid by employers, other employees, or shareholders, a mere redistribution of wealth will occur.

165. The position of the SEC that interests in pension plans are thus exempted is discussed in note 35 *supra*.

166. Apparently the shared jurisdiction came about because the two Senate committees with jurisdiction over ERISA wanted to entrust its administration to different agencies. The Senate Finance Committee wanted to give jurisdiction to the IRS and the Senate Labor Committee (now the Senate Human Resources Committee) wanted the Department of Labor to administer ERISA. The dual jurisdiction is a result of a compromise between the two views. Scheibla, *Revamping ERISA*, Barron's, May 1, 1978, at 4, 5, col. 2.

For a discussion of these complex jurisdictional relationships, see Lee, *The "Elaborate Interweaving of Jurisdiction" Labor and Administration and Enforcement of ERISA and Beyond*, 10 U. RICH. L. REV. 463 (1976).

to propose the formation of a new federal agency with exclusive jurisdiction over pension plans.[167] Existing difficulties will be further compounded by SEC involvement which will, almost certainly, increase the already high administrative costs of ERISA. In the context of ERISA, and the existing exemption of pension plans from the reporting and registration provisions of the securities acts, it does not appear to be efficient to classify employee expectancy interests in pension plans as securities and thereby to add the SEC and the federal securities laws to the already long list of federal agencies and laws which govern private pension plans.

Consider next the possibilities that application of the securities laws under *Daniel* will produce better information at comparable cost or will beneficially alter the timing and delivery of that information. Some have heralded the application of the securities laws because their application has been thought to increase the protection of employees and their pension expectations by requiring disclosure of information earlier than does ERISA.[168] It appears, however, that the court of appeals in *Daniel* was incorrect in its assumption that application of the antifraud provisions would produce that result, since, according to the SEC, substantially all pension plans are exempted from the registration and reporting provisions of the securities acts.[169] The antifraud sections merely prohibit misleading or deceptive statements; they do not require detailed affirmative disclosure of any specific information.[170]

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167. According to a recent feature article in Barron's, the Department of Labor and the IRS cannot agree on how to proceed under ERISA and employers often receive conflicting answers from the two agencies. Scheibla, *Revamping ERISA*, Barron's, May 1, 1978, at 4, 5, col. 3. According to the same article, a bill has recently been approved by the Senate Finance Committee which attempts to define and separate the jurisdiction of the two agencies, thereby minimizing overlap. Some legislators oppose this approach and favor the creation of a new agency with exclusive jurisdiction over ERISA. *Id.*

Senators Williams and Javits have introduced a bill in the Senate which would overhaul many portions of ERISA. S. 3017, 95th Cong., 2d Sess., 124 CONG. REC. 6581 (1978). This bill calls for the creation of a new federal agency, the Employee Benefits Commission, which would have exclusive responsibility for enforcing ERISA. *Authors of Private Pension Fund Law Seek Rules To Solve Problems It Created*, Wall St. J., May 2, 1978, at 5, col. 1. For further discussion of this proposed legislation, see note 183 *infra*.

168. Defendants have not shown that ERISA would provide relief to persons who have acquired an interest in a pension fund where false or misleading representations have been made at inception or during subsequent ratifications, or upon a job offer. Affirmance of the judgment below will supplement ERISA by providing a self-executing compulsion to disclose adequate information at such times, including a statistically determinable risk that many employees covered by a plan will never receive their pension benefits.

Daniel v. International Bhd. of Teamsters, 561 F.2d 1223, 1248-49 (7th Cir. 1977) (footnotes omitted), *cert. granted*, 98 S. Ct. 1232 (1978).

169. *See* note 35 *supra*.

170. The SEC agrees with this position. *See* note 174 *infra*.

Moreover, it is not likely that any information produced as a result of *Daniel* will be "better" information.[171] This seems so because the principal way of determining what facts are material, and must thus be disclosed to preclude securities antifraud liability is through judicial or administrative hindsight. The application of such hindsight is demonstrated by the court of appeals' statement the antifraud provisions require disclosure of a "statistically determinable risk that many employees covered by a plan will never receive their pension benefits."[172] This problem prompted Senators Williams and Javits to ask the chairman of the Commission for written guidelines detailing the categories of pension plan information required to be disclosed under the anti fraud sections.[173] The Commission did not provide the requested guidelines on the grounds that the antifraud provisions do not contain any requirement of detailed affirmative disclosure.[174]

Since there are not, and apparently cannot be, any guidelines indicating in advance what type of information must be furnished to employees or when it must be furnished, it is virtually certain that the antifraud provisions will not produce "better" information at comparable costs. Nor can the antifraud sections beneficially alter the timing and delivery of information. The uncertainty over what type of information must be disclosed and when it must be disclosed will most probably increase the already significant costs imposed by the *Daniel* decision.

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171. It is doubtful that application of the antifraud provisions will result in increased pension plan disclosures. It is more likely that the *Daniel* holding will result in less, rather than more, disclosure since wary and well-advised employers, unions, and plan trustees may make no statements or representations whatsoever about the pension plan prior to the time that written disclosures are mandated by ERISA. For a discussion of these written disclosures, see notes 110-17 *supra* and accompanying text.

172. Daniel v. International Bhd. of Teamsters, 561 F.2d 1223, 1249 (7th Cir. 1977), *cert. granted*, 98 S. Ct. 1232 (1978).

173. Letter from Senators Williams and Javits to SEC Chairman Williams (Nov. 21, 1977), *reprinted in* 4 J. PENS. PLAN & COMPLIANCE 8 (1978).

174. [T]he antifraud provisions do not constitute a general requirement of detailed affirmative disclosure, either oral or written. Nor do they require that documents be filed with and processed by the Commission.

. . . [T]here is, and can be, no definite list of items which must be disclosed under the antifraud provisions.

. . . [T]he antifraud provisions rely on the concept of materiality, and the courts have consistently stressed that materiality must be judged on a case-by-case basis. . . . There is no "specific rule" as to what facts are material: that determination must be made "on a case-by-case basis according to the fact pattern of each transaction."

Memorandum from the SEC Office of General Counsel to SEC Chairman Williams (Dec. 7, 1977), *reprinted in* 4 J. PENS. PLAN & COMPLIANCE 11, 14 (1978) (sent to Senators Williams and Javits by SEC Chairman Williams in response to their November 21, 1977 letter).

Even if the existing exemption of pension plans from the registration and reporting requirements were removed, it is doubtful that the detailed information on plan assets and investments thereby produced would be of significant value to employees. Given ERISA's early vesting requirements and the fact that receipt of vested pension benefits is now, or shortly will be, insured by the federal government through the Pension Benefit Guaranty Corporation,[175] the risk traditionally associated with an investment in a security has largely been removed.[176]

Information concerning the participation, vesting and break in service provisions of the pension plan is now provided under ERISA.[177] It is highly questionable whether the earlier delivery of this information is important. Any false information disseminated to employees at job offer, plan inception or at ratification of a collective bargaining agreement covering a pension plan[178] will be corrected in a relatively short time by the easily understood and accurate plan description furnished to employees under ERISA shortly after they become plan participants.[179] Thus, the value of having accurate information somewhat earlier may be comparatively inconsequential in view of the high costs associated with application of the securities laws.

Application of the securities laws to pension plans will not reduce the cost of producing information. Instead, it will probably increase the cost. It will not produce better information at comparable cost. Nor will it beneficially alter the timing or delivery of information. In light of these realities, it is extremely unlikely that *Daniel* will produce any economic benefit to society.

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175. For a discussion of plan termination insurance, see notes 94-96 *supra* and accompanying text.

176. Employees whose benefits have not fully vested are at risk but their risk has little to do with plan assets and investments. Information on plan assets and investments which would be produced under the registration and reporting provisions would be of little value to those employees. Their real risk is that the pension plan or their employer's operations will be discontinued. Thus, the information truly relevant to them concerns participating employers' operations and not plan assets and investments.

Furthermore some employers may already be furnishing this information in another context. Those employers who have chosen to enter the nation's capital market, the real focus of the federal securities law, are already producing and publicizing this type of information under the securities law. Other employers who have not entered the public capital market are not publicizing this information. Compulsory public disclosure of this type of financial information merely because an employer maintains a pension plan is unwarranted. There are obvious political and financial ramifications involved in such a decision and the judiciary is ill-equipped to assess them.

177. For a discussion of the new disclosure requirements, see notes 110-17 *supra* and accompanying text.

178. *See* note 168 *supra*.

179. *See* note 113 *supra* and accompanying text.

V. CONCLUSION

This author cannot understand why additional regulation of pension plans through the securities law is necessary or appropriate. There is no need to contort the definition of an investment contract to gerrymander expectancy interests in mandatory, non-contributory defined benefit plans into the securities acts. There is no evidence that to do so would encourage informed investor decision making, one of the primary purposes behind the securities acts. The traditional benefit associated with labeling something as a security is the increased affirmative disclosure of detailed information required by the registration and reporting provisions of the securities acts. This will not occur here because substantially all pension plans are exempted from these requirements.

Moreover, the detailed information generated by the registration and reporting requirements would be costly to produce and would be of little interest to employees. Their primary concern is with the vesting and eligibility provisions of their pension plans. Information of this type is already provided to them under ERISA. It is not cost-effective to use the securities law to provide it at a somewhat earlier time. Any additional information concerning the investment policies of the pension trust or the value of its assets is of no value to employees. The early vesting and ultimate receipt of vested benefits is guaranteed by ERISA.

Some persons would justify application of the securities laws to pension plans by arguing that the antifraud provisions of those laws operate as a federal fraud statute which would rectify and deter fraud.[180] P.T. Barnum and many before and after him have used a variety of selling techniques to part buyers from their money. Fraud existed long before Congress, the federal securities laws or even the SEC, and there is considerable evidence to suggest its continuing existence despite their exemplary efforts to bring it to an end. Absent evidence that the securities law or the SEC is more efficient at preventing pension fraud than are the available alternatives—which include ERISA, the Internal Revenue Service, the Department of Labor, the Pension Benefit Guaranty

180. SEC Chairman Williams recently appeared before the Senate Human Resources Committee in connection with S. 3017, 95th Cong., 2d Sess., 124 CONG. REC. 6581 (1978) which, among other things, would preclude application of the antifraud provisions of the securities acts to employee interests in pension plans. Chairman Williams argued that the antifraud provisions of the federal securities acts should apply to pension plans since they would prevent and rectify fraud. *SEC Chief is Wary of Proposal to Exempt Pension Funds from Antifraud Lawsuits*, Wall St. J., Aug. 16, 1978, at 6, col. 2.

Corporation, and state law remedies—there is no reason not to leave the matter in those already numerous hands. The availability of some of these remedies is demonstrated by the fact that Mr. Daniel and those emulating him have plead several other legal theories in their complaints.[181]

The federal courts have had great difficulty in resisting repeated entreaties to expand the scope of the federal securities laws. This is probably due in part to the attractiveness and apparent reasonableness of requests for more information about whatever may be involved, and the usually unarticulated assumption that such information is essentially costless to produce. It is generally assumed by courts that the social benefits of extending the federal securities laws will exceed the social costs.

It has been argued that this is a dubious proposition even as to the registration provisions of the 1933 Securities Act.[182] Regardless of the validity of that argument, it seems clear that application of the antifraud provisions to pension plans is not an efficient way to increase the future flow of relevant information, even assuming that such an increase is desirable. It would be far better for Congress simply to specify what disclosures are required,[183] thereby preventing the court

181. Since the time of the district court's decision in *Daniel*, at least 20 pension cases have been filed in the district courts seeking relief under the federal securities law in addition to other relief requested. Ten include claims for relief under ERISA and 20 include claims for relief based on other laws such as fraud, breach of fiduciary duty, and breach of contract. For more information on these cases, see Appendix A.

182. *See, e.g.*, Stigler, *Public Regulation of the Securities Markets*, 19 BUS. LAW. 721 (1964).

183. The question is now before the Supreme Court and Congress. On May 1, 1978, Senators Williams and Javits introduced the proposed ERISA Improvements Act of 1978, S. 3017, 95th Cong., 2d Sess., 124 CONG. REC. 6851 (1978). In its present form, the bill will preclude application of the securities laws to interests in private employee benefit plans such as mandatory, non-contributory defined benefit plans. Section 274(2) of S. 3017 states that interests in such plans "shall not be characterized as or deemed to be, a security within the meaning of the Securities Act of 1933, the Securities Exchange Act of 1934, or any law of any State which regulates securities. . . ." Section 274 exempts from the securities laws all plans covered by ERISA except individual account plans in which participation is voluntary.

The issue has also recently been considered by the Federal Securities Code Project of the American Law Institute. This project is an attempt to integrate into one statute the various laws under which the SEC currently has administrative responsibility. It is hoped that the new code will eliminate the duplications and complexities which have arisen under the 7 statutes over which the SEC now has jurisdiction. Cheek, *Exemptions Under the Proposed Federal Securities Code*, 30 VAND. L. REV. 355, 355 (1977).

A consensus of the advisory group which assisted the Reporter, Professor Louis Loss, in drafting the Code, and a substantial majority at the October 1977 meeting of an American Bar Association committee felt that it was not efficient to have the SEC as well as the IRS congestion which will be a natural result of the subjective standards of proof permitted by the *Daniel* court. When such congressional action is possible, it seems inappropriate to burden the judicial branch with the task of resolving the issue of who said what to whom about a pension plan, most likely at least a decade ago. A poorer use of resources, even in a society that has a wholesome regard for litigation, can hardly be imagined.

It is difficult to believe that a court would have reached the result reached in *Daniel* if it had reflected upon the implications of its decision in the context of some clearly-stated desirable and achievable social ends, and had it then considered the most cost-effective means of achieving those ends. If the end was to increase the future flow of information, the means chosen were not cost-effective. Furthermore, the end of giving Mr. Daniel and others like him the pension that they want is simply not achievable.

The *Daniel* court's expansion of the securities law to regulate employee interests in pension plans appears to be counterproductive. While this does not necessarily imply that judicial expansion in other contexts will not be cost-efficient, it does raise the question of whether courts are equipped to perform what many would describe as legislative functions. It may be observed, for example, that courts are often inclined to respond to a litigant's superficially sympathetic entreaties by expanding the laws without regard to the costs or benefits produced

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and Department of Labor in the business of protecting employees. It was felt that if ERISA did not adequately cover a particular type of pension plan, Congress should be urged to amend ERISA. The advisory group concluded that the SEC should not be in the business of regulating pension plans. ALI FEDERAL SECURITIES CODE § 302(f)(2) Note (3) (Mar. 1978 Draft).

Suggestions were made that the Proposed Official Draft be amended to except interests in non-contributory, mandatory pension plans from the definition of a security in order to correct the unsettled state of the law created by the *Daniel* decision. Cheek, *Exemptions Under the Proposed Federal Securities Code*, 30 VAND. L. REV. 355, 387-88 n.96 (1977).

At its annual meeting on May 19, 1978, the ALI approved the Proposed Official Draft, as amended, to reflect certain comments made at or before the meeting and authorized the Reporter to make further changes of an editorial or technical nature. The ALI declined to take any position on the issue of employee interests in non-contributory mandatory pension plans. Instead, it authorized the drafting of alternative sections, including one which would except such interests from the definition of a security (ALI FED. SECURITIES CODE, SUPPLEMENT TO PROPOSED OFFICIAL DRAFT 4-5 (July 1978) (§ 299.53(b)(10) (undrafted)), and another which would include such interests within the definition of a security with regard to exemptions from registration and reporting requirements. *Id.* (§ 302(f)(2)).

The Institute declined to take a position "[b]ecause of (1) the pendency of the *Daniel* case, (2) the introduction on May 1, 1978, of S. 3017, 95th Cong., [2d Sess., 124 CONG. REC. (1978)] the proposed ERISA Improvements Act of 1978, and (3) the political overtones of the question . . . ." *Id.* at 5.

by such expansion. If courts are to continue to perform functions which are primarily the province of legislatures, it would be desirable for them to confine their expansions of the law to situations in which the benefits of those expansions clearly outweigh the costs.

The *Daniel* court would have done much better if it had performed a rough but clear-headed cost-benefit analysis. This same approach, applied in other cases and in other areas of the law, could help other courts to avoid reaching inefficient results. It would also help to distinguish those cases in which it makes economic sense to apply the federal securities law from those in which it does not.

Appendix A

Cases Filed Seeking Relief Under the Securities Law on Pension or Other Benefit Plan Claims Since Daniel v. International Brotherhood of Teamsters†

Case name Case number Date filed	Type of Plan (if known)	Were ERISA Counts Pled?	Were Other Counts Pled?	Was the Claim Filed as a Plaintiff Class Action?	Was the Pension Trust Fund Named as Defendant?	Was the Case Decided on the Securities Counts?*
Blassie v. Amalgamated Meat Cutters & Butchers Workman of North America Retirement Plan Trust Fund, No. 76-C-681 (N.D. Ill. 1976)	Multi	Yes	Yes	No	Yes	Stayed**
Assay v. Hallmark Cards, Inc., No. C 76-1 (N.D. Iowa 1976)	Single	No	Yes	Yes	Yes	Yes
Stoilzing v. Robbins, No. 770464-CV-W-4 (W.D. Mo. June 19, 1977)	Mandatory Noncontributory Multi	Yes	Yes	No	Yes	No
Skytt v. Waggoner, No. 77-1550 (C.D. Cal. 1977)	Mandatory Contributory Multi	Yes	Yes	No	No	No
Cinnamon v. Brooks, No. 77-204 (C.D. Cal. March 22, 1977)	Multi	Yes	Yes	No	No	Yes
Ross v. International Bhd. of Teamsters, No. 77-1650 (N.D. Cal. July 29, 1977)	Mandatory Noncontributory Multi	No	Yes	No	Yes	No
Pliner v. Central States, Southeast & Southwest Areas Pension Fund, No. C 77-55 (N.D. Ohio 1977)	Mandatory Noncontributory Multi	No	Yes	No	Yes	No
Patton v. Central States, Southeast & Southwest Areas Pension Fund, No. C76-1354 (N.D. Ohio 1976)	Mandatory Noncontributory Multi	No	Yes	No	Yes	No
Papuga v. International Bhd. of Teamsters, No. 77C 2327 (N.D. Ill. June 29, 1977)	Mandatory Noncontributory Multi	No	Yes	No	No	No
O'Neill v. Marriott, No. M-77-495 (D. Md. 1977)	Contributory Voluntary Single	Yes	Yes	Yes	No	No
McCart v. Hartzer, No. 76-292-1 (S.D. Iowa Sept. 20, 1976)	Mandatory Noncontributory Multi	Yes	Yes	No	Yes	No
Dutchak v. International Bhd. of Teamsters, No. 76-C-3803 (N.D. Ill. 1976)	Mandatory Noncontributory Multi	No	Yes	Yes	Yes	No
Crabtree v. International Bhd. of Teamsters, No. 76-610 Ky. (E.D. Ky. 1976)	Mandatory Noncontributory Multi	No	Yes	No	Yes	No
Coffey v. McCarthy, No. 77-1863-C (D. Mass. 1977)	Mandatory Noncontributory Multi	No	Yes	No	Yes	No
Weins v. International Bhd. of Teamsters, No. 76-2517-IH (C.D. Cal. Aug. 6, 1976)	Mandatory Noncontributory Multi	Yes	Yes	No	Yes	Yes
Schlansky v. United Merchants & Mfrs., Inc., No. 76 C 5799 (S.D.N.Y. 1976)	Single	Yes	Yes	Yes	No	Yes
Robinson v. UMW Health & Retirement Funds, No. 770698 (D.D.C. 1977)	Multi	No	Yes	Yes	Yes	Yes
Hurn v. Reitrement Fund Trust of the Plumbing, Heating & Piping Indus. of S. Cal., No. 76-2487-AAH (C.D. Cal. 1976)	Multi	Yes	Yes	No	Yes	Yes
Kerch v. General Chauffeurs, Helpers & Sales Drivers Union Local No. 325, No. 78020096 (W.D. Ill. Jan. 12, 1978)	Mandatory Noncontributory Multi	Yes	Yes	No	Yes	No
Dudo v. Schaffer, No. 78-467 (E.D. Pa. 1978)	Mandatory Noncontributory Multi	No	Yes	No	Yes	No

† With the exception of Robinson v. UMW Health & Retirement Funds, No. 770698 (D.D.C. 1977), all of the cases summarized involve claims for benefits under pension plans. *Robinson* involved an employee benefit plan providing permanent health care benefits.
* For a discussion of the cases decided on the securities counts, see note 34 *supra*.
** Pending the *Daniel* decision.