MISCLASSIFICATION AND EMPLOYER DISCRETION UNDER ERISA

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In October 1998, the United States Department of Labor filed suit against Time Warner Inc., a company that employs approximately 40,000 people, charging that the corporation illegally misclassified several hundred freelance writers, reporters, and photographers as independent contractors in order to avoid granting them employee benefits.¹ This is the first time that the Department of Labor has brought suit claiming that workers were improperly denied benefits.

Also in October 1998, the United States Court of Appeals for the Ninth Circuit held in Burrey v. Pacific Gas & Electric Co.² that a group of clerical workers supplied by a temporary employment agency could sue the company utilizing their services for benefits if they met the common-law definition of employee.³ The court refused to allow the company discretion to determine whether its benefit plans covered workers "leased" from an outside agency.⁴

As a result of these and other recent cases,⁵ it is unclear whether employers may exclude certain classes of workers from employee benefits programs. The Ninth Circuit in Vizcaino v. Microsoft found that the software giant had misclassified employees as independent contractors in order to deny them benefits.⁶ Other circuits have come to the opposite conclusion in cases involving Exxon⁷ and Dupont.⁸ Employers aware of

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³ See id. at 394.
⁴ See id. at 391.
⁵ See infra Parts I.B-C.
⁷ See Abraham v. Exxon Corp., 85 F.3d 1126 (5th Cir. 1996); infra text accompanying notes 127-41.
⁸ See Clark v. E.I. Dupont De Nemours & Co., 105 F.3d 646 (4th Cir. 1997); infra
these results are uncertain when they may depart from traditional employment arrangements and when the law requires them to include workers in their employee benefit programs. Historically, the role of the courts and of the Department of Labor has been limited to ensuring that employment arrangements are free of fraud and deceptive practice. When determining what employment arrangements best meet their needs, employers should be able to make informed decisions about the use of independent contractors, leased workers, and temporary employees. Companies should be able to provide benefits to employees without fear that the federal government will later compel them to extend identical benefits to entire classes of workers against their will and contrary to their original intentions.

The Department of Labor's recent attempt to use the courts to compel Time Warner to extend benefits to classes of workers that the company did not intend to be covered by benefits is misguided and should have been rejected by the district court. Courts have traditionally left the arrangement between freelance workers and the organizations that contract for their labor to the parties involved and deferred to employers' decisions regarding which workers will be covered by employee benefit plans. In the past, a suit claiming improper denial of benefits, such as the Time Warner case, could only have been brought by the aggrieved individuals. By bringing suit in the Secretary's name, the Department of Labor seeks to substantially expand its authority so that it may bring suit on behalf of classes of workers without identifying individual plaintiffs and without deferring to employers.

The Employee Retirement Income Security Act of 1974 ("ERISA") was enacted to combat fraud and deceptive practice by employers providing pension plans and other employee benefit plans. Related tax incentives promote the social goals of expanding the availability of private benefits programs. If the Department of Labor is allowed to use ERISA to force employers to go beyond what the market, aided by tax incentives, commands, more employers will be tempted to opt out of the voluntary system altogether, or at least to reduce benefits to the vanishing point.

9. See Herman v. Time Warner Inc., 56 F. Supp.2d 411 (S.D.N.Y. 1999). On September 3, 1999, the district court denied Time Warner's motion to dismiss, holding that the Department of Labor had stated a claim that Time Warner had breached its fiduciary duty by misclassifying and denying benefits to temporary employees and independent contractors. The court also held that the Department of Labor's suit was "appropriate." See id. at 417-18; infra Part IV.

10. See infra Part III.A.


12. See infra notes 13-15 and accompanying text.
In the United States, all employer-sponsored employee benefit programs are voluntary. Federal law does not require employers to provide health or retirement benefits to any workers. In the absence of unconstitutional discrimination, federal law does not prohibit employers from providing benefits to one group of workers and not to another. Once an employer does decide to provide benefits, its promises to employees come within the enforcement scope of ERISA. The tax code provides incentives for those employers whose plans do not discriminate in favor of highly-compensated employees. For employer contributions to be tax deductible, pension and benefit plans must meet the "nondiscrimination" requirements of the Internal Revenue Code. These rules do not require that benefits be extended to all workers.

Congress intended ERISA to prevent fraud and deceptive promises in the provision of benefits to covered employees. It was intended that the Act would to facilitate the voluntary growth of private pension and employee benefit programs. It was never intended to mandate coverage for all classes of workers. Using ERISA to force employers to extend benefits to unintended classes of workers runs contrary to the purpose of the statute and to the tradition of voluntary growth in employee benefit programs. Any attempt by the government to make the extension of benefits compulsory, either through legislation or through the courts, is unlikely to result in an increase in the total amount of benefits provided. Given the high costs of benefits, employers will be forced to compensate for mandated increases in one area by reducing benefits in others, or by eliminating benefits programs altogether.

The first part of this Comment will briefly review the legislative history of ERISA and the statutory purposes behind it. It will demonstrate

14. See id. ¶ 401(a) ("A trust ... shall constitute a qualified trust ... (4) if the contributions or benefits provided do not discriminate in favor of highly compensated employees ... .") This six-line subsection is supplemented by over 350 pages of Treasury Regulations.
15. See Treas. Reg. ¶ 1.410(b)-4(b) (1999) (stating that classifications for determining eligibility for benefits must be "reasonable" and "established under objective business criteria").
16. See ERISA ¶ 2(a) (stating that the policy of ERISA is to require disclosure and provide safeguards "with respect to the establishment, operation, and administration" of employee benefit plans).
19. See id. at 728.
that Congress, in enacting ERISA, did not intend to create a broad social program. The second part of this Comment will consider employers' responses to changing employment demands in the context of ERISA, and the rise of contingent work arrangements, particularly the use of leased or temporary employees. The third part of this Comment will consider a number of recent federal court cases addressing the problems with contingent work arrangements. It will show that the courts have consistently interpreted ERISA as affording employers broad discretion in creating and maintaining plans for the benefit of their employees. This deferential approach is consistent with the intent of Congress in enacting ERISA, and with the public policy of promoting the growth of employee benefits programs through voluntary employer participation.

Finally, this Comment will consider the implications of the Department of Labor's suit, sustained by the district court in *Herman v. Time Warner Inc.* That suit is a clear departure from the intent of Congress in enacting ERISA and from Supreme Court precedent in keeping with that intent. It runs counter to twenty-five years of development of employee benefit programs under ERISA. The suit is an attempt to remove decision-making responsibility away from employers and to legislate employee benefit coverage through the federal courts. Congress and the courts have chosen not to dictate terms of employee benefit plans to employers. The Department of Labor should not be able to do so either.

I. LEGISLATIVE HISTORY AND PURPOSES OF ERISA

President Gerald Ford signed ERISA into law on Labor Day, 1974. The law was the culmination of a process that had been under way since at least 1963. In that year the Studebaker automobile company terminated production at its South Bend, Indiana, auto plant and 4,400 employees, members of the United Auto Workers lost all or part of their pension benefits. At the time there were no requirements for mandatory minimum funding of private pension plans and there was no insurance to guarantee benefits. Private pension plans were still a fairly new phenomenon and the government had preferred to let the plans police themselves. Other than

22. See Michael Allen, The Studebaker Incident and Its Influence on the Private Pension Plan Reform Movement, in LANGBEIN & WOLK, supra note 21, at 62; see also Gordon, supra note 21, at 69-70.
23. Private pension plans had only become widespread as a result of union activity in the mining, steel, and auto industries in the late 1940s. See WILLIAM C. GREENOUGH &
IS CLASSIFICATION AND EMPLOYER DISCRETION disclosure requirements enacted in 1958, there had been no government regulation of private pension plans prior to the enactment of ERISA in 1974.24

In 1965 a Senate investigation revealed that New Jersey labor leader George Barasch had set up two union pension plans in ways that allowed him to legally divert pension funds for his personal use.25 He appropriated millions of dollars as "consulting fees" and as donations to "charitable organizations" controlled by him in Liberia and Puerto Rico.26 At the time, the law imposed no fiduciary duties on pension plan administrators or trustees and provided no remedies. Without any enforcement mechanism, it was impossible to prevent or punish the abuses of Barasch and others like him.27 As a result, two of the main purposes of ERISA were to impose fiduciary duties and to provide remedies for breach of those duties.

In 1967, Senator Jacob Javits introduced the bill that would eventually become ERISA.28 Debate over the bill continued until 1971, when the Senate Labor Subcommittee released a report showing that only five percent of employees covered by private pension plans ever received benefits.29 Most employees were denied benefits because of minimum age requirements or vesting requirements that demanded up to thirty years of service or more before any benefits could be received. In the Studebaker case, a fifty-nine year old worker with thirty-eight years of service was denied benefits because he had not reached the age of sixty years when the plant closed.30 The law at the time contained no vesting requirements—most plans specified that benefits were "voluntary gifts" from employers and that workers had no contractual or legal rights to benefits.31 ERISA was designed to correct this situation by imposing minimum vesting requirements and defining the rights of employees under their employers' plans.

Public support for pension reform was growing. In 1973 consumer advocate Ralph Nader published a popular book entitled You and Your Pension.32 Nader called for the government to take over the pension

Francis P. King, Pension Plans and Public Policy, at 27 (1976), reprinted in Langbein & Wolk, supra note 21, at 12-14.

24. The Welfare and Pension Plans Disclosure Act of 1958 ("WPPDA") required full disclosure to participants and beneficiaries, but provided no remedies for participants and gave no enforcement power to any government agency. See Gordon, supra note 21, at 68.
25. See id. at 71.
26. See id. at 71.
27. See id. at 71-72.
28. See id. at 72.
29. See id. at 73.
30. See Allen, supra note 22, at 64.
system, create a series of mutual funds to be licensed by the SEC, and provide immediate vesting and unlimited portability. Nader was never called to testify at the Senate hearings because the Senate's goal was to reform and regulate the private pension system, not to create a government-sponsored system in its place.

Shortly after the bill was signed, Senator Javits succinctly stated the reform and regulatory purposes of ERISA:

The problem ... was how to maintain the voluntary growth of private plans while at the same time making needed structural reforms in such areas as vesting, funding, termination, etc., so as to safeguard workers against loss of their earned or anticipated benefits. ... [The] new law represents an overall effort to strike a balance between the clearly-demonstrated needs of workers for greater protection and the desirability of avoiding the homogenization of pension plans into a federally-dictated structure that would discourage voluntary initiatives for further expansion and improvement.

ERISA was a response to the failure of pension promises in Studebaker and similar plans, to the failure of private pension plans to self-police for abuses like those of Barasch, and to the millions of disappointed workers who were being denied benefits because of strict vesting requirements. The law was intended to encourage and regulate private pension plans. In enacting ERISA, Congress assumed that employee benefit plans would continue to be voluntary. Congress did not intend ERISA as a radical change and did not expect that it would force employers to extend benefits to classes of workers that would not otherwise be covered. Latter-day efforts to use ERISA to force employers to extend benefits to additional classes of workers are contrary to the legislative history and purpose of ERISA.

II. EMPLOYERS' RESPONSES TO ERISA: THE RISE OF CONTINGENT WORK ARRANGEMENTS

In the years since the passage of ERISA, the landscape of work in the United States has changed but Congress has chosen to leave ERISA very much the same. The law was originally intended as a regulatory
framework for a voluntary system of pensions and employee benefits. That purpose has been maintained by Congress and by the courts. From the beginning, Congress has allowed employers freedom in deciding how to structure work relationships and how to implement benefit programs. The rise of contingent work arrangements, including employee leasing, temporary help, and subcontracting, has occurred without substantial interference by Congress or the courts. Congress has neither extended the reach of ERISA nor made its provisions mandatory. This hands-off attitude is in keeping with the purpose of ERISA to promote the growth of voluntary employee benefit programs.

Employers in recent years have sought greater flexibility in work arrangements in order to respond to the pressure of global competition and to cope with legal requirements and the threat of litigation. The burden of pension commitments has at times become unbearable for some employers and has driven others toward consolidation. The rapidly increasing cost of health care has forced employers to place more of the burden of health insurance directly on employees and has contributed to the rise of managed care. Many employers have sought to sever the employment relationship altogether, and to distance themselves from workers in order to avoid liability.

Thirty-six percent of working-age Americans with income of less than twice the official poverty level have no health insurance. Eight percent of all American families with heads of household under age sixty-five have out-of-pocket health care costs greater than ten percent of their household income. Given these figures, advocates of social change have suggested that more of the health insurance burden and of the retirement income burden should be placed on employers. Working people who rely on part-time or temporary jobs are often not covered by employers' health insurance and pension plans. Proponents of employer-based solutions argue that federal laws governing employee benefits should be amended to eliminate the loopholes that allow employers to avoid paying benefits to workers who lack full-time employee status. They argue that the law


40. See id.

41. See, e.g., Sharon Dietrich et al., *Work Reform: The Other Side of Welfare Reform*, 9 STAN. L. & POL'Y REV. 53, 60 (1998) (arguing that "amendments should be passed for ERISA's participation and vesting standards, as well as for the anti-discrimination and other statutes that employers manipulate to avoid covering contingent workers").

should prevent employers from utilizing "peripheral" workers as a permanent source of cheap labor.\textsuperscript{43}

Today, workers are often "leased" from outside agencies on either a temporary or a long-term basis instead of being directly employed. For-fee employment agencies have been around since the 1890s.\textsuperscript{44} Because of their transitory relationship with workers, they have been closely regulated to prevent abuses such as the charging of excessive fees. Temporary help agencies, on the other hand, did not appear until the late 1940s.\textsuperscript{45} At first, some states treated them as a type of employment agency and attempted to regulate them as such. At the same time, state revenue departments and the IRS found identification of workers with agencies to be preferable to self-employment for purposes of collecting income taxes.\textsuperscript{46} Today, taxing authorities regularly recognize temporary help agencies as employers, even though that treatment often must coexist with conflicting treatment of their status by other government agencies and by the courts.\textsuperscript{47}

During the 1950s and 1960s, the temporary help industry lobbied state legislatures to exempt its members from regulation as employment agencies and to recognize their status as employers.\textsuperscript{48} By the early 1970s, all but two states had recognized that temporary help agencies do not present the same dangers, such as the charging of excessive fees, that traditional employment agencies do, and had therefore deregulated the temporary help industry. Its growth has been steady ever since.\textsuperscript{49}

Since 1982, temporary employment has grown three times as fast as overall employment.\textsuperscript{50} Temporary help agencies have increased employment 240\% since 1984, creating twenty percent of all new jobs.\textsuperscript{51} Manpower Temporary Help Agency is now the largest employer in the United States, with over 600,000 employees.\textsuperscript{52}

Several factors have contributed to the growth of temporary employment. First, temporary workers are widely used in the fastest

\textsuperscript{45} See id.
\textsuperscript{46} See id. at 180 n.9.
\textsuperscript{47} See id. at 180.
\textsuperscript{48} See id. at 181-82.
\textsuperscript{49} See id. at 185-87.
\textsuperscript{50} See Peter Cappelli et al., Change at Work 75 (1997).
\textsuperscript{51} See id. at 76.
\textsuperscript{52} See id.
growing segments of the economy—the trade and service industries. Second, many of today's "high-performance organizations" believe that a "buffer" of temporary employees improves the sense of job security and morale of their permanent "core" employees. Third, some temporary employees provide specialized skills that may not be available in-house. Finally, many employers use temporary workers with the hope of reducing labor and benefits costs, avoiding the costs of compliance with employment laws, and reducing the risks of litigation.

Whether, and to what extent, employers should be able to use contingent work arrangements to reduce labor costs and avoid liability is a question of public policy. Congress could have adopted a policy that would have made benefits mandatory for all common-law employees, but with ERISA it adopted a policy that allowed employers the flexibility to determine who is an employee for purposes of benefits. ERISA promotes and regulates voluntary employee benefit programs. It has never been used to dictate the arrangements that may be made between employers and workers.

III. JUDICIAL REVIEW OF CONTINGENT WORK ARRANGEMENTS

The congressional policy of promoting the growth of voluntary employee benefit programs has been carried out by the courts that have interpreted and applied ERISA. Much recent litigation has centered around deciding who is an employee under ERISA and what rights employees have. The definition of employee is of critical importance because that definition can determine whether a worker or class of workers is entitled to benefits. When Congress drafted ERISA, it deliberately left the definition of "employee" open-ended, thus leaving decisions about eligibility for benefits up to employers.

In 1989, the Supreme Court ruled in Firestone Tire & Rubber Co. v. Bruch, that, where the terms of an employee benefit plan allow, courts should defer to an employer in determining who is an employee for purposes of participation in a plan. Three years later, in Nationwide

53. See id. at 76-77.
54. See id. (stating that most Title VII and tort liability arises in the context of hiring and firing and wage and promotion decisions, which are not issues with temporary employees).
56. ERISA defines "employee" as "any individual employed by an employer." ERISA § 3(6). An "employer" is defined as "any person acting directly as an employer, or indirectly in the interest of an employer ...." ERISA § 3(5).
58. See 489 U.S. 101, 115 (1989) (finding that deference should be given to the administrator if the benefit plan specifically gives the administrator such discretion to
Mutual Insurance Co. v. Darden, the Supreme Court rejected arguments that employment status should be defined by a worker's expectations of receiving benefits. The Darden Court held that the traditional common law of agency should apply when a court needs to define who qualifies as an employee. The Court endorsed the common law test because it "turns on factual variables within an employer's knowledge." The Court held that employers should be able "to figure out who their 'employees' are and what, by extension, their pension-fund obligations will be."

The definition of "employee" and the benefits attached to a worker's status are matters best left to the discretion of the employers and employees themselves. The law need only inquire whether employment arrangements are made freely and are fully-informed. Courts have made it difficult for employers to "misclassify" employees as independent contractors or to "outsource" employment functions for the purpose of reducing benefits, but at the same time they have preserved the rights of employers to selectively grant benefits, to amend benefit plans, and to interpret plans in determine eligibility).

59. See 503 U.S. at 326-27.

60. The issue in Darden was whether the plaintiff had standing as an employee to bring suit, not whether his status as an employee would entitle him to benefits. The Court adopted the test it had previously used in interpreting the Copyright Act of 1976, 17 U.S.C. § 101:

In determining whether a hired party is an employee under the general common law of agency, we consider the hiring party's right to control the manner and means by which the product is accomplished. Among the other factors relevant to this inquiry are the skill required; the source of the instrumentalities and tools; the location of the work; the duration of the relationship between the parties; whether the hiring party has the right to assign additional projects to the hired party; the extent of the hired party's discretion over when and how long to work; the method of payment; the hired party's role in hiring and paying assistants; whether the work is part of the regular business of the hiring party; whether the hiring party is in business; the provision of employee benefits; and the tax treatment of the hired party.


61. Id. at 327. The Internal Revenue Service uses a twenty-factor common-law definition that also turns on the facts of the case. See Rev. Rul. 87-41, 1987-1 C.B. 296. Factors not specifically addressed in the Darden definition include whether (1) the employer trains the worker; (2) the worker is integrated into the employer's operations; (3) the worker must submit oral or written reports to the employer; (4) the worker has a significant investment in facilities used in performing the work; (5) the worker stands to realize a profit or suffer a loss; and (6) the employer has the right to discharge or terminate the worker.

62. Darden, 503 U.S. at 327.

63. See Vizcaino v. Microsoft Corp., 120 F.3d 1006 (9th Cir. 1997); see also infra Part II.B.

methods that are not unreasonable.65

A. The Standard of Review: Firestone Tire & Rubber Co. v. Bruch

The 1989 Supreme Court decision in Firestone Tire & Rubber Co. v. Bruch66 provides the background for recent cases regarding the treatment of contingent workers. Firestone defines the standard of judicial review courts must apply to fiduciaries' decisions concerning workers' eligibility for benefits. Prior to Firestone, courts had applied an "arbitrary and capricious" standard in reviewing employers' decisions denying benefits to employees.67 Under that standard, an employer's interpretation of its plan would be reversed only if "a plan provision as interpreted had the effect of denying an application for benefits unreasonably, or as it came to be said, arbitrarily and capriciously ...."68 The Firestone Court rejected the arbitrary and capricious standard, finding that, in the absence of language in the plan granting discretionary power to the plan administrator, courts should apply a de novo standard, "review[ing] the employee's claim as it would ... any other contract claim — by looking to the terms of the plan and other manifestations of the parties' intent."69 Under arbitrary and capricious review, courts defer to the interpretation of the plan administrator and rarely find the denial of benefits unreasonable. Under de novo review courts do not defer to the plan administrator's interpretation, but rather interpret the plan themselves.70 Ambiguities are much more likely to be resolved in favor of the employee under de novo review.

In Firestone, Firestone Tire and Rubber Company sold five plastics plants to Occidental Petroleum Company.71 Most of the 500 Firestone employees in the plants continued without interruption as employees of Occidental.72 Several of the employees nonetheless sought compensation under Firestone's termination pay plan, which provided for severance pay following a "reduction in work force."73 These employees argued that the transfer from Firestone to Occidental constituted such a reduction.74 Firestone's plan administrator refused to provide severance pay, finding that the transfers were not a "reduction in work force" within the meaning

65. See Vizcaino, 120 F.3d at 1009.
67. See id. at 109.
68. Id. (quoting Van Boxel v. Journal Co. Employees' Pension Trust, 836 F.2d 1048, 1052 (7th Cir. 1987)).
69. Id. at 112-13.
70. See id. at 115.
71. See id. at 105.
72. See id.
73. See id. at 105-06.
74. See id. at 106.
The employees brought a class action suit under ERISA § 502(a)(1)(B), which allows a participant or beneficiary of a plan to bring suit "to recover benefits due to him under the terms of his plan." The district court granted summary judgment for Firestone, holding that its refusal of benefits was not arbitrary or capricious. The Court of Appeals for the Third Circuit reversed, applying a de novo standard of review rather than an arbitrary and capricious standard. The Court noted that the arbitrary or capricious standard is not appropriate where there is potential conflict of interest because an employer is both fiduciary and administrator of an unfunded benefit plan.

The arbitrary and capricious standard was imported into ERISA jurisprudence from the Labor Management Relations Act (Taft-Hartley) ("LMRA"). The Supreme Court in Firestone decided that the federal common law of ERISA should be guided instead by trust law. A deferential standard of review is appropriate under trust law only when a trustee is granted discretionary powers by the trust instrument. Absent such a grant of power, the trustee has no discretion to interpret the terms of a trust agreement and the courts will construe the trust agreements under contract law principles, without deference to either party. ERISA defines a fiduciary as one who exercises some degree of discretionary control; it does not confer unlimited discretionary control. The Court concluded that a denial of benefits challenged under ERISA § 502(a)(1)(B) should be reviewed under a de novo standard unless the plan grants the administrator or fiduciary discretionary authority to determine eligibility and to construe terms.

At the time the Firestone case was decided, many employers became concerned that courts would no longer grant deference to the decisions of plan administrators regarding eligibility for benefits. To the contrary, Firestone was not a serious blow to plan sponsors. The Court had provided an "out" by allowing de novo review to apply "unless the benefit plan gives the administrator or fiduciary discretionary authority to determine eligibility for benefits or to construe the terms of the plan."

75. Id.
76. ERISA § 502(a)(1)(B); Firestone, 489 U.S. at 106.
77. See Firestone, 489 U.S. at 106-07.
78. See id. at 107.
80. See Firestone, 489 U.S. at 110-11.
81. See id. at 115.
82. See id. at 112-13.
83. See ERISA § 3(21)(A)(i) (defining a fiduciary as one who "exercises any discretionary authority or discretionary control respecting management of [a] plan or . . . respecting management or disposition of its assets . . ."); Firestone, 489 U.S. at 113.
84. See Firestone, 489 U.S. 101 at 115.
85. Id.
Consequently, employers have simply amended their plans to include terms granting discretionary authority to plan administrators to determine eligibility for benefits and to construe terms of their plans. Plan administrators have not lost their discretionary authority. The Firestone Court has merely reinforced the fundamental notion that the terms of the plan govern. If the terms of the plan so provide, the administrator has discretion. If the plan does not grant discretion, the plan is treated as any other contract. Today, plans routinely include language granting the plan administrator discretionary authority to determine eligibility and to construe the terms of the plan. Ultimately, Firestone did not have the feared effect of replacing arbitrary and capricious review with de novo review. Firestone stands merely for the proposition that the plan administrator's authority comes from the terms of the plan itself.

B. The Ninth Circuit: Vizcaino v. Microsoft

The discretionary authority of employers to determine eligibility for benefits under their plans has been challenged in a number of recent cases in which employers were claimed to have illegally "misclassified" certain workers as independent contractors in order to deny them benefits. The most prominent and perhaps most protracted of these cases is Vizcaino v. Microsoft Corp. Plaintiffs in Vizcaino were workers who were contracted to Microsoft between 1987 and 1990 as software testers, production editors, proofreaders, formatters, and indexers. These workers were college-educated and one had a law degree. They were paid a higher cash wage in return for providing their own tax withholding, insurance, and benefits. When they started work, they signed two documents regarding their status as independent contractors. One stated in part that the worker "agree[d] to be responsible for all federal and state taxes, withholding, social security, insurance and other benefits." The other document explained that "you are self-employed and responsible to pay all your own insurance and benefits." The freelancers' functions were essentially identical to those of regular employees who received full benefits. They were paid,
however, through the company's accounts payable department instead of
through the payroll department and they were not paid overtime. Each
had worked continuously for more than a year.

In 1989 and 1990, the Internal Revenue Service reviewed Microsoft's
employment records as part of an enforcement effort to combat a low
compliance rate among independent contractors. Applying the common-
law definition of "employee," the IRS found that Microsoft exercised
significant control over workers it had classified as independent
contractors, and ordered Microsoft to pay withholding and Federal
Insurance Contribution Act ("FICA") taxes. Microsoft agreed to pay the
taxes and to pay overtime retroactively. Some of the independent
contractors were converted into regular employees, while others were
required to accept employment with a temporary employment agency.
Their duties remained unchanged.

Plaintiffs then attempted to claim eligibility as employees
retroactively under each of Microsoft's employee benefit plans, including
vacation, sick days, holiday pay, and health insurance, as well as the
company's 401(k) retirement savings plan and its employee stock
ownership plan ("ESOP"). The Microsoft plan administrator refused
their claims because they had contractually waived any rights to benefits
when they signed the documents regarding their status as independent
contractors, and because they were not "regular, full-time employees in
approved headcount positions." The plaintiffs took their claims to
federal district court. The district court referred the case to a magistrate
judge, who recommended the rejection of all claims except those under the
401(k) and the ESOP. The magistrate found that the terms of the 401(k)
were ambiguous, so that the doctrine of contra proferentem required

96. See id.
97. See id.
98. See id. at 1202 n.2. The IRS, estimating that independent contractors underpaid
taxes by two to three billion dollars a year, eventually reclassified 527,000 workers. Many
of these workers ended up employed by temporary help agencies. See Gonos, supra note
44, at 180 n.9.
99. See Vizcaino, 97 F.3d at 1190-91.
100. See id.
101. See id. at 1191.
102. See id.
103. See id.
104. Id.
105. See id.
106. See id. at 1191-92
107. The court explained the rule of contra proferentem as follows: "[w]hen a plan is
ambiguous on its face, we may, and typically do, consider extrinsic evidence to interpret it.
If the ambiguity persists even after resort to extrinsic evidence, we generally apply the rule
of contra proferentem and construe the ambiguity against the drafter." Id. at 1194 (citations
omitted). This rule is highly unfavorable to the employer.
construction in favor of the plaintiffs.\footnote{8}

The district court rejected the magistrate's recommendations regarding the 401(k) and the ESOP.\footnote{9} It found that \textit{contra proferentem} was inapplicable to the 401(k) because the intent of the parties to deny participation was unambiguous.\footnote{10}

The plaintiffs appealed, and a three-judge panel of the United States Court of Appeals for the Ninth Circuit, with one judge dissenting, reversed, agreeing with the magistrate on the issue of ambiguity.\footnote{11} The 401(k) defined "employee" as "any common-law employee who receives remuneration for personal services rendered to the employer and who is on the United States payroll of the employer."\footnote{12} On appeal, Microsoft conceded that the plaintiffs were common-law employees, but argued for the first time that "on the United States payroll" meant that participation was limited to those who were paid through the company's payroll department, and thus excluded independent contractors, who were paid through the accounts payable department.\footnote{13} The court of appeals found Microsoft's construction reasonable, but also found that an "ordinary meaning" interpretation could allow it to conclude that "payroll" meant "a list of persons to be paid."\footnote{14} Since the plan administrator had not construed the term "on the United States payroll," the court reviewed the term de novo and applied the rule of \textit{contra proferentem} in favor of plaintiffs, noting incidentally that it found plaintiffs' reading more reasonable.\footnote{15}

The dissenting judge argued that the plaintiffs entered their work arrangement with their eyes open and that they had no expectation of receiving benefits.\footnote{16} He further argued that the IRS's classification of workers as common-law employees for purposes of tax collection is compatible with the parties' freedom to contract another arrangement for purposes of employee benefits:

\begin{quote}
[T]he majority seems to overlook the constitutional right of
\end{quote}

\footnotetext{8}{See id. at 1191-92. Since the ESOP was not an ERISA plan, the courts treated it under Washington state contract law. For that reason I will not deal with it in detail here. The magistrate found that because the ESOP expressly adopted the conditions of the Internal Revenue Code requiring extension of the stock-purchase offer to all common-law employees, and because Microsoft had incorrectly told the plaintiffs that they were not common-law employees, the district court should find that the plaintiffs were eligible.}

\footnotetext{9}{See id. at 1192}

\footnotetext{10}{See id. With regard to the ESOP, the district court ruled that no offer was made and that the plaintiffs could not have relied on any expectation of receiving benefits.}

\footnotetext{11}{See id. at 1196.}

\footnotetext{12}{Id. at 1192.}

\footnotetext{13}{See id. at 1193.}

\footnotetext{14}{Id. at 1194.}

\footnotetext{15}{See id. at 1196.}

\footnotetext{16}{See id. at 1201.}
private parties freely to enter into contracts of their own choice and benefit. It is not for the courts under these circumstances to add clauses to agreements that the parties never contemplated .... Congress designed ERISA to protect benefits workers already had, not to give them benefits for which they did not contract.\footnote{117}

On rehearing en banc, the full court agreed with the majority of the three-judge panel that the plaintiffs were common-law employees and that the agreements failed to waive their rights to benefits, but it remanded to the district court for further remand to the plan administrator for construction of the term "on the United States payroll."\footnote{118} Six of eleven judges favored remand on the issue of eligibility for the 401(k).\footnote{119} The opinion of the court suggested that the plan administrator should find in favor of plaintiffs.\footnote{120} Three of the six judges, however, writing in concurrence, argued that Microsoft should be free "to classify employees for participation or non-participation in an ERISA plan based on whether the employees were regular hires paid through the Payroll department or 'freelancers' paid through the Accounts Payable department."\footnote{121}

As was the case after Firestone, many employers have viewed the Vizcaino decision with consternation, fearing that courts would void employees' agreements to waive benefits, thus depriving them of an effective means of determining eligibility. The implications of the case are not that extreme. Microsoft, by using waiver agreements, made clear its intent not to provide benefits to certain workers. The court ignored that intent because Microsoft conceded that plaintiffs were in fact common-law employees.\footnote{122} It is still possible for employers to differentiate independent contractors from regular employees by clear documentation of their status and by separate arrangements for their compensation.\footnote{123} Requiring independent contractors to sign waivers of benefits may still be effective if

\footnote{117. \emph{Id.} at 1203.}
\footnote{118. \emph{See} Vizcaino v. Microsoft, 120 F.3d 1006, 1013, 1015 (9th Cir. 1997) ("[W]e should not allow ourselves to be seduced into making a decision which belongs to the plan administrator in the first instance."). The majority also agreed that plaintiffs were eligible for the ESOP. Litigation on the ESOP continues. \emph{See} Vizcaino v. Microsoft Corp., 1998 WL 762381 (W.D. Wash. July 15, 1998), remanded by Vizcaino v. United States Dist. Court for the Western Dist. of Washington, 173 F.3d 713 (9th Cir. 1999).}
\footnote{119. \emph{See} Vizcaino, 120 F.3d at 1015}
\footnote{120. \emph{See id.} at 1013 (stating that "the plan administrator should pay careful attention 'to the panel's construction of 'on the United States payroll'".)
}
\footnote{121. \emph{Vizcaino}, 120 F.3d at 1022-23 (O'Scannlain, J., concurring in part) (arguing that "the court's statements do not bind the plan administrator in any way"). These three judges dissented from the finding that plaintiffs were eligible for the ESOP.
}
\footnote{122. \emph{See} Vizcaino, 97 F.3d at 1192-93.
}
\footnote{123. \emph{See} Renate M. de Haas, Vizcaino v. Microsoft, 13 BERKELEY TECH. L.J. 483, 498 (1998).}
those waivers include terms excluding workers who are later reclassified as employees by the IRS.\textsuperscript{124}

Most important, the Court of Appeals for the Ninth Circuit relieved Microsoft of liability when it remanded the 401(k) issue to the plan administrator. Assuming that the administrator would find that "on the United States payroll" excluded plaintiffs, it is unlikely that the district court would find abuse of discretion.\textsuperscript{125} In effect, the court of appeals had already found that Microsoft's plan administrator did have the discretion to find plaintiffs ineligible for the 401(k). Even though Microsoft had not presented its "on the United States payroll" argument to the trial court, the court of appeals allowed the argument.\textsuperscript{126} Further, although only three members of the en banc court found the argument convincing, it still granted Microsoft discretion to find that the term excluded plaintiffs.

\textit{Vizcaino} illustrates that an employer's discretion in determining eligibility for benefits is not lost when workers are reclassified by the I.R.S. Even where the plan administrator fails to construe terms of the plan, as Microsoft did with the term "on the United States payroll," a court will likely remand the case rather than preempt the employer's discretion. \textit{Vizcaino} should therefore not be regarded as a defeat for employer discretion. Employers must be cautious when drafting and interpreting plans and waivers, but even when caution fails, courts are reluctant to make eligibility decisions for them.

\section*{C. Other Courts of Appeals: Less Confusion}

Other court of appeals cases have involved plan language that more explicitly excluded non-employees, and plan administrators who more clearly exercised their discretion in interpreting their plans. Where plans have been drafted unambiguously and where plan administrators have interpreted their plans unequivocally, it has been easier for courts to defer to employers' discretion in denying benefits to independent contractors and leased employees.

The Court of Appeals for the Fifth Circuit case \textit{Abraham v. Exxon}\textsuperscript{127} was a suit brought by workers whose functions resembled those of regular Exxon employees, but who were nominally employed by outside agencies

\textsuperscript{124}. See id. at 497 (citing Microsoft Employees Who Were Misclassified as Independent Contractors Get Benefits, 5 ERISA LITIG. REP. 10 (1996) (recommending plan language providing that "the cash payments to [independent contractors] represent their sole compensation, even if they are eventually reclassified as employees").
\textsuperscript{125}. See \textit{En Banc Decision by 9th Circuit in Microsoft Does Something}, 6 ERISA LITIG. REP. 4, 7 (1997).
\textsuperscript{126}. See de Haas, supra note 123, at 487-88.
\textsuperscript{127}. 85 F.3d 1126 (5th Cir. 1996).
that leased their services to Exxon. The ERISA plan specifically excluded leased employees and other "special agreement" employees. As Microsoft did in Vizcaino, Exxon conceded that plaintiffs were common-law employees.

Plaintiffs in Abraham relied on the district court case of Renda v. Adam Meldrum & Anderson Co. in which the court interpreted the minimum participation requirements of ERISA § 202(a)(1)(A) prohibiting discrimination on the basis of age or length of service. The Renda court found that section 202(a) effectively prohibits discrimination against any class of employees, other than those under twenty-one or with less than one year of service. The Abraham court disagreed, and held that an employer is free to deny participation "on a basis other than age or length of service."

The Renda court also relied on Treasury regulations requiring that plans must be nondiscriminatory in order to qualify for special tax treatment. The Renda court held that the Treasury regulations should be used to determine who is eligible for benefits under an ERISA plan. The Abraham court disagreed here also, holding that a plan's failure to comply with Treasury regulations could result in a loss of tax benefits, but "does not permit a court to rewrite the plan to include additional employees."

In affirming the district court's grant of summary judgment, the Abraham court held that the lower court correctly deferred to the plan administrator's discretion. The court elaborated on the process by which a district court should review a plan administrator's decision to refuse benefits. In determining whether the plan administrator's decision is "legally correct," the court looks to: "(1) whether the administrator has given the plan a uniform construction, (2) whether the interpretation is

128. See id. at 1128.
129. See id.
130. See id. at 1129.
132. See ERISA § 202(a) (stating that a plan may not discriminate on the basis of age, other than to require that a participant be older than 21, or on the basis of length of service, other than to require a minimum of one year of service).
133. See Renda, 806 F. Supp. at 1081, cited in Abraham, 85 F.3d at 1130.
134. Abraham, 85 F.3d at 1130.
137. Abraham, 85 F.3d at 1131; cf. Crouch v. Mo-Kan Iron Workers Welfare Fund, 740 F.2d 805, 809 (10th Cir. 1984) (finding an exception where an explicit provision in the ERISA plan declares that it was to be "construed to meet the requirements of ERISA").
138. See Abraham, 85 F.3d at 1131 (finding that the plan gave the administrator "discretionary and final authority to determine eligibility ... [and] to interpret this ... Plan") (citing Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 115 (1989)).
139. Id.
consistent with a fair reading of the plan, and (3) any unanticipated costs resulting from different interpretations of the plan.\textsuperscript{140} The Abraham court held that Exxon's exclusion of leased employees met the first two standards and that their inclusion would require extending benefits to 16,000 additional employees.\textsuperscript{141}

Abraham grants broad discretion to employers in determining eligibility for benefits; the terms of the plan as construed by the plan administrator are paramount. Even the loss of the plan's qualification for tax deductions does not invalidate the employer's discretion. Under Abraham, a court will even go so far as to consider the costs of expanded eligibility in deferring to the plan administrator.

In Clark v. E.I. DuPont de Nemours & Co.\textsuperscript{142} the Court of Appeals for the Fourth Circuit also deferred to a plan administrator's decision to deny benefits to a leased employee.\textsuperscript{143} Clark worked for DuPont's construction division from 1962 until 1970.\textsuperscript{144} He was terminated when DuPont eliminated the division.\textsuperscript{145} Between 1973 and 1993, Clark worked for various companies that performed contract work for DuPont.\textsuperscript{146} Clark then applied for benefits under DuPont's insurance and vacation pay plans, as well as under its stock ownership, savings, and investment plans.\textsuperscript{147} The plan administrator denied Clark benefits on the ground that he was not eligible "under the plain language of the Plans."\textsuperscript{148} The district court, even assuming that Clark was a common-law employee, granted summary judgment for DuPont finding that the language of the plans specifically excluded leased employees.\textsuperscript{149}

DuPont's insurance and vacation plans granted eligibility to "any person designated by the Company as a full time employee... on the roll... who continues to work at least 20 hours per week on a regular

\textsuperscript{140} Id. (citing Wildbur v. ARCO Chem. Co., 974 F.2d 631, 638 (5th Cir. 1992), clarified by 979 F.2d 1013 (5th Cir. 1992)).
\textsuperscript{141} See id. at 1131-32. Even though the court in Abraham found plaintiffs' Renda argument without merit, it found that Exxon's plan administrator should have complied with plaintiffs' request for information under the plan. See ERISA § 502(c)(1)(B). The court remanded to the district court for determination of whether civil penalties should be assessed against the plan administrator, but even here it allowed the district court to give the administrator an "out" if it found that he had acted in good faith in refusing the information. See Abraham, 85 F.3d at 1132.
\textsuperscript{143} See id. at *3.
\textsuperscript{144} See id. at *1.
\textsuperscript{145} See id.
\textsuperscript{146} See id.
\textsuperscript{147} See id.
\textsuperscript{148} Id. at *1.
\textsuperscript{149} See id.
basis." The plan administrator had always defined "on the roll" to exclude independent contractors and leased employees. The court of appeals found that the administrator's interpretation was unequivocal and was not an abuse of discretion. The ESOP and the savings plan contained language recognizing that leased employees had to be counted along with regular employees for tax qualification purposes, but expressly excluded them from the receipt of benefits. The court, citing Abraham, refused to find that the Internal Revenue Code or Treasury regulations extended substantive rights to all common-law employees under ERISA plans.

The Court of Appeals for the Tenth Circuit likewise relied on Abraham in Bronk v. Mountain States Telephone & Telegraph, Inc., another case involving leased employees. The plan administrator in Bronk determined that the plans covered only "regular employees" and that leased employees were not "regular employees." The court rejected the same ERISA § 202(a) argument based on Renda that the Fifth Circuit rejected in Abraham. It also referred to an IRS notice specifically addressing whether leased employees must be eligible for benefits. It quoted Q & A-14 of Notice 84-11:

Q-14. Must a leased employee participate in the plan maintained by the recipient [of leased employee services]?

A-14. No. Section 414(n)(1)(A) requires only that a leased employee be treated as an employee; it does not require that a leased employee be a participant in the recipient's qualified plan.

Thus, the IRS confirms that reclassification of workers for tax purposes does not override the employer's discretion in determining eligibility for benefits.

Taken together, these cases show that courts will generally defer to plan administrators who determine that leased employees or independent contractors are not eligible for benefits. The deferential Firestone standard is alive and well. The problem in Vizcaino was that Microsoft left the interpretation of the term "on the United States payroll" to the court. The

150. Id. at *3.
151. See id.
152. See id. at *3.
153. See id. at *3 n.2.
154. See id. at *4; Abraham v. Exxon Corp., 85 F.3d 1126, 1130 (5th Cir. 1996).
155. 140 F.3d 1335 (10th Cir. 1998).
156. See id. at 1337.
157. See id. at 1338-39.
158. Id. at 1339 (quoting I.R.S. Notice 84-11, available in WL, FTX-RELS).
159. See Vizcaino v. Microsoft, 120 F.3d 1006, 1013 (9th Cir. 1997); see also supra text
three-judge panel of the Court of Appeals for the Ninth Circuit surprised Microsoft by finding the term ambiguous and construing it against the company, but the full court ultimately remanded the ERISA issue to the plan administrator for construction of the term. In Abraham, Clark, and Bronk the courts dealt with terms that had already been construed by the plan administrators, and the rule of deferential review was clear.

D. The Court of Appeals for the Ninth Circuit Again: Burrey v. Pacific Gas & Electric

In October 1998 the Court of Appeals for the Ninth Circuit decided Burrey v. Pacific Gas & Electric Co. Plaintiffs in this case were clerical workers employed by several outside agencies in succession between 1982 and 1994, and leased to Pacific Gas & Electric Company ("PG&E"). PG&E maintained several employee benefit plans, including health and severance plans, that did not specifically exclude leased employees from coverage. PG&E's retirement and savings plans did expressly exclude "leased employees, as defined by Section 414(n) of the Internal Revenue Code." The district court granted PG&E's motion for summary judgment, finding that plaintiffs were excluded from the retirement and savings plans as leased employees, and that they lacked standing to sue under the other plans because the benefits had not vested.

The court of appeals reviewed the plan administrator's interpretation of the plan under a de novo standard because the plan incorporated by reference the terms of I.R.C. § 414(n), defining "leased employees." Because the plan required the administrator to interpret a federal statute, the court refused to defer to the plan administrator's discretion in interpreting that term of the plan.

At the time that plaintiffs claimed to have been covered by the PG&E plans, I.R.C. § 414(n) read as follows:

[T]he term "leased employee" means any person who is not an employee of the recipient and who provides services to the

accompanying notes 111-15.

160. See Vizcaino, 120 F.3d at 1018.
161. See id. at 1015.
162. 159 F.3d 388 (9th Cir. 1998).
163. See id. at 391.
164. See id. at 392.
165. See id.
166. See id. at 391-92. A plan cannot give an administrator discretion to interpret a federal statute. See id. at 392. The court found that "[t]he interpretation of § 414(n) is a question of law which we review de novo." Id. (citing Spink v. Lockheed Corp., 125 F.3d 1257, 1260 (9th Cir. 1997) (finding that "interpretation of ERISA, a federal statute, is reviewed de novo").
recipient if—

(A) such services are provided pursuant to an agreement between the recipient and any other person (in this subsection referred to as the "leasing organization"),

(B) such person has performed such services for the recipient . . . on a substantially full-time basis for at least 1 year, and

(C) such services are of a type historically performed, in the business field of the recipient, by employees.167

The district court determined that plaintiffs were leased employees under this definition, whether they were considered common-law employees or not.168 The court of appeals, however, focused its analysis on the language "who is not an employee of the recipient" in the first line of the subsection.169 Since the statute does not define "employee" in this context, the court held that "employee' as used in § 414(n) means 'common-law employee."170 The court then concluded that if the plaintiffs were common-law employees, they could not be considered "leased employees" as defined in § 414(m) and could not be excluded from benefits as "leased employees" under the plan.171

The district court relied on Abraham in holding that leased workers may be excluded from benefit plans even though they qualify as common-law employees.172 The court of appeals did not contradict this principle. Its holding was much narrower. It merely held that when a plan relies on I.R.C. § 414(n) to provide its definition of leased employees, that definition includes only those leased workers who cannot be classified as common-law employees.173 The court of appeals remanded to the district court to


168. See Burrey, 159 F.3d at 391.

169. See id. at 394.

170. Id.

171. See id. at 393. The court also referred to the legislative history of the 1996 amendment, which stated that under both the old and new versions "the determination of whether someone is a leased employee is made after determining whether the individual is a common-law employee of the recipient." S. Rep. No. 104-281, at 93, reprinted in 1996 U.S.C.C.A.N. 1567.

172. See Burrey, 159 F.3d at 394.

173. See id.; cf. Clark v. E.I. DuPont De Nemours & Co., 105 F.3d 646, No. 95-2845, 1997 WL 6958, at *3 (unpublished disposition) (4th Cir. Jan. 9, 1997) (holding that a plan administrator may deny benefits to leased employees under the terms of a plan that excludes workers "who must be treated as employees of the Company for limited purposes under the 'leased employee' provisions of § 414(n) of the [I.R.C.]") (brackets in original)); supra text accompanying notes 142-54; see also Wolf v. Coca-Cola Co., 200 F.3d 1337, 1241-42 (11th
determine whether plaintiffs were common-law employees. For employers, the implication is simple: if you incorporate federal statutes into the terms of your plan, you may cede discretion to the courts.

IV. A NEW ROLE FOR THE DEPARTMENT OF LABOR: HERMAN V. TIME WARNER

In the past, suits challenging the denial of benefits have been brought by individual plan participants under ERISA § 502(a)(1)(B) "to recover benefits due." The recent suit against Time Warner was brought instead by Secretary of Labor Alexis Herman, following an investigation by the Department of Labor's Pension and Welfare Benefits Administration ("PWBA"). This represents a radical departure in the procedure by which such suits may be brought.

Until recently, ERISA was interpreted to allow individuals to bring suit against employers for denial of benefits, or for breach of fiduciary duty in the administration of a plan. In the latter case, individuals could recover damages only on behalf of the plan, not on their own behalf. The Secretary of Labor could bring suit on behalf of a plan for breach of fiduciary duty, but could not bring suit on behalf of individuals for benefits denied. That scheme was disrupted by the Supreme Court's decision in Varity Corp. v. Howe when, for the first time, the Court allowed individual plan participants and beneficiaries to bring suit to recover on their own behalf in a case not involving denial of benefits. Varity was a suit brought by individuals, but the Court suggested in dicta that in the future the Secretary of Labor might be able to bring suit to recover on behalf of individual participants and beneficiaries. Herman v. Time Warner is the Department of Labor's first effort to take advantage of that license.

Cir. 2000) (distinguishing Vizcaino and Burrey on the ground that a leased employee who is found to be a common-law employee must also be found eligible for benefits under the terms of the plan).

174. See Burrey, 159 F.3d at 394.
177. See id. at 144.
178. See id. at 142 n.9 (noting that "[i]nclusion of the Secretary of Labor is indicative of Congress' intent that actions for breach of fiduciary duty be brought in a representative capacity on behalf of the plan as a whole").
180. See id. at 492.
181. See id. at 510.
Varity Corporation was the parent company of Massey-Ferguson, Inc., a manufacturer of farm equipment. Varity developed a plan called "Project Sunshine," to dispose of money-losing divisions of Massey-Ferguson, and to thereby relieve itself of obligations under medical and other employee welfare benefit plans associated with those divisions. Varity persuaded 1,500 Massey-Ferguson employees to transfer to a new subsidiary called Massey Combines by assuring them that their benefits would be secure. It also assigned the benefit obligations of 4,000 retirees to Massey Combines. In fact, Massey Combines was insolvent from its date of incorporation and its books concealed a negative forty-six million dollar net worth. By the end of its second year, Massey Combines was bankrupt and its employees were without benefits.

Because Massey Combines was bankrupt, its non-pension benefit plans ceased to exist and its employees could not bring suit for denial of benefits. Nor could they bring suit against Varity, because they were no longer participants in its plans. The district court found that Varity was liable for breach of fiduciary duty for having deceived the employees about the viability of Massey Combines and the security of their benefits. However, if a suit for breach of fiduciary duty permitted recovery only on behalf of the plan, the employees would have had no remedy. Therefore, the court found that the employees were entitled to a remedy on their own behalf under ERISA.

In deciding whether the employees were indeed entitled to a remedy, the Supreme Court carefully analyzed ERISA § 502, the section providing for civil enforcement of ERISA. Section 502(a) lists "[p]ersons empowered to bring a civil action." The most frequently used provision of the section is § 502(a)(1)(B), which provides that:

A civil action may be brought—

(1) by a participant or beneficiary—

... (B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan ...
This provision is regularly used by individuals who have been denied benefits under their plans.\textsuperscript{191} It provides a cause of action only for plan participants or beneficiaries, not for the government. In \textit{Varity}, however, the employees had no cause of action under § 502(a)(1) because the plans had been terminated upon the bankruptcy of Massey Combines.\textsuperscript{192}

Subsection 502(a)(2) allows a civil action to be brought by the Secretary of Labor "for appropriate relief under § 409." Section 409, entitled "Liability for breach of fiduciary duty," provides only for recovery by the plan as an entity, not by individual plan participants.\textsuperscript{193} Under § 409, a fiduciary may be required to:

\begin{quote}
make good to [the] plan any losses to the plan resulting from . . . breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary.\textsuperscript{194}
\end{quote}

Section 409 provides for damages in the form of compensation or disgorgement in favor of the plan. Its most severe remedy is removal of the offending fiduciary. It does not address denial of benefits to plan participants or beneficiaries. Thus, § 502(a)(2) does not provide a cause of action to the Secretary of Labor on behalf of individual plan participants or beneficiaries. \textit{Varity} breached its fiduciary duties, but § 502(a)(2) provided no remedy for its employees.\textsuperscript{195}

Individual plaintiffs may look to § 502(a)(3), which provides for a general cause of action:

\begin{quote}
by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this title or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this title or the terms of the plan.\textsuperscript{196}
\end{quote}

In \textit{Varity} the Supreme Court found that § 502(a)(3) allows recovery for individual plan participants and beneficiaries.\textsuperscript{197} The Court concluded that "it is hard to imagine why Congress would want to immunize breaches of fiduciary obligation that harm individuals by denying injured

\begin{itemize}
\item \textsuperscript{191} See Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 106 (1989).
\item \textsuperscript{192} See \textit{Varity}, 516 U.S. at 515.
\item \textsuperscript{193} See Massachusetts Mut. Life Ins. Co. v. Russell, 473 U.S. 134, 144 (1985) (finding that "Congress did not intend [§ 409] to authorize any relief except for the plan itself").
\item \textsuperscript{194} ERISA § 409(a).
\item \textsuperscript{195} See \textit{Varity}, 516 U.S. at 509; \textit{Russell}, 473 U.S. at 146.
\item \textsuperscript{196} ERISA § 502(a)(3).
\item \textsuperscript{197} See \textit{Varity}, 516 U.S. at 515.
\end{itemize}
beneficiaries a remedy."\(^{198}\) This ruling allows the individual plaintiffs to sue plan administrators for compensatory damages when they have no cause of action for denial of benefits under § 502(a)(1).

While \textit{Varity} allows recovery for individuals under § 502(a)(3), that provision still does not allow the Secretary of Labor to sue for recovery on behalf of individuals. Another subsection, § 502(a)(5), is parallel to § 502(a)(3) and provides a general cause of action to the Secretary. Subsection 502(a)(5) allows a civil suit "by the Secretary (A) to enjoin any act or practice which violates any provision of this title, or (B) to obtain other appropriate equitable relief . . . ."\(^{199}\) Until recently, this subsection would not have been interpreted to provide recovery for individual participants, but the Supreme Court's reasoning in \textit{Varity} opens that door as well.\(^{200}\)

In \textit{Varity}, the Court noted Congress' 1989 addition of ERISA § 502(l), dealing with the calculation of certain civil penalties.\(^{201}\) Subsection 502(l) takes account of amounts "ordered by a court to be paid by such fiduciary . . . to a plan or its participants and beneficiaries in a judicial proceeding instituted by the Secretary under subsection . . . (a)(5)."\(^{202}\) The Court concluded from the language of this amendment that in the future "the sort of relief provided by both subsection (5) and, by implication, subsection (3), would include an award to 'participants and beneficiaries,' rather than to the 'plan,' for breach of fiduciary obligation."\(^{203}\) The Court assumed that Congress intended to provide recovery to individuals for breach of fiduciary duty in suits brought either by individuals or by the Secretary of Labor.\(^{204}\)

The \textit{Time Warner} case marks the first time the Secretary of Labor has taken advantage of this opening.\(^{205}\) In response to the suit, Time Warner stated that the Department of Labor's actions "are unprecedented and represent a clear departure from the DOL's longstanding recognition of the limits of its jurisdiction."\(^{206}\) The suit is unprecedented, but after the Supreme Court's opinion in \textit{Varity}, the Department of Labor has some

\(^{198}\) \textit{Id.} at 513.

\(^{199}\) ERISA § 502(a)(5). This subsection is parallel to § 502(a)(3), except that § 502(a)(5) does not provide a cause of action for violation of the terms of the plan or to enforce the terms of the plan.

\(^{200}\) \textit{516} U.S. at 510.

\(^{201}\) \textit{See id.}

\(^{202}\) ERISA § 502(l)(2)(B).

\(^{203}\) \textit{Varity}, 516 U.S. at 510.

\(^{204}\) \textit{See id.}

\(^{205}\) \textit{See Herman v. Time Warner Inc.}, 56 F. Supp.2d 411, 418 (S.D.N.Y. 1999) (quoting \textit{Varity}, 516 U.S. at 511 ("a plan administrator engages in a fiduciary act when making a discretionary determination about whether a claimant is entitled to benefits under the terms of the plan documents")).

\(^{206}\) \textit{See White, supra note 175.}
rationale for its action.

The Department of Labor can claim statutory authority to bring suit under ERISA § 502(a)(5), but it remains questionable whether the Time Warner suit is what Congress and the Supreme Court intended. Varity involved a gross breach of fiduciary duty. The company persuaded employees to transfer to a new subsidiary with the intention of bankrupting the subsidiary in order to dispose of benefits obligations. Worker misclassification suits have traditionally been brought under ERISA § 502(a)(1)(B) "to recover benefits due" because they involve not the plan as a whole, but rather the benefits claims of individual workers. In Time Warner, the Department of Labor is recharacterizing a misclassification claim as a fiduciary duty claim.

In Varity, the Supreme Court anticipated that a plaintiff might "repackage his or her 'denial of benefits' claim as a claim for 'breach of fiduciary duty,'" but it discounted the possibility that such a change in procedure would have any effect on decision making by plan administrators. The Court implied that the deferential standard of Firestone should apply to fiduciary duty claims as well as to denial of benefits claims. It noted that the Firestone standard of review for benefits eligibility decisions was based on the same principles of trust law that govern review of fiduciary conduct. Nonetheless, where plaintiffs are allowed to bring claims for denial of benefits under the fiduciary duty provisions of ERISA, plan administrators are denied the opportunity to determine eligibility and the determination is made in the first instance by the district court.

Perhaps in anticipation of possible abuses by the Department of Labor, the Court limited the effect of its finding in Varity, referring to the language of § 502(a)(3), which authorizes "other appropriate equitable relief" for breach of fiduciary duty. The Court suggested that relief under § 502(a)(3) would not be "appropriate" where recovery is available through other ERISA provisions. The Court granted relief to Varity's

207. See 516 U.S. at 498.
208. See id. at 493-94.
209. See 56 F. Supp.2d at 418. The district court rejected Time Warner's argument "that the government's breach of fiduciary duty claim is in reality an impermissible claim for benefits . . . " Id. The court accepted the Department of Labor's argument that the plans themselves may have been damaged by Time Warner's failure to include certain workers. See id. Ironically, the court held that by not seeking "to restore specific benefits to particular workers," id. at 418 n.3, the Department of Labor had properly "alleged injury to the plans." Id. at 418. This approach allows the Department of Labor to bring suit against any company that utilizes any workers who are not provided full employee benefits.
210. Id. at 513.
211. See id. at 514-15.
213. See Varity, 516 U.S. at 515.
employees under § 502(a)(3) only because they would otherwise have been
denied a remedy.\textsuperscript{214} Time Warner's freelancers would not have been denied
a remedy in the absence of the Department of Labor's suit.\textsuperscript{215} They could
have requested benefits from the plan administrator. Had the plan
administrator refused, they would have had a colorable claim for denial of
benefits under § 502(a)(1)(B), and could have brought suit on their own
behalf.\textsuperscript{216} Given the availability of recovery to the individual workers
under § 502(a)(1)(B), the Department of Labor should not have been able
to bring suit under § 502(a)(5).

Alternatively, the freelancers, like the transferred employees in \textit{Varity},
could have bypassed review by the plan administrator and brought suit
under § 502(a)(3) for breach of fiduciary duty. However, if they had
brought suit under § 502(a)(3) when they could have brought suit under §
502(a)(1)(B) for denial of benefits, the Supreme Court's reasoning in \textit{Varity}
would demand that a court "respect the 'policy choices reflected in the
inclusion of certain remedies and the exclusion of others''\textsuperscript{217} in the statute
and dismiss the case. \textit{Time Warner} is distinguishable from \textit{Varity} because
the freelancers in \textit{Time Warner} did not pursue benefits on their own behalf,
either under the ERISA provisions for denial of benefits or under those for
breach of fiduciary duty.

The Department of Labor is pursuing yet a third alternative by filing
suit under § 502(a)(5) on behalf of the freelancers. The Supreme Court in
\textit{Varity} intended to provide a remedy of last resort for a group of employees
who were the victims of fiduciary malfeasance and who would otherwise
not have had a remedy. The Court did not intend to provide a menu of
remedies for workers to defeat employer discretion in deciding eligibility
for benefits. Nor could it have intended to provide a means for the

\textsuperscript{214} See id.; \textit{Time Warner}, 56 F. Supp.2d at 417 ("The government may rely on the
catchall provision [of § 502(a)(5)] if the equitable relief required for complete relief is
unavailable under the other provisions in the statute.") (citing \textit{Varity}, 516 U.S. at 512).

\textsuperscript{215} The district court disagrees: "governmental action is appropriate here. Misclassified
employees, for example, may not even know that their rights under ERISA might have been
violated, a great many employees may have been affected, and the public also may have a
strong interest in the issues presented." \textit{Time Warner}, 56 F. Supp.2d at 417-18. Under this
reasoning the Department of Labor need only allege that workers who might have been
eligible might have been denied benefits had they requested them.

\textsuperscript{216} See id. at 418. The district court held that individuals claiming to have been
misclassified need not exhaust their administrative remedies because the employer would
deny them access to the process as ineligible individuals anyway. The court misunderstands
the administrative process. A worker is not required to be eligible for benefits before
applying to the plan administrator for benefits. See ERISA § 503 (requiring the plan
administrator to give a "participant" reasons for refusal of benefits and to provide a
procedure for review); see also \textit{Firestone Tire & Rubber Co. v. Bruch}, 489 U.S. 101, 117
(1989) (holding that "participant" includes a claimant who has "a colorable claim that . . . he
or she will prevail in a suit for benefits.").

\textsuperscript{217} \textit{Varity}, 516 U.S. at 515.
By bringing suit under the fiduciary duty requirements of ERISA, the Department of Labor is attempting to bypass the usual review process applied to individual claims. By repackaging a denial of benefits claim as a fiduciary duty claim the Department of Labor is attempting to deprive the plan administrator of the discretion to determine eligibility for benefits and to construe the terms of the plans. The courts have made it clear that ERISA should not be interpreted to compel employers to extend benefits to unintended classes of workers. The Department of Labor's action in *Time Warner* is an attempt to compel an employer to provide benefits to an unintended class of workers without review by the employer's plan administrator and in the absence of a complaint by the workers themselves. Neither Congress nor the Supreme Court could have intended to grant that authority to the Department of Labor.

V. CONCLUSION

ERISA was passed in 1974 for the purpose of promoting the growth of voluntary employee benefit programs. That purpose has survived twenty-five years of change in the workplace. That same time period has seen dramatic growth in employee participation in pension and welfare benefit plans. Congress chose to promote this growth by allowing employers the freedom to structure work arrangements and to classify workers for purposes of benefits. Congress has likewise refrained from closely regulating the temporary help industry and has allowed the development of new, more flexible staffing alternatives without mandating benefits.

The courts have recognized and supported Congress' purpose by allowing employers discretion in drafting and interpreting employee benefit plans. The Supreme Court set the standard in *Firestone* by finding that the terms of the plan are paramount and that, where the plan so provides, the plan administrator's discretion will prevail. While plan interpretation is a complex task, recent cases reinforce the principle of employer discretion.

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218. The Department of Labor has also asked the court to appoint an independent fiduciary to audit Time Warner's plans. See *Time Warner*, 56 F. Supp.2d at 415; *Independent Contractors: Time Warner Misclassified Employees Due Benefits, Labor Department Charges*, BNA EMPLOYMENT POL'Y & L. DAILY, Oct. 29, 1998, at d11. This amounts to enforcement overkill. Such a measure has been taken in the past only in cases where the plan fiduciaries presented an ongoing threat to the integrity of the fund. See *Donovan v. Bierwirth*, 680 F.2d 263 (2d Cir. 1982) (finding appointment of independent investment manager unnecessary where plan trustees had used $44 million of plan funds to ward off a takeover, resulting in an $11.8 million loss); *cf. Donovan v. Mazzola*, 716 F.2d 1226 (9th Cir. 1983) (appointing investment manager where plan trustees made over $1.5 million in unsecured loans and paid $250,000 to a crony for a "feasibility study").
The Department of Labor's suit against Time Warner is an attempt to turn away from the intention of Congress in enacting ERISA and to reverse the direction of the courts in promoting employer discretion. Congress granted that discretion under ERISA in 1974, and neither Congress nor the courts have seen fit to withdraw it. The Department of Labor should not be allowed to supplant employer discretion either, and should not be able to dictate eligibility for benefits by threatening employers with lawsuits for supposed misclassification of workers.