The Equal Employment Opportunity Commission (“EEOC”) issued proposed regulations on July 14, 2003, that would permit employer-sponsored retiree health plans to reduce or eliminate the benefits for Medicare-eligible retirees without running afoul of the Age Discrimination in Employment Act of 1967 (“ADEA”). The proposed rule is a reversal of the position that the EEOC advocated in a brief submitted in support of the retirees in the Third Circuit’s ruling in *Erie County Retirees Ass’n v. County of Erie*, 220 F.3d 193, 210-11 (3d Cir. 2000), *cert. denied*, 121 S. Ct. 1247 (March 5, 2001). In that case, the EEOC argued, and the Third Circuit held, that a retiree health plan presumptively violates the ADEA if it makes distinctions based on the retiree’s eligibility for Medicare.

**Background – Erie County Decision and its Aftermath**

The *Erie County* case arose when cost increases caused Erie County, Pennsylvania to change the health coverage for its retirees. The county provided retirees who were eligible for Medicare with coverage under an HMO, while retirees who were not yet eligible for Medicare were covered under a point-of-service plan that combined the features of an HMO with those of a traditional indemnity plan. The Medicare-eligible retirees brought suit against the county, arguing that the county had violated the ADEA by placing them in the HMO-only plan. The U.S. District Court for the Western District of Pennsylvania concluded that the county was entitled to summary judgment on its claims because the legislative history of the ADEA indicated that the ADEA was not intended to apply to retirees.

The Third Circuit reversed the lower court, holding that the retirees were entitled to ADEA’s protection, even though they were no longer employed. This portion of the decision is significant, because it contradicts the prevailing view that the ADEA does not apply to retirees.

The Third Circuit also found that, because an individual becomes eligible for Medicare upon reaching age 65, Medicare eligibility is a direct proxy for age. Specifically, a distinction based on eligibility for Medicare is the same as a distinction on the basis of age. Under the ADEA, once it has been determined that a distinction has been based on age, it is necessary to determine whether an exception to the rules permits that distinction to be made. The only
exception potentially relevant in this case was the “equal benefit or equal cost” standard, under which an employer must either provide equal benefits to older and younger workers, or must incur the same costs for benefits on behalf of older and younger workers.

Accordingly, the Third Circuit remanded the case to district court to determine whether Erie County satisfied the “equal benefit or equal cost” exception. The Third Circuit held, however, that Erie County could not take any credit for the costs Medicare incurs in providing benefits. By barring consideration of Medicare costs, the decision in *Erie County* effectively precluded an employer from relying on the equal cost rule in evaluating distinctions in retiree health benefits depending on a retiree’s eligibility for Medicare. In addition, on remand, the district court ruled that Erie County’s program did not pass the “equal benefit” exception to the ADEA for several reasons. *Erie County Retirees Ass’n v. County of Erie*, 140 F.Supp.2d 466 (W.D. Pa. 2001).

Erie County was therefore required to provide the same benefits to Medicare-eligible retirees and pre-Medicare retirees. Given the economic climate and the spiraling costs of health care, the county achieved parity between the Medicare-eligible retirees and pre-Medicare retirees by reducing the benefits of the pre-Medicare retirees. As a result, the pre-Medicare retirees were required to pay more for health benefits that offered fewer choices.

The Third Circuit’s reasoning in the *Erie County* case followed the reasoning proposed by the EEOC in an *amicus curae* brief. In October 2000, the EEOC incorporated the Third Circuit’s position in its “Compliance Manual” as part of the agency’s national enforcement policy on the ADEA. However, in August 2001, the EEOC announced that it wanted to study the relationship between the ADEA and employer-sponsored retiree health plans further, and it rescinded those portions of its Compliance Manual that discussed the *Erie County* decision.

**EEOC’s Position in the Proposed Regulations**

Under the ADEA the EEOC has the authority to issue reasonable exemptions that the EEOC finds “necessary and proper in the public interest.” 29 U.S.C. § 628. The EEOC used this authority to propose a narrowly-drawn exemption, in the form of the proposed regulations, to permit the practice of coordinating employer-provided retiree health coverage with eligibility for Medicare.

Thus, the proposed regulations state that it is not a violation of the ADEA to alter, reduce or eliminate health benefits for retirees when the participant becomes eligible for Medicare health benefits or comparable State health benefits. No other aspects of ADEA coverage and no employee benefits other than retiree health benefits are affected by the proposed regulations.

An Appendix to the proposed regulations makes clear that the exemption is also intended to apply to dependent and/or spousal health benefits that are included as part of the health...
benefits provided to retirees. However, dependent and/or spousal benefits need not be identical to benefits provided to retirees; thus, dependent and/or spousal benefits may be altered, reduced or eliminated, regardless of whether the health benefits for retirees are similarly altered, reduced or eliminated.

The proposed exemption, which the EEOC intends to apply to existing and newly-created employer-provided retiree health plans, is proposed to be applicable on the date of publication of a final rule in the Federal Register. Thus, employers that are within the states covered by the Third Circuit – which includes Pennsylvania, New Jersey, Delaware and the Virgin Islands – or that have retirees within these areas are, for now, still subject to the standards set forth in the Erie County decision. However, given that the EEOC has withdrawn its enforcement guidance and issued the proposed regulations, we believe that the practical effect in the interim period before publication of final rules is that the EEOC will not enforce the Erie County decision as it applies to retiree health plans that are coordinated with Medicare.

If you have questions concerning this memorandum or the proposed EEOC regulations regarding the exception to the ADEA, please contact any of the following members of our Employee Benefits and Executive Compensation practice.

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