OFFICIAL TRANSCRIPT

PROCEEDINGS BEFORE

THE SUPREME COURT

OF THE

UNITED STATES

CAPTION: HUGHES AIRCRAFT COMPANY, ET AL., Petitioners v.

STANLEY I. JACOBSON, ET AL.

CASE NO: No. 97-1287 C-2

PLACE: Washington, D.C.

DATE: Monday, November 2, 1998

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Supreme Court U.S.

IN THE SUPREME COURT OF THE UNITED STATES

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HUGHES AIRCRAFT COMPANY, :

ET AL., :

Petitioners :

v. : No. 97-1287

STANLEY I. JACOBSON, ET AL. :

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Washington, D.C.

Monday, November 2, 1998

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 10:02 a.m.

APPEARANCES:

PAUL T. CAPPUCCIO, ESQ., Washington, D.C.; on behalf of the Petitioners.

LISA BLATT, ESQ., Assistant to the Solicitor General, Department of Justice, Washington, D.C.; on behalf of the United States, as amicus curiae, supporting the Petitioners.

SETH KUPFERBERG, ESQ., New York, New York; on behalf of the Respondents.

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PROCEEDINGS

(10:02 a.m.)

CHIEF JUSTICE REHNQUIST: We'll hear argument first this morning in Number 97-1287, Hughes Aircraft Company v. Stanley Jacobson.

Mr. Cappuccio.

ORAL ARGUMENT OF PAUL T. CAPPUCCIO

ON BEHALF OF THE PETITIONERS

MR. CAPPUCCIO: Thank you, Mr. Chief Justice, and may it please the Court:

The nub of this case, I believe, is that the post termination surplus asset allocation rules buried in section 1344(d) of ERISA cannot become the tail that wags the rest of the statute. Those rules do not create an entitlement that restricts the legitimate uses to which surplus plan assets, or any plan assets, can be put, but that is how the respondents would have it in this case.

The respondents do not contend that they have not received every benefit that they were ever promised under the Hughes pension plan.

QUESTION: This is a defined benefit plan, Mr. Cappuccio?

MR. CAPPUCCIO: Yes, Your Honor.

QUESTION: And your point is that they have received the benefits defined under the plan?

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MR. CAPPUCCIO: That's correct, Your Honor. In a defined benefit plan, the employee takes no risk that the plan will not perform well. Rather, the employee is guaranteed from day 1, Justice O'Connor, that he or she will receive fixed benefits that are at least equal to all of his or her contributions.

QUESTION: And I suppose under that plan there might be a deficit instead of a surplus.

MR. CAPPUCCIO: There certainly may well be, Your Honor. That's absolutely right.

QUESTION: And the theory of the court below, if there were a deficit, would be what?

MR. CAPPUCCIO: I think the theory of the court below would be that the employer would have to make up the difference, which is, in fact, how a defined benefits plan works, so I think what your question points out, Your Honor, is the theory of the court below in a sense creates a defined contribution plan with a defined benefits floor, which as Judge Easterbrook --

QUESTION: Are these defined benefit plans becoming used less often in today's world? Is this -- are they almost extinct as a species, or still exist?

MR. CAPPUCCIO: I think they're still very much around, Your Honor. I think the general trend is to move towards defined contribution plans, and also to move away

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from contributions to defined benefit plans, and I think the reason for that is as a general sense today that employees want to invest their own money. For example, in this case Hughes has a 401k plan, so if they're not contributing they can take that extra money and put it into the 401k plan, and --

QUESTION: If this were a voluntary plan, then would the employees be entitled to all the benefits?

MR. CAPPUCCIO: There is a provision in section 1054 of ERISA that provides if you are allowed to make voluntary contributions over and above the mandatory contributions, that you vest in those also, but here the contributions are mandatory. The mere fact that at --

QUESTION: They're man -- after the amendment they were not mandatory because you could go to the other side. You could go to the other side of the plan.

MR. CAPPUCCIO: I would disagree, Justice Kennedy. The mere fact that on one day you have a choice whether or not -- which plan to be in doesn't then make the contributions voluntary once you select that plan. I mean, it's voluntary only in the distant sense that you could decide to be an employee or not an employee. That doesn't --

QUESTION: You had to make the election at one time and then you were -- you couldn't reelect to go under

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the noncontributory --

MR. CAPPUCCIO: I believe that's correct, Your Honor. I believe it was a one-time election, and it certainly --

QUESTION: Mr. Cappuccio, did you mean to say, which plan you choose to be in?

MR. CAPPUCCIO: I'm sorry. I meant to say which benefit structure --

QUESTION: I see.

MR. CAPPUCCIO: Let me take that one on --

(Laughter.)

MR. CAPPUCCIO: -- directly, and that is that it's alleged in this case that somehow a factual issue has been raised because one of our employees at one point referred to this as the new plan, okay.

People speak in colloquial terms all the time, I think that's a good thing, and people use the word new when they mean amended. I had that -- not only have I had the slip here at the podium, Justice Stevens, but when I was preparing for this case I wanted to see what ERISA said before and after the 1986 amendments, and I said to my associate, can you get me the statute, and he said to me, well, here's the old statute, here's the new statute, and I said, well, it's a good thing we're not in the Ninth Circuit. You would have just created a question of fact.

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But I think the point is is that 1) we're not bound by colloquialisms like that, and second, people say new when they mean amended all the time, and the case can't turn on that.

QUESTION: Well, if you could change from the contributory to the noncontributory at any time, then it would look more like a voluntary plan.

MR. CAPPUCCIO: No, Your Honor, I don't think the fact that you could even -- which is not this case, that you could switch back and forth, would make the contributions any less mandatory.

It would still, if you're going to participate in this plan, they would be mandatory contributions, and therefore under section 1053 and 1054 you would only vest in your contributions plus the statutory interest rate and not in all the upside, and anything else, Your Honor, transforms this plan and any other defined benefits plan into exactly what Justice O'Connor pointed to, which is a defined benefits, defined contribution floor, a benefits floor with a defined contribution upside, and that really I think wrecks the basic dichotomy that is in the statute.

QUESTION: Mr. Cappuccio, is this kind of amendment commonplace, or is it extraordinary, that you go from a contributory plan to one in which there are no contributions?

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MR. CAPPUCCIO: Justice Ginsburg, I think it's quite common. In fact, I think it's the usual amendment these days. I know in this case it's the same way that the union plan went, that the employer and the union in the bargaining plan -- remember, we have the nonbargaining plan here.

In the other plan, the union and the employer agreed to go from a contributory structure to a noncontributory structure, and again, I think it's because it's a sense by employers that they want to give employees some choice in how to invest their money, and at least when the stock market was doing well, that employees had a lot of other options that they wanted to avail themselves of.

Whether in light of the last, you know, 6 months, people are still going to be doing that, is another question, but that just shows you that there could have well been a downside here.

QUESTION: You make the point that in amending the plan you are not acting as a fiduciary and that what Spink held, but is there any -- any control over what legitimately constitutes an amendment to the plan?

MR. CAPPUCCIO: Justice Ginsburg, there's -- certainly to say that the -- the answer is yes. The -- to say that the employer is not a fiduciary in amending the

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plan is not to say that the employer has discretion to do whatever he wants, whatever it wants.

The employer is still bound by the substantive provisions of ERISA that apply whether or not one is a fiduciary, which we would concede include the anti-inurement provision here, and also the vesting and nonforfeitures, forfeiture provisions and the asset distribution provisions, so to say that one is not a fiduciary here just means to say that the amendment must comply with the rest of ERISA, but -- and to say but there's no broader duty that exists out there.

And of course, if there were a broader duty to plan participants it would be a sort of, a hopelessly conflicting situation, right, because the employer would be under conflicting fiduciary duties.

When we're deciding how to structure the benefit program for active employees and retired employees, to whom do we owe the fiduciary duty. Is it to the active employees, to the retired employees, is it also to our shareholders?

You can't have that sort of conflicting fiduciary duty, which is one of the reasons why this Court held in Spink that in designing a plan or amending the design of a plan the employer is acting as a plan sponsor.

QUESTION: What was the case you just referred

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to?

MR. CAPPUCCIO: I'm sorry. Spink v. Lockheed, which was decided 2 years by this Court, reversed in the Ninth Circuit.

QUESTION: Mr. Cappuccio, am I right in my understanding that there is no finding here that the assets transferred for the benefit of the new noncontributory option are themselves attributable to contributions by the employees under the plan as originally drafted?

MR. CAPPUCCIO: That's right, Your Honor, there's no such finding.

QUESTION: What if there were? Would your position be different?

MR. CAPPUCCIO: My position, Your Honor, would not be any different, because my position is that this is a defined benefits plan, and even if the employees had made all the contributions, okay, the deal would still be the same. They would be guaranteed that they would get back at least those contributions plus a statutory interest rate as a floor. In fact, the defined benefits were set significantly higher --

QUESTION: Uh-huh.

MR. CAPPUCCIO: -- okay. But having been guaranteed that rate of return, they would not be entitled

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to the surplus.

In my world, Justice Souter --

QUESTION: They're guaranteed more than the right of return. They're also guaranteed the promised benefits, which are a good deal higher than that.

MR. CAPPUCCIO: That's exactly right, Your Honor. I said that -- I misspoke, that the floor is their contributions plus their rate of return, but --

QUESTION: The floor of what must be guaranteed.

MR. CAPPUCCIO: The floor of what must be guaranteed, but in fact the defined benefits are -- although I don't have the particulars here are regularly significantly above that.

Justice Scalia, the way I like to think about it is, these people are promised, like, one or two standard deviations off performance, or good performance, and what they give up for that is the possibility of bad performance, or three or four standard deviations, and that's a perfectly fine deal and, frankly, it's one I wish I had over the last 6 months.

QUESTION: So basically, to use a term that has come up in the briefs, I guess the only real difference between this and an insurance policy is the consequence on dissolution, on termination.

MR. CAPPUCCIO: Well, I guess I'd be somewhat

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hesitant to say it's exactly the same, Justice Souter, because, of course, an insurance policy is not backed up by the Government, as this is here, and there are other restrictions that ERISA places on the use of funds that I believe are not on an insurance company, but with those qualifications it would be similar, that's right.

Let me address just briefly the nonfiduciary claims brought by the respondents, the claims that do not depend on a fiduciary duty, the anti-inurement vesting and post termination asset distribution claims.

We go over in the briefs that these fail for a variety of reasons, but I'd like to focus the Court today on I think what the one silver bullet is that will kill every one of those claims without having to decide anything else, and that is the one plan, two plan issue, for unless the respondents can defend the holding by the court of appeals that it's an open question of fact whether there is one plan or two plans here, then all of their claims implode.

Because, of course, if there's one plan here there can't be any anti-inurement violation, if there's one plan here, even if you let them prevail on their ambitious duty to terminate claim, there can't be a wasting trust, because people are still coming into the plan, and they're vesting and forfeiture claim would also

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fail.

Now, the court of appeals held that it was a disputed issue of fact whether it was one plan or two. It is not. That is, as Judge Norris pointed out in his dissent, an erroneous conclusion of law disguised as a question of fact.

The relevant facts in this case are undisputed. They are, what are the particular changes that Hughes made to the plan, and the fact that at least on the face of the documents those changes are structured as an amendment rather than as a second, separate plan.

Framed correctly, the relevant legal question becomes, is there anything in the law that prevents Hughes from structuring the transaction the way they did, and deems what Hughes did two plans as a matter of law, and the answer to that is plainly no. Respondents have not pointed to anything in ERISA or anywhere else that would limit -- that would prevent Hughes from doing this as an amendment.

By the way, these are always done as amendments. All one has to do is look at the plan in this case to see that it's a series of about six amendments.

And to the contrary the Government has at least two regulations on point that specifically allow a single plan to have multiple benefit structures. The Department

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of Labor has a regulation to that effect, and the IRS has a regulation to that effect, both of which are cited in our briefs.

Indeed, the same IRS regulation that allows multiple benefit structures says that a plan is a single plan when on an ongoing basis all of the plan assets are available to pay benefits to employees who are covered by the plan. In other words, is there a single pool of assets?

I will defer to the Solicitor General's Office on the reasons for the single asset test, but I believe them to be that the Government thinks it's important to focus on a single pool of assets for purposes of determining whether the minimum funding requirements, which are the real protection in ERISA, are met in any case and also, I would suppose, that the single pool of asset test furthers the important Government interest by encouraging employers to do just what we did here, which is to have multiple benefit structures with one single pool of assets and thereby pool and reduce risk.

But in any event, whatever the reasons for that, it's a Government regulation and under that Government regulation we clearly have one plan here.

Now, the rule advanced by the respondents as to whether there's one plan or two plans, that some lay fact-

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finder from California, I suppose, years after the fact is going to determine whether the changes to the plan exceeded some unspecified level of significance, is, I would submit, the worst and most destabilizing possible rules.

It is not only inherently arbitrary, but it's wildly destabilizing of our pension system. It would call into question as a possible anti-inurement violation any routine amendment that the employer made either increasing or changing benefits for some group of employees, or adding a new category of participants.

It would thus deprive both employers and employees alike of the very security that ERISA is intended to encourage and promote and, of course, it would become doubly destabilizing when combined with petitioner's termination claim, since it could turn out that years after the fact there was an unwitting termination and suddenly people who thought they were accruing benefits find out that they were not accruing benefits.

Let me just very briefly, as I'm cutting into my rebuttal time, address the termination claim. Respondents have completely abandoned the only termination claim that they brought in their complaint. Count IV of their complaint alleged that Hughes was in violation of ERISA's

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post termination asset distribution provision, section 1344, because Hughes had in fact "effective January 1, 1991" terminated the plan.

The court of appeals reversed the district court's dismissal of that count on the ground that there was a disputed issue of fact as to whether in fact the plan had terminated in 1991.

In this Court -- I think it's very significant, in this Court the respondents do not even attempt to defend either the holding of the court of appeals, or the count they brought in their complaint. They now concede that the only way to have a termination, at least the only means to have a termination, is through the procedures of section 1341 and 1342 of the statute, and they concede that no such termination has occurred here.

They now contend that, quote, the relevant issue for this Court is whether Hughes can be ordered on a going-forward basis to use those procedures to terminate the plan, but the respondents never brought any such duty to terminate claim. Nowhere in their complaint is any duty to terminate alleged, and nowhere in their complaint is any cause of action to enforce that duty identified.

Rather, the only claim that they brought was a claim for a violation of the asset distribution provisions. That requires that there had been a

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determination. They now concede that there's not. There is nothing more for this Court to do than to affirm the district court's dismissal of the complaint.

Thank you, and if I could, I'll save the balance of my time.

QUESTION: Thank you, Mr. Cappuccio.

Ms. Blatt, we'll hear from you.

ORAL ARGUMENT OF LISA S. BLATT

ON BEHALF OF THE UNITED STATES, AS AMICUS CURIAE, SUPPORTING THE PETITIONERS

MS. BLATT: Thank you, Mr. Chief Justice, and may it please the Court:

I would first like to address the contention in this case that Hughes created a new benefit structure that constitutes a different plan under ERISA. We disagree with that contention for two reasons. First, as reflected in a Department of Treasury regulation, it is the position of all three agencies responsible for enforcing and administering ERISA that a single plan may contain multiple benefit structures as long as all plan assets are available to pay benefits to all plan participants.

That principle furthers ERISA's fundamental goal that there is a restricted asset pool that is sufficient and available to satisfy the employer's promise to pay benefits. The principle also reflects the employer's

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general discretion over plan design decisions.

Second, the factual circumstances test advanced by respondents would be unworkable, because it would call into question any plan amendment that either raises benefits for some but not all of plan participants, or adds a new category of plan participants.

I would also like to address the issue of plan termination. As participants in a defined benefit plan, respondents are entitled to receive both their promised and vested benefits, and there is no allegation in this case that Hughes has deprived any employee of those benefits. Moreover, Hughes bears the entire investment risk under the plan and must comply with ERISA's minimum funding provisions.

The security of respondents' benefits is also protected by title IV's insurance program, but unless and until the plan terminates under the exclusive means of title IV, ERISA does not grant participants in a defined benefit plan a right to a distribution of plan assets, and because it's clear in this case that Hughes has not terminated its plan, the plan is ongoing --

QUESTION: Well, Ms. Blatt, what do you make of the apparently new claim asserted now that the court should order a termination?

MS. BLATT: Well, we don't think that there's

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any basis for implying either the right or the remedy. There's -- it's also our position that even if there was such a basis for reading this common law doctrine into a heavily regulated statute, this is clearly not a common law wasting trust.

Under both benefit structures you've got tens of thousands of employees accruing benefits, and that unquestionably furthers the plan's express purpose to provide pension benefits to eligible employees to stimulate their interest in the company and also to attract them, and far from -- what termination would do is cease those accruals, and all those employees would be without benefits and future accruals, and that would be not only inconsistent with the purpose of the plan, it would be very bad for the purpose of ERISA.

ERISA obviously wants to -- one of the important purposes is to encourage the growth and maintenance of these plans, and there are very, very specific provisions in title IV when a plan can be terminated, and the involuntary termination provisions of section 1342 set forth the criteria for the Government to come in and terminate a plan, and the whole point of even the voluntary termination provisions in section 1341 are to make it more difficult for employers to terminate.

Either the plan assets have to be sufficient to

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pay benefits and all the plan liabilities, or they have to demonstrate economic distress criteria, so it's a quite comprehensive provision and even if there was some -- and there's certainly nothing in the statute that says -- excuse me.

There's no violation that's alleged of the statute that respondents would be trying to get a remedy for, but even if assuming they had an alleged violation, there's no remedy, and so we just don't -- and even if there was a remedy, this wouldn't meet the criteria of a wasting trust.

QUESTION: I take it that your -- the position of the Solicitor General is not significantly different from that of the dissent, is it, Judge Norris' dissent. Is there any difference?

MS. BLATT: Not that comes to mind.

QUESTION: No. Thank you.

MS. BLATT: So basically our point is, it's a good thing that this plan is ongoing, and as long as it's ongoing, the plan assets are available to pay participants, and if -- Justice Souter, if I could just go back to one of your points on, if there's been a transfer here, I mean, because this is one plan there never was a transfer of assets. The assets just remain available under the plan, and the employer can use them to pay

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benefits and make amendments.

In fact, the employer could raise benefits or create an early retirement program like the employer did in Spink and like the employer did here.

QUESTION: Have there been any cases -- have there been any cases in which amendments have been so extensive that the Government has determined there are really two plans? Are there any regulations or cases on that point?

MS. BLATT: No. The restrictions on amendments are similar to what Mr. Cappuccio said. They can't throw the plan into a significant underfunding, they can't violate the anti-inurement provision, and then the key one that's under the regulation is, you have to have a single pool of assets that's available to pay all the benefits, so you can't set up segregated asset pools, but I'm not aware of any amendment that attempted to do that and call it one plan.

And that would be just -- for all, almost all of the provisions of ERISA, for minimum funding, for reporting, for tax qualification, for fiduciary duty provisions, the Government has got to know what a plan is to have a starting point for what a plan is, and what they look to is whether there's a -- what the pool of assets is and what the corresponding liabilities are, and that's the

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way the statute's been administered, and that's reflected in the Department of Treasury's regulation.

QUESTION: Ms. Blatt, I was just going to say, my -- I guess my use of the word transfer was not the right term, but even if there had been a transfer under 1050 -- section 1058, the result would be the same so long as the benefits for the beneficiaries of the plan for which the transfer had been made were covered.

MS. BLATT: Certainly you'd have a case -- if you've set up a separate plan and then merged them, you would have that result. If there's a spin-off it gets a little more complicated, because there are provisions in the tax code that govern how that has to be done.

But the point is --

QUESTION: So far as ERISA itself was concerned, it would be the same result, wouldn't it?

MS. BLATT: For purposes of 1058, there -- I'm not sure what the question is, but you first have to start out, figure out what you're starting with, and all we have here is one plan. If you had -- it might be a different question if you had completely separate plan to begin with, but here we just have an amendment. There's always been one asset pool, and all that Hughes did was amend its plan to make plan assets available to pay benefits to plan participants, so --

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If there are no further questions --

QUESTION: Thank you, Ms. Blatt.

Mr. Kupferberg, we'll hear from you.

ORAL ARGUMENT OF SETH KUPFERBERG

ON BEHALF OF THE RESPONDENTS

MR. KUPFERBERG: Mr. Chief Justice, and may it please the Court:

The nub of this case, as Mr. Cappuccio put it, is Hughes' use of the billion dollar surplus in the contributory plan, which was funded in very large part by the contributions of the employee participants, in order to pay Hughes' separate obligations to a new plan as it initially announced that it was establishing for a virtually completely different group of employees without hardly any overlap, paying completely different benefits.

Mr. Cappuccio in his remarks this morning again referred to it as two plans, Hughes' announcement referred to it as two plans, and announced that a new noncontributory plan would be funded entirely by Hughes.

There was nothing wrong with creating a new noncontributory plan for new employees and nonparticipants in the old contributory plan, but that was a separate plan, as Hughes itself said, to be funded by Hughes, and not to be funded out of contributory plan assets.

QUESTION: Now, Mr. Kupferberg, the Solicitor

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General says all three agencies of Government responsible for this say this was not a new plan.

MR. KUPFERBERG: Well, they said that in their brief, but contrary to what was argued this morning, I don't believe that there's any regulation that says that. On the contrary, the Treasury regulation to which Ms. Blatt referred is a regulation that by its own terms -- it can be found on page 128a of the petition for cert -- by its own terms it refers solely in the context of a merger of two plans.

Indeed, it says specifically that it does not apply unless more than a single plan is involved.

QUESTION: What do you believe the legal test for deciding whether there's a new plan -- obviously, it's of considerable significance.

MR. KUPFERBERG: It is certainly of great significance to this case and, indeed, while Mr. Cappuccio --

QUESTION: I asked you --

MR. KUPFERBERG: The legal test is -- it's a common sense test. The plan is not a define -- the definition in ERISA is a circular definition. It says a plan is either a welfare plan or a pension plan. Beyond that there is no definition.

It is essentially a common sense test, and all

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the circuits --

QUESTION: Well, where does it stem from? What body of law?

MR. KUPFERBERG: The criteria that has been recognized for -- to determine whether a plan exists by virtually all the circuits, beginning with the Donovan v. Dillingham decision of the Eleventh Circuit, are -- look at what the benefits are, look at who the participants are, look at the funding source, look at the mechanism for paying benefits.

QUESTION: And after you've done all that, then --

MR. KUPFERBERG: If those are completely different, we would contend that there are obviously two plans.

QUESTION: So it's an ex post determination in every case, I take it.

MR. KUPFERBERG: It is a determination that must be made in every case. In this case --

QUESTION: But -- and it has to be made after the fact, I suppose.

MR. KUPFERBERG: I'm not sure what you mean by after the fact, Mr. Chief Justice.

QUESTION: Well, if you have those four variables --

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MR. KUPFERBERG: Yes.

QUESTION: -- nobody is going to be able to tell until some, you know, judge or jury --

MR. KUPFERBERG: You can tell -- you can tell right from the terms of these two plans that none of these four variables are the same.

QUESTION: Yes, but --

MR. KUPFERBERG: The noncontributory plan --

QUESTION: May I just interrupt?

MR. KUPFERBERG: Yes, sure.

QUESTION: But suppose you have, as you do in this case, a common pool of assets.

MR. KUPFERBERG: Yes.

QUESTION: Are there any examples you can give us of a common pool of assets with multiple benefit structures which would be more than one plan?

MR. KUPFERBERG: There can be multiple benefit structures in one plan, but those are -- normally all the participants are free to choose which benefit structure they wish to take advantage of.

Here, what Hughes did was to close participation in the contributory plan, say nobody can join after December 1991, and we will take the billion dollar surplus generated from the participant contributions and use it to pay the benefits of what is defined in the new plan -- the

new nonparticipatory --

QUESTION: Well, but suppose --

MR. KUPFERBERG: -- plan by its own terms defines participants as all those except those in the contributory --

QUESTION: Supposing from the outset of the plan they had two classes of employees, one of whom would get one set of benefits and another -- the truck drivers are one, and manufacturing employees another. They get entirely separate benefits, but they -- and the plan is entirely funded by the employer, but -- and there's one pool of assets that covers both sets of benefits. There would be one plan or two, under your view?

MR. KUPFERBERG: If it was entirely funded by the employer, I think that --

QUESTION: Be one --

MR. KUPFERBERG: That would be one plan, or at least --

QUESTION: Supposing it's entirely funded by employee contributions, 10 percent of their wages, say.

MR. KUPFERBERG: If it's entirely funded by employee contributions, we would contend that the anti-inurement provision of ERISA, section 403, which says that the assets of a plan shall never inure to the benefit of the employer, and that even on plan termination those

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assets must be distributed if there is a surplus to the employees who contributed for them, would prevent the employer from taking the money, paid in by one group of --

QUESTION: Well, but that's a long answer. Are you saying that makes it two plans, or is it one plan?

MR. KUPFERBERG: I think that certainly on a motion to dismiss, which this was, it would be two plans --

QUESTION: Well -- no, I -- you --

MR. KUPFERBERG: If it's a factual question --

QUESTION: I've given you the facts. I've given you the facts. There's an original plan set up, and say there's a joint contribution, some by the employer and some by the employee, and there -- one class of employees gets one set of benefits, which is entirely different from the benefits paid to another set. Now, is it one plan or two?

MR. KUPFERBERG: I think on those facts it would be two plans. Our facts are much clearer than --

QUESTION: So the test is whether there are differing sets of benefits.

MR. KUPFERBERG: Differing sets of benefits and different participants, yes.

QUESTION: I don't understand the regulation you quoted. You quoted a regulation --

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MR. KUPFERBERG: Yes.

QUESTION: -- on page 128a.

MR. KUPFERBERG: Yes.

QUESTION: But then you didn't seem to read or refer to its definition. In my copy it says, a plan is a single plan if and only if on an ongoing basis all of the plan assets are available to pay benefits to employees who are covered by the plan and their beneficiaries.

MR. KUPFERBERG: That's correct, Justice Breyer, but -- but --

QUESTION: That's what it says. Now, you agree with that definition.

MR. KUPFERBERG: Well --

QUESTION: Do you agree with the definition, or do you not?

MR. KUPFERBERG: For purposes of this section that is the definition.

QUESTION: I'm sorry, I'm asking you if you agree with that definition.

MR. KUPFERBERG: For purposes of that section, yes.

QUESTION: Yes.

MR. KUPFERBERG: Not for purposes of this case.

QUESTION: Oh. In other words, you're saying that this definition is not a correct definition for

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your -- for what?

MR. KUPFERBERG: For this case.

QUESTION: Why not?

MR. KUPFERBERG: Because that regulation says, for purposes of this section, which deals solely with mergers of plans.

QUESTION: All right. Now can I ask you a different --

MR. KUPFERBERG: There was no contention in this case that there was a merger of a plan.

QUESTION: All right. I have the answer to the question. Now I'll ask you a different question.

MR. KUPFERBERG: Okay.

QUESTION: The different question is, is it conceded that all of the plan assets are available to pay benefits to employees who are covered by the plan?

MR. KUPFERBERG: Hughes is using them for that purpose --

QUESTION: Are you conceding that, yes or no?

MR. KUPFERBERG: No. We say that they are not available --

QUESTION: You are not conceding that. All right. Fine. So you say, in other words, that all of the assets of this plan are not available to pay benefits to employees who are covered.

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MR. KUPFERBERG: We say --

QUESTION: Okay.

MR. KUPFERBERG: That is correct.

QUESTION: Could you refer me to the document in which that -- I guess that may be a disputed issue of fact. Will you refer me to the document in the record that says you do not agree with that, that says, in our plan it is not the case that all the plan assets are available to pay benefits to employees, because I missed that. I didn't see --

MR. KUPFERBERG: I --

QUESTION: I thought that was conceded.

MR. KUPFERBERG: Section 6.5 of the contributory plan said that there shall never be an amendment under which assets of the plan are used for any purpose, other than to pay benefits to participants in this plan. That contributory plan also defines participants --

QUESTION: No, no, what I'm asking for, because I won't be able to take it in orally, could you refer me to the page in the record where it says with, I hope, clarity, that you dispute the factual proposition, or the legal proposition that all of the plan assets are available to pay benefits to the employees?

MR. KUPFERBERG: Justice Breyer, I'm not sure I understand the question.

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QUESTION: I'm saying -- I'm trying to find out -- I read you this.

MR. KUPFERBERG: Yes.

QUESTION: I read all of the plan assets are available to pay benefits to employees. That's what seems to be the definition in the section to which you referred, for purposes of that section.

MR. KUPFERBERG: Right.

QUESTION: So I said, is there a factual dispute, yes or no, as to whether that sentence is satisfied here. You said yes, there is a factual dispute.

MR. KUPFERBERG: That sentence --

QUESTION: So now I'm asking where in the record I can find out that there is that factual dispute.

MR. KUPFERBERG: That sentence would be satisfied if there had been a merger here, but that definition applies only --

QUESTION: No, I'm asking a different -- I won't ask it any more. I --

MR. KUPFERBERG: I'm sorry, Justice Breyer. I'm --

QUESTION: Well, let me try. What he wants to know is, where in the record does it appear that you joined issue with your opponents on that point?

MR. KUPFERBERG: On the --

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QUESTION: Where did you say no, that provision in fact is not satisfied? Where in your pleadings, for example?

MR. KUPFERBERG: The complaint alleges that Hughes created a new noncontributory plan and is improperly using surplus assets of the contributory plan to fund benefits of participants in the new noncontributory plan. That's on -- in the joint appendix on page 26. It's paragraphs 27 and 30 of the complaint.

The nub of the complaint here is that Hughes created a new noncontributory plan, announced that it would be funded by Hughes and then, instead of doing that, took money out of the contributory plan, which under section 403, the anti-inurement provision of ERISA, must be used solely for the purpose of paying benefits to participants in the contributory plan, and is using it to pay a separate obligation to nonparticipants in the plan.

QUESTION: Mr. Kupferberg, suppose at the outset Hughes had written, we now have a contributory plan.

MR. KUPFERBERG: Yes.

QUESTION: We reserve the right to amend that plan to make it noncontributory, at which time all of the people who are then covered would have the choice of one plan or the other, and the new employees would have only the noncontributory plan. Suppose that had all been said

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at the outset, here we have a contributory plan, but we reserve the right to make it noncontributory.

MR. KUPFERBERG: Even if that had all been said at the outset, Justice Ginsburg, we believe it would have been prohibited by the anti-inurement clause, which both Mr. Cappuccio today and the Solicitor General in its brief acknowledge is a substantive provision of ERISA, but in this case, in fact, the contributory plan said just the opposite.

Section 6.5 of the contributory plan said that Hughes has the right to amend the plan provided, however, that there shall never be an amendment under which assets of the plan are used for any purpose other than paying benefits to participants in this plan as defined in this plan, and the plan, the contributory plan defined participants as those paying contributions.

The participants in the new noncontributory plan are completely different people, and --

QUESTION: I'm not sure that I understand what is your answer to my question. Same plant employees, same category of employees.

MR. KUPFERBERG: Right.

QUESTION: The plant says at the outset, employees, we have this plan. We reserve the right to change it, at which time those of you who were here --

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MR. KUPFERBERG: My answer, Justice Ginsburg, is, even if the plan had said that, we would still see a violation of section 403, because an amendment cannot -- or an original plan cannot be in contravention of any provision of ERISA, including the anti-inurement clause, which protects --

QUESTION: But these benefits -- this is only being used for benefits for people who are in this category of employment, so how does that violate the anti-inurement provision?

MR. KUPFERBERG: Well, it would be being used for -- in your hypothetical, I think only for people who were hired after a certain date, or -- unless participation in both, what would then genuinely be too benefit structures, if participation in both benefit structures remained open to everybody, that might be a different question, but I'm not sure if you were --

QUESTION: Why does it inure to the benefit of the employer if it goes to a separate group of employees, but does not inure to the benefit of the employer if it goes to the current group of employees?

MR. KUPFERBERG: Because under ERISA, under this Court's decision in Lockheed, it's proper for a plan to pay benefits to participants in that plan. That is not a violation of ERISA.

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But to take money from the plan for a separate --

QUESTION: So the whole argument hinges on your assertion that there are two plans.

MR. KUPFERBERG: Much of the argument does hinge on --

QUESTION: The entire argument, because it's clear that money that is given to employees does not inure to the benefit of the employer for purposes of ERISA. That's the whole theory of it.

MR. KUPFERBERG: Our adversary's argument depends on the proposition that there is just one plan. Over and over I counted 14 times in their brief they said, it's proper for us to pay a new benefit to participants in the plan.

Our contention here is that this is not participants in the plan. This is no different from if Hughes used --

QUESTION: I think that's right. I think they would accept that, that their case hinges on the fact that there's one plan, and yours hinges on the fact that there's two.

MR. KUPFERBERG: If --

QUESTION: Do you acknowledge that if there's -- if there are not two plans, you have no case?

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MR. KUPFERBERG: We think there could be a potential anti-inurement claim if the reversionary interest of employees even in one plan was completely wiped out, but the case is much clearer in that there are, we believe, clearly two plans.

QUESTION: Excuse me. I don't know what you mean, if the reversionary were completely wiped out --

MR. KUPFERBERG: Sec --

QUESTION: Even if they got the defined benefits?

MR. KUPFERBERG: Yes. Sec -- ERISA does not solely protect defined benefits. That's obviously one important purpose of ERISA, but ERISA had other purposes as well.

One of them, which is recognized in section 403, the anti-inurement clause, and in section 1344, is that employees who contribute to a plan in addition to their right to the defined benefit have a reversionary interest if the plan ever terminates in the surplus that was generated by their contributions.

When ERISA was passed, one of the abuses that was on Congress' mind --

QUESTION: Where is that contained?

MR. KUPFERBERG: In ERISA? It's contained in section 403, which refers as an exception to section 1344.

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The -- section 1344 is part of title IV, dealing with termination provisions, with termination of plans.

When ERISA was passed --

QUESTION: But I don't see that the anti-inurement provision, which says that the assets of a plan shall never inure to the benefit of any employer, and held for exclusive -- creates what you call a reversionary interest.

MR. KUPFERBERG: What creates the reversionary interest is section 1344(d). In section 1103 the anti-inurement claims -- I'm sorry, the anti-inurement provision, says that except -- with the following exceptions the assets of a plan shall never inure to the benefit of the employer.

There are two exceptions that are mentioned that I think are relevant here. One is, it refers to a transfer of benefits, a transfer of the assets under section 420 of the Internal Revenue Code.

QUESTION: Which section are you now referring to, Mr. Kupferberg?

MR. KUPFERBERG: 1103, 403.

QUESTION: 1103, yes.

MR. KUPFERBERG: 403 mentions a transfer of assets under section 420 of the Internal Revenue Code. What that refers to is the use of pension plan assets to

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pay health benefits.

The fact that there's an exception here indicates that had there not been this exception payment of health benefits would have been inurement to the employer.

Section 403 also says there's another exception, that inurement to the employer is permitted pursuant to section 1344, which refers to distribution on plan termination, and under certain circumstances under 1344 an employer on termination can take the assets that were generated from its contributions. It can never take the assets generated from the employee contributions.

QUESTION: So in your opinion, then, if a typical company has, let's say, 50 or 100,000 employees, and there are all kinds of different classes of benefit, and one day the employer says, well, I'm going to create another new class of benefit, as it's his right, and it turns out that this new class of benefit, when you work it out actuarially, will be funded in part by money that were he not to create this new class of benefit might have been used by other classes of employees to pay those pensions at some time, or at least they're attributable to those.

Every time that happens, which could be, let's say, on the average of 10,000 times a week across an economy with 240 million people, every time that happens,

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what has happened is there are new plans created, and all the provisions of ERISA that come into play --

MR. KUPFERBERG: No, not every time that happens.

QUESTION: -- all these anti-inurement things --

MR. KUPFERBERG: Not every time that happens.

QUESTION: No. Well then, what's -- when?

MR. KUPFERBERG: We would say that if it could be alleged and shown that there was a sufficiently drastic effect on the plan as it previously existed --

QUESTION: All right. So then, what's the definition of these words, drastic effect? In other words, you're saying if, in fact, there is an attributable surplus at this moment in time -- the stock market changes, of course, but at this moment in time there's a $2 surplus, and so in fact those $2 might help to fund this new class of benefits. That, I take it, is not drastic.

MR. KUPFERBERG: That's correct.

QUESTION: All right. But $20 billion would be.

MR. KUPFERBERG: $20 billion probably would be.

QUESTION: All right. So what we're going to do is involve the Federal courts in deciding what is or is not drastic, and do we just use the word drastic, or is there something else we might use?

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MR. KUPFERBERG: I think that in difficult cases there might be problems drawing the line. Because there are clearly two plans here, I don't --

QUESTION: What's an easy case? Wait, when you say there are two plans --

MR. KUPFERBERG: This --

QUESTION: You can't say there are two plans at the moment. What we're looking for is the defining legal characteristic that tells us whether there are two plans, and right now it seems to me to hinge on the word drastic.

MR. KUPFERBERG: We --

QUESTION: So what I'm asking you is, what's the definition of drastic? How do we deal with that?

MR. KUPFERBERG: I think that with respect, Justice Breyer, I think we can say there are two plans here at the moment, because here the participants, there is virtually no overlap, the benefits are totally different, Hughes itself announced that this was a new plan to be funded entirely by Hughes.

While I agree that there could be difficult problems drawing lines in other cases -- and this is the same kind of argument that is raised in every ERISA case and maybe in every other case. In the Varity Corps. case it was argued that if the intentional misrepresentations here are permitted, then every time a prediction turns out

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to be false, this will wind up in court.

QUESTION: Of course, there is here another way. You say it's up to the employer. He can do what he wants. He pays the employees the benefits he promised them. If he wants to terminate the plan he can. If he doesn't want to, he doesn't have to. Now, what's wrong with that?

MR. KUPFERBERG: What -- there's nothing wrong with that. What is wrong is for the employer to take surplus assets out of the contributory plan and use it to pay a separate debt to a different employee.

QUESTION: Then why isn't your answer the same with the $2 example?

MR. KUPFERBERG: I think a $2 example would be de minimis. If --

QUESTION: Okay, but in principle. In principle, your answer would be the same.

MR. KUPFERBERG: The employer -- if it's taking money out of one plan to pay benefits under a different plan, my answer would be the same, yes.

QUESTION: Mr. Kupferberg, I'm trying to find some statutory language that we can talk about here, as opposed to drastic. You rely a lot on section 403.

MR. KUPFERBERG: Yes.

QUESTION: Where is that contained in the materials? I don't find it in the appendix.

MR. KUPFERBERG: Section 403 is found at page 90a of the petition for cert, it can be found.

QUESTION: 90a, but it's not in the appendix --

MR. KUPFERBERG: I -- it's not in the appendix. It is quoted in --

QUESTION: -- which is entitled, Pertinent Statutory Provisions?

MR. KUPFERBERG: I believe the pertinent statutory provisions are in the petition for cert. I don't think they were repeated in the joint appendix. At any rate, I didn't write the page number down.

It's also, I believe, quoted a number of times in the briefs. It says there --

QUESTION: May --

MR. KUPFERBERG: It has much more absolute language than drastic. It says, shall never inure to the benefit of the employer.

QUESTION: May I just ask, your case really boils down to a claim that the word participants in 6.5(b) does not include the people who would benefit from what we've described as a second plan?

MR. KUPFERBERG: That's correct --

QUESTION: Yes.

MR. KUPFERBERG: And that's the way it's defined in the plan.

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QUESTION: And is the term participant defined in the trust instrument?

MR. KUPFERBERG: Is it defined in the contributory plan? Yes, it is, Your Honor.

QUESTION: In the definitions section, is it or it isn't?

MR. KUPFERBERG: Yes. It's -- we quote it in our brief on page --

QUESTION: It's not in the --

MR. KUPFERBERG: It's section 1.45 of -- I'm sorry, Your Honor. It's quoted on pages 4 to 5 of our brief, I believe.

QUESTION: Page 4 to 5 of the red brief?

MR. KUPFERBERG: Of the red brief, that's correct.

QUESTION: A participant is any person included in the plan as provided, and so forth.

MR. KUPFERBERG: Right.

QUESTION: So it really boils down to the question of whether it's one or two plans, because if it's one plan, then participant does pick up the new people.

MR. KUPFERBERG: I think that's correct.

QUESTION: So your whole case really depends on whether it's one or two plans.

MR. KUPFERBERG: I think on both sides much of

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the case depends on that, yes.

QUESTION: May I ask also on your anti-inurement argument, supposing the plan, jointly funded plan, both employers and employees contribute, has a big surplus, as is alleged this one was, and the sponsor adopted an amendment saying, there'll be no contributions for the next 3 years because there's plenty of -- the actuaries have told us there's plenty of money in the fund. Would that violate the statute?

MR. KUPFERBERG: Probably not, certainly not as clearly as what we allege happened here.

QUESTION: Why would that provide any greater benefit for the employer than this does?

MR. KUPFERBERG: Because the employer here is taking money out of the plan --

QUESTION: No, it's having -- the plan pays these people. That's the taking out you're talking about.

MR. KUPFERBERG: Yes.

QUESTION: No money ever goes into the employer's general funds.

MR. KUPFERBERG: But this was money that the employer had promised to pay out of its own assets.

QUESTION: Well, but there is -- it has used its own assets to create a fund that's adequate to pay off all the defined benefits.

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MR. KUPFERBERG: It has not contributed anything to the new noncontributory plan. It has not contributed anything to either plan since 1986.

It announced in 1990 we're creating this plan to be funded entirely by Hughes.

QUESTION: Well, supposing they --

MR. KUPFERBERG: It didn't say entirely by your --

QUESTION: Supposing then in my example, in addition to saying there'll be no contributions for the next 3 years, they also had a second amendment at the same time, an additional group of employees shall now become eligible for benefits. You just add another 1,000 employees. Would that make a second plan?

MR. KUPFERBERG: Probably not, however, if it added instead of 1,000 employees 1 million employees, so that the whole nature of the plan was being changed, possibly --

QUESTION: But there's enough -- even if there's enough money to pay the million, to pay the benefits for the million? Why is 1 million different from 1,000? I don't understand.

MR. KUPFERBERG: We think there's a fiduciary obligation to consider the reversionary interest recognized by section 1344.

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This case is much easier than that hypothetical precisely because Hughes is not simply making a change of -- in some minor aspect of the plan. It announced that it was creating a new benefit plan for different employees to be funded by Hughes, and it took money out of the surplus of the contributory plan paid for by the participants in the contributory plan --

QUESTION: Mr. Kupferberg, what you described, then, was characterized by Hughes -- it seems quite accurate. You say the fiduciary obligation to protect the reversionary interest, that what you are saying is that this is not a defined benefit program, it is indeed a defined contribution program with a defined benefit floor, this kind of hybrid.

MR. KUPFERBERG: No, Justice Ginsburg. It's a defined benefit plan, but employees have rights beyond simply getting their defined benefit. Again, when ERISA was passed Congress was concerned not only that promises be kept, but the Elgin Watch Company, which had pocketed a surplus that was paid for by employees, that was one of the abuses that Congress was concerned with.

In the Varity Corps case last term it was argued employees got everything they were entitled to under the terms of the plan. Employees -- one important purpose of ERISA is that defined benefits be paid, but it is also an

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important purpose of ERISA, stated in section 403, that money not be taken out of a plan in order to pay an employer's separate obligations, and that is exactly what happened here. Hughes took money --

QUESTION: Well then, in answer to Justice Stevens' hypothetical there is no difference between the 1,000 beneficiaries and the million beneficiaries.

MR. KUPFERBERG: For purposes of the two plan versus one distinction, that's correct, Justice Souter.

In conclusion, again, an employer cannot take money out of a plan meant for, defined as for one group of participants, paid for by those participants --

QUESTION: But -- because I know your basic argument, but if I said, I think a plan is just using the common assets for all the employees, you would say, no, no, that's wrong.

MR. KUPFERBERG: Yes.

QUESTION: For these purposes.

MR. KUPFERBERG: Yes.

QUESTION: And your best authority that you would cite in support of your statement, that's wrong, is what?

MR. KUPFERBERG: Section 403.

QUESTION: But is there any case or anything? Section 403, and what else?

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MR. KUPFERBERG: The Donovan v. Dillingham criteria for when a plan exists are common sense criteria. Donovan v. --

QUESTION: Wait -- section 403 --

MR. KUPFERBERG: Right.

QUESTION: Okay, and what else?

MR. KUPFERBERG: The Donovan v. Dillingham, and there's a line of cases springing from that, recognize the criteria for when a plan exists.

If all those criteria are different, just as if you said the criteria for a piece of music are harmony, melody, and rhythm, if the harmony is different, the melody is different, and the rhythm is different, it's two different pieces of music, and potentially if there was a question of degree that could be decided by the fact-finder in a copyright case.

Here, this is a motion to dismiss. It is up to the district court to hear and determine whether there are two plans, as we contend, and we think the facts will clearly demonstrate that.

The Department of Labor in an interpretive letter, I -- although the Solicitor General obviously has backed away from that, itself recognized that this is a question of fact, whether there's one plan or two.

Mr. Cappuccio in his brief says, well, that

was -- that's different, because here it's all out of one funding source. That was a welfare plan.

Welfare plans are paid out of corporate assets. There was one funding source there.

The plan is a common sense term, there's -- it's not a term of art, and the Donovan v. Dillingham criteria are sensible criteria. If you apply them here, it's clear that there are two plans, and Hughes is taking money out of the contributory plan that was generated by the employees' own hard-earned after-tax money and is using that to pay it's separate obligations to the noncontributory plan.

QUESTION: Termination, do you think termination is a term of art?

MR. KUPFERBERG: Termination is not a term of art, no.

QUESTION: That is not, either.

MR. KUPFERBERG: Term -- I'm sorry, termination is a term that ERISA does define. What we say on termination is that the court can order Hughes to use the means for termination provided in title IV. Our complaint could have been clearer in alleging that.

This complaint was dismissed without leave to amend. If there's any doubt about what we're saying, although we think we've made it clear in briefs in the

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Ninth Circuit as well as here --

QUESTION: Did you argue to the Ninth Circuit that you should have been granted leave to amend?

MR. KUPFERBERG: We did not, because we believe our -- even the original complaint, what was always intended was --

QUESTION: I think you've answered the question. Thank you, Mr. Kupferberg.

MR. KUPFERBERG: Thank you, Chief Justice Rehnquist..

QUESTION: Mr. Cappuccio, you have 3 minutes remaining.

REBUTTAL ARGUMENT OF PAUL T. CAPPUCCIO

ON BEHALF OF THE PETITIONERS

MR. CAPPUCCIO: Very briefly, Justice Breyer, our position of the Donovan line of cases is that first of all it's a court of appeals case, and it only speaks to the issue as to when a promise is sufficiently definite so that it becomes a plan and is covered by ERISA. That's not particularly helpful in determining whether there's one plan.

QUESTION: And the statutory cite for 403 is what?

MR. CAPPUCCIO: The statutory cite for 403 is --

QUESTION: 1103. It's 1103.

MR. CAPPUCCIO: It's 1103(c) on page --

QUESTION: I wish counsel would stick to using either the --

MR. CAPPUCCIO: Yes. It's on page --

QUESTION: -- U.S.C. --

MR. CAPPUCCIO: -- 92a of the -- in the petition.

QUESTION: Right.

MR. CAPPUCCIO: Justice Scalia, or maybe Justice Stevens, I forget, I forget who raised it, on the question of who's a participant, for purposes of the anti-inurement provision, at the very least that would have to be governed by the statutory definition of participant, not the definition in the plan.

I'm going beyond the briefs, because this point hasn't been raised, but ERISA defines participant as any employee or former employee who is or may become eligible, so they are the same participants in this case, because the nonbargaining employees, whether or not they ever contributed, were always able to become eligible by contributing, so for purposes of the statute it's the same group of participants.

Now, I heard today yet another new claim for the first time, which is that somehow this is a breach of section 6.5(b) of the plan. That was a claim not raised

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in the court of appeals, not addressed in the court of appeals, not in the op, not even in the respondent's brief, so that claim is not here, but it would fail anyway.

QUESTION: Except I really think that claim is just another way of stating the basic position there are two plans. That's his argument.

MR. CAPPUCCIO: That's right, and of course nothing would -- 6.5(b) doesn't say we won't make any amendments that affect who's a participant. In fact, anything we do, since the eligibility requirements are incorporated, would affect who's a participant.

That's -- the sort of ultimate irony on the 6.5(b) claim would be that if it prevailed we couldn't pay the respondents' benefits, because section 2.4 of the plan excludes retired employees from the definition of participant. It would just be absurd.

If there are no further questions, I'll submit.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Cappuccio. The case is submitted.

(Whereupon, at 10:59 a.m., the case in the above-entitled matter was submitted.)

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