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the conflict between ERISA and local healthcare reform

AT A GLANCE

In 2007, two different federal courts held that the Employee Retirement Income Security Act (ERISA) pre-empts some version of pay-or-play laws enacted in Maryland and New York. ERISA continues to complicate the states' ability to include employers in efforts to reform health coverage financing.

Persistent inaction by the executive and legislative branches of the federal government on the growing problems of uninsured persons and inadequate funding for Medicaid created a void for healthcare reform that is being filled at the state, county, and city level. The legality of such efforts is placed in doubt by the broad preemptive powers of the Employee Retirement Income Security Act of 1974 (ERISA), which applies to pensions and other fringe benefits such as health care.

A recent preliminary ruling by the Ninth Circuit Court of Appeals sets the stage for a potential "split" in the decisions of the courts of appeal on the preemptive scope of ERISA to state and local health reform initiatives. Should the final decision of the Ninth Circuit create this split, the issue would be ripe for the U.S. Supreme Court to decide the preemption issue near the time that a new federal administration addresses the issue of health reform after a political campaign emphasizing health care as a domestic issue.

The Role of ERISA

Congress enacted ERISA to serve as the primary body of law governing employment-based retirement and health benefits in the private sector. To ensure a uniform regulatory regime over such benefits, and thereby save multistate employers from having to cope with costly and confusing regulatory obligations of numerous states, counties, and municipalities, Congress armed ERISA with a provision preempting state regulation of privately insured health benefit plans.

Section 514(a) of ERISA preempts all state laws that "relate to" employee benefit plans. This preemption contains an exception that a state may continue to regulate the business of insurance, commonly referred to as the "savings" clause. However, there is an exception to the savings clause (called the "deemer" clause) that prevents states from deeming employee welfare benefit plans to be in the business of insurance. Courts typically find ERISA preemption where the state law either refers to a plan or affects the plan's benefits, structure, or administration.

At the least, the issue of ERISA preemption may be at the cusp of legal resolution.

A test of whether a state law "affects" a plan's benefits, structure, or administration is of potentially infinite scope. The U.S. Supreme Court has ruled on several occasions that ERISA does not preempt state laws in traditional areas of state police power that are not directed at ERISA plans or do not interfere with the law's objective of uniform national administration of an employer's health plan (*New York State Conference of Blue Cross & Blue Shield Plans, et al. v. Travelers Ins. Co.*). The *Travelers Ins. Co.* case, in particular, ruled that ERISA did not preempt a state law within a traditional area of state regulatory authority that had the effect of increasing the cost of an ERISA plan.

As interpreted by the courts, a balance exists between ERISA preempting state laws that interfere with a uniform national administration of employer-sponsored health plans and states' freedom to exercise their traditional powers even if this exercise has some "effect" on ERISA plans. As states and local entities have addressed healthcare reform, they have attempted to structure their measures to fall within the existing case law to survive an ERISA challenge.

The Maryland "Wal-Mart" Case

Maryland provided the subject of the first Court of Appeals decision addressing the issue of ERISA preemption of a healthcare reform law. In 2006, the Maryland General Assembly enacted a "fair share" law that required employers with 10,000 or more Maryland employees to spend at least 8 percent of their total payroll on employee health insurance or pay the shortfall to the state. Wal-Mart, with about 16,000 Maryland employees, was the only employer subject to the law. The Retail Industry Leaders Association (RILA) sued the Maryland Secretary of Labor to enjoin the enforcement of the fair share law. RILA was successful at the district court level, and the case was appealed to the Fourth Circuit Court of Appeals.

In January 2007, by a 2-to-1 decision, the Fourth Circuit affirmed the decision of the district court that the fair share law was preempted by ERISA (*Retail Industry Leaders Association v. Fielder*). The court explained that the option for Wal-Mart to either reach the minimum spending threshold or pay the difference to the state was not a "rational choice" because no employer would decide to pay money to the state instead of paying it to its employees as a benefit. The court used a "slippery slope" argument, pointing out the inevitable effect of allowing such local laws to stand. "If permitted to stand, these laws would force Wal-Mart to tailor its healthcare benefit plans to each specific state, and even to specific cities and counties. This is precisely the regulatory balkanization that Congress sought to avoid by enacting ERISA's preemption provision."

The dissenting justice noted "the explosive growth in the cost of Medicaid" and that "the federal government ... has consistently called upon the states to function as laboratories for developing workable solutions." The Maryland fair share law was not preempted by ERISA, according to the dissent, because the employer's option to pay the shortfall in the form of an assessment to the state "offers a means of compliance that does not impact ERISA plans." Moreover, the dissenting justice noted that the fair share law did not impede an employer's ability to administer

CASES CITED

Cal. Div. of Labor Standards Enforcement v. Dillingham Constr., 519 U.S. 316, 330 (1997)
DeBuono v. NYSA-ILA Medical Services Fund, 520 U.S. 806, 814 (1997)
Golden Gate Restaurant Association v. City and County of San Francisco, 2008 West Law 90078 (2008)
New York State Conference of Blue Cross & Blue Shield Plans, et al. v. Travelers Ins. Co., 514 U.S. at 661 (1995)
Retail Industry Leaders Association v. Fielder, 475 F.3d 180 (4th Cir. 2007)
Retail Industry Leaders Association v. Suffolk County, 497 F. Supp.2d 403 (E.D.N.Y. 2007)

ERISA plans under nationally uniform provisions because it did not "dictate a plan's system for processing claims, paying benefits, or determining beneficiaries."

Six months later, based on a fair share law enacted by Suffolk County (*Retail Industry Leaders Association v. Suffolk County*), a district court in New York reached the same decision as did the Fourth Circuit in the *Fielder* case. This law also applied only to large employers, but in this case was not focused solely on Wal-Mart.

If the courts cannot find a way to allow local health reform initiatives to move forward, then Congress may well amend ERISA.

The San Francisco Health Care Security Ordinance

In July 2006, the San Francisco Board of Supervisors passed, and the mayor signed into law, the San Francisco Health Care Security Ordinance. The ordinance mandates that covered employers make required healthcare expenditures to or on behalf of certain employees each quarter. The San Francisco ordinance covers a much larger group of employers than the single-employer focus of the Maryland and Suffolk County laws: employers with an average of at least 20 employees performing work for compensation in a quarter and all not-for-profit corporations with an average of at least 50 employees in a quarter. If an employer does not make required healthcare expenditures on behalf of employees in some other way, it must meet its spending requirement by making payments directly to the city.

The ordinance is also of broader application because it applies to all employers meeting the ordinance's thresholds whether the employer has an ERISA plan for all of its employees, has a plan for only some of its employees, or has no ERISA plan. Moreover, no employer is forced to create or maintain an ERISA plan or any level of benefits under the plan. Instead, the employer can choose from options that best meet its needs so long as the minimum spending requirement of the ordinance is met. For example, the employer could have no plan and make the minimum payment directly to the city, have an ERISA plan in which less than the minimum spending amount is spent and pay the balance to the city, or have an ERISA plan for which spending on healthcare coverage meets the spending limit.

The Golden Gate Restaurant Association filed an action in the United States District Court to enjoin the implementation of the ordinance on the basis that it is preempted by ERISA. The district court agreed and enjoined the ordinance. San Francisco then filed a motion in the Ninth Circuit Court of Appeals to stay the district court's injunction pending the city's appeal of its ruling in the Ninth Circuit. The Ninth Circuit stayed the injunction, thereby allowing the San Francisco ordinance to take effect, pending a decision from the Ninth Circuit on the validity of the ordinance (*Golden Gate Restaurant Association v. City and County of San Francisco*).

The Ninth Circuit explained that within the meaning of ERISA's preemption provision, the ordinance does not have a connection with employee benefit plans and is highly unlikely to have a reference to employee benefit plans. Similar to the argument of the dissent in the Wal-Mart case, the Ninth Circuit pointed out that because employers have the option of making payment to the city, the ordinance does not require employers to establish ERISA plans, or make changes or pay certain levels of healthcare benefits to members of existing ERISA plans.

It is important to understand that the current Ninth Circuit decision is only an interim decision pending briefing and a ruling on the merits. At press time, the hearing was anticipated to occur in April or May of this year, with a decision coming at some point later. Thus, while the opinion stated that San Francisco has "a probability, even a strong likelihood, of success in [its] argument that the ordinance is not preempted by ERISA," the Ninth Circuit has not yet ruled on the issue.