Collision Course: ERISA Preemption and State Health Care Reform

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Health care reform is shaping up to be a hot topic in the 2008 Presidential election. Several states, however, have decided to move ahead with their own reform programs rather than wait for a federal solution.

Three of those states — Massachusetts, Vermont, and Maine — have passed legislation intended to yield near universal coverage for their residents. Other states have passed, or are considering, legislation which would force some employers (especially large, “big box” retailers like Wal-Mart) to make larger contributions to their health plans. Both types of legislation face an uncertain future in light of ERISA’s federal regulatory scheme for health plans.

ERISA PREEMPTION IN A NUTSHELL

One of ERISA’s primary purposes is to remove barriers to the uniform administration of employee benefit plans throughout the United States. Conflicting state law requirements can disrupt uniform administration, so ERISA expressly declares that its rules “supersede any and all State laws [that] relate to any employee benefit plan.” Consistent with this language, the Supreme Court has held that ERISA preemption is deliberately expansive and designed to establish benefit plan regulation as exclusively a federal concern. Thus, the general rule is that ERISA completely preempts any state law that “relates to” an employee benefit plan.

A special exception to this rule exists for insurance regulation. States remain free to regulate the content and sale of insurance policies, even if those policies are purchased by an employee benefit plan.

PREEMPTION’S EFFECT ON STATE REFORM

ERISA preemption poses an obvious problem to state health care reform. Any state law that attempts to regulate the terms of a health plan clearly has a connection with, or reference to, such a plan, and is thus preempted by ERISA. The result is that such laws would be deemed unenforceable with respect to employer-sponsored plans.

MARYLAND’s “BIG BOX” LAW

In January 2006, Maryland passed a health care contribution mandate called the “Fair Share Act.” The law required covered employers to contribute an amount equal to eight percent of their total wage payments in Maryland to health care, or to pay a tax to Maryland equal to the difference between eight percent of their wage payments and their actual health care contributions.

The Fair Share Act applied only to for-profit organizations that employed more than 10,000 people in Maryland. Not coincidentally, Wal-Mart is the only employer in Maryland to fit that description. Thus, many concluded that the law was designed to force Wal-Mart to contribute more towards its employees’ health coverage.

The Act was immediately challenged in court by a coalition of retail employers. The coalition alleged that the Act was preempted by ERISA because it essentially required affected employers to establish a health plan. A Maryland federal district court agreed and struck down the law.

Maryland appealed the district court’s decision to the Fourth Circuit Court of Appeals. Among other things, Maryland argued that the Fair Share Act did not directly regulate health plans because employers could “opt out” of the minimum health care requirement by paying a tax.

The Fourth Circuit agreed that ERISA does not preempt Maryland laws that establish general taxes, or laws that regulate health care providers or insurers. It reasoned that a state law aimed at one of these permitted activities is not preempted, even though it indirectly affects benefit plans. But the Court concluded that under the Fair Share Act,
the "only rational choice" employers have is to structure their health care plans to meet the minimum spending threshold. Therefore, the Court concluded that the Act affected benefit plans in more than an indirect fashion, and thus was preempted by ERISA.

The Fourth Circuit’s decision leaves many questions unanswered. In particular, it does not indicate what the outcome would be if a state’s health care law did give employers a “rational choice” between additional health care spending and paying a tax. For example, if a state law required an employer to contribute eight percent of wages to health care or pay a one percent tax, the employer might find it rational to pay the tax. Although this kind of provision would still clearly be “related to” employee benefit plans, its effect on such plans arguably would be indirect. It therefore might escape ERISA preemption.

Several states in other federal Circuits are considering “big box” health care laws, so additional (and possibly conflicting) court decisions on this topic are a virtual certainty.

**Universal Coverage Laws**

State laws that attempt to require universal health coverage may also face ERISA preemption challenges, but probably on only a partial basis. Some aspects of the universal coverage laws that have been enacted in Maine, Massachusetts, and Vermont — such as Medicaid expansion, voluntary public health plans, and individual health mandates — are clearly outside of ERISA’s scope, and thus should withstand an ERISA challenge.

Other aspects of these laws, however, are probably preempted by ERISA. Both Massachusetts and Vermont have “play-or-pay” provisions that impose taxes on employers that do not offer minimum levels of health care coverage. Although some practitioners believe that these provisions do not impose a sufficient burden on employers to be preempted, it is more likely that a court would find them preempted by ERISA for the same reasons that the Fourth Circuit found Maryland’s Fair Share Act preempted. A “play-or-pay” provision may not require an employer to modify its health care plans, but it is still a powerful form of state coercion that interferes with the uniform administration of benefits.

Interestingly, no employer or group has yet challenged Massachusetts’s or Vermont’s universal coverage laws. In the case of Massachusetts, this may be because the individual coverage mandate, which forces individuals to obtain health insurance, makes an ERISA preemption challenge largely meaningless. Employers may be able to challenge the “play-or-pay” provision, but ERISA — which governs employers, but not individual employees — offers no grounds for challenging the individual mandate.

Thus, a business with Massachusetts employees may have no choice but to offer health care coverage meeting Massachusetts’ standards.