

ERISA: The Fly in the Ointment for Universal Health Insurance

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During his long career as an action hero, Arnold Schwarzenegger always managed to escape plot twists that threatened an unhappy ending. But as the governor of California, he will need more than a good scriptwriter to save his much-ballyhooed push for universal health insurance coverage.

Thanks to an appellate court decision in January, Schwarzenegger's insurance initiative is doomed to fail. The Fourth Circuit's decision in *Retail Industry Leaders Association v. Fielder* essentially killed one of the funding sources needed to make this form of universal health insurance a reality.

Schwarzenegger's plan calls for all individuals to obtain health insurance through a variety of means, including employer-sponsored coverage, coverage on the individual market, and an expanded Medicaid program. To fund the costs of insurance for the 4.8 million Californians who lack health insurance, the state would impose a 4% payroll tax on employers that do not offer health insurance. But the new Fourth Circuit decision suggests that "pay or play" provisions such as Schwarzenegger's, or even the ones in Pennsylvania's and Oregon's recently-proposed plans, may run afoul of ERISA.

Congress enacted ERISA – the Employee Retirement Income Security Act of 1974 – to provide a uniform regulatory regime for employee benefit plans. Congress enacted ERISA to provide a uniform regulatory regime for employee benefit plans. Most of the act's 600 pages address pension plans rather than health insurance benefits. But ERISA includes a preemption provision that has hamstrung states in dealing with a variety of health insurance benefits issues, from HMO care rationing in the 1990s, to employer coverage mandates and "play or pay" requirements.

ERISA preempts state laws that have a "connection with" or "reference to" self-funded employee health benefits plans. When ERISA was enacted in 1974, most employers bought health insurance plans for their employees through an insurance company. The insurance game is much different in 2007, and most workers are now insured through self-funded plans. In these programs, employers rather than insurance companies are on the hook for workers' claims. If an insurance company is involved, it typically manages the plan, but doesn't fund it.

Like Schwarzenegger's proposed scheme, Maryland's law imposed a tax on employers. It required for-profit companies with more than 10,000 employees that did not spend at least 8% of their payroll on health benefits, self-funded or otherwise, to pay the difference in cost to Maryland.

Because it concerned taxes rather than benefits, shouldn't ERISA have been irrelevant?

Not according to the Fourth Circuit. It saw the 8% threshold as a “required” minimum expenditure for employee health benefits. And because only firms that failed to meet that minimum would be subject to the tax, the court ruled such a mechanism “a quintessential fee or penalty, not a tax.”

From there, under the extraordinary broad scope that courts have given to ERISA preemption, it’s easy to connect the dots and predict the undoing of any universal health insurance program that relies on payroll taxes for funding.

Preemption schemes based on ERISA may not be all-dominating, but they’re close. Maryland tried to get around the ERISA sinkhole by claiming that its law imposed only “indirect” economic incentives on employers to encourage them to provide employee health benefits. The court disagreed. It found that this constituted a required minimum expenditure on health benefits, and thus implicated ERISA. “If permitted to stand,” the court wrote, “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.”

States that want to pursue universal health insurance will, by necessity, require some form of “balkanization” to fund their programs – unless they elect to drop employer-sponsored coverage out of the mix altogether. Theoretically, that might not be a bad thing, but as a practical matter, employer-sponsored coverage is pervasive, and will probably be part of any successful plan to extend health coverage broadly in the near future.

Congress gave Hawaii a statutory exception from this type of ERISA preemption, to accommodate the state’s mandate that employers provide health insurance to their employees. Wal-Mart’s business in Hawaii has not noticeably collapsed as a result. Congress would do all of us a favor by amending ERISA to allow all states to regulate their employee health benefit plans, at least in the context of health coverage expansion. Without these ERISA amendments, it’s likely that all “play or pay” programs will ultimately fail – and that’s a steep price to pay for a 1974 piece of legislation whose current ramifications far surpass its original intent.

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