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Billing It to the Boss

State 'fair share' laws on medical insurance unfairly burden employers.

BY THOMAS P. GIES

Last month, Massachusetts passed legislation intended to ensure that all its residents have health care coverage. A controversial "pay or play" provision requires any employer with more than 10 employees to either provide health care coverage or pay an annual "fair share" fee to the state.

In January the Maryland Legislature enacted the so-called Wal-Mart bill. It requires all private employers with more than 10,000 Maryland employees to spend 8 percent of payroll on health insurance or pay the difference to a fund maintained by the state. Various fair-share bills are pending in more than 20 other states.

Employers should pay attention to the next big trend in employment regulation. Fair-share legislation is likely to have a negative impact, even on large companies that provide health care coverage.

IT'S A RIGHT?

Some businesses may wonder how we got to a point where people assert that employees have a "right" to have their employers pay a portion of the cost of providing medical coverage, at a cost to be determined by state regulators. After all, no federal law requires employers to provide medical coverage. By contrast, most people do not assert that employees have a right to employer-subsidized transportation. What is it about health care?

History provides some partial answers. Many of the health care system's current problems originated with decisions made soon after World War II, when no one anticipated how much health care would cost 50 years later. Labor unions were successful in pressuring many employers to provide fringe benefits, including medical coverage. Employers often believed it would be cheaper to agree to such requests in lieu of paying higher wages. And once the benefit was created, these employers frequently extended medical coverage to their nonunion employees.

In 1974, Congress passed the Employee Retirement Income Security Act. ERISA in no way requires employers to provide any type of employee-benefit plan, nor does it dictate the kind of coverage an employer must provide in a health care plan. ERISA does pre-empt state insurance regulation of self-insured companies, however, and many companies responded by becoming self-insured. Approximately 40 million Americans receive medical coverage from such employers.

One of the advantages of being self-insured is the ERISA exemption enables large employers to provide health care coverage at lower cost. The cost savings come in part from being able to offer a uniform benefit package throughout the country and avoiding a variety of state mandated-benefit laws that dictate the substantive terms of employer health care programs. Employers who provide health care coverage through traditional insurance arrangements must comply with these requirements.

Companies began to pay even more attention to health care costs in the early 1990s after Financial Accounting Standards Board Statement No. 106 required them to include the cost of providing health care in their financial statements.

The relentless increase in the cost of health care in recent years has generated several responses. Most employers have embraced managed care. Some companies have tried to reduce costs by modifying or eliminating retiree coverage. Many employers have shifted to self-insured arrangements. Still others have decided to terminate coverage altogether or to make it available to a limited number of employees.

On the political front, Congress considered and rejected a health care reform proposal initiated in President Bill Clinton's first term. Twelve years later, health care costs continue to rise sharply. While there's a sense that the system is broken, there is little consensus about the cure.

QUESTIONABLE LAW

The fair-share movement arose as a reaction to this troubled system. Supporters argue that some employers fail to provide adequate health care coverage for workers and their families,

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resulting in these companies shifting costs onto state and local taxpayers, who are responsible for funding state Medicaid programs. These advocates contend that it is appropriate to force employers to help financially strapped state governments with the rising cost of Medicaid by paying their "fair share."

As these arguments influence the state legislatures, however, they are spawning both questionable law and bad public policy.

The principal legal question is whether states have the authority to legislate in this area in light of ERISA's very broad preemption provision.

ERISA Section 514, 29 U.S.C. §1144, supersedes any state and local laws that "relate to" employee-benefit plans. A series of Supreme Court decisions have given a very broad reading to this provision, interpreting it to include any state law that "has a connection with or reference to" an ERISA plan. This line of cases includes *Metropolitan Life Insurance v. Massachusetts* (1985) and *District of Columbia v. Greater Washington Board of Trade* (1992), which established that ERISA pre-empts state mandated-benefit laws as applied to plans of self-insured employers.

Litigation challenging the new Maryland law on ERISA preemption grounds is pending in federal district court. The lawsuit claims that the statute is legally indistinguishable from other state mandated-benefit laws that have been pre-empted and that it is inconsistent with ERISA's goal of promoting uniform administration of employee-benefit plans across the country. The lawsuit also contends that the statute violates the Constitution's equal protection clause by treating a certain class of employers in an arbitrary manner.

Application of the Supreme Court's ERISA pre-emption cases to state fair-share laws will require reconciling the Court's earlier decisions on the scope of Section 514 with more recent decisions suggesting a less expansive approach to ERISA pre-emption of state laws of general application. For example, *New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Insurance Co.* (1995) and *California Division of Labor Standards Enforcement v. Dillingham Construction* (1997) criticized the Court's prior effort to interpret the term "relates to" in uncritically literal terms.

Language in these later decisions suggests that the pre-emption issue should be analyzed in terms of the purposes of ERISA and that state laws of general applicability will not be pre-empted merely because they have an "indirect economic effect" on ERISA plans. Supporters of the Maryland law, relying on *Travelers* and *Dillingham*, argue that the statute is immune from pre-emption because it regulates employers and, in any case, does not mandate any change in the terms of any existing ERISA plans.

Lawyers familiar with this area of the law know it to be chaotic. The better reading of the Supreme Court's pre-emption cases suggests that the Maryland law should be struck down. Nothing in *Travelers* and *Dillingham* suggests any intention by the Court to retreat from its consistent endorsement of the importance of advancing ERISA's goal of uniform benefit-plan administration across the states. Justice Samuel Alito Jr., whose body of work in the U.S. Court of Appeals for the 3rd Circuit has not addressed this issue, may have the opportunity to make a significant contribution to this corner of preemption law.

Bad Policy

Beyond the legal issue, fair-share bills are unlikely to meet the policy expectations of their adherents.

Most of the uninsured are people who would not be helped by these laws, either because they work for smaller employers not covered by the laws or because they are unemployed. Studies suggest a substantial number of uninsured individuals are younger, relatively healthy employees who are in between jobs and who seem to be making rational short-term economic decisions not to buy health insurance.

More significant, fair-share laws will do little to control the continued high rate of inflation in the health care sector. Critics correctly observe that mandated-benefit laws tend to reduce wages. They are also right in predicting that the net effect of the fair-share laws will be that some companies will drop or cut back on health care coverage. For example, some Massachusetts employers might find it cheaper to pay into the state fund, rather than incur the expense of maintaining their own health care plans.

It is inevitable that this law will increase the cost of doing business for Massachusetts employers. Once a state government is given the authority to determine an employer's fair share of providing health care to the uninsured, the urge to shift additional costs to employers will be irresistible. The initial, relatively modest the play-or-pay provision in the Massachusetts law is only the beginning.

Fair-share laws also will cause headaches for employers who already provide health insurance coverage. Self-insured companies now are able to maintain a uniform plan across the country. Fair-share laws will erase this flexibility, requiring companies to comply with a patchwork of differing mandates.

Fair share laws also typically include other mandates on all employers, even those who are self-insured. As an example, the Massachusetts law requires all employers to maintain "cafeteria plans." The statute also contains additional reporting and nondiscrimination obligations applicable to all employers. And some of the bills pending across the country go substantially further than either the Maryland or Massachusetts legislation in mandating the level of benefits that employers must provide.

Legislation will not deter employers from continuing to rely on basic economics in deciding where to locate operations. Many companies have fled California in recent years because of the high cost of doing business there. Mandated-benefit laws can only hurt a state trying to attract and keep new businesses.

Unions at Work

The goal of fair-share laws should also be viewed with skepticism. Notwithstanding the professed concern for the plight of state taxpayers, organized labor has co-opted this issue for its own purposes.

Unions continue to press for laws that would increase the employer's burden in this area. They believe it's an employer's responsibility to pay for employees' health care, and they recog-

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nize that imposing such mandates on all employers would reduce the competitive disadvantage facing many unionized companies with generous health care coverage.

Taking a cue from complaints made against companies that relocated to Bermuda to avoid their alleged fair share of income taxes, unions have once again tried to make employers the bad guys. And even initial victories aren't enough: The AFL-CIO opposes the Massachusetts law because it does not transfer *enough* costs to employers.

Mandated-benefit laws are the wrong answer to a difficult problem. Only a national solution forged by Congress can hope to address the myriad issues facing the health care system. Since no one expects anything like that to happen this year, employers should keep a close eye on state capitals.

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