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December 1, 2005

Mr. Ronald Wineholt
Vice President of Government Affairs
Maryland Chamber of Commerce
60 West Street, Suite 100
Annapolis, Maryland 21401

Re: "Fair Share Health Care Fund Act" Proposal - ERISA Preemption

Dear Mr. Wineholt:

You asked us to review whether the Employee Retirement Income Security Act of 1974 preempts the proposed "Fair Share Health Care Fund Act" as reflected in Senate Bill 790 and House Bill 1284 (the "Proposal"). Although the Supreme Court has not ruled directly on a similar State law, we believe that it is likely that the Act would be found to be preempted by ERISA if it were enacted.

I. Overview of the Proposal

Among other things, the Proposal provides that, if an employer does not spend at least a designated percentage of its employees' total wages on employee health care costs, the employer must pay an amount equal to the difference between the designated percentage and what it actually pays to the State-run Fair Share Health Care Fund. In essence, the Proposal mandates that employers incur a specified level of health benefits costs for their employees, either directly through their employer-sponsored health plans or through a combination of contributions to their employer-sponsored health plans and contributions to the State-run Fund.

II. ERISA's Preemption Rule

ERISA section 514(a) provides that ERISA "supersedes... all State laws insofar as they... relate to any employee benefit plan...." One of the principal purposes of ERISA was to eliminate the possibility of a tangle of State laws impacting employee benefit plans, and instead to create a single, comprehensive, thoughtful, federal regulatory scheme for employer-provided benefits. Since ERISA's enactment in 1974, the courts repeatedly have struck down State laws directly or indirectly relating to employee benefit plans.

(The so-called "savings clause" of ERISA section 514 allows States to regulate insurance, but the so-called "deemer clause" of ERISA section 514 prohibits States from deeming employee benefit plans to be "insurance" in order to be able to regulate them under the savings clause. For example,

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the deemer clause prohibits a State from concluding that an employer's self-funded employee health plan is "insurance" in order to claim that the State may regulate it under the savings clause.)

III. ERISA's Preemption Rule as Interpreted by the Courts

The Supreme Court has interpreted the preemption clause to give the clause a "broad common-sense meaning," concluding that "even if [a State] law is not specifically designed to affect [an employee benefit plan], or the effect is only indirect," ERISA preempts the State law. Ingersoll-Rand Co. v. McClendon, 498 U.S. 133 (1990). The Court has struck down State laws if they merely "relate to" an employee benefit plan, concluding that "[a] law 'relates to' an employee benefit plan ... if it has a connection with or reference to such a plan". Shaw v. Delta Air Lines, Inc., 463 U.S. 85 (1983).

The Court has held that ERISA preempts State laws that require employers to provide employee benefits measured against some State-mandated reference point. For example, in District of Columbia v. Greater Washington Board of Trade, 506 U.S. 125 (1992), the Court, in applying the Shaw "reference to" test, held that ERISA preempted a local workers' compensation law that required employers to provide health plan coverage equivalent coverage to that provided by the local workers' compensation program.

The Court also has stated specifically that ERISA preempts State laws imposing a "substantive coverage requirement" or mandating certain benefits. For example, in Metropolitan Life Insurance Co. v. Massachusetts, 471 U.S. 724 (1985), the Court considered whether ERISA preempted a State law mandating particular benefits in health insurance contracts issued in the State. The Court upheld the law under the savings clause, but noted that the law "directly affected" employee benefit plans and therefore that the deemer clause protects self-funded ERISA plans from this type of regulation.

IV. Analysis

The Proposal is the type of State law intended to be preempted by ERISA. Specifically, the Proposal is a direct attempt to try to force employers to provide employee health benefits meeting a State-mandated design (i.e., costing at least the designated percentage of total wages), either directly or through a combination of contributions to their own plans plus contributions to the Fair Share Health Care Fund.

Giving ERISA's preemption clause the "broad common-sense meaning" required under Ingersoll-Rand, the Proposal clearly would affect employer's benefit plans, requiring them either to modify their health plans directly to "top them up" to the required cost or modify their health plans indirectly by supplementing their costs with contributions to the State Fund. And the Proposal falls squarely within the type of State law found to be preempted in Greater Washington Board of Trade; that is, a State law mandating benefits measured against a State-mandated reference point (i.e., the 8% cost mandated in the Proposal).

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Finally, it could be argued fairly that the Proposal also imposes a "substantive coverage requirement" on employers, thereby falling within the category of State laws that are preempted under Metropolitan Life. That is, although ERISA -- and its protective preemption provision -- leave employers free to provide any type of (or no) health benefits to their employees, the Proposal mandates the provision of substantive health coverage, either directly through employer-sponsored plans or indirectly through the State Fund.

(Supporters of State law proposals that attempt to regulate ERISA-governed employee benefit plans often cite the Supreme Court's decision in New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Insurance, 514 U.S. 645 (1995). In that case, a group of commercial insurers challenged a New York law that permitted hospitals to impose surcharges on charges incurred by individuals covered by a commercial insurer, but not on individuals covered by a Blue Cross/Blue Shield plan. The Court held that this State law was not preempted because the law did not relate to employee benefit plans but rather related to hospital charges. Although this law had the indirect effect of causing insured employee benefit plans purchasing their insurance coverage from insurers other than Blue Cross to incur greater costs than employee benefit plans purchasing insurance through Blue Cross or employee benefit plans that were self-funded, the Court found the impact of the State hospital surcharge law on employee benefit plans to be too tenuous to fall within the scope of ERISA's preemption rule. Of course, unlike the surcharge on insurers rule of the New York law, the Proposal -- by its very terms -- imposes employee benefit plan obligations directly on employers, whether the employers' benefit plans are insured or self-funded. Therefore, the Travelers decision does not support a claim that the Proposal avoids ERISA's preemption rule. In fact, the Court in Travelers stated expressly, in reference to its decision in Greater Washington Board of Trade, that a State law that "specifically relates to welfare benefit plans regulated by ERISA [like the law in question in that case] on that basis alone is pre-empted".

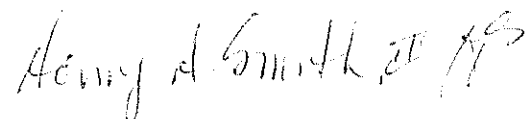
(It is of interest that the Attorney General's bill review letter on the Proposal did not speak to the ERISA preemption issue.)

V. Conclusion

For the reasons cited above, if the Proposal was enacted, we believe that the courts would find it to be preempted by ERISA.

Please let me know if you have any questions on the above, or if you would like to discuss this issue in further detail.

Very truly yours,



Henry A. Smith, III