RILA v. Fielder: Preempting Pay-or-Play

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Confronted with rapidly escalating healthcare costs\(^1\) and growing public support for health care reform,\(^2\) many states have begun experimenting with new approaches to expand access to health care coverage. Among those strategies has been the concept of “pay-or-play”: the idea that employers, particularly large employers, should be required to provide health insurance for their workers or pay into a state-operated fund that will. In *Retail Industry Leaders Association v. Fielder*, the Fourth Circuit Court of Appeals considered the compatibility of Maryland’s Fair Share Health Care Fund Act, a leading example of the pay-or-play approach, with the federal Employee Retirement Income Security Act (ERISA), and concluded that the Maryland law was preempted by ERISA.\(^3\) The Fourth Circuit’s decision and reasoning establishes a foundation for challenges to similar pay-or-play statutes being considered by other states and may shift the health care reform spotlight from state laboratories to Congress.

**Factual Background**

On January 12, 2006, the Maryland General Assembly overrode Governor Robert Ehrlich, Jr.’s veto\(^4\) and enacted the Fair Share Health Care

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\(^2\) Public support for the idea that the federal government should ensure that all Americans have health care coverage – a major reform proposal – has risen from 59% in January 2000 to 69% in November 2006. Pollingreport.com, Health Policy, http://www.pollingreport.com/health3.htm (last visited Sept. 22, 2007) (Gallup Poll conducted Nov. 9-12, 2006, surveying 1,004 adults). A similar poll showed that public support for the statement “the federal government should guarantee health insurance for all Americans” rose from 56% in August 1996 to 64% in February 2007. New York Times/CBS News Poll 15 (Feb. 23-27, 2007) (surveying 1,281 adults).

\(^3\) *Retail Industry Leaders Ass’n v. Fielder*, 475 F.3d 180, 195-97 (4th Cir. 2007).

The Fair Share Act ("Fair Share Act"). The Fair Share Act required private-sector, for-profit employers with more than 10,000 employees to either spend at least eight percent of their wage bill on employee health care or pay the difference between eight percent of their wage bill and their spending on health care to the state’s Fair Share Health Care Fund ("Fund"). The Fund, in turn, would supplement state Medicaid and children’s health care programs. Non-complying employers would be subject to a $250,000 penalty. Affected employers were also required to report annually to the state the percentage of wages they had spent on health care.

The General Assembly adopted the Fair Share Act after hearing testimony and analyses warning of the rising costs of the Maryland Medical Assistance Program (comprised of Medicaid and children’s health care programs) and highlighting Wal-Mart’s reliance on state health care programs. A report by the Department of Legislative Services cited other states’ claims that Wal-Mart’s low wages and limited employee benefits had driven its employees and their dependents to the rolls of public health plans and noted the disparity between the 45% of Wal-Mart employees covered by company health plans and the 90% of employees with some health insurance. The report also mentioned a recently-passed California law requiring employers to provide their employees with health insurance or contribute to a state fund that would do so.

Wal-Mart would have been the only employer directly affected by the Fair Share Act. The three other Maryland employers with more than 10,000 employees were a non-profit subject to a lower six percent spending threshold, a company already spending more than eight percent of wages on health care, and an organization subject to an alternate calculation due to the higher wages paid to its employees. Wal-Mart, in contrast, had an estimated 16,000 employees in Maryland and spent between seven and eight percent of its payroll on health care.

The Retail Industry Leaders Association ("RILA"), a trade association representing Wal-Mart, brought suit against Maryland Secretary of Labor,
Licensing and Regulation James Fielder, seeking a declaration that the Fair Share Act was preempted by ERISA and an injunction against its enforcement. The district court for the District of Maryland concluded that the Fair Share Act was preempted by ERISA and granted RILA’s motion for summary judgment.

The Fourth Circuit Opinion

In a 2-1 decision, the Fourth Circuit Court of Appeals affirmed the district court’s holding that the Fair Share Act’s pay-or-play mandate did not avoid ERISA preemption because covered employers’ alternatives to changing their ERISA plans—paying into the state Fund or increasing spending on non-ERISA plans—were not reasonable. Rather, the Court concluded that because the Fair Share Act effectively required covered employers to increase contributions to their ERISA plans, it had a “connection with” ERISA plans and was thus preempted by ERISA.

ERISA provides comprehensive federal regulation of employee benefit plans, including almost all employer-funded health plans, but gives employers discretion to set the terms of those plans. In order to maintain a uniform system of regulation, ERISA preempts state laws that “relate to” an ERISA plan. The Supreme Court has held that a state law “relates to” an ERISA plan when it “has a connection with” an ERISA plan.

In finding that the Fair Share Act had a “connection with” an ERISA plan, the Fourth Circuit relied on Shaw v. Delta Air Lines, Inc., in which the Supreme Court held that a New York statute prohibiting employee benefit plans from discriminating on the basis of pregnancy was preempted by ERISA because it required employers to structure their plans in a certain way. The Fourth Circuit noted that under Shaw and its progeny, state laws requiring employee benefit plans to provide specific benefits or levels of benefits were routinely preempted.

The Court accepted as “the decision of any reasonable employer” Wal-Mart’s claim that, if faced with the choice of paying into the Fund or increasing spending on employee health care, it would choose the latter option. The Court reasoned that because employers providing additional health care benefits would reap the benefits of increased employee retention

16. Id.
18. RILA, 475 F.3d at 195-97.
19. Id. at 193-94.
20. Id. at 190-91.
21. Id. at 191.
22. Id.
24. RILA, 475 F.3d at 192.
25. Id at 193.
and performance, their "only rational choice" was to increase spending on their ERISA plans and meet the Fair Share Act's eight percent threshold.\(^\text{26}\) As a result, the Court concluded that Fair Share Act's requirements would have "a connection with" ERISA plans under the rule of Shaw, and accordingly held that the Fair Share Act was preempted by ERISA.\(^\text{27}\)

The Court rejected Secretary Fielder's argument that, because the Fair Share Act allowed employers to comply by increasing spending on non-ERISA plans or paying into the Fund, it actually gave employers a choice and did not impose mandates on company ERISA plans. Therefore, Secretary Fielder argued, the Fair Share Act did not have a "connection with" ERISA plans and should not be preempted.\(^\text{28}\)

To support his argument against preemption, Secretary Fielder invoked New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Insurance\(^\text{29}\) and California Division of Labor Standards Enforcement v. Dillingham Construction.\(^\text{30}\) In Travelers, a New York statute required hospitals to levy a surcharge on patients served by insurance carriers other than Blue Cross and Blue Shield, the effect of which made the selected carriers more attractive to ERISA plans and other insurance purchasers.\(^\text{31}\) The Supreme Court reasoned that because the statute had only "an indirect economic influence"\(^\text{32}\) on plan administration, it did not have a "connection with" ERISA plans and was not preempted.\(^\text{33}\) Similarly, in Dillingham, the Supreme Court held that a California prevailing wage law allowing contractors to pay a lower wage to apprentices in state-approved apprenticeship programs covered by ERISA,\(^\text{34}\) thus giving the programs an incentive to meet state certification requirements,\(^\text{35}\) created incentives "but [did] not dictate the choices facing ERISA plans," and was not preempted.\(^\text{36}\)

The Fourth Circuit sharply distinguished the Fair Share Act from the statutes in Travelers and Dillingham on the grounds that the statutes in those cases acted on hospitals and third-party employers, respectively, and only indirectly affected ERISA plans. In contrast, the Court reasoned that the Fair Share Act directly affected employers' design of their ERISA plans.\(^\text{37}\) The Court found that the "tighter causal link between regulation

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\(^{26}\) Id. at 193-94.

\(^{27}\) Id. at 194.

\(^{28}\) Id. at 195.

\(^{29}\) 514 U.S. 645 (1995).

\(^{30}\) 519 U.S. 316 (1997).

\(^{31}\) Travelers, 514 U.S. at 649-51, 659.

\(^{32}\) Id. at 659.

\(^{33}\) Id. at 662.

\(^{34}\) Dillingham, 519 U.S. at 319.

\(^{35}\) Id. at 330.

\(^{36}\) Id. at 334.

\(^{37}\) RILA, 475 F.3d at 195-96.
and employers’ ERISA plans” under the Fair Share Act rendered the comparison to Travelers and Dillingham inapposite.38

The Court also found that the Fair Share Act’s non-ERISA options for compliance were not “meaningful alternatives” to their ERISA-related options.39 The Court conceded that employers could increase their non-ERISA health care spending by providing on-site medical clinics or contributing to employee Health Savings Accounts. However, because on-site clinics could provide only limited care before coming within ERISA, and only those Wal-Mart employees covered by high-deductible insurance plans would be eligible for Health Savings Accounts, the Court concluded that neither approach would allow employers to significantly increase their non-ERISA health care expenditures.40 In addition, the court found that simply contributing to non-ERISA plans would require a company to coordinate with its ERISA plan, because an employer complying with the Fair Share Act by contributing to Health Savings Accounts would have to refrain from providing ERISA plan benefits that would render employees ineligible for Health Savings Accounts.41 Because such decisions regarding non-ERISA plans would affect ERISA plans, the Fourth Circuit concluded that the ability of employers to comply with the Fair Share Act through their non-ERISA plans did not save the Fair Share Act from preemption.42

The Court similarly rejected Secretary Fielder’s claim that employers could comply with the Fair Share Act by paying into the Fund.43 The Secretary alleged that an employer whose health care spending was near the eight percent requirement might find it less expensive to pay into the Fund than to modify its health care plan.44 However, the Court reasoned that the need for such a “stylized scenario” to make payment into the Fund a

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38. Id.
39. Id. at 196.
41. RILA, 475 F.3d at 196. Health Savings Accounts are only available to individuals who are covered by a high deductible health care plan and not covered by a more comprehensive plan. 26 U.S.C. § 223(c)(1) (2006).
42. RILA, 475 F.3d at 197.
43. Id.
44. Id.
rational option underscored its conclusion that the Fair Share Act would generally motivate employers to modify their ERISA plans rather than contribute to the Fund.\textsuperscript{45}

The Fourth Circuit raised a final concern that the Fair Share Act and similar state laws would require nation-wide employers to monitor state laws and alter their plans on a state-by-state basis.\textsuperscript{46} The Court's apprehension stemmed from \textit{Egelhoff v. Egelhoff}, in which the Supreme Court held that a Washington statute was not saved from preemption simply because employee benefit plans were able to opt out of compliance.\textsuperscript{47} The \textit{Egelhoff} court found that, while plan administrators could avoid the statute by opting out in plan documents, the need for administrators to keep track of opt-out requirements on a state-by-state basis would conflict with the uniformity purpose of ERISA preemption.\textsuperscript{48} Likewise, the Fourth Circuit concluded that the Fair Share Act would require employers to comply with state health care requirements on a state-by-state basis, resulting in a similar conflict with the purposes of ERISA preemption.\textsuperscript{49}

\textbf{Judge Michael's Dissent}

Judge Michael dissented from the Court's opinion, arguing that the ability of employers to comply with the Fair Share Act by paying an assessment to the state instead of modifying their ERISA plans saved the Act from preemption.\textsuperscript{50} While Michael rebutted each of the Court's arguments individually—arguing, in turn, that the Fair Share Act did not force employers to maintain an ERISA plan, did not mandate a set level of ERISA benefits, and did not interfere with an employer's ability to maintain a nationally uniform plan—the heart of his dissent was that the conclusion that "[u]nder the Act employers have the option of either paying an assessment or increasing ERISA plan health insurance. This choice is real."\textsuperscript{51} Michael cast doubt on Wal-Mart's claim that it would prefer to provide increased benefits instead of paying into the Fund, but noted that even if Wal-Mart chose to offer improved benefits to comply with the Fair Share Act, its decision to do so would be a business decision based on the new incentives created by the Act rather than an action forced upon Wal-Mart.\textsuperscript{52} Unless the "assessment [was] so high as to make its selection financially untenable" for companies, Michael reasoned that the option of paying into the Fund gave employers a means of compliance that did not

\begin{footnotes}
\item[45.] \textit{Id.}
\item[46.] \textit{Id.}
\item[47.] 532 U.S. 141, 150-52 (2001).
\item[48.] \textit{Id.} at 151.
\item[49.] \textit{RILA}, 475 F.3d at 197.
\item[50.] \textit{Id.} at 201 (Michael, J., dissenting).
\item[51.] \textit{Id.} at 202 (Michael, J., dissenting).
\item[52.] \textit{Id.} at 202-03 (Michael, J., dissenting).
\end{footnotes}
require it to modify an ERISA plan, and accordingly concluded that the Fair Share Act should not be preempted.\textsuperscript{53}

\textit{The Impact of RILA v. Fielder}

On April 16, 2007, Maryland Attorney General Douglas Gansler announced that the state would not petition for a writ of certiorari before the Supreme Court, laying the Fair Share Act to rest.\textsuperscript{54} \textit{RILA v. Fielder} has potentially far-reaching effects if the Fourth Circuit’s reasoning is adopted by other courts. \textit{RILA}’s holding that the Fair Share Act’s pay-or-play provisions do not allow the Act to escape ERISA preemption\textsuperscript{55} is broad enough to apply to many, if not most, state health care coverage statutes targeting employers. Furthermore, the Fourth Circuit’s reasoning—that the Fair Share Act would force employers to increase spending on ERISA plans because no “reasonable employer” would choose to pay increased state taxes instead of altering its ERISA plans,\textsuperscript{56} and that other non-ERISA related options were not “meaningful alternatives”\textsuperscript{57}—could potentially be extended to preempt a wide range of health care statutes giving employers multiple options for compliance. Even if amending an ERISA plan was only one of many options, a statute’s opponents might argue that the other options were not “meaningful alternatives” or that any “reasonable employer” would choose to modify their ERISA plan instead.

It is unclear whether the Fourth Circuit’s decision alone has stalled pay-or-play health care efforts in other states. In 2005, nineteen states considered pay-or-play legislation,\textsuperscript{58} In 2006, that figure rose to twenty-eight.\textsuperscript{59} The fate of those bills and the introduction of similar bills in 2007 may reveal whether pay-or-play campaigns have lost or retained momentum.

If other courts follow the Fourth Circuit’s decision and pay-or-play efforts are stalled, it seems unlikely that the setback will permanently weaken efforts to improve access to health care. Instead, the momentum that built behind pay-or-play will probably be redirected towards other efforts that avoid ERISA preemption, including state laws focusing on

\textsuperscript{53} Id. at 200, 203 (Michael, J., dissenting).
\textsuperscript{55} \textit{RILA}, 475 F.3d at 183.
\textsuperscript{56} Id. at 193-94, 197.
\textsuperscript{57} Id. at 196.
individual—rather than employer—mandates, and federal action. Indeed, by blocking this form of state experimentation through ERISA preemption, the Fourth Circuit has probably re-focused attention on health care as a federal rather than a state issue, and may have lent strength to calls for Congressional action.

Edward Takashima, J.D. 2009 (UC Berkeley)

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60. Individual mandates require individuals to purchase or obtain health care insurance, as opposed to employer mandates, which require employers to provide health care insurance for employees. An individual mandate was the core of Massachusetts’ 2006 health care reform act. See 2006 Mass. Legis. Serv. Ch. 58 (West).