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# Protections for ERISA Self-Insured Employee Welfare Benefit Plan Participants: New Possibilities for State Action in the Event of Plan Failure

Mark A. Edwards

*Mitchell Hamline School of Law*, [mark.edwards@mitchellhamline.edu](mailto:mark.edwards@mitchellhamline.edu)

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# Protections for ERISA Self-Insured Employee Welfare Benefit Plan Participants: New Possibilities for State Action in the Event of Plan Failure

## **Abstract**

Employees who receive health benefits through ERISA self-insured plans need protection when self-insured plans fail. Because of the breadth of ERISA preemption, states have been unable to assess ERISA self-insured plans for contribution to state insurance guaranty funds, and thus have been unable to include those employees in the protection of those funds. Further, attempts at federal reform to protect these employees have failed to garner support. However, under the recent *Travelers*, *United Wire*, and *Safeco* decisions, it may be possible for states to assess ERISA self-insured funds and their participants through a combination of hospital use surcharges and taxes on the sale of stop-loss insurance for contribution to state insurance guaranty funds. This Comment explores ERISA preemption analysis in light of these recent cases, and suggests state reforms to protect plan participants in the event of plan failure. Part II explores ERISA preemption analysis in greater depth. Part III examines recent cases that have created new possibilities for state health care reform by limiting the scope of ERISA preemption. Part IV proposes state reforms to protect participants in self-insured plans in the event of plan failure. Specifically, this Comment proposes that through a combination of surcharges on hospital use and taxes on the sale of stop-loss insurance, states can act within the bounds of ERISA preemption to include self-insured health plan participants in the protection of state insurance guaranty funds. Copyright 2010 by The Board of Regents of the University of Wisconsin System; Reprinted by permission of the Wisconsin Law Review.

## **Keywords**

Employee Retirement Income Security Act of 1974, employee benefit plans, pension, savings clause, deemer clause

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# PROTECTIONS FOR ERISA SELF-INSURED EMPLOYEE WELFARE BENEFIT PLAN PARTICIPANTS: NEW POSSIBILITIES FOR STATE ACTION IN THE EVENT OF PLAN FAILURE

MARK ALAN EDWARDS\*

## I. INTRODUCTION

Congress enacted the Employee Retirement Income Security Act of 1974 (ERISA)<sup>1</sup> to protect employees by securing their employee benefit plans.<sup>2</sup> Specifically, Congress sought to provide a uniform set of laws and protections that would preempt dozens of often conflicting state laws that "relate to" employee benefit plans.<sup>3</sup> In enacting ERISA, Congress was chiefly concerned with "abuse and mismanagement in the private pension system."<sup>4</sup> Although its substantive requirements are primarily directed toward retirement pension plans (as indicated in the Act's title), ERISA governs all employee welfare plans, including employee health benefit plans.<sup>5</sup>

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\* B.A., University of Massachusetts at Amherst, 1992; J.D., University of Wisconsin Law School, Class of 1998. With thanks to Kate and Alun, for their incredible love and patience.

1. Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended at 29 U.S.C. §§ 1001-1461 (1994)).

2. See *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 90 (1983); see also ERISA § 2, 29 U.S.C. § 1001.

3. ERISA § 514(a), 29 U.S.C. § 1144(a).

4. BARBARA J. COLEMAN, *PRIMER ON EMPLOYEE RETIREMENT INCOME SECURITY ACT 1* (4th ed. 1993).

5. ERISA § 4(a), 29 U.S.C. § 1003(a). ERISA mandates reporting, disclosure, participation, vesting, funding, and fiduciary requirements for employee benefit plans. However, the participation, vesting, and funding requirements *do not* apply to employee welfare (health) benefit plans. See ERISA §§ 101, 201, 301, 401, 29 U.S.C. §§ 1021, 1051, 1081, 1101. Employee welfare plans governed by ERISA are those that pay the following benefits through insurance: medical, hospital, or surgical care; and benefits paid upon death, accident, disability, or sickness. ERISA § 3(1), 29 U.S.C. § 1002(2)(A). However, the following plans are not governed by ERISA: government plans; church plans; plans which receive no contributions from employers of participants; and plans maintained solely to comply with workers' compensation, unemployment compensation, or disability insurance laws. ERISA § 4(a), 29 U.S.C. § 1003(a).

ERISA preempts state laws that “relate to” employee health benefit plans.<sup>6</sup> However, “any law of any State which regulates insurance, banking, or securities” is saved from preemption.<sup>7</sup> Thus while states may not regulate employee health benefit plans directly, they may do so indirectly by regulating insurance companies and insurance contracts purchased by those plans.<sup>8</sup> However, an employee welfare benefit plan that is self-insured—in other words, that does not purchase outside insurance to cover its plan—may not be deemed an insurance company for purposes of state regulation.<sup>9</sup>

Self-insured plans thus are exempt from state regulation. Yet ERISA provides participants in self-insured employee health benefit plans little protection in the event of plan failure.<sup>10</sup> ERISA did create the Pension Benefit Guaranty Corporation (PBGC), funded primarily through mandatory premiums paid by private pension plans. The PBGC provides employee pension plan participants with some of their expected basic benefits (usually those already vested) in the event of pension plan failure.<sup>11</sup> But ERISA created no such guaranty for employee welfare plan participants, including employee health plan participants. Moreover, it imposed no minimum funding requirement for employee welfare plans. Self-insured employee welfare benefit plans thus are more susceptible to plan failure.<sup>12</sup>

Like many states, Wisconsin maintains an insurance guaranty fund in order to pay outstanding health care bills when insurance company

6. ERISA § 514(a), 29 U.S.C. § 1144(a).

7. ERISA § 514(b)(2)(A), 29 U.S.C. 1144(b)(2)(A).

8. FMC Corp. v. Holliday, 498 U.S. 52, 61 (1990).

9. ERISA § 514(b)(2)(B), 29 U.S.C. § 1144(b)(2)(B).

10. Under ERISA §§ 502(a)(2),(3), 29 U.S.C. 1132 (a)(2), (3) plan participants or their beneficiaries are authorized to sue plan fiduciaries for breach of fiduciary duties under § 409(a), 29 U.S.C. 1109(a) if losses result from imprudent action by fiduciaries. Until very recently, however, any recovery from such actions flowed to the plan rather than to the participant or beneficiary who brought suit. See *Massachusetts Life Ins. Co. v. Russell*, 473 U.S. 134 (1985). But see *Varity Corp. v. Howe*, 116 S. Ct. 1065 (1996).

11. ERISA § 4002, 29 U.S.C. § 1302.

12. The National Association of Insurance Commissioners has recently warned that due to the lack of minimum funding requirements and the inability of states to monitor them, participants in self-insured plans have far fewer protections than participants in insurance company plans. Robert Pear, *State Regulators Seek Power over Self-Insured Employers*, N.Y. TIMES, Sept. 21, 1994, at B7. As Fred C. Nepple, chief counsel of the Wisconsin Office of the Insurance Commissioner has warned, “The administrators of these plans know we cannot audit them or review their files . . . We . . . have no authority.” *Id.*; see also David J. Brummond, *Federal Preemption of State Insurance Regulation Under ERISA*, 62 IOWA L. REV. 57, 117 n.474 (1976) (noting that state regulators are concerned that with the absence of minimum funding requirements for self-insured plans “inadequate amounts of money will be set aside to pay benefit claims”).

plans fail.<sup>13</sup> The fund is maintained through taxes and surcharges collected from insurance company plans and their participants.<sup>14</sup> ERISA does not preempt these taxes and surcharges because they regulate insurance.<sup>15</sup> Self-insured plans are regulated differently.<sup>16</sup> Because participants in self-insured plans do not contribute to state insurance guaranty funds, they are not covered in the event of plan failure.<sup>17</sup> When self-insured plans fail, participants are left unexpectedly to cover their own unpaid health care bills. For example, a Wisconsin manufacturer's self-insured employee health benefit plan recently failed. Its employees were unexpectedly saddled with thousands of dollars in unpaid health care bills.<sup>18</sup> The participants' health care provider faced a difficult choice: they could pursue their patients for payment, or forgive the unpaid bills and distribute the loss to other employers and patients through higher fees.<sup>19</sup>

The scope of ERISA preemption has been limited, however, by recent decisions in the United States Supreme Court<sup>20</sup> and three courts of appeals.<sup>21</sup> These decisions have created new possibilities for states

13. WIS. STAT. § 646 (1995-1996); *see also* ALA. CODE § 27-44-3 (1975); ARK. CODE ANN. § 23-96-107 (Michie 1995); CAL. INS. CODE § 1067.02 (West 1995-96); COLO. REV. STAT. ANN. § 10-20-104 (1996); CONN. GEN. STAT. ANN. § 38a-860 (West 1997); DEL. CODE ANN. tit. 18, § 4403 (1996); D.C. CODE ANN. § 35-1942 (1995-96); GA. CODE ANN. § 33-38-2 (1996); HAW. REV. STAT. § 431:16-203 (1996); 215 ILL. REV. STAT. ch. 73, para. 1065.80-3 (1997); KAN. STAT. ANN. § 40-3003 (1995); MINN. STAT. ANN. § 61B.19 (West 1996); MISS. CODE ANN. 83-23-205 (1972); MO. CODE ANN. § 376.717 (1996); MONT. CODE ANN. § 33-10-201 (1996); N.H. REV. STAT. ANN. § 408-B:5 (1995); N.J. STAT. ANN. § 17B:32A-3 (West 1996); N.D. CENT. CODE § 26.1-38.1-01 (1995); OHIO REV. CODE ANN. § 3956.04 (Baldwin 1996); OKLA. STAT. ANN. tit. 36, § 2025 (West 1996); PA. STAT. ANN. tit. 40, § 991.1703 (West 1996); R.I. GEN. LAWS § 27-34.3-3 (1956); S.D. CODIFIED LAWS ANN. § 58-29C-3 (1997); VT. STAT. ANN. tit. 8, § 4153 (1995); VA. CODE ANN. § 38.2-1700 (Michie 1996); WASH. REV. CODE ANN. § 48.32A.020 (West 1996); W. VA. CODE § 33-26A-3 (1966).

14. WIS. STAT. § 646 (1995-1996).

15. *See, e.g.,* New York Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co., 115 S. Ct. 1671, 1680 (1995) [hereinafter *Travelers I*]; Metropolitan Life Ins. Co. v. Massachusetts, 471 U.S. 724 (1985).

16. *See, e.g.,* General Split Corp. v. Mitchell, 523 F. Supp. 427, 430-31 (E.D. Wis. 1981).

17. WIS. STAT. § 646.01(b)(9) (1995-1996).

18. Interview with Robert Richards, Director of Patient Advocacy, and Jeanan Yasiri, Manager of Community Services, Dean Medical Center, in Madison, Wis. (1995).

19. *Id.*

20. *See Travelers I*, 115 S. Ct. 1671 (1995).

21. *See Travelers Ins. Co. v. Pataki*, 63 F.3d 89 (2d Cir. 1995) [hereinafter *Travelers II*]; *Safeco Life Ins. Co. v. Musser*, 65 F.3d 647 (7th Cir. 1995); *United Wire, Metal and Mach. Health and Welfare Fund v. Morristown Memorial Hosp.*, 995 F.2d 1179 (3d Cir. 1993), *cert. denied*, 510 U.S. 944 (1993).

to provide protection to self-insured plan participants while fostering a more competitive health care market. These rulings may authorize states to collect contributions to state insurance guaranty funds through surcharges on hospital use by self-insured plan participants,<sup>22</sup> and by taxes on the sale of stop-loss insurance to self-insured plans.<sup>23</sup> Because self-insured plans may now be forced to contribute to state insurance guaranty funds, plan participants may be covered by the state insurance guaranty funds when self-insured plans fail.

This Comment explores ERISA preemption analysis in light of these recent cases, and suggests state reforms to protect plan participants in the event of plan failure. Part II explores ERISA preemption analysis in greater depth. Part III examines recent cases that have created new possibilities for state health care reform by limiting the scope of ERISA preemption. Part IV proposes state reforms to protect participants in self-insured plans in the event of plan failure. Specifically, this Comment proposes that through a combination of surcharges on hospital use and taxes on the sale of stop-loss insurance, states can act within the bounds of ERISA preemption to include self-insured health plan participants in the protection of state insurance guaranty funds.

## II. ERISA PREEMPTION

### A. ERISA's Three Step Preemption Analysis

Courts apply a three-step analysis to determine whether ERISA preempts state law causes of action against and state regulation of employee welfare benefit plans.<sup>24</sup> First, they apply ERISA's preemption

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22. *Travelers II*, 63 F.3d at 89.

23. *Safeco*, 65 F.3d at 647. Stop-loss insurance is a form of catastrophic insurance purchased by otherwise self-insured plans. If claims against the plan exceed plan assets, stop-loss insurance is used to pay those excess claims. The majority of appellate courts agree that the purchase of stop-loss insurance by self-insured plans does not negate the plan's self-insured status. See *Thompson v. Talquin Build. Prods.*, 928 F.2d 649 (4th Cir. 1991); *Brown v. Granatelli*, 897 F.2d 1351 (5th Cir. 1990), *cert. denied*, 498 U.S. 848 (1990); *United Food & Commercial Workers and Employers Ariz. Health & Welfare Trust v. Pacyga*, 801 F.2d 1157 (9th Cir. 1986); *Moore v. Provident Life and Accident Ins. Co.*, 786 F.2d 922 (9th Cir. 1986). *But see* *Northern Group Servs., Inc. v. Auto Owners Ins. Co.*, 833 F.2d 85 (6th Cir. 1987), *cert. denied sub nom. Northern Group Servs., Inc. v. State Farm Mut. Auto. Ins. Co.*, 486 U.S. 1017 (1988); *Michigan United Food & Commercial Workers Unions v. Baerwaldt*, 767 F.2d 308 (6th Cir. 1985), *cert. denied*, 474 U.S. 1059 (1986). See generally Jeffrey G. Lenhart, *ERISA Preemption: The Effect of Stop-Loss Insurance on Self-Insured Health Plans*, 14 VA. TAX REV. 615 (1995).

24. Lenhart, *supra* note 23, at 619.

clause, section 514(a).<sup>25</sup> The clause preempts a state law if it “relate[s] to” an ERISA covered employee benefit plan. If the state law does not relate to an ERISA employee benefit plan, it is not preempted, and steps two and three are unnecessary.<sup>26</sup> If a state law does relate to an ERISA plan within the meaning of the preemption clause, the second step is to apply the “savings” clause, ERISA § 514(b)(2)(A).<sup>27</sup> A state law that would otherwise be preempted because it relates to an ERISA plan is saved from preemption if the law regulates the insurance industry.<sup>28</sup> Thus states retain their traditional power to regulate the insurance industry,<sup>29</sup> even if that regulation ultimately relates to an ERISA plan.

Step three qualifies the savings clause by applying the “deemer” clause, ERISA § 514(b)(2)(B).<sup>30</sup> The deemer clause states that a self-insured plan may not be deemed an insurance organization for the purposes of state regulation. Thus, a law that relates to an ERISA plan but is saved from preemption because it regulates insurance is nonetheless preempted by the deemer clause as applied to self-insured plans.

Not surprisingly, much litigation has arisen regarding the interpretation of each of the three steps. As the Supreme Court has wryly noted, the preemption sections of ERISA are “not a model of legislative drafting . . . while Congress occasionally decides to return to the States what it has previously taken away, it does not normally do both at the same time.”<sup>31</sup> Alas, the Court’s ERISA preemption jurisprudence is also not a model of judicial reasoning. The next section explores in greater detail how the Court applies these steps.

## 1. PREEMPTION

ERISA § 514(a) preempts “any and all State laws insofar as they may now or hereafter relate to any employee benefit plan.”<sup>32</sup> A state law relates to a benefit plan “if it has a connection with or reference to such a plan.”<sup>33</sup> Courts have interpreted this standard quite broadly,

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25. ERISA § 514(a), 29 U.S.C. § 1144(a).

26. *Travelers II*, 63 F.3d 89, 93 (2d Cir. 1995).

27. ERISA § 514(b)(2)(A), 29 U.S.C. § 1144(b)(2)(A).

28. *Id.*

29. Under the McCarran-Ferguson Act of 1945, states retain their power to regulate “the business of insurance” and no federal law may preempt that power without specifically stating its intention to do so. 15 U.S.C. § 1012(b) (1994). The “savings clause” reaffirms that power. ERISA § 514(b)(2)(A), 29 U.S.C. § 1144(b)(2)(A).

30. ERISA § 514(b)(2)(B), 29 U.S.C. § 1144(b)(2)(B).

31. *Metropolitan Life Ins. Co. v. Massachusetts*, 471 U.S. 724, 739-40 (1985).

32. ERISA § 514(a), 29 U.S.C. § 1144(a).

33. *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 96-97 (1983).

particularly as applied to causes of action brought under state law by plan participants or their beneficiaries.<sup>34</sup> The parade of ERISA preemption horrors is long and familiar.<sup>35</sup> Causes of action brought by participants under state law which have been preempted include wrongful death,<sup>36</sup> wrongful discharge,<sup>37</sup> unfair claims denials,<sup>38</sup> misrepresentation,<sup>39</sup> breach of contract,<sup>40</sup> negligence,<sup>41</sup> infliction of emotional distress,<sup>42</sup> unfair insurance practices,<sup>43</sup> breach of the covenant of good faith and fair dealing,<sup>44</sup> breach of statutory duties,<sup>45</sup> tortious interference,<sup>46</sup> bad faith,<sup>47</sup> breach of fiduciary duties,<sup>48</sup> fraud,<sup>49</sup> and conspiracy to defraud.<sup>50</sup> Several frustrated courts have noted the devastating impact of ERISA preemption on the ability of self-insured plan participants to obtain their reasonable benefits expectations.<sup>51</sup>

34. *FMC Corp. v. Holliday*, 498 U.S. 52, 58 (1990) ("The pre-emption clause is conspicuous for its breadth.").

35. See Jayne Elizabeth Zanglein, *Closing the Gap: Safeguarding Participants' Rights by Expanding the Federal Common Law of ERISA*, 72 WASH. U. L.Q. 671 (1994).

36. See *Corcoran v. United HealthCare, Inc.*, 965 F.2d 1321 (5th Cir.), *cert. denied*, 506 U.S. 1033 (1992).

37. See *Ingersoll-Rand Co. v. McClendon*, 498 U.S. 133 (1990).

38. See *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41 (1987).

39. See *Degan v. Ford Motor Co.*, 869 F.2d 889 (5th Cir. 1989).

40. See *Kuhl v. Lincoln Nat'l Health Plan*, 999 F.2d 298 (8th Cir. 1993), *cert. denied*, 510 U.S. 1045 (1994).

41. See *Greany v. Western Farm Bureau Life Ins. Co.*, 973 F.2d 812 (9th Cir. 1992).

42. See *Powell v. Chesapeake & Potomac Tel. Co.*, 780 F.2d 419, (4th Cir. 1985), *cert. denied*, 476 U.S. 1170 (1986).

43. See *Kanne v. Connecticut Gen. Life Ins. Co.*, 867 F.2d 489 (9th Cir. 1988), *cert. denied*, 492 U.S. 906 (1989).

44. *Id.*

45. *Id.*

46. *Kuhl*, 999 F.2d at 302-03.

47. *Tomczyk v. Blue Cross & Blue Shield*, 715 F. Supp. 914 (E.D. Wis. 1989), *aff'd*, 951 F.2d 771 (7th Cir. 1991), *cert. denied*, 504 U.S. 940 (1992).

48. *Davidian v. Southern California Meat Cutters Union*, 859 F.2d 134 (9th Cir. 1988).

49. *Johnson v. District 2 Marine Eng. Beneficial Ass'n*, 857 F.2d 514 (9th Cir. 1988).

50. *Jelicic v. Hartford Ins. Co.*, 917 F.2d 1307 (9th Cir. 1990), *cert. denied*, 502 U.S. 839 (1991).

51. See, e.g., *Smith v. Hartford Ins. Group*, 6 F.3d 131, 146 (3d Cir. 1993) (Hutchinson, J., dissenting) ("The feeling of unfairness is palpable."); *Sanson v. General Motors Corp.*, 966 F.2d 618, 623, 625 (11th Cir. 1992) (Birch, J., dissenting) ("An employer in this circuit can now hoodwink a long time employee and leave him stranded without any recourse whatsoever . . . obviously the Supreme Court needs to do some serious bushhogging in the ERISA preemption thicket."), *cert. denied*, 507 U.S. 984 (1993); *Olson v. General Dynamics Corp.*, 960 F.2d 1418, 1423-24 (9th Cir. 1991)

Perhaps the clearest example of the stunning breadth of ERISA preemption of state law causes of action is revealed in *Ingersoll-Rand Co. v. McClendon*.<sup>52</sup> In *Ingersoll-Rand*, the United States Supreme Court ruled that ERISA preempts employee wrongful discharge claims in which an employee alleges that the discharge was motivated by the employer's desire to avoid making contributions to the employee's ERISA-covered pension fund.<sup>53</sup> The Court reasoned that in order to determine the veracity of the employee's allegations it must determine whether an ERISA-covered pension fund existed.<sup>54</sup> Because the state cause of action forced the Court to acknowledge the *existence* of the plan, the state cause of action related to an ERISA plan, and was therefore preempted.<sup>55</sup> Further, the Court noted that preemption can be triggered even if the state law in question is not designed to affect ERISA plans, affects them only indirectly, or is consistent with ERISA's substantive requirements.<sup>56</sup>

Direct—and to some extent, indirect—state regulation of ERISA plans is also preempted. Courts have found that ERISA preempts laws that “provide an alternative cause of action to employees to collect benefits protected by ERISA, [which] refer specifically to ERISA plans and apply solely to them, or interfere with the calculation of benefits owed to an employee.”<sup>57</sup> For example, in *Shaw v. Delta Airlines, Inc.*,<sup>58</sup> the Supreme Court ruled that the New York Human Rights Law, which forbade employment discrimination based on pregnancy and mandated that employers offer disability benefits for pregnancy, had “a connection” to employee benefits plans, and therefore was related to such plans.<sup>59</sup> The Court concluded that ERISA preempted the law “insofar as it prohibits practices that are lawful under federal law.”<sup>60</sup> In other words, as long as the state law sought to prevent employee benefits discrimination not unlawful under federal law, ERISA preempted it.

While the scope of ERISA's preemption is broad, there are some limitations to its reach. But the courts have been unclear about where

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(Reinhardt, J., concurring) (“[A] statute designed to safeguard employee retirement benefits has, all too frequently, been used to deprive employees of rights they previously enjoyed under state law while failing to provide any comparable federal remedy.”), *cert. denied*, 504 U.S. 986 (1992).

52. 498 U.S. 133 (1990).

53. *Ingersoll-Rand*, 498 U.S. at 145.

54. *Id.* at 140.

55. *Id.*

56. *Id.* at 139 (citing *Metropolitan Life*, 471 U.S. at 739).

57. *AETNA Life Ins. Co. v. Borges*, 869 F.2d 142, 146 (2d Cir. 1989), *cert. denied*, 493 U.S. 811 (1990).

58. 463 U.S. 85 (1983).

59. *Shaw*, 463 U.S. at 96.

60. *Id.* at 108.

those boundaries lie.<sup>61</sup> Courts have concocted a host of nebulous tests and have applied them inconsistently. For example, ERISA does not always preempt state laws that are “of general application—often traditional exercises of state power or regulatory authority—whose effect on ERISA plans is incidental,”<sup>62</sup> or whose impact on an ERISA-covered plan is “tenuous, remote, or peripheral.”<sup>63</sup> Rather, preemption is triggered by “an effect on the primary administrative functions of benefit plans, such as determining an employee’s eligibility for a benefit and the amount of that benefit.”<sup>64</sup> Thus ERISA does not preempt state laws requiring companies to make lump-sum severance payments when closing a plant,<sup>65</sup> laws prescribing what hospitals can charge (and thereby preventing plans from negotiating their own rates with the hospitals),<sup>66</sup> laws imposing a city income tax of general application that affects employee contributions to benefit plans,<sup>67</sup> and general escheat laws.<sup>68</sup>

In *Mackey v. Lanier Collection Agency & Service, Inc.*,<sup>69</sup> the Supreme Court found that ERISA preempted a Georgia statute that singled out ERISA welfare plan benefits for protective treatment under state garnishment procedures.<sup>70</sup> However, ERISA did not forbid the garnishment of welfare benefits even where the purpose of the garnishments was to collect judgments against plan participants.<sup>71</sup> In other words, neither state nor federal law protected plan benefits from garnishment. The Court held that since ERISA expressly bars the garnishment of pension benefit plans, but is silent on the matter of garnishment of welfare benefit plans, “Congress did not intend to preclude state-law attachment of ERISA welfare plan benefits.”<sup>72</sup>

This reasoning reveals more the breadth than the limits of ERISA preemption; one can infer that actions against welfare benefit plans are not barred only where Congress has been silent with regard to such actions while explicitly barring actions against ERISA pension plans. Had

61. As more than one confused court has understated, “the distinction between state laws that ‘relate to’ employee benefit plans and those that have only a ‘tenuous, remote, or peripheral’ impact is not always clear.” *AETNA*, 869 F.2d at 145.

62. *Id.* at 146.

63. *Id.* at 145 (citing *Shaw*, 463 U.S. at 100 n.21).

64. *Id.* at 146-47.

65. *See Fort Halifax Packing Co. v. Coyne*, 482 U.S. 1 (1987).

66. *See Rebaldo v. Cuomo*, 749 F.2d 133 (6th Cir. 1985), *cert denied*, 472 U.S. 1008.

67. *See Firestone Tire & Rubber Co. v. Neusser*, 810 F.2d 550 (6th Cir. 1987).

68. *AETNA*, 869 F.2d at 147.

69. 486 U.S. 825 (1988).

70. *Mackey*, 486 U.S. at 829.

71. *Id.* at 832.

72. *Id.* at 838.

Congress been completely silent, the Court would have presumed preemption of the cause of action against both types of ERISA plans.<sup>73</sup> Writing in dissent, Justice Kennedy argued that the breadth of ERISA's preemption clause mandates the presumption that it preempts the garnishment laws as applied to ERISA employee benefit plans. He reasoned that these laws related to the plans by subjecting them to administrative burdens.<sup>74</sup>

The only thing undeniably clear about ERISA's preemption clause is its breadth. The clause preempts all state law causes of action. It also preempts all direct state regulations of ERISA plans—regulations which affect the structure, administration, or benefits offered; have a connection or reference to ERISA plans; provide an alternate cause of action to employees to collect benefits provided by ERISA; refer specifically to ERISA plans and apply solely to them; or interfere with the calculation of benefits owed to an employee. State regulations which have an indirect affect on ERISA plans—that is, regulations which are of general applicability and which have tenuous, remote and peripheral economic and administrative affects on ERISA plans—are not preempted. In reality, these are little more than labels applied by courts groping their way through the ERISA preemption analysis. However, ERISA provides one important limitation to the scope of its own preemption: the savings clause.

## 2. THE SAVINGS CLAUSE

The second step in ERISA preemption analysis is application of the savings clause. Section 514(b)(2)(A) saves from preemption any state law regulating insurance.<sup>75</sup> A law that relates to insurance is not preempted, even though that insurance is used by an ERISA plan.<sup>76</sup> Thus in *Metropolitan Life Insurance Co. v. Massachusetts*,<sup>77</sup> the Supreme Court found that ERISA did not preempt a Massachusetts statute requiring that minimum mental health care benefits be provided to employees through insurance sold in the state.<sup>78</sup> Because the law regulated insurance, it was saved from otherwise certain preemption by section 514(b)(2)(A).<sup>79</sup>

The savings clause saves from ERISA preemption a host of traditional state regulations governing the sale of insurance within the

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73. *Id.* at 837.

74. *Id.* at 842 (Kennedy, J., dissenting).

75. ERISA § 514(a)(2)(A), 29 U.S.C. § 1144(a)(2)(A).

76. *Id.*

77. 471 U.S. 724 (1985).

78. *Metropolitan Life*, 471 U.S. at 744.

79. *Id.* at 739.

state. For example, as the Court noted in *Metropolitan Life*, all fifty states now require that insurance coverage of infants begin at birth, rather than at some time shortly thereafter, as had been market practice prior to regulation.<sup>80</sup> Further, many states require that insurers offer particular kinds of coverage, or coverage provided by particular types of health care providers.<sup>81</sup> ERISA does not preempt these regulations of insurance despite relating to ERISA employee benefit plans, because the savings clause saves them from preemption.

### 3. THE DEEMER CLAUSE

The third step in the preemption analysis requires application of ERISA § 514(b)(2)(B), the deemer clause.<sup>82</sup> Section 514(b)(2)(B) states that self-insured plans cannot be deemed an insurance organization for purposes of state regulation.<sup>83</sup> In other words, any law preempted by ERISA, but preserved by the savings clause as regulating insurance, is nonetheless preempted as applied to self-insured plans. Thus the statute at issue in *Metropolitan Life* was saved from preemption as applied to employee benefit plans that purchased insurance, but was again preempted as applied to self-funded plans because those plans could not be deemed insurance.<sup>84</sup> As the Court acknowledged, this interpretation “results in a distinction between insured and uninsured plans, leaving the former open to indirect regulation while the latter are not.”<sup>85</sup> However, the Court has justified that interpretation as merely giving life to a distinction created by Congress in section 514(b)(2)(B), “a distinction Congress is aware of and one it has chosen not to alter.”<sup>86</sup>

In *FMC Corp. v. Holliday*,<sup>87</sup> the Supreme Court ruled that ERISA preempted a Pennsylvania anti-subrogation law<sup>88</sup> as it applied to self-insured employee health benefit plans, but not as it applied to contract-

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80. *Id.* at 729 (citing Appellate Brief for American Public Health Association et al. as *Amici Curiae* (listing state statutes)).

81. *Id.*

82. ERISA § 514(b)(2)(B), 29 U.S.C. § 1144(b)(2)(B).

83. *Id.*

84. *Metropolitan Life*, 471 U.S. at 747.

85. *Id.*

86. *Id.* (citing H.R. Rep. No. 94-1785, a 1977 Activity Report of the House Committee on Education and Labor that recognized the difference in treatment between insured and self-insured plans).

87. 498 U.S. 52 (1990).

88. Section 1720 of Pennsylvania's Motor Vehicle Financial Responsibility Law, 75 PA. CONST. STAT. § 1720 (1987), prohibited employee benefit plans, as well as other insurance arrangements, from collecting reimbursement of health care expenses paid out by the plan to participants who had subsequently recovered damages in tort.

insured plans.<sup>89</sup> The Court acknowledged the odd distinction drawn between the regulation of contract-insured and self-insured plans, but held that the deemer clause mandated it: "Our interpretation of the deemer clause makes clear that if a plan is insured, a State may regulate it indirectly through regulation of its insurer and its insurer's insurance contracts; if the plan is uninsured, the State may not regulate it."<sup>90</sup>

Justice Stevens, dissenting, argued that the Court's interpretation of ERISA drew "a broad and illogical distinction between benefit plans that are funded by the employer (self-insured plans) and those that are insured by regulated insurance companies (insured plans)."<sup>91</sup> Justice Stevens reminded the Court that from the standpoint of plan participants, who are intended to be the prime beneficiaries of ERISA, there is "no apparent reason" for drawing such a distinction.<sup>92</sup> Further, according to Stevens, such an interpretation would undermine the congressional intent in passing ERISA of providing uniformity in employee benefit laws.<sup>93</sup>

Justice Stevens also argued that applying the deemer clause and savings clause was unnecessary because the Court should not have found that the anti-subrogation statute related to an employee benefit plan at all.<sup>94</sup> He argued that the anti-subrogation statute was not unambiguously the kind of law Congress intended to preempt with respect to employee benefit plans, and that where there was ambiguity regarding a statutory preemption of state law, the Court should apply a strong presumption against preemption.<sup>95</sup> Applying that presumption, Stevens first found that Congress did not intend to preempt Pennsylvania's anti-subrogation statute as applied to ERISA plans. Second, even if it did, it certainly did not intend to "pre-empt enforcement of that statute against self-insured plans while preserving enforcement against insured plans."<sup>96</sup>

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89. *FMC Corp.*, 498 U.S. at 65.

90. *Id.* at 64.

91. *Id.* at 65 (Stevens, J., dissenting).

92. *Id.* at 66 (Stevens, J., dissenting).

93. *Id.* (Stevens, J., dissenting).

94. *FMC Corp.*, 498 U.S. at 66 (Stevens, J., dissenting).

95. *Id.* at 67 (Stevens, J., dissenting) (citing *Mackey v. Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825 (1988)).

96. *Id.* (Stevens, J., dissenting).

### III. RECENT CASES THAT OPEN THE POSSIBILITY FOR STATE ACTION FOR THE PROTECTION OF PLAN PARTICIPANTS IN THE EVENT OF PLAN FAILURE

#### A. Failures of the Past

As demonstrated in *Shaw*, *Metropolitan Life*, and *Holliday*, ERISA preemption can undo state laws aimed at various aspects of health care reform. State attempts to reform health care have been turned back either by ERISA preemption generally, or—for state laws that regulate insurance and are thus saved by the savings clause—by the deemer clause's preemption of those laws as applied to self-insured plans.

For example, in *St. Paul Electrical Workers Welfare Fund v. Markman*,<sup>97</sup> self-insurers successfully challenged the application of certain provisions of the Minnesota Comprehensive Health Insurance Act to their plans.<sup>98</sup> Among its several provisions, the Act created substantive and reporting mandates for insurers. Self-insurers argued that the Act subjected them to both substantive and reporting requirements of state insurance laws, and was thus preempted by the deemer clause.<sup>99</sup> The court agreed, and permanently enjoined the state from enforcing the Act's requirements against self-insured plans.<sup>100</sup>

Similarly, in *General Split Corp. v. Mitchell*,<sup>101</sup> the court held that ERISA preempted the provisions of a Wisconsin law as applied to self-insured ERISA plans. The provisions mandated certain conversion benefits for health insurance plans and established the Wisconsin Health Insurance Risk Sharing Plan (HIRSP), a program that provides health insurance to individuals whose physical or mental conditions prevent them from obtaining private market health insurance.<sup>102</sup> Relying largely on *St. Paul Electrical Workers*, the court held that the law mandating conversion benefits related to ERISA plans, but was saved from preemption as applied to insurance contract plans through the savings clause.<sup>103</sup> However, the court found that the deemer clause preempted state imposition of substantive provisions on self-insured ERISA plans.<sup>104</sup> Further, the court held that the provision mandating tax assessments for contribution to the HIRSP fund, which otherwise would

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97. 490 F. Supp. 931 (D. Minn. 1980).
  98. *St. Paul Elec. Workers*, 490 F. Supp. at 934.
  99. *Id.* at 933.
  100. *Id.* at 934.
  101. 523 F. Supp. 427 (E.D. Wis. 1981).
  102. *Mitchell*, 523 F. Supp. at 430.
  103. *Id.*
  104. *Id.*

have been preempted by ERISA for relating to an employee benefit plan, was not preempted as applied to insurance contract plans because of the savings clause.<sup>105</sup> Nevertheless, it was preempted as applied to self-insured plans because of the deemer clause.<sup>106</sup> The state argued that even if it could not tax the self-insured plans themselves, it could tax the sale of stop-loss insurance to them under traditional insurance regulation powers. But this argument was rejected.<sup>107</sup> The court observed that the state did not assess the tax on the stop-loss premium paid by the plans, but rather on the level of benefits the plans themselves paid out to participants.<sup>108</sup> Therefore, the court concluded that the tax applied to the plans themselves and not to the sale of stop-loss insurance to the plans.<sup>109</sup>

### B. United Wire

In *United Wire, Metal and Machine Health and Welfare Fund v. Morristown Memorial Hospital*,<sup>110</sup> the United States Court of Appeals for the Third Circuit held that ERISA did not preempt a New Jersey statute<sup>111</sup> that forced self-insured plans to pay hospital use surcharges.<sup>112</sup> The surcharges were used by the state to pay the costs of indigent care and bad debts, state medicare subsidies, as well as to reimburse hospitals for discounts given to other types of plans.<sup>113</sup> The district court had held that ERISA preempted the statute.<sup>114</sup> It reasoned that the statute would subject ERISA plans to administrative costs, and force them to pay hospital costs for non-participants in their plans.<sup>115</sup> Therefore, the statute related to the plans, triggering preemption.<sup>116</sup> The Court of Appeals disagreed.<sup>117</sup>

The court first noted the breadth of ERISA's preemption. The court explained that a law relates to an ERISA plan "if it is specifically designed to affect employee benefit plans, if it singles out such plans for

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105. *Id.*

106. *Id.* at 431.

107. *Mitchell*, 523 F. Supp. at 431.

108. *Id.*

109. *Id.*

110. 995 F.2d 1179 (3d Cir. 1993).

111. N.J. STAT. ANN. § 26:2H-1 (repealed 1993).

112. *United Wire*, 995 F.2d at 1189.

113. *Id.* at 1196.

114. *United Wire, Metal & Mach. Health and Welfare Fund v. Morristown Memorial Hosp.*, 793 F. Supp. 524, 537 (D.N.J. 1992).

115. *Id.*

116. *Id.*

117. *United Wire*, 995 F.2d at 1196.

special treatment, or if the rights or restrictions it creates are predicated on the existence of such a plan."<sup>118</sup> Further, ERISA may preempt a state law even though there is no "direct nexus" with ERISA plans, provided the effect of the state law is to restrict the options of ERISA plans in their choice of benefits, structure, reporting and administration, or if such laws would impair the ability of an ERISA plan to function simultaneously in more than one state.<sup>119</sup>

Despite the breadth of ERISA preemption, the court upheld the New Jersey law. The court noted the state law in question was one of general applicability, did not single out ERISA plans for special treatment, and functioned regardless of the existence of ERISA plans. Moreover, the effect of the law—an increase in the costs of hospital use—was no different from any number of state regulations that increased the costs of hospital use, such as utility costs, employee wages, and waste disposal costs.<sup>120</sup> The court considered the surcharges a function of the state police power to control the price of certain services and commodities, such as public utilities, minimum wages, and rent control.<sup>121</sup> The court held that the Congress could not have intended indirect economic influence of such regulations on plan costs to trigger ERISA's preemption clause.<sup>122</sup> The statute was not intended to regulate the affairs of ERISA plans.<sup>123</sup> It did not single out ERISA plans for special treatment, nor did it predicate rights or obligations on the existence of such plans.<sup>124</sup> The statute did not dictate or restrict either the structure of ERISA plans or the conduct of their affairs.<sup>125</sup> It did not impair the ability of such a plan to operate simultaneously in more than one state.<sup>126</sup> Finally, the statute had only an indirect economic influence on the plans, not unlike

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118. *Id.* at 1192 (citing *District of Columbia v. Greater Washington Bd. of Trade*, 506 U.S. 125 (1992); *Ingersoll-Rand Co. v. McClendon*, 498 U.S. 133 (1990); *Mackey v. Lanier Collection Agency & Serv., Inc.*, 486 U.S. 825 (1988); *McCoy v. Massachusetts Inst. of Technology*, 950 F.2d 13 (1st Cir. 1991); *Bricklayers Local 33 v. America's Marble Source*, 950 F.2d 114 (3d Cir. 1991); *McMahon v. McDowell* 794 F.2d 100 (3d Cir. 1986), *cert. denied*, 479 U.S. 971 (1986)).

119. *United Wire*, 995 F.2d at 1193 (citing *FMC Corp. v. Holliday*, 498 U.S. 52 (1990); *Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504 (1981); *Hampton Indus., Inc. v. Sparrow*, 981 F.2d 726 (4th Cir. 1992); *Nat'l Elevator Indus., Inc. v. Calhoun*, 957 F.2d 1555 (10th Cir. 1992); *Arkansas Blue Cross & Blue Shield v. St. Mary's Hospital*, 947 F.2d 1341 (8th Cir. 1991), *cert. denied*, 504 U.S. 957 (1992); *Michigan Carpenters Council v. C.J. Rogers, Inc.*, 933 F.2d 376 (6th Cir. 1991)).

120. *Id.*

121. *Id.*

122. *Id.*

123. *Id.* at 1195.

124. *United Wire*, 995 F.2d at 1195.

125. *Id.* at 1179.

126. *Id.*

any number of other factors that increase the costs of doing business.<sup>127</sup> Therefore, the statute did not relate to the plans strongly enough to trigger preemption.<sup>128</sup>

The court noted that this ruling squarely conflicted with a recent decision of the Southern District of New York. In *Travelers Insurance Co. v. Cuomo*,<sup>129</sup> the New York court had found that a nearly identical New York statute mandating hospital surcharges for certain types of insurers was preempted as applied to ERISA-covered employee benefit plans. The Supreme Court eventually resolved the conflict in *Travelers Insurance Co. v. Pataki (Travelers I)*.<sup>130</sup>

### C. Travelers I

In *Travelers I*, the Supreme Court limited the scope of ERISA preemption by unanimously holding that ERISA did not preempt a New York statute requiring hospitals to collect surcharges from patients covered by commercial insurers, but not from patients insured by Blue Cross/Blue Shield.<sup>131</sup> The insurers had claimed that the statute “related to” employee benefit plans and was therefore preempted by ERISA.<sup>132</sup>

The Court applied the *Shaw* related to test to the New York statute. It reasoned that in determining whether the statute had a “connection with” an ERISA plan, it would look to ERISA’s objectives as a guide to what Congress intended to preempt.<sup>133</sup> The Court then reasoned that ERISA preempted state laws that mandated employee benefit structures or their administration, as well as laws that provided alternate ERISA enforcement mechanisms.<sup>134</sup> The surcharges did not fall within those categories.<sup>135</sup> New York intended the surcharges only to make Blue Cross/Blue Shield more attractive than other commercial insurers, because, unlike the latter, Blue Cross helped the state provide insurance to people who could not otherwise afford or obtain it.<sup>136</sup> The Court was undeterred by the fact that the statute created cost discrepancies between different types of insurance because it found that cost uniformity was not

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127. *Id.* at 1196.

128. *Id.*

129. 813 F. Supp 996 (S.D.N.Y. 1993).

130. 115 S. Ct. 1671 (1995).

131. *Travelers I*, 115 S. Ct. at 1683; *see also* N.Y. PUB. HEALTH LAW §§ 2807, 2807-c(1)(b), 2807-c(1)(a) (McKinney 1993).

132. *Travelers I*, 115 S. Ct. at 1675.

133. *Id.* at 1677.

134. *Id.* at 1680.

135. *Id.* at 1679.

136. *Id.* at 1678.

an objective of ERISA.<sup>137</sup> Moreover, echoing *United Wire*, the Court reasoned that the indirect economic effect of the surcharges in increasing plan costs was not unlike many other costs of state regulation faced by insurers, such as quality control standards and workplace regulation, which do not trigger preemption.<sup>138</sup> Hence, the Court concluded that both the purpose and effect of the New York statute did not directly relate to the objectives of ERISA, and was thus not preempted by it.<sup>139</sup>

Indeed, the Supreme Court's reading of the preemption clause in *Travelers I* revealed even more tolerance for state regulation than the Third Circuit in *United Wire*. For example, while *United Wire* emphasized that the surcharge statute in question was of general applicability and did not single out ERISA plans for special treatment, *Travelers I* made no mention of those considerations. In fact, the surcharge statute at issue in *Travelers I* was not of general applicability because it applied only to some employee benefit plan participants' hospital usage (including ERISA self-funded plan members) and not others. The Court made clear that ERISA does not preempt only direct regulation of ERISA plans. It noted that "a state law might produce such acute, albeit indirect, economic effects, by intent or otherwise, as to force an ERISA plan to adopt a certain scheme of substantive coverage or effectively restrict its choice of insurers, and that such a state law might indeed be pre-empted."<sup>140</sup> But the New York statute did not have that effect; it affected "only indirectly the relative prices of insurance policies, a result no different from myriad state laws in areas traditionally subject to local regulation, which Congress could not possibly have intended to eliminate."<sup>141</sup>

In other words, laws which indirectly affect the relative prices of ERISA-covered insurance plans, but which do not impact those plans by regulating the terms or administration of them, do not relate to those plans strongly enough to trigger preemption. Because those state laws do not "relate to" employee benefit plans strongly enough to trigger preemption, it would seem that neither the savings clause nor the deemer clause applies. However, the Court did not consider whether the surcharge was preempted as applied to self-insured plans.<sup>142</sup> Instead, it remanded the question to the court of appeals, which had not expressly addressed the preemption of surcharges on self-insured plans.<sup>143</sup>

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137. *Travelers I*, 115 S. Ct. at 1678.

138. *Id.*

139. *Id.*

140. *Id.* at 1683.

141. *Id.* at 1683.

142. *Travelers I*, 115 S. Ct. at 1675 n.4.

143. *Id.*

#### D. Travelers II, on remand

On remand, the Second Circuit Court of Appeals ruled that ERISA did not preempt the surcharges as applied to self-insured plans.<sup>144</sup> As the court of appeals read “ERISA’s Delphic preemption provision,”<sup>145</sup> a plan’s self-insured status is relevant for purposes of applying the deemer clause when a statute relating to an employee benefit plan has been spared preemption by the savings clause.<sup>146</sup> Because the Supreme Court had held that the New York statute did not relate to ERISA plans generally, it could not “nevertheless, still relate to self-insured plans specifically.”<sup>147</sup> The court reasoned that the indirect effect of the surcharge on self-insured plans is the same as the effect on other ERISA plans; if the effect does not trigger preemption for other ERISA plans, it cannot do so for self-insured plans.<sup>148</sup> Like the surcharges on other plans, the surcharges on self-insured plans do “not bind plan administrators to any particular choice.”<sup>149</sup> Relying on the Supreme Court decision in *Travelers I*, the court of appeals thus held that New York may assess surcharges on hospital use by members of ERISA self-insured employee health benefit plans.<sup>150</sup>

#### E. Safeco v. Musser

The United States Court of Appeals for the Seventh Circuit recently held that Wisconsin may levy taxes on the sale of stop-loss insurance to otherwise self-insured ERISA plans without triggering preemption.<sup>151</sup> Wisconsin uses the taxes collected from health insurers to fund the HIRSP.<sup>152</sup> The plaintiff insurance companies claimed that the statute, which concededly regulated insurance, was saved as applied to contract-insurance plans, but was preempted by the deemer clause as applied to the sale of stop-loss insurance to otherwise self-insured plans.<sup>153</sup> The Seventh Circuit postponed its decision pending the Supreme Court’s

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144. *Travelers II*, 63 F.3d 89, 93 (2d Cir. 1995).

145. *Id.*

146. *Id.*

147. *Id.* (emphasis deleted).

148. *Id.*

149. *Travelers II*, 63 F.3d at 94 (quoting *Travelers I*, 115 S. Ct. at 1679).

150. *Id.* at 94-95.

151. *Safeco Life Ins. Co. v. Musser*, 65 F.3d 647, 648 (7th Cir. 1995).

152. *Id.*; see also *General Split Corp. v. Mitchell*, 523 F. Supp. 427, 429 (E.D. Wis. 1981).

153. *Safeco*, 65 F.3d at 650.

decision in *Travelers I*.<sup>154</sup> Relying on the *Travelers I* and *II* decisions, the Seventh Circuit disagreed.<sup>155</sup>

The court held that the HIRSP assessments did not relate to ERISA plans within the meaning of ERISA's preemption doctrine.<sup>156</sup> Like the surcharges at issue in *Travelers I* and *II*, the HIRSP assessments were held to have an indirect influence on the plans, because they did not bind plan administrators to any particular choice.<sup>157</sup> Like the surcharges, the assessments impacted the plans through increased costs without attempting to mandate what benefits were offered or how they were administered: "[b]ecause the HIRSP assessments imposed by Wisconsin on health insurance carriers do not interfere with the provisions or administration of ERISA plans, the assessments do not relate to such plans in a manner significant enough to implicate the preemption clause of the statute."<sup>158</sup> Thus there was no need to undergo the second and third stages of the preemption analysis.<sup>159</sup> Further, unlike the assessments at issue in *Mitchell*, these assessments were based on the sale of the stop-loss insurance, not on the level of benefits paid out by the individual plans.<sup>160</sup>

#### IV. PROPOSALS FOR REFORM TO PROTECT SELF-INSURED PLAN PARTICIPANTS IN THE EVENT OF PLAN FAILURE

##### *A. Possibilities for Federal Reform*

The most logical way to reform the preemption effects of a federal statute such as ERISA is to amend the statute itself. Recently, the Clinton Administration's Health Security Act of 1993 attempted to reform ERISA so as to protect self-insured plan participants and health care providers in the event of plan failure. The proposed Act mandated minimum funding requirements for self-insured employee welfare plans.<sup>161</sup> It also

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154. *Id.* at 651 n.3.

155. *Id.* at 653.

156. *Id.*

157. *Id.*

158. *Safeco*, 65 F.3d at 653.

159. *Id.*

160. *Id.*

161. Self-funded health plans would have been required to maintain a trust fund at a level equal to the estimated amount owed to health care providers. The trust fund would have been protected by special status in bankruptcy proceedings in the event of employer failure. The Department of Labor would have overseen a national guaranty fund for self-insured health plans to provide financial protection for participants and health care providers in the event of plan failure. As previously noted, because states have been unable to assess self-insured plans for contribution to state insurance guaranty funds, most

established a national employee welfare benefit guaranty corporation to insure that self-insured plan participants would be able to cover outstanding health care bills if and when plans failed.<sup>162</sup> These reforms would have provided significant protection for self-insured plan participants in the event of plan failure.<sup>163</sup> But Congress failed to pass the Act.<sup>164</sup> Despite Congress' increased interest in shifting power from the federal government to state governments, it has shown little interest in reforming or removing ERISA's preemption power.<sup>165</sup> As increasing numbers of businesses offer self-insured plans free from state regulation, it seems less likely that federal reform will emerge easily or quickly. Therefore, in the absence of federal reform, states should act within the permissible bounds of ERISA preemption to protect self-insured plan participants faced with outstanding health care bills arising from plan failure.

### B. Possibilities for State Reform

Like many states, Wisconsin has an insurance guaranty fund to protect insurance plan participants in the event of plan failure.<sup>166</sup> The state finances the insurance guaranty fund by assessing taxes on insurance company plans.<sup>167</sup> However, because self-insured plans have not been assessed for taxes to contribute to those funds (because they are preempted by ERISA's deemer clause), self-insured plan participants are not included in the guaranty fund's protection.<sup>168</sup>

However, under the *Travelers* and *Safeco* decisions, it may be possible for Wisconsin, as well as other states, to indirectly assess all employee health benefit plans, including self-insured, for contribution to state insurance guaranty funds. The state could levy taxes on the sale of stop-loss insurance and impose hospital use surcharges without triggering ERISA's preemption clause. A direct tax on self-insured plans based on their level of income would still almost certainly trigger ERISA

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self-insured plan participants are not included in the protection of those funds. See THE WHITE HOUSE DOMESTIC POLICY COUNCIL, THE PRESIDENT'S HEALTH SECURITY PLAN: THE CLINTON BLUEPRINT 79-80 (1993); see also *supra* part III.A.

162. WHITE HOUSE DOMESTIC POLICY COUNCIL, *supra* note 162, at 79-80.

163. *Id.*

164. See J. Geisel, *Reforms Doomed from Start*, BUS. INS., Dec. 26, 1994, at 32.

165. See James E. Holloway, *ERISA, Preemption and Comprehensive Federal Health Care: A Call for "Cooperative Federalism" to Preserve the States' Role in Formulating Health Care Policy*, 16 CAMPBELL L. REV. 405, 406-08, 454-55 (1994).

166. WIS. STAT. § 646 (1995-1996).

167. WIS. STAT. § 646.51. Such taxes would be preempted by ERISA, but are saved by the savings clause.

168. WIS. STAT. § 646.01(b)(9).

preemption, as it did in *Mitchell*. However, generally applicable surcharges on hospital use and assessments on the sale of stop-loss insurance would have the same indirect economic influence on the plans as those allowed under *Travelers I* and *II*, *United Wire*, and *Safeco*.

Although such surcharges and assessments might result in slight price discrepancies between self-insured and contract-insured plans, the Supreme Court noted in *Travelers I* that price uniformity is not an object of ERISA.<sup>169</sup> Price discrepancies are unlikely, however, because contract-insured plans already must contribute to the guaranty funds through taxes; in fact, the result might be price equalization. Any argument that self-insured plans were being singled out for extra burdens would seem specious in light of the special privileges such plans currently enjoy.

ERISA self-insured health benefit plans have a clear competitive advantage over insurance contract plans, because self-insured plans have been able to avoid assessments such as contributions to state insurance guaranty funds and HIRSP, as well as minimum funding requirements. Indeed, this is one reason for the rapidly growing popularity of self-funded plans among employers. *Travelers*, *United Wire* and *Safeco* may be understood as an attempt to correct this unintended health care market advantage. The state interest in a competitive and safe health care market should encourage reformers to explore the possibility of assessing self-funded health care plans for contribution to state insurance guaranty funds.

Unlike the assessments levied on the sale of stop-loss insurance allowed in *Safeco*, those proposed here would use the collected revenues to contribute to the state insurance guaranty fund rather than to purchase insurance for those cannot obtain it in the private market (e.g., HIRSP). Beyond that, the assessments and surcharges proposed here are notably similar to the ones allowed in *United Wire*, *Travelers*, and *Safeco*. Like them, the surcharges and assessments suggested here would have almost no influence on the provisions or administration of the plans. Unlike the statute mandating disability benefits for pregnant employees preempted in *Shaw*, for example, these taxes and surcharges would not determine the substantive provisions of plans.

For preemption purposes, what the state does with the revenues collected from assessments on the sale of stop-loss insurance should be irrelevant. Assessments on the sale of stop-loss insurance collected to benefit the state insurance guaranty fund do not relate to self-funded plans more directly than assessments collected to benefit insurance programs for people who cannot obtain it in the private market. As long as the

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169. *Travelers I*, 115 S. Ct. 1671, 1680 (1995).

surcharges and assessments proposed here have a similarly *indirect* impact on the plans (i.e., they do not directly affect the administration or substantive choices of the plans) they will not relate to those plans, and thus like the surcharges and assessments allowed in *Travelers*, *United Wire* and *Safeco*, should not trigger ERISA preemption. Self-insured plans would no longer be able to avoid contributing to state insurance guaranty funds.

Of course some allowance would have to be made for distinctions among self-insured plans. Self-insured plans that do not purchase stop-loss insurance could be assessed entirely through surcharges on hospital use, while plans that do purchase stop-loss insurance could be assessed either entirely through taxes on the sale of the stop-loss insurance, or through a combination of taxes on that sale and surcharges on hospital use. One unintended effect of taxing the sale of stop-loss insurance may be to reduce the number of plans that purchase it. However, revenue for the state insurance guaranty fund lost through a reduction in the purchase of stop-loss insurance could be made up by hospital use surcharges. Thus, contributions to the state insurance guaranty fund might be maintained despite the reduction in the purchase of stop-loss insurance.

Further, while stop-loss insurance provides some protection for plan participants in the event of plan failure, it is neither necessarily adequate nor uniform. An employer may purchase stop-loss insurance at any level she desires, and may tailor the plan to suit particular needs. Thus stop-loss insurance plans differ from employer to employer in regard to the amount of protection they provide. In contrast, protection through the state insurance guaranty fund is adequate to cover outstanding bills regardless of employer preferences. Therefore plan participants face less risk when protected by the state insurance guaranty fund than by stop-loss insurance. Even if some plans decide to forgo stop-loss insurance in response to taxes on its sale, the alternate surcharge mechanism would provide satisfactory protection through contributions to the state insurance guaranty fund. Furthermore, assessments could be structured to create incentives for plans to purchase stop-loss insurance by assessing more through hospital use surcharges than through taxes on the sale of stop-loss insurance.

Another more serious unintended effect of the surcharges and taxes proposed here might be to reduce the number of employers who offer their employees health insurance plans at all. However, the number of employers driven from offering health insurance because of these surcharges and taxes is unlikely to be significant for at least two reasons. First, employers can pass along the slight increase in insurance costs directly to the employees. As the *United Wire*, *Travelers* and *Safeco* courts carefully noted, these assessments do not create extra administrative burdens for the employer. Although employees might have

to pay slightly more, they would be purchasing protection they do not now enjoy. Secondly, most Americans who have health insurance receive it through their employer. In order for an employer to remain attractive to employees, she may be willing to pay the slightly higher costs of providing insurance.

In addition, the value to participants of an unsafe plan may not be much greater than the value of no plan at all. Participants in unsafe plans are probably unaware of the plan's financial status, and thus do not know that they should seek insurance coverage elsewhere. While this proposal might drive some plans from the market, all remaining plans would be guaranteed. Thus although some employees may no longer be able to obtain insurance from their employers, all who do, as well as everyone else who obtains insurance through other sources would at least be protected in the event of plan failure.

If enacted, the taxes and surcharges proposed here would almost certainly result in litigation. ERISA preemption analysis is complex, unclear, and in flux. Given the complexity and uncertainty of ERISA preemption analysis, states might be unwilling to explore the possibilities offered by the *Travelers*, *United Wire* and *Safeco* decisions. Furthermore, levying new taxes and surcharges has no political appeal. However, states have long been frustrated by the ability of self-funded plans to escape legitimate state regulation because of federal ERISA preemption. Framed by the rhetoric of federalism and the state's legitimate interest in providing its citizens with a competitive and safe health care market—a task Congress originally intended ERISA to accomplish—the specter of new taxes and surcharges is much less politically daunting. Indeed state judiciaries have long noted the “inconsistency [of enforcing ERISA preemption] with pious rhetoric emanating from Washington about returning government to the people at state and local levels.”<sup>170</sup>

Some states have already begun to indicate a willingness to examine the new possibilities offered by *Travelers* and *Safeco*. For example, the Wisconsin Office of the Insurance Commissioner recently urged the state legislature to reconsider funding mechanisms for HIRSP in light of these decisions: “[T]he Supreme Court and the Seventh Circuit Court of Appeals have signaled a new willingness to broaden state authority in this area. The lack of clarity should encourage you to thoroughly explore the possibilities now afforded the state to take advantage of this trend.”<sup>171</sup>

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170. *Commercial Life Ins. Co. v. Superior Court*, 764 P.2d 1059, 1069 (Cal. 1988) (Mosk, J., dissenting).

171. Testimony Relating to the Health Insurance Risk-Sharing Plan before the Senate Insurance Committee and Assembly Committee on Insurance, Securities, and Corporate Policy offered on behalf of Commissioner of Insurance Josephine W. Musser by Peter C. Farrow, Insurance Administrator (Oct. 19, 1995).

As the Office cautioned, “a direct assessment on self-funded health plans would be preempted and this preemption could not be avoided by simply removing any references to health plans from the language of the statute.”<sup>172</sup> Nevertheless, the Office advised the legislature that “the *Travelers* and *Safeco* decisions illustrate how states may indirectly affect health plans without fear of preemption.”<sup>173</sup>

Surcharges on hospital use and assessments on the sale of stop-loss insurance should survive ERISA’s preemption. They would also be equitable. A properly designed funding mechanism would protect self-insured plan participants without imposing external costs on Wisconsin taxpayers. It would do so by setting the contribution to the state insurance guaranty fund through hospital use surcharges and taxes on the sale of stop-loss insurance equal to the potential need of self-insured plan participants for protection. Thus, two unfair situations would be avoided: the failure of a self-insured plan would not suddenly burden plan participants with outstanding health care bills; and the protection of such plan participants generally would not be subsidized by taxpayers. Instead, through surcharges and assessments now allowed without triggering ERISA preemption, self-insured plans and their participants would fund their own protection.

#### V. CONCLUSION

Employees who receive health benefits through ERISA self-insured plans need protection when self-insured plans fail. Because of the breadth of ERISA preemption, states have been unable to assess ERISA self-insured plans for contribution to state insurance guaranty funds, and thus have been unable to include those employees in the protection of those funds. Further, attempts at federal reform to protect these employees have failed to garner support. However, under the recent *Travelers*, *United Wire*, and *Safeco* decisions, it may be possible for states to assess ERISA self-insured funds and their participants through a combination of hospital use surcharges and taxes on the sale of stop-loss insurance for contribution to state insurance guaranty funds. Contributions to the state insurance guaranty fund from self-insured plans and their participants would protect employees who receive health benefits through ERISA self-insured plans from plan failure. States should explore ways of drawing these contributions from hospital use surcharges and taxes on the sale of stop-loss insurance.

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172. *Id.*

173. *Id.*

