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Regulation of Employee Welfare Benefit Plans: The Scope of ERISA's Preemption and the State Power to Regulate Insurance

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REGULATION OF EMPLOYEE WELFARE BENEFIT PLANS: THE SCOPE OF ERISA'S PREEMPTION AND THE STATE POWER TO REGULATE INSURANCE

I. INTRODUCTION

In 1974 Congress enacted the Employee Retirement Income Security Act,[1] which was hailed as landmark social legislation in the area of pension and welfare plan reform.[2] It has been characterized as the "greatest development in the life of the American worker since social security."[3] ERISA was enacted to remedy many of the defects and problems associated with employee pension and welfare benefit plans. A primary objective was to strengthen the private employee benefit plan system to provide for the retirement and financial security of employees and their families and, no less importantly, to encourage the growth of this system. Many employees were losing anticipated pension and welfare benefits because of the lack of vesting provisions,[4] the financial instability of benefit plans, imprudent investment by plan trustees, theft of plan assets, and plan termination without adequate funds to cover accrued liabilities.[5]

ERISA is a lengthy and complex regulatory framework setting out

1. Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, § 1, 88 Stat. 829 (codified in scattered sections of titles 5, 16, 26, 29, 31, 42 U.S.C.) [hereinafter cited as ERISA]. ERISA was enacted pursuant to congressional power to regulate interstate commerce under the commerce clause, U.S. CONST. art. 1, § 8, cl. 3; 29 U.S.C. § 1001(a) (1976). In order to avoid confusion, section numbers used in the text will be those of ERISA rather than those of Title 29 U.S.C. Each section will be footnoted to 29 U.S.C. the first time it is mentioned herein.

2. 120 CONG. REC. 29933 (1974) (remarks of Senator Jacob J. Javits).

3. *Id.*

4. Vested interest is defined as: "A present right or title to a thing, which carries with it an existing right of alienation, even though the right to possession or enjoyment may be postponed to some uncertain time in the future." BLACK'S LAW DICTIONARY 1735 (4th ed. 1968). 29 U.S.C. § 1053 (1976) provides for minimum vesting standards. However, § 1051 provides that part 2 of ERISA (provisions relating to participation and vesting) shall not apply to employee welfare benefit plans. *See The Employee Retirement Income Security Act of 1974: Policies and Problems,* 26 SYRACUSE L. REV. 539 (1974) [hereinafter cited as *ERISA: Policies and Problems*], for a detailed explanation of ERISA's vesting provisions.

5. 29 U.S.C. § 1001 (1976). *See also* BUSINESS WEEK, Aug. 14, 1978, at 60 for a rough guide to the magnitude of unfunded pension fund obligations for 100 of the largest U.S. corporations. It is interesting to note the unfunded vested benefit obligations as a percent of net worth. For example, Lockheed's liability is 185% of its corporate net worth. Of the 100 corporations surveyed, total pension and retirement expenses for their most recent fiscal year equaled $11.8 billion. *Id.* at 64.

standards for welfare[6] and pension[7] plan reporting and disclosure,[8] fiduciary responsibility,[9] administration and enforcement.[10] Included within the Act are elaborate vesting,[11] funding,[12] and termination insurance[13] requirements which are applicable only to pension plans.

The term, employee benefit plan, as used in ERISA, is the generic term covering both pension and welfare plans. A welfare plan includes coverage for medical, hospitalization, and disability benefits. It can also include dental coverage and prepaid legal plans.[14] Although an ERISA objective is welfare plan regulation, pension plans are the main subject of congressional concern and are the focus of the statutory scheme.[15] ERISA does not provide for the substantive regulation of benefit requirements for welfare plans.[16] The result is a statutory vacuum for welfare plans. Some states have attempted to fill this vacuum by enacting legislation requiring that certain types of benefits be included in group health insurance[17] which is purchased by

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6. An example welfare benefit plan covered by ERISA is defined as:
[A]ny plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise, (A) medical, surgical, or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits. . . .
29 U.S.C. § 1002(1) (1976).

7. An employee pension plan within ERISA is defined as:
[A]ny plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program —
(A) provides retirement income to employees. . . .
29 U.S.C. § 1002(2) (1976).

8. 29 U.S.C. §§ 1021-1031 (1976).

9. *Id.* §§ 1101-1114.

10. *Id.* §§ 1131-1144.

11. *Id.* §§ 1051-1061.

12. *Id.* §§ 1081-1086.

13. *Id.* §§ 1301-1381.

14. *See generally* Comment, *The Effect of ERISA on Prepaid Legal Services,* 27 BAYLOR L. REV. 566 (1975).

15. 29 U.S.C. § 1001 (1976); *See also ERISA: Policies and Problems, supra* note 4, at 549.

16. There is little or no legislative history on the notable absence of such requirements. It could be implied that this area was to be left to the states to regulate. On the other hand, the detail that was written into section 514 of the Act, 29 U.S.C. § 1144 (1976), (the preemption provision), and the detailed exclusions from preemption, like the applicable criminal laws of a state, negate this argument. 29 U.S.C. § 1144(b)(4) (1976). No mention is made of exempting state laws that regulate substantive provisions of employee welfare benefit plans.

17. *See, e.g.,* N.H. REV. STAT. ANN. chs. 415:18-a, 419:5-a, 420:5-a (Supp. 1977) (requires that coverage for the treatment of mental illness be included in all group

employee welfare benefit plans, or by indirectly regulating welfare benefit plans.[18] Many states view this legislation as socially progressive because it is designed to provide increased benefits and protect against illusory benefits.[19] This policy, however, can produce the opposite of the expected result in some cases and is counter-productive to the goal of national uniformity sought by Congress.[20]

To eliminate conflict with state and local regulation, ERISA grants control to the federal government over the establishment, conduct, supervision, and regulation of employee benefit plans.[21] Congress considered the number of employees enrolled in employee benefit plans to be of such magnitude, and to so affect interstate commerce, that federal uniform control is necessary to assure minimum standards.[22] To assure federal control ERISA contains sweeping preemption language. Section 514(a) states that ERISA "shall supersede any and all state laws insofar as they . . . relate to any employee benefit plan."[23]

Notwithstanding its broad language, section 514 has spawned litigation over the extent to which ERISA preempts state law.[24] ERISA's scope of preemption is a question of great importance not only to state legislators and insurance regulators, but also to employers who maintain employee benefit plans. The states need to know the extent to which their insurance laws are preempted. Employers need to be aware of the state law with which they must comply in administering employee welfare benefit plans. The judiciary has been called on to

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health insurance policies); N.Y. INS. LAW § 162-a (McKinney 1966 & Supp. 1977-1978) (requires group health insurance to provide coverage for maternity care).

18. *See* notes 54-57 and accompanying text *infra.*

19. *See* Kline, *ERISA: Preemption & Prepaid,* 1 NEW DIRECTIONS IN LEGAL SERVICES 6 (1978); Brummond, *Federal Preemption of State Insurance Regulation Under ERISA,* 62 IOWA L. REV. 57 (1976).

20. *See* notes 21-22 and accompanying text *infra.*

21. National Bank of N. America v. International Bhd. of Electrical Workers, 400 N.Y.S.2d 482 (Sup. Ct. 1977).

22. 29 U.S.C. § 1001 (1976).

23. 29 U.S.C. § 1144(a) (1976) provides:

> Except as provided in subsection (b) of this section, the provisions of this subchapter and subchapter III of this chapter shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 1003(a) of this title and not exempt under section 1003(b) of this title. This section shall take effect on January 1, 1975.

24. *See, e.g.,* Wadsworth v. Whaland, 562 F.2d 70 (1st Cir. 1977), *cert. denied,* 98 S. Ct. 1630 (1978); Standard Oil Co. v. Agsalud, 442 F. Supp. 695 (N.D. Cal. 1977); Old Stone Bank v. Michaelson, 439 F. Supp. 252 (D.R.I. 1977); Wayne Chemical, Inc. v. Columbus Agency Serv. Corp., 426 F. Supp. 316 (N.D. Ind. 1977), *modified,* 567 F.2d 692 (7th Cir. 1977); Hewlett-Packard Co. v. Barnes, 425 F. Supp. 1294 (N.D. Cal. 1977), *aff'd,* 571 F.2d 502 (9th Cir. 1978).

arbitrate this conflict.[25] Much of the litigation concerning ERISA's preemptive scope has dealt with the states' power to mandate substantive benefits in welfare plans.[26]

This comment focuses on employee welfare benefit plans and examines the legislative history prior to enactment of ERISA as well as legislative material subsequent to enactment. To understand ERISA's preemptive scope and the effect which state laws mandating specific coverages have upon welfare benefit plans, an analysis of section 514 is necessary. An examination of the interpretation of section 514 by the courts illustrates its practical effect upon state laws mandating specific health coverage.

II. CONGRESSIONAL INTENT TO PREEMPT

ERISA specifically repealed the Welfare and Pension Plan Disclosure Act of 1958.[27] The Disclosure Act recognized and preserved state authority to prescribe regulations for the operation and administration of employee welfare and pension benefit plans.[28] It also provided for a reporting system which required plan administrators to file plan descriptions and annual reports with the Secretary of Labor. Reports were to be furnished upon request to plan participants. Nevertheless, this Act, characterized as a "glorified filing system,"[29] proved inadequate because it failed to provide the Secretary with enforcement powers.[30] Out of this shortcoming grew ERISA.

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25. Federal district courts have exclusive jurisdiction to hear actions brought under §§ 1001-1144 except when brought by a participant or beneficiary to recover benefits or to enforce or clarify rights under the plan. In this case state courts have concurrent jurisdiction. 29 U.S.C. § 1132 (1976).

26. *See, e.g.*, cases cited note 24 *supra*.

27. 29 U.S.C. §§ 301-309 (1970) (repealed by 29 U.S.C. § 1031(a) (1976)).

28. *Id.* § 309; *See* S. REP. NO. 1440, 85th Cong., 2d Sess. 1, *reprinted in* [1958] U.S. CODE CONG. & AD. NEWS 4137, 4137.

29. *ERISA: Policies and Problems, supra* note 4 (quoting *Administration Proposal to Amend the 1958 Welfare and Pension Plan Disclosure Act: Hearings on S. 1994 before the Subcommittee on Labor of the Senate Committee on Labor and Public Welfare,* 87th Cong., 1st Sess. 15 (1961); *see also* 120 CONG. REC. 20194 (1974)), *quoted at* 544.

30. *See ERISA: Policies and Problems, supra* note 4. Under the Disclosure Act it was anticipated that participants would police their own plans by obtaining plan descriptions and annual reports from the Secretary of Labor. However, this reliance on participant policing proved unworkable since the plans were often so complex that "an average plan participant, even where he has been furnished an explanation of his plan provisions, often [could] not comprehend them because of the technicalities and complexities of the language used." HOUSE COMMITTEE ON EDUCATION AND LABOR, EMPLOYEE BENEFIT SECURITY ACT OF 1973, H.R. REP. NO. 533, 93d Cong., 1st Sess. 8, *reprinted in* [1974] U.S. CODE CONG. & AD. NEWS 4639, 4646. ERISA contains a provision which requires plan descriptions to "be written in a manner calculated to be understood by the average plan particpant." 29 U.S.C. § 1022 (1976).

Through ERISA, Congress intended to establish a single, uniform regulatory scheme for employee benfit plans. ERISA's broad preemption has been described by one supporter as its crowning achievement, in that the sole power to control and regulate employee benefit plans was reserved to the federal government.[31] Legislative history reveals that Congress considered limited preemption, but rejected it in favor of a broader scope of preemption.[32] The original House version would have limited preemption to specific enumerated areas of federal regulation under ERISA such as reporting, disclosure, and fiduciary responsibility.[33] The original Senate version would have restricted preemption to the subject matters regulated by ERISA.[34] After careful consideration, a joint conference committee[35] rejected both the House and Senate versions and drafted the language which was ultimately enacted as section 514, the preemption section of ERISA.[36]

The rationale behind broad preemption was to eliminate the threat of inconsistent state and local regulation,[37] and to avoid "the possibility of endless litigation over . . . potentially conflicting State laws hastily contrived to deal with some particular aspect of private welfare or pension benefit plans."[38] As finally passed, ERISA preempted not just state laws relating to reporting, disclosure, and fiduciary responsibility, but superseded all state laws which in any way relate to employee benefit plans.[39] Congress made its intent clear.[40]

31. 120 CONG. REC. 29197 (1974) (remarks of Representative Dent, Chairman of the House Subcommittee on Labor, one of ERISA's sponsors and most ardent supporters).

32. *Id.*

33. H.R. 2, 93d Cong., 1st Sess., 120 CONG. REC. 4742 (1974) provides in pertinent part:

> It is hereby declared to be the express intent of Congress that . . . the provisions of Part 1 of this subtitle shall supersede any and all laws of the States and of political subdivisions thereof insofar as they may now or hereafter relate to the reporting and disclosure responsibilities, and fiduciary responsibilities, of persons acting on behalf of any employee benefit plan.

34. The Senate version, H.R. 2, 93d Cong., 1st Sess., 120 CONG. REC. 5002 (1974), provides in pertinent part:

> It is hereby declared to be the express intent of Congress that . . . the provisions of this Act or the Welfare and Pension Plans Disclosure Act shall supersede any and all laws of the States and of political subdivisions thereof insofar as they now or hereafter relate to the subject matters regulated by this Act or the Welfare and Pension Plan Disclosure Act.

35. H.R. REP. NO. 93-1280, 93d Cong., 2d Sess., *reprinted in* [1974] U.S. CODE CONG. & AD. NEWS 5038, 5038.

36. 29 U.S.C. § 1144 (1976).

37. 120 CONG. REC. 29933 (1974) (remarks of Senator Harrison Williams, Jr.). *See also* H.R. REP. NO. 93-1280, 93d Cong., 1st Sess., *reprinted in* [1974] U.S. CODE CONG. & AD. NEWS 5038, 5038. *See generally* Brummond, *supra* note 19.

38. 120 CONG. REC. 29942 (1974) (remarks of Senator Jacob J. Javits).

39. 29 U.S.C. § 1144(a) (1976).

40. A broad preemption provision eliminat[es] not only conflicting state laws

III. SECTION 514 OF ERISA—THE PREEMPTIVE LANGUAGE

An analysis of the interrelationship of the clauses within section 514 indicates a unified scheme for exclusive federal control over employee benefit plans. Section 514(a),[41] the relating clause, lays the foundation for the scope of preemption. Section 514(b)(2)(A),[42] the savings clause, and section 514(b)(2)(B),[43] the deemer clause, refine the scope of section 514(a).

A. *The Relating Clause*

Section 514(a) states in pertinent part that ERISA "shall supersede any and all State laws insofar as they . . . *relate* to any employee benefit plan."[44] This section defines the parameters of preemption so that any relation to an employee benefit plan by a state law, is prohibited. "Relate" is a broad and imprecise term and it will be left to the courts to define it. "Relate," however, is not equivalent to "regulate," which implies a narrower preemptive scope. A state law which mandates what benefits an employee will receive under a welfare plan is a law which "relates" to an employee benefit plan, whether or not it directly regulates the plan, and therefore would be preempted.

Additional support for a broad interpretation is found in section 514(c)(2). "The term 'State' includes a State, any political subdivision thereof, . . . which purports to regulate, *directly or indirectly*, the terms and conditions of employee benefit plans."[45] It is difficult to

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pursuing the same regulatory goals as the federal laws but also any state rule or action, however meritorious, that might in any way interfere with or make more burdensome the establishment or operation of employee benefit plans.

All measures at the state level that would regulate any aspect of a plan are invalidated by the broad sweep of the preemption, even if the aspect is not addressed by the federal law. They need not even be directed specifically to employee benefit plans but may only affect them as part of a more general class.

Pfennigstorf and Kimball, *Employee Legal Service Plans: Conflicts Between Federal and State Regulation*, 1976 AM. B.F. RES. J. 787, 831-32 (1976).

41. 29 U.S.C. § 1144(a) (1976); *see* note 23 *supra*.

42. 29 U.S.C. § 1144(b)(2)(A) (1976) provides in part: "[E]xcept as provided in subparagraph (B), nothing in this title shall be construed to exempt or relieve any person from any law of any State which regulates insurance, banking or securities."

43. 29 U.S.C. § 1144(b)(2)(B) (1976) provides:

Neither an employee benefit plan described in section 4(a) [29 U.S.C. § 1003(a)], which is not exempt under section 4(b) [29 U.S.C. § 1003(b)] (other than a plan established primarily for the purpose of providing death benefits), nor any trust established under such a plan, shall be deemed to be an insurance company or other insurer, bank, trust company, or investment company or to be engaged in the business of insurance or banking for purposes of any law of any State purporting to regulate insurance companies, insurance contracts, banks, trusts companies, or investment companies.

44. 29 U.S.C. § 1144(a) (1976) (emphasis added).

45. 29 U.S.C. § 1144(c)(2) (1976) (emphasis added).

determine why Congress sought to combat the problem of indirect state regulation in this subsection as opposed to in the relating clause. The legislative history is silent on this particular point. Regardless of where the prohibition against indirect state regulation appears, it nevertheless aids in defining the preemptive scope.

B. *The Savings Clause*

Congress clarified the extent of preemption by preserving state authority in those areas of traditional insurance regulation. Section 514(b)(2)(A), the savings clause, states in relevant part that ERISA "shall [not] be construed to exempt or relieve any person from any law of any state which regulates insurance."

This clause has been the source of much confusion. The savings clause reflects the policy of the McCarron-Ferguson Act,[46] which left the states the power to regulate the business of insurance.[47] That Act provides that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance."[48]

"The business of insurance"[49] was interpreted by the Supreme Court in *SEC v. National Securities, Inc.*[50] The Court stated that laws which focus on the relationship between the insurance company and the policy holder, such as the selling and advertising of policies and the licensing of companies and their agents were included within the concept of the business of insurance.[51] "[T]he type of policy which could be issued, its reliability, interpretation and enforcement—these [are] the core of the 'business of insurance'."[52]

State mandated benefit coverage for welfare benefit plans does affect the type of policy which can be issued by insurers to employee benefit plans. Thus, those state laws which fall within the purview of the business of insurance are not superseded by any federal act unless

46. 15 U.S.C. § 1011-1015 (1976). This legislation was enacted in response to United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533 (1944), which held that the business of insurance was interstate in nature and was thus subject to federal regulation.

47. 29 U.S.C. § 1144(d) (1976) also supports this proposition. Subsection (d) provides that "[n]othing in this subchapter shall be construed to alter, amend, modify, invalidate, impair, or supersede any law of the United States (except as provided in section 111 [29 U.S.C. § 1031] and 307(b) [29 U.S.C. § 1137(b)]) or any rule or regulation issued under any such law."

48. 15 U.S.C. § 1012 (1976).

49. *Id.*

50. 393 U.S. 453 (1969).

51. *Id.* at 460.

52. *Id.*

the act specifically relates to the business of insurance. ERISA does not purport to extend its regulations to the insurance industry as a whole, nor was it intended to reach so far.[53] It does, however, relate to the business of insurance insofar as it regulates employee benefit plans. Reading the savings clause and the relating clause together, and noting the preemption under the McCarron-Ferguson Act if a federal act relates to the business of insurance, leads to the conclusion that state laws which regulate the business of insurance and also relate to an employee benefit plan are preempted.

C. *The Deemer Clause*

Section 514(b)(2)(B), the deemer clause, states in pertinent part that "an employee benefit plan . . . shall [not] be deemed to be an insurance company or . . . engaged in the business of insurance . . . for purposes of any law of any State purporting to regulate insurance companies."[54] The deemer clause was enacted to further clarify the field which Congress intended ERISA to preempt. This clause represents a congressional attempt to prevent a state from regulating an employee benefit plan through circumvention of the relating clause by claiming the power to regulate a plan under the savings clause. Consequently, a state may not label any ERISA plan as being in the business of insurance in order to subject it to state insurance law.[55] Such state action would defeat a primary goal of ERISA "to reserve to federal authority the sole power to regulate the field of covered employee benefit plans."[56]

When both sections (a) and (b) of section 514 are examined together, it becomes clear that Congress intended total federal control over employee benefit plans. The relating clause indicates the area of state law to be preempted while the savings clause preserves state primacy in the relationship between the insurer and the insured and indicates the laws Congress did not intend to preempt. Relation to an employee benefit plan is the mechanism which triggers preemption. The savings clause would preserve a state law that regulated the licensing of insurance agents, regardless of whether the agent sold insurance to an employee welfare benefit plan.[57] Congress did not intend such a

53. 29 U.S.C. § 1002 (1976).

54. 29 U.S.C. § 1144(b)(2)(B) (1976).

55. *See* Brummond, *supra* note 19, at 98-99, which suggests that self-insured plans satisfy the accepted elements of an insurance arrangement, and that the presumption in section 514(b)(2)(B) that these plans are not insurance is somewhat surprising. The author also suggests that it may be possible for the Burger Court to strike down the deemer clause if it finds no rational basis to support the presumption.

56. Guthrie v. Dow Chemical Co., 445 F. Supp. 311, 314 (S.D. Tex. 1978).

57. *See* note 51 and accompanying text *supra.*

law to be preempted. When the state law mandates what type of insurance a welfare benefit plan must purchase, however, it is directly regulating employee benefit plans and should therefore be preempted.

IV. CONFLICTING INTERPRETATIONS—A CASE LAW OVERVIEW

The courts which have had occasion to interpret section 514 are divided on the question of the scope of preemption. Several courts desiring to uphold state law have ascribed a limited scope of preemption to ERISA by relying on the savings clause.[58] Others have held that any control over employee welfare benefit plans triggers preemption.[59]

A. *Narrow Reading of Preemption*

The leading case adopting a narrow view of preemption is *Wadsworth v. Whaland,*[60] which involved a New Hampshire law that required all insurers issuing group health insurance policies in the state to include coverage for mental illness.[61] Several welfare benefit plan administrators sought an injunction against enforcement claiming the law was preempted by ERISA.[62] The adminstrators argued that by imposing mandatory mental illness coverage on group health insurance policies the state law indirectly imposed control on the benefits an employee would receive under an employee welfare benefit plan. Thus they claimed that the law related to plans covered by ERISA and was preempted.[63] However, the court was not persuaded by this reasoning.[64]

The *Wadsworth* court interpreted ERISA as mandating broad preemption. Although New Hampshire's law indirectly related to employee welfare benefit plans and would appear to be subject to preemption, the court concluded preemption was not automatic because of the application of the savings clause. Despite the broad

58. *See, e.g.,* Wadsworth v. Whaland, 562 F.2d 70 (1st Cir. 1977), *cert. denied* 98 S. Ct. 1630 (1978); Old Stone Bank v. Michaelson, 439 F. Supp. 252 (D.R.I. 1977).

59. *See* Hewlett-Packard v. Barnes, 425 F. Supp. 1294 (N.D. Cal. 1977), *aff'd,* 571 F.2d 502 (9th Cir. 1978); Wayne Chemical, Inc. v. Columbus Agency Serv. Corp., 426 F. Supp. 316 (N.D. Ind.), *modified,* 567 F.2d 692 (7th Cir. 1977); *see generally* Okin, *Preemption of State Insurance Regulation by ERISA,* 13 FORUM 652 (1978).

60. 562 F.2d 70 (1st Cir. 1977), *cert. denied,* 98 S. Ct. 1630 (1978).

61. N.H. REV. STAT. ANN. chs. 415:18-a, 419:5-a, 420:5-a.

62. 562 F.2d at 72-73.

63. *Id.* at 76.

64. The court stated: "[w]e agree with plaintiffs that Chapter 57 is a law which indirectly relates to employee benefit plans and is subject to preemption. However, we cannot agree that preemption necessarily follows. Chapter 57 is also a state law regulating insurance and is expressly exempted from preemption by section 514(b)(2)(A) [the savings clause]." *Id.* at 77.

scope of preemption ascribed to ERISA, the net effect of the decision is a considerable narrowing of the preemptive scope.

The *Wadsworth* court, in effect, applied the clauses within section 514 in an order reverse from that in which they are written. Implied in the court's reasoning is that the initial inquiry should be whether the contested state law is a law that regulates the business of insurance, falling within the savings clause, section 514(b)(2)(A). If the answer is affirmative, the court should hold that preemption does not occur. If the answer is negative, then the court should determine whether the law relates to the employee benefit plan, falling within the relating clause, section 514(a). If so, then preemption occurs. The court's reasoning emphasizes a clause representing a "distinctly subordinate policy within the section"[65] when it considers that the savings clause rather than the relating clause controls the scope of preemption.[66]

This decision has been followed by courts that are desirous of upholding state law and need a basis to find narrow preemption because the legislative history and the words of section 514 do not support such a finding.[67]

In *Insurers' Action Council, Inc. v. Heaton*[68] the court faced a situation almost identical to that in *Wadsworth*. The Minnesota Comprehensive Health Insurance Act[69] required all insurers that issue health insurance policies to provide a minimum level of benefits. It also required employers who offer health care plans to their employees to provide a particular type of health plan. Plaintiff insurance companies brought suit to enjoin enforcement of the Minnesota law claiming ERISA preempted the area. The court held the statute was not preempted because it was also a law that regulated the business of insurance.[70] The court acknowledged its narrow reading of section 514. It reasoned that the conflict between ERISA and state law must be

65. HOUSE COMM. ON EDUCATION AND LABOR, 94TH CONG., 2D SESS., ERISA OVERSIGHT REPORT OF THE PENSION TASK FORCE 9 (Comm. Print 1977).

> With respect to regulation of the activities of certain employee benefit plans . . . , federal authority has been expressly extended to occupy the field to the exclusion of state authority subject to certain exceptions. These exceptions are designed to delineate affirmatively the limits of the "field" preempted by section 514(a), and articulate a second, but distinctly subordinate policy within the section of preserving state authority insofar as it does not relate to any plan.

Id.

66. *See* Brummond, *supra* note 19, at 66-67, which also puts forth this order of inquiry in determining whether a state insurance law is preempted by ERISA.

67. *See* Hamberlin v. VIP Insurance Trust, 434 F. Supp. 1196 (D. Ariz. 1977); Old Stone Bank v. Michaelson, 439 F. Supp. 252 (D.R.I. 1977).

68. 423 F. Supp. 921 (D. Minn. 1976).

69. MINN. STAT. ANN. § 62E.01 (West Supp. 1976).

70. 423 F. Supp. at 926.

very clear in order to trigger preemption;[71] in effect the court adopted the original Senate version of limited preemption.[72]

The pivotal point in these cases is that the challenged state laws were not intended to control or regulate employee benefit plans.[73] The state laws were directed at regulating an area within the state's power to regulate—the business of insurance.[74] Therefore, the fact that the law as enforced relates to employee benefit plans is incidental.

Under the reasoning of the *Wadsworth* decision and cases following its reasoning,[75] state laws regulating the benefits an employee receives under a group insurance plan will be upheld even though the result infringes on employee welfare benefit plans. Under the narrow view this will be tolerated even though it contravenes the expressed intent of Congress to completely occupy the field of employee benefit plans.[76]

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71. *Id.*

72. *See* note 34 and accompanying text *supra.*

73. Section 514 makes no mention of a state law's intent in defining the scope of preemption. *See also* Wadsworth v. Whaland, 562 F.2d 70 (1st Cir. 1977), *cert. denied,* 98 S. Ct. 1630 (1978).

74. New York is an example of another state which imposes control over the content of health insurance policies. In Health Ins. Ass'n of America v. Harnett, 89 Misc. 2d 795, 395 N.Y.S.2d 372 (1977), the plaintiffs sought a declaration of unconstitutionality of a New York law that requires every health insurance policy issued in the state to include coverage for maternity care. The court upheld the law; however, it was not challenged on grounds of preemption by ERISA. *See also* 30 N.Y.U. CONF. LAB. 257 (1976).

75. In Hamberlin v. VIP Insurance Trust, 434 F. Supp. 1196 (D. Ariz. 1977), the court quoted extensively from *Insurer's Action Council.* The court concluded that ERISA's preemptive scope was narrow. *See also* Old Stone Bank v. Michealson, 439 F. Supp. 252 (D.R.I. 1977). Here the court was confronted with a situation similar to that in *Wadsworth.* The bank adopted an ERISA pension plan which included four investment options. Rhode Island law, R.I. GEN. LAWS § 19-5-17 (1968), required the State Board of Bank Incorporation's approval of the investment options before they could be implemented. The Board denied approval. The bank sought an injunction, claiming the law was preempted by ERISA. The court relied on *Wadsworth* to hold that the Rhode Island law was not preempted. The court stated that the law was designed to regulate banking activities and not employee benefit plans, and therefore came within the scope of the savings clause. The court went on to hold that merely because the banking activities are prompted by a plan regulated by ERISA, the Board is not deprived of its jurisdiction. As in *Wadsworth,* the *Old Stone Bank* court chose the policy of state regulation over federal control of ERISA plans.

76. A tangentially related preemption question arising under the savings clause concerns securities law. The savings clause also exempts from preemption state securities laws. This area is being pulled into the arena of controversy through Daniel v. Int'l Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977), *cert. granted,* 98 S. Ct. 1232 (1978). The defendants argued against a claim that a participant's interest in a pension plan is a security, that ERISA repealed the anti-fraud provisions of the 1933 and 1934 Securities Acts insofar as they apply to union pension funds. The court partially rejected this argument finding it "unwarranted to impute an intent on the part of Congress for ERISA to override the federal or state securities laws." *Id.* at 1249.

B. *Broad Reading of Preemption*

The broad view of preemption "that Congress intended absolute preemption of the field of employee benefit plans"[77] is best demonstrated by the decision in *Hewlett-Packard Co. v. Barnes*.[78] The California Knox-Keene Health Care Service Plan Act[79] regulated the delivery of health care services to residents who participate in health care plans. The Act also sought to regulate self-funded plans. California considered these plans to be a unique form of insurance arrangement and thus subject to state law because of its power to regulate the business of insurance.[80] The plaintiffs were administrators of plans covered by ERISA as well as by the Knox-Keene Act. The plan administrators challenged the Act on the grounds that it was preempted by ERISA.[81] The court agreed and held that the Act was preempted to the extent that it applied to employee welfare benefit plans.

The state argued that because the Knox-Keene Act regulated the business of insurance it was saved from preemption by the savings clause. In essence the state was deeming self-funded plans to be in the business of insurance and thereby claiming the power to regulate them in direct contravention of the prohibition in the deemer clause. The court stated:

> In seeking to regulate plaintiffs' plans pursuant to Knox-Keene under the theory that the statute applies to and that such plans constitute "insurance," defendant contravenes the clear intent of Section 514(a) and (b) of ERISA that employee benefit plans, so dubbed or under any other name, be free of state regulation.[82]

In response to the *Daniel* decision, Senators Williams and Javits have introduced S. 3017, 95th Cong., 2d Sess. § 274 (1978), to clarify the applicability of federal and state securities laws to plans subject to ERISA. Section 274 provides that ERISA supersedes federal and state securities laws to the extent that such laws may be applied to the interest of an employee in an employee benefit plan.

Another case considering the extent of ERISA's preemptive scope is now pending before the United States District Court for Connecticut. Nat'l Carriers' Conference Comm. v. Heffernan, 440 F. Supp. 128 (D. Conn. 1977). The issue is whether a state may tax benefits paid by an employee welfare benefit plan to participants and beneficiaries. The savings clause exempts from preemption state insurance, banking and securities laws but not state tax laws.

See also Air Line Pilots Ass'n. Int'l v. Northwest Airlines, Inc., 444 F. Supp. 1138 (D.D.C. 1978) (where ERISA was found not to have preempted the Railway Labor Act); Malone v. White Motor Corp., 435 U.S. 497 (1978); 7 N.C. CENT. L.J. 358 (1976).

77. Azzaro v. Harnett, 414 F. Supp. 473, 474 (S.D.N.Y. 1976).
78. 425 F. Supp. 1294 (N.D. Cal. 1977), *aff'd*, 571 F.2d 502 (9th Cir. 1978).
79. CAL. HEALTH & SAFETY CODE §§ 1340-1399.64 (West Supp. 1971-1977).
80. 425 F. Supp. at 1300.
81. *Id.* at 1296.
82. *Id.* at 1300.

In contrast, the *Wadsworth* court construed the deemer clause as supporting state supremacy in the regulation of insurance.[83] The court stated that "on its face the deemer provision does not prohibit a state from indirectly affecting plans by regulating the contents of group insurance policies purchased by the plans."[84] The *Wadsworth* court, however, failed in its reading to incorporate the prohibition against indirect state regulation found in section 514(c)(2).[85]

The *Hewlett-Packard* decision has been followed in several other cases.[86] Hawaii's Prepaid Health Care Act,[87] which required all workers to be covered by a comprehensive prepaid health care plan with minimum benefit levels,[88] was held preempted by ERISA in *Standard Oil Co. of California v. Agsalud.*[89] The court noted the absence of ERISA provisions dealing with substantive benefits and the absence of legislative history on this particular point, but nevertheless concluded it could not contravene the plain meaning of the statute.[90] The state argued that ERISA and the Act should be allowed to coexist since they regulated different spheres of employee welfare benefit plans and that, in any event, Hawaii's Act did not relate to those aspects of employee welfare benefit plans covered by ERISA. The court replied that '[t]here is simply no basis in the language of [section] 514(a) for distinguishing between types of state laws all of which 'relate to' employee benefit plans. When Congress says 'any and all State laws' courts cannot conclude that Congress really meant to say 'some but not all State laws.' "[92]

C. *Collateral Effects of the Broad Reading of Preemption*

Although broad preemption should prevent litigation over the preemption question because preemption would be automatic, it does have the adverse effect of creating certain vacuums in the regulation of

83. 562 F.2d at 78.
84. *Id.*
85. *See* note 45 and accompanying text *supra.*
86. *See, e.g.,* Wayne Chem., Inc. v. Columbus Agency Serv. Corp., 426 F. Supp. 316 (N.D. Ind.), *modified,* 567 F.2d 692 (7th Cir. 1977); Bell v. Employee Sec. Benefit Ass'n, 437 F. Supp. 382 (D. Kan. 1977).
87. HAW. REV. STAT. §§ 393-1 to 393-51 (1976).
88. *Id.* at § 393-11.
89. 442 F. Supp. 695 (N.D. Cal. 1977). In response to this decision, Representatives Heftel and Akaka have introduced H.R. 6944, 95th Cong., 1st Sess. (1977), which would amend ERISA to clarify the status of Hawaii's Prepaid Health Care Law as not preempted by ERISA.
90. *Id.* at 706-07.
91. *Id.* at 706.
92. *Id.* at 707.

the substantive content of employee welfare benefit plans.[93] The courts that have been faced with such a situation have begun to fashion a federal common law.

In *Wayne Chemical, Inc. v. Columbus Agency Service Corp.*[94] the district court recognized ERISA's broad preemptive scope and found state law inoperative. As a result, the court found it necessary to fashion a federal rule of decision.[95] The court ordered the defendant insurer to issue a conversion policy for a plan participant although the insurer claimed that coverage had been transferred to another insurer. The court used state law on this point as a guide in fashioning its order. In *Riley v. MEBA Pension Trust*[96] the court stated that implicit in section 514(a) was the development of a federal common law with respect to employee benefit plans.[97]

A few resourceful entrepreneurs have attempted to take advantage of ERISA's broad preemption of state law. The scheme is to set up a group insurance plan and characterize it as a "welfare benefit plan" in an effort to avoid state law which regulates insurance companies. These ventures are known as multiple employer trusts, commonly called "METS."

In *Bell v. Employee Security Benefit Association*[98] the court blocked this tactic, stating that "just as a state cannot regulate an employee benefit plan by calling it 'insurance,' neither can defendants . . . be free of state regulation by terming [their plan] an employee benefit plan."[99] The Seventh Circuit Court of Appeals, in *Wayne Chemical, Inc. v. Columbus Agency Service Corp.*,[100] used this rationale to sidestep the preemption issue, and found that the plan in question was not an ERISA plan and thus was subject to state law. Finding these commercial insurance plans outside the scope of ERISA comports with the legislative history. "Where a 'plan' is, in effect, an entrepreneurial venture, it is outside the policy of section 514."[101]

The dichotomy between the narrow and broad readings of preemption can best be understood in the context of intent versus effect. The

93. *See* notes 16-17 and accompanying text *supra; see also* Ellis v. Lionikis, 152 N.J. Super. 321, 377 A.2d 1208 (1977).

94. 426 F. Supp. 316 (N.D. Ind.), *modified,* 567 F.2d 692 (7th Cir. 1977).

95. *Id.* at 321.

96. 570 F.2d 406 (2d Cir. 1977).

97. *Id.* at 413.

98. 437 F. Supp. 382 (D. Kan. 1977).

99. *Id.* at 390.

100. 567 F.2d 692 (7th Cir. 1977). The court of appeals modified the district court's finding of broad preemption.

101. ACTIVITY REPORT OF THE COMMITTEE ON EDUCATION AND LABOR, H.R. REP. NO. 94-1785, 94th Cong., 2d Sess. 48 (1977).

Hewlett-Packard standard of analysis focuses on the effect that state law has on employee welfare benefit plans. The *Wadsworth* standard of analysis focuses on the intent of the state regulation which relates to employee welfare benefit plans.[102] Thus, under the *Wadsworth* rationale, indirect regulation of employee welfare benefit plans will be tolerated if the state's intent is to regulate the business of insurance.

Regulating the content of group health insurance policies is clearly within the purview of the McCarron-Ferguson Act. It is the regulation of the business of insurace which at the same time relates to employee benefit plans. Clearly, both congressional policies of reserving to the states the regulation of the business of insurance and of total federal control over employee benefit plans cannot be fully implemented. A balanced compromise can be struck by preempting state law only insofar as it applies to employee benefit plans. This reconciliation leaves to the states the power to regulate the business of insurance outside the field of employee benefit plans while assuring the federal government control over employee welfare benefit plans.

Should Congress decide to amend section 514 to further clarify the preemptive scope, it should consider the effect analysis of state law. Regardless of a state's intent in enacting a law which relates to employee welfare benefit plans, the net result is infringement in an area reserved to federal control.

In the four years since ERISA's enactment the effects of judicial interpretations have begun to make themselves felt. The Pension Task Force[103] recognized this problem and attempted to point out the breadth of section 514, stating that "with respect to regulation of the activities of certain employee benefit plans (those subject to ERISA jurisdiction), federal authority has been expressly extended to occupy the field to the exclusion of state authority . . . leav[ing] no room for effective state regulation."[104] The Task Force went on to reiterate the purpose behind ERISA's broad preemption by concluding that "the

102. The *Wadsworth* court noted that there was no intent on the part of New Hampshire to directly regulate plaintiffs' plans. Section 514, however, makes no mention of a state law's intent when defining what laws are preempted.

103. 29 U.S.C.A. §§ 1221-1222 (Supp. 1978) provides for the formation of a Joint Pension Task Force which is to report to Congress on the implementation of ERISA. One of the matters to be studied by the Task Force and reported on to Congress was the effect of federal preemption of state law.

104. HOUSE COMM. ON EDUCATION AND LABOR, 94TH CONG., 2D SESS., OVERSIGHT REPORT OF THE PENSION TASK FORCE 9 (Comm. Print 1977), [hereinafter cited as OVERSIGHT REPORT]. The Task Force recently held hearings on the preemption issue and the ERISA Industry Committee and The American Council of Life Insurance and The Health Insurance Association of America indicated strong support for ERISA's preemption of state laws that regulate employee benefit plans. *See This Week in Congress,* June 2, 1978.

Federal interest and the need for national uniformity are so great that enforcement of state regulation should be precluded."[105]

If ERISA is not amended to include a firmer congressional directive, states will continue to mandate certain coverage requirements. The states believe they can increase employee benefits under welfare benefit plans and further protect their residents. Substantive benefit requirements by states are seen as desirable in that they prevent an employer with substantial bargaining power from creating a plan with minimal coverage. State substantive regulation may also permit states to experiment with various types of benefit plans and to adapt them to peculiar local conditions in each state.[106]

Conversely, there are practical considerations which militate against continued state regulation. The cost of compliance with state laws that require specific coverages is pushing some plans close to bankruptcy.[107] Plan administrators may be forced to drop other desired benefits[108] in order to supply state mandated benefits and still keep the costs reasonable and affordable.[109] For benefit plans covering workers in more than one state, the administration expense necessary to comply with numerous state requirements is an obvious burden. An additional impact of state regulation is to deny plan participants the right to choose the coverage package they desire.[110]

ERISA was enacted to assure that the working populace would

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105. OVERSIGHT REPORT, *supra* note 104, at 9. *See also* 29 U.S.C. § 1001 (1976). *But cf.* SENATE COMM. ON HUMAN RESOURCES, 95TH CONG., 1ST SESS., OVERSIGHT OF ERISA (1977) (Senator Javits expressed concern that section 514 may have gone further than desired. It should be noted that this was not a report by the Pension Task Force). *Id.* at 61.

106. *See* Brummond, *supra* note 19, at 117.

107. *See* Wadsworth v. Whaland, 562 F.2d 70 (1st Cir. 1977), *cert. denied*, 98 S. Ct. 1630 (1978) (plaintiff administrators argued that bankruptcy was a possible result of compliance with state law which required certain benefits).

108. "In one case, a union welfare plan in New Hampshire was forced to discontinue vision and dental coverage for participants to pay for the cost of adding state-mandated mental health care coverage to the plan." BUSINESS INSURANCE, June 12, 1978, at 6, col. 4.

109. This cost is forcing some employers to become uninsured or self-insured. *See* Brummond, *supra* note 19; *see also* Statement by William Gibb before the Senate Human Resources Subcommittee on Labor and the Senate Finance Subcommittee on Private Pension Plans and Employee Fringe Benefits, (August 17, 1978), at 31.

110. BUSINESS INSURANCE, June 12, 1978, at 6, col. 1. (remarks of Representative Erlinborn).

The plans are established and the level of contributions are stipulated by collective bargaining agreements. However, the benefits to be received under the welfare plans are not stipulated, they are determined by the plan administrators with the aid of insurance consultants. Wadsworth v. Whaland, 562 F.2d 70 (1st Cir. 1977), *cert. denied*, 98 S. Ct. 1630 (1978).

receive pension benefits upon retirement and welfare plan benefits.[111] Should some plans be forced to discontinue some needed benefits because of state requirements, the purpose of ERISA to secure employee benefits under these plans and national uniformity would be partially defeated.[112] Although ERISA protects the quantifiable aspects of welfare benefits plans, it does not cover the qualitative aspects. State mandated benefits may fail to meet the needs of employees and their families and thus threaten their financial security, which is a primary goal of ERISA, by forcing employees to pay extra for the benefits they prefer to those required by state law.[113] This should be an area of primary concern for the Pension Task Force.

D. *Concern for Federalism*

A key consideration in the ultimate success of either the broad or narrow readings of section 514's preemption of employee welfare plans may well be the Burger Court's concern for federalism. In recent years there has been an effort by the Burger Court to favor the state when there is a preemption question.[114]

Recent decisions of the Supreme Court concerning the preemption doctrine reveal an inclination to uphold state regulation when challenged on preemption grounds.[115] The Supreme Court stated in *Jones v. Rath Packing Co.*[116] that when "the field which Congress is said to have preempted has been traditionally occupied by the States . . . 'we start with the assumption that the historic police powers of the states were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.'"[117] The states' power to regulate the business of insurance would be given great weight as an area traditionally occupied by the states. An argument can be made, however,

111. S. REP. NO. 383, 93d Cong., 2d Sess. 3, *reprinted in* [1974] U.S. CODE CONG. & AD. NEWS 4890.

112. As for pension plans, "more terminations have occurred in the nearly four years since ERISA's enactment than in the previous four decades." Mulock, *The Positive Side of ERISA: Quadrupled Contributions and Insurance in Certain Defined Benefit Plans for Closely Held Corporations,* CERTIFIED LIFE UNDERWRITER J. July, 1978, at 29. *See also* note 5 *supra.*

113. *See* note 2-5 and accompanying text *supra.*

114. *See* 3 U. DAY. L. REV. 237 (1978). It is beyond the scope of this comment to adequately discuss the preemption doctrine. *See generally* 75 COLUM. L. REV. 623 (1975) for an excellent treatment of the subject. Hirsch, *Toward A New View of Federal Preemption,* 1972 U. ILL. L.F. 515 (1972).

115. *See, e.g.,* Goldstein v. California, 412 U.S. 546 (1973); Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470 (1974). *See also* Engdahl, *Preemptive Capability of Federal Power,* 45 U. COLO. L. REV. 51 (1973).

116. 430 U.S. 519, *rehearing denied,* 431 U.S. 925 (1977).

117. *Id.* at 525 (quoting Rice v. Santa Fe Elevator Corp., 381 U.S. 218, 230 (1967)).

that a literal reading of section 514 and its legislative history reveal a "clear and manifest purpose of Congress"[118] to entirely control the field of employee benefit plans. Nonetheless, given the current posture of the Supreme Court,[119] the presumption in favor of state laws that mandate certain coverages be provided by employee benefits plans is one that may prove difficult to overcome.

V. CONCLUSION

It is evident that Congress intended, through the enactment of section 514, to regulate the entire field of employee benefit plans.[120] Although pension plan security is the major objective of ERISA, welfare benefit plans are nevertheless included within ERISA's regulatory scheme.

Congress intended only to preempt state law insofar as it relates to employee benefit plans. ERISA is not an attempt to completely deprive the states of their power to regulate insurance. The states' power to regulate the business of insurance is reaffirmed by the savings clause. Congress saw the need for national uniformity and control and sought to remove only the field of employee benefit plans from state control.

Section 514 specifically preempts state laws which mandate certain substantive coverage in employee benefit plans. If Congress desires to exercise total control over employee benefit plans and regain what has been lost through the states' regulation of the content of welfare benefit plans, then new legislation is needed—possibly in the form of an amendment to section 514. Further study is needed to decide among at least three alternatives: (1) regulating the content of welfare plans on a national scale so that ERISA would not only protect whatever benefits are already provided by a welfare plan but would also regulate the quality of benefits it provides; (2) regulating the content by the states because of the need to adapt to local exigencies; or (3) allowing the content of welfare plans to be determined by the free play of the market if bargainers are in fairly equal positions.

As the two views of ERISA's preemptive scope take shape, their implication should be carefully considered. Some state laws mandating substantive benefits are allowed to stand and regulate employee welfare benefit plans. Other state regulations are preempted and overturned. Substantive benefit provisions of welfare plans should have received more attention at the time of ERISA's enactment. Investiga-

118. *Id.*
119. *See* 75 COLUM. L. REV. 623 (1975).
120. *See* notes 27-40 and accompanying text *supra.*

tion of the current operation of employee welfare benefit plans and the need for regulation of substantive benefits should be a major concern of the Pension Task Force.

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