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California

Ninth Circuit Upholds San Francisco Health Care Security Ordinance Against Preemption Challenge

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By:
Nancy L. Ober

A three-judge panel of the United States Court of Appeals for the Ninth Circuit has upheld San Francisco's employer health care spending mandate, reversing a district court judgment holding that the ordinance is preempted by ERISA. The court's decision means that the employer spending component of the Health Care Security Ordinance will likely continue in effect barring Supreme Court intervention.

Background

The San Francisco Health Care Security Ordinance (HCSO) is described at length in a previous ASAP, "*Another New Headache for Employers: San Francisco's Health Care Security Ordinance*," December 2007. In brief, the ordinance has two components, a City-sponsored Health Access Program (HAP) and an employer spending requirement.

Under the spending requirement, covered employers must spend a minimum amount on health care for each hour worked by their covered employees. An employer whose health care expenditures do not meet the ordinance minimum may satisfy its spending requirement in a number of ways, including by providing its own health insurance plan or by making payments on behalf of its employees into the HAP, entitling them to membership in a health care network at discounted fees or to a medical expense reimbursement account.

Upon passage of the ordinance, the Golden Gate Restaurant Association filed suit to block the employer spending requirement on ERISA preemption grounds. In December 2007, shortly before the January 1, 2008, effective date, the district court issued its ruling holding the spending requirement preempted. The City of San Francisco appealed, and the Ninth Circuit granted a stay of the district court judgment, allowing the HCSO to go into effect on January 9, 2008 pending the decision on appeal.

The Ninth Circuit Decision

In considering the City's appeal, the Ninth Circuit started from the premise that the HCSO enjoys a presumption against preemption because it operates in a field traditionally occupied by state and local government - the provision of health care to the indigent. The court then addressed and rejected the arguments for ERISA preemption advanced by the restaurant association, which was joined by the U.S. Department of Labor as an amicus on appeal.

The court first considered whether the ordinance provision for payments into the HAP (the "City payment option") creates an ERISA plan, either because it imposes administrative burdens on employers, or because the HAP itself is an ERISA plan. Agreeing with the district court, the Ninth Circuit concluded that the administrative requirements on employers - the obligation to track hours worked by employees in San Francisco and to calculate and make payments to the City - do not meet the criteria for an ERISA plan. Employers' obligations end when they make the required payment to the City, and do not involve the potential for mismanagement of funds or other abuses which ERISA was intended to prevent. Nor is the HAP itself an ERISA plan. The HAP is a "government entitlement program" primarily funded by taxpayers, not a plan established or maintained by an employer, as ERISA requires. Employers have no control over the operation of the HAP. The City controls eligibility and benefits, and can terminate or modify the HAP at any time.

Next, the Ninth Circuit rejected the argument that the ordinance has an impermissible "connection with" or "reference to" employers' ERISA plans. It concluded that there is no impermissible connection because the ordinance does not regulate benefits or charges for benefits under ERISA plans. The obligations on employers apply whether or not the employer has an ERISA plan. The ordinance may influence some employers to make their required health care expenditures through an ERISA plan rather than the City payment option, but such "indirect economic influence" is "entirely permissible" according to the court. Nor does the ordinance make forbidden "reference to" ERISA plans. Employer obligations are not measured by the level of benefits provided by an ERISA plan, but by the amount of employer payments to any of the options under the ordinance, including the City option.

Finally, the court disagreed with the argument that the ordinance is preempted under a Fourth Circuit decision, *Retail Industry Leaders Association v. Fielder*, 475 F.3d 180 (4th Cir. 2007), which struck down a Maryland statute requiring employers with 10,000 or more Maryland employees (a category which included only Wal-Mart) to spend 8% of their total payrolls on employees' health insurance benefits or pay the shortfall in spending to the state. The court distinguished *Fielder* on the ground that the Maryland statute effectively forced contributions to an ERISA plan, because no "reasonable employer" would pay the state when it could contribute to its own ERISA plan for employees. In contrast, the Ninth Circuit panel stated that the City payment option under the HCSO offers employers "a realistic alternative" to creating or modifying an ERISA plan.

What's Next?

It is probable that the Golden Gate Restaurant will ask the Ninth Circuit to grant a discretionary *en banc* (11 judge) review of the 3-judge panel decision. Failing such relief, eventual Supreme Court review seems likely, given the high level of public interest in health care, and at least the appearance of a split in the circuits. In the meantime, the employer spending requirement continues in effect, with increases in the spending requirement and a reduction in the minimum hours per week covered employees must work in San Francisco (from 10 to 8) effective January 1, 2009.

Nancy L. Ober is a shareholder in Littler Mendelson's San Francisco office. If you would like further information, please contact your Littler attorney at 1.888.Littler, info@littler.com, or Ms. Ober at nlober@littler.com.



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