San Francisco Health Care Law Survives ERISA Preemption
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The federal benefits law does not preempt a San Francisco ordinance establishing minimum health care spending requirements for employers with regard to certain employees working in the city and county, the Ninth Circuit Court of Appeals has ruled. In a case that attracted great attention from employer, labor and health care advocacy groups, the court upheld the validity of San Francisco’s Health Care Security Ordinance. The court’s September 30 Golden Gate Restaurant Ass’n v. City and County of San Francisco decision allows the San Francisco Ordinance requiring certain employers to spend a specified minimum amount toward certain health care expenses for employees working within the City and County of San Francisco to remain effective, despite the federal Employee Retirement Income Security Act (ERISA). Accordingly, employers with employees working in San Francisco need to ensure compliance with the Ordinance, which became effective on January 1, 2008. The Ninth Circuit covers the federal courts in California, Oregon, Washington, Idaho, Alaska, Hawaii and Arizona, and this decision is binding in those federal courts.

Summary of Decision
Two key observations support, in large part, the court’s lengthy decision. First, the Ninth Circuit found the Ordinance does not require employers either to establish an ERISA plan or modify an existing ERISA plan in order to comply with its provisions. The court noted all employers subject to the Ordinance have the option to make payments directly to San Francisco to satisfy the minimum health care expenses spending requirement. The court found inapplicable an analysis of a sister circuit in Retail Industry Leaders Ass’n v. Fielder, 475 F.3d 180 (4th Cir. 2007), where it was held ERISA preempted an analogous Maryland statute, in part because it presented employers with a “Hobson’s Choice,” that is, no choice but to alter an existing ERISA plan. (A trial-level court in New York reached a similar conclusion in Retail Industry Leaders Assoc. v. Suffolk County, E.D.N.Y., No. 06 CV 00531 (ADS) (ETB) (July 14, 2007).)

The Ninth Circuit reasoned, however, that, unlike the Maryland law, the City’s Ordinance was more comprehensive, offering employers a “meaningful alternative” to modifying existing ERISA plans or establishing new ones. The court pointed to a free or discounted health insurance plan available to certain employees, as well as to medical reimbursement accounts for certain employees operated by San Francisco and partially funded through employer contributions pursuant to the Ordinance. Therefore, the Ninth Circuit concluded that its holding does not create a conflict between the Federal Circuit Courts of Appeal. This is a view that some dispute and would support the U.S. Supreme Court reviewing the case.

Second, the Ninth Circuit observed the Ordinance is not concerned with the nature of the benefits provided to employees, but only the dollar amount of the payments for those benefits. Ignoring that any payments counted towards satisfying the Ordinance must be made by an employer for the purpose of providing health care services or reimbursing the cost of such services, the court stated that there would be little to differentiate such payments from wages. For this reason, among others, the court concluded making such payments to employees would not create an ERISA plan.

The court also found that the record keeping and administrative obligations required under the Ordinance were of little consequence to its analysis. It found these obligations insufficient to upset ERISA’s central purpose of providing a uniform regulatory regime over employee benefit plans, and thus did not conflict with the federal law.
With state and local jurisdictions seeking to address rising health care costs through their own legislative measures, it appears likely that more employers, particularly those with operations in more than one state, will have to deal with such enactments.

Complying with the Ordinance

As of January 1, 2008, employers who engaged in business within the City and County of San Francisco and averaged 50 or more employees (including those who worked within or outside of San Francisco) per week during a quarter, are required to make certain Health Care Expenditures ("HCE") to or on behalf of their "covered employees." Employers who averaged 20 or more employees per week during a quarter are required to begin compliance with the Ordinance as of April 1, 2008.

Which Employees Benefit

With few exceptions, a "covered employee" is any person who works within the City and County of San Francisco, who qualifies as an employee entitled to payment of minimum wage, has worked for the employer for 90 calendar days, and averages at least 10 hours of work per week in the City and County in 2008 (at least 8 hours of work per week in 2009). Those excluded from the Ordinance include:

1. employees who waived their right to the HCE because they receive health care benefits from another employer;
2. managers, supervisors, and contracted employees who earn at least $76,851 annually in 2008, and $80,397 or $38.65/hour in 2009;
3. certain trainees employed by non-profit organizations;
4. employees covered by the San Francisco Health Care Accountability Ordinance (which covers employees who work for employers that contract with San Francisco); and
5. employees covered by Medicare.

How Much Must Be Paid To, Or On Behalf Of, Covered Employees

A required HCE is any amount paid by a covered employer to its covered employees, or to a third-party on behalf of its covered employees, for the purpose of providing health care services or reimbursing the cost of such services. Examples include: increased health, dental and vision benefits or employer-paid premiums; contributions to a health savings account; reimbursement for expenses incurred in the purchase of health care services; and payments to the City to fund membership in the Health Access Program or reimbursement accounts maintained by the City.

An employer who averages 100 or more employees per week during a quarter is required to make a HCE of $1.76 for each hour paid to a covered employee during the quarter in 2008 ($1.85 in 2009). An employer who averages 20-99 employees per week during a quarter is required to make a HCE of $1.17 for each hour paid to a covered employee in 2008 ($1.23 in 2009). "Hours paid" includes hours worked, paid vacation hours, paid time off, and paid sick leave hours. A small favor to employers: there is a cap of 172 hours in a single month, or 516 hours in a single quarter.

Penalties for Violating the Ordinance

The San Francisco Office of Labor Standards Enforcement (OLSE) is the agency that enforces the Ordinance. The OLSE may order employers who violate the Ordinance to take appropriate corrective action. If corrective action is not taken, the agency may impose administrative penalties on employers. Penalties are a debt to the City and the City Attorney may file suit to collect. Further, the City also may create and impose liens against any property owned or operated by an employer who fails to pay a penalty. An OLSE determination of a violation may be appealed to a hearing officer appointed by the City Controller. The hearing officer's decision may be reviewed only by a writ proceeding in the Superior Court.

Employers who fail to make HCEs may be subject to penalties of up to 1½ times the total expenditures that an employer failed to make, plus simple annual interest up to 10% from the date payment should have been made; but the total may not exceed $1,000 for each employee for each week that the expenditures were not made. Other administrative penalties may be imposed by the OLSE, including:

- $25 per day for each day an employer fails to cooperate with an audit or investigation;
- $25 per employee if the employer does not provide reasonable access to records for audit or investigation;
- $500 for failure to maintain and retain records or failure to satisfy annual reporting requirements;
- $25 per day for each day an employer reduces the number of employees to achieve a lower HCE rate or to avoid being a "covered employer"; and
- $100 per day per person for violation of the anti-retaliation and discrimination provision of the Ordinance.

An Option for Meeting the HCE Requirement
While the Ninth Circuit noted that many employers (approximately 700) have decided to comply with the Ordinance by making the required payments to San Francisco, other employers have preferred to make these payments available to their employees directly, hoping, in part, to foster good employee relations. Some of these employers have adopted a narrowly-tailored health reimbursement arrangement (HRA) that provides for the tax-free reimbursement of certain health care expenses. Of course, as with any ERISA plan, there are certain compliance requirements, including the preparation of a summary plan description and processing claims timely.

The San Francisco Health Care Ordinance creates a number of challenges for employers who have employees working in the city and county. Jackson Lewis attorneys are available to assist you to meet those challenges.

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