U.S. Department of Labor

Pension and Welfare Benefits Administration
Washington, D.C. 20210

March 25, 1996

96-06A
ERISA SEC. 514(a)

Mr. Peter E. Braveman
Vice President for Legal Affairs
Cedars-Sinai Medical Center
Department of Legal Affairs
8700 Beverly Boulevard, Suite 2112
Los Angeles, California 90048-1865

Dear Mr. Braveman:

This is in response to your request for an advisory opinion concerning the applicability of Title I of the Employee Retirement Income Security Act of 1974 (ERISA). Specifically, you ask whether California's Knox-Keene Health Care Service Plan Act of 1975, California Health & Safety Code Section 1340 et seq. (Knox-Keene), would be preempted by section 514(a) of Title I of ERISA if it were applied to prohibit a welfare benefit plan from providing participants with incentives to influence their choices among alternative benefits offered under the plan.

You advise that Cedars-Sinai Medical Center (Cedars) maintains the Cedars Health Care Premium Payment Plan (the Health Care Plan) to provide health care benefits to its employees. Cedars has structured the Health Care Plan to allow participants to choose among several alternative health care options, including a preferred provider organization, a point-of-service plan and four different health care maintenance organizations (HMOs). The HMO options are offered through two third-party payers, Maxicare and Blue Cross of California. You represent that Cedars offers incentives to employees who elect either of the two HMOs that use the services of physicians who are members of Cedars-Sinai Health Associates or the Medical Group of Beverly Hills. These options that are favored by the plan are the Cedars-Sinai Care option (the C-S Care Option) and the Cedars-Sinai Health Plan HMO option (the C-S HP Option), which are both offered by Maxicare. The incentives offered by Cedars include reduced monthly cost for coverage, no deductibles, and low or no co-payments for employees who choose either the C-S Care Option or the C-S HP Option. In addition, Cedars offers an enrollment bonus to single employees who would pay no monthly premiums under the other Maxicare HMO options for selecting the C-S HP Option. Cedars offers the enrollment bonus as part of the Cedars' Flex Spending Account Plan (the Flex Plan), which qualifies as a "cafeteria plan" under section 125 of the Internal Revenue Code. Pursuant to the terms of the Flex Plan, the enrollment bonus is distributed in cash to those employees who select the C-S HP Option.

In correspondence dated September 29, 1994 and October 11, 1994, the California Department of Corporations (DOC) informed Maxicare that the enrollment bonus described above violated regulations issued pursuant to Knox-Keene. Those regulations, contained in the California Code of Regulations Title 10, Section 1300.46, state that:

No person subject to the provisions of [Knox-Keene] shall offer or otherwise distribute any bonus or gratuity to potential subscribers for the purpose of inducing enrollment or to existing subscribers for the purpose of inducing continuation of enrollment.

Section 514 of title I of ERISA provides, in pertinent part:

Except as provided in subsection (b) of this section, the provisions of this title and title IV shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 4(a) and not exempt under section 4(b).

Thus, section 514(a) of ERISA broadly preempts all state laws insofar as they "relate to" employee benefit plans covered by Title I of ERISA, subject only to certain exceptions as expressly provided in section 514(b) of ERISA.

In Opinion 76-90 (issued July 14, 1976), the Department of Labor (the Department) expressed the view that, to the extent Knox-Keene is interpreted to apply to ERISA-covered plans, it is preempted by ERISA. In that Opinion, the Department indicated that Knox-Keene's provisions concerning mandatory health care services and coverage, annual reporting requirements and licensing requirements, among others, are the types of provisions that would contravene the objectives of ERISA's preemption clause if applied to ERISA-covered plans.

In Hewlett-Packard Co. v. Barnes, 425 F. Supp. 1294 (N.D. Cal. 1977), aff'd, 571 F.2d 502 (9th Cir.), cert denied, 439 U.S. 831 (1978), the District Court held that state regulation of self-funded ERISA-covered employee benefit plans under Knox-Keene is preempted by section 514(a) of ERISA. On appeal, the U.S Court of Appeals, affirming the opinion of the District Court, stated:

We hold that ERISA preempts California's Knox-Keene Act to the extent that Knox-Keene seeks to regulate ERISA-covered employee benefit plans. If California desires to regulate such employee benefit plans as part of its comprehensive health care service legislation, then California must ask Congress to make appropriate changes in ERISA. Hewlett Packard Co. v. Barnes, 571 F.2d 502, 505 (1978).

The Department agrees with the position taken in Barnes that the attempted regulation of ERISA-covered plans through Knox- Keene is inconsistent with the objectives of ERISA's broad preemption clause. See New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co., 115 S.Ct. 1671, 1677 (1995)("The basic thrust of the preemption clause was to avoid a multiplicity of regulation in order to permit the nationally uniform administration of employee benefit plans.").

The holding in Barnes applies regardless of whether a plan is self-insured or fully insured. State laws that regulate insurance do not reach self-funded employee benefit plans because, pursuant to section 514(b)(2)(B), such plans may not be deemed to be insurance companies, other insurers, or engaged in the business of insurance for purposes of such state laws. State laws that regulate insurance do affect plans that purchase insurance, but only indirectly, through regulation of the plan's insurer and its insurance contracts. See FMC Corp. v. Holliday, 498 U.S. 52 (1990). Under section 514(b)(2)(B) of ERISA, an ERISA plan, whether insured or not, may not be directly regulated by state insurance laws. Therefore, it is the position of the Department that, to the extent that Knox-Keene is interpreted to prohibit employee benefit plans covered by Title I of ERISA from paying enrollment bonuses, it is preempted by section 514(a) of ERISA.

This letter constitutes an advisory opinion under ERISA Procedure 76-1. Accordingly, it is issued subject to the provisions of the procedure, including section 10 thereof relating to the effect of advisory opinions.

Sincerely,

Susan G. Lahne
Chief, Division of Coverage
Office of Regulations and Interpretations