

APPEALS COURT REVIVES SAN FRANCISCO'S EMPLOYER HEALTHCARE MANDATE

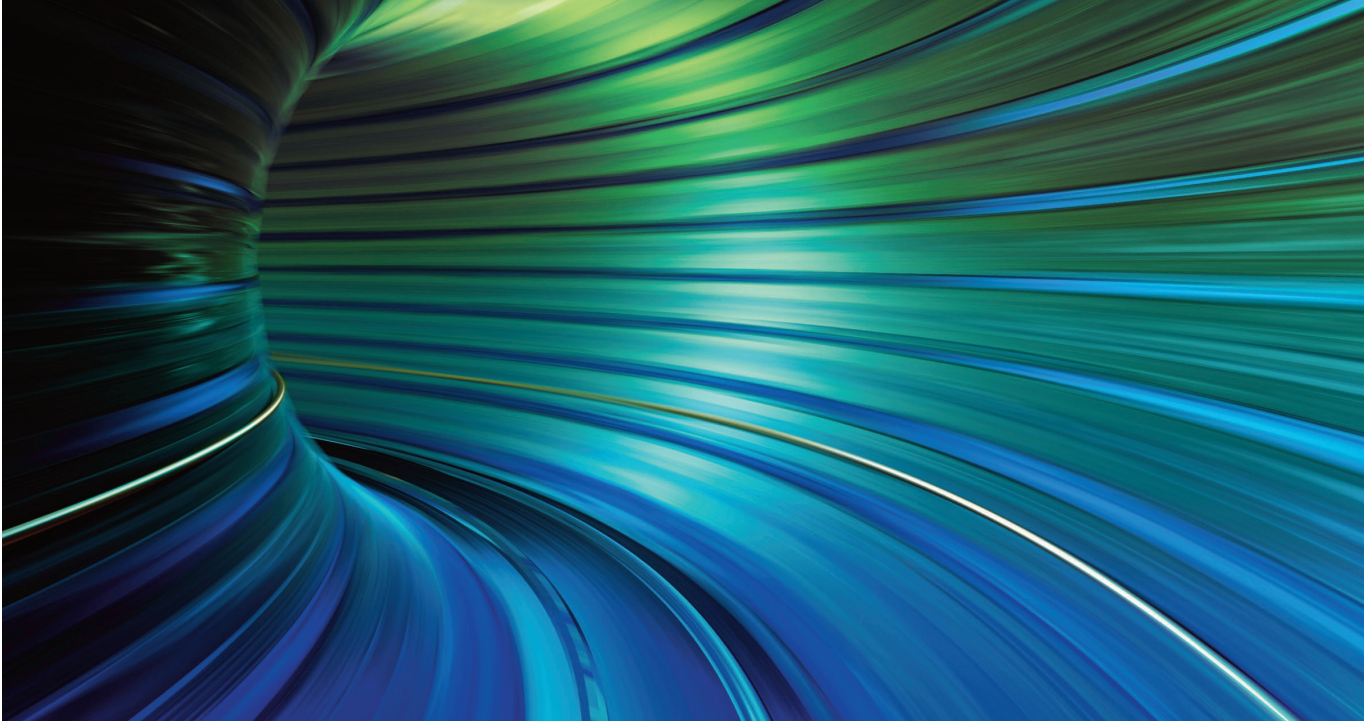
Employers breathed a sigh of relief when, days before the January 1, 2008 effective date of the San Francisco Health Care Security Ordinance (HCSO), a federal district court held that ERISA preempts the HCSO's minimum employer contribution requirement. The relief was short-lived, however. On January 9, 2008, a federal appeals court ruled that San Francisco can enforce the employer contribution requirement while the city appeals the district court's ruling. The appeals court's action leaves employers with some difficult decisions in the next few months.

Although the appeals court's ruling allows immediate enforcement of the employer contribution mandate, the ruling did *not* reverse the district court's holding that ERISA preempts the minimum contribution requirement. The appeals court will decide separately on the district court's preemption holding. In its January 9 decision, however, the appeals court signaled that it is likely to reverse the district court's holding. In fact, the appeals court found that the city had shown a "strong likelihood" of success in arguing that ERISA does not preempt the contribution requirement. This decision is not expected before summer of 2008.

So what now for employers? Compliance is required, but if the appeals court holds that the requirements are preempted, then employer compliance will have been unnecessary. Even if the appeals court holds that the contribution requirement is not preempted, that decision



may eventually be reversed. A decision against preemption would create a split in the circuit courts because another federal appeals court held that ERISA preempts a Maryland law that had a contribution requirement similar to the HCSO's. A split in the circuits would increase the likelihood that this case would end up before the U.S. Supreme Court. If the Supreme Court were to accept this case for review, no final decision would be likely before 2009. This leaves many employers asking whether they should amend their plans to extend coverage to all of the employees covered by the contribution requirement – or take a wait-and-see approach.



CONFLICTING CONSIDERATIONS

Most employers have benefit plans for their full-time employees that meet the HCSO requirements. The difficult issue for them under the HCSO is covering part-time employees who work as few as 10 hours per week. As reluctant as employers may be to add these benefits, many would probably prefer adding benefits (that can after all help them attract qualified employees) to HCSO's alternative – paying into the city's program. At the same time, employers may believe that the appeals court's decision is an aberration and that the contribution requirement will ultimately be found preempted. Many employers will also consider the fact that once expanded benefits are announced, it can be difficult to withdraw them.

As for timing, the rules are in effect as of January 9, but employers' first real compliance obligations will be due on April 30, 2008. This is the first deadline for an employer to meet the minimum contribution requirement, and also when the first annual report from employers is due. This first report need not reflect compliance with the contribution requirement because it will refer to 2007, before compliance was required. If an employer plans to meet the minimum contribution requirement by providing benefits, however, it must implement necessary plan changes very soon.

For the employer wanting to take the wait-and-see approach, there is one option that provides flexibility and compliance: contributing the minimum amount to the public program established by the HCSO. If the courts ultimately uphold the law, employers can then decide in a more stable environment how they wish to comply. Willis strongly recommends that employers discuss their response to the HCSO with their legal counsel and weigh the various risks carefully before proceeding.

HCSO BACKGROUND

In addition to establishing a healthcare program, San Francisco's HCSO requires that medium-sized and large businesses make certain minimum contributions toward their San Francisco employees' healthcare. Under the minimum contribution provision, an employer may either contribute to a medical plan (or other health benefits) or pay into the public program established by the HCSO. As written, the law was scheduled to take effect January 1, 2008. (See Willis' *Employee Benefits Alert, Issue 112* for information on the HCSO's effective date provisions.) The effective date was moved to January 9, 2008, the date of the appeals court ruling.

A business is covered by the mandate if it engages in business within the city of San Francisco, is required to obtain a San Francisco business registration certificate, and employs 20 or more employees per week. The HCSO does not apply to nonprofit organizations with fewer than 50 employees or to for-profit employers with fewer than 20 employees. To arrive at an official employee count, all employees must be counted regardless of location. If the number of employees fluctuates, employer size is based on the weekly average number of persons performing work for compensation.

EMPLOYEES COVERED

The HCSO covers employees who have been employed for at least 90 calendar days (not necessarily continuously or even in the same calendar year) and who work at least 10 hours per week in San Francisco. This requirement drops to eight hours on January 1, 2009.

Employers are not required to make expenditures for employees who qualify for certain exemptions. The categories of exempt employees are:

- Employees who voluntarily complete an official form waiving the right to have the employer make expenditures on their behalf because they are receiving healthcare from another employer
- Managers, supervisors and confidential employees earning more than \$76,851 during 2008 (this amount is indexed)
- Employees covered by Medicare or TRICARE/CHAMPUS
- Employees who are employed by a nonprofit corporation for up to one year as trainees in a bona fide training program consistent with federal law
- Employees who receive healthcare benefits pursuant to the San Francisco Health Care Accountability Ordinance (e.g., employees of city contractors)

THE MINIMUM CONTRIBUTION

The ordinance requires that employers make a quarterly healthcare expenditure to, or on behalf of, each of its qualifying San Francisco employees. A healthcare expenditure is any amount paid by the employer to its San Francisco employees or to a third party on behalf of its employees for the purpose of providing healthcare services or reimbursing the cost of such services.

Healthcare services include medical, dental and vision-care services or goods that, if unreimbursed, would qualify as tax deductible medical care expenses under Section 213 of



the Internal Revenue Code. They also include services or goods having substantially the same purpose or effect as such deductible expenses.

The employer determines how it will make the required expenditures and may utilize a variety of different ways to comply. Examples of healthcare expenditures that meet the requirements are:

- Payment of premiums for health insurance coverage for the covered employee
- Payments to the city to fund membership for the covered employee in Healthy San Francisco, the public program established by the HCSO
- Payments to a city-sponsored medical reimbursement account for the employee
- Expenditures made by self-funded plans (including administrative costs paid to a third party)
- Contributions on behalf of the covered employee to a health spending account, such as a health reimbursement arrangement, a flexible spending account or a health savings account
- Cash reimbursements to the covered employee for expenses incurred in the purchase of healthcare services, such as pharmacy bills

Payments made on behalf of an employee for dependents, such as a spouse, domestic partner or child, are included.

CALCULATING THE MINIMUM

The minimum required healthcare expenditure is calculated on a quarterly basis for each employee by multiplying the total number of hours paid to the employee by the applicable healthcare expenditure rate. *Hours paid* is defined as the hours during a quarter for which a person is paid wages for work performed within San Francisco or for which a person is entitled to be paid wages, including paid vacation hours, paid time off, and paid sick leave hours (but not exceeding 172 hours in a single month or 516 hours in a single quarter).

EMPLOYER HEALTH CARE EXPENDITURE RATE SCHEDULE (all rates per hour)			
BUSINESS SIZE	JANUARY 9, 2008	April 1, 2008	JANUARY 1, 2009
100+ Employees	\$1.76		\$1.85
50-99 Employees	\$1.17		\$1.23
20-49 Employees	Not Applicable	\$1.17	
1-19 Employees	Not Applicable		
Non-Profit Organizations with < 50 Employees	Not Applicable		

Starting January 1, 2010, rates will be determined on an annual basis. The Office of Labor Standards Enforcement (OLSE) will publish rates for each calendar year by March 1 of the preceding year.

Employers must make a minimum quarterly healthcare expenditure on behalf of each covered employee. Payments for one employee that exceed the minimum requirement cannot be used to meet the minimum requirement for another employee. In addition, expenditures made for an employee in one quarter that exceed the minimum required cannot be applied to reduce the minimum required expenditure for the employee in any other quarter. There are limited exceptions to these rules for employers that offer employees uniform or self-insured coverage.

UNIFORM COVERAGE

One exception is intended to cancel out the effect of an employer making lower contributions toward individual coverage than it makes toward family coverage. An employer providing uniform health coverage to a group of covered employees complies with the expenditure requirement for those employees if the average expenditure rate per employee meets or exceeds the employer's applicable expenditure rate. To calculate the average hourly expenditure rate, divide the total amount of healthcare expenditures made for the group of covered employees during a quarter by the total number of hours paid to those employees during that quarter.

The employer has the option of including in its calculation only those employees having the uniform coverage who are also covered by the ordinance or including all covered employees who have the uniform coverage. The ability of an employer to aggregate expenditures under this exception is limited to those employees with the same type of

coverage (e.g., an employer can aggregate the expenditures for those covered by an HMO but cannot aggregate the expenditures for those covered by an HMO with the expenditures of those covered by a PPO).

SELF-FUNDED PLANS

If the employer's plan is self-funded, the employer is excused from making the minimum expenditure for each employee as long as the preceding year's average hourly expenditure rate per employee meets or exceeds the required expenditure rate. To calculate the average hourly expenditure rate, divide the total amount of healthcare expenditures made for employees by the total number of hours paid to employees during the year. The employer has the option of including in its calculation only those employees covered by both the self-funded plan and the ordinance or including all employees participating in the self-funded plan (provided that all employees receive the same coverage). If the employer's expenditure rate in the previous year does not meet or exceed the current year's required expenditure rate, the employer must make expenditures in the current year to close the gap.

The city has created a **flow chart** that explains how to calculate the minimum healthcare expenditure.

The expenditure may be spread out, but must be made no later than 30 days after the end of each calendar quarter. By that time, the minimum expenditure for the preceding quarter must be made in full. Details about making payments to the city, if that is the option the employer chooses, can be found on the Healthy San Francisco **website**.

REPORTING REQUIREMENTS

Employers are required to annually report their healthcare expenditures to the city, which expects to have the forms for reporting 2007 information mailed by the end of January. The filing deadline has been extended from February 29 to April 30. The city will include the new compliance dates with its mailing. A **sample of the form** can be found online. **NOTE: because the data on the form will be electronically scanned, employers cannot use downloaded or photocopied forms.** As the employer mandate did not go into effect until 2008, the initial annual report will reflect the employer's voluntary 2007 businesses practice.

If the employer chooses to satisfy its obligation under the law by making payments to the city, then it must provide employees with **notice** that informs them when a deposit to the city has been made on their behalf. The city has not specified the time or manner for providing this notice.

In order to treat an employee as exempt due to their receiving healthcare benefits through another employer (e.g., through another job or the spouse's employer), the employer must collect a signed form from the employee waiving his or her rights to the healthcare expenditure. The employee has the right to cancel or revoke the waiver at any time, and an employer is prohibited from forcing or coercing the employee to sign the form. The employer must receive a signed form from the employee each year in order for the employee to remain exempt.

RECORDKEEPING

Employers must maintain records going back four years for each employee. Upon request, the employer must provide the OLSE reasonable access to those records. The required records include:

- Itemized pay statements that provide such information as gross wages earned, total hours worked (unless salaried), the employer's name and address, and the name and social security number of the employee
- The employee's address, telephone number and first day of work
- Records of healthcare expenditures made, including how the expenditures were calculated and proof that the expenditures were made
- A signed voluntary waiver form for each employee for whom the employer is claiming an exemption due to other coverage
- A copy of the Notice to Employee of Payment to the City with respect to employees for whom the employer made such contributions

San Francisco has a variety of resources available to employers with questions regarding their obligations under the ordinance. In addition to the materials (forms, Q/A, etc.) available on its **website**, the OLSE is available to answer questions by phone at 415 554 7892 or by email at **HCSO@sfgov.org**.



KEY CONTACTS

US BENEFITS OFFICE LOCATIONS

Atlanta, GA
404 224 5000

Austin, TX
800 861 9851

Baltimore, MD
410 527 1200

Birmingham, AL
205 871 3871

Boston, MA
617 437 6900

Cary, NC
919 459 3000

Charlotte, NC
704 376 9161

Chicago, IL
312 621 4700

Cincinnati, OH
513 762 7855

Cleveland, OH
216 861 9100

Columbus, OH
614 766 8900

Dallas, TX
972 385 9800

Denver, CO
303 218 4020

Detroit, MI
248 735 7580

Farmington, CT
860 284 6147

Florham Park, NJ
973 410 1022

Ft. Worth, TX
817 335 2115

Grand Rapids, MI
616 954 7829

Greenville, SC
864 232 9999

Houston, TX
713 961 3800

Jacksonville, FL
904 355 4600

Knoxville, TN
865 588 8101

Las Vegas, NV
702 432 7100

Long Island, NY
516 941 0260

Los Angeles, CA
213 607 6300

Memphis, TN
901 248 3100

Miami, FL
305 373 8460

Milwaukee, WI
414 271 9800

Minneapolis, MN
763 302 7100

Mobile, AL
251 433 0441

Naples, FL
239 659 4500

Nashville, TN
615 872 3700

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504 581 6151

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212 915 5422

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402 391 1044

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949 885 1200

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