

IN THE
UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

The Insurance Board Under The Social Insurance
Plan Of Bethlehem Steel Corporation and
Subsidiary Companies, et al,

Appellants,

v.

William Muir, Acting Insurance Commissioner
of the Commonwealth of Pennsylvania,

Appellee.

On Appeal from the United States District Court
for the Middle District of Pennsylvania

BRIEF FOR AMERICAN DENTAL ASSOCIATION,
AMERICAN ASSOCIATION OF ORAL AND MAXILLOFACIAL SURGEONS,
AMERICAN ASSOCIATION OF ORTHODONTISTS, AMERICAN ASSOCIATION
OF ORTHODONTIC SURGEONS, AND
AMERICAN ASSOCIATION OF ORTHODONTIC SURGEONS,
IN SUPPORT OF APPELLEE.

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BRIEF OF AMICUS CURIAE IN SUPPORT OF APPELLEE

INTEREST OF AMICUS CURIAE

This brief is submitted on behalf of the American Dental Association, the American Association of Oral and Maxillofacial Surgeons, the American Podiatric Medical Association, the American Psychological Association, and the American Chiropractic Association. These associations in the aggregate represent well over 250,000 professional health care providers, and each association individually is the largest group of persons practicing in that specialty.

The associations have been active in the state legislatures, United States Congress and the courts concerning state insurance laws similar to the law at issue in this case because such laws have a major impact on the provision of

health care services. They have been particularly concerned with the erosion of the states' historical authority over insurers and other entities, such as Blue Cross/Blue Shield ("BC/BS") that perform a similar function, through expansive interpretations of the preemption provision of the Employee Retirement Income Security Act of 1974 ("ERISA"). Despite the defeat of one major attempt by insurers to evade state regulation in Metropolitan Life Insurance Co. v. Massachusetts, 105 S. Ct. 2380 (1985), the associations now find that the insurance industry is making the same arguments in a slightly different factual context in order to again claim exemption from state regulation.

This is an important issue for persons who have supported state regulation of insurers. If companies that have historically been pervasively regulated by the states can evade that regulation by restructuring one aspect of their contracts, the efficacy of state regulation will be seriously undermined. In light of the Supreme Court's ringing reaffirmation of the states' authority over insurance companies in Metropolitan, such a result would be as contrary to the law as it is to sound public policy.

STATEMENT OF THE CASE

The factual and procedural background of this case is virtually identical to Metropolitan. Both cases involve a mandated benefit/freedom of choice statute enacted as part of the state's comprehensive laws regulating insurance. The

mandated benefit portion of the law requires that all contracts for the provision of health benefits issued by insurance companies licensed to do business in the state must provide for reimbursement of a minimum amount of mental health expenses. The freedom of choice portion of the law prohibits an insurance company from discriminating against licensed providers of health care services.

Both the Commonwealth of Massachusetts and the Commonwealth of Pennsylvania sought to enforce their laws against insurance companies licensed to do business in the state. Metropolitan Life in Massachusetts and BC/BS here had taken the position that the respective laws would require them to pursue reimbursement policies contrary to the provisions of the employee benefit plans that contracted with them. Instead of challenging the propriety of these laws against the standards defining the scope of a state's regulatory authority over insurers, however, both Metropolitan Life and BC/BS chose to defend their non-compliance by claiming that ERISA preempted the laws.

As will become apparent, we support the result but not the reasoning of the court below which held that ERISA did not preempt Pennsylvania's mandated benefit/mandated provider law. Rather, we believe the same result should be reached pursuant to the analysis used by the Supreme Court in Metropolitan.

SUMMARY OF ARGUMENT

Appellant's case is perched precariously on the sole distinction between this case and Metropolitan -- that

Bethlehem Steel retains risk in its arrangement with BC/BS. That there is any credibility to that case is due to the coincidence that the above distinction does have legal significance for some purposes. In fact, we would agree that BC/BS is probably not exempt from the antitrust laws for its activities under the McCarran-Ferguson Act's antitrust exemption. That does not, however, have anything at all to do with the Court's reasoning in Metropolitan. No matter how many times appellants prove their one point, it does not disguise the fact that their case is fundamentally out of legal context.

This case -- like Metropolitan -- requires a proper understanding of the states' broad authority over insurance companies. Specifically, the analysis must begin with the obvious: the business practices of BC/BS are pervasively regulated by the Commonwealth of Pennsylvania and the contract between BC/BS and Bethlehem Steel is an aspect of the former's business. Significantly, BC/BS is not claiming in this case that Pennsylvania could not regulate its business contracts under its insurance laws. Such a contention would be contrary to numerous cases holding that activities of BC/BS, including many that are not the "business of insurance" within the meaning of the antitrust exemption in the McCarran-Ferguson Act, are properly subject to the state's police power.

Rather, the issue presented by appellants here is whether ERISA preempts what would otherwise be a legitimate aspect of the state regulation of BC/BS. Their first argument

in support of that contention is that Section 514(b)(2)(A) which saves from preemption "any law of any state which regulates insurance" (hereinafter referred to as the "savings clause"), does not apply to the regulation of any practice of an insurance company that is not exempted by the McCarran-Ferguson Act from the antitrust laws as the "business of insurance." We contend that Congress intended to preserve state regulation of insurance companies, as well as state control over the "business of insurance." This construction is consistent with Metropolitan, the statutory language, and the Supreme Court's precedents involving McCarran-Ferguson. As the Supreme Court made clear in Metropolitan, Congress intended to preserve the full scope of state insurance law which has always been considered to apply to insurance companies even when they are not engaged in the "business of insurance."

Appellants' second contention is that the Pennsylvania state law must fail as indirect regulation of the Bethlehem Steel plan, despite the Supreme Court's explicit recognition in Metropolitan that indirect regulation of employee benefit plans is permissible under ERISA. Appellants argue, however, that the fact that Bethlehem Steel retains risk in its arrangement with BC/BS reverses the holding in Metropolitan. This is supposedly based on ERISA Section 514(b)(2)(B), which prohibits a state from deeming an employee benefit plan to be an insurance company for purposes of applying state law (hereinafter referred to as the "deemer clause"). In appellants' view, that

provision prohibits any application of state law where one of the parties to a transaction is a self-insured employee benefit plan, even when the party which is the subject of regulation is an insurer that has always been pervasively regulated by the state. We contend that the deemer clause by its terms neither prohibits indirect regulation nor sets forth any special rules for self-insured plans. Rather, it prohibits the direct regulation of employee benefit plans -- both insured and self-insured -- by the state. As a result, the deemer clause no more applies to Pennsylvania's attempt to enforce its law against BC/BS than it did to Massachusetts' attempt to enforce its laws in Metropolitan: in both cases, the state was regulating an insurer and not deeming a plan to be an insurance company. In sum, when a company such as Bethlehem Steel chooses to contract with a regulated entity, it must take that entity as it finds it; conversely, once BC/BS contracts with a self-insured plan, it does not suddenly lose its character as a regulated entity.

ARGUMENT

I. THE STATES HAVE TRADITIONALLY REGULATED ALL ASPECTS OF THE BUSINESS CONDUCTED BY BC/BS.

This case begins with the obvious -- the Commonwealth of Pennsylvania pervasively regulates the business activities of BC/BS, and the provision of services to Bethlehem Steel constitutes a business activity. Although we do not understand appellants to be suggesting that the Commonwealth could not

legitimately regulate BC/BS when it provides services such as those in this case absent ERISA, it may be helpful to clarify any misunderstanding generated by appellants' approach to this case.

The courts have long recognized the states' pervasive authority over insurers -- what the Supreme Court has called the states' "special relation to insurance." Osborn v. Ozlin, 310 U.S. 53, 65 (1940). It is the price insurers pay for the privilege of doing business in the state. As one court has noted with respect to BC/BS:

The statute creating the Blue Cross program provides certain benefits to and imposes certain burdens on Blue Cross so as to enable it to accomplish its statutory purposes.

Borland v. Bayonne Hospital, 300 A.2d 584, 592 (Sup. Ct. N.J., Chancery 1973), aff'd, 369 A.2d 1 (N.J. 1977).

Consistent with that grant of pervasive authority, the Pennsylvania statute regulates virtually all of BC/BS's activities. See, e.g., 40 P.S. § 6321 (maintenance of reserves); § 6322 (territorial restrictions); § 6324 (relationships with doctors providing services); § 6328 (organization); § 6329 (Department of Insurance approval of contracts); § 6330 (investment of funds). And where the statute may be silent, the courts have not hesitated to sanction the regulatory role of the Department of Insurance. See, e.g., Pennsylvania Dental Association v. Commonwealth of Pennsylvania, 398 A.2d 729 (Commonwealth Ct. of Pa. 1979) (Department of Insurance can

regulate BC/BS review of dental practices); Pennsylvania Association of Life Underwriters v. Commonwealth of Pennsylvania, 393 A.2d 1131 (Pa. 1978) (sales practices of insurers); Borland v. Bayonne Hospital, supra (contracts between BC/BS and hospitals).

Although this list could be expanded almost indefinitely, we deliberately chose cases and cited statutory provisions that involved activities that are not the "business of insurance" within the meaning of the McCarran-Ferguson Act antitrust exemption. This is not surprising -- there has never been any question that state regulation of insurance applies to activities that do not constitute the "business of insurance." The Supreme Court made this clear in Group Life & Health Insurance v. Royal Drug Co., 440 U.S. 205, 231 n. 38 (1979):

Many aspects of insurance companies are regulated by state law, but are not the 'business of insurance . . .'

This Court has implicitly recognized that state regulation of a practice of an insurance company does not mean that the practice is the "business of insurance" within the meaning of the McCarran-Ferguson Act. In both cases, the SEC v. Variable Annuity Life Ins. Co., 359 U.S. 65, 79 S.Ct. 618, 3 L.Ed.2d 640, and SEC v. National Securities, Inc., 393 U.S. 453, 89 S.Ct. 564, 21 L.Ed.2d 668, the challenged conduct was regulated by the State Insurance Commissioner, but this Court held that the practices were not the "business of insurance."

Instead of the "business of insurance" formulation, the Court in Royal Drug held that state regulation extends more

generally to the "activities . . . [or] business of insurance companies." Id. at 219 n. 18. Indeed, the breadth of this authority has always allowed the states to use their insurance laws in precisely the way Pennsylvania is attempting to use its law here: to indirectly serve social policies by regulating practices that do not involve the companies' assumption of risk. For example, in Insurance Dept. v. Saint Lukes Hospital of Bethlehem, 342 A.2d 773 (Pa. Comm. Ct. 1975), the Department of Insurance required hospitals that contracted with BC/BS to put in certain administrative controls as a condition to the approval of the contract. The hospitals argued that the state was trying to "indirectly . . . assume superintendency over hospital administration and fiscal management" (id. at 781), but the court sustained the regulation as a proper incident of the states' authority over BC/BS.¹ More generally, the Supreme Court has held that states can require insurers to contribute to a pool for uninsured motorists because of the states' pervasive authority over insurers, including the requirement "that local needs be serviced by the business." California Auto Association Inter-Insurance Bureau v. Maloney, 341 U.S. 105, 110 (1951).

¹ Significantly, the Supreme Court held in Royal Drug, supra, that BC/BS's provider agreements did not constitute the "business of insurance." Thus, the Saint Lukes case above is virtually identical to the case here as to whether Pennsylvania can regulate BC/BS contracts that are not the "business of insurance" to indirectly serve other social policies.

Thus, the fact that Pennsylvania is seeking to use its authority over BC/BS's claims administration business to further its legislative judgment that the risk of mental illness should be spread across the state is hardly noteworthy. Indeed, the business of claims administration has always been a matter of state regulation. Most states, including Pennsylvania, have adopted Unfair Insurance Practices Acts which regulate, among other things, claims practices. See 40 P.S. § 1171.5(a)(10) (1985). The National Association of State Insurance Commissioners has even promulgated a Uniform Administration Law governing this subject. See II NAIC, Model Laws, Regulations & Guidelines § 910-1. See also, II 1976 NAIC Proceedings 400-402 (indicating support for the administrators law from a wide spectrum of the insurance industry).

Although we do not subscribe to the legal reasoning of the court below, its decision is based on a sound intuitive grasp of the realities here. There is no question that BC/BS's contract with Bethlehem Steel differs little from its contracts with other entities in which it assumes some of the risk. Its activities here -- issuance of BC/BS cards to participants, utilization of BC/BS provider agreements, claims review, actuarial services, underwriting analysis -- are just as much traditional core activities of insurance companies as when they are performed in contracts where some of the risk is assumed. Indeed, there is no practical difference between the two situations from the perspectives of the participants and health care providers, who deal with BC/BS here in the same fashion as

when the contract between BC/BS and the employer also includes some assumption of risk.²

According to the Washington Business Group on Health, amicus curiae, twenty percent of the business of BC/BS now consists of arrangements similar to the one with Bethlehem Steel here. Given the state's historical role as the regulator of all of BC/BS's business activities, it is inconceivable that such a large (and growing) portion of those business activities would be held to be outside the scope of the state's regulatory authority. In fact, as noted above, we do not understand appellants to be making that argument; their argument is that ERISA prohibits what would otherwise be a legitimate exercise of the police power to regulate insurance. But, as we now show, that argument misperceives both the language of the ERISA preemption provision and the unanimous opinion of the Supreme Court in Metropolitan.

II. THE SAVINGS CLAUSE IN ERISA PRESERVES THE FULL SCOPE OF THE STATES' AUTHORITY OVER INSURERS.

The fact that appellants have not chosen to challenge Pennsylvania's ability to regulate the business activities of BC/BS absent ERISA is significant. It means that they must find something in the statutory language or Metropolitan that

² As we show below, there is also little practical difference from the perspective of Bethlehem Steel and BC/BS. The lines between uninsured, self-insured, partially insured and fully insured plans have been virtually obliterated in the kind of sophisticated market that exists today in health insurance. See n. 7, infra.

supports the proposition that only a portion of state regulation of insurance was saved by Congress in ERISA. To meet their burden, appellants contend that BC/BS is not providing any "insurance" in this arrangement for purposes of the savings clause's preservation of "laws regulating insurance." We read that phrase more broadly to preserve state regulation over the business activities of insurance companies.³ As we now show, our reading is much more consistent with the precedents.

Appellants' burden is made more onerous by the presumption applicable here. Although appellants begin their argument with an ode to the breadth of ERISA's general preemption provision, versus the supposed narrow savings clause, their reasoning quickly runs afoul of Metropolitan. For the Court there made no secret of the proper presumption for judicial consideration of ERISA preemption cases, reaffirming its consistent precedent that "[w]e . . . must presume that Congress did not intend to pre-empt areas of traditional state regulation. See Jones v. Rath Packing Co., 430 U.S. at 525, 97 S. Ct., at 1309." Metropolitan, *supra*, 105 S. Ct. at 2389. As the Court has elsewhere stated, the task of the courts is not to find an interpretation that ousts state law (as appellants urge here), but rather to "reconcile the

³ We assume without discussion that whatever distinctions there may be between commercial insurers and service corporations such as BC/BS are not relevant to this case. Thus, we will, for the sake of convenience, refer to BC/BS as an insurance company or insurer for purposes of the savings and deemer clauses. See, e.g., Metropolitan, *supra*, 105 S. Ct. at 2383 n. 1.

operation of both statutory schemes." Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware, 414 U.S. 117, 127 (1973). This is no less true of ERISA: "the presumption is against pre-emption, and we are not inclined to read limitations into federal statutes in order to enlarge their pre-emptive scope." Metropolitan, supra, 105 S. Ct. at 2390. As the Court concluded, "while the general pre-emption clause broadly preempts state law, the savings clause appears broadly to preserve the states' lawmaking power over much of the same regulation." Id. at 2389 (emphasis added).⁴

Consistent with this expressed refusal to read limitations into statutes to find preemption, the Court in Metropolitan rejected various attempts by petitioners there to restrict the plain meaning of the savings clause. Specifically, petitioners there complained that mandated benefit laws were not really "insurance laws," but "health laws" aimed at indirectly regulating the health plans of employers, and that Congress had not intended to save from preemption such "innovative" laws that interfered with an employer's asserted freedom to design health plans.

⁴ In reaching that conclusion, the Court examined the legislative history of ERISA for some indication that Congress had intended to preserve only certain portions of state insurance law. It concluded, however, that "[t]here is a complete absence of evidence that Congress intended [a] narrow reading of the savings clause." Metropolitan, supra, 105 S. Ct. at 2392. On the contrary, the Court held that the last-minute changes to the preemption provision in the ERISA House-Senate conference "gave the insurance savings clause a much more significant role, as a provision that saved an entire body of law from the sweeping general pre-emption clause." Id. at 2392 n. 23 (emphasis added).

Undaunted by the Supreme Court's unanimous rejection of these limitations on the savings clause in Metropolitan, appellants here have suggested yet another limitation on state regulation, arguing that Congress meant to preserve only laws that regulate practices that constitute the "business of insurance." The same reasoning used by the Court in Metropolitan to reject the limitations urged there, however, applies with equal force here.

The Court in Metropolitan began with the "common-sense view" that the regulation of insurance contracts surely constituted a law "regulating insurance." Id. at 2390. Our analysis of the statutory language starts there as well: common-sense suggests that regulation of insurance companies also constitutes a law "regulating insurance."

As in Metropolitan, the statutory language explicitly supports our formulation. Thus, the Court in Metropolitan relied on textual analysis of the savings clause and the deemer clause to hold that the savings clause preserved laws regulating the provisions of insurance contracts. Noting that the deemer clause prohibits a state from deeming an employee benefit plan to be an insurance company "for purposes of any law of any state purporting to regulate . . . insurance contracts . . . ," the Court reasoned that "[u]nless Congress intended to include laws regulating insurance contracts within the scope of the insurance savings clause, it would have been unnecessary for the deemer clause explicitly to exempt such laws" Id. at 2390.

The deemer clause has the same effect here by providing that the states cannot deem an employee benefit plan "to be an insurance company or other insurer . . . or to be engaged in the business of insurance . . . for purposes of any law of any State purporting to regulate insurance companies" (emphasis added). By its terms, the deemer clause sets forth Congress' understanding that states regulate both "insurance companies" and the "business of insurance." Just as the Supreme Court reasoned in Metropolitan, if the savings clause were intended to preserve only laws regulating the "business of insurance," it would have been unnecessary to include in the deemer clause laws regulating "insurance companies."

Thus, appellants' attempt to read limitations into the savings clause is fundamentally inconsistent with Metropolitan, the language of the statute, the legislative history and the traditional judicial presumption against preemption. These factors compel a holding that the savings clause applies to both state regulation of insurance companies, as well as regulation of the "business of insurance."

Appellants' reliance on the McCarran-Ferguson Act does not change that result; on the contrary, that law strongly supports the state's position here. Appellants' basic position is that despite BC/BS's paramount role in the provision of benefits to Bethlehem Steel's employees, it is not engaged in the "business of insurance" because it does not bear the insurance risk in the arrangement. We would agree that appellants would have a strong case if BC/BS were being sued

for violation of the federal antitrust laws -- the exemption in McCarran-Ferguson from the antitrust laws for certain activities of insurance companies has been interpreted to require that the challenged activity involve some assumption of risk by the insurer. But that is not this case; the issue here is whether state regulation of insurance should be preserved. And that issue involves a quite different section of the McCarran-Ferguson Act, and compels a very different conclusion from that urged by appellants.

We find it strange that appellants should call this Court's attention to the McCarran-Ferguson Act cases because they so strongly negate their position here. Chief among these cases is Group Life & Health Insurance v. Royal Drug Co., supra. The issue there was whether the antitrust laws applied to agreements between BC/BS and participating pharmacies. The Court ultimately held that such agreements did not constitute the "business of insurance" for purposes of the McCarran-Ferguson Act's antitrust exemption.

The narrow majority was challenged by a vigorous dissent which relied primarily on the fact that the states regulated BC/BS participation agreements under their insurance laws. The majority, however, distinguished between McCarran-Ferguson's broad preservation of state authority over insurance companies and that Act's narrow antitrust exemption for certain practices constituting the "business of insurance." Because of its central importance to this case, we think it important to

quote the Supreme Court at length (id. at 219 n. 13) (emphasis added):

There is no question that the primary purpose of the McCarran-Ferguson Act was to preserve state regulation of the activities of insurance companies, as it existed before the South-Eastern Underwriters case. The power of the States to regulate and tax insurance companies was threatened after that case, because of its holding that insurance companies are in interstate commerce. The McCarran-Ferguson Act operates to assure that the States are free to regulate insurance companies without fear of Commerce Clause attack. The question in the present case, however, is one under the quite different secondary purpose of the McCarran-Ferguson Act - to give insurance companies only a limited exemption from the antitrust laws.

In short, the McCarran-Ferguson Act freed the States to continue to regulate and tax the business of insurance companies, in spite of the Commerce Clause. It did not, however, exempt the business of insurance companies from the antitrust laws. It exempted only "the business of insurance."

Thus, the Supreme Court in Royal Drug carefully distinguished between the states' unquestioned regulatory authority over the "business of insurance companies" and the limited antitrust exemption for the "business of insurance." The question for this case is whether the Supreme Court's discussion of McCarran-Ferguson in Metropolitan refers to the former or the latter. The answer to that question was explicitly set forth in Metropolitan when the Court referred to the "primary concern" of Congress in the McCarran-Ferguson Act, which, as noted, was the preservation of state authority over insurance companies, and not the more narrow intent in that Act to exempt certain of those regulated activities from federal

insurance companies, and not the more narrow intent in that Act to exempt certain of those regulated activities from federal law as the "business of insurance."⁵ As the Court noted, McCarran-Ferguson and the savings clause both "serve the same federal policy" of preserving state regulation.⁶ Metropolitan, supra, 105 S. Ct. at 2392 n. 21.

⁵ For this reason, we disagree with the reasoning of the court in Powell v. Chesapeake & Potomac Telephone Co. of Virginia, 780 F.2d 419 (4th Cir. 1985). In holding that the savings clause did not preserve laws regulating the activities of insurance companies, as opposed to laws regulating the "business of insurance," the court relied on language from the Supreme Court's opinion in SEC v. National Securities, Inc., 393 U.S. 453 (1969). According to the Fourth Circuit, that case held that McCarran-Ferguson only applied to the "business of insurance." But, the reasoning from National Securities cited in Powell refers to the preemption of federal law (whether the States were "supreme in regulating all the activities of insurance companies" (see, Powell, supra at 423)), and not to the "primary concern" of McCarran-Ferguson -- preservation of the states' control over the activities of insurance companies. As the Supreme Court made clear in both National Securities and Royal Drug, there was no dispute in National Securities that the states had authority over the insurance companies; rather, the issue was whether that regulatory control was sufficient to oust federal law. See especially, Royal Drug, supra, 440 U.S. at 219 n. 18 (quoted at length at p. 8, supra). In short, the Powell court, like appellants here, simply relied on the wrong part of McCarran-Ferguson.

⁶ Indeed, the Court's discussion of the three factors used in McCarran-Ferguson cases reveals this distinction. While the Court discussed the "spreading [of] risk" as one factor to consider, it did so in a quite different context than that used by appellants here. Specifically, the Court did not focus on whether the contracts with Metropolitan transferred risk to the insurer, but on the fact that the state law "was intended to effectuate the legislative judgment that the risk of mental-health care should be shared." This corresponds to one of the fundamental purposes of state insurance regulation -- what one theorist has called the "socialization of risk" -- to spread risk across the state through regulatory control over insurance companies. See Kimball, The Purposes of Insurance Regulation: A Preliminary Inquiry in the Theory of Insurance Law, 45 Minn. L. Rev. 471, 511-514 (1961).

over the activities of insurance companies. As the First Circuit has reasoned, Congress designed the preemption provision and savings clause with full knowledge of the "functions and scope of employee benefit plans," especially the substantial role played by insurance companies in those plans. See Wadsworth v. Whaland, 562 F.2d 70, 78 (1st Cir. 1977), cert. den., 435 U.S. 980 (1980). We think it apparent that the savings clause was intended to eliminate the danger that the expansive protection from state law afforded plans in the general preemption provision would leave insurance companies essentially unregulated. Under this construction, the task of the courts in cases such as this one is to determine whether the company claiming preemption is an insurance company regulated under state law.

By contrast, appellants' restrictive interpretation of the savings clause would require consideration of fine distinctions concerning where the risk lies in particular arrangements. This would lead to enormous confusion for the line between "insurance" and "self-insurance" is not easy to draw, particularly with respect to the sophisticated arrangements between large employers and insurers that are commonplace today. Some forms of "insurance" place considerable risk on the employer, while other forms of "self-insurance" involve risk-taking on the part of the insurer.⁷ Nor is it uncommon for intergrated plans to

⁷ For example, most large plans with "insurance" have experience-rated contracts, where favorable claims (Footnote continued on next page.)

insure some benefits and self-insure others, while insurance companies sometimes lay off part or all of the risk in reinsurance transactions. Under appellants' theory, the courts will need to decide whether enough risk has been transferred in these gray areas, thereby guaranteeing different results in virtually identical cases.⁸

Moreover, one of the most disadvantaged groups under appellants' preferred solution would be the participants in these plans -- the very class ERISA was intended to protect. As noted above, state insurance law provides important safeguards for beneficiaries in areas such as claims administration. For that reason, the courts have consistently held that state law provides remedies for improper handling of claims by

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experience leads to refunds and bad experience leads to increases. In "retrospective rating," the employer pays a percentage of the projected claims at the beginning of the year and pays the remainder after adjustment for claims experience. Many BC/BS plans are community-rated, which means that premiums increase or decrease in relation to the claims experience of a community group. In other words, much of the risk in these "insured" plans remains with the employer.

Conversely, many "self-insured" plans purchase stop-loss coverage to shift the risk of large losses to insurers. Other self-insured plans enter into "minimum premium" arrangements with insurance companies that also involve risk-assumption by both the plan and the insurer.

See generally, Handel, New Directions in Welfare Plan Benefits: Instituting Health Care Cost Containment Programs 107-112 (Int'l. Found. 1984).

⁸ This has already occurred in other Circuits. Thus, appellants cite Moore v. Provident Life and Accident Insurance Co., 786 F.2d 922 (9th Cir. 1986), where the court held that state law was preempted because the insurer provided only "stop-loss" coverage; that is, it assumed the risk only when claims exceeded a certain amount. (Footnote continued on next page.)

insurance companies that service employee benefit plans. See, e.g., Lessard v. Metropolitan Life Ins. Co., 613 F. Supp. 1263, 1272 (D. Me. 1985); Kanne v. Connecticut Gen'l Life Ins. Co., 607 F. Supp. 899, 905 (C.D. Cal. 1985); Presti v. Connecticut Gen'l Life Ins. Co., 605 F. Supp. 163, 167 (N.D. Cal. 1985); McLaughlin v. Connecticut Gen'l Life Ins. Co., 565 F. Supp. 434, 443-44 (N.D. Cal. 1983); Eversole v. Metropolitan Life Ins. Co., 500 F. Supp. 1162, 1168 (C.D. Cal. 1980). Appellants have advanced no reason why the participants of Bethlehem Steel's plan should have no recourse against BC/BS when it violates the state laws that have always governed its conduct.

In sum, we urge the Court to adopt the common-sense notion that the savings clause preserves state regulation of insurance companies. Metropolitan could not be any clearer with respect to the breadth of the ERISA savings clause, and cannot be distinguished by inventing a limitation on that clause that is merely a variation on the theories so soundly rejected by the Court. After Metropolitan, there can be no question that Congress intended in ERISA to preserve the full scope of the states' authority over the business practices of insurance companies.

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This decision is directly contrary to Michigan United Food and Commerical Workers Unions v. Baerwaldt, 767 F.2d 308 (6th Cir. 1985), cert. den., No. 85-810 (1986). In that case, the insurance company provided the same services as Provident did in the Ninth Circuit case, but the court held that the state law was not preempted because the company in Baerwaldt provided stop-loss insurance.

III. THE DEEMER CLAUSE DOES NOT EXEMPT INSURANCE COMPANIES FROM STATE REGULATION WHEN THEY CONTRACT WITH SELF-INSURED PLANS.

In the preceding section, we argued that Metropolitan cannot be interpreted to sustain appellants' argument that the savings clause should apply only to state laws regulating those business practices that constitute the "business of insurance." This section addresses appellants' only other argument -- that the deemer clause not only exempts the Bethlehem Steel plan from state law, but also every entity that contracts with it. As we now show, appellants fare no better with this attempt to evade state regulation.

There is no question that Pennsylvania's attempt to regulate BC/BS has an impact on Bethlehem Steel's plan as it is currently constituted. It is now well settled, however, that, where a state has regulatory authority over an entity, it does not lose that authority simply because the entity contracts with an employee benefit plan.

This is, of course, one of the principal lessons of Metropolitan. The petitioners there, like BC/BS here, argued that they were exempt from state law because they contracted with an employee benefit plan. In a sense, they were attempting to "borrow" the plan's exemption from state law on the theory that regulation of them constituted impermissible indirect regulation of the plan. As we have already exhaustively discussed, this argument was even more emphatically rejected than a unanimous decision would suggest.

The same principle has been affirmed in other cases involving self-insured plans. For example, in Rebaldo v. Cuomo, 749 F.2d 133 (2nd Cir. 1984), the court held that a state law that "prescribe[d] hospital rates chargeable to self-insured benefit plans" was not preempted by ERISA. Similarly, in Wayne Chemical Corp. v. Columbus Agency Service Corp., 567 F.2d 692 (7th Cir. 1977), the court held that a broker that had organized a self-insured multiple employer trust was subject to state insurance law. See also, Activity Report of the House Committee on Education & Labor, H.R. Rep. No. 94-1785, at p. 48 (1977) (reasoning that organizers of self-insured multiple employer trusts are subject to state regulation "even though state action is barred with respect to the plans" which contract with the trust).⁹

Appellants' attempt to forge a different rule in this case is based on the theory that the deemer clause constitutes a kind of "super-preemption" for self-insured plans and all who contract with them. We believe that the deemer clause merely

⁹ The longstanding problems of the states and federal government in dealing with self-insured multiple employer trusts illustrate still other dangers inherent in appellants' position. These trusts pool contributions from small employers for purposes of self-insuring benefits. When the states moved to regulate them under their insurance laws, organizers of the trusts claimed exemption from state law on the theory that the deemer clause prohibited regulation of self-insured plans. The Department of Labor countered by taking the position in a series of advisory opinions that, while the self-insured plans that subscribed to the trust were exempt from state law because of the deemer clause, the trust itself was not. See, e.g., DOL Advisory Op. 81-84A (Dec. 9, 1981); DOL Advisory Op. 81-73A (Sept. 24, 1981); DOL Advisory Op. 80-10A (Feb. 11, 1980); DOL Advisory Op. 79-54A (Aug. 5, 1979).

prohibits direct regulation of any employee benefit plan, and does not purport to distinguish between insured and self-insured plans for purposes of the potential indirect effect on the plan of state regulation of an entity that contracts with it.

Resolution of this dispute requires an interpretation of the deemer clause. As the Supreme Court has repeatedly held, such interpretation must "begin with the language employed by Congress and the assumption that the ordinary meaning of that language accurately expresses the legislative purpose." Park 'n Fly, Inc. v. Dollar Park and Fly, Inc., 105 S. Ct. 658, 662 (1985). It is, therefore, noteworthy that appellants have never explained precisely where in the language of the deemer provision appears any mention of self-insured plans, much less the entities that contract with them.

The deemer provision, on its face, provides that a state may not take the position that an employee benefit plan covered by ERISA is an insurance company or engaged in the business of insurance. Even though Congress has elsewhere in the preemption provision made distinctions based on the insured or self-insured nature of a plan,¹⁰ there is no mention of any such distinction in the deemer clause. By its express terms, the deemer provision applies to any kind of employee benefit plan, whether self-insured or not.

¹⁰ See ERISA § 514(b)(6), which distinguishes between "fully insured" (defined in § 514(b)(6)(D)) and "not fully insured" plans for purposes of the application of state law. Since these provisions do not apply to plans sponsored by a single employer, they are not directly relevant to this case.

Although the ERISA preemption provision is admittedly convoluted, it does constitute a logical whole. It is clear that Congress wished to preempt state laws relating to plans. It is equally clear, especially after Metropolitan, that Congress did not want to open a regulatory void by limiting the states' authority over insurance companies and therefore enacted the savings clause. In this context, the deemer clause appears as Congress' instruction that state insurance law should not be broadened beyond insurance companies -- as some states were attempting to do -- by creating the fiction that an employee benefit plan is an insurance company.¹¹ See generally, Hewlett-Packard Co. v. Barnes, 425 F. Supp. 1294, 1300 (N.D. Cal. 1977), aff'd., 571 F.2d 502 (9th Cir. 1978) (deemer clause prohibits states from considering plans "to be a unique variety of insurance arrangement").

Thus, the deemer clause, on its face, applies to one state activity -- calling a plan an insurance company and then regulating that plan as such an entity. Pennsylvania is no more doing that in this case than was the Commonwealth of Massachusetts in Metropolitan; both states' actions were directed at undoubted insurance companies and not at the

¹¹ While ERISA was being considered, a few states were attempting to exact premium taxes from employee benefit plans on the theory that they were unlicensed insurance companies. See, e.g., State ex rel. Farmer v. Monsanto Co., 517 S.W.2d 129 (Mo. 1975); Mutual Life Insurance Co. v. New York State Tax Commission, 32 N.Y.2d 348, 298 N.E.2d 672 (1973). This appears to have been the reason for the deemer provision. See, Sullivan, Regulatory Aspects of the ERISA of 1974, 1974 Proc. Leg. Soc. Am. Life Conv. 15, 49-52.

employee benefit plans that contracted with them. In other words, appellants' argument that the state is violating the deemer clause here simply does not fit the "ordinary meaning of the language" of the provision.

Appellants' attempt to supplement the language of the deemer clause to support their case rests almost exclusively on the Supreme Court's observation in Metropolitan that uninsured plans are not subject to "indirect regulation." That observation, however, is simply not strong enough to support the entire weight of appellants' case. To begin with, that sentence is dictum since uninsured plans were not involved in Metropolitan. Nor is it likely that the Court was even thinking of the situation here where an arguably self-insured plan utilizes the services of an insurance company. Rather, the Court's observation was probably based on the assumption that, if a plan is uninsured, there is no insurance company to regulate in the arrangement and the only way for the state to affect the plan is by calling it an insurance company and directly regulating it as such in contravention of the deemer provision.¹²

That the Supreme Court in Metropolitan understood the plain meaning of the deemer provision to be aimed at prohibiting direct regulation of plans is clear. In its first discussion of the deemer clause, the Court noted that, in light

¹² The fact that the Supreme Court referred to "uninsured" plans is significant because there is a distinction between the terms of art, self-insured and uninsured. The latter refers generally to plans where there is no insurance company involvement. See Handel, supra, at 108.

of that provision, "Massachusetts has never tried to enforce [its law] as applied to benefit plans directly." Metropolitan, supra, 105 S. Ct. at 2387 n. 14 (emphasis added). In its second reference, during its discussion of the fact that the deemer clause mentions law regulating insurance contracts, the Court stated (id. at 2390) (emphasis added):

Unless Congress intended to include laws regulating insurance contracts within the scope of the insurance savings claim, it would have been unnecessary for the deemer clause explicitly to exempt such laws from the savings clause when they are applied directly to benefit plans.

The plain meaning of the statutory language, the discussion in Metropolitan, the structure of the preemption provision, and the legislative history all point to the conclusion that the deemer clause was intended to prevent a state from directly regulating an employee benefit plan. At the same time, that clause has been interpreted by the Supreme Court to apply to both insured and self-insured plans, and has further been interpreted not to prohibit indirect regulation of the former. There is simply no evidence that the deemer clause was meant to confer exemptions from state law for entities that contract with self-insured plans on some theory that those plans should be more protected from indirect regulation than plans that transfer some risk to the insurer.¹³

¹³ We are aware that two Fifth Circuit cases -- Light v. Blue Cross & Blue Shield of Alabama, 790 F.2d 1247 (5th Cir. 1986) and Children's Hospital v. Whitcomb, 778 F.2d 239 (5th Cir. 1985) -- can be read to set forth a per se rule that, whenever a plan is self-insured, state law is automatically preempted. It is apparent, however, that neither court even considered, much less rejected, the arguments advanced here.

Indeed, there is no reason whatsoever to treat Bethlehem Steel any differently from the companies that contracted with the insurance companies in Metropolitan. Those companies wished to pursue reimbursement policies that were at odds with the legislative judgment of the states, but they gave up that opportunity when they chose to contract with a regulated entity. As the Washington Business Group on Health, amicus curiae, has pointed out, many employers choose instead to preserve their immunity from state law by avoiding any arrangement with regulated entities in their employee benefit plans. That option was, and is, available to Bethlehem Steel. But, when Bethlehem Steel chooses an entity such as BC/BS to provide services to its plan, it must take that entity as it finds it. As the United States has elsewhere stated in support of mandated benefit laws under ERISA: "Congress did not intend to confer any special exemption or privilege on [plans] as [purchasers of services from insurers]. [S]ales to them must conform to the same rules as those to any other . . . buyer." Memorandum for the United States as Amicus Curiae, Wadsworth v. Whaland, 435 U.S. 980 (1978).¹⁴

¹⁴ Any other rule would lead to strange results. For example, it is clear that variable annuities are not "insurance" for purposes of federal law (see SEC v. Variable Annuity Life Ins. Co., 359 U.S. 65 (1959)), yet are regulated by the states (id. at 69). Under appellants' theory, this state regulation would be preempted whenever the product is sold to an employee benefit plan. This reasoning would also apply to state banking and securities laws, which are referred to in the savings clause. Thus, banks that service plans would presumably be exempt from state banking laws, while underwriters could sell to plans securities that have not complied with state Blue (Footnote continued on next page.)

Finally, whatever policy there might be for exempting Bethlehem Steel from state law certainly does not apply to BC/BS. It is axiomatic that BC/BS is not only extensively regulated by Pennsylvania, but is a creation of that state's legislature. To allow it to escape state legislation -- to hold that it has somehow ceased to be an insurance company regulated by Pennsylvania in connection with twenty percent of its business -- would be a truly extraordinary, and unfortunate, result.

CONCLUSION

In the final analysis, this case is not about fine legal distinctions concerning risk assumption, or even the exercise in statutory construction borrowed in this brief from Metropolitan. Rather, this case concerns a compact between the Congress, the states and the insurance industry concerning the states' regulatory authority over insurance companies that has endured for over forty years. The Commonwealth of Pennsylvania complied with its responsibilities under that compact by enacting legislation after due consideration, a process in which BC/BS and employers such as Bethlehem Steel are not exactly unrepresented.. The Supreme Court in Metropolitan determined that Congress had intended to abide by that compact by according great respect to the legislative process by which

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Sky statutes. These consequences become even more incongruous if the determinant of whether state banking or securities laws applies to regulated entities is the insured or self-insured nature of the plans.

a state regulates insurance companies. We urge this Court to do the same.

For the foregoing reasons, we urge the Court to affirm the judgment below.

Respectfully submitted,



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