

## ERISA at 50: No Midlife Crisis for ERISA Preemption

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### AT A GLANCE

While the Employee Retirement Income Security Act of 1974 (ERISA) is best known for regulating employer-sponsored retirement benefits, it also applies to employer-sponsored benefit plans more broadly, including employer-sponsored health plans. Significantly, ERISA effectively preempts state and local regulation of self-funded, employer-provided health benefits. The scope of this has generated some degree of debate. Proponents of ERISA preemption point to the creation of a uniform and predictable regulatory environment for employers with respect to their ERISA-governed benefit offerings, while its detractors believe that state and local governments ought to have a greater role in pursuing health care reform beyond their current ability to regulate health insurance. To better understand the value of ERISA preemption to large employers, the Employee Benefit Research Institute and the American Benefits Council conducted roundtable discussions with over a dozen benefits executives at large companies.

### Key Insights

- ERISA was enacted, in part, in response to high-profile cases in which workers received substantially smaller retirement benefits than were promised as a result of poorly funded pension plans. However, ERISA does not apply solely to retirement benefits, but also to many employer-sponsored benefits in general, including most employer-sponsored health benefits.
- An important provision in ERISA — a legal framework commonly referred to as ERISA preemption — effectively renders the federal government the sole regulator of self-funded employer-sponsored health benefits. State and local governments, responding in part to incentives to improve health care outcomes for their constituents and in part to various stakeholders, occasionally pass legislation that may encroach upon ERISA preemption. While these challenges have not completely eroded ERISA preemption, recent court cases have created some uncertainty around the scope of ERISA preemption and the prevailing view that federal law generally should be the sole source of regulation of self-funded group health plans.
- To gauge the value that ERISA preemption provides for employers, the Employee Benefit Research Institute and the American Benefits Council interviewed benefits executives at large employers in a roundtable format.
- Three main themes emerged in the roundtable discussions. First, under ERISA preemption, there is a uniform landscape of regulations rather than a patchwork of 50 different state-level regulations, which makes it possible for an employer operating in more than one state to administer and offer benefits equitably to their employees, regardless of the state or locality where those employees are located. Second, ERISA preemption reduces administrative costs and burdens, thus enabling employers to deliver richer benefits and lower-cost coverage to their workers. Third, ERISA preemption fosters innovation that would otherwise be stifled by different states requiring different coverages or administrative rules (such as claims procedures or the like).
- Employers remain committed to providing health benefits to employees and their families. If ERISA preemption were eroded, however, benefits executives would worry about higher costs for providing health benefits and would likely closely watch their competitors to determine next steps.

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# ERISA at 50: No Midlife Crisis for ERISA Preemption

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## A Brief Primer on ERISA

The Employee Retirement Income Security Act (ERISA), as its name suggests, was initially best known for establishing standards for employer-sponsored retirement plans. Passed in 1974, the appetite for pension reform was brought about by several high-profile incidents involving poorly funded and mismanaged pension plans that resulted in beneficiaries receiving much smaller payouts than they had been promised, as was the case with the pension plan of Studebaker, an automobile manufacturer.<sup>1</sup> ERISA established basic fiduciary standards for retirement plan trustees, including requirements for reporting to the federal government, a responsibility to disclose information to workers, and minimum funding levels. However, the law applies not only to defined benefit pension plans, but also to employer-sponsored health plans.

A crucial component of ERISA is the legal framework that effectively overrides state and local regulation of employee benefit plans. This legal framework, known as ERISA preemption, supersedes state or local laws to the extent they “relate to any employee benefit plan.” In crafting a law that supersedes state and local benefits legislation, Congress intended for ERISA to establish a nationally uniform standard for employee benefit plans and aimed to avoid the evolution of a patchwork of different state-level regulations and requirements that could stand as a deterrent to employers voluntarily offering benefits to their employees.<sup>2</sup>

Employers who self-insure (or self-fund) their health plans are exempted from state and local regulations; employers who purchase fully insured plans from insurance carriers, however, are effectively subject to state and local laws, because ERISA preemption permits states to continue to regulate insurance companies and insurance products. Since self-funded, employer-provided health plans would only be subject to federal law, this enables employers who sponsor such plans to offer consistent benefits to workers across state lines. Proponents of ERISA preemption point to this uniformity as easing administrative burdens and costs for multi-state employers while also allowing them to tailor their benefits to the needs of their work force and provide benefits equitably, regardless of where those workers live or work.

The current ERISA preemption framework is not without its detractors, however. In general, state and local legislators have a vested interest in and strong incentives for passing laws that could reduce the costs patients pay out of pocket for certain types of health care or mandate coverage of certain health services for their constituents. Moreover, various stakeholders in the health care ecosystem bring issues to state and local legislators to consider, including efforts to protect certain types of businesses and regulate others. Therefore, according to those who take a dim view of ERISA preemption, it is justified for state and local legislators to pass laws that affect self-funded, employer-sponsored health benefits, including efforts to lower costs paid by patients, prohibit certain plan designs, mandate coverage of certain services or drugs beyond those required under federal law, and dictate which providers must be allowed in network. Such an objective has underpinned some of the recent legislative efforts that have encroached upon the ERISA preemption framework.

ERISA preemption has thus far mostly survived legal challenges and been solidified by court rulings and case law. Per the legislative language of ERISA, it preempts state and local laws that explicitly regulate health plans. In *Shaw v. Delta Air Lines*, for instance, the U.S. Supreme Court ruled in 1983 that a New York state law requiring pregnancy-related disability benefits in employer-sponsored health insurance plans was preempted by ERISA. This case established a sweeping standard for which state laws run afoul of ERISA preemption. Namely, state laws “having a connection with or referring to” an employee benefit plan would be preempted by ERISA.

Like most matters that end up before the U.S. Supreme Court, there is ambiguity as to whether a particular law has an impermissible interaction with ERISA. As such, ERISA preemption has evolved through case law. For instance, in 2020, an Arkansas law setting minimum reimbursement amounts for pharmacy benefit managers (PBMs) was challenged as

running afoul of ERISA preemption on the basis that the law could potentially impact the price of administering a prescription drug plan as part of an employer-sponsored health benefits plan. However, the Supreme Court ruled in *Rutledge v. Pharmaceutical Care Management Association* that “the mechanisms [of the Arkansas law] do not require plan administrators to structure their benefits in any particular manner,” and thus, the Arkansas law is not preempted by ERISA. Further challenges may be forthcoming. For instance, in 2023 Florida legislators passed a law regulating PBMs located in the state, and the law appears to apply to both commercial health plans as well as self-insured health plans.

The erosion of ERISA preemption could have profound impacts on employers and workers. Legislators intended for ERISA to preempt state and local laws to prevent employers from having to navigate a patchwork of different regulatory regimes depending on the state(s) in which they operate.<sup>3</sup> Should state and local legislators continue to pass legislation that chips away at ERISA preemption, employers may have to adhere to different sets of regulations depending on where their workers are located or reside. Dealing with these regulations could affect both the cost of providing health benefits and employers’ appetite to continue providing health benefits.

To mark the 50<sup>th</sup> anniversary of the passage of ERISA, as well as to develop a better understanding of the value of ERISA preemption to employers, the Employee Benefit Research Institute (EBRI) and the American Benefits Council<sup>4</sup> conducted a series of focus groups with benefits decision makers at large employers. These companies employed over 600,000 workers in aggregate, covered over one million lives in their health care programs, and accounted for over \$7 billion in health care spending. Not only are large employers more likely to be at the forefront of innovative benefits programs, but they are also more likely to have operations and employ workers in multiple states and, thereby, to rely upon ERISA preemption. The focus groups with benefits decision makers about ERISA preemption touched on several different employee benefit plans but focused on health benefits, as this area is currently a flashpoint.

The roundtable discussions with the focus groups lasted for two hours, and each focus group consisted of roughly half a dozen participants. These participants held job titles such as vice president of benefits, head of global benefits, and ERISA and benefits counsel and were closely involved with their respective firms’ benefits designs and offerings. The focus groups were structured in such a way that the same questions were asked of each group, but they were loosely structured to give respondents room to expound on a particular question if it proved to generate a fruitful discussion.

## **What Does ERISA Preemption Mean to You?**

We began our roundtable discussions by asking benefits executives about how they viewed ERISA preemption. Praise for ERISA preemption was unanimous; essentially, without ERISA preemption, “it would be prohibitively burdensome [to provide health benefits],” offered one executive at a high-tech manufacturer. This sentiment was echoed by others in the group: “Without preemption, it can make the administration of a self-funded health plan really difficult,” added an executive at a media conglomerate.

As this discussion progressed, several themes emerged. Benefits decision makers indicated that ERISA preemption provides immense value to employers and that value manifests in three primary ways. First, benefits executives valued the regulatory certainty that ERISA preemption offers. For companies that have operations in multiple states, sponsoring a single plan with uniform standards is less administratively burdensome than sponsoring a health plan subject to a patchwork of different state- and local-level regulations. Second, they recognized that ERISA preemption enables their firms to innovate and provide customized benefits targeted toward addressing the specific needs of their work force. Third, they appreciated that ERISA preemption effectively reduces the cost of providing benefits for their work force, due to the reduced administrative burden.

## **Uniform Standards, Uniform Benefits**

One of the biggest benefits that ERISA preemption offers employers is a uniform standard for employee benefit plans. Additionally, the carveout for self-funded plans such that they are regulated solely at the federal level provides

employers additional regulatory certainty. Benefits executives in the roundtable discussion expressed a strong appreciation for their ability to offer a consistent menu of benefits across the various states in which they operate.

Rather than benefits differing based on employee location, employers place value on ERISA preemption enabling them to offer a consistent, location-agnostic set of benefits. “We have a strong desire for everyone to have equal benefits regardless of where they sit,” said a benefits executive at a tech company, adding, “If we had to have different benefit offerings in each state, I don’t know what we’d do.” Roundtable participants also highlighted fairness and equity concerns as a motivation to offer a consistent set of benefits across all workplaces. “The equity piece is a large conversation now that more people are virtual. If one worker lives in Colorado and one lives in New Jersey, and they get different benefits, that’s not equitable,” explained a benefits executive at an insurance company. “We see this now on certain aspects of paid leave; you may get 13 weeks in one state and eight in another state. How do you make it equitable?”

The ability to offer a consistent set of benefits has second-order advantages as well. “For us, it’s the consistency in terms of administration and being able to offer similar plans across the various states,” explained one benefits executive at a manufacturing firm. “Having a uniform set of rules to follow keeps costs lower,” added a benefits executive at a utility company, citing lower compliance costs as an additional benefit of ERISA preemption. Moreover, employees also benefit from “a consistent employee experience ... across states,” noted a benefits executive at a consumer goods conglomerate.

Additionally, employers view the consistent benefits made possible by ERISA preemption as a tool for increasing work force mobility. If a worker for a firm with operations in multiple states moves from a satellite office in one state to the company headquarters in another, they know they will have access to a similar menu of benefits. “[With ERISA preemption,] we’ve removed a barrier to the mobility of talent, because they know their benefits are staying consistent,” remarked one senior benefits executive at a telecommunications firm. And not only will employees have access to a similar menu of benefits, they can also be confident that a health plan in one state will cover the same health conditions as a similar plan in another state.

## **Innovation**

Proponents of ERISA preemption have cited innovation as an important benefit of preemption. Employers that self-insure their benefits are better able to address issues specific to their work force rather than being subject to mandates by various state and local initiatives that can apply via regulation of the carrier or a specific insurance product. “I can’t imagine a state-by-state regime telling us what to manage,” said one benefits executive at an airline. “ERISA is the path to innovation,” agreed a benefits executive at an insurance company, adding, “If we had to be subject to varying state mandates, it’d be a nonstarter.”

Each employer has a unique work force with attendant unique needs and concerns, particularly in terms of health care utilization. A manufacturing firm with a large blue-collar work force will have different health care requirements than a tech company with a predominantly white-collar work force, for instance. ERISA preemption “has given us the freedom and flexibility to be innovative, and we have done that. Going to a 50-state [patchwork] solution is the opposite of innovative,” explained a benefits executive at a telecommunications firm. A one-size-fits-all, top-down approach from state and local legislators not only worried the benefits decision makers with whom we spoke, but could also undercut their ability to tailor benefits that best serve their work force in the most efficient manner possible.

Rather, the benefits executives we spoke to preferred a more targeted approach to designing their benefits. “A lot of innovation comes from point solutions helping employees live healthier, better lives,” observed a benefits executive at an insurance company. “People in Congress don’t think companies do any innovation; [they think] that we just pay for stuff,” lamented a benefits executive at a utility company, while pointing out areas in which self-funded employers — enabled by ERISA preemption — have produced innovation, such as directing patients to Centers of Excellence and providing assistance and information to patients using specialty drugs to improve adherence and save money. A regime

in which different states can mandate different coverages is not conducive to enabling employers to best tailor their health benefit programs to both address the needs of their employees and also contain costs.

## High Quality, Low Costs

While employers and employees alike face rising health care costs, benefits executives praised ERISA preemption for enabling their companies to deliver high-quality health benefits while mitigating the cost burden on both the plan sponsor and workers. “ERISA is the framework that allows all of this to happen in a cost-efficient manner that benefits all,” observed a benefits executive at a telecommunications firm. Roundtable participants highlighted two channels by which ERISA preemption enables employers to improve the quality of health benefits and realize cost savings.

First, ERISA preemption reduces costs for employers by reducing administrative burdens and leveraging economies of scale. In a hypothetical world in which ERISA preemption disappeared, “I’d have to double my staff, or hire more consultants to manage the complexities ... it’s like turning a single benefit plan into 50 benefit plans,” said one executive at a telecommunications firm. “If we had to communicate different plans with different designs to different audiences, we’d have to get additional staff for that as well,” added an executive at an insurance firm. A third executive agreed, adding, “If it wasn’t doubling the staff, you’d be doubling the costs, because you need consultants to help you out. It’s more effort to do something that is running efficiently right now.” Not all benefits decision makers have completed cost projections for a world in which ERISA preemption does not exist, but there was unanimous agreement that administrative costs would increase.

Furthermore, ERISA preemption enables employers to use their size to lower costs. Specifically, benefits decision makers cited the ability to negotiate with outside vendors and third-party administrators to leverage economies of scale, a practice that could be threatened by the erosion of ERISA preemption. “If you can’t use the same provider [in each state] on the PBM side, the costs go up. That’s the whole point of just being able to go to [a single vendor]: We can control our costs better,” explained one benefits executive at a media conglomerate, adding, “When you lose that control by having to go with a number of different providers, it’s going to end up costing more.” That sentiment was echoed by others. “ERISA allows us to negotiate with vendors on a larger scale so we can pool our risk and get more competitive pricing,” added a benefits executive at an insurance firm. Another benefits executive observed that the “[economy of scale] accrues to the benefit of your employees ... employees save money by virtue of their employers using their scale to negotiate.” Importantly, workers may ultimately bear the costs incurred by the erosion of ERISA preemption.

Second, benefits executives reported that ERISA preemption helps their companies save money by improving health care outcomes through the use of innovative plan designs and strategies that might otherwise bump up against individual state laws in the absence of preemption. “We were able to put in an ACO [accountable care organization], which has driven better control over quality and outcomes if certain metrics are met,” explained an executive at a manufacturing company. Better care also manifests in a stronger work force: “People can’t come to work if they’re sick,” as an executive at an insurance company bluntly put it. Driving better outcomes for patients can ameliorate that. “We’re getting productivity in two ways: [Workers] are healthier and they’re staying on top of their costs,” explained a benefits executive at a manufacturing firm.

Several benefits executives worried that, in a world without ERISA preemption, self-funded health plans would not be tenable. “You won’t be able to have self-insured plans anymore, which will jack up the price. You’ll have to give it over to an insurer ... the reason we all self-insure is because [fully insuring] is too expensive. That’s going to have to be something else the company has to consider,” said an executive at an entertainment conglomerate. While not completely ruling out dropping health benefits, one executive at a manufacturing firm predicted that “our [health] program would not be as rich if ERISA preemption were lifted.”

## Commitments to Health Benefits

To the extent ERISA preemption is eroded by the courts, Congress, states, or localities, employers may reconsider their approach to offering health benefits altogether. While several participants voiced doubt that they could continue offering health benefits in the more difficult and uncertain regulatory environment created if ERISA preemption were to disappear, most indicated that there would still exist an appetite to provide employer-sponsored health benefits.

Some executives indicated that their decision might be driven by competitive pressures. “We’d look at what our competitors are doing and do that,” said an executive at a transportation company. “You’d have the issue of competitors; if someone can go work somewhere else to get better benefits, they will,” added an executive at a media conglomerate, indicating that providing health benefits functions as a recruitment and retention tool and would likely continue to do so in the future. “Everyone is going to have the same problem [competing for talent],” they added.

In addition to competitive pressures, executives indicated that they preferred to retain control of health benefits, all else being equal. In general, roundtable participants found the option of shunting workers toward state-run health insurance exchanges in lieu of providing health benefits themselves to be unpalatable. “Exchanges haven’t always been the most stable, and state to state, options are very different,” observed an executive at a consumer goods conglomerate. “There’s an element of paternalism. As soon as you take that away, everyone is on their own, and there’s nobody saying ‘hey, we’re here to help you,’” added an executive at a transportation company, referring to the support employers provide their workers to navigate their health benefits and issues in the claims process.

Benefits decision makers did note that their companies already face headwinds in providing health benefits to their work force. In particular, “It’s hard to justify the prices of drugs in the U.S. vs. abroad,” noted one executive at a trade association that represents several large companies. “We all have ROE [return on equity] targets ... and if there’s a way to say, look, you’re hurting shareholder value, it becomes a question [to drop health benefits],” added an executive at an insurance company. “If and when costs become much more unsustainable — I think we’re closer than just 5–10 years out — all of us will be looking at what tradeoffs we have to make,” a benefits executive at a manufacturing firm observed soberly. While there was no consensus on exactly how far into the future the cost of providing health benefits might become unsustainable, that potential tipping point looms large in executives’ minds.

Still, while roundtable participants expressed a sense that there were challenges in providing health benefits, they indicated their companies would continue to do so for the foreseeable future. One benefits executive at an insurance company responded that their firm would stop offering health benefits “when we stop adding value,” an individualized calculation that each employer must conduct on its own. “The trend line is ugly,” quipped one executive at an airline, referring to the pace at which spending on health care was increasing, “but not any uglier than before.”

## Conclusion

Currently, employer-sponsored health benefits exist in a superimposed regulatory environment. Employers who purchase insurance through a carrier — otherwise known as fully insured health plans — find themselves effectively subject to federal regulations as well as state and local ones. Self-funded arrangements, however, are regulated solely at the federal level, thanks to ERISA preemption.

However, the ERISA preemption framework is not guaranteed to be retained in its current form indefinitely. Potential conflicts and challenges to ERISA preemption can arise whenever state or local governments pass laws that could be interpreted as relating to — and potentially having an impermissible connection with — employee benefit plans. Recent examples include a 2020 Vermont law requiring contraceptives to be covered at no cost, or a recent “pay or play” health insurance ordinance in Seattle that set a minimum expenditure employers must pay toward employee health care benefits, along with other disclosure requirements. While ERISA preemption has persisted despite these legal challenges thus far, that may not always be the case as courts take evolving views of the scope of ERISA preemption. Furthermore, while this research focused exclusively on health benefits, it should be noted that retirement plans also operate under ERISA’s framework. Consequently, one should expect that many of the benefits of preemption that apply to health plans highlighted by the roundtable participants (e.g., administrative consistency for employers and equitable benefits for employees of a company working in different states) apply to retirement plans as well.

The roundtable participants made clear the immense value that ERISA preemption offers their organizations. The legal framework allows companies to offer a consistent menu of high-quality benefits to workers across state lines and fosters employer innovations that address those workers' specific needs. Were ERISA preemption to disappear, benefits executives were not exactly sure how their companies would adapt to the uncertain world and potential morass of state-level regulations, but they recognized that health benefits are still an important tool to recruit and retain a high-quality work force.

## Endnotes

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<sup>1</sup> Wooten, James A "The Most Glorious Story of Failure in the Business: The Studebaker-Packard Corporation and the Origins of ERISA," *Buffalo Law Review*, 2001.

<sup>2</sup> Copeland, Craig and Bill Pierron. "Implications of ERISA for Health Benefits and the Number of Self-Funded ERISA Plans," *EBRI Issue Brief* no. 193, January 1998.

<sup>3</sup> Pierron, Bill, and Paul Fronstin. "ERISA Pre-Emption: Implications of Health Reform and Coverage," *EBRI Issue Brief* no. 314, February 2008.

<sup>4</sup> The American Benefits Council is the national trade association for companies concerned about federal legislation and regulations affecting all aspects of the employee benefits system. The Council's members represent the entire spectrum of the private employee benefits community and either sponsor directly or administer retirement and health plans covering more than 100 million Americans.