Policy Brief

A Historical Overview of Hawaii's Prepaid Health Care Act

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INTRODUCTION

As a project of the Hawaii Institute for Public Affairs (HIPA), The Hawaii Uninsured Project (HUP) is developing solutions to cover Hawaii's medically uninsured population.[1] HUP acts as a neutral convener and has formed various work groups to address targeted populations of the uninsured.

While HUP's work groups were formed to examine potential solutions to cover the uninsured, the Prepaid Health Care Act (PHCA) Work Group was established to study the impact of the PHCA on Hawaii. The PHCA Work Group includes representatives from business (small and large), labor (public and private), policymakers, health plan providers, health care providers, academia, and advocacy groups.

In particular, the PHCA Work Group, in conjunction with the University of Hawaii Social Science Research Institute, is examining the impact of the Act on Hawaii's labor markets and health insurance coverage. The group takes no position and will make no recommendations on the repeal, amendment or retention of the PHCA. As the PHCA approaches its 30th anniversary, HUP's objective analysis on the impact of the PHCA is both timely and relevant.

It should be noted that the impact of the PHCA is broad-reaching and multi-faceted, ranging from the impact on health insurance coverage, labor markets, costs of doing business in Hawaii, and its impact on health care as a whole. Before those issues can be addressed, it is essential that a basic understanding of the PHCA be established. There is much confusion in the community about the purpose and provisions of the PHCA, including the context in which it was adopted.

The purpose of this Historical Brief is to provide background and history on Hawaii's PHCA. The PHCA requires employers who employ persons for twenty hours or more a week for four consecutive weeks to provide them with health insurance. Enacted in 1974, the PHCA is the cornerstone to the provision of health care in Hawaii.

This Historical Brief will explain the provisions of the PHCA; examine the legislative history of the PHCA; and discuss the legal challenges and exemption resulting from the federal Employee Retirement Income Security Act (ERISA). While there has been much discussion on the various issues of the PHCA and its impact, this Brief will be limited to a description and history of the PHCA. Such understanding of the PHCA is fundamental to the overall discussion on the PHCA which is pervasive in today's discussion on business, labor, and health care. This Historical Brief is the first in a series of policy briefs devoted to fact-based research and analysis on the PHCA.

The Prepaid Health Care Act

The Hawaii Prepaid Health Care Act, Chapter 393, Hawaii Revised Statutes (HRS) was enacted on September 2, 1974, with an implementation date of January 1, 1975. It is administered by the Hawaii Department of Labor and Industrial Relations (DLIR), Disability Compensation Division. The Prepaid Health Care Advisory Council reviews and provides recommendations to the Director of DLIR to ensure that the applicant plans meet the prevalent plan standards under the PHCA (See discussion below in the "prevalent plan").[2]

Objective and Provisions of the PHCA

The primary purpose of the PHCA is to provide a certain degree of coverage and protection against the high costs of health care for those employees who do not have access to adequate health insurance coverage.[3] Under the PHCA, employers are required to pay a portion of the employee's individual premium such that the employee's share is no more than 1.5 percent of their annual wages. Under this law, employees who work 20 hours or more a week for four consecutive weeks are covered while certain groups of workers are exempt from the provision. Hawaii is the only state in the nation with a law mandating that employers provide health insurance to their employees under the PHCA.

The main components of the PHCA are as follows:[4]

- Employers must provide prepaid health insurance coverage for all employees who work for 20 hours or more for 4 consecutive weeks, and earn a gross monthly income of 86.67 times the State's minimum hourly wage.
- The employer and the employee may share the costs for the health insurance premiums. The employer can withhold 50 percent of the premium cost from employees, not to exceed 1.5 percent of their monthly gross wages. The employer must pay for the balance of the costs.
- Coverage for the prepaid health insurance plan must include benefits for: inpatient and outpatient hospital care; surgical services, including anesthesia and post-surgical services; home, office, and hospital physician visits; diagnostic laboratory services and x-ray services; and maternity care.
- The required prepaid health care plan must meet prevailing plan standards which are established by the "prevalent plan," which is the plan with the largest number of subscribers in the state.
- The Prepaid Health Care Advisory Council reviews the plan applicants and recommends the approval of the plans to the Director of DLIR.
- Exempt workers are as follows: government employees, seasonal employees, family-type employment (spouse working for spouse), real estate persons or insurance agents paid solely by commission, collective bargaining workers, and those who work less than 20 hours per week for a given employer.
- Employees may decline employer's coverage if they have health insurance from another means or if they decline coverage for religious reasons.

History and Legislative Intent of the PHCA
Serious discussion for the PHCA started when the Hawaii State Legislature ("Legislature") in 1967 passed and the Governor enacted Act 198 which tasked the Legislative Reference Bureau to study temporary disability insurance and prepaid health insurance. The Legislature commissioned two studies by Dr. Stefan Riesenfeld of the University of California at Berkeley. The first study was titled Temporary Disability Insurance; the second study titled Prepaid Health Care in Hawaii.[5] Both of Dr. Riesenfeld's studies resulted in the passage of landmark legislation in their respective areas.[6,7]

Dr. Riesenfeld conducted a comprehensive study of both the national and local health insurance marketplace relating to both public and private insurance offerings and enrollment. Dr. Riesenfeld's findings were the basis of the PHCA, which was considered at the time to be the most feasible plan to provide prepaid health care to employees under the age of 65. In addition to addressing the Legislature's target population (ages 19-64), the PHCA used existing systems (private and government based systems of financing and delivery) and community standards (the plans that were prevalent in the community).[8]

In the 1960's there was much discussion at the national level on the provision of compulsory national health insurance.[9] Acknowledging this discussion, the Legislature included a clause in the PHCA which would invalidate the Act if a form of national health insurance was developed and implemented. However, since the 1960's, no such federally mandated program has been enacted.

When the development of the PHCA started in 1973, legislators were faced with many of the same issues and concerns that we face today: rising health care costs, limited access to health insurance and services for some, and Hawaii's economic concerns, among others. One senator opined that the bill "would not be feasible at this time due to the economic situation of the State of Hawaii".[10] This could very well be a statement that is made today. The Legislature also discussed the issues of increasing health care needs and rising health care costs, conversations that are still going on today.[11] Nonetheless, these lawmakers saw a compelling need to cover more people with health insurance by way of enacting the PHCA. Much thought and discussion went into the development of the PHCA, including issues relating to actual benefits, pressure on employees, and undue costs on employers.

The drafters of the PHCA were concerned about the benefits that were to be provided by the prevalent plan and to ensure that the benefits should be reasonable and medically sound.[12] They also wanted the benefits to focus on preventive care and early medical attention.[13] While the PHCA was to promote preventive health care and early medical attention, the PHCA was also drafted to ensure that the employee would have coverage when "the employee most critically needs the health care," namely when an employee is hospitalized or so ill that it prevents them from working.[14] Lawmakers thus included a provision which requires the employer to pay for their share of the premium for a minimum of three months.[15]

The drafters were also aware of the potential pressures of non-hiring or firing that the employee may face if pressed by an employer to waive coverage or pay more of the premium.[16] The PHCA prohibits the waiver of rights for health insurance coverage or agreement to pay a greater share of the premium by the employee.[17] While the drafters wanted to "encourage coverage of dependents", they did not intend to have employers cover the dependents under the Plan A of the PHCA because of the potential added costs.[18]

PHCA and the ERISA Preemptive Clause

The Federal Employee Retirement Income Security Act of 1974 **(**ERISA), is administered by the U.S. Department of Labor and regulates pension and employee benefit programs, including employment based health insurance coverage operated by private employers or unions.[19] There are some exceptions where ERISA regulations do not apply, e.g., government and religious organizations. ERISA was enacted as a means to remedy private pension plan fraud and mismanagement by providing comprehensive federal standards to safeguard employee pension and benefit programs.[20] Specific guidelines regarding fiduciary standards, funding standards, reporting and disclosure standards, etc. were developed through ERISA.[21]

There are two ERISA provisions that directly affect the PHCA: ERISA Supercedure/Preemptive Clause; and Hawaii's ERISA Exemption/Waiver.

ERISA Supercedure/Preemption Provision

The pertinent section of the ERISA Preemption Clause is as follows:[22]

> *Except as provided in subsection (b) of this section, the provisions of the subchapter and subchapter II of this chapter shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 1003(a) of this title and not exempt under section 1003(b) of this title. This section shall take effect on January 1, 1975.*

This broad provision essentially preempts *any* state law that conflicts with the ERISA provision and thereby prohibits states from enacting statutes which are contrary to ERISA. Essentially, under this preemption clause, states cannot require employers to offer health coverage or dictate the terms of its health plan coverage by way of employer's premium share, benefits, etc.[23] These very areas where ERISA claims province were the same areas that the PHCA mandated. Consequently, the passage of ERISA established a jurisdictional showdown between the State of Hawaii's PHCA and the federal government's ERISA.

This showdown culminated in Standard Oil Company of California v. Joshua C. Agsalud and set the stage for subsequent legal challenges.[24] In 1976, Standard Oil Company of California, filed an action for declaratory and injunctive relief from the PHCA, as

Standard Oil provided a self-funded health care plan that did not comply with the PHCA standards. In 1977, the U.S. District Court of Northern California ruled in favor of the plaintiff, and in 1980, the U.S. Court of Appeals, Ninth Circuit, upheld the District Court's decision in favor of Standard Oil.[25] In its findings, the circuit court ruled that the PHCA fell under, and was therefore preempted by, ERISA. This ruling highlighted the fact that in order for the PHCA to be valid, an exemption from ERISA was needed.

Hawaii's ERISA Exemption

To avoid the preemptive provision of ERISA, and therefore uphold Hawaii's PHCA, Hawaii's Congressional delegation pursued and obtained an ERISA exemption. The exemption was signed into law by President Ronald Reagan in 1982. In particular, the waiver provided Hawaii with the nation's only exemption to the preemptive provisions of ERISA, as follows: [26]

> *(B) Nothing in subparagraph (A) shall be construed to exempt from subsection (a) of this section -*
> *(ii) any amendment of the Hawaii Prepaid Health Care Act enacted after September 2, 1974, to the extent it provides for more than the effective administration of such Act as in effect on such date.*

The ERISA exemption is specific to the Hawaii Prepaid Health Care Act as enacted on September 2, 1974, and prohibits any substantive changes to the PHCA. According to a 1999 opinion by Hawaii's Attorney General, any substantive amendment to the PHCA that provides more than "effective administration" of the Act is subject to the preemptive clause. The Attorney General's opinion also stated that while substantive amendments are subject to preemption, passing it would not necessarily jeopardize the original pre-amendment PHCA provisions. Hence, to substantially amend the PHCA, another Hawaii-specific ERISA waiver would be required. Alternatively, elimination of the ERISA preemptive provision, although unlikely, could be pursued.

It should be noted that throughout the legal challenges in *Standard Oil* and the pursuit of the ERISA waiver, the PHCA remained in effect. During that five year period, very few employers dropped the coverage under the advisement of DLIR and the Hawaii Employers Council.[27]

The ERISA exemption has had both positive and negative effects on the PHCA. The positive effect is that it provided the State with the ability to provide health insurance to more people by way of the PHCA. The negative effects stem from the preemption clause which fixed the PHCA to its passage date in 1974. This inability to modify the PHCA to keep up with the times, national influences, and the needs of the community has been an issue for many stakeholders. While the ERISA exemption disallows any substantive amendment to the PHCA, changes to the prevalent plan benefits can and have been made by way of changes to the insurance laws by the Legislature.[28]

CONCLUSION

As the PHCA nears its 30th anniversary, it is important for key decision-makers to understand the context in which the Act was debated and passed. In 1974, when the PHCA was passed, lawmakers dealt with similar concerns as they do today. Debate about the cost of health care, impact on employers and employees, and the need to provide health care to Hawaii's residents are embodied in the legislative history of the Act. Nonetheless, lawmakers in 1974, realizing that the PHCA did not cover all employees e.g., part-time workers, self-employed, etc. passed the landmark legislation that provides a predominate base for health insurance coverage in Hawaii.

The PHCA, however, was met with significant legal challenges. In 1980, in *Standard Oil*, the U.S. Court of Appeals for the Ninth Circuit affirmed the lower court's decision that the PHCA was subject to ERISA's preemptive provision. The provision therefore invalidated the Act. To avoid the federal preemption, a special waiver was granted by Congress in 1982, which provides Hawaii with the only ERISA exemption in the nation. Any substantive amendment to the PHCA to the extent that it provides more than "effective administration" of the Act is subject to the preemptive clause, and therefore invalid. Due to the ERISA exemption, for all intents and purposes, the PHCA is frozen in time and does not account for market fluctuations, changes in the Hawaii economy, and costs of health care. Nonetheless, the PHCA continues to play a significant role in Hawaii's health care system, which will be the topic of future policy briefs from the Hawaii Uninsured Project.

For more information on The Hawaii Uninsured Project, visit our web site at
www.HealthCoverageHawaii.org.

To request a presentation, contact Carol Taniguchi at 808.585.7931.

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Acknowledgments

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U.S. Code, Annotated, Title 29, Section 1144(a)

U.S. Court of Appeals, Ninth Circuit, <u>Standard Oil Company of California v. Joshua C. Agsalud et al., No. 78-1095</u>, 1980.

Endnotes

1 The Hawaii Institute for Public Affairs is a private non-profit (501(c)3) organization dedicated to the development of sound, fact-based public policy and decision making.

2 Hawaii Revised Statutes; Prepaid Health Care Act, Chapter 393, State of Hawaii, 2003.

3 Ibid

4 Ibid

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