ERISA Preemption: Akzo v Thiokol

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The preemption issue considered in Akzo and Thiokol centers upon the provisions of the SBTA which add back “compensation” to the “tax base.” SBTA §9 defines “tax base” as “business income, before apportionment or allocation,” subject to a number of adjustments prescribed by §9.1 One of the §9 add back adjustments is compensation as defined in SBTA §4.2 In turn, §4(3)3 of the SBTA defines “compensation” in this fashion:

All wages, salaries, fees, … payments to a pension, retirement, or profit sharing plan and payments for insurance for which employees are the beneficiaries, including payments under health and welfare and non-insured benefit plans.

Thus, in order to properly compute Single Business Tax (“SBT”) base, and hence, SBT liability, contributions to ERISA plans must be considered. This addback provision of the SBTA must then be read in conjunction with the broad preemptive language of ERISA. Section 514(a) of ERISA preempts “any and all state laws insofar as they may now or hereafter relate to any employee benefit plan.”4 State tax laws are specifically embraced by the ERISA preemption provision under §514(b)(5)(B) which provides that “[n]othing in subparagraph (A) shall be construed to exempt from subsection (a) of this section—(i) any state tax law relating to employee benefit plans.”5 The question that has been presented to and addressed by the District Courts in Akzo and Thiokol is whether the broad preemption clause of ERISA supersedes the SBTA to the extent it “relates to” employee benefit plans. The decisions in both Akzo and Thiokol have been appealed to the Sixth Circuit Court of Appeals.

THE ANALYTICAL FRAMEWORK

The focus of the preemption analysis engaged in by both Akzo and Thiokol is on the term “relate to” as used in ERISA §514(a).6 If a state law such as the SBTA “relates to” an employee benefit plan, it is preempted. In what has become a black letter explanation of the meaning of “relate to,” the United States Supreme Court in Shaw v Delta Airlines, Inc, 463 US 85; 77 L Ed 2d 490; 103 S Ct 2890 (1983) (hereinafter referred to as “Shaw”) said a law “relates to” an employee benefit plan, in the normal sense, if it has a “connection with” or a “reference to” such a plan.7 In Shaw, however, the Court made clear that not all state laws that have a “connection with” an ERISA plan are preempted. Some state laws are said to affect ERISA plans in too “tenuous, remote or peripheral” a manner to warrant a finding that they relate to a plan.8

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One issue which the state in Akzo and Thiokol argued was left open by the United States Supreme Court in Shaw was whether the “tenuous, remote or peripheral” exception to the “relate to” test applied both to state laws which had a “connection with” an ERISA plan and to state laws which specifically “referred to” an ERISA plan. If each prong is subject to the tenuous, remote or peripheral standard, all state laws must be analyzed under a three part test: (i) Does the law have a connection with an ERISA plan? (ii) Does the law “relate to” an employee benefit plan? (iii) Does the law have a tenuous, remote, or peripheral connection to the ERISA plan? The decision in Akzo indicates that only the second prong is subject to the tenuous, remote or peripheral standard. If a law meets the requirements for both the “connection with” and “relate to” tests, it is preempted.
If the state law has a “connection with” an ERISA plan but does not specifically refer to the plan, the law must then be analyzed to determine if it has a connection with the plan in something more than a tenuous, remote or peripheral manner.

Several United States Supreme Court cases have applied the “tenous, remote or peripheral” exception only to “connection with” cases. In 1988, the United States Supreme Court in Mackey v Lanier Collections Agency & Service, Inc, 486 US 825; 100 L Ed 2d 836; 108 S Ct 2182 (1988), addressed ERISA preemption in the context of a statute containing a specific reference to an ERISA covered plan. There, the Court found preemption with respect to a Georgia law that specifically referred to ERISA plans in exempting them from a generally applicable garnishment procedure. The Court observed that “[o]n several occasions since our decision in Shaw, we have reaffirmed this rule, concluding that state laws which make ‘reference to’ ERISA plans are laws that ‘relate to’ those plans within the meaning of §514(a).” The Court concluded that “[t]he state statute’s express reference to ERISA plans suffices to bring it within the federal law’s preemptive reach.”

Thereafter, in FMC Corp v Holliday, 498 US 52; 112 L Ed 2d 356; 111 S Ct 403 (1990), the Court dealt separately with both
the “reference to” and “connection with” branches of the analysis for finding that the state statute “relates to” a covered benefit plan. In that case, despite the fact that the Court found that the “insurance savings clause” of ERISA excepted the Pennsylvania statute from operation of the preemption provision, the Court observed:

We made clear in Shaw v Delta Airlines, supra, that a law relates to an employee welfare benefit plan if it has a “connection with or reference to such a plan.” [citation omitted] We based our reading in part on the plain language of the statute. Congress used the words “relate to” in §514(a) in their broad sense.” [citation omitted] It did not mean to preempt only state laws specifically designed to affect employee benefit plans. That interpretation would have made it unnecessary for Congress to enact §514(b)(4) which exempts from preemption “generally applicable criminal laws of a state.... We also emphasize that to interpret the preemption clause to apply only to state laws dealing with the subject matters covered by ERISA, such as reporting, disclosure and fiduciary duties, would be incompatible with the provision’s legislative history because the House and Senate versions of the bill that became ERISA contained limited preemption clauses, applicable only to state laws relating to specific subjects covered by ERISA. These were rejected in favor of the present language of the Act, “indicating that the section’s preemptive scope was as broad as its language.”

Then, in District of Columbia v Greater Washington Board of Trade, ___ US __: 113 S Ct 580; 121 L Ed 2d 513 (1992) (hereinafter referred to as “Greater Washington”), the United States Supreme Court put this issue to rest. There, the Court acknowledged that the tenuous, remote or peripheral standard is inapplicable where the state statute under review contains a reference to employee benefit plans regulated by ERISA. In Greater Washington, the Court considered a District of Columbia enactment that required an employer providing health insurance coverage for its employees to provide equivalent coverage for employees receiving or eligible to receive workers’ compensation benefits. In testing whether the provision related to a covered employee benefit plan for purposes of ERISA §514(a), the Court said that the state law in question there “specifically refers to ERISA welfare benefit plans regulated by ERISA and on that basis alone is preempted.”

In analyzing the New York health insurance surcharge laws, the Supreme Court observed that nothing in the language of ERISA or the context of its passage indicates that Congress chose to displace general health care regulation which historically has been a matter of local concern.

Subsequent to the decision in Greater Washington (and, of course, subsequent to the decisions in Akzo and Thiokol), the United States Supreme Court had the opportunity to consider yet another ERISA preemption case. On April 26, 1993, the Court handed down its decision in New York State Conference of Blue Cross and Blue Shield Plans, et al. v Travelers Insurance Company, et al., Docket No. 93-1408 (hereinafter referred to as “New York Blue Cross”). In that case, the United States Supreme Court sought to determine whether surcharges imposed upon patients and HMO’s were preempted by ERISA.

The Court initially made reference to the Shaw test which explains that a law relates to an employee benefit plan if it has a “connection with or reference to such a plan.” The Court ruled out the latter alternative because the surcharge statutes could not, in the Court’s view, be said to make “reference to” ERISA plans in any manner. This still left the question whether the surcharge laws had a “connection with” the ERISA plans.

In analyzing the New York health insurance surcharge laws, the Supreme Court observed that nothing in the language of ERISA or the context of its passage indicates that Congress chose to displace general health care regulation which historically has been a matter of local concern. By contrast, the preemption clause of ERISA specifically includes within its preemptive sweep any state tax law relating to employee benefit plans. The critical feature of the New York surcharge was that it did not bind plan administrators to any particular choice for health insurance. The Court observed that a New York ERISA plan may choose among commercial insurers, HMO’s and Blue Cross plans to acquire health insurance. The existence of this choice saved the New York insurance charges from preemption because their indirect economic influence did not bind plan administrators to any particular choice.

Of particular significance in the New York Blue Cross case is the reaffirmation of the Greater Washington “one step” analysis of “reference to” preemption cases. If, as suggested by some, the United States Supreme Court only inadvertently stated that a state statute which “refers to” an ERISA plan is preempted on that basis alone, the United States Supreme Court had the perfect opportunity to correct that position in New York Blue Cross. The Court’s application of the alternative tests set forth in Shaw suggests that the Supreme Court has and will adhere to its position in Greater Washington.

APPLICATION OF PREEMPTION ANALYSIS TO SBTA

As will become evident, the decisions of Judge Hillman and Judge Bell in Thiokol and Akzo, respectively, were based in large part upon their respective interpretations of the decision of the United States Supreme Court in Greater Washington. Although the taxpayers in both Akzo and Thiokol still vehemently argue that the SBTA “relates to” ERISA in more than a tenuous, remote or peripheral manner (thus satisfying the “connection with” or “peripheral” prong of the Shaw test), resolution of this issue by the Sixth Circuit Court of Appeals may hinge upon the Court’s view of the United States Supreme Court decision in Greater Washington.

In Thiokol, Judge Hillman initially approached the preemption issue by reference to the familiar Shaw “relate to” standard. The Thiokol Court recognized that “relate to” as used in §514(a) should be given a broad common sense meaning. While ERISA preemption is expansive, the Court stated that it is not all encompassing.

The Shaw Court found that, “some state actions may affect employee benefit plans in too tenuous, remote or peripheral a manner to warrant a finding that the law ‘relates to’ the plan... The task then is to determine the precise relationship between a state law and an ERISA plan, specifically answering the questions whether the state law affects an
ERISA plan in too tenuous, remote or peripheral a manner to "relate to" the plan.14

In reaching his conclusion, Judge Hillman relied upon the decision of the United States Third Circuit Court of Appeals in United Wire v Morristown Memorial Hospital, 995 F2d 1179 (3d Cir 1993), cert den ___ US ____; 126 L Ed 2d 332; 114 S Ct 382 (1993) (hereinafter referred to as "United Wire"). In that case, the Court determined that a law which "relates to" an ERISA plan will only be preempted if the law is specifically designed to affect ERISA plans, if it singles out such plans for special treatment, or if it is predicated on the existence of such plans. Each factor identified in United Wire, the Thiokol Court observed, relates to whether the law is neutral and general. The Court in United Wire determined that, because the statute in question was a law of general applicability which functioned without regard to the existence of ERISA plans (that is, it was both neutral and general), the statute did not "relate to" ERISA.15

The Thiokol Court recognized, however, that other courts have found that state laws can "relate to" ERISA, and thus be preempted, even if they are neutral laws of general application.16 So, the Thiokol Court's determination that the SBTA is a neutral tax law of general application did not end the analysis. Even laws of neutral and general application are preempted by ERISA if they affect an ERISA plan in more than a tenuous, remote or peripheral manner.17

The Court then turned to Firestone Tire & Rubber Co v Neuser; 810 F 2d 550 (CA 6 1987) (hereinafter referred to as "Firestone"), in which the Court identified three factors to be examined in ascertaining whether a law's affect on an ERISA plan is "too tenuous, remote or peripheral." Whether the state law reflects a traditional exercise of state authority; whether the state law affects relations among the ERISA entities, i.e., the employer, the plan, the plan fiduciaries, and plan beneficiaries; and whether the effect of the state law on the ERISA plan is incidental. In applying the Firestone factors, the Court first noted that the Michigan SBTA involves an area of traditional state regulation. However, the Court recognized that this factor was not particularly useful as it did not have any relationship to, or impact upon, whether the law affected an ERISA plan.18

Judge Hillman also found that the SBT affects employers in their capacity as employers without regard to their status as plan sponsors, and does not affect the relations among the employer, the plan, the administrator, fiduciaries or beneficiaries. Judge Hillman's decision on this point contains a specific finding that the SBT is levied against all employers regardless of whether or not they contribute to an ERISA plan. He also concluded that the SBT has only an incidental affect on ERISA plans. Although, acknowledging that the SBT may affect total ERISA contributions by employers, the effect, in Judge Hillman's view, is tenuous, remote and peripheral. This is due to the fact that it fails to affect the relationship among any ERISA entities, while the affect on total contributions to ERISA plans is incidental because it simply fails to allow for a deduction for plan contributions. The Court specified that "the SBT is not preempted by ERISA merely because it imposes a cost on business."19

The second basis for Judge Hillman's decision is his conclusion that the opinion of the United States Supreme Court in Greater Washington did not hold that a state statute which makes a specific reference to welfare benefit plans regulated by ERISA is, on that basis alone, preempted. In Judge Hillman's view, "a mere reference to ERISA within the state tax law does not, in and of itself, mandate preemption."20 The Court explained:

While a mere reference to ERISA establishes that a law "relates to" ERISA, the law is preempted by ERISA only if it "relates to" ERISA in something more than a "tenuous, remote or peripheral manner"... Since that pronouncement, the Court has consistently reiterated this standard... The Court's standard necessarily establishes a two part test for laws which refer to ERISA. A law "relates to" ERISA if it has a "reference to" an ERISA plan, but is preempted only if it "relates to" ERISA in something more than a "tenuous, remote or peripheral" manner.21

In finding as it did, the Court refused to read the United States Supreme Court's pronouncement in Greater Washington as standing for the proposition that a state statute may be preempted by ERISA if it "refers to" an ERISA plan, despite the fact that, in Greater Washington, Justice Thomas stated that a state law which "specifically refers to welfare benefit plans regulated by ERISA" is "on that basis alone" preempted. While recognizing that the Court in Greater Washington appeared to adopt a "one part bright line rule," Judge Hillman found that, even after Greater Washington, the "tenuous, remote or peripheral" standard set forth in Shaw controlled the disposition of the case. The Court stated:

While a single sentence of the majority's opinion in Greater Washington appears to overturn the ten year old Shaw test, all other evidence, and common sense reasoning, establishes that the Court did not overturn the Shaw standard.22

Judge Hillman cited four specific reasons for this conclusion. First, he read Greater Washington as directly overturning the Shaw test, without so much as an acknowledgement of doing so. Because the Court did not articulate reasons for what Judge Hillman perceived was an overturning of Shaw, and the ambiguous nature of its explanation and "mere reference to" language, Judge Hillman felt compelled to follow the "well established precedent set forth in Shaw."23 Second, after Greater Washington, no court had found a state statute to be preempted by ERISA merely because it made reference to it. Third, the "bright line, mere-reference-to-test" apparently adopted in Greater Washington forced an "unrealistic and illogical game of semantics upon state legislatures, demanding only that they do not use the forbidden words."24 Finally, the

Until resolution of the pending Sixth Circuit Court of Appeals cases in Akzo and Thiokol, ERISA-based claims filed in the Michigan Court of Claims will be held in abeyance.

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use of this bright line rule might cause the preemption of hundreds of existing state laws, if challenged.

Unlike Judge Hillman, Judge Bell in Akzo, while agreeing with the bulk of Judge Hillman’s analysis with regard to the nature of the SBT and its connection with ERISA plans, disagreed with Judge Hillman’s analysis of the impact of Greater Washington. In essence, Judge Bell viewed the Shaw “relate to” preemption standard as creating two distinct tests to determine ERISA preemption, only one of which employed the tenuous, remote or peripheral standard.

The analysis by the Court in Akzo began, like Thiokol, with the familiar Shaw test that a state law “relates to” an employee benefit plan if it has a connection with or reference to such a plan. Accordingly, the Court found that the question of whether a state law relates to an ERISA plan is answered in the affirmative in two distinct situations: Where the state law has a “connection with” an ERISA plan, or where the state law “refers to” an ERISA plan.

Like Judge Hillman in Thiokol, Judge Bell focused on the standard established by the Supreme Court for state laws which affect employee benefit plans in too “tenuous, remote or peripheral” a manner. The state argued that Shaw establishes that the tenuous, remote or peripheral exception applies to any state law which relates to an ERISA plan regardless of whether it relates to the plan as a result of its connection with the plan or its reference to the plan.

The Court in Akzo disagreed, finding that the United States Supreme Court rejected this very argument in Greater Washington. Unlike the Court in Thiokol, the Akzo Court had no trouble finding that a state law which refers to an ERISA plan can be preempted “on that basis alone.” The Court found that the United States Supreme Court in Greater Washington made it clear that the tenuous, remote or peripheral exception applies to “connection with” situations when it: Failed to consider the exception with regard to a “reference to” situation; and said that “preemption does not occur, however, if the state law only has ‘tenuous, remote or peripheral connection with covered plans’” (emphasis added).

Given its interpretation of Greater Washington, the Court concluded that, since §4(3) of the SBTA refers to plans regulated by ERISA, it is, on that basis alone, preempted. Judge Bell’s decision has set the stage for resolution of the issue by the Sixth Circuit Court of Appeals.

CONCLUSION

While Judge Hillman and Judge Bell substantially agreed upon how the 89 compensation addback provisions of the SBTA relate to ERISA, they fundamentally disagreed upon the proper analysis. Resolution of the ERISA preemption issue may very well turn upon which Court has properly interpreted the United States Supreme Court’s holding in Greater Washington. Nonetheless, the Sixth Circuit Court of Appeals will also be presented with the taxpayer’s additional argument that the compensation addback provisions of the SBTA relate to an ERISA plan in more than a tenuous, remote or peripheral manner. So, the Sixth Circuit will also have an opportunity to take a fresh look at the scope and application of the tenuous, remote and peripheral exception as it applies to the SBTA.

Michigan taxpayers should consider excluding from SBT base contributions made to pension and profit sharing plans, health and life insurance premiums and fees paid for administration of plans, subject to ERISA, on the authority of Akzo. Until resolution of the pending Sixth Circuit Court of Appeals cases in Akzo and Thiokol, ERISA-based claims filed in the Michigan Court of Claims will be held in abeyance.

Footnotes
1. MCL 208.9; MSA 7558.9.
2. MCL 208.9(3); MSA 7558.9(3).
3. MCL 208.4(3); MSA 7558.4(3).
4. 29 USC §1144(a).
5. 29 USC §1144(b)(1)(B)(i).
6. 29 USC §1144(a).
7. 77 L Ed 2d at 501.
8. 77 L Ed 2d at 503, fn 21.
9. 100 L Ed 2d at 843.
10. 100 L Ed 2d at 844.
11. 112 L Ed 2d at 354-365.
12. 121 L Ed 2d at 520.
13. In Greater Washington, Justice Stevens authored a separate dissenting opinion which suggests that the majority did not reaffirm its one step analysis of reference to preemption cases by mere inadvertence.
14. 858 F Supp at 676.
15. 858 F Supp at 679.
16. 858 F Supp at 679.
17. 858 F Supp at 680.
18. 858 F Supp at 680.
19. 858 F Supp at 681.
20. 858 F Supp at 681.
21. 858 F Supp at 681-682.
22. 858 F Supp at 682.
23. 858 F Supp at 682.
24. 858 F Supp at 683.
25. ERISA preemption was raised by the taxpayer in Akzo not only as to the “substantive” issue, but also as to the validity of the 90-day statute of limitations period for bringing an action based on federal law or the Constitution. The Court in Akzo concluded that MCL 205.27a(6) does not make reference to an ERISA plan and is not, therefore, preempted on that basis. The Court then concluded that §27a(6) has, at most, only a tenuous, remote or peripheral connection with a covered plan and so, on that basis as well, it is not preempted by ERISA. The Court also found that MCL 205.27a(6) was not invalid on constitutional grounds. The Court found that a stable public fisc was the rational basis which supported the legislation.
26. To his opinion in Akzo, Judge Bell in fact expressed his agreement with all of Judge Hillman’s findings except his conclusion that a state law is not preempted by ERISA, merely because it “refers to” an ERISA plan.
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