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Employee Benefits

Procedure

After the U.S. Supreme Court's opinion in *Board of Trustees of the National Elevator Industry Health Benefit Plan* holding that ERISA prohibits suits by benefits plans where the beneficiary spent the settlement money on nontraceable items, attorneys from Paul Hastings LLP suggest that plans enhance their monitoring efforts, review the adequacy of their subrogation clauses and act promptly when seeking reimbursement from plan participants.

Equity Aids the Vigilant: The Supreme Court's *Montanile* Decision And Its Lessons for ERISA Plans' Efforts To Recover Medical Payments



By Igor V. Timofeyev, Eric R. Keller and Mark Poerio

The U.S. Supreme Court's recent decision in *Board of Trustees of the National Elevator Industry Health Benefit Plan*, 84 U.S.L.W. 4046, 2016 BL 14200 (U.S. Jan. 20, 2016), resolved a deep conflict among lower courts as to when an employee benefits plan may recover medical payments from a plan beneficiary who later receives a third-party settlement payment for his injuries.

The Court held that the Employee Retirement Income Security Act of 1974 (''ERISA'') prohibits a suit by the plan where the beneficiary has already spent all the settlement money on nontraceable items. Such a suit, the Court explained, is not an action seeking ''equitable relief''—the only type of suit by a plan fiduciary authorized under ERISA.

The Supreme Court portrayed its ruling, issued by an 8-1 majority, as merely applying prior precedents construing Section 502(a)(3) of ERISA, 29 U.S.C. § 1132(a)(3).

By rejecting the plan's efforts to analogize its suit to several types of relief historically awarded by equity courts, however, the high court has constrained plan fiduciaries' ability to pursue reimbursement claims against plan beneficiaries. At the same time, the Court stressed the limited nature of its ruling, emphasizing the various tools plan fiduciaries have at their disposal to enforce beneficiaries' reimbursement obligations.

In the wake of *Montanile*, ERISA plan fiduciaries may wish to strengthen both the subrogation clauses in

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their employment benefits agreements and the claims-related provisions of their plans. Plan fiduciaries should also examine the adequacy of their efforts to monitor third-party litigation involving paid medical benefits claims.

Background

Robert Montanile was a participant in an ERISA health benefits plan administered by the Board of Trustees of the National Elevator Industry Health Benefits Plan (''the Board''). The plan—similar to many other employee benefits plans governed by ERISA—provided for the payment of a participant's covered medical expenses, such as expenses incurred due to an injury. The plan also contained a subrogation clause (again, typical for ERISA-covered plans) requiring a participant to reimburse the plan if he later recovers money for his injury from a third party. In addition, participants were required to notify the plan and obtain its consent before settling such third-party claims.[1]

In December 2008, Montanile was severely injured in a traffic accident. The plan paid over $120,000 for his medical care.

Montanile signed an agreement reaffirming his obligation under the subrogation clause to reimburse the plan for any recovery he may obtain as a result of any legal action or settlement. Montanile then sued the driver of the vehicle that injured him and obtained a $500,000 settlement, of which he paid $260,000 to his attorneys. Montanile's attorneys held most of the remaining settlement sum in a client trust account.[2]

The Board sought reimbursement of the previously paid medical expenses, but Montanile's attorneys objected to the plan's right to recover that amount. After unsuccessful negotiations, Montanile's attorneys informed the Board that they would disburse the remaining settlement funds to Montanile unless the Board objected within 14 days. The Board did not respond within that time, and Montanile's attorney transferred to him the remaining funds.[3]

Six months later, the Board sued Montanile in federal district court under Section 502(a)(3), seeking reimbursement of the medical expenses paid by the plan.

Section 502(a)(3) authorizes a plan fiduciary to bring a civil action ''to obtain . . . appropriate equitable relief . . . to enforce any provisions of [ERISA] or the terms of the plan.''[4] The Board argued that it was entitled to equitable restitution in the form of a constructive trust or equitable lien with respect to any settlement funds or property in Montanile's actual or constructive possession. The Board also sought an order enjoining Montanile from dissipating any settlement funds.[5]

The district court granted summary judgment to the Board. The court held that, even if Montanile had dissipated some or all of the settlement funds, the Board was entitled to reimbursement from Montanile's general assets.[6] The court reasoned that the plan's terms created an equitable lien by agreement in any third-party recovery received by Montanile, and a subsequent dissipation of assets was immaterial to the plan's ability to enforce the lien.

The U.S. Court of Appeals for the Eleventh Circuit affirmed, opining that an ERISA plan can always enforce an equitable lien once the lien attaches, and that the beneficiary's subsequent dissipation of the funds could not destroy the lien. The court of appeals held that, in such circumstances, the plan can recover out of a participant's general assets.[7] Because this question divided federal circuit courts, the Supreme Court granted certiorari to resolve the conflict.[8]

Supreme Court's Decision

The Supreme Court reversed, in an 8-1 opinion.[9] Writing for the majority, Justice Thomas first examined the Court's precedents prescribing the framework for determining whether a plan fiduciary's lawsuit is of a type permitted under Section 502(a)(3). In accordance with these precedents, the Court explained, ''the term 'equitable relief' in § 502(a)(3) is limited to 'those categories of relief that were *typically* available in equity' '' before the merger of law and equity in federal court in 1938.[10] Whether the remedy is legal or equitable depends on '' '[(1)] the basis for [the plaintiff's] claim and [(2)] the nature of the underlying remedies sought.' ''[11]

The Court then examined closely three of its prior decisions concerning the ability of ERISA plans to recover medical expense payments from participants under the subrogation clauses—*Great-West Life & Annuity Insurance Co. v. Knudson*, 534 U.S. 204 (2002); *Sereboff v. Mid Atlantic Med. Servs., Inc.*, 547 U.S. 356 (2006); and *US Airways, Inc. v. McCutchen*, 81 U.S.L.W. 4236, 2013 BL 101433 (U.S. 2013). In all three cases, the plan fiduciary sought reimbursement for medical expenses after the plan participant recovered money from a third party. The Court concluded that, under these precedents, the Board had an equitable *basis* for its claim. By virtue of the plan's subrogation clause, an equitable lien by agreement attached to Montanile's litigation settlement fund when he obtained title to that fund.[12] The Court then noted that the nature of the Board's *remedy* would also have been equitable ''had it immediately sued to enforce the lien against the settlement fund.''[13]

The prior decisions, however, did not resolve whether a plan's lawsuit brought against a beneficiary that had already dissipated the settlement assets is still a suit seeking an equitable remedy within the meaning of Section 502(a)(3). To answer that question, the Court

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[1] *Board of Trustees of the National Elevator Industry Health Benefit Plan*, 2016 BL 14200, at *3 (Jan. 20, 2016).

[2] *Id.*

[3] *Id.*

[4] 29 U.S.C. § 1132(a)(3)(B)(ii).

[5] *Montanile*, at *4. Montanile stipulated that he still possessed some of the settlement proceeds.

[6] *Id.*

[7] *Id.*

[8] *Id.*

[9] Justice Thomas wrote the majority opinion, while Justice Ginsburg dissented. The remaining justices joined the majority opinion in its entirely, except for Justice Alito, who did not join the section of the opinion discussing whether the Court's ruling was consonant with ERISA's objectives, and whether the plan had adequate means to ensure recovery of the benefits paid to the beneficiary.

[10] *Montanile* at *4 (quoting *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 256 (1993)) (emphasis in original).

[11] *Id.* (quoting *Sereboff v. Mid Atlantic Med. Servs., Inc.*, 547 U.S. 356, 363 (2006)) (alterations in original).

[12] *Id.* at *4-*6.

[13] *Id.* at *6.

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turned to ''standard equity treatises,'' because they ''establish 'basic' contours' of what equitable relief was typically available in premerger equity courts.''[14]

Under traditional principles of equity, the Court explained, a plaintiff could ordinarily enforce an equitable lien only against specifically identified funds remaining in the defendant's possession or traceable items (such as a car) that the defendant purchased with these funds. If, however, the defendant dissipated the funds on nontraceable items (such as food or travel), that eliminated the lien. The plaintiff may then have a personal claim against the defendant's general assets, but such recovery is a *legal*—not equitable—remedy and therefore not authorized under Section 502(a)(3).[15]

The Court rejected the Board's efforts to analogize its lawsuit to relief previously awarded by equity courts under substitute money decrees, deficiency judgments, and the swollen assets doctrine. The first two were legal remedies that equity courts awarded as part of their ancillary jurisdiction, and the Court reasoned that ''equitable relief'' under Section 502(a)(3) does not extend to such remedies because they ''were not relief 'typically available in equity.' ''[16]

The Supreme Court then rejected the Board's reliance on the swollen assets doctrine, holding that the doctrine would not authorize recovery from a defendant's general assets where these assets were increased through a fund that wrongfully belonged to defendant.[17]

Finally, the Court rejected the argument that prohibiting employee benefits plans from pursuing a participant's general assets was contrary to ERISA's objective of protecting plan assets. In the Court's view, ERISA plans ''know how much medical care that participants and beneficiaries require, and have the incentive to investigate and track expensive claims''; moreover, the plans can require participants ''to notify the plan of legal process against third parties and to give the plan a right of subrogation.''[18]

The Court noted that in the instant case, the Board had sufficient notice of Montanile's settlement; had the opportunity to object to the notice that the remaining settlement funds would be distributed to Montanile; and had the option of suing immediately (before the dissipation of the funds), instead of waiting six months.[19]

Justice Ginsburg was the sole dissenter. She reiterated the view articulated over a decade ago in her dissent in *Great-West*—that the Court had erred in reading Section 502(a)(3)'s reference to ''equitable relief'' as adopting a strict legal/equitable distinction when determining what actions are permitted under that provision, and in looking towards the historical principles of equity in defining Section 502(a)(3)'s scope.[20]

Practical Implications

The Court's holding that employee benefits plans may not seek to recover their medical expense payments from a participant's general assets has considerable significance to ERISA plans and practitioners. Aside from resolving the question that has divided federal courts, the *Montanile* ruling demonstrates that the Supreme Court remains reluctant to expand the scope of Section 502(a)(3). The Court's opinion will require the plans to enhance their monitoring efforts, to review the adequacy of their subrogation clauses, and to act promptly when seeking reimbursement from plan participants. At the same time, the Court stressed the limited nature of its holding and emphasized that the ERISA-covered plans should have sufficient safeguards to ensure recovery of the paid-out medical benefits.

Interestingly, Justice Thomas wrote a unanimous 2013 Court decision finding that ERISA plans could require that participants assert claims for benefits within a period shorter than the statute of limitations period that would otherwise apply.[21] There is also room for plans to designate required forums for litigation, based on a Sixth Circuit decision for which the Supreme Court denied review earlier this month.[22]

The extent to which employee benefits plans are able to use these preventive measures to limit the impact of the Court's opinion is likely to be fleshed out in subsequent litigation.

The immediate importance of *Montanile* is that it has decisively settled the question that has divided federal courts of appeals—namely, whether an employee benefits plan can seek reimbursement of settlement funds from a participant's general assets.[23]

The Supreme Court made clear that, even if a plan had an initial lien by agreement by virtue of a subrogation clause, the plan may not pursue such recovery under Section 502(a)(3) if the specific settlement funds have been entirely dissipated.

As Justice Ginsburg cautioned, the Court's ruling may create a perverse incentive for ERISA beneficiaries to ''spend[] the settlement funds rapidly on nontrace-

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[14] *Id.* at *4 (quoting *Great-West*, 534 U.S. at 217).

[15] *Id.* at *6-*7. The Court rejected the argument that equitable liens by agreement were exempted from the equity's general traceability requirement and could be enforced against a defendant's general assets. As the Court explained, although a lien by agreement does not require a physical taking of the plaintiff's property (because it concerns the defendant's constructive possession of a fund to which the plaintiff is entitled), the plaintiff nevertheless must identify a specific fund in the defendants' possession to enforce the lien. (discussing *Sereboff*, 547 U.S. at 365, and *Barnes v. Alexander*, 232 U.S. 117, 123 (1914)).

[16] *Id.* at *8 (quoting *Mertens*, 508 U.S. at 256).

[17] *Id.* The Court, however, left open the possibility that Section 502(a)(3) may permit a suit based on a more narrow version of the swollen assets theory—that comingling a specifically identified fund (with an attached lien) with a different fund does not destroy the lien (citing authorities).

[18] *Id.* at *10. The Court also noted that, in any event, arguments based on ERISA's purpose could not overcome what the majority considered to be the plain textual meaning of Section 502(a)(3). *Id.* at 13. Justice Alito did not joint this portion of the Court's opinion.

[19] *Id.* Because the record did not demonstrate to what extent the settlement funds was comingled with Montanile's general asserts and whether the funds were entirely dissipated, the Court remanded the case so the lower courts could make that determination. *Id.*

[20] *Id.* (Ginsburg, J., dissenting).

[21] *Heimeshoff v. Hartford Life & Acc. Ins. Co.*, 82 U.S.L.W. 4035, 2013 BL 345916 (U.S. 2013) (generally approving plan-based limitations periods unless ''unreasonably short'').

[22] *Smith v. Aegon Cos. Pension Plan*, 769 F.3d 922 (6th Cir. 2014), *cert. denied*, 84 U.S.L.W. 3382 (U.S. Jan. 11, 2016).

[23] *See Montanile* at *10 n.2 (citing conflicting decisions by the First, Second, Third, Sixth, Seventh, Eighth, and Ninth Circuits).

able items.''[24] The ERISA plan fiduciaries, therefore, would want to prevent being placed in a situation where they may be left with no remedy under ERISA against a beneficiary who breaches the equitable lien created by virtue of the subrogation clause. These considerations apply equally in a plan's enforcement of equitable liens for the overpayment of plan benefits.

To protect the plan from these risks, plan sponsors and fiduciaries should ensure that both the plan document and the plan's summary plan description create an equitable lien by agreement and require participants to promptly notify the plan about any recoveries sought against a third party, to provide periodic updates, and to seek the plan's consent both to the settlement and to the distribution of the settlement proceeds to the participant.

Upon receiving such notification or otherwise becoming aware of a possible third-party recovery, the plan should promptly assert and pursue claims to recover overpayments or obtain reimbursement, including providing written notice to the attorney holding the settlement funds, filing suit, or obtaining other security for the plan.

The plan should also be prepared to pursue ''tracing'' of assets spent or comingled by participants.

Lawsuits to obtain recovery could include a request for a preemptive injunction or a temporary restraining order, requiring that the disputed portion of the amount recovered from a third party be set aside pending the resolution of the reimbursement claim.[25]

If the plan terms and the state subrogation law allow, these measures could also include suing the responsible third party directly as the beneficiary's subrogee, or intervening in the participant's lawsuit to protect the plan's recovery rights.[26]

As a general matter, *Montanile* demonstrates that the Court is reluctant to read Section 502(a)(3)'s reference to ''equitable relief'' broadly.

The Court reiterated its prior holdings in *Mertens* and *Great-West* that this term is limited to remedies '' '*typically* available' '' from equity courts in the pre-1938 era, defined by reference to ''standard treatises on equity.''[27] Notably, both of these precedents were decided by a closely divided Court and elicited vigorous dissents that urged a broader construction of Section 502(a)(3).[28] This time, however, the Court's ruling was issued by a lopsided 8-1 majority. Even Justice Breyer, who joined Justice Ginsburg's dissent in *Great-West*, has signed on to the majority opinion without separate comments or reservations.

The *Montanile* Court extended its precedents of *Mertens* and *Great-West* by rejecting the argument that remedies that equity courts were authorized under their ancillary jurisdiction (such as substitute money decrees or deficiency judgments) could qualify as ''equitable relief'' under Section 502(a)(3).[29]

The opinion signals that in a future case involving this provision of ERISA, the Court is likely to adopt a similarly narrow approach when construing the scope of the term ''equitable relief.''

While the extent (and the limits) of *Montanile* will be fleshed out in subsequent lower courts decisions, ERISA plan fiduciaries should be aware of the Supreme Court's underlying message: If you want to protect your recovery rights, build in adequate safeguards into your plans and act promptly; do not count on federal courts to allow leeway with respect to either ERISA's statutory remedies or weakly drafted claim provisions within plans.

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[24] *Id.* (Ginsburg, J., dissenting).

[25] Indeed, the U.S. Solicitor General and the U.S. Department of Labor suggested such measures in an *amicus* brief to the Court. *See* Br. for the United States as *Amicus Curiae*, at 30-31, *Board of Trustees of the National Elevator Industry Health Benefit Plan*, No. 14-723, (July 13, 2015) (citing cases).

[26] *See id.* at 30 (citing cases).

[27] *Montanile* at *4 (quoting *Mertens*, 508 U.S. at 256, and citing *Great-West*, 534 U.S. at 217).

[28] *See Mertens*, 508 U.S. at 263-73 (White, J., dissenting); *Great-West*, 534 U.S. at 224-34 (Ginsburg, J., dissenting).

[29] *Montanile* at *8.

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