ERISA and the Supremes (and other less Vocal Groups)

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Overview

- SCOTUS: drafting considerations—the power of contracts!
- Courts of Appeal: angry judges and keeping attorney-client communications safe.
- Other eyeball grabbers—major exposure.

SCOTUS--Key Drafting Cases

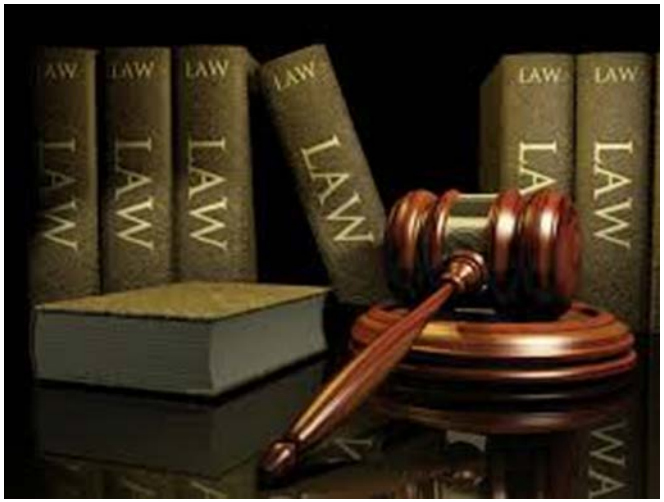
- *Heimeshoff v. Hartford Life & Accident Insurance*
  - Decided December 16, 2013
- *U.S. Airways v. McCutchen*
  - Decided April 16, 2013
- *CIGNA Corp. v. Amara*
  - Decided May 16, 2011
- *United States v. Windsor*
  - Decided June 26, 2013

Heimeshoff v. Hartford Life & Accident Insurance

- Unanimous Court
- Can a Plan set both the Limitation Period for filing a claim and also establish when the Limitation Period will begin to run?
- **Yes**, *if*: (1) the Plan allows for a reasonable period of time to seek judicial review and (2) the period does not conflict with statutory authority.

Heimeshoff - Background Info

- ERISA does not have a limitation period for Denial of Benefits.
- Limitation period is analogous to state law statute of limitation period.
- Analogous state law limitations periods
  - Contract law—6 years in Washington
  - Insurance law—1 year in Washington



Heimeshoff - Background Info (con't)

- Cause of action does not accrue (i.e. lawsuit not allowed) until Plan issues final denial.
- Usually, accrual starts the limitations period.
  - Discovery Rule – when plaintiff discovers or should have discovered the claim or injury.
  - Repudiation Rule – where there has been a clear repudiation of a claim or injury.
- What if a contract between the parties says that the limitations period starts before accrual?

Heimeshoff - Background Info (con't)

- Courts have held shorter limitation periods may be imposed by contract.
  - This depends on applicable statutes.
- Shorter limitation periods are often upheld unless "manifestly unreasonable."

Heimeshoff - Facts

- Plaintiff worked for Wal-Mart for 20 years.
- In 2005, filed Disability Claim for injuries caused by Fibromyalgia; Hartford (LTD administrator) denied claim but indicated claim would be reopened if further evidence submitted.
  - Hartford waived the 180 day appeal deadline, granted extensions.
- Claim was reopened in 2006-2007 and Plaintiff was given until September 30, 2007 to submit additional evidence – "Proof of loss" date established by Plan.

Heimeshoff - Facts (con't)

- A final denial was issued on November 26, 2007.
- November 18, 2010 Plaintiff filed suit in federal court.
- Suit filed within 6 years of the claim; suit filed within 3 years of the denial.
- Plan required proof of loss by September 30, 2007 and required suit to be filed within 3 years of proof of loss.
  - "Legal action cannot be taken against The Hartford . . . [more than] 3 years after the time written proof of loss is required to be furnished according to the terms of the policy."

Heimeshoff - Decision

- District Court dismissed;
- Second Circuit affirmed;
- Supreme Court granted review.

Heimeshoff - Review

- Whether a contractual period can begin to run prior to the exhaustion of administrative remedies.
  - Yes
  - No tolling of statute of limitations during the administrative review process.
- Recent Supreme Court decisions enforce Plan terms unless unreasonable or prohibited.
- Limitation period will be upheld unless:
  - (1) unreasonably short; or
  - (2) conflicts with other statutory authority.

Heimeshoff – What Does This Mean for Me?

- Pensions – Courts have been reluctant to start limitation periods prior to retirement and forty years later Employers may not have records to contest employee allegations.
- Start Limitation Period Early by Creative Plan Drafting.
  - Service, Compensation, Eligibility disputes run three years from date that employee receives a statement showing service, compensation, or entry date or if not enrolled, the date that should have been enrolled.
- Medical/Disability – three years (perhaps even two years) from the date that claim arose.
  - SCOTUS *may have* suggested that two years is okay—may depend on average administrative review process time.

Heimeshoff – Quick Word of Warning

- Failure to meet internal review deadlines grants Participant *immediate* access to judicial review.
- And, *equity to the rescue*!
  - Waiver or estoppel
    - Aimed at bad behavior
  - Equitable tolling
    - Internal and judicial review diligently pursued
    - Extraordinary circumstances (undefined)

U.S. Airways v. McCutchen

- Half-unanimous.
- Subrogation: permits ERISA medical plans to recover medical expenses from third party recoveries.
- However, the extent that medical plan can recover depends on Plan language.
- Examine Plan language to ensure compliance with *McCutchen*.

McCutchen - Facts

- Employee participated in the U.S. Airways Medical Plan (self-insured).
- McCutchen was involved in a serious auto accident. The Plan paid $66,866 in medical expenses.
- His damages, including loss of earnings were estimated to be in excess of 1 Million Dollars. McCutchen is disabled.

McCutchen – Facts (con't)

- McCutchen settled with the negligent driver for $10,000 and his own insurer for $100,000, i.e. total $110,000.
  - Limited insurance coverage, multiple serious injuries and fatalities.
- He paid his attorneys $44,000 and he kept $66,000.
- Plan demanded payment of $66,866.
- McCutchen argued that his equitable defenses should override the Plan language. McCutchen argued that it was not equitable to require him to pay the Plan, when he had not been made whole for his injuries.

McCutchen - Background

- Under state law, Plan can only be reimbursed if injured party was "made whole" for his injuries. This is still the law for insurance plans, but not for self-insured plans due to ERISA preemption.
- Because McCutchen was not "made whole" by the payment of $66,000, Plan could not be reimbursed, if "make whole" doctrine was applicable.

McCutchen - Decision

- Everyone agrees:
  - U.S. Airways Plan stated recovery would be on a "First Dollar Basis regardless of whether injured party was made whole."
  - Supreme Court held that Plan language controlled and state law preempted.
- So US Airways recovers its $66K, right?
  - Not so fast….

McCutchen - Decision

- 5-4 decision.
- Equity does not trump contractual language…
  - … but it can fill a "contractual gap."
- Subrogation language was silent on attorney fees – so filled the contractual gap by holding Plan had to pay a portion of the settlement to the attorneys.
  - "Common-fund doctrine" bridges the gap

McCutchen – Drafting Implications for Employer

- Draft broad "First Dollar Recovery" subrogation language.
- Avoid "Contractual Gaps" by dealing with attorney fees and expenses. Plan can refuse to pay any attorney fees.
  - Example: plan may recover its litigation expenses, pay 25% (including fees on appeal) to attorneys after expenses recouped, and then entitled to first dollar recovery.
- Make sure there is a reference to subrogation in the Plan (not just the SPD).

McCutchen – Quick Litigation Tip

- If the other side's theory of what the Plan requires is based solely on the SPD, not the Plan itself, *point that out!*
- SCOTUS analyzed the SPD as if it was the Plan itself because the parties relied on it as such at trial and before the Court of Appeals.

CIGNA Corp. v. Amara

- Half-unanimous (again).
- Holds that terms of the Plan are enforceable and that terms of a Summary Plan Description are not terms of the Plan.
- Plan Sponsors should ensure that terms that they wish to enforce are in the "Plan document."
- If the SPD is the only operational document, make sure that the SPD states that it is both the Plan and the Summary.

Amara - Facts

- CIGNA notifies employees of changes (TBD) to its Pension Plan in 1997.
- CIGNA makes changes (retroactive) in 1998:
  - Ending defined benefit plan.
  - Individual retirement accounts, with an initial balance equal to value of employee's already earned benefits.
- Represented to employees that:
  - this plan was more advantageous to them
  - "one advantage the company will not get … is cost savings."
- Also may have "focused on NOT providing employees before and after samples of the Pension Plan changes."
  - Not something you want in an internal memo produced in discovery.

Amara - Decision

- SCOTUS—liar liar.
  - New plan saved CIGNA $10 million annually (never mind that these funds were spent on other employee benefits)
  - *Possibly* less advantageous to employees in multiple ways
    - Early retirement
    - Survival probability discount in initial deposit
    - Shifted risk of change in interest rates
  - Intentional misleading of employees.
- What about the remedy?

Amara - Remedy

- Equitable Remedy
  - Step One: Court orders Plan reformed to capture prior benefits.
  - Step Two: Court orders Plan enforced as reformed.
- Basis
  - Not allowed under 502(a)(1)(B)—does not permit altering contract terms.
    - Everyone agrees with this point
    - Expressly rejects Solicitor General's argument that the SPD terms are Plan terms.

Amara - Remedy

- Basis (cont.)
  - Allowed under 502(a)(3)
    - A civil action may be brought (3) by a participant, beneficiary, or fiduciary (B) to obtain other appropriate equitable relief.
  - *Not* everyone agrees with this point.
    - 2 Justices concurr in result, calling the Court's 502(a)(3) analysis dicta.
    - Majority's opinion may suggest 502(a)(3) language is dicta
    - …but good luck making that argument.

Amara - Implications

- Plaintiffs are looking for "Plan Documents" as the only enforceable terms – A "Wrap" document wrapping all your Plan provisions and incorporating subrogation clauses is one method of dealing with this issue.
- If your SPD is your Plan document make sure this dual purpose is stated in the document, so that you can produce it as "the Plan."
- *Amara*, clearly established that equitable remedies are enforceable and it has opened the doors of litigation in this area.

United States v. Windsor

- Not unanimous. Not even close.
- Defense of Marriage Act (DOMA) definition of "marriage" as between a man and a woman is unconstitutional.
- Changed the definition of Spouse for federal tax purposes and ERISA. Plan documents and SPDs must be reviewed for compliance.

United States v. Windsor

- As of September 16, 2013 (IRS Notice Date) Spouse should be defined broadly:
  - A person (including person of the same sex) who is lawfully married, including a common law marriage, to a Participant under the laws of any domestic or foreign jurisdiction having the legal authority to sanction such marriage.
- Plans are reexamining their policy with respect to the recognition of domestic partners.
- IRS will likely issue notice on the retroactive implications of *Windsor* within the next few months. IRS is not planning on additional guidance after this next planned notice.

Windsor - Facts

- Edith Windsor and Thea Spyer were married in a same-sex ceremony in Ontario, Canada.
- They were residents of New York.
- New York recognized their Ontario marriage as valid.
  - so, basically, the death of DOMA is brought to you by:

Windsor – Facts (cont.)

- Ms. Spyer died in 2009 leaving her entire estate to Windsor.
- If Windsor was a Spouse under federal law, the property would not be taxed due to the marital deduction.
- Because Section 3 of DOMA defined marriage as a union between a man and woman, Windsor was not a Spouse for federal tax purposes and paid $363,053 in estate taxes, for which she filed a refund.

Windsor - Decision

- Recognized as a Protected Class those Same-Sex marriages made lawful by a state.
- Discrimination against same-sex marriages violates due process, equal protection, and federalism.
- Section 2 of DOMA – states do not have to recognize same sex marriage performed in other states – was not before the Court.
- Section 2 is being attacked on equal protection, the right of interstate travel, and the privileges and immunities clause. As Scalia dissent notes, the Supreme Court majority would likely strike down this section.

Windsor - Decision

- Long legal battle ahead; only 14 states and Washington, D.C. permit same-sex marriages.
- Some states, such as North Carolina, have Constitutional amendments that are difficult to change:
  - Marriage between a man and an woman is the only legal union that shall be valid or "recognized" by this state.
- Keep out of the legal fray by defining Spouse broadly for all your benefit programs.
- If define Spouse narrowly, expect litigation.
- Be on look out for additional guidance on the retroactive application.

Rochow v. Life Ins. Co. of America – 6th Circuit
December 6, 2013

- 6th Circuit Post-*Amara* Decision gives Plan Sponsors a reason to check their fiduciary policy limits.
- Awarded back disability benefits, plus $2.8 Million as disgorged profits for failing to pay claim earlier, i.e., total award of $3.8 Million.

Rochow - Background

- A denial of a claim for benefits is generally also a fiduciary breach – failure to follow plan documents.
- Prior case law held that if you could recover as a claim for benefits you could ***not*** also recover as a fiduciary breach.
- Supreme Court in *Mertens v. Hewitt* held that punitive damages are not recoverable.

Rochow - Facts

- Plaintiff suffered from a rare and debilitating brain infection.
- He was demoted and eventually terminated from employment.
- LINA (Life Insurance Co. of North America) denied claim (three times) as he did not file disability claim until after termination of employment, i.e., not actively at work.
- The District Court found that LINA acted arbitrarily and capriciously and held for Plaintiff.
- LINA appealed and the case was remanded to District Court for an Accounting and Damages.
- Plaintiff had died so remand was handled by his estate.

Rochow - Decision

- Court held that Plaintiff's withheld benefits were $910,629.64.
- Found that LINA made between 11 and 39 percent annually on its assets and awarded an additional $2.9 in disgorged profits.
  - LINA's calculation--$32,732.
- LINA injured Plaintiff in two ways:
  - Denied benefits—pay out benefits
  - Breached fiduciary duty—disgorge profits

- District Court was clearly mad at LINA for its appeals and delay.
  - "If no remedy beyond the award of benefits were allowed, insurance companies would have the perverse incentive to deny benefits for as long as possible, risking only litigation costs in the process."

Rochow - Implications

- While wrongfully decided, clearly opens *Amara* floodgates.
- Plaintiffs will start doing discovery on rate of return on corporate assets.
- Until Supreme Court decides this issue, litigation in all circuits has become more expensive and risky.

Stephan v. Unum Life – 9th Circuit – Your Plan Committee and Attorney Client Privilege

- Attorney/Client privilege generally prevents disclosure of communications with your attorney.
- Fiduciary exception – representing the Plan, the real client is the Participant who can waive the privilege.
- Two Methods to Avoid Fiduciary Exceptions:
  1. Settlor Matter – such as adopting, amending or terminating Plan.
  2. Representing the Plan fiduciary with respect to litigation advice – i.e., the fiduciary's own litigation exposure.

Stephan - Facts

- Stephan accepted a job offer with a base salary of $200,000 and a guaranteed bonus of $300,000, conditioned only upon satisfactory job performance at year end.
- Four months later a bicycle accident resulted in a severed spinal cord and he became a quadriplegic.
- UNUM based the disability benefits on the base salary, excluding bonus.

Stephan – Facts (con't)

- UNUM requested advice from counsel whether the bonus should be considered within the Plan's definition of earnings.
- UNUM withheld document because they were prepared in anticipation of litigation negating the fiduciary exception.
- Ninth Circuit held that the advice related to Plan administration and was given prior to final appeal determination so advice was discoverable.

Stephan - Implications

- Typical Discovery Request after *Stephan*:

  Any and all internal memos, including any in-house and outside counsel's advice and opinions, as there is no privilege due to the fiduciary exception.

- To Protect the Privilege:
  - Avoid third parties, such as consultants, being present at confidential meetings or copied on correspondence.
  - Label communications as Settlor communications whenever possible.
  - Write minutes with a view that minutes will be produced in discovery.

Other Big Exposure Cases and Cases of Interest

- Revenue Sharing and Excessive Plan Fees
  - *Beesley v. International Paper* – allegations of $58 Million in unreasonable recordkeeping expenses and imprudent investment in Company stock – settled for $30 Million.
  - *Tussey v. ABB, Inc.* – fiduciaries individually liable for $13.4 Million for failure to monitor recordkeeping fees; $21.8 Million for improper mapping of funds to less desirable investments; and $1.7 Million for loss float income.

Other Big Exposure Cases and Cases of Interest (con't)

- *Fifth Third Bancorp v. Dundenhoeffer* – Supreme Court will decide whether an investment in employer securities enjoys a "prudence presumption." If not presumed prudent, fewer plans will hold employer securities.
  - Question Presented to SCOTUS (paraphrased): Do employee stock ownership plan managers have a legal duty to stop investing in the company's own stock when they know it has become risky?
- *Dignity Health, et. al.*, ERISA exempts Church Plans. Plaintiffs have recently challenged the Church exemption of large affiliated groups. At risk is violation of ERISA funding and notice rules and liability for fiduciary violations. The North District of California held that the non-profit hospitals even though affiliated with the Catholic Church were not "church plans" exempt from ERISA. The defined benefit plan of the group was unfunded by $1.2 Billion, if ERISA applies.
  - Court not persuaded by IRS guidance or contrary case law in other jurisdictions

Lessons from Fiduciary Cases:

- Examine investment returns.
- Examine revenue sharing arrangements.
- Examine Plan fees.
- Examine how Plan fees are being allocated to Participants.
- If you are using retail rather than institutional shares in a large Plan – get out your checkbook now and write plaintiffs a check as you will likely lose.
- Hire experts and ask questions.

Summary

- Litigation is on the rise.
- Draft Plan documents with an eye towards litigation.
  - Shorter limitations periods.
  - Maximize subrogation recoveries.
  - Make sure you have an enforceable Plan document.
- Conduct fiduciary training.
  - Hire experts.
  - Ask questions.
  - Review Plan fees and revenue sharing.
- Communicate in writing with a view that written documents will be discoverable.
  - Do not copy outside third parties.
- Don’t make the court mad at you.