THE NATIONAL LAW JOURNAL

IN FOCUS

MONDAY, JANUARY 29, 2001

EMPLOYMENT LAW

ALM

Posner proposes ERISA plan 'safe harbor' language

Judge acts as drafter to give presumption of correctness to administrators' decisions.

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SPECIAL TO THE NATIONAL LAW JOURNAL

HARRY POTTER AND Ali Baba are not the only characters who invoke the power of "magic words." Lawyers adorn contracts with boilerplate phrases in the hope that the magic of shopworn words will ward off evil (lawsuits). The world of employee benefits disputes is no different. A recent case has given us some new magic to consider.

Although Chief Judge Richard A. Posner of the U.S. Court of Appeals for the 7th Circuit was unable to pull a rabbit out of his hat by settling the antitrust dispute between the government and Microsoft Corp.—he was the court-appointed mediator—he did recently resolve a nettlesome problem that has haunted the Employee Retirement Income Security Act (ERISA), the law governing employee benefit plans. The problem Judge Posner tackled was: Under what circumstances should a court reviewing a denied claim for employee benefits substitute its own judgment for that of the plan's administrator?

Why, one may ask, was there confusion? Well, this problem began in 1989, when the U.S. Supreme Court decided that courts reviewing a participant's denied claim for employee benefits had been far too deferential to claims decisions made by plan administrators. In *Firestone Tire & Rubber Co. v. Bruch*,[1] the Supreme Court announced that a plan administrator's interpretation of the terms in an employee benefit plan would be subject to "Judge Judy" review—called "de novo" review by lawyers—because the court gives no presumption of correctness to a plan administrator's decision to grant or deny a claim for benefits. In other words, like Judge Judy on television, the reviewing court will make the call as to whether the participant is entitled to employee benefits under the plan's terms.

The Supreme Court explained in *Firestone*, however, that if a plan contains special language giving the administrator the power to construe the plan's terms and to determine who is eligible for benefits, then the administrator's decision would be deferred to under the "abuse of discretion" standard of review.

The degree of deference under the abuse-of-discretion standard is most commonly referred to by the familiar description that the administrator's reading will be upheld unless it is "arbitrary and capricious." The meaning of those words has been fleshed out further in several cases. For example, in *Pokratz v. Jones Dairy Farm*,[2] the court stated that the standard calls for "the least demanding form of judicial review of administrative action": "Although it is an overstatement to say that a decision is not arbitrary or capricious whenever a court can review the reasons stated for the decision without a loud guffaw, it is not much of an overstatement."

Other reviewing courts, such as the court in *Cuddington v. Northern Indiana Public Service Co.*,[3] have extracted from earlier case law a less colorful but more helpful standard: "If the trustee makes an informed judgment and articulates an explanation for it that is satisfactory in light of the relevant facts, i.e., one that makes a 'rational connection' between the issue to be decided, the evidence in the case, the text under consideration, and the conclusion reached, then the trustee's decision is final."

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To defer or not to defer

Judge Posner confronted the annoying task of nitpicking the words of a plan to determine whether or not to defer to the decision of the plan administrator. In *Herzberger v. Standard Insurance Co.*,[4] Carolyn Herzberger had sought disability benefits from her plan for chronic fatigue syndrome.[5] The plan administrator had denied the claim by determining that Ms. Herzberger's real problem was a mental disorder, for which the plan placed a tight lid on the amount of disability benefits payable. The dispute centered on plan language stating that the plan administrator "will pay the...benefit upon receipt of satisfactory written proof that you have become disabled." Chief Judge Posner concluded that "this language, standing alone (and there is nothing to qualify or amplify it), does not take the plan out of the default rule entitling the disappointed applicant to plenary [de novo] review."[6]

Chief Judge Posner explained that he was devising "safe harbor" language that would guarantee a presumption of correctness to the administrator's decision, so that employees would know what their rights are under employee benefit plans: "The very existence of 'rights' under such plans depends on the degree of discretion lodged in the administrator. The broader that discretion, the less solid an entitlement the employee has and the more important it may be to him, therefore, to supplement his ERISA plan with other forms of insurance. In these circumstances, the employer should have to make clear whether a plan confers solid rights or merely the 'right' to appeal to the discretion of the plan's administrator.

"We should do what we can to clarify the rights and duties of the parties to ERISA plans. Judges are quick to say what is prohibited, but perhaps too slow to say what is permitted and by doing so dispel legal risk. We have therefore drafted, and commend to employers, the following 'safe harbor' language for inclusion in ERISA plans: 'Benefits under this plan will be paid only if the plan administrator decides in his discretion that the applicant is entitled to them.'...An ERISA plan that contains such language will not be opened to being characterized as entitling the applicant for benefits to plenary judicial review of a decision turning him down.... Equally clearly, the presumption of plenary review is not rebutted by the plan stating merely that benefits will be paid only if the plan administrator determines they are due or only if the applicant submits satisfactory proof of his entitlement to them."[7]

Adopting 'safe harbor' language

Has the demon of ambiguity been dispatched forever from this question? Time will tell. In the hope of avoiding future litigation, it is recommended that plan sponsors adopt Judge Posner's "safe harbor" language quoted above. All employee benefit plans should be reviewed to determine whether they contain appropriate language informing participants of the level of discretion used by the administrator in deciding their claims. Deficient plan language can be transformed through the special magic of a plan amendment. Failure to heed Judge Posner's sage advice may result in seven years of bad employee-benefit-plan luck..

1. 489 U.S. 101 (1989).
2. 771 F.2d 206, 209 (7th Cir. 1985).
3. 33 F.3d 813, 817 (7th Cir. 1994).
4. 205 F.3d 327 (7th Cir. 2000).
5. Id. at 332.
6. Id. at 333.
7. Id. at 330. NLJ

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