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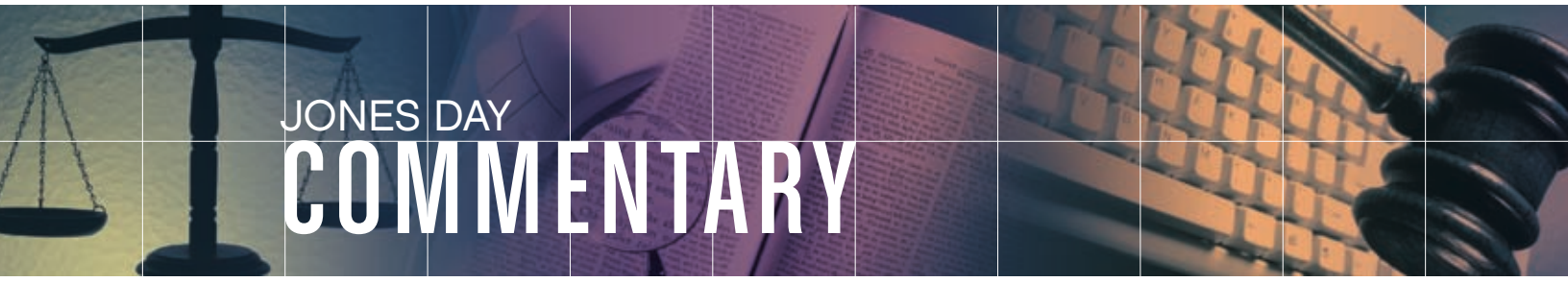

"FOLLOW THE MONEY"

Apparently Deep Throat was right. His proven method of "following the money" to ferret out political scandals has recently been employed to solve one of ERISA's most nettlesome problems: Can an employer-sponsored medical plan force a participant to repay it after the participant has been reimbursed by another for these same plan expenses? Believe it or not, this question has tortured the minds of ERISA lawyers and the federal courts for the past four years. It seems like only yesterday that the Supreme Court began our collective efforts to put Humpty Dumpty back together again in *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 122 S. Ct. 708 (2002). For ERISA lawyers, Humpty Dumpty is something called "subrogation." Before *Great-West*, ERISA-regulated medical plans could routinely enforce repayment provisions ("subrogation clauses") to recover the costs of plan benefits that were reimbursed by third parties. After *Great-West*, they could not. The health-plan repayment clause works like this: A plan participant who breaks his leg in a car accident will have his medical plan pay to fix his leg. The participant will then sue to recover the costs of these same medical-plan benefits (among other things) from the other driver's auto insurance carrier. The health plan, upon learning of the participant's good fortune in recovering from the other driver's auto insurance carrier, asks the participant to repay the medical plan. After all, is it really fair for the participant to recover twice for fixing his broken leg?

GREAT-WEST'S POINT

The Supreme Court confused us by its insistence in *Great-West* that any recovery by the medical plan had to satisfy the strictures described by the ancient courts of equity. The key problem for the medical plan in *Great-West* was that the "restitution" it sought was not "equitable" relief under ERISA because it could not point to specific property it wanted to be restored. Here is what happened: A medical plan filed a lawsuit in federal court to enforce its clause in *Great-West*. Janette Knudson had been rendered a quadriplegic because of a car accident. Janette filed a lawsuit in state court to recover from the car manufacturer and others and eventually negotiated a settlement for more than $600,000. In the settlement agreement,

she earmarked $13,000 to pay for the medical plan's claim of more than $400,000 in medical-plan benefits. The federal district court rejected the medical plan's claim. On appeal, the medical plan's fiduciaries argued that the relief they sought was "equitable" and "appropriate" under ERISA § 502(a)(3), 29 U.S.C. § 1132(a)(3). The Supreme Court disagreed, finding that the medical plan's attempt to recover money from the beneficiary for amounts recovered from the third party was not "equitable" and, thus, the remedy was unavailable under § 502(a)(3). The Supreme Court left open the possibility of an equitable remedy "where money or property identified as belonging in good conscience to the plaintiff could clearly be traced to particular funds or property in the defendant's possession." *Great-West*, 534 U.S. at 213. In that situation, the medical-plan plaintiffs could seek restitution in equity in the form of a constructive trust or an equitable lien. *Id*. at 213.

The nub of the repayment problem for an ERISA-regulated medical plan is that the remedies available under ERISA's catchall provision (§ 502(a)(3)) are limited. While "equitable" forms of relief can be used, monetary relief is unavailable. *Mertens v. Hewitt Associates*, 508 U.S. 248, 113 S. Ct. 2063 (1993). In *Great-West,* the Supreme Court explained that § 502(a)(3) authorizes the use of "traditional" forms of equitable relief only, *i.e*., "those categories of relief that were typically available in equity (such as injunction, mandamus, and restitution, but not compensatory damages)." *Great-West Life*, 534 U.S. at 726; *Mertens*, 508 U.S. at 256. "[M]oney damages … , the classic form of legal relief" are unavailable under § 502(a)(3). *Mertens*, 508 U.S. at 255.

As the Supreme Court oft reminds us, the parsimony in ERISA remedies is no accident: "The six carefully integrated civil enforcement provisions found in § 502(a) of the statute as finally enacted, however, provide strong evidence that Congress did not intend to authorize other remedies that it simply forgot to incorporate expressly." *Massachusetts Mutual Life Ins. Co. v. Russell*, 473 U.S. 134, 146, 105 S. Ct. 3085, 3092 (1985).

ERISA's private enforcement provisions (set forth in ERISA §§ 502(a)(1)(B), 502(a)(2), and 502(a)(3)) are specific. Plaintiffs who want additional plan benefits can file suit under ERISA § 502(a)(1)(B). A participant who believes the plan's fiduciaries are liars, crooks, or incompetent can sue the plan's fiduciaries to make the plan whole for losses under § 502(a)(2). Finally, there is a "catchall" provision under ERISA § 502(a)(3). This "kitchen sink" remedy allows claims by participants, beneficiaries, or fiduciaries: "(A) to enjoin any act or practice which violates any provision of [ERISA] or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of [ERISA] or the terms of the plan." In *Great-West*, the Supreme Court ruled that medical-plan fiduciaries seeking to enforce a medical plan's repayment clause against plan participants or beneficiaries must do so under ERISA's catchall provision § 502(a)(3).

A number of circuit courts of appeals interpreted *Great-West* to mean the Supreme Court had closed the door to the enforcement of a medical plan's repayment provision. For example, in *Westaff (USA), Inc. v. Arce*, 298 F.3d 1164 (9th Cir. 2002), the Ninth Circuit responded with an emphatic "hell no" to the question of whether a medical plan's repayment clause could be enforced in federal court. According to the Ninth Circuit, even where the ERISA-regulated medical plan asserts a right to particular property or funds held by the plan participant, the medical plan's demand for repayment of those funds is not within an ancient equity court's ghoulish definition of "equitable" relief. In *Westaff*, the parties had entered into a repayment agreement under which the medical plan would be entitled to recover all medical benefits paid from a third-party settlement. The participant recovered from the third party and then placed the recovered money into an escrow account pending resolution of the medical plan's claim for reimbursement. In an attempt to avoid the application of *Great-West*, the medical plan characterized its claim as one for equitable relief and sought a declaratory judgment that it was entitled to these funds. Refusing to be tricked by word play, the Ninth Circuit clung to the literal holding of *Great-West*, finding that restitution was a legal remedy regardless of what the claim was called, and regardless of whether the specific money sought was identified by the plaintiff's medical plan. Accordingly, the medical plan's right to repayment of the medical benefits provided could not be enforced under ERISA.

Other circuit courts of appeals interpreted *Great-West* to mean that so long as funds recovered from a third party are identified and have not been distributed, the medical plan may seek the "equitable" remedy of a constructive trust or equitable lien on those amounts. *Admin. Comm. of Wal-Mart*

Associates Health & Welfare Plan v. Willard, 393 F.3d 1119 (10th Cir. 2004); *Bombardier Aerospace Employee Welfare Benefits Plan v. Ferrer, Poiret & Wansbrough*, 354 F.3d 348 (5th Cir. 2003).

SEREBOFF'S COUNTERPOINT

Because the federal courts of appeals were in complete disagreement as to whether a medical plan could enforce its repayment provisions, the U.S. Supreme Court entered the fray. *Sereboff v. Mid Atlantic Medical Services, Inc*., _____ U.S. _____, 126 S. Ct. 1869 (2006). The Sereboffs had been involved in an automobile accident in California and had suffered injuries. The Mid Atlantic plan had paid for the couple's medical expenses. The Sereboffs later filed a lawsuit in state court against several third parties and eventually settled for $750,000. Although Mid Atlantic sent the Sereboffs' attorney several letters asserting a $75,000 lien on the anticipated proceeds from the lawsuit for the Mid Atlantic plan's medical expenses, the Sereboffs' attorney never responded.

Mid Atlantic filed suit in federal court in Maryland under ERISA § 502(a)(3), seeking to collect from the Sereboffs the $75,000 in medical expenses it had paid on their behalf. Since the Sereboffs' attorney had already paid out the settlement proceeds to the Sereboffs, Mid Atlantic sought a temporary restraining order and preliminary injunction requiring the Sereboffs to retain and set aside at least $75,000 from the settlement proceeds. The district court approved a stipulation by the parties to "preserve $75,000" of the settlement funds in an investment account until the court ruled on the merits of the case and all appeals, if any, were exhausted.

On the merits, both the district court and the Fourth Circuit Court of Appeals found in Mid Atlantic's favor and ordered the Sereboffs to pay Mid Atlantic $75,000, plus interest, with a deduction for Mid Atlantic's share of the attorneys' fees and court costs the Sereboffs had incurred in state court.

Chief Justice Roberts, writing for a unanimous Supreme Court, ruled that enforcing a medical plan's repayment agreement qualifies as "equitable" relief under ERISA. Like all great ERISA decisions, *Sereboff* begins with a description of the plan's terms:

> The plan provides for payment of certain covered medical expenses and contains an "Acts of Third Parties" provision. This provision "applies when [a beneficiary is] sick or injured as a result of the act or omission of another person or party," and requires a beneficiary who "receives benefits" under the plan for such injuries to "reimburse [Mid Atlantic]" for those benefits from "[a]ll recoveries from a third party (whether by lawsuit, settlement, or otherwise)." … The provision states that "[Mid Atlantic's] share of the recovery will not be reduced because [the beneficiary] has not received the full damages claimed, unless [Mid Atlantic] agrees in writing to a reduction."

126 S. Ct. at 1872.

For Chief Justice Roberts, the medical plan acted properly by enforcing its repayment provision because it "followed the money":

> It [Mid Atlantic] alleged breach of contract and sought money, to be sure, but it sought its recovery through a constructive trust or equitable lien on a specifically identified fund, not from the Sereboffs' assets generally, as would be the case with a contract action at law. ERISA provides for equitable remedies *to enforce plan terms*, so the fact that the action involves a breach of contract can hardly be enough to prove relief is not equitable; that would make § 502(a)(3)(B)(ii) an empty promise. This Court in *Knudson* did not reject Great-West's suit out of hand because it alleged a breach of contract and sought money, but because Great-West did not seek to recover a particular fund from the defendant. Mid Atlantic does.

126 S. Ct. at 1874.

This holding indicates that because ERISA plans are in essence contracts, they can use equitable remedies to enforce their terms. To paraphrase the Supreme Court, an ERISA-regulated medical plan's contractual agreement for repayment can be enforced through "equity" under ERISA § 502(a)(3) by filing an action for an equitable lien or for a constructive trust. *Id.* Although the Sereboffs argued that the Supreme Court's decision in *Knudson* imposed a strict "tracing requirement" on all equitable actions to recover money, Justice Roberts decided that the Sereboffs were confused. Mid Atlantic was suing on an "equitable lien imposed by agreement," not on an "equitable lien sought as a mat-

ter of restitution." *Id*. at 1875-1876. Because Mid Atlantic was suing on an "equitable lien imposed by agreement," there was no requirement that the money over which the lien was asserted be in existence when the contract containing the lien provision was executed. *Id*. at 1876. This means that for a medical-plan fiduciary to recover in a subrogation claim, the plan document (usually a summary plan description) must state that the participant is to repay the plan from any monies recovered from a third-party tort-feasor. Finally, the Supreme Court explained that because the action was for breach of contract enforced by an equitable lien, the "parcel of equitable defenses the Sereboffs claim accompany any such action are beside the point." *Id*. at 1877. An equitable remedy based on a contractual agreement was very different from a purely equitable claim and, in the words of the Court, was not "a freestanding action for equitable subrogation." *Id*.

Whether *Sereboff* is the last word on the enforcement of a medical plan's repayment provisions remains to be seen. We do not yet know whether the plan provision entitled "Acts of Third Parties" is the only magic phrase required to create an equitable lien to fend off the ghouls of ancient equity. As all good lawyers know, facts matter. In *Sereboff*, the district court approved the parties' agreement to set aside $75,000 in an investment account until the case was resolved. Was *Sereboff* an easy case because Mid Atlantic pursued $75,000 that was already identifiable and set aside in an investment account? What happens if there is no segregated investment account? Worse, can the medical plan recover if the participant hides the money or gives the money away?

The Fat Lady has not yet sung. Disputes about a medical plan's right to repayment will continue. Although the Supreme Court's pragmatic approach to this problem in *Sereboff* has narrowed the playing field, the intensely factual nature of these disputes means ERISA lawyers will be forced to find new ways to "follow the money."

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