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BENEFIT NEWS BRIEFS

U.S. DISTRICT COURT REJECTS ARGUMENT THAT ERISA PROHIBITS SUBROGATION BY GROUP HEALTH PLANS

In the aftermath of the U.S. Supreme Court decision in *Great-West v. Knudson*, there have been a number of district court decisions leading to the conclusion that *Great-West* does NOT preclude legal action under ERISA and/or under state laws for the recovery of amounts paid by a plan for medical expenses when a participant also receives reimbursement for the medical expenses from a third party.

The district court decision discussed below, *Schulenberg v. The Rawlings Company*, illustrates the reasoning being followed in many of these cases. The thrust of this decision is that funds may still seek recovery under section 502(a)(3)(C) of ERISA if the suit does not impose personal liability on the participant which means that the funds to be recovered are still identifiable and are preserved in a separate fund and are not in the direct possession of the participant.

In addition, this latest district court decision makes it clear that a plan might be better off seeking recovery under state lien laws, rather than under ERISA, by making a constructive lien against a third party reimbursement amount if the amount is still being retained in a separate fund.

The citation for this case is: *Schulenberg v. The Rawlings Company,* U.S. District Court for Nevada, CVN03-0134-HDM(VPC), August 20, 2003. Full text is available from the TIC Research Department or at Westlaw 22129230.

THE FACTS

Schulenberg was injured in a car accident in 1999, hired an attorney, and recovered $25,000 from a third party insurer. Meanwhile, her medical bills were paid by her ERISA health plan which has a subrogation and reimbursement clause. Between 2000 and 2003, the plan contacted Schulenberg's attorney ten times stating its intent to place a lien against any amount recovered from a third party insurer, as provided for under the plan's subrogation clause.

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In response, Schulenberg filed suit in a U.S. district court alleging that the plan's subrogation clause was prohibited under ERISA and that any attempt to enforce the clause was a breach of fiduciary duty. The suit also alleged certain violations of RICO and the Fair Debt Collections Act (allegations later dismissed by the judge).

Schulenberg's suit was filed against the Rawlings Company, a firm to which the plan had delegated the responsibility for collection of the debt owed by Schulenberg.

THE DISTRICT COURT'S RESPONSE

The U.S. District Court for Nevada concluded that: "There is nothing in ERISA which prohibits a subrogation clause nor prohibits a plan from attempting to recover monies under such a clause."

However, while approving plan's right to include a subrogation clause, the district court conceded that recent decisions by the U.S. Supreme Court (the *Great-West* case) and by the Ninth Circuit Court (*Honolulu Joint Apprenticeship* case, 332 F.3d 1234, 2003) "reflect a steadily shrinking field of appropriate equitable relief."

For example, the U.S. Supreme Court in the *Great-West* decision concluded that a plan could NOT recover subrogation amounts by relying on a claim for "appropriate equitable relief" under ERISA section **502(a)(3)(B)** which allows a participant, a beneficiary, or a fiduciary "to obtain other appropriate equitable relief.". In the *Great-West* case the beneficiary sustained serious injuries in an auto accident and the plan incurred over $330,000 in medical expenses which the trustees, acting as fiduciaries, attempted to recover under its subrogation provisions. The claim itself ask for "appropriate equitable relief" under section 502(a)(3)(B) of ERISA. **However, the Supreme Court ruled that the plan was not seeking equitable relief but rather legal relief or monetary relief, a form of relief not authorized by this ERISA section. (For details on the *Great-West v. Knudson* case, see *Client Bulletin 2002-7*, 2/18/02, pages 3-5.)**

In a decision by the Ninth Circuit (*Honolulu Apprenticeship Training Plan v. Foster*), an apprenticeship training plan was precluded from recovering money from an apprentice after he went to work for a non-union employer, an event which required the participant to reimburse the plan for the cost of his education (about $10,000) if he went to work for a non-signatory employer. Again the court ruled that this was a contractual dispute and therefore, recovery could not be sought under the "appropriate equitable relief" provision in ERISA section 502(a)(3)(B).

Despite these two decisions, the Nevada District Court states for clarification purposes that:

> **These two cases did not hold, … that the assertion of reimbursement claims violated any law or were otherwise improper.** Rather, they hold that the remedies sought in those cases could not be pursued in federal court under ERISA because the remedies amount to monetary damages, while ERISA provides only for equitable relief. **These cases did not specifically foreclose all possible federal or state remedies nor did they render the underlying debt void.** In dicta, the *Great-West*

> county stated that "there may have been other means for petitioners to obtain the essentially legal relief that they seek … petitioners could have intervened in the state-tort action or [initiated] a direct action by petitioners against respondents **asserting state law claims such as breach of contract.** (emphasis added)

The district court did not resolve the issue of whether or how the plan could ultimately collect from Schulenberg. Looking specifically at the facts in the *Schulenberg* cases, the Nevada district court observes:

> Plaintiff reached a settlement in a third party tort action and **placed the proceeds [of $25,000] in a fund pending resolution of the instant matter.** No proceeds have been paid to the defendant. Defendant has placed a lien on the fund and has issued numerous demand letters giving Plaintiff notice of the lien. None of these letters, however, make a demand for payment pursuant to plan provisions or even make reference to a contractual right to reimbursement. Further, Defendant has made no attempt to filing suit, or otherwise, to collect from Plaintiff on their demand for reimbursement. **There is no bar to plan provisions requiring reimbursement or to demands for reimbursement.** (emphasis added – from text of the decision).

CONCLUDING OBSERVATIONS

Unlike most subrogation cases where the plan is suing the participant, here the participant was suing the plan for merely having a subrogation provision (calling it a breach of fiduciary duty) so the court dealt only with this single issue. (There were some other issues which the court readily dismissed.)

Editorial Comment: At this stage of litigation over subrogation issues, it seems appropriate to conclude that the federal courts seem to agree that subrogation and reimbursement clauses are not illegal if they are included in its plan document and/or SPD. However, filing suit under ERISA section 502 requesting "other appropriate equitable relief" is a loser unless the amount sought by the plan is physically sitting in a separate fund and if paid to the plan, will not result in any personal liability for the participant.

The subrogation litigation to date also seems to suggest that fund counsel should carefully consider, before going the litigation route to collect, whether the chances of success are better in state court than in a federal district court.

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