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ERISA Plan Cannot Recover Spent Settlement Funds, High Court Rules

The Supreme Court recently limited a health plan's ability to recoup the medical expenses it paid on behalf of a participant injured in a car accident before he obtained — and spent — a settlement award in his lawsuit against the drunk driver who hit him. The Court refused the plan's claim for recovery from the participant's general assets, ruling that a plan can seek equitable relief only against specifically identified settlement funds in the participant's possession or traceable items that he purchased with those funds. In light of this decision, plans should track participants' third-party claims and act promptly to preserve their reimbursement rights. It remains to be seen if the ruling will be applied in the context of retirement plan overpayments.

Background

ERISA provides a vehicle for plan participants to recover plan benefits and, in certain circumstances, for plans to seek recovery of payments made to plan participants. Among other things, ERISA Section 502(a)(3) allows plan fiduciaries to bring suit to obtain "appropriate equitable relief" to enforce the plan's terms.

Most ERISA-governed health plans contain subrogation and reimbursement provisions generally allowing the plan to recover benefits paid to a participant or beneficiary for injuries or illnesses caused by a third party. In determining whether a claim for relief is "equitable" — and thus can be brought under Section 502(a)(3) — courts look at both the basis for underlying claim and the nature of the remedy sought.

> **Comment**. While often referenced interchangeably, subrogation and reimbursement are distinct concepts. A plan exercises its subrogation right to "stand in the shoes" of the participant or beneficiary when it brings legal action against a third party to recover benefits. On the other hand, if the participant or beneficiary has already received payment from the third party, a plan exercises its reimbursement right in collecting for benefits paid.

Plan Paid Out, Later Sought Reimbursement from Participant's Settlement

Robert Montanile participated in the National Elevator Industry Health Benefit Plan (Plan), an ERISA plan that contained express subrogation and reimbursement provisions. After Montanile was injured in a car accident, the Plan paid over $120,000 for his medical care. Montanile later sued the drunk driver who hit him and obtained a $500,000 settlement. Roughly $260,000 of the settlement went toward Montanile's attorneys' fees and costs, with the remainder held in a client trust account. The Plan's Board of Trustees (Board) sought reimbursement from Montanile for the medical expenses the Plan paid. After negotiations over the amount to be repaid broke down, Montanile's attorney told the Board that he would distribute the remaining settlement funds to Montanile, unless it objected within 14 days. When the Board did not respond, the attorney sent Montanile the remainder.

Six months later, the Board sued Montanile under Section 502(a)(3), seeking an "equitable lien" on any settlement funds in Montanile's "actual or constructive" possession, and an order enjoining Montanile from spending those funds. By then, Montanile had spent almost all of the funds he had received. Both the trial court and then the Eleventh Circuit ruled that his underlying repayment obligation remained, and that the Plan was entitled to reimbursement from his general assets.

Because circuit courts of appeal were divided on the question of whether an ERISA-covered plan can enforce an equitable lien against a participant or beneficiary's general assets to recover an alleged plan overpayment when the overpaid funds are no longer specifically identifiable, the Supreme Court agreed to hear Montanile's case.

No Reimbursement Right Where Participant Dissipated Settlement Funds

In an 8-1 ruling, the Supreme Court decided on January 20, 2016, that a plan fiduciary cannot sue under Section 502(a)(3) to attach a participant's general assets when the participant dissipates the settlement on nontraceable items because, in those circumstances, the suit is not one for equitable relief. Whether relief is legal or equitable depends on the basis of the claim and the nature of the remedy sought. The Court concluded that even though the basis for the Board's claim in *Montanile* was equitable (reimbursement for medical expenses after Montanile's third-party settlement), the remedy the Board sought may not have been. To sustain an equitable lien, the Board would have had to identify a specific fund (1) to which the lien initially attached, and (2) that was intact in Montanile's possession. If Montanile spent the entire settlement fund on nontraceable items, the Board could not meet this second requirement. In that scenario, the relief sought would be "legal" rather than "equitable" and, as such, would not be authorized under Section 502(a)(3).

> **Comment.** This conclusion is consistent with several earlier Supreme Court cases involving similar facts where the Court stuck to traditional equitable principles in interpreting "appropriate equitable relief," refusing to adopt a more expansive definition.

The Board's argument that it should be allowed to collect from Montanile's general assets where the participant "wrongfully dissipate[d] the equitable lien to thwart its enforcement" did not sway the Court. Nor did the Board's assertion that allowing the Plan to collect from Montanile's general assets would best protect plan assets. As the Court noted, the Board not only knew about the settlement, but squandered its chance to object to the distribution of remaining funds to Montanile. Even after Montanile received the funds, the Board could have filed suit immediately, but it did not — instead waiting half a year to do so.

Because the trial court found that the Plan could recover from Montanile's general assets, it never determined whether Montanile had kept his settlement fund separate from his general assets and dissipated the entire fund on nontraceable assets. Thus, the Court sent the case back to the trial court for that determination.

Justice Ruth Bader Ginsberg, the lone dissenter, criticized what she called the Court's "bizarre conclusion" allowing Montanile to escape his reimbursement obligation by quickly spending the settlement funds on nontraceable items.

In Other Supreme Court Employee Benefits News

On January 19, 2016, the Supreme Court refused to hear *Sissel v. Dep't of Health & Human Services,* a constitutional challenge to the Affordable Care Act's (ACA) individual mandate. The case claimed that the ACA violated the Origination Clause of the U.S. Constitution — which requires all bills raising revenue to start in the House of Representatives — because the bill was introduced in the Senate. The trial court dismissed this case, a ruling that the **appeals court** affirmed. The Supreme Court's decision not to take the case follows rulings upholding the ACA both times the Court has entertained major challenges to this law. See our **June 25, 2015** *FYI Alert* and **June 28, 2012** *For Your Information*.

Key Plan Design and Administration Takeaways

Sponsors should ensure that their plan documents contain appropriate subrogation and reimbursement provisions, and see to it that SPDs and other plan communications clearly describe those provisions in layman's terms.

But post-*Montanile*, even the best drafted plan document language may not be enough to protect a plan's subrogation and reimbursement rights. Because participants and beneficiaries may be able to escape repayment obligations by quickly spending settlement funds on nontraceable items, plans should be aware, and track the status, of third-party disputes relating to plan benefits. They should consult with legal counsel about, if and when to initiate, or participate in, litigation to recover sums the plan paid out.

> **Comment.** Failing to timely pursue and collect settlement proceeds to which a plan is entitled under its subrogation and reimbursement provisions could itself become the basis for a breach of fiduciary duty claim brought by other plan participants. For this reason, some plans' provisions allow — but do not require — the plan to pursue subrogation and reimbursement rights.

While the facts of *Montanile* are health plan-specific, the Court's rigid view of ERISA's "equitable relief" provision could also have implications for retirement plans. In the common scenario of a retirement plan overpayment, it is possible that *Montanile* could be understood to limit a plan's ability to recoup previously distributed benefits that are not maintained in a specifically identifiable account separate from the participant's or beneficiary's general assets, such as an IRA account. However, if *Montanile* does apply in that context, it should not affect a plan's ability to reduce future payments slated for distribution.

In Closing

The *Montanile* case highlights the costly consequences of fiduciaries' failure to timely pursue recovery of payments made to plan participants. In light of this ruling, sponsors should review their plan provisions along with their procedures for monitoring third-party disputes involving participants and beneficiaries to ensure prompt action to protect plan reimbursement rights.

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