MATTHIESEN, WICKERT & LEHRER, S.C.

A FULL SERVICE INSURANCE LAW FIRM

1111 E. Sumner Street, P.O. Box 270670, Hartford, WI 53027-0670

(800) 637-9176 (262) 673-7850 Fax (262) 673-3766

http://www.mwl-law.com

<<< SPECIAL HEALTH INSURANCE SUBROGATION ALERT >>>

HEALTH INSURANCE

A SUPREME VICTORY FOR ERISA SUBROGATION

Today, in what can only be described as a major victory for subrogating insurance carriers and health plans, the Supreme Court rendered a decision in the case of *Sereboff v. Mid Atlantic Medical Services, No. 05-250 (547 U.S. ___),* upholding the right of an ERISA Plan to file a federal suit for reimbursement. This landmark decision overturns prior inconsistent decisions from the 6th and 9th Circuits, and clarifies the confusion, which has existed in this area since the Supreme Court's 2002 decision in *Great-West Life & Annuity Ins. Co. v. Knudson.* Chief Justice John Roberts, writing the unanimous decision for the Court, held that a Plan's efforts to seek reimbursement through a constructive trust or equitable lien are considered "equitable", not "legal", whenever the funds sought are in the possession of the Plan beneficiary, and eliminated any need for "tracing funds" where a Plan provides for reimbursement on its face.

In this case, Joel and Marlene Sereboff were injured in an automobile accident in California. For their injuries, the Sereboffs received approximately $75,000.00 from an ERISA-covered Plan, which was administered in Maryland. The Sereboffs filed suit in California and received a $750,000.00 settlement from the tortfeasoer. The Plan contained a reimbursement provision that required covered persons to reimburse the Plan to the extent of benefits paid when a covered person recovers from another party. Pursuant to this language, the Plan requested that the Sereboffs reimburse the Plan as required under the terms of the Plan, but they refused.

The Plan responded by filing suit against the Sereboffs, seeking "appropriate equitable relief" under ERISA § 502(a)(3). The Sereboffs stipulated to hold an amount equal to the lien in their investment account until the litigation could be resolved. The district court held that the Plan was entitled to equitable relief against the funds in the investment account pursuant to *Great-West Life & Annuity Ins. Co. v. Knudson.* The Sereboffs appealed and the 4th Circuit affirmed, declaring that the funds could be traced even though they had been placed in an account holding unrelated funds of the Sereboffs, and noting that these funds belonged in good conscience to the Plan. The Supreme Court granted review to the Sereboffs in order to decide a split between the federal appellate court over whether the ERISA Plan's action for reimbursement was "equitable."

In an unusually concise opinion, the *Sereboff* decision contained three main points of import. First, the Court easily distinguished the *Knudson* case because the Plan member in *Knudson* did not have possession of the funds, which were being held in a "Special Needs Trust", stating that "*The 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*." By contrast, because the funds in this case were being held and controlled by the Sereboffs, *Knudson* did not apply.

Second the Court went on to explain its reasoning for holding that a breach of contract action can be equitable. It was forced to examine cases addressing the differing concepts of law versus equity when the United States judiciary was split between courts of law and courts of equity. It analogized this case to *Barnes v. Alexander*, 232 U.S. 117 (1914) a nearly 100-year-old decision that addressed two attorneys' dispute over their entitlement to a third attorney's settlement. In that case, two attorneys sought to create an equitable lien against the settlement based upon a prior promise from a third attorney. The Court likened the third attorney's promise to the first two attorneys to the ERISA Plan's reimbursement clause. Because the *Barnes* Court allowed the equitable claim, Justice Roberts held that the Sereboff's ERISA Plan "could rely on a 'familiar rul[e] of equity' to collect for the medical bills it had paid on the Sereboff' behalf." In essence, today the Supreme Court held for the first time that in ERISA subrogation, a Plan beneficiary becomes a trustee for the Plan the moment he or she receives a third party settlement. Noting that there are two types of equitable liens, the Court declared that where, as in ERISA subrogation, an equitable lien is sought to enforce an equitable lien established through the terms of an agreement (viz., the reimbursement terms of the Plan itself), there will be no tracing of the funds required as there is in cases involving an equitable lien sought as a matter of restitution.

Finally, the Chief Justice dismissed the Sereboff's claim that equitable remedies like make-whole or common fund would apply to the Plan's lien, where the contractual language specifically disavowed their application. In dismissing this claim, the Court acknowledged the difference between contractual and mere equitable subrogation. Justice Roberts wrote that the Plan's "claim is not considered equitable because it is a subrogation claim." Instead the Court noted that the claim was based on an express agreement, which overrides the apparent equitable considerations.

Never to be underestimated, be assured that trial lawyers will latch onto two potential weaknesses in this decision which may give them new areas in which to attack subrogating health Plans. First, because the decision noted that a constructive trust would attach to "*that portion of the total recovery which is due [the Plan] for benefits paid",* expect plaintiffs' lawyers to attempt to gerrymander settlements by designating all damages recovered as compensating pain and suffering, not medical expenses, and thereafter argue that *Sereboff* forbids reimbursement of these damages. Second, because the decision so strongly distinguished the facts therein from the facts in *Knudson,* where the monies were not in the possession of the beneficiary, but rather placed in a special needs trust, we can expect plaintiffs' lawyers to try more structured settlements and creation of trusts in order to bypass the new *Sereboff* decision.

IMPLICATIONS

The Court's decision is a clear victory for subrogation practitioners and its positive impact should not be underestimated. The entire country is now unified again, and practitioners no longer need to seek creative ways to avoid troublesome jurisdictions such as the 6th and 9th Circuits, in which the courts had declared any effort to enforce a reimbursement provision as "legal" rather than

"equitable". The decision is also of significant importance because it finally acknowledges what many of us have been arguing for years - namely, that subrogation is not inherently equitable. The Court's acknowledgment of this fact may trickle down to even fully insured Plans, who seek to contractually disclaim the made-whole or common fund doctrines. Additional information and complete copy of this brand new decision can be found on our website at www.mwl-law.com.

HEALTH INSURANCE

PENSION PROTECTION ACT OF 2005 IN CONFERENCE COMMITTEE

We previously reported to you on the proposed Pension Protection Act of 2005, which has the potential to eviscerate the confusion and damage inflicted on health insurance subrogation and reimbursement actions by the *Great-West Life & Annuity Ins. Co. v. Knudson* decision of 2002. On December 15, 2005, House Republicans mustered a majority to pass H.R. 2830 (Pension Protection Act of 2005) after refusing to allow a vote on a Democratic alternative offered by Representatives Charles Rangel and George Miller. The Bill, sponsored by Representative John Boehner (R) of Ohio, includes ' 307, entitled "Recovery by Reimbursement or Subrogation with Respect to Provided Benefits". That section reads as follows:

> *(a) In general - Section 502(a) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1132(a)) is amended by adding, after and below paragraph (9), the following new sentence:*
>
> > *"Actions described under paragraph (3) include an action by a fiduciary for recovery of amounts on behalf of the plan enforcing terms of the plan that provide a right of recovery by reimbursement or subrogation with respect to benefits provided to or for a participant or beneficiary."*
>
> *(b) Effective date - Amendment made by Subsection (a) shall take effect on January 1, 2006.*

The report of the Committee on Ways and Means indicates that the intent of this Amendment is to nullify "recent court decisions that have undermined the ability of health plans to recover costs paid out to participants that are awarded additional damages for the same claim". The report indicates that H.R. 2830 is an attempt to clarify that health plans and employers are able to enforce their routine reimbursement provisions with greater certainty.

The Senate did not pass ' 307 in its version of the Pension Reform Bill, and a conference committee is working on final language. It is unclear when the conference committee will complete its work, but make no mistake about it - trial lawyers are working overtime and spending big dollars to see to it that ' 307 does not find its way into the final version of the Bill. Below is a "Congressional Recess Alert" I received today as a member of the Association of Trial Lawyers of America (ATLA). As you can see, trial lawyers are lobbying conferees on this bill to keep ' 307 out of the final version of the bill - and for obvious reasons. They believe the *Knudson* decision helps them destroy and eliminate your health insurance subrogation and reimbursement rights - and they are right.

As subrogation professionals, I believe we have a responsibility to actively lobby our elected representatives by letting them know how important it is that our reimbursement rights accurately reflect the benefit of the bargain set forth in our plan language. They should be reminded that subrogation/reimbursement is not a windfall for large, wealthy insurance companies - it is a significant tool of underwriting used to hold down insurance premiums and ensure the viability of health insurance for all Americans. The underlying and often ignored philosophy behind the doctrine of subrogation is that if the plan does not recoup benefits it pays out where a third party is responsible, the injured party receives a double recovery by recovering once from the plan, and again from the tortfeasor. Instead of passing the cost of the injuries or damage on to the negligent party responsible for the loss, a world without subrogation/reimbursement leaves that cost straddling the shoulders of small and large employers throughout the country - increasing the cost of business, and ultimately the cost of their products.

Contrary to the assertion by the trial lawyers from ATLA, please look at the list of Congressional conferees for this Bill below, and let yours know that the House's ' 307 is vital not only to pension reform, but also to the vitality and longevity of the overall health care system in our country.

We will continue to keep you posted on the history and progress of this significant Bill, either through NASP communications such as this one or through our firm electronic newsletter.

*****ATLA Congressional Recess Alert*** 4/7/06**

Yesterday, Congress adjourned for a two week recess. While they are home, please contact them about two important issues.

Thank you -Ken Suggs, ATLA President

ERISA - Insurance Industry to Recover Before Victim Receives a Dime

Kathleen Fleming's case is one you may know too well. During a hospital stay, her medical team failed to properly respond to her choking. She suffered severe brain damage, and now requires around-the-clock attendance. Her future medical care will likely cost between 12 and 13 million dollars. While Kathleen was able to recover for medical negligence, she only received 2 million dollars to cover her future medical care costs.

The House of Representatives included a provision in its version of the Pension Reform bill that would allow ERISA insurers to take all or part of a victim's compensation. Insurers could sue these victims in order to be reimbursed for the costs of care. Because the Senate did not pass this provision in its version of the Pension Reform bill, a conference committee is working on final language. It is unclear when the conference committee will complete its work, so it is imperative that you contact the conferees and your Member of Congress right away.

Take Action - Send a Letter

If your Member of Congress is on the following list, they are a conferee on this bill. Call and tell them this unfair provision should not be included in the Conference Report. It has nothing to do with pension reform:

Send a Message to Congress.

Sen. Charles Grassley (R-IA): (202) 224-3744
Sen. Max Baucus (D-MT): (202) 224-2651
Sen. Judd Gregg (R-VT): (202) 224-3324
Sen. Kent Conrad (D-ND): (202) 224-2043
Sen. Trent Lott (R-MS): (202) 224-6253
Sen. Orrin Hatch (R-Utah): (202) 224-5251
Sen. Olympia Snowe (R-ME): (202) 224-5344
Sen. Rick Santorum (R-PA): (202) 224-6324
Sen. Michael Enzi (R-WY): (202) 224-3424
Sen. Mike DeWine (R-OH): (202) 224-2315
Sen. Johnny Isakson (R-GA): (202) 224-3643
Sen. John Rockefeller (D-WV): (202) 224-6472
Sen. Jeff Bingaman (D-NM): (202) 224-5521
Sen. Edward Kennedy (D-MA): (202) 224-4543
Sen. Tom Harkin (D-IA): (202) 224-3254
Sen. Barbara Mikulski (D-MD): (202) 224-4654
Rep. Buck McKeon (R-CA 25): (202) 225-1956
Rep. Sam Johnson (R-TX 3): (202) 225-4201
Rep. John Kline (R-MN 2): (202) 225-2271
Rep. Patrick Tiberi (R-OH 12): (202) 225-5355
Rep. George Miller (D-CA 7): (202) 225-2095
Rep. Donald Payne (D-NJ 10): (202) 225-3436
Rep. Robert Andrews (D-NJ 1): (202) 225-6501

In addition to our monthly electronic subrogation newsletter, we pride ourselves in providing the most current updates and developments in insurance and subrogation law through periodic subrogation alerts and updates. This is a service provided exclusively to clients and friends of Matthiesen, Wickert & Lehrer, S.C. This Health Insurance Subrogation Alert is in addition to our regular monthly subrogation newsletter. If anyone has co-workers or associates who wish to be placed on our e-mail mailing list, please provide their e-mail addresses to Rose Thomson at rthomson@mwl-law.com . We appreciate your friendship and your business.