

Equitable Relief under ERISA: Supreme Court Allows a Fiduciary to Recover Expenses Paid to a Beneficiary Who Subsequently Recovered Damages from a Third Party in a Tort Action Lawsuit – *Sereboff v. Mid Atlantic Medical Services*<sup>1</sup> – The Supreme Court unanimously held that a fiduciary’s attempt to recover expenses paid to a beneficiary, who subsequently recovers damages from a third party in a tort action lawsuit, constitutes equitable relief under the Employee Retirement Security Act of 1974 (“ERISA”),<sup>2</sup> so long as the action is equivalent to the recovery of a contractually-created equitable lien on specifically identifiable funds in the beneficiary’s possession.<sup>3</sup>

Marlene Sereboff and her husband, Joel, (the “Sereboffs”) received health insurance under her employer-sponsored plan.<sup>4</sup> The plan was administered by respondent Mid Atlantic Medical Services, Inc. (“Mid Atlantic”) and covered by ERISA.<sup>5</sup> The contract contained an “Acts of Third Parties” provision that applied when a third party’s act or omission caused a beneficiary’s illness or injury.<sup>6</sup> In the event a beneficiary receives benefits under the plan for such injuries, the beneficiary must “reimburse [Mid Atlantic]’ for those benefits from “[a]ll recoveries from a third party (whether by lawsuit, settlement, or otherwise).”<sup>7</sup> Shortly after their involvement in an automobile accident, the Sereboffs filed a tort action lawsuit in California state court seeking compensatory damages for their resulting injuries.<sup>8</sup> In accordance with the “Acts of Third Parties” provision in their contract, Mid Atlantic notified the Sereboffs repeatedly during the litigation of its intention to claim a lien on the Sereboffs’ recovery equivalent to the \$74,869.37 in benefit payments it previously issued to the couple.<sup>9</sup> When the Sereboffs declined to pay Mid Atlantic after settling the litigation for \$750,000, Mid Atlantic filed suit in District Court under ERISA § 502(a)(3).<sup>10</sup>

Because the Sereboffs had already received the proceeds from their settlement, Mid Atlantic requested a temporary restraining order and a preliminary injunction from the District Court requiring the couple to set aside the disputed amount.<sup>11</sup> The Sereboffs complied and placed the money in an investment account pending the District Court’s decision and all subsequent appeals.<sup>12</sup> The District Court held in favor of Mid Atlantic and ordered the Sereboffs to pay the disputed amount plus interest, while allowing for the deduction of the Sereboffs’ state court legal fees.<sup>13</sup> The Fourth Circuit affirmed, in relevant part, on the Sereboffs’ appeal.<sup>14</sup> The Supreme Court granted certiorari to resolve the divide amongst the other Circuit Courts on the question of whether a fiduciary’s action for reimbursement constitutes equitable relief under ERISA.<sup>15</sup>

Under ERISA § 502(a)(3), a fiduciary may “(A) enjoin any act or practice which violates any provision of this subchapter or the terms of the plan, or (B) obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this subchapter or the terms of the plan.”<sup>16</sup> The Court noted that several recent decisions had shaped the

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<sup>1</sup> 126 S. Ct. 1869 (2006).

<sup>2</sup> Employee Retirement Security Act (ERISA) of 1974, 29 U.S.C. §§ 1001-1461 (2000).

<sup>3</sup> *Sereboff*, 126 S. Ct. at 1872.

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

<sup>6</sup> *Id.*

<sup>7</sup> *Id.* (quoting *Pet. For Cert.* 38a).

<sup>8</sup> *Sereboff*, 126 S. Ct. at 1872.

<sup>9</sup> *Id.* at 1872-1873.

<sup>10</sup> 29 U.S.C. § 1132(a)(3) (2000) (addressing the right of an ERISA fiduciary to bring suit to enforce violations of the terms of an ERISA plan).

<sup>11</sup> *Sereboff*, 126 S. Ct. at 1873.

<sup>12</sup> *Id.*

<sup>13</sup> *Mid Atlantic Medical Services, Inc. v. Sereboff*, 303 F. Supp. 2d 691, 701 (Md. 2004).

<sup>14</sup> See *Mid Atlantic Medical Services, Inc. v. Sereboff*, 407 F.3d 212 (4th Cir. 2005).

<sup>15</sup> *Sereboff*, 126 S. Ct. at 1873.

<sup>16</sup> 29 U.S.C. § 1132(a)(3) (2000) (emphasis added).

definition of equitable relief under these circumstances.<sup>17</sup> In *Mertens v. Hewitt Associates*,<sup>18</sup> the Court held that equitable relief included those categories of relief that were typically available in equity in the days of the divided bench, but did not include actions for mere compensatory damages.<sup>19</sup> The Court expanded upon this definition in *Great-West Life & Annuity Ins. Co. v. Knudson*.<sup>20</sup> In *Knudson*, the Court held that one aspect of equitable restitution was that it sought to impose a constructive trust or equitable lien on "particular funds or property in the defendant's possession."<sup>21</sup> Here, the Court held that the nature of Mid Atlantic's claim could be characterized as equitable.<sup>22</sup> Mid Atlantic sought its recovery through an equitable lien on a specifically identified fund, and not from the Sereboffs' assets generally, as would be the case with a mere contract action at law.<sup>23</sup> The Court cited *Barnes v. Alexander*,<sup>24</sup> a case from the days of the divided bench, to support the equitable nature of Mid Atlantic's claim.<sup>25</sup> The Court explained that *Barnes* allowed a fiduciary to follow a portion of the recovery into the beneficiaries' hands as soon as the settlement fund was identified and impose on that portion an equitable lien.<sup>26</sup>

The Sereboffs offered three important counterarguments that the Court refuted. First, they claimed that Mid Atlantic's suit would not have satisfied the "strict tracing rules" required for equitable restitution at common law.<sup>27</sup> Such a rule required that the fiduciary be able to trace the money or property to some particular funds or assets.<sup>28</sup> Here, the Court distinguished between an equitable lien sought as a matter of restitution, and a contractually-created equitable lien of the sort at issue in *Barnes*.<sup>29</sup> The Court found that it made no difference in *Barnes* that the fiduciary could not identify the original asset which was improperly acquired and converted into property the defendant held.<sup>30</sup> Thus, because Mid Atlantic sought to enforce a contractually-created equitable lien analogous to the one in *Barnes*, it did not matter that Mid Atlantic was incapable of tracing the assets either.<sup>31</sup>

Second, the Sereboffs argued that under *Trist v. Child*,<sup>32</sup> equity originally required identification of the fund to which a contractually-specified lien was attached at the time of contract formation.<sup>33</sup> Here, because the automobile accident had yet to occur, the fund Mid Atlantic desired to place a lien upon was not identifiable at the time of contract formation.<sup>34</sup> Thus, the Sereboffs argued that Mid Atlantic's claim was not an equitable one.<sup>35</sup> The Court, however, dismissed the language relied on by the Sereboffs in *Trist* as dicta,<sup>36</sup> and the Sereboffs were unable to offer any other case law to undermine the indication in *Barnes* that the fund over which a lien is asserted does not need to be in existence when the contract containing the lien provision is executed.<sup>37</sup>

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<sup>17</sup> Sereboff, 126 S. Ct. at 1874-75.

<sup>18</sup> 508 U.S. 248 (1993).

<sup>19</sup> Id. at 256.

<sup>20</sup> 534 U.S. 204 (2002).

<sup>21</sup> Id. at 213.

<sup>22</sup> Sereboff, 126 S. Ct. at 1874.

<sup>23</sup> Id.

<sup>24</sup> 232 U.S. 117 (1914).

<sup>25</sup> Sereboff, 126 S. Ct. at 1875.

<sup>26</sup> Id.

<sup>27</sup> Id.

<sup>28</sup> Id.

<sup>29</sup> Id.

<sup>30</sup> Id.

<sup>31</sup> Id.

<sup>32</sup> 88 U.S. 441 (1875).

<sup>33</sup> Sereboff, 126 S. Ct. at 1876 (citing *Trist*, 88 U.S. at 447).

<sup>34</sup> Sereboff, 126 S. Ct. at 1876.

<sup>35</sup> Id.

<sup>36</sup> Id. (declaring the relevant language in *Trist* to be dicta because the contract containing the lien provision at issue in the case was illegal).

<sup>37</sup> Id.

Last, the Sereboffs suggested that the lower courts erred in allowing enforcement of the "Acts of Third Parties" provision without imposing various limitations that are traditionally applicable to an equitable subrogation action.<sup>38</sup> The specific equitable defense the Sereboffs asserted was that subrogation may be pursued only after a victim has been made whole for his injuries.<sup>39</sup> The Sereboffs advanced this argument despite language in the "Acts of Third Parties" provision allowing Mid Atlantic to recover its total payout regardless of whether the beneficiary received the full damages claimed.<sup>40</sup> In refuting this argument, the Court reiterated that Mid Atlantic's action to enforce the "Acts of Third Parties" provision constituted an equitable remedy because it was indistinguishable from an action to enforce a contractually-created equitable lien, and not because it was a subrogation claim.<sup>41</sup> Thus, the defense that the Sereboffs asserted was irrelevant.<sup>42</sup>

Sereboff essentially rectified the split amongst the circuit courts by holding that a fiduciary's action to recover expenses from a beneficiary that received damage payments by a third party is equitable under ERISA § 502(a)(3). The facts in *Sereboff*, however, leave some questions unanswered. Attorneys Charles Stewart and Robin Schachter point out that it is unclear whether the existence of an "Acts of Third Parties" provision sufficiently establishes a contractually-created equitable lien, or "whether the equitable lien was permitted by the fact that the District Court approved a stipulation by the parties agreeing to preserve a specified amount in an investment account until the District Court ruled on the merits and all appeals were exhausted."<sup>43</sup> If the funds had not been placed in a segregated investment account or if the beneficiary had not continued to hold the money, the Court might have held differently.<sup>44</sup> Thus, fiduciaries in the health insurance industry should act quickly to enforce a contractually-created equitable lien on an identifiable fund once a plan beneficiary receives a judgment or settlement from a third party.<sup>45</sup> At a minimum, *Sereboff* holds that this type of fact pattern should allow for an equitable cause of action under ERISA § 502(a)(3).

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<sup>38</sup> *Id.* at 1877.

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

<sup>43</sup> Posting of Charles Stewart and Robin Schachter to SCOTUSblog, [http://www.scotusblog.com/movabletype/archives/2006/05/mondays\\_decisio.html](http://www.scotusblog.com/movabletype/archives/2006/05/mondays_decisio.html) (May 18, 2006 16:13 EST).

<sup>44</sup> C. Mark Humbert, *The Supreme Court Revisits Third-Part Reimbursement Claims Under ERISA: Sereboff v. Mid-Atlantic Medical Services, Inc.*, *Health Law*, Aug. 2006, at 1, 4.

<sup>45</sup> *Id.*