

Appellate Reports and Cases in Brief

A health plan's right to reimbursement for "other equitable relief" under ERISA is limited to specific, identifiable funds within the beneficiary's control

By Jeffrey I. Ehrlich

Montanile v. Board of Trustees of the National Elevator Industry Health Benefit Plan

(2016) __ S.Ct.__ (U.S. Supreme Court)

Who needs to know about this case? Lawyers with clients who may owe their health plans reimbursement for costs incurred to treat medical expenses, when the plans are subject to ERISA.

Why it's important: Makes clear that the plan's right to reimbursement under ERISA's provision for "other equitable relief" is limited to specific, identifiable funds within the beneficiary's control. Hence, if the beneficiary has dissipated the funds before the reimbursement suit is filed, the claim cannot be satisfied out of the beneficiary's general assets.

Synopsis: Montanile was injured in an auto accident with a drunk driver. His ERISA plan paid $120,000 for his medical expenses. He then sued the driver, and obtained a $500,000 settlement. When he notified the plan, it sought reimbursement. His counsel argued that the plan was not entitled to reimbursement. The parties attempted to reach an agreement on reimbursement, but failed. His attorney then informed the plan that, unless it objected within 14 days, he would disburse the proceeds held in his trust account to Montanile. The plan did not object, and the funds were disbursed. Six months later, the plan sued Montanile for reimbursement in federal court, asserting a claim under ERISA, § 503(a)(3), 29 U.S.C. § 1132(a)(3), which authorizes an action by plan fiduciaries to obtain "appropriate equitable relief."

The district court granted summary judgment for the plan, rejecting Montanile's claim that he had spent most of the settlement funds, leaving no specific, identifiable fund separate from his general assets against which the plan's equitable lien could attach. The Court of Appeals for the 11th Circuit affirmed. The Supreme Court reversed.

Section 502(a)(3) of ERISA authorizes plan fiduciaries like the Board of Trustees to bring civil suits "to obtain other appropriate equitable relief ... to enforce ... the terms of the plan." The Supreme Court's cases explain that the term "equitable relief" in § 502(a)(3) is limited to "those categories of relief that were *typically* available in equity" during the days of the divided bench (meaning, the period before 1938 when courts of law and equity were separate). (*Mertens v. Hewitt Associates* (1993) 508 U.S. 248, 256. Under the Court's precedents, whether the remedy a plaintiff seeks "is legal or equitable depends on [(1)] the basis for [the plaintiff's] claim and [(2)] the nature of the underlying remedies sought." (*Sereboff v. Mid Atlantic Medical Services, Inc.* (2006) 547 U.S. 356, 363.)

In its prior cases, the Court had determined that a reimbursement claim by the plan was an equitable claim. But the Court's prior cases did not resolve whether the *remedy* that the plan sought – an equitable lien by agreement against the beneficiary's general assets – is equitable in nature. Applying its prior precedents, the Court determined that it was not.

The Court explained that, at equity, a plaintiff could ordinarily enforce an equitable lien only against specifically identified funds that remain in the defendant's possession or against traceable items that the defendant purchased with the funds (e.g., identifiable property like a car). A defendant's expenditure of the entire identifiable fund on nontraceable items (like food or travel) destroys an equitable lien. The plaintiff then may have a personal claim against the defendant's general assets – but recovering out of those assets is a *legal* remedy, not an equitable one. Hence, the Court remanded to the district court to determine if any of Montanile's assets were traceable.

Justice Ginsberg filed brief dissenting opinion, which is worth reading:

> Montanile received a $500,000 settlement out of which he had pledged to reimburse his health benefit plan for expenditures on his behalf of at least $121,044.02. . . . He can escape that reimbursement obligation, the Court decides, by spending the settlement funds rapidly on nontraceable items…. What brings the Court to that bizarre conclusion? As developed in my dissenting opinion in *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 224-234, the Court erred profoundly in that case by reading the work product of a Congress sitting in 1974 as "unravel[ling] forty years of fusion of law and equity,

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solely by employing the benign sounding word 'equitable' when authorizing 'appropriate equitable relief.'" Langbein, What ERISA Means by "Equitable": The Supreme Court's Trail of Error in *Russell, Mertens,* and *Great-West,* 103 Colum. L. Rev. 1317, 1365 (2003). The Court has been persuasively counseled "to confess its error." (*Ibid.)* I would not perpetuate *Great-West* 's mistake, and would therefore affirm the judgment of the Court of Appeals for the Eleventh Circuit.

Hampton v. County of San Diego
(2015) __ Cal.4th __ (Cal. Supreme.)

Who needs to know about this case: Lawyers handling claims against public entities when the design-immunity defense is asserted.

Why it's important: Holds that the "discretionary approval" element of the design-immunity defense can be satisfied even if the official who exercises the discretionary authority to approve the design does so without realizing that the design deviated from the governing standards.

Synopsis: A public entity may be liable for injuries caused by dangerous conditions of public property. (Gov. Code, §§ 830, 835.) An entity may avoid liability, however, through the affirmative defense of design immunity. (§ 830.6.) "A public entity claiming design immunity must establish three elements: (1) a causal relationship between the plan or design and the accident; (2) discretionary approval of the plan or design prior to construction; and (3) substantial evidence supporting the reasonableness of the plan or design." (*Cornette v. Department of Transportation* (2001) 26 Cal.4th 63, 66.)

Here, plaintiff Randall Keith Hampton was seriously injured in a collision between his vehicle and another that occurred at the intersection of Miller and Cole Grade Roads in San Diego County. Hampton sued the County of San Diego for maintaining an allegedly dangerous condition of public property. The claim was that the design and construction of the intersection where the accident occurred afforded inadequate visibility under applicable County design standards for a driver turning left from Miller Road onto Cole Grade Road.

The County moved for summary judgment, claiming design immunity under section 830.6. In support, it relied on a declaration from an expert explaining that before construction began the plans were "signed by David Solomon, a licensed civil engineer and traffic engineer who served as Deputy County Engineer and was in charge of the County of San Diego Design Engineering Section. As the person in charge of the County's Design Engineering Section, Solomon had been delegated by the County Board of Supervisors . . . [the] discretion and authority to approve plans such as [the improvement plan]. After the project was completed, 'as-built' plans were approved and signed by John Bidwell, a licensed civil engineer who served as senior Civil Engineer of the County's Design Engineering section on April 13, 1998."

In opposing the motion, the Hamptons argued that the design plans proffered by the County did not show a geographic feature – the high, raised embankment covered with shrubs – that allegedly would seriously impede the visibility or "sight distance" available to a motorist who stopped at the stop sign on Miller Road and sought to turn left onto Cole Grade Road. They argued that the embankment rendered visibility plainly inadequate under applicable County standards. The Hamptons argued that the County could not meet the element of discretionary approval because the engineers who approved the design were evidently not aware that it failed to meet County standards.

The Supreme Court concluded that the "discretionary" element in the three-part test for the design-immunity defense did not require a showing by the public entity that the person who exercised discretionary authority was aware of the applicable standards for the design, or the design's compliance with them. Rather, that issue is included within the third part of the test, which asks whether there is substantial evidence surrounding the reasonableness of the design. "[It] is the reasonableness element of section 830.6 that supplies the statutory bulwark against arbitrary abuse of discretion in the initial planning decision."

Hence, "considered as a whole, it appears plain that section 830.6 was intended to avoid second-guessing the initial design decision adopted by an employee vested with authority to approve it, except to the extent the Court determines that the employee's approval of the design was unreasonable. It is at the reasonableness stage that the Court would consider whether an employee, in either knowingly or unknowingly approving a design that deviates from applicable standards, adopted a design that a 'reasonable legislative body or other body or employee could have approved.'"

Sheppard, Mullin, Richter & Hampton, LLP v. J-M Manufacturing

(2016) _ Cal.App.4th __ (2d Dist., Div. 4.)

Who needs to know about this case: (1) All lawyers; (2) lawyers seeking to overturn an arbitration award.

Why it's important: (1) Holds that Sheppard, Mullin's conflict-waiver provision was void, rendering the firm's representation of two clients with adverse interests a violation of Rule 3-310. (2) This violation rendered the entire contract between the firm and client unenforceable. (3) Under the California Arbitration Act, the enforceability of the contract was an issue for a court to decide; not an arbitrator. (4) The court held that the arbitrator erred in finding in favor of Sheppard Mullin, and that because its contract violated Rule 3-310, the firm was not allowed to charge the client for any fees, meaning it stood to refund $1.3 million in fees to the client.

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Synopsis: J-M manufactured PVC pipe. In 2006, a qui tam action was initiated against it on behalf of roughly 200 real parties in interest. J-M retained Sheppard, Mullin to defend it. The firm represented J-M for sixteen months, billing about 10,000 hours, generating fees of $3.8 million. Before the firm was retained, its conflicts check showed that one of its partners represented South Tahoe Public Utilities District (South Tahoe), one of the qui-tam plaintiffs, on unrelated labor-and-employment matters. Upon this discovery, Sheppard, Mullin drafted a conflict-waiver provision that it inserted in its retainer agreement with J-M. The provision did not inform J-M about the concurrent representation, nor did the firm provide that information independently of the retainer.

South Tahoe raised the conflict issue in the qui-tam case and moved to disqualify Sheppard, Mullin. The firm offered South Tahoe free services and payment of $250,000 in exchange for a conflict waiver, but South Tahoe declined, and the trial court disqualified Sheppard Mullin. The firm later sued J-M to recover $1.3 million in unpaid fees. The case was sent to arbitration based on an arbitration clause in the Sheppard, Mullin retainer agreement. A 3-arbitrator panel ruled in favor of Sheppard, Mullin and ordered J-M to pay $1.2 million, plus interest. The trial court confirmed the award, and J-M appealed. Reversed.

(1.) Sheppard, Mullin's fee agreement said that the agreement would be governed by California law. Hence, the California Arbitration Act (CAA), and not the Federal Arbitration Act (FAA) would govern. This is significant, because under the CAA, unlike the FAA, the issue of the contract's validity as a whole is determined by the trial court, not the arbitrator. Here, J-M challenged the validity of the entire retainer agreement based on the claimed violation of Rule 3-310.

(2.) Rule 3-310(C)(3) states that an attorney "shall not, without the informed written consent of each client ... [r]epresent a client in a matter and at the same time in a separate matter accept as a client a person or entity whose interest in the first matter is adverse to the client in the first matter. "'Informed written consent' means the client's ... written agreement to the representation following written disclosure." (Rule 3-310(A)(2).)

Here, because Sheppard, Mullin failed to fully disclose to J-M that it was concurrently representing South Tahoe, a plaintiff in the qui-tam action against J-M, the "boilerplate" conflict waiver that Sheppard, Mullin had inserted in its retainer agreement was unenforceable because there had been no "informed" consent to waive any conflict.

(3.) Sheppard, Mullin's violation of Rule 3-310 rendered its retainer agreement with J-M unenforceable.

A contract in violation of Rule 3-310(C) is against the public interest. Rule 3-310 and conflict of interest rules are designed to assure the attorney's absolute and undivided loyalty and commitment to the client and the protection of client confidences. The primary value at stake in cases of simultaneous or dual representation is the attorney's duty – and the client's legitimate expectation – of loyalty, rather than confidentiality. "A client who learns that his or her lawyer is also representing a litigation adversary, even with respect to a matter wholly unrelated to the one for which counsel was retained, cannot long be expected to sustain the level of confidence and trust in counsel that is one of the foundations of the professional relationship." (*Flatt v. Superior Court* (1994) 9 Cal.4th 275, 285. "Sheppard Mullin breached this essential basis for trust and security as to both J-M and South Tahoe."

The attorney's duty of undivided loyalty that forms the basis of Rule 3-310 constitutes the very foundation of an attorney-client relationship. The firm's retainer agreement with J-M, which violated Rule 3-310(C), therefore violated an expression of public policy. The trial court erred in holding that the agreement was valid and enforceable.

(4.) Because its agreement with J-M violated Rule 3-310, Sheppard, Mullin was not entitled to any fees for its representation of J-M under the contract – nor to any recovery in quantum meruit.

California cases have drawn a line between cases involving serious ethical violations such as conflicts of interest, in which compensation is prohibited, and technical violations or potential conflicts, in which compensation may be allowed.

> The conflict here pervaded the entire relationship between Sheppard Mullin and J-M. Even if, as Sheppard Mullin argues, it was not working for South Tahoe at the time the Agreement was signed, it nonetheless began working for South Tahoe three weeks later, thereby representing adverse clients without telling either client about the actual conflict. The violation caused Sheppard Mullin to be disqualified from representing J-M in the Qui Tam Action – the very purpose for which J-M had hired it. It is clear, therefore, that Sheppard Mullin's ethical breach went to the very heart of its relationship with J-M.

Hence, Sheppard, Mullin was not entitled to any fees for its work for J-M. This is so even if J-M suffered no actual damages. And it would defeat the finding that the firm's violation of Rule 3-310 violated public policy to allow it to nevertheless recover its fees on a quantum meruit theory. J-M therefore is entitled to recover any fees it paid Sheppard, Mullin once the actual conflict began.



Ehrlich

Jeffrey I. Ehrlich is the principal of the Ehrlich Law Firm, *with offices in Encino and Claremont, California. He is a cum laude graduate of the Harvard Law School, a certified appellate specialist by the California Board of Legal Specialization, and a member of the CAALA Board of Governors. He is the editor-in-chief of Advocate magazine.*

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