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New Ninth Circuit Decision May Make It Easier For Participants To Challenge ERISA Benefit Denials

When a claim for benefits from an ERISA plan is denied, the participant has the right to sue the plan in federal court to overturn the denial. A significant issue in any such court action is what – if any – deference should the court give the plan administrator's decision to deny the claim. The best result for the plan is an "abuse of discretion" standard. The best result for the plan participant is a *de novo* review, which means the court will review every fact and decide whether it would have made the same decision.

Named for the case in which the abuse of discretion standard was best explained, most plans include so-called *Firestone* language which gives the plan administrator broad discretion to consider claims. The general rule is that where the plan includes *Firestone* language, the court will apply the abuse of discretion standard of review.

To counter this difficult standard or review, ERISA benefit claimants have argued that various circumstances require application of a *de novo* standard of review notwithstanding the plan's inclusion of *Firestone* language. One such circumstance arises when a conflict of interest potentially influences the plan administrator's judgment. Where such a conflict exists, some courts have concluded that the administrator is not be entitled to discretion and have applied the *de novo* standard.

One type of conflict of interest ERISA benefit claimants have argued is where the plan administrator is also the funding source of the plan. This may arise where the plan is insured, and the insurance company also serves as plan administrator with the discretion to deny claims. It may also arise in a self-funded plan, where the employer pays the benefits out of general assets and also serves as plan administrator in reviewing claims. Claimants argue that this dual role creates an inherent conflict because the administrator has a financial incentive to deny claims. This is known as a "structural conflict of interest."

A recent case in the Ninth Circuit (which hears ERISA cases from Montana, Idaho, Washington, Oregon, California, Nevada, Arizona, Alaska, and Hawaii), sheds new light on how a "structural conflict of interest" will affect the standard of review applied by courts in those states. The case is *Abatie v. Alta Health & Life Insurance Company*, and was decided August 15, 2006.

Before *Abatie*, the mere existence of a "structural conflict of interest" alone was insufficient in the Ninth Circuit to change the standard of review to *de novo*. Instead, Ninth Circuit cases engaged in a burden shifting approach. To obtain a *de novo* standard of review, the claimant first had the burden of proving "material, probative evidence beyond the mere fact of the apparent conflict, tending to show that the fiduciary's self-interest caused a breach of the administrator's fiduciary obligations to the beneficiary." *Atwood v. Newmont Gold Co.*, 45 F.3d 1317, 1323 (9th Cir. 1995). Upon such a showing, the burden shifted to the plan administrator to prove that the conflict did not affect the decision to deny benefits. If the administrator could not meet this burden, then the *de novo* standard would apply.

Under the burden-shifting approach, it was relatively difficult for claimants to meet their initial burden of proving additional evidence of a breach of fiduciary duty. As a result, plan administrators

were more likely to be favored with an abuse of discretion standard of review. In the new *Abatie* case, however, the Ninth Circuit has rejected the burden-shifting approach in favor of a more claimant-favorable approach. *Abatie* directs that district courts consider the nature and extent of the conflict as a factor to determine whether the administrator abused its discretion:

> A district court, when faced with the facts and circumstances, must decide in each case how much or how little to credit the plan administrator's reason for denying insurance coverage. An egregious conflict may weigh more heavily (that is, may cause the court to find an abuse of discretion more readily) than a minor, technical conflict might.

Characterized another way, the district court should exercise an appropriate degree of skepticism, depending upon the nature of the conflict.

> The level of skepticism with which a court views a conflicted administrator's decision may be low if a structural conflict of interest is unaccompanied, for example, by any evidence of malice, of self-dealing, or of a parsimonious claims-granting history. A court may weight a conflict more heavily if, for example, the administrator provides inconsistent reasons for denial.

The *Abatie* standard essentially follows the "sliding scale" approach used by other circuits, though the Ninth Circuit expressly rejected that label for the new standard.

Based on the *Abatie* examples, the easiest way for a claimant to prove an "egregious conflict" would likely be to show that the administrator provided "inconsistent reasons for denial." Administrators should expect this argument whenever its communications to a claimant are susceptible to more than one interpretation. As a result, administrators should be vigilant to ensure that their reasons for denial are complete and consistent with previous communications. Without the formal burden-shifting approach that pre-dated *Abatie*, even minor inconsistencies may receive some weight by district courts.

The practical effect of *Abatie* will be that administrators defending ERISA denial-of-benefits claims can expect somewhat more extensive discovery in litigation. In denial-of-benefits claims, the only evidence relevant to the merits of the case is nearly always contained in the administrative record. As a result, district courts often limit discovery to the administrative record. Discovery beyond the administrative record is proper, however, if it is probative of issues affecting the standard of review.

Before *Abatie*, claimants often did not seek discovery beyond the administrative record because their burden was so high. Following *Abatie*, administrators should expect standard discovery requests seeking information beyond the administrative record, for the purpose of proving an "egregious conflict." Indeed, the *Abatie* Court expressly recognized that more extensive discovery may be required under the new system.

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