-- *N.J.L.J.* --
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ADVISORY COMMITTEE ON PROFESSIONAL ETHICS
Appointed by the Supreme Court of New Jersey

OPINION 727

ERISA-Governed Health Benefits Plans and Subrogation Agreements

The Advisory Committee on Professional Ethics received an inquiry from a lawyer who represents a plaintiff in a personal injury lawsuit arising from a motor vehicle accident. Plaintiff participated in a self-funded health benefits plan ("Plan") through his workplace. The Plan was established under the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 *U.S.C.A.* Section 1001 *et seq.* After the personal injury lawsuit was filed, the Plan requested that both plaintiff and his lawyer sign a subrogation agreement providing that the Plan will be reimbursed, from any settlement or judgment, for medical expenses it paid to the plaintiff.

Plaintiff's lawyer inquires whether he may, consistent with the *Rules of Professional Conduct*, "personally guarantee a client's failure to repay an asserted reimbursement interest out of the personal injury recovery obtained with the services of the attorney to the client's health insurance company." The Committee finds that a lawyer may not agree to personally guarantee a client's repayment of monies to the Plan, though a lawyer may agree to satisfy a valid lien out of funds in the lawyer's possession.

The subrogation agreement Inquirer presented to the Committee provides that the Plan will pay medical expenses to the participating employee but if the employee obtains compensation from an insurance company or other third party for his injuries, the employee must agree to repay the Plan the amount of benefits received from the recovery obtained. The agreement states that the Plan will have "a first lien and subrogation rights" on the amount recovered; the employee will notify the Plan on agreeing to any settlement; and the employee will not claim a deduction or setoff. The agreement further provides: "In the event the Recovery is paid to your attorney or other representative, such attorney or other representative shall be required to pay to the Plan the total amount of the Lien prior to disbursement of the Recovery to you or any other person or entity. Your attorney agrees to this by signing the attached Execution Sections." If both the employee and the lawyer do not sign the agreement, the Plan will not pay the employee any medical benefits.

As noted above, Inquirer states that he reads this agreement as requiring him to "personally guarantee a client's failure to repay an asserted reimbursement interest out of the personal injury recovery obtained with the services of the attorney." The agreement could also be viewed as requiring the lawyer to acknowledge and protect the Plan's lien and pay the required amount over to the Plan prior to disbursing monies to the client or other persons.

The Committee will not render opinions on substantive law or construe the subrogation agreement. The Committee notes, however, that ERISA preempts State law and federal courts interpret ERISA in a manner that promotes national uniformity. Several courts have reviewed subrogation provisions in ERISA-governed health benefits

plans and examined the role of the plaintiff's lawyer in protecting the plan's lien. Circuit courts have ruled that lawyers are subject to suit under ERISA for failing to turn over to the plan the portion of the recovery it claimed – regardless of whether the lawyer signed a subrogation agreement promising to protect the lien. Research has not disclosed any decision stating that a plan's subrogation agreement imposes on a lawyer a requirement to "personally guarantee" the client's performance or otherwise become a fiduciary to the plan.

Courts had previously held that an ERISA plan administrator could not obtain reimbursement from a lawyer who holds settlement funds subject to a subrogation claim unless the lawyer signed a contract with the plan. *See, e.g., Hotel Employees & Restaurant Employees Int'l Union Welfare Fund v. Gentner*, 50 *F.*3d 719 (9th Cir. 1995). This line of decisions was overturned by the United States Supreme Court's analysis in *Harris Trust and Savings Bank v. Salomon Smith Barney*, 530 *U.S.* 238, 120 *S.Ct.* 2180, 147 *L.Ed.* 2d 187 (2000). Now, a lawsuit can be sustained under ERISA against a lawyer who is not a signator to the plan under equitable principles of constructive trust. *Sereboff v. Mid Atlantic Medical Services, Inc.,* 547 *U.S.* 356, 126 *S.Ct.* 1869, 164 *L.Ed.* 2d 612 (2006); *Bombardier Aerospace Employee Welfare Benefits Plan v. Ferrer, Poirot and Wansbrough, 354 F.*3d 348 (5th Cir. 2003), *cert. den.* 541 *U.S.* 1072, 124 *S.Ct.* 2412, 158 *L.Ed.* 2d 981 (2004). Reimbursement to the plan can take priority over attorney's fees expended to obtain the recovery. *U.S. Airways, Inc. v. McCutchen*, __ *U.S.* __, 133 *S.Ct.* 1537, 185 *L.Ed.* 2d 654 (2013).

The ERISA plan administrator in *Bombardier* sought a constructive trust for monies held by the law firm after settlement of a personal injury action. The law firm

argued that it does not owe a fiduciary duty to the plan since it did not sign the subrogation agreement. The court found that the law firm is not a plan fiduciary though, pursuant to the Supreme Court's reasoning in *Harris Trust and Savings Bank*, *supra*, it can still be held liable to the plan pursuant to ERISA. *Id.* at 352.

Other Circuits have reached similar results. For example, in *The Longaberger Co. v. Kolt*, 586 *F.*3d 459 (6th Cir. 2009), the personal injury case settled for $135,000 and the plan asserted subrogation rights to medical payments of over $113,000. The lawyer took $45,000 of the settlement proceeds as attorney's fees; the remaining amount to be disbursed to the client was less than the amount the plan claimed. The plan document claimed full subrogation rights with no reduction for attorney's fees.

The lawyer argued that he was not a plan fiduciary and had not signed a contract with the plan so he cannot be held liable to the plan in the ERISA suit. The court disagreed, ruling that the plan could assert its lien over the portion of the monies that the lawyer had disbursed to himself as attorney's fees and impose a constructive trust under ERISA. *Id.* at 469. *See also Wal-Mart Stores, Inc., Associates' Health and Welfare Plan v. Wells*, 213 *F.*3d 398, 401 (7th Cir.), *cert. den.* 531 *U.S.* 985, 121 *S.Ct.* 441, 148 *L.Ed.* 2d 447 (2000) (a law firm that held settlement monies against which the plan asserted its lien is subject to a constructive trust in an ERISA action).

In *Southern Council of Industrial Workers v. Ford*, 83 *F.*3d 966 (8th Cir. 1996), the lawyer did not protect the lien and disbursed settlement monies to the client, who reimbursed to the plan only a portion of the amount it claimed. Both the lawyer and his client had signed a subrogation agreement with the plan. The plan brought suit. The

court decided that the lawyer is not a fiduciary of the plan and signing the subrogation agreement did not foist such fiduciary duties on him. *Id.* at 968.

Some plans, like the one presented to the Committee in this inquiry, condition continued payment of medical benefits to the plan participant on the lawyer's signature on the subrogation agreement. In *Kress v. Food Employers Labor Relations Ass'n*, 391 *F.*3d 563 (4th Cir. 2004), the lawyer refused to sign the subrogation agreement and the plan denied payment for medical expenses for both the plan participant and his family. Seeking reinstatement of medical coverage, the plan participant brought suit against the plan. The court found that the plan may, consistent with ERISA, condition the payment of medical benefits on a lawyer's signature on a subrogation agreement. *Id.* at 569-570. "Since circuit law interpreting ERISA plainly permits a plan to recoup any advance it has made to a participant before an attorney makes a claim on a subsequent award, we see no reason to impede a plan from requiring pre-commitment to this state of affairs." *Id.* at 569.

The lawyer further argued that the plan's claim to a share of his fees is unfair. The court disagreed:

> But this purported unfairness is nothing more than commonplace economic calculus. Attorneys considering taking a case on contingency commonly factor the likelihood of success and the magnitude of recovery into their decision. "Many tort claims involve considerable risk and insufficient reward. Attorneys, however, carefully screen these claims and reject a large portion, including most denominated as high risk." Lester Brickman, *The Market for Contingent Fee-Financed Tort Litigation: Is It Price Competitive?*, 25 *Cardozo L. Rev.* 65, 98 (2003). A given plan's subrogation rules obviously make the payment of fees more or less likely, and prudent attorneys would factor those rules into their calculus as well. If the participant and his attorney conclude that private litigation will not produce a sufficient recovery to make the litigation worthwhile, they need not bring the case. Often, however,

> an attorney might estimate that a jury award or settlement – with possible pain and suffering damages – will far exceed the amount to be reimbursed to a plan. This is the same calculation commonly made in non-ERISA contexts, but with one further factor to add to the equations.
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> [*Id.* at 570.]

The Committee previously considered lawyers' ethical obligations when a client seeks to assign a portion of recovery in a personal injury suit to a third-party factor. Opinion 691, 163 *N.J.L.J.* 220 (January 15, 2001). When a client obtains a loan from an outside entity that will be paid back from the client's portion of a personal injury settlement or judgment, the client's lawyer ordinarily is required to sign a contract acknowledging the lien and agreeing to forward that amount out of net proceeds directly to the lender. The Committee found nothing inherently unethical in this arrangement, provided the lender does not "seek to control the direction of the litigation" and the lawyer does not undertake "responsibilities to the factor which could in any way impair his or her duty of undivided fidelity to the client." *Id.*

Rule of Professional Conduct 1.15(b) requires that lawyers notify persons who have an interest in funds received by the lawyer and "promptly deliver" to those persons funds they are entitled to receive. A lawyer does not violate the *Rules of Professional Conduct* when he or she agrees to protect a valid lien, though a lawyer who knowingly disregards a legitimate claim by lienholders can be subject to discipline.

As noted above, the Committee will not construe the subrogation agreement. If the subrogation agreement at issue here requires the lawyer to personally guarantee the client's repayment to the Plan out of monies disbursed to the client by the lawyer, then ethical issues arise. *Rule of Professional Conduct* 1.8(e) prohibits a lawyer from

providing financial assistance to a client in connection with pending or contemplated litigation; a personal guarantee is considered improper financial assistance to a client. *See* Opinion 719, 202 *N.J.L.J.* 997 (December 13, 2010). If, however, the agreement requires the lawyer to acknowledge the lien and satisfy it out of funds in the lawyer's possession, and the plan does not attempt to control the direction of the litigation or otherwise interfere with the lawyer's duties to the client, ethical issues do not arise.