

June 12, 2000

COURT REINS IN SUITS UNDER FEDERAL PENSION LAW

(*Pegram v. Herdrich*, No. 98-1949)

The U.S. Supreme Court today issued a decision that should go a long way toward reining in the continuing expansion of civil lawsuits brought under the Employee Retirement Income Security Act of 1974 (ERISA), the federal pension law.

ERISA permits an individual to sue fiduciaries under an employee benefits plan whenever they violate their fiduciary duties to the plan. Overturning the lower-court decision in the case, the Supreme Court unanimously held that Health Maintenance Organizations ("HMOs") and their physicians are not acting as health plan fiduciaries when they decide what form of medical treatment to provide to plan members, and thus that such treatment decisions are not subject to ERISA suits.

The Court's decision in *Pegram v. Herdrich* was a victory for the Washington Legal Foundation (WLF), which had filed a brief urging that the plaintiff's ERISA claims be rejected. WLF argued that the decision in the lower court threatened to undermine health care in this nation by allowing a patient to sue his health care provider under ERISA any time the provider took into account cost considerations when deciding how to treat the patient.

The case involved an Illinois woman whose doctor (in a decision designed to reduce costs) delayed performing tests that would have revealed appendicitis. Her appendix burst before the tests were performed, and the woman was hospitalized for several days with peritonitis. The woman then filed a medical malpractice claim under Illinois state law; that suit has been concluded with the payment of a \$25,000 judgment against the doctor.

The issue before the Supreme Court was whether the Plaintiff should *also* be permitted to file an ERISA suit against her HMO and the doctor, based on a claim that they violated their fiduciary duties under ERISA to act in her best interests. The Plaintiff claimed that ERISA prohibits any employer-financed health care plan from providing financial incentives to their doctors to reduce the costs of services rendered. In this case, the HMO had agreed to pay the doctor who treated the Plaintiff a bonus if the plan maintained profitability by containing the aggregate cost of treating patients enrolled in

the health care plan.

The U.S. Court of Appeals for the Seventh Circuit in Chicago held that both health care plans and their doctors owe a fiduciary duty under ERISA to act solely in the best interests of their health plan members when making medical treatment decisions. The appeals court said that health care plans and doctors breach that duty when they create financial incentives that could cause doctors to provide sub-optimal care in order to save costs.

In reversing that decision, the Supreme Court agreed with WLF that HMOs could not survive if they were not permitted to take steps to control health care costs. The Court held that Congress has consistently supported the HMO model and thus could not have intended to drive HMOs out of business by permitting breach-of-duty suits every time that HMOs take cost into account in making treatment decisions.

"The number one problem in health care today is finding ways to hold down costs so that quality health care will continue to be affordable to all Americans," said WLF Chief Counsel Richard Samp after reviewing the Court's decision. "The Supreme Court's decision supports that effort by absolving HMOs from liability for adopting cost-containment measures. One of the principal purposes of HMOs and other forms of managed care is to contain costs by ensuring that unnecessary tests and procedures are not performed; but unless health plans are permitted to reward physicians who are successful in controlling costs, costs will never be contained. The result will be to make quality health care unaffordable to an increasing percentage of the population," Samp said.

WLF argued in its brief that ERISA imposes a fiduciary duty on HMOs to deal fairly with plan members when deciding whether to pay for particular medical services. But the initial decision regarding the appropriate level of medical care is not subject to regulation under ERISA, WLF argued; rather, such decisions are made by treating physicians and are subject to review under state tort law.

WLF is a public interest law and policy center with supporters in all 50 states. It devotes a significant portion of its resources to promoting civil justice reform, including efforts to rein in overly expansive theories of tort liability. WLF filed its brief in November 1999 with the pro bono assistance of Lonie A. Hassel and William Hanrahan of the Groom Law Group, Chartered, a Washington, D.C. law firm. WLF also filed a brief in the case in July 1999, urging the Supreme Court to review the case. The Supreme Court agreed to do so in September 1999.

* * *

For further information, contact WLF Chief Counsel Richard Samp at (202) 588-0302.