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'Plan Documents Rule' Yields Opposing Results When Applied to Disputing Beneficiaries

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March 8, 2013 — The "plan documents rule" provides that a state law judgment — other than a properly qualified domestic relations order — cannot override contrary beneficiary designation terms of an ERISA-covered employee benefit plan. Yet two recent court decisions demonstrate how difficult it can be in practice to enforce this seemingly simple rule.

In the first case, involving pension benefits, the court found that a participant's beneficiary designation under the terms of an ERISA plan trumps contrary language in a divorce decree. However, the court imposed a constructive trust on the benefit payment to bring about the intent of the state law decree. A constructive trust is a legal device used to distinguish property possession and property ownership. Although a person may possess certain property, a court can "construct" a trust around that property, which means that the possessor only holds the property, in trust, for the rightful owner. The court then determines the rightful owner by applying equitable principles.

In a second case, involving life insurance benefits, the court also applied the plan documents rule to find that a beneficiary designation under the terms of the plan could not be overridden by a state law decree. This court refused to impose a constructive trust and concluded that, in the absence of a valid QDRO assigning the life insurance proceeds, the plan documents control and designate the proper beneficiary.

Court Finds ERISA Beneficiary Designation Trumps Divorce Decree

Clear plan language — and beneficiary designations consistent with that language — generally cannot be overridden by contrary divorce terms that attempt to assign or alienate a plan benefit. As introduced above, this is sometimes referred to as the plan document rule. Some courts, however, have allowed a divorce decree to override a beneficiary designation and the plan document rule. Recently, a court acknowledged that it was bound to follow the plan document rule, but invoked equity to achieve the divorce decree's intent.

The facts

The facts in *Board of Trustees of the Indiana State Council of Plasters & Cement Masons Pension Fund v. Sheline*, 2013 WL 408812 (W.D. Mich. Jan 31, 2013), are predictable. Husband Gary designates his then-wife, Carol, as the beneficiary of his pension benefit from an ERISA-covered pension plan. Gary and Carol divorce, and a Michigan state court enters a judgment of divorce decreeing that Gary's pension is his "sole and separate property, free and clear of any and all claims" of Carol. Although not stated in the facts of the case, it does not appear that the judgment of divorce was ever submitted to the plan as a QDRO.

Following his divorce from Carol, Gary then marries Linda, and subsequently dies without ever having changed his beneficiary designation under the plan from Carol to Linda. Facing competing claims for the pension benefit, the plan files an interpleader action (a procedural device that brings all contending parties before the court to determine the proper benefit recipient) in federal court asking the U.S. District Court for the Western District of Michigan to determine to whom the pension benefit should be paid. Linda filed a claim in the interpleader action against Carol, asking the court to award Linda, as representative of Gary's estate, the pension benefit.

The decision

On cross-motions for summary judgment, the court was compelled to follow the established principle articulated at least twice by the 6th U.S. Circuit Court of Appeals (and many other courts) that plan documents trump any contrary language in the divorce decree. In fact, Linda conceded this point in her motion for summary judgment. Consequently, the plan in this case must pay the pension benefit to Carol, the properly designated beneficiary under the terms of the plan. It's the "what comes next" that makes this case noteworthy for the purposes of assigning plan benefits.

The court also found that although Carol had a right to *receive* the pension benefit under ERISA, her right to *retain* that benefit was not subject to ERISA. Once the benefit has been paid from the ERISA-covered plan, the right to retain that payment can be waived, subjecting the benefit proceeds to a constructive trust. Under a court-imposed constructive trust, while the person receiving the benefit payment may have physical custody of the property, the ownership interest of that property may be waived.

As a matter of Michigan state law, and consistent with two prior cases heard by the U.S. District Court for the Eastern District of Michigan, the court found that Carol's waiver of her right to retain the amount of Gary's pension benefit mentioned in the divorce decree "was explicit and is enforceable under Michigan Law." As a result, the court ordered the plan to pay the pension benefit to Carol.

However, because Carol waived her right to retain the benefit, "equity requires the Court to also order Carol, upon receipt of the Pension Fund benefits, to promptly pay an amount equal to those benefits to [Linda], as representative of Gary's estate." Further, the court order explicitly discharged the plan from all further liability to Linda and Carol upon payment to Carol.

Analysis

In this case, the court uses its powers to fashion a remedy that respects, at least initially, the plan document rule but ultimately finds a result that respects the parties' intent as expressed by the divorce decree, despite the plan's provisions. Imposing a constructive trust as a judicially created exception to the anti-alienation provisions of ERISA may achieve an equitable result, but the rule it creates also may undermine the principles and policies of ERISA's anti-alienation provisions.

If *Sheline* embodies the proposition that unqualified DROs, if valid under state law, can be recognized in federal court, plans will be forced more frequently to file interpleader actions when faced with disputing beneficiaries. These cases will require judicial intervention, because plan administrators should not be in the position of determining state law issues and do not have the power to invoke constructive trusts. Plans cannot simply ignore unqualified divorce decrees they receive or of which they become aware.

Court Enforces Welfare Plan's Beneficiary Designation Provisions over Divorce Decree

In a case with facts similar to *Sheline,* but relevant to welfare benefits, the court reached an opposite decision, finding that the ERISA plan's beneficiary designation provisions cannot be overridden by the contrary terms of state court judgments dissolving a marriage. In the absence of a valid QDRO creating an alternate payee for the life insurance benefit, the court declined to impose a constructive trust and ordered the benefit to be paid in accordance with the plan's beneficiary provisions.

The facts

The employer in *Metropolitan Life Insurance Co. v. McCray,* 2013 WL 398791 (E.D. Mo. 2013), sponsored an ERISA-covered welfare benefit plan that provided death benefits to its employees' beneficiaries. The plan was funded by a life insurance contract from MetLife. Participant Johnny McCray was married to, and then divorced from, Lizzie McCray. The terms of the divorce decree required Johnny to maintain Lizzie as the beneficiary of his death benefit from the plan, which he did not do. Johnny then married Aza Reed and subsequently died. Lizzie and Aza both claimed the death benefit from MetLife, and MetLife filed an interpleader action asking the U.S. District Court for the Eastern District of Missouri to determine the proper recipient of the benefit.

The decision

The court applied the plan documents rule and found that the provisions of the ERISA plan governing the appropriate beneficiary of the death benefit win out over the contrary provisions in the divorce decree. Although the parties disputed the facts surrounding the beneficiary designation, the court found that under either version of the facts, the plan document provided that the participant's spouse on his date of death was the beneficiary. This meant that Aza was entitled to the death benefit.

First, the court found that ERISA expressly preempts the assignment of benefits provisions in this divorce decree. Second, the court found that the divorce decree could not be considered a QDRO because the decree did not clearly specify the welfare benefit plan to which the DRO applies, as required under ERISA Section 206(d)(3)(C). Third, the court declined to impose a constructive trust on the death benefit because "[a]pplying state equitable doctrines under these circumstances would be inconsistent with ERISA's preemptive force and its explicit statutory commands."

Analysis

The result in *McCray* is curious because the court applies the QDRO rules to a welfare benefit plan The QDRO rules are a statutory exception to the anti-alienation provision of ERISA, which applies only to pension benefits, not welfare benefits. A welfare plan beneficiary may assign benefit proceeds to some other party; therefore there is no ERISA provision that would preempt the state divorce decree.

Nevertheless, some courts have applied the QDRO rules to welfare benefits before. This could explain why the divorce decree at issue in *McCray* did not clearly specify the welfare benefit plan. The court's decision enforces the plan documents rule for a welfare benefit plan, and underscores the point that a plan may need court assistance to extricate itself from a beneficiary dispute and avoid double payment.

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