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Second Circuit Holds Taft-Hartley Funds Are Inherently Conflicted, Potentially Affects Outcome and Scope of Future Benefit Claims Litigation

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On June 24, 2010, the U.S. Court of Appeals for the Second Circuit held, in *Durakovic v. Building Service 32 BJ Pension Fund*, 2010 WL 2519645 (2d Cir. 2010), that Taft-Hartley funds (administered by boards of trustees consisting of an equal number of union and employer representatives) are inherently conflicted when making benefit determinations, and that this conflict needs to be considered by federal district courts when reviewing plan determinations under an arbitrary and capricious standard of review. The decision could potentially lead to significantly increased risks of liability and litigation costs for Taft-Hartley funds.

Background

In *Metropolitan Life Insurance Co. v. Glenn*, 128 S. Ct. 2343 (2008), the Supreme Court held that the structural conflict affecting insurance companies that both decide and pay claims for benefits is a factor for courts to weigh in determining whether an insurance company abused its discretion in denying a claim for benefits, but does not modify the arbitrary and capricious standard of review that ordinarily applies to such determinations. The *Glenn* decision established a two-step analysis for courts that are asked to review claims determinations. The first step is to determine whether a structural conflict exists because the administrator both evaluates claims for benefits and pays for them. If so, the court then goes on to determine how much weight the conflict should be afforded in determining whether the administrator abused its discretion in denying the claim. The decision provided no specific guidance, however, as to how this standard should apply to Taft-Hartley plans.

The Second Circuit's Decision

In *Durakovic*, a long-time office cleaner who suffered chronic pain and weakness in the years following a 1999 automobile accident applied for disability benefits from her union-sponsored plans. The plans provided benefits to those deemed totally and permanently unable to engage in any further employment for which the applicant was vocationally qualified. After consideration of a report from the Social Security Administration, two reports from Durakovic's treating physician and two reports from independent physicians, the plans' Board of Trustees denied Durakovic's claim and appeal. Durakovic subsequently filed suit in federal district court challenging the funds' decision.

On appeal, neither party disputed that the challenged decision was subject to an arbitrary and capricious standard of review by the court, since the plan documents accorded the Board of Trustees with the discretion to make benefit determinations. Both parties challenged, however, the district court's decision that "the Funds' conflict [was] a factor, albeit a relatively unimportant one." The plans argued that they were not conflicted within the meaning of *Glenn* because Taft-Hartley funds are administered by an entity composed equally of union and employer representatives. Durakovic argued that the conflict should have been accorded more weight.

The Second Circuit first concluded that a structural conflict exists for all Taft Hartley funds. In so holding, the Court reasoned that while the employer representatives on the Board of Trustees have fiduciary interests that weigh in favor of the trusts' beneficiaries they also have representational and other interests that weigh to the contrary, *i.e.*, the rejection of claims will reduce future employer contributions. According to the court: "That the board is . . . evenly balanced between union and employer does not negate the conflict . . . And that the administrator is here a trust, rather than the employer itself or a third-party for-profit institution, does not control."

The Second Circuit acknowledged that its finding of an inherent conflict was at odds with the view of the Ninth Circuit, which held in *Anderson v. Suburban Teamsters of N. Ill. Pension Fund Bd. of Trs.*, 588 F.3d 641, 648 (9th Cir. 2009) that a Taft-Hartley fund is not conflicted within the meaning of *Glenn* because it is a multi-employer trust in which the trustees do not have a personal interest and evaluations are made by a balanced board of trustees. The Second Circuit found that the Ninth Circuit's decision rested on a "shaky foundation."

Having concluded that a conflict existed, the Second Circuit next determined that the Board of Trustees' decision was "unsupported by substantial evidence, and therefore arbitrary and capricious," because it did not afford Durakovic's treating physician reports sufficient weight and the plans' independent report inappropriately concluded that Durakovic was vocationally qualified for three occupations. It therefore reversed the district court's judgment and granted summary judgment in favor of the Durakovic. The Court did not explain whether its ruling was directly justified by its finding with respect to the plans.

Implications

The Second Circuit's conclusion that all Taft Hartley funds suffer from an inherent conflict may result in increased litigation costs as there may be a more frequent effort by the plaintiffs' bar to conduct discovery into the extent to which the inherent conflict influenced a benefit determination. Whether or not the outcome of these claims will ultimately be affected remains to be seen, however. Notwithstanding the requirement that district court's treat Taft Hartley plans as inherently conflicted, the district courts retain the discretion as to how much weight to accord the conflict.

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