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ERISA Litigation Pitfalls — The “Deemed Exhausted” Rule And Its Strict Compliance Standard



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One of the most widely used defenses in ERISA litigation is a plaintiff's failure to exhaust his or her administrative remedies. Although defendants often obtain early dismissal for failure to exhaust administrative remedies, there is a significant statutory pitfall that ERISA defendants must be aware of. This provision, known as the “deemed exhausted” rule, states that a plaintiff's administrative remedies will be deemed exhausted if the plan has failed to establish or follow certain claims procedures set forth in the rule. 29 C.F.R. § 2560.503-1(l)(1).

The “deemed exhausted” rule, states: “In the case of the failure of a plan to establish or follow claims procedures consistent with the requirements of this section, a claimant shall be deemed to have exhausted the administrative remedies available under the plan and shall be entitled to pursue any available remedies under section 502(a) of the Act on the basis that the plan has failed to provide a reasonable claims procedure that would yield a decision on the merits of the claim.”

Generally speaking, the purpose of 29 C.F.R. § 2560.503-1 is to establish minimum requirements for employee benefit plans with respect to claims for benefits by participants and beneficiaries. Some of the most important claims procedures in 29 C.F.R. § 2560.503-1 that must be established and followed include detailed requirements concerning the manner and content of notification of benefit determinations, and benefit determinations on review. 29 C.F.R. § 2560.503-1(g),(j). Also important are the requirements for the timing of notification of benefit determinations, and benefit determinations on review, 29 C.F.R. § 2560.503-1(f),(i), as well as the requirements for appeals of adverse benefit determinations. 29 C.F.R. § 2560.503-1(h). The rule also

contains more general requirements for the establishment and maintenance of reasonable claims procedures that must be adhered to. 29 C.F.R. § 2560.503-1(b)-(e).

The “deemed exhausted” rule seeks to implement a strict compliance standard, such that any failure to comply with all the requirements of 29 C.F.R. § 2560.503-1 will trigger the rule and prevent defendants from arguing exhaustion. However, courts have construed the “deemed exhausted” rule narrowly and have been reluctant to find that a technical or de minimus deficiency triggers the “deemed exhausted” rule, opting instead for a substantial compliance standard. For example, in *McCay v. Drummond Co., Inc.*, the Court found that even though a notice of denial of benefits did not fully comply with ERISA's technical requirements, the “deemed exhausted” rule was not triggered and exhaustion was not excused. 509 F. App'x 944, 947 (11th Cir. 2013). Citing to 29 C.F.R. § 2560.503-1(l), the *McCay* Court stated: “[W]e cannot say that the notice failed to provide a ‘reasonable claims procedure’ in this case since, as the record shows, McCay eventually was able to follow the appeals procedures”

Likewise, in *Holmes v. Colorado Coalition for the Homeless Long Term Disability Plan*, the Court held that even though the plan did not comply with various technical ERISA requirements, exhaustion was still required, notwithstanding 29 C.F.R. § 2560.503-1(l), because the claimant had a fair opportunity to follow the plan's appeals process and was not prejudiced by the deficiencies. 762 F.3d 1195, 1213-14 (10th Cir. 2014). In doing so, the Court determined that the “deemed exhausted” rule is only triggered when technical non-compliance prejudices a claimant's right to enjoy a reasonable claims procedure.

Other circuits have also rejected technical non-compliance with ERISA's requirements as a basis for

avoiding exhaustion, and require that a claimant follow a plan's appeals process to invoke 29 C.F.R. § 2560.503-1(l). *Schorsch v. Reliance Standard Life Ins. Co.*, 693 F.3d 734, 742 (7th Cir. 2012) (finding that 29 C.F.R. § 2560.503-1(l) does not apply to a claimant who does not attempt to follow a plan's administrative review process because the rule assumes that the claimant attempted to do so but was blocked by the lack of a reasonable claims procedure); *Chorosevic v. MetLife Choices*, 600 F.3d 934, 944 (8th Cir. 2010) (holding that claimant was required to exhaust administrative remedies, notwithstanding 29 C.F.R. § 2560.503-1(l), where "the ERISA plan's actions or omissions [did not] deprive the claimant of information or materials necessary to prepare for administrative review or for an appeal to federal courts").

In *Perrino v. Southern Bell Telephone & Telephone Co.*, the Eleventh Circuit explained why technical non-compliance with ERISA's requirements does not abrogate the exhaustion requirement, stating:

"Appellants argue that we should recognize a new exception to our exhaustion requirement; namely, that an employer's noncompliance with ERISA's technical requirements (for example, creating a summary plan description, or delineating a formal claims procedure) should excuse a plaintiff's duty to exhaust administrative remedies We find Appellants' arguments unpersuasive. After reviewing the relevant federal regulations and our prior precedent, we decline to create an exception to the exhaustion requirement in this case Our prior precedent makes clear that the exhaustion requirement for ERISA claims should not be excused for technical violations of ERISA regulations that do not deny plaintiffs meaningful access to an administrative remedy procedure through which they may receive an adequate remedy [I]t makes little sense to excuse plaintiffs from the exhaustion requirement where an employer is technically noncompliant with ERISA's procedural requirements but, as the district court determined in this case, the plaintiffs still had a fair and reasonable opportunity to pursue a claim through an administrative scheme prior to filing suit in federal court."

Although various appellate courts have narrowly interpreted 29 C.F.R. § 2560.503-1(l), others have taken a more expansive view, such as the Second Circuit in *Halo v. Yale Health Plan, Director of Benefits & Records Yale University*, 819 F.3d 42, 57 (2d Cir. 2016). The *Halo* court reasoned that courts "should be reluctant to disturb the regulatory scheme the Department has devised under authority expressly granted to it by Congress . . . [and] we reject the substantial compliance

doctrine because it is inconsistent with the Department's regulations." The Court went on to explain that the Department of Labor has acknowledged that, even under 29 C.F.R. § 2560.503-1(l), inadvertent and harmless deviations in the processing of a particular claim should not trigger the "deemed exhausted" rule as long as the plan has established procedures in full conformity with 29 C.F.R. 2560.503-1. *Id.* Thus, the Second Circuit concluded that a claim will be reviewed de novo, (as opposed to an arbitrary and capricious standard), unless the plan can show that it has established procedures in full conformity with 29 C.F.R. § 2560.503-1 and can demonstrate that its failure to comply with these requirements in processing a specific claim was inadvertent and harmless. *See also Spinedex Physical Therapy USA Inc. v. United Healthcare of Arizona, Inc.*, 770 F.3d 1282, 1299 (9th Cir. 2014) (adopting the Department of Labor's interpretation that anything more than a de minimis violation of the requirements in 29 C.F.R. § 2560.503-1 triggers the "deemed exhausted" rule).

Further, in cases where claimants are actually prejudiced by the absence of fair and reasonable claims procedures, courts find that the "deemed exhausted" rule has been triggered. *See, e.g., Eastman Kodak Co. v. STWB, Inc.*, 452 F.3d 215, 223 (2d Cir. 2006) (finding that plaintiff's claim was deemed exhausted where the plan had no claims procedure and only implemented a retroactive claims procedure after the plaintiff brought a lawsuit seeking benefits under the plan).

The takeaway is that an employee benefit plan's compliance with the claims procedures in 29 C.F.R. § 2560.503-1 is very important at the litigation stage. Therefore, it is critical to ensure that an employee benefit plans' claims procedures are fully compliant and consistently applied. However, in situations where there may be a lack of technical compliance with these requirements, there is a substantial body of case law that can support dismissal for failure to exhaust administrative remedies, notwithstanding the strict compliance standard set forth in 29 C.F.R. § 2560.503-1(l).

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