

No. 13-1773/13-1859

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IN THE UNITED STATES COURT OF APPEALS  
FOR THE SIXTH CIRCUIT

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HI-LEX CONTROLS INC., HI-LEX AMERICA, INC., AND THE  
HI-LEX CORPORATION HEALTH AND WELFARE PLAN,  
Plaintiffs-Appellees-Cross-Appellants,

v.

BLUE CROSS BLUE SHIELD OF MICHIGAN,  
Appellees.

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On Appeal from the United States District Court  
for the Eastern District of Michigan  
Southern Division  
No. 11-cv-12557

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BRIEF OF THE SECRETARY OF LABOR, THOMAS E. PEREZ, AS  
AMICUS CURIAE IN SUPPORT OF APPELLEES

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**TABLE OF CONTENTS**

|  | Page |
|--|------|
| TABLE OF AUTHORITIES .....   | iv   |
| THE SECRETARY'S INTEREST.....  | 1    |
| STATEMENT OF THE CASE.....   | 1    |
| I. Factual Background .....  | 1    |
| II. Procedural History .....   | 4    |
| SUMMARY OF THE ARGUMENT .....  | 7    |
| ARGUMENT .....   | 8    |
| I. The District Court Properly Construed And Applied The "Fraud or<br>Concealment" Provision In The Statute of Limitations ..... | 8    |
| A. "Fraud or Concealment" Applies to Either Fraud or<br>Concealment .....  | 8    |
| B. Blue Cross Engaged in Both Fraud and Concealment, as well<br>as Fraudulent Concealment.....                                   | 16   |
| C. The Secretary's Reading Comports with ERISA's Purpose .....   | 17   |
| D. Narrower Interpretations of Section 413 by Other Circuits are<br>Unpersuasive.....  | 19   |
| II. Blue Cross Acted As A Fiduciary When It Unilaterally Paid Itself the<br>Disputed Fees .....                                  | 20   |

**TABLE OF CONTENTS—(continued)**

|  | Page |
|--|------|
| III. The District Court Correctly Held That Blue Cross Breached Its Duty<br>By Misrepresenting or Concealing Material Facts And<br>By Engaging In Self-Dealing. .... | 29   |
| CONCLUSION ....  | 34   |
| CERTIFICATE OF COMPLIANCE  |      |
| CERTIFICATE OF SERVICE   |      |

**TABLE OF AUTHORITIES**

| Federal Cases:   | Page               |
|--|--------------------|
| <u>Bailey v. Glover</u> ,<br>88 U.S. (21 Wall) 342 (1984).....                         | 13, 14, 18         |
| <u>Barker v. Am. Mobil Power Corp.</u> ,<br>64 F.3d 1397 (9th Cir. 1995).....          | 19 n.6             |
| <u>Bates v. Preble</u> ,<br>151 U.S. 149 (1894) .....                                  | 13                 |
| <u>Becker v. Eastman Kodak Co.</u> ,<br>120 F.3d 5 (2d Cir. 1997) .....                | 30                 |
| <u>Bowerman v. Wal-Mart Stores, Inc.</u> ,<br>226 F.3d 574 (7th Cir. 2000).....        | 30                 |
| <u>Briscoe v. Fine</u> ,<br>444 F.3d 478 (6th Cir. 2006).....                          | 20, 21, 21 n.7, 22 |
| <u>Brown v. Owens Corning Inv. Review Comm.</u> ,<br>622 F.3d 564 (6th Cir. 2010)..... | 9 n.2              |
| <u>Bryan v. United States</u> ,<br>99 F.2d 549 (10th Cir. 1938).....                   | 14 n.5             |
| <u>Caputo v. Pfizer</u> ,<br>267 F.3d 181 (2nd Cir. 2001) .....                        | 6 & passim         |
| <u>Cataldo v. U.S. Steel Corp.</u> ,<br>676 F.3d 542 (6th Cir. 2012).....              | 9 n.2, 10, 19      |
| <u>Chao v. Crouse</u> ,<br>346 F.Supp.2d 975 (S.D. Ind. 2004) .....                    | 27                 |
| <u>Chao v. Day</u> ,<br>436 F.3d 234 (D.C. Cir. 2006).....                             | 28, 29             |

| Federal Cases-(continued):   | Page    |
|--|---------|
| <u>Chevron U.S.A., Inc.v. Natural Res. Def. Council, Inc.,</u><br>467 U.S. 837( 1984) .....  | 32 n.12 |
| <u>Chiarella v. United States,</u><br>445 U.S. 222 (1980) .....  | 11, 12  |
| <u>Connors v. Hallmark &amp; Son Coal Co.,</u><br>935 F.2d 336 (D.C.Cir. 1991)(Ginsburg J.) .....                                    | 20      |
| <u>Cutaiar v. Marshall,</u><br>590 F.2d 523 (3d Cir. 1979) .....   | 31      |
| <u>de la Fuente v. FDIC,</u><br>332 F.3d 1208 (9th Cir. 2003) .....  | 12 n.4  |
| <u>Dirks v. SEC,</u><br>463 U.S. 646 (1983) .....  | 12 n.3  |
| <u>Donovan v. Cunningham,</u><br>716 F.2d 1455 (5th Cir. 1983) .....   | 1       |
| <u>Dudenhoeffer v. Fifth Third Bancorp,</u><br>692 F.3d 410 (6th Cir. 2012), <u>pet. for cert. pending</u><br>No.12-751 (U.S.) ..... | 15, 30  |
| <u>East Jordan Plastics, Inc. v. Blue Cross and Blue Shield of Michigan,</u><br>2013 WL 1876117 (E.D. Mich. 2013) .....              | 16      |
| <u>Firestone Tire &amp; Rubber Co. v. Bruch,</u><br>489 U.S. 101 (1989) .....  | 14, 15  |
| <u>Freund v. Marshall &amp; Ilsley Bank,</u><br>485 F. Supp. 629 (W. D.Wisc. 1979) .....   | 32      |
| <u>GGNSC Springfield LLC v. NLRB,</u><br>721 F.3d 403 (6th Cir. 2013) .....  | 9       |

| Federal Cases-(continued):   | Page   |
|--|--------|
| <u>Griggs v. E.I. DuPont de Nemours &amp; Co.</u> ,<br>237 F.3d 371 (4th Cir. 2001) .....  | 30     |
| <u>Grindstaff v. Green</u> ,<br>133 F.3d 416 (6th Cir. 1998) .....   | 14     |
| <u>Guyan Int'l v. Prof'l Benefits Adm'rs, Inc.</u> ,<br>689 F.3d 798, 797-98 (6th Cir. 2012).....  | 23, 26 |
| <u>Harris Trust and Sav. Bank v. Salomon Smith Barney, Inc.</u> ,<br>530 U.S. 238 (2000) .....   | 9      |
| <u>Harte v. Bethlehem Steel Corp.</u> ,<br>214 F.3d 446 (3rd Cir. 2000).....   | 29     |
| <u>Holmberg v. Armbrecht</u> ,<br>327 U.S. 392 (1946) .....  | 13, 18 |
| <u>In re Carter</u> , 553 F.3d 979, 985 (6th Cir. 2009) .....  | 10     |
| <u>In re Halpin</u> ,<br>566 F.3d 286 (2d Cir. 2009) .....   | 25     |
| <u>In re Unisys "ERISA" Litig.</u> ,<br>242 F.3d 497 (3d Cir. 2010)(Mannsman, J., concurring in part<br>and concurring in the result)..... | 18     |
| <u>In re WorldCom Inc. "ERISA" Litig.</u> ,<br>263 F. Supp. 2d 745 (S.D.N.Y. 2003).....  | 29     |
| <u>J. Geils Band Emp. Benefit Plan v. Smith Barney</u> ,<br>76 F.3d 1245 (1st Cir. 1996) .....   | 19 n.6 |
| <u>Jamesbury Corp. v. Worcester Valve Co.</u> ,<br>443 F.2d 205 (1st Cir. 1971) .....  | 14 n.5 |
| <u>Krohn v. Huron Mem'l Hosp.</u> ,<br>173 F.3d 542 (6th Cir.1999) .....   | 30     |

| Federal Cases-(continued):  | Page           |
|---|----------------|
| <u>Kurz v. Philadelphia Elec. Co.</u> ,<br>96 F.3d 1544 (3rd Cir. 1996).....  | 19 n.6         |
| <u>Larson v. Northrop Corp.</u> ,<br>21 F.3d 1164 (D.C. Cir. 1994).....   | 19 n.6         |
| <u>Leigh v. Engle</u> ,<br>727 F. 2d 113 (7th Cir. 1984).....   | 31             |
| <u>Libbey-Owens-Ford Co. v. Blue Cross and Blue Shield Mut. of Ohio</u> ,<br>982 F.2d 1031 (6th Cir. 1993).....   | 26             |
| <u>Lockhart v. Napolitan</u> ,<br>573 F.3d 251 (6th Cir. 2009).....   | 10             |
| <u>Mass. Mut. Life Ins. Co. v. Russell</u> ,<br>473 U.S. 134 (1985) .....   | 31             |
| <u>McLemore v. Regions Bank</u> ,<br>682 F.3d 414 (6th Cir. 2012).....  | 21 n.7, 22 n.8 |
| <u>Med. Mut. of Ohio v. K. Amalia Enter., Inc.</u> ,<br>548 F.3d 383 (6th Cir. 2008).....   | 17             |
| <u>Merck &amp; Co., Inc. v. Reynolds</u> ,<br>559 U.S. 633 (2010) .....   | 18             |
| <u>Mertens v. Hewitt Assoc.</u> ,<br>508 U.S. 248 (1993) .....  | 14, 20         |
| <u>Metzler v. Solidarity of Labor Org. Health &amp; Welfare Fund</u> ,<br>1998 WL 477964 (S.D.N.Y. 1998) <u>aff'd sub nom</u><br><u>Herman v. Goldstein</u> , 224 F.3d 128 (2d Cir. 2000) ..... | 28             |
| <u>NLRB v. Edward G. Budd Mfg.,Co.</u> ,<br>169 F.2d 571(6th Cir. 1948).....  | 9              |

| Federal Cases-(continued):  | Page               |
|---|--------------------|
| <u>Patelco Credit Union v. Sahni,</u><br>262 F.3d 897 (9th Cir. 2001) .....   | 33                 |
| <u>Pinney Dock &amp; Transport Co. v. Penn Cent. Corp.,</u><br>838 F.2d 1445 (6th Cir. 1988) .....                          | 13, 14             |
| <u>Pipefitters Local 636 Ins. Fund v. Blue Cross and Blue Shield<br/>of Michigan,</u><br>722 F.3d 861 (6th Cir. 2013) ..... | 21, 21 n.7, 22, 23 |
| <u>Radiology Ctr. v. Stifel Nicolaus &amp; Co.,</u><br>919 F.2d 1216 . (7th Cir. 1990) .....                                | 19 n.6             |
| <u>Rutledge v. Boston Woven Hose &amp; Rubber Co.,</u><br>576 F.2d 248 (9th Cir. 1978) .....                                | 14 n.5             |
| <u>Schaefer v. Arkansas Med. Soc'y,</u><br>853 F.2d 1487 (8th Cir. 1988) .....  | 19, 19 n.6         |
| <u>Seaway Food Town, Inc. v. Med. Mutual of Ohio,</u><br>347 F.3d 610 (6th Cir. 2003) .....                                 | 22 n.8             |
| <u>SEC v. Cochran,</u><br>214 F.3d 1261 (10th Cir. 2000) .....  | 12 n.4             |
| <u>SEC v. Zandford,</u><br>535 U.S. 813 (2002) .....  | 12                 |
| <u>Smith v. Provident Bank,</u><br>170 F.3d 609 (6th Cir. 1999) .....   | 20, 21 n.7         |
| <u>Sprint Commc'ns Co., L.P. v. F.C.C.,</u><br>76 F.3d 1221 (D.C. Cir. 1996).....   | 14 n.5             |

| Federal Cases-(continued):   | Page   |
|--|--------|
| <u>State of Tex. v. Allan Const. Co., Inc.</u> ,<br>851 F.2d 1526 (5th Cir. 1988).....   | 14 n.5 |
| <u>Swanson v. Wilson</u> ,<br>423 Fed. Appx. 587 (6th Cir. 2011) .....   | 12     |
| <u>United States v. Brown</u> ,<br>79 F.3d 1550(11th Cir. 1996), <u>overruled on other grounds</u> ,<br><u>United States v, Svete</u> , 556 F.3d 1157 (11th Cir. 2009) (en banc) ..... | 12 n.4 |
| <u>United States v. Grizzle</u> ,<br>933 F.2d 943 (11th Cir. 1991).....  | 24     |
| <u>United States v. Hagan</u> ,,<br>521 U.S. 642 (1997) .....  | 12 n.4 |
| <u>United States v. Holzer</u> ,<br>816 F.2d 304(7th Cir.) <u>vacated</u><br>484 U.S. 807 (1987) .....   | 12 n.4 |
| <u>Varity Corp. v. Howe</u> ,<br>516 U.S. 489 (1996) .....   | 29, 30 |
| <u>Venture Global Eng'g, LLC v. Satyam Computer Servs. Ltd.</u> ,<br>730 F.3d 580 (6th Cir. 2013).....   | 14     |
| <u>Whitfield v. Tomasso</u> ,<br>682 F. Supp. 1287 (E.D.N.Y. 1988).....  | 33     |
| <br>Federal Statutes:  |        |
| <br>Employment Retirement Income Security Act of 1974, (Title I),<br>as amended, 29 U.S.C. § 1001 <u>et seq</u> :  |        |
| Section 2, 29 U.S.C. § 1001. ....  | 1      |

Section 3(21), 29 U.S.C. § 1002(21)..... 15

Federal Statutes-(continued): Page

Section 3(21)(A), 29 U.S.C. § 1002(21)(A)..... 20

Section 404(a), 29 U.S.C. § 1104(a) ..... 31

Section 404(a)(1), 29 U.S.C. § 1104(a)(1)..... 30

Section 404(a)(1)(A), 1104(a)(1)(A)..... 29

Section 404(a)(1)(B), 1104(a)(1)(B) ..... 29

Section 406(a), 29 U.S.C. § 1106(a) ..... 5

Section 406(b), 29 U.S.C. § 1106(b)..... 5, 31, 32 n.12, 33 n.13

Section 406(b)(1), 29 U.S.C. § 1106(b)(1)..... 5, 8, 31, 32

Section 408, 29 U.S.C. § 1108 ..... 33 n.13

Section 408(a), 29 U.S.C. § 1108(a) ..... 33 n.13

Section 408(b)(2), 29 U.S.C. § 1108(b)(2)..... 5, 32, 32 n.12

Section 413, 29 U.S.C. § 1113 ..... 6, 7, 8, 9, 10

Section 502(a), 29 U.S.C. § 1132(a) ..... 1

Federal Regulations: Page

29 C.F.R. § 2510.3-101..... 25

29 C.F.R. § 2510.3-102..... 25

29 C.F.R. § 2510.3-102(a)(1)..... 24

29 CFR § 2550.408b-2(e) ..... 32

29 C.F.R. § 2550.408b-2(e)(1)..... 12, 32 n.12

Miscellaneous:

|  |                    |
|--|--------------------|
| F.R.A.P. 29(a) .....   | 1                  |
| S. Rep. No. 93-127 (1973),<br>U.S.C.C.A.N. 1974, 4639, 4865 .....  | 14                 |
| PWBA Information Letter to Narrvel E. Hall,<br>1993 WL 137025, (April 30, 1993).....                     | 28                 |
| McCormick Letter, 1994 WL 707770 (DOL, August 11, 1994).....   | 28 n.11            |
| U. S. Dep't of Labor Field Assistance Bulletin No. 2002-3,<br>2002 WL 32502487 (EBSA Nov. 5, 2002) ..... | 28 n.11            |
| 92-24A, DOL Adv. Op. ,<br>1992 WL 337539 (Nov. 6, 1992) .....  | 24, 25, 25 n.9, 26 |
| 93-14A, DOL Adv. Op.(May 5, 1993) .....  | 25                 |
| 94-31A, DOL Adv. Op.(Sept. 9, 1994) .....  | 26                 |
| Restatement (Second) of Trusts § 173, cmt. d (1973) .....  | 30                 |
| <u>Black's Law Dictionary</u> 788 (rev. 4th ed. 1968) .....  | 11                 |

## THE SECRETARY'S INTEREST

The Secretary of Labor is charged with interpreting and enforcing the provisions of Title I of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended, 29 U.S.C. § 1001 et seq. Civil actions brought by fiduciaries, participants, and beneficiaries under 29 U.S.C. § 1132(a) to remedy fiduciary breaches are essential means of enforcing Title I of ERISA. The Secretary therefore has a strong interest in the interpretation of ERISA's statute of limitations provisions as they apply in private actions and could be applied to the Secretary's own enforcement actions. Likewise, the Secretary has a strong interest in ensuring that those who control plan assets are subject to ERISA's strict fiduciary obligations. See Donovan v. Cunningham, 716 F.2d 1455, 1462-63 (5th Cir. 1983).

The Secretary files this amicus brief pursuant to Federal Rule of Appellate Procedure 29(a).

## STATEMENT OF THE CASE

### I. Factual Background

This case involves fees ("Disputed Fees") that Defendant-Appellant Blue Cross Blue Shield of Michigan allocated to itself as additional compensation for its administration of an ERISA health plan sponsored and administered by Plaintiff-Appellee Hi-Lex Controls Incorporated. RE 246, Findings of Fact and

Conclusions of Law ("FFCL"), PageID# 15413. Hi-Lex alleges that Blue Cross acted fraudulently by falsely stating that the Disputed Fees were charges for medical services to be paid to hospitals. In fact, Blue Cross pocketed a portion of these payments as fees to itself, not hospitals, from assets of the plan that it controlled without authorization from Hi-Lex. RE1, Complaint, PageID# 6. As the third-party administrator of Hi-Lex's self-insured health plan (the "Plan") since at least 1991, Blue Cross was responsible for processing and paying employee health claims and negotiating with hospitals and health care providers. RE 246, FFCL, PageID# 15413-15. Hi-Lex entered into Administrative Service Contracts with Blue Cross, renewing the contracts each year. Id. Under the contracts, Hi-Lex paid Blue Cross a monthly per-capita administrative fee, and Blue Cross agreed to pay covered health care claims on behalf of Hi-Lex out of a Blue Cross-controlled account to which Hi-Lex deposited money for this purpose. Id., PageID# 15415-16.

Hi-Lex sent money via weekly wire transfer, including both employee and employer contributions, to the Blue Cross bank account, with the amount based on estimates that Blue Cross provided Hi-Lex each quarter. Id., PageID# 15415. Blue Cross used that money to pay the plan's claims and its own fees. Blue Cross quarterly reconciled the amounts it paid for claims; if Hi-Lex's wire transfers failed

to cover the quarter's obligations, Blue Cross adjusted the estimate upward for the next quarter. RE 112, Order, PageID# 4754-55; Appellees' Appx. P. 828-833.

In 1987-88, Blue Cross began charging various surcharges and subsidies as add-ons ("Add-On Fees") to the bills of its self-funded customers such as Hi-Lex. Over 200,000 employee members left Blue Cross in 1989, and many other customers refused to pay the Add-On Fees. RE 246, FFCL, PageID# 15416-17.

In 1993, Blue Cross replaced the disclosed Add-On Fees with the undisclosed Disputed Fees. Unlike the Add-On Fees, which were transparent on the bills to customers like Hi-Lex, these administrative fees were concealed in marked-up hospital claims and "no longer visible" to its customers because they falsely appeared to be money owed to hospitals. Id., PageID# 15417. Blue Cross's accountants and actuaries determined what expenses Blue Cross wanted to recoup through the Disputed Fees, and then determined how much the hospital claims charged to the customers had to be falsely marked up in order to reach that amount. Id., PageID# 15420.

Blue Cross told customers that with the new pricing arrangement, the fixed administrative fee would decrease, but deliberately omitted the Disputed Fees from the statement of the total administrative fees to be paid, making it seem to customers that they were paying less in fees than they in fact paid. Instead, the amount of Disputed Fees added to the facility or hospital charges were

misleadingly included in the "Total Claims Expense" which were reported as such in monthly, quarterly, and annual claims reports to Hi-Lex. Id., PageID# 15421-22, 15424. Blue Cross misrepresented to Hi-Lex that Hi-Lex's funds were only being used to pay actual claims, disclosed administrative fees, and stop-loss premiums. Id., PageID# 15423. In the annual renewals, Blue Cross stated that its "Administrative Fee is all-inclusive," omitting the fact that Blue Cross also secretly retained the Disputed Fees from assets of the plan as another form of administrative compensation. Id., PageID# 15424.

Hi-Lex filed suit against Blue Cross in June 2011, alleging self-dealing and breach of fiduciary duty in (a) charging hidden fees, (b) failing to disclose hidden fees, and (c) making false or intentionally misleading statements concerning the fees, including fraudulently concealing them. Id., PageID# 15413.

## II. Procedural History

The district court granted summary judgment in part and denied it in part on September 7, 2012. RE 112, Order.<sup>1</sup> The district court found that Blue Cross was a functional fiduciary because it exercised practical control over plan funds by using its authority to set its own compensation with the plan contributions that had

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<sup>1</sup> The court found a state court decision upholding Blue Cross's collection of the same hidden fees non-binding, because it did not consider or resolve ERISA claims or issues, such as claims of false and misleading statements. Id., PageID# 4744-45.

been forwarded to Blue Cross for the provision of benefits. Id., PageID# 4747-49. The court, citing Sixth Circuit cases with "nearly identical" facts to this case, concluded that Blue Cross had fiduciary control over plan assets regardless of whether Blue Cross segregated the funds it received. Id., PageID# 4754-55.

The court also held that, when Blue Cross unilaterally allocated Disputed Fees to itself, it committed a prohibited transaction under ERISA section 406(b)(1), 29 U.S.C. § 1106(b)(1), which prohibits fiduciaries from dealing with plan assets in their own interest. Id., PageID# 4757-58. The court later ruled that Blue Cross could not assert ERISA section 408(b)(2) as an affirmative defense, because it had violated section 406(b), and section 408(b)(2) is only available as a defense against section 406(a) claims. RE 139, Order, PageID# 5058.

After a bench trial, the court ruled in Hi-Lex's favor on the remaining claims on May 23, 2013. RE 246, FFCL. The court made detailed factual findings, including that Blue Cross knowingly gave Hi-Lex false reports and intended to deceive Hi-Lex about the Disputed Fees. Id., PageID# 15423, 15424, 15427, 15431, 15436, 15440, 15442. The court also found that Hi-Lex could not have discovered the Disputed Fees before June 2007, when Blue Cross included a disclosure of the precise amount of Disputed Fees paid in 2006, that Hi-Lex was diligent in reviewing Blue Cross's reports until 2007, when its CFO failed to read the pie charts disclosing these fees, and that a hypothetical diligent company would

not have discovered the Disputed Fees before that time. Id., PageID# 15439-50. The court thus concluded that Hi-Lex timely filed its suit within six years after the date when it should have learned of the Disputed Fees, using ERISA's special limitations period for fraud or concealment, 29 U.S.C. § 1113, under which the plaintiff may file "not later than six years after the date of discovery of such breach or violation." Id., PageID# 15467. The district court rejected Blue Cross's argument that "fraud or concealment" applied only if the defendant had engaged in some additional behavior designed to conceal the fiduciary breach, even if the fiduciary breach itself involved fraud. Id., PageID# 15460-65 (citing Caputo v. Pfizer, 267 F.3d 181 (2nd Cir. 2000)).

The court found that Hi-Lex proved with particularity at trial that Blue Cross made knowing misrepresentations and omissions, therefore proving fraud. Id., PageID# 15465-66. The court found the six years ran from August 21, 2007, the date on which Hi-Lex should have discovered the misrepresentations, and therefore the 2011 suit was timely. Id., PageID# 15458-59. The court also held that Hi-Lex proved "fraudulent concealment" based on Blue Cross's separate conduct to conceal the hidden Disputed Fees, meeting the higher standard of the other Circuits. Id., PageID# 15468.

On the merits, the court concluded that Blue Cross was a fiduciary that violated its duties by giving Hi-Lex false and misleading information about the

nature and extent of the Disputed Fees, by failing to disclose information about its fees even if not specifically requested, and by engaging in prohibited self-dealing. Id., PageID# 15455. The court held that Hi-Lex was entitled to restitution of all Disputed Fees from 1994 to 2011. The court entered judgment for over \$5 million, plus costs, interest, and attorney fees. Id., PageID# 15450-51.

### SUMMARY OF ARGUMENT

I. ERISA section 413 provides that where participants and the Secretary have been prevented from discovering fiduciary breaches via "fraud or concealment," they may sue within six years after they discover the breach. The district court correctly read section 413 to give independent meaning to both terms disjunctively, rather than requiring both fraud and additional concealment of the fraud. This approach respects the text of the statute and the ordinary meaning of the terms "fraud" and "concealment." It also is consistent with Supreme Court and Sixth Circuit holdings that material omissions by fiduciaries are fraud, and that self-concealing fraud by fiduciaries, without additional concealment efforts, delays the running of a claim. The district court correctly found that Blue Cross's deceptive conduct kept Hi-Lex from discovering the claim before 2007, and therefore the suit is timely.

II. Under this Court's precedents, Blue Cross acted as a fiduciary by exercising undisclosed, unilateral control over plan funds when it retained part of

the funds from the employer and employee contributions Hi-Lex sent. By disguising administrative fees as hospital payments for covered benefits and pocketing them without authorization, Blue Cross unilaterally modified the fees charged and breached its fiduciary duty to disclose material information.

Moreover, the funds Hi-Lex forwarded to Blue Cross's account were earmarked for the payment of plan benefits with multiple indicia of the plan's beneficial interest in those monies, and therefore were plan assets. Thus, Blue Cross cannot disclaim that it had control over plan assets when it unilaterally set the fees that it hid from Hi-Lex's scrutiny.

III. Blue Cross's covert retention of plan funds constituted impermissible self-dealing. Under ERISA section 406(b)(1), fiduciaries are prohibited from dealing with plan assets in their own interest. No "reasonable compensation" exemption applies because fiduciaries are strictly prohibited from receiving any self-dealing compensation.

### ARGUMENT

#### I. THE DISTRICT COURT PROPERLY CONSTRUED AND APPLIED THE "FRAUD OR CONCEALMENT" PROVISION OF ERISA'S STATUTE OF LIMITATIONS

##### A. "Fraud or Concealment" Applies to Either Fraud or Concealment

ERISA's statute of limitations (section 413) states, in relevant part, that "in the case of fraud or concealment, such action may be commenced not later than six

years after the date of discovery of such breach or violation." 29 U.S.C. § 1113. The scope of this "fraud or concealment" proviso remains an open question in the Sixth Circuit.<sup>2</sup> "In ERISA cases, '[a]s in any case of statutory construction, [the court's] analysis begins with the text of the statute.'" Harris Trust and Sav. Bank v. Salomon Smith Barney, Inc., 530 U.S. 238, 254 (2000). The pertinent text of section 413 gives plaintiffs six years after the discovery of a breach to file suit where there is "fraud or concealment." 29 U.S.C. § 1113 (emphasis added). The disjunctive word "or" should be construed literally, because "[i]f Congress had intended the words to be construed in the conjunctive instead of the disjunctive it could easily have used the word 'and' and reached that result. Its failure to do so, together with the use of the word 'or' leads us to construe the statute in the disjunctive." NLRB v. Edward G Budd Mfg. Co., 169 F.2d 571, 576 (6th Cir. 1948) (citation omitted). Thus, "fraud" in ERISA section 413 is distinct from, and not synonymous with, "concealment." Equating the terms or reading them conjunctively disregards the plain text and risks "render[ing] one term superfluous, a reading we must try to avoid." See GGNSC Springfield LLC v. NLRB, 721 F.3d 403, 410 (6th Cir. 2013).

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<sup>2</sup> Blue Cross suggests that this Circuit determined the proper interpretation of "fraud or concealment" in Brown v. Owens Corning Inv. Review Comm., 622 F.3d 564, 573 (6th Cir. 2010). (Br. at 65). After Brown, however, this Court explicitly stated that it has not decided the standard for construing "fraud or concealment." Cataldo v. U.S. Steel Corp., 676 F.3d 542, 549-51 (6th Cir. 2012).

The district court therefore correctly read "fraud or concealment" disjunctively and gave each term independent meaning. RE 246, FFCL, PageID# 15461-64. In doing so, the court sensibly followed the Second Circuit's reasoning from Caputo v. Pfizer, 267 F.3d 181, 189-90 (2nd Cir. 2001), which explained that "principles of statutory interpretation counsel strongly against merging the two terms," because affording a statute its full and plain meaning requires "giving each term independent significance (as one must when terms are used in the disjunctive unless the context dictates otherwise)." Id.; see Cataldo v. U.S. Steel Corp., 676 F.3d 542, 551 (6th Cir. 2012) (finding Caputo's rationale "persuasive").

Because ERISA does not define the terms "fraud" and "concealment," the Court "must determine the meaning of the term[s] from [their] ordinary, contemporary, common meaning at the time Congress enacted the statute," Lockhart v. Napolitano, 573 F.3d 251, 258 (6th Cir. 2009) (citation omitted), while mindful of the "familiar canon of statutory construction that remedial legislation [such as ERISA] should be construed broadly to effectuate its purpose." In re Carter, 553 F.3d 979, 985 (6th Cir. 2009) (citation omitted). Traditionally, "fraud" is defined as "a false representation of a matter of fact [by] misleading allegations or by concealment of that which should have been disclosed, which . . . is intended to deceive another so that he shall act upon it to his legal injury;" "concealment" is defined as "withholding of something which one knows and which one, in duty, is

bound to reveal." Caputo, 267 F.3d at 189-90 (quoting Black's Law Dictionary, 788 (Rev. 4th ed. 1968)). Applying these contemporary definitions, the pertinent section 413 provision is satisfied if there is: (1) "fraud," which occurs when "a fiduciary . . . breached its duty by making a knowing misrepresentation or omission of a material fact to induce an employee/beneficiary to act to his detriment;" or (2) "concealment," which occurs if the fiduciary "engaged in acts to hinder the discovery of a breach of fiduciary duty." Id. at 190 (citation omitted). In other words, "fraud or concealment" occurs if the fiduciary engages in a knowing misrepresentation that has the intent to deceive or induce detrimental reliance or either knowingly withholds pertinent information or actively conceals the underlying breach. Id. (construing section 413 to apply to fraud or fraudulent concealment).

In truth, it is apparent that these definitions overlap and, specifically, that a material omission can fall under either heading. What matters, however, is that the foregoing interpretation is consistent with the Supreme Court's and the Sixth Circuit's treatment of "fraud" in the fiduciary context as including an omission of material information. In Chiarella v. United States, 445 U.S. 222 (1980), the Supreme Court stated that "one who fails to disclose material information . . . commits fraud only when he is under a duty to do so. And the duty to disclose arises when one party has information 'that the other [party] is entitled to know

because of a fiduciary or other similar relation of trust and confidence between them." Id. at 228 (citation omitted). More recently, the Supreme Court held that a "fraudulent scheme" existed, in part, because "any distinction between omissions and misrepresentations is illusory in the context of a broker who has a fiduciary duty to her clients." SEC v. Zandford, 535 U.S. 813, 824 (2002).<sup>3</sup> This Court has likewise held that a fiduciary commits "fraud" when he fails to disclose material information to individuals in a trust relationship. Swanson v. Wilson, 423 Fed. Appx. 587, 599 n.5 (6th Cir. 2011) (interpreting California law) ("Where there is a [fiduciary] duty to disclose, the disclosure must be full and complete, and any material misrepresentation or concealment will amount to fraud").<sup>4</sup>

Moreover, under a doctrine sometimes called "fraudulent concealment," "fraud" includes "self-concealment" or "passive concealment" where there is a fiduciary relationship. Under this long-established doctrine, as applied to statutes of limitations like section 413 of ERISA, when a "fraud has been concealed, or is of such character as to conceal itself, the statute [of limitations] does not begin to

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<sup>3</sup> Accord United States v. Hagan, 521 U.S. 642, 652 (1997); Dirks v. SEC, 463 U.S. 646, 653 (1983).

<sup>4</sup> Other circuits are in accord. See, e.g., de la Fuente v. FDIC, 332 F.3d 1208, 1222-23 (9th Cir. 2003); SEC v. Cochran, 214 F.3d 1261, 1264-65 (10th Cir. 2000); United States v. Brown, 79 F.3d 1550, 1557 (11th Cir. 1996), overruled on other grounds United States v. Svete, 556 F.3d 1157 (11th Cir. 2009) (en banc); United States v. Holzer, 816 F.2d 304, 307 (7th Cir.), vacated, 484 U.S. 807 (1987).

run until the fraud is discovered." Bailey v. Glover, 88 U.S. (21 Wall.) 342 (1874).

In Bailey, the Supreme Court considered whether to extend the fraudulent concealment doctrine to "actions at law," and explained that:

[I]n suits in equity the decided weight of authority is in favor of the proposition that where the party injured by the fraud remains in ignorance of it without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party.

Id. at 348. Subsequently, the Court elaborated that "if the fraud itself be secret in its nature, and such that its existence cannot be readily ascertained, or if there be fiduciary relationships between the parties, there need be no evidence of a fraudulent concealment other than that implied from the transaction itself." Bates v. Preble, 151 U.S. 149, 160-61 (1894). After the merger of the courts of law and equity, the Supreme Court reaffirmed its finding in Bailey that equity requires "no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party." Holmberg v. Armbrecht, 327 U.S. 392, 397 (1946).

In Pinney Dock & Transport Co. v. Penn Cent. Corp., the Sixth Circuit extensively examined Bailey and agreed that, to show fraudulent concealment, "affirmative acts of concealment must be shown except in cases founded on fraud or breach of fiduciary duty," in which case "self-concealing misconduct may be sufficient." 838 F.2d 1445, 1471 (6th Cir. 1988) (citation omitted). Accordingly,

"the wrongful concealment prong is satisfied by a showing that the fraud was self-concealing." Venture Global Eng'g, LLC v. Satyam Computer Servs., Ltd., 730 F.3d 580, 587 (6th Cir. 2013) (citing Bailey & Pinney Dock). Other circuits agree with this principle.<sup>5</sup> Thus, the Supreme Court, Sixth Circuit, and other Circuits recognize "self-concealing" fraud or "passive concealment" as a type of "fraud" (or "fraudulent concealment") where there is a fiduciary relationship – without regard for "special efforts" or additional affirmative acts to conceal.

No more is required under ERISA to establish "fraud or concealment" under section 413. "[A]t common law, the courts of equity had exclusive jurisdiction over virtually all actions by beneficiaries for breach of trust." Mertens v. Hewitt Associates, 508 U.S. 248, 256 (1993). Moreover, "ERISA abounds in the language and terminology of trust law [and] ERISA's legislative history confirms that the Act's fiduciary responsibility provisions . . . 'codif[y] and mak[e] applicable to [ERISA] fiduciaries certain principles developed in the evolution of the law of trusts.'" Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 110 (1989); Grindstaff v. Green, 133 F.3d 416, 432 (6th Cir. 1998); S. Rep. No. 93-127, p. 29 (1973), as reprinted in U.S.C.C. A. N. 1974, 4639, 4865 (Congress recognized that

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<sup>5</sup> Sprint Commc'ns Co., L.P. v. F.C.C., 76 F.3d 1221, 1226-227 (D.C. Cir. 1996); State of Tex. v. Allan Const. Co., Inc., 851 F.2d 1526, 1532-33 & n.29 (5th Cir. 1988); Rutledge v. Boston Woven Hose & Rubber Co., 576 F.2d 248, 250 (9th Cir. 1978); Jamesbury Corp. v. Worcester Valve Co., 443 F.2d 205, 209 (1st Cir. 1971); Bryan v. United States, 99 F.2d 549, 553 (10th Cir. 1938).

"[an ERISA] fiduciary is one who occupies a position of confidence or trust."). Accordingly, "courts are to develop a 'federal common law of rights and obligations under ERISA-regulated plans' . . . guided by principles of trust law." Firestone, 489 U.S. at 110 (citation omitted). It follows that the fiduciary exception to the "fraudulent concealment" doctrine enunciated by the Supreme Court and this Circuit applies to ERISA, which imposes fiduciary relationships and obligations on those in positions of trust, 29 U.S.C. §§ 1002(21), 1104, and particularly to ERISA section 413, which is lodged in the statute's "fiduciary responsibility" section.

This fiduciary exception is triggered by a fiduciary's disclosure obligations, and the Sixth Circuit recognizes in the ERISA context that the "duty to inform is a constant thread in the relationship between beneficiary and trustee; it entails not only a negative duty not to misinform, but an affirmative duty to inform when the trustee knows that silence might be harmful." Dudenhoeffer v. Fifth Third Bancorp, 692 F.3d 410, 420 (6th Cir. 2012), pet. for cert. pending, No. 12-751 (U.S.). Because ERISA fiduciaries have a duty to disclose material information to participants and beneficiaries, the statute of limitations under ERISA section 413's "fraud or concealment" clause is triggered either by a fiduciary's fraudulent misrepresentations or its purposeful failure to disclose (i.e., concealment of) material information, and does not begin to run until discovery of the breach.

B. Blue Cross Engaged in Both Fraud and Concealment, as well as Fraudulent Concealment

In this case, plaintiffs alleged and the district court properly found that Blue Cross committed "fraud" within the meaning of ERISA section 413. The district court determined that Blue Cross owed plaintiffs a fiduciary duty to reveal its fees, RE 246, FFCL, PageID# 15451-53, but instead Blue Cross materially misrepresented these fees, and went "to great lengths to ensure that the Disputed Fees were not disclosed to the customer." See id., PageID# 15421; see also, e.g., id., PageID# 15421-41. The court also found that Blue Cross knowingly made fraudulent and misleading representations that would lead Hi-Lex to wrongly believe it had received full disclosure regarding Blue Cross' fees. Id., PageID# 15442, 15446-49; see East Jordan Plastics, Inc. v. Blue Cross and Blue Shield of Michigan, 2013 WL 1876117, \*4-5 (E.D. Mich. 2013) (finding that the same language Blue Cross used in its contracts with Hi-Lex was misleading). Blue Cross made "knowing misrepresentation[s] and] omission[s] of a material fact to induce [Hi-Lex] to act to his detriment." Caputo, 267 F.3d at 189. Accordingly, Blue Cross engaged in both "fraud and concealment," easily satisfying the disjunctive "fraud or concealment" standard.

Blue Cross also committed "fraudulent concealment" because Blue Cross owed a fiduciary disclosure obligation to Hi-Lex, but knowingly failed to disclose

material information to Hi-Lex regarding the fees it was charging. The court further determined that reasonable diligence could not have discovered the fraudulence prior to August 2007, when Hi-Lex first received notice of the Disputed Fees and the claim began to run. Thus, Hi-Lex timely filed suit in June 2011, less than four years after its claims accrued. See Med. Mut. of Ohio v. K. Amalia Enterprises Inc., 548 F.3d 383, 391 (6th Cir. 2008) (applying discovery rule in ERISA case).

C. The Secretary's Reading Comports with ERISA's Purpose

The Secretary's reading of the "fraud or concealment" provision best comports with ERISA's remedial purpose, by protecting participants and the Secretary when, due to "fraud or concealment" by plan fiduciaries, they are unaware of statutory breaches by these fiduciaries. In that circumstance, the statute delays accrual of the claim until the breach is or should have been discovered. "Clearly, Congress intended to provide a lengthier statute of limitations where the fiduciary breached its duty by misrepresenting or failing to disclose a material fact that ERISA required the fiduciary to disclose." Caputo, 267 F.3d at 190. Indeed, the Supreme Court "long ago recognized that something different was needed in the case of fraud, where a defendant's deceptive conduct may prevent a plaintiff from even knowing that he or she has been defrauded. Otherwise, "'the law which was designed to prevent fraud' could become 'the

means by which it is made successful and secure." Merck & Co., Inc. v. Reynolds, 559 U.S. 633, 644 (2010) (quoting Bailey, 88 U.S. (21 Wall.) at 349; emphasis in original).

As the Supreme Court has consistently opined, "[t]o hold that . . . by committing a fraud in a manner that it concealed itself until such time as the party committing the fraud could plead the statute of limitations to protect it, is to make the law which was designed to prevent fraud the means by which it is made successful and secure." Bailey, 88 U.S. (21 Wall.) at 349. Thus, "'where a plaintiff has been injured by fraud and remains in ignorance without any fault . . . on his part, the bar of the statute does not begin to run until the fraud is discovered.'" Merck, 559 U.S. at 644 (quoting Holmberg, 327 U.S. at 397; emphasis in original). These considerations are particularly appropriate in the ERISA context, because "[t]he law does not require one to suspect his fiduciary. Surely no one would contend that the . . . statute of limitations was intended to impose upon the defrauded party the burden of discovering a fraud perpetrated by one standing in a position of trust." In re Unisys "ERISA" Litig., 242 F.3d 497, 514 (3d Cir. 2010) (Mansmann, J., concurring in part, and concurring in the result) (citation omitted).

D. Narrower Interpretations of Section 413 by Other Circuits are Unpersuasive

The district court was correct to adopt the Second Circuit's approach and not to follow the circuits that require a showing of additional affirmative steps to conceal the violation independent of the fiduciary breach that gave rise to the plaintiffs' claim.<sup>6</sup> First, by disregarding the disjunctive "or" in ERISA section 413's "fraud or concealment" provision, these court have abandoned straightforward textual analysis and thereby deprived "fraud" and "concealment" of their independent (albeit overlapping) meanings. See Cataldo, 676 F.3d at 550-51 (referring to Caputo's "persuasive contrary interpretation"). Second, in recasting "fraud or concealment" as "fraudulent concealment" in its narrowest formulation, these courts fail to consider the well-established, broader application of the fraudulent concealment doctrine to fiduciaries who engage in self-concealing fraud, as described above. See, e.g., Schaefer v. Arkansas Med. Soc'y, 853 F.2d 1487, 1491-92 (8th Cir. 1988). Third, these decisions are contrary to ERISA 413's purpose of ensuring that if "the injury is not of the sort that can readily be discovered when it occurs, then the action will accrue, and the limitations period

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<sup>6</sup> Kurz v. Philadelphia Elec. Co., 96 F.3d 1544, 1552 (3d Cir. 1996); J. Geils Band Emp. Benefit Plan v. Smith Barney Shearson, Inc., 76 F.3d 1245, 1252 (1st Cir. 1996); Barker v. Am. Mobil Power Corp., 64 F.3d 1397, 1401-02 (9th Cir. 1995); Larson v. Northrop Corp., 21 F.3d 1164, 1172-73 (D.C. Cir. 1994); Radiology Ctr. v. Stifel Nicolaus & Co., 919 F.2d 1216, 1220 (7th Cir. 1990); Schaefer 853 F.2d at 1491-92 .

commence, only when the plaintiff has discovered . . . the injury." Connors v. Hallmark & Son Coal Co., 935 F.2d 336, 343 (D.C. Cir. 1991) (Ginsburg, J).

II. BLUE CROSS ACTED AS A FIDUCIARY WHEN IT UNILATERALLY PAID ITSELF THE DISPUTED FEES

Under ERISA, a person is a fiduciary to the extent he "exercises any authority or control respecting management or disposition of [the plan's] assets." ERISA section 3(21)(A), 29 U.S.C. § 1002(21)(A). Fiduciary status under ERISA is defined "not in terms of formal trusteeship, but in functional terms of control and authority." Mertens v. Hewitt Assocs., 508 U.S. 248, 260-62 (1993); see Smith v. Provident Bank, 170 F.3d 609, 613 (6th Cir. 1999). Blue Cross was a fiduciary because it exercised authority or control over plan assets when it unilaterally paid itself undisclosed fees from the assets of the Hi-Lex health plan.

This Court's controlling authority holds that administrators for health plans exercise authority over plan assets (and thereby act as fiduciaries) when they take funds contributed by employers for health benefits under arrangements analogous to those here. In Briscoe v. Fine, 444 F.3d 478, 489-495 (6th Cir. 2006), an employer deposited contributions into an account in the name of both the employer and the plan's third-party administrator, and the administrator disbursed funds from the account to pay health service providers for participants in the employer's self-funded plan. Like Hi-Lex in this case, the employer paid into the account out of its general assets in amounts based on the claims experience and expenses incurred by

the administrator. As here, the administrator exerted unilateral control over the plan funds, in that case by retaining part of the account after its termination as an "administrative fee." Briscoe held that the "unilateral disposition of funds held in an account over which it exerted control makes it a fiduciary". Id. at 490.

Similarly, in another case against Blue Cross concerning the same contracts as in this case, this Court found that Blue Cross was a fiduciary when it chose to assess the same fees that Hi-Lex disputes here against an account that held deposits for the payment of plan benefits. Pipefitters Local 636 Ins. Fund v. Blue Cross and Blue Shield of Michigan, 722 F.3d 861, 866-67 (6th Cir. 2013). The Court held that Blue Cross was a fiduciary because it exercised unilateral authority in assessing the fees. Id. at 866-67 (finding that Blue Cross's authority was hidden in "opaque language" that "in no way cabins [Blue Cross's] discretion to charge or set" fees).<sup>7</sup>

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<sup>7</sup> Blue Cross argues (Br. 34) that Pipefitters is distinguishable because the money there was paid into a trust. However, the Sixth Circuit similarly found fiduciary status in Briscoe, where the money was simply paid into an account that was not denominated a trust. Rather, the Court decided both Pipefitters and Briscoe on the ground that when a service provider unilaterally sets its fee with no opportunity for a plan fiduciary to review and approve, it exercises authority over plan assets and therefore acts as a fiduciary. Compare Smith, 170 F.3d at 612-613 (bank's unauthorized transfer of plan's assets made it a fiduciary) with McLemore v. Regions Bank, 682 F.3d 414, 424 (6th Cir. 2012) (bank was not fiduciary when allegedly unreasonable fees were agreed to by plan fiduciary).

Here too, the district court found that Blue Cross exercised undisclosed unilateral authority over disposition of the contributions intended for the benefit of the plan participants. RE 112, Order, PageID# 4747-50. Pipefitters and Briscoe are therefore controlling.<sup>8</sup> The district court correctly concluded that Blue Cross's unilateral decision to expend additional employer and employee contributions on itself, rather than on plan benefits or other legitimate purposes, was sufficient to make it a functional fiduciary. According to the facts found by the court, Blue Cross secretly paid itself the Disputed Fees from employee and employer contributions which were intended for the provision of health benefits. Hi-Lex regularly deposited these contributions, including employee contributions after 2003, by wire transfer to the Blue Cross's pooled plan account established for the payment of plan benefits and expenses. RE 108, Motion for Summary Judgment, Ex. X, ¶4. Blue Cross retained more of the plan contributions than Hi-Lex had contracted to pay from the plan's assets by deceiving Hi-Lex as to the amount it was keeping for itself while disguising expenditures as payments to hospitals. This exercise of practical and unilateral control over the plan's money and ability to

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<sup>8</sup> Neither Seaway Food Town, Inc. v. Medical Mutual of Ohio, 347 F.3d 610, 619 (6th Cir. 2003) nor McLemore are to the contrary. Both cases involve third parties who retained nondiscretionary fees that other plan fiduciaries independently approved in arm's-length negotiation. Thus, they merely stand for the proposition that adherence to a contract does not create fiduciary status, "unless the term authorizes the party to exercise discretion with respect to that right." RE 112, Order, PageID# 4751 (emphasis in original). When a contract establishes a right to a determinate fee, as in Seaway and McLemore, there is no discretion.

allocate an administrative fee to itself, demonstrated discretionary control over plan assets comparable to what existed in Pipefitters. See also Guyan Int'l v. Prof'l Benefits Adm'rs, 689 F.3d 793, 798 (6th Cir. 2012) (fact that third-party administrator "used plan funds in ways contrary to how it had agreed to use them demonstrates that [TPA] had practical control over Plan funds once it received them from the Plaintiffs").

Thus, by disguising administrative fees as seemingly legitimate hospital payments, Blue Cross surreptitiously misappropriated plan assets, without Hi-Lex's knowledge or approval, and arrogated to itself discretion over fees that Hi-Lex did not even know about. Blue Cross's fraudulent and misleading conduct in this regard was a breach of its fiduciary duties. Given the district court's factual findings that Blue Cross's conduct was fraudulent and misleading, Hi-Lex had every right to expect to be told about any fees it was paying for Blue Cross's services; instead, Blue Cross willfully misled Hi-Lex into believing that the fees were lower than they actually were and that the benefits paid were greater than the medical providers actually charged. Indeed, the breakdown between those two very different categories of expense would be of great interest to any plan fiduciary like Hi-Lex. If told the truth, Hi-Lex might well have sought reimbursements, insisted on renegotiating its contract, or filed legal action earlier. Indeed, when Blue Cross had disclosed the Add-On fees, it lost over 200,000 members in one

year, and roughly half of the Add-On fees were not paid because customers refused. RE 246, FFCL, PageID# 15416-7.

Contrary to Blue Cross's asserted belief, the funds Hi-Lex transferred to Blue Cross on behalf of the plan were plan assets, as Blue Cross has previously admitted. See Joint Final Pretrial Order ("[p]ursuant to the ASC's and Schedule A's, BCBSM administered the healthcare claims for the Plan by paying covered employee healthcare claims on behalf of the Plan from the Plan's plan assets") (Doc #240 at 4) (emphasis added). The Secretary's regulations state unequivocally that employee contributions, such as the money deducted from employees' paychecks here since 2003, constitute plan assets under Title I of ERISA once they reasonably can be, or as here, are "segregated from the employer's general assets." 29 C.F.R. § 2510.3-102(a)(1). See also United States v. Grizzle, 933 F.2d 943, 946-47 (11th Cir. 1991) (plan assets include employee contributions, even when they have not been delivered yet to the plan). The Department has explicitly advised that "all amounts that a participant pays to or has withheld by an employer for purposes of obtaining benefits under a plan will constitute plan assets without regard to when related plan expenses or benefits are paid by the employer." AO 92-24A, 1992 WL 337539. Because Blue Cross diverted these contributions from their intended purpose by unilaterally retaining higher fees than agreed upon, it exercised fiduciary authority over plan assets.

The employer contributions that Hi-Lex forwarded to Blue Cross were also plan assets insofar as they were earmarked for the payment of plan benefits. ERISA does not supply a specialized definition of "plan assets."<sup>9</sup> As a result, "the assets of an employee benefit plan generally are to be identified on the basis of ordinary notions of property rights" in the absence of specific regulations. AO 92-24A, 1992 WL 337539, \*2; In re Halpin, 566 F.3d 286, 289 (2d Cir. 2009) (citing AO 93-14A (May 5, 1993)). Under this test, "the assets of a welfare plan generally include any property, tangible or intangible, in which the plan has a beneficial ownership interest." AO 92-24A, 1992 WL 337539, \*2. The requisite "beneficial interest" in particular assets is generally satisfied if, for example, the employer "sets up a separate account with a bank or other third party in the name of the plan, or specifically indicates in the plan documents or instruments that separately maintained funds belong to the plan." Id. Such accounts do not, therefore, necessarily have to be in the form of a formal trust. Id. at \*2-3.

There are multiple indicia of the plan's beneficial interest in the funds here. The payments that Hi-Lex forwarded to Blue Cross were earmarked for plan benefits and plan expenses, and were sent to a separate multi-plan pooled account

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<sup>9</sup> The Department has promulgated regulations defining plan assets in only two specific contexts: employee contributions, when a participant pays or has amounts withheld by an employer for contribution to a plan, 29 C.F.R. § 2510.3-102, and plan investments in another entity, 29 C.F.R. § 2510.3-101. AO 92-24A at \*2.

maintained by Blue Cross. Blue Cross exercised check-writing control over the account for these plan purposes, and Blue Cross was expressly permitted to withhold funds from the account for agreed-to administrative fees for its services to the plan. See AO 94-31A (Sept. 9, 1994); see also AO 92-24A ("We note that drawing benefit checks on a TPA account, as opposed to an employer account, may suggest to participants that there is an independent source of funds securing payment of their benefits under the plan."). Blue Cross kept detailed records of the funds Hi-Lex wired and accounted for them, reporting quarterly to Hi-Lex the amounts it paid in plan claims and fees<sup>10</sup>, and any surplus from the previous quarter, which Blue Cross rolled over for the next quarter's claims and expenses. See, e.g., Appellees' Appx. p. 818.

This Court has found in cases with similar fact patterns that accounts containing contributions on behalf of plans contained plan assets. See Guyan, 689 F.3d at 797-98 (plan's third-party administrator was fiduciary because premium payments were paid directly into its corporate account on behalf of plan, and it exercised authority to write checks on that account, had control over where plan funds were deposited and how and when they were disbursed); Libbey-Owens-Ford v. Blue Cross and Blue Shield of Ohio, 982 F.2d 1031, 1035-36 (6th Cir. 1993) (holding that Blue Cross was a fiduciary as a result of its authority to

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<sup>10</sup> The Disputed Fees were tallied under claims rather than expenses. RE 246, FFCL, PageID# 15422.

" earmark the funds that Libbey-Owens-Ford allocated to the plan"); cf. Chao v. Crouse, 346 F. Supp. 2d 975, 985 (S.D. Ind. 2004) (employer premiums deposited directly into third-party administrator's corporate accounts were plan assets, and the exercise of authority and control over the accounts made the administrator a fiduciary).

Blue Cross incorrectly argues (Br. 31-32) that because Hi-Lex's summary plan description ("SPD") stated that benefit payments are "paid directly out of the general assets of the Company" and that there is "no special fund or trust from which self-insured benefits are paid," no plan assets exist in this case. This language in the SPD was not accurate in two critical respects. First, as explained above, the employee contributions that Hi-Lex withheld from the employees' paychecks became plan assets at the point when they could be reasonably segregated from the employer's general assets and remained plan assets when deposited in Blue Cross's special account for the payment of the plan's benefits and expenses. Second, contrary to the language of the SPD, the employer and employee contribution were deposited in a "special fund" controlled by Blue Cross from which the self-insured benefits were paid. Moreover, as previously noted, the Sixth Circuit has already rejected such arguments in the context of similar self-funded plans. Therefore, as explained above, Blue Cross's argument about plan assets is meritless.

Furthermore, by unilaterally causing the Hi-Lex plan to pay higher fees, without Hi-Lex's knowing fiduciary assessment of whether those fees were prudent, Blue Cross exercised authority and control over plan assets and thereby became a functional fiduciary. See, e.g., Metzler v. Solidarity of Labor Organizations Health & Welfare Fund, 1998 WL 477964, \*7 (S.D.N.Y. 1998) (Medco exercised discretion over plan assets by setting total amount of participating employers' contributions and retaining difference between contributions and amount used for benefits, thereby unilaterally determining its own fee and hiding fee from plan fiduciary), aff'd sub nom Herman v. Goldstein, 224 F.3d 128 (2nd Cir. 2000); PWBA Information Letter to Narrvel E. Hall, 1993 WL 1370525, \*4 (stating that "authority to unilaterally modify the fees charged . . . could involve the exercise of fiduciary discretion to cause the plan to pay an additional fee" which it had no opportunity to review or authorize).<sup>11</sup> Cf. Chao v. Day, 436 F.3d 234, 236-37 (D.C. Cir. 2006) (insurance broker who kept plan funds

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<sup>11</sup> Cf. McCormick Letter, 1994 WL 707770 (stating that in the Secretary of Labor's view, banks that earn income from the "float" on outstanding benefit checks are benefiting themselves with plan assets at the expense of the plan's interest and thereby exercising fiduciary discretion, unless they openly negotiate with independent plan fiduciaries to retain earnings on the float as part of their overall compensation). In FAB 2002-3, 2002 WL 32502487 (EBSA), the Secretary further stated that open negotiation and full and fair disclosure are intended to ensure that service providers provide sufficient information to allow plan fiduciaries to make informed assessments concerning the prudence of the arrangement. Id. at \*1-2.

rather than using them to pay premiums had authority or control over plan assets and was fiduciary).

III. THE DISTRICT COURT CORRECTLY HELD THAT BLUE CROSS BREACHED ITS DUTY BY MISREPRESENTING OR CONCEALING MATERIAL FACTS AND ENGAGING IN SELF-DEALING

Blue Cross argues (Br. 61-62) that it had no duty to disclose the amount of the Disputed Fees because none of ERISA's specific reporting provisions required disclosure of the fees at issue. But fiduciaries violate their core duties of prudence and loyalty under ERISA sections 404(a)(1)(A) and (B), 29 U.S.C. §§ 1104(a)(1)(A) and (B), by lying to or misleading plan participants, and by failing to disclose material information, even if not enumerated in ERISA's specific reporting provisions or regulations. See Harte v. Bethlehem Steel Corp., 214 F.3d 446, 451 n.6 (3d Cir. 2000); see generally Varsity Corp. v. Howe, 516 U.S. 489, 506 (1996). The same duty to disclose material information is owed to other fiduciaries of the plan. See In re WorldCom Inc. ERISA Litig., 263 F.Supp.2d 745, 765 (S.D.N.Y.2003) (allegation that fiduciary failed to disclose to other fiduciaries material information regarding prudence of investing in company stock sufficed to state claim).

Under the common law of trusts that Varsity recognized is incorporated into ERISA in this context, a trustee has "a duty to communicate to the beneficiary material facts affecting the interest of the beneficiary which he knows the

beneficiary does not know and which the beneficiary needs to know for his protection in dealing with a third person." The Restatement (Second) of Trusts § 173, cmt. d (1959); Varity, 516 U.S. at 506 ("To participate knowingly and significantly in deceiving a plan's beneficiaries in order to save the employer money at the beneficiaries' expense is not to act 'solely in the interest of the participants and beneficiaries.' As other courts have held, '[I]ying is inconsistent with the duty of loyalty owed by all fiduciaries and codified in section 404(a)(1) of ERISA") (citations omitted). This duty of candor when dealing with plan participants (or, here, co-fiduciaries) encompasses intentional omissions as well as affirmative misrepresentations. See Dudenhoeffer v. Fifth Third Bancorp, 692 F.3d 410, 420 (6th Cir. 2012) (the "duty to inform is a constant thread in the relationship between beneficiary and trustee [including] an affirmative duty to inform when the trustee knows that silence might be harmful"); Krohn v. Huron Mem'l Hosp., 173 F.3d 542, 547-48, 550 (6th Cir.1999); Griggs v. E.I. DuPont de Nemours & Co., 237 F.3d 371, 381 (4th Cir. 2001); Becker v. Eastman Kodak Co., 120 F.3d 5, 9 (2d Cir. 1997); Bowerman v. Wal-Mart Stores, Inc., 226 F.3d 574, 590 (7th Cir. 2000). Thus, the district court correctly concluded that Blue Cross breached its fiduciary duty of loyalty under section 404(a), 29 U.S.C. § 1104(a), by intentionally misrepresenting the nature of the Disputed Fees, disguising them as seemingly legitimate hospital fees to thwart Hi-Lex's ability to determine for itself

whether the fees were reasonable and within its contractual obligation to pay. RE 246, FFCL, PageID# 15454-56.

Moreover, having concluded that Blue Cross was a fiduciary as a result of its unauthorized use of plan assets, the district court also rightly and necessarily concluded that Blue Cross was culpable for self-dealing in violation of ERISA section 406(b)(1), which provides that a fiduciary shall not "deal with assets of the plan in his own interest or for his own account." 29 U.S.C. § 1106(b)(1). In enacting ERISA, the "crucible of congressional concern was the misuse and mismanagement of plan assets," particularly self-dealing by plan managers. Mass. Mut. Life Ins. Co. v. Russell, 473 U.S. 134, 141 n. 8 (1985). No investigation into the motives or prudence of a particular transaction is required to establish violations of ERISA section 406. Congress "intended to create an easily applied per se prohibition . . . of certain transactions, no matter how fair." Cutaiar v. Marshall, 590 F.2d 523, 529-30 (3d Cir. 1979). ERISA section 406(b) is to be "read broadly in light of Congress' concern with the welfare of plan beneficiaries." Leigh v. Engle, 727 F. 2d 113, 126 (7th Cir. 1984) ("The entire statutory scheme of ERISA demonstrates Congress' overriding concern with the protection of plan beneficiaries, and we would be reluctant to construe narrowly any protective provisions of the Act.").

Blue Cross's covert retention of Disputed Fees from plan assets for its own benefit, while acting as the Plan's fiduciary and at the expense of the Plan and its participants, epitomizes the kind of self-dealing that ERISA section 406 (b)(1) flatly prohibits. Section 406(b) prohibits any fiduciary "from acting in a situation in which he has a personal interest which may conflict with the interest of the plan for which he asks." Freund v. Marshall & Ilsley Bank, 485 F. Supp. 629, 637 (W.D. Wisc. 1979). Thus, when a fiduciary deals with plan assets in his own interest in violation of section 406(b), the "reasonable compensation" exemption in Section 408 of ERISA provides no safe harbor, 29 U.S.C. § 1108(b)(2); see 29 CFR § 2550.408b-2(e)(1), and no other exemption applies to such self-dealing.<sup>12</sup>

The "reasonable compensation" exemption exists to allow necessary transactions under reasonable contractual arrangements between plans and service providers that would otherwise be prohibited by ERISA section 406(a), 29 U.S.C. § 1106(a). Section 406(a) prohibits transactions between plans and "parties in interest," but section 408(b)(2) exempts service providers receiving "reasonable compensation" for necessary services to plans. However, the exemption does not

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<sup>12</sup> 29 CFR § 2550.408b-2(e)(1) states, in pertinent part, that "If the furnishings of . . . a service involves an act described in section 406(b) of the Act (relating to acts involving conflicts of interest by fiduciaries), such an act constitutes a separate transaction which is not exempt under section 408(b)(2) of the Act. " This reasonable interpretation of the statute is entitled to the highest judicial deference. See Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842-43 (1984).

apply to fiduciary self-dealing, such as unilaterally paying oneself fees from plan assets and lying to cover it up. Section 406(b)(1) bars fiduciaries from receiving compensation for services to plans if self-dealing is involved in the transaction. Patelco Credit Union v. Sahni, 262 F.3d 897, 910-11 (9th Cir. 2001) (408(b)(2) provides no safe harbor for self-dealing); see Whitfield v. Tomasso, 682 F. Supp. 1287, 1304 (E.D.N.Y. 1988). No amount of self-dealing is permissible. Blue Cross, which egregiously violated this prohibition here, thus incorrectly claims (Br. 58-60) that it can use the exemption to apply "savings" from network access to offset the judgment.<sup>13</sup> If Blue Cross believed that its fees were inadequate, it should have negotiated for higher fees in an arms-length transaction, not simply taken the money from funds intended to fund ERISA-covered benefits.

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<sup>13</sup> Blue Cross argues (Br. 60) that because the Secretary issues prohibited transaction exemptions under section 408 for transactions that would otherwise violate section 406(b), section 408 must necessarily apply to section 406(b). However, Blue Cross ignores the Secretary's regulatory interpretation of the statute as barring any exemption from a self-dealing violation. Furthermore, even if an exemption were theoretically permitted in this situation, section 408(a), which is the source of the Secretary's authority to grant exemptions to certain otherwise prohibited transactions, permits the Secretary to grant only those exemptions that are in the interests of the plan and its participants and beneficiaries, and protective of the rights of participants and beneficiaries. Neither of those factors applies to the egregious facts of this case. In any event, Blue Cross has not sought and the Secretary has not granted an exemption here.

## CONCLUSION

For the reasons stated, the district court decision should be affirmed.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I hereby certify that the foregoing brief complies with the type-volume limitations provided in Fed. R. App. P. 32(a)(7)(B). The foregoing brief contains 8,249 words of Times New Roman (14 point) regular type. The word processing software used to prepare brief was Microsoft Office Word 2010.

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Dated: December 10, 2013

CERTIFICATE OF SERVICE

I hereby certify that on this 10th day of December, 2013, pursuant to 6th Cir.

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