St. Mary's Law Journal

Volume 22 | Number 4 Article 11

1-1-1991

# ERISA Preempts All Texas Causes of Action That Relate to an Employee Benefit Plan Including the Insurance Code, the Deceptive Trade Practices Act and Common Law.

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# RECENT DEVELOPMENTS

**INSURANCE—ERISA—ERISA PREEMPTS ALL TEXAS CAUSES OF ACTION THAT RELATE TO AN EMPLOYEE BENEFIT PLAN INCLUDING THE INSURANCE CODE, THE DECEPTIVE TRADE PRACTICES ACT AND COMMON LAW.** *Cathey v. Metropolitan Life Ins. Co.*, 34 Tex. Sup. Ct. J. 309 (Jan. 30, 1991).

In the mid-1970's, Bette Cathey was diagnosed as having multiple sclerosis. Cathey's physicians recommended home nursing care due to her worsening condition. At the time, Cathey assumed that the cost of her medical care would be covered by her husband's insurance plan. This plan, the "Dow" plan, was a group insurance plan her husband had acquired through his employer, Dow Chemical.

Until 1985, Metropolitan Life Insurance Company ("Met") paid for Mrs. Cathey's nursing expenses pursuant to its role as the claims administrator. In 1985, however, Met informed the Catheys that payment for the home nursing care would be discontinued because no medical necessity existed.

In response, the Catheys filed suit against Met alleging multiple common law and statutory causes of action including: (1) breach of contract under the Texas Insurance Code article 3.62; (2) unfair insurance practices under the Texas Insurance Code article 21.21; (3) deceptive trade practices, unfair insurance practices, and unconscionable conduct in violation of sections 17.46 and 17.50 of the Texas Deceptive Trade Practices Act; and (4) breach of the duty of good faith and fair dealing, negligence, and gross negligence. The Catheys did not assert any federal causes of action pursuant to the Employee Retirement Income Security Act ("ERISA").

The trial court found each cause of action preempted by ERISA and rendered summary judgment in favor of the defendants. The court of appeals affirmed the trial court's summary judgment, holding that all of the Cathey's causes of action were preempted by ERISA. The Texas Supreme Court, in turn, affirmed the appeals court decision and ruled that ERISA preempted all of the Cathey's state law causes of action.

ERISA was enacted in 1974 to improve employee benefit and pension

plans. *See Shaw v. Delta Airlines Inc.*, 463 U.S. 85, 90 (1983); *see also* H.R. REP. NO. 93-533, 93d Cong., 2d Sess. __, *reprinted in* 1974 U.S. CODE CONG. & ADMIN. NEWS 4639, 4639. ERISA accomplished this goal by requiring plan administrators to follow extensive reporting, disclosure, and fiduciary responsibilities in regard to both pension and welfare plans. Employee Retirement Income Security Act (ERISA), 29 U.S.C. §§ 1021-1031, 1101-1114 (1974) (current version at 29 U.S.C. § 1021-1031, 1101-1114 (1988)). ERISA does not, however, mandate that employers provide benefits or determine what types of benefits an employer must provide. *Shaw*, 463 U.S. at 91. ERISA was also intended to provide employees with benefit and pension plan protection that state laws had formerly been unable to achieve. *See* Note, *Defining the Contours of ERISA Preemption of State Insurance Regulation: Making Employee Benefit Plan Regulation an Exclusively Federal Concern*, 42 VAND. L. REV. 607-08 (1989). Thus, Congress included a broad preemption provision that would result in ERISA preempting any state law that "related to" an employee benefit plan. *See* Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1144 (1974) (current version at 29 U.S.C. § 1144 (1988)); *see also Pilot Life Ins. Co. v. Dedeaux*, 481 U. S. 41, 45-47 (1987) (defining broad nature of ERISA preemption provision). In *Shaw v. Delta Air Lines, Inc.*, the United States Supreme Court defined "relate to" to mean "a connection with or reference to such a plan." 463 U.S. at 96-97. Congress originally attempted to mitigate the effect of the "preemption" clause by creating three statutory exceptions to preemption in what is commonly known as the "savings clause." *See* Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1144(b)(2)(A) (1974) (current version at 29 U.S.C. § 1144 (b)(2)(A) (1988)); *see also* Chittenden, *ERISA Preemption: The Demise of Bad Faith Actions in Group Insurance Cases*, 12 S. ILL. U.L.J. 517, 519 (1988). These exceptions save from preemption any state law which regulates insurance, banking, or securities. *See* Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1144(b)(2)(A) (1988). However, the "savings clause" is modified by the "deemer clause" which states that no employee benefit plan shall be "deemed" to be an insurance company in order to fall within "savings clause" protection. Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1144(b)(2)(B) (1988).

Although an employer may provide a combination of pension, health, and life insurance benefits, it is generally recognized that providing "medical, surgical, hospital, death or disability" benefits will bring the plan within the ERISA requirements. *See* Bishop & Denney, *Hello ERISA, Good-Bye Bad Faith: Federal Preemption of DTPA, Insurance Code, and Common Law Bad Faith Claims*, 41 BAYLOR L. REV. 267, 270 (1989); *see also* Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1002(1)(A) (1988). Once the plan is considered an "ERISA" plan, any state law which "relates

to" the plan will be preempted unless it falls within the "savings clause." *Metropolitan Life Ins. Co. v. Massachusetts*, 471 U.S. 724, 732-33 (1985).

One of the most confusing conflicts between the preemption and savings clauses arises when an employee, subject to an ERISA plan, attempts to sue his benefit plan insurer pursuant to a state statutory or common law cause of action. *See* Comment, *ERISA Preemption of California Tort and Bad Faith Law: What's Left?*, 22 U.S.F. L. REV. 519, 533 (1988) (noting unclear nature of ERISA preemption). The United States Supreme Court was faced with such a conflict in *Pilot Life*, and held that state law claims for common law breach of contract and tort, brought by employees against their benefit plan insurers, were preempted by ERISA. 481 U.S. at 47-51. The Court reasoned that to fall within the savings clause of ERISA, a state law must satisfy a three prong test that shows: (1) the law in question has the effect of spreading a policyholder's risk; (2) the law is "an integral part of the policy relationship;" and (3) the law "is limited to entities within the insurance industry." *Id.* at 48-52; *see also* McCarren-Ferguson Act, 15 U.S.C. §§ 1011-1015 (1988) (Act defines "business of insurance" in original federal grant of state's regulatory powers). Applying this test, the *Pilot Life* Court determined that the state causes of action in question were of general application, not specifically designed to regulate insurance, and were thus preempted by ERISA. *See Pilot Life*, 481 U.S. at 50.

Following *Pilot Life*, courts have consistently held that state laws which were not specifically designed to regulate insurance would be preempted by ERISA when applied to benefit plan insurers. *See, e.g., Iron Workers Mid-South Pension Fund v. Terotechnology*, 891 F.2d 548, 553 (5th Cir. 1990); *Ramirez v. Inter-Continental Hotels*, 890 F.2d 760, 762-63 (5th Cir. 1989); *Cefalu v. B.F. Goodrich*, 871 F.2d 1290, 1294-95 (5th Cir. 1989). A sampling of state common law claims that cannot be brought against an ERISA plan insurer includes: (1) breach of implied covenant of good faith and fair dealing; (2) breach of contract; (3) outrage and fraudulent denial of coverage; (4) bad faith; and (5) negligence. *See Ramirez*, 890 F.2d at 762-63 (negligence preempted); *Cantrell v. Great Republic Ins. Co.*, 873 F.2d 1249, 1252-54 (9th Cir. 1989) (good faith and fair dealing preempted); *Settles v. Golden Rule Ins. Co.*, 715 F. Supp. 1021, 1023 (D. Kan. 1989) (outrage and fraudulent denial of coverage preempted); *Tomcyzk v. Blue Cross & Blue Shield United*, 715 F. Supp. 914, 917 (E.D. Wis. 1989) (bad faith preempted); *Shaw v. International Ass'n of Machinists and Aerospace Workers*, 563 F. Supp. 653, 658-59 (C.D. Cal. 1983), *aff'd*, 750 F.2d 1458 (9th Cir. 1985) (breach of contract preempted). In addition, a number of state statutes have been preempted, including a wide range of categories such as: (1) state criminal laws specifically directed at benefit plans; (2) state health insurance acts; and (3) state securities regulations. *See St. Paul Elec. Workers Welfare Fund v. Markman*, 490 F. Supp. 931, 934 (D. Minn. 1980) (health insurance act pre-

empted); *Hurn v. Retirement Fund Trust of Plumbing, Heating & Piping Indus.*, 424 F. Supp. 80, 82 (C.D. Cal. 1976) (state securities laws prempted); *Commonwealth v. Federico*, 419 N.E.2d 1374, 1377-78 (Mass. 1981) (criminal laws preempted). Aside from these barriers to state law causes of action, it is possible under the *Pilot Life* standard for a state statute to "regulate insurance" within the meaning of the "savings clause." *See, e.g., Northern Group Servs., Inc. v. Auto Owners Ins. Co.*, 833 F.2d 85, 95 (6th Cir. 1987) (statute requiring ERISA coordination with no-fault auto insurers not preempted); *United Food & Commercial Workers v. Pacyga*, 801 F.2d 1157, 1161 (9th Cir. 1986) (allowing coordination of benefits statute); *State Farm Mut. Auto Ins. Co. v. American Community Mut. Ins. Co.*, 659 F. Supp. 635, 637 n.2 (E.D. Mich. 1987) (allowing coordination of no-fault insurance with other policies). For instance, in *Blue Cross and Blue Shield v. Bell*, the Tenth Circuit Court of Appeals considered a Kansas statute that required insurers to include certain minimum coverages in their policies. 798 F.2d 1331, 1334-36 (10th Cir. 1986). The court applied the three prong test set out in *Pilot Life* and found that all three elements were satisfied. *Id.* at 1334-35. Thus, the statute was saved from preemption. *Id.* at 1336.

Similar to other jurisdictions, Texas has a number of common law and statutory causes of action that may be brought against an insurer for his wrongful conduct. Among the most prevalent are actions for: (1) delay in payment of losses; (2) unfair competition and practices; (3) deceptive trade practices; and (4) numerous common law claims including misrepresentation, breach of contract, fraud, and bad faith. *See* TEX. INS. CODE ANN. arts. 3.62, 21.21 (Vernon 1981 & Supp. 1991); TEX. BUS. & COM. CODE ANN. § 17.50 (Vernon 1987 & Supp. 1991); Bishop & Denney, *Hello ERISA, Good-Bye Bad Faith: Federal Preemption of DTPA, Insurance Code, and Common Law Bad Faith Claims*, 41 BAYLOR L. REV. 267, 272-73 (1989). The Fifth Circuit Court of Appeals has considered some of these causes of action when asserted against benefit plan insurers, and has often held that such actions are preempted by ERISA. *See, e.g., Ramirez*, 890 F.2d at 762-64; *Boren v. N.L. Indus.*, 889 F.2d 1463, 1465-66 (5th Cir. 1989), *cert. denied*, ___ U.S. ___, 110 S. Ct. 3283, 111 L. Ed. 2d 792 (1990); *Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan Enters.*, 793 F.2d 1456, 1465 (5th Cir. 1986), *cert. denied*, 479 U.S. 1034 (1987). In the recent case of *Ramirez v. Inter-Continental Hotels*, an employee covered by a group medical plan sued his employer and benefit plan insurer alleging breach of contract, breach of fiduciary duty, negligence, and violations of the Texas Insurance Code and the Deceptive Trade Practices Act (DTPA). 890 F.2d at 762. The Fifth Circuit Court of Appeals analyzed the common law and statutory DTPA causes of action and held that the claims were preempted. *Id.* at 763-64. Further, the court applied the *Pilot Life* three prong test and determined that article 21.21 of the Texas Insurance Code, regulating unfair

competition and practices, was not a law that regulated insurance within the savings clause definition and was also preempted. *Id.*

Texas state courts have also been faced with similar claims made by insureds against their benefit plan insurers, and have quickly preempted those same statutory and common law causes of action alleged in *Ramirez*. *See, e.g.*, *Silva v. Aetna Life Ins. Co.*, No. 13-90-147-CV (Tex. App.—Corpus Christi Jan. 24,1991, n.w.h.)(WL 5088); *Cathey v. Metropolitan Life Ins. Co.*, 764 S.W.2d 286, 290-91 (Tex. App.—Houston [1st Dist.] 1988), *aff'd*, 34 Tex. Sup. Ct. J. 309 (Jan. 30, 1991); *Gorman v. Life Ins. Co. of N. Am.*, 752 S.W.2d 710, 714 (Tex. App.—Houston [1st Dist.] 1988, writ granted); *E-Systems, Inc., v. Taylor*, 744 S.W.2d 956, 958-60 (Tex. App.—Dallas 1988, writ denied); *Sams v. N.L. Indus., Inc.*, 735 S.W.2d 486, 489 (Tex. App.—Houston [1st Dist.] 1987, no writ); *Giles v. TI Employees Pension Plan*, 715 S.W.2d 58, 59 (Tex. App.—Dallas 1986, writ ref'd n.r.e.); *see also Ingersoll-Rand Co. v. McClendon*, 779 S.W.2d 69, 71 (Tex. 1989), *rev'd*, __ U.S. __, __, 111 S. Ct. 403, 486, __ L. Ed. 2d __, __ (1990). Generally, the common law causes of action were the easiest to preempt because they related to a benefit plan, but were clearly not specifically designed to regulate insurance. *See Cathey*, 764 S.W.2d at 290. In contrast, Texas employees held out, hoping that Texas' state courts would find that articles 3.62 and 21.21 of the Texas Insurance Code were laws that were specifically designed to regulate insurance within the savings clause. *See Silva*, No. 13-90-147-CV (WL 5088) (employee's sole state law cause of action article 21.21 Insurance Code). In fact, the Houston Court of Appeals for the First District in *Cathey v. Metropolitan Life* noted that the Texas legislature's express purpose in enacting article 21.21 was to regulate trade practices in the business of insurance. 764 S.W.2d at 291. Following this intent, the court concluded that article 21.21 did fit the *Pilot Life* three prong test to qualify a state law for the savings clause. *Id.* However, the court ruled that the deemer clause prevented any state regulation of an insurance company's conduct concerning a benefit plan or its participants. *Id.*

With the declaration in *Cathey* that article 21.21 fell within the savings clause, other inroads into ERISA began to emerge. In *Hermann Hosp. v. Aetna Life Ins. Co.*, the Houston Court of Appeals for the Fourteenth District held that a hospital which had been assigned a patient's benefit plan proceeds could sue the benefit plan insurer for negligent misrepresentation and unfair and deceptive trade practices under article 21.21 of the Texas Insurance Code. 803 S.W.2d 351, __ (Tex. App.—Houston [14th Dist.] 1990, n.w.h.); *see also Memorial Hosp. Sys. v. Northbrook Life Ins. Co.*, 904 F.2d 236, 245-50 (5th Cir. 1990) (allowing article 21.21 claim, negligent misrepresentation, equitable estoppel). The court, relying on a Fifth Circuit case, *Memorial Hosp. Sys. v. Northbrook Life Ins. Co.*, reasoned that the hospital's claims were not preempted because the "gravamen" of the hospital's

claim was not based upon the policy proceeds, but upon an "independent" misrepresentation by the insurance company. *Hermann Hosp.*, 803 S.W.2d at ___.

The Texas Supreme Court also seemed to be divided over the extent of the ERISA preemption. In *McClendon v. Ingersoll-Rand Co.*, the court, in a 5-4 decision, held that an employer who had fired an employee to avoid paying retirement benefits could still be sued for wrongful discharge despite ERISA's preemption provision. 779 S.W.2d 69, 71-73 (Tex. 1989), *rev'd*, ___ U.S. ___, 111 S. Ct. 403, ___ L. Ed. 2d ___ (1990). Thus, with the lower court in *Cathey* declaring that article 21.21 falls within the savings clause and preemption exceptions being recognized for benefit plan assignees such as hospitals, it appeared possible that the Texas Supreme Court's division would at least preserve article 21.21 as a weapon for employees against their benefit plan insurers. However, on December 3, 1990, the United States Supreme Court reversed the Texas Supreme Court's decision in *Ingersoll-Rand Co. v. McClendon*. *See* ___ U.S. ___, ___, 111 S. Ct. 478, 483, ___ L. Ed. 2d ___, ___ (1990). The Court noted that the Texas wrongful discharge action in question specifically mentioned benefit plans which in turn gave the Court no difficulty in concluding that the cause of action "relates to" a benefit plan. ___ U.S. at ___, 111 S. Ct. at 483, ___ L. Ed. 2d at ___. *See generally* TEX. GOV'T CODE ANN. Title 8 (Vernon Supp. 1990) (statutes evidence strong interest in pension and benefit plans). In addition, the Court held that the employee's claims were preempted even though he was not suing for the benefit plan proceeds, but for future lost wages. *Ingersoll Rand Co.*, ___ U.S. at ___, 111 S. Ct. at 481, ___ L. Ed. 2d at ___.

Following what may be described as a cue from the United States Supreme Court, the Texas Supreme Court in *Cathey* finally ruled that causes of action based in state law, brought by an employee against his benefit plan insurer, are preempted by ERISA. The court first recited the relevant portion of the ERISA preemption provisions that had given ERISA such far reaching authority. In addition, the Court referred to the United States Supreme Court's decisions in *Pilot Life*, *Shaw*, and most recently *Ingersoll-Rand Co.* which have given ERISA's preemption provision a loosely defined and broad interpretation. Finally, the court recited the Fifth Circuit's decisions and other Texas decisions that have followed the United States Supreme Court's lead in preempting Texas' common law and statutory causes of action. From this broad base of judicial authority, the Court concluded that the Cathey's state law claims were "related to" a benefit plan and were thus preempted by ERISA.

The anticipation that the Texas Supreme Court would rule that article 21.21 was within the savings clause was quickly dispelled when the court ruled that the United States Supreme Court decisions in *Pilot Life* and *Ingersoll-Rand Co.* evidenced strong congressional intent that all causes of action

for improper claims processing be preempted by ERISA. Unfortunately, the court saw it as unnecessary to analyze the Texas Insurance Code's provisions according to the three prong "savings clause" test developed in *Pilot Life*.

Justice Doggett, in his concurring opinion, noted the failure of the Texas Supreme Court and United States Supreme Court to fully recognize the savings clause and the deference Congress had intended for state insurance regulation when it passed the McCarren-Ferguson Act. Justice Doggett illuminated the fact that as a result, employees who obtained health care insurance from their employers would be left without a wide array of state law claims that an individual purchaser of the exact same policy would have at his disposal.

It is clear from the volume of precedent in federal and state courts that the decision in *Cathey* is somewhat predictable. In one decision, the Texas Supreme Court took away the right of a Texas worker to sue his benefit plan insurer. This decision may only have done what the United States Supreme Court in *Ingersoll-Rand Co. v. McClendon* indicated that it might eventually do if presented with a similar case. However, it is disappointing that the Texas Supreme Court did not go into greater analysis of the Texas Insurance Code's article 21.21 and its relation to ERISA's savings clause. The Texas Supreme Court did, fortunately, restrict its decision to the facts presented in *Cathey*, leaving intact for appeal situations similar to those in *Hermann Hosp.* where an assignee of an employee's benefit plan proceeds sues an insurance company, not for the proceeds of the policy, but for its independent wrongful conduct.

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