ASSESSING THE IMPACT OF CONFLICT OF INTEREST ON THE DECISIONS OF ERISA FIDUCIARIES

The Honorable H. Brent McKnight[*]

"No one can serve two masters."[1]

> A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions. Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court.[2]

The Employee Retirement Income Security Act of 1974 (ERISA)[3] permits fiduciaries with a conflict of interest to make decisions about granting or denying benefits, but it requires that the decisions be made solely for the beneficiaries.[4] When a denial of benefits by a fiduciary with a conflict of interest is contested under § 1132(a)(1)(B) of the ERISA statute,[5] courts must decide whether the decision to deny benefits was influenced by compromised loyalty. In other words, courts must determine whether the discretion accorded the fiduciary by the plan language was abused. How courts should make this decision is the subject of this article.

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[1] *Matthew* 6:24a (New King James Version).

[2] Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928) (Cardozo, C.J.) (citations omitted).

[3] *See* 29 U.S.C. §§ 1001-1461 (1994).

[4] *See* John H. Langbein, *The Supreme Court Flunks Trusts*, 1990 SUP. CT. REV. 207, 213. As Professor Langbein observed,

> Perhaps the feature of ERISA architecture that most clearly manifests the tension within ERISA's transposed norms of private trust law is ERISA's authorization of the nonneutral fiduciary. This is the creature who holds center stage in [*Bruch v. Firestone Tire & Rubber Co.*, 828 F.2d 134 (3d Cir. 1987)]. ERISA section 408(c)(3) authorizes the employer or other plan sponsor to have its own "officer, employee, agent, or other representative" serve as the trustee or in other fiduciary capacities for the plan.

Id.

[5] *See* 29 U.S.C. § 1132(a)(1)(B) (1994).

ERISA does not specify the appropriate standard of judicial review for a fiduciary decision. Instead, courts are instructed to develop a federal common law informed by principles of trust law.[6] In *Firestone Tire & Rubber Co. v. Bruch*,[7] the United States Supreme Court handed down the basic principles to guide this inquiry. The Fourth Circuit Court of Appeals has appropriated these principles in tests designed to require and guide consideration of the various ways conflict of interest can influence the fiduciary's decision. In *Booth v. Wal-Mart Stores, Inc.*,[8] the Fourth Circuit provided a comprehensive restatement of these tests. This article discusses how these tests operate.

One of the greatest difficulties in the current case law is that conflict of interest in ERISA cases is subject to a determination of "reasonableness." As in other areas of the law, the normative turbulence imported by the fact-designation "conflict of interest" roils the analytic of "reasonableness." It is unclear how the water is to be calmed. A great strength of the Fourth Circuit's approach is that it recognizes and captures the complexity of the decision. It acknowledges that conflict of interest works in various ways. It recognizes the difficulty of its inferential detection by reviewing courts. It attempts no simple answers to a complicated problem. The approach reflects several consequences: *Firestone*'s making conflict of interest, with its normative overtones, just one factor among others not to carry its normative load; categorizing conflict of interest with those other factors despite its different nature and its effects on those other factors; displacing conflict of interest from its centrality in the Third Circuit's *Bruch v. Firestone Tire & Rubber Co.*[9] decision, "the still point of the turning world,"[10] to mere commonality among other factors; and ERISA permitting fiduciaries to have conflicts in the first place because of the goal to encourage companies to set up plans, not as a result of fidelity to trust principles.

In the sections that follow, this article discusses *Firestone* and the uncertainty it has caused by its analysis of conflict of interest; the differing approaches other circuits have adopted to complete *Firestone*'s analysis; the Fourth Circuit's approach to *Firestone*; and the Fourth Circuit's recognition and elucidation of the various ways conflict of interest can influence a fiduciary's decision.

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[6] *See* Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 110 (1989).

[7] 489 U.S. 101 (1989).

[8] 201 F.3d 335 (4th Cir. 2000).

[9] 828 F.2d 134 (3d Cir. 1987).

[10] T.S. ELIOT, *Burnt Norton*, *in* COLLECTED POEMS 177, 177 (1963).

I. UNCERTAINTY CAUSED BY *FIRESTONE*'S ANALYSIS OF CONFLICT OF INTEREST

> Consistent with the established principles of trust law, we hold that a denial of benefits challenged under § 1132(a)(1)(B) is to be reviewed under a *de novo* standard unless the benefit plan gives the administrator or fiduciary discretionary authority to determine eligibility for benefits or to construe the terms of the plan. *Because we do not rest our decision on the concern for impartiality that guided the Court of Appeals*, we need not distinguish between types of plans or focus on the motivations of plan administrators and fiduciaries. *Thus, for purposes of actions under § 1132(a)(1)(B), the de novo standard of review applies regardless of whether the plan at issue is funded or unfunded and regardless of whether the administrator or fiduciary is operating under a possible or actual conflict of interest. Of course, if a benefit plan gives discretion to an administrator or fiduciary who is operating under a conflict of interest, that conflict must be weighed as a "facto[r] in determining whether there is an abuse of discretion."*[11]

With these words, the Supreme Court announced the standard governing review of denial of benefits challenged under ERISA § 1132(a)(1)(B). A reviewing court is first required to decide whether the plan confers discretion on the fiduciary.[12] If the plan does not, the decision is to be reviewed under a *de novo* standard.[13] If the plan does, however, the decision is to be reviewed under an abuse of discretion standard, even if the fiduciary has a conflict of interest.[14] Whether a conflict of interest exists is only to be weighed as a factor in determining whether there is abuse of discretion.[15]

The Supreme Court's *Firestone Tire & Rubber Co. v. Bruch*[16] decision affirmed the Third Circuit's *Bruch v. Firestone Tire & Rubber Co.*[17] decision, but it changed the analysis in an important way. The Third Circuit placed conflict of interest at the center of its analysis—its major premise—while the Supreme Court relegated conflict of interest to the status of one factor or consideration among others. Where the Third Circuit regarded conflict of interest as normatively *sui generis* and controlling in light of the ancient imperative of judicial vigilance against its effect, the Supreme Court treated it in the same vein as factors without necessary normative import, leaving the lower courts to

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[11] *Firestone*, 489 U.S. at 115 (quoting RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. d (1959)) (citation omitted) (second and third emphases added).

[12] *See id.*

[13] *See id.*

[14] *See id.*

[15] *See id.*

[16] 489 U.S. 101 (1989).

[17] 828 F.2d 134 (3d Cir. 1987).

accomplish the integration. As might have been anticipated, the circuits have not agreed, which will be considered in more detail below.

The *Firestone* case arose out of Firestone Tire & Rubber Co.'s sale of its Plastics Division to Occidental Petroleum Co. on November 3, 1980.[18] Most of the salaried employees of the Plastics Division were given the opportunity to remain in the positions they held with Firestone.[19] Most of these employees accepted the opportunity.[20]

Firestone maintained three welfare or pension plans covering severance, retirement, and stock purchase.[21] After the sale, Firestone denied severance pay and certain early retirement benefits, and it did not satisfy class members' inquiries about vesting of rights to purchase stock.[22] Plaintiffs filed an ERISA action against Firestone.[23]

Based on construction of the plan's language, the district court deferred to decisions by the plan administrator and granted summary judgment to Firestone on these ERISA claims.[24] The court also dismissed several other counts.[25]

> At the heart of the district court's opinion granting summary judgment . . . was the court's deference to decisions by the plan administrator. . . . The district court believed that it could not reverse the administrators' constructions of the plans' terms unless they were arbitrary and capricious, and it felt obliged to uphold the administrator's decisions given that standard of review.
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> At the core of the plaintiffs' challenge to the district court's decision is their contention that the district court should not have applied the arbitrary and capricious standard . . . .[26]

The Third Circuit affirmed the district court's grant of summary judgment as to Count III (denial of early retirement benefits) and Count V (vesting of stock purchase rights) but reversed as to Count I (severance pay, with the administrator's decision resting entirely upon a construction of a key term in the plan) and Count VII (proper response to request for information).[27] What the Third Circuit opinion turned on was its treatment of the "arbitrary and capricious" standard of review.

The Third Circuit's treatment of the "arbitrary and capricious" standard of review hinged on the existence of (or the "fact" of) conflict of

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[18] *See* 489 U.S. at 105.
[19] *See id.*
[20] *See id.*
[21] *See id.*
[22] *See id.* at 106.
[23] *See id.*
[24] *See id.* at 106-07.
[25] *See Bruch*, 828 F.2d at 137.
[26] *Id.*
[27] *See id.* at 136.

interest and the "role" it played in the case. The facts that Firestone itself administered the plan and that Firestone was the sole source of funding for the severance pay plan (Count I) were keys to this opinion.[28] This was a classic, inescapable conflict of interest, which the court underscored in the second sentence of the first paragraph of the opinion.

> [M]ost courts of appeals have applied the arbitrary and capricious standard when considering challenges to plan administrators' denial of benefits. Most of these courts—though . . . not all—have applied this standard without stopping to ascertain whether the plan's funding obligations gave the plan administrator an interest adverse to the claimants with respect to the question whether benefits should be paid.
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> The arbitrary and capricious standard has not been applied unanimously, however, or without misgivings. First, recognizing the possibility that an interested decisionmaker's bias may prejudice him against the claimant and thereby deprive the claimant of an impartial hearing, this Court has explained in detail why it refused to defer to decisions made under ERISA by such fiduciaries.[29]

After thoughtfully discussing cases applying the arbitrary and capricious standard in instances in which the decisionmaker is the judge in its own cause—vulnerable to the pull of divided loyalty—and after discussing the teaching of the Restatement (Second) of Trusts, the court concluded that

> [t]he same degree of deference should be accorded to investment decisions made by plan administrators, so long as a conflict of interest is not alleged. . . . [A]s the discussion of the common law principles also makes clear, deference is inappropriate to the extent that the party who is alleged to have benefited from the challenged decision is not a beneficiary.[30]

As to the Firestone plan, the court remanded the question of whether the trustee had not in fact been impartial.[31] The court noted that, in any event, the trustee's impartiality could not be guaranteed:

> In the unfunded pension plan at issue in Count I of the complaint in this case, however, there is no assurance of the trustee's impartiality. The plan is controlled entirely by the employer, not by a group evenly divided between employer and employees. Because the plan is unfunded, every dollar provided in benefits is a dollar spent by defendant Firestone, the employer; and every dollar saved by the administrator on behalf of his employer is a dollar in Firestone's pocket. As we have already seen, the principle articulated in § 187 does not govern judicial review of such a trustee's decisions.[32]

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[28] *See id.*

[29] *Id.* at 138-39 (citations omitted).

[30] *Id.* at 144-45 (footnote & citation omitted).

[31] *See id.* at 136.

[32] *Id.* at 144.

It is important to recognize that the court considered deference appropriate *if* no conflict of interest were alleged. Quoting from the *Meinhard v. Salmon*[33] decision, which prefaces this article, the court found that the principles of trust law require the decisions of trustees to be scrutinized "with the greatest possible care."[34] The analytical starting point for review should be "principles governing construction of contracts between parties bargaining at arms' length,"[35] "steering a middle course"[36] between resolving any ambiguity in favor of the beneficiaries and allowing the trustee's decision to stand unless it is unreasonable.[37] The court did not call this *de novo* review, but its analysis suggests an approach consistent with *de novo* review. The court went so far as to say that applying the arbitrary and capricious standard was "wrong."[38] According to this court's language and practice, then, the analysis is not accomplished by treating conflict of interest as a factor in determining whether the decision was arbitrary and capricious, but by employing a different analysis altogether: one that is contract-based. The court does not commit to using contract-based analysis in reviewing decisions that do not turn upon defining a term in the contract, but it never retreats from its thesis that conflict of interest, taken alone, renders the arbitrary and capricious standard inappropriate.

The Supreme Court granted certiorari[39] in part to resolve conflicts among the circuits as to the appropriate standard of review in challenges to denials of benefits brought pursuant to § 1132(a)(1)(B). In its decision of February 21, 1989, the Court did "not rest [its] decision on the concern for impartiality that guided the Court of Appeals."[40] Rather, Justice O'Connor's opinion instructed that reviewing courts are to ask whether the plan "gives the administrator or fiduciary discretionary authority to determine eligibility for benefits or to construe the terms of the plan."[41] Thus, absent discretionary authority, a denial of benefits is to be reviewed under a *de novo* standard.[42] If the plan confers discretionary authority, a denial of benefits is to be reviewed under an abuse of discretion standard.[43] Rather than triggering *de novo* review, conflict of

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[33] 164 N.E. 545 (N.Y. 1928).

[34] *Bruch*, 828 F.2d at 145.

[35] *Id.*

[36] *Id.*

[37] *See id.*

[38] *Id.* at 147.

[39] *See* Firestone Tire & Rubber Co. v. Bruch, 485 U.S. 986 (1988).

[40] *Firestone*, 489 U.S. at 115.

[41] *Id.*

[42] *See id.*

[43] *See id.* The Court notes that in the law of trusts "[a] trustee may be given power to construe disputed or doubtful terms, and in such circumstances the trustee's

interest is to be weighed as a factor in determining whether there is abuse of discretion.[44] If the plan grants discretion, the standard of review is to be abuse of discretion, even if there is a conflict of interest. The Court rested its conclusion on trust law principles, making "a deferential standard of review appropriate when a trustee exercises discretionary powers," on the condition that the plan granted the trustees those powers.[45]

The Court did not discuss how reviewing courts are to weigh the conflict of interest factor. It merely quoted from comment d to section 187 of the Restatement (Second) of Trusts, which reads as follows:

> d. Factors in determining whether there is an abuse of discretion. In determining the question whether the trustee is guilty of an abuse of discretion in exercising or failing to exercise a power, the following circumstances may be relevant: (1) the extent of the discretion conferred upon the trustee by the terms of the trust; (2) the purposes of the trust; (3) the nature of the power; (4) the existence or non-existence, the definiteness or indefiniteness, of an external standard by which the reasonableness of the trustee's conduct can be judged; (5) the motives of the trustee in exercising or refraining from exercising the power; (6) the existence or nonexistence of an interest in the trustee conflicting with that of the beneficiaries.[46]

The Restatement provides no guidance on how to weigh a conflict of interest and refers to its existence rather than its effect. Its effect is addressed in the following comment, which only provides that where a conflict of interest exists, the court may "interfere":

> e. No abuse of discretion. If discretion is conferred upon the trustee in the exercise of a power, the court will not interfere unless the trustee in exercising or failing to exercise the power acts dishonestly, *or with an improper even though not a dishonest motive*, or fails to use his

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interpretation will not be disturbed *if reasonable*." *Id.* at 111 (emphasis added). As the text will show, much will turn upon what "reasonable" means and how it is affected by conflict of interest.

[44] *See id.* at 115.

[45] *Id.* at 111. Professor Langbein criticizes the Court's derivation of a trustee's discretionary powers from the plan as inconsistent with basic trust principles:

> Thus, the Supreme Court reasons that, as a matter of trust law, deference to the trustee's decisionmaking is appropriate only when the trust power in question is particularly granted by the trust instrument.
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> This distinction between trust powers that derive from the background law of trust, and those that derive from the trust instrument, is fundamentally mistaken. It is refuted in the very source that the Court treats as authoritative, section 187 of the Restatement of Trusts. The trustee has discretion unless the instrument or some particular doctrine of trust law denies discretion. Discretion is the norm. What the Supreme Court in *Bruch* calls "the trust law *de novo* standard of review" is simply nonexistent in trust law.

Langbein, *supra* note 4, at 218-19 (footnotes omitted).

[46] RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. d (1959).

> judgment, or acts beyond the bounds of a reasonable judgment. The mere fact that if the discretion had been conferred upon the court, the court would have exercised the power differently, is not a sufficient reason for interfering with the exercise of the power by the trustee.[47]

How, then, is conflict of interest to be weighed? The Court's language is arguably consistent with lessened deference or *de novo* review. The circuits have divided in their answers.

II. HOW THE CIRCUITS HAVE INTERPRETED *FIRESTONE*'S TREATMENT OF CONFLICT OF INTEREST

Where there is conflict of interest, the circuits differ not concerning whether, but how, to lessen deference. There is a very rough division between the "sliding scale" and "presumptively void" courts.[48] This division is inadequate to capture the nuances pertinent to defining the circuits' tests. For example, in Ninth Circuit cases, reference is made to what might be termed a sliding scale analysis[49] and a presumptively void analysis,[50] although the Ninth Circuit has adopted a presumptively void approach.[51] As will be discussed, Fourth Circuit cases refer both to sliding scale analysis and a "considered as if free of conflict" test,[52] which arguably carries *de novo* overtones of *a priori* correctness analysis characteristic of at least the Eleventh Circuit's version of the presumptively void test.[53] This is only to say that such large categorizations are Procrustean and necessarily so, for, as discussed below, conflict of interest is multi-dimensional in its potential impact on fiduciary decisions. Reviewing courts, to be faithful to *Firestone Tire & Rubber Co. v. Bruch*,[54] must approach from more than one direction. This

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[47] *Id.* § 187 cmt. e (emphasis added). The Restatement (Third) leaves these comments unchanged.

[48] Courts in the Eighth and Tenth Circuits have referred to the division in these terms. *See* Buttram v. Central States, Southeast & Southwest Areas Health & Welfare Fund, 76 F.3d 896, 900 n.6 (8th Cir. 1996); Chambers v. Family Health Plan Corp., 100 F.3d 818, 825-27 (10th Cir. 1996).

[49] *See* Taft v. Equitable Life Assurance Soc'y, 9 F.3d 1469, 1474 (9th Cir. 1993) ("Because [of a conflict of interest], we therefore 'impose a more *stringent* version of the abuse of discretion standard.'" (quoting Bogue v. Ampex Corp., 976 F.2d 1319, 1325 (9th Cir. 1992))).

[50] *See* Atwood v. Newmont Gold Co., 45 F.3d 1317, 1323 (9th Cir. 1995) ("Where the affected beneficiary has come forward with material evidence of a violation of the administrator's fiduciary obligation, we should not defer to the administrator's presumptively void decision.").

[51] *See id.*

[52] *See, e.g.*, Doe v. Group Hospitalization & Med. Servs., 3 F.3d 80, 87 (4th Cir. 1993); Ellis v. Metropolitan Life Ins. Co., 126 F.3d 228, 233 (4th Cir. 1997).

[53] *See* Brown v. Blue Cross & Blue Shield, 898 F.2d 1556, 1563-68 (11th Cir. 1990).

[54] 489 U.S. 101 (1989).

situation necessarily results from relegating conflict of interest to the analytical status of one factor among others (although not like the others), rather than, as in the Third Circuit *Bruch v. Firestone Tire & Rubber Co.*[55] opinion, "the still point" around which the rest turns.[56]

A. The "Presumptively Void" Approach

Two cases exemplify the presumptively void approach. First, in *Brown v. Blue Cross & Blue Shield*,[57] the Eleventh Circuit adopted a burden-shifting scheme.[58] If the plaintiff shows a substantial conflict of interest, the burden shifts to the defendant to show that its denial of benefits was not influenced by the conflict.[59] Where substantial conflict of interest is shown, the decision is presumed arbitrary and capricious.[60] This presumption can be rebutted by demonstrating that the decision works to the benefit of all plan beneficiaries.[61]

Brown came before the Eleventh Circuit on appeal after the district court granted summary judgment in favor of Blue Cross/Blue Shield.[62]

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[55] 828 F.2d 134 (3d Cir. 1987).

[56] ELIOT, *supra* note 10, at 177.

[57] 898 F.2d 1556 (11th Cir. 1990).

[58] *See id.* at 1566; *see also* Godfrey v. BellSouth Telecomms., 89 F.3d 755 (11th Cir. 1996); Florence Nightingale Nursing Serv. v. Blue Cross/Blue Shield, 41 F.3d 1476 (11th Cir. 1995), *cert. denied*, 514 U.S. 1128 (1995); Lee v. Blue Cross/Blue Shield, 10 F.3d 1547 (11th Cir. 1994); Anderson v. Blue Cross/Blue Shield, 907 F.2d 1072 (11th Cir. 1990); Newell v. Prudential Ins. Co. of America, 904 F.2d 644 (11th Cir. 1990); Jett v. Blue Cross & Blue Shield, 890 F.2d 1137 (11th Cir. 1989); Freeman v. Sickness and Accident Disability Plan of AT&T Techs., 823 F. Supp. 404 (S.D. Miss. 1993).

[59] *See Brown*, 898 F.2d at 1566.

[60] *See id.* at 1566-67. The reader will recall that *Firestone* made reference to "abuse of discretion." Commentators and courts have discussed the relationship between the earlier and well-established "arbitrary and capricious" and the announced "abuse of discretion" standards. Professor Langbein stated that "[t]his abuse-of-discretion standard is simply the arbitrary-and-capricious standard by another name." Langbein, *supra* note 4, at 218. A Seventh Circuit decision, *Morton v. Smith*, 91 F.3d 867, 870 (7th Cir. 1996), distinguished the terms by reference to the flexibility allowed administrators in plans. A Tenth Circuit decision, noting *Morton*, agrees with the majority of courts that the distinction is semantic and not substantive. *See* Chambers v. Family Health Plan Corp., 100 F.3d 818, 825 n.1 (10th Cir. 1996). The Fourth Circuit has recognized more than a semantic distinction but, following *Firestone*, has reiterated that abuse of discretion is the standard:

> First, we continue to recognize that an "arbitrary and capricious" standard is more deferential to the fiduciary than is an "abuse of discretion" standard. And second, we affirm that the abuse of discretion standard, not the arbitrary and capricious standard, is the appropriate one for judicial review of a fiduciary's discretionary decision under ERISA.

Booth v. Wal-Mart Stores, Inc., 201 F.3d 335, 341 (4th Cir. 2000).

[61] *See Brown*, 898 F.2d at 1567.

[62] *See id.* at 1558.

Brown had been denied hospitalization benefits on the ground that he failed to obtain pre-admission certification.[63] Blue Cross/Blue Shield, which denied the benefits, was responsible for paying the claim.[64] Thus, there was an "inherent conflict between the roles assumed by an insurance company that administers claims under a policy it issued."[65]

Recognizing that the contracting parties had bargained to give Blue Cross/Blue Shield discretion, the court concluded that full *de novo* review would be inappropriate because it failed to take the parties' bargain into account.[66] How, then, under an abuse of discretion standard, should the *fact* and *effect* of conflict of interest be recognized?[67] The court discussed the *fact* of conflict of interest in terms of its "strength," which means, at least in part, whether it is "inherent."[68] It is the strength, substantiality, or significance of the conflict that triggers burden shifting.[69] Although these terms are not precisely defined, common to each term is the conflict's inherence or positioning vis-a-vis the decisions the fiduciary is permitted by the terms of the plan.[70] Thus, "[t]he inherent conflict between the fiduciary role and the profit-making objective of an insurance company makes a highly deferential standard of review inappropriate."[71] Such a consideration has "sliding scale" overtones. In the sliding scale analysis, the stronger the conflict is, the narrower the acceptable range of decisions will be.[72]

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[63] *See id.*

[64] *See id.* at 1561.

[65] *Id.*

[66] *See id.* at 1563.

[67] In the words of the court, "Our task is to develop a coherent method for integrating factors such as self-interest into the legal standard for reviewing benefits determinations." *Id.* at 1561.

[68] *Id.* at 1561-62.

[69] *See id.* at 1564.

[70] This aspect of *Brown*'s reasoning has been noted in *Bailey v. Blue Cross & Blue Shield*, a Fourth Circuit opinion:

> A more thorough explanation might have been necessary had the conflict of interest not been as total as that in this case, where Blue Cross stood as the single beneficiary of a substantial sum based on its denial of benefits. *Cf.* [*Brown*, 898 F.2d at 1564] ("When the members of a tribunal—for example, the trustees of a pension fund—have a serious conflict of interest, the proper deference to give may be slight, even zero; the decision if wrong may be unreasonable.").

67 F.3d 53, 57 (4th Cir. 1995).

[71] *Brown*, 898 F.2d at 1562.

[72] The *Brown* court acknowledged what is a starting point for sliding scale analysis, namely, that except in the theoretical instance in which the conflict is so strong that discretion reduces to zero (this would be the point at which abuse of discretion and *de novo* analysis are one and the same), there is a range of decisions which qualify as "reasonable." Interestingly, having acknowledged that there is a range of acceptable decisions, the

The fact of conflict of interest sets the "outer boundaries of [the] inquiry."[73] The *Brown* court next turned to the effect of conflict of interest. As we shall see with the Fourth Circuit,[74] the analysis should begin by reference to the factors listed in Comment d to section 187 of the Restatement (Second) of Trusts. The sixth and final factor listed there is "the existence or nonexistence of an interest in the trustee conflicting with that of the beneficiaries."[75] That is, whatever we say about the effect of conflict of interest should begin with a recognition of its interplay among factors not carrying their normative loads.[76] Further, whatever conclusions we are to draw about the effect of conflict of interest in a particular case are likely to be inferential (circumstantial). The conclusions are inferred from the fact of conflict of interest in interaction with the decision of and the reasonableness of the fiduciary.[77]

Brown court later treated reasonableness in terms of "right" and "wrong" and *de novo* (meaning *a priori*) analysis. *Id.* at 1566 n.12. Judge Posner recognized the range of decision before *Firestone*: "the arbitrary and capricious standard may be a range, not a point." Van Boxel v. Journal Co. Employees' Pension Trust, 836 F.2d 1048, 1052 (7th Cir. 1987), *quoted in Brown*, 898 F.2d at 1564.

[73] *Brown*, 898 F.2d at 1564.

[74] *See supra* Part III.

[75] RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. d (1959).

[76] The fifth factor, "the motives of the trustee in exercising or refraining from exercising the power," is the exception. *Id.* Conflict of interest, the sixth factor, is one variety of the fifth factor. Both factors are conceptually distinct from the first four (extent of discretion, purposes of the trust, nature of the power, external standards of reasonableness). What might be within the range of acceptability, taking only the first four into account, could be nonetheless improper because the decision was made in one way, as opposed to other ways within acceptability, as a result of the pull of improper motive, including divided loyalty. Such considerations prompted the *Brown* court to require a "*de novo*" (*a priori*) determination of "right" (the first four factors) so as to see what would be "wrong" (error as to the first four factors, or the pull of improper motive or divided loyalty). As will be discussed in the section on the Fourth Circuit, these considerations also prompted the court in *Doe v. Group Hospitalization & Medical Services*, 3 F.3d 80 (4th Cir. 1993), to require an inquiry of what would be acceptable freedom from conflict of interest. Implicit in these approaches is the recognition that the first four factors are categorically different from the last two. The courts were suggesting approaches to the integration of the categorically different factors that *Firestone* required. *Brown* explicitly called for *de novo* review (despite *Firestone*'s limitation of *de novo* review to plans without fiduciary discretion, and despite having explicitly adopted the abuse of discretion standard earlier in the opinion). What *Brown* called *de novo* review can, perhaps, be distinguished from what *Firestone* proscribed in that it is a species of *a priori* determinations considered necessary to the abuse of discretion review. *Doe*'s formulation ("free of conflict of interest") recognized the necessity of the *a priori* determination, but it avoided talk about right and wrong and *de novo* assessment, which seems to displace abuse of discretion. At least arguably, *Brown* called for a return to *de novo* review where there is conflict of interest. The *Brown* Court seemed troubled by the same concerns that prompted the Third Circuit's analysis in *Bruch*.

[77] Despite the admonition that the result will not be disturbed if "reasonable," a court probably would not be likely to overlook conflict of interest (and its effects) proved by direct evidence.

Brown addressed the problem of assessing the effect of conflict of interest by shifting burdens:

> In accordance with the foregoing common law principles, we hold that when a plan beneficiary demonstrates a substantial conflict of interest on the part of the fiduciary responsible for benefits determinations, the burden shifts to the fiduciary to prove that its interpretation of plan provisions committed to its discretion was not tainted by self-interest. That is, a wrong but apparently reasonable interpretation is arbitrary and capricious if it advances the conflicting interest of the fiduciary at the expense of the affected beneficiary or beneficiaries unless the fiduciary justifies the interpretation on the ground of its benefit to the class of all participants and beneficiaries.[78]

In an important footnote to this holding, the court stated, "It is fundamental that the fiduciary's interpretation first must be 'wrong' from the perspective of *de novo* review before a reviewing court is concerned with the self-interest of the fiduciary."[79]

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[78] *Brown*, 898 F.2d at 1566-67.

[79] *Id.* at 1566 n.12 (citations omitted). The Court later disclaimed *de novo* review:

> We emphasize the central theme of our exposition: well-established common-law principles of trusts teach that a fiduciary operating under a conflict of interest may be entitled to review by the arbitrary and capricious standard for its discretionary decisions as provided in the ERISA plan documents, but the degree of deference actually exercised in application of the standard will be significantly diminished. A court should not exercise *de novo* review, but the area of discretion to which deference is paid must be confined narrowly to decisions for which a conflicted fiduciary can demonstrate that it is operating exclusively in the interests of the plan participants and beneficiaries.

Id. at 1568. The fiduciary must "dispel[] the notion that its conflict of interest has tainted its judgment." *Id.* If so, the arbitrary and capricious evaluation is conducted by reference to "other measures," *id.*, presumably the first four factors of the Restatement (Second). *See* discussion *supra* note 76.

If the fiduciary is to meet this burden other than by proving the negative, it must be by showing that the decision was within the range of reasonableness. If so, it is unclear how *de novo* review by reference to a standard determined by the court is thereby avoided.

In *Anderson v. Blue Cross/Blue Shield*, an Eleventh Circuit Court reached that conclusion:

> [The *Brown*] court created a higher standard of review for such situations, requiring the fiduciary to "prove that its interpretation of plan provisions committed to its discretion was not tainted by self-interest" and to show that it operated "exclusively in the interest of the plan participants and beneficiaries." This court held that "a wrong but apparently reasonable interpretation is arbitrary and capricious if it advances the conflicting interest of the fiduciary at the expense of the affected beneficiary or beneficiaries unless the fiduciary justifies the interpretation on the ground of its benefit to the class of all participants and beneficiaries." Practically, we first must determine the legally correct plan interpretation; then, if HMG has interpreted the contract differently, we must ascertain whether HMG was arbitrary and capricious in using a different interpretation.

907 F.2d 1072, 1076 (11th Cir. 1990) (citations omitted).

By shifting the burden of proving the fact that conflict of interest did not have improper effect to the fiduciary, *Brown*, while calling conflict of interest a factor in an abuse of discretion analysis, in fact adopted a modified *de novo* review. Because of this, at least two circuits reject *Brown* as inconsistent with *Firestone*.[80]

The Ninth Circuit, however, has adopted an analysis similar to that of *Brown*. In *Atwood v. Newmont Gold Co.*,[81] the second case exemplifying the presumptively void approach, the court explicitly opted for the *Brown* approach, considering it more consistent with established trust law principles:

> [T]here are at least two very different formulations of the standard. The Fourth and Seventh Circuits use a variable "sliding scale," always applying the abuse of discretion standard, but decreasing the deference given to a conflicted fiduciary's decision in proportion to the seriousness of the conflict. The Eleventh Circuit applies a two-tier standard, using traditional abuse of discretion review unless a "serious conflict" is shown, at which point it will employ a more searching review. Under this standard, if a conflicted fiduciary's interpretation which advances the fiduciary's interest at the expense of the beneficiary's is "wrong" under *de novo* review but still "apparently reasonable," the fiduciary has committed an abuse of discretion unless the plan can show that the interpretation was not made to serve its conflicting interest.
>
> A review of our own cases shows that we have employed a methodology similar to that of the Eleventh Circuit. We ultimately apply a traditional abuse of discretion standard to the decisions of apparently conflicted employer- or insurer-fiduciaries *unless* the affected beneficiary comes forward with further evidence indicating

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[80] *See id.* at 442 (citations omitted); *see also* Whitney v. Empire Blue Cross & Blue Shield, 106 F.3d 475, 477 (2d Cir. 1997). In *Chambers v. Family Health Plan Corp.*, the court forthrightly stated:

> We reject the "presumptively void" test as inconsistent with our holding in *Pitman* [*v. Blue Cross & Blue Shield*, 24 F.3d 118 (10th Cir. 1994)] and the Supreme Court's dictum in *Firestone*. We conclude that the sliding scale approach more closely adheres to the Supreme Court's instruction to treat a conflict of interest as a "facto[r] in determining whether there is an abuse of discretion."

100 F.3d 818, 826 (10th Cir. 1996) (quoting *Firestone*, 489 U.S. at 115).

In *Pagan v. NYNEX Pension Plan*, the Second Circuit distinguished *Brown* as inconsistent with *Bruch*:

> *Bruch* instructs us, however, that the existence of such an alleged conflict does not operate to change the standard of review, but rather becomes "a facto[r] in determining whether there is an abuse of discretion." . . . Accordingly, we review the NYNEX Committee's decision under the arbitrary and capricious standard, irrespective of whether the NYNEX Committee was operating under a possible or actual conflict of interest.

52 F.3d 438, 442 (2d Cir. 1995) (citations omitted).

[81] 45 F.3d 1317 (9th Cir. 1995).

> that the conflicting interest caused a breach of the administrator's fiduciary duty to the beneficiary.
>
> The "less deferential" standard under which we review apparently conflicted fiduciaries has two steps. First, we must determine whether the affected beneficiary has provided material, probative evidence, beyond the mere fact of the apparent conflict, tending to show that the fiduciary's self-interest caused a breach of the administrator's fiduciary obligations to the beneficiary. If not, we apply our traditional abuse of discretion review. On the other hand, if the beneficiary *has* made the required showing, the principles of trust law require us to act very skeptically in deferring to the discretion of an administrator who appears to have committed a breach of fiduciary duty.
>
> Under the common law of trusts, any action taken by a trustee in violation of a fiduciary obligation is presumptively void. Where the affected beneficiary has come forward with material evidence of a violation of the administrator's fiduciary obligation, we should not defer to the administrator's presumptively void decision. In that circumstance, the plan bears the burden of producing evidence to show that the conflict of interest did not affect the decision to deny benefits. If the plan cannot carry that burden, we will review the decision *de novo*, without deference to the administrator's tainted exercise of discretion.[82]

While *Atwood* required proof of the effect of conflict of interest to trigger the presumptively void burden shifting,[83] *Brown* required only a showing of its existence and that it is "serious."[84] Thus, in its recognition of the subtleties of effect of divided loyalty, the *Brown* test is thus the more radical of the two. However, both tests depart from treating conflict of interest as one factor among others in a standard abuse of discretion analysis, such as that called for by *Firestone*. While a sliding scale analysis certainly modifies the abuse of discretion test, it does not depart from that standard. In fealty to what the adopting courts believe to be traditional trust principles, the presumptively void test goes beyond even a modified abuse of discretion analysis. Arguably, it departs from that standard altogether in adjusting for the implicit or explicit effect of conflict of interest. *Brown* forthrightly incorporated *de novo* review, which *Firestone* reserved for plans that do not give discretion to fiduciaries.

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[82] *Id.* at 1322-23 (citations omitted).

[83] *See also* Estate of Shockley v. Alyeska Pipeline Serv. Co., 130 F.3d 403 (9th Cir. 1997); Lang v. Long-Term Disability Plan of Sponsor Applied Remote Tech., Inc., 125 F.3d 794 (9th Cir. 1997); Podolan v. Aetna Life Ins. Co., 107 F.3d 17 (9th Cir. 1997); Snow v. Standard Ins. Co., 87 F.3d 327 (9th Cir. 1996); Winters v. Costco Wholesale Corp., 49 F.3d 550 (9th Cir. 1995), *cert. denied*, 516 U.S. 908 (1995).

[84] See the discussion in *Brown* to the effect that it is unnecessary to demonstrate that the fiduciary succumbed to the pull of divided loyalty and that the effect of conflict of interest may be "unconscious[]." *Brown*, 898 F.2d at 1565-66.

B. The "Sliding Scale" Approach

This article has considered the presumptively void approach taken by the Eleventh and Ninth Circuits. It now turns to the Second and Fourth Circuits, which have adopted "sliding scale" approaches. (Because this article considers the Fourth Circuit approach to be the best approach currently employed by courts, the article will cover it extensively in Parts III and IV).

Pagan v. NYNEX Pension Plan[85] involved a § 1132(a)(1)(B) challenge to a denial of long-term disability benefits by a fiduciary acting under a plan bestowing broad discretion.[86] Citing the *Brown* decision, Pagan contended that deference should not be afforded and that the arbitrary and capricious standard should not apply because the fiduciary labored under a conflict of interest.[87] The alleged conflict was that NYNEX funded the pension plan from operating revenues, thus giving NYNEX an incentive to deny benefits.[88] Members of the NYNEX committee served as plan administrators while also being NYNEX employees.[89]

The court rejected *Brown* as inconsistent with *Bruch*.[90] It stated that the existence of a conflict of interest does not change the standard of review but is a factor in determining whether discretion was abused.[91] Therefore, the denial was reviewed under the arbitrary and capricious standard:

> Under the arbitrary and capricious standard of review, we may overturn a decision to deny benefits only if it was "without reason, unsupported by substantial evidence or erroneous as a matter of law." This scope of review is narrow, thus we are not free to substitute our own judgment for that of the NYNEX Committee as if we were considering the issue of eligibility anew.[92]

The court clarified that "[w]here it is necessary for a reviewing court to choose between two competing yet reasonable interpretations of a pension plan, this Court must accept that offered by the administrators."[93] Finally, "[n]or does Pagan's argument that the presence of a potential conflict of interest warrant [sic] a different

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[85] 52 F.3d 438 (2d Cir. 1995).

[86] *See id.*

[87] *See id.* at 442.

[88] *See id.*

[89] *See id.*

[90] *See id.*

[91] *See id.* at 442.

[92] *Id.* (citations omitted).

[93] *Id.* at 443 (citation omitted).

conclusion. Pagan fails to explain how such an alleged conflict affected the reasonableness of the Committee's decision."[94]

Unlike *Brown*, *Pagan* did not gauge the substantiality or effect of a conflict of interest by engaging in a *de novo* determination and comparison with the actual decision; nor did *Pagan* engage in *Brown*'s burden-shifting in the event of substantial conflict. To the contrary, *Pagan* did not show "how" the conflict "affected" the "reasonableness" of the decision. The court did not say what this requirement means or how it could be satisfied. How could the fact or effect of conflict of interest render an otherwise reasonable decision unreasonable? Is it not the ethical duty of a reviewing court to take conflict of interest into account irrespective of whether the decision is otherwise reasonable? The court did not say that the presence of a conflict of interest, apart from its effect, can render a decision unreasonable. The court was merely looking to the effect of the conflict of interest. Thus, the pull of divided loyalty goes unmonitored if the decision is within the range of reasonableness.

These were the concerns *Brown* attempted to address. The difficulty, as *Pagan* recognized, is that *Brown* took us outside *Bruch*. *Pagan* left us asking whether conflict of interest can be treated as a factor, as *Bruch* required. At the same time, *Pagan* recognized and acted upon the several possibilities of the manifestation of conflict of interest. In other words, if we are no longer to take a Third Circuit *Bruch* approach, making conflict of interest the gatekeeper to the architecture of reasonableness, can we fairly assess its impact?

The *Pagan* approach was refined in *Sullivan v. LTV Aerospace & Defense Co.*[95] The Second Circuit affirmed the district court's denial of summary judgment where the plaintiffs offered an alternative and reasonable interpretation of the plan and raised questions of fact as to whether a conflict of interest had influenced the choice between two reasonable interpretations.[96] The action challenged a denial of severance benefits to former (downsized) employees of the Sierra Research Division of LTV under the LTV Key Employee Retention Plan, an unfunded discretionary plan where the administrator was an employee of the sponsoring company.[97] (This conflict of interest is similar to that in *Pagan*, where the plan was unfunded and members of the administrative committee were employees of the plan sponsors.)[98]

The court refined the *Pagan* analysis as follows:

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[94] *Id.* (citation omitted).

[95] 82 F.3d 1251 (2d Cir. 1996).

[96] *See id.* at 1257.

[97] *See id.* at 1255.

[98] *See supra* text accompanying note 89.

> [A]s we stated in *Pagan*, we decline to concur with the rule in *Brown* and adhere to the arbitrary and capricious standard of review in cases turning on whether the decision was based on an alleged conflict of interest, unless the conflict affected the choice of a reasonable interpretation.
>
> In reviewing the plaintiff's conflict of interest claim in *Pagan* we affirmed summary judgment in favor of the administrator because Pagan failed to explain how the conflict of interest affected the Committee's interpretation. Following the standard of *Firestone* and *Pagan*, we conclude that, in cases where the plan administrator is shown to have a conflict of interest, the test for determining whether the administrator's interpretation of the plan is arbitrary and capricious is as follows: Two inquiries are pertinent. First, whether the determination made by the administrator is reasonable, in light of possible competing interpretations of the plan; second, whether the evidence shows that the administrator was in fact influenced by such conflict. If the court finds that the administrator was in fact influenced by the conflict of interest, the deference otherwise accorded the administrator's decision drops away and the court interprets the plan *de novo*.[99]

Later in the opinion, the court stated, "[I]n *Pagan* we determined that a reasonable interpretation of the Plan will stand unless the participants can show not only that a potential conflict of interest exists, . . . but that the 'conflict affected the reasonableness of the Committee's decision.'"[100]

The *Sullivan* formulation does not recognize the seriousness of the conflict in and of itself; the court recognizes only its effect. The burden remains on the plaintiff to demonstrate its effect. If the fiduciary's interpretation is "reasonable" *and* plaintiff offers evidence that the reasonable decision was "influenced" by a conflict of interest, the court conducts a *de novo* review.

If reasonableness apart from the fact or effect of conflict of interest is the lodestar, however, and the decision is reasonable by that standard, why should further inquiry be conducted? The explanation must be that the influence of conflict of interest taints an otherwise reasonable decision. How does one take the influence into account? The court answers by conducting a *de novo* review. Have we then gone beyond the arbitrary and capricious or abuse of discretion standards? Has the court acknowledged the concerns of *Brown* and found that it must go the same route? Can conflict of interest be treated appropriately as a "factor," as *Firestone* seems to require?[101]

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[99] *Sullivan*, 82 F.3d at 1255-56.

[100] *Id.* at 1259 (quoting *Pagan*, 52 F.3d at 443).

[101] The standard enunciated in *Pagan* and *Sullivan* was reiterated in *Whitney v. Empire Blue Cross & Blue Shield*, 106 F.3d 475, 477 (2d Cir. 1997).

III. THE FOURTH CIRCUIT APPROACH

The second "sliding scale" circuit we shall consider is the Fourth.[102] In its decisions, the Fourth Circuit has remained faithful to the abuse of discretion standard in *Bruch v. Firestone Tire & Rubber Co.*[103] At the same time, the court recognizes that conflict of interest is a factor for which the several dimensions of its effect must be taken into account. The Fourth Circuit has shown that the various aspects of conflict of interest necessary for full consideration can be integrated into the review of a denial of benefits without a full-fledged *de novo* analysis. This is accomplished by charting a course between *Brown v. Blue Cross & Blue Shield*[104] and *Sullivan v. LTV Aerospace & Defense Co.*[105]

The questions a court must ask to satisfy the Fourth Circuit's analysis emerge from several seminal cases. A court must first determine whether the decision is "reasonable."[106] The *de Nobel v. Vitro Corp.*[107] court listed several reasonableness factors: whether the decision is consistent with plan goals; whether plan language would be rendered meaningless or internally inconsistent; whether the decision contravenes the procedural or substantive requirements of ERISA; and whether the provisions of the plan have been correctly and consistently applied.[108]

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[102] Time and space do not permit a complete review of the evolution of the Fourth Circuit's standard. Any such review would discuss at least the following cases. *See* Booth v. Wal-Mart Stores, Inc., 201 F.3d. 335 (4th Cir. 2000); Brogan v. Holland, 105 F.3d 158 (4th Cir. 1997); Ellis v. Metropolitan Life Ins. Co., 126 F.3d 228 (4th Cir. 1997); Martin v. Blue Cross & Blue Shield, 115 F.3d 1201 (4th Cir. 1997); Bedrick v. Travelers Ins. Co., 93 F.3d 149 (4th Cir. 1996); Haley v. Paul Revere Life Ins. Co., 77 F.3d 84 (4th Cir. 1996); Jenkins v. Montgomery Indus., Inc., 77 F.3d 740 (4th Cir. 1996); Bailey v. Blue Cross & Blue Shield, 67 F.3d 53 (4th Cir. 1995); Bernstein v. CapitalCare, Inc., 70 F.3d 783 (4th Cir. 1995); Fagan v. National Stabilization Agreement of Sheet Metal Indus. Trust Fund, 60 F.3d 175 (4th Cir. 1995); Hickey v. Digital Equip. Corp., 43 F.3d 941 (4th Cir. 1995); Sheppard & Enoch Pratt Hosp., Inc. v. Travelers Ins. Co., 32 F.3d 120 (4th Cir. 1994); Doe v. Group Hospitalization & Med. Servs., 3 F.3d 80 (4th Cir. 1993); Lockhart v. UMWA 1974 Pension Trust, 5 F.3d 74 (4th Cir. 1993); Bidwill v. Garvey, 943 F.2d 498 (4th Cir. 1991), *cert. denied*, 502 U.S. 1099 (1992); Richards v. Health & UMWA Retirement Funds, 895 F.2d 133 (4th Cir. 1990); de Nobel v. Vitro Corp., 885 F.2d 1180 (4th Cir. 1989); *see also* Jonathan P. Heyl, *Bedrick v. Travelers Insurance Co.: the Fourth Circuit's Continued Attempt to Work With the "Doctrinal Hash" of the Standard of Review in ERISA Benefit-Denial Cases*, 75 N.C. L. REV. 2382 (1997).

[103] 828 F.2d 134 (3d Cir. 1987).

[104] 898 F.2d 1556 (11th Cir. 1990).

[105] 82 F.3d 1251 (2d Cir. 1996).

[106] *See de Nobel*, 885 F.2d at 1188 (quoting Holland v. Burlington Indus., 772 F.2d 1140, 1149 (4th Cir. 1985)) ("The dispositive principle remains, however, that where plan fiduciaries have offered a 'reasonable interpretation' of disputed provisions, 'courts may not replace [it] with an interpretation of their own'— and therefore cannot disturb as an 'abuse of discretion' the challenged benefits determination.").

[107] 885 F.2d 1180 (4th Cir. 1989).

[108] *See id* at 1188.

Conflict of interest is not listed as a factor until later in the opinion. When the court reaches conflict of interest, it is clear that this "factor" is considered only once the opinion is deemed "reasonable" on other grounds:

> The question of interpretation that lies at the heart of the parties' dispute in this case is an extremely close one. That alone, given that we must defer to any "reasonable" administrative construction of the Plan, constrains us to find here no "abuse of discretion"— presuming, of course, that the Vitro trustees operated under no substantial "conflict of interest." The question that remains, therefore, is whether the record before us bears out the retirees' allegations of administrative bias.
>
> The *Bruch* Court made clear that, even under the deferential "abuse of discretion" standard of review, evidence of administrative bias remains relevant. . . . Here, however, there simply is no evidence in the record to suggest that the Vitro administrators' benefit determinations were tainted by any such conflict of interest.[109]

The conflict was not so substantial or inherent as to presume bias and, indeed, was the sort of conflict the statute itself contemplates.[110]

The court recognized that conflict of interest was a different kind of factor from those determining reasonableness. A plan interpretation could be reasonable and, yet, abuse discretion. Reasonableness emerges as a question of logic and consistency with plan language and with plan and statutory purposes. The court further recognized that both the *fact* and *effect* of conflict of interest may bear upon a determination of whether discretion was abused.

In *Doe v. Group Hospitalization & Medical Services*,[111] the court was squarely presented with a conflict of interest and required to determine its effect. The plan insured and compensated Blue Cross with a fixed premium determined by actuary tables.[112] If the allowed claims exceeded the assumed risk, Blue Cross lost profit.[113] The court deemed this conflict "inherent" but nonetheless part of the bargained-for contract.[114]

Citing the *Brown* decision, the plaintiffs contended that, as a result of this conflict, the court should not accord the fiduciary's decision any deference.[115] "Indeed, they direct us to the statement in *Brown* where the court concluded that when a substantial conflict of interest is demonstrated, 'the burden shifts to the fiduciary to prove that its

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[109] *Id.* at 1191.

[110] *See id.*

[111] 3 F.3d 80 (4th Cir. 1993).

[112] *See id.* at 86.

[113] *See id.*

[114] *Id.*

[115] *See id.*

interpretation of plan provisions committed to its discretion was not tainted by self-interest.'"[116]

The court did not adopt *Brown*'s analysis. Rather, the court announced that conflict of interest would be treated as a factor in determining abuse of discretion, as *Firestone Tire & Rubber Co. v. Bruch*[117] requires.[118] Doing so, however, requires first assessing the logic and consistency factors of reasonableness. This amounts to the *de Nobel* analysis in test form:

> Under the common law a fiduciary may be authorized to act despite a conflict of interest by the terms of the trust instrument. But this consent does not mean that the fiduciary's judgment will not be scrutinized more closely than when he acts solely in the interest of the beneficiaries. Even the most careful and sensitive fiduciary in those circumstances may unconsciously favor its profit interest over the interests of the plan, leaving beneficiaries less protected than when the trustee acts without self-interest and solely for the benefit of the plan. As noted in *Firestone*, these same principles apply in the ERISA context, and a conflict of interest environment is thus a factor to be considered in determining whether authorized discretion has been abused.
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> Because of the presence of a substantial conflict of interest, we therefore must alter our standard of review. We hold that when a fiduciary exercises discretion in interpreting a disputed term of the contract where one interpretation will further the financial interests of the fiduciary, we will not act as deferentially as would otherwise be appropriate. Rather, we will review the merits of the interpretation to determine whether it is consistent with an exercise of discretion by a fiduciary acting free of the interests that conflict with those of the beneficiaries. In short, the fiduciary decision will be entitled to some deference, but this deference will be lessened to the degree necessary to neutralize any untoward influence resulting from the conflict.[119]

In this formulation, the court again recognized that the fact and effect of conflict of interest must be considered in determining whether discretion has been abused. This acts both to limit the range of what might be considered reasonable and to test the choice within that range. The choice must be *consistent with* the choice of a conflict-free fiduciary. Thus, a reviewing court cannot rest with "an ordinary abuse-of-discretion analysis, albeit '[w]ith these considerations [*Doe*] in mind[.]'"[120] "A fiduciary with a conflict of interest must act as if he is 'free' of such a

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[116] *Id.* (quoting *Brown*, 898 F.2d at 1566).

[117] 489 U.S. 101 (1989).

[118] *See Doe*, 3 F.3d at 87.

[119] *Id.* at 86-87 (citations omitted).

[120] Bedrick v. Travelers Ins. Co., 93 F.3d 149, 152-53 (4th Cir. 1996) (quoting the district court opinion).

conflict. 'Free' is an absolute. There is no balancing of interests; ERISA commands undivided loyalty to the plan participants."[121]

In *Haley v. Paul Revere Life Ins. Co.*,[122] the court framed the appropriate analysis as follows:

> While *de novo* review is inappropriate when reviewing an administrator's exercise of discretion, it is proper in deciding the two questions of contractual interpretation and performance: (1) whether the plan confers discretion upon the administrator to make the decision at issue; and (2) whether the administrator's decision falls within the scope of discretion conferred.
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> In sum, when reviewing an ERISA plan administrator's decision to grant or deny plan benefits, a court must first decide *de novo* whether the plan's language prescribes the benefit or whether it confers discretion on the administrator to determine the benefit. If the plan confers discretion, the court must decide, again *de novo*, whether the administrator, in making its determination, acted within the scope of that discretion. And, finally, if the plan administrator's decision falls within the scope of the administrator's contractually conferred discretion, the court may review the merits of an administrator's decision only for an abuse of discretion. The court must not disturb the administrator's decision if it is reasonable, even if the court itself would have reached a different conclusion.
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> Finally, in deciding whether an administrator has abused its contractually conferred discretion, a court should consider, to the extent relevant: (1) the scope of the discretion conferred; (2) the purpose of the plan provision in which the discretion is granted; (3) any external standard relevant to the exercise of that discretion; (4) the administrator's motives; and (5) any conflict of interest under which the administrator operates in making its decision.[123]

The practical application of this standard requires one to grasp the interplay between reasonableness and abuse of discretion. The court may review the merits of the decision only for abuse of discretion, and, if it is reasonable, the court may not disturb the administrator's decision. Yet reasonableness and abuse of discretion are not synonymous. A decision can be reasonable in the sense of being rationally related to the plan, the statute, and their purposes, and yet be improperly influenced by conflict of interest. This is recognized by the court's recitation of factors in abuse of discretion. The first three factors have to do with rational relationship to the plan and the final two (including conflict of interest) deal with motivation in reaching the decision.

"Reasonable" must, therefore, be understood as being within the range of choices set by recognition of the fact of conflict of interest.

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[121] *Id.* at 154 (citation omitted).

[122] 77 F.3d 84 (4th Cir. 1996).

[123] *Id.* at 89 (citations omitted).

Within that range, it must not be determined or influenced by the pull of that conflict. The fiduciary is free to elect within that set of choices, defined by rational relation to the plan and its purposes, not influenced by divided loyalty, nor limited in scope by the strength of the conflict of interest. The court will defer to that election. The following section explores this analysis in greater detail.

The Fourth Circuit most recently discussed the reasonableness/abuse of discretion inquiry in *Booth v. Wal-Mart Stores, Inc.*[124] *Booth* involved a challenge to a denial of medical expenses under an employee benefit plan.[125] The plan's preexisting condition exclusion was the basis for denial.[126] Determining that the fiduciary could not be found to have abused its contractually conferred discretion, the court framed the analysis as follows:

> [W]e repeat that the standard for review under ERISA of a fiduciary's discretionary decision is for abuse of discretion, and we will not disturb such a decision if it is reasonable.
>
> In determining whether a fiduciary's exercise of discretion is reasonable, numerous factors have been identified as relevant, both in the cases applying ERISA and in principles of trust law. In *Firestone*, for example, the Supreme Court indicated that the fact that a fiduciary operates under a conflict of interest *must* be weighed in determining whether there is an abuse of discretion.
>
> Combining these various criteria for determining the reasonableness of a fiduciary's discretionary decision, we conclude that a court may consider, but is not limited to, such factors as: (1) the language of the plan; (2) the purposes and goals of the plan; (3) the adequacy of the materials considered to make the decision and the degree to which they support it; (4) whether the fiduciary's interpretation was consistent with other provisions in the plan and with earlier interpretations of the plan; (5) whether the decisionmaking process was reasoned and principled; (6) whether the decision was consistent with the procedural and substantive requirements of ERISA; (7) any external standard relevant to the exercise of discretion; and (8) the fiduciary's motives and any conflict of interest it may have.[127]

A footnote to the eighth factor elaborated the role of conflict of interest:

> A fiduciary's conflict of interest, in addition to serving as a factor in the reasonableness inquiry, may operate to reduce the deference given to a discretionary decision of that fiduciary. We have held that a court, presented with a fiduciary's conflict of interest, may lessen the deference given to the fiduciary's discretionary decision to the extent

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[124] 201 F.3d 335 (4th Cir. 2000). The opinion was written by Judge Niemeyer, who also wrote the *Doe* and *Haley* opinions.

[125] *See id.* at 338.

[126] *See id.*

[127] *Id.* at 342-43 (citations omitted).

necessary to "neutralize any untoward influence resulting from that conflict."[128]

Booth reaffirmed the now well-established framework for reviewing fiduciary decisions for reasonableness/abuse of discretion. Within that framework, conflict of interest serves both as a reasonableness factor and as a limitation on the deference accorded the decision. Unlike *Brown*, it acknowledges the impact of conflict of interest without *de novo* analysis and burden shifting. Unlike *Sullivan*, it recognizes the fact of conflict of interest as well as its effect.

IV. THE FOURTH CIRCUIT'S RECOGNITION AND ELUCIDATION OF THE VARIOUS WAYS CONFLICT OF INTEREST CAN INFLUENCE A FIDUCIARY'S DECISION

A strong theme of philosopher Ludwig Wittgenstein's later works is that language should be investigated by seeing how words actually function in sentences.[129] When we take off our glasses[130] and see the world as it is, he argues, we see that the meaning and usage of words is not captured by a one-to-one mapping of subject onto object.

Likewise, to understand and control the workings of conflict of interest, courts must examine its various workings. As the Fourth Circuit has recognized, this means asking not one question but several in recognition of its multi-dimensional effect on fiduciary decisionmaking.

Thus, *Booth v. Wal-Mart Stores, Inc.*,[131] teaches that, *in addition to* serving as a factor in the reasonableness inquiry, conflict of interest operates to reduce the deference given to a discretionary decision of a

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[128] *Id.* at 343 n.2 (quoting *Doe*, 3 F.3d at 87).

[129] *See* LUDWIG WITTENSTEIN, THE BLUE AND BROWN BOOKS (2d ed. 1960); LUDWIG WITTENSTEIN, PHILOSOPHICAL INVESTIGATIONS (G.E.M. Anscombe trans., Macmillan Publ'g Co. 3d ed. 1968) [hereinafter PHILOSOPHICAL INVESTIGATIONS]. For example, Wittenstein observed:

> 115. A *picture* held us captive. And we could not get outside it, for it lay in our language and language seemed to repeat it to us inexorably.
>
> 116. When philosophers use a word—"knowledge," "being," "object," "I," "proposition," "name"—and try to grasp the *essence* of the thing, one must always ask oneself: is the word ever actually used in this way in the language-game which is its original home?—
>
> What *we* do is to bring words back from their metaphysical to their everyday use.
>
> . . . .
>
> 122. A main source of our failure to understand is that we do not *command a clear view* of the use of our words.

PHILOSOPHICAL INVESTIGATIONS, *supra*, at 48°–49°.

[130] *See id.* at 45° n.103 ("It is like a pair of glasses on our nose through which we see whatever we look at. It never occurs to us to take them off.").

[131] 201 F.3d 335 (4th Cir. 2000).

fiduciary to the extent necessary to neutralize "untoward influence."[132] *Doe* teaches that where there is a conflict of interest, the reviewing court should review the merits of the interpretation to determine whether it is consistent with an exercise of discretion by a fiduciary *acting free of the conflict of interest.*

A. The Influence of Conflict of Interest

These Fourth Circuit tests address the influence of a conflict of interest. There are two aspects to influence. First, there is the *fact and nature* of the conflict—the influence occasioned by the *nature and severity* of the conflict *in and of itself* (when *Doe v. Group Hospitalization & Medical Services*[133] refers to a "substantial" conflict) for which the Fourth Circuit counsels a hermeneutic of suspicion. Second, there are the *consequences* of the conflict, for which there are two subcategories.

The first subcategory is where the effect is inferred circumstantially from the decision. There are at least two possibilities. First, a choice *within* the range of what the court considers "reasonable" may be encouraged or even determined by the pull of the conflict. In other words, the erstwhile reasonable decision may not be what it would have been without the effect of the conflict. This would require an *a priori* determination of what a reasonable decision could be in the absence of a conflict (the *Doe* test). Second, where the fiduciary's decision is outside the range of what is "reasonable," either the error or the pull of the conflict could be the cause for the "unreasonableness."

The second subcategory is where there is direct evidence that improper loyalty influenced the decision.

To simplify, after one assesses the impact of conflict of interest according to the criteria supplied by the Fourth Circuit, a court must examine the operation of conflict of interest in at least the following guise:

1. The fact and nature of the conflict.
2. The consequences of the conflict.
   a. Inferred circumstantially from the decision.
      (i) Where the decision is within the range of what is determined to be reasonable considering other factors in the absence of the conflict.
      (ii) Where the decision is outside the range of what is determined to be reasonable, considering other factors in the absence of the conflict (plain error, or the influence of a conflict).

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[132] *Id.* at 343 n.2.

[133] 3 F.3d 80 (4th Cir. 1993).

b. Deduced directly from evidence about the making of the decision.

In making this assessment, the Fourth Circuit teaches that conflict of interest plays two roles: it circumscribes the range of what may count as reasonable (lessening deference to negate the effect of untoward influence— the "sliding scale"), and it contributes to an assessment of reasonableness *within* that range (a criterion for determining reasonableness). The fact and nature of the conflict narrow the range. The consequences of the conflict guide the assessment of reasonableness within the range.

By comparison, football is played according to rules and within boundary lines at the ends and sides of the field. Play must be within the bounds and by the rules. In fiduciary decisions, the fact and nature of conflict of interest locate the goal lines and side lines. The effect of conflict of interest referees the plays (and whistles some that are otherwise not by the rules).

B. The Roles of Conflict of Interest

There are two roles of conflict of interest: (1) to reduce the fiduciary's discretion; and (2) to assess reasonableness.

1. Reducing Discretion of the Fiduciary

First, conflict of interest operates to reduce the discretion that would otherwise be afforded the fiduciary. In practice, reducing discretion means narrowing the range of reasonable choices. The stronger the conflict is, the narrower the range will be. There are, however, at least two difficulties in application.

The first difficulty is that there is no *a priori* authoritative and unambiguously direct rule prescribing how much narrowing should occur. Nor are we at present afforded guidance as to the limits of this narrowing. The question remains, for example, whether there is a conflict so serious as to narrow the range of reasonableness to zero. The answers must await the evolution of federal common law. In the meantime (and even thereafter), this lack of guidance entails a weakening of predictability.

The second difficulty is ambiguity in what is understood by the term "reasonable." The ambiguity is between the use of "reasonable" as a logic term apart from normative considerations and its use as a term that incorporates logical and normative considerations.

Thus, a "reasonable" determination could be understood as one that is congruent with the language of the plan and its purposes and what is derived by some acceptable middle axiom between the plan and the

instant facts (the first seven *Booth* factors). Taken in this light, a fiduciary's determination could be reasonable and yet be outside the range set by the normative governor, conflict of interest. Indeed, ERISA presumes that conflicted fiduciaries can render reasonable decisions.

The alternative, which is the approach of *Doe* and *Booth*, is to include the fact of conflict of interest in the calculus of what is allowed to count as "reasonable," both in reference to the range and to decisions within that range. It is unclear how or in what measure the presence of a conflict of interest works to draw a line between what is reasonable and what is not reasonable. If the presence of a conflict of interest sets the bounds of reasonableness, then we must ask both in theory and in practice how the fact of conflict of interest operates to render, as between two determinations, each derived from a fair interpretation of the plan, the one reasonable and the other unreasonable. This would narrow the range and purge the effect of untoward influence. In theory, this depends upon whether the conflict of interest divided the fiduciary's loyalties and if this can be discerned. In practice, this requires the exercise of sound judgment on a case-by-case basis.[134]

2. Assessing Reasonableness

We turn next to the second role of conflict of interest: contributing to (being a "factor" in) an assessment of reasonableness *within* the range of what may count as reasonable. Applying *Firestone Tire & Rubber Co. v. Bruch*,[135] *Booth* listed conflict of interest as a factor along with other factors, such as the language, purposes, and goals of the plan; the materials considered by the fiduciary; the consistency and reasoning process of the fiduciary; and any relevant external standards.

Conflict of interest, however, is different than the other factors in the *Booth* list. Conflict of interest affects how the fiduciary construes the other factors. It assigns a reason to why the fiduciary interpreted and applied the plan as he or she did. It looks to motive, not technique. Its logic and influence are normative.

This realization is implicit in *Doe*'s directive to examine the merits of the interpretation. Whether the realization is consistent with an exercise of discretion by a fiduciary acting free of the conflict of interest must be determined. One should take the conflict of interest factor out and ask what the outcomes could be. Then, presumably, variance from that outcome would permit an inference of improper motive. At first glance this seems akin to the directive of *Brown*, to determine the "right" answer first.

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[134] *See* Haley v. Paul Revere Life Ins. Co., 77 F.3d 84, 89 (4th Cir. 1996).

[135] 489 U.S. 101 (1989).

If the "right" answer is determined first, then is the court conducting a *de novo* review? The Court in *Brown v. Blue Cross & Blue Shield*[136] suggested that this is so: "[i]t is fundamental that the fiduciary's interpretation first must be 'wrong' from the perspective of *de novo* review before a reviewing court is concerned with the self-interest of the fiduciary."[137] In *Klebe v. Mitre Group Health Care Plan*,[138] the district court agreed:

> This Court chooses to follow the lead of the Eleventh Circuit, and thus consider first, "from the perspective of *de novo* review," whether MITRE's decision to deny John Klebe's coverage under his lifetime medical benefit limitation was correct. If the decision is judged incorrect but reasonable, the Court may find it necessary to proceed to the self-interest analysis; if, however, the Court judges the decision reasonable and correct, the inquiry will be at an end.[139]

Firestone prescribes *de novo* review unless the plan confers discretion. Where the plan confers discretion, respecting the contract the parties have negotiated, the court is to conduct its review according to the abuse of discretion standard. Yet in *Klebe*, where the language of the plan conferred discretion sufficient to implicate review for abuse of discretion[140] and the fiduciary operated under a conflict of interest, the court found it necessary to review the decision *de novo*. Moreover, "[w]henever the less deferential standard applies, a court may substitute its own judgment if it disagrees with the conflicted decisionmaker, even if the decisionmaker's determination is reasonable."[141]

This approach seems to be at odds with the Fourth Circuit. The Fourth Circuit holds that if the decision is reasonable, after taking conflict of interest into account, the decision will not be disturbed. *Klebe,* following *Brown*, suggested that in practice, *de novo* review is necessary to determine the impact of the conflict of interest.

As the above analysis shows, it is a constrained and delimited sort of *de novo* review, not right versus wrong. It is the bounds of reason understood by the nuanced exercise of judgment. Close examination shows that taking conflict of interest into account requires deciding what will count as reasonable in two respects: the range of possible choices, and within that range, the out-of-bounds lines (as well as the play within those boundaries). Departures from what will count as reasonable may permit an inference that conflict of interest influenced the decision. Whether this is called a modified *de novo* review or a modified abuse of

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[136] 898 F.2d 1556 (11th Cir. 1990).

[137] *Id.* at 1566 n.12.

[138] 894 F. Supp. 898 (D. Md. 1995), *aff'd*, 91 F.3d 131 (4th Cir. 1996).

[139] *Id.* at 904 (citation omitted).

[140] *See id.* at 902.

[141] *Id.* at 903.

discretion review, it is distinguishable from *de novo* review because of the respect accorded the decision of the fiduciary. In plain and simple terms, it asks what is "reasonable" rather than what is "right."

V. CONCLUSION

As this article has illustrated, one of the greatest difficulties in the current case law is that conflict of interest in ERISA cases is subject to a determination of "reasonableness." Although there are conflicts in the circuit courts concerning this determination, the Fourth Circuit provides a standard for determining reasonableness that has the potential to calm the troubled waters in this area. The Fourth Circuit's standard is the best standard currently available because it is sensitive to the complexities of factoring in conflict of interest *and* to the requirements of *Firestone*. It is a principled, nuanced appropriation of the teaching of *Firestone*, which requires deciding courts to examine not just the fact of conflict of interest, but also its nature and the various ways it can exert its influence. In this way, the Fourth Circuit accomplishes a more principled approach than the other circuits by holding the trustee more accountable to prevent and rectify wrongly motivated decisions, yet still fitting its methodology within ERISA's framework, thus taking into account the complexity of the decision.