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DISTRICT OF UTAH

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF UTAH

BY: _____
DEPUTY CLERK

CENTRAL DIVISION

**SHERRY KNIGHT, individually and as
personal representative of the estate of
DEAN KNIGHT, and the class of
similarly situated individuals and entities,**

Plaintiffs,

v.

**AMERICAN MEDICAL SECURITY,
INC., UNITED WISCONSIN LIFE
INSURANCE COMPANY, AMERICAN
MEDICAL SECURITY TRUST, and its
trustee AMSOUTH BANK,**

Defendants.

**MEMORANDUM DECISION AND
ORDER**

Case No. 2:03 CV 1096 DAK

This matter is before the court on Defendants' Motion to Dismiss the Amended Complaint Pursuant to Fed. R. Civ. P. 12(b)(6). A hearing on the motions was held on May 24, 2004. At the hearing, plaintiffs Sherry Knight and the estate of Dean Knight ("Knights"), were represented by Brian S. King, Attorney at Law, and Robert G. Wing of Prince, Yeates & Geldzahler. Defendants American Medical Security, Inc., United Wisconsin Life Insurance Company, and American Medical Security Trust and its Trustee AmSouth Bank ("Defendants") were represented by Paul M. Belnap of Strong & Hanni and David S. Clancy of Skadden, Arps, Slate, Meagher & Flom. Before the

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hearing, the court considered carefully the memoranda and other materials submitted by the parties. Since taking the matter under advisement, the court has further considered the law and facts relating to this motion. Now being fully advised, the court renders the following Memorandum Decision and Order.

I. MOTION TO DISMISS

A. Standard of Review

In reviewing a motion to dismiss under Rule 12(b)(6), “[a]ll well-pleaded facts, as distinguished from conclusory allegations, must be taken as true.” *Rutz v. McDonnell*, 299 F.3d 1173, 1181(10th Cir. 2002) (quoting *Swanson v. Bixler*, 750 F.2d 810, 813 (10th Cir. 1984). “The court must view all reasonable inferences in favor of the plaintiff, and the pleadings must be liberally construed.” *Id.* “In addition to the complaint, the district court may consider documents referred to in the complaint if the documents are central to the plaintiff’s claim and the parties do not dispute the documents’ authenticity.” *Jacobsen v. Deseret Book Co.*, 287 F.3d 936, 941 (10th Cir. 2002). Moreover, the actual terms of a document attached or referenced in a complaint take precedent over the allegations in the complaint characterizing the document. *See Jacobsen*, 287 F.3d at 942 (“the legal effect of an incorporated document considered on a motion to dismiss is to be determined by the document’s terms rather than by the allegations of the pleader in the complaint.”) (internal quotations and citations omitted).

B. Procedural Background

This lawsuit was removed by the Defendants to federal court based upon federal question jurisdiction arising from the Knights’ alleged cause of action under the Employee Retirement Income

Security Act of 1974 (“ERISA”), 29 U.S.C. § 1001, *et. seq.*. Shortly after removal, the Knights filed an amended complaint. The amended complaint alleges six causes of action: (1) violation of ERISA; (2) Negligence in Drafting the Insurance Policy; (3) Breach of the Implied Covenant of Good Faith and Fair Dealing; (4) Declaratory and Injunctive Relief; (5) Imposition of a Constructive Trust; and (6) Equitable Estoppel. In addition, the plaintiffs allege that a class action is appropriate in this case. To date, plaintiffs have not moved for class certification nor have they named or identified any additional plaintiffs other than the Knights. Defendants’ motion seeks to dismiss plaintiffs’ Amended Complaint and Proposed Class Action in its entirety.

C. Factual Background

Dean Knight obtained medical insurance from the defendants in 1999. The policy was originally issued to Dean Knight and other employees of Fashion Corner, Inc. as part of an employee benefit plan governed by ERISA. However, prior to the time the medical expenses that are at issue in this case arose, the policy was converted from an employer-sponsored plan to a private or individual plan. Mr. Knight was diagnosed with cancer and received extensive medical treatment until his death on September 22, 2003. The Knights’ claims arise from defendants’ alleged failure to fully disclose the amounts covered under the policy for particular medical services and defendants’ failure to pay the full amount of the medical services that were billed to plaintiffs.

D. Discussion

The threshold issue to be determined on this motion is whether claims arising under a conversion policy are governed by ERISA. At the outset, it is important to note the difference

between “conversion rights” and a “conversion policy.” ERISA plans often have “conversion rights” or an option that can be exercised by a plan participant upon leaving his or her employment that allows the participant to continue coverage by converting to an individual policy. The Knights’ conversion rights are not at issue in this lawsuit. As evidenced by the policy, the Knights successfully converted to an individual policy prior to the time the subject claims arose. The question presented in this case is whether a policy that has been converted from an ERISA plan to an individual policy (“conversion policy” or “converted policy”) is governed by ERISA.

The court rejects the Knights’ argument that for the purposes of a Rule 12(b)(6) motion the court must accept as true their allegation that the policy is governed by ERISA. As previously discussed, the court is not required to accept conclusory allegations as true. This is especially true when the conclusory statement is a legal conclusion. More importantly, the Knights have attached a copy of the policy as an exhibit to their original complaint and made numerous references to the policy in their amended complaint. Accordingly, the court need not rely upon the Knights’ characterizations of the policy but can look to the actual terms of the policy to determine its legal significance. The policy and other documents attached by the Knights as exhibits to their complaint contain the terms “CONV” and “CONVERSION” indicating that it was a policy converted from a group plan. Moreover, the policy names Dean Knight as both the employer and the insured, further demonstrating that it is an individual policy.

The Tenth Circuit has not specifically addressed the issue of whether a conversion policy is governed by ERISA. Other circuits have reached various results, but the majority of courts have held that conversion policies are not governed by ERISA. *See Crawley v. Oxford Health Plans, Inc.*, 309

F. Supp. 2d 261, 265 (D. Conn. 2004) (“While the circuits have split on this issue, the majority of courts considering this issue have reached the same conclusion.”). The leading case on the applicability of ERISA to conversion policies appears to be *Demars v. Cigna Corporation*, 173 F.3d 443 (1st Cir. 1999). In *Demars*, the court held that a “conversion policy is not an employee welfare benefit plan.” *Id.* at 450 (internal quotations omitted). *Demars* carefully and persuasively draws a distinction between a claim relating to a conversion right that is governed by ERISA and a claim relating to the conversion policy itself that is not governed by ERISA. *Id.* at 448. In determining whether a conversion policy is an employee welfare benefit plan subject to ERISA, the *Demar* court looked to the purpose of Congress in enacting ERISA:

In passing ERISA, Congress’s purpose was twofold: to protect employees and to protect employers. Congress wanted to safeguard employee interests by reducing the threat of abuse or mismanagement of funds that had been accumulated to finance employee benefits, while at the same time safeguarding employer interests by eliminating the threat of conflicting and inconsistent State and local regulation of employee benefit plans.

Neither concern seems to be strongly implicated here. There is little threat of abuse of funds in the ERISA sense. While there is a risk that funds accumulated to finance benefits under the conversion policy could be mismanaged or abused, there is no risk of [plaintiff’s] former employer abusing or mismanaging these funds, since it does not control them, or indeed have any tie to them. Rather, it is the insurers who issued the policy—defendants here—who are in a position to possibly abuse or mismanage the funds. Yet Congress placed into ERISA an express disavowal of any intent to regulate insurers qua insurers. *See* 29 U.S.C. § 1144(b)(2).

Id. at 446 (internal quotations and citations omitted).

The cases cited by the Knights to argue that an ERISA policy that is converted to an

individual policy is still governed by ERISA are not persuasive. Plaintiffs cite *Peterson v. American Life & Health Ins. Co.*, 48 F.3d 404 (9th Cir. 1995) to argue that a converted policy is still governed by ERISA even though six years later in *Waks v. Empire Blue Cross/Blue Shield*, 263 F.3d 872 (9th Cir. 2001) the Ninth Circuit made it very clear that *Peterson* should not be read to hold that a converted policy continues to be subject to ERISA. *Id.* at 876 (“We did not have a converted policy before us [in *Peterson*] and did not hold that a converted policy continues to be subject to ERISA.”). Like most courts, the Ninth Circuit has adopted the reasoning of *Demars* and held that a converted policy is not subject to ERISA. *Id.* at 877 (“*Demars* persuasively explains that ERISA preemption applies neither to converted policies generally, nor to specific types of converted policies.”). The Knights also cite the Eighth Circuit’s decision in *Painter v. Golden Rule Insurance Company*, 121 F.3d 436, 439-40 (8th Cir. 1997) to argue a conversion policy is governed under ERISA. The *Painter* case was decided before the *Demars* decision and has been widely criticized by other courts. *See Demars*, 173 F.3d at 449 (noting that the *Painter* decision fails “to consider whether conversion policies implicate any of ERISA’s underlying purposes.”).

The court finds the case law holding that a conversion policy is not governed by ERISA to be persuasive and well reasoned. The court holds that the Knights’ policy is not an employee welfare benefit plan subject to ERISA. Accordingly, the Knights’ causes of action and claims for relief based upon ERISA must be dismissed. The court expresses no opinion as to whether potential class participants have claims subject to ERISA as no such claims are currently before the court.

The court’s determination that the Knights’ policy is not governed under ERISA effectively disposes of all the Knights’ claims arising under federal law. Accordingly, defendants’ federal

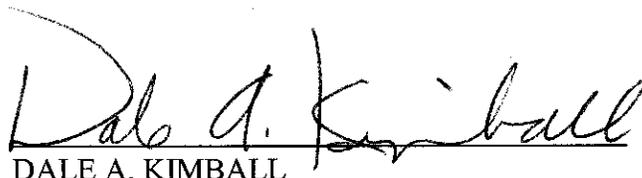
question basis for removing this case to federal court no longer exists. Pursuant to 28 U.S.C. § 1367(c)(3), the court declines to exercise supplemental jurisdiction over the state law claims in this matter. See *Lancaster v. Independent School District No. 5*, 149 F.3d 1228, 1236 (10th Cir. 1998) (affirming district court's decision to decline to exercise supplemental jurisdiction over remaining state law claims); see also *Board of County Commissioners of Sweetwater County v. Geringer*, 297 F.3d 1108, 1115 n. 6 (10th Cir. 2002) (noting the Tenth Circuit generally admonishes district courts to not exercise jurisdiction over state law claims after dismissing all federal claims). The court expresses no opinion as to the merits of the Knights' state law claims.

II. CONCLUSION

For the foregoing reasons, IT IS HEREBY ORDERED that: (1) Defendants' Motion to Dismiss the Amended Complaint is GRANTED in part, and DENIED in part. The Knights' claims for relief under ERISA are dismissed. (2) The Clerk of the Court is directed to remand this case to the Third Judicial District Court, in and for Salt Lake County, State of Utah for further proceedings related to the remaining causes of action.

DATED this 18th day of June, 2004.

BY THE COURT:



DALE A. KIMBALL
United States District Judge

United States District Court
for the
District of Utah
June 21, 2004

* * CERTIFICATE OF SERVICE OF CLERK * *

Re: 2:03-cv-01096

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