SLEET, District Judge

I. INTRODUCTION

On June 15, 1999, Sussex Auto Center, Inc., a Delaware corporation, filed a complaint on its own behalf and on behalf of Carol and Brenda Smith (collectively "Sussex") against Optimum Choice, Inc. (OCI), a health maintenance organization. Sussex's only cause of action presently before the court is an ERISA violation pursuant to 29 U.S.C. § 1132(a)(1)(B) for alleged wrongful denials of benefits under a Delaware small employer group employee health benefit plan (the "Sussex Plan").[1] OCI filed a counterclaim against Sussex under 29 U.S.C. § 1132(a)(1)(B)(3) alleging that since Sussex breached its fiduciary duty, it is liable for any losses incurred by the Smiths.

Because of numerous discovery disputes, the court extended the discovery and the dispositive motion cut-off dates several times and entered a briefing schedule. OCI filed a motion for summary judgment on August 28, 2000 (D.I. 85) and Sussex filed a cross motion for summary judgment on September 22, 2000 (D.I. 93). Since the parties agreed that the dispute was one of law – not of fact – the court took the case off its trial calendar and held oral argument on the motions on April 25, 2001. Because the court finds that OCI did not improperly retroactively terminate the Sussex Plan and deny benefits within the meaning of the statute, it will enter summary judgment in OCI's favor. The court, however, declines to directly address OCI's counterclaim on the merits. The following sections more throughly explain the basis for the court's ruling.

II. STANDARD OF REVIEW

The court must apply two standards of review. The first, the general summary judgment standard,

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[1]On December 3, 1999, the court dismissed the second cause of action, a state claim for an alleged violation of 18 Del. C. § 2702 (D.I. 29).

is uncontested. The court must enter summary judgment in favor of a party when, "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." *See* Fed. R. Civ. P. 56(c). An issue is "genuine" if a reasonable jury could return a verdict for the plaintiff given the evidence. *See Blizzard v. Hastings,* 886 F. Supp. 405, 408 (D. Del. 1995). An issue is "material" only if it might affect the outcome of the suit under governing law. *See Anderson v. Liberty Lobby*, 477 U.S. 242, 248 (1986). Since the parties agree (and the court finds) that there is no genuine issue of material fact, the court will treat the dispute as one purely of law.

Generally in ERISA cases, courts are faced with a choice of the appropriate level of deference to afford the insurer's decision. The parties bitterly contest the appropriate standard the court should use in evaluating OCI's actions in this case. OCI maintains that the court should use either the de novo or arbitrary and capricious standard[2] to review its actions. Sussex contends that the court should undertake either de novo or heightened arbitrary and capricious review[3] of OCI's retroactive termination. After

[2]The arbitrary and capricious standard is the most deferential one available. If the ERISA plan in question grants a sufficient level of discretion to deny coverage or determine eligibility, the court must apply some form of the aforementioned standard. Under this standard, the court grants the decision maker substantial deference and upholds the action taken unless it is not clearly supported by evidence in the record or the administrator has failed to comply with plan procedures. *See, e.g., Orvosh v. Program of Group Ins. for Salaried Employees of Volkswagen of America*, 222 F.3d 123 129 (3d Cir. 2000) (citing cases).

[3]The heightened arbitrary and capricious standard is a slight modification to the arbitrary and capricious level of review. This standard is invoked when an insurer both determines eligibility and funds the plan. This increased scrutiny is designed to address the possibility of an economic incentive to deny coverage. Under this standard, the court is deferential, but not absolutely so. According to the Third Circuit, a "sliding scale" approach must be used and district courts must "consider the nature and degree of the apparent conflict with a view to shaping their arbitrary and capricious review of the benefits determinations of discretionary decisionmakers." *See Pinto v. Reliance Standard. Life Ins.*

considering the position of the parties – as advanced in their submissions and at oral argument – and conducting its own review of the relevant case law, the court believes that de novo review is appropriate in this case.[4]

De novo review is the applicable standard of review in ERISA actions where the relevant plan does not give any discretionary authority to determine eligibility or construe benefits. *See Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 108-15 (1989). The key inquiry, in deciding whether to apply de novo review is the level of discretion the plan affords. If the plan does not afford discretion, de novo review is appropriate. If, however, the plan is unclear about where discretion lies, de novo review is also appropriate since ambiguities in ERISA plans should be construed in favor of the insured.[5] *See Heasley v. Belden & Blake, Corp.*, 2 F.3d 1249, 1257-58 (3d Cir. 1993). There are two reasons why de novo review is appropriate in this case; either OCI had no discretion or the level of discretion is so ill-defined as to require that court review the record on its own.

First, the Sussex Plan language is structured so that it is not entirely clear whether Sussex or OCI ultimately has discretion in determining eligibility. Although Sussex appears to be able to set eligibility or

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Co., 214 F.3d 366, 392-393 (3d Cir. 2000) (announcing factors for court to consider are sophistication of the parties, information accessible to them, and exact financial arrangement between insurer and employer).

[4]In determining de novo review is appropriate, the court considered – and rejected – the parties' arguments regarding the other standards.

[5]Sussex claims that there is no ambiguity since the issue is not whether OCI could have denied benefits but that it did so retroactively in violation of the express language of the Sussex Plan.

participation requirements, the requirements cannot be changed unless OCI agrees in writing.[6] OCI does have some discretion in interpretation, however.[7] But, this discretion is not unfettered since the Sussex Plan provides that the parties may submit to binding arbitration "any terms of this Agreement"; presumably there would be no right to arbitration on terms of the agreement if one party had absolute discretion to interpret the terms. Given the uncertainty surrounding the relationship between the parties, the court believes de novo review is appropriate.

Second, Sussex's contention that OCI had no discretion on the issues relevant to this case provides another, perhaps contradictory, reason to apply a de novo standard of review. Sussex argues that the language of the Sussex Plan is clear – OCI is required to give 30 days notice before termination by OCI. As noted above, where there is an absence of discretion the court should engage in a de novo review. Although it is true that the 30 day provision does not appear to provide OCI discretion, one point of contention in this case is whether Sussex's actions rendered it ineligible for coverage, regardless of the notice requirement. As a result, both parties have some discretion in determining eligibility. Under either analysis, therefore, the court should use de novo review.

Once the court determines that de novo review is the correct standard, the question then becomes

[6]According to the Face Sheet, Sussex's only eligibility requirement is "date of hire". The Evidence of Coverage (EOC) states that to be eligible, a subscriber or dependent must (1) live or work in the "OCI Service Area" and (2) pass an OCI health evaluation. The EOC defines "Service Area" as "that geographic area, described by the enclosed map, in which OCI provides health services to Members." According to Sussex, it was not provided such a map. Although Sussex maintains that the blame for failing to provide a "service area" map rests entirely on OCI, the court notes that Sussex was aware that such a map existed and never requested it.

[7]Section 8.3 states of the Sussex Plan, "OCI may adopt reasonable policies, procedures, rules and interpretations to promote orderly and efficient administration of this Agreement, and Employer agrees to cooperate with OCI in administering such rules and regulations."

what evidence the court may consider in evaluating the denial of benefits.[8] Although there is a split among the circuits, the Third Circuit has held that "a district court exercising de novo review over an ERISA determination . . . is not limited to the evidence before the Fund's Administrator." *See Luby v. Teamsters Health, Welfare, and Pension Trust Funds*, 944 F.2d 1176, 1185 (3d Cir. 1991). The exception to this rule is that if the record before the Plan Administrator is "sufficiently developed" then the district court may omit additional evidence.[9] *See id.*

Sussex maintains that permitting OCI – the insurer – to introduce additional evidence would undermine the rationale of *Luby*, and serve as nothing more than an ex post justification for OCI's actions. Although it is true that the *Luby* court allowed the insured (rather than the insurer) to introduce additional evidence, the holding of the case is not so limited. As the Third Circuit noted, a court's function in exercising de novo review is to use all available evidence to determine the empirically correct result, not to defer to OCI's decision. *See id.* (stating that limiting evidence is contrary to scope of de novo review since "court's inquiry is not limited by the . . . record, nor is any deference due the . . . conclusion [under review.]") (internal quotations and citations omitted). In the exchange of correspondence after the initial termination notice, Sussex responded to questions from OCI regarding its operation in an apparent attempt to overcome OCI's termination decision. Thus, prohibiting the submission of further proof by OCI to rebut Sussex's statements may be unfair.[10]

[8]Most of the cases in this area deal with whether the plan participant rather than the insurer can offer additional evidence. *See infra*.

[9]In *Luby*, there was no evidentiary record for the court to review.

[10]In its papers and during oral argument, Sussex continually referred to evidence not before OCI at the time of termination to explain why it still fit within the Sussex Plan after it sold its auto parts

III. BACKGROUND

Although the parties largely agree on the basic facts, they dispute whether the court should consider evidence OCI obtained during discovery and submitted for consideration. Since the court has already concluded that it would examine the entire record under de novo review, it will not distinguish between facts OCI knew before and after July 9, 1998.[11]

Sussex was a closely held Delaware corporation that was engaged in the business of auto repair which purchased the Sussex Plan from OCI effective October 15, 1996. Sussex employed six full time employees, including John Smith, Jr., John Smith III, and Brenda Smith. John Smith Jr. and John Smith III were both enrolled in the plan with their spouses, Carol and Brenda respectively, as their dependents.[12]

On August 1, 1997, Sussex sold its auto parts business to Murray Motors, Inc., let the non-Smith

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business. Although Sussex is entitled to make arguments in the alternative, such citation to – and reliance on – the "extrinsic" record to support its position "under any standard of review" potentially undermines its position on the appropriate scope of review.

[11]Under the other two review standards, the court may not normally consider evidence that was not before OCI at the time of its decision to terminate the Sussex Plan. Under both the "arbitrary and capricious" and "heightened arbitrary and capricious" standards of review, "the [c]ourt is limited to the evidence that was before the administrator when [it] made the decision being reviewed." *See Mitchell v. Eastman Kodak Co.*, 113 F.3d 433, 440 (3d Cir. 1997) (citations omitted); *see also O'Sullivan v. Metropolitan Life Ins. Co.*, 114 F. Supp.2d 303, 309 (D.N.J. 2000) (finding in denial of benefits case applying heightened arbitrary and capricious standard that looking beyond administrative record would undermine ERISA's goals) (citing cases). If a term is vague, however, courts may look to evidence that was not before the insurer for assistance in interpreting the plan. *See O'Sullivan*, 114 F. Supp.2d at 310 (citing *Vega v. Nat'l Life Ins. Servs., Inc.*, 188 F.3d 287, 300 (5th Cir. 1999). As more fully described below, the relevant terms in the Sussex Plan are unclear. Therefore, the court's reliance on additional evidence is appropriate under any standard of review.

[12]To avoid confusion, the court will refer to the Smiths by their first name throughout this memorandum opinion.

employees go,[13] signed a three year non-compete agreement and vacated its Delaware location. On or about August 2, 1997, the Sussex officers (John, Jr., John III, and Brenda Smith)[14] decided to continue paying the OCI health coverage premiums for the Sussex Plan "in lieu of salaries." Sussex did not inform OCI of any of these changes to its operations.

After selling the auto business, John III and Brenda Smith applied for and received Delaware unemployment insurance benefits. They collected benefits for 17 and four weeks respectively.[15] Brenda later found other full time employment. John III worked for a short time and then enrolled in an aviation repair course, his current field of employment. John, Jr. enrolled in a radiology training program, which he completed in 1999. He now works as a radiology technologist.

On or about April, 1998, OCI undertook an investigation into Sussex and determined that Sussex was not a "group" or an "actively participating group in Delaware." The investigator based this finding on, among other things, (1) OCI's computer records indicated that Sussex changed its address from Laurel, Delaware to an address in Rhodesdale, Maryland,[16] (2) the telephone number for Sussex was disconnected, (3) "the people at Murray Motors . . . said [Sussex] sold the business to them and they were occupying that place of business," (4) an internet search did not reveal an address or location for Sussex

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[13]Murray Motors subsequently hired two former non-Smith Sussex employees.

[14]Although there is no conclusive evidence in the record, since Sussex was a closely held corporation, John, Jr., John III, and Brenda Smith appeared to constitute the officers, board, and shareholders of the corporation. *See infra*, note 30.

[15]John, Jr. signed the "employer" section of the unemployment applications and stated that Sussex was out of business with no plans to rehire John III or Brenda.

[16]This address is the home residence of John III and Brenda. Brenda was listed in OCI's records as the contact person for Sussex.

in Delaware and (5) there was no "business listing" for Sussex in Delaware.[17] Based on its belief that Sussex had changed its address, among other things, OCI concluded that Sussex was no longer an "eligible employer" under the Sussex Plan. OCI therefore sent Sussex a letter on July 9, 1998 which retroactively terminated the Sussex Plan as of November 15, 1997.[18] The letter to Sussex generated a further exchange of letters between the parties regarding the status of Sussex. Although OCI stated in its initial letter that it had terminated coverage, it appeared that if Sussex could address its concerns, OCI would change or reconsider its decision.

The apparent catalyst for this dispute is the unfortunate reality of Carol and Brenda's medical problems. Carol was diagnosed with lymphoma prior to Sussex's sale of its auto business. Her treatments commenced on November 19, 1997, and were pre-approved by OCI 30 days in advance, according to the terms of the coverage. According to Sussex, Carol underwent treatment, believing herself covered under the Sussex Plan.[19] Brenda underwent a similarly pre-approved voluntary tubal ligation on January

[17]During discovery, OCI also learned that (1) Sussex let its business license lapse after December 21, 1997, and never renewed it or obtained any other business licenses, (2) Sussex wrote to the Delaware Division of Revenue stating that it was "inactive," "out of business," and had sold [the] business," and (3) Sussex neither paid wages nor unemployment or payroll taxes after August 1, 1997. John, Jr. notified the Delaware Unemployment Insurance Division that Sussex's auto business was sold on August 1, 1997.

[18]November 15, 1997 was the date Sussex changed its address in OCI's database from Delaware to Maryland. OCI retroactively terminated the Sussex Plan to this date because at the time it sent the letter the information it possessed suggested that this was when Sussex "ceased to exist." In its papers, OCI contends that subsequent investigation revealed that Sussex actually "ceased to exist" on August 1, 1997 and it could have retroactively terminated the Sussex Plan on that date.

[19]Sussex claims that had Carol known she would not be covered under the Sussex Plan, she would have enrolled in alternative health coverage provided by her employer that would have covered her treatment. This fact, however, did not enter into the court's consideration of the issues in the present case. *See* note 29, *infra*.

2, 1998. As mentioned above, both women were beneficiaries under the Sussex Plan. Together, the medical expenses for Carol and Brenda were approximately $130,000.

III. DISCUSSION

Although the parties present numerous issues in their papers, the court believes there are essentially two crucial questions that must be answered in order to resolve this case. First, whether relevant Delaware Insurance Code provisions should be read into the Sussex Plan. Second, whether OCI could retroactively terminate the Sussex Plan without giving 30 days written notice. Although the issues involved overlap to a certain extent, the court will discuss them separately.

A. Should the Court Read 18 Del. C. § 7202(16) and (34) Into the Sussex Plan?

OCI argues that the terms "eligible employee" and "eligible employer" contained in Sussex Plan must incorporate 18 Del. C. § 7202(16) and (34).[20] OCI claims that, given the language of these sections, by covering Sussex and the Smiths after November 15, 1997, would have violated Delaware law. Sussex counters that the Sussex Plan contained no reference to applicable Delaware law and that, in any event, any violation of Delaware law would be preempted by ERISA.[21]

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[20]18 Del. C. § 7202 contains the definitions for regulating Delaware Small Employer Health Insurance. *See* 18 Del. C. § 7203 ("This chapter shall apply to any health benefit plan provided by a small employer which provides coverage to the employees of such small employer in this State.") 18 Del. C. § 7202(16) states in pertinent part, "'[e]ligible employee' means an employee who works on a full-time basis and has a normal work week of 30 or more hours." 18 Del. C. § 7202(34) states, "'small employer' mean any person, firm, corporation, partnership, or association that is actively engaged in business . . . ." OCI maintains that it would be "ridiculous and overbearing" to expressly include every single applicable state law in the Sussex Plan.

[21]ERISA preempts state statutes that "relate to" an ERISA benefit plan. The Supreme Court has held that ERISA preemption is "deliberately expansive". *See Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 46 (1987). A state law relates to an ERISA plan "if it has a connection with or reference to such a plan". *See Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 96-97 (1983). In this case, there is no

The Sussex Plan and the EOC contain what can be termed vague definitions of eligibility.[22] The EOC states "an individual must live or work in the OCI Service Area and be entitled to participate in the Subscriber's Group Health Program. . . ." The EOC also defines an eligible employee as a Group member who qualifies for health care coverage under the Group's eligibility requirements. The Sussex Plan states that the eligibility requirements are determined by "the Employer" and are "date of hire."

1. ERISA Analysis

Generally, ERISA preempts state laws that relate to any employee benefit plan. *See* 29 U.S.C. § 1144(a). Both parties agree, however, that where "ERISA does not have a specific guideline, the courts can look to federal common law, or in some instances, state law for resolution of an issue." *See* Pl. Rep. Br. Sum. J. at 18; *see also* Def. Op. Br. Sum. J. at 23. The question, therefore, becomes whether ERISA is indeed silent on the issues raised in this case. If so, the court may look to federal common law or to state statutes to interpret the Sussex Plan. *See Jones v. United States Life Ins.* Co., 12 F. Supp. 383, 388-89 (D. N.J. 1998) (citing cases).

Although Sussex takes various positions in its briefing, it ultimately argues that 29 U.S.C. § 1133 is applicable to this case.[23] Section 1133 provides that every employee benefit plan shall:

(1) provide adequate notice in writing to any participant whose *claim* for benefits under

argument that the Sussex Plan was an ERISA plan. The question is whether state law is preempted.

[22]Although generally contract terms are given their plain meaning, in the ERISA context ambiguities may be interpreted against the insurer. However, there is a state law directly on point. A requirement of continued employment or being engaged in business seems a basic assumption to the terms of this – or any Group health plan. *See* Section IVA2, *infra*.

[23]Sussex had originally argued that 29 § U.S.C. 1341 was also relevant but later withdrew its assertion. *See* Pl. Reply Br. Sum. J. at 18.

> the plan has been denied, setting forth the specific reasons for such denial, written in a manner calculated to be understood by the participant, and (2) afford a reasonable opportunity to any participant whose *claim* for benefits has been denied for a full and fair review by the appropriate named fiduciary of the decision denying the claim.

29 U.S.C. § 1133 (emphasis added). From the face of the statute (and the pertinent regulations),[24] it appears that this section applies to denials of claims rather than to the denial or cancellation of an entire plan. Indeed, many cases interpreting and applying § 1133 deal with specific claims and the myriad of associated administrative procedures. *See, e.g., Amato v. Bernard*, 618 F.2d 559, 566 (9th Cir. 1980) (stating that Congress' apparent intent in § 1133 was, among other things, "to promote the consistent treatment of claims for benefits; to provide a nonadversarial method of claims settlement; and to minimize the costs of claims settlement for all concerned); *see generally* Cooke, ERISA Practice and Proc. (2d ed.) § 8.19 (describing effect and legal requirements under § 1133).

Even if the court were to find that § 1133 applied and was violated, Sussex would not be entitled to the damages it seeks. *See Ashenbaugh v. Crucible, Inc.*, 854 F.2d 1516, 1532 (3d Cir. 1988) (noting that "general principle" that "employer's or plan's failure to comply with ERISA's procedural requirements does not entitle a claimant to a substantive remedy."). Rather, the appropriate course of action would be to remand the termination decision to OCI so that Sussex could "get the benefit of a full and fair review." *See Syed v. Hercules, Inc.*, 214 F.3d 144, 162 (3d Cir. 2001) (refusing to impose sanctions on company for denial of disability benefits since, inter alia, remedy would be improper and denial letter adequately

[24] The Secretary of the Department of Labor has established regulations for when a plan or an employer denies a claim and how the claimant may seek review of that denial; there is absolutely no mention of denial of an entire plan. *See* 29 C.F.R. § 2560.503-1(f).

stated reasons) (citing cases).[25] The court, therefore, concludes that § 1133 is inapplicable to OCI's decision to terminate the Sussex Plan.[26] As a result, Sussex may not rely on § 1133; ERISA is silent on the issues in the case.

2. Sussex Plan Analysis

The court must next determine whether various other requirements for "eligible employee" and "small employer" can be read into the Sussex Plan. Sussex's position appears to be that since OCI neither expressly defined "eligible employee" or "eligible employer" nor refers to 18 Del. C. §§ 7202(16) and (34) in the Sussex Plan it had no notice of the requirements of the statute. Therefore, Sussex contends, 18 Del. C. §§ 7202(16) and (34) should not be considered part of the Sussex Plan. In response, OCI states that Sussex points to no law (either under ERISA or state law) that requires OCI to expressly define an "eligible employer" or "eligible employee" in its plan documents so that the employer and employees have notice of terms (1) which have a "plain meaning," (2) are already defined by state law, (3) and are "impliedly incorporated" into all contracts.

The court believes that 18 Del. C. § 7202(16) and (34) can properly be read into the Sussex Plan

[25]As is noted below, even if OCI did not give ample notice prior to termination, the subsequent exchange of letters between the parties cured any procedural defect. *See* note 40 & accompanying text, *infra*.

[26]In its papers, OCI cites and discusses a case from the Eastern District of New York to support its reading of § 1133. *See Camarda v. Pan Am. World Airways, Inc.*, 956 F. Supp. 299, 310-11 (E.D.N.Y. 1997). The court has reviewed *Camarda* and finds its comments on § 1133 persuasive and instructive, especially those relating to the intent of the statute. Although Sussex attempts to distinguish *Camarda*, the case it cites does not unequivocally support its position. In *Kodes v. Warren Corp.*, the court found § 1133 applicable to plan terminations but acknowledged that *Camarda* took the opposite view. 24 F. Supp.2d 93, 103 (D. Mass. 1998). Not only is the court not bound to follow *Kodes*, there is no discussion or reasoning in the opinion, nor do the cases it cites uniformly support Sussex's position. *See id.*

since (1) federal common law and state law provides definitions of vague terms which are used in health insurance contracts and (2) even if Sussex was unaware of the exact definitions of "eligible employer" and "eligible employee" under Delaware law, continued employment is a implicit condition of the Sussex Plan.[27]

First, as noted above, the court can rely on any relevant evidence to assist it in interpreting vague terms in the Sussex Plan. ERISA is unhelpful in defining an "employee" within the context of an insurance. *See Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 323 (1992) (finding that ERISA's definition of employee is "circular and explains nothing"). However, under federal common law – and common sense – there appears to be a requirement that a person must actually be working to be an employee. *See id. at* 323-34 (applying general common law agency principles in determining whether individual is employee); *Matinchek v. John Alden Life Ins. Co.*, 93 F.3d 96, 100 (3d. Cir. 1996) (citing *Darden* approvingly and finding traditional agency principles apply in ERISA cases); *see also* 26 C.F.R. § 31.3121(d)-1(c) (Department of Labor regulations stating that determining employment relationship includes "usual common law rules").

Not only does federal common law support the need for continued employment, but the definitions of "eligible employer" and "eligible employee" in 18 Del. C. § 7202(16) and (34) provide the court better guidance as to the subjective intent and belief of the Smiths at the time they entered into the Sussex Plan. Additionally, although the Smiths claim that they were unaware of the provisions of 18 Del. C. § 7202(16)

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[27]Sussex contends that reading 18 Del. C. § 7202(16) and (34) into the Sussex Plan violates the ERISA "plain English" requirement of 29 U.S.C. § 1022. The court disagrees, however, since the Sussex Plan did include a section on eligibility. Although the court agrees that ERISA plans must clearly state eligibility requirements, allowing Sussex to contend that the term "date of hire" (which it chose) does not suggest actual employment as a criterion would render the requirement meaningless.

and (34), the court notes that this fact is usually insufficient to excuse or exempt them from the statute's effect.[28] Although ERISA is a complicated statutory scheme, the basic assumption of continued employment is not beyond the understanding of the ordinary citizen. At minimum, the Smiths should have realized that the fundamental change that occurred in the character of Sussex on or after August 1, 1997 which may have raised concern. As a result, the Smiths should have sought OCI's position on the issue.[29]

Sussex's argument that the Smiths failed to make a distinction between their roles as officers/board members/shareholders[30] on the one hand and employees of the corporation on the other is unavailing. According to Sussex, the Sussex Plan covered the Smiths in their capacities as both officers and employees of the corporation. Therefore, the Smiths did not believe that the changes the corporation underwent subsequent to August 1, 1997 were material to OCI. This logic flies in the face of federal common law, Department of Labor Regulations, and Third Circuit precedent. *See Matinchek*, 93 F.3d at 100-02. The distinction between "employers" and "employees" is firmly established. As the Third Circuit has stated, "[i]t would appear axiomatic that the employer-employee relationship is predicated on the relationship between two different people." *See id*, at 101-02. Thus, the Smiths cannot claim that they saw no

[28]Additionally, Sussex has not pointed to any evidence in the record to suggest that the Smiths did not believe continued employment was an implicit condition of the Sussex Plan. Instead, Sussex's attorney merely stated this position at oral argument.

[29]At oral argument, Sussex stated that the fact that Carol could have elected to enroll in health insurance through her employment suggests that the Smiths believed they acted correctly. The court does not agree with this statement. First, whether Carol could have procured coverage elsewhere is irrelevant to OCI's actions. Second, the court does not presume the Smiths had ill-intent in not informing OCI of the changes to Sussex. Rather, Sussex had an obligation to inform OCI of changes which would assist in the administration of the Sussex Plan. *See* note 39, *infra*.

[30]As noted above, John, Jr., John III, and Brenda were more than just employers. *See* note 14, *supra*.

difference between their actions in their corporate and their employee capacities; respecting the corporate form requires no less.

Sussex attempts to distinguish *Matinchek* on the facts. In its brief, Sussex argues that since the Sussex Plan originally covered both the Smiths (employer-employees) and other employees, the Third Circuit's reasoning in *Matinchek* about federal common law ERISA is inapplicable. The court is not persuaded and believes that the Third Circuit's concerns are equally applicable to this situation. Additionally, the Smiths' actions underscore the court's reasoning. Acting in their official corporate capacity, John, Jr., John III, and Brenda Smith passed a board resolution authorizing the payment of OCI's premiums "in lieu of salaries." Not only did they know enough to respect the corporate form, but the corporate minutes suggest the action was done to benefit "officers of the corporation" (rather than employees).[31] Furthermore, the "date of hire" eligibility requirement does not make sense for the Smiths acting in their corporate capacity. Although officers are hired, board members are usually elected, and shareholders normally just own stock.

Second, the requirement of employment in the Sussex Plan is not only simple common sense but also is implicit in Face Sheet (and the EOC). As noted above, one of the eligibility requirements is "date of hire." Making hiring an employee a condition of coverage suggests that continued employment is necessary for coverage. Indeed, the court does not understand Sussex to argue that OCI must continue coverage until Sussex sends notification that an employee has been terminated. In other words, Sussex

[31] The corporate minutes from August 2, 1997 state, inter alia, ". . . all monies received from the sale of assets of Sussex Auto Center, Inc. will be invested until such time as a viable business plan is reactivated. All officers of the corporation will defer salaries at this time. The Corporation agrees to cover benefits, i.e. health care coverage during this period."

does not appear to contend that even if OCI independently learns of an employee's termination, it cannot, under any circumstances, discontinue coverage until it hears from Sussex. The record demonstrates that Sussex knew to inform OCI when it terminated employees – it did so for non-Smith employees who worked for Sussex. Although the John, Jr. and John III continued in their capacity as officers of the corporation, they do not contend that they were still employees of the corporation.[32]

B. Did OCI Improperly Retroactively Terminate the Sussex Plan?

As an initial matter, this issue blends into the above discussion on implied terms of the Sussex Plan. OCI's argument is essentially that since Sussex, by its actions, removed itself from coverage under the Plan, OCI had authority to terminate it. Sussex retorts that although it sold "substantially all of its assets,"[33] it continued to pay Delaware taxes and the corporation remained in good standing in Delaware. According to Sussex's attorney, as of September 24, 1998, "[Sussex] is in the process of relocating and regrouping" and John F. Smith, Jr. and John F. Smith, III "are in the process of retraining for careers in new fields of expertise, so that the corporation can once again commence earning an income."[34] Therefore, determining whether 18 Del. C. §§ 7202(16) and (34) are part of the Sussex Plan essentially determines whether OCI

[32]Sussex's counsel stated at oral argument that after August 1, 1997 the Smiths settled receivables and participated for a short time in an auto parts telephone hotline. The main focus, however, was on retraining with an eye toward future reimbursement by the corporation. Thus, there was little (if any) income flowing into Sussex after August 2, 1997.

[33]OCI disagrees with this characterization since and believes that Sussex sold "all" its assets. The court need not decide this issue since it finds that Sussex's actions were sufficient to trigger the notice requirement under the Sussex Plan. *See* infra.

[34]According to the facts, however, Sussex let its business license expire on December 21, 1997. Presumably, Sussex would have to reapply for a new license if the corporation was to engage in a new type of retail business.

properly terminated coverage.

The Sussex Plan language states, in pertinent part, that "[i]n the event of a material breach of any terms and provisions of this Agreement, this Agreement may be terminated by the nonbreaching party, upon thirty (30) days prior written notice to the other party." *See* Sussex Plan § 6.3. Sussex argues that OCI acted improperly since it failed to give the requisite notice. OCI would presumably respond that § 6.3 does not apply since Sussex breached the terms of the Sussex Plan and was (or should have been) on notice of possible termination.

Both Sussex and OCI agree that the question of whether an ERISA plan can be retroactively terminated when an employer fails to notify the health carrier of material information concerning the status of its employees who are no longer employed is one of first impression in this circuit. Indeed, neither party cites any authority to directly support its position. Instead, OCI attempts to analogize this situation to one where retroactive termination resulted from material misrepresentations and omissions *before* the plan went into effect. Sussex contends that this analogy is inappropriate since once the parties agree to the terms of the plan, the language of the plan governs; there is no evidence of any wrongful conduct or omissions by Sussex at the time the plan was agreed upon. Furthermore, Sussex argues that the issue is not whether it breached, but rather whether the breach entitles OCI to retroactively terminate the Sussex Plan (the plan documents only specifically contemplate prospective termination). In looking for guidance, the court concludes OCI's analogy is apt. OCI offers both caselaw and an affidavit to support its position.[35]

[35]The affidavit is from Gregg P. Allen, M.D. and is the subject of a separate motion to strike by Sussex (D.I. 96). The affidavit is extrinsic evidence and is proper since the court is reviewing the record de novo. Dr. Allen is purported to be an expert in "HMO administration." As an expert, he is allowed to give opinions on facts. Parts of Dr. Allen's affidavit, however, appear to usurp the court's

The cases on which OCI principally relies are *Brasure v. Optimum Choice, Inc.*, 37 F. Supp.2d 340 (D. Del. 1999), and *Oglesby v. Penn Mutual Life Ins. Co.*, 877 F. Supp. 872 (D. Del 1994), *aff'd*, 127 F.3d 1096 (3d Cir. 1997). In *Brasure*, the plaintiff omitted or misstated his prior medical history on his individual risk assessment form that OCI (the defendant in that case as well) used to determine eligibility for coverage.[36] After covering him for approximately two years, OCI discovered that Brasure had not been forthcoming regarding his medical history. As a result, it retroactively terminated his coverage back to the date he enrolled in the plan. In support of its motion for summary judgment, OCI employees testified that if they been aware of Brasure's actual medical condition, they would have rejected health coverage based on medical underwriting risk guidelines. In deciding the case, Judge Schwartz held that Brasure's failure to disclose his medical history was material, that he breached his duty, and that OCI was not under a duty to investigate further. *See Brasure*, 37 F. Supp.2d at 346. In *Oglesby*, Judge Schwartz applied Delaware law and held that:

> an enrollee had a duty to disclose information concerning any material physical disease in his past that is known to him. If the enrollee does not do so he or she has failed to meet the duty to act with utmost fairness. Where the duty of utmost fairness is not met due to the applicant's knowledge, Delaware courts have consistently held that a court may grant rescission on an insurance contract based on a misrepresentation.

Oglesby, 877 F. Supp. at 888.

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role in deciding issues of law. For example, Dr. Allen reads the "plain language" of 18 Del. C. §§ 7207(16) and (34) and applies it to this case in what he believes is the "only" interpretation. Additionally, Dr. Allen states that Sussex's failure to inform OCI of the change in the status of its employees meant that OCI had "no choice" in terminating the Sussex Plan. Rather than striking the affidavit, the court will accept Dr. Allen's affidavit for what it is worth and views it as an opinion it may agree or disagree with in addressing the legal issues in the case.

[36]In filling out the form, Brasure did not inform OCI that he had undergone surgery in the past five years. In reality, Brasure had splenectomy surgery in October, 1994.

Even if the analogy between *Brasure* and *Oglesby* on one hand and Sussex on the other is imperfect, the law is clear that when parties enter into an ERISA plan, they are charged with informing each other of "material" information. As Judge Schwartz stated, "[u]nder federal common law, a misstated or omitted fact is deemed 'material' if it could reasonably be considered as affecting either the insurer's decision to enter into the contract, its evaluation or calculation of risk, or its calculation of the premium to be charged." *See Brasure*, 37 F. Supp.2d 340, 345 (citing cases). Furthermore, "failure to disclose conditions known to the applicant that would affect the risk renders the policy voidable."[37] *See id.*; *cf. Shelton v. Annuity Bd. of The Southern Baptist Convention*, 915 F. Supp. 124, 128-30 (E.D. Mo. 1996) (holding that since plaintiff "ceased being a salaried employee" he was not eligible for coverage under clearly defined ERISA plan, notwithstanding his "change of circumstances" argument).

In this case, it is not disputed that Sussex's character as a corporation changed dramatically after August 1, 1997. At minimum, Sussex sold much of property and its name, changed its business address from Delaware to Maryland, fired its employees, stopped paying employee wages and signed a two year non-compete agreement. Although Sussex maintains that the Smiths were in the process of retraining and looking for other business opportunities, there is no dispute that the corporation was no longer generating an income stream on the level it was prior to August 1, 1997. At best, Sussex was a corporation in suspended animation and at worst it was merely a shell. Nevertheless, Sussex knew it had implicit obligations to OCI; Sussex informed OCI of two important changes – the address change and the

[37] According to the Second Restatement of Contracts § 7, a "voidable" contract is "one where the parties have the power, by a manifestation of election to do so, to avoid the legal relations created by the contract, or by a ratification of the contract to extinguish the avoidance."

termination of two non-Smith employees. These facts suggest that, at minimum, Sussex should have informed OCI of important changes in the life of the corporation, rather than picking and choosing what it deemed important..

The court does not mean to suggest any fraudulent motivation by the Smiths in failing to inform OCI of the changes to Sussex. Rather, the issue is whether OCI should be held accountable for the Smith's actions (or more appropriately inactions). In essence, OCI was no longer dealing with the same entity with which it contracted. Although Sussex paints the issue as one of "retroactive termination," doing so appears to put the cart before the horse; it was Sussex's transformation, rather than OCI's actions, that rendered the Sussex Plan voidable.[38]

Furthermore, *Corbari v. St. Joseph's Omni Health Plan*, presents a slightly more analogous situation. 38 F. Supp.2d 861 (E.D. Cal. 1998). In 1993, Corbari began working and enrolled in the Omni Healthcare plan (the "Omni Plan") through his employer. At the time of his enrollment, he lived in Modesto, California and also owned a house in Orange County, California.[39] In May, 1996, Corbari relocated to Southern California and began working on commission (rather than on salary). He lived in Southern California and traveled back and forth to Modesto. Although the agreement was supposed to be

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[38]Section 1.3 of the Sussex Plan states, "[n]o change in the Employer's eligibility or participation requirements shall be permitted to affect the eligibility or enrollment under this Agreement unless such change is agreed to in writing by OCI." Section 8.6 states, "[e]mployer must furnish OCI with any data required by OCI for coverage of Eligible Employees and Dependents under this Agreement. In addition, Employer must provide timely notification to any changes in membership, *such as*: family status, a child ceasing to be a Dependant, or death." (emphasis added). According to the language of the Sussex Plan, the list of membership changes is non-exclusive. Therefore, Sussex arguably did not fulfill its duty to OCI.

[39]Modesto was in the Plan's "service area" but Orange County was not. *See id.*, at 863, n.1.

“temporary,” the parties left it open-ended. Corbari never notified Omni of the change.

On August 18, 1996, Corbari suffered an aneurysm and was taken to a hospital in Southern California. On the hospital admission form, Corbari listed his address as Huntington Beach (in Southern California) rather than in Modesto. While in the hospital, an employee of Omni informed Corbari’s employer that the Omni Plan covered employees who were “temporarily” out of the service area. Subsequently, Corbari’s employer notified Omni that Corbari “moved to Southern California as the Company’s Commissioned Sales Representative . . . .” but did not mention that the change in location and employment status were temporary. After receiving the letter, Omni informed Corbari’s employer that it was attempting to defraud the Omni Plan by enrolling an employee who worked outside of the service area and was not a salaried employee. On September 30, 1996, Omni sent Corbari a letter terminating coverage retroactive to June 1, 1996 on the grounds that he “had become ineligible . . . because he no longer lived or worked in Omni’s service area, and was not a salaried employee.” *See Corbari*, 38 F. Supp.2d at 863.

Although the Omni Plan better defined both the service area and who was an “employee” than the Sussex Plan did, the principle of retroactive termination based on changed circumstances is the same. Importantly, neither Corbari nor his employer notified Omni of any change in his residency or salary at the time of the changes in his status. In this case, Sussex (1) remained a Delaware corporation but changed its address to John III and Brenda’s residence in Rhodesdale, Maryland on November 15, 1997 and (2) no longer paid the Smiths a salary for working (they largely acted in their corporate capacity). Like Omni, OCI retroactively terminated the Sussex Plan to the date Sussex moved out of the service area.

Finally, although OCI sent Sussex a letter on July 9, 1998 which terminated coverage as of

November 15, 1997, the parties subsequently exchanged a series of letters. In these letters, counsel for Sussex first sent OCI information regarding Sussex's status. On August 4, 1998, OCI sent Sussex a series of questions and stated "[OCI] is willing to review this situation further with you . . . ." As a result, Sussex sent OCI another letter answering its questions and asking some of its own. OCI's last letter is dated October 20, 1998 and concludes, "[y]ou have provided me with no new evidence . . . that would persuade me that the employees that were covered under the Sussex Auto Center, Inc. group contract are still active employees of the company. Therefore, we are unable to reinstate coverage."

Even if OCI's original letter terminated coverage without sufficient notice (a conclusion the court already rejected), the subsequent exchange of letters allowed Sussex an opportunity to argue its case and convince OCI that it acted improperly. Since OCI's final letter (and final decision) is more than three months after its initial one, it functionally gave Sussex more than ample notice of its decision to terminate the Sussex Plan. In this light, the court believes that Sussex's claim of improper termination without 30 days notice is a distinction without a difference. Even assuming OCI did not give proper notice to Sussex before retroactively terminating the Sussex Plan, the several month exchange of letters made any error harmless.[40]

The court does not agree with Sussex that under no circumstance could OCI have retroactively terminated the Sussex Plan. Such a result would potentially mean that insurers would be hamstrung and

[40]At oral argument, Sussex weakly attempted to distinguish the court's analysis by stating that since the letters were exchanged by Sussex's attorney after the initial termination letter, the notice was ineffective. Although the court agrees that this was not the normal method of notice under the Sussex Plan, it is beside the point. Instead, the letters *functionally* operated as notice – among other goals, the point of notice is to allow an insured to challenge a decision. Sussex attempted to convince OCI of its position. That Sussex's efforts failed speaks more to the facts than the timing of the notice.

forced to accept the consequences of any action by insured parties so long as it was done in secret. Not only would this undermine the relationship between the parties, it would also encourage inefficiencies in the delivery of health insurance.

VI. CONCLUSION

Upon reviewing the record de novo – including evidence not before OCI on July 9, 1998 – the court concludes that OCI did not (1) wrongfully retroactively terminate the Sussex Plan to November 15, 1997 and (2) improperly deny or retract health benefit payments for Carol and Brenda Smith after November 15, 1997. In reaching this conclusion, the court finds that ERISA does not preeempt 18 Del C. § 7202(16) and (34) and that the statutory definitions are implicitly read into the Sussex Plan. Although the court will enter summary judgment in favor of OCI on Sussex's claims, it declines to rule explicitly on the merits of OCI's counterclaim since it believes doing so is unnecessary.[41] The court will issue an appropriate order consistent with this memorandum opinion.

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[41] In its counterclaim, OCI stated that since Sussex allegedly breached its fiduciary duty, Sussex should be held responsible for contribution and indemnity if it was found liable. Since the court holds that OCI acted properly and is not liable, such a ruling is unnecessary . Furthermore, the practical effect of finding Sussex responsible for a breach of fiduciary duty is nil; requiring Sussex to pay the Smiths for denied benefits is nothing more than forcing them to repay themselves.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE

SUSSEX AUTO CENTER, INC., a corporation of the State of Delaware on its own behalf and on behalf of CAROL P. SMITH and BRENDA M. SMITH, individually,	)	Civil Case No. 99-376-GMS
Plaintiffs,	)	
v.	)	
OPTIMUM CHOICE, INC., a corporation of the State of Maryland, conducting business in the State of Delaware,	)	
Defendant.	)	

MEMORANDUM OPINION

John A. Sergovic, Jr., Esq. of SERGOVIC, ELLIS & SHIREY, P.A. Wilmington, Delaware.
Attorney for Plaintiffs and Counterclaim Defendants.

Curtis J. Crowther, Esq. of WHITE AND WILLIAMS LLP, Wilmington, Delaware. Of Counsel:
David A. Manoogian, Esq. and Joanna Jesperson, Esq., of EPSTEIN, BECKER & GREEN, P.C.,
Washington, D.C.
Attorneys for Defendant and Counterclaim Plaintiff.

July 20, 2001
Wilmington, Delaware.

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Plaintiffs,	)	
v.	)	
OPTIMUM CHOICE, INC., a corporation of the State of Maryland, conducting business in the State of Delaware,	)	
Defendant.	)	

ORDER

For the reasons stated in the court's Memorandum Opinion of the same date, IT IS HEREBY ORDERED THAT:

1. OCI's motion for summary judgment (D.I. 85) is GRANTED in part.[42]

2. Summary judgment be and is hereby ENTERED in favor of OCI on all claims against it in this action.

3. Sussex's motion to motion to strike (D.I. 96) is DENIED as moot.

4. OCI shall return any and all premiums paid by Sussex on or after November 15, 1997. Any timely appeal to the Third Circuit will stay OCI's repayment obligation.

Dated: July 20, 2001

Gregory M. Sleet
UNITED STATES DISTRICT JUDGE

[42]The court believes that the entry of summary judgment in favor of OCI renders its claim against Sussex moot. Any ruling on the merits would most likely be an advisory opinion. *See* Mem. Op, at note 41.