

Second Circuit Grants Fund's Audit Request Well Beyond CBA Coverage

By Robert R. Perry

September 9, 2022

Meet the Authors



Robert R. Perry

Principal
212-545-4000
Robert.Perry@jacksonlewis.com

Related Services

Employee Benefits
Labor Relations

In a decision that bodes poorly for unionized employers, the U.S. Court of Appeals for the Second Circuit recently held that a union benefit fund was contractually entitled to conduct an audit whose scope far exceeded the bargaining unit for whom fund contributions were required. Since the employer did not produce evidence that the fund trustees' conduct of the audit breached their ERISA fiduciary duties, the court held that the fund was entitled to conduct the requested audit. *New York State Nurses Association Benefits Fund v. Nyack Hospital*, No. 20-378 (2d Cir. Aug. 19, 2022).

Factual Background

The facts in *Nyack Hospital* are not unusual. Nyack Hospital (the Hospital) had about 1,400 employees, one-third of whom were registered nurses. Most of these nurses were covered by a collective bargaining agreement (CBA) between the Hospital and the New York State Nurses Association (NYSNA). Of the Hospital's 900 or so non-nurse employees, about 700 were represented by three other unions.

The NYSNA Benefits Fund (the Fund) is a multiemployer fringe benefit fund that provides health and welfare benefits to eligible employees of hospitals who are parties to CBAs with NYSNA. Under the Hospital's CBA, regular full-time and part-time employees are covered employees eligible for coverage under the Fund for whom Hospital contributions are required; per diem employees and temporary employees are not eligible. The only employees for whom Fund contributions could therefore possibly be required were registered nurses.

The Fund's Information and Audit Requests

Like most multiemployer benefit funds, the Fund relies on employer self-reporting and periodic payroll audits to make sure that all required contributions are properly remitted by employers. Several documents addressed the Fund's and the Hospital's rights and obligations in this regard. The CBA requires the Hospital to provide the Fund trustees with documentation reasonably necessary "to establish... the number of and identity of such Employees for whom contributions were made during the term of" the agreement. Via a written acknowledgement (Acknowledgement) required under the CBA, the Hospital agreed to be bound by and subject to the Fund's governing trust agreement (Trust Agreement). Under the Trust Agreement (which by its terms trumped the CBA in the event of a conflict except where otherwise provided in the Acknowledgement), the Fund may "have an audit made by independent certified public accountants of the payroll and wage records of any Employer in connection with the said Employer Contributions, Employee Contributions, and/or reports."

Relying on this authority, the Fund notified the Hospital that the Fund's auditors intended to conduct an audit of the Hospital's payroll and related data and requested information for all

of the Hospital's workforce. This request covered many employees (including the Hospital's executive team and engineering staff) who were neither arguably covered by the CBA nor remotely eligible for Fund benefits. The Fund's justification for this (at least arguably) overbroad request was that the requested records were needed to: (1) make sure that the Hospital made all contributions required under the CBA; and (2) allow the Fund to identify all eligible employees and notify them of their status and rights to benefits.

When discussions regarding potential compromises (such as the parties entering into a confidentiality agreement) collapsed and the Hospital eventually refused to provide information for any employees other than those covered by the CBA (e.g., the registered nurses), the Fund filed suit in Federal district court seeking an order compelling the production of the information and the conduct of the audit.

The District Court Action Limits the Audit to Registered Nurses

The Fund's suit alleged that the Hospital's failure to comply with the Trust Agreement's audit provision violated ERISA and the Labor Management Relations Act. After the Hospital's motion to dismiss the audit as overbroad and impermissible was denied, cross-motions for summary judgment followed. The Fund argued that its auditors were entitled to look at the payroll records of all employees, and the Hospital argued that the Fund was entitled to audit only the payroll records of registered nurses who were covered by the CBA.

The district court granted the Hospital's motion in part, finding that the Fund had produced no evidence that "an audit of all of Nyack's employees' payroll records, as opposed to just registered nurses" would further any of the Fund's stated purposes. The district court concluded that an audit of all of the Hospital's registered nurses (not just those covered by the CBA) was appropriate. Both parties appealed, with the Fund arguing that the scope of the audit framed by the district court was too narrow and the Hospital arguing that it was too broad.

The Second Circuit Reverses

Majority Opinion

The Second Circuit reversed the court below. The Court began by analyzing the scope of an ERISA-covered plan's audit authority under the Supreme Court's decision in *Central States, Southeast and Southwest Areas Pension Fund v. Central Transport, Inc.*, 472 U.S. 559 (1985) (*Central States*). *Central States* similarly involved a fund seeking to audit a group far broader than that covered by the applicable CBA. The *Central States* trust agreement was similarly vague; it permitted the trustees to "examine the pertinent records of each Employer at the Employer's place of business whenever such examination is deemed necessary or advisable by the Trustees in connection with the proper administration of the Trust."

Central States held that the trustees had the authority to conduct the requested audit under the foregoing provision of the trust agreement, and that reviewing records of persons who were not participants was "entirely reasonable in light of ERISA's policies." The only limit placed on a fund's contractual audit rights was where the audit was being used by the trustees to further purposes that were at odds with the trustees' fiduciary duties under ERISA. Accordingly, *Central States* holds (at least according to the majority opinion) that a court should enforce an audit request that is otherwise permitted under the trust agreement unless the conduct of such audit would breach the trustees' fiduciary duties of

loyalty or prudence. The Court cited audits that were disguised efforts “to expand plan coverage beyond the class defined in the plans’ terms or to acquire information about the employers to advance union goals,” or “clearly wasteful of plan assets or unrelated to legitimate plan concerns” as examples of forbidden conduct.

As the Court applied the *Central States* framework, any audit request that falls within the scope of what is permitted will be enforced unless the employer has offered evidence that the implementation of such a request would breach the trustees’ fiduciary duties of loyalty or prudence.

Noting that “the language of the Trust Agreement is phrased in broad terms, without any words of limitation,” the Court first found that the audit was within the scope of the Trust Agreement’s audit provision. In so doing, it ignored arguments advanced by the Hospital (and ultimately by the dissent, discussed below) that the broad language of the Trust Agreement should be narrowed and restricted to what the Hospital was required to provide under the CBA (documentation reasonably necessary for the Fund to identify the number and identity of employees for whom contributions were made), and that any “expansive” reading of the Trust Agreement was “undercut by the CBA.”

Having concluded that the requested audit was within the Trust Agreement’s permissible audit scope, the Court turned to whether the Hospital had offered evidence that the implementation of the requested audit would result in a breach of the Fund trustees’ fiduciary duties under ERISA. Since such evidence was not surprisingly lacking, the majority held that the Fund was allowed to conduct the requested audit.

The majority opinion seemingly scolded the district court for not (likely due to its “erroneous ruling as to the scope of the documents Nyack was required to provide”) considering whether a confidentiality agreement (which the Fund’s auditors had offered) was necessary or sufficient to address the Hospital’s concerns against the potential misuse of confidential information, instructing the district court to “exercise its considerable discretion to determine whether and how to issue an appropriate confidentiality order.”

Dissenting Opinion

In a lengthy dissent, Judge Carney did not accept that the Trust Agreement or *Central States* compelled an all-employee audit.

With respect to the scope of the Trust Agreement’s audit provision, the dissent noted that the audit clause does not use the word “all” or otherwise unmistakably indicate a comprehensive workforce-wide obligation. To the contrary, it refers to and identifies payroll records with reference to the Hospital’s contribution obligations (which is limited to registered nurses). Further, the dissent argued, the scope of the “the payroll and wage records” that the Hospital was required to produce must be read in tandem with the CBA and limited accordingly. In sum, the dissent argued, the plain language of the Trust Agreement did not support the Fund’s request for an audit of the Hospital’s entire workforce.

With respect to *Central States*, the dissent argued that the majority “overread” that decision by implying that in the absence of a demonstrated violation of fiduciary duties by the employer, a district court lacks discretion to limit the scope of a requested audit. To the contrary, the dissent argued, where there is ambiguity in the authorizing documents (which

ambiguity would arguably be present here), “*Central States* does not constrain the district court from crafting a suitable production order.”

Take-Aways

Nyack Hospital illustrates one of the hazards faced by employers with multiemployer contribution obligations, that of an overly intrusive fund audit. Despite all bargaining unit members being registered nurses, the Hospital was ordered to produce records for their entire workforce, two-thirds of whom were not registered nurses. The decision also illustrates the importance of an employer anticipating this issue and addressing it during bargaining. As the majority noted, if the Hospital wanted to limit its production obligations, the place in which to have done so would have been in the Acknowledgment (in which it unequivocally agreed to be bound by the Trust Agreement).

The one bright note seems to be the emphasis that the Second Circuit placed on providing appropriate confidentiality protections for the employer. Such protections could help alleviate some concerns when an employer is presented with a fund’s information/audit request.

If you have any questions or require anything further, please contact the author.

©2022 Jackson Lewis P.C. This material is provided for informational purposes only. It is not intended to constitute legal advice nor does it create a client-lawyer relationship between Jackson Lewis and any recipient. Recipients should consult with counsel before taking any actions based on the information contained within this material. This material may be considered attorney advertising in some jurisdictions. Prior results do not guarantee a similar outcome.

Focused on labor and employment law since 1958, Jackson Lewis P.C.'s 1000+ attorneys located in major cities nationwide consistently identify and respond to new ways workplace law intersects business. We help employers develop proactive strategies, strong policies and business-oriented solutions to cultivate high-functioning workforces that are engaged, stable and diverse, and share our clients' goals to emphasize inclusivity and respect for the contribution of every employee. For more information, visit <https://www.jacksonlewis.com>.