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MONTHLY ELECTRONIC SUBROGATION NEWSLETTER JULY 2007

TO CLIENTS AND FRIENDS OF MATTHIESEN, WICKERT & LEHRER, S.C.:

This monthly electronic subrogation newsletter is a service provided exclusively to clients and friends of Matthiesen, Wickert & Lehrer, S.C. The vagaries and complexity of nationwide subrogation have, for many lawyers and insurance professionals, made keeping current with changing subrogation law in all fifty states an arduous and laborious task. It is the goal of Matthiesen, Wickert & Lehrer, S.C. and this electronic subrogation newsletter, to assist in the dissemination of new developments in subrogation law and the continuing education of recovery professionals. If anyone has co-workers or associates who wish to be placed on our e-mail mailing list, please provide their e-mail addresses to Rose Thomson at rthomson@mwl-law.com. We appreciate your friendship and your business.

WORKERS' COMPENSATION SUBROGATION

TO INTERVENE OR NOT INTERVENE?

That Is the Question in California Workers' Compensation Subrogation

Workers' compensation carriers across the country continue to wrestle with the seemingly simple decision as to whether they should protect their subrogation interests by intervening into California third-party actions or simply file a Notice of Lien, and hope some of the third-party funds will find its way to them. This article will analyze the applicable law relating to this issue, and provide the subrogation professional with some guidance in making the right decision in the right case.

Understanding the nuances of the somewhat complicated and confusing subrogation law in California is instrumental in formulating the right decision when it comes to protecting your workers' compensation subrogation interests. The California Act makes clear that either the employee or employer may bring a third-party action. Such an action must be brought within the two-year statute of limitations for personal injury and wrongful death actions in California, and this statute is not tolled by the fact that special damages may be accruing or workers' compensation payments may be in the process of being made during this time period. The employer is entitled to file an independent action against the third party, intervene into an employee's lawsuit filed against a third party, or file a Notice of Lien in the pending third-party action. If the civil action against the third-party tortfeasor is brought by the employee alone, the employer can apply for first lien against the judgment for damages in the amount of the employer's expenditure for compensation together with amounts to which he or she may be entitled for special damages under California Labor Code § 3852. This has become known as filing a "Notice of Lien".

The simple act of filing a Notice of Lien is attractive and deceptively simple for any subrogation professional. It seems relatively easy to do, and the downside is not readily apparent. Filing a Notice of Lien doesn't work any magic other than putting the salient parties on notice of a carrier's workers' compensation subrogation interest. It doesn't give a subrogated party any greater rights than already exist under California law, but serves only to memorialize notice to the parties. It will help ensure that the parties do not settle without giving notice to the carrier. It can be filed with the court for no fee. However, this is absolutely the weakest form of enforcing a worker's compensation carrier's subrogation interest. It should be used in smaller cases, cases in which there are limited third-party insurance limits, or cases with obviously weak liability. A worker can "settle around" a workers' compensation carrier by expressly

excluding from his/her settlement with the third party the carrier's reimbursement claim. Merely filing a Notice of Lien will not protect the carrier should the parties settle around the carrier and will not give the carrier any protection from the plaintiff's attorney's claim for attorney's fees which will be paid out of the carrier's lien. The foregoing is true even where the worker is killed. The risk of proceeding with only a Notice of Lien must be weighed against the potential cost of intervening and putting into play more strenuous protection and participation options.

In essence, the workers' compensation carrier may do one of three things to protect its workers' compensation liens: (1) bring an action directly against the tortfeasor on its own; (2) join as party plaintiff by intervening in third-party action brought by the employee; or (3) allow the employee to prosecute the action and then apply for first lien against the resulting judgment or settlement.

The level of activity a carrier chooses will have a direct effect on the amount of a carrier's recovery, or whether the carrier will be able to recover at all. The less active a carrier is in a case, the more likely a plaintiff and defendant will settle around the carrier, knowing that there is no way that the carrier, with its limited activity and involvement in the case, will be able to gear up and try the case. Larger files (lien and/or credit combined) and files with better liability are usually candidates for interventions as opposed to mere Notices of Liens. The level of activity a carrier chooses to engage in after filing an intervention will also depend on those same criteria. Section 3862 provides for "perfecting a lien" upon a judgment in a third-party action. It reads as follows:

> ***§ 3862. Enforcement of employer's lien against judgment.*** *Any employer entitled to and who has been allowed and has perfected a lien upon the judgment or award in favor of an employee against any third party for damages occasioned to the same employer by payment of compensation, expenses of medical treatment, and any other charges under this act, may enforce payment of the lien against the third party, or, in case the damages recovered by the employee have been paid to the employee, against the employee to the extent of the lien, in the manner provided for enforcement of money judgments generally*.

This section, along with § 3852, seems to be the statutory source of authority in California for filing a Notice of Lien in those cases which may not justify an intervention or the filing of an independent third-party action by the carrier. However, as indicated above, the filing of such Notice of Lien doesn't appear to have any more force or effect than simply giving all parties notice of the carrier's statutory subrogation interest under California law, and can leave the subrogated carrier vulnerable to a variety of lien avoidance techniques which California trial lawyers regularly avail themselves of.

Filing an intervention and active participation have benefits beyond merely thwarting the plaintiff's attorney's effort to settle around you or take a significant portion of your lien as an attorney's fee. In California, a carrier's lien can be substantially reduced by the percentage of employer negligence which is found to exist. Therefore, an employer is only reimbursed for the amount by which its compensation liability exceeds its proportional share of the worker's recovery. Even in a case involving a lot of employer negligence in which any recovery is unlikely, active participation in the case may well result in a significant increase in the amount of future credit the carrier is entitled to, over what would have otherwise been available in the absence of such efforts. We all know that in many cases, the future credit and reserve takedown can be more valuable to the carrier than the lien recovery.

Twenty-five years of workers' compensation subrogation experience has taught us that most of our clients see a net recovery of between 25% and 35% of their lien when utilizing a simple Notice of Lien. In cases involving smaller liens (less than $25,000), this may be the preferred method of protection. This is because after deducting attorneys' fees incurred by subrogation counsel, attorneys' fees possibly awarded to plaintiffs' counsel, and a pro rata share of costs, the $25,000 lien may be reduced to as little as $10,000. Utilizing a Notice of Lien in such cases, especially such smaller cases where liability is speculative, a recovery of $8,000 may be expected, and the two methods of protecting your lien yield similar results, without the risk of incurring fees and costs and receiving a defense verdict on the third-party case to boot.

On the other hand, in cases of clear liability and/or in cases where the lien is between $25,000 and $100,000, the decision as to whether to intervene or to simply file a Notice of Lien should be evaluated in a risk/benefit manner, calculating likely recoveries in comparison with likely expenses. Approximately 75% of the time, these calculations lead to the conclusion that intervening will be the smarter option – increasing your net recovery and showing your insureds that you are serious and aggressive about protecting their subrogation interests and keeping their risk modifier low.

In cases involving liens of more than $100,000, the intervention route is almost universally the smartest choice. Only in cases involving the slimmest of third-party liability should liens of this size be protected only with a Notice of Lien. In this category of larger lien files, it is important to engage experienced subrogation counsel. The reason? Counsel must advise you as to three levels of activity which can be undertaken. Whether your subrogation counsel employs low, medium, or high levels of participation in the third-party case, will determine whether the carrier has an ability to defeat any claim for attorney's fees made by the workers' compensation attorney. If an employer or carrier actively participates in procurement of a common fund, apportionment is inappropriate and can be avoided. However, merely showing up for depositions or filing one or two documents, lacking in any real substance, does not qualify as active participation and may not be sufficient to defeat the worker's right to receive a contribution to the costs of the procurement of the third-party settlement. In general, an employee is entitled to attorneys' fees as long as there was no active participation by the carrier in the third-party litigation.

In the larger cases (more than $100,000), the level of activity should be determined by both the strength of the third-party liability and the sufficiency of third-party liability insurance available. The stronger the liability and the more insurance available, the higher the level of activity should be. This is because higher activity will increase the carrier's net recovery disproportionate to the cost necessary to increase it. Although the figures vary, every dollar spent on subrogation efforts in such cases can realize $10 or more in increased recoveries.

Quality subrogation counsel should help subrogation professionals decipher the many options which California workers' compensation law presents. Whether to file a Notice of Lien or intervene into a third-party action, whether to be active or passive in the third-party action, etc. all must be determined by looking at all of the variables which present themselves in the great State of California.

MADE WHOLE DOCTRINE

CALIFORNIA COURT NARROWS MADE WHOLE DOCTRINE

Allstate Ins. Co. v. Superior Court, 2007 WL 1704017 (Cal. App. 2007).

On June 14, 2007, the California Court of Appeals for the 4th District struck a blow for the good guys in the ongoing made whole battle which is waging in this country's courts. As some courts broadly apply the doctrine to defeat virtually any subrogation or reimbursement right – even going so far as to apply it to workers' compensation scenarios – other courts have rationally scaled back its applicability and more narrowly apply it to only a specifically defined set of facts. California has joined a growing list of states that hold that the insured's attorney's fees should not be deducted before determining whether that insured has been "made whole".

In *Allstate Ins. Co. v. Superior Court,* Tony Delanzo was injured in an automobile accident. Allstate paid Delanzo $4,203.36. Delanzo then settled his claim against the third-party tortfeasor for $11,000, and received the settlement payment in full. Delanzo alleged he incurred attorney fees of $3,850 and costs of $2,076.84 (for a total of $5,926.84) to obtain this settlement. Allstate requested that Delanzo repay the $4,203.36 under Allstate's policy provision, which states:

> *"Subrogation Rights. When we pay, your rights of recovery from anyone else become ours up to the amount we have paid. You must protect these rights and help us enforce them."*

In response, Delanzo paid Allstate $1,696.13, which Allstate agreed was in full satisfaction of its reimbursement claim. Allstate agreed to the reduction based on the common-fund rule that an insurer is required to deduct from its reimbursement a pro rata portion of the insured's attorneys' fees and costs incurred to recover covered losses against a third-party tortfeasor when the insurer had knowledge of, but did not participate in, the litigation. (NOTE: In California an insurer can avoid such a reduction by participating in the third-party action – a good reason to engage subrogation counsel in most cases.) Delanzo filed a class action lawsuit alleging that Allstate's reimbursement claim was improper and unlawful because Delanzo was not first "made whole" by the third-party settlement ($11,000) plus the amount received from Allstate ($4,203.36), when taking into account the attorneys' fees and costs incurred to obtain the settlement ($5,926.84).

The issue for the Court of Appeals was whether, under California law, the made whole rule precludes an insurer's reimbursement from its insured under a med-pay policy provision after the insured obtains a recovery from a third party which fully compensates the insured for his or her personal injury losses, but the insured's attorneys' fees and costs reduce that amount such that the insured's net recovery is less than his or her total losses? The court held that it did not.

In understanding the impact this decision may have on the ubiquitous made whole defense, it is important to understand the interplay between subrogation, reimbursement, and the made whole doctrine. Traditionally, an insurer that pays its insured's claim is entitled to recover the payment from the third party who caused the insured's covered loss. This concept is called subrogation, and can arise by contract, statute, or equitable principles. *Hodge v. Kirkpatrick Development, Inc.*, 130 Cal. App.4th 540 (Cal. App. 2005). Upon subrogation, "the insurer succeeds to its insured's rights against the third party in the amount the insurer paid." The insurer's subrogation right is similar to its right to reimbursement from its own insured, and many courts refer to the two concepts under the umbrella rubric of "subrogation." *Progressive West Ins. Co. v. Yolo County Superior Court*, 37 Cal. Rptr.3d 434 (Cal. App. 2005). But unlike true subrogation, the insurer's reimbursement right is contingent on an actual recovery by the insured from a third party. For certain types of claims, an insurer has no subrogation rights directly against a third party, and must seek recovery only by reimbursement. In California, a claim for personal injuries is not subject to subrogation because this claim cannot be assigned. California courts hold that an insurer may obtain reimbursement of proceeds paid for personal injuries by enforcing policy provisions entitling the insurer to reimbursement from its insured.

The made whole rule is a common law exception to an insurer's subrogation right. As applied in California, the rule generally precludes an insurer from recovering *any* third-party funds unless and until the insured has been made whole for the loss. *Progressive West Ins. Co.*, supra. The applicability of the doctrine generally depends on whether the insured has been completely compensated for all the elements of damages, not merely those for which the insurer has indemnified the insured. California courts have historically applied the made whole rule in property loss claims. *Finnell v. Goodman & Co. Bank,* 156 Cal. 18 (Cal. 1909). However, one court recently held for the first time that the doctrine applies in a personal injury (reimbursement) context under no-fault med-pay insurance coverage. *Progressive West Ins. Co.,* supra. The *Progressive West Ins. Co.* court was not asked to decide, and did not discuss, whether or not to include attorneys' fees in calculating whether the insured was "made whole". The specific issue presented here regarding the proper calculation of the insured's recovery under the made whole rule is one of first impression by the courts in this state. One California court applied the made whole doctrine in a property insurance case and mentioned the issue of whether attorneys' fees and costs are deducted from the insured's recovery for purposes of this rule, but the court's ultimate determination on the issue was unclear. *Plut v. Fireman's Fund Ins. Co.*, 85 Cal. App.4th 98 (Cal. App. 2000).

The impact of this decision, while ostensibly applying only to med-pay cases, is surely going to impact made whole decisions involving other lines of insurance, including health, property, etc. Assume that an insured recovers $6,000 in damages from a third-party tortfeasor and this amount reflects the insured's total personal injury losses caused by the tortfeasor. His insurer had previously paid him $2,000 for his covered medical expenses; thus the insured obtained a total of $8,000. The insured's attorney's fees and

costs to collect the $6,000 were $2,400. Under this new decision, the insurer is not entitled to reimbursement of any portion of the amount paid to the insured by the tortfeasor, because the insured has been made whole. This is because the insured's gross recovery ($6,000 plus $2,000 = $8,000) is more than the insured's total personal injury losses of $6,000, and thus any retention of the $2,000 (minus $800, which is the pro rata amount attributable to collecting damages for the covered injuries) would result in double recovery by the insured.

While the logic of such a decision is crystal clear – the insured contracted for his own attorney's fee and the insurer should not be saddled with the decision by the insured to give away one-third, 40%, or even greater amounts of his cause of action by engaging an attorney – many courts across the country still fall limp in deciding cases in which the "poor" insured is pitted against the monolithic insurance company with its endless supply of money. Few courts actually bother factoring in the societal and economic benefits of subrogation in helping to keep insurance premiums low for the insuring public. Our thanks to the 4th District California Court of Appeals for not letting passion overcome common sense legal analysis in arriving at their decision.

MADE WHOLE DOCTRINE

MWL TO DRAFT NASP AMICUS BRIEF IN LANDMARK MADE WHOLE CASE

Muller v. Society Insurance, 730 N.W.2d 668 (Wis. App. 2007), *review granted*.

Wisconsin is known as the "mother of all made whole states". This is because the first made whole decision in the country - *Garrity v. Rural Mutual Ins. Co.* - was decided in Wisconsin in 1977. On June 12, 2007, the Wisconsin Supreme Court granted review of a Wisconsin Court of Appeal's decision with far-reaching subrogation implications. Gary Wickert has been asked to draft an amicus curiae brief on behalf of the National Association of Subrogation Professionals ("NASP") in the appeal of *Muller v. Society Ins.*, 730 N.W.2d 668 (Wis. App. 2007), because states around the country look to Wisconsin law for guidance in crafting their own made whole law. *Muller* could be a turning point for subrogated carriers everywhere.

In *Muller*, a fire destroyed the Mullers' sporting goods store, and a third-party action was filed against an electrical contractor named Jerrick, who had liability insurance with limits of $1 million. The Mullers named their subrogated property insurer, Society Insurance Company, as a party defendant. Society paid $407,378.88 in benefits to the Mullers, and at mediation, tentatively settled directly with the third party for only $190,000, pending a determination of the Mullers' claims, and was not to be implemented until after the Mullers released their claims. The Mullers later settled for $120,000 for uninsured and other losses not covered by Society's settlement or Society's previous payment, and asked the trial court to declare that they were not "made whole". The court ruled that to the extent the payments from Society and the Mullers' settlement did not make them whole, the Mullers were entitled to recover the difference from Society's settlement. The Mullers and Society agreed that the Mullers' uninsured loss was $59,725.60, and Society appealed the trial court's ruling.

The issue to be addressed by the Supreme Court is whether a subrogated insurer is allowed to pursue its own subrogation claim and settle it for an amount it deems sufficient, when there is plenty of third party insurance and no limited funds over which the insurer and insured are competing? The Supreme Court could decide, as a few jurisdictions already have touched on, that an insured is made whole if there are plenty of third-party liability limits available to satisfy the claims of both the insurer and the insured. The Court of Appeals answered the above question in the affirmative. It decided that when a carrier settles its subrogation claim with the tortfeasor first and there are not limited third-party insurance limits over which the insured and insurer are competing, the insured cannot claim it was not made whole and recover part of the subrogated carrier's settlement proceeds. *Garrity* stands for the principle that if the insured is not made whole and it must compete with its insured for a limited partial payment, and the insured has been paid to assume the risk of loss, no subrogation should be allowed. However, if there are sufficient funds to cover the claimed losses, there is no issue regarding made whole. Here, there were more than enough

funds to cover all claims, and the Mullers did not provide an indemnification against Society's claims. The court rejected the Mullers' contentions that the funds available to settle their claims were limited, thereby preventing them from being made whole. The Mullers claimed that the amount a plaintiff has available to recover from is limited to how much a defendant is willing to pay to settle the claim – here, $310,000. The Court of Appeals rejected this because the plaintiffs offered no authority for this proposition.

The made whole doctrine applies only where there are limited third-party funds, creating a competition that prevented the insured from being made whole. Here, the $1 million policy was far more than necessary to cover all claims. While the court did not hold per se that policy limits are the measure of whether a fund is limited, they are certainly a significant factor in determining whether limited funds exist. The Mullers characterize Society's tentative settlement agreement as an "underhanded tactic", which inhibited their ability to settle their claims. The Court of Appeals could not understand how a tentative agreement, expressly contingent upon the insured resolving its claims, inhibits the insured's ability to be made whole. Unlike *Schulte*, the Mullers did not agree to indemnify Jerrick against Society in their agreement. After this decision, the illusory nature of such indemnification will become apparent, if that is all plaintiffs have to do to avoid a subrogation interest.

In summary, the Court of Appeals held that there is no limited fund situation which gives rise to made whole issues when there are sufficient funds to cover all the losses, there are no indemnification agreements, or there is an opportunity to recover from those funds. Through settlement, the Mullers made a conscious choice to settle for less than their limits. This choice cannot be tied to any limited funds. Had Society chose not to pursue its subrogation claim, the Mullers would not have been able to recover any more monies – because they have not established in the absence of subrogation the amount of Society's settlement that would have gone toward the satisfaction of their damages. The Court of Appeals believed that the Mullers should not be entitled to more money simply because Society pursued its subrogation interests. On June 12, 2007, the Wisconsin Supreme Court granted review of this decision. Their thinking on granting review is not readily apparent, but one thing is certain - the decision will have far-reaching ramifications for the subrogation industry and beyond. We will keep you posted on all developments with regard to the appeal and the amicus curiae brief.

KEYNOTE SPEECH AT EXECUSUMMIT:

WORKERS' COMPENSATION SUBROGATION IN THE NEW MILLENNIUM

Gary Wickert has agreed to be the keynote speaker at the upcoming Execusummit Conference on Workers' Compensation Subrogation Strategies in New York on August 8th and 9th, 2007, at the Club Quarters Downtown New York Hotel & Bull Run Conference Center. The subject will be "Workers' Compensation Subrogation In The New Millennium".

Workers' compensation subrogation isn't what it used to be. The news is both good and bad. Federal and state courts continue to throw obstacles in the way of legitimate subrogation claims and consistently seem to bend over backwards to strip carriers of recovery rights. Legislatures and lawmakers continue to chip away at subrogation rights - perhaps out of ignorance or lack of appreciation for the importance and societal value of subrogation in the workers' compensation setting. Handled correctly and with working knowledge of the issues, claims professionals can navigate subrogation minefields and maximize their recoveries. Despite the prejudice against and lack of understanding of the subrogated carrier's rights, the news is not all bad. There are new and exciting opportunities to assist carriers in increasing their recoveries and even pursuing some claims for attorneys' fees and costs in the process. 21st Century subrogation has seen some new and more liberal subrogation statutes evolve, and more national and global economy presenting new opportunities to apply extra-territorial subrogation principles and laws in states where recoveries would otherwise be limited or eliminated altogether. For information on the Execusummit Conference, please call (800) 905-9357 x 705, or send an e-mail to registration@execusummit.com.

NEW THIRD EDITION OF WORKERS' COMPENSATION SUBROGATION IN ALL 50 STATES RELEASED!

The much anticipated third edition of our workers' compensation subrogation book has just been released by the publisher. Attached is a brochure detailing much of what the new book has to offer. There have been many changes and additions, and the new edition is more than 1,300 pages long - an additional 300 pages over the previous edition.

The Third Edition of *Workers' Compensation Subrogation In All 50 States* is the most expansive and thorough edition yet. For the first time, the book includes the actual full text of the relevant workers' compensation statutes for all 50 states. A more comprehensive treatment of extra-territorial subrogation law and statutory employer/borrowed servant issues has been included in the new edition as well. A few states have completely revised and amended statutes dealing with workers' compensation subrogation, and a full treatment of all such new legislation, including pending legislation, has been included in the book. Finally, we have added hundreds of new state and federal decisions, both reported and unreported, making the third edition the ultimate resource and training tool for subrogation professionals with any responsibility for workers' compensation subrogation. To order your copy of the book, please call (800) 887-4064, or view the book online at http://www.jurispub.com.

THIRD EDITION WC BOOK BROCHURE

WELCOME TO THE FIRM ....

Matthiesen, Wickert & Lehrer, S.C. is proud to announce that Daniel Borck has joined the firm as an associate. Daniel graduated in 1996 from the University of Chicago with a Bachelor of Arts degree, with honors, in Public Policy Studies. He was on the Dean's List the 1994-1995 school year, Varsity Letterman with the University of Chicago Men's Baseball team from 1992 to 1996 and a volunteer for the Chicago Special Olympics in 1995 and 1996. Daniel earned his J.D. in 1999 from Marquette University Law School in Milwaukee. While attending Marquette, he was a teaching assistant for Legal Research and Writing I, II, III at a local Paralegal Training Program.

Before joining Matthiesen, Wickert & Lehrer, S.C., Daniel practiced for five and half years with the firm of Wagner, Falconer & Judd, Ltd. where he obtained extensive courtroom experience in areas including criminal defense, employment, landlord tenant, real estate, contract and family law. Daniel lives in Mukwonago, Wisconsin with his wife, Christine, and daughter, Katherine. We welcome this new addition to our firm, which continues to provide quality insurance litigation representation for clients in Wisconsin and throughout North America.
