MATTHIESEN, WICKERT & LEHRER, S.C.

A FULL SERVICE INSURANCE LAW FIRM

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MONTHLY ELECTRONIC SUBROGATION NEWSLETTER JUNE 2006

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

We are pleased to present our monthly electronic subrogation newsletter. This 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 subrogation developments and 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.

HEALTH INSURANCE

REIMBURSEMENT OF DEDUCTIBLES

In the world of subrogation, the issue of how much of an insured's deductible must be reimbursed to the insured after a carrier makes a successful subrogation recovery, remains a perplexing and confusing issue for subrogation professionals. It rivals ERISA preemption in health insurance subrogation and the no-fault laws of certain states as being the most confusing and least understood area of subrogation. Even experienced subrogation professionals and lawyers simply get it wrong when it comes to understanding and employing the law surrounding the obligation of a subrogated carrier to reimburse an insured a deductible. This article strives to shed some light on this confusing and often misinterpreted area of subrogation law.

Subrogation professionals often assume that if a state employs or recognizes the "made whole doctrine", then the insured must be totally reimbursed for its out-of-pocket deductible and any uninsured losses, before a carrier can subrogate. Unfortunately, this over simplistic view and application of the made whole doctrine is not only erroneous, but also results in reduced subrogation recoveries for carriers across the country. Surprisingly, the obligation of an insurer to reimburse some or all of its insured's deductible has very little to do with the made whole doctrine in most states.

The made whole doctrine generally provides that under the common law subrogation principle of equity, an insured is entitled to be "made whole" before a subrogated insurer can participate in a recovery from a tortfeasor. Ins. Co. of North America v. Lexow, 602 So.2d 528 (Fla. 1992). Insureds may argue that the made whole doctrine prevents an insurer from subrogating or recovering anything on its subrogated interest whenever the insured has not been fully reimbursed for its deductible. Unfortunately, although observed and recognized by a large number of subrogation professionals throughout our industry, this view is incorrect. Although the specific law involved may change from state to state, the general consensus is that the made whole doctrine does not give an insured an affirmative right or cause of action against its insurer to be "made whole", beyond the payment of the insurance policy proceeds involved. Schonau v. Geico General Ins. Co., 903 So.2d 285 (Fla. App. 2005). Rather, the made whole doctrine may be used only as

a defense by insureds to protect the insured's direct recovery from a tortfeasor, where the insured also lays claim to a limited amount of third party proceeds based on subrogation. Florida Farm Bureau Ins. Co. v. Martin, 377 So.2d 827 (Fla. 1979). Decisions from across the country applying the made whole doctrine essentially hold that where an insurer and insured simultaneously attempt to recover all of their damages from a tortfeasor who cannot (because of insolvency, limited insurance coverage, or other reasons) pay the full value of damages, the insured has priority of recovery over the insurer's subrogation interest. This is far different from an insured claiming it is entitled to 100% of its deductible before an insurer can subrogate on its own. Even the leading case in the country on the made whole doctrine involved a dispute over limited third party insurance proceeds between an insured and its insurer. Garrity v. Rural Mutual Ins. Co., 253 N.W.2d 512 (Wis. 1977). An insured always has the right to pursue a tortfeasor independently for its deductible, and that right alone is sufficient to allow the subrogee insurance company to keep its settlement, even if the insured is not made whole. Paulson v. Allstate Ins. Co., 665 N.W.2d 744 (Wis. 2003). Even one of the leading treatises on insurance, in its very first statement on the made whole rule, raises the threshold issue of insufficient funds: "In many instances, the insurer and insured both have rights of recovery against the third party primarily liable for the loss, if the amount recoverable from the third party is insufficient to completely satisfy the claims of both." *Couch on Insurance*, § 223.133, at 223-145 (3d Ed. 2000).

The **Utah** Court of Appeals recently decided a case in which an insurer reimbursed an insured its deductible, but not before reducing the deductible based on depreciation of property damage caused by a fire. Birch v. Fire Ins. Exchange, 2005 WL 2298130 (Utah App. Sept. 22, 2005). In that case, fire damaged the insured's property, and their insurance policy provided for full replacement costs, subject to a $500 deductible. The carrier subrogated against the tortfeasor, but was able to recover only the depreciated value of the property. It then reimbursed its insured its deductible, but first reduced it based on the depreciation of the property. The insured argued that the made whole rule should focus not on what he might legally have recovered from the tortfeasor, but rather on the total damages or loss he sustained. The court disagreed, and held that the reduction of the deductible was allowed because the maximum recoverable in the tort action was less than the replacement value insurance payment made by the insurer.

The **Florida** Court of Appeals astutely recognizes that a blanket application of the erroneous notion that an insured must recover its deductible first before a carrier will be allowed to recover dollar-one of any subrogation interest, will guarantee that insurance companies will simply readjust their premiums to pass on the added cost to consumers. Monte de Oca v. State Farm, 2004 WL 2955008 (Fla. App. 2004). It held that a 50% reimbursement of a deductible where the plaintiff was 50% at fault, was perfectly equitable. What's more, a third party tortfeasor lacks any standing to complain that an insurance company cannot subrogate until its insured has been totally reimbursed its deductible or otherwise "made whole". Nationwide Property & Casualty Ins. Co. v. DPF Architects, 792 So.2d 369 (Ala. 2000). Unless the insureds have intervened into the action to claim a right of recovery which would otherwise be prohibited due to lack of third party proceeds or insurance coverage, a carrier is allowed to subrogate, notwithstanding the fact that the insured has not been made whole by complete reimbursement of its deductible. The only party withstanding to object to the insurer's lack of reimbursement of 100% of a deductible is the insured - and even then, it should only be able to complain when the insured is making an affirmative claim and third party proceeds are insufficient to satisfy both the insured's uninsured loss and the carrier's subrogation interest. Economy Fire & Casualty Co. v. Goar, 564 So.2d 867 (Ala. 1990).

It should be clear then, that the so-called "dollar-one states" are a misnomer, and have little application to whether and to what extent a deductible must be reimbursed to an insured. The term simply refers to whether or not a state recognizes and applies the made whole doctrine as described above. But if the made whole doctrine doesn't give the insurance industry guidance as to when and under what circumstances a deductible must be reimbursed, in whole or in part, what does? The answer, where it has been declared, is usually derived from the specific insurance regulations and administrative codes of each particular state.

Twenty-two states contain specific regulations or administrative codes which specifically and, in detail, govern when and under what circumstances an insured's deductible should be reimbursed by a subrogating insurer. For example, in **Texas**, the Texas Insurance Code § 542.204 specifically requires an insurer to "take action" to recover a deductible within one year from the date a claim is paid or ninety days before the statute of limitations runs - whichever is sooner. If it does not, the law requires an insurer to pay a deductible back to its insured. However, this burden does not apply if an insured is notified that no subrogation will be pursued and the insured is authorized to proceed on his own to recover any losses it deems it has suffered. However, this code section applies only to private passenger automobile policies. No other applicable statute, administrative code provision or case law gives us guidance for matters involving fire and casualty, property, or health insurance subrogation. However, the Texas Department of Insurance indicates that the reimbursement of the insurance deductible in a third party claim is usually dictated by the level of recovery - usually a pro-rata reimbursement based on the percentage of recovery. However, the Department warns that a carrier must be consistent on its deductible reimbursement policy.

California law requires that every insurer that makes a subrogation demand must include in every such demand the insured's deductible. 10 CA A.D.C. § 2695.7. Insurers must share subrogation recoveries on a pro-rata basis in order to reimburse a pro-rata share of their insureds' deductibles. A pro-rata share of legal expenses and fees may be deducted on a pro-rata basis, if actually incurred. **Iowa** law requires that an insurer shall, upon the insured's request, include the insured's deductible in any subrogation demand. Iowa A.D.C. 191-15.43 (507B). Any subrogation recoveries will be shared on a pro-rata basis with the insured unless the deductible amount has otherwise been recovered. **New York** law requires an insurer which has made a physical damage third party subrogation recovery to mail or hand deliver to the insured a pro-rata share of the insured's deductible, within thirty days after such recovery. N.Y. Ins. Reg. 64, § 216.7(g)(1). **Wyoming**, on the other hand, has enacted a specific statute which requires that an insurer reimburse its insured its deductible, in full, before any part of the recovery is applied to any other use. Wy. Stat. § 26-13-113. If the deductible exceeds the recovery made by the insurer, the entire recovery must be paid to the insured.

And so it goes that twenty-two states have enacted insurance regulations or statutes specifically governing the duties of a subrogated carrier in subrogation settings. Of the other twenty-eight states, twenty-one have no applicable statute, provision, or case law. In light of the fact that most of the states which have enacted regulations appear to apply a pro-rata reimbursement philosophy, an advisable policy with regard to reimbursement of deductibles in states which have not made any pronouncement, is to follow the pro-rata reimbursement formula.

Seven states have specific case law which governs procedure in these situations. **North Carolina** requires an insurer to pay the deductible first out of any subrogation recovery absent some alternate agreement. St. Paul Fire & Marine v. Rhodes, 198 S.E.2d 482 (N.C. 1973). The **South Dakota** Supreme Court has held that an insured can collect even if its insured has not been made whole by reimbursement of a deductible. Julson v. Federated Mutual Ins. Co., 562 N.W.2d 117 (S.D. 1997). **Washington** follows the blanket rule that an insured must made whole before an insurer can collect any excess, and the Department of Insurance advises that it relies on this case law to establish that a deductible must be reimbursed in full before a carrier can collect. Theringer v. American Motors Ins., 855 P.2d 191 (Wash. 1978). **Alabama** has left the entire issue to be governed by the terms of the insurance policy. Ex Parte State Farm & Casualty Co., 764 So.2d 543 (Ala. 2000).

It is possible that the twenty-one undecided states may fall in line at some point on either side of the fence - either requiring a deductible to be reimbursed in full before any subrogation recovery can be had or allowing a carrier to subrogate either without regard to reimbursement of the deductible or after reimbursement of a pro-rata share of the deductible. A summary chart of the deductible reimbursement laws of all fifty states can be found at the website of Matthiesen, Wickert & Lehrer at www.mwl-law.com. Please direct any questions you may have with regard to this fifty state chart to its chief architect, Elizabeth Co at eco@mwl-law.com.

WORKERS' COMPENSATION

FAILURE TO FILE FLORIDA "NOTICE OF PAYMENT" OF WORKERS' COMPENSATION BENEFITS WAIVES SUBROGATION RIGHTS

Workers' compensation subrogation in Florida is a little peculiar. Although the statute indicates that a worker's compensation carrier which has paid benefits to an injured worker "is subrogated to the employee's rights against the third party", a carrier is not allowed to intervene into a pending third party filed by an injured worker. F.S.A. § 440.39. Instead, a carrier must file a "Notice of Payment of Compensation and Medical Benefits" ("Notice of Lien"), which will then constitute a lien upon any judgment or settlement recovered, to the extent that the court determines its pro-rata share of compensation and medical benefits paid or to be paid under the workers' compensation law. If a worker fails to bring a third party action within one year, the carrier may bring the third party action on its own after giving thirty days notice to the injured employee. The majority of the time, however, the worker files the third party action, and the worker's compensation carrier is left to take action to protect its worker's compensation lien.

In Summit Claims Management, Inc. v. Lawyers Express Trucking, Inc., 913 So.2d 1182 (Fla. App. 2005), the Florida Court of Appeals has made subrogation rights of workers' compensation carriers more hazardous in Florida. Although § 440.39 places no time limitation on the filing of a "Notice of Lien", the Court of Appeals has held that a "reasonable interpretation" of the statute is that such notice must be filed before any settlement or judgment is recovered. In *Summit Claims Management,* the Court of Appeals held that to interpret the statute any other way would lead to the inequitable result wherein parties could reach a settlement that did not include the amount later sought to be asserted as a lien. Making no exceptions for situations in which the injured worker and other parties have actual notice or knowledge of a workers' compensation lien, the Court of Appeals has held that if a workers' compensation carrier fails to file a "Notice of Payment" in a third party action prior to settlement of the worker's action, the carrier is not entitled to recover its worker's compensation lien.

In *Summit Claims Management*, the injured worker had failed to provide the carrier with notice of a third party action, yet it was shown that the carrier had actual knowledge of the third party suit. The court held that the carrier, which failed to file a "Notice of Payment", was barred from recovering its subrogation interests because it failed to file the notice. This ruling opens the door for gerrymandering and litigation sleight-up-hand maneuvers by plaintiffs' counsel who will realize that if they quickly settle a third party action and argue that the worker's compensation carrier had "actual knowledge" of the action, they may be able to settle the suit without having to repay the worker's compensation carrier a substantial worker's compensation lien. Workers may also attempt to give notice to a carrier and then promptly settle the suit thereafter, without giving the carrier a chance to file its "Notice of Payment". Care should be taken to promptly file the appropriate notices and actively protect a worker's compensation carrier's lien in the State of Florida, so as to avoid the harsh result of this decision. For information about aggressive subrogation in Florida, contact Gary Wickert at gwickert@mwl-law.com.

COURT REPORTING

COURT REPORTERS STRIKE BACK: Many States Banning Insurance Company Requirements To Use Specific Court Reporters

Insurance companies draft them and impose them on defense and subrogation counsel because they are trying to get a handle on and contain spiraling litigation costs. Lawyers accept and adhere to them because they are a significant condition to receiving file assignments and litigation work from their insurance company clients. Court reporting firms loathe them, unless they happen to be the court reporting firm that wins a large insurance company's lottery to be placed on its litigation management guidelines as the "official court reporting firm." We are talking about contracts entered into between insurance companies and court reporting firms to provide exclusive court reporting services for an insurance company's litigation

needs over a specific period of time. We are also talking about litigation management guidelines imposed on subrogation and defense counsel by insurance companies, requiring the attorneys to use certain vendors or litigation services, including court reporters, as a condition precedent to receiving litigation files from that insurance company. Court reporters who have been shut out of the process are beginning to strike back, and recent developments have changed the landscape of this select contracting process, at least in certain states. More and more states are passing anti-contracting legislation, prohibiting the use of court reporters pursuant to such exclusive contracts. The trend is sure to continue.

In November of 1997, forty-two court reporters from twenty-four different states met in Chicago to address concerns felt nationwide about the erosion of impartiality in the American legal system which had manifested itself in contracts between insurance companies and court reporters requiring only specific court reporters to handle all litigation for that insurance company. Citizens for Impartial Justice (CIJ) was later incorporated and joined forces with the National Court Reporter's Association (NCRA), to lobby legislators and government officials about abusive practices which they felt threatened the right of the public to receive fair and impartial justice within the civil justice system. These efforts have begun to bear fruit. On April 12, 2004, **Wisconsin** became the 29th state to prohibit or limit such contracts for deposition services. Governor Doyle signed legislation which amended § 804.03 of the Wisconsin Statutes to include the following language:

> *"No deposition may be taken before a person who has entered into a contract for court reporting services unless the contract is limited to a particular action or incident."* Wis. Stat. § 804.03(3) (2004).

The Wisconsin legislature had considered such anti-contracting proposals many times before it finally decided that it was a significant step to maintaining the impartiality of court reporters.

New Jersey has also entered into the fray, and its attorney general has upheld that state's anti-contracting law, advising court reporters that they would be subject to discipline if they entered into such contracts with insurance companies. The attorney general opined that such contracts do affect the impartiality of court reporters, whose bread and butter comes continually and almost exclusively from one particular party to the litigation. N.J. Admin. Code § 13:43-5.4. The attorney general, in issuing his opinion, used a 2002 State Farm Insurance Company pricing offer that was distributed to court reporters as an example of such third party contracting practices which would, in the attorney general's opinion, affect the impartiality of court reporters. The attorney general's opinion stated:

> *"Exclusive contracting agreements between court reporters and large insurance companies, which are parties to a civil action, bring into question the impartiality of reporters, the cornerstone of the reporting profession."*

With more than 150 insurance company and/or insurance industry clients, we have taken thousands of depositions using court reporters selected pursuant to such contract requirements. We must say that, in our many years of practice, we have never suspected that any of the court reporters we have used were anything other than partial and unbiased. Unfortunately, the industry will have to play with the hand that it has now been dealt.

Over half of the states in the country now have anti-contracting rules, legislation, or attorney general opinions on their books. The following is a state-by-state synopsis of the current status of such anti-contracting laws:

Alabama	No contracting legislation/rules in place.
Alaska	No contracting legislation/rules in place.
Arizona	Anti-contracting rules in place.
Arkansas	Anti-contracting rules in place.
California	Anti-contracting legislation in place.
Colorado	No contracting legislation/rules in place.
Connecticut	Anti-contracting rules in place.

District of Columbia	No contracting legislation/rules in place.
Delaware	Anti-contracting rules in place.
Florida	No contracting legislation/rules in place.
Georgia	Legislation prohibiting contracting in place.
Hawai'i	Legislation prohibiting contracting in place.
Idaho	No contracting legislation/rules in place.
Illinois	Anti-contracting rules in place.
Indiana	Legislation prohibiting contracting in place.
Iowa	Legislation prohibiting contracting in place.
Kansas	No contracting legislation/rules in place.
Kentucky	Legislation prohibiting contracting in place.
Louisiana	Legislation prohibiting contracting in place.
Maine	No contracting legislation/rules in place.
Maryland	No contracting legislation/rules in place.
Massachusetts	Contracting legislation in place.
Michigan	Legislation prohibiting contracting in place.
Minnesota	No CSR, contracting legislation/rules in place.
Mississippi	No contracting legislation/rules in place.
Missouri	No contracting legislation/rules in place.
Montana	No contracting legislation/rules in place.
Nebraska	No contracting legislation/rules in place.
Nevada	Rules prohibiting contracting in place.
New Hampshire	Anti-contracting legislation in place.
New Jersey	Contracting rules in place.
New Mexico	Rules prohibiting contracting in place.
New York	No contracting legislation/rules in place.
North Carolina	Contracting rules in place.
North Dakota	No contracting legislation/rules in place.
Ohio	Contracting legislation in place.
Oklahoma	Contracting legislation in place.
Oregon	Contracting legislation.
Pennsylvania	No contracting legislation/rules in place.
Rhode Island	No contracting legislation/rules in place.
South Carolina	No contracting legislation/rules in place.
South Dakota	No contracting legislation/rules in place.
Tennessee	Contracting legislation in place.
Texas	Legislation prohibiting contracting in place.
Utah	Legislation prohibiting contracting in place.
Vermont	No contracting legislation/rules in place.
Virginia	No contracting legislation/rules in place.
Washington	Mandatory CSR, no contracting legislation/rules in place.
West Virginia	Legislation prohibited contracting in place.
Wisconsin	Anti-contracting statute in place. Wis. Stat. § 804.03(3).
Wyoming	No contracting legislation/rules in place.

Above information was obtained from CIJ website at http://www.cijonline.org/legislation.htm.

Unfortunately, this appears to be a slippery slope. If we are to assume impropriety and the potential partiality of court reporters simply because they have contracted with an insurance company, it seems that we would also have to question law firms who use court reporting firms owned by firm or lawyers within that firm - a growing practice in states like **Texas**. While many lay persons are mystified at the high cost of simply transcribing words spoken in a deposition, arbitration, or hearing, especially in this age of technology, they must also realize and acknowledge that the fate of a particular law suit or claim may hinge on the disposition of one syllable, one word, even one letter.

For the last decade, we have been telling friends and relatives who have sought our counsel with regard to a potential future career in certified shorthand reporting, that technology which would eclipse this ostensibly archaic method of transcribing testimony and events, were imminent. We have been wrong. Until a more reliable and trustworthy form of recording such testimony is sound, developed, and proven, certified shorthand reporting remains the most reliable method of capturing and integrating the spoken word into a comprehensive and accurate information base for the benefit of the public and private sectors. With a tough regimen of ethical standards, testing and certification, educational opportunities, communications, and government relations, certifying shorthand reporting remains the only game in town.

Legislation and government actions prohibiting or limiting contracting practices, such as have now been prohibited in more than half of all states are certain to grow. The insurance industry and the legal profession will all have to grow with it.
