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MONTHLY ELECTRONIC SUBROGATION NEWSLETTER SEPTEMBER 2006

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.

PROPERTY SUBROGATION

DUPLEX: SUBROGATING LANDLORD/TENANT PROPERTY LOSSES

By Gary L. Wickert

In the 2003 Miramax comedy *Duplex*, Ben Stiller and Drew Barrymore are Brooklyn landlords to a pesky, rent-controlled tenant named Mrs. Connelly, played by Eileen Essell. Efforts to get rid of Connelly fail and the tenant's careless actions cause a fire which nearly destroys the entire building. The fact that Ben Stiller's fire insurer had to pay for the property damage was a tedious and mundane fact not mentioned in the movie. If art truly imitated life, the movie would have divulged the fact that under New York law, the fire insurance company paying the damages had a subrogated cause of action against the tenant for recovery of the damages it had to pay for. Surprisingly, however, the insurer would have no subrogation rights if the movie were set a few miles north in Connecticut, or in a number of other states where such a subrogation action against the tenant is prohibited. Understanding when, where, and why such subrogation actions by a landlord's insurer against a tenant are permitted or prohibited is critical to maximizing property subrogation recoveries and is, conveniently, the focus of this article.

Unlike New York, many states follow something known as the *Sutton Doctrine*, whereby, absent an agreement to the contrary, a tenant is considered to be a co-insured of the landlord with respect to fire damage to leased residential premises, and, therefore, the landlord's insurer who pays for the damages caused by the negligence of the tenant may not sue the tenant in subrogation because it would be tantamount to suing its own insured. The "*Sutton Doctrine*" originated with the Oklahoma Court of Appeals decision of Sutton v. Jondahl, 532 P.2d 478 (Okla. App. 1975). It is a doctrine decided on "basic equity and fundamental justice" (dangerous words for subrogation professionals) rather than on specific language contained in a lease agreement. Under this doctrine, unless the terms of the lease itself establish a tenant's liability for loss from a negligently started fire, the landlord's insurance is deemed liable for the mutual benefit of both

landlord and tenant. Allstate Ins. Co. v. Watson, 2005 WL 457846 (Tenn. App. 2005); Tri-Par Invs. v. Sousa, 680 N.W.2d 190 (Neb. 2004); DiLullo v. Joseph, 259 Conn. 847, 853, 792 A.2d 819, 822 (Conn. 2002); Lexington Ins. Co. v. Raboin, 712 A.2d 1011, 1016-1017, *aff'd* 723 A.2d 397 (Del. Super. 1998); GNS Partnership v. Fullmer, 873 P.2d 1157, 1163-1164 (Utah App. 1994); Community Credit Union of New Rockford, N.D. v. Homelvig, 487 N.W.2d 602, 605 (N.D. 1992); Cascade Trailer Ct. v. Beeson, 50 Wash. App. 678, 687-688, 749 P.2d 761, 766 (Wash. App. 1998), *review denied* 110 Wash.2d 1030; New Hampshire Ins. Group v. Labombard, 155 Mich. App. 369, 376-377, 399 N.W.2d 527, 531 (Mich. App. 1986); Alaska Ins. Co. v. RCA Alaska Communications, 623 P.2d 1216, 1218 (Alaska 1981). Seeming more like our U.S. Supreme Court waffling over interpretation of the Constitution than a state court of appeals deciding a subrogation issue, the court in *Sutton* announced that the principle of subrogation is a "fluid concept" depending upon the particular facts and circumstances of a given case for its applicability, and is not a rigid rule of law. The "*Sutton*" principle is derived from recognition of a relational reality, namely, that both landlord and tenant have an insurable interest in the rented premises - the former owns the fee and the latter has a possessory interest. As the theory goes, it is considered a matter of sound business practice that the fire insurance premium paid has to be considered in establishing the rent rate on the rental unit. Such premium was chargeable against the rent as an overhead or operating expense, and therefore, the tenant actually paid the premium as part of the monthly rental. The court in *Sutton* went on to say that:

> *"Prospective tenants ordinarily rely upon the owner of the dwelling to provide fire protection for the realty (as distinguished from personal property) absent an express agreement otherwise. Certainly it would not likely occur to a reasonably prudent tenant that the premises were without fire insurance protection or if there was such protection it did not inure to his benefit and that he would need to take out another fire policy to protect himself from any loss during his occupancy. Perhaps this comes about because the companies themselves have accepted coverage of a tenant as a natural thing. Otherwise their insurance salesmen would have long ago made such need a matter of common knowledge by promoting the sale to tenants of a second fire insurance policy to cover the real estate."* Sutton, 532 P.2d at 482.

Subrogation, however, aims to place the ultimate burden for the loss on the wrongdoer, and prevents a double recovery to the insured. Some states have rejected the *Sutton Doctrine* and instead have gone with the more logical approach that there must be a "clear and unequivocal expression exonerating the tenant from liability from negligent conduct" before the tenant gets a free ride. Britton v. Wooten, 817 S.W.2d 443, 447 (Ky. 1991); New Hampshire Ins. Co. v. Hewins, 6 Kan.App.2d 259, 260, 261-262, 627 P.2d 1159, 1161 (Kan. App. 1981); Sears, Roebuck & Co. v. Poling, 248 Iowa 582, 588-589, 81 N.W.2d 462, 465-466 (Iowa 1957). The Supreme Court of Iowa has held that the landlord and tenant have "separate estates capable of being separately valued and separately insured." Neubauer v. Hostetter, 485 N.W.2d 87 (Iowa 1992). The Supreme Court of Arkansas has said that:

> *"the fiction that by paying the rent, the lessee paid the insurance premium is not appropriate…such a fiction ignores the fact that more often than not the market, i.e., supply and demand, is the controlling factor in fixing and negotiating rents."* Page v. Scott, 567 S.W.2d 101 (Ark. 1978).

The court also noted that if there had been no insurance, the landlord's right to recover against the tenant would have been beyond question. It also rejected the argument that recovery by the insurer from the tenant would result in a windfall to the insurer, as this not only ignores the principles and purposes of subrogation, but the same could be said for a subrogation action against an independent third party, such as the manufacturer of a defective coffee maker. Id. at 103. Just to the south of Brooklyn, New Jersey has said that it finds no binding case law or reason in common sense that would hold that where the landlord would have had a claim against a tenant, the existence of insurance obtained by the landlord, paid for by the landlord from the landlord's own unrestricted funds, and for the benefit of the landlord, should exculpate the tenant from the consequence of negligent conduct – absent an express agreement to that effect. Zoppi v. Traurig, 598 A.2d 19 (N.J. Super. 1990).

Subrogation professionals should therefore be mindful that the application of the *Sutton Doctrine* is only the beginning in investigating whether a tenant may be pursued for subrogation. Exculpatory clauses and mutual releases contained in lease agreements may well devastate an insurer's subrogation rights above and beyond any right to pursue a tenant based on the application of this doctrine. However, whether or not a tenant is deemed to be a "co-insured" under the landlord's fire insurance policy is still an important first step in determining whether subrogation rights exist.

There are conflicting policy arguments on both sides of the *Sutton Doctrine* issue. The 9th Circuit Court of Appeals has indicated that in order to determine whether the tenant should be considered a co-insured, courts need to look at whether the insurance policy was obtained for the benefit of the tenant as well as the landlord. Aetna Ins. Co. v. Craftwall of Idaho, 757 F.2d 1030 (9th Cir. 1985). Once the landlord has agreed to carry insurance for the benefit of both parties, the subrogated insurer may not sue the tenant for fire damage resulting from the tenant's negligence. Page v. Scott, 567 S.W.2d 101, 103 (Ark. 1978); West American Ins. Co. v. Pic Way Shoes of Central Michigan, Inc., 313 N.W.2d 187, 188 (Mich. App. 1981), *citing* Woodruff v. Wilson Oil Co., 382 N.E.2d 1009 (Ind. App. 1978); Pendlebury v. Western Casualty & Surety Co., 406 P.2d 129, 136 (Idaho 1965) (insurer barred from subrogation action against own insured). Obviously, this begs the question of whether the landlord also obtained fire insurance for the benefit of the tenant. It is important to look at the lease agreement to find out what was the intent of the parties. Even if the parties merely discussed insurance generally, without specific reference to fire insurance, fire insurance should be presumed to be covered by the agreement. Evans v. Sack, 67 N.E.2d 758, 760 (Mass. 1946); 49 *Am.Jur.2d*, Landlord and Tenant § 272 at 287 (1970); 51C *Corpus Juris Secundum*, Landlord and Tenant § 374 at 1000 n. 68 (1968). The states are deeply divided on the issue.

When applied to commercial lease settings, if the tenant was shielded from a subrogation suit, the commercial tenant's own liability insurer would also acquire a windfall, since it first receives a premium to insure the tenant for his own negligent acts, but then escapes having to pay for an anticipatable fire loss. In addition, the collateral source rule would be undermined if the court released the tenant essentially because the landlord had insurance. More importantly, if the tenant is deemed to be a co-insured without any such intent expressed in the lease contract between the parties, the court would be rewriting the landlord's fire insurance contract, which unambiguously provides that the landlord alone has been insured.

While the laws of the various states differ when it comes to whether the *Sutton Rule* is or isn't applied as a blanket rule, the question arises as to whether the lease sufficiently indicates the intent of the parties was that the fire insurance obtained by the landlord is for their mutual benefit, when the lease terms merely state that "the Landlord will obtain fire insurance." Some jurisdictions feel that the mere obligation for the landlord to obtain fire insurance, is sufficient to indicate that the insurance is for the mutual benefit of the landlord and the tenant. Waterway Terminals v. P.S. Lord, 406 P.2d 556 (Or. 1965) (However, note that in this case the lease also contained an exculpatory clause which would have been neutered if the subrogation suit was allowed to proceed). The logic used is that the tenant would not have negotiated for the requirement that the landlord obtain fire insurance if it didn't benefit him at all. Many states have taken a more relaxed, case by case approach, holding that a tenant's liability to the landlord's subrogating insurer for negligently causing a fire depends on the intent and reasonable expectations of the parties to the lease as ascertained from the lease as a whole. General Accident Fire & Life Assurance Corp. v. Traders Furniture Co., 401 P.2d 157 (Ariz. App. 1981); Page v. Scott, 567 S.W.2d 101, 103 (Ark. 1978); Fire Ins. Exch. v. Hammond, 83 Cal. App.4th 313, 99 Cal. Rptr.2d 596, 602 (2000); Koch v. Spann, 92 P.3d 146 (Or. App. 2004).

The ability to subrogate effectively and negotiate successfully in landlord/tenant situations depends on a subrogation professional's familiarity with the laws of the particular jurisdiction involved. A chart depicting the property subrogation laws of all 50 states with respect to landlord/tenant subrogation settings can be found on our website at http://www.mwl-law.com. The link to the Landlord/Tenant Subrogation Chart can be found on our home page along with other charts, including: Statutes of Limitations for All 50 States, Contributory Negligence/Comparative Fault Chart for All 50 States, 50 State Deductible Reimbursement Chart, and many others.

AUTOMOBILE SUBROGATION

CHONG V. STATE FARM, 428 F.Supp.2d 1136 (S.D. Cal. 2006)
Assault On Subrogation Continues

A California class action lawsuit was recently filed against State Farm Mutual Automobile Insurance Company, which could have dire ramifications for carriers subrogating for medical payments in automobile policies, and other non-workers' compensation subrogation interests. Kathleen Chong was involved in an automobile accident, and recovered first party med pay benefits in the amount of $5,000 from State Farm. Chong then filed suit against the third party and State Farm, with full knowledge of the lawsuit, sat back and didn't engage subrogation counsel or otherwise assists in the lawsuit. Chong spent $28,000 in litigation costs and settled the case for $65,000. Only then did State Farm step in and demand reimbursement of the $5,000 it had paid. Chong responded by filing a class action suit against State Farm, claiming that it acted improperly because "her net recovery after taking into account her attorney's fees and costs were far below the amount she needed to make her whole."

State Farm filed a motion to dismiss, arguing that California had not adopted a "blanket make whole rule", and that no California case had ever held that an insured's payment of attorney's fees meant that the insured was not made whole. On April 7, 2006, the District Court disagreed, holding that:

> *"Under California's common law make whole rule, a carrier that has knowledge of a policyholder's tort action and decides not to participate in it may not seek reimbursement from the successful policyholder unless the policyholder's tort recovery exceeds his actual loss. California courts have held that this means a policyholder must only reimburse the nonparticipating carrier for the surplus, if any, remaining after the policyholder satisfies 'his loss in full and his reasonable expenses incurred in the recovery.' 'Thus, when an insurer elects not to participate in the insured's action against a tortfeasor, the insurer is entitled to subrogation only after the insured has recouped his loss and some or all of his litigation expenses incurred in the action against the tortfeasor.' This rule applies regardless of whether the carrier's asserted subrogation right is equitable or contractual."*

California, therefore, joins the minority of cases which follow the illogical rule that the insured's attorney's fees and costs must be taken into account when determining whether the insured has been made whole. The federal district court did, however, remind us that in California, parties can contract around the made whole doctrine. For smaller subrogation interests, however, it is now incumbent upon health insurers to engage subrogation counsel, or face the possibility that their entire lien will be disallowed. While ERISA-covered health plans and workers' compensation subrogation claims are probably exempt from the scope of this overreaching decision, most other lines of insurance subrogation will be directly affected.

This decision is insidious not just because it upholds the made whole doctrine, and not because it requires a carrier to engage subrogation counsel who will need to walk the tight rope between being so active as to be cost-ineffective and not being active enough. The decision is questionable because it literally makes it impossible for an insured to ever be made whole. Unless an insured does not hire a lawyer and incurs no costs, there is no chance that he can be made whole – unless we assume that liability insurance companies will be paying out significantly more than the damages sustained by the insured. The only silver lining of this case is the fact that the court left intact the ability of the insured and the insurer to contract around the made whole doctrine in the terms of the policy or otherwise.

Anyone who has litigated the made whole issue in Georgia knows the feeling. If there is one iota of damages for which the insured is not recompensed – subrogation is denied. It is a harsh rule and one which overlooks or discounts entirely the very purpose of subrogation in the first place. One of the chief purposes of subrogation is to place the loss ultimately on the wrongdoer or tortfeasor who caused the loss in the first place. Courts have stressed that one goal of subrogation is to place the burden for a loss on the party ultimately liable or responsible for it and by whom it should have been discharged, and to relieve entirely the insurer or surety who indemnified the loss and who in equity was not primarily liable for the loss. Fireman's Fund Ins. Co. v. Maryland Cas. Co., 65 Cal. App.4th 1279, 1296, 77 Cal. Rptr.2d 296 (1998). An additional purpose which underlies the doctrine of subrogation is that it prevents the policyholder from receiving more than he or she bargained for from the contract of insurance. In essence, this prevents a "double recovery" by the insured. Commentators in the field have suggested that if the insurer has only contracted to indemnify the insured for losses incurred, denying the insurer subrogation rights in effect rewrites the policy and allows the insured to retain benefits not contracted for. Kimball & Davis, *The Extension of Insurance Subrogation*, 60 Mich. L. Rev. 841, 841-42 (1962). Another key function of the subrogation doctrine is that it returns the excess, duplicative proceeds to the insurer

who can then recycle them in the form of lower insurance premiums. Fleming, John G., *The Collateral Source Rule and Loss Allocation in Tort Law*, 54 Cal. L. Rev. 1478, 1481-84 (1966). In short, subrogation is a key mechanism by which insurance premiums are kept in check and held to a minimum.

Insurance is a plan of risk management or risk sharing. Lynch, Margaret E., *The Business of Insurance*, at 7 (5th ed. Rev. 1993). F. Joseph DuBray points out in an excellent article on the benefits of subrogation that for a certain price or "premium", a person or entity is offered an opportunity to share the costs of a defined possible economic loss or risk. DuBray, Joseph F., *A Response To The Anti-Subrogation Argument: What Really Emerged From Pandora's Box*, 41 S.D. L. Rev. 264 (1996). This risk sharing is normally done by an insurance company or health plan, although persons may choose to self-insure or spread the effects of a risk through group plans. Since the risk or loss covered by the insurance is in the future, the exact risk or loss is not known when the insurance contractor or policy is issued. Id. All who are sharing the risk – insurer and insured – view the risk as the probable amount of loss, and the amount of coverage and the premium for the insurance actually purchased are calculated on this unknown. Id at 271.

Correct measurement and assessment of the loss potential is the very foundation of any system of insurance. This assessment is accomplished only through the careful analysis or prior experience with loss, costs of administration of the insurance, the application of probability, or the mathematics of chance, as well as the likelihood that any loss will be recouped through the vehicle of subrogation. The insured decides, before he pays the premium, how much of the potential loss he wishes to bear, when he decides on the limits of coverage desired and whether he wishes to purchase a contract of insurance that provides for subrogation.

Any negative financial implications of subrogation for the insured can be avoided by specifically requesting a policy without a subrogation or reimbursement clause. If subrogation recovery were not available for insurance companies – as is increasingly becoming the case in some states – the actual cost of insuring the past known risk would increase accordingly and the projected future costs would likewise have to be adjusted upward in the form of increased premiums. Id at 273. Subrogation costs not realized, or eliminated due to the erroneous application of equitable doctrines such as the made whole or common fund, are reflected in and spread over future premiums among the issuing insurer and all of the insureds purchasing the same insurance. As a result, all who shared the risk during the time the claim was paid, and all who share the future risk, subsidize the reduction or elimination of subrogation recoveries or the payment to an insured that did not honor his or her subrogation agreement. Id.

Many judges, attorneys, and lay persons – including jurors sitting on subrogation cases – do not understand subrogation. They cannot understand or comprehend why a wealthy insurance company, having accepted "confiscatory" premiums from an insured and thereafter paid a loss suffered by the insured, should be able to recover the losses it has paid from a culpable third party – sometimes to the detriment of the insured. They rationalize that paying the loss is simply what the insurance company contracted to do in exchange for the insurance premiums it received. Many judges and appellate courts around the country have undertaken an anti-subrogation jihad, attacking subrogation as "harsh" and "unfair", erroneously applying equitable defenses to contractual subrogation. Several states have enacted anti-subrogation statutes, with the logic that if anybody should suffer it should be the large insurance company or wealthy health plan which

has accepted premiums for years without paying a claim. However, the notion that a successfully subrogating insurance company is granted a "windfall" is simply not true.

Because any risk insured against is in the future and the actual risk is unknown, the actual costs of administering the risk are likewise unknown, and the premium paid toward these uncertain events represents a payment to address probable, not actual, expense amounts. DuBray, Joseph F., *A Response To The Anti-Subrogation Argument: What Really Emerged From Pandora's Box*, 41 S.D. L. Rev. 264 at 273 (1996). DuBray points out that because of these "unknowns", there is no known "margin" between the risks or losses that have been insured against and the premiums that have been collected to address the actual costs of paying the loss to come. Because there is no known "margin", there are no "windfalls" in the calculations, as has been suggested by opponents of subrogation. Lynch, Margaret E., *The Business of Insurance* at 7 (5th ed. Rev. 1993).

DuBray points out that revenue gained by the insurer, whether through subrogation collection, premium collection, or otherwise, is applied toward responding to the actual risk that is required to be paid by the insurer under the terms of the contract or policy. DuBray, Joseph F., *A Response To The Anti-Subrogation Argument: What Really Emerged From Pandora's Box*, 41 S.D. L. Rev. 264 at 273 (1996). Only experience will reveal whether the premiums collected, subrogation recovered, and revenue from other sources, will prove sufficient to cover the actual risks and expenses. DuBray notes that "as a source of revenue, subrogation operates to reduce the actual past cost total used in the calculation of probable future insurance risk or loss on which future premiums will be based." Id. Therefore, subrogation does figure into the insurance experience calculation as "revenue", not a "windfall", as suggested by anti-subrogation proponents. Independent recognition of subrogation as an appropriate and generally accepted source of revenue for an insurance carrier is even codified in the insurance laws and regulations of some states. S.D.C.L. § 58-29C-26 (specifying sources for the South Dakota Life and Health Insurance Guaranty Association to look to in addition to contributions from member insurers to ensure sufficient funds for operation - including "subrogation gains").

The biggest assault on subrogation has come in the form of the "made whole doctrine". Yet, the entire made whole argument flies in the face of existing subrogation law. For example, in many states, if an insured recovers from a collateral source, the liability of the insurer under a contract of indemnity is reduced to the extent of such collateral recovery. Hart v. State Farm Mutual Automobile Ins. Co., 248 N.W.2d 881 (S.D. 1976). Also, if an insured impairs an insurer's subrogation rights, the insured may be barred from recovery under the insurance contract for the loss sustained. These results are incongruous with the argument that an insured should be able to disregard an insurer's subrogation rights because the insured was not made whole. As is noted by one court, "It is a fact of life that there are many occasions where the injuries and damages exceed the coverage afforded by insurance. That does not make the insurers automatic insurers of that excess." Helmbolt v. LeMars Mutual Ins. Co., 404 N.W.2d 55 (S.D. 1987). Unfortunately, in California, it apparently does.

HEALTH INSURANCE SUBROGATION

PENNSYLVANIA HIGH COURT EXEMPTS HMO's FROM ANTI-SUBROGATION STATUTE

Wirth v. Aetna U.S. Healthcare, 2006 WL 2408747 (Pa. 2006).

The ability of HMOs to subrogate in Pennsylvania actually got a little easier last month. While Pennsylvania recognizes both the equitable and contractual rights of subrogation, Holloran v. Larrieu, 637 A.2d 317 (Pa. Super. 1994); Daley-Sand v. West American Ins. Co., 564 A.2d 965 (Pa. Super. 1989) (holding that even with contractual subrogation language, subrogation is equitable in nature); Allstate Ins. Co. v. Clarke, 527 A.2d 1021 (Pa. Super. 1987), and while a health insurer is entitled to enforce its subrogation and reimbursement clauses, Chow ex rel. Chow v. Rosen, 812 A.2d 587 (Pa. 2002); Metropolitan Life Ins. Co. v. Bodge, 560 A.2d 175 (Pa. Super. 1989); Roudebush v. Wolfe, 1999 WL 1539802 (Ct. of Common Pleas of Pa. 1999), Section 1720 of the Pennsylvania Motor Vehicle Financial Responsibility Act, 75 P.S. § 1720 (1990), provides as follows:

> *"In actions arising out of the maintenance or use of a motor vehicle, there shall be no right of subrogation or reimbursement from a claimant's tort recovery with respect to workers' compensation benefits, benefits available under § 1711 (relating to required benefits), § 1712 (relating to availability of benefits) or § 1715 (relating to availability of adequate limits) or benefits paid or payable by a program, group contractor or other arrangements whether primary or excess under § 1719 (relating to Coordination of Benefits)."* Id.

One would hope that, like New Jersey, Pennsylvania would recognize that ERISA preempts such a destructive piece of legislation when it comes to subrogation. Unfortunately, one Pennsylvania federal court has confirmed that § 1797 of Pennsylvania's Motor Vehicle Financial Responsibility Law ("MVFRL") does regulate insurance, Benefits Concepts v. Macera, 413 F.2d 404 (E.D. Pa. 2005), which means that it is saved from preemption under ERISA and does apply to the health insurance subrogation rights of HMOs. It notes that unlike **New Jersey**'s anti-subrogation law, which appears in the state's general laws on civil actions, Pennsylvania's anti-subrogation provision appears in the insurance laws themselves. In *Benefit Concepts v. Macera,* the court found that § 1797 of the MVFRL did regulate insurance, but because the plan involved there was self-funded, the deemer clause prevented the law from being "saved" from preemption – and it was preempted by ERISA. Another federal court, in an unreported decision, also indicates that § 1720 *does* regulate insurance, and therefore will be saved from preemption where the plan is fully-insured. Medlar v. Regence Group, 2005 WL 1241881 (E.D. Pa. 2005). The court in the unreported *Medlar* decision notes that while the **3rd Circuit** has held that **New Jersey**'s anti-subrogation provisions did not "regulate insurance" for purposes of the saving clause, New Jersey's anti-subrogation law appeared in that state's general section on civil actions, while the Pennsylvania anti-subrogation law appears in the MVFRL and is specifically designed to regulate the escalating costs of motor vehicle insurance. The *Medlar* court ultimately found that § 1720 was not preempted like **New Jersey**'s anti-subrogation statute. Although § 1720 regulates insurance

and was “saved” from preemption as a result, the fact that it was a fully-insured plan meant that the deemer clause would not prevent it from being “saved” from preemption. Because the law was held not to be preempted due to the plan being fully-insured and not self-funded, § 1720 was not preempted.

There had, however, been some confusion with regard to HMOs in Pennsylvania. A Pennsylvania statute appears to exempt HMOs from the laws of Pennsylvania which are enforced with regard to insurance corporations or to any law enacted relating to the business of insurance unless such law specifically and in direct terms applies to such HMOs. 40 P.S. § 1560 (1998). This is because HMOs operate within and must comply with certain statutes governing HMOs. 40 P.S. § 1551 (1998) *(Health Maintenance Organization Act*). This summer, the **3rd Circuit** Court of Appeals took notice of the conflict between § 1720 and § 1560, and certified this issue to the Pennsylvania Supreme Court. Wirth v. Aetna U.S. Healthcare, 137 Fed. Appx. 455 (3rd Cir. 2005). On August 22, 2006, the Pennsylvania Supreme Court answered the question in the affirmative, and held that an HMO is exempt from the anti-subrogation provision of the MVFRL. Wirth v. Aetna U.S. Healthcare, 2006 WL 2408747 (Pa. 2006).

The Supreme Court noted that § 1720 does not provide “specifically and in exact terms that it applies to a health maintenance organization.” On the other hand, the Court took notice of the fact that the purpose of § 1560(a) was to permit and encourage the formation and regulation of HMOs. It declared that § 1560(a) of the Act, which provides that an HMO operating pursuant to the Act shall not be subject to “the laws of this State now in force relating to insurance corporations engaged in the business of insurance nor to any law hereafter enacted relating to the business of insurance unless such law specifically and in exact terms applies to such Health Maintenance Organization”, took preference over the conflicting § 1720.

This means that HMOs which are not ERISA-covered and self-funded may still subrogate in Pennsylvania free of the anti-subrogation provisions of § 1720. The General Assembly recognized that the anti-subrogation provisions of § 1720 alone do not cover “every conceivable type of healthcare arrangement,” as Wirth contends, absent additional language that overcomes the statutory exemptions for certain types of benefits. Similar to HMOs, hospital plan corporations and professional health care service corporations are exempt from insurance statutes that do not “specifically refer and apply” to them. See, Pa. C.S. § 6103(a) (*Hospital Plan Corporations*), 40 Pa. C.S. § 6307 (*Professional Health Service Corporations*).

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