



Sleeping with the enemy:

FEDERAL STATUTE CREATES OPPORTUNITY FOR
SUBROGATION STIPULATION IN WORKERS'
COMPENSATION FILES

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Greek mythology and subrogation have much in common. In mythology, as a punishment from the Gods for his trickery, Sisyphus was compelled to roll a huge rock up a steep hill. Each time he reached the top of the hill, the rock rolled down the other side and he had to begin again. In subrogation, recovery professionals must daily negotiate the trickery and deception of trial lawyers looking to greatly reduce or eliminate their workers' compensation subrogation interests. Purported stipulations and subrogation reimbursement agreements seemingly roll down the other side of the subrogation hill when real dollars are put on the table, setting the subrogator to his task all over again. Therefore, effective negotiation strategies and successful ploys are worth their weight in gold. One such strategy is a little-known tactic which involves use of a federal statute.

Trial lawyers spend a great deal of time and money keeping their third-party personal injury suits pending in favorable venues in state courts around the country. When the plaintiff is a citizen of a different state than every defendant in such a suit, federal diversity jurisdiction can be invoked by the defendants under 28 U.S.C. §1332 and a state court lawsuit can be removed to federal court where its value plummets. Most lawyers eschew federal court – even to the point of adding defendants with little or no potential culpability in order to destroy diversity – because federal court judges do not allow much latitude in discovery, federal rules are stricter and the cases are often pushed to trial more quickly than a meticulous trial lawyer would like.

Subrogating workers' compensation carriers should always be looking for ways to strike a reimbursement agreement with a plaintiff's attorney, in which the compensation lien is repaid with a reduced or eliminated deduction for attorney's fees, costs or made whole considerations, where applicable. A nice tactic to consider in workers' compensation subrogation cases involves a federal statute located at 28 U.S.C. §1445(c). That federal statute provides as follows:

"A civil action in any state court arising under the workman's compensation laws of such state may not be removed to any district court of the United States."

Therefore, if this section applies, a third-party lawsuit cannot be removed to federal court by the defendants, even if there is complete diversity or a federal question involved. When there is a plaintiff's attorney involved in a subrogation file you are handling and it looks like diversity or the existence of a federal question leaves no option but filing in, or removal to, federal court, consider negotiating with the plaintiff's attorney to keep the suit in state court by means of this federal statute. The subrogation laws of most states allow a workers' compensation carrier to file a third-party action if the worker does not and, in some cases, even if he does. If the carrier and claimant's counsel agree, the compensation carrier might consider filing the third-party suit, with the claimant

intervening as party plaintiff later on. In this fashion, the above federal statute may prevent removal of the case. This is music to the ears of plaintiff's attorneys looking desperately to avoid removal to federal court from favorable venues. In Missouri, for example, the federal district court case of *Pemiscot-Dunklin Electric Coop v. Jacobson*, 2006 WL 2432026 (E.D. Mo. August 18, 2006) clearly indicates that a third-party suit filed by a compensation carrier under §187.150 of the Missouri workers' compensation subrogation statutes is a suit "arising under the workman's compensation laws" of Missouri. The same is true in most states. Therefore, in exchange for guaranteeing the carrier a complete recovery, perhaps with a reduced claim for attorney's fees or no claim at all, the value of the plaintiff's case can double or triple by remaining in state court in a favorable venue. In Texas, trial lawyers will give up their first born child to keep large personal injury cases in state district court in Brownsville, or elsewhere in the Valley, where verdicts are double what they are elsewhere in the state.

The viability of this maneuver depends entirely on whether the ability of a workers' compensation carrier to file a third-party action stems from a state's common law or whether it is expressly provided for in the state's workers' compensation statutes. In the case of the former, the third-party suit might not be considered to have arisen under the workers' compensation laws of the state and removal to federal court would be allowed. In the case of the latter, §1445(c) would prevent removal and give the subrogating carrier the ability to help out the plaintiff's attorney by preventing the dreaded removal to federal court. The 8th Circuit, construing Missouri law, has confirmed that this statute prevents removal regardless of whether federal jurisdiction arises due to diversity of citizenship of the parties or the existence of a federal question. *Humphrey v. Sequentia, Inc.*, 58 F.3d 1238 (8th Cir. 1995). Any third-party action filed by a carrier pursuant to this strategy should clearly delineate that it is being filed pursuant to the specific statute in that state which grants carriers the right to file.

If the plaintiff's attorney agrees to protect your subrogation interest – or a pre-agreed high percentage of it – and not claim any attorney's fees or only a drastically reduced percentage for fees, you not only save fees and costs because your subrogation counsel can be relatively inactive and passive in the case, but the reduction in attorney's fees agreed on helps maximize your subrogation recovery. Everyone is happy. The plaintiff gets a bigger recovery, which translates into a bigger future credit for you. The plaintiff's attorney gets a bigger fee from a bigger pie. The workers' compensation carrier maximizes its subrogation recovery and its future credit, while paying less in attorney's fees which would not be included in the credit if paid. In short, everybody wins. The stone finally comes to rest at the top of the hill.

law of the jurisdiction. In the context of a tort action based upon negligence, the measure of damages is the diminution in the FMV of property. Diminution in FMV is quantified by taking the difference between the FMV of property immediately before and after a loss. Often, the quantification of damages based upon FMV can be substantially different from a calculation of damages based upon ACV or RCV. The distinction between what is paid under an insurance policy and what is recoverable in court can be confusing and lead to problems in identifying appropriate damages witnesses.

Who Can Testify As To The Value Of Damaged Property?

Different measures of direct damages require testimony from various persons. There are some instances where very specialized experts are needed or where no expert is needed at all. Looking first to claims for damage to real property, someone familiar with the repair of damaged buildings can likely be qualified to provide expert testimony about the cost of repairs since this primarily requires only thorough knowledge of the costs of building materials, labor and equipment. However, this will do little good at the time of trial if the law requires that damages be measured as the diminution in FMV. In order to present evidence on diminution in FMV, a real estate appraiser will likely be needed. On the other hand, some jurisdictions such as Pennsylvania, do not require an expert opinion as to FMV. Courts in Pennsylvania accept the "owner opinion rule" and permit property owners to offer an opinion as to the FMV of their property. The rule is based upon the premise that the owner of property is familiar with the cost of the property, the age of the property and the market value of the property. It is important to consult with subrogation counsel early on in order to determine what measure of damages the courts in your jurisdiction follow and what experts, if any, will be needed to offer an opinion on damages at the time of trial.

While owners of real and personal property can sometimes testify as to its value, expert testimony is almost always needed for inventory claims. Generally, this is because inventory claims involve far more items than people can mentally keep track of and inventory tends to turn over relatively quickly compared to real property or the contents of one's home. This is compounded by the fact that many businesses do not electronically track their inventory in real time. Without real time data as to what items were in inventory at the time of loss, a forensic accountant will have to be retained. Forensic accountants specialize in calculating and quantifying losses and economic damage utilizing an understanding of business information, financial reporting systems, accounting, and litigation procedures. A forensic accountant will evaluate past invoices, receipts, purchase data, income tax records and sales data. After reconstructing the value of the lost or damaged inventory, the forensic accountant can then offer an opinion as to the value of the inventory on hand at the time of loss. It is important to remember that the forensic accountant must be qualified as an expert to offer such opinion testimony. He or she should be able to testify that the system used in evaluating the inventory is based upon generally accepted accounting principles and is commonly used in the accounting field outside of the courtroom. Also remember that the amount paid under the claim for damaged inventory may be much greater than the recoverable amount. Some policies will allow for payment of the selling price of damaged goods when the law

only allows for the recovery of the cost of the goods to the seller. Unless the insured lost sales as the result of the loss of inventory, the recoverable amount is the cost of replacement inventory, not the selling price of the inventory. Often, a claim which results in lost inventory will also result in damage to equipment within the building.

Equipment claims also illustrate the need for specialized expertise. Equipment can encompass anything from refrigerated display cases to plastic molding machines to forklifts. Expensive and sometimes unique industrial equipment, such as a large metal press, cannot be priced by simple internet research alone. The value of such equipment is affected by market factors other than age and condition alone. These factors include the geographical location of the equipment, the current supply and demand and the style of the equipment. For example, older equipment will likely be obsolete or outdated and thus less valuable on the open market. Experts with specific knowledge of the type of equipment and the market for that equipment, such as used equipment brokers and dealers, must be called upon to provide testimony in these areas. These experts should have experience buying and selling the type of equipment at issue and should be familiar with current market conditions.

How To Evaluate Consequential Damages

As noted above, consequential damages are physically intangible and thus harder to evaluate. One of the most common items of consequential damages is loss of business income. Business income losses arise when an insured's business is unable to operate or is limited in its ability to operate after a loss. Most businesses will suffer a loss of business income after a fire or flood, whether it is a retail store that must close for cleanup or a factory that has to stop production to replace water damaged equipment. Evaluating a claim for loss of business income requires looking at the past performance of the business and determining if there has been an unanticipated decrease in performance since the loss. Be mindful that all businesses have trends. A pool supply store will have greater sales in spring and summer, while a car dealer may do better after tax time. These trends will be the same regardless of a loss and must be taken into account. For example, the pool supply store experienced a loss at the end of the summer. As a result of the loss, portions of the store were unusable for two weeks and certain inventory could not be sold. During those two weeks sales dropped dramatically. While some of that drop may have been due to the loss, most of it may simply be due to the fact that it was the end of the summer season. Understanding and calculating such trends cannot be done without the expertise of an accountant of actuary.

Who Can Testify As To Consequential Damages Such As Loss Of Business Income?

Much like an inventory claim where there is no electronic data available, a claim for loss of business income will require the reconstruction and evaluation of past financial data. A forensic accountant or an actuary will need to investigate past sales data, sales trends, market factors and inventory and then calculate the loss of income. It is important that the forensic accountant be familiar with the market trends of the business being evaluated, be able to identify his or her sources of data and be able to testify that the methods used were based upon >>

accepted accounting or actuarial principles. While the accountant or actuary will rely upon information from the insureds, the insureds themselves are not qualified in most jurisdictions to offer an opinion as to their loss of income. Certain states, however, such as Texas and Idaho, will allow the owner of a business to testify concerning lost profits, with the accuracy of this testimony going to the weight of the opinion and not its admissibility. In certain states, just as with claims for real property, the owner of a business is presumed to be familiar with its value. As noted earlier, consulting with subrogation counsel early on will help you determine the law in your jurisdiction and what type of expert, if any, is necessary to present your claim.

Proving Cases That Involve Direct And Consequential Damages

Many claims are comprised of both direct and consequential damages and will require opinions from multiple experts. In a recent case handled by the authors, a barn collapse killed and injured a stock of dairy cows. Expertise from local cattle auctioneers was required to establish the value of the deceased cattle (direct damages, business personal property). As for the injured animals, some had stopped producing milk while others were producing much less than before the loss. A dairy production expert had to be consulted to explain the loss in production and how it was related to the trauma from the collapse (consequential damages, loss of business income). A forensic accountant then pulled all of these figures together. As you can see, claims for loss of business income are, unfortunately, one of the most subjective categories of consequential damages. Experts will need to be well-versed in

their field to justify their conclusions on claims such as these. They must be able to clearly explain their methodology and the sources of data they relied upon. The cattle auctioneer noted above had to be able to show sales figures for similar cattle and offer some background on the local cattle market. It was also necessary for the dairy production expert in the above case to ascertain the weight and age of each cow, the average milk production to date, the health history of the cows and the facts of the loss and its aftermath. The forensic accountant illustrated how these numbers combine to equal a total damages figure. Without these experts working together, it would be impossible to get an accurate picture of the overall damages incurred by the insured.

Putting on your best case is not just about having the right evidence; it is about having the right experts to evaluate and present that evidence to the jury. As noted in the above examples, specialized knowledge is necessary to calculate the extent of damage for most inventory, equipment and business interruption claims. Selecting an expert who is familiar with the measure of damages and the type of property itself (e.g., store fixtures, industrial metal presses, cattle) is essential to presenting credible damages testimony. This will often result in the need for opinions from multiple experts with diverse expertise. By working with subrogation counsel early to discuss the law of damages in your jurisdiction, including the measure of damages, who may offer testimony, and what expert or combination of experts are best suited to testify on these issues, you can ensure that your next case is a recoverable case.