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Equitable Subrogation: Can an Insurance Company Have Its Cake and Eat It Too?

Tanya Scott, J.D.

Tanya Scott is a partner in the Albuquerque law firm of Teel and Scott, P.C., which practices primarily in the areas of personal injury, medical malpractice and insurance bad faith.

In local personal injury practice, an insurance company's subrogation interest has been historically limited to those instances in which the insurance contract specifically grants the right to recoup payments made, either by right of subrogation or an assignment of the cause of action. However, insurance companies with no such contractual provisions are increasingly asserting subrogation claims for insurance payments to insureds made under various coverages as a result of damages inflicted by a tortfeasor. Unfortunately, the overwhelming majority of states allow such subrogation claims even in the absence of a contractual right. The governing of the claims by equitable principles, however, still leaves much maneuvering room for the personal injury attorney representing the client who has received some compensation from his or her own insurance carrier.

Tanya Scott

Subrogation is a doctrine which has evolved to place the burden of paying for the infliction of injury squarely upon the party that is responsible for the injury.[1] The doctrine also finds support in the desire to prevent an injured party from gaining a double recovery.[2] The application of the doctrine is essentially to place the insurance company into the shoes of the injured party for the prosecution of the claim to the extent of payments made under the policy

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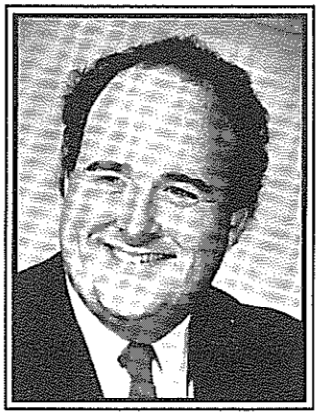
Where's The Passion?

Don Keenan, J.D.

Don C. Keenan of Atlanta practices in the areas of personal injury and wrongful death including auto accidents, medical negligence, products liability and workers' compensation. He is the President of the American Board of Trial Advocates. This is an abbreviated version of "Where's the Passion?" which was delivered June 21, 1991 at NMTLA's Ultimate Trial Seminar in Santa Fe.

Let's see if we can get some agreement on some things. I think all of us agree that as far as opening statements, cross-examination and closing argument are concerned that damned near anybody, be they a lawyer or a non-lawyer, can be taught how to do it. In my mind, my wife is the best cross-examiner I can find. None of you can even come close to her. If you go to any of the law schools you're going to see people who, from a skills standpoint, you're just going to shake your head and say, "God damned they're good." It's just like anybody can be taught how to play a piano. You can be taught how to paint. You can be taught how to play the fiddle. I think you'll agree with me that what separates the mediocre and the good from the great



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for damages caused by the third party tortfeasor.[3] The claim remains the same. Only the beneficial ownership of the claim changes.[4]

Subrogation is one of two types, conventional or legal.[5] It can be created by virtue of a statutory enactment granting the right to an insurance company,[6] or a governmental agency which has assumed medical expenses on behalf of the plaintiff.[7] Conventional subrogation arises from a contractual agreement between insured and insurer.[8] Legal subrogation, on the other hand, arises from operation of law whenever an insurance company pays the debt which in equity and good conscience should be paid by the tortfeasor.[9] Courts which have considered the question have overwhelmingly determined that an insurance company is subrogated to the interests of its insured in pursuing a claim against the tortfeasor to the extent of payments made to the insured, despite the lack of language in the policy which would create such a right.

Courts have expressed this principle in a variety of ways: legal or equitable subrogation does not arise from contract, but from the equities between the parties.[10] As a creature of equity, it does not depend upon a contractual provision between the parties.[11] Regardless of an express contract provision, an insurer may be entitled to subrogation.[12] The right of subrogation arises by operation of law without regard to whether there is any provision in the policy.[13] An insurance company is subrogated to the rights of the insured either by the express terms of the policy, or on the grounds of general equitable principles.[14]

This is also the view which has been embraced by the New Mexico Supreme Court.[15] Quoting **Fidelity & Deposit Co. of Maryland v. Atherton,**[16] the Supreme Court stated as follows:

> "Subrogation is not necessarily founded upon contract [citations omitted]. It is an equitable remedy of civil law origin whereby through a supposed succession to the legal rights of another, a loss is put ultimately on that one who in equity and good conscience should pay it." [citations omitted].[17]

Quoting Appleman on Insurance,[18] the Supreme Court continued as follows:

> "An insurer generally is entitled to subrogation either by contract or in equity for the amount of the indemnity paid. Indeed it has been stated that the doctrine of subrogation does not depend primarily upon statutory or policy provisions, but originates in the general principles of equity, and will be applied or not according to the dictates of equity and good conscience and considerations of public policy. Such doctrine is founded upon the relationship of the parties and upon equitable principles, for the purpose of accomplishing the substantial ends of justice. Subrogation rests on the maxim that no one should be enriched by another's loss. And a subrogation action by insurer is not a suit on the insurance contract but an independent action in which equitable principles are applied to shift the loss, for which the insurer has compensated its insured, to one who caused the loss or who is legally responsible for a loss caused by another and whose equitable position is inferior to the insurer's."[19]

The jurisdictions which have refused to allow insurance companies to assert subrogation claims, either conventional or legal, have primarily based their reasoning on the inability to split a cause of action for personal injuries.[20]

The concern of Arizona courts in disallowing subrogation claims by insurance companies has been the public policy consideration of allowing an insurance company to reap the benefits of its premiums and then to also recover from the tortfeasor.

Arizona has disallowed both legal and conventional subrogation by insurance companies in personal injury lawsuits, reasoning both that subrogation involves an unlawful splitting of a cause of action, and that it violates public policy considerations. The Arizona Supreme Court in **State Farm Fire and Casualty Co. v. Knapp,**[21] declined to entertain a subrogation claim by an insurance company, noting that subrogation amounts to an assignment and claims for personal injury are not assignable. The court expressed fear that recognizing an insurance company's claim for subrogation was fraught with dire possibilities and would be like opening a Pandora's box of problems. Presumably, the court foresaw the procedural morass which would result in trying to accomodate the insurance company's interest in the litigation after recognition that an insurance company owns a piece of the lawsuit.[22]

The major concern of the Arizona courts, however, has been public policy considerations of allowing an insurance company to reap the benefits of its premiums, and then recover from the tortfeasor what it has paid its insured pursuant to its contract.[23] The countervailing interest of the plaintiff is to achieve a complete recovery from the tortfeasor who caused the injuries. The court in **Allstate Ins. Co. v. Druke**[24] considered a claim by an insurance company for medical expenses of the plaintiff paid by the plaintiff's own insurance company. The company then sought recovery from the third party tortfeasor for those amounts the company had paid. The court reasoned that while the plaintiff may have been fully indemnified for his medical expenses from his own insurance company, he most likely had other significant losses arising from his injury which were not monetarily

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indemnifiable, and not insurable. Thus, the insurance company was seeking full recovery of all amounts paid under its medical coverage without regard to whether or not the plaintiff had been made whole for his injuries through settlement with, or a judgment against, the party responsible for his injuries.

The Arizona Supreme Court further articulated the unfairness of allowing the insurance company to reap the benefits of its bargain with its insured, and then seek reimbursement for the amounts it had paid under its contract.

Also, to require an injured policy holder to return to his insurer the benefits for which he has paid premiums is to deny him the benefits of this thrift and foresight. In terms of public policy, the only justification for allowing an insurance company to recoup the benefits it contracted to pay out in exchange for the receipt of premium payments which are presumably actuarially adequate would be the lowering of premium rates as a result of such recoupment. This is generally not the case:

> "Subrogation is a windfall to the insurer. It plays no part in the rate schedules (or only a minor one), and no reduction is made in insuring interests * * * where the subrogation right will obviously be worth something." [citations omitted].[25]

Oklahoma has achieved the same result statutorily, refusing approval of insurance contracts which contain subrogation clauses.

Oklahoma has achieved the same result statutorily, refusing approval of insurance contracts which contain subrogation clauses. In **Aetna Cas. and Sur. Co. v. State Bd., Etc.,**[26] the Supreme Court considered a challenge to an order of the Oklahoma State Board for Property and Casualty Rates which had disapproved the appellant's policy with a subrogation clause for medical payments made on behalf of the insured. The court acknowledged that the underlying purposes of the subrogation remedy are to place the ultimate loss upon the wrongdoer, as well as prevent a double recovery. However, the court considered the important interests of the injured party and refused to overturn the decision of the insurance board, reasoning as follows:

> "In personal insurance contracts, however, the exact loss is never totally capable of ascertainment, and therefore the same reasons militating against double recovery do not obtain. The general rule, therefore, is that the insurer is not subrogated to the insured's right or the beneficiary's rights under the contract of personal injury."[27]

New Mexico litigants have already had the argument concerning the unassignability of personal injury claims foreclosed by earlier appellate court opinions. The Supreme Court has held in a case considering a specific contractual provision for subrogation that the unassignability of personal injury claims is not the law in New Mexico insofar as it involves a claim of subrogation.[28]

The equitable arguments, however, may still contain some viability, at least in the realm of legal subrogation. The Supreme Court has held that contractual or conventional subrogation is a matter of contract between the parties and is valid.[29] In **March v. Mountain States Mut. Cas. Co.,**[30] the court refused to consider the equitable arguments opposing subrogation because the case before the court involved contractual subrogation which it deemed to be valid. No discussion concerning equitable subrogation or legal subrogation is in the opinion. Given the long history of recognition of equitable subrogation, however, it seems unlikely that the Court will adopt a wholesale disavowal of the validity of the doctrine.[31]

The plaintiff's attorney's most promising attack on the doctrine of subrogation is still through the weighing of the respective equities of the plaintiff and the insurance company.

In the absence of statutory or judicial abrogation of the equitable remedy of subrogation, the plaintiff's attorney's most promising attack on the application of the doctrine is still through the weighing of the respective equities of the plaintiff and the insurance company. Subrogation is an equitable remedy and thus subject to equitable principles.[32] Because subrogation is equitable, it is not a matter of right.[33] It will never be enforced when the equities are equal or the respective rights are not clear.[34] It is a fluid concept which depends upon the particular facts of a given case for its application.[35] To some facts it will adhere, to others it will not.[36]

The primary factor weighing against the allowance of a subrogation claim in favor of an insurance company in the personal injury realm is whether the injured plaintiff has been totally compensated for his or her injuries. "Equitable principles apply to subrogation and the insured is entitled to be made whole before the insurer may recover any portion of the recovery from the tortfeasor."[37] As an equitable doctrine, it may be invoked only under circumstances where justice demands, and the rights of those seeking subrogation have a greater equity than those opposing subrogation.[38]

In **Transamerica Insurance Company v. Barnes,**[39] the court considered a subrogation claim by an insurance company which had paid medical expenses on behalf of the injured plaintiff. The company had notified its insured of its subrogation interest, but had refused to participate in the plaintiff's action or allow plaintiff's counsel to act on the company's behalf. Having settled his claim against the

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tortfeasor, the insurance company then sought reimbursement from the plaintiff of those amounts paid for medical benefits.

The **Transamerica**[40] court, citing equitable principles, refused to allow the insurance company an unfettered right to recover the amounts paid on its insured's behalf. Because the settlement reached between the plaintiff and the defendant did not spell out the various allocations of monies to the various items of damage suffered by the plaintiff,[41] the court could weigh the equities and determine whether or not the plaintiff had been fully compensated for his loss. Instead, the court placed the burden upon the insurance company seeking subrogation to prove that the damages covered by the settlement were the same as those paid by the insurance company in order to establish the greater equity. The mere receipt of payments by the plaintiff from the tortfeasor does not require the conclusion that the insurance company is entitled to a return of those amounts paid to plaintiff under its contract of insurance.[42]

A similar result was reached by the Washington Supreme Court in **Elovich v. Nationwide Ins. Co.**,[43] where the court held that a subrogation right arises only after the plaintiff has been fully compensated for his injuries. Similarly in **Hill v. State Farm Mut. Auto Ins. Co.**,[44] the Utah Supreme Court held that in the absence of an express contract to the contrary, the insured must be made whole before the insurer is entitled to be reimbursed. Once again, the burden is placed squarely upon the insurance company to demonstrate that the plaintiff was adequately compensated before the company is entitled to a recovery.[45] The court also warned against assuming that the amount of damages suffered by the plaintiff is coextensive with the amount of settlement because there are a plethora of reasons which will convince a plaintiff to settle his or her claim in an amount less than his actual damages, including the possible insolvency of the defendant, the plaintiff's immediate need for money, and the likelihood of success at trial.[46] Noncontractual subrogation rights will only be enforced on behalf of the party maintaining a superior equitable position and an insurance company cannot be superior unless the insured has been completely compensated.[47]

Noncontractual subrogation rights will only be enforced on behalf of a party maintaining a superior equitable position and an insurance company cannot be superior unless the insured has been fully compensated.

In a case involving statutorily created subrogation rights, the New Mexico Court of Appeals let stand the determination of the lower court that the equities of the case demanded that the Health and Social Services Department have its subrogation claim greatly reduced after a quadriplegic plaintiff made a settlement with the tortfeasor responsible for her injuries.[48] While the court did not require that the plaintiff be made whole before HSSD's subrogation claim could be satisfied, it certainly embraced the notion that equitable considerations will govern the division of any settlement or judgment achieved by the plaintiff.[49]

An insurance company claiming a subrogation right is also subject to the same defenses which could have been raised against the plaintiff on the underlying claim.[50] Thus, a reduction of plaintiff's recovery through a finding of comparative fault by plaintiff, or some other tortfeasor which is immune from liability, or judgment proof, should likewise operate to reduce the insurance company's recovery by the same percentage.

The practitioner should also be mindful of the ways in which an insurance company may waive its subrogation rights. The initial burden is placed upon the insurance company to protect its right of subrogation.[51] The company may not sit on its rights without expecting to lose them.[52] The company may also waive its rights by arbitrarily refusing permission for the insured to settle his claims against the tortfeasor, or by denying plaintiff's claim for indemnity against his own company.[53]

The failure or refusal of an insurance company to participate in the insured's claim or make arrangements for protecting its own interests may also weigh against the company in the equitable balance once the plaintiff recovers from the tortfeasor causing his injuries.[54] Even though the court may not find that a waiver of the right has occurred, the failure to protect its own interests will weigh against the company when the equities are considered.[55]

The enforcement of a subrogation claim arising from uninsured or underinsured motorist coverage may be denied in certain circumstances because of separate public policy considerations which surround uninsured and underinsured motorist coverage.[56] Subrogation claims which prevent a motorist from recovering at least his or her uninsured or underinsured motorist coverages may be unenforceable.[57]

An insurance company may also attempt to raise a subrogation claim against a tortfeasor who is, in reality, an insured under the policy.[58] This situation may arise when the tortfeasor is a relative of the named insured, and thus is really an insured under the policy. An insurance company may not assert a subrogation claim against its own insured because it has indemnified the insured for the very risk which it assumed and for which it received a premium.[59] Subrogation exists only with respect to rights of the insurer against third persons to whom the insurer owes no duty.[60]

Finally, even assuming that the insurance company is entitled to some recovery of the amounts paid under its insurance coverages, the company may still be responsible

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for a portion of the costs and fees expended by the plaintiff in securing the settlement or judgment.[61] This would be particularly true if the company has relied upon the plaintiff and his or her counsel in prosecuting the action. New Mexico has embraced this notion in the workers' compensation arena, acknowledging that the efforts of the plaintiff and his or her counsel should not go unrewarded when an insurance company seeks reimbursement of amounts paid under the Workers' Compensation Act.[62] Presumably the same reasoning would apply in the subrogation area.

Plaintiffs' attorneys who have received notice of a pending subrogation claim from an insurance company might also be wise to request assistance from the insurance company for costs to be expended in the case. Even though the insurance company may ultimately be liable for a pro rata share of the costs expended in the prosecution of the claim if the plaintiff prevails on the underlying claim against the tortfeasor, the company's exposure for costs should be no less than the plaintiff's from the beginning. A refusal by the company to contribute to the costs of prosecuting the action early on may also result in a waiver of the subrogation right,[63] or at least be weighed in the equitable balance when the time for determining the insurance company's portion of the recovery arises.[64]

Insurance companies without specific subrogation contractual provisions are nonetheless claiming the benefits of equitable or legal subrogation to recover benefits paid under their policies for injuries which have been inflicted upon plaintiffs by others. This method of subrogation has been specifically recognized and validated by New Mexico appellate courts. While it does not seem likely that our appellate courts will disavow approval of equitable subrogation in the future, the door is still very much open to limit or deny recovery to companies which have paid under their policies pursuant to their contractual obligation to do so. The plaintiff's attorney should carefully evaluate the behavior of the insurance company, the public policy considerations which are implicated, the nature of the claims raised, and the equities on both sides of the issue to determine whether the claim for equitable subrogation can be defeated or at least limited in scope.[65]

ENDNOTES

1. **Sexton v. Continental Casualty Co.**, 816 P.2d 1135 (Okla. 1991).

2. **Marquez v. Prudential Property and Cas. Ins. Co.**, 620 P.2d 29 (Colo. 1980).

3. **Union Ins. Co. v. R.C.A. Corp.**, 724 P.2d 80 (Colo. App. 1986).

4. *Ibid.*

5. **United States Fidelity & G. Co. v. Raton Nat. Gas Co.**, 86 N.M. 160, 521 P.2d 122 (1974).

6. **Farmer's Ins. Co. v. Farm Bureau, Etc.**, 608 P.2d 933 (Kan. 1980).

7. **White v. Sutherland**, 92 N.M. 187, 585 P.2d 331 (Ct. App. 1978).

8. **United States Fidelity & G. Co. v. Raton Nat. Gas Co.**, *supra.*

9. *Ibid.*

10. **Republic Underwriters v. Fire Ins. Exchange**, 655 P.2d 544 (Okla. 1983).

11. **Lawyers' Title Guar. Fund v. Sanders**, 571 P.2d 454 (Okla. 1977).

12. **Transamerica Insurance Company v. Barnes**, 505 P.2d 783 (Utah 1972).

13. **New Hampshire Ins. Co. v. Kansas Power & Light Co.**, 510 P.2d 1194 (Kan. 1973).

14. **North America v. State Farm Mut. Auto. Ins. Co.**, 663 P.2d 953 (Alaska 1983).

15. **United States Fidelity & G. Co. v. Raton Nat. Gas Co.**, *supra.*

16. 47 N.M. 443, 448, 144 P.2d 157, 160 (1943).

17. 86 N.M. at 162.

18. 6A Appleman, **Insurance Law and Practice**, § 4054 at 142-144.

19. **United States Fidelity & G. Co. v. Raton Nat. Gas Co.**, *supra* at 162-163.

20. *See, generally,* Annot., 19 A.L.R.3d 1054 (1968).

21. 484 P.2d 181 (Ariz. 1971).

22. New Mexico has recognized that a subrogated insurance company has an enforceable right, and thus is a necessary and indispensable party to a lawsuit. **Sellman v. Haddock,** 62 N.M. 391, 310 P.2d 1045 (1957). This holding necessarily led to the procedural quagmire of how to join the plaintiff's insurer in the action, without prejudicing the plaintiff in the eyes of the jury. The court resolved the question by allowing the defendant's insurance company to also be named as a nominal party. **Maurer v. Thorpe,** 95 N.M. 286, 621 P.2d 503 (1980) and **Campbell v. Benson,** 97 N.M. 147, 637 P.2d 578 (Ct.App. 1981). The latest resolution of the dilemma involves allowing the plaintiff to pursue the entire claim on his own behalf and on behalf of his insurer, with the subrogation claim being tried to the court at the conclusion of the jury trial if the plaintiff prevails. **Safeco Ins. Co. v. U.S. Fidelity & Guar. Co., 101 N.M. 148, 679 P.2d 816 (1984).**

23. **Allstate Ins. Co. v. Druke,** 576 P.2d 489 (Ariz. 1978).

24. *Ibid.*

25. *Ibid* at 492.

26. 637 P.2d 1251 (Okla. 1981).

27. *Ibid* at 1255.

28. **Jacobson v. State Farm Mutual Automobile Ins. Co.**, 83 N.M. 280, 491 P.2d 168 (1971).

29. **March v. Mountain States Mut. Cas. Co.**, 101 N.M. 689, 687 P.2d 1040 (1984).

30. *Ibid.*

31. **United States Fidelity & G. Co. v. Raton Nat. Gas Co.**, *supra;* **Safeco Ins. Co. v. U.S. Fidelity & Guar. Co.**, *supra.*

32. **Transamerica Insurance Company v. Barnes**, 505 P.2d 783 (Utah 1972).

33. **Fireman's Fund Ins. v. Morse Sig. Dev.**, 198 Cal. Rptr. 756 (Cal. App. 2 Dist. 1984).

34. *Ibid.*

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