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Subrogation and Liens

Judy Kostura

Author Contact Information:

Judy Kostura

Kostura & Putman, P.C.

2901 Bee Cave Road, Suite L

Austin, TX 78746

Judy@KosturaPutmanLaw.com

512.328.9099



JUDY KOSTURA

THE COMMISSIONER'S HOUSE AT HERITAGE SQUARE
2901 Bee Cave Road, Suite L, Austin, Texas 78746
Judy@KosturaPutmanLaw.com

Licenses: Texas Supreme Court: 1980; Western District, Federal Court: 1988
Legal Practice: Kostura & Putman, P.C., kosturaputmanlaw.com; Personal Injury Practice

AV Rating by Martindale-Hubbell (highest ranking for competence and ethics)

Experience: Trucking and Commercial Vehicle Collisions, Automobile Collisions, Premises Liability, Wrongful Death, Burn Injuries, DWI Injuries, Attack by Vicious Animals, Subrogation and Liens, Insurance Bad Faith, Medical Provider Representation on Deposition and Subpoena Disputes

Author: Personal Injury Form Book for West Publishing Co.

CLE presentations to: American Assn of Justice, Texas Trial Lawyers Assn, UT School of Law, State Bar of Texas, University of Houston Law School, South Texas College of Law, Texas Advanced Paralegal Seminar, Capital Area Trial Lawyers Assn, Austin Bar Assn, South Plains Trial Lawyer Assn., Texas Academy of Family Law Specialists

CLE topics: Effective Demand Letters to Maximize Damages; Medical Records Privilege and Ethics of Redacting Medical Records; Sufficiency of the Evidence on Appeal; Subrogation and Liens; Client Communications; *In re North Cypress* Webinar; Tex. Civ. Prac. Rem. Code 18.001 Affidavits; Legislative Update 2019

Course Director: State Bar of Texas Advanced Civil Trial, 2023

Course Director: State Bar of Texas Advanced Evidence & Discovery, 2016

Course Director: State Bar of Texas Advanced Personal Injury Seminar, 2013

Course Director: State Bar of Texas Damages Seminar, February 2011

Professional Affiliations: Life Fellow, Texas Bar Foundation

Texas Trial Lawyers Assn: Board of Directors; Executive & Nominating Committees (2005-2006) (2017-2018), Vice President of CLE (2018); Committees (various): CLE, Communications, Budget Capital Area Trial Lawyers Association (President 1999-2000, Executive Committee through 2015) Travis County Bar Association, Board of Directors (1995-1998)

Lawyer Referral Service Board of Trustees through 2018 (Chair 1995-1998)

Pro Bono College of Law, over 100 hours of Pro Bono Public Service (various)

Professional Honors: *State Bar of Texas Gene Cavin Award for Continuing Education, 2022*

Texas Watch Champion of Justice 2019

Texas Monthly Super Lawyer 2015, 2016, 2017, 2018, 2019, 2020, 2021, 2022, 2023

Texas Monthly Top 50 Texas Women & Texas Monthly Top 50 Central/W. Texas 2016

Texas Monthly Top Women Attorneys in Texas 2021

Texas Trial Lawyers Assn Resolution of Appreciation for Legis. Contributions 2013

Scott Ozmun Trial Lawyer of the Year Capital Area Trial Lawyers Assn 2011

John Howie Spirit of Mentorship Award Texas Trial Lawyers Association 2006

Million Dollar Advocates Forum

Education: Doctor of Jurisprudence, UT Austin: 1980; BA With Honors, UT Austin: 1977

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For Fun:

They're out to get you
To capture you and make you, spellbound
Howling and prowling
You're shivering, quivering, spellbound
You cannot run and you cannot hide

Yeah, you've gotta face it, baby
Things go bump in the night
Wherever you run and wherever you hide
Yeah, you've gotta face it, baby
Things go bump, bump, bump in the night
Things That Go Bump in the Night, by the Allstars

SUBROGATION AND LIENS

I. OVERVIEW OF SUBROGATION, HISTORY, FEDERAL AND STATE BALANCING ACT, AND COMMON LAW EQUITABLE PRINCIPLES.

A. History of state and federal regulation of insurance

Subrogation is an element of insurance law. In 1944, the United States Supreme Court determined that “insurance” is a form of interstate commerce subject to federal regulation; see *United States v. South-Eastern Underwriters Assoc.*, 322 U.S. 533 (1944). Shortly thereafter, Congress passed the McCarran-Ferguson Act, 15 U.S.C.S. § 1011 and following. The McCarran-Ferguson Act granted authority to the states to regulate the “business of insurance.” Various federal laws continued to govern the “peripherals of the industry (labor, tax, securities).” State laws which regulated the core nature of the insurance business therefore overrode most federal laws to the contrary. This paper is designed to analyze the myriad of state and federal statutes and cases on the topic of subrogation, from the standpoint of the plaintiff’s personal injury practitioner.

In an attempt to harmonize the proliferation of insurance policies and laws and to protect workers, Congress passed the Employee Retirement and Income Security Act, commonly known as ERISA, in 1974. ERISA did not vitiate the McCarran-Ferguson’s grant of state regulation; it did spawn a spate of lawsuits trying to determine which state laws qualify as state regulation (not-preempted by ERISA) and which laws deal with peripheral issues (pre-empted by ERISA). ERISA also recognized that some health plans are self-funded, not funded by insurance premiums, and those plans are exempt from state regulation.

The shifting of risk through the payment of premiums is the most fundamental principle of insurance. Subrogation is a bastardization of that risk-shifting principle. Therefore, subrogation should come within the “core business” of insurance and be subject to state regulation for all premium funded insurance policies. A Florida court traced the history and analysis:

[T]he court in *Pilot* looked to case law interpreting the phrase “business of insurance” under the McCarran-Ferguson Act. *Id.* This law, taken as a whole, provided three criteria for determining whether a practice would fall under the “business of insurance.” *Id.* Namely:

“[F]irst, whether the practice has the effect of transferring or spreading a policyholder's

risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry.” *Union Labor Life Ins. Co. v. Pireno*, 458 U.S. 119, 129, 102 S.Ct. 3002, 3009, 73 L.Ed.2d 647 (1982) (emphasis in original). *Id.* at 48-49.

However, more recently, in *Kentucky Ass'n of Health Plans, Inc. v. Miller*, 538 U.S. 329, 341-42 (2003), the Supreme Court receded from the McCarran-Ferguson factors, stating:

Today we make a clean break from the McCarran-Ferguson factors and hold that for a state law to be deemed a “law ... which regulates insurance” under § 1144(b)(2)(A), it must satisfy two requirements. First, the state law must be specifically directed toward entities engaged in insurance. See *Pilot Life, supra*, at 50, 107 S.Ct. 1549, *UNUM, supra*, at 368, 119 S.Ct. 1380; *Rush Prudential, supra*, at 366, 122 S.Ct. 2151. Second ... the state law must substantially affect the risk pooling arrangement between the insurer and the insured. Kentucky's law satisfies each of these requirements.

The majority of cases addressing state subrogation and collateral source statutes have determined that they are laws regulating insurance. In *FMC Corp. v. Holliday*, 498 U.S. 52, 60-61 (1990), the Supreme Court considered whether a Pennsylvania anti-subrogation statute was a law “regulating insurance” and held:

There is no dispute that the Pennsylvania law falls within ERISA's insurance saving clause.... Section 1720 directly controls the terms of insurance contracts by invalidating any subrogation provisions that they contain. See *Metropolitan Life Ins. Co. v. Massachusetts*, 471 U.S., at 740-741, 105 S.Ct., at 2389-2390. It does not merely have an impact on the insurance industry; it is aimed at it. See *Pilot Life Ins. Co. v. Dedeaux*, 481 U.S. 41, 50, 107 S.Ct. 1549, 1554, 95 L.Ed.2d 39 (1987). This returns the matter of subrogation to state law. *Coleman v. BCBS of Alabama, Inc.*, No. 1D10-1366, (D. Ct of Appeal Florida, 1st Dist. - Dec. 8, 2010)

This paper reviews U.S. and Texas subrogation interests and liens in favor of Veterans Administration, Medicare, Medicaid, workers' compensation, Hospital Liens, or child support liens. It covers

conventional/contractual subrogation interests, including ERISA Employee Welfare Benefit Plans and Non-ERISA Plans, Self-funded Pools, Private Health Insurance, Government Employer or Church Sponsored Plans, Medical Payments Coverage, Uninsured/Underinsured Motorist Coverage, Vehicle Property Damage, and HMO's. It also covers equitable subrogation imposed by law. It analyzes the effect of the Texas Supreme Court's decision in *Fortis Benefits v. Cantu*, 234 S.W.3d 642, 649 (Tex. 2007), NO. 05-0791, on the made whole doctrine, and the legislative reform of *Fortis* by the passage of Ch. 140A Civ. Prac. and Rem. Code, effective on 01/01/2014. See Section I.E.1.B, Ch. 140A of this paper for a discussion of the *Liberty Mutual Ins. Co. v. Transit Mix Concrete & Materials Co.*, No. 06-12-00117-CV, (___ S.W.3d ___ June 28, 2013, pet. den.) case and the statute's effective date for 3rd party and 1st party claims.

B. Definitions.

"Subrogation" has been defined as the "substitution of one person in the place of another with reference to a lawful claim, demand or right." Black's Law Dictionary. "Subrogation is the substitution of one person in the place of another, whether as creditor or as the possessor of some lawful claim, so that he who is substituted succeeds to the rights of the other in relation to the debt or claim. . . . By subrogation, a court of equity, for the purpose of doing exact justice between parties in a given transaction, places one of them, to whom a legal right does not belong, in the position of a party to whom the right does belong." 53 Tex.Jur.2d Subrogation § 1, at 429 (1964).

Although some courts use "subrogation" and "reimbursement" interchangeably, they are distinct concepts. The "subrogee" is the entity – usually an insurer -- which paid benefits to the subrogor (injured plaintiff) and has a right to stand in the shoes of the plaintiff, with respect to the plaintiff's liability claims, and sue the tortfeasor. The "subrogor" is the one who contracted away his or her rights of recovery to the subrogee. A right of reimbursement requires the person with the original claim (injured plaintiff) to turn over collected claim proceeds to the insurer claiming the right of reimbursement from its own insured. See *Charla Aldous v. Darwin Nat'l Assurance Co.*, 851 F.3d 473, 485, No. 16-10537-CV0 (5th Cir. 03/16/17) (revised to rescind part III.B.4 on 05/11/2018) which denied an insurer the right to collect from its own insured because it failed to exercise its contractual subrogation interest against the third party and had no right of reimbursement against its insured. See also *Freitas v. Geisinger Health Plan*, (M.D. Pa. May 27, 2021) 2021 WL 2156740, in which plaintiffs survived a 12(b)(6) motion. The court held those plaintiffs' suit stated claims that their insurer inappropriately demanded reimbursement of insurance benefits when a

subrogation provision did not include a right of reimbursement; for wrongful denial of benefits; for breach of fiduciary duty; for misrepresentation of the insurance terms; for breach of the duty to disclose material information; and for wrongful interpretation of the insurance policy. [The court later granted summary judgment to the plan when another plan document, more complete and containing a right of reimbursement, surfaced during additional discovery.]

A subrogation interest is not the same as a lien and a subrogee is not automatically a secured lienholder. Subrogation and assignments were equated by the 5th Circuit in *Associated International Ins. Co. v. Scottsdale Ins. Co.*, 16-20465 (5th Cir. 07/07/17): "[S]ubrogation works much like an assignment: both transfer rights from the assignor to the assignee. See *Hamilton v. United Healthcare of La., Inc.*, 310 F.3d 385, 397 (5th Cir.) (Garza, J., concurring) ("[I]n essence, subrogation is an assignment."): COUCH ON INSURANCE § 222:54 (noting that the distinction between assignment and subrogation may be "academic and not a substantive matter"). Although subrogees stand in the shoes of the subrogors, they cannot seek the same statutory or punitive damages as the subrogors; *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Ins. Co. of N. Am.*, 955 S.W.2d 120, 133 (Tex. App. – Houston [14th Dist.] 1997), *aff'd sub nom. Keck, Mahin & Cate v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 20 S.W.3d 692 (Tex. 2000). From *Union Fire*:

On the issue of statutory or punitive damages and equitable subrogation, a majority of the justices agreed that as a general rule, subrogation gives indemnity and no more. *American Centennial*, 843 S.W.2d at 485 (citing *Phipps v. Fuqua*, 32 S.W.2d 660, 663 (Tex.Civ.App. — Amarillo 1930, writ ref'd)). In other words, a party who successfully brings suit based on the doctrine of equitable subrogation can only recover the amount he was required to pay because of the actions of the defendant. This view of equitable subrogation was adopted by the Dallas Court of Appeals in *Interfirst Bank Dallas v. United States Fidelity Guar. Co.*, 774 S.W.2d 391, 399 (Tex.App. — Dallas 1989, writ denied). In that case, the court held subrogation rights cover only the amount paid to discharge the obligation; it does not entitle the subrogee to cost or expenses. *Id.* Therefore, based on the general tenets of the doctrine of equitable subrogation, a majority of the supreme court agreed that an excess carrier is not entitled to recover damages to recover statutory or punitive damages. *American Centennial*, 843 S.W.2d at 485 (citations omitted). We will follow the view of the majority of the supreme court justices, and therefore hold that an excess carrier, who brings suit based on the

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