


WHOSE MONEY IS IT ANYWAY? A QUICK-REFERENCE GUIDE TO CARRIERS' SUBROGATION RIGHTS AFTER PAYING WORKERS' COMPENSATION BENEFITS

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You represent a workers' compensation carrier who just paid out a ton of money for an on-the-job injury. Now, you learn that the injured employee has recovered a substantial sum of money from a third party based on the same injuries. Can your client recoup any of the money it paid in workers' compensation benefits from the employee's recovery against the third party? This article is a quick-reference guide to the controlling authorities on this issue in each of the fifty states.

Generally, states fall into one of three different categories: (1) those that apply the "make-whole" doctrine; (2) those that give the carrier priority over the employee's third-party recovery, also known as "first monies" states; and (3) those that fall somewhere in between and attempt to apportion the recovery.

I. Make-Whole States

In "make-whole" states, "an insurer will not receive any of the proceeds from the settlement of a [third-party] claim, except to the extent that the settlement funds exceed the amount necessary to fully compensate the insured for the loss suffered."[1] Only six states apply the make-whole doctrine: Arkansas, Georgia, Kentucky, Montana, New Mexico, and Vermont.[2] Employees in these states enjoy strong protection of their third-party recoveries.

Courts are sometimes faced with the task of applying this common-law doctrine in the context of a statutory framework that, by its language, seems to allow the carriers to recover out of the "first-monies" received from a third party, *i.e.*, before the employee is "made whole." For example, in *Gen. Accident Ins. Co. of Am. v. Jaynes*, the Arkansas Supreme Court held that an "insurer's right to subrogation [does] not arise until the insured [is] made whole."[3] This made application of Arkansas's first monies-type statute contingent on the employee first being made whole by any third-party recovery.

In *Jaynes* the plaintiffs were the wife and two children of an individual killed in a car accident. The other vehicle belonged to the defendant. Jaynes's wife and two children received $101,000 in benefits from the defendant's workers' compensation carrier. After filing suit against third parties, the plaintiffs settled for $18,500. The carrier asserted a lien on the plaintiffs' settlement proceeds based on the Arkansas statute, which first deducts costs of collection from the recovery, then allows an employee to keep one-third of the remainder, and subsequently allows the carrier to recoup the benefits it paid the employee regardless of whether the one-third over or under compensates the employee.[4] The circuit court ruled in the plaintiffs' favor, finding that the statute only applied after the employee or his family was made whole. It also found that $18,500 did not make the plaintiffs whole, and therefore denied the carrier's lien. The carrier appealed. The Supreme Court of Arkansas agreed with the circuit court. The court reconciled the statute with the common law by finding that the statute only becomes applicable after the employee is made whole.[5]

Arkansas's lower courts and the Workers' Compensation Commission have followed their Supreme Court's lead. For example, in *J.B. Hunt Transp., Inc. v. Knight*, the employee recovered workers' compensation benefits and also brought a third-party action to recover for the same injuries.[6] In his claim against the third party, the employee valued his damages at $1.8 million.[7] But without filing suit, he and his family settled the claim for $3.3 million apportioned as follows, after deducting costs and expenses:

1 Black's Law Dictionary 967 (7th ed. 1999).

2 Ark. Code Ann. § 11-9-410; Ga. Code Ann. § 34-9-11.1; Ky. Rev. Stat. Ann. § 342.700; Mont. Code Ann. § 39-71-412; N.M. Stat. Ann. § 52-5-17; Vt. Stat. Ann. tit. 23 § 624.

3 33 S.W.3d 161, 166 (Ark. 2000).

4 Ark. Code Ann. § 11-9-410.

5 *Gen. Accident Ins. Co. Of Am. v. Jaynes*, 33 S.W.3d 161,166 (Ark. 2000).

6 J.B. Hunt Transp., Inc. v. Knight, 2006 WL 2879457 *1 (Ark. Ct. App. Oct. 11, 2006).

7 This assessment was submitted to the administrative law judge (ALJ) without objection from the insurance carrier.

WHOSE MONEY...

$1.4 million to the employee; $236,938 to his spouse; and $470,000 to his minor children.

The employee contested the carrier's lien, arguing that he had not been "made whole" because he only received $1.4 million of his $1.8 million in damages. The Workers' Compensation Commission adopted the ALJ's determination that "[the carrier] was not allowed to assert its subrogation rights against a third-party settlement because [the employee] was not made whole by the settlement agreement."[8] Affirming the Commission's decision, the court of appeals rejected the carrier's primary argument that its lien was statutorily protected, citing *Jaynes*.[9]

Georgia courts are similarly protective of employees, holding that "the employer has no right of reimbursement [under the state's statutory workers' compensation lien] unless the employee has been fully compensated for his injuries, including both economic and non-economic damages."[10] And whether the employee has been fully compensated is determined by "the trial court and not a jury."[11]

In addition to the determination of whether an employee has been made whole being an entirely judicial decision, Georgia courts put substantive and procedural obstacles between the employee's recovery and the carrier's lien. For example, the carrier bears the burden of establishing that the employee has been wholly compensated[12] and courts cannot consider affirmative defenses like contributory negligence or assumption of the risk.[13] In addition, Georgia imposes the unique procedural burden of requiring the carrier to intervene in the claimant's tort action to protect and enforce its subrogation lien.[14] The carrier cannot simply wait and collect from the employee after settlement or adjudication of the third-party claim.

In Montana, the make-whole doctrine is a matter of constitutional right: "Montana's firm public policy disallows subrogation prior to full recovery by damaged parties. This is embodied in Article II, Section 16 of Montana's Constitution, and has been applied repeatedly by [the Montana Supreme Court.]"[15] And similar to Georgia, Montana does not decrease the value of an employee's loss by any comparative negligence.[16] As a countervailing factor, however, Montana does add the "amounts received and to be received under the workers' compensation claim . . . to the amounts otherwise received from third party claims . . . ."[17] In other words, a carrier can subrogate against a Montana employee's third-party recovery when the sum of the workers' compensation payment and the third-party recovery exceeds the amount necessary for the employee to be "made whole."

II. First-Monies States

Thirty-one states allow carriers to subrogate against the "first monies" recovered by the employee in a third-party settlement or judgment.[18] In these states, no consideration is given to whether the employee has been fully compensated or "made whole." Some states even deny the employee a right to recover transaction costs, whether they are attorneys' fees or collection costs generally.

A. First Monies, *Without* Deduction for Transaction Costs

Nineteen of the first-monies states allow the carrier to recover the totality of its payments from any employee third-party recovery, without deducting litigation costs. These states include: Alabama, Alaska, California, Colorado, Connecticut, Florida, Hawaii, Idaho, Maine, Mississippi, Nevada, New Jersey, Oregon, Pennsylvania, Rhode Island, Tennessee, Texas,

8 *J.B. Hunt Transp., Inc.*, 2006 WL 2879457, at *1.

9 *Id.* at *4 (citing *Jaynes*, 33 S.W.3d at 167).

10 Leigh Martin May and Geoffroy E. Pope, *The Nuts and Bolts of Reimbursement and Subrogation Issues*, *available at* http://www.butlerwooten.com/CM/Articles/Subrogation percent20gtla.pdf, last accessed March 11, 2009, (citing Canal Ins. Co. v. Liberty Mut. Ins. Co., 570 S.E.2d 60, 63-64 (Ga. Ct. App. 2002); Ga. Code Ann. § 34-9-11.1).

11 *Canal Ins.*, 570 S.E.2d at 65.

12 Hartford v. Federal Express, 559 S.E.2d 530, 532 (Ga. Ct. App. 2002) (holding insurer failed to prove complete compensation).

13 *Id.*

14 *Canal Ins.*, 570 S.E.2d at 63.

15 Oberson v. Federated Mut. Ins. Co., 126 P.3d 459, 462 (Mont. 2005).

16 State Fund v. McMillan, 31 P.3d 347, 349 (Mont. 2001).

17 *Id.*

18 Ala. Code § 25-5-11; Alaska Stat. § 20.30.015; Cal. Labor Code § 3852; Colo. Rev. Stat. § 8-41-203; Conn. Gen. Stat. § 31-293; Fla. Stat. § 440.39; Haw. Rev. Stat. § 386-8; Idaho Code Ann. § 72-211; Me. Rev. Stat. Ann. tit. 39-A, § 107; Md. Code Ann. Lab. & Empl. § 9-901 to 903; Miss. Code Ann. § 71-3-71; Nev. Rev. Stat. § 616C.215; N.J. Stat. Ann. § 34:15-40; Or. Rev. Stat. § 656.593; 77 Pa. Const. Stat. Ann. § 671; R.I. Gen. Laws § 28-29-1; Tenn. Code Ann. § 50-6-112; Tex. Labor Code Ann. §§ 417.001-417.004; Va. Code Ann. § 65.2-309; W. Va. Code Ann. S 23-2A-1; Ariz. Rev. Stat. Ann. § 23-1023(D); 19 Del. Code Ann. § 2363; 820 Ill. Comp. Stat. Ann. 305/5(b); Iowa Code § 85.22; Mass. Gen. Laws Ann. ch 152 § 15; Mich. Comp. Laws Ann. 418.827(5); N.H. Rev. Stat. Ann. § 281-A:13; N.D. Cent. Code § 65-01-09; S.D. Codified Laws § 62-4-38 to 40; Md. Code Ann. Lab. & Empl. § 9-901 to 903; N.Y. Workers' Comp. Law § 29.

Virginia, and West Virginia. The statutes in most of these states are very similar, if not identical, and do not require individual treatment. Instead, we discuss decisions from some particularly unequivocal courts to illustrate policy priorities in these states.

In Texas's view, allowing carriers to recover from the first monies received, without deduction, prevents double recovery and strengthens the workers' compensation system.[19] California's justification, on the other hand, focuses on the goal of rehabilitation, which it views as the underlying policy of workers' compensation schemes in general:

> [C]ompensation benefits . . . are not intended to make whole, persons who have suffered 'detriment from the unlawful acts or omission of another.' [U]nrelated to concepts of 'fault' or 'wrong,' benefits paid under the compensation system are ultimately tied to the notion that injured workers are to be compensated for their loss of competitive status in the labor market. The purpose of workers' compensation is to rehabilitate, not to indemnify.[20]

Similarly, most of these states also disallow deductions for the employer's negligence. Nevada's statute makes its policy behind this clear: "The injured employee . . . [is] not entitled to double recovery for the same injury, notwithstanding any act or omission of the employer or a person in the same employ which was a direct or proximate cause of the employee's injury."[21]

B. First Monies, *With* Deduction for Transaction Costs

Twelve of the first-monies states allow for a deduction for either litigation or attorneys' costs, generally referred to as transaction costs: Arizona, Delaware, Illinois, Iowa, Louisiana, Massachusetts, Maryland, Michigan, New Hampshire, North Dakota, South Dakota, and New York. Generally, this is done in one of four ways: (1) straight-line deduction of attorneys' fees; (2) pro-rata allocation of attorneys' fees; (3) a set percentage of the employee's recovery; or (4) a requirement that the carrier pay a certain amount of its own lien to the employee's attorney.

1. Straight-Line Deduction of Attorneys' Fees

Five states allow an employee to recoup some or all transaction costs before the carrier can collect on a first-monies lien: Arizona, Maryland, Iowa, New York, and Michigan. For example, Maryland's statute governing carriers' liens provides that "if the covered employee or the dependents of the covered employee recover damages, the covered employee or dependents . . . first, *may deduct the costs and expenses of the covered employee or dependents for the action . . .*"[22] Iowa, however, is slightly more restrictive than the others, because it only allows recovery for attorneys' fees.[23]

2. Pro Rata Allocation of Attorneys' Fees

Delaware, Massachusetts, and New Hampshire follow the *pro rata* method of apportioning transaction costs. Under the *pro rata* scheme, a carrier's recovery is reduced by the same proportion as the employee's recovery was reduced for the payment of attorneys' fees. In other words, if the employee's attorneys' fees totaled one-third of her recovery, the carrier's lien would also be reduced by one-third.[24] As one court rationalized, "Since the employee's award was reduced by one-third to pay his attorney, this Court held that the insurance company's reimbursement should also be reduced by one-third to achieve an equitable result."[25]

3. Statutorily Imposed Fees

Illinois and North Dakota impose a contingent fee on the carrier as a percentage of the carrier's recovery. Illinois requires the carrier to "pay his pro rata share of all costs and reasonably necessary expenses in connection with such third-party [actions] . . . ."[26] But if the "services of [the employee's] attorney . . . have resulted in or substantially contributed to the procurement by suit, settlement or otherwise of the proceeds . . . then in the absence of other agreement, the carrier shall pay such attorney 25% of the gross amount of such reimbursement."[27] In other words, once the carrier recovers all payments made to the employee, and in the absence of any other agreement, it will have to pay twenty-five percent of that reimbursement to the attorney. Theoretically, this decreases the employee's transaction costs on the front end of the third-party litigation. An

19 Tex. Mut. Ins. Co. v. Ledbetter, 251 S.W.3d 31, 35 (Tex. 2008).
20 Rodgers v. Workers' Comp. Appeals, 682 P.2d 1068, 1077 (Cal. 1984) (internal citation omitted).
21 Nev. Rev. Stat. § 616C.215.
22 Md. Code Ann. Lab. & Empl. § 9-902 (emphasis added).
23 Iowa Code § 85.22.
24 *See, e.g.*, Roadway Express v. Folk, 817 A.2d 772, 775 (Del. 2002) (internal citation omitted).
25 *Id.*
26 820 Ill. Comp. Stat. Ann. 305/5(b).
27 *Id.*

attorney could be willing to reduce his fees, because he or she knows that he or she will be entitled to twenty-five percent of whatever the employee has already received in benefits.

In North Dakota, carriers are liable for more than just attorneys' fees.[28] In fact, the statute divides "costs of the action" and "attorneys' fees" into separate categories.[29] The carrier is first liable for one-half of "all costs of the action, exclusive of attorneys' fees . . . before recovery of damages."[30] If the parties settle before judgment, the carrier must pay twenty-five percent of its recovery in attorneys' fees. If the employee is awarded a judgment either by a court or through ADR, then the carrier must pay "[33.3 percent] of the subrogation interest recovered for the organization . . . ."[31] This encourages early settlement without recourse to third-party neutrals and aggressively tackles the issue of transaction costs.

4. Caps on Carrier's Share of Fees

South Dakota caps the fees that carriers must pay when recouping workers' compensation payments at 35 percent of the compensation paid. Louisiana has a three-part formula, the third part of which caps attorneys' fees to a percentage of the carrier's recovery. Although, the statute provides for a "first dollar lien or privilege on the proceeds of the employee's recovery from a third person,"[32] it also reduces the carrier's recovery by the employer's comparative negligence.[33] Additionally, the carrier must bear its "proportionate share of attorney's fees and costs incurred in obtaining recovery from the third party, up to a limit of one third of its intervention."[34] Louisiana, therefore, combines elements of the three subrogation methods: first monies, reduction based on the employer's negligence, reduction for transaction costs, and a cap on those transaction costs.

III. Other Schemes

The remaining thirteen states fall along a spectrum of the above methods for apportioning employee recoveries.[35]

A. Reverse First Monies

Minnesota, Wisconsin, and Washington apply what we will call "reverse first monies." Generally, under a

28 N.D. Cent. Code § 65-01-09.

29 *Id*.

30 *Id*.

31 *Id*.

32 La. Rev. Stat. Ann. § 23:1101 to 1103.

33 *Id*.§ 23:1101(B).

34 *Id*. § 23:1103(c)(1).

35 Minn. Stat. § 176.061; Wis. Stat. Ann. § 102.29; Wash. Rev. Code Ann. § 51.24-060; Wyo. Stat. Ann. § 27-14-105(a); Ind. Code §§ 22-3-1-1, 34-51-2-19; Kan. Stat. Ann. § 44-

"reverse first monies" scheme, the reasonable costs associated with the third-party recovery are deducted from the gross settlement amount to obtain what we will call the "Adjusted Gross Recovery." The employee is then paid a fixed percentage of the Adjusted Gross Recovery. After the employee has been paid her fixed percentage, the carrier then recoups its payments from the remainder of the Adjusted Gross Recovery. If there are any funds remaining after the carrier has been reimbursed, that residual either goes to the employee or is used as an allowance to the employer for potential future payments.

B. First Monies with a Cap

Wyoming's scheme is unique. A carrier may recoup its payments up to one-third of the employee's third-party recovery. In other words, one-third, but no more, of the employee's third-party recovery is available to the carrier to recoup its payments.

C. Statutory Formulas

Indiana, Kansas, Missouri, Oklahoma, Utah, and Ohio all have varying methods or caveats to determine the extent of a carrier's subrogation rights. This section provides a brief overview of each method, as well as statutory references to facilitate further research.

1. Indiana

Indiana allows courts to consider the employer's negligence to diminish the carrier's recovery. The net effect is to protect the employee's recovery by reducing the carrier's claim on the proceeds. This particular statutory construction encourages carriers to participate in the suit and defend the employer's "good name" so as to minimize its share of comparative fault.

2. Kansas

Kansas's formula is similar to Indiana's in that it allows reduction of the carrier's recovery by an amount proportional to the employer's comparative negligence. The formula is as follows:

> [Subrogation Interest] – [[Total Recovery] x [Employer's Percentage Fault]] = [Carrier Recovery][36]

If the formula results in a negative number the carrier recovers nothing. This may well be the harshest application of the comparative-fault rule to a carrier's reimbursement lien for workers' compensation benefits.

3. Missouri and Oklahoma

Missouri's scheme is similar to a first-monies scheme with an attorneys' fees deduction. But it has a second step that splits the recovery proportionally:

> (1) the expenses of the third party litigation should be deducted from the third party recovery; (2) the balance should be apportioned in the same ratio that the amount paid by the employer at the time of the third party recovery bears to the total amount recovered from the third party . . . .[37]
>
> For example, assume the carrier paid the employee $100,000, and the employee recovered $500,000 from a third-party. The employee's "expenses" totaled $50,000. The employee at that point is left with $450,000.Twenty percent of that (100,000/500,000 = 1/5 = 20 percent) goes to the carrier, so the carrier will receive $90,000. Oklahoma uses this formula as well.[38]

4. Utah

Under Utah's scheme, the "reasonable expense of the action . . . shall be paid and charged proportionately against the parties . . . ."[39] After the deduction of transaction costs, the carrier's lien may be reduced by the percentage of the employer's fault; however, if third parties are more than 60 percent at fault, then there is no reduction for the employer's fault.[40]

5. Ohio

In Ohio, the employee receives an "amount equal to the uncompensated damages divided by the sum of the subrogation interest plus the uncompensated damages, multiplied by the net amount recovered."[41] The carrier receives "an amount equal to the subrogation interest divided by the sum of the subrogation interest plus the uncompensated damages, multiplied by the net amount recovered."[42]

504; Mo. Rev. Stat. § 287.150; Okla. Stat. tit. 85, § 44; Utah Code Ann. § 34 A-2-106; Ohio Rev. Code Ann. § 4123.931(B) for settlement and § 4123.931(D) for trial; N.C. Gen. Stat. § 97-10.2; S.C. Code Ann. § 42-1-560; Neb. Rev. Stat. § 48-118.

36 Enfield v. A.B. Chance Co., 228 F.3d 1245, 1251-52 (10th Cir. 2000) (citing Brabander v. W. Co-op Elec., 811 P.2d 1216, 1219 (Kan. 1991).

37 Ruediger v. Kallmeyer Bros. Serv., 501 S.W.2d 56, 59 (Mo. 1973) (applying Mo. Rev. Stat. § 287.150).

38 *See* Okla. Stat. tit. 85, § 44I.

39 Utah Code Ann. § 34 A-2-106(5)(a).

40 *Id*.§ 34 A-2-106(5)(b)(1).

41 Ohio Rev. Code Ann. § 4123.931(B) for settlement and § 4123.931(D) for trial.

42 *Id*.

D. Third-Party Neutral Determination of the Appropriate Carrier Recovery

North Carolina, South Carolina, and Nebraska are in a category of their own because their statutes establish proportional apportionment between the insurance carrier and the employee by a third-party neutral. For example, in North Carolina a judge determines the carrier's lien, and can take into account the litigation costs.[43] The statute provides the judge with guidelines regarding calculation but not a formula.[44] Nebraska similarly allows the parties to apply to the court for a "fair and equitable distribution of the proceeds of any judgment or settlement" if they cannot come to an agreement.[45]

Under South Carolina's scheme, the Workers' Compensation Commission determines the carrier's recovery.[46] The Commission, however, is only entitled to decrease the carrier's lien in proportion to what the Commission considers to be the employee's actual damages.[47] Thus, if the employee was under-compensated by a jury, the Commission can compensate for that by disallowing a portion of the carrier's lien.

IV. Summary

Carriers in all fifty states have some right to obtain a lien on an employee's third-party recovery, but there are varying methods of calculating the value of the lien. As the following chart demonstrates, most states use one of two schemes: first-monies or make whole. The remainder uses some combination of those two primary schemes, or leaves the determination of the value to a third-party neutral.

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See Figure 2 on page 7.

43 N.C. Gen. Stat. § 97-10.2(j).
44 *Id.*
45 Neb. Rev. Stat. § 48-118. *See also* Turco v. Schuning, 716 N.W.2d 415, 417-18 (Neb. 2006).
46 S.C. Code Ann. § 42-1-560.
47 *Id.*

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After Paying Workers' Compensation Benefits

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Illustrations

MAKE WHOLE	• Arkansas • Georgia • Kentucky		• Montana • New Mexico • Vermont	
FIRST MONIES	**Reduction for transaction costs/attorneys' fees** • Arizona • Delaware • Illinois • Iowa • Louisiana • Maryland • Massachusetts • Michigan • New Hampshire • New York • North Dakota • South Dakota		**No reduction for transaction costs/attorneys' fees** • Alabama • Alaska • California • Colorado • Connecticut • Florida • Hawaii • Idaho • Maine • Mississippi • Nevada • New Jersey • Oregon • Pennsylvania • Rhode Island • Tennessee • Texas • Virginia • West Virginia	
OTHER SCHEMES	**Reverse first monies** • Minnesota • Washington • Wisconsin.	**First monies with a cap** • Wyoming	**Statutory formulas** • Indiana • Kansas • Missouri • Oklahoma • Utah • Ohio	**Third-party neutral determination of the appropriate carrier recovery** • Nebraska • North Carolina • South Carolina

Figure 1.

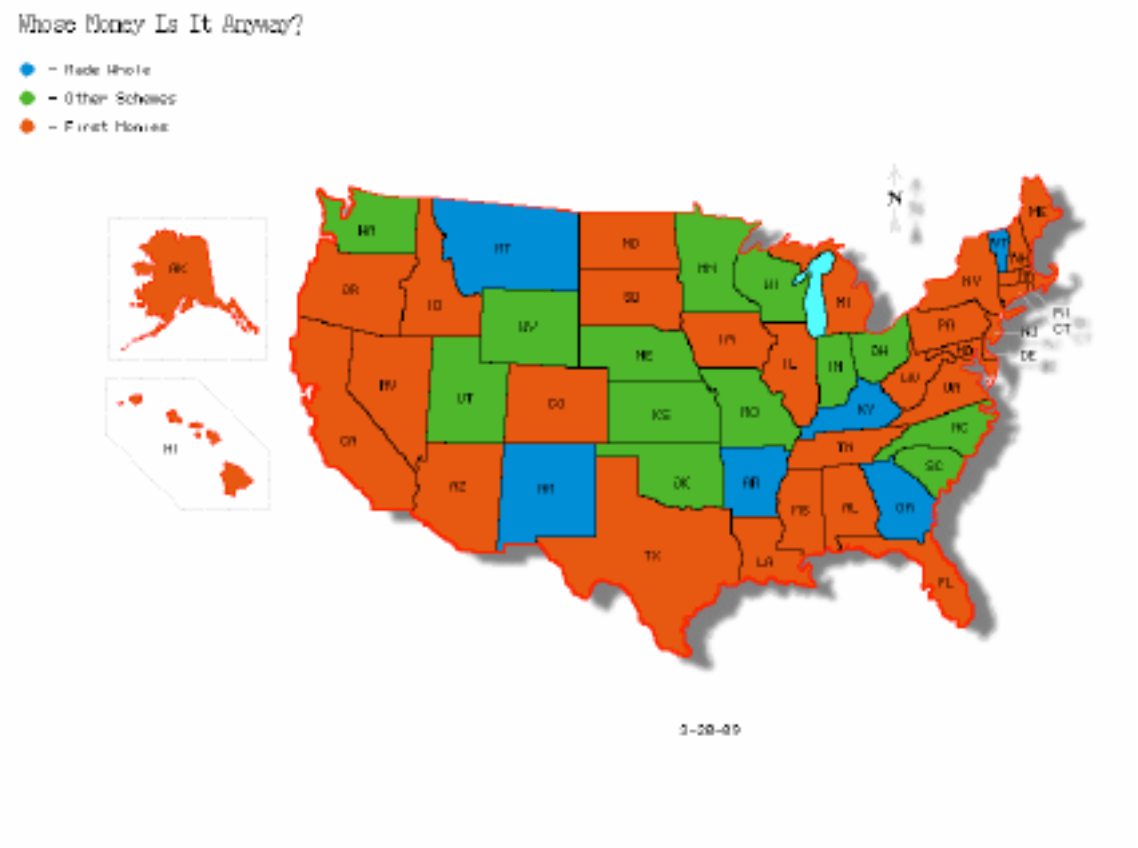

Figure 2.