JOINT PURSUIT OF RECOVERY WITH AN INSURED: ISSUES FOR THE SUBROGATING CARRIER TO CONSIDER

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The subrogation claim of an insurance carrier does not always include all the damages incurred by an insured which are potentially recoverable from responsible parties as a result of the loss. The insured may possess a claim in addition to the subrogation claim if the policy included a deductible or if the insured incurred damages outside the scope of coverage provided by the policy. Concurrent pursuit of recovery by the subrogating carrier and the insured can yield benefits for both the carrier and the insured. However, not every case is appropriate for joint representation. Jointly pursuing recovery of both the subrogation claim and the uninsured loss involves certain issues that must be addressed at the outset of the joint recovery effort so that the advantages of the joint recovery effort can be fully realized and the potential dangers avoided.

Both the subrogating carrier and the insured become actual clients of counsel in a joint recovery effort. Conflicts may arise between the subrogating carrier and the insured when their interests differ. The conflicts may present obstacles to, or delay, recovery from a responsible third party. As the duty of loyalty prevents an attorney from concurrently representing clients with adverse interests in the same matter without an informed and written waiver, these potential conflicts of interests and other issues must be addressed in writing by the subrogating carrier and the insured prior to commencing the joint recovery effort, and by counsel prior to undertaking the concurrent representation. One highly effective method of addressing these issues is the execution of a joint representation and proration agreement.

In California, an insured is the real party in interest with respect to any damages outside the scope of payments made by the subrogating carrier, including any deductible. Therefore, both the insured and the subrogating insurer are considered real parties-in-interest when an
insurer has paid only a part of an insured’s loss. Counsel for the subrogating carrier may not pursue recovery of any portion of the insured’s loss, including the deductible, without obtaining permission from both the insured and the subrogating carrier. In pursuing recovery of any portion of the insured’s uninsured loss, the insured is an actual client of the attorney and all the typical duties and obligations of the lawyer to the client arise in this relationship. An insurer who has not fully compensated an insured for a loss cannot commence an action in the name of its insured without the execution of an agreement authorizing the insurer to sue in the name of the insured. An insurer must obtain authorization to commence an action in the name of an insured even when the uninsured loss consists of a deductible only.

Jointly pursuing recovery of a subrogation claim and an uninsured loss may necessitate two (2) independent agreements being reached before recovery efforts can be undertaken.

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2 In Arizona, Nevada, and Utah, whether an insurer can litigate its subrogation action in the name of the insured is dependent on whether the insurer has paid part of the loss, versus the insured’s entire loss. If the insurer is only partially subrogated (i.e., only part of insured’s loss has been paid), both insurer and insured are real parties in interests, and an insurer may sue in the insured’s name. However, if the insurer has paid the insured’s entire loss, insurer is the only "real party in interest" and must sue in its own name. Hamman-McFarland Lumber Co. (Ariz.App. 1972) 492 P.2d 437, 439; Central National Insurance Co. v. Dizon (1977) 93 Nev. 86, 559 P.2d 1187; Duboise v. State Farm Mutual Automobile Insurance Co. (1980) 96 Nev. 877, 619 P.2d 1223, 1224; Transamerica Insurance co. v. Barnes (Utah 1972) 505 P.2d 783, 786. Idaho has yet to address this issue.

3 In Arizona and Nevada, an insurer is not required to add an insured’s deductible or uninsured loss to its subrogation action; maintaining two separate suits (i.e., one by insured and another by insurer) is not considered a "splitting of actions." Commercial Union Insurance Co. v. Lewis & Roca (1995) 183 Ariz. 250, 902 P.2d 1354; Smith v. Hutchins (1977) 93 Nev. 43, 566 P.2d 1136.
Although these agreements may be independent, they may be executed together within one
document, such as a joint representation and proration agreement. The first agreement is an
agreement between the insured and the subrogating carrier. The second agreement is the
agreement between counsel and the insured to address the formation of the attorney-client
relationship. Pursuant to a joint representation and proration agreement, the subrogating carrier
and the insured agree, among other things (1) to concurrent representation by counsel, (2) as to
their respective rights and obligations in the, litigation, and, (3) as to their respective rights to
any recovery obtained. Such an agreement should reduce or eliminate the potential for the
interests of the carrier and the insured to become adverse during the recovery effort and avoid
potential conflicts of interest developing for counsel. Such an agreement helps to avoid
disagreements during litigation that could jeopardize or delay settlement of the claim and
recovery.

The fact that an insured and a subrogating carrier may both have a claim against a third
party for damages arising from a loss does not necessarily mean that their interests will be
identical in any action to recover the damages. Although the subrogating carrier may technically
“stand in the shoes” of its insured, the interests of the subrogating carrier I and the insured can
easily, and frequently do, become adverse in a recovery effort, especially when the available
funds from which recovery may be obtained are substantially less than the damages incurred. A
conflict may also arise between the carrier and the insured as to the damages actually provable
and/or recoverable by each. A conflict may arise between the carrier and the insured as to which
has the priority interest in any recovery. Both Idaho and California maintain the general rule that an insurer is entitled to be "made whole" first out of any recovery from a third party, and the insured is entitled to any remaining balance. Cedarholm v. State Farm Mut., Ins. Co. (Idaho 1959) 338 P.2d 93; Travelers Indem.
joint recovery effort may ensure that actual conflicts do not develop which force the parties into adversarial positions and destroy the joint recovery effort. Addressing the potential conflicts at the outset of the recovery effort aids in ensuring that the benefits of the joint effort are fully realized.

The benefits of jointly pursuing a recovery effort may flow to both the subrogating carrier and the insured. A joint recovery effort may permit the carrier to pursue recovery in the name of the insured. Maintaining the action in the name of the insured only, may help to avoid possible juror bias against an insurance company and take advantage of possible juror sympathy or empathy toward the actual injured party. Prejudice against insurance companies has been known to reduce damage awards by juries in actions involving insurance companies as named plaintiffs. Additionally, joint recovery efforts may help to facilitate or ensure cooperation of the insured during litigation and at trial. The subrogating carrier may also decrease its cost burden in a joint recovery effort as the insured may be responsible for satisfying from any recovery, its pro-rata share of costs incurred in the recovery effort.

A joint recovery effort may benefit an insured by allowing the insured to pursue recovery of an uninsured loss without incurring, up front, the potentially onerous costs and expenses of litigation. The significant costs and expenses of litigation deter many insureds from pursuing recovery of small uninsured losses. A joint recovery effort does not usually cause the subrogating carrier to incur additional costs as the subrogating carrier would expect to incur the costs regardless of the insured’s involvement in the recovery effort. The subrogating carrier may be able to obtain reimbursement for the insured’s pro-rata share of the costs incurred in the event

Cal.App4th 533 (insured allowed first recovery where no subrogation agreement was executed assigning insurer all rights, claims, demands and interests which insured had against any party responsible for the loss, and where insurer did not assist in insured’s legal representation). However, Arizona, Nevada and New Mexico have yet to address this recovery issue.
of any recovery by the insured. Although a joint representation proration agreement may provide otherwise, the insured may not be responsible for any out of pocket costs during the course of litigation, but may only be responsible for its pro-rata share of fees and costs when recovery is obtained.

A joint recovery effort, however, is not without dangers. As discussed previously, conflicts can develop between the subrogating carrier and the insured forcing the parties into adversarial positions. It is imperative that the potential for such conflicts be addressed at the outset of the joint recovery effort. For example, a fire loss may result in a Four Hundred Thousand Dollar ($400,000.00) subrogation claim and a Three Hundred Thousand Dollar ($300,000.00) uninsured claim against a third party. If the third party offers the limits of a Five Hundred Thousand Dollar ($500,000.00) liability policy and has no other assets from which recovery may be obtained, an adversarial relationship may be created between the subrogating carrier and the insured unless a prior agreement has been reached as to how such recovery will be apportioned and who has ultimate control over settlement. Another adversarial situation could be created if a third party with insurance sufficient to cover the entire loss disputes the amount of the uninsured loss. For example, if the third party offers Four Hundred Thousand Dollars ($400,000.00) to the subrogating carrier and only Fifty Thousand Dollars ($50,000.00) to the insured while requiring that any settlement involve all parties and completely resolve all claims, a conflict may arise. Both situations can create obstacles to recovery or may result in delayed recovery. Both situations can result in disqualification of the attorney handling the concurrent representation due to the development of a conflict of interest. The disqualification of counsel can result in additional costs and expenses for all parties involved.

The potential conflicts and other issues which must be addressed prior to a joint recovery effort can be addressed through a joint representation and proration agreement executed by both
the subrogating carrier and the insured. The agreement should set forth the specific understanding of the parties regarding the joint recovery effort in detail. The agreement should describe and/or address the following issues:

- Authority for the attorney to represent the insured;
- Which party has ultimate settlement authority;
- Responsibility for payment of costs and expenses incurred in litigation (the carrier may front all costs and recoup the insured’s pro-rata share from any recovery);
- The apportionment of any recovery;
- The apportionment of any interest recovered;
- A provision to the effect that, if the case proceeds to a jury verdict, the jury verdict will determine each party’s respective right to recovery;
- The effect of any determination, as a matter of law, that any portion of either party’s claimed damages are not recoverable.

The agreement should address all potential conflicts that could arise between the insurer and the insured as well as address all contingencies that might arise during the course of the recovery effort. Such issues include responsibility for attorney’s fees, costs of litigation, non-recoverability of claimed damages, punitive damages, settlement authority, and duties of defending against counterclaims. A joint representation agreement can prevent disputes over the distribution of recovery proceeds and the sharing of expenses. A joint representation agreement should explicitly define the priority of recovery.
Both subrogation receipts and loan receipts constitute written attempts to define the rights and obligations of the insurer/subrogee and the insured/subrogor with regard to indemnification from the actual wrongdoer. However, litigation agreements, such as joint representation and proration agreements, are usually broader in scope than standard subrogation receipts or loan receipts and specifically control the relationship between counsel, the subrogating carrier and the insured. A joint representation/proration agreement can accomplish the limited purposes of subrogation loan receipts and the broader purposes of litigation agreements.

The joint representation agreement must clearly and accurately define the intent of the parties to the agreement. The agreement operates as a guideline and control device throughout the course of the recovery effort. A sample joint representation agreement accompanies this paper.

A joint recover effort can yield benefit for the parties involved. However, care must be taken to ensure that the potential conflicts inherent in joint recovery efforts are avoided. Importantly, the insured’s consent to the agreement must be informed consent. The insured must be clearly advised as to how the agreement may affect his or her rights and be allowed the opportunity to consult another lawyer, should he or she desire, with respect to the agreement.
SAMPLE

PRORATION AGREEMENT

This AGREEMENT is entered into this _ day of _, 1998, by and between the Subrogating Carrier Insurance Company ("Subrogating Carrier") and the Insured Company, Inc. ("Insured").

WHEREAS, Subrogating Carrier insured the structures owned by the Insured at the property addressed as 100 Main Street in Niceview, California ("subject property"). On or about July 3, 1992, a fire occurred at the subject property. Total damages arising from the fire have been determined to be $100,000.00. Subrogating Carrier made payment to the Insured in the amount of $90,000.00, which represents 90% of the total damages now believed to have been sustained by the Insured as a result of the fire.

WHEREAS, the Insured sustained loss not covered by insurance as a result of the fire in the amount of $10,000.00, or 10% of the total damages now believed to have been sustained by the Insured as a result of the fire.

WHEREAS, the cause of the fire and the resulting damages sustained by the Insured and Subrogating Carrier were due to the acts and omissions of third parties and, as a result thereof, Subrogating Carrier has exercised its subrogation rights with respect to its payments to the Insured and Subrogating Carrier will institute an action in the name of the Insured Company, Inc. to recover the total insured and uninsured damages from those persons or entities believed responsible for the fire and resultant damage.

WHEREAS, the parties hereto wish to resolve between themselves the further handling of such action, their rights and responsibilities with respect to such action, and with respect to

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This sample contains examples of provisions you may wish to use subject to negotiation with the insured.
any recoveries made in such action. Such action will be filed in the Superior Court of the State of California, County of Niceview.

NOW, THEREFORE, Subrogating Carrier and the Insured Company, Inc., with respect to the legal action identified herein, agree to the following Proration Agreement with other terms and conditions:

1. Except as may be adjusted pursuant to Paragraphs 4 and 5 below, Subrogating Carrier shall have a 90% interest in any recovery from such legal action after deduction of attorney’s fees.

2. Except as may be adjusted pursuant to Paragraphs 4 and 5 below, the Insured shall have a 10% interest in any recovery from such action after deduction of attorney’s fees.

3. For the purposes of this Proration Agreement, including preceding paragraphs 1 and 2, attorneys’ fees are defined as 33 1/3% (1/3) of any gross recovery prior to the deduction of the reasonable costs and expenses of litigation.

4. Any monies actually recovered shall be applied first to the parties’ compensatory damage claims and then to any award of interest. Subrogating Carrier’s pro-rata interest in all recoveries shall be 90% until such time that its interest (prior to the deduction of attorney’s fees and costs and expenses of litigation) equals the amount paid to the Insured under the policy (or such lesser amount as determined pursuant to Paragraph 5 below), plus interest (if recovered). The Insured shall receive 100% of any additional recovery, and Subrogating Carrier and the Insured’s pro-rata share of costs and expenses of litigation shall be adjusted to reflect the actual recovery by each party.
5. In the event that any portion of the damage claimed by the respective parties hereto is not recoverable as a matter of law, the pro-rata apportionment shall be redetermined. In the event of trial, the jury verdict will determine the parties’ respective interests with respect to each element of damages. Any reduction in interest will only become final upon either the written agreement of the parties or a final, nonappealable order. The costs and expenses of appeal from any final order reducing such party’s interest, however, shall be borne solely by the party adversely affected.

6. Subrogating Carrier shall have the absolute and unconditional right and discretion to enter into any settlement it deems advisable with respect to the above action, subject only to the right of the Insured to recover its pro-rata interest in such settlement.

7. Subrogating Carrier will initially be responsible for all costs and expenses of litigation but, in the event of a recovery with respect to the Insured’s interest as defined herein, the Insured will be responsible to reimburse Subrogating Carrier its pro-rata share (10%) of the reasonable costs and expenses incurred. However, the Insured will not be responsible to reimburse Subrogating Carrier an amount greater than its 10% interest in the recovery after the deduction of attorneys’ fees.

8. Subrogating Carrier agrees that, in the event it elects to withdraw its damage claims, it will continue to cooperate with the Insured in the Insured’s prosecution of its uninsured damage claim by providing to the Insured documents from Subrogating Carrier’s file pertaining to the loss, but it is agreed that Subrogating Carrier will not be responsible for any costs or expenses of litigation incurred by the Insured after the withdrawal of Subrogating Carrier’s damage claims.
9. Subrogating Carrier has the right, if it so chooses, to retain separate legal counsel to represent its interest in the litigation above-described. If it so chooses, Subrogating Carrier shall be solely responsible for its own counsel’s attorney’s fees and in no event shall such attorney’s fees be included within the costs and expenses of litigation to be shared by the parties as set forth herein. Subrogating Carrier has elected not to engage separate counsel, and the Insured and Subrogating Carrier agree that the law firm of Cozen and O’Connor will represent their joint interests as described herein.

THIS AGREEMENT constitutes the entire agreement between Subrogating Carrier and the Insured with respect to the handling of the legal action identified herein and may be executed in counterpart or duplicate. The parties hereto have been advised by counsel as to the contents of this AGREEMENT, and, intending to be legally bound thereby hereunto set their hands.

DATED:_______________________ SUBROGATING CARRIER INSURANCE COMPANY

BY:___________________________

DATED:_______________________ INSURED COMPANY, INC.

BY:___________________________