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WHOSE FIRST DOLLAR IS IT, ANYWAY ?

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One of the issues forever vexing insurers, insureds and counsel is the distribution of a subrogation recovery which amounts to less than the total loss. To the chagrin of the insurance industry, a cursory review of Sapiano v. Williamsburg Nat. Ins. Co. (1994) 28 Cal.App.4th 533 appears to entitle the insured to first dollar recovery, up to the full amount of its loss. A more careful analysis of the Sapiano decision suggests that its impact on subrogating carriers will generally be much less onerous.

The Sapiano case arose from a motor vehicle accident. The collision occurred when a vehicle owned by Anthony R. Sapiano collided with an automobile negligently stopped on the freeway by another driver.

The fair market value of Sapiano's vehicle at the time of the collision was \$20,000. Pursuant to a first party policy of insurance, Williamsburg National Insurance Company paid Sapiano \$14,500 for the damage to that vehicle. That amount represented the policy limits of \$15,000, less the applicable \$500 deductible.

Sapiano subsequently filed suit for personal injuries and property damage against the responsible third party. The personal injury aspect of that suit was settled for the liability policy limits of \$15,000.

Sapiano was offered policy limits of \$10,000 for the property damage portion of his case. That settlement was derailed when Williamsburg asserted that its subrogation rights were paramount to the interests of Sapiano with respect to those proceeds.

The basis for Williamsburg's claim was a subrogation clause in its policy which contractually obligated the insured to transfer all rights to recovery against third parties. Sapiano challenged the applicability of that provision, contending that Williamsburg had no right to any recovery until Sapiano was made whole for his property damage loss.

In order to break the logjam, Sapiano instituted a declaratory relief action against Williamsburg. That action sought a judicial interpretation of the subrogation clause.

The trial court ruled in favor of Sapiano. The court's rationale was that an insurer cannot assert a contractual right to repayment from the insured when the total amount available from insurance and third party tortfeasors is insufficient to compensate the insured for the full loss.

The Sapiano court commenced its analysis by reviewing the historical underpinnings of the subrogation doctrine. Recognizing subrogation's equitable origins, the Sapiano court noted that California cases consistently applied the general rule that a subrogee may not enforce its claim until its insured is completely made whole.

Williamsburg attempted to distinguish the general rule on the grounds that it was attempting to assert “conventional” subrogation, arising from its contractual provision, rather than “legal” or “equitable” subrogation. The Sapiano court was unmoved by that distinction, relying upon well-established authority for the proposition that the general rule applies to conventional as well as legal subrogation unless the contract by which such right is created provides otherwise.

The Sapiano court acknowledged that the parties to an insurance contract could explicitly provide in their policy that the insurer has a priority regardless of whether the insured is first made whole. Such a priority was recognized in Samura v. Kaiser Foundation Health Plan, Inc. (1993) 17 Cal.App.4th 1284 wherein a health plan agreement specifically provided for subrogation upon payment, regardless of whether the total amount of recovery by the health plan member was less than the actual loss suffered.

Finally, the Sapiano court factually distinguished Travelers Indem. Co. v. Ingebretsen (1974) 38 Cal.App.3d 858, the only authority cited by Williamsburg for the proposition that an insurer was entitled to be subrogated to a recovery against a wrongdoer without regard to whether the insured had first been made whole. The Travelers case was held to be inapposite on two separate grounds.

First, the Sapiano court emphasized that in Travelers a detailed subrogation agreement had been executed pursuant to which the carrier had been assigned all rights, claims, demands and interests which the insured had against any party responsible for the loss. The Sapiano court also noted that the insurer’s attorneys in Travelers had assisted the insured’s attorneys and had borne a portion of the expenses in the third party litigation. Conversely, Williamsburg had not assisted Sapiano during the prosecution of the third party case. Williamsburg only sought to become actively involved after Sapiano had negotiated a proposed settlement. The inequity inherent in such conduct was readily apparent to the Sapiano court.

The Sapiano decision, although at first blush harsh to subrogating carriers, does not represent a departure from long-settled California law. Insureds have traditionally been entitled to recover the full amount of their loss prior to any recovery by their insurers. In order to vigilantly protect their subrogation rights, insurers should take the following steps:

First, insurers must be mindful of the language contained in the subrogation clause of their policy. Such language must be as specific as possible with respect to the rights of the insurer to pursue subrogation regardless of whether their insured is first made whole. Any ambiguity in such a provision will be strictly construed against the insurer, precluding subrogation until the insured is made whole.

Secondly, insurers must obtain subrogation receipts from their insureds. Such subrogation receipts should expressly and unambiguously assign and transfer to the carrier all rights, title and interest of the insureds to any third party recovery.

Finally, insurers must promptly and actively pursue their subrogation rights. Perhaps the most enduring lesson of Sapiano is that “he who hesitates to subrogate is lost.”