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Insurance Law

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INSURANCE LAW

I. INTRODUCTION

During the survey period, January 31, 1988, through August 1, 1989, the New Mexico judiciary addressed insurance law issues relating to the general areas of procedure[1] and coverage.[2] In addition, the court of appeals considered the rights of an insurer under subrogation principles.[3] In administrative law, the supreme court addressed issues regarding the powers of the Superintendent of Insurance vis-a-vis the Insurance Board and due process rights of a rate service organization in a rate-making hearing.[4] The supreme court also decided a bad faith action involving the failure to pay a first-party claim.[5] Finally, the court of appeals considered whether a common law negligence action was preempted by ERISA.[6]

II. PROCEDURE

Three cases decided by the courts involved procedural issues. The supreme court examined the relationship between the Uniform Arbitration Act[7] and the Declaratory Judgment Act[8] and considered whether an action was time-barred under the Hospital Lien Act.[9] The court of appeals addressed the preliminary procedural issue of its subject matter jurisdiction to determine an uninsured motorist dispute.[10]

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1. Guaranty Nat'l Ins. Co. v. Valdez, 107 N.M. 764, 764 P.2d 1322 (1988) (relationship between Uniform Arbitration Act and Declaratory Judgment Act), *see infra* notes 11-53 and accompanying text; Regents of Univ. of N.M. v. Lacey, 107 N.M. 742, 764 P.2d 873 (1988) (Hospital Lien Act), *see infra* notes 54-87 and accompanying text; State Farm Mut. Auto Ins. Co. v. Maidment, 107 N.M. 568, 761 P.2d 446 (Ct. App.), *cert. denied*, 107 N.M. 413, 759 P.2d 200 (1988) (subject matter jurisdiction), *see infra* notes 88-96 and accompanying text.

2. State Farm Mut. Auto Ins. Co. v. Maidment, 107 N.M. 568, 761 P.2d 446 (uninsured motorist/punitive damages), *see infra* notes 270-308 and accompanying text; Castorena v. Colonial Life & Accident Ins. Co., 107 N.M. 460, 760 P.2d 152 (1988) (exclusionary provision), *see infra* notes 101-18 and accompanying text; Jimenez v. Foundation Reserve Ins. Co., 107 N.M. 322, 757 P.2d 792 (1988) (underinsured motorist/stacking), *see infra* notes 224-48 and accompanying text; Amoco Prod. Co. v. Action Well Serv., 107 N.M. 208, 755 P.2d 52 (1988) (anti-indemnity statute), *see infra* notes 309-32 and accompanying text; Allstate Ins. Co. v. Graham, 106 N.M. 779, 750 P.2d 1105 (1988) (uninsured motorist/definition of "occupants"), *see infra* notes 249-69 and accompanying text; Morro v. Farmers Ins. Group, 106 N.M. 669, 748 P.2d 512 (1988) (underinsured motorist/stacking), *see infra* notes 206-23 and accompanying text.

3. Farmers Ins. Group v. Martinez, 107 N.M. 82, 752 P.2d 797 (Ct. App. 1988). *See infra* notes 333-60 and accompanying text.

4. National Council on Compensation Ins. v. New Mexico St. Corp. Comm'n, 107 N.M. 278, 756 P.2d 558 (1988). This case is not treated in this article. A full treatment of this case will appear in Survey, *Administrative Law*, 21 N.M.L. REV. ____ (1991).

5. Jessen v. National Excess Ins. Co., 108 N.M. 625, 776 P.2d 1244 (1989). *See infra* notes 365-417 and accompanying text.

6. Sappington v. Covington, 108 N.M. 155, 768 P.2d 354 (Ct. App. 1988). *See infra* notes 418-41 and accompanying text.

7. N.M. STAT. ANN. §§ 44-7-1 to -22 (1978).

8. *Id.* §§ 44-6-1 to -15 (1978).

9. *Id.* §§ 48-8-1 to 48-8-6 (Repl. Pamp. 1987).

10. State Farm Mut. Auto Ins. Co. v. Maidment, 107 N.M. 568, 761 P.2d 446 (Ct. App.), *cert. denied*, 107 N.M. 413, 759 P.2d 700 (1988).

A. *Arbitration and Declaratory Judgment*

In *Guaranty National Insurance Company v. Valdez*,[11] the supreme court reviewed a trial court's exercise of discretion to grant declaratory relief when an insurance policy provides for arbitration.[12] Valdez was injured by an underinsured motorist while driving his grandfather's car.[13] The grandfather had two automobile insurance policies with Guaranty for two separate cars.[14] Only one of these policies covered the car involved in the accident.[15] The insurance policy contained the following arbitration provision: "Determination as to whether an insured person is legally entitled to recover damages or the amount of damages shall be made by agreement between the insured person and us. If no agreement is reached, the decision will be made by arbitration."[16] Guaranty sought declaratory relief on four grounds.[17] Valdez responded with a motion to dismiss asserting that the arbitration provision of the insurance contract was applicable, and that the claim should go through arbitration alone.[18] The trial court granted the motion to dismiss.[19]

On appeal, Guaranty argued that another provision of the insurance contract applied,[20] and only the issues of liability and damages, not issues of coverage, were subject to arbitration.[21] Valdez countered that Guaranty was reading the provision out of context and that the coverage issues of "stacking" and "offset of benefits" were subject to arbitration.[22] To resolve the dispute, the court examined the relationship between the Uniform Arbitration Act[23] and the Declaratory Judgment Act.[24]

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11. 107 N.M. 764, 764 P.2d 1322 (1988).
12. *Id.* at 765, 764 P.2d at 1323.
13. *Id.*
14. *Id.*
15. *Id.*
16. *Id.*
17. *Id.* The grounds for declaration were:
    1. That Valdez was covered by only one of the two automobile insurance policies of his grandfather.
    2. That the limits of liability were the same under the policy for the grandfather's wrecked vehicle and under the tortfeasor's policy.
    3. That Valdez was not entitled to underinsured motorist coverage.
    4. That Guaranty owed Valdez nothing, under either policy provision.

Id.
18. *Id.*
19. *Id.*
20. *Id.* at 766, 764 P.2d at 1324. The provision as reproduced in the opinion stated:
    If an insured person and we do not agree
    (1) that the person is legally entitled to recover damages from the owner or operator of an uninsured motor vehicle, or
    (2) as to the amount of payment under this Part, then upon written demand of either, the issue shall be settled by arbitration in accordance with the rules of the American Arbitration Association, and judgement upon the award rendered by the arbitrators may be entered in any court having jurisdiction thereof. The insured person and we each agree to consider ourselves bound and to be bound by any award made by the arbitrators pursuant to this coverage.
21. *Id.*
22. *Id.*
23. N.M. STAT. ANN. §§ 44-7-1 to -22 (1978).
24. *Id.* §§ 44-6-1 to -15 (1978).

The standard of review of the trial court's exercise of discretion to refuse or grant declaratory relief is whether such discretion was based on good reason.[25] Good reason is determined by whether the court's discretion was "liberally exercised to effectuate the purposes of the [declaratory judgment] statute."[26] The statutory purpose, in turn, is "to settle and afford relief from uncertainty and insecurity with respect to other legal relations, and to be liberally construed and administered."[27]

The supreme court held that the trial court did not exercise good reason by refusing to consider Guaranty's complaint for declaratory judgment.[28] Following *Gonzales v. United Southwest National Bank*,[29] the court found that the complaint for declaratory judgment raised questions of law arising from the disputed interpretation of an arbitration contract, and thus the proper forum for resolution was the trial court.[30] Further, the court held that although questions of law can be arbitrated, if one party resists arbitration and seeks determination of the legal issue in court, then that party must be heard in court.[31] Although a party waives his rights to traditional procedural safeguards and to traditional appeals when it agrees to arbitration, the right of a party who contends that a particular issue is not arbitrable and who seeks pre-arbitration judicial review of the issue may not be denied.[32]

The holding reflects the court's misgivings about the limited scope of judicial review of an arbitration award. An arbitration award may not be vacated on grounds that the relief granted by the arbitrator would not be granted in judicial adjudications.[33] The court stated it opposed the language of New Mexico's version of the Uniform Arbitration Act limiting judicial review because it deprives a party of his or her right to the traditional safeguards afforded to parties who appeal judgments of a trial court.[34] In addition, the court noted that in the federal context, the United States Supreme Court criticized arbitration because arbitrators become the sole decisionmakers on questions of fault and are not bound by the rules of evidence.[35]

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25. *Valdez*, 107 N.M. at 766, 764 P.2d at 1324 (citing Sunwest Bank of Clovis v. Clovis IV, 106 N.M. 149, 154, 740 P.2d 699, 704 (1987)). A trial court may exercise discretion to grant or refuse declaratory relief under section 44-6-7 of the Declaratory Judgment Act. Section 44-6-7 provides that "[t]he court may refuse to render or enter a declaratory judgment or decree where such judgment or decree, if rendered or entered, would not terminate the uncertainty or controversy giving rise to the proceeding." N.M. STAT. ANN. § 44-6-7 (1978).

26. National Liberty Ins. Co. of Am. v. Silva, 43 N.M. 283, 289, 92 P.2d 161, 167 (1939).

27. N.M. STAT. ANN. § 44-4-14 (1978).

28. *Valdez*, 107 N.M. at 766, 764 P.2d at 1324.

29. 93 N.M. 522, 602 P.2d 619 (1979).

30. *Valdez*, 107 N.M. at 766, 764 P.2d at 1324.

31. *Id.*

32. *Id.* at 767, 764 P.2d at 1325.

33. *Id. See* N.M. STAT. ANN. § 44-7-12(A)(5) (1978) ("The fact that the relief granted was such that it could not or would not be granted by a court of law or equity is not grounds for vacating or refusing to confirm the award.").

34. *Id.*

35. *Id.* (citing Bernhart v. Polygraphic Co. of Am., 350 U.S. 198, 203 n.4 (1956)).

The arbitration provision in *Valdez* arose out of an uninsured motorist policy.[36] The standard uninsured motorist policy contains an arbitration provision.[37] Given the pervasive use of these provisions in uninsured motorist policies, it is important to note some general developments in arbitration in New Mexico.

New Mexico's former arbitration statute was a "present controversy" statute.[38] A "present controversy" statute applies to disputes arising at the time of the signing of the arbitration provision.[39] It was generally thought that arbitration provisions in uninsured motorists claims were not subject to the old arbitration statute because uninsured motorist disputes arise in the future after the signing of the arbitration provision.[40]

In 1969, in order to make uninsured motorist arbitration provisions enforceable,[41] New Mexico enacted the de novo appeal statute.[42] This statute specifically provided that arbitration awards arising under an uninsured motorist provision or an automobile liability insurance policy could be appealed to any district court for a trial de novo.[43] Subsequently, in 1971, New Mexico adopted The Uniform Arbitration Act, which differed from the old arbitration statute because it applied to present and future arbitration disputes.[44] The Uniform Arbitration Act contains no provision that the aggrieved party may appeal for a trial de novo.[45] Rather, the Act provides that appeals can be taken from six types of court orders,[46] and "the appeals shall be taken in the manner and to the same extent as from orders or judgments in a civil action."[47]

The court resolved the inconsistency between the trial de novo statute and the appeal procedure of the Uniform Arbitration Act in *Dairyland Insurance Co. v. Rose*.[48] In *Dairyland*, the supreme court considered the relationship between the trial de novo statute and the Uniform Arbitration

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36. *Valdez*, 107 N.M. at 765, 764 P.2d at 1323.

37. 2 WIDISS, UNINSURED AND UNDERINSURED MOTORIST INSURANCE § 45.1, at 133 (1987). This provision states generally that: either party may make a written demand for arbitration in the event that the claimant and the insurer do not agree: (1) whether that person is legally entitled to recover damages under this endorsement, or (2) as to the amount of damages. *Id.* § 45.3, at 134.

38. Note, *Uninsured Motorist Arbitration*, 3 N.M.L. REV. 220, 223 (1973).

39. *Id.*

40. Dairyland Ins. Co. v. Rose, 92 N.M. 527, 530, 591 P.2d 281, 284 (1979).

41. *Id.* at 531, 591 P.2d at 285.

42. N.M. STAT ANN. § 65-5-303 (Repl. Pamp. 1988).

43. *Id.*

44. Note, *supra* note 38, at 225.

45. N.M. STAT. ANN. §§ 44-7-1 to -22 (1978).

46. (1) an order denying an application to compel arbitration made under Section 2 [44-7-2 NMSA 1978];
(2) an order granting an application to stay arbitration made under Subsection B of Section 2 [44-7-2 NMSA 1978];
(3) an order confirming or denying confirmation of an award;
(4) an order modifying or correcting an award;
(5) an order vacating an award without directing a rehearing; or
(6) a judgment or decree entered pursuant to the provisions of the Uniform Arbitration Acts [44-7-1 to 44-7-22 NMSA 1978].
N.M. STAT. ANN. § 44-7-19(A) (1978).

47. *Id.* § 44-7-19(B) (1978).

48. 92 N.M. 527, 591 P.2d 281 (1979).

Act and held that the trial de novo was repealed by implication in the Uniform Arbitration Act.[49] The court stated that "the Legislature and the courts have expressed a strong policy preference for resolution of disputes by arbitration."[50]

According to *Valdez*, if a party resists arbitration and seeks a declaratory judgment by the trial court, the trial court must hear the issue.[51] Should the trial court, however, determine that the parties agreed to arbitrate the issues raised in the complaint, the court may require the parties to arbitrate the issues.[52] In *Valdez*, the court reversed the trial court's dismissal and remanded with instructions to consider the complaint for declaratory judgment on its merits.[53]

B. The Hospital Lien Act

The Hospital Lien Act[54] allows a hospital, which has provided emergency, medical, or other service to any patient injured in an accident and not covered by workers' compensation laws, to assert a lien "upon that part of the judgment, settlement or compromise going or belonging to such patient . . . ."[55] The Hospital Lien Act provides procedures for filing and notice,[56] as well as release of hospital liens.[57] Further, this act sets forth the persons liable for payment and a one-year limitation of actions period.[58] At issue in *Regents of the University of New Mexico v. Lacey*[59] was the interpretation of the limitation of actions provision. That provision states that "[l]iability of the person, firm or corporation for the satisfaction of the hospital lien shall continue for a period of one year after the date of any payment of any money to the patient, his heirs or legal representatives as damages or under a contract of compromise or settlement."[60]

The only New Mexico case which has construed this provision involved a situation where the payment was made to the patient.[61] The court held that payment of any money to a patient must be actually received by the patient to begin the tolling of the statute of limitations.[62] In *Lacey* the situation involved payment to a "legal representative," and the supreme court further construed the terms "payment"[63] and "legal representative."[64]

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49. *Id.* at 530, 591 P.2d at 284.
50. *Id.*
51. *Valdez*, 107 N.M. at 766, 764 P.2d at 1324.
52. *Id.* at 767, 764 P.2d at 1325.
53. *Id.*
54. N.M. STAT. ANN. §§ 48-8-1 to -7 (Repl. Pamp. 1987).
55. *Id.* § 48-8-1(A) (Repl. Pamp. 1987).
56. *Id.* § 48-8-2 (Repl. Pamp. 1987).
57. *Id.* § 48-8-5 (Repl. Pamp. 1987).
58. *Id.* § 48-8-3 (Repl. Pamp. 1987).
59. 107 N.M. 742, 764 P.2d 873 (1987).
60. N.M. STAT. ANN. § 48-8-3(B) (Repl. Pamp. 1987).
61. Regents of Univ. of N.M. v. Firemen's Fund Ins. Co., 103 N.M. 709, 712 P.2d 1371 (1986).
62. *Id.* at 711-12, 712 P.2d at 1373-74.
63. *Lacey*, 107 N.M. at 744, 764 P.2d at 874.
64. Id.

The defendant, Lacey, was involved in a collision with an automobile while riding his motorcycle.[65] The automobile driver was at fault and was insured by Liberty Mutual.[66] Lacey incurred hospital expenses of $20,594.51 at the University of New Mexico (UNM) Hospital.[67] The Regents filed their notice of a hospital lien in accordance with section 48-8-2 of the Act on April 26, 1985.[68]

The salient facts in the case involved the time sequence of events. Thirteen months after the Regents filed their hospital lien, Liberty Mutual issued a $58,265.35 check on behalf of its insured to Lacey's attorney. The check was received on May 28, 1986, endorsed by Lacey and deposited into his attorney's trust account on November 6, 1986.[69] Subsequently, on November 10, 1986, Lacey's attorney sought a fifty percent reduction in Lacey's hospital fees.[70] UNM Hospital refused the reduction, asserting that they were constitutionally prohibited from receiving less than full payment.[71] Lacey's attorney disregarded the hospital's refusal and sent UNM Hospital a check for only $10,000 on January 15, 1987.[72] Six months later, on June 19, 1987, the Regents of UNM sued Lacey and Liberty Mutual for debt and money due on an open account and for enforcement of their hospital lien.[73] Lacey's attorney moved for dismissal on the basis that the suit was time-barred pursuant to section 48-8-3(B) of the Act.[74] The trial court held that the one-year statute of limitations began to toll on May 28, 1986, the date Lacey's attorney received the check.[75] Therefore, the suit, brought on June 19, 1987, was dismissed.[76]

On appeal, the Regents of UNM made three arguments to delay the tolling of the statute of limitations.[77] First, because the check for $58,265.35 was accompanied by three requirements for a release[78] and was not endorsed and deposited until November 6, 1986, the Regents asserted that "payment of any money" was not satisfied, and thus, the statutory period did not begin to run before November 10, 1986.[79] Second, the Regents asserted that payment to an attorney was not payment to a "legal representative" within the statute.[80] Finally, the Regents argued that misrepresentation by Liberty Mutual on November 10, 1986, tolled the statute of limitations.[81]

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65. *Id.* at 743, 764 P.2d at 873.
66. *Id.*
67. *Id.*
68. *Id.*
69. *Id.*
70. *Id.*
71. *Id.*
72. *Id.*
73. *Id.*
74. *Id.*
75. *Id.*
76. *Id.*
77. *Id.*
78. *Id.* Accompanying the check was a release form requiring Lacey to fill in the date he signed the release, to write that he read the release, and to sign his name in front of a notary.
79. *Id.*
80. *Id.*
81. *Id.* at 744-45, 764 P.2d at 875-76.

The court held that although delivery of a check was not *per se* payment, payment occurred when the check was delivered to Lacey's counsel.[82] Further, the court held that Lacey's attorney was a legal representative under the statute interpreting "legal representative" in a broad sense.[83]

In addressing the alleged misrepresentation, the court set forth the elements of equitable estoppel and found that the facts of *Lacey* did not support estoppel.[84] First, the Regents did not prove misrepresentation by Liberty Mutual.[85] Second, the Regents did not lack knowledge of the facts regarding the one year statute of limitations.[86] Third, the Regents knew payment was made no later than November 1986. Therefore, they did not lack knowledge of the fact of payment.[87]

C. *Subject Matter Jurisdiction*

In *State Farm Mutual Automobile Insurance Co. v. Maidment*,[88] the court of appeals considered the preliminary procedural issue of jurisdiction to determine an uninsured motorist claim.[89] Rule of Appellate Procedure 12-102(A)(1)[90] provides that appeals from the district court will be taken to the supreme court when "one or more counts of the complaint alleges a breach of contract or otherwise sounds in contract." Maidment argued that the court of appeals lacked jurisdiction because the controversy arose out of an insurance contract and required interpretation of the rights and obligations of the parties to the contract.[91]

The court conceded that the obligations of an insurer are determined by contract principles.[92] However, the court of appeals had previously decided in *Sandoval v. Valdez*[93] that where the resolution of the case is contingent upon the tort liability of the uninsured motorist, the court

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82. *Id.* at 743-44, 764 P.2d at 874-75 (citing Franciscan Hotel Co. v. Albuquerque Hotel Co., 37 N.M. 456, 472, 24 P.2d 718, 726 (1933) (if upon delivery of the check, drawer has sufficient funds in drawee bank and the check is paid upon presentment, the date of payment will be deemed to have been made as of original delivery date)).

83. *Id.* at 744, 764 P.2d at 875. The court held "[a] legal representative, defined in its broadest sense, is one who stands in place of another and represents the interests of another; a person who oversees the legal affairs of another." *Id.*

84. *Id.* at 745, 764 P.2d at 876 (citing Capo v. Century Life Ins. Co., 94 N.M. 373, 377, 610 P.2d 1202, 1206 (1980)). For the party to be estopped, (1) the party's conduct must amount to a false representation or concealment of material facts; (2) the party must intend such conduct shall be acted upon; (3) the party must have knowledge, actual or constructive, of the real facts. For the party claiming estoppel, (1) the party must show lack of knowledge and means of knowledge of the truth as to the facts in question; (2) the party must rely upon the conduct of the party estopped; and (3) action taken upon such reliance must prejudice the party. *Id.*

85. *Id.*

86. *Id.*

87. *Id.*

88. 107 N.M. 568, 761 P.2d 446 (Ct. App. 1988).

89. *Id.* at 569-70, 761 P.2d at 447-48. For a full discussion of the substantive issues in *Maidment*, see *infra* notes 270-308 and accompanying text.

90. SUP. CT. RULES ANN. 12-102(A)(2) (Recomp. 1986).

91. *Maidment*, 107 N.M. at 569, 761 P.2d at 447.

92. *Id.* at 570, 761 P.2d at 448.

93. 91 N.M. 705, 580 P.2d 131 (Ct. App. 1978).

of appeals has jurisdiction. The issue in *Maidment* was the availability of punitive damages.[94] An insured person may recover punitive damages from his insurer if he could have recovered them from the uninsured motorist.[95] Since recovery of punitive damages is contingent upon the tort liability of the uninsured motorist, the court found that it had jurisdiction.[96]

II. COVERAGE

The majority of cases decided in the insurance area involved coverage issues.[97] The appellate courts considered exclusionary provisions,[98] uninsured/underinsured motorists coverage[99] and the validity of an insurance provision in an indemnity contract.[100]

A. Exclusionary Provisions

In *Castorena v. Colonial Life & Accidental Insurance Co.*,[101] the supreme court construed a liability provision which excluded loss caused by disease or medical procedures. Castorena, a diabetic, had a hypoglycemic seizure while driving; he veered off the road and hit a sign.[102] Castorena was not injured in the accident, but he was transported to a local hospital because he was in a coma.[103] At the hospital, Castorena was given an intravenous (IV) solution for insulin shock.[104] The IV needle was improperly inserted, causing Castorena's left hand to later become gangrenous.[105] Surgery on the hand was unsuccessful and Castorena's left arm was amputated below the elbow.[106]

The policy provided coverage for a single dismemberment arising out of "accidental injury," defined as "bodily injury effected solely, directly, independently and exclusively of all other causes by accident during the term of this Policy."[107] Additionally, the policy excluded loss for "disease

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94. *Maidment*, 107 N.M. at 570, 761 P.2d at 448.

95. Stewart v. State Farm Mut. Auto Ins. Co., 104 N.M. 744, 747, 726 P.2d 1374, 1377 (1986). *See* N.M. STAT. ANN. § 66-5-301(A) (Repl. Pamp. 1984) (uninsured motorist insurance is "for the protection of persons . . . who are legally entitled to recover damages").

96. *Maidment*, 107 N.M. at 570, 761 P.2d at 448.

97. L'Allier v. Turnacliff, 107 N.M. 382, 758 P.2d 796 (1988), decided a coverage issue, but is not discussed below because it restates an existing principle of law concerning insurable interests. *L'Allier* held that it is not necessary to have title in an automobile in order to have an insurable interest in the automobile. This holding is in accordance with the principle set forth in Forsythe v. Central Mut. Ins. Co. of N.Y., 84 N.M. 461, 505 P.2d 56 (1973).

98. Castorena v. Colonial Life & Accident Ins. Co., 107 N.M. 460, 760 P.2d 152.

99. State Farm Mut. Auto. Ins. Co. v. Maidment, 107 N.M. 568, 761 P.2d 446 (Ct. App.), *cert. denied*, 107 N.M. 413, 759 P.2d 200 (1988); Jimenez v. Foundation Reserve Ins. Co., 107 N.M. 322, 757 P.2d 792 (1988); Allstate Ins. Co. v. Graham, 106 N.M. 779, 750 P.2d 1105 (1988); Morro v. Farmers Ins. Group, 106 N.M. 669, 748 P.2d 512 (1988).

100. Amoco Prod. Co. v. Action Well Serv., 107 N.M. 208, 755 P.2d 52 (1988).

101. 107 N.M. 460, 760 P.2d 152 (1988).

102. *Id.* at 461, 760 P.2d at 153.

103. *Id.*

104. *Id.*

105. *Id.*

106. *Id.*

107. *Id.* at 462, 760 P.2d at 154.

or any degenerative process; physical or mental infirmity, medical, surgical or diagnostic procedure therefor."[108]

Castorena sought recovery for the loss of his left arm under his policy with Colonial. He claimed that the loss was caused by the *accidental insertion* of the IV needle.[109] Colonial denied the request, stating that the amputation was not the result of the accident, but rather was the result of a medical procedure for the diabetic condition and was subject to the exclusionary provision.[110]

The court interpreted the "accidental injury" exclusionary provision to exclude the improper treatment undertaken as a result of his diabetic seizure.[111] Following a 1966 New Jersey Superior Court decision, *Dinkowitz v. Prudential Insurance Co. of America*,[112] the supreme court found that

> loss resulting from medical or surgical treatment of a bodily condition caused by accidental means does not exempt the insurer from payment of benefits under the exclusionary clause, while a loss resulting from treatment of a bodily condition *not* caused by accidental means is one which is expressly excluded from coverage of the benefit by the limiting language of the exclusionary clause.[113]

The court further noted that a mistake by a treating physician may be an "accident"; however, if the mistake occurs during "medical treatment" as defined by the exclusionary clause, "it is not a risk assumed by the insurance company within the language of the policy."[114]

The court, finding the language of the policy unambiguous, strictly enforced the exclusion.[115] The court held that "but for" Castorena's diabetic condition, the insertion of the IV needle would have been unnecessary.[116] Castorena was not injured in the accident; rather his loss was due to the pre-existing diabetic condition.[117] The exclusionary provision, clear and unambiguous in excluding treatment of a bodily condition not caused by an accident, would be rendered meaningless if the provision was not enforced.[118]

B. Uninsured/Underinsured Motorist Coverage

Three cases were decided by the supreme court involving uninsured/underinsured motorists provisions.[119] The supreme court decided two stack-

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108. *Id.*
109. *Id.* (emphasis added).
110. *Id.*
111. *Id.*
112. 90 N.J. Super. 181, 216 A.2d 613 (Law Div. 1966).
113. *Castorena*, 107 N.M. at 462, 760 P.2d at 154 (emphasis in original).
114. *Id.* (citing *Dinkowitz*, 90 N.J. Super. at 188, 216 A.2d at 618).
115. *Id.*
116. *Id.*
117. *Id.*
118. *Id.* Although not explained, the rationale inheres from the contractual focus of the case. Since the court began its analysis with the general principle that "the obligation of a liability insurer is contractual," and the exclusionary provision was not ambiguous, the court followed the insurance contract and enforced the exclusion as written. *Id.*
119. Jimenez v. Foundation Reserve Ins. Co., 107 N.M. 322, 757 P.2d 792 (1988); Morro v. Farmers Ins. Group, 106 N.M. 669, 748 P.2d 512 (1988); Allstate Ins. Co. v. Graham, 106 N.M. 779, 750 P.2d 1105 (1988).

ing disputes[120] and construed the term "occupant" under a particular uninsured motorist provision.[121]

1. The Uninsured Motorist Statute

The uninsured motorist statute[122] mandates that all automobile liability policies issued in New Mexico contain uninsured[123] and underinsured[124] motorist protection unless the insured rejects the coverage.[125] An underinsured motorist is one whose total bodily injury insurance coverage "applicable at the time of the accident is less than the limits of liability under the insured's uninsured motorist statute."[126] To be afforded protection under the uninsured or underinsured motorist statute, the persons insured must be "legally entitled to recover damages from owners or operators of uninsured motor vehicles."[127]

The purpose underlying the statute is "to protect persons injured in automobile accidents from losses which because of the tortfeasor's lack of liability coverage, would otherwise go uncompensated."[128] Moreover, "[t]he uninsured motorist statute must be liberally construed to implement this purpose of compensating those injured through no fault of their own."[129] Liberal construction has promoted the use of stacking in New Mexico, and the general trend is to favor stacking.[130]

2. Stacking

As the New Mexico Supreme Court has defined the term, "[s]tacking refers to an insured's attempted recovery of damages by aggregating the coverage under more than one policy or under one policy covering more than one automobile."[131] The scope of stacking has gradually evolved through the decisions in five cases.[132] To understand the two cases in the survey period which expand existing precedent, a review of the New Mexico law is necessary.

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120. *Jimenez*, 107 N.M. 322, 757 P.2d 792; *Morro*, 106 N.M. 669, 748 P.2d 512.
121. Allstate Ins. Co. v. Graham, 106 N.M. 779, 750 P.2d 1105.
122. N.M. STAT. ANN. § 66-5-301 (Repl. Pamp. 1989).
123. *Id.* § 66-5-301(A) (Repl. Pamp. 1989).
124. *Id.* § 66-5-301(B) (Repl. Pamp. 1989).
125. *Id.* § 66-5-301(C) (Repl. Pamp. 1989).
126. *Id.* § 66-5-301(B) (Repl. Pamp. 1989).
127. *Id.* § 66-5-301(A) (Repl. Pamp. 1989). "[T]he insured must establish . . . a substantive right to recover damages from the uninsured motorist." R. JERRY, UNDERSTANDING INSURANCE LAW § 133(b)(1) (1987).
128. Chavez v. State Farm Mut. Auto. Ins. Co., 87 N.M. 327, 329, 533 P.2d 100, 102 (1975) (quoting Abate v. Pioneer Mutual Cas. Co., 22 Ohio St. 2d 161, 165, 258 N.E.2d 429, 432 (1970)).
129. *Id.*
130. Lopez v. Foundation Reserve Ins. Co., 98 N.M. 166, 169, 646 P.2d 1230, 1233 (1982) (citing Taft v. Cerwonka, 433 A.2d 215, 218 (1981)).
131. Gamboa v. Allstate Ins. Co., 104 N.M. 756, 757, 726 P.2d 1386, 1387 (1986).
132. *See* Sloan v. Dairyland Ins. Co., 86 N.M. 65, 519 P.2d 301 (1974); Lopez v. Foundation Reserve Ins. Co., 98 N.M. 166, 646 P.2d 1230 (1982); Konnick v. Farmers Ins. Co. of Ariz., 103 N.M. 112, 703 P.2d 889 (1985); Schmick v. State Farm Mut. Auto. Ins. Co., 103 N.M. 216, 704 P.2d 1092 (1985); Gamboa v. Allstate Ins. Co., 104 N.M. 756, 726 P.2d 1386 (1986).

a. The development of stacking in New Mexico. The first case permitting stacking in New Mexico was *Sloan v. Dairyland Insurance Co.*[133] In *Sloan*, the insured was killed while riding as a passenger in an automobile struck by an uninsured motorist.[134] The amount of damages exceeded $20,000.[135] The estate recovered $10,000 under the insurance policy covering the automobile involved in the accident.[136] The estate then sought to recover under the decedent's own policy which covered a car not involved in the accident.[137] The supreme court permitted the decedent's estate to stack the policy covering the automobile involved in the accident with the decedent's policy covering a car not involved in the accident.[138]

The insurance company asserted the defense of "other insurance"; that is, since the insured had already been paid under one policy by another insurance company, she was not entitled to recover under her own policy which contained a clause excluding any coverage in excess of the limit of liability.[139] To allow recovery under more than one policy would award the insured a "windfall."[140] The insurance company asserted that the legislature intended only to allow stacking up to the minimum statutory protection. At that time the minimum protection was $10,000.[141]

The court stated that the "better reasoned" view allowed coverage under more than one policy.[142] After interpreting the uninsured motorist statute, the supreme court reasoned that "[w]e find in our statutory scheme a minimum uninsured motorist coverage without difficulty, but are unable to perceive a maximum."[143] The court also recognized that an insurance company should not be able to avoid coverage "for which it contracted and received a premium."[144] This opened the door to the development of stacking law in New Mexico.

Sloan allowed inter-policy stacking, the stacking of two policies. The next case, *Lopez v. Foundation Reserve Insurance Co.*,[145] allowed intra-policy stacking, the stacking within one policy. Intra-policy stacking arises when one insurance policy covers more than one of the insured's vehicles. In *Lopez*, the court also began to develop distinctions between types of insureds.[146]

Lopez, the insured, and a passenger riding in his car, James Torres, were killed in a collision with an uninsured motorist.[147] Lopez had an

133. 86 N.M. 65, 519 P.2d 301 (1974).
134. *Id.* at 66, 519 P.2d at 302.
135. *Id.*
136. *Id.*
137. *Id.*
138. *Id.* at 67, 519 P.2d at 303.
139. *Id.* at 66, 519 P.2d at 302.
140. *Id.* at 68, 519 P.2d at 304.
141. *Id.*
142. *Id.* at 67, 519 P.2d at 303.
143. *Id.* at 68, 519 P.2d at 304.
144. *Id.*
145. 98 N.M. 166, 646 P.2d 1230 (1982).
146. *Id.* at 169, 646 P.2d at 1233.
147. *Id.* at 167, 646 P.2d at 1231.

existing policy covering two cars, each with an uninsured motorist coverage of $15,000 per person and $30,000 per accident.[148] The policy also contained a limit of liability provision. The insurance company asserted that this provision limited the combined recovery for both Lopez and Torres to $30,000.[149]

The court found the limit of liability provision to be ambiguous and construed it against the insurance company.[150] The court analyzed *Sloan* and found that the trend is to favor stacking.[151] The court reasoned that "the intent of the legislature is to assure that no insured motorist will remain uncompensated for injuries caused by an uninsured motorist."[152] The court also stated that an additional policy rationale for allowing stacking is that stacking meets "the reasonable expectations of the insured."[153] The doctrine of "reasonable expectations" evades definition. Some courts interpret the reasonable expectations from the viewpoint of the insured who purchased the policy, other courts consider a reasonable person in the insured's position.[154] Presumably, the court followed the reasonable expectations of the insured.

In *Lopez*, the court held that where multiple uninsured motorist premiums have been charged "it is only fair that the insured be permitted to stack the coverages for which he has paid."[155] This applies even when the second premium to be stacked is reduced.[156] The crucial distinction set forth in *Lopez* is that in order for policies to be stacked, separate premiums must be paid on the policy.[157] Stacking is not determined by the number of policies in force but by the number of premiums paid.[158]

In *Lopez*, the court also distinguished between the named insured and the passenger and held that a passenger could only recover under the policy of the automobile involved in the accident.[159] Later this distinction between types of insureds would develop into distinctions between "classes" of insureds.[160]

The next major decision, *Konnick v. State Farm Mutual Automobile Insurance Co.*,[161] expanded the use of stacking to underinsured motorist

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148. *Id.*
149. *Id.* at 168, 646 P.2d at 1232.
150. *Id.*
151. *Id.* at 169, 646 P.2d at 1233.
152. *Id.* at 170, 646 P.2d at 1234.
153. *Id.*
154. R. JERRY, *supra* note 127, § 25D.
155. *Lopez*, 98 N.M. at 171, 646 P.2d at 1235.
156. *Id.* The premium on the second automobile was one dollar less than the premium on the first automobile. The insurance company argued that the lesser premium was charged because of the "lesser likelihood of both vehicles being operated at the same time, and therefore, being 'at risk' at the same time." Thus, Foundation asserted one risk was meant to be covered and the policies should not be stacked. *Id.* at 172, 646 P.2d at 1236.
157. *Id.* at 171, 646 P.2d at 1235.
158. *Id.*
159. *Id.*
160. *See* Konnick v. State Farm Mut. Auto. Ins. Co., 103 N.M. 112, 115, 703 P.2d 889, 892 (1985).
161. *Id.*

policies. Tiffany Konnick, the insured's stepdaughter, was injured in a collision with an insured motorist.[162] Konnick's medical expenses resulting from the accident exceeded $100,000.[163] The insured driver only had $15,000 of liability coverage.[164] Konnick's stepfather had two automobile policies providing uninsured and underinsured motorist coverage of $15,000 per automobile.[165] Konnick was paid $15,000 from the other driver and $15,000 under one of her stepfather's policies.[166] Konnick then sought coverage under her stepfather's second uninsured and underinsured policy.[167] The trial court permitted stacking of underinsured motorist policies.[168]

The insurance company appealed, arguing that the policy considerations underlying uninsured and underinsured motorist coverage are "intrinsically different," and therefore underinsured motorist policies should not be stacked.[169] The supreme court rejected this argument and held that "as with uninsured motorist coverage, an insured is entitled to stack underinsured motorist policies for which separate premiums have been paid."[170]

In *Konnick*, the court made the distinction between classes of insureds first noted in *Lopez*.[171] The insurance company asserted that Tiffany Konnick, like the passenger in *Lopez*, was entitled only to recovery under the car involved in the accident.[172] The supreme court distinguished *Lopez* on the basis that Konnick was a relative.[173] The court again used the doctrine of "reasonable expectations" and held the stepfather would reasonably expect that his stepdaughter would be covered for injuries caused by an underinsured motorist.[174]

The supreme court stated the policy recognized two classes of insureds for the purpose of coverage in this case.[175] "Class one" insureds include the "named insured as stated in the policy, the spouse, and relatives residing in the household."[176] "Class two" insureds "enjoy insured status only while they occupy the insured vehicle."[177] Under the terms of the policy in *Konnick*, relatives residing in the household of the insured could stack underinsured motorist policies.[178]

In *Schmick v. State Farm Mutual Automobile Insurance Co.*,[179] the supreme court allowed the insured to stack uninsured motorist policies

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162. *Id.* at 113, 703 P.2d at 890.
163. *Id.*
164. *Id.*
165. *Id.*
166. *Id.*
167. *Id.*
168. *Id.*
169. *Id.* at 114, 703 P.2d at 891.
170. *Id.*
171. *Id.*
172. *Id.* at 114-15, 703 P.2d at 891-92.
173. *Id.* at 115, 703 P.2d at 892.
174. *Id.* at 116, 703 P.2d at 893.
175. *Id.*
176. *Id.* at 115, 703 P.2d at 892.
177. *Id.*
178. *Id.*
179. 103 N.M. 216, 704 P.2d 1092 (1985).

to determine whether the tortfeasor was underinsured. Schmick, the plaintiff, had two uninsured motorist policies for two separate cars.[180] Each policy had an underinsured motorist provision for coverage up to $15,000.[181] Schmick was a named insured under one policy.[182] Under the other policy, Schmick's husband was the named insured. Thus, Schmick was covered under the second policy because she was the spouse.[183] Each policy also contained a provision excluding uninsured motorist coverage to an insured while occupying another motor vehicle owned by the named insured or any relative resident in the same household.[184]

Schmick was injured while driving the automobile for which she was the named insured.[185] The other driver's insurance company paid Schmick $25,000, the full amount of the other driver's liability coverage.[186] Schmick brought a declaratory judgment action against her insurer, seeking to stack her two underinsured motorist policies and recover the full amount of $30,000.[187] The trial court allowed Schmick to stack her underinsured motorist coverage but offset this stacked amount by the liability coverage already received from the other driver.[188] Schmick was only allowed to recover the difference between her stacked underinsured motorist coverage and the liability coverage of the other driver, or $5,000.[189] The trial court determined that the underinsured motorist protection was only intended to supplement the amount paid by the underinsured motorist, up to "the limits of liability under all bodily injury liability insurance applicable at the time of the accident."[190]

The supreme court affirmed the district court's decision.[191] The court allowed the underinsured motorist policies to be stacked; however, the court held that the amount recoverable was different from that recoverable under uninsured motorist claims because the legislature specifically set forth in the statute "the minimum and maximum amount an insured can collect from his underinsured motorist carrier."[192] The court stated, "Therefore, an insured collects from his underinsured motorist carrier the difference between his uninsured motorist coverage and the tortfeasor's liability coverage or the difference between his damages and the tortfeasor's liability coverage, whichever is less."[193]

Additionally, the court found the exclusionary provision to be ambiguous and construed the provision against State Farm.[194] More importantly,

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180. *Id.* at 217, 704 P.2d at 1093.
181. *Id.* at 218, 704 P.2d at 1094.
182. *Id.* at 217, 704 P.2d at 1093.
183. *Id.*
184. *Id.* at 220, 704 P.2d at 1096.
185. *Id.* at 218, 704 P.2d at 1094.
186. *Id.*
187. *Id.* at 217-18, 704 P.2d at 1093-94.
188. *Id.* at 218, 704 P.2d at 1094.
189. *Id.*
190. *Id.* (quoting N.M. STAT. ANN. § 66-5-301(B) (Repl. Pamp. 1989)).
191. *Id.* at 224, 704 P.2d at 1100.
192. *Id.* at 222, 704 P.2d at 1098.
193. *Id.*
194. *Id.* at 221, 704 P.2d at 1097. *See supra* note 184 and accompanying text.

the court held that the provision was void as against public policy.[195] Since the insured was "legally entitled" to recover damages and the tortfeasor was underinsured, excluding recovery under one of the policies would be "against the policy of compensating persons injured through no fault of their own."[196]

In the last case prior to the survey period, *Gamboa v. Allstate Insurance Co.*,[197] the court placed some limitations on stacking. Ernesto Gamboa was riding in his father's car; Andrew Trujillo was driving the car.[198] Gamboa and Trujillo were killed in a collision with an uninsured motorist.[199] Gamboa's father had an uninsured motorist policy for the car involved in the accident. The estates of Gamboa and Trujillo each recovered $15,000 under this policy.[200] Trujillo's father had an uninsured motorist policy with Allstate Insurance Company on another automobile, not involved in the accident.[201] Gamboa's estate sought recovery under Trujillo's father's policy.[202]

At issue was whether Gamboa was an insured under Trujillo's father's policy.[203] Since the insurance policy was clear in defining insureds, the supreme court strictly interpreted the policy provisions.[204] Gamboa was denied coverage because he did not fall within class one insurance coverage as defined by the policy.[205]

b. Stacking cases during the survey period. In *Morro v. Farmers Insurance Group*,[206] the supreme court allowed an insured to stack three policies. Under two policies Morro was a class one insured, and under the third policy she was a class two insured.[207] Each policy was then credited with a prorated offset from the underinsured motorist's liability proceeds.

While putting groceries into the trunk of her daughter's car, Caroline Morro was struck by a car driven by a third party. She sustained serious injuries.[208] Morro could have recovered under the liability insurance policy of the third party, her daughter's automobile policy with Foundation Reserve, or her own two automobile policies with Farmers Insurance covering cars not involved in the accident.[209] Each policy had a $25,000

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195. *Id.*
196. *Id.*
197. 104 N.M. 756, 726 P.2d 1386 (1986).
198. *Id.* at 757, 726 P.2d at 1387.
199. *Id.*
200. *Id.*
201. *Id.*
202. *Id.*
203. *Id.*
204. *Id.* at 760, 726 P.2d at 1390. The supreme court held that "considering the contract as a whole we find the policy language is unambiguous." *Id.*
205. *Id.*
206. 106 N.M. 669, 748 P.2d 512 (1988).
207. *Id.* at 670, 748 P.2d at 513.
208. *Id.*
209. *Id.*

limit.[210] As the named insured, Morro was a class one insured under her two policies.[211] She was a class two insured under her daughter's policy because she was an occupant of the car involved in the accident.[212]

Morro settled with the third party for $25,000.[213] She then sought recovery from her daughter's insurer, Foundation Reserve, by stacking her daughter's policy with her own two policies.[214] If all policies were stacked, the coverage would be $75,000, making the third party underinsured by $50,000.[215]

The trial court granted summary judgment in Morro's favor.[216] Foundation Reserve appealed, claiming Morro was not entitled to stack class one and class two policies to determine underinsured status.[217] Foundation further asserted that the third party was not underinsured because the third party's coverage was "not less than, but equal to, the maximum limits of uninsured motorist coverage ($25,000)."[218]

The issue in this case was a question of first impression.[219] In affirming the trial court, the supreme court extracted principles from the preceding cases to reach its decision. Quoting *Schmick*, the court noted that the legislature intended the injured insured to be put in the same position as if the tortfeasor had liability coverage equaling the amount of underinsured motorist coverage purchased for the insured's benefit.[220] The court further noted the reasonable expectations, described in *Konnick*, that an insured who purchases a policy and pays premiums "expects that benefits will be paid to an occupant if an underinsured motorist injures the occupant of the insured vehicle."[221] Therefore, the daughter could reasonably expect her mother to be covered. Finally, the only limitations on stacking are "that the insured legally be entitled to recover damages and that the negligent driver be either uninsured or underinsured."[222] Thus, the court held that case law "overwhelmingly" supported allowing class one and class two uninsured motorist coverage to be stacked and continued the trend favoring stacking.[223]

In *Jimenez v. Foundation Reserve Insurance Co.*,[224] the supreme court was asked to enforce a clear and unambiguous liability provision prohibiting stacking of multiple uninsured motorist premiums. The court

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210. *Id.*
211. *Id.*
212. *Id.*
213. *Id.*
214. *Id.*
215. *Id.*
216. *Id.*
217. *Id.*
218. *Id.*
219. *Id.*
220. *Id.* at 672, 748 P.2d at 515.
221. *Id.* at 671, 748 P.2d at 514.
222. *Id.*
223. *Id.* at 672, 748 P.2d at 515.
224. 107 N.M. 322, 757 P.2d 798 (1988).

applied a two-part test to review the exclusionary provision.[225] To be enforced, the exclusionary provision must be clear and unambiguous, and it must not conflict with public policy as found either in express statutory language or legislative intent.[226] The court found that although the limit of liability provision passed the first test, it was nonetheless void because it violated public policy.[227]

Jimenez, the plaintiff, was injured in a car accident.[228] At the time of the accident, Jimenez had a policy in effect with Foundation Reserve, under which he paid two premiums to cover two separate vehicles.[229] The policy insured each vehicle for uninsured motorist coverage of $25,000 per person per accident, and $50,000 per accident.[230] The policy also contained a limit of liability provision that denied multiple uninsured motorist coverage claims.[231] At trial the parties stipulated damages of $50,000 with Jimenez receiving one-half of this amount from the the negligent driver's insurer.[232] Jimenez then sought to stack his uninsured motorist coverage in order to receive underinsured motorist coverage from Foundation Reserve.[233] Foundation Reserve refused, claiming that the negligent driver was not underinsured because the limit of liability provision only entitled Jimenez to $25,000.[234] Summary judgment was granted in favor of Jimenez.[235]

The court's analysis of the exclusionary provision began with the well-settled principle that the legislative intent of the uninsured motorist statute is to compensate an injured person to the extent of insurance liability purchased for his or her own benefit.[236] Pursuant to *Schmick*, exclusionary provisions which attempt to limit stacking are void as against public policy.[237] Even though *Schmick* was distinguishable because the exclu-

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225. *Id.* at 324, 757 P.2d at 794 (citing March v. Mountain States Mut. Cas. Co., 101 N.M. 689, 691, 687 P.2d 1040, 1042 (1984)).

226. *Id.*

227. *Id.*

228. *Id.* at 323, 757 P.2d at 793.

229. *Id.*

230. *Id.*

231. *Id.* The insurance policy provided,

> The limit of liability shown in the Declarations for "each person" for uninsured motorist coverage is our maximum limit of liability for all damages for bodily injury sustained by any one person in any one auto accident. Subject to this limit for "each person," the limit of liability shown in the Declarations for "each accident" for Uninsured Motorist Coverage is our maximum limit of liability for all damages for bodily injury resulting from any one auto accident. This is the most we will pay regardless of the number of covered persons, claims made, vehicles or premiums shown in the Declarations, or vehicles involved in the auto accident.

232. *Id.*

233. *Id.*

234. *Id.*

235. *Id.*

236. *Id.* at 324, 757 P.2d at 794 (citing Schmick v. State Farm Mut. Auto. Ins. Co., 103 N.M. 216, 704 P.2d 1092 (1985)).

237. *Id.* In *Schmick*, the court held a clause excluding coverage while occupying a vehicle owned by the named insured "other than" the insured motor vehicle was "void as against New Mexico's policy of compensating persons injured through no fault of their own." 103 N.M. 216, 221, 704 P.2d 1092, 1097. For a discussion of *Schmick*, see *supra* notes 179-96 and accompanying text.

sionary provision in that case was ambiguous, the court stated that the issue of ambiguity was not determinative.[238]

The court recognized that when an insured has purchased multiple premiums he would reasonably expect to be compensated and should be compensated when injured through no fault of his own.[239] Thus, when an insured has paid separate premiums on different vehicles for uninsured/underinsured coverage, it is "particularly repugnant to public policy" to prohibit stacking.[240] An insurance company may not "collect a premium for certain protection and then take it away by a limiting clause."[241] Applying the formula set forth in *Schmick*, the court allowed Jimenez to recover "[t]he difference between his uninsured motorist coverage and the tortfeasor's liability coverage or the difference between his damages and the tortfeasor's liability coverage, whichever is less."[242]

The dissenting opinion by Justice Stowers focused on the contractual aspects of the case.[243] Justice Stowers asserted that no statutory public policy exists which either prohibits or requires stacking.[244] In the absence of such a policy, Justice Stowers vigorously criticized the majority for rewriting the clear terms contained in the insurance contract.[245] He argued that straightforward contractual analysis would appropriately dispose of the case.[246] As such, the policy would be construed by the parties' intent at the time it was made and in light of an objective, reasonable person standard.[247] According to Justice Stowers, parties entering a contractual relationship are bound thereby, and Jimenez should have been bound by the clause limiting liability.[248]

3. The Definition of "Occupant"

An insurance policy is a contract, and policy coverage inevitably involves an interpretation of the terms of the insurance contract. *Allstate Insurance Co. v. Graham*[249] presented the supreme court with a question of first impression asking the court to define the term "occupant" in an uninsured motorist provision.[250]

Graham drove her father's car to help her friend, Pearl Silva, fix a flat tire on Silva's car.[251] Graham met with Silva and they took the flat

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238. *Jimenez*, 107 N.M. at 324, 757 P.2d at 794.
239. *Id.* at 325, 757 P.2d at 795. This is so, despite the clear limit-of-liability clause, "because case law in this jurisdiction repeatedly has stated the public policy which allows uninsured/underinsured motorist coverage to be stacked when separate premiums are paid for additional coverage." *Id.*
240. *Id.* at 324, 757 P.2d at 794.
241. *Id.* at 326, 757 P.2d at 796 (quoting Allstate Ins. Co. v. Maglish, 94 Nev. 699, ____, 586 P.2d 313, 315 (1978)).
242. *Id.*
243. *Id.* at 327, 757 P.2d at 797.
244. *Id.* at 328, 757 P.2d at 798.
245. *Id.*
246. *Id.*
247. *Id.*
248. *Id.* at 329, 757 P.2d at 799.
249. 106 N.M. 779, 750 P.2d 1105 (1988).
250. *Id.* at 780, 750 P.2d at 1106.
251. *Id.* at 779, 750 P.2d at 1105.

tire to be repaired.[252] Upon returning from the repair shop, Graham parked her father's car approximately three feet in front of Silva's car.[253] Graham proceeded to change Silva's flat tire and was struck by another car as it ran off the road.[254] The car which struck Graham, and Silva's car, was uninsured.[255] The only possible coverage for Graham was under the uninsured motorist provision of her father's car.[256]

The father's policy applied to the named insured as well as "any other person while occupying an insured motor vehicle."[257] Graham conceded that she was only entitled to coverage under this section.[258] "Occupying" was further defined in the policy as "in or upon or entering into or alighting from."[259] Thus, whether Graham had coverage hinged upon the interpretation of the word "occupying."[260]

The lower court granted summary judgment to Graham.[261] On appeal, the supreme court reversed the district court and granted summary judgment to Allstate.[262] The supreme court looked to other jurisdictions for guidance and identified factors that courts have used to determine the definition of occupant.[263] These factors include distance in time and space[264] and a "reasonable connection" between the claimant and the vehicle at the time of the accident.[265] The court denied Graham's assertion that the term "occupying" was ambiguous and determined the issue on the claimant's close proximity to the car while engaged in an activity "so related to its operation and use as to be an integral part of the claimant's occupancy and use of the car."[266] The court held that Graham "simply was not engaged in a transaction oriented to the use of the [father's car] at the time of the accident."[267] The court reasoned that the purpose in *using* the car was to deliver the spare tire, rather than to change the flat tire.[268] Since this purpose was accomplished when the father's car was parked and the tire was delivered, the accident was not related to the use of the father's car.[269] Thus, the term "occupant," as

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252. *Id.*
253. *Id.*
254. *Id.*
255. *Id.*
256. *Id.*
257. *Id.* at 780, 750 P.2d at 1106.
258. *Id.*
259. *Id.*
260. *Id.*
261. *Id.* at 779, 750 P.2d at 1105.
262. *Id.* at 780-81, 750 P.2d at 1106-07.
263. *Id.* at 780, 750 P.2d at 1106.
264. *Id.* The court noted that "[i]n some cases, the distance in space or time the claimant is from the car is the controlling factor." *Id.* (citing Greer v. Kenilworth Ins. Co., 60 Ill. App. 3d 22, 376 N.E.2d 346 (1978) (where an insured standing ten to fifteen feet away was not "occupying" the vehicle)).
265. *Id.* (citing Manning v. Summit Home Ins. Co., 128 Ariz. 79, 623 P.2d 1235 (Ct. App. 1980)).
266. *Id.*
267. *Id.*
268. *Id.*
269. *Id.*

judicially construed and modified by the concept of use, was not broad enough to cover Graham.

4. Punitive Damages

In *State Farm Mutual Automobile Insurance Co. v. Maidment*,[270] the court of appeals denied an insured the ability to recover punitive damages under his uninsured motorist policy when the tortfeasor died before the award was made. Maidment was riding his motorcycle when he was involved in a collision with an automobile driven by an uninsured motorist.[271] The uninsured motorist died before Maidment's claim was submitted to arbitration.[272] Subsequently, the arbitrators found the deceased uninsured motorist to be grossly negligent[273] and awarded Maidment $175,000 in compensatory damages and recommended that the district court award $25,000 in punitive damages.[274] Maidment applied for confirmation of the arbitration award and the trial court accepted the arbitrators' recommendation.[275] State Farm appealed the portion of the judgment awarding punitive damages.[276]

Two cases in New Mexico analyze the issue of whether punitive damages are recoverable.[277] In a 1986 case, *Stewart v. State Farm Mutual Automobile Insurance Co.*,[278] the supreme court held that an insured who has been injured by an uninsured tortfeasor and awarded a judgment of punitive damages may collect the punitive damages from his own insurance company.[279] The holding of *Stewart* is that "an insured may recover punitive damages from his insurer if he would be legally entitled to recover them from the uninsured tortfeasor."[280] This principle follows the language of the uninsured motorist statute.[281] The second case, *Baker v. Armstrong*,[282] decided one year later, dealt with the contrary situation, in which the insured is the tortfeasor. In *Baker*, the court held that an insured who has punitive damages assessed against him can recover them from his insurance company.[283]

The public policy principles developed in *Stewart* and *Baker* created a framework for deciding *Maidment*. In *Stewart*, the court noted that

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270. 107 N.M. 568, 761 P.2d 446 (Ct. App. 1988). For a discussion of the court's jurisdiction to decide the issue in *Maidment*, see *supra* notes 88-96 and accompanying text.

271. *Maidment*, 107 N.M. at 569, 761 P.2d at 447.

272. *Id.*

273. *Id.* at 571, 761 P.2d at 449.

274. *Id.* at 569, 761 P.2d at 447.

275. *Id.*

276. *Id.*

277. Stewart v. State Farm Mut. Auto. Ins. Co., 104 N.M. 744, 726 P.2d 1374 (1986); Baker v. Armstrong, 106 N.M. 395, 744 P.2d 170 (1987).

278. 104 N.M. 744, 726 P.2d 1374.

279. *Id.* at 747, 726 P.2d at 1377.

280. *Id.*

281. *See* N.M. STAT. ANN. § 66-5-301(A) (Repl. Pamp. 1989).

282. 106 N.M. 395, 744 P.2d 170. This case is treated fully in Sanders, *Insurance Law*, 19 N.M.L. REV. 717, 729-31 (1989).

283. *Baker*, 106 N.M. at 398, 744 P.2d at 173.

the legislative purpose behind mandatory uninsured motorist coverage is to "protect the insured against the financially unresponsible motorist, not to protect the insurance company."[284] In addition, while the court recognized that the policy of punitive damages is to punish the tortfeasor and compensate the victim, the court found that punishment would not be subverted because the insurance company would have subrogation rights against the tortfeasor.[285] Punishment was not subverted because the burden was merely shifted from the insured to the insurance company to file suit against the tortfeasor.[286]

In *Baker*, the public policy consideration centered on the insurability of punitive damages. First, the court noted that an insured contemplates protection for any claims for which he may become liable during the operation of the insured automobile.[287] Therefore, insuring punitive damages meets the reasonable expectations of the insured.[288] The court rejected *Northwestern National Casualty Co. v. McNulty*.[289] *McNulty* held that insuring punitive damages is against public policy because punishment and deterrence would serve no useful purpose if the wrongdoer could shift the risk to an insurance company.[290] In *Baker*, the court held that the purchase of insurance does not encourage wrongful acts and deterrence is not diminished because "it is common knowledge that the prospect of canceled coverage or rated premiums is a strong deterrent to bad driving in today's society."[291]

The principle of *Stewart*—that to recover punitive damages from the insurance company, the insured must be legally entitled to recover from the tortfeasor—barred recovery to Maidment.[292] The court held that punitive damages may not be recovered from the estate of the tortfeasor because the object of punitive damages is to punish the tortfeasor and not his innocent heirs.[293] Since Maidment was not "legally entitled" to the damages from the tortfeasor he could not recover them from his own insurance company.[294] Maidment creatively argued that he met the "legally entitled to" criteria because "entitlement vests at the moment of impact."[295] Maidment asserted that when the fault of the tortfeasor is established, the insured becomes legally entitled to punitive damages.[296] The court rejected this argument and held that survival of the tortfeasor

284. *Stewart*, 104 N.M. 743, 746, 726 P.2d 1374, 1376 (quoting Gantt v. L & G Air Conditioning, 101 N.M. 208, 213, 680 P.2d 348, 353 (Ct. App. 1983)).
285. *Id.* at 747, 726 P.2d at 1377.
286. *Id.*
287. *Baker*, 106 N.M. at 396, 744 P.2d at 171.
288. *Id.*
289. 307 F.2d 432 (5th Cir. 1962).
290. *Id.* at 440.
291. 106 N.M. at 398, 744 P.2d at 173.
292. *Maidment*, 107 N.M. at 569, 761 P.2d at 447.
293. *Id.* at 571, 761 P.2d at 449 (citing Lohr v. Byrd, 522 So. 2d 845 (Fla. 1988)).
294. *Id.* at 569, 761 P.2d at 447.
295. *Id.* at 572, 761 P.2d at 450.
296. *Id.*

was necessary for recovery of punitive damages.[297] The court stated that if "the insured had only to establish the uninsured motorist's fault, together with damages, it takes no crystal ball to predict the difficulties the courts might encounter."[298]

The court harkened back to *Stewart* in two more respects. First, the policy of punitive damages is to punish the tortfeasor and not to compensate the victim.[299] The court concluded that punishment was not possible in *Maidment* because the tortfeasor was dead.[300] Moreover, the court reiterated the policy underlying *Stewart*: that punishment is not subverted when the insurance company can file suit against the tortfeasor.[301] Since the insurance company could not file suit against the estate of the tortfeasor, the underlying policy of *Stewart* would not be fulfilled.[302] In other words, in *Stewart*, the burden of filing suit was "merely shifted"[303] to the insurance company to file suit, but in *Maidment* the insurance company could not file suit at all. Therefore, punitive damages were improper.[304]

The deterrence considerations were different from those outlined in *Baker*. In *Baker*, the court focused on the effect of deterrence on the tortfeasor himself.[305] Maidment asserted general deterrence considerations; that is, punitive damages should be awarded because they serve as a warning to others.[306] The court recognized the goal of deterring others but held that such deterrence is "inextricably tied" to the tortfeasor.[307] Maidment's argument failed because the tortfeasor died and the opportunity for general deterrence expired with him.[308]

C. *Validity of an Insurance Clause in an Indemnity Contract*

In *Amoco Production Co. v. Action Well Service*,[309] the supreme court examined the insurance provision of the anti-indemnity statute.[310] The anti-indemnity statute applies to oil, gas, or water wells, and any mineral mine.[311] This statute prohibits agreements or covenants which attempt to indemnify liability for death, bodily injury, property injury, or any other loss, "or any combination of these arising from the sole or concurrent

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297. *Id.*
298. *Id.* at 573-74, 761 P.2d at 451-52.
299. *Id.* at 571, 761 P.2d at 449.
300. *Id.*
301. *Id.* at 574, 761 P.2d at 452.
302. *Id.*
303. *Stewart*, 104 N.M. at 747, 726 P.2d at 1377.
304. *Maidment*, 107 N.M. at 574, 761 P.2d at 452.
305. *Baker*, 106 N.M. at 397-98, 744 P.2d at 172-73.
306. *Maidment*, 107 N.M. at 571, 761 P.2d at 449.
307. *Id.* "If the tortfeasor cannot be punished, it follows that there can be no general deterrence." *Id.*
308. *See id.*
309. 107 N.M. 208, 755 P.2d 52 (1988). For a full discussion and analysis of this case, see Note, *New Mexico Interprets the Insurance Clause in the Oil and Gas Anti-Indemnity Statute:* Amoco Production Co. v. Action Well Service, Inc., 20 N.M.L. REV. 179 (1990).
310. N.M. STAT. ANN. § 56-7-2 (Repl. Pamp. 1989).
311. *Id.*

negligence of the indemnitee."[312] The statute expressly provides that such an agreement or covenant "is against public policy and void and unenforceable."[313] The statute also contains an exception for insurance, stating that "[t]his provision shall not affect the validity of any insurance contract or any benefit conferred by the Workmen's Compensation Act."[314]

Amoco Production Company (Amoco) owned and maintained an oil lease site where Action Well Service Company (Action Well) was working as an independent contractor.[315] Amoco and Action Well entered into an indemnity contract providing that Amoco would not be held liable for the injury or death of Action Well employees.[316] This indemnity contract further provided that Action Well "agrees to *insure* this assumption of liability."[317]

Freddie Wagoner, an employee of Action Well, was killed while working at the oil lease site owned and maintained by Amoco.[318] Wagoner's estate sued Amoco and the parties eventually settled out of court for $500,000.[319] Amoco then sought reimbursement from Action Well under the indemnity contract.[320] Action Well had procured insurance for the indemnity agreement with two different companies.[321] One company had become insolvent by the time the dispute arose.[322] The other insurance agreement was with Harbor Insurance Company.[323]

At issue was whether the insurance provision was valid under the anti-indemnity statute and whether Action Well should have honored the indemnity contract.[324] In the leading New Mexico case construing this statute, *Guitard v. Gulf Oil Co.*,[325] the supreme court held that an agreement in which the indemnitor would indemnify the indemnitee for the indemnitor's negligence was valid.[326] The reverse is not true, however. The indemnitee cannot contract away liability for his own negligence.[327] Amoco argued on appeal that, despite the holding in *Guitard*, the company had a right to contract with Action Well that Action Well would insure Amoco's liability.[328] The court rejected the argument and decided the case in accordance with the public policy rationale of *Guitard*.[329]

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312. *Id.* § 56-7-2(A)(4) (Repl. Pamp. 1989).
313. *Id.*
314. *Id.*
315. *Amoco*, 107 N.M. at 209, 755 P.2d at 53.
316. *Id.*
317. *Id.* (emphasis in original).
318. *Id.*
319. *Id.*
320. *Id.*
321. *Id.*
322. *Id.*
323. *Id.* This agreement provided that Harbor "shall have the right and shall be given the opportunity to associate with [Action] in defense and control of any claim or suit reasonably likely to involve [Harbor]." *Id.*
324. *Id.*
325. 100 N.M. 358, 670 P.2d 969 (Ct. App.), *cert. denied*, 100 N.M. 327, 670 P.2d 581 (1983).
326. *See id.* at 362, 670 P.2d at 973.
327. *Id.* at 361, 670 P.2d at 972.
328. *Amoco*, 107 N.M. at 210, 755 P.2d at 54.
329. *Id.* at 211, 755 P.2d at 55.

In *Guitard*, the court stated that "the public policy behind section 56-7-2(A) is to promote safety."[330] The statute promoted safety by not allowing the indemnitee, generally the operator of the well or mine, "to delegate to subcontractors his duty to see that the well or mine is safe."[331] Thus, the court in *Amoco* held that the language providing for the validity of insurance contracts applied "to insurance purchased by the indemnitor to protect *its* interests and not the interests of the indemnitee."[332]

III. SUBROGATION

The doctrine of subrogation recognizes that the liability insurer has an obligation to pay its injured insured but also has a right to recover the amount paid to the insured from the tortfeasor.[333] In *Farmers Insurance Group of Companies v. Martinez*,[334] the court of appeals addressed the issue of the subrogation rights of an insurer after the dismissal with prejudice of the insured's lawsuit against the tortfeasor. The court did not apply ordinary res judicata principles to determine whether the insurer should be barred in a subsequent suit against the tortfeasor.[335] Instead the court set forth principles which depended on the tortfeasor's knowledge of the insurer's subrogation claim.[336]

In *Martinez*, the insured, Katherine Barreras, was injured by the tortfeasor, Martinez.[337] Barreras filed suit against Martinez but later voluntarily decided not to pursue the action.[338] The court dismissed the case with prejudice.[339] Subsequently, the insurer, Farmers Insurance Group of Companies (Farmers Insurance) filed suit against Martinez, joining Barreras as a party plaintiff.[340] Farmers Insurance sought reimbursement from Martinez for the medical expenses it had allegedly paid Barreras.[341] Martinez filed a motion to dismiss, asserting the defense of res judicata.[342] Farmers Insurance dropped Barreras from its lawsuit and opposed the motion to dismiss.[343] The trial court ruled that Barreras' prior action against Martinez barred the subsequent action.[344]

The court of appeals reversed the motion to dismiss and remanded to the trial court for an evidentiary hearing.[345] The court held that the

330. *Guitard*, 100 N.M. at 361, 670 P.2d at 972.
331. *Id.* at 362, 670 P.2d at 973.
332. *Amoco*, 107 N.M. at 211, 755 P.2d at 55 (emphasis in original).
333. 16 M. RHODES, COUCH ON INSURANCE § 61.37 (2d ed. 1984).
334. 107 N.M. 82, 752 P.2d 797 (Ct. App. 1988).
335. *Id.* at 83, 752 P.2d at 798.
336. *Id.* at 83-84, 752 P.2d at 798-99.
337. *Id.* at 83, 752 P.2d at 798.
338. *Id.*
339. *Id.*
340. *Id.*
341. *Id.*
342. *Id.*
343. *Id.*
344. *Id.*
345. *Id.* at 84, 752 P.2d at 799. On appeal three calendar notices were filed. The third calendar notice proposed to reverse and remand to the trial court for an evidentiary hearing. No memorandum in opposition to the third calendar notice was filed by Martinez. *Id.*

tortfeasor's knowledge of a subrogation claim is necessary to determine whether the subsequent action in this case should be barred.[346] The trial court was instructed to find when the insurance payment was made and whether the tortfeasor had knowledge of the insurance payment.[347]

The court noted that subrogation, whether legal or conventional,[348] "is an equitable remedy, and equitable principles control its application."[349] Therefore, "subrogation is properly analyzed under the law governing such claims and not under ordinary res judicata principles."[350]

The court recognized three principles governing the application of res judicata in subrogation cases. First, "[i]f an insured settles with a tortfeasor *before* an insurer has paid damages to the insured, the insurer's subrogation rights are destroyed and the settlement is a bar to a suit by the insurer against the tortfeasor."[351] It is a general principle of subrogation that an insurance company's rights to subrogation do not arise until the insurance company pays damages to its insured.[352] Thus, the insurance company cannot claim subrogation rights until it has paid damages.[353]

Second, "[i]f an insured files suit against, and settles with, the tortfeasor *after* receiving payment from the insurer, and the tortfeasor had knowledge of that payment or of the insurer's subrogation claim, the settlement will not be a bar to the insurer's suit against the tortfeasor."[354] The basis for this principle is that if a tortfeasor has knowledge of a settlement between the insurer and insured and he nevertheless procures a release and settlement with the insured, he is committing fraud upon the insurer.[355]

Third, "[i]f, on the other hand, an insured files suit against, and settles with, the tortfeasor after receiving payment from the insurer, and the tortfeasor has no notice or knowledge of that payment or of the insurer's subrogation claim, the settlement will bar the insurer's suit against the tortfeasor."[356] This principle differs from the second principle above because the tortfeasor is settling in good faith and without knowledge.[357]

The court noted that the holding in a New Mexico subrogation case, *United States Fidelity & Guaranty Co. v. Raton Natural Gas Co.*,[358] was

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346. *Id.*

347. *Id.*

348. "'Legal subrogation' . . . is a principle of equity; it is effected by operation of law and arises out of a relationship that need not be contractually based. 'Conventional subrogation' arises out of the contractual relationship." R. JERRY, *supra* note 127, § 96(b).

349. *Martinez*, 107 N.M. at 83, 752 P.2d at 798.

350. *Id.*

351. *Id.* (emphasis in original). This principle has been applied in the following cases: March v. Mountain States Mut. Cas. Co., 101 N.M. 689, 692, 687 P.2d 1040, 1043 (1984); Jacobsen v. State Farm Mut. Auto. Ins. Co., 83 N.M. 280, 491 P.2d 168 (1971); Motto v. State Farm Mut. Auto. Ins. Co., 81 N.M. 35, 462 P.2d 620 (1969); Armijo v. Foundation Reserve Ins. Co., 75 N.M. 592, 408 P.2d 750 (1965).

352. *See* R. JERRY, *supra* note 127, § 96(h).

353. *Id.* at 465.

354. *Martinez*, 107 N.M. at 84, 752 P.2d at 799 (emphasis in original).

355. M. RHODES, *supra* note 333, § 61:201.

356. 107 N.M. at 84, 752 P.2d at 799.

357. M. RHODES, *supra* note 333, § 61:203.

358. 86 N.M. 160, 521 P.2d 122 (1974).

"premised on the fact that the tortfeasor had knowledge of the insurer's payment to the insured" and did not allow "the single cause of action rule, which is a form of res judicata, . . . to bar the insurer's lawsuit."[359] Thus, the court considered the tortfeasor's knowledge of payment and a subrogation claim "crucial to the application of res judicata in such cases."[360]

IV. BAD FAITH

The fundamental duties of an insurer to its insured are threefold: to pay proceeds, to defend, and to settle.[361] The relationship between insurer and insured, however, also implies good faith and fair dealing.[362] When insurers do not act in accordance with the standard of good faith they may be liable in a bad faith action.[363] Bad faith can be founded either in contract or in tort; New Mexico recognizes both causes of action.[364]

In *Jessen v. National Excess Insurance Co.*,[365] the supreme court affirmed an award of punitive damages in a first-party bad faith claim. The supreme court considered several issues. First, the court addressed whether the trial court erred in its instructions to the jury on punitive damages[366] and the standard of proof required to prove punitive damages.[367] The court also considered whether the trial court erred by not instructing the jury on a comparative bad faith standard.[368] Further, the court addressed whether the insurer could be liable for the bad faith of an independent contractor.[369] Finally, the court considered whether the attorneys, fees assessed against the insurance company were proper.[370]

Larry Jessen and Michael McCoun, airplane pilots, first procured insurance under a lessor's policy with National Excess Insurance Company (National) for a Cessna 310 airplane.[371] Part of this policy required Jessen to provide information about his piloting experience.[372] Jessen telephoned Ruth Corbett, an agent of National, and told her he had a current medical certificate and 1200 hours of total flying time.[373] One month

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359. *Martinez*, 107 N.M. at 84, 752 P.2d at 799.
360. *Id.*
361. R. JERRY, *supra* note 127, § 25(g).
362. *Id.*
363. *Id.*
364. The first New Mexico case to actually uphold an award of punitive damages in an insurance bad faith action based on breach of contract was Curtiss v. Aetna Life Ins. Co., 90 N.M. 105, 560 P.2d 169 (Ct. App.), *cert. denied*, 90 N.M. 7, 558 P.2d 619 (1976). The following cases have recognized the tort of bad faith: State Farm Gen. Ins. Co. v. Clifton, 86 N.M. 757, 759, 527 P.2d 798, 800 (1974); Travelers Ins. Co. v. Montoya, 90 N.M. 556, 566 P.2d 105 (Ct. App. 1977); Chavez v. Chenoweth, 89 N.M. 423, 429, 553 P.2d 703, 709 (Ct. App. 1976).
365. 108 N.M. 625, 776 P.2d 1244 (1989).
366. *Id.* at 627, 776 P.2d at 1246.
367. *Id.* at 628, 776 P.2d at 1247.
368. *Id.* at 630, 776 P.2d at 1249.
369. *Id.* at 629, 776 P.2d at 1248.
370. *Id.* at 630, 776 P.2d at 1249.
371. *Id.* at 626, 776 P.2d at 1245.
372. *Id.*
373. *Id.*

after Jensen and McCoun were added to the lessor's policy, they decided to buy the airplane and sought to continue the insurance coverage under the previous airplane owner's policy with National.[374] Jessen contacted Corbett, signed an insurance application, and paid one-third of the first year's premium.[375] Two days later, Jessen and McCoun were involved in an airplane accident; although they received only minor injuries, the plane was destroyed.[376]

National conducted an independent investigation of the crash.[377] The pilot logbook, the only verification of Jessen's flight experience, was never found.[378] Jessen, however, signed an Airman's Records Release allowing National's investigator to obtain copies of Jessen's records from the FAA.[379] Jessen also offered National an affidavit stating that the 1200 hours flying time was accurately represented in the insurance application.[380]

Six months later National made a settlement offer of $11,000; however, the policy provided coverage up to $25,000.[381] Jessen and McCoun refused to settle and filed an action for bad faith and breach of contract.[382] Two years passed before the case came to trial; during this time National neither paid nor denied Jessen and McCoun's claim.[383]

At trial, the court instructed the jury that Jessen and McCoun had the burden of proof to show that National failed within a reasonable amount of time to pay proceeds as required by the policy, and in doing so, deviated from appropriate standards used in the insurance industry.[384] The court defined bad faith to the jury as "refusal to pay or delay in paying the claim for frivolous or unfounded reasons."[385] The jury awarded $25,000 compensatory damages and $75,000 punitive damages.[386] National appealed, arguing that the evidence was insufficient to support a jury instruction on punitive damages.[387]

In New Mexico, "bad faith supports an award of punitive damages upon a finding of entitlement to compensatory damages."[388] New Mexico has two standards for punitive damages in a breach of contract action. Punitive damages may be awarded "when the defendant's conduct was malicious, fraudulent, oppressive, or committed recklessly with a wanton

374. *Id.*
375. *Id.*
376. *Id.*
377. *Id.*
378. *Id.*
379. *Id.*
380. *Id.*
381. *Id.*
382. *Id.*
383. *Id.* at 627, 776 P.2d at 1246.
384. *Id.*
385. *Id.*
386. *Id.* at 626, 776 P.2d at 1245.
387. *Id.* at 627, 776 P.2d at 1246.
388. *Id.* (citing United Nuclear Corp. v. Allendale Mut. Ins. Co., 103 N.M. 480, 485, 709 P.2d 649, 654 (1985)).

disregard for the plaintiff's rights."[389] Secondly, in appropriate cases, punitive damages may be awarded for conduct which was "grossly negligent."[390] In *Jessen*, punitive damages were sought for grossly negligent conduct; accordingly, the supreme court reviewed the evidence to see if the award was supported under this standard.[391] National's witness testified that the claim would have been paid if Jessen had produced the logbook and that National believed it was not obligated to pay until the flight experience was positively verified.[392] On the other side, the court noted evidence that an investigator for National only spent seventy-two hours investigating the claim and did not attempt to fully verify Jessen's flight experience, despite access to the information.[393] Further, Jessen's expert testified that National's conduct was not in accordance with accepted industry standards and had "put an unduly harsh burden on the plaintiff."[394] Finally, the investigation did not reveal any misrepresentation on the part of Jessen.[395] Given this evidence, the supreme court held that an instruction of punitive damages was appropriate when the evidence "shows that the insurer utterly failed to exercise care for the interests of the insured in denying or delaying payment on an insurance policy."[396]

The trial court had instructed the jury that the standard of proof for punitive damages was "preponderance of the evidence," as set forth in *United Nuclear Corp. v. Allendale Mutual Insurance Co.*[397] National argued for the higher "clear and convincing" standard.[398] The court declined to readdress the *Allendale* standard because the plaintiffs had "justifiably relied" on this standard.[399]

The court also considered the absence of a jury instruction on comparative bad faith.[400] National asserted that since the trial court had instructed the jury on misrepresentations by the insured, the court should have also instructed the jury on a comparative bad faith standard.[401] National's support for this contention was twofold. First, New Mexico has recognized comparative negligence since *Bartlett v. New Mexico Welding Supply*.[402] Second, a California court has held that comparative fault applies in bad faith cases.[403] In *Jessen*, the supreme court held that the

389. *Id.* at 628, 776 P.2d at 1247 (citing Green Tree Acceptance Co. v. Layton, 108 N.M. 171, 173, 769 P.2d 84, 86 (1989)).
390. *Id.* (citing Valdez v. Cillessen & Son, 105 N.M. 575, 734 P.2d 1258 (1987); Valdez v. Warner, 106 N.M. 305, 742 P.2d 517 (Ct. App.), *cert. quashed*, 106 N.M. 353, 742 P.2d 1058 (1987)).
391. *Id.* at 627-28, 776 P.2d at 1246-47.
392. *Id.*
393. *Id.* at 627, 776 P.2d at 1246.
394. *Id.* at 628, 776 P.2d at 1247.
395. *Id.*
396. *Id.*
397. 103 N.M. 480, 484, 709 P.2d 649, 654 (1983).
398. *Jessen*, 108 N.M. at 628, 776 P.2d at 1247.
399. *Id.* at 629, 776 P.2d at 1248.
400. *Id.* at 630, 776 P.2d at 1249.
401. *Id.*
402. 98 N.M. 152, 646 P.2d 579 (Ct. App.), *cert. denied*, 98 N.M. 336, 648 P.2d 794 (1982).
403. California Cas. Gen. Ins. Co. v. Superior Court, 173 Cal. App. 3d 274, 218 Cal. Rptr. 817 (1985).

trial court's failure to give a comparative bad faith instruction was not error, because the jury considered but did not find misrepresentation.[404] If the jury had found misrepresentation by the plaintiff, Jessen, this finding would have barred an award of compensatory and punitive damages pursuant to the terms of the insurance policy.[405]

National also asserted that punitive damages should not be assessed against it for the acts of the investigator, an independent contractor.[406] The court rejected this defense.[407] The court noted that an absolute duty, imposed by the common law, statute, or municipal ordinance, cannot be delegated to an independent contractor.[408] Particularly in insurance dealings, "the duty of good faith dealing by parties to an insurance contract has been recognized as a nondelegable duty."[409] This led the court to hold that the acts of an independent contractor did not relieve National of its liability.[410]

Finally, National argued that the award of attorneys' fees was improper.[411] National asserted that under the statutory provision for attorneys' fees and costs,[412] the trial court must find the insurer acted unreasonably in failing to pay the claim.[413] Since no such finding was made, National asserted that the trial court erred in awarding attorneys' fees.[414] The court held that because the trial court instructed the jury on a reckless as well as a gross negligence standard, the award of punitive damages implied a finding of unreasonableness.[415] Unreasonableness may be implied because the unreasonable tortious action "is subsumed under the more egregious standards of recklessness or gross negligence."[416] Further, the standard for reviewing a punitive damages award is abuse of discretion, and "[b]ased on the implied finding of unreasonableness, the trial court did not abuse its discretion."[417]

V. FEDERAL PREEMPTION

Sappington v. Covington[418] involved a common law negligence claim alleged by Sappington against insurance agents James Covington and Larry G. Brodie. Sappington, an employee of Levy Auto Supply (Levy),

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404. *Jessen*, 108 N.M. at 630, 776 P.2d at 1249.
405. *Id.*
406. *Id.* at 629, 776 P.2d at 1248.
407. *Id.*
408. *Id.* (citing Budagher v. Amrep Corp., 97 N.M. 116, 121, 637 P.2d 547, 552 (1981)).
409. *Id.* (citing Timmon v. Royal Globe Ins. Co., 653 P.2d 907 (Okla. 1982)).
410. *Id.* Alternatively, the evidence provided adequate support to find ratification of the investigator's actions by National. *Id.* at 628, 776 P.2d at 1249.
411. *Id.* at 628, 776 P.2d at 1249.
412. N.M. STAT. ANN. § 39-2-1 (1978).
413. *Jessen*, 108 N.M. at 630, 776 P.2d at 1249.
414. *Id.*
415. *Id.*
416. *Id.*
417. *Id.* at 630-31, 776 P.2d at 1249-50.
418. 108 N.M. 155, 768 P.2d 354 (Ct. App. 1988).

incurred hospital expenses of approximately $20,000 during an illness.[419] Sappington unsuccessfully sought reimbursement under an insurance plan purported to be for the benefit of Levy's employees.[420] Sappington filed suit against Covington.[421]

The complaint alleged that the insurance policy was issued by a company which was not licensed to do business in New Mexico, that insolvency proceedings had begun against the company in Texas, and that the insurance agents represented that the plaintiff was fully insured.[422] The complaint further alleged that the insurance agent negligently failed to determine the status of the company and sold the insurance policy without first determining whether or not the company was solvent.[423] Finally, the complaint alleged that the agents knew or should have known that the company issuing the policy was not in good standing in New Mexico.[424]

The defendant moved for dismissal on the grounds that the claim was barred by federal preemption under the Employee Retirement Income Security Act of 1974 (ERISA).[425] The motion to dismiss was denied.[426] The court of appeals granted interlocutory appeal to consider the preemption issue.[427]

"The supremacy clause mandates that federal law overrides, i.e., preempts, any state regulation where there is an actual conflict between two sets of legislation such that both cannot stand."[428] Insurance law, which is pervasively regulated by the states, is not ordinarily subject to federal preemption. Under the McCarran Ferguson Act[429] Congress provided that "the business of insurance . . . shall be subject to the laws of the several States"[430] and "[n]o Act of Congress shall be construed to invalidate, impair or supersede any law enacted by any State for the purpose of regulating the business of insurance."[431]

ERISA, however, contains a broad preemption clause which provides that, with few exceptions, the Act "shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan."[432] It was not disputed that the health insurance policy involved

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419. *Id.* at 156, 768 P.2d at 355.
420. *Id.*
421. *Id.*
422. *Id.*
423. *Id.*
424. *Id.*
425. *Id.*
426. *Id.*
427. *Id.*
428. J. NOWAK, R. ROTUNDA & J. YOUNG, CONSTITUTIONAL LAW § 9.1, at 295 (3d ed. 1986).
429. 15 U.S.C. §§ 1011-1015 (1985).
430. 15 U.S.C. § 1012(a) (1985).
431. 15 U.S.C. § 1012(b) (1985).
432. 29 U.S.C. § 1144(a) (1985). The ERISA preemption structure is three-part. The preemption clause is modified by a "savings clause," 29 U.S.C. § 1144(b)(2)(A), and in turn, the "savings clause" is modified by a "deemer clause," 29 U.S.C. § 1144(b)(2)(B). Although the preemption statement is broad, the "savings clause" gives the states latitude to regulate in banking, insurance, or securities. As stated in section 1144(b)(2)(A), "nothing in this subchapter shall be construed to exempt or relieve any person from any law of any State which regulates insurance, banking or

in this case was an employee benefit plan under which any interest in the benefits of the plan would be protected by ERISA.[433] Any state law directly or indirectly related to the employee benefit plan would be preempted by ERISA.[434] Furthermore, the words "relate to" are broadly interpreted when considering the extent of federal preemption.[435]

The court, however, concluded that Congress did not intend for state law on the negligence of insurance agents in selling valid policies to be preempted by ERISA.[436] "The relief sought by plaintiff does not affect the administration of any plan, nor is plaintiff's claim of liability against defendant predicated on any right or standard contained in ERISA."[437]

ERISA "does not attempt to set standards for or regulate the conduct of insurance agents involved in acquiring or establising an employee benefit plan if the agent is not further involved in creation or administration of the plan."[438] More importantly, ERISA does not "set standards or attempt to regulate the purchase or sale of insurance policies that, because of the alleged conduct of an agent, never in fact ripen into a [sic] ERISA-regulated employee benefit plan."[439] Applying these principles, the court of appeals emphasized that Sappington's claim focused on the sale of an insurance policy preceding the institution of a benefit plan.[440] Thus, the court of appeals affirmed the trial court's denial of the defendant's motion to dismiss.[441]

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securities." However, the "deemer clause" prevents states from trying to avoid ERISA under the pretext of the "savings clause."

> Neither an employee benefit plan . . . nor any trust established under such a plan, shall be deemed to be an insurance company or other insurer, bank, trust company, or investment company or to be engaged in the business of insurance or banking for purposes of any law of any State purporting to regulate insurance companies, insurance contracts, banks, trust companies, or investment companies.

Id. § 1144(b)(2)(B).

433. *Sappington*, 108 N.M. at 157, 768 P.2d at 356. The court held that the purpose of ERISA was

> to protect the interests of participants in employee benefit plans by requiring disclosure and reporting of financial and other information to participants by establishing standards of conduct, responsibility, and obligation, for plan fiduciaries, and by providing appropriate remedies and sanctions for breach of the duties set forth in the statute.

Id. at 156, 768 P.2d at 355 (citing 29 U.S.C. § 1001(b) (1985)).

434. *Id.* at 157-58, 768 P.2d at 356-57.

435. *Id.* at 156, 768 P.2d at 355 (citing Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41 (1987)).

436. *Id.* at 158, 768 P.2d at 357. In Metropolitan Life Ins. Co. v. Massachusetts, 471 U.S. 724, 741 (1985), the Supreme Court stated that state laws regulating those who sell insurance and their sales practices do not "relate to" employee benefit plans and are not preempted.

437. *Sappington*, 108 N.M. at 158, 768 P.2d at 357.

438. *Id.*

439. *Id.*

440. *Id.*

441. *Id.*