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Katy Brautigam

Alexander Blewett III School of Law

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PRECAP; *West v. USAA*: A Legal Obligation to Subrogate?

Katy Brautigam

I. QUESTION PRESENTED

Is an insurance carrier legally obligated to honor a known TRICARE lien in the settlement of a third-party liability claim? If not, is the carrier's attempt to do so unreasonable as a matter of law?

This case is noteworthy because it presents the Court with its first opportunity to consider what subrogation obligations exist between an insurance company, a federal health benefits program, and an injured claimant in the context of a third-party liability claim. The Court's decision as to the insurer's lien obligations could have a substantial impact upon future tort victims in third-party liability claims in Montana.

II. FACTUAL AND PROCEDURAL BACKGROUND

Peter Lee and three others were injured in a one-car automobile accident caused by Julian Perez in December 2012.¹ Perez was insured through United Services Automobile Association and USAA Casualty Insurance Company (collectively, "USAA").² USAA determined that Perez was 100% at fault for the accident.³ Lee was active duty military and a beneficiary of TRICARE, a federal health benefits program for members of the armed forces.⁴

The damages to Lee and the three passengers involved in the accident exceeded \$100,000, surpassing the limits of Perez's liability policy with USAA.⁵ Lee and the other injured parties agreed to hold Perez harmless for all claims, including the TRICARE liens, in exchange for USAA's coverage of the policy limits.⁶ USAA would not cover the limits unless TRICARE was added to the settlement check as a secondary payer or until written waivers of lien had been obtained from TRICARE.⁷ USAA maintained that it was legally obligated to resolve the TRICARE liens before it could settle the case.⁸

Lee's legal guardian Elizabeth West sued USAA for bad faith after USAA refused to settle.⁹ West maintained that USAA sought to

¹ Appellee's Response Brief, *West v. USAA*, 2015 WL 3427104 at *4 (Mont. 2016) (No. DA 16-0097).

² Appellant's Opening Brief, *West v. USAA*, 2015 WL 3006010 at *1 (Mont. 2016) (No. DA 16-0097).

³ Appellee's Response Brief, *supra* note 1, at *5.

⁴ *Id.* at *4, Appellant's Opening Brief, *supra* note 2, at *4.

⁵ Appellee's Response Brief, *supra* note 1, at *3-5.

⁶ *Id.* at *3.

⁷ *Id.* at *5.

⁸ Appellant's Opening Brief, *supra* note 2, at *9.

⁹ Appellee's Response Brief, *supra* note 1, at *3.

delay payment to the injured party while benefitting from the interest on the TRICARE lien and exposing its insured to excess judgment.¹⁰

On October 26, 2015, District Court Judge Gregory G. Pinski of the Eighth Judicial District in Cascade County found in favor of West, granting summary judgment on the claim of bad faith.¹¹ The court found that USAA was not required under federal law to fulfill the TRICARE lien, and that its attempt to do so was unreasonable as a matter of law.¹² Judgment was entered against USAA in the amount of \$1,464,000.¹³ USAA filed a Motion to Alter or Amend Judgment on November 19, 2015, which was denied.¹⁴ USAA filed its appeal with the Supreme Court of Montana on May 20, 2016.¹⁵ West filed a motion to dismiss, which was denied on August 9, 2016.¹⁶

III. SUMMARY OF ARGUMENTS

USAA brings four claims on appeal: (1) whether the district court erred in concluding TRICARE was not a secondary payer; (2) whether the district court erred in finding that the TRICARE liens imposed no obligation requiring USAA to fulfill TRICARE's lien; (3) whether the district court erred in ruling that USAA did not have a reasonable basis in law and fact to protect TRICARE's lien; and (4) whether the district court erred in analyzing the legal principles that apply to liens.¹⁷

Of these, the primary issues that the oral argument is likely to focus on are: (1) whether an insurer carrier has a legal duty to honor a known TRICARE lien in a settlement of a third-party liability claim; and, (2) if there is no legal duty, then was it unreasonable for USAA to attempt to honor the TRICARE lien as part of the settlement?¹⁸

A. *An Insurance Carrier's Duties to Fulfill Known Liens in Third Party Liability Claims*

1. *USAA's Argument*

The first main issue on appeal is whether USAA's had a duty to fulfill a known lien with TRICARE before settling a third-party liability

¹⁰ *Id.*

¹¹ Appellant's Opening Brief, *supra* note 2, at *2.

¹² *Id.*

¹³ *Id.*

¹⁴ *Id.*

¹⁵ *Id.* at *39.

¹⁶ Order at *1, *West v. USAA*, <https://supremecourtdocket.mt.gov/view/DA%2016-0097%20Deny%20--%20Order?id={A0767156-0000-C610-A9AD-984E290FBA53}> (Mont. August 9, 2016) (No. DA 16-0097).

¹⁷ Appellant's Opening Brief, *supra* note 2, at *1.

¹⁸ *Id.*

claim.¹⁹ USAA argues that it was legally required under federal law to fulfill a known TRICARE lien before reaching a settlement with West.²⁰

USAA relies upon the Federal Medical Care Recovery Act, 42 U.S.C. § 2651, as its primary authority for its legal obligation to fulfill an known TRICARE lien.²¹ The Federal Medical Care Recovery Act enables the Federal Government to recover some of its annual expenses used to provide medical care to military personnel who have been injured by tortious conduct from third parties.²² The Act also seeks to prevent the unjust enrichment of victims, tortfeasors, and tortfeasor's insurance companies.²³ Because TRICARE is a federal healthcare benefits program, USAA argues that 42 U.S.C. § 2651 applies to TRICARE.²⁴

USAA's argument next relies upon a handful of federal regulations, the primary one being 42 C.F.R. § 411.24(i)(1).²⁵ The regulation states that if a Medicare lien is not fulfilled, the primary payer must reimburse Medicare even if it has already reimbursed the beneficiary or other party.²⁶ USAA contends that although this regulation explicitly applies to Medicare, it implicitly includes TRICARE because applicable law governing TRICARE contains similar automatic first payer provisions like Medicare.²⁷ Thus, as the primary payer, USAA maintains that it had an obligation to honor the TRICARE lien before settling with West in order to avoid additional liability under federal law.²⁸

USAA then relies upon Mont. Code Ann. § 71-3-1117, which provides that an insurer will assume liability for failing to fulfill a known lien with a healthcare physician.²⁹ USAA contends that as an insurer, it was required under Montana law to fulfill their lien with TRICARE.

2. *West's Argument*

West agrees there is no question that the TRICARE liens needed to be resolved, and that USAA's potential liability to TRICARE existed, but she argues that USAA was fully protected by Lee and the other injured passengers, given their promise to resolve the liens and hold USAA harmless for any liens.³⁰

¹⁹ *Id.*

²⁰ *Id.* at *7.

²¹ *Id.*

²² *United States v. Trammel*, 899 F.2d 1483, 1486-87 (6th Cir. 1990).

²³ *Id.*

²⁴ Appellant's Opening Brief, *supra* note 2, at *4.

²⁵ *Id.* at *3.

²⁶ 42 C.F.R. § 411.24§ 411.24(i)(1) (Lexis Advance through the September 14, 2016).

²⁷ Appellant's Opening Brief, *supra* note 2, at *12.

²⁸ *Id.* at *12-14.

²⁹ MONT. CODE ANN. § 71-3-1117 (2015).

³⁰ Appellee's Response Brief, *supra* note 1, at *10-11, 15.

First, West argues that that 42 U.S.C. § 2651 does not require TRICARE to be added as a payee, because the statute contains no requirement that TRICARE must be added as a payee.³¹ Furthermore, the statute does not preclude a lien from being satisfied by injured claimants, nor does it require that lien payments must come directly from the insurer.³² Rather, the lien may be satisfied by the insurer's payments to the plaintiffs, who in turn agree to satisfy the lien and hold the insurer harmless.³³ Then, the plaintiffs' attorneys ensure that the lien is paid, because they are ethically bound to do so.³⁴

Next, West maintains that 42 C.F.R. § 411.24(i)(1) does not apply to TRICARE.³⁵ This statute expressly provides that an insurer is only liable "if Medicare is not reimbursed" and does not mention TRICARE.³⁶ Additionally, the statute only holds an insurer liable if the lien is not satisfied, but it does not require that the satisfaction come directly from the insurer.³⁷

Finally, West highlights USAA's inconsistency in requiring that TRICARE be added to Lee's check.³⁸ Although USAA contends that it was required under federal law to add TRICARE as a payee, USAA issued various checks to the other individuals involved in the same crash without adding TRICARE as a payee on those checks before resolving the TRICARE liens.³⁹

B. Whether an Insurance Carrier's Attempt to Fulfill Known Liens in a Third-Party Liability Claim Before Settling was Unreasonable as a Matter of Law or Bad Faith

1. USAA's Argument

The second issue on appeal is whether USAA's attempts to fulfill TRICARE's lien before settling was unreasonable as a matter of law or done in bad faith.⁴⁰ USAA contends that the district court erred in finding its actions unreasonable as a matter of law due to the court's first error in finding that USAA was not required to add TRICARE as a payee.⁴¹ USAA argues that the threshold issue was whether it was obligated under federal law to add TRICARE as a payee, but since the court did not agree with

³¹ *Id.* at *12–13.

³² *Id.* at *13.

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.* at *14.

³⁶ 42 C.F.R. § 411.24(i)(1); Plaintiff and Appellee's response brief, at *14.

³⁷ Appellee's Response Brief, *supra* note 1, at *14.

³⁸ *Id.* at *12.

³⁹ *Id.* at *11–12.

⁴⁰ Appellant's Opening Brief, *supra* note 2, at *1.

⁴¹ *Id.* at *10.

USAA, it found its actions unreasonable.⁴² “Once the District Court leaped to the erroneous conclusion that secondary payer status did not apply to TRICARE, it became the building block upon which all other erroneous conclusions reached by the District Court were built.”⁴³ USAA contends that because it was required to add TRICARE as a payee, there can be no bad faith failure to settle.⁴⁴ USAA additionally argues that the question of its reasonableness was a question of fact which should have remained with the jury.⁴⁵

2. *West’s Argument*

First, West relies on case law to show that a defendant’s inclusion of Medicare as a payee on a settlement check has been found to establish bad faith as a matter of law.⁴⁶ This is true despite Medicare’s “super lien” status per 42 U.S.C. § 1395y(b)(7) and 42 U.S.C. § 1395y(b)(8).⁴⁷ TRICARE is not held to such stringent requirements under federal law.⁴⁸ Thus, because courts have precluded insurers from adding Medicare as a payee and have found bad faith as a matter of law in some cases when insurers have attempted to do so, USAA’s inclusion of TRICARE as a payee is likewise required and constitutes bad faith as a matter of law in this case.⁴⁹

Next, West relies on a public policy argument to demonstrate that USAA’s actions were unreasonable. West contends that the promise by plaintiffs to indemnify and hold USAA harmless was a sufficient mechanism to resolve the TRICARE liens.⁵⁰ West’s attorneys have an ethical obligation to resolve these liens after putting them into a trust account according to Montana Rule of Professional Conduct 1.15(b).⁵¹ West asserts that this is a more fair, efficient, and customary way of resolving liens in Montana.⁵² Instead, USAA contended that it was legally required under federal law to ensure the payment of the TRICARE liens itself by adding TRICARE to the check prior to settlement.⁵³ West claims that USAA had an underlying motive for requiring TRICARE’s inclusion on the check.⁵⁴ USAA sought to delay settlement and earn interest on the

⁴² *Id.*

⁴³ *Id.*

⁴⁴ Appellee’s Response Brief, *supra* note 1, at *19.

⁴⁵ Appellant’s Opening Brief, *supra* note 2, at *10–11.

⁴⁶ Appellee’s Response Brief, *supra* note 1, at *18 (citing *Wisinski v. Am. Com. Group, Inc.*, 2011 WL 13744, at * 18 (W.D. Pa. Jan. 4, 2011); (*Reiners v. St. Landry Hosp. Serv. Dist. Two*, 2007—158 (La. App. 3 Cir. May 30, 2007)).

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *Id.* at *22.

⁵¹ *Id.* at *22.

⁵² *Id.* at *30.

⁵³ Appellant’s Opening Brief, *supra* note 2, at *7.

⁵⁴ Appellee’s Response Brief, *supra* note 1, at *21.

money for itself rather than allowing the victim and/or the IOLTA trust fund to do so.⁵⁵

Additionally, West contends that USAA's actions represent a pattern of bad faith and a "money saving scheme."⁵⁶ According to West, USAA's "self-serving approach to lien resolution is terribly unwieldy" and undermines "the ability of tort victims to resolve liens in an efficient manner."⁵⁷ USAA's "scheme" allows it to profit by holding onto the tort victim's settlement funds, prohibits tort victims from directly resolving liens with TRICARE, and prevents the plaintiffs' attorneys from complying with their ethical obligations.⁵⁸ USAA was sanctioned for similar conduct in 2011 by another court and did not appeal.⁵⁹

IV. ANALYSIS

This case hinges on an insurer's duties and fairness to tort victims. Ruling in West's favor would preserve the current lien resolution system that promotes the use of an attorney's trust account to hold the lien funds. Ruling in USAA's favor would create a duty on insurance carriers to resolve liens themselves before settling the claims with the injured parties. This would uphold the insurance practice of subrogation, which is becoming more common.

The Court may find that West has the more persuasive argument according to precedent and a strict interpretation of the federal statutes and regulations implicated in this case. A plain reading of the statutes and regulations demonstrates that TRICARE is not required to be named as a payee on settlement checks.⁶⁰ Additionally, federal courts have yet to hold that TRICARE is required to be added as a payee.⁶¹ Furthermore, there are several decisions from state courts holding that federal benefits programs like Medicare are not required to be added as payees, despite the presence of outstanding Medicare liens, when the plaintiff has agreed to hold the insurer harmless.⁶²

On the other hand, USAA has a strong argument from a practical and policy standpoint. If USAA was indeed acting in good faith in to fulfill what it considered to be an obligation under federal law, it had to choose between a sanction for failing to fulfill the TRICARE lien, or promptly setting the case and relying on West's attorneys to fulfill the lien. USAA had good reason to want to avoid a possible federal sanction, and it likely felt that it could not count on West holding USAA harmless.

⁵⁵ *Id.* at *9.

⁵⁶ *Id.* at *11.

⁵⁷ *Id.* at *21.

⁵⁸ *Id.* at *21–22.

⁵⁹ *Id.* at *25 (citing *Katz v. USAA Cas. Ins. Co.*, 2011 WL 11555131 (Fla. Cir. Ct. March 2, 2011)).

⁶⁰ *Id.* at *16–17.

⁶¹ *Id.*

⁶² *Id.* at *17.

Additionally, USAA likely did not want to rely on a third party to fulfill USAA's obligations to the federal government.

In weighing these arguments, the Court may also consider Mont. Code Ann. § 71-3-1117, which was relied upon by USAA. On its face, the statute applies only to healthcare physicians.⁶³ Insurance companies are not mentioned in the statute, so the Court may consider whether to extend it to protect insurance companies from liability if liens are not fulfilled.

As to the reasonableness and good faith argument, the Court is likely to look at USAA's business practices of subrogation to determine if there is a pattern of delay when attempting to fulfill liens. If West's allegations regarding USAA's delay and profiting scheme are correct, USAA may be in violation of Montana Code Annotated § 33-18-201, which lays out the obligations of insurance companies in Montana. Specifically, § 33-18-201(5) and (6) provide that insurers are to promptly settle cases.⁶⁴ If the Court rules in West's favor, it might consider whether USAA's subrogation policies violate this statute by failing to promptly settle cases.

V. SUMMARY

This case presents strong arguments on both sides. Although West won on summary judgment at the district court level, the Montana Supreme Court has decided to fully hear USAA's appeal, denying West's motion to dismiss USAA's case on procedural grounds.⁶⁵ This is a case of first impression in Montana and presents the Court with the opportunity to consider an insurance carrier's obligations to fulfill liens owed to a federal health benefits program.

⁶³ MONT. CODE ANN. § 71-3-1117.

⁶⁴ MONT. CODE ANN. § 33-18-201(5), (6).

⁶⁵ Order, *supra* note 16, at *1.