May 25, 2016

Subrogation of Medical-Expense Claims: A Proposal for Future Study

When an accident victim's medical expenses are initially paid for by a third party, that third party may seek reimbursement of those expenses from the victim, if the victim recovers from the person who caused the accident. Rights to reimbursement are frequently asserted by a variety of health care providers, including private health insurance companies, self-funded employer sponsored insurance (ERISA) plans, Medicare, and Medicaid. No uniform rules exist for determining reimbursement rights of these various health care providers, which gives rise to complicated issues for tort victims, their attorneys, health plans, the federal government, and individual states.

On April 28, 2016, the James Humphreys Center for Complex Litigation at The George Washington University Law School held a roundtable discussion to explore the myriad issues that arise by virtue of an actual or potential third-party right of recovery. Law professors, practicing lawyers, and compliance consultants attended, and an expert in lien resolution joined by teleconference. We actively sought out representatives from the Departments of Health & Human Services, Justice, and Labor, all of whom have responsibilities for subrogation components of various federal programs, but all declined to send either participants or even observers. The attendees, who are listed at the conclusion of this proposal, agreed that lien resolution, and the "subrogation" issues that arise, present many important, unresolved questions of law and professional responsibility for both experienced and new attorneys. [1]

It was the consensus of the conference participants that further study of subrogation would benefit litigants, the legal community, and the efficient administration of justice within the legal system. This proposal attempts to summarize many of the difficulties and challenges explored by the conference participants in the hope that the Section on Torts and Insurance Practice of the American Bar Association will consider subrogation as a topic for further study.

At the conference, the participants worked from a set of hypotheticals intended to illustrate various subrogation issues that litigants in the tort system frequently face. Even these simple hypotheticals, which are attached to this proposal, are greatly complicated because of different laws governing different types of third-party payers – private insurance companies, Medicare, Medicaid, or ERISA plans, some of which also vary on a state by state basis. With that source of complexity in mind, this proposal presents eight issues which the participants identified as particularly worthy of future exploration.

---

[1] Although "subrogation" may not be the technically correct term for all of these third-party claims, this proposal will use it in the interest of simplicity.

1. Duties of disclosure and investigation

Must the accident victim's attorney inquire as to the source of payment for the victim's accident-related medical bills? Must the attorney inform the payer about a potential or pending lawsuit, or the successful recovery of damages?

It was noted by conference participants that payers commonly require providers of medical services to obtain information from patients on whether an injury is the result of an accident. Using this disclosure, along with medical treatment codes entered by health care providers,[2] payers have some ability to identify patients with potential lawsuits and expenses attributable to an accident. What responsibility does the victim's attorney, under rules of professional responsibility or otherwise, have to cooperate in providing this information, and what are the potential consequences to the victim if his or her attorney fails to provide the requested information?

Does the accident victim or his attorney have a legal obligation to inform the payer about filed lawsuits or recovery of damages? When does any such duty arise and on what basis is it imposed? At present, Medicare seems to require only notice of payments, not of pending lawsuits. In some states, Medicaid requires attorneys to notify it of the commencement of legal proceedings. Non-government plans vary in their requirements. For ERISA plans, plan documents may impose contractual duties on employees, but most employees will not be aware of their contractual responsibilities to the plan administrator.

What are the victim's attorney's duties? Must the attorney investigate potential rights of subrogation? Will she be held liable (or violate rules of professional responsibility) for failing to inform a third-party payer? Can the attorney be personally liable for mishandling of a subrogation claim? According to some conference participants, dissipation of a damage award paid to a client might extinguish a payer's rights *against the victim*, but leave the victim's attorney responsible, for reimbursement of the payer's costs.

Finally, for defendants, what are their duties of disclosure to third-party payers, and what obligation to investigate might they, their attorneys, and their liability insurance carriers have to health care payers? Must the possibility of subrogation be investigated by the defense? Does this depend on whether the collateral source rule is applicable or who is the potential lien holder?

2. Legal status of subrogation for various types of third-party payers

What laws govern the right to subrogation, and how do they differ for the various types of third-party payers? According to conference participants, Medicare asserts a statutory right to reimbursement, and private or ERISA plans typically have contractual rights. Handling of

---

[2] The recently implemented ICD-10 standard for medical coding classifies medical treatments in detail, which enables payers to track past accident-related claims and to anticipate future costs of treatment.

Medicaid subrogation will vary from state to state. At least one state has attempted to enact laws setting forth default rules governing the division of damage awards between victim and subrogated payer and information that must be included in settlements or jury verdicts to facilitate that division.

How do subrogation laws differ from one state to another? To what extent do any provisions of Medicare, Medicaid, and ERISA preempt state laws – both substantive and procedural – related to subrogation? Does subrogation operate as a "lien" on the award, or does the duty to reimburse encompass a different legal or equitable remedy?

3. Third-party payers' potential obligation to cooperate

Conference participants noted that a plaintiff's attorney should attempt to negotiate with third-party payers early in the claims process, assuming the payer will participate. The reason is that those holding subrogation claims often take the position that once a settlement amount has been determined, there is nothing to "settle" that enables them to compromise the amount owed. Several topics for future study were identified: Do payers have an obligation to cooperate with beneficiaries regarding subrogation claims? Must payers acknowledge communications regarding subrogation? Must they negotiate in good faith regarding subrogation? Should failure to assert a right to subrogation prior to an award of damages, or refusal to negotiate the lien with the victim, compromise a payer's right to share in the award?

It was noted that the Center for Medicare and Medicaid Studies (CMS) rarely agrees to cooperate with Medicare beneficiaries who seek the agency's commitment to reduce part or all of a claim for subrogation. Anecdotally, local offices of CMS have sometimes agreed to talk with plaintiff's lawyers concerning subrogation, and in a few mass-tort cases, CMS has agreed to contractually limit subrogation according to pre-negotiated formulas. But CMS appears unwilling or unable to respond to routine individual inquiries until there is a resolution of the case. Would default legal rules or a simplified administrative mechanism enable CMS to handle subrogation of Medicare claims more effectively and fairly for both plaintiffs and defendants, as well as Medicare?

4. Conflicts among various claimants

The accident victim, the subrogated payer, and the attorneys all want to be paid in full. But they will have conflicting interests whenever a damage award is insufficient to fully compensate all of them. Whose right to payment is paramount? How is the remainder split?

Medicare and self-funded ERISA plans assert their superior right to payment. What happens when repayment to Medicare or an ERISA plan results in insufficient funds to compensate the tort victim or compensate the victim's attorney? Practicing attorneys report enduring the angry reactions of clients who are informed that most of the settlement will go to reimburse Medicare for its expenditures. When the award is insufficient, *who* determines how it is apportioned? Does Medicare have a right to accept less than full payment for its claim, and if not, should it have that right or even an obligation to do so under certain circumstances? If nothing remains for the client, does an attorney have a legal, or moral, duty to reduce her fee?

Does Medicare or another third-party payer have an obligation to pay its pro-rata portion of the attorney's fee, and if not, should it? Does a payer's refusal to pay its part of the attorney's fee create a free-rider problem? Does free-riding impair incentives to pursue accident claims? [3]

5. Issues of representation: who is the real client?

If, after deduction for attorney's fees and subrogation, the victim is left with almost nothing, who was the real client? Does the attorney owe lawyer-client duties to the third-party payer who will receive the bulk of the recovery? When must an attorney make payments to the holder of a subrogation claim contrary to the client's best interests? How are these ethical conflicts resolved? For instance, if an attorney thinks her client's dissipation of funds will extinguish the payer's equitable lien, may he or she advise the client to accept and spend the money before the plan takes action to protect its interest? What legal reforms might help to resolve any existing conflicts-of-interest, particularly regarding division of damage awards? Can, for example, verdict forms or settlement agreements be used to determine how the damages will be divided?

6. Payment of future medical expenses

When a damage award includes compensation for future medical expenses, a third-party payer might assert a right to a portion of that payment to reimburse it for those future payments. Generally, Medicaid cannot make such claims, because the victim may not be on Medicaid when future expenses are incurred. But because Medicare beneficiaries generally remain eligible for Medicare for life, CMS takes the position that federal law entitles it to obtain repayment for anticipated future expenses paid by it, as well as those already incurred. In workers' compensation recoveries, Medicare encourages beneficiaries to create a medical set-aside (MSA) trust from which future accident-related medical expenses will be paid.[4] Conference participants noted that Medicare's policies for set-asides for other types of awards are less clear than for workers' compensation. For ERISA plans, it is possible that they could assert claims for future

---

[3] In some states, individual physicians or "medical funding organizations" who are willing to underwrite medical costs, instead of taking a lower amount from a third party payer, will take a contingent interest in an accident victim's tort claim as compensation for treatment through what is commonly referred to as a "letter of protection." Such arrangements complicate the question of how much was "paid," and hence is subject to subrogation, and in some cases, it affects the proper measure of damages for the victim if the case proceeds to trial.

[4] Apparently, tort plaintiffs eligible for Medicaid are similarly allowed to put their damage awards into revocable trusts so that they can retain the award without forfeiting their means-tested eligibility for Medicaid.

medical expense payments, but that would be proper only if the victim remained on the same plan.

7. Settlement of mass-injury cases

The last topic addressed by the conference was how mass-injury cases should be handled. The hypothetical imagined pollution of a city's water supply, but the issues raised by this hypothetical can be generalized to any situation in which many people are injured, or potentially injured, by the same cause. Of particular interest to the conference participants was how to settle claims based on harms from prior events, but for which the injuries which are not yet manifest. The assumptions are that the approximate number of future injuries and the range of their severity can be predicted with some likelihood in a given population, but it is impossible to identify actual victims or what course of treatment they will require. In these complex multi-plaintiff situations, is there a simple way to arrive at rough justice on the subrogation issue for the potentially injured plaintiffs? An expert in mass-injury awards related his experience with using epidemiological data to predict future medical expenses, classify plaintiffs by injury type, and allocating damage awards according to preset formulas. For at least some mass-injury cases, it has been possible to negotiate subrogation in advance, with payers agreeing up front to receive a set percentage of each beneficiary's future damages payments. If that is a feasible approach for some mass torts, might it be workable for the more common single victim injury?

The second crucial issue in mass-injury, non-class action cases is how to obtain agreement to a settlement offer among many co-plaintiffs. It is increasingly common for all plaintiffs to agree to be bound by any settlement agreement which gains the approval of a negotiated fraction of all the co-plaintiffs (e.g., 70%). This mechanism prevents a few holdouts from scuttling a deal that the supermajority finds reasonable. This mechanism could be applied to situations in which subrogation complicates settlement negotiation, but is that desirable?

8. Enforcement Issues

Particularly under ERISA, there has been considerable litigation regarding the proper method of assertion of subrogation claims. Similar issues arise under other laws, and one question that should be addressed is whether simplified procedures should be adopted that will entitle valid subrogation claims to be enforced, with a maximum of clarity and efficiency, and a minimum of cost and burden to victims, defendants, and their counsel. Although not discussed at the conference, the federal Medical Care Recovery Act, which is most commonly used to reimburse the United States for the costs of medical treatment of members of the military injured by the negligence of third parties, employs a different means of recovery used for other subrogation claims, and therefore should be considered as part of any study.

9. Education of lawyers about subrogation

Conference participants suggested that subrogation is more complicated than many lawyers recognize and that better education and reference resources would improve the quality of representation victims receive and resolve current ethical issues faced by the bar. They agreed that even attorneys who specialize in cases raising theses issue may be uncertain how to resolve asserted liens because of the many different, complicated laws that may apply depending on the identity of the lien holder.

If not fully informed about subrogation, a lawyer might miss vital opportunities for negotiation that are only available early in the representation. For example, if an attorney believes that a pending settlement will be insufficient to fully compensate the victim after reimbursement of paid medical expenses, the attorney should attempt to negotiate with the payer *before* settlement. Conference participants suggested, for example, that after settlement, an ERISA plan administrator cannot – as a fiduciary to the plan – negotiate the amount of subrogation. *Before* settlement, however, the administrator may release the plan's right of subrogation in exchange for a reduced amount of reimbursement without breaching any fiduciary duty. Development of educational programs and resources on the substantive, procedural, and ethical aspects of subrogation would, the conference participants agreed, help lawyers avoid subrogation pitfalls like this and many others.

++++++++

As expected, the conference raised many complex and intertwined issues. We hope that this summary reveals enough of the many problems relating to subrogation to incite some interest in the topic and that the Torts and Insurance Practice Section of the American Bar Association will consider subrogation as a subject for future study.

Alan Morrison & Roger Trangsrud [5]

[5] A draft of this proposal was circulated to other conference participants for their suggestions. They did not have a final sign off, and hence the responsibility for it is ours. We gratefully acknowledge the assistance in the preparation of this proposal of James Whittle, Class of 2016 at The George Washington University Law School.

Participants - Subrogation Conference

Affiliations For Identification Purposes Only

Shana DeCaro, DeCaro & Kaplen, LLP

David Farber, King & Spalding

Matt Garretson, The Garretson Group

Jan Gilbert, Motley Rice

Suzanne Jackson, George Washington Law School

Michael V. Kaplen, DeCaro & Kaplen, LLP

Francis McGovern, Duke Law School

Michael Merlino, Sedgwick CMS

Alan Morrison, George Washington Law School

Brian Rabinovitz, North Carolina Attorney General's Office

Heather Sanderson, Franco Signor

Marc Salm, Publix Super Markets

Peter Stris, Stris & Maher

Jay Tidmarsh, Notre Dame Law School

John Tomsky, Sullivan Papain Block McGrath & Cannavo

Roger Trangsrud, George Washington Law School

Mary Helen Wimberly, Hogan Lovells