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Fortis Benefits v. Cantu: The Un-"whole"-y Doctrine

On November 2, 2007, the Supreme Court of Texas denied Vanessa Cantu's and Ford Motor Company's motion for rehearing in a case against Fortis Benefits. By doing so, the Court solidified its first move away from what is known as the "made whole" doctrine. *Fortis Benefits v. Cantu*, 234 S.W.3d 642 (Tex. 2007).

A. The Background Facts

Vanessa Cantu ("Cantu") was seriously injured in an automobile accident. Fortis Benefits ("Fortis"), as her insurer, provided Cantu with benefits under her medical insurance policy. Later, Cantu filed a lawsuit against the driver of the car in which she was riding at the time of the accident, the driver's employer, the seller of the vehicle, and Ford Motor Company ("Ford")—the manufacturer of the vehicle. Fortis intervened asserting that it was entitled to equitable subrogation and reimbursement from any tort recovery in the amount of medical benefits paid under its policy. During a pre-trial conference, Fortis agreed with all the parties to be excused from the proceedings, looking only to Cantu during the post-verdict phase to resolve its claims.

Prior to trial, Cantu settled with the defendants for $1.445 million. Cantu and Fortis disagreed as to the amount of the settlement, if any, that should be paid to Fortis. As such, Cantu moved for summary judgment claiming that she had not been "made whole" by the settlement. Cantu contended that her past and future medical expenses (sans amounts for pain and suffering and the like) exceeded the settlement amount plus the amount paid to her by Fortis. Thus, Cantu argued, "the 'made whole' doctrine precluded Fortis's contractual claims of subrogation and reimbursement." *Id.* at 644. The trial court granted Cantu's motion for summary judgment and a divided court of appeals affirmed. *See Fortis Benefits v. Cantu*, 170 S.W.3d 755 (Tex. App.—Waco 2006, pet. granted). The Supreme Court, however, reversed and remanded the case to the trial court for further proceedings.

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CASES TO WATCH:

Excess Underwriters at Lloyd's, London v. Frank's Casing Crew & Rental Tools, Inc., 2005 WL 1252321 (Tex. May 27, 2005) (pending on rehearing) (whether Texas recognizes a right of recoupment by an insurer against its insured)

Fairfield Ins. Co. v. Stephens Martin Paving, 381 F.3d 435 (5th Cir. 2004) (certified to the Supreme Court of Texas and argued on November 9, 2004) (whether an award of punitive damages is insurable under an employers liability policy)

Ulico Cas. Co. v. Allied Pilots Ass'n, 187 S.W.3d 91 (Tex. App.—Ft. Worth 2005, pet. granted) (argued on April 11, 2007) (whether Texas recognizes coverage by waiver and/or estoppel when an insurer undertakes the defense without adequately reserving rights)

American Home Assur. Co., Inc. v. Unauthorized Practice of Law Comm., 121 S.W.3d 831 (Tex. App.—Eastland 2003, pet granted) (argued on September 28, 2005) (scope of the tripartite relationship between insurer, insured, and defense counsel retained by insurer)

B. The "Made Whole" Doctrine

The Supreme Court of Texas first recognized the "made whole" doctrine in *Ortiz v. Great Southern Fire & Casualty Insurance Co.*, 597 S.W.2d 342 (Tex. 1980). The Court, in *Ortiz*, reversed a lower court's decision and held that "[a]n insurer is not entitled to subrogation if the insured's loss is in excess of the amounts recovered from the insurer and the third party causing the loss." *Fortis Benefits*, 234 S.W.3d at 645 (quoting *Ortiz*, 597 S.W.2d at 343). The Court explained that in deciding *Ortiz* it recognized that equity cuts both ways depending on the facts of a situation. Thus, just as equity requires prevention of an insured from obtaining a double recovery—first from the insurer and then from the tortfeasor—equity also means that if either the insured or insurer must recover less than its losses, then the insurer must take the loss as the insured paid the insurer to assume that risk. *Id.* In other words, the insured must be "made whole" before the insurer.

In *Fortis Benefits*, the Court made clear that had Fortis sought *equitable* subrogation, then *Ortiz* would have been controlling case law. Because Fortis sought *contractual* rights of "subrogation" and "reimbursement," however, the "made whole" doctrine did not apply. The Court discussed a Fifth Circuit opinion, as well as an El Paso Court of Appeals decision upon which the Fifth Circuit had relied. *Id.* at 646 (citing *Oss v. United Servs. Automobile Ass'n* , 807 F.2d 457 (5th Cir. 1987); *Means v. United Fid. Life Ins. Co.*, 550 S.W.2d 302 (Tex. Civ. App.—El Paso 1977, writ ref'd n.r.e.)). In *Oss*, the Fifth Circuit held that, in Texas, "the same principles govern both equitable and contractual subrogation," and therefore the "made whole" doctrine applied. *Id.* at 646 (quoting *Oss*, 807 F.2d at 460 (citing *Means*, 550 S.W.2d at 309)). Nevertheless, the Supreme Court rejected those decisions because *Oss* relied on *Means*, which was issued "against a legal landscape that did not yet include the 'made whole' doctrine." *Id.*

Turning to the differences between "legal" (or equitable) and "conventional" (or contractual) subrogation, the Court noted that the first depends on principles of equity while the second is governed by contract and the rules of contract interpretation. The Court discussed the Austin Court of Appeals findings that the right of subrogation has been given "unusually 'hospitable' treatment" in Texas, and that express subrogation agreements are given "considerable weight." *Id.* (citing *Lexington Ins. Co. v. Gray*, 775 S.W.2d 679, 683 (Tex. App.—Austin 1989, writ denied)). The Court also discussed the Austin Court of Appeals opinion in *Esparza v. Scott & White Health Plan*, in which it backed down from its

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CASES TO WATCH:
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OneBeacon Ins. Co. v. Don's Building Supply, Inc., 2007 WL 2258192 (5th Cir. Aug. 8, 2007) (certifying trigger issue to the Supreme Court of Texas)

Pine Oak Builders, Inc. v. Great Am. Lloyds Ins. Co., 2006 WL 1892669 (Tex. App.—Houston [14th Dist.] July 6, 2006, pet. granted) (scope of the eight-corners rule and proper trigger theory to apply to "property damage" cases)

Johnson v. State Farm Lloyds, 204 S.W.2d 897 (Tex. App.—Dallas 2006, pet. granted) (scope of the standard appraisal clause)

PAJ, Inc. v. Hanover Ins. Co., 170 S.W.3d 258 (Tex. App.—Dallas 2005, pet. granted) (whether a prejudice requirement for late notice applies to Coverage B)

Crocker v. National Union Fire Ins. Co. of Pittsburgh, Pa., 466 F.3d 347 (5th Cir. 2006) (certified to the Supreme Court of Texas and argued on January 25, 2007) (whether notice by the named insured inures to the benefit of an additional insured)

Lexington opinion. *Id.* at 647 (citing *Esparza*, 909 S.W.2d 548 (Tex. App.—Austin 1995, writ denied)). In *Esparza*, the appellate court held that a contractual subrogation provision does not answer the question of *when* and *how much* an insurer should be entitled to through subrogation. *Id.* (citing *Esparza*, 909 S.W.2d at 552). That court concluded that contracts "'confirm, but [do] not expand, the equitable subrogation rights of insurers,' and the equities must still be balanced to achieve justice." *Id.* (citations omitted).

The Supreme Court of Texas then said in *Fortis Benefits*:

> We do not disagree that equitable and contractual subrogation rest upon common principles, but contract rights generally arise from contract language; they do not derive their validity from principles of equity but directly from the parties' agreement. The policy declares the parties' rights and obligations, which are not generally supplanted by court-fashioned equitable rules that might apply, as a default gap-filler, in the absence of a valid contract. If subrogation arises independent of any contract, then an express subrogation agreement would be superfluous and serve only to acknowledge this preexisting right, a position we reject.

Id. at 647 (abrogating *Esparza*, 909 S.W.2d 548).

The Court found that its refusal to extend the "made whole" doctrine to contractual rights of subrogation and reimbursement was not a novel concept. It discussed precedent from the U.S. Supreme Court and the Fifth Circuit, dealing with ERISA subrogation cases. *Id.* at 648 (citing *Sereboff v. Mid Atlantic Medical Servs., Inc.*, ___ U.S. ___, 126 S.Ct. 1869, 164 L.Ed.2d 612 (2006); *Walker v. Wal-Mart Stores, Inc.*, 159 F.3d 938 (5th Cir. 1998) (per curiam). In *Sereboff*, the U.S. Supreme Court held that an ERISA health plan that included a written subrogation right could not be altered by equitable defenses that were "beside the point." *Id.* (quoting *Sereboff*, 126 S.Ct. at 1877). And, in *Walker*, the Fifth Circuit held that language in an ERISA health plan providing for recovery against "any and all" third-party settlements meant the insurer was entitled to reimbursement for all medical benefits paid under the plan. *Id.* (citing *Walker*, 159 F.3d at 939–40).

Finally, the Court reiterated that "equity follows the law," and so equitable doctrines must "conform to contractual and statutory

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mandates, not the other way around." *Id.* Thus, unless a contract violates positive law or public policy, equity must yield. Finding that subrogation and reimbursement claims clearly do not violate Texas public policy, the Court refused to allow equity to stand in the way of the parties' contract. *Id.* at 649. Similarly, the Court was "loathe" to rewrite the terms' of the parties' contract, noting that the Department of Insurance or the Legislature were better suited for that job. *Id.* "We agree with those courts holding that contract-based subrogation rights should be governed by the parties' express agreement and not invalidated by equitable considerations that might control by default in the absence of an agreement." *Id.* at 650.

C. Applying the Terms of the Parties' Contract

Having found that the "made whole" doctrine must yield to the parties' contractual agreement, the Court addressed the terms of the insurance policy at issue. The provision entitled "Subrogation Right" entitled Fortis the right of subrogation to *all* rights of recovery Cantu may have against *any* person or organization, including the proceeds of *any* settlement, but limited to the amount of benefits actually paid by Fortis. The Court said: "Nowhere does this provision suggest that Cantu must first be 'made whole' for Fortis to recover." *Id.* at 651. As such, the specific language in the party's contract controlled and the equities embedded in the "made whole" doctrine were pushed aside. Thus, the Court held that Fortis was entitled to recover the total amount of benefits it paid to Cantu from the $1.445 settlement. *Id.*

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Commentary:

For nearly three decades, Texas insureds have been entitled to the benefit of equity through the "made whole" doctrine. The *Fortis Benefits* decision, however, has changed the insurance law landscape. While logical on its surface, the Court's opinion deals a blow to insureds by prioritizing contract language over equity. Even so, as the Court noted, bargained-for contractual rights should take a back seat to positive law and public policy. And, shouldn't Texas public policy include the right of an insured to be "made whole" before its insurer that it paid premiums to is paid back?

The effects of the *Fortis Benefits* decision may not be clear quite yet. One can assume, though, that the "reasoning" of the decision will extend beyond health insurance to all forms of policies that contain specific subrogation language like that in *Fortis Benefits*. As such, after *Fortis Benefits*, the "made whole" doctrine probably will mean that insureds will "retain less" of their settlements with third parties.

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Lee H. Shidlofsky is a founding partner of Visser Shidlofsky LLP. His practice is devoted to representing and counseling corporate policyholders in the area of insurance law, risk management, contractual risk transfer, and extra-contractual issues. He is Treasurer of the Insurance Law Section and holds a council position in the Construction Law Section of the State Bar of Texas. He is the author of numerous articles and seminar papers and is a frequent speaker at continuing legal education seminars in Texas and across the country. Mr. Shidlofsky has been named a "Super Lawyer" by Texas Monthly Magazine each year since 2004, including a ranking as a Top 50 attorney in the Central and West Texas Region for 2007, and is ranked as a top insurance coverage lawyer by Chambers USA and Who's Who Legal.

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The Insurance Law Practice Group represents corporate policyholders that are in disputes with their insurance companies, provides advice to plaintiffs in complex litigation on how to best maximize an insurance recovery, and provides risk-management consultation in connection with a wide-variety of contractual risk transfer issues. The Insurance Law Practice Group handles first-party and third-party insurance claims in state and federal courts at both the trial and appellate court levels. The Insurance Law Practice Group is committed to practical and pragmatic solutions to insurance issues.

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