Anti-Subrogation and Setoff Provisions in Tort Claims Acts, and Unsettled Federal Preemption Issues

by Karen Tracy McElhinny and Paul D. Ellis

Anti-subrogation and collateral source setoff statutes are powerful weapons in a municipal attorney's arsenal:[1] they reduce settlement value, discourage the filing of lawsuits against municipalities, and limit risk at trial. However, aggressive federal Medicare reimbursement efforts weaken this weapon. This article summarizes anti-subrogation and setoff provisions, as judicially interpreted; discusses how municipal lawyers can use these provisions and argue for their adoption or extension; and discusses the significant financial loss to municipalities if courts rule that the federal Medicare reimbursement statute[2] preempts state anti-subrogation and setoff provisions.

Valuable Swords and Shields

Municipalities are faced with a plethora of litigation. Fortunately, in some states, municipalities also have protection against subrogation claims and the ability to offset collateral source payments against judgments in tort actions. For example, imagine a case where liability is a concern for a city, and the plaintiff claims $100,000 in medical bills, $90,000 of which have been paid by his private insurance carrier, with the plaintiff paying the balance out of his own pocket. The city attorney advises the plaintiff's attorney about the statutory anti-subrogation and setoff provisions, which shield the city from liability for the amount paid by the insurer, and convinces him to settle the case for $10,000 to $20,000. Where cities are self-insured or have a very high self-insured retention (SIR) limit, this can result in a significant savings in litigation and settlement costs.[3]

In cases where the municipality contests liability or has a business reason to try the case, the city attorney can use the anti-subrogation and setoff provisions as a sword, and move to preclude a plaintiff from claiming the "sticker price" of his medical bills (the $100,000 in the previous example), limiting him to his actual out-of-pocket damages at trial. Or, in some jurisdictions, the city may be able to advise the jury of the amounts paid by an insurer. This tool provides the defendant municipality with an evidentiary advantage at trial, and may result in savings even if the city is found liable.

In some states, municipalities are afforded both statutory protections against subrogation, and a setoff of collateral sources. For example, in New Jersey, if a claimant:

> receives or is entitled to receive benefits for the injuries allegedly incurred from a policy or policies of insurance or any other source other than a joint tortfeasor, such benefits shall be disclosed to the court and the amount thereof which duplicates any benefit contained in the award shall be deducted from any award against a public entity or public employee recovered by such claimant; provided, however, that nothing in this provision shall be construed to limit the rights of a beneficiary under a life insurance policy. No insurer or other person shall be entitled to bring an action under a subrogation provision and an insurance contract against a public entity or public employee.[4]

In other states, such as West Virginia and Pennsylvania,[5] courts have construed statutes that contain only an anti-subrogation or setoff provision as providing both kinds of protection. Court rulings in these states may help municipalities in other states in seeking a broader interpretation of statutory provisions. West Virginia's statute contains an anti-subrogation provision that states "[a]ll actions filed against a political subdivision shall be filed in the name of the real party or parties of interest and in no event may any claim be presented or recovery be had under the right of subrogation."[6] The West Virginia court has interpreted this provision as barring:

> a direct claim against and recovery from a political subdivision by a party claiming under a right of subrogation to the claim of another party against the subdivision; and also requires that there be an offset of any recovery by an injured plaintiff from a political subdivision in the amount of first-party insurance proceeds received by the plaintiff as compensation for their injuries or damages.[7]

Under Pennsylvania's statute, if:

> a claimant receives or is entitled to receive benefits under a policy of insurance other than a life insurance policy as a result of losses for which damages are recoverable [as listed in the section], the amount of such benefits shall be deducted from the amount of damages which would otherwise be recoverable by such claimant.[8]

Pennsylvania courts have interpreted this provision as prohibiting actions against municipalities by subrogated insurers.[9] Pennsylvania courts found that the equitable doctrine of subrogation places the subrogee in the same position as the one to whom he is subrogated; as such, because the injured party cannot recover against a political subdivision for amounts paid by an insurance carrier, the insurance carrier cannot have greater rights than he to whom it is subrogated.[10] This rationale could prove helpful in resisting subrogation efforts under Medicare reimbursement statutes.

Medicare and Preemption

A more difficult issue arises when a municipality faces a plaintiff whose medical bills have been paid not by a private insurer, but by the federal Medicare program.[11] The aging popula-

tion of America[12] means that the typical personal injury plaintiff in coming years will likely have his medical bills paid by Medicare.

Congress amended the Medicare Secondary Payment Statute[13] (MSP) with the passage of the Medicare, Medicaid and SCHIP Extension Act of 2007[14] (MMSEA). Recently, portions of MMSEA became effective, requiring Responsible Reporting Entities (RREs),[15] including insurers and self-insured entities, to report settlements to the Centers for Medicare and Medicaid Services (CMS) when damages were paid by Medicare.[16] The MMSEA contains substantial civil penalties for a failure to timely report a settlement to CMS.[17] While the statute has provided for subrogation and reimbursement rights for the federal government for some time, CMS has only recently begun aggressive enforcement, especially in cases not involving worker's compensation.[18] As such, municipalities in states with anti-subrogation or setoff provisions must determine how to comply with the MMSEA and MSP while, at the same time, protecting taxpayers' interests.

Medicare reimbursement and reporting requirements hamper the ability of municipalities to settle cases and protect themselves from excessive liability for damages that may be only tangentially related to the alleged negligence of the municipality. Consider our earlier example, where liability is a concern for the city and the plaintiff claims $100,000 in medical bills. Assume that Medicare has paid $90,000 for the medical care that the plaintiff claims as damages in the lawsuit, and that the plaintiff, again, has paid $10,000 out of his own pocket. Whereas the municipality settled the case reasonably for $10,000 to $20,000 when a private insurer was involved, the municipality here must protect Medicare's interests in recouping conditional payments for the plaintiff's medical care. If the city were to settle the case with the plaintiff, without reporting the settlement to CMS and paying CMS whatever amount CMS determines it is entitled to from the settlement, the city itself (assuming it has a SIR), as well as the city attorney and the city's insurer, can face substantial fines and (in the case of the individuals), personal liability. In addition, if the Medicare statute preempts the anti-subrogation statute, the city will have to pay CMS the amount CMS determines it is owed if the city wants to settle the case. Therefore, the city will either have to enter into a settlement agreement with the plaintiff (conditioned on CMS's approval) to pay a much higher amount—likely $100,000 or more—or take the case to trial. If the city takes the case to trial, the plaintiff will likely raise the issue of whether the setoff provisions in the state statute are preempted by the Medicare statutes.

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There is little case law on whether Medicare reimbursement statutes preempt state anti-subrogation laws. In *Lamb v. Village of Quincy*,[19] Lois Lamb had brought a slip and fall lawsuit against the Village of Quincy and received $13,573.01 in payments from Medicare for her medical bills. The trial court deducted that amount from the award against the Village. The Lambs appealed, arguing that the Ohio anti-subrogation and setoff provision was preempted by the Medicare reimbursement statute, 42 U.S.C. §1395y(b)(2). The Ohio Court of Appeals disagreed, finding that the Medicare reimbursement statute did *not* preempt Ohio's abrogation of the collateral source rule in suits against political subdivisions.[20]

The *Lamb* court noted that "Congress did not expressly state an intent to preempt state law, nor does Ohio's law law interfere with an application of this portion of the federal statute. Both statutes can, and do, exist harmoniously without one doing damage to the other."[21] However, the court also found that the federal Medicare reimbursement statute did preempt that portion of Ohio's statute that precluded subrogation:

> Section 1395y(b)(2)(B)(i) ... provides that when payment for an injury can be made under a worker's compensation plan or under an automobile or liability insurance policy, Medicare payments are conditional upon reimbursement to the federal government. Section 1395y(b)(2)(B)(ii) ... authorizes the United States to recover Medicare payments by bringing an action against 'any entity' which is required or responsible to pay under a primary plan. Section 2651(a), Title 42, U.S. Code authorizes the federal government to bring an independent cause of action against tortfeasors such as the Village of Quincy.[22]

Thus, "because these statutes and regulations specifically provide for the

continued on page 16



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federal government to be subrogated to any right or claim that an injured party may assert against a tortfeasor," the court concluded that the portion of Ohio's law, abrogating the subrogation rights of insurers against political subdivisions, had been "preempted by the federal government's statutory right to seek reimbursement for Medicare benefits received by the injured party."[23]

It does not appear from the *Lamb* opinion that the court considered whether the subrogee, Medicare, could succeed to a right not possessed by its subrogor, Ms. Lamb.[24] Accordingly, it would seem that the court's decision is at odds with the Ohio Supreme Court's later decision in *Galanos* v. *City of Cleveland*,[25] in that the *Lamb* court left intact the setoff provision that precluded Lamb from recovering for the medical bills paid by Medicare, but allowed Medicare to stand in her shoes and collect those payments. Thus, even under Ohio jurisprudence, a colorable argument exists that the rights of a subrogee cannot exceed the rights of its subrogor and, as such, the state anti-subrogation provisions are still viable when Medicare has paid a plaintiff's medical bills.

Dealing with Medicare Preemption

Municipal lawyers can use Ohio jurisprudence to argue that, even if Medicare reimbursement statutes preempt the anti-subrogation provisions of state laws, they do not preempt the setoff provisions of those laws.[26] This may be more difficult in those jurisdictions in which the setoff provisions are not explicitly stated in the state law.[27]

When faced with claims that the Medicare reimbursement statutes preempt anti-subrogation statutes, municipal lawyers can argue that the equitable doctrine of subrogation places the subrogee in the same position as the one to whom he is subrogated. It follows that, because the injured party cannot recover against a political subdivision for amounts paid by collateral sources, neither can Medicare. This is likely the best approach for those litigating in states with explicit setoff provisions in their statutes.[28]

Municipal attorneys can also argue that the Medicare statute does not *expressly* state that it is intended to preempt state statutes that provide for immunity from subrogation. Absent express preemption language, there is no compelling reason why the Medicare statute should take precedence over an equally valid statute that reflects the policies and values of the state. Both serve different purposes: the Medicare statute is intended to protect federal funds; the state statutes are intended to protect municipalities' funds. Further, the current federal Administration believes a statute no longer presumptively takes precedence simply because it was promulgated by the federal, as opposed to a state, government.[29]

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Anti-subrogation, collateral source rule setoffs, and federal preemption by Medicare statutes are evolving issues that merit attention by municipalities.[30] As more and more municipalities must select insurance arrangements that leave them with a substantial SIR, an increased exposure for medical bills paid by Medicare can create deficits in the public coffers.

Notes

1. Some states have abrogated the collateral source rule for all claims, and in those states, municipalities do not have separate protections from subrogation. Other states do not have anti-subrogation or setoff statutes.
2. 42 U.S.C. §1395y(b)(2) (West 2011).
3. In *Foster v. City of Keyser*, 501 S.E.2d 165, 186 n.18 (W.Va. 1997), the West Virginia Supreme Court noted "the clear and sole purpose of the statute is to provide financial benefit to political subdivisions." Similarly, the Ohio courts have stated: "The statute serves two purposes. It conserves financial resources of political subdivisions by limiting the tort liability. Secondly, it permits injured persons, who have no source of reimbursement for their damages, to recover for a tort committed by the political subdivisions." Menefee v. Queen City Metro, 550 N.E.2d 181, 182 (Ohio 1990).
4. N.J. STAT. ANN. § 59:9-2(e) (2000). *See* Hayes v. Pitts Grove Township Bd. of Educ., 635 A.2d 998 (N.J. Super. Ct. App. Div. 1994); Furey v. County of Ocean, 641 A.2d 1091 (N.J. Super. Ct. App. Div. 1994) (finding municipality entitled to setoff for social security and worker's compensation payments); Waldorf v. Shuta, 142 F.3d 601 (3d Cir. 1998) (finding Borough of Kenilworth entitled to a setoff for social security benefits). These cases support the proposition that the anti-subrogation and setoff provisions apply to government payments. *See also*, OHIO REV. CODE ANN. § 2744.05(B) (West 2011). This provides, "if a claimant receives or is entitled to receive benefits for injuries or loss allegedly incurred from a policy or policies of insurance or any other source, the benefits shall be disclosed to the court, and the amount of the benefits shall be deducted from any award against a political subdivision recovered by that claimant. No insurer or other person is entitled to bring an action under a subrogation provision in an insurance or other contract against a political subdivision with respect to those benefits. The amount of the benefit shall be deducted from an award against a political subdivision under division (B)(1) of this section regardless of whether the claimant may be under an obligation to pay back the benefit upon recovery, in whole or in part, for the claim. A claimant whose benefits have been deducted from an award under subdivision (B)(1) of this section is not considered fully compensated and shall not be required to reimburse a subrogated claim for benefits deducted from an award pursuant to division (B)(1) of this section."
5. W. VA. CODE §29-12A-13(c) (1986); 42 PA. CONS. STAT. ANN. §8553(d) (2007). Nebraska has a provision in its Political Subdivisions Tort Claims Act pertaining to vehicular pursuit claims that states, in

pertinent part, "[t]his section shall not relieve any public or private source required statutorily or contractually to pay benefits for disability or loss of earned income or medical expenses of the duty to pay such benefits when due. No such source of payment shall have any right of subrogation or contribution against the political subdivision." NEB. REV. STAT. § 13-911 (1981).
6. W. VA. CODE §29-12A-13(c) (1986).
7. Foster v. City of Keyser, 501 S.E.2d 165, 168 (W.Va. 1997). The court based its decision, in part, upon the rationale that reducing a plaintiff's recovery by the amount of first-party insurance proceeds a plaintiff received was consistent with the overall statutory purpose of the Act, by relieving the political subdivision from paying for damages to the extent the injured party had been compensated by the party's insurance. *Id*. at 187.
8. 42 PA. CONS. STAT. § 8553(d) (2007).
9. Michel v. City of Bethlehem, 478 A.2d 164, 165 (Pa. Commw. Ct. 1984).
10. *Id*. at 166.
11. A related issue is how courts will apply the anti-subrogation and setoff provisions in situations where the injured party's medical bills were paid not by a private insurer, but by a state Medicaid program. Decisions in this area have been inconsistent. *Compare* Galanos v. City of Cleveland, 638 N.E.2d 530 (Ohio 1994) (in claim brought against city where medicals bills paid by Ohio's Department of Human Services pursuant to the Medicaid program, a statute granting right of setoff for collateral benefits to political subdivisions precluded the Department of Human Services from exercising its right of subrogation) *with* Marmorino v. Housing Auth. of City of Newark, 461 A.2d 171 (N.J. Super. Ct. Law Div. 1983) (in a conflict between the Tort Claims Act, providing defendant with credit for collateral source of payments to plaintiff, and the Medicaid assistance program, a plaintiff in her action against Newark Housing Authority was not barred from including, as part of her damages, an amount for medical expenses paid by Medicaid, but court directs that if plaintiff succeeds, Medicaid is to be reimbursed).
12. *See* U.S. Census Bureau, *Current Population Reports*, May 2010, noting "[t]he population is also expected to become much older, with nearly one in five U.S. residents aged 65 and older in 2030."
13. 42 U.S.C.§ 1395y(b)(2) (West 2011).
14. *See generally*, 42 U.S.C. §1395y(b)(8) (West 2011).
15. If your municipality has a self-insured retention, it is a Responsible Reporting Entity.
16. *See* Roy A. Franco, Jeffrey J. Signor and Thomas S. Thornton III, *Resolution of a Case With a Medicare Claimant?*, FOR THE DEFENSE (May 2009), available at http://tinyurl.com/3n3h6lh (last visited May 09, 2011).
17. 42 U.S.C. § 1395y(b)(8)(C)-(E) (West 2011).
18. 42 U.S.C. §1395y(b)(2)(A)(iii) - (iv) (West 2011).
19. 636 N.E.2d 412 (Ohio Ct. App. 1983). The *Lamb* case was decided prior to the U.S. Supreme Court's decision in *FMC Corp. v. Holliday*, 498 U.S. 52 (1990). There, the Supreme Court held that anti-subrogation provisions in Pennsylvania's Motor Vehicle Financial Responsibility Law were preempted by ERISA, when such employee benefit plans were self-funded. *Id*. at 59. Some might argue that *FMC Corp*. signals a tendency to find that federal statutes preempt state statutes, but we would contend it is inapposite to the issue of whether Medicare reimbursement statutes preempt municipal anti-subrogation and setoff statutes. We also contend that more recent policy statements by the current federal Administration signal a new era of post-*FMC Corp*. anti-preemption. *See* Memorandum for the Heads of Executive Departments and Agencies, 74 Fed. Reg. 24693 (May 20, 2009).
20. 636 N.E.2d at 416. *See also*, Buchman v. Wayne Trace Local School Dist. Bd. of Educ., 652 N.E.2d 952 (Ohio 1995) (Social Security and Medicare benefits are the type of collateral source benefits contemplated by the Ohio law, R.C. 2744.05(B), and, as future collateral benefits, are deductible from the jury's verdict against a political subdivision).
21. *Id*.
22. *Id*.
23. *Id*.
24. *See* Galanos v. City of Cleveland, 638 N.E.2d 530 (Ohio 1994).
25. *Id*.
26. Based on *Lamb v. Village of Quincy*, 636 N.E.2d 412 (Ohio Ct. App. 1983) and *Buchman v. Wayne Trace Local School Dist. Bd. of Educ*., 652 N.E.2d 952 (Ohio 1995).
27. *See* Foster v. City of Keyser, 501 S.E.2d 165 (W.Va. 1997).
28. *See Galanos*, 638 N.E.2d at 532.
29. Memorandum for the Heads of Executive Departments and Agencies, 74 Fed. Reg. 24693 (May 20, 2009).
30. Another possible avenue is to advocate changes in federal legislation to alleviate the financial burden on municipalities caused by Medicare reimbursement statutes. Currently, one bill, H.R. 1063, the Strengthening Medicare and Repaying Taxpayers Act of 2011, proposes amendments to Medicare statutes that would make it easier to comply with the MMSEA. H.R. 1063, 112th Cong. (2011). As of March 14, 2011, the bill had been referred to the House Committee on Ways and Means. At the time this article was written, it was unclear whether the bill would pass. ML

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