UNDERINSURED MOTORIST COVERAGE: THE VALIDITY OF CONSENT TO SETTLE CLAUSES

TABLE OF CONTENTS

I. Underinsured Motorist Coverage 504
II. Consent to Settle Clauses 505
III. The Issue 505
IV. A Sample of Courts' Rulings on the Validity of Consent to Settle Clauses 506
A. Louisiana 506
B. Minnesota 507
C. New Mexico 509
D. Wisconsin 510
E. New Jersey 511
F. Texas 513
G. Washington 514
H. Iowa 516
V. Summation 518
VI. Conclusion 519

This note will discuss consent to settle clauses as they apply to underinsured motorist provisions in automobile insurance policies. A number of jurisdictions, including most recently Iowa, have ruled on the validity of these clauses, and the holdings of the courts are varied. Since many of the cases look to the prior decisions for guidance, they will be discussed in chronological order. Not every decision on this issue will be discussed. The decisions discussed in this note are those which this author considers a representative sampling of the jurisdictions. Most of these decisions include valuable analyses. Other jurisdictions have decided this issue, but not all have provided helpful or insightful opinions.[1]

As will be seen, courts look to any number of factors in determining the validity of consent to settle clauses in underinsured motorist provisions. These factors include statutory language and interpretation, policy language and interpretation, and the recognition or non-recognition of subrogation rights. Before discussing specific cases, it is important to understand underinsured motorist coverage and its purpose, and also the consent to settle clause and its purpose.

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1. *See, e.g.*, State Farm Mut. Auto. Ins. Co. v. Taglianetti, 122 A.D.2d 40, 504 N.Y.S.2d 476 (App. Div. 1986).

I. Underinsured Motorist Coverage

A typical underinsured motorist statute is Chapter 516A of the Iowa Code.[2] This chapter was originally enacted in 1967 to provide for uninsured motorist coverage.[3] The Iowa Supreme Court held that this chapter did not cover the situation involving an underinsured motorist.[4] In 1980, Chapter 516A was amended to include underinsured motorist coverage.[5] Section 516A.1 now reads, in part:

> No automobile liability or motor vehicle liability insurance policy insuring against liability for bodily injury or death arising out of the ownership, maintenance, or use of a motor vehicle shall be delivered or issued for delivery in this state with respect to any motor vehicle registered or principally garaged in this state, unless coverage is provided in such policy or supplemental thereto, for the protection of persons insured under such policy who are legally entitled to recover damages from the owner or operator of an uninsured motor vehicle or a hit-and-run motor vehicle or an underinsured motor vehicle . . . .
>
> However, the named insured may reject all of such coverage, or reject the uninsured motor vehicle or hit-and-run motor vehicle coverage, or reject the underinsured motor vehicle coverage, by written rejections signed by the named insured . . . .[6]

Simply put, this section requires all companies writing automobile policies in Iowa to offer uninsured and underinsured motorist coverage. This offer may be rejected only in writing by the insured.

It is important to understand the difference between uninsured and underinsured motorist coverage. An "uninsured motorist" is one who has no liability insurance to cover injuries sustained by others caused by his acts.[7] In this situation, if the insured party has uninsured motorist (UM) coverage, the UM carrier will pay the claim just as if the responsible party had liability coverage. This coverage is subject to the UM policy limits. The purpose is to guarantee a minimum recovery equal to the amount the responsible party is required to carry by statute.[8]

An "underinsured motorist" is one who has liability insurance, but not in an amount sufficient to compensate the victim fully.[9] This may be illustrated by an example in which the responsible party has liability limits of $25,000, and the insured has damages greater than the policy limits. In this situation the insured may look to his underinsured motorist (UIM) carrier

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2. Iowa Code §§ 516A.1-A.4 (1987).
3. Iowa Code Ann. §§ 516A.1-A.4 (West 1988).
4. *See* Detrick v. Aetna Cas. & Sur. Co., 261 Iowa 1246, 1253, 158 N.W.2d 99, 105 (1968).
5. 1980 Iowa Acts ch. 1106, §§ 6-7.
6. Iowa Code § 516A.1 (1987).
7. *See* Kluiter v. State Farm Mut. Auto. Ins. Co., 417 N.W.2d 74, 74-75 (Iowa 1987).
8. *Id.*
9. *Id.*

to pay his damages in excess of the payment received from the responsible party. Again, the amount the insured may recover from his UIM carrier is subject to the UIM policy limits. The purpose of UIM coverage is to compensate the insured for loss not covered by the responsible party's liability insurance or other resources.[10]

The above fact pattern is a simple illustration of UIM coverage, but it represents the basic idea. Exclusionary clauses are often added to UIM policies. One such exclusion found in many UIM policies is the "consent to settle" clause.

II. Consent to Settle Clauses

A consent to settle clause is often found in the "exclusions" section of automobile liability policies. Such a clause may state: "[T]he insurer does not provide Underinsured Motorist Coverage for bodily injury sustained by any person if that person or the legal representative settles the bodily injury claim without the insurer's consent."[11] If a consent to settle clause is in the policy, the insured must have any proposed settlement approved by the UIM carrier. Otherwise, the insured will be prohibited from making a claim for his UIM benefits. The purpose of the consent to settle clause is to protect the insurer's subrogation rights against the tortfeasor, and to eliminate the possibility of collusive cooperation between the insured and the tortfeasor.[12]

III. The Issue

This note will focus on the validity of consent to settle clauses in UIM policies. The problem which arises most often is illustrated by the following fact pattern: A and B are involved in a serious automobile accident caused by B's negligence. B has $100,000 in liability coverage. A has UIM coverage with policy limits of $200,000. A suffers damages in excess of $300,000. A wants to settle with B for B's $100,000 policy limits. Following this settlement, A plans to collect his $200,000 UIM limits. If A's UIM carrier will not consent to the settlement, can A settle with B without voiding his UIM coverage?

Recognizing that his liability is clear and that A's damages are in excess of $100,000, B would naturally want to settle with A for the policy limits to avoid costly litigation and to protect himself from excess liability. A would also want to settle to avoid costly and lengthy litigation and to expedite payment for his injuries. Depending on the jurisdiction, A's options may vary greatly. Sometimes the options are not clear.

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10. American States Ins. Co. v. Tollari, 362 N.W.2d 519, 522 (Iowa 1985).

11. 2 A. Widiss, Uninsured & Underinsured Motorist Insurance § 43.3 n.4 (2d ed. 1987).

12. *See* Sanford v. Richardson, 252 So. 2d 922, 926 (La. App. 1971).

IV. A Sample of Courts' Rulings on the Validity of Consent to Settle Clauses

A. *Louisiana*

In 1979, the Louisiana Supreme Court ruled on the validity of a consent to settle clause in the landmark case of *Niemann v. Travelers Insurance Co.*[13] This case was one of the first cases to deal with a fact pattern resembling the example above: the insured first settled with the tortfeasor and executed releases in favor of the tortfeasor and the tortfeasor's insurance carrier,[14] and then brought a claim against his UIM carrier.[15] The insurer claimed that the consent to settle clause had been violated, and that the insured could not bring the action.[16] The court stated that the issue presented was "whether a 'consent to settle clause' in an uninsured motorist policy is valid and operative, and whether a plaintiff who without his UM [UIM] carrier's consent settles and releases an Underinsured tortfeasor and that tortfeasor's liability insurance carrier has defeated his cause of action against the UM [UIM] carrier."[17]

Although the court had previously held that a consent to settle clause in a UM policy was invalid because it abrogated the UM coverage mandated by statute,[18] the court recognized that UIM coverage was a different matter.[19] The UIM policy in question contained both a consent to settle clause and a section providing the carrier with subrogation rights.[20] The court stated that if the insurer had subrogation rights which might have been affected by the plaintiff's release of an underinsured motorist, the consent to settle clause served a purpose—to protect those rights.[21] Therefore, the question was whether the UIM carrier had any rights which might have been impaired or prejudiced by the plaintiff's settlement with and release of the tortfeasor.[22] If the UIM carrier had no subrogation rights, the consent to settle clause served no purpose.[23]

The court looked to the state's underinsured motorist statute.[24] The Louisiana statute is very similar to the Iowa statute discussed above. The court concluded that the statute did not sanction a consent to settle clause, which in operation might serve to block the statutorily mandated UIM cov-

13. Niemann v. Travelers Ins. Co., 368 So. 2d 1003 (La. 1979).
14. *Id.* at 1004.
15. *Id.*
16. *Id.* at 1004-05.
17. *Id.* at 1004.
18. *See* Hebert v. Green, 311 So. 2d 223 (La. 1975).
19. Niemann v. Travelers Ins. Co., 368 So. 2d at 1006.
20. *Id.* at 1005.
21. *Id.* at 1006.
22. *Id.*
23. *Id.*
24. *Id.* at 1007.

erage.[25] The statute did not afford the UIM carrier subrogation rights, but only a right to reimbursement.[26] The court concluded: "No settlement or judgment has or will 'result from the exercise of the insured's rights against' the underinsured tortfeasor with respect to that portion of plaintiff's damages concerning which defendant would otherwise have reimbursement rights."[27]

The court recognized that its strict reading of the statute might seem harsh, but it also recognized that there might be public policy reasons to avoid a broad interpretation of the statute.[28] The court asked rhetorically, "Why should the insurer, mandated by statute to afford UM [UIM] coverage and receiving a premium for exposure over liability limits of the underinsured motorist, have the right to interfere with its insured's settlement with a liability carrier within policy limits, and that carrier's insured?"[29]

Although the court found it unnecessary to decide the case on considerations of public policy, it did discuss public policy in a footnote.[30] The court restated views presented in an earlier case, saying that compromises are to be favored.[31] If settlement and compromise are to be favored, then the parties should not be subjected to the direction and consent of an insurance company.[32] The court concluded: "A just weighing of the factors involved requires that the best interests of the public be protected by assuring that the plaintiffs-insureds be given a fair opportunity to recover . . . the fruits of the coverage for which they have readily paid premiums."[33]

The court determined that if the UIM carrier was to be granted a right to subrogation, the legislature would have to amend the UIM statute.[34] The court held that since the statute presently did not grant a right of subrogation, the subrogation clause of the policy was illegal, and that the consent to settle clause was without binding effect upon the insured and was invalid.[35]

B. *Minnesota*

In 1983, the consolidated case of *Schmidt v. Clothier*[36] gave the Minnesota Supreme Court an opportunity to rule on the validity of a consent to settle clause. The court formulated a procedure whereby the insured could

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25. *Id.* at 1006.
26. *Id.* at 1007.
27. *Id.*
28. *Id.*
29. *Id.*
30. *Id.* n.7.
31. *Id.* (quoting Hebert v. Green, 311 So. 2d 223, 229 (La. 1975) (quoting Moreau v. State Farm Mut. Auto. Ins. Co., 298 So. 2d 907, 913 (La. App. 1974) (Fruge, J., dissenting))).
32. *Id.*
33. *Id.*
34. *Id.* at 1008.
35. *Id.*
36. Schmidt v. Clothier, 338 N.W.2d 256 (Minn. 1983).

settle with the tortfeasor and still collect on his own UIM policy, and the UIM carrier could still protect its right to subrogation.

The facts of the first consolidated case are all which need be set out. The tortfeasor offered to settle with the insured for $100,000 in exchange for a full release.[37] The insured also carried $100,000 of UIM coverage.[38] Because it was clear that her damages exceeded $265,000 and that the tortfeasor was underinsured, the insured notified her UIM carrier that she intended to settle with the tortfeasor.[39] The UIM carrier refused to acquiesce in the settlement.[40] The relevant issue was "whether a general release executed as part of a settlement with the tortfeasor destroys the underinsurer's subrogation rights or precludes the insured from recovering underinsurance benefits."[41]

The UIM carrier argued that by settling with the tortfeasor, the insured destroyed the UIM carrier's right to subrogation as granted by statute.[42] Unlike the Louisiana and Iowa statutes previously discussed, the Minnesota No-Fault Automobile Insurance Act contained a subrogation section.[43] The court stated that "[s]ubrogation is a limited, not absolute, right that comes into existence only after the insurer has paid benefits to its insured . . . ."[44] Only after the insurer has paid the insured's UIM benefits will a subsequent release of the tortfeasor by the insured not affect the subrogation rights of the insurer.[45] No subrogation rights will arise if the tortfeasor is released before payment by the insurer.[46]

The UIM carrier argued that since its subrogation rights had been destroyed, it should not be required to pay the insured, since it had no hope of recovering damages from the tortfeasor.[47] But the court stated:

> It is the public policy of Minnesota that injured persons should not, by virtue of having purchased underinsurance, be placed in a financial position inferior to that which they would have held had the tortfeasor been fully insured . . . . Thus, we hold that settlement and release of an underinsured tortfeasor does not prelude recovery of underinsurance benefits.[48]

However, the court recognized that the UIM carrier must be able to protect itself in some manner. The court noted: "Subrogation rights depend

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37. *Id.* at 259.
38. *Id.*
39. *Id.*
40. *Id.*
41. *Id.* at 260.
42. *Id.* at 261.
43. MINN. STAT. § 65B.49 subd. 6(e) (1978) (repealed 1980).
44. Schmidt v. Clothier, 338 N.W.2d at 261-62.
45. *Id.* at 262.
46. *Id.*
47. *Id.*
48. *Id.*

on 'general principles of equity and the nature of the contract of insurance.' "[49] In this situation the equities balance in favor of the UIM carrier.[50] Since the UIM carrier can only protect its rights by paying the UIM benefits prior to the release of the tortfeasor, the UIM carrier is entitled to have notice of any tentative settlement and must be given an opportunity to protect its rights by paying the UIM benefits before the release of the tortfeasor.[51]

The court developed a procedure whereby the insurer could protect its rights. If an insured wanted to settle with a tortfeasor, he had to notify the insurer and give the insurer thirty days in which to give its consent.[52] The insurer could consent to the settlement, thereby forfeiting its right to subrogation and becoming liable for any claim by its insured.[53] If the insurer wanted to withhold consent and protect its subrogation rights, it had to tender a check to the insured for the settlement amount; it could then exercise its subrogation rights against the tortfeasor.[54] The UIM carrier could also settle the insured's claim for UIM benefits and still retain subrogation rights regardless of any subsequent settlement with the tortfeasor.[55] If the insurer did nothing, consent was assumed and all subrogation rights were extinguished; the insured could still receive UIM benefits.[56]

C. *New Mexico*

In *March v. Mountain States Mutual Casualty Co.*,[57] the Supreme Court of New Mexico also decided the validity of a consent to settle clause. In this case, the insured settled with the tortfeasor in exchange for a full release without the UIM carrier's consent.[58] When the insured later filed a claim with the UIM carrier, the insurer denied coverage, stating that the contract had been breached when the settlement was made without its consent.[59]

The court confirmed that the purpose of the consent to settle clause is to protect the insurer's subrogation rights.[60] The insured argued that the insurer had no subrogation rights, or alternatively that the insured's de-

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49. *Id.* (quoting Bacich v. Homeland Ins. Co., 212 Minn. 375, 376, 3 N.W.2d 665, 665 (1942)).
50. *Id.* at 263.
51. *Id.*
52. *Id.*
53. *Id.*
54. *Id.*
55. *Id.*
56. *Id.*
57. March v. Mountain States Mut. Cas. Co., 101 N.M. 689, 687 P.2d 1040 (1984).
58. *Id.* at ____, 687 P.2d at 1041.
59. *Id.*
60. *Id.* at ____, 687 P.2d at 1043.

struction of those rights did not affect the policy obligation.[61] Since the insurer paid no damages to the insured, the insurer possessed no subrogation rights.[62] The court determined that a settlement violated the policy's subrogation provision whether the settlement occurred before or after the insurer's payment of loss.[63] The court concluded that although a right of subrogation does not arise until a loss payment is made, a contingent right of subrogation arises when the loss occurs.[64]

The court clearly decided this case on a contractual basis. The insured argued that public policy dictated that such policy provisions should be void, and that New Mexico's insurance statutes did not specifically provide for subrogation.[65] The insured relied on the holding of *Niemann v. Travelers Insurance Co.*[66] The court responded by stating: "Although New Mexico insurance statutes do not specifically provide for subrogation rights, this Court has consistently recognized such rights as legitimate contractual matters and has implicitly authorized the use of consent provisions as a device to protect those rights."[67] The court held that the subrogation and consent provisions in UIM policies were valid, and that the insured can be denied UIM benefits if a settlement and release are executed without the insurer's consent.[68]

D. *Wisconsin*

In *Vogt v. Schroeder*,[69] the Wisconsin Supreme Court was faced with a consent to settle clause in a UIM policy. This clause was also accompanied by a subrogation provision.[70] The tortfeasor's insurer argued that subrogation rights should not be granted to the UIM carrier because there was no danger that a double recovery would occur.[71] The Wisconsin court had previously stated that subrogation has generally been an equity action to prevent double recovery on the part of the insured.[72] By the very nature of UIM coverage, the insured could not possibly be made more than whole; therefore no double recovery could occur.[73]

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61. *Id.* at ____, 687 P.2d at 1042.
62. *Id.*
63. *Id.*
64. *Id.* at ____, 687 P.2d at 1042-43.
65. *Id.* at ____, 687 P.2d at 1043.
66. *Id.* at ____, 687 P.2d at 1043-44 (citing Niemann v. Travelers Ins. Co., 368 So. 2d 1003 (La. 1979)).
67. *Id.* at ____, 687 P.2d at 1043.
68. *Id.* at ____, 687 P.2d at 1044.
69. Vogt v. Schroeder, 129 Wis. 2d 3, 383 N.W.2d 876 (1986).
70. *Id.* at ____, 383 N.W.2d at 878.
71. *Id.* at ____, 383 N.W.2d at 879.
72. *Id. See* Rimes v. State Farm Mut. Auto. Ins. Co., 106 Wis. 2d 263, 316 N.W.2d 348 (1982); Garrity v. Rural Mut. Ins. Co., 77 Wis. 2d 537, 253 N.W.2d 512 (1977).
73. Vogt v. Schroeder, 129 Wis. 2d 3, ____, 383 N.W.2d 876, 879 (1986).

The court noted that this argument had surface plausibility, but:

> [I]t overlooks the fact that subrogation is an equitable doctrine and depends upon a just resolution of a dispute under a particular set of facts . . . .
>
> There is a distinct and separate equitable policy—that the wrongdoer should be responsible for his conduct and not be allowed to go scot-free by failing to respond in damages while another, an indemnitor for the injured party, is required to do so.[74]

The court concluded, just as did the Minnesota Supreme Court in *Schmidt v. Clothier*,[75] that the UIM carrier had subrogation rights against the tortfeasor and his insurer to the extent of any benefits the UIM carrier paid to its insured.[76] After quoting the language of *Schmidt* extensively, the court concluded that the procedure developed by the Minnesota court was the procedure to be used in Wisconsin.[77] It deviated from the Minnesota procedure by refusing to set a specific time limit for the UIM carrier to act, and instead leaving it to the trial court on remand to determine a reasonable time.[78] Interestingly, this court did not discuss the relevant UIM statute in its holding.

E. *New Jersey*

In *Longworth v. Ohio Casualty Group of Insurance Companies*,[79] a New Jersey superior court determined the validity of a consent to settle clause. The facts in this case were slightly different from those in the previously discussed cases.

In *Longworth*, the insured filed a declaratory judgment action against her UIM carrier seeking benefits under her UIM policy.[80] There was also an underlying tort action involving the insured and the underinsured tortfeasor.[81] The tortfeasor had wanted to settle for his policy limits in return for a full release, but the insured could not settle without her UIM carrier's consent if she was to collect her UIM benefits.[82] The UIM carrier refused to consent to the settlement and insisted that the underlying tort action must be taken to judgment before any obligation could arise on the part of the UIM carrier.[83]

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74. *Id.* at ____, 383 N.W.2d at 879-80.
75. *See supra* notes 36-56 and accompanying text.
76. Vogt v. Schroeder, 129 Wis. 2d 3, ____, 383 N.W.2d 876, 879-80 (1986).
77. *Id.* at ____, 383 N.W.2d at 885.
78. *Id.*
79. Longsworth v. Ohio Cas. Group of Ins. Cos., 213 N.J. Super. 70, 516 A.2d 287 (Law Div. 1986).
80. *Id.* at ____, 516 A.2d at 289.
81. *Id.*
82. *Id.* at ____, 516 A.2d at 293.
83. *Id.* at ____, 516 A.2d at 289.

The court recognized that the validity of the consent to settle clause depended on possession by the UIM carrier of a right to subrogation against the tortfeasor.[84] The court noted that courts were split on this question, and it gave a brief overview of some of the previously discussed cases.[85]

The court looked to the relevant New Jersey statutes, and indicated that the purpose of the statutorily created UIM coverage was to protect victims from insufficiently insured drivers.[86] Therefore, in order to carry out this purpose, limitations in the insurance contract attempting to restrict this coverage were to be strictly construed against the insurer.[87] The insurer in this case was forcing the insured to proceed with the underlying litigation, and the court viewed this as contrary to the purposes of the statutes designed to protect the victim and expedite his recovery.[88] The court concluded:

> The subrogation clause in question delays compensation rather than promoting prompt compensation, increases litigation rather than decreasing litigation, chills settlement and compromise rather than encouraging out of court resolution of claims and seeks to give control of the litigation to Ohio [the insurer] where such authority is not conferred by statute.[89]

This is the same conclusion which had been reached in a prior New Jersey decision concerning a consent to settle provision in an uninsured motorist policy.[90] Although the court recognized that UIM coverage differed from UM coverage, and that it was optional under the statute, the public policy considerations for rejecting consent to settle clauses in UM coverage were pertinent to UIM coverage.[91] The court asked: "[Why] should a provision . . . frustrate the purpose of a comprehensive reparation package?"[92]

The insurer argued that since the UIM coverage was optional, the parties were free to contract with one another for specific rights and benefits.[93] Therefore the right to subrogation was a legitimate contract provision.[94] The court disagreed, recognizing that insurance contracts are contracts of adhe-

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84. *Id.* at ____, 516 A.2d at 290.

85. *Id.* at ____, 516 A.2d at 290-91. (Among the cases cited by the court were March v. Mountain States Mut. Cas. Co., 101 N.M. 689, 687 P.2d 1040 (1984); Niemann v. Travelers Ins. Co., 368 So. 2d 1003 (La. 1979); Schmidt v. Clothier, 338 N.W.2d 256 (Minn. 1983); and Vogt v. Schroeder, 129 Wis. 2d 3, 383 N.W.2d 876 (1986)).

86. *Id.* at ____, 516 A.2d at 291.

87. *Id.* at ____, 516 A.2d at 292.

88. *Id.* at ____, 516 A.2d at 293.

89. *Id.*

90. *Id. See* Government Employees Ins. Co. v. Shara, 137 N.J. Super. 142, 348 A.2d 212 (Ch. Div. 1975).

91. Longworth v. Ohio Cas. Group of Ins. Cos., 213 N.J. Super. 70, ____, 516 A.2d 287, 294 (Law Div. 1986).

92. *Id.* at ____, 516 A.2d at 294.

93. *Id.* at ____, 516 A.2d at 295.

94. *Id.*

sion.[95] The insured is not free to negotiate the terms of the contract, and the contracts are unilaterally prepared by the insurer.[96]

Further, the court noted that the right of subrogation was controlled by New Jersey statute.[97] The court concluded that the subrogation statute was not meant to be read in conjunction with the UIM statute, and that if a UIM carrier was to have a right to subrogation:

> Such right will have to be extended by the express mandate of the Legislature . . . . This court is satisfied that the history of the automobile reparation statutes indicates that where the Legislature intends that a right of subrogation should exist, it expressly and affirmatively extends the right to subrogate. No such right has been extended in the underinsured context.[98]

In holding that a subrogation provision containing a consent to settle clause was invalid, the court suggested that to keep similar controversies from arising in the future, the legislature should provide a procedure for resolving UIM claims.[99] The court made reference to *Schmidt v. Clothier* as an example of such a procedure.[100]

F. *Texas*

A Texas court of appeals wrote a very brief opinion upholding the validity of a consent to settle clause in *Miller v. Hanover Insurance Co.*[101] This case involved the conventional fact pattern—the insured settled with the tortfeasor without the consent of the UIM carrier and then filed a claim for his UIM benefits.[102]

The insured argued that the consent to settle clause was against public policy.[103] The court recognized that the right to subrogation had been upheld in cases dealing with uninsured motorist coverage, and that the purpose of consent to settle clauses was to protect those subrogation rights.[104] In a prior case dealing with uninsured motorist coverage, *Castorena v. Employers Casualty Co.*,[105] the court had held: "[T]he exclusionary clause is valid and enforceable. It does not deprive an insured of the protection required by the Texas uninsured motorist statute."[106]

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95. *Id.*
96. *Id.*
97. *Id.* (citing N.J. STAT. ANN. § 39:6A-9.1 (West Supp. 1987)).
98. *Id.* at ____, 516 A.2d at 296.
99. *Id.* at ____, 516 A.2d at 298.
100. *Id.*
101. Miller v. Hanover Ins. Co., 718 S.W.2d 429 (Tex. Ct. App. 1986).
102. *Id.* at 430.
103. *Id.*
104. *Id.*
105. Castorena v. Employers Cas. Co., 526 S.W.2d 680 (Tex. Civ. App. 1975).
106. *Id.* at 681-82.

The court in *Miller* made no effort to differentiate between UM coverage and UIM coverage. Since the insured settled with the tortfeasor without the insurer's consent, thereby destroying the insurer's subrogation rights, the insured could not collect his UIM benefits.[107]

G. *Washington*

There are two important cases from Washington which discuss consent to settle clauses in UIM policies. The first case, decided in 1985 by the Washington Supreme Court, is *Elovich v. Nationwide Insurance Co.*[108] This case involved multiple defendants and settlements. One of the issues addressed by the court was "whether a plaintiff forfeits his right to collect under UIM coverage if he violates the 'consent to settle' clause in the policy."[109]

The insurer argued that since it never received notice of the settlement negotiations and was never asked to consent to the settlements, the insured's claim should be dismissed, because the policy provision was violated.[110] The court noted that a number of prior cases had ruled that insurers' attempts to place contractual limitations on the insured's right to recover when the tortfeasor is insufficiently insured are invalid.[111] Consent to settle clauses had previously been held invalid as contrary to public policy in Washington UM cases.[112] The rationale was that: "Exclusionary clauses violate the statutorily enunciated public policy of protecting insureds from uncompensated injury."[113]

However, the court recognized that these decisions had been handed down prior to the 1980 statutory amendments providing specifically for UIM coverage.[114] The court looked to the Louisiana decisions (the Louisiana statutes are substantially the same as Washington's) and noted that those decisions "continued to recognize the overriding public importance of maximum compensation."[115] Further, the court stated that the legislature's primary concern in adopting the amendments was for those injured in auto accidents.[116] The court concluded that consent to settle clauses were still void as contrary to public policy.[117]

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107. Miller v. Hanover Ins. Co., 718 S.W.2d at 430.

108. Elovich v. Nationwide Ins. Co., 104 Wash. 2d 543, 707 P.2d 1319 (1985).

109. *Id.* at ____, 707 P.2d at 1325.

110. *Id.*

111. *Id.* (*see* Touchette v. Northwestern Mut. Ins. Co., 80 Wash. 2d 327, 494 P.2d 479 (1972); State Farm Mut. Auto. Ins. Co. v. Bafus, 77 Wash. 2d 720, 466 P.2d 159 (1970); Solesski v. Oregon Auto. Ins. Co., 11 Wash. App. 850, 526 P.2d 68 (1974)).

112. *Id.* (*see* Hawaiian Ins. & Guar. Co. v. Mead, 14 Wash. App. 43, 538 P.2d 865 (1975)).

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.*

117. *Id.*

In 1987 the Washington Supreme Court expanded the *Elovich* holding in *Hamilton v. Farmers Insurance Company of Washington.*[118] In *Hamilton*, the insured settled with the tortfeasor for the tortfeasor's policy limits after unsuccessfully attempting to get the UIM carrier's consent to the settlement.[119] The tortfeasor had other assets worth approximately $13,600.[120] Because the tortfeasor had been released, the insurer was unable to reach those additional assets.[121]

The court restated its holding in *Elovich* that the consent to settle clause was invalid.[122] Nonetheless, the insurer argued that the settlement and release prejudiced its right to subrogation against the tortfeasor's other assets.[123] The insurer contended "that it should be entitled to offset its payment to the insured by the amount of available assets of the tortfeasor which are shielded from recovery by the release."[124] In determining if the insurer had a right to subrogation which could be prejudiced, the court was guided by the holding of the Supreme Court of Louisiana in *Niemann.*[125] Following *Niemann*, the court in *Hamilton* concluded:

> The Legislature has not provided for subrogation rights that would reduce the statutorily mandated coverage, but has *only granted a right of reimbursement* from the insured when a settlement or judgment results in an excess recovery. Equitable or contractual subrogation rights cannot be engrafted onto the statutory scheme to thwart its intended purpose [of fully compensating the injured insured].[126]

Therefore, the insurer had no rights which were prejudiced by the insured's settlement with the tortfeasor for the tortfeasor's policy limits.[127]

The court also recognized the holding of the Supreme Court of Minnesota in *Schmidt v. Clothier.*[128] The court adopted part of the *Schmidt* holding and determined that the insurer "can succeed to the rights of the insured against the tortfeasor by (1) paying the underinsurance benefits prior to release of the tortfeasor and (2) substituting a payment to the insured in an amount equal to the tentative settlement."[129] Only in this way could an insurer obtain subrogation rights against additional assets of the tortfeasor. However, the court concluded: "Any recovery against the tortfeasor over the

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118. Hamilton v. Farmers Ins. Co., 107 Wash. 2d 721, 733 P.2d 213 (1987).
119. *Id.* at ____, 733 P.2d at 215.
120. *Id.* at ____, 733 P.2d at 214.
121. *Id.* at ____, 733 P.2d at 215.
122. *Id.* at ____, 733 P.2d at 217.
123. *Id.*
124. *Id.*
125. *Id.* at ____, 733 P.2d at 218.
126. *Id.* at ____, 733 P.2d at 219 (emphasis in original).
127. *Id.* at ____, 733 P.2d at 220.
128. *Id.* at ____, 733 P.2d at 219-20 (citing Schmidt v. Clothier, 338 N.W.2d 256 (Minn. 1983)).
129. *Id.* at ____, 733 P.2d at 220.

amount of the substituted settlement payment must be applied first to any uncompensated damages of the injured insured. Only after the insured is fully compensated can the underinsurer retain any excess recovery."[130]

H. *Iowa*

The most recent ruling on the validity of the consent to settle clause came from Iowa. In *Kapadia v. Preferred Risk Mutual Insurance Co.*,[131] the insured settled with the tortfeasor for the tortfeasor's $15,000 policy limits without the consent of her UIM carrier.[132] The insurer refused to pay the UIM benefits, and the insured filed suit.[133] The trial court granted the insurer's motion for summary judgment, concluding that the consent to settle provision was a valid method by which the insurer could protect its subrogation rights.[134] The court found that these rights were "conceivabl[y] granted an insurer by Iowa Code section 516A.4 (1981)."[135] The court concluded that such clauses did not violate public policy.[136]

On appeal the insured argued that consent to settle clauses were not authorized by the UIM statute, and that such clause violated the public policy of that statute.[137] The Supreme Court of Iowa stated that the purpose of UIM coverage was "to provide compensation to the extent of injury, subject to the limits of the particular policy."[138] But the UIM statute only required that such coverage be *offered*; it did not require that UIM coverage be *in effect* in all policies written in Iowa.[139] Therefore, the statute "makes the relative rights of the insurer and insured, following payment of policy benefits, 'subject to the terms and conditions' of the policy."[140]

The policy in question stated that the insured could not settle with the tortfeasor without the insurer's consent, and that the insured could not do anything to prejudice the insurer's right of subrogation.[141] Although Iowa's UIM statute did not specifically provide for subrogation rights, the court stated:

> Our jurisprudence has long imposed such rights of subrogation as a matter of law. We do not construe a statute so as to take away common-law rights existing at the time of the statute's enactment unless that result is imperatively required. In addition, we note that contract-based

130. *Id.* at ____, 733 P.2d at 220-21.
131. Kapadia v. Preferred Risk Mut. Ins. Co., 418 N.W.2d 848 (Iowa 1988).
132. *Id.* at 849.
133. *Id.*
134. *Id.*
135. *Id.* at 850. (Section 516A.4 is the reimbursement provision of the UM/UIM chapter.)
136. *Id.*
137. *Id.*
138. *Id.*
139. *Id.*
140. *Id.* at 851.
141. *Id.*

> subrogation rights—known as a "conventional subrogation"—are not subject to the rule which stays their enforcement until the subrogator . . . is made whole.[142]

Only when a policy provision failed to provide the coverage required by the statute had the court held the provision invalid.[143]

Since the coverage required by statute was made available, the question before the court was whether an insurer "may attempt to protect its interests by use of subrogation and consent-to-settle clauses."[144] Although the statute was not written to protect the insurer, the court did not think that it could be used to destroy the insurer's legitimate interests.[145] The court held "that such subrogation clauses are consistent with the language and spirit of chapter 516A and that they may be protected by the use of consent-to-settlement clauses."[146] The court specifically emphasized that its holding merely stated that the statute allowed for this type of subrogation clause, and that it did not reach the question whether the statute granted subrogation rights in favor of the insurer.[147]

However, the court went further. The court did not believe that the insured should be denied recovery merely because she breached the clause.[148] The court concluded that "a demonstration [must] be made of actual prejudice to the insurer prior to its discharge under the consent-to-settlement clause."[149] The defendant insurer had the ultimate burden of showing actual prejudice when it asserted such a defense.[150] To establish prejudice, the insurer had to prove "that, absent such a breach, it could have collected from the tort-feasor under its rights embraced by the contractual subrogation clause."[151] Since the issue of prejudice was not appropriate for summary judgment resolution, the court reversed and remanded the case to the district court for a determination of prejudice.[152]

The court stated that the insurer has the burden of proving prejudice; but how significant must the lost subrogation rights be before the insurer may deny benefits? Clearly if the tortfeasor is judgment-proof, the loss is what a Florida court has termed an "illusionary loss."[153] Therefore, even

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142. *Id.* (citations omitted).

143. *Id.* (*See* Lindahl v. Howe, 345 N.W.2d 548 (Iowa 1985); Rodman v. State Farm Mut. Auto. Ins. Co., 208 N.W.2d 903 (Iowa 1973)).

144. *Id.*

145. *Id.*

146. *Id.*

147. *Id.* at 852.

148. *Id.*

149. *Id.*

150. *Id.*

151. *Id.*

152. *Id.*

153. *See* Southeastern Fidelity Ins. Co. v. Earnest, 395 So. 2d 330, 331 (Fla. Dist. Ct. App. 1981).

though subrogation rights have been destroyed by the settlement, the insurer is not actually prejudiced, since it could not realistically have exercised its subrogation rights.

But what happens when the tortfeasor does have some reachable assets? If the assets are shielded by the settlement, can prejudice be established regardless of the amount of the assets? Or must the assets be in a certain amount before the insurer is actually prejudiced? If the insured is damaged in excess of $150,000 and settled with the tortfeasor for the tortfeasor's policy limits of $100,000, is the UIM insurer prejudiced if the tortfeasor had an additional $5,000 in assets? What if the tortfeasor had an additional $10,000? The Iowa Supreme Court did not address these questions in its opinion.

Although the insurer might be unable to reach the tortfeasor's additional $5,000, it would generally be beneficial for the insured to settle for the $100,000 policy limits to avoid possible lengthy and costly litigation. The additional $5,000 might be insignificant to the insured; would its loss be so prejudicial to the insurer that it could deny UIM benefits? Unfortunately, in a case such as this, the insured is in a difficult situation. If the insurer refuses to consent to a settlement, the insured may still settle and hope that the insurer cannot prove prejudice. But the insured cannot tell how much prejudice the insurer must show before it can deny payment of the UIM benefits. The insured runs the risk of losing his benefits by settling with the tortfeasor. If the insured does not settle when the insurer refuses consent, he protects his right to UIM benefits, but he must also litigate his claim against the tortfeasor to judgment. The insured is faced with two options: either settle with the tortfeasor and risk losing his UIM benefits, or protect his UIM benefits by proceeding to trial and possibly encountering hardship while involved in lengthy litigation. The decision may be difficult. In Iowa the insured is clearly not afforded the protection he might have in some other jurisdictions.

V. Summation

The validity of consent to settle clauses depends on the existence of a right to subrogation. In determining whether the UIM carrier has subrogation rights and whether those rights can be protected by consent to settle clauses, courts look to relevant UIM statutes and to the contractual language of the UIM policy in question. As the previously discussed cases have shown, courts have interpreted the statutes and policies in a variety of ways. The courts have determined that consent to settle clauses are either:

1. not valid as against public policy and the coverage mandated by statute;

2. valid because the contractual or common law right of subrogation is not prohibited by statute or public policy; or

3. valid, but the insurer must follow an established procedure to protect

its rights.

Louisiana, New Jersey, and Washington are examples of jurisdictions holding that the UIM statutes do not permit subrogation and consent to settle clauses.[154] Since the public policy behind the statutes is to fully compensate the insured for his injuries, the insurer may not attempt to limit the coverage required by statute. If the insurer is to have a right to subrogation, these courts have concluded that the state legislatures must provide for it. However, the Washington court did recognize a limited right of subrogation if the insurer pays the UIM benefits and substitutes a check for the settlement amount.[155] The insured must be fully compensated before the insurer acquires any subrogation rights.[156]

New Mexico, Texas, and Iowa are jurisdictions which have held that consent to settle clauses are valid.[157] These courts have held that the UIM statutes do not forbid subrogation or consent to settle clauses to protect subrogation rights, and that the contractual language of the policy is controlling. In New Mexico and Texas, a breach of the consent to settle clause will deny the insured UIM benefits. However, the Iowa court held that a breach of the clause does not necessarily exclude UIM coverage.[158] In Iowa the insurer must prove that its subrogation rights have been prejudiced before the UIM coverage is void.[159]

Minnesota and Wisconsin have upheld the validity of consent to settle clauses, but have limited their application by establishing specific procedures which the insured and insurer must follow.[160] These procedures permit the insured to proceed with a settlement without jeopardizing his UIM benefits. These procedures also permit the UIM carrier to protect its subrogation rights.

VI. Conclusion

Which of the above holdings is the most equitable to all parties affected by an automobile accident involving an insured? While they protect the insured to the fullest extent, the jurisdictions which hold consent to settle clauses invalid leave the UIM carrier with no rights to assert. Since the insurer is denied subrogation rights, the tortfeasor may not be held responsi-

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154. *See supra* notes 13-35 and accompanying text, notes 79-100 and accompanying text, and notes 108-30 and accompanying text, respectively.

155. *See* Hamilton v. Farmers Ins. Co., 107 Wash. 2d 721, ____, 733 P.2d 213, 220-21 (1987).

156. *Id.*

157. *See supra* notes 57-68 and accompanying text, notes 101-07 and accompanying text, and notes 131-53 and accompanying text, respectively.

158. *See* Kapadia v. Preferred Risk Mut. Ins. Co., 418 N.W.2d 848, 852 (Iowa 1988).

159. *Id.*

160. *See supra* notes 36-56 and accompanying text, and notes 69-78 and accompanying text, respectively.

ble to the fullest extent for his actions. The insurer should be permitted to reach the tortfeasor's available assets not included in the settlement. The insurer, who provides UIM coverage at a relatively low cost, should not be denied an avenue of recourse against the tortfeasor. But these courts have suggested that if the insurer is to have rights, the legislatures must provide for them.

The jurisdictions which uphold the validity of consent to settle clauses either ignore the UIM statutes or find that the statutes do not prohibit such clauses. Contract provisions and common law subrogation rights are not superseded by the UIM statutes. The contract rights do not deny the insured UIM benefits, but merely require the insurer's consent to any settlement. By insisting on the contract provisions, the insurer may preserve its right to look to the tortfeasor to be responsible for the insured's injuries. The problem presented by these holdings is that they allow the insurer to control the insured's case. By withholding consent, the insurer can force the insured to litigate his case to the end. This discourages compromise and settlement, and may deny the insured prompt compensation for his injuries. The insurer's rights are protected in these jurisdictions, but the insured is limited in his options.

The Iowa decision takes a middle position by upholding the validity of the consent to settle clause, but at the same time permitting the insured to violate the clause and still obtain UIM benefits. This is beneficial because it may protect the insured when the insurer unreasonably refuses to consent to the settlement. But it leaves the insured in a difficult position, in which he must either settle with the tortfeasor and hope that the insurer cannot prove prejudice, or litigate the case to judgment and protect his UIM benefits. Without the insurer's consent to settle, the insured is forced to pursue possibly lengthy and costly litigation, or settle and risk losing UIM benefits. Because it uses prejudice as a basis for denying UIM benefits, the Iowa decision fails to protect the insured as much as it should. The concept of prejudice is unclear, and the insured may have to make a risky decision. Such a decision should be unnecessary.

The jurisdictions upholding consent to settle clauses but limiting their use by specific procedures appear to have found the most equitable solution. The insurer is given the option of consenting to the settlement, thereby destroying its subrogation rights, or paying UIM benefits and substituting a check in the amount of the settlement offer, thereby protecting its subrogation rights. Such a procedure protects the rights of both the insured and the insurer. The insured is placed in a favorable position because, no matter what the insurer does, the insured will still receive the settlement amount and the UIM benefits. The insured will not be denied the benefits contemplated by the UIM statutes.

The insurer is also accorded its rights. If the insurer believes that it can recover from the tortfeasor an amount greater than the settlement offer, it may protect its subrogation rights. If the insurer determines that its subro-

gation rights are worthless, it may consent to the settlement. Given these options, the insurer may protect its rights and prevent any collusion between the insured and the tortfeasor. Under such a procedure, the tortfeasor is held fully responsible for his actions.

The procedure outlined above may be adopted by a court or established by statute. The Minnesota and Wisconsin Supreme Courts have upheld the validity of consent to settle clauses and have adopted such a procedure.[161] The Washington Supreme Court, although it held the consent to settle clause invalid, has recognized that the insurer may acquire subrogation rights by using a similar procedure.[162]

In Florida such a procedure has been established by statute.[163] The statute states that a settlement agreement shall be submitted to the insurer and that the insurer shall have thirty days in which to approve of the settlement.[164] If the insurer approves of the settlement, it waives its subrogation rights.[165] If the insurer does not approve of the settlement, the insured may file a joint suit against the tortfeasor and the UIM carrier to determine their respective liabilities.[166] A Florida court has ruled that if an insured does not follow this procedure, he may still obtain his UIM benefits if he can prove that the insurer was not prejudiced by the settlement.[167]

The Florida procedure is not as effective as the procedure adopted in Minnesota and Wisconsin. The Florida procedure places the burden of litigation on the insured when the insurer asserts its rights by withholding consent. If the insured is forced to become involved in lengthy litigation, he will not receive his just compensation promptly. And if the insured does settle without the insurer's consent, he does not know if he will receive his UIM benefits. The question must be settled by litigation.

By contrast, the Minnesota procedure ensures prompt compensation for the insured. If the insurer wishes to withhold consent to the settlement, the insurer assumes the burden of litigation by paying the insured the settlement amount. Since the burden of litigation is placed on the insurer, the insurer is less likely to withhold consent to a settlement unreasonably. Such a procedure is clearly in the best interests of both the insured and the insurer.

Thomas H. Fell

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161. *See* Schmidt v. Clothier, 338 N.W.2d 256 (Minn. 1983); Vogt v. Schroeder, 129 Wis. 2d 3, 383 N.W.2d 876 (1986).

162. *See* Hamilton v. Farmers Ins. Co., 107 Wash. 2d 721, ____, 733 P.2d 213, 220-21 (1987).

163. FLA. STAT. ANN. § 627.727(6) (West 1984).

164. *Id.*

165. *Id.*

166. *Id.*

167. *See* New Hampshire Ins. Co. v. Knight, 506 So. 2d 75 (Fla. Dist. Ct. App. 1987).