STATE OF MINNESOTA
IN COURT OF APPEALS
A11-11

Bakita Isaac,
Respondent,

vs.

Vy Thanh Ho, et al.,
Appellants,

Auto Club Insurance Association, intervenor,
Respondent.

Filed August 8, 2011
Affirmed in part and reversed in part
Halbrooks, Judge

Hennepin County District Court
File No. 27-CV-09-3997

Jason R. Vohnoutka, Vohnoutka Law Office, Ltd., Minneapolis, Minnesota (for respondent Isaac)

Paul J. Rocheford, Paul E. D. Darsow, J. Kevin Kirchner, Arthur, Chapman, Kettering, Smetak & Pikala, P.A., Minneapolis, Minnesota (for appellants)

John R. Crawford, Benjamin A. Johnson, Johnson & Lindberg, P.A., Minneapolis, Minnesota (for respondent Auto Club Insurance Association)

Considered and decided by Halbrooks, Presiding Judge; Bjorkman, Judge; and Collins, Judge.*

* Retired judge of the district court, serving as judge of the Minnesota Court of Appeals by appointment pursuant to Minn. Const. art. VI, § 10.

U N P U B L I S H E D O P I N I O N

HALBROOKS, Judge

In this dispute involving underinsured-motorist insurance coverage, appellants argue that the district court erred by denying their motion for judgment as a matter of law (JMOL). The district court determined that the liability settlement agreement between appellants and respondent was nullified by the underinsured-motorist insurer's substitution of its check and that there was no basis for appellants' dismissal. Appellants also challenge the district court's award of judgment to respondent Auto Club Insurance Association in the amount of $11,152.70. Because we conclude that the district court did not err by denying the motion for JMOL, we affirm in part. But because we conclude that Auto Club is not entitled to recoup the sum that it paid as a substitution for the liability settlement, we also reverse in part.

FACTS

On September 9, 2007, appellant Vy Thanh Ho was driving a vehicle that was owned by appellant Lien Ho when he was involved in an accident with respondent Bakita Isaac. Isaac sued appellants for negligence. Appellants' vehicle was insured by Progressive Preferred with a liability coverage limit of $50,000. Over the course of settlement negotiations, Isaac made two offers of settlement to appellants pursuant to Minn. R. Civ. P. 68, both of which contained the following language: "This offer of judgment is subject only to proper notice to the underinsured motorist carrier(s) to allow them to exercise their right to stop the settlement by substituting their check" pursuant to

Schmidt v. Clothier, 338 N.W.2d 256 (Minn. 1983). No settlement occurred as a result of either offer.

On October 2, 2009, Progressive, on behalf of appellants, continued to negotiate with Isaac, and at the end of a telephone conversation, Isaac's attorney stated that if Progressive were to offer Isaac $10,665, he would recommend that Isaac accept it. On October 6, 2009, Isaac received a settlement check from Progressive in the amount of $10,665 as well as a release of Isaac's claims against appellants and a stipulation of dismissal with prejudice.

The following day, Isaac sent notice of the settlement to her underinsured-motorist (UIM) carrier, Auto Club. The notice stated that Auto Club had "thirty (30) days in which to either acquiesce in that settlement and lose your right to subrogation or to prevent such settlement by exchanging your draft for that of Progressive Insurance Company in the amount of the proposed settlement." The notice also indicated Isaac's intent to pursue a UIM claim against Auto Club. Auto Club substituted its draft for Progressive's within the 30-day period, sending Isaac a check for $10,665. Isaac subsequently returned Progressive's settlement check along with the unsigned release and stipulation for dismissal. Auto Club then intervened in the negligence lawsuit, with no objection from appellants.

Appellants moved for summary judgment, arguing that Auto Club's substitution of its draft for Progressive's did not eliminate the settlement agreement between them and Isaac, and, therefore, appellants should be dismissed from the negligence lawsuit. The district court denied appellants' motion for summary judgment on the ground that the

parties' settlement was expressly conditioned on Auto Club's waiver of its subrogation rights and that the agreement "voluntarily granted Auto Club the power to terminate the tentative settlement." The case continued to trial, and the jury returned a verdict finding appellants 95% at fault and Isaac 5% at fault for the accident. The jury awarded damages to Isaac totaling $58,739.44.

Appellants subsequently moved for JMOL on the same basis that they had asserted in their summary-judgment motion and again argued that they should have been dismissed. The district court denied appellants' motion for JMOL, reasoning that "[t]he proposed settlement between [respondent] and [appellants] was expressly conditioned on Auto Club's agreement to waive its subrogation interest. By substituting its draft for Progressive's, Auto Club stopped the settlement." Moreover, the district court concluded that a UIM carrier's substitution of its check does not require dismissal of the tortfeasor.

Appellants also moved for collateral-source offsets, arguing, in part, that they were entitled to an offset in the amount of $10,665—the proposed settlement amount. The district court denied the request to offset Isaac's award by this amount, reasoning that appellants were "not entitled to a reduction in damage amount because no settlement existed between [appellants] and [respondent]." After considering the remainder of appellants' motion, the district court reduced Isaac's recovery by $14,555.18; the final award to Isaac after reduction of collateral sources totaled $44,184.26. After determining costs and disbursements, the district court entered judgment in favor of Isaac in the amount of $45,765.97 and in favor of Auto Club in the amount of $11,152.70 (the amount of its substituted draft plus prejudgment interest). This appeal follows.

D E C I S I O N

I.

This court reviews de novo the district court's denial of a motion for JMOL under Minn. R. Civ. P. 50.02. *Kidwell v. Sybaritic, Inc.*, 749 N.W.2d 855, 861 (Minn. App. 2008), *aff'd*, 784 N.W.2d 220 (Minn. 2010). In reviewing a denial of a motion for JMOL, we view the evidence in the light most favorable to the prevailing party. *Bahr v. Boise Cascade Corp.*, 766 N.W.2d 910, 919 (Minn. 2009). JMOL should be granted "only in those unequivocal cases where (1) in the light of the evidence as a whole, it would clearly be the duty of the [district] court to set aside a contrary verdict as being manifestly against the entire evidence, or where (2) it would be contrary to the law applicable to the case." *Jerry's Enters., Inc. v. Larkin, Hoffman, Daly & Lindgren, Ltd.*, 711 N.W.2d 811, 816 (Minn. 2006) (quotation omitted). Appellants maintain that the district court erred as a matter of law by denying their motions for summary judgment and JMOL, thereby keeping them in the case.

UIM coverage is first-party coverage that, as excess coverage, may be available to compensate an insured if the tortfeasor has been determined by either judgment or settlement to be underinsured. 22 Britton D. Weimer et al., *Minnesota Practice* § 8:19 (2d ed. 2010). An insured who wishes to pursue a claim for UIM benefits may proceed against the tortfeasor in district court under a negligence theory, and to the extent the damages awarded exceed the tortfeasor's liability limits, she may pursue a subsequent claim for UIM benefits against her insurer. *See Washington v. Milbank Ins. Co.*, 562 N.W.2d 801, 805 (Minn. 1997).

Alternatively, the insured may opt to engage in settlement negotiations with the tortfeasor. *See id.* If the insured chooses to accept a tortfeasor's settlement offer, she must provide her UIM carrier with a *Schmidt* notice of the tentative settlement in order to protect the UIM carrier's right to subrogation to recover the underinsurance benefits it paid. *See Schmidt*, 338 N.W.2d at 263. The UIM carrier has 30 days to substitute its draft for the settlement amount.[1] *Id.* If the UIM carrier substitutes its check for the tortfeasor's, the UIM carrier preserves its right to pursue a subrogation claim against the tortfeasor to recover "all or a portion of the sums the underinsurer has paid the injured claimant." *Emp'rs Mut. Cos. v. Nordstrom*, 495 N.W.2d 855, 856 (Minn. 1993).

Here, the district court concluded that Auto Club's substitution of its check operated to prevent the settlement between appellants and Isaac, and appellants were therefore not entitled to dismissal from Isaac's tort claim. The district court ruled, in part, that the parties contracted outside the scope of *Schmidt* when they permitted Auto Club to prevent the settlement with its substituted draft.

While we agree with the district court's ultimate conclusion, we base our decision not only on the language of the parties' agreement but also on the principles outlined in *Schmidt*. The *Schmidt* notice provided to Auto Club clearly stated that Isaac had received an "offer of settlement," and informed Auto Club that it had "thirty (30) days in which to either acquiesce in that settlement . . . or to *prevent such settlement* by exchanging your draft . . . in the amount of the proposed settlement." (Emphasis added.) The notice

[1] This decision requires the UIM carrier to weigh the value and likelihood of recovery in a subrogation claim. *See Am. Family Mut. Ins. Co. v. Baumann*, 459 N.W.2d 923, 925 (Minn. 1990).

further provided that Isaac would finalize the proposed settlement in the event that Auto Club opted not to substitute its draft. This notice is clear that the settlement proposed by appellants was not full and final and was instead subject to acquiescence by Auto Club. Appellants received a copy of Isaac's letter to Auto Club.

The notice that Isaac provided to Auto Club conformed with Minnesota law. In *Schmidt*, the supreme court considered in great detail the UIM-benefits procedure and characterized an agreement between a plaintiff and a defendant as a "tentative settlement agreement." *Schmidt*, 338 N.W.2d at 263. A settlement agreement between a plaintiff and a defendant is not final until the UIM carrier acquiesces in the settlement by allowing the 30-day period to lapse without substitution of its draft. If the UIM carrier wishes to preserve its subrogation rights, it must substitute its check. *See id.* This act "prevent[s] an insured from settling the claim." *Van Kampen v. Waseca Mut. Ins. Co.*, 754 N.W.2d 578, 584 (Minn. App. 2008). The supreme court stated in *Schmidt* that when the UIM carrier substitutes its check, it may decide to "negotiate a better settlement or . . . proceed to trial in the insured's name." 338 N.W.2d at 263; *see also Gusk v. Farm Bureau Mut. Ins. Co.*, 559 N.W.2d 421, 424 (Minn. 1997) ("*Schmidt v. Clothier* substitutions, by their very nature, prevent settlements between insureds and tortfeasors."). Contrary to appellants' arguments, the proposed settlement between them and Isaac was only tentative at the time that Auto Club was provided with the *Schmidt* notice; Auto Club's draft substitution operated to prevent their settlement from becoming final.

In support of their argument that the district court erred by not dismissing them from the negligence case, appellants place heavy reliance on footnote three from the *Washington* case. In footnote three, the supreme court noted:

> Technically, no settlement is reached when the UIM carrier follows the *Schmidt-Clothier* procedure and substitutes its draft for that of the tortfeasor's insurance company. However, the UIM carrier's substitution operates as the equivalent of a settlement between the party claiming damages and the tortfeasor because the tortfeasor is released from further liability to the party claiming damages, but, at the same time, the UIM insurer retains a subrogation right against the tortfeasor's insurance company.

Washington, 562 N.W.2d at 806 n.3. We are not persuaded that the supreme court's comment in this footnote is dispositive of this issue. Further, *Washington* is distinguishable from this case.

The plaintiffs in *Washington* sued Presley, the alleged at-fault driver, for negligence. *Id.* at 803. Presley and his insurer, State Farm Insurance Company, agreed to pay the plaintiffs $20,000—$10,000 less than the remaining liability limit—to resolve Presley's potential liability.[2] *Id.* The plaintiffs provided their UIM carrier, Milbank Insurance Company, with notice of their settlement with Presley. *Id.* Milbank substituted its draft, but also required the plaintiffs to sign a loan agreement, one term of which stated that "it is understood and agreed that Milbank's repayment right is as

[2] Because plaintiff Ruth Washington was in the course and scope of her employment when the accident occurred, State Fund Insurance, her employer's workers' compensation insurer, paid for her medical and wage-loss benefits. *Washington*, 562 N.W.2d at 803. At the settlement conference, State Fund agreed to accept $20,000 from State Farm. *Id.* As a result, $30,000 of liability coverage remained. *Id.*

creditor and not as subrogee." *Id.* The plaintiffs signed the agreement, and dismissed their negligence claim against Presley. *Id.*

The plaintiffs sought to arbitrate their UIM claim; Milbank refused to do so based, in part, on the terms of the loan agreement. *Id.* at 804. The plaintiffs then commenced a new lawsuit against Presley based on the same causes of action that had been dismissed. *Id.* Presley moved for dismissal, and the district court granted his motion. *Id.* This court affirmed. *Id.*

The plaintiffs then commenced a declaratory-judgment action against Milbank. *Id.* Milbank moved the district court to order the plaintiffs to proceed with the tort action against Presley until (1) they obtained a judgment in excess of Presley's $50,000 liability limit; (2) agreed to a settlement with Presley equal to the liability limit; or (3) reached a settlement with Presley that Milbank agreed to. *Id.* The district court ordered UIM arbitration, and Milbank appealed, arguing that "*Nordstrom* fundamentally altered the *Schmidt v. Clothier* landscape." *Id.* at 804-05. This court affirmed, and the supreme court accepted review. *Id.* at 804.

The focus of the supreme court's analysis was Milbank's assertion that under *Nordstrom*, a UIM claimant must first obtain a judgment against the tortfeasor or reach a settlement at least equal to the tortfeasor's liability limits. *Id.* at 805. The supreme court disagreed, stating that *Nordstrom* "merely clarified" *Schmidt*. *Id.* at 806. The supreme court's references to procedures following a UIM carrier's draft substitution was, at most, dictum; the supreme court expressly declined to address Milbank's specific arguments.

Id. at 806. Accordingly, we conclude that appellants' reliance on *Washington* is misplaced.

In this case, the proposed settlement agreement between Isaac and appellants was just that: a proposed agreement. Because Auto Club's substitution prevented the settlement from becoming final, there was no error in the district court's denial of appellants' motion. Appellants have not provided us with any authority to support their argument that dismissal of a tortfeasor is required after a UIM carrier substitutes its draft for the proposed liability settlement amount.

Based on our review of the caselaw, we note that district courts have both granted and denied motions to dismiss in similar circumstances. For example, in *Husfeldt v. Willmsen*, the UIM carrier substituted its draft in the amount of the proposed settlement, and the tortfeasor sought dismissal of the claims against him. 434 N.W.2d 480, 481 (Minn. App. 1989). The district court denied that motion. *Id.* The tortfeasor did not challenge the denial of the motion on appeal. *Id.*; *see also Traver v. Farm Bureau Mut. Ins. Co.*, 418 N.W.2d 727, 729 (Minn. App. 1988) (noting that the underlying lawsuit against the tortfeasor continued after the UIM carrier substituted its draft), *review denied* (Minn. Apr. 15, 1988).

Because we conclude that the district court's decision is supported by the well-established principles outlined in *Schmidt* and its progeny, we affirm its decision to deny appellants' motion for JMOL.

II.

Appellants contend that the district court erred by ordering judgment of $11,152.70 to Auto Club. Appellants maintain that because the jury ultimately determined that they were not underinsured, Auto Club's right of subrogation did not mature and its payment of $10,665 was a voluntary payment for which Auto Club has no right of subrogation. Based on the principles articulated by the supreme court in *Gusk*, we agree.

In *Gusk*, the supreme court addressed "the legal effect of a *Schmidt v. Clothier* substitution on an insurer's liability for uninsured motorist coverage." 559 N.W.2d at 422. Gusk, who was on a bike, lost control of his bike when an unidentified motorist almost collided with him. *Id.* Gusk was then struck by a vehicle driven by Spencer. *Id.* Gusk asserted first-party claims against his insurer, Farm Bureau Mutual Insurance Company, for both UIM and uninsured (UM) benefits, in addition to the third-party liability claim against the two alleged tortfeasors.[3] *Id.* Before trial, Gusk and Spencer reached a tentative settlement for $80,000 of Spencer's $100,000 liability limit. *Id.* Farm Bureau received notice under *Schmidt*. *Id.* In response, Farm Bureau substituted its $80,000 draft in order to preserve its subrogation rights, and the negligence case proceeded to trial, with Farm Bureau added as a defendant based on the UM claim. *Id.* The jury returned a verdict for Gusk; but after offsets, Gusk's net damage award was less than the $80,000 that Farm Bureau had paid in substitution. *Id.*

[3] Gusk had $50,000 in UIM coverage and $50,000 in UM coverage with Farm Bureau. *Gusk*, 559 N.W.2d at 422.

Farm Bureau moved the district court for judgment notwithstanding the verdict,[4] seeking to offset its contractual liability for UM benefits against the $80,000 it paid to prevent the liability settlement. *Id.* The district court denied the motion. *Id.* This court affirmed. *Id.* at 423.

On review, the supreme court held, in part, "it should be clear that a subsequent jury verdict less than the amount of a *Schmidt v. Clothier* substitution cannot justify a 'refund' of that substitution." *Id.* at 424. The supreme court stated that "[a] substitution is a payment to the plaintiff for the protection of an insurer's potential right of subrogation; its creation was not intended to deprive insureds of the benefit of their tentative settlement bargain." *Id.*

In this case, judgment for Isaac was entered in the amount of $45,765.97—a sum that is less than appellants' liability coverage of $50,000. Therefore, it was ultimately determined that appellants were not underinsured. A subrogation claim arises only when the UIM carrier is required to pay underinsurance benefits to its insured. *Schmidt*, 338 N.W.2d at 261. It follows that if the tortfeasor is not underinsured, a UIM claim does not arise and the UIM carrier's right of subrogation does not mature.

The district court determined that Auto Club exercised its subrogation rights when it substituted its draft, but we conclude that the absence of a UIM claim is fatal to Auto Club's subrogation interest. Auto Club's payment to Isaac of $10,665 was based on its assessment of the worth of a potential subrogation claim. By substituting its check, Auto

[4] The supreme court amended rule 50.02 in 2006, changing the name of a motion for judgment notwithstanding the verdict to JMOL.

Club assumed the risk that a UIM claim might not arise and that it might forfeit its payment. *See Gusk*, 559 N.W.2d at 424. Because we conclude that the district court erred in ordering judgment in the amount of $11,152.70 in favor of Auto Club, we reverse that judgment.

Affirmed in part and reversed in part.