Devilish Details:

Step-Downs and Tricky UM/UIM Clauses

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I. THE STEP-DOWN CLAUSE NIGHTMARE

A. OVERVIEW OF STEP-DOWN CLAUSES

As a starting point, this issue is often complicated by the fact that there are different terms used to describe these provisions. Most commonly, these provisions are referred to as "*step-down*" clauses or "*intrafamily*" exclusionary clauses. For consistency, the phrase "*step-down*" will be used throughout this paper.

Generally speaking, step-down provisions apply when one family member pursues a claim, most often a liability claim, against another family member. The purpose of step-down clauses is to reduce the liability coverage applicable to the one family member's claim against the other to the state-mandated minimum amount of liability coverage. Under MCL 500.3009(1), the state-mandated minimum amount of liability coverage is only $20,000 per person or $40,000 per accident (if there are two or more victims). Accordingly, step-down provisions have the effect of reducing the amount of liability coverage stated on the declaration page to the state-mandated minimum of $20,000 per person/$40,000 per accident.

Perhaps the most illustrative way to describe step-down provisions, however, is not through technical terminology. Rather, the effect of a step-down clause can be illustrated with the following hypothetical. This author is the proud father of a wonderful five-year-old boy named Elliot. This author also carries $1,000,000 in liability coverage on his 2015 Nissan Altima. Suppose that this author is driving that Nissan Altima with two passengers in the backseat: his son, Elliot; and Elliot's friend, Oscar. Suppose further that this author is driving while intoxicated and using his cell phone. The author runs a red light, causes a terrible collision, and catastrophically injures both boys. Under normal circumstances, both children would be equally entitled to make a claim under this author's $1,000,000 liability policy. If this author's liability policy contained a step-down provision, however, those usual circumstances are drastically altered for Elliot. That is, if this author's insurance policy contained a step-down provision, Elliot's claim is capped at $20,000. Oscar's claim, however, is unchanged, and Oscar is entitled to make a claim for up to the full amount of the liability insurance policy limits.

This hypothetical illustrates the complete unfairness and injustice created by step-down provisions. As the hypothetical shows, both boys, Elliot and Oscar, are equally injured. In addition, neither child did anything to cause or contribute to the collision. Yet Elliot's claim is limited to a tiny fraction of Oscar's claim simply because of the insertion of one or two sentences in an insurance policy of which Elliot had no knowledge.

Unfortunately, as discussed below, Michigan appellate courts do not share this author's outrage at these repugnant clauses. Nevertheless, it is respectfully submitted that one must view step-down provisions with a strong opinion of their unfairness in order to properly analyze what, if anything, can be done for victims.

For their part, insurance companies attempt to defend the use of step-down provisions because they claim they are somehow necessary to prevent so-called fraud. Perhaps this justification was true at one point in time, but it is submitted that such a justification is now completely unwarranted for a number of reasons.

First, nearly every sophisticated insurer has extensive language in its policy regarding fraudulent claims. Those provisions are designed to protect the insurance company and do a sufficient job on their own to address fraudulent claims. Second, Michigan has a series of laws that make it a crime to commit insurance fraud. Specifically, under MCL 500.4511(1), a person who commits a fraudulent insurance act is guilty of a felony punishable by as many as four years in prison and a fine of up to $50,000, as well as payment of restitution. Third, it is axiomatic that a plaintiff, no matter who that person is, has the burden of proving their case at trial. Thus, to the extent that an insurer believes that a claim involving one family member against another is unsupported, the insurer has plenty of tools available to attack the legal merits of that claim. Fourth, nearly all automobile accidents occurring in our populated state in the advent of the modern age are witnessed by someone else. This author, however, has never seen a step-down provision that is removed when a claim is corroborated by a witness. It is therefore respectfully submitted that all of the bases for step-down provisions are entirely specious.

B. SURVEY OF STEP-DOWN PROVISIONS AND MICHIGAN INSURERS

This subsection attempts to provide, as best this author can, a basic overview of those auto insurers who do and do not use step-down provisions in their "*standard*" Michigan auto policies. This information is being provided with a few important caveats. Specifically, this author has done his professional best to collect "*standard*" insurance policies from various Michigan insurers. Those policies, however, are frequently revised and substituted with new policies and/or amendatory language.

Accordingly, it cannot be emphasized enough that anyone representing an individual with a claim involving a step-down provision must obtain a complete, certified copy of the automobile insurance policy in effect at the time of the collision. Only upon a careful review of the policy can the practitioner make the determination about whether a step-down provision exists and what, if anything, can be done to challenge it. It should also be noted that step-down provisions can occur in different sections of the policy. Most often, they are included in the "*exclusions*" sections of the policy. But the entire policy must be read together in order to gain an accurate assessment.

Listed below is this author's attempt to catalog all of the auto insurers who write insurance in Michigan who do use step-down provisions in their "*standard*" auto policies:

- Progressive
- Farm Bureau
- GEICO
- Grange
- USAA

Of those auto insurers who use step-downs, perhaps none is more prolific in terms of the volume coverage written than Progressive. Accordingly, attorneys representing auto accident victims should always be mindful of the step-down issue when handling a claim involving a Progressive policy.

Attached as ***Exhibit 1*** is a complete copy of Progressive's standard Michigan auto insurance policy that was obtained earlier in 2015 concerning an automobile accident that occurred in 2013. The step-down provision that applies to liability claims in the Progressive policy can be found on pages 3 and 4 of ***Exhibit 1***. The full language of the Progressive's step-down is as follows:

> *"Coverage under this Part I, including our duty to defend, will not apply to any insured person for. . . 11. bodily injury to you or a relative. This exclusion applies only to damages in excess of the minimum limit mandated by the motor vehicle financial responsibility law of Michigan."*

Progressive's Policy Ex. 1, at 3-4.

As with all step-downs, the provision itself often includes terms of art that are defined elsewhere in the policy, including phrases such as *"you"* or *"insured." Id.* The step-down provision in Progressive's policy references the policy's definitions of *"you"* and *"relative." Id.* The definitions of these terms in Progressive's policy can be found on pages 1 and 2. Those definitions are as follows:

> *"'Relative' means a person residing in the same household as you, and related to you by blood, marriage, or adoption, and includes a ward, step-child, or foster child. Your unmarried dependent children temporarily away from home will qualify as a relative if they intend to continue to reside in your household. . . .'You' and 'your' mean: a. a person shown as a named insured on the declarations page; and b. the spouse of a named insured if residing in the same household at the time of the loss."*

Id. at 2.

Progressive's definitions of these words, particularly the phrase "*relative,*" are vast and accompany a wide array of potential claimants. Simply put, Progressive's step-down provision will reduce intra-familial liability claims when those claims involve bodily injuries sustained by the named insured(s), any relative of the insured (including adopted children, step-children, and foster children) who live in the same household as the insured, or children who temporarily live away from home as the named insured (so long as those children intend to continue to reside in the insured's home). If any of these individuals sustain bodily injury and pursue a claim against another, the step-down will limit the bodily injury claim to $20,000.

Second only to Progressive in terms of prolific insurers who use step-down provisions is Farm Bureau. Included as ***Exhibit 2*** is a copy of Farm Bureau's "*standard*" automobile policy that was obtained in 2014 in connection with a claim that occurred in 2014. Farm Bureau's step-down provision regarding liability claims can be found on pages 5 and 6 of Farm Bureau's policy. The step-down provision in Farm Bureau's policy states in pertinent part:

> *"We do not provide Liability Coverage for any Insured: . . . m. for bodily injury to you or to any family member that exceeds the minimum statutory limits of the financial responsibility law or any similar laws of the State of Michigan or any other state or province in which an otherwise covered auto accident occurs."*

Farm Bureau's Policy Ex. 2, at 5-6.

Farm Bureau's step-down provision references the policy definition of "*family member.*" *Id.* at 6. Farm Bureau's policy defines family member as follows:

> *"Family member means a person related to you by blood, marriage, or adoption who is a resident of your household. This includes: 1. Your ward or foster child; 2. A dependent child while away from home attending any school or college; and 3. A member of the United States military while away from home during their first enlistment."*

Id. at 3.

Farm Bureau's step-down functions are almost identical to Progressive's. Specifically, Farm Bureau's step-down provision and the incorporated definition of "*family member*" reduce bodily injury claims sustained by an insured or any family member (including adopted children, wards, or foster children, as well as college students) to $20,000. Perhaps even more offensively, the Farm Bureau policy also imposes the step-down language to members of the United States military.

This paper does not include copies of the standard auto policy issued by GEICO, Grange, or USAA. Based on this author's professional experience and review of the case law, however, these insurers use step-downs as part of their "*standard*" Michigan auto policies. In fact, two of the cases discussed in the next section involve GEICO and USAA.

It is also worth noting and commending those auto insurers who do not incorporate step-down provisions into their policies. As the next section will explain, Michigan courts have, and likely will continue to, enforce these step-down provisions. In other words, it is presumed that most auto insurers know that they can "*get away with*" step-down provisions. Therefore, those who choose to not use step-down provisions should be acknowledged. While many of us in the trial bar have differences of opinion with various insurers, we should recognize those who do not make the morally repugnant choice of using step-down provisions. It is this author's experience that the following insurers do not use step-down provisions in their standard Michigan policies:

- Auto-Owners/Home-Owners
- Liberty Mutual
- Citizens
- State Farm
- AAA
- Allstate

C. SIGNIFICANT CASE LAW REGARDING STEP-DOWN CLAUSES

In order to understand the case law dealing with step-down provisions, one must keep in mind the requirements of Michigan statutes regarding mandatory insurance. In the auto context, Michigan law requires that all drivers maintain minimum liability coverage in the amount of $20,000 per person/$40,000 per accident (MCL 500.3009) and no-fault PIP coverage (*see* MCL 500.3101 *et seq.*).

As a general proposition, Michigan courts will not enforce insurance contracts that contravene the requirements of Michigan statutes. However, to the extent that Michigan statutes are silent on an issue otherwise addressed in an insurance contract, then the trend in Michigan courts is to enforce the insurance contract as written.

This latter point was perhaps most evident in the Michigan Supreme Court's 2012 case of *DeFrain v State Farm Mut. Auto. Ins. Co.*, 491 Mich. 359 (2012). As many remember, in this case, the Michigan Supreme Court upheld the enforcement of a 30-day notice to exclude uninsured motorist coverage to man in a coma. *Id.* at 376. The Court's decision in *DeFrain* was a high watermark regarding the trend in Michigan jurisprudence to strictly enforce insurance policy language that does not otherwise conflict with Michigan statutes.

An illustration of this point in the context of step-down clause is best demonstrated in the case of *Farmers Insurance Exchange v Kurzmann*, 257 Mich. App. 412 (2003). *Kurzmann* involved a tragic case where one brother was seriously injured in an automobile accident caused by the negligence of another brother. *Id.* at 413. The vehicle was owned by the boys' father. *Id.* at 414. The injured son's mother, Kathryn Kurzmann, pursued a liability claim against the negligent son and her husband. *Id.* Her claim was denied by the liability insurer, Farmers, even though the insurance in effect at the time of the collision had liability limits of $250,000 per person/$500,000 per accident. *Id.* at 414-15.

Farmers' denial in *Kurzmann* was a complete denial of its duty to defend and provide any coverage. *Id.* at 414. Farmers relied on the exclusion section of its policy that stated that it was not liable "*for bodily injury to an injured person." Id.* Like so many policies, the phrase "*injured person"* was defined in the Farmers' policy as "*you or any family member." Id.* Farmers therefore took the position that it had no duty to defend the defendant driver or defendant owner, and was not required to pay anything toward the liability claim. *Id.* at 414-15. In the alternative, Farmers argued that its indemnification obligation could not exceed the statutory minimum of $20,000 in liability coverage. *Id.* at 415-16.

On appeal, the Court of Appeals upheld the trial court's denial of Farmers' motion for summary disposition and affirmed the trial court's granting of disposition in favor of the plaintiff. *Id.* at 424. The Court of Appeals held that Farmers' exclusionary clause was both ambiguous and void as against public policy. *Id.* at 419, 422. As a result, the Court of Appeals held that <u>none</u> of Farmers' exclusionary policy could apply to the claims in the case. *Id.* at 422. In other words, the outcome of the Court of Appeals' decision was that the plaintiff was allowed to pursue liability claims up to the $250,000 maximum coverage available under Farmers' policy. *Id.*

It is important to note, however, that the central basis for the Court of Appeals' holding in *Kurzmann* was the fact that the exclusionary language used by Farmers violated Michigan statute because it created a situation where there was <u>no insurance coverage whatsoever</u> . *Id.* at 418-19. In other words, Farmers' exclusion went beyond limiting the liability claim to the state-mandated minimum $20,000 and eliminated the claim altogether because of the specific language of the exclusion. *Id.* The *Kurzmann* court reviewed well-established Michigan law that held that an insurance policy cannot exclude coverages that are required by Michigan law, such as minimum bodily injury liability coverages and no-fault coverage. *Id.* In this regard, the Court held:

> *"For more than twenty years, it has been against the public policy of this state to include a provision in an insurance policy that excludes coverage for bodily injury to any insured or a member of the insured's family (internal citations omitted). Under MCL § 257.520(b)(2), liability insurance policies are required to insure the*

person named therein and any other person, as insured, using any such motor vehicle or motor vehicles with the express or implied permission of such named insured, against loss from the liability imposed by law for damages arising out of the ownership, maintenance or use of such motor vehicle . . . The Michigan no-fault act, MCL § 500.3101 et. seq. similarly requires that an automobile insurance policy provide for residual liability. Thus it is clear from the pleadings alone that Farmers' exclusionary clause was void as against public policy".

Id.

Simply put, the exclusionary clause used by Farmers struck down by the *Kurzmann* court went too far. *Id.* The exclusionary clause attempted to eliminate all insurance involving claims between family members. *Id.* The Court of Appeals held that an insurance company was not able to circumvent the requirements of state law by using such language in its policy. *Id.* at 418-19, 424.

Kurzmann is sometimes mistakenly interpreted to mean that step-down provisions are illegal. In fact, it more likely that the opposite is true. That is, both published and unpublished cases hold that step-down provisions are enforceable, so long as they maintain the state-mandated minimum liability insurance coverage. This point was illustrated by the Court of Appeals in two cases in the 1990s.

In *Bogas v Allstate Insurance Company*, 221 Mich. App. 576, 577-78 (1996), the Michigan Court of Appeals upheld an exclusion in an umbrella liability policy that barred claims for personal injuries by an insured's "*resident spouse and any other person related to the named insured by blood, marriage, or adoption who resides in the named insured's household*." On appeal, the Court of Appeals rejected plaintiff's argument that Allstate's clause was against public policy. *Id.* at 578. In this regard, the Court of Appeals noted that there is a distinction between those exclusions that eliminate compulsory insurance and those that do not. *Id.* The Court of Appeals acknowledged that cases such as *State Farm Mutual Automobile Insurance Company v Sivey*, 404 Mich. 51 (1978), voided household exclusions for compulsory insurance policies such as no-fault PIP policies. *Id.* On the other hand, the Court noted that an umbrella policy was not a compulsory policy. Thus, Allstate was free to exclude coverage for claims between family members:

"Rather, we agree with defendant that the public policy considerations discussed in Sivey, supra, which made a household exclusion for a compulsory automobile policy void are not relevant for optional policies, such as the umbrella policy at issue. Our Supreme Court's decision in Sivey, supra, was based upon the fact that the motor vehicle financial responsibility act, M.C.L. § 257.520(b); M.S.A. § 9.2220(b), specifically required that policies of liability insurance provide coverage for liability arising out of the ownership, maintenance, or use of a motor vehicle. . . . Because the

umbrella policy at issue, an optional insurance policy that applied not only to liability arising from the use of an automobile but also other personal activities of the insured, does not conflict with any statutory provisions mandating the coverage that the household exclusion excludes, we hold that the exclusion in the policy is enforceable."

Id.

A similar holding was reached by the Court of Appeals in *Farm Bureau Mutual Insurance Company v Moore,* 190 Mich. App. 115 (1991). This case involved injuries sustained by a plaintiff while at the construction site of her parents' cottage. *Id.* at 116. The plaintiff suffered total paralysis as a result of an injury to her spinal cord caused by a falling wall, and she pursued a claim under her parents' homeowner's insurance policy. *Id.* That policy, which was written by Farm Bureau, had an exclusion for liability claims for bodily injuries to an insured or resident of the insured. *Id.* at 117. On appeal, the Court of Appeals rejected plaintiff's argument that the Farm Bureau policy violated earlier Michigan law regarding intrafamily immunity. *Id.* In that regard, the Court stated as follows:

"There is, however, a major difference between striking down the common-law intrafamily immunity doctrine and limiting an insurance company's ability to write coverage exclusions into insurance contracts. In a case decided after Plumley, Powers v DAIIE, 427 Mich. 602; 398 N.W.2d 411 (1986), the Court recognized the validity of exclusionary clauses: 'We would hold today that a no-fault insurer may exclude coverage for residual liability when an insured is driving a vehicle owned by a resident family member, so long as the exclusion is clearly and unambiguously stated.'" (internal citations omitted)

Id. at 117-18.

In addition to this published authority, the Michigan Court of Appeals has recently rendered at least two unpublished decisions that specifically address the enforceability of step-down provisions in automobile insurance policies. In sum, the Court of Appeals has held in these unpublished cases that step-down provisions are enforceable, provided that the step-down provisions permit the injured family member to claim at least the state-mandated minimum coverage of $20,000 per person/$40,000 per occurrence. These unpublished cases are discussed below.

In 2006, the Court of Appeals rendered a decision in the case of *GEICO Indemnity Insurance Company v Williamson*, 2006 Mich. App. LEXIS 255 (August 17, 2006). A copy of the *Williamson* opinion is included in the materials at ***Exhibit 3***. In this case, a wife was injured in a car driven by her husband. *Id.* at *1. The husband had automobile liability insurance coverage through GEICO in the amount of $100,000 per person/$300,000 per

occurrence. *Id.* GEICO claimed that, under the step-down provision in its auto insurance policy, the wife was permitted to make a liability claim no greater than $20,000. *Id.* The step-down provision in the GEICO policy stated: "*We will not defend any suit for damages if one or more of the following exclusions listed below applies. 1. Bodily injury to any insured or any relative of an insured residing in his household is not covered in excess of the minimum financial responsibility limit." Id.* at *2. The Court of Appeals rejected the wife's argument that the language was ambiguous and affirmed the trial court's granting of summary judgment in favor of GEICO. *Id.* As the Court stated:

> *"Defendants argue that this language unambiguously provides that the limit applies only to plaintiff's duty to defend, and not its duty to pay. Alternatively, they argue that the placement of the clause regarding the duty to defend before and above the exclusions renders the meaning of the exclusion ambiguous. We agree with the trial court's conclusion that, although the policy is inartfully worded and clumsily arranged, (internal citation omitted), it nonetheless unambiguously sets forth the exclusion as an exclusion to coverage, as well as limiting plaintiff's duty to defend. Thus, we affirm the trial court's grant of summary disposition to plaintiff."*
>
> *Id.*

In 2008, the Court of Appeals issued another unpublished decision that dealt an even larger blow to auto accident victims subject to step-down provisions. Specifically, in *Ruzak v USAA Insurance Agency*, 2008 Mich. App. LEXIS 1318 (June 24, 2008), the Court of Appeals issued a more lengthy decision regarding the enforceability and public policy considerations attendant to a step-down provision in a USAA automobile insurance policy. *Id.* A copy of the *Ruzak* decision is included at ***Exhibit 4***.

Similar to *Williamson*, the plaintiff in *Ruzak* was a wife who was severely injured when her husband lost control of a truck that he was driving, leading to a collision with a nearby tree. *Id.* at *1-2. The husband was covered under a USAA automobile insurance policy that provided liability coverage in the amount of $300,000 per person/$500,000 per accident. *Id.* at *2. Unfortunately, the USAA insurance policy included a step-down provision that stated:

> *"There is no coverage for [bodily injury] for which a covered person becomes legally responsible to pay a member of that covered person's family residing in that covered person's household. This exclusion applies only to the extent that the limits of liability for this coverage exceed $20,000 for each person or $40,000 for each accident."*
>
> *Id.*

Credit is owed to the trial court in the *Ruzak* case who refused to enforce the step-down provision in the USAA policy. *Id.* at *2-3. Although the trial court found that the step-down provision was unambiguous, the trial court refused to enforce it on the basis that it was "*repugnant, reprehensible and unconscionable.*" *Id.* at *3.

Unfortunately, the Court of Appeals did not agree with the trial court. *Id.* at *5-10. The Court of Appeals first reviewed the language of the step-down provision and pertinent Michigan case law and held that the step-down provision was unambiguous. *Id.* at *4-5.

More troubling, however, was the Court of Appeals' reversal of the trial court's decision not to enforce the step-down provision on public policy grounds. *Id.* at *7-8. In this regard, the Court of Appeals held: "*That the trial court improperly substituted its own policy choice in resolving this matter in favor of plaintiff.*" *Id.* The Court of Appeals went on to say that USAA's step-down provision did not violate the law because it did not entirely eliminate liability coverage for the injured spouse. *Id.* at *8. In this regard, the Court of Appeals stated:

> *"Here, there was no evidence that clearly demonstrated that the contested provision transgresses the law. While plaintiff argues that the contested provision is void because it entirely eliminates liability coverage for bodily injury suffered by a family member of the insured, this argument lacks merit. Family members have the statutory minimum coverage because the policy is written in conformity with the residual liability coverage positions of MCL 500.3131 and MCL 500.3009(1)."*
>
> *Id.*

It should be noted that the Court of Appeals' assessment regarding the mechanics of the USAA policy and the fact that it retained the state minimum liability coverage is correct. More troubling, however, is the Court of Appeals' discussion that follows explaining its rationale for why this step-down provision was neither procedurally or substantively unconscionable.

The court first noted that the standard for substantive unconscionability is "'*whether a term is substantively unreasonable where the inequity of the term is so extreme as to shock the conscious.*'" *Id.* at *9-10 (quoting *Clark v Daimer Chrysler Corp.*, 268 Mich. App. 138, 144 (2005)). Using rather circular reasoning, the court held that the step-down provision did not shock the conscious because an insurer was free to limit the scope of its coverage, and the step-down provision still comported with the state-mandated liability insurance limits. *Id.* The court also held that USAA's step-down was not procedurally unconscionable because the husband-insured could have purchased auto insurance through another carrier. *Id.* at *10. Here, the court stated:

"In the instant case, there was no evidence that [the husband] had no other options regarding automobile insurance and that his only choice was to accept the terms as presented in defendant's policy. Under a fair appraisal of the circumstances [the husband] was free to accept the policy terms or reject them and to obtain automobile insurance through another provider. Thus, we conclude that procedural unconscionability was not present. In addition, substantive unconscionability is not present because the inequity of the term is not so extreme as to shock the conscious. An insurer is free to define or limit the scope of coverage as long as the policy language fairly leads to only one reasonable interpretation and is not in contravention of public policy (internal citations omitted). As already stated, the limited scope of coverage in the contested provision comports with the minimum coverage requirements of MCL 500.3131 and MCL 500.3009(1)."

Id.

It is respectfully submitted that the *Ruzak* court's analysis of the unconscionability issue in *Ruzak* is flawed. As to substantive unconscionability, the Court seems to be taking a position that the only benchmark for determining the unconscionability of a contract is state statute. In other words, so long as a contract comports with state statutes, the Court of Appeals' opinion in *Ruzak* stands for the proposition that it cannot, by definition, be deemed substantively unconscionable. The implicit result here is that the courts have no role in answering the question of what is substantively unconscionable.

More troubling, however, is the court's analysis regarding procedural unconscionability. In this regard, the *Ruzak* court reasoned that the USAA policy was not unconscionable because the husband-insured could have purchased a policy with another insurer. *Id.* While this is most likely factually correct, the court side-stepped the real procedural unconscionability issue presented in *Ruzak*. That is, what if all auto insurers in the state of Michigan elected to use step-downs? In that case, no one would be able to purchase an auto insurance policy that was free from a family step-down. In that case, every time a family member was catastrophically injured by the negligence of another family member, that family member's liability claim would be capped at $20,000 per person.

Thus, the *Ruzak* court's analysis seems to imply that the court is not interested in addressing procedural unconscionability until all insurers in the state of Michigan elect to insert step-down provisions in their automobile insurance contracts. Certainly, as the foregoing analysis demonstrates, all auto insurers throughout Michigan could legally use step-down provisions. The question for the courts, however, should be whether or not those step-down provisions are procedurally unconscionable. It is respectfully submitted that they are and that the *Ruzak* court simply "*punted*" on this issue.

The cases described above lead to one general conclusion: so long as step-down provisions retain PIP coverage and liability coverage for the state-mandated minimum of $20,000 per person/$40,000 per occurrence, those step-down provisions are enforceable Again, it is respectfully suggested that this is jurisprudentially and morally wrong. Unfortunately, it does appear to be the most accurate statement of current Michigan law. However, not all hope should be lost. There are possible ways to attack step-down provisions in each individual case. Those possible strategies are outlined in the next subsection.

D. SUGGESTED STRATEGIES FOR DEALING WITH STEP-DOWNS

Although the current state of Michigan law is not hopeful regarding step-downs, there are issues that should be considered whenever a practitioner encounters one of these provisions. Obviously, the strategies outlined below are only this author's thoughts, and they are not an exhaustive list of potential mechanisms for dealing with step-downs.

1. Carefully analyze the family relationship and residency of the injured person

As the discussion above demonstrates, the enforceability of a step-down provision against an injured person will depend entirely on the specific language used in that step-down provision. The Progressive and Farm Bureau step-downs cited above show how important it is to analyze the specific language of the policy with regard to the relationship between the family members who are subject to the step-down and the residency of those family members. *See*, Progressive's Policy Ex. 1; *see also*, Farm Bureau's policy Ex. 2.

As the Progressive and Farm Bureau step-down provisions show, step-downs apply only to the class of family members as defined in the policy. Unfortunately, both Progressive and Farm Bureau have inserted language that covers nearly any possible family member. However, not all insurers may be as sophisticated. It is therefore suggested that the definition of family member used in the policy must be carefully examined to determine whether or not the injured family member falls within that definition.

In addition, most step-downs apply only to family members who "*reside*" with the named insured or other drivers listed on the policy. Obviously, the definition of one's "*residency*" has been the subject of much discussion in Michigan auto law jurisprudence. Suffice to say, however, that to the extent that there are any ambiguities with regard to the injured person's residency at the time of injury, those ambiguities should be explored and used on behalf of the injured person.

2. Watch out for total exclusions against liability claims by injured family members

The above discussion makes clear that step-down provisions are only enforceable if the step-down retains the state-mandated liability insurance requirements of $20,000 per person/$40,000 per accident. It cannot be emphasized enough that the step-down provision in any individual case must be carefully examined to insure that the provision retains these minimum liability insurance limits. If the minimum liability insurance limits are not retained by the step-down, then current Michigan law holds that the entire step-down is void. This was the precise holding in the case of *Farmers Insurance Exchange v Kurzmann*, 257 Mich. App. 412 (2003), as discussed above. Of course, most insurers are probably aware of this holding. Nevertheless, a step-down must be closely examined to make sure that it retains all state-mandated insurance requirements. If it does not, than the practitioner should take the position that the entirety of the step-down provision is void, and cite *Kurzmann* for this proposition.

3. Explore any ambiguities in the step-down provision

The practitioner should also closely examine all of the language in the insurance policy that pertains to the step-down to determine whether or not there is an argument for ambiguity in the policy. In this regard, the practitioner should also remember that the step-down itself is at odds with the stated amount of liability coverage on the declaration page. The case law discussed above does indicate that it is an upward battle to prove that the policy language is ambiguous. Nevertheless, all efforts should be made to exploit any ambiguity in the policy because of the consequences of a judicial determination regarding ambiguity.

The goal of identifying any ambiguity in the policy is not to invalidate the step-down provision. Rather, if a step-down or associated policy language is deemed ambiguous by a court, then Michigan law holds that the injured person is entitled to bring in extrinsic evidence concerning their understanding of the policy. Obviously, when it comes to step-downs, this is an advantageous position for an injured person. It is almost certain that no injured person subject to a step-down ever had any understanding or knowledge of what a step-down provision was before it was too late. Accordingly, if the practitioner is able to convince the trial court that the policy is ambiguous, than the practitioner will be able to introduce evidence of the client's understanding regarding the liability coverage. From a trial perspective, testimony regarding a catastrophically injured person's understanding of the basic workings of an insurance contract will most certainly resonate with a jury. In addition, a jury is likely to be disgusted by an insurer's use of a step-down provision.

As such, some basic points of Michigan law are worth remembering. Michigan courts have long held that *"[a]n insurance contract is ambiguous when its provisions are capable of conflicting interpretations." Farm Bureau Mut. Ins. Co. v Nikkel,* 460 Mich. 558, 556 (1999). This principle was recently affirmed by the Michigan Supreme Court in *Klapp v United Insurance Group Agency, Inc.*, 468 Mich. 459, 480 (2003), where the Court stated: *"If two provisions of the same contract irreconcilably conflict, than the language of the contract is ambiguous."* In addition, Michigan courts have held that "*[i]n interpreting ambiguous terms of an insurance policy, this court will construe the policy in favor of the insured." Frankenmuth Mut. Ins. Co. v Masters,* 460 Mich. 105, 111 (1999). Furthermore, the existence of an ambiguity in an insurance policy allows the insured to introduce extrinsic evidence in order to interpret the terms of the policy. 468 Mich. at 470. As the Michigan Supreme Court held in *Klapp:*

> *"Where a written contract is ambiguous, a factual question is presented as to the meaning of its provisions, requiring a factual determination as to the intent of the parties in entering the contract. Thus, the fact finder must interpret the contract's terms, in light of the apparent purpose of the contract as a whole, the rules of contract construction, and extrinsic evidence of intent and meaning."*
>
> *Id.*

This principle is significant because Michigan courts have held that the extrinsic evidence that may be considered include the parties' understanding of the contract terms. *Id.* at 469-70. As the Supreme Court stated in *Klapp: "If the contract in question were ambiguous . . . extrinsic evidence, particularly evidence which would indicate the contemporaneous understanding of the parties, would be admissible as an aid in construction of the disputed terms." Id.* (quoting *Penzien v Dielectric Products Engineering Co., Inc.*, 374 Mich. 444, 449 (1965)).

Accordingly, all step-down provisions should be carefully analyzed with these concepts in mind. In terms of negotiating, practitioners should also consider arguing to the adjuster or defense counsel about the potential existence of ambiguity. Certainly, large auto insurers have an interest in preventing a court ruling that their step-down is ambiguous.

4. Don't overlook the UIM section of the policy

Step-down provisions have the effect of lowering the liability coverage applicable to the injured person to an amount that is less than the value of the injured person's damages. Accordingly, step-downs have the practical effect creating a liability claim against a tortfeasor with only a $20,000 liability policy. In this regard, one needs to carefully consider the existence of any potential underinsured (*"UIM")* motorist coverage under the subject policy.

Unfortunately, most insurers appreciate this issue and include corollary step-down language in the UIM sections of their policy. For example, the Farm Bureau policy included at ***Exhibit 2*** states: *"This coverage does not apply to . . . 9. Any claim or suit by you or any family member against you or any family member for bodily injury to you or any family member."* Farm Bureau's policy, *supra* at 17.

Yet the practitioner should not assume that the UIM portion of the subject policy contains corollary language that would also subject an UIM claim for the same step-down. Therefore, the UIM language should be closely examined to see whether or not there is any potential for exploiting the ambiguity in the language of the UIM section of the policy.

If the practitioner successfully identifies an avenue for a UIM claim under a policy that otherwise contains a liability step-down, then the practitioner must carefully craft a release of the liability claim that preserves all UIM claims. In addition, that language should state that settlement of the liability claim (that is subject to the step-down) gives the settlement consent required under the UIM portion of the policy, and that the insurer will not raise any failure to obtain consent later. A redacted example of a settlement release involving a catastrophically injured Progressive insured is included in the materials at ***Exhibit 5***. This release language attempts to preserve any and all possible UIM claims even though the claimant was subject to Progressive's step-down provision under the liability section of the policy. *See* Redacted Settlement Release Ex. 5, at 1-2.

5. Preserve all derivative loss of consortium claims

Often times, the practitioner will consider all the foregoing and conclude that the step-down provision is enforceable. Even under that scenario, the practitioner should examine if there are any claims that derive from the serious injury to the victim. Most obviously, such derivative claims include claims for spousal loss of consortium and the loss of parental consortium sustained by minor children. It should be remembered that Michigan still recognizes the loss of consortium sustained by children when a parent is seriously injured. *See, Berger v Weber,* 411 Mich. 1 (1979).

Accordingly, the practitioner must be mindful of the effect of settling the claim of the injured person that is subject to the step-down. For example, assume that a wife was injured when her son negligently drove the vehicle. The wife obviously has a claim for her own personal injuries, and the husband has a derivative claim for his loss of consortium. Similarly, assume that a wife is injured in a motor vehicle accident caused by her husband's negligence. The wife's minor children have a claim for their loss of consortium.

Even if the wife's claim is subject to a step-down and limited to $20,000, if the practitioner does not represent the other claimants with derivative claims, the release must be carefully worded so as to preserve those derivative claims. Included in the materials at ***Exhibit 5*** is language that Progressive agreed to in connection with a release of a catastrophically injured mother. That release expressly preserves the rights of the mother's children to pursue loss of consortium claims. *See,* Redacted Settlement Release, *supra* at 2. Although it is likely true that the children's claims are also subject to the step-down, preserving their claims at least allows the family to gain some additional compensation. In other words, two claims subject to a step-down are better than one.

6. Consider claims against independent insurance agents

One of the most troubling aspects about step-down provisions is the general ignorance in the insurance agent community about this problem. This author has spoken with various insurance agents who are either ignorant of the problem or do not know which of the various insurers use step-downs. It is respectfully suggested that any insurance agent that does not understand this issue is not living up to his or her professional standards and duty to their customers. Therefore, any claims subject to a step-down should also be reviewed with an eye towards whether or not a claim can be pursued against the insurance agent. Claims against insurance agents are challenging under Michigan law, and the general principles of Michigan law regarding these cases are outlined below.

The first issue to examine is whether the insurance agent is an independent agent or an exclusive (also known as a "*captive*") agent. Unfortunately, step-downs appear most commonly with the large insurers such as Progressive or GEICO, who sell their policies online or through captive agents. Michigan courts have held that an exclusive agent is deemed an agent of the insurer. *See Harts v Farmer Ins. Exch.,* 461 Mich. 1, 7 (1999). Accordingly, if an auto insurance policy containing a step-down is sold through an exclusive agent, then there is most likely no separate claim against the agent. *Id.*

On the other hand, Michigan courts have held that independent insurance agents owe a duty of loyalty and good faith to the insured. *See Burton v Burton*, 332 Mich. 326, 337 (1952). In *Genesee Food Service, Inc. v The Meadowbrook, Inc.*, 279 Mich. App. 649, 656 (2008), the Court of Appeals described the duty owed by an independent agent as follows:

> *"[B]ecause [the agents] were independent insurance agents when they assisted [the] plaintiffs, their primary fiduciary duty of loyalty rested with [the] plaintiffs, who could depend on this duty of loyalty to ensure that [the agents] were acting in their best interests, both in terms of finding an insurer that could provide them with the most comprehensive coverage and ensuring that the insurance contract properly addressed their needs."*

Although independent insurance agents owe a duty of loyalty and good faith to an insured, Michigan courts have held that an independent insurance agent does not have an affirmative duty to advise a client regarding the adequacy of a policy's coverage. *See Mate v Wolverine Mut. Ins. Co.*, 233 Mich. App. 14, 22 (1998). Nevertheless, there is an exception to this rule of no affirmative duty when an event occurs that alters the nature of the relationship between the agent and the insured. Specifically, in *Harts v Farmer Insurance Exchange,* 461 Mich. 1, 10-11 (1999), the Michigan Supreme Court held that a "*special relationship"* between an independent insurance agent and an insured arises in the following circumstances:

> *"(1) the agent misrepresents the nature or extent of the coverage offered or provided, (2) an ambiguous request is made that requires a clarification, (3) an inquiry is made that may require advice and the agent, though he need not, gives advice that is inaccurate, or (4) the agent assumes an additional duty by either express agreement with or promise to the insured*."

If an insured can show that one of these circumstances existed between the insured and the independent agent, then the insured will be able to establish that there was a "*special relationship." Id.* Thus, if the insured can then further show that the independent agent failed to adequately advise the insured regarding the adequacy of coverage that results from a step-down, then the insured should have a cognizable claim against the independent agent. *Id.* Obviously, these circumstances will be unique and will depend on the specific facts and circumstances of an individual case. However, a practitioner dealing with a step-down provision involving a catastrophically injured client should carefully interview the clients to determine whether it is possible to pursue a claim against an independent insurance agent.

E. A CALL TO ACTION!

This author respectfully submits that this entire paper should not exist. That is, in a society that supposedly values family and children, we should all adamantly insist that step-downs are indefensible and unacceptable. What is most disturbing about step-downs is that they take away the rights of people, most notably children, who have no culpability in the event that caused their injury, and who had no knowledge of or participation in the procurement of the insurance contract that so drastically limits their legal rights. It is therefore incumbent upon all of us to educate the public about this problem and to use any available opportunity to call out this repugnant conduct.

We should first educate our friends, co-workers, church members, and the public at large about the issue of step-downs. We should then carefully keep track of those insurance companies that use step-down provisions in their "*standard*" Michigan automobile insurance policies. Next, we should advise as many people as possible to never purchase an automobile insurance policy through an insurer that uses a step-down provision. In this respect, our goal should be to effectuate change in the insurance marketplace so that insurers like Progressive, Farm Bureau, and GEICO decide that it is no longer in their financial interest to write insurance policies that contain step-down provisions.

In addition, we also need to educate regulators and legislators about this issue. The insurance industry's position regarding step-downs is indefensible. Accordingly, if we engage regulators and legislators on this issue, they will most likely see the correctness of our position. In that regard, attached as ***Exhibit 6*** is a copy of a document entitled "*Your Guide to Automobile Insurance for Michigan Consumers"* authored and promulgated by the Department of Insurance and Financial Services (DIFS). Not surprisingly, this publication makes no reference whatsoever to the issue of step-down provisions. *Id*. Each time one of us represents an injured person who is subject to a step-down provision, we should advise DIFS about this problem in hopes of getting that regulatory agency to consider banning step-downs in Michigan auto insurance policies.

From a legislative perspective, we should encourage legislators to consider bills that ban step-down provisions. Yet the most effective legislative solution to the step-down problem is to amend the state statutes regarding the state-mandated amounts of liability insurance coverage. *See* MCL 500.3009. As the case law above discusses, step-down provisions are enforceable only if the step-downs retain the state-mandated limits of liability coverage. In other words, if MCL 500.3009 were amended so as to require all motorists to have at least $100,000 in liability coverage, then no person would be subject to a step-down that reduces their liability claim to $20,000.

III. PROBLEMATIC UNINSURED (UM) AND UNDERINSURED MOTORIST (UIM) CLAUSES

Any practitioner representing a seriously injured car accident victim has dealt with the issue of uninsured ("UM") and underinsured ("UIM") motorist claims. Previously, Michigan statutes included mandatory uninsured motorist coverage. This statute used to appear at MCLA 500.3010, and required at least $10,000 in uninsured motorist coverage. Unfortunately, Michigan repealed the mandatory uninsured motorist statute.

Thus, there is currently no state statute that requires drivers to carry any uninsured or underinsured motorist coverage. Consequently, there are no state statutes that deal with regulation of UM or UIM coverage. Yet as any auto accident victim lawyer knows, UM/UIM coverage is some of the most important coverage that families can purchase to protect themselves. Accordingly, many Michiganders have purchased some form of UM and/or UIM coverage. However, since there is no state statute regarding UM/UIM coverages, the legal issues regarding these claims are, generally speaking, solely governed by the language of the UM/UIM portions of the automobile insurance policies. Accordingly, any attorney representing an auto accident victim involving an UM/UIM claim must carefully review the language of that policy in order to understand the client's rights and how best to protect those rights.

Due to the fact that UM/UIM coverage is governed entirely by the terms of the auto insurance contract, many auto insurers use widely different language in the UM/UIM portions of their policies. Unfortunately, some auto insurers have inserted clauses in the UM/UIM portions of their policies that are very unfavorable to the insured. Practices by auto insurers in this regard vary widely between insurers and are frequently subject to change. Nevertheless, this section of the paper is intended to provide an overview with some of the common clauses that auto insurers use in the UM/UIM portions of their policies. As discussed below, the most frequent problems occur in cases where an injured person can claim UM/UIM benefits from more than one insurer.

A. EXCLUSIONS FOR "*SAME OR SIMILAR*" COVERAGE

When an injured person is involved in a motor vehicle accident in a car that is not owned by the injured person, there are often claims with multiple insurers for UM/UIM benefits. It is incumbent upon the practitioner to examine all of the possible auto insurers that may have exposure for the client's UM/UIM claims. Once that examination is complete, the practitioner should then closely compare the provisions of the different auto insurance policies to determine how those policies may or may not harmonize.

One of the first issues the practitioner should identify is whether either of the applicable auto insurance policies have a general exclusion for UM/UIM benefits in the event of coverage under multiple policies. It has been this practitioner's experience that this circumstance most frequently arises in connection with UM/UIM claims made under AAA (a/k/a ACIA) policies.

Attached to these materials at ***Exhibit 7*** is a copy of AAA's "*standard*" Michigan auto insurance policy. Page 11 of AAA's policy lists the exclusions that apply to claims for UM/UIM benefits. AAA's policy contains the following exclusion:

> *"This coverage does not apply to bodily injuries sustained by an injured person: . . . (b) while occupying a motor vehicle which provides the same or similar coverage for you or a resident relative. However, this exclusion will not apply to the extent that the Limit of Liability of this coverage is greater in amount than the liability of that same or similar coverage. . . ."*
>
> AAA's Policy Ex. 7, at 11.

The exact language of this exclusion was examined by the Michigan Court of Appeals in *American States Insurance Company v Kesten*, 221 Mich. App. 330 (1996). In *Kesten*, the plaintiff was a passenger in a car driven by a friend when that vehicle was struck by another vehicle driven by an uninsured motorist. *Id.* at 331. The friend's vehicle was insured by American States under a policy that had $100,000 in UM benefits. *Id.* at 333. The plaintiff also had an auto policy issued by AAA that included $20,000 in UM coverage. *Id.* at 332. The plaintiff's policy with AAA included the same exclusion cited above. *Id.*

On appeal, the Court of Appeals reversed the trial court's determination that AAA had liability for $20,000 in UM benefits. *Id.* at 334. Specifically, the Court of Appeals held that AAA's exclusion was clear and unambiguous. *Id.* at 333. That is, where the injured AAA policyholder was able to collect UM benefits in excess of those available under the UM policy, the Court of Appeals held that the AAA's UM coverage did not apply:

> *"As stated above, the language under 'Exclusions' is plain that if 'you' (the insured) are a passenger in a car, as here, that has UM coverage — and this UM coverage covers you, then ACIA's UM coverage does not cover you. There is nothing about this exclusion that is ambiguous."*
>
> *Id.*

Accordingly, when a client has UM benefits through AAA and where that client also has UM coverage available through another insurer in an amount that is greater than the AAA coverage, there is no claim for UM/UIM benefits under the AAA policy.

It should be noted, however, that this author once had a lengthy discussion with AAA's counsel regarding the language of this exclusion. During that exchange, AAA's counsel indicated his view that the exclusionary language cited above also pertains to UM claims by AAA's insured where the UM coverage under the AAA policy exceeds that available through another insurer. In other words, AAA's counsel took the position that AAA is entitled to reduce its UM exposure by the amount available through another auto insurer.

Perhaps it is easier to state it in terms of a hypothetical. This author's case involved a young man who had $250,000 in UM benefits through AAA and was an occupant of a motor vehicle struck by an uninsured motorist that had $100,000 in UM coverage through Auto-Owners. This author argued that the exclusion cited above had no application to this author's client's claim because the amount of AAA's UM coverage exceeded that of the UM coverage available on the vehicle occupied by this author's client. Yet AAA's counsel took the position that because the client had $100,000 in other UM coverage, AAA could reduce its overall exposure on its UM claim by $100,000, thereby creating a situation where this author's client could only claim $150,000 under the AAA policy. In sum, the dispute between this author and AAA's counsel turned on the meaning of the phrase "*to the extent*" as used in AAA's exclusion cited above. At this point in time, this author is unaware of any published or unpublished case that resolves the dispute. Nevertheless, other practitioners should be aware of this issue when handling UM/UIM claims under a AAA policy where the injured person also has coverage available through another auto insurer.

B. "*OTHER INSURANCE*" CLAUSES

Nearly every Michigan auto insurance includes a clause within the UM/UIM portion of the policy that is typically entitled "*Other Insurance.*" Again, the language of these provisions of the policy must be carefully analyzed, particularly when a practitioner represents a client that has claims for UM/UIM benefits with more than one auto insurer. Here is the "*other insurance*" language from the standard AAA policy that is included at ***Exhibit 7***:

> *"If there is other uninsured/underinsured motorist coverage with us or any other insurer for a loss covered by this part, we will only be liable to pay for the damages recoverable in the same proportion that the limit of liability of this coverage bears to the sum of all the applicable limits of liability that cover the loss. However, we will not be liable under this coverage to pay more than our proportionate share, as determined in the manner provided for in the previous sentence, of an amount equal to the highest limit of liability that is applicable to the loss."*

AAA's Policy, *supra* at *12.*

This language is cumbersome and confusing. In sum, this language essentially sets out a mathematical equation that must be solved in order to determine the amount of exposure that one particular insurer may have for a UM/UIM claim.

Let's use the scenario referenced above. Suppose the client is involved in an accident involving an uninsured driver while an occupant of a vehicle that had $100,000 in UM coverage. The client has $250,000 in UM coverage through AAA. As such, the total amount of UM coverage available to this particular client is $350,000. The "*other insurance*" clause requires that the practitioner determine what is often called each insurer's "*proportionate share*." This requires dividing the amount of AAA's limit of UM coverage ($250,000) by the total amount of all available UM coverage ($350,000). Dividing these two numbers yields 71.43%. In other words, under the "*other insurance*" clause of the AAA contract, it is required to pay 71.43% of the client's total damages.

This practitioner had a discussion with AAA's counsel regarding a different interpretation of the proportionate share calculation. The difference in opinion stems from the different reading of the exclusionary clause discussed in the preceding section That is, AAA's counsel posited, under the hypothetical discussed above, that the calculation of AAA's proportionate share of the client's damages should be determined by dividing the $150,000 (that AAA's counsel posited was its overall limit of liability pursuant to the exclusion discussed above) by $250,000, which AAA's counsel believed was the sum of AAA's $150,000 limit of liability and Auto-Owners' $100,000 limit of liability. Under that analysis, AAA's counsel posited that its proportionate share of the client's damages would be only 60% ($150,000/$250,000). Suffice to say that this author is unaware of any case law that resolves this dispute. Nevertheless, this author and AAA's counsel did agree that this dispute would be resolved by a judicial interpretation of AAA's exclusionary language discussed in the preceding section.

C. "*EXCESS*" PROVISIONS IN UM/UIM POLICIES

There is another problem that sometimes presents itself when representing a client who has claims for UM/UIM coverage with multiple insurers: What insurer does the client turn to first for UM/UIM benefits? Again, the answer to this question will depend upon the language of the UM/UIM portions of each auto insurer's contract. In this regard, the practitioner should be mindful of clauses in auto insurers' contracts that attempt to make their UM/UIM coverage "*excess*" to other UM/UIM coverages.

Perhaps the most prolific insurer to use an excess clause in the UM/UIM portion of its auto policies is Progressive. As stated in the standard auto policy at ***Exhibit 1***, Progressive's "*other insurance*" clause states as follows:

> "*If there is any other applicable uninsured or underinsured motorist coverage, we will pay only our share of the damages. Our share is the proportion that our limit of liability bears to the total of all available coverage limits. However, any insurance we provide with respect to a vehicle that is not a covered auto will be excess over any other uninsured or underinsured motorist coverage.*"

Progressive's Policy, *supra* at 16.

Notably, the first two sentences of this provision are essentially identical to the language used in the AAA policy. That is, the practitioner must calculate what proportion Progressive's UM/UIM coverage bears to the total of all available UM/UIM coverages. Under this clause, Progressive is obligated only to pay that proportionate share.

What makes Progressive's policy different, however, is the last section of the provision cited above. That is, Progressive expressly states that <u>any</u> UM/UIM benefits that it pays will be excess over any other available UM/UIM coverage when the claim does not involve a covered auto. *Id.* <u>Caution: This is a trap for the unweary!</u> Essentially, this provision requires that the Progressive insured exhausts all available UM/UIM coverages through other auto insurers. If the practitioner does not exhaust the coverages available through other insurers, then the practitioner should expect that Progressive will take the position that it does not have to pay anything for UM/UIM benefits

What if the UM/UIM portions of both insurers responsible for the claim <u>both</u> had excess language like Progressive's? This is a potentially troubling problem that does not appear to have been addressed specifically by Michigan appellate courts following the repeal of the mandatory uninsured motorist statute.

Adjusters and lawyers sometimes reference the unwritten "*follow the vehicle*" rule. This rule generally stands for the principle that the UM/UIM policy covering the vehicle involved in the accident should be primary over any other policies. This author, however, has been unable to find any recent published or unpublished case expressly recognizing the "*follow the vehicle*" rule.

There is, however, one Michigan Court of Appeals case that dealt with this issue while Michigan still had a mandatory uninsured motorist statute. That case is *Werner v Travelers Indemnity Company*, 55 Mich. App. 390 (1974). There are a couple of caveats regarding the *Werner* decision. First, and perhaps most significantly, *Werner* was written before the Michigan legislature repealed the mandatory uninsured motorist statute. Thus, a good argument can be made that it does not apply in the current statutory environment. Second, the language discussed below in the *Werner* decision is true dicta. In short, the *Werner* court did not have to address this issue specifically because of a procedural flaw in how the case reached the Court of Appeals. However, the *Werner* court went through a

lengthy discussion about how to analyze a situation involving claims for UM coverage through multiple insurers.

Werner involved a claim for UM benefits when the plaintiff was injured by an uninsured motorist while an occupant of a vehicle driven by her friend, Thomas Hendren. *Id.* at 392. Thomas Hendren had $10,000 in uninsured motorist coverage through his policy with American Fellowship Mutual Insurance Company. *Id.* The plaintiff (the occupant of Hendren's vehicle) also had $10,000 in uninsured motorist coverage through Travelers Indemnity Company. *Id.* The Travelers' policy included an "*excess insurance*" provision that, like the Progressive policy cited above, made coverage under that policy excess over any other similar available insurance. *Id.* at 393. The trial court determined that the first $10,000 of any award should be paid by the American Fellowship policy (the insurer of the vehicle involved in the accident) and that any additional award should be paid by Travelers. *Id.*

Defendant Travelers appealed and argued that the total damages should be apportioned equitably between the two insurers. *Id.* at 395. Although the Court of Appeals held that Travelers' argument was procedurally flawed, it went out of its way to note that it agreed with the trial court's analysis. *Id.* In other words, the Court of Appeals stated, in strong dicta, that it was proper to exhaust the UM coverages on the vehicle occupied before imposing liability on the UM insurer of the occupant whose vehicle was not involved in the collision. *Id.* at 395-96. The Court of Appeals stated:

> *"In such a situation, it is generally held that the policy issued to the owner of the vehicle (Hendren) involved in the particular accident at hand is the 'primary' policy, and the company which issued that policy (American Fellowship) is liable to the limits of the policy without apportionment, despite the presence of a 'pro rata' clause contained in that policy. . . . [I]n a situation such as the one at hand, where the plaintiff's damages do not exceed the total amount of the two policies, the excess insurance clause is given effect, and the policy which covers the owner of the vehicle involved in the accident was held to be primarily responsible, and its policy of limits had to be exhausted before the excess insurance of the policy covering the passenger 'comes into play'."*
>
> *Id.* at 396.

Thus, if two auto insurers invoke excess clauses in a claim for UM/UIM benefits, the practitioner should consider *Werner* to stand for the proposition that the insurer of the vehicle involved in the accident has primary responsibility to pay the UM benefits. Again, to preserve the UM/UIM claim with the insurer whose vehicle was not involved in the accident, the practitioner must exhaust the UM/UIM coverage through the insurer of the vehicle involved in the accident. Once again, caution must be exercised here in order to

make sure that the clauses are properly analyzed and the appropriate steps taken in negotiation and settlement.

D. SETOFFS AGAINST UM/UIM CLAIMS FOR PIP BENEFITS PAID

One of the most troubling efforts by auto insurers is an attempt to reduce any UM/UIM benefits by any PIP benefits that the same auto insurer paid in connection with the same accident. This is particularly troubling because it has the effect of rendering the UM/UIM coverage nonexistent. It is no secret that the most significant component of a claim is the injured person's PIP benefits, including their medical expenses and lost wages under MCL 500.3107. These claims typically (and very quickly) exceed the amount of UM/UIM coverage that the insured person separately purchased. Thus, if insurers are allowed to reduce the amount of PIP benefits paid to the insured from any UM/UIM claim, most UM/UIM claims will be reduced to zero.

Perhaps the most prolific insurer attempting to use PIP setoffs in UM/UIM claims is Farm Bureau Insurance. Again, attached as ***Exhibit 2*** is a copy of Farm Bureau's "*standard*" Michigan auto insurance policy. The setoff for PIP benefits paid against UM/UIM claims is included on page 17 of that policy. That provision states as follows:

> *"The amount payable for this Uninsured Motorist Coverage will be reduced by any amounts paid or payable for the same bodily injury: a. under Part I- Liability Coverage or Part II - Michigan No-Fault Coverages of this policy. . . "*

Farm Bureau's Policy, supra at 17.

The question then becomes whether or not a policy like the one used by Farm Bureau is permitted under Michigan law. It is this author's conclusion that the answer to this question is not entirely clear, but the weight of authority is against enforcement of this kind of provision.

It should be noted that, at one point in time, the Michigan Supreme Court made it abundantly clear that an insurer was not permitted to reduce UM/UIM coverage by PIP benefits paid. This was the clear holding in *Bradley v Mid-Century Insurance Company,* 409 Mich. 1 (1979). In this case, the court held that an insurer was not permitted to reduce UM/UIM coverage by PIP benefits paid because the insured purchased two separate coverages (i.e., PIP and UM/UIM). Permitting this setoff would eliminate one of those coverages and defeat the reasonable expectations of the insured. *Id.* at 23. The Michigan Supreme Court stated:

"The insured paid premiums in exchange for coverage above and beyond that afforded under the no-fault act; the premium was not paid with the expectation that coverage would be afforded only in cases where no-fault benefits are paid in amounts substantially less than the limits of uninsured motorist coverage but non-economic loss is so severe as to entitle the insured to collect from the uninsured tortfeasor. A contrary holding would tend to make the coverage illusory and defeat the reasonable expectations of insureds and the policy of the no-fault act to distinguish between economic and non-economic loss."

Id.

Until 2003, the rule that an insurance company could not reduce UM/UIM benefits by PIP benefits otherwise paid was clear. However, in 2003, the Michigan Supreme Court rendered its decision in *Wilkie v Auto-Owners Insurance Company*, 469 Mich. 41 (2003). It should be noted that *Wilkie* did not involve the issue of setoffs against UM/UIM claims for PIP benefits paid. Yet *Wilkie* was significant because it disavowed the "*reasonable expectations*" doctrine that was cited in *Bradley*. *Id.* at 62. The Michigan Supreme Court held:

"In sum, the rule of reasonable expectations clearly has no application when interpreting an unambiguous contract because a policyholder cannot be said to have reasonably expected something different from the clear language of the contract. Further, it is already well established that ambiguous language should be construed against the drafter, i.e., the insurer. Therefore, stating that ambiguous language should be interpreted in favor of the policyholder's reasonable expectations adds nothing to the way in which Michigan courts construe contracts, and thus the rule of reasonable expectations should be abolished. . . . Accordingly, we hold that the rule of reasonable expectations has no application in Michigan, and those cases that recognized this doctrine are to that extent overruled."

Id.

Obviously, *Wilkie* is problematic for the ongoing viability of the holding in *Bradley*. Certainly, insurers will claim that *Bradley* was overruled by the reasoning in *Wilkie* because *Bradley* was analyzed under the reasonable expectation doctrine. However, it is not entirely fair to characterize the *Bradley* holding as resting on only the reasonable expectation doctrine. The *Bradley* court reached its holding also because a contrary holding would have rendered UM/UIM coverage illusory. *Bradley*, 409 Mich. at 65-66. As such, attorneys representing auto accident victims should not concede defeat on the viability of *Bradley*.

Apart from *Bradley*, however, attorneys representing auto accident victims also have a strong statutory argument that prohibit an insurer from subtracting PIP benefits paid from UM/UIM claims. This statutory arguments is found in Section 3116 of the Michigan No-Fault Act.

Section 3116(2) sets forth the three limited circumstances under which a no-fault insurer is entitled to assert a lien against a tort claim. Under this subsection, a no-fault insurer is only permitted to assert a lien against a tort claim in out-of-state accidents, intentional torts, or claims directly against uninsured drivers.

When an insurer attempts to reduce its liability for UM/UIM motorist benefits by offsetting what it paid in PIP benefits, it is, in essence, asserting a lien or other reimbursement type claim against a "*claim in tort*," even though UIM is a contractual benefit. Therefore, an argument should be made that Section 3116 sets forth the exclusive, preemptive rules regarding any situation when a PIP insurer is seeking to reimburse itself out of a tort-based recovery for PIP benefits it previously paid. Section 3116 only permits a PIP insurer to assert such a claim in the three limited factual scenarios spelled out in Section 3116(2). None of these involve the garden variety tort/UIM claim for Michigan-based accidents.

Moreover, the Michigan appellate courts have extended the "*Section 3116 model*" to other types of tort-based reimbursement claims asserted by insurers who did not pay no-fault PIP benefits, i.e., workers' compensation benefits *(see, Great American v Queen*, 410 Mich. 73 (1980)) and health insurance benefits (*Great Lakes American Life Ins. v Citizens Ins. Co.*, 191 Mich. App. 589 (1991)). All of these insurers were denied any access to tort compensation for economic benefits that were paid in lieu of no-fault PIP benefits. Therefore, Section 3116 and these appellate cases prohibit a PIP insurer from benefitting in any way from a tort settlement, except as permitted by Section 3116(2) and applicable case law.