1998

Underinsured Motorist Coverage in Minnesota: Old Precedents in a New Era

Theodore J. Smetak

Follow this and additional works at: http://open.mitchellhamline.edu/wmlr

Recommended Citation
Available at: http://open.mitchellhamline.edu/wmlr/vol24/iss4/14

This Article is brought to you for free and open access by the Law Reviews and Journals at Mitchell Hamline Open Access. It has been accepted for inclusion in William Mitchell Law Review by an authorized administrator of Mitchell Hamline Open Access. For more information, please contact sean.felhofer@mitchellhamline.edu.

© Mitchell Hamline School of Law
UNDERINSURED MOTORIST COVERAGE IN MINNESOTA: OLD PRECEDENTS IN A NEW ERA

Theodore J. Smetak†

I. INTRODUCTION ........................................................................858
II. EVOLUTION OF THE USE OF UNINSURED AND
UNDERINSURED MOTORIST COVERAGES IN MINNESOTA'S
AUTOMOBILE INSURANCE SYSTEM .........................................860
   A. Overview of Uninsured Motorist (UM) Coverage: A Substitu-
tute for Tortfeasor's Liability Insurance ....................................862
   B. Overview of UIM Coverage: A First Party Supplement to
Tortfeasor's Inadequate Liability Limits .....................................863
   C. Variations in Underinsured Motorist Systems Generally .........865
   D. Four Eras in the Evolution of UIM in Minnesota .................867
      1. "Difference of Limits" UIM 1972 to 1975 ........................867
      2. Add On or "Damages Less Limits" UIM 1975 to 1985 ...868
      3. "Limits Less Paid" UIM—The Broton Era: October 1,
         1985 to August 1, 1989 ..............................................870
      4. Minnesota's Present "Damages less Paid," a Modified
         Add On UIM Law: Accidents after August 1, 1989 ....872
   E. Comparison of Minnesota's "Old" and "New" UIM Sys-
tems: Of Gap Shifting and Changing Dynamics .....................873
III. IS THE AT-FAULT VEHICLE UNDERINSURED? ISSUES
INVOLVING THE COMPARISON OF ACTUAL DAMAGES WITH
LIABILITY LIMITS .......................................................................877
   A. What Are "Actual Damages?" ............................................878
   B. To What "Limit" Are the Actual Damages Compared to
Determine Whether a Motorist is Underinsured? .................879
      1. Multiple Claimants .....................................................880
      2. Vicariously Liable Parties ............................................881
      3. Multiple Tortfeasors ...................................................882
   C. When is the At-Fault Underinsured Vehicle Not "Underin-
sured?" ..............................................................................889

† Shareholder, Arthur, Chapman, Kettering, Smetak & Pikala, P.A., Min-
neapolis, Minnesota. J.D., cum laude, 1975, University of Minnesota.
I. INTRODUCTION

This article focuses on Minnesota's underinsured motorist insurance coverage as an element of Minnesota's current, comprehensive automobile insurance system. More than any other aspect of the modern Minnesota automobile insurance system, underinsured motorist coverage has undergone change. The changes have not been minor; indeed the fundamental philosophical premise of underinsured motorist itself has been radically altered over the years. It is unlikely that any other state has as varied a history to its underinsured motorist system as does Minnesota. This article also attempts to identify several areas of tension which currently exist within the underinsured motorist system. With the benefit of historical perspective, the article will describe the sources of that tension.

Determining the amount of underinsured motorist recoveries is a function of several elements. One significant element is the underinsured motorist system in place. Nationwide there are three distinct underinsured motorist programs, each of which is capable of yielding a different dollar figure for a given claim simply because of the system's rules. At various times, Minnesota has utilized each
of the three systems as its governing law. Currently, Minnesota has a fourth, even more liberal, system in place.

Changing systems produces different results, not only in terms of the dollar figure recoverable but even in terms of whether the coverage is available at all. The rules which determine whether, and in what amount, underinsured motorist coverage is available bring into play the statutes\(^1\) as well as policy language. Fundamental philosophical premises underlying access to the first party underinsured (and uninsured) motorist insurance have been changed. Case precedents which were reasonable and workable under previous insurance systems do not meaningfully apply to current cases involving underinsured motorist insurance.

Because underinsured motorist insurance is a first party coverage intended to supplement the inadequate motoring liability insurance of an at-fault tortfeasor, changes in the exposure of motoring tortfeasors (such as changes in joint and several liability rules) have an impact upon the underinsured motorist coverage.

In an earlier era, when Minnesota’s underinsured motorist law embodied a system different from the present one, the Minnesota Supreme Court carefully balanced the rights of the injured person, the underinsured motorist insurer and the motoring tortfeasor with the result that the *Schmidt v. Clothier*\(^2\) procedure was set. This procedure, named after the 1983 case, set certain mechanical rules to be followed. The *Schmidt v. Clothier* procedure, and the “right” of the underinsured motorist insurer to substitute its own funds to preserve a subrogation right, continues to play a major role in the underinsured motorist system. In one sense, a current hotbed of litigation involves whether the *Schmidt v. Clothier*\(^3\) procedures provide a meaningful subrogation opportunity for the underinsured motorist carrier at a time when the current underinsured motorist law is based upon a radically different type of underinsured compensation.

Minnesota is witnessing a new wave of litigation over underinsured motorist entitlement; much of that litigation involves the struggle to apply, in a meaningful manner, precedents from an earlier underinsured motorist era. This paper explores some of the issues and their origins in order to shed light on how the underin-

\(^1\) Since 1985, Minnesota has had a statutory “source” system for underinsured motorist claims. *See* Minn. Stat. § 65B.49, subd. 3a (1996).

\(^2\) 338 N.W.2d 256, 260-61 (Minn. 1983).

\(^3\) *See id.*
II. EVOLUTION OF THE USE OF UNINSURED AND UNDERINSURED MOTORIST COVERAGES IN MINNESOTA'S AUTOMOBILE INSURANCE SYSTEM

Although Minnesota has for some years now required both uninsured motorist (UM) and under-insured motorist (UIM) coverages to be part of automobile insurance policies for Minnesota residents, that has not always been the case. Since the inception of Minnesota's No-Fault Act in January 1975, Minnesota has been a "compulsory insurance" state, requiring everyone who must register a motor vehicle to secure certain types and amounts of insurance. Before that time, Minnesota moved from a "financial responsibility" system to become a "compulsory insurance" system.

Minnesota Statutes, section 65B.48 obligates vehicle owners to obtain insurance (or to qualify as a self-insurer), while section 65B.49 specifies just what types and amounts of insurance coverages must be included in any such plan. During its evolution and before the UM and UIM coverage became mandatory for residents, Minnesota law imposed varying obligations upon insurers to acquaint consumers with optional coverages. The state thereby specified, to one degree or another, the scope of available coverage. At different times, the insurance industry had to "make available" or later "offer" certain optional coverages. Those were but steps in the process of a slow movement toward mandatory inclusion of the UM and UIM coverages for residents.

5. These sections are known as the Minnesota No-Fault Automobile Insurance Act. See Schmidt, 338 N.W.2d at 260. It is a curious bit of word play that in a financial responsibility system only motorists who have demonstrated that they are irresponsible (meaning they have not been able to satisfy a motoring judgment against them) are required to insure against future tort obligations. Those who have not failed to respond to tort claims against them are, in such a system, presumed responsible and may drive without insurance.
6. See Minn. Stat. § 65B.48 (1996). "Every owner of a motor vehicle of a type which is required to be registered or licensed or is principally garaged in this state shall maintain during the period in which operation or use is contemplated . . . ." Id.
8. A non-resident owner of a motor vehicle is not required to maintain UM and UIM coverages on the policy insuring the vehicle. See id. § 65B.48 (1). The non-resident's policy need only afford the required levels of basic economic loss coverage and bodily injury and property damage coverages while the vehicle is in the state. An out-of-state policy will not be "written-up" to provide Minnesota UM
UM coverage has been a mandatory coverage since 1967 and was incorporated into the No-Fault Act when the Act became effective January 1, 1975. UIM coverage was introduced in the state in 1972 as an optional coverage that was required to be made available to policyholders. It was incorporated into the No-Fault Act in 1975 as an optional coverage that was required to be offered. The coverage became mandatory in all policies issued or renewed after October 1, 1985. All motor vehicles of a type required to be registered or principally garaged in the state are required to be insured under a plan of reparation security affording UM and UIM coverages during the period when use is contemplated. Although the No-Fault Act requires bodily injury (BI) liability limits of $30,000 per person/$60,000 per accident, the statutory limits for UM and UIM coverages are only $25,000 per person/$50,000 per accident. There is no statutory requirement that an insurer offer increased limits to policyholders.

All motorists subject to the state’s control must carry minimum limits liability (BI) coverage and they must have No-Fault or personal injury protection (PIP) coverage. The reasoning is that near universal “no-fault” benefits protection is necessary to implement Minnesota’s No-Fault system. The nearly universal availability of PIP benefits played a role in reducing access to the court system. Also, minimum liability limits play a role in ensuring adequate compensation. By contrast, the state seemingly has less of an interest in ensuring that non-residents, injured while traveling through Minnesota, have UM or UIM coverage.

or UIM coverage under the No-Fault Act’s statutory conformity provision. See id. § 65B.50. Out-of-state insurers licensed to do business in the state are only required to provide the minimum basic economic loss and liability coverages required by the Minnesota No-Fault Act while the vehicle is in the state. See Aguilar v. Texas Farmers Ins. Co., 504 N.W.2d 791, 794 (Minn. Ct. App. 1993) (finding that non-resident owners need only carry basic economic loss and residual liability coverages); Hedin v. State Farm Mut. Auto. Ins. Co., 351 N.W.2d 407, 409 (Minn. Ct. App. 1984) (stating that insurance companies licensed to transact business in Minnesota are not required to “write up” nonresident policies to the Minnesota statutory minimum); Cantu v. Atlanta Cas. Co., 535 N.W.2d 291, 292 (Minn. 1995), reh’g denied, (Minn. Sept. 11, 1995).

11. See id. § 65B.49(3)(1).
12. See id. § 65B.49, subd. 3a(1).
13. See id. subd. 3a(3).
A. Overview of Uninsured Motorist (UM) Coverage: A Substitute for Tortfeasor's Liability Insurance

In financial responsibility systems (where only irresponsible motorists are required to purchase liability insurance) many motorists are actually unable to pay the tort judgments resulting from their ownership or use of motor vehicles.\textsuperscript{14} Even under compulsory liability insurance systems (where every motorist/owner is required to insure against tort liability) there are always some vehicles operating without insurance.\textsuperscript{15} Uninsured motorist coverage is intended to provide, for the benefit of those who purchase it, a first party to substitute for the liability insurance an at-fault motorist should have had.\textsuperscript{16} Basically, a UM carrier's obligation "is to pay, subject to its policy limits, benefits [the insured] would otherwise have collected in tort damages from the uninsured motorist."\textsuperscript{17} UM coverage is "in effect a substitute for insurance that the tortfeasor should have had."\textsuperscript{18}

Minnesota's UM history is not complicated. UM coverage became a mandatory coverage in Minnesota in 1967.\textsuperscript{19} The statute initially provided that the policyholder could reject the coverage, but that provision was eliminated in 1969.\textsuperscript{20} After adoption of the No-Fault Act in 1975, UM coverage continued to be a mandatory

\textsuperscript{14} Interestingly, UM coverage was conceived by the insurance industry in the 1950s in response to pressure to adopt compulsory liability insurance. The industry sought to avoid having to insure all motorists at a time when, in most states, liability insurance was not mandatory. UM coverage has come to play a role in virtually all of the states whose systems mandate liability insurance. One way or another, then, the industry ended up "insuring" against the tort liabilities of all motorists in systems such as Minnesota's.

\textsuperscript{15} With no pretext at scientific surveying, twenty-plus years of practice convinces this writer that uninsured motorists are disproportionately involved in motoring accidents.

\textsuperscript{16} \textit{See} McIntosh v. State Farm Mut. Auto. Ins. Co., 488 N.W.2d 476, 478-79 (Minn. 1992) (citing 8C APPLEMAN, INSURANCE LAW & PRACTICE § 5067.45, at 49-50 (1981)). Uninsured motorist coverage "more closely resembles . . . a substitute liability policy which stands as proxy for that which the uninsured motorist chose not to carry." \textit{Id.}

\textsuperscript{17} State Farm Mut. Auto. Ins. Co. v. Galloway, 373 N.W.2d 301, 305 (Minn. 1985). \textit{See also} Brunmeier v. Farmers Ins. Exch., 296 Minn. 328, 331-32, 208 N.W.2d 860, 862 (1973) (finding that the legislature intended "to confer on automobile liability policyholders benefits against uninsured motorists in no less amount than such policyholders would have realized against insured motorists").

\textsuperscript{18} Van Tassel v. Horace Mann Ins. Co., 296 Minn. 181, 189, 207 N.W.2d 348, 353 (1973). \textit{See also} McIntosh, 488 N.W.2d at 478.

\textsuperscript{19} \textit{See} 1967 Minn. Laws ch. 837.

\textsuperscript{20} \textit{See} 1969 Minn. Laws ch. 630.
coverage. In addition, insurers were required to offer optional UM coverage to their policyholders so that the UM limits would equal the liability limits selected by the insured. 21 Numerous "failure to offer" claims arose. The mandatory offer statute was repealed on April 12, 1980. 22

B. Overview of UIM Coverage: A First Party Supplement to Tortfeasor's Inadequate Liability Limits

UIM coverage has its genesis in the inadequacies of uninsured motorist legislation. It was conceived in the 1960s and was designed to provide protection for the risk that the damages sustained by the insured would not be adequately indemnified by the liability coverage of the negligent insured motorist. If the offending motorist had at least the minimum liability insurance limits required by Minnesota but, if that BI limit was not sufficient to fully pay the damages caused by that motorist, the motorist was underinsured. Underinsured motorist (UIM) is a first party coverage intended to supplement such inadequate BI coverage. Although Minnesota's mandatory liability insurance limits are the highest of any of the states, the damages sustained by the motoring public can often exceed the limits of a minimally-insured ($30,000 per person/$60,000 per accident) tortfeasor. In other states with lower liability limits, it is even more likely that the damages will exceed the available liability limits.

Some states chose to deal with the inadequately (but legally) insured tortfeasor by modifying the state's uninsured motorist system. By changing the definition of "uninsured motorist" to encompass underinsured situations, some states have a single coverage. Minnesota has not used that method; 23 uninsured motorist and underinsured motorist coverages apply to separate risks in Minnesota.

Whether the motorist is underinsured is pivotal in determining whether an injured person may access the state's UIM system. Any statutory determination of when UIM coverage is applicable, when the motorist is "underinsured," is generally predicated upon

23. From 1985 to 1989, Minnesota combined the UM and UIM into a single coverage limit. Basically, the two separate risks were covered jointly, subject to one overall policy limit. Minnesota has never defined an uninsured motorist to include an underinsured motorist.
some type of comparison of the injured party's damages with the
tortfeasor's bodily injury (BI) liability insurance. A motorist is un-
derinsured when he is insured but the amount of liability insurance
is not enough to compensate the injured person for the damages
sustained in the motoring accident.

Two principles remain constant and need to be understood
when considering whether a UIM claim exists:

1. The insured can never recover UIM benefits unless he or
   she can establish that the tortfeasor is underinsured (i.e.,
   the damages the tortfeasor is legally obligated to pay ex-
   ceed the tortfeasor's BI limits); and

2. The fundamental character of UIM coverage, as an excess
   coverage to liability insurance, has not been changed.

Regardless of the date of loss, UIM coverage is not to be
 treated as an alternative to liability coverage. It is an ex-
 cess coverage.

Those two principles are basic and elemental under Minne-
sota's UIM system and under UIM concepts generally. These
principles go to the heart of the term underinsured. But, once any sys-
 tem is accessed (once there is an "underinsured motorist"),
different UIM systems provide differing levels of compensation. In

24. See, e.g., Richards v. Milwaukee Ins. Co., 518 N.W.2d 26, 28 (Minn. 1994),
reh'g denied, (Minn. Aug. 18, 1994) (finding that "actual damages" relative to an
underinsured motor vehicle is the total tortfeasor liability exclusive of the no-fault
coverage); Royal-Milbank Ins. Co. v. Busse, 474 N.W.2d 441, 443 (Minn. Ct. App.
1991) (holding that UIM benefits will only be paid when the "applicable bodily
injury liability policy is less than the amount needed to compensate the injured
party"); Brosdahl v. Minnesota Mut. Fire & Cas. Co., 437 N.W.2d 695, 697 (Minn.
Ct. App. 1989) (stating that UIM benefits may be claimed before pursuing a claim
against the tortfeasors).

25. See, e.g., Thommen v. Ill. Farmers Ins. Co., 437 N.W.2d 561, 654 (Minn.
1989) (holding that UIM coverage provides any excess insurance protection to
which the insured is entitled); Onasch v. Auto-Owners Ins. Co., 444 N.W.2d 587,
590 (Minn. Ct. App.), rev. denied, (Minn. 1989) (stressing that UIM should only be
sought after settlement negotiations have taken place with the tortfeasor's ins-
urer); Johnson v. American Family Mut. Ins. Co., 426 N.W.2d 419, 422 (Minn.
1988) (finding that UIM coverage is excess coverage, not optional protection).

26. See Onasch, 444 N.W.2d at 590.

27. A large factor contributing to the current tension in Minnesota's still-
evolving UIM system can be traced to these factors. As explored in more detail
when discussing the "shifting of gap responsibility," there is a concern that Minne-
sota's current UIM system allows or compels the underinsured motorist insurance
to be used as if it were the underlying liability insurance. UIM theory would gen-
berally provide that UIM coverage is a supplement, not a substitute, for inadequate
liability limits.
part, the difference between the systems reflect differing public policies. Just as states differ in terms of whether the coverage should simply be “made available,” be “offered,” or become a mandatory coverage, so too do the various systems yield different underinsured motorist recoveries.

C. Variations in Underinsured Motorist Systems Generally

Nationwide there are three main variants, each its own “underinsured motorist system.” They may be roughly characterized as follows:

1. The Pure “Limits Less Limits” or “Difference of the Limits” Coverage Form. Under this kind of system, the UIM carrier’s liability is measured by the lesser of: (a) the difference between the UIM limits and BI limits or (b) the amount of uncompensated damages which exceed the BI limits. Recovery under this system is possible only if the UIM limits exceed the tortfeasor’s BI limits. Another way of looking at such a system is that its goal is to allow the injured purchaser of UIM coverage to supplement the tortfeasor’s liability insurance up to the level of compensation chosen when the UIM limit was selected. The choices made by the purchaser of UIM coverage, under this system, play a large role in fixing the amount of UIM recovery. Under this system, if the injured UIM insured chooses to settle for less than the motorist’s full liability limit, the consequences are borne by the claimant.

2. The Pure “Limits Less Paid” Coverage Form. The UIM carrier’s liability is measured by the lesser of: (a) the difference between the UIM limits and the amounts paid by the tortfeasor or (b) the uncompensated damages. This system is somewhat like the “limits less limits” variety in that the goal is to provide supplementation, if necessary, up to the injured person’s pre-selected UIM limit. In such a system, the UIM coverage supplements from the dollar figure paid by the tortfeasor. (Note that even in this system, the offending motorist must be underinsured in the sense that the damages must exceed the tortfeasor’s liability insurance coverage. If the motorist has adequate insurance to pay the full damages, the motorist is not underinsured and the UIM coverage is not available.)

3. The Pure “Add-On” or “Damages Less Limits” Coverage Form.
The UIM carrier’s liability is measured by the lesser of: (a) the UIM limits or (b) the damages less the tortfeasor’s BI limits. The UIM coverage is available, under such a system, on top of the tortfeasor’s liability limits. This system contemplates that the offending motorist’s full liability limits will be credited against the insured’s damages. However, if the tortfeasor’s limits do not fully compensate the injured person, that person’s entire UIM limit is available as an excess reservoir of coverage. When selecting a UIM coverage limit in such a system, the consumer is basically buying a floating first party coverage, available on top of the tortfeasor’s limit.

Minnesota’s UIM system has undergone more change than that in any other jurisdiction. Its history is complex. Virtually every aspect of a UIM claim depends upon the controlling law at the time of the accident. During its UIM history, Minnesota has adopted and used each and every one of the three basic UIM systems described above. To make matters even more complicated, in 1989 Minnesota adopted a hybrid fourth approach, one by which the entire UIM limit floats and supplements, if the motorist is underinsured, the amount paid by the tortfeasor. That is a “modified add on” or “damages less paid” system. What should the injured person with a qualifying injury claim caused by an “underinsured motorist” recover? That seemingly simple question is like asking “how large is a horse?” It depends upon whether the “horse” is a Clydesdale, a quarter horse or a Shetland Pony. Each may be considered a horse and yet there are major differences. Similarly, underinsured motorist coverage is very different depending upon which UIM system is in place. And, in a rare state such as Minnesota, where each system has been in place at one time, the answer depends upon when the accident happened. Each system has its own expectations and processes; it creates its own dynamics. This article explores some of the rules which have evolved and raises questions regarding whether processes and procedures logical and workable under one system have a meaningful place in any of the other systems.

An example will help illustrate the differences between the three coverage forms (and Minnesota’s current “fourth” form). Assume the following facts:

- The insured sustains damages of $40,000 in a motoring accident caused by a single, insured motorist.
- The tortfeasor’s BI liability limits are $30,000.
• The UIM limits are $30,000.
• The insured settles with the tortfeasor for $25,000 and therefore has uncompensated damages of $15,000.

Depending upon which UIM system is in place, that one single fact pattern produces a UIM recovery of zero, $5,000, $10,000 or $15,000. Using the “difference of limits” system, $30,000 less $30,000 is zero. Using “damages less BI limits,” $40,000 less $30,000 is $10,000. Using “UIM limit less paid,” $30,000 less $25,000 is $5,000. If “damages less paid” system is used $40,000 less $25,000 is $15,000. Although the difference (zero to $15,000) might seem slight, that is the range based upon a fairly small bodily injury claim with small insurance limits. The difference between the systems is staggering as the dollar sums and policy limits increase.

D. Four Eras in the Evolution of UIM in Minnesota

What follows is a more detailed historical review of the various UIM systems which Minnesota has had in place over time.

1. “Difference of Limits” UIM 1972 to 1975

From January 1, 1972, to January 1, 1975, when the No-Fault Act was adopted, UIM coverage was a supplemental coverage that insurers were required to “make available” to policyholders. Under the statute, UIM coverage was premised on a pure “limits less limits” system. If the UIM limits did not exceed the BI limits, no UIM recovery could be made, regardless of the amount of damages sustained.

In addition, the injured person was entitled to add together the UIM limits under any insurance policy which identified the injured person as an insured. “Stacking” of UIM (as well as UM) coverages was permitted, despite policy language purporting to prohibit stacking. This is a significant factor affecting access. The

28. See Jacobson v. Illinois Farmers Ins. Co., 264 N.W.2d 804, 807 (Minn. 1978) (stating that policyholder must “opt in” to coverage made available, otherwise, he or she will not receive it).
30. See Holman v. All Nation Ins. Co., 288 N.W.2d 244, 251 (Minn. 1980) (finding that separately listed policy coverages may be stacked).
31. See id.
premise upon which such "first party" coverages were made available emphasized that the coverage primarily insured the person as opposed to the vehicle. Although the coverage was written on different vehicles, the coverage was viewed as available equally under many policies at one time.

Under this "difference of limits" system, the UIM carrier was allowed to deduct the tortfeasor's BI limits from the UIM limits. The UIM limit chosen by the consumer acted as a benchmark. If the motorist was validly insured but his/her liability limits were less than that figure selected by the insured, the injured insured could supplement the tortfeasor's liability limits in order to bring the total recovery up to the selected level of compensation.

Consider the motivation of an injured person under such a system. Irrespective of whether the injured person collected one hundred percent of the tortfeasor's BI liability limits, the UIM claim began where the BI limit left off. The injured person had no incentive to settle for less than the BI limits. (That is a dynamic which plays a major role in the current state of Minnesota UIM law.) Although the appellate courts were not faced with "below limits" settlement cases, it was clear that the claimant would "eat the gap" resulting from such a settlement. This "difference of limits" law mandated a set-off equal to the full BI limits without regard for the fact the insured may have settled for a lesser amount.32

2. Add On or "Damages Less Limits" UIM 1975 to 1985

Effective January 1, 1975, UIM coverage was changed from the "limits less limits" format to a pure "add-on" coverage form.33 No longer would the UIM recovery depend upon a difference between the limits of the two policies. The UIM coverage limit was available to "add on" to the BI limits if necessary to fully compensate the injured person who had the protection of UIM coverage. From 1975 to April 12, 1980, the so-called "mandatory offer era," UIM coverage was an optional coverage that was a part of a package that insurers were required to "offer" their policyholders.34 (Note that a mandatory offer may be viewed as one step beyond "make available." Such distinctions suggest the coverage is imbued with a

33. See Holman, 288 N.W.2d at 249.
34. See Act of April 11, 1974, ch. 408, § 9, 1974 Minn. Laws 762, 773, 774 (codified as MINN. STAT. § 65B.49(6)(e) (1974)).
Because of the shift from the "limits less limits" to an "add on" system, the courts of Minnesota began to see "below limits" settlements. In Schmidt v. Clothier, the court held exhaustion clauses void and allowed insureds to settle with the tortfeasor's insurer for an amount less than the liability limits. However, the insured had to "eat the gap" between the liability settlement amount and the liability limits. The UIM carrier was entitled to set off the full BI limits from the total damages.

Clearly, a disincentive was created by the application of the "damages less limits" system. For example, if the insured chose to settle at some figure less than the full BI limits, the insured absorbed the "gap" resulting from the below limits settlement when making a UIM claim. The UIM coverage started where the BI coverage limit left off, regardless of what figure the insured chose to accept in settlement.

The fact that the injured insured absorbed the "gap" resulting from "leaving BI money on the table" resulted in comparatively few settlements at substantially discounted figures. The gaps tended, historically, to be small during this period of Minnesota's UIM history. (Note that the seminal Schmidt v. Clothier doctrine was laid down during this era.)

There were fewer UIM "substitutions" during this era as well. For one thing, the settlements tended to be at or near the tortfeasor's BI limits. Also, the UIM insurer was given "credit" for the full BI limits despite a below-limits settlement with the tortfeasor. As a result, there was comparatively less incentive for UIM insurers to "substitute" so as to pursue subrogation recoveries.

During the mandatory offer period, the insurer had the burden of proving that it had made a commercially reasonable offer of UIM coverage. If it failed, UIM coverage would be written into the policy by operation of law. Numerous failure to offer claims arose. The problems resulting from the mandatory offer provision, including the burden of proof and standards to be applied in determining whether a valid offer had been made (and the fact that...
imposed coverages would be "stacked") inevitably led to repeal of the mandatory offer statute on April 12, 1980.  

From April 12, 1980 to October 1, 1985, there were no statutes which either defined or described the scope of UIM coverage in Minnesota. Many insurers did not offer the coverage. If UIM coverage did not appear on the declarations page of the policy and the insured could not establish that a premium was paid for UIM coverage, no claim could be made.  

For those insurers that continued to offer UIM coverage after repeal, the UIM system was considered to remain the same. Minnesota courts continued to apply the legal principles developed under the repealed statutes to UIM coverage after repeal. Thus, UIM coverage, to the extent it was contained in the policy, remained an "add on" type coverage and would be stacked. Policy terms were enforced only to the extent consistent with the principles developed under the repealed statute.  


In 1985, rising insurance costs, which had been traced in part to the prior law requiring expansive interpretation of automobile insurance coverages, resulted in major revisions to UM and UIM law. UIM coverage was elevated to a mandatory coverage. The most significant change was the legislature’s attempt to return the calculation of UIM benefits to a "limits less limits" basis from the "add on" coverage that had existed since 1975. The initial bill contained an exhaustion requirement which would have obligated the insured to exhaust the tortfeasor’s liability insurance (BI) coverage
before turning to the UIM coverage. The adoption of such a provision would have returned Minnesota to the “limits less limits” system used from 1972 to 1975.

However, through the amendment process, the exhaustion clause was deleted. What inevitably emerged was a “limits less paid” system. The UIM carrier’s liability was measured by the lesser of: (a) the difference between the UIM limits and the amounts paid by the tortfeasor or (b) the uncompensated damages. As a result, UIM benefits could not be collected if the injured person recovered an amount equal to or in excess of the BI limits from the tortfeasor.

In addition, the 1985 legislation had the following effects:
1. UM and UIM coverages became a combined single coverage;
2. UM/UIM coverages could no longer be stacked;
3. Primary responsibility for the “gap” (i.e., the difference between the BI limits and the liability settlement amount) was shifted from the insured to the UIM carrier;
4. A statutory priority or “Source” system for payment of UM and UIM claims was created, one which exists to this day, and
5. A geographical restriction which prevented an insured from recovering UM or UIM benefits while occupying an owned but uninsured vehicle was imposed.

Under the 1985 law, an insured was still allowed to settle with the tortfeasor for an amount less than the tortfeasor’s BI limits. There was, as noted, no exhaustion requirement. However, under the 1985 law, the primary responsibility for the “gap” was shifted to the UIM carrier. This was a reversal of the majority opinion in Schmidt v. Clothier, which had placed responsibility for the “gap” on the insured.

47. See Broton, 428 N.W.2d at 90; see also Kothrade v. American Family Mut. Ins. Co., 462 N.W.2d 413, 417 (Minn. Ct. App. 1990).
49. See Broton, 428 N.W.2d at 89-90.
50. 338 N.W.2d 256, 261 (Minn. 1983).

Less than four years after its last major revamping of UIM law, the legislature once again amended the statutes. The major features of the 1989 legislation included:

1. UIM coverage was converted into a modified "add-on" coverage form;
2. UM and UIM coverages were once again separate coverages with separate limits, and
3. In cases involving multiple defendants, a UIM claim may be made where any one of the motoring tortfeasors fit within the definition of an "underinsured motor vehicle."  

It is important to recognize that Minnesota's present UIM system, the result of the 1985 and 1989 changes, is not the same "add on" coverage which existed from 1975 to 1985. Under that system, the UIM carrier was only responsible for uncompensated damages which were in excess of the tortfeasor's BI limits. The UIM carrier was entitled to deduct the underlying BI limits from the damages, regardless of whether the full BI limits had been paid.  

Under the 1989 law, an insured was still allowed to settle with the tortfeasor for an amount less than the tortfeasor's BI limits. Whether a UIM claim could always be made and whether the UIM carrier would be responsible for the "gap" in all cases was an open issue under the 1989 law as well as under the 1985 law. The Nordstrom case suggests that the answers to these issues may depend on whether the insured made the "best possible settlement" with the tortfeasor's BI carrier. In any event, it is clear that a UIM carrier is not automatically entitled to deduct the underlying liability limits from the damages, as it was from 1975 to 1985. As the case law presently stands, the UIM carrier is only entitled to deduct the amounts paid to the insured by the tortfeasor.

In this sense, the present UIM system can most appropriately be described as a "damages less paid" system. The UIM carrier's

51. This was a legislative reversal of Johnson v. American Family Mut. Ins. Co., 426 N.W.2d 419, 422 (Minn. 1988).
52. See Schmidt v. Clothier, 338 N.W.2d 256, 261 (Minn. 1983).
potential liability is measured by the lesser of: (a) the UIM limits or (b) the total damages less the amounts paid by the tortfeasor.

E. Comparison of Minnesota’s “Old” and “New” UIM Systems: Of Gap Shifting and Changing Dynamics

As noted above, over time, four different UIM systems have passed across the landscape of Minnesota. But, like glaciers, not all have left the same impression. Two systems are much more important than the others. One is the “Add-on” (or “damages less limits”) system. The other is the current “Modified Add-on” system under which the damages are reduced not by the BI limit but by the amount “paid” to the injured motorist. Both UIM systems deal with an “underinsured motorist” situation where the at-fault motorist has inadequate liability insurance to pay the injured person for all of their recoverable damages. But the two systems are fundamentally different in terms of the UIM insurer’s exposure. Also, the dynamics within each system differ.

Current UIM law is the post-1989 “damages less paid” system. However, the case law rules which are being applied to determine the rights and responsibilities of the parties to the current UIM system were in significant part laid down during the earlier “damages less limits” era. One of the most important procedural “rules” was laid down during the earlier pure “add-on” system: the Schmidt v. Clothier rule. That is an important rule because at the time it was decided, Minnesota had no appellate law addressing the respective rights of the UIM claimant (to consider settlement of her tort claim in such a way as to avoid forfeiting UIM coverage) and the UIM insurer (to be able to pursue “subrogation” to recover any payments it made to the injured person from tortfeasors.) In deciding Schmidt v. Clothier, the Minnesota Supreme Court carefully considered the competing purposes of the parties affected by a UIM issue and weighed the workings and objectives of the then-current UIM system. The system has changed in a dramatic way since Schmidt v. Clothier. At the time, the injured party who decided to settle with a tortfeasor for less than the liability limits did so at his or her

---

55. 338 N.W.2d at 260-61. The Schmidt court held “that the underinsurer is liable only for the amount of damages suffered by the insured in excess of the liability limits of the defendant.” The underinsurance claim was thus not dependent on the conditions of any eventual settlement. Id. at 261.

56. Id.

57. See supra notes 51-55 and accompanying text.
The "gap" between the full BI limits and the settlement was absorbed by the claimant,\textsuperscript{59} and the UIM insurer was given credit for the full BI limits.\textsuperscript{60}

As a result, the court found it significant that an injured motor vehicle victim would have incentive to obtain substantially all of the BI limits. After all, any cost of accepting less was borne by the injured party; the UIM insurer could not complain. The UIM insurer received full credit for the amount of the limits, paid or not. Thus, the UIM insurer's objection to below-limits settlements was not given much weight at the time of \textit{Schmidt v. Clothier}.\textsuperscript{61}

Today, Minnesota's UIM system is radically different. Under current law the "gap" may be and often is shifted from the claimant, who decides on the settlement amount, to the UIM insurer. This "shifting of responsibility for the gap" plays a dramatic role and is a major source of the tension within Minnesota's UIM system. The next section discusses the impact of the shift by comparing Minnesota's "old" UIM law\textsuperscript{62} with the "new" UIM law.\textsuperscript{63} Significantly, those rules and procedures for handling UIM claims and underlying tort claims were laid down during the \textit{Schmidt v. Clothier} era.\textsuperscript{64} Although these rules still exist today, problems arise when the rules are applied in today's system.\textsuperscript{65}

One single factor, shifting the responsibility for the gap, has played a major role in creating the turmoil which currently exists in Minnesota. This era of Minnesota's UIM history has seen an explosion of "below limits" BI settlements because an insured could proceed with a UIM claim despite agreeing to a settlement. One of the most striking differences between the two laws is the potential impact of the "gap." Where the insured "eats the gap," few cases are

\begin{itemize}
\item \textsuperscript{58} See Schmidt, 338 N.W.2d at 261.
\item \textsuperscript{59} See id.
\item \textsuperscript{60} See id.
\item \textsuperscript{61} Id.
\item \textsuperscript{62} "Old" UIM law here refers to that in effect at the time of \textit{Schmidt v. Clothier}, 1983. At that time, Minnesota had a pure add on UIM system.
\item \textsuperscript{63} "New" here refers to the modified add on system in effect since 1989.
\item \textsuperscript{64} 338 N.W.2d at 260-61.
\item \textsuperscript{65} The term "problems" is not intended to pass value judgment upon one system or another. The "problems" which appear today involve more UIM litigation, more objections to UIM claims, more denials of entitlement to UIM coverage and the related confusion as to how the UIM insurer may or may not pursue recovery. All of those "problems" are relatively unique to the current UIM system, having been largely worked out satisfactorily during the \textit{Schmidt v. Clothier} era. The imbalance between the workings of the two systems plays a role in virtually all of the listed dispute areas.
\end{itemize}
settled with substantial discounts. However, if the UIM insurer must “pay the gap,” then the insured loses incentive to pursue the tortfeasor’s BI insurer for the full BI limits. As the gaps grow, the UIM insurer resists paying for damages which “should have been paid by the BI insurer.” Each system, then, has its own dynamics.

The “old” role of UIM provided a reservoir of coverage available to the extent that the tortfeasor’s BI limits were inadequate. Rather than exhausting the BI coverage and then pursuing recovery from the tortfeasor’s assets, the injured person could resort to the UIM coverage. The UIM coverage did not come into play except to the extent that the damages exceeded the BI limit. At what figure the claimant chose to settle was comparatively unimportant at that time; choosing to settle at a discount did not penalize the underinsured motorist insurer.

Under the “old” UIM law, if the injured person chose to settle below the BI limits, the “gap” was absorbed by the claimant; the UIM coverage applied at the same dollar level, equal to the tortfeasor’s BI limits.

Many UIM claims are contested today because if the motorist is truly underinsured (liability limits are inadequate to fully compensate the injured motorist) the UIM insurer objects that it must “drop down” so as to pay for damages which are below the BI limit.

The seemingly simple shifting of responsibility for the “gap” has, more than anything else, caused the greatest amount of tension in Minnesota’s UIM system. To avoid paying for damages which should have been paid by the BI insurer, UIM insurers strive harder to avoid coverage obligations. In addition, under the current system, there may well be more “substitutions.” The UIM insurer often “substitutes” its own money equal to the tentative BI settlement in order to preserve rights to subrogation against the remaining, unpaid BI coverage limits. That practice has led to confusion as to the procedures to be followed after substitution. Does the substitution prevent a settlement so that the BI case should proceed? Can the UIM claim be processed immediately or must it

---

66. The obvious self-interest of the injured party to obtain maximum recovery for him/herself ensures that if settlement below limits would penalize the injured person, they would logically try to obtain as much as possible from the BI insurer.
67. 338 N.W.2d at 260-61.
68. To the contrary, if the injured party chose to settle for less than 100% of the liability limits, the UIM insurer could pursue subrogation (after making UIM payment) against the BI limits which were “left on the table” as a result of a below-limits settlement.

Published by Mitchell Hamline Open Access, 1998
await some further resolution of the underlying tort claim? Is the subrogation handled in the name of the UIM insurer as subrogee or in the name of the original injured party? What if the ultimate assessment of liability and damages differs from that assumed when the tentative settlement was reached? Fortunately, courts have answered some of the above questions. The remainder of this paper addresses certain of the unanswered and evolving issues.

Other factors have caused tension in Minnesota's UIM system as well as the "gap" issues discussed above. Access to UIM coversages has been fundamentally changed over the years. UIM coverage no longer primarily follows the person. Instead, after 1985, UIM coverage is more closely linked to the vehicle. That, in turn, not only determines what UIM coverage is or is not available but validates policy exclusions which were invalid under earlier UIM systems.

In addition, the underlying tort liability climate has changed. Most importantly, joint and several tort liability rules have changed. Because the motorist's tort liability is the cornerstone for determining the UIM insurer's obligation, changes in the tort system impact the UIM system. The topics examined include the following:

- Is the At-Fault Vehicle "Underinsured?" The defining characteristic of an "underinsured motorist" is that the actual damages, recoverable by the injured person, exceed the liability limits. How is that comparison made when there are multiple claimants, each of whom has a conflicting claim against the liability limits? What if there are multiple tortfeasors, each of whom has a separate tort liability insurance policy amount? Even more fundamentally, what if the at-fault vehicle is one which is owned by the injured party? By that person's family members? (This involves the role of

69. The interesting role of tort caps is beyond the scope of this paper. But see Ronning v. Citizens Sec. Mut. Ins. Co., 557 N.W.2d 363, 365 (Minn. Ct. App. 1996) (finding that the government vehicle exclusion to a UIM policy was void as against public policy). Limiting municipal tort liability to $200,000 did not preclude an insured, whose damages exceeded that amount, from recovering underinsured motorist (UIM) benefits in connection with an accident involving a government-owned vehicle. See id. at 366; see also MINN. STAT. § 466.04 (1994). In 1997, the statutory limit for municipal tort liability was increased to $300,000. See MINN. STAT. § 466.04(1)(a)(1) (Supp. 1997). Minnesota will likely soon have to address whether the tort liability cap of an owner of a rental vehicle will limit the UIM claim. See MINN. STAT. § 65B.49(5a)(i)(2) (1996).
exclusions to the UIM coverage: whether the exclusions are valid or void. That brings into play the conceptual basis of the "risk" which has been insured: is the offending vehicle one which, for various reasons, should not be considered underinsured so as to allow the injured party to recover UIM benefits?)

- The State's Source system. In 1985, a fundamental shift took place. Not only did the legislature eliminate "stacking" of UM and UIM coverages, the legislature altered the connection between the individual and the policy in other ways. Those changes dictate different UIM results and render certain case law doubtful when applied to the "new" UIM system.

- The relationship between the tort system and the UIM system. This relationship is examined briefly, with emphasis upon certain key areas where there is currently tension in the system. Great progress has been made in understanding the procedural requirements before a UIM claim may be made. It is now clear that the underlying BI claim must proceed to tort judgment or to the "tentative settlement" stage before a UIM claim may be presented. But, beyond that, what about developments in the Alternative Dispute Resolution (ADR) arena? Are the methods which are increasingly being used to resolve the underlying BI claim consistent with the fact that there is another party, the UIM insurer, who has rights flowing from the tort claim? Finally, this section examines a seemingly simple concept: how does one calculate the damages which an insured is "legally entitled to recover" from a tortfeasor? Does that figure differ when a UIM claim is made? Has a new wrinkle been introduced: the abolition of "joint and several liability" when a UIM claim is made?

III. IS THE AT-FAULT VEHICLE UNDERINSURED? ISSUES INVOLVING THE COMPARISON OF ACTUAL DAMAGES WITH LIABILITY LIMITS

It is axiomatic that before a UIM claim may be asserted, the motor vehicle or motorcycle which caused the injuries must be underinsured as defined in the system. As the Minnesota Supreme Court has observed: "That the motor vehicle which causes the injury falls within [this] definition is, of course, necessary to invoke
Despite the change from an "add-on" coverage to a "limits less paid" coverage in 1985 and the subsequent change back to a "modified add-on" form of coverage in 1989, the definition of an "underinsured motor vehicle" has always mandated a comparison of the insured's damages and the tortfeasor's liability limits since the Act was introduced in 1975. If the insured cannot establish that the negligent motorist was "underinsured," no recovery of UIM benefits can be made regardless of which UIM system happens to be in place.

This simple precondition to recovering UIM benefits, whether the motorist is underinsured, starts with a comparison of the tort damages which the injured person is legally entitled to recover with the tortfeasor's limit of insurance. In the simple case with one injured person and one at-fault motorist, the answer is easily determined. But what if there is more than one BI limit applicable to pay the tort liability of that single motorist? More than one tortfeasor? Multiple claimants who share, and thus exhaust, the liability insurance? There is an issue that is only recently surfacing having to do with the role "joint and several liability" should play in the UIM area. Finally, there is a more fundamental, philosophical issue: what if the at-fault vehicle is not owned and driven by a stranger? This latter issue has seen a fair amount of litigation; the issue is phrased in terms of whether a family-owned vehicle exclusion or a geographic exclusion is enforceable or whether there is an underinsured motor vehicle.

A. What are "actual damages?"

One element in the test, the phrase "actual damages," refers to the damages the insured is legally entitled to recover from the tort-
feasor. Actual damages, for purposes of UIM, refer generally to the amount of money which the injured person is legally entitled to recover from the at-fault motorist. In applying the statute, the total damages are first reduced by the no-fault benefits paid or payable and any collateral source off-sets. Afterwards, damages are further reduced to reflect the injured party’s comparative fault. Net damages are then compared to the tortfeasor’s liability limits. The tortfeasor is underinsured only if those actual damages exceed the available BI limits.

Logically, there ought be little or no difference whether actual damages are calculated under the tort system or under the UIM system. After all, the UIM coverage is intended to act as a first party supplement to the tortfeasor’s liability insurance. The benchmark refers to the tort judgment for which the at-fault motorist is underinsured.

B. To what “limit” are the actual damages compared to determine whether a motorist is underinsured?

The damages must exceed the tortfeasor’s automobile insurance limits in order for the motorist to be considered underinsured. A tortfeasor is not underinsured if the judgment is less than the tortfeasor’s BI limits. If there is only one motorist, and if there is one applicable liability insurance policy, the comparison is relatively simple. Do the actual damages which the injured person is legally entitled to recover exceed that single liability limit? But is there just one BI “limit?” There may be several insurance policies which together comprise the automobile liability insurance and thus create the dollar limit which the damages must exceed before the motorist is underinsured. For example, if a vehicle is negligently driven by a non-owner with the permission of the owner, there are often two automobile liability insurance limits which apply to the tort claim. The motorist would not be underinsured.

73. See Richards v. Milwaukee Ins. Co., 518 N.W.2d 26, 28 (Minn. 1994), reh’g denied, (Minn. Aug. 18, 1994).
74. See id.
75. See id.
76. See id.
77. See Richards, 518 N.W.2d at 28.
78. See Costello v. Aetna Cas. & Sur. Co., 472 N.W.2d 324, 326 (Minn. 1991) (denying UIM claim where jury award in the tort suit was less than BI limits).
79. Typically, the vehicle owner’s liability coverage applies. The policy is written to provide for tort liability “arising out of” the ownership, maintenance or use
unless the damages exceed the combined limits of the liability insurance on that motor vehicle. An even simpler, although less common, example involves a vehicle owner/operator who carries a standard automobile insurance policy and an excess liability or umbrella insurance policy. Umbrella policies duplicate and broaden the coverage which standard automobile insurance affords. If the combined insurance of the automobile policy and the excess liability policy is sufficient to pay for the victim’s damages, then the motorist is not underinsured. In short, to determine if a motorist is underinsured, the collectible damages are compared with the automobile and applicable excess automobile insurance limits.

The application of the statutory definition of an underinsured motor vehicle becomes somewhat more complex when there are multiple claimants, vicariously liable parties, multiple tortfeasors or non-motoring tortfeasors. These issues are addressed below.

1. Multiple Claimants

How should the threshold definition of underinsured be applied when a motorist injures several persons? Consider, for example, that one single motorist (with minimum $30,000 per person liability insurance/$60,000 per accident) injures four people. If each person has $35,000 in damages, one can conclude that the motorist is underinsured. After all, the $35,000 damage figure exceeds the $30,000 per person liability limit as to each injured person. But what if each person’s injuries were valued at $25,000? If one compares each individual’s damages and the “per person” liability limit, none of the injured people could make an underinsured motorist claim. Is that how the comparison should be made?

The statute does not address the possibility that a tortfeasor’s liability limits may be distributed among multiple claimants, leaving some individuals under-compensated in circumstances where, by some standard, the motorist was underinsured. By comparing the damages to the limits of liability rather than to the coverage which is actually available, the underinsured definition creates an issue to
whether the full *per person* limits are to be compared to each person's damages or whether the *per accident* liability limits are to be compared with the collective damages sustained by all injured persons.

In *Kothrade v. American Family Mutual Insurance Company*, the Minnesota Court of Appeals held that the appropriate comparison in multiple claimant cases is between the damages collectively sustained by the injured claimants and the tortfeasor's *per accident* liability limits. This interpretation of the threshold underinsured requirement neither expands the UIM beyond the use contemplated in the insurance system nor prevents access where it is reasonably necessary to fulfill the underinsured purpose.

2. Vicariously Liable Parties

Often automobile liability insurance applies not to the active fault of the motorist but instead protects the vicariously liable owner from tort liability. In a common case where an owner allows another to drive his or her car, two liability insurance policies may be available—that of the owner and that of the driver. Both the owner's automobile liability insurance and the driver's automobile liability insurance afford the kind of primary coverage which UIM is intended to supplement. Logically, then, a UIM claim exists only if the damages exceed the combined liability limits applicable to a single vehicle. In order to be underinsured, therefore, the insured's actual damages must exceed the total amount of liability protection available to the active tortfeasor and to any vicariously liable party.

All liability policies which insure the negligent operation of the tortfeasor's vehicle are considered in determining underinsurability. Thus, in addition to the owner's coverage, the liability coverage available to the operator of the vehicle, to the tortfeasor's employer or to any other vicariously liable party will be considered. This approach is consistent with the conceptual basis of underinsured motorist coverage. Coverage is accessed only if there is not enough liability insurance available to pay for damages caused by a

---

80. 462 N.W.2d 413 (Minn. Ct. App. 1990).
81. *Id.* See also Ballanger v. Toenjes, 362 N.W.2d 2 (Minn. Ct. App.) (holding that a suit by multiple claimants was properly settled within the policyholder's per accident liability limits), *rev. dismissed.* (Minn. 1985).
negligent motorist.

3. Multiple Tortfeasors

Underinsured motorist coverage is necessary only when insufficient liability insurance exists to compensate for the motoring injury. The definition of underinsured motorist requires one to compare the recoverable damages to the underinsured motorist's liability limits. With that premise in mind, what if there is more than one at-fault motorist? Is there an underinsured motorist claim in such a case?

The answer depends upon two variables. When examining Minnesota precedents in the UIM area, one must keep in mind that there have been changes at different times in the UIM "system" and in the "joint and several liability" rules. First of all, does the UIM system contemplate that coverage is available only if the combined limits of all tortfeasors are inadequate to fully compensate the injured person? Or does the UIM system allow a UIM claim to be made if the damages exceed the tort liability limits of one single tortfeasor, without regard for the existence of other insured motoring tortfeasors?

Until 1989, Minnesota required that damages exceed the combined liability limits of all jointly and severally liable tortfeasors. In 1989, Minnesota changed the law to allow a UIM claim whenever any one motorist of several was underinsured. As a result of this change in the law, pre-1989 and post-1989 claims differ.

Second, when aggregating the liability limits of several motoring tortfeasors, the implicit assumption has been that each motorist is jointly and severally liable to the injured person. From that flows the assumption that all of the liability insurance of all such tortfeasors is available to compensate, as primary coverage, the tort damages of an injured person. The fundamental concept, whether the motorist is underinsured, requires comparison of the damages with available liability limits.

Total actual damages, in isolation of tort liability for those damages, is meaningless. Similarly, the total of the motorists' tort liability insurance is meaningless unless the total of those liability limits

83. See Minn. Stat. § 65B.49, subd. 4a (1996).
84. See Richards v. Milwaukee Ins. Co., 518 N.W.2d 26, 28 (Minn. 1994) (stating that to trigger a UIM claim, total damages must be reduced by comparative fault and by appropriate set-offs to yield a dollar sum for which the tortfeasor is legally liable).
policies is actually available to pay toward the damages. That, in turn, depends upon whether the several motorists are fully jointly and severally liable for the actual damages.

During most of Minnesota's UIM history, a motorist with only one percent of the comparative fault could have judgment entered against him or her for 100% of the total damages. But that rule has changed. A motorist with only one percent comparative fault is no longer jointly and severally liable for the full damages. As a result of this change in the statute, certain cases applying pre-1988 joint and several liability principles cannot be meaningfully applied to more recent accident claims.

After August 1, 1988, motorists with nominal degrees of fault have been liable only for four times the actual percentage of fault attributed to them. In such a case, it is not helpful to compare the total damages recoverable from all tortfeasors to a specific tortfeasor's BI limits, because such a tortfeasor may be liable only for a fraction of that amount. Put another way, it is not logical to add the total amounts of the liability limits for each of several motoring tortfeasors if only a fraction of those limits, the amount available to pay a tort judgment, is available to pay to the injured person. Accordingly, if one must decide whether a motorist is "underinsured," logic dictates that one should analyze a tortfeasor's liability coverage with the joint and several liability law in mind.

For example, if one of two motorists is ten percent at fault, has $30,000 of liability insurance and the total damages of $60,000, that motorist would not be considered underinsured. When the tort liability of that partially at-fault (ten percent) motorist is assessed, his degree of fault is less than that which would make him fully jointly and severally liable for one hundred percent of the damages. Instead, applying Minnesota's joint and several liability statute, that motorist could never be responsible for more than $24,000. Be-

85. See Johnson v. American Family Mut. Auto. Ins. Co., 426 N.W.2d 419 (Minn. 1988). The Johnson court held that a motor vehicle would be considered underinsured only where the insured's damages exceed the "combined liability limits of all tortfeasors." Id. at 423. Johnson, a passenger in a school bus, was injured when the bus collided with an automobile. Id. at 419. The bus had $1,000,000 in liability limits, and the automobile had $100,000 in BI limits. Id. at 420. Because Johnson's damages did not exceed $1,100,000 (the combined BI limits of both tortfeasors) Johnson did not have a UIM claim because neither motorist was underinsured. Id. at 422.

86. See MINN. STAT. § 604.02, subd. 1 (1996).

87. This figure can be calculated as follows: ten percent of fault times four is forty percent. Forty percent of the $60,000 damages is $24,000.
cause that motorist has, in this example, $30,000 of liability insurance, he is not underinsured. The damages this tortfeasor is legally obligated to pay are less than his available bodily injury liability insurance limit. Therefore, that motorist would not be underinsured.

By contrast, the second motorist in the example above (ninety percent at fault) would be fully jointly and severally liable for one hundred percent of the damages. If the liability limits of the second motorist are not enough to pay all of the tort damages, that motorist is underinsured. His or her BI limits are not enough to pay the tort judgment which could be entered against that motorist.

A court performs this joint and several liability analysis after the jury makes findings of fault. While UIM coverage is, generally speaking, intended to provide a first party source to pay the uncompensated amount of a tort judgment which exceeds the liability limits of a motoring tortfeasor, not all tort judgments automatically translate into the amount of the UIM insurer's obligation. In "conversion" and "family auto exclusion" cases discussed above, the amount of the judgment is not dispositive of the UIM insurer's obligation. The judgment, although binding on a tortfeasor, is merely the starting point. If recovering the tort judgment from the UIM insurer would essentially "convert" inexpensive UIM coverage into additional BI coverage, some part of the judgment is not recoverable from the UIM insurer.88

a. Multiple Tortfeasors: Before the 1988 Joint and Several Liability Change and Before the August 1, 1989 UIM Law Change

In Johnson v. American Family Mutual Automobile Insurance Company,89 the Minnesota Supreme Court held that a motor vehicle can be considered underinsured only where the insured's damages exceed the "combined liability limits of all tortfeasors."90 The claim in Johnson arose out of a 1978 accident.91 The school bus in which the Johnson boy was riding swerved into a ditch in order to avoid an illegally parked automobile.92 The bus was insured for liability cov-

89. 426 N.W.2d 419 (Minn. 1988).
90. See id. at 423.
91. See id. at 419.
92. See id.
verage in the amount of $1,000,000, and the automobile was insured with liability limits in the amount of $100,000. Johnson's guardian ad litem commenced suit against both drivers and eventually settled with the automobile insurer for the liability limits of $100,000. Johnson also released the bus's liability insurer in consideration of $35,000.

These amounts did not adequately compensate Johnson for his injuries. Johnson's guardian ad litem then commenced a UIM arbitration proceeding against Johnson's UIM insurer, American Family. Johnson's guardian ad litem contended that American Family was required to pay damages to the extent they exceeded $135,000, the amounts paid by the tortfeasors. American Family asserted that they were entitled to set-off the combined liability limits, and since Johnson's damages did not exceed that amount, UIM coverage was not available.

The Minnesota Court of Appeals disagreed with American Family's position, stating that liability for UIM benefits is "measured by the amount by which the injured party's damages exceed the liability insurance limits of the primary culpable defendant." The court of appeals reached this conclusion, in part, by noting that the 1978 definition of an underinsured motor vehicle suggested that the limits of liability of only one vehicle should be used because it made "reference only to the other vehicle." The Minnesota Supreme Court reversed. Noting that at the time of the accident each tortfeasor remained jointly and severally liable for the entire award, the court denied entitlement to UIM benefits, stating:

"Underinsured motorist coverage is not an alternative to liability coverage . . . . Because Johnson's damages did not exceed the combined liability limits of all tortfeasors, the

93. See id. at 420.
94. See id.
95. See id.
96. See id.
97. See id.
98. See id.
100. Id. at 176 n.1. (emphasis in original).
101. See Johnson, 426 N.W.2d at 422.
vehicles were not really underinsured . . . . [The] only way for the under insurance concept to have any consistency is to consider the liability limits of all tortfeasors in determining the amount recoverable by an injured insured. Since each could be liable for the entire amount, the liability insurance limits of each must be considered . . . .

As noted above, Johnson's accident occurred in 1978. What about the 1985 legislative changes? The fundamental nature of UIM coverage, which compensates injured persons for damages sustained in excess of the available liability limits, was not altered by the 1985 legislation. Consequently, Johnson would apply to claims governed by the 1985 laws.

b. Multiple Tortfeasors: After the August 1, 1988 Joint and Several Change

Application of Johnson to claims arising out of accidents occurring prior to August 1, 1988, posed no problem. The full combined liability limits of all tortfeasors had to be considered because even a small degree of fault made the motorist fully liable for any judgment. In such a case, an underinsured motorist claim was determined by comparing the damages to the total available liability insurance from all tortfeasors because each was fully jointly and severally liable. However, applying Johnson to claims arising on or after August 1, 1988, was complicated by the 1988 amendment to Minnesota Statutes section 604.02. Under that statute, a tortfeasor had to be at least fifteen percent negligent before he or she could be liable for the whole award. A tortfeasor whose fault was less than fifteen percent could only be liable for four times the percentage of fault attributable to that person.

A determination of whether a motor vehicle is underinsured must include or consider, therefore, the respective percentages of fault of each tortfeasor under the joint and several liability statute. An underinsured motor vehicle should be deemed involved whenever the injured claimant's damages exceed the combined limits of

102. See id.
105. See MINN. STAT. § 604.02 (1996).
106. See id. From this comes the phrase "four times fifteen" as a reminder that those tortfeasors with relatively nominal, 15% or less, fault can only be required to pay "four times" the amount of their actual percentage of fault.
bodily injury liability that are actually available to the claimant after proper application of joint and several liability principles. For example, if one tortfeasor is less than fifteen percent at fault for an accident, Minnesota Statutes section 604.02 would prevent the injured insured from collecting the full liability limits of that tortfeasor. The portion of the liability limits of the marginally culpable tortfeasor that is unavailable to the insured should not be considered in determining whether there is an underinsured motor vehicle.

c. Multiple Tortfeasors: After the August 1, 1989, UIM Law Change

Effective August 1, 1989, Minnesota Statutes section 65B.49, subdivision 4a was amended to provide that "[i]f a person is injured by two or more vehicles, underinsured motorist coverage is payable whenever any one of those vehicles meets the definition of underinsured motor vehicle in section 65B.43, subdivision 17." 107 After 1989, then, a motorist is underinsured if that individual motorist is liable to the injured party and if the damages for which that motorist is liable exceed the available liability insurance limit for that tortfeasor. The legislature apparently sought, by this amendment, to overrule the holding in Johnson.

But what if the amount of that "other" motorist's tort liability (whose tort obligation was determined with joint and several liability principles in mind) includes some damages which should have been insured under the BI coverage of the same policy under which the UIM claim is made? Would that be improper "conversion?"

_Lahr v. American Family Mutual Insurance Company_, 108 arose after the 1988 joint and several liability change and after the 1989 change which allowed an injured party to make a UIM claim whenever any one motorist was underinsured. In _Lahr_, the Minnesota Court of Appeals held that applying joint and several liability was improper for determining whether the motorist was underinsured. 109 _Lahr_ was a passenger in one automobile when it collided

---

107. MINN. STAT. § 65B.49, subd. 4a (1996) (emphasis added).
109. See id. at 735. The question is whether _Lahr_ represent the first shot in a volley of new litigation over the joint and several status of underinsured motorists (with a separate standard than that used in the underlying tort/liability insurance and even in the uninsured motorist arenas) or whether _Lahr_ is simply another
with another. Lahr claimed underinsured motorist coverage from American Family as insurer of the car in which Lahr was riding. Lahr’s damages were $290,000. Peura, the driver of Lahr’s car, was ninety percent at fault, and the other driver, Kvisto, was only ten percent at fault. Peura’s liability insurer paid its $50,000 BI limit; Kvisto’s liability insurer settled under its $100,000 BI limit for $80,000.

Lahr could not, of course, argue that Peura was an underinsured motorist for purposes of collecting under Peura’s UIM coverage. That would be blatant “conversion” of UIM into BI. American Family had paid the liability insurance coverage on the occupied vehicle but objected to paying its UIM coverage to passenger Lahr. Lahr claimed, however, that Kvisto was an “underinsured motor vehicle” entitling Lahr to recover UIM coverage from American Family, based upon joint and several principles.

The issue presented in Lahr was whether Kvisto, the other motorist, was underinsured. Kvisto’s percentage of fault, ten percent, amounted to $29,000. If joint and several liability principles were applied, however, Kvisto would be liable for more than that ten percent of the total damages. Lahr argued that if Kvisto were jointly and severally liable for four times Kvisto’s ten percent of fault, then Kvisto could be liable for $116,000. Lahr further argued that since this $116,000 exceeded Kvisto’s liability limit of $100,000 Kvisto should be considered an underinsured motorist for purposes of accessing Peura’s UIM coverage.

The court of appeals refused to allow Lahr to recover UIM coverage under the same policy which had paid its BI limits to...

“conversion” case.

110. See Lahr, 551 N.W.2d at 732.
111. See id. at 732-33.
112. See id. at 733.
113. See id.
114. See id.
115. Of course, if Lahr had her own insurance policy, nothing would have prevented her from supplementing the inadequate BI coverage of host Peura from Lahr’s own UIM coverage.
116. See Lahr, 551 N.W.2d at 733.
117. See id.
118. See id.
119. See id.
120. See id.
121. See id.
122. See id.
Although the opinion contains statements which, if taken literally, seem to disallow the use of joint and several principles in any UIM claim, the court's underlying concern involved "conversion." The court noted, "The use of Peura's liability to trigger UIM coverage violates the underlying policy of Myers and Thommen. Accordingly, the district court erred in applying joint and several liability."124

One reading of Lahr, consistent with the "conversion" cases, is simply that the court of appeals was not willing to allow a passenger to collect both BI and UIM payments for the same risk (i.e., the negligent driving of host Peura). Allowing Lahr to collect both benefits could well be recognized as "conversion" since the ninety percent of fault attributable to Peura would form the basis for payment under both coverages. The objection to conversion is to prevent applying two separate coverages, BI and UIM, to the same risk.

The dissent in Lahr would have applied joint and several principles, thereby allowing passenger Lahr to recover up to the amount of damages ($116,000) for which Kvisto would be jointly and severally liable, reduced by the BI payment made by Kvisto's insurer.125

Lahr will likely be revisited in other cases where the application of joint and several liability will not result in shifting fault from the host driver to the other, potentially underinsured, driver. For example, consider if Lahr had been injured while riding in Peura's car when it collided with two other cars. Assume that each of the three vehicles had equal fault, thirty-three and one-third percent each. Would Lahr limit the UIM claim to one-third of the total damages or would the joint and several liability of the other two motorists form the basis of the UIM claim? This question is thus far unanswered. But future cases involving Lahr will reveal what role joint and several liability plays where there are multiple tortfeasors and how, in that context, the UIM exposure should be calculated.

C. When is the At-Fault Underinsured Vehicle Not "Underinsured?"

The dollar sum of a tort judgment will not always automatically translate into an underinsured motorist recovery. Rather, Minnesota courts have struggled to draw a line beyond which it would be
improper to allow a passenger to collect both the liability insurance on the vehicle and to collect UIM coverage for the same negligent driving.

In many ways, the role of underinsured motorist coverage in Minnesota parallels the role of tort liability insurance. Both types of insurance generally derive from and obligate the insurer to pay the amount of damages that an injured person is legally entitled to recover from a motoring tortfeasor. Underinsured motorist coverage is a first-party coverage which provides a supplement to inadequate tort liability insurance coverage. Liability coverage, on the other hand, is a third-party coverage. The liability insurer commits to pay to a third person (i.e., the injured claimant) the damages which he or she is legally entitled to recover as a result of the fault of the insured motorist.

It is important to note that both types of coverage apply to a specifically insured "risk." Tort liability insurance, in Minnesota, primarily follows the vehicle. In particular, since 1985, the insured risk has been primarily linked to the insured vehicle. The concept of "risk" is fundamental to insurance; shifting of identifiable "risks" is what insurance is about. Significantly, some risks are excluded from both the BI and from the UM and UIM coverages. 126 A few of these risks are discussed below.

In the liability insurance area, Minnesota has regularly enforced language which prevents the extension of a policy's liability protection from one vehicle (owned and insured by the insured) to another, if that other vehicle is also owned by the insured. The reason behind this approach is to prevent an insured from extending the insurance on one vehicle to many vehicles that should be insured separately. Consequently, language which prevents this extension or conversion of liability coverage from one vehicle to several has found its way into virtually all automobile liability insurance policies. The language used to prevent this extension is typically found in an exclusion which has come to be referred to as the "family auto exclusion." Although the exclusion first came about in the liability coverage, it has come to be used in uninsured127 and underinsured motorist policies.

126. See McIntosh v. State Farm Mut. Auto. Ins. Co., 488 N.W.2d 476, 479-80 (Minn. 1992) (ruling that an injury which results from being intentionally run down with an automobile is not a risk covered under the liability (BI) policy or the UM or UIM coverages).

127. By enforcing the exclusionary language of the "family auto exclusion" or
The same exclusionary concept, the "family auto exclusion," has been dealt with in the underinsured motorist coverage area. At its simplest, the exclusion prevents the insured vehicle, covered by the liability coverage in the amount selected by the owner, from also being treated as an underinsured motor vehicle under the same policy. If the at-fault vehicle was another vehicle owned by the insured, the exclusion was easily applied. In less clear-cut cases, however, Minnesota courts have struggled to balance shifting public policies. Before the 1985 statutory changes to the UM/UIM system, both UM and UIM policies were deemed to essentially follow the person and not the vehicle. Thus, before 1985 Minnesota law allowed the "stacking" of all UM or UIM coverages available to a person under several potentially available policies. At some point, however, these policy objectives shifted; allowing recovery of the UM or UIM coverage became unacceptable.

Minnesota's UIM history, in terms of its application to the family auto exclusion, shows the struggle as the courts have tried to apply these shifting policies. More recently, the appellate courts have come to recognize that the post-1985 statutes not only validate the family auto exclusions, but impose the limitation even in the absence of an exclusion or limitation in the insurance policy.

1. The "Family Auto Exclusion"

a. Roots of the "Family Auto Exclusion" in Liability Coverage: Exclusion of Risks Resulting from Other Owned, Non-Insured Vehicles

In most instances, a liability policy is issued for the ownership and use of a specific owned automobile. Automobile insurers have regularly included language in standard automobile policies denying coverage when the accident results from an insured's use of another owned vehicle. For example, the policy may specify that:

We do not provide liability coverage for the ownership, maintenance or use of:

Any vehicle, other than the Described Vehicle which

the restrictive definition of "uninsured motor vehicle," Minnesota courts prevented a vehicle owner from purchasing one liability policy and effectively extending it to other vehicles which were owned but uninsured. 128. The court often explains that it is necessary to apply the exclusion to prevent the "conversion" of inexpensively obtained underinsured motorist coverage from serving as additional liability coverage on the same vehicle.
is owned by you or furnished or available for your regular use.

Such an exclusion has been upheld both before and after passage of the No-Fault Act. The validity of the exclusion derives from the fact that the main risk insured is the ownership/operation of the designated vehicle. Because of this basic risk-based premise underlying liability insurance, such limitations on coverage have routinely been enforced. In 1973, the Wisconsin Supreme Court stated "without this limitation a person could purchase just one policy on only one automobile and thereby secure coverage for all the other vehicles he may own or vehicles the members of his family own while residents of the same household." 129

Minnesota courts have rejected all challenges to the validity of this type of exclusion when applied to either a named insured, or to family members who operate a vehicle they own or have available for their regular use. 130 The courts have concluded that the risk involved in the ownership or use of another owned motor vehicle should be insured under a policy issued for that vehicle. 131

The basic risk-based premise underlying liability coverage and setting effective limits upon the scope of the liability coverage has not changed. If anything, evolution to a compulsory insurance system which compels each owner of a motor vehicle to obtain automobile liability insurance supports enforcement of exclusions. While recognizing that no-fault benefits and uninsured motorist benefits had been payable under the same circumstances at that time, the Minnesota Supreme Court stated in Toomey v. Krone. 132 "The Minnesota No-Fault Act has not altered the basic framework of liability law. The premise underlying no-fault and uninsured motorist coverage is first-party in nature, as opposed to third-party coverage involved in the instant case." 133

The Minnesota Supreme Court enforced the exclusion in Toomey, preventing the liability coverage from extending to another

---

132. See supra note 129 and accompanying text.
133. Toomey, 306 N.W.2d at 550
134. Id.
OWNED UNINSURED VEHICLE.\textsuperscript{135} The \textit{Toomey} holding underscores one of the key differences between liability coverage (which primarily “follows the vehicle”) and first-party coverages (such as no-fault, uninsured and underinsured motorist coverage) that, in the past, tended to “follow the person.”

\subsection*{b. Liability Insurance: Exclusion of Risks Resulting from Operation/Use of Other Vehicles Regularly Furnished or Available for Use}

The same “family auto” exclusion set out above serves a dual purpose. Not only does the exclusion prevent liability coverage from applying to risks from operating other owned vehicles, it also prevents coverage under one policy from extending to the insured’s use of another vehicle which is available for the regular use of that person.

Understanding the conceptual basis by which Minnesota applies the family auto exclusion in the liability insurance area helps one understand the enforcement of a comparable family auto exclusion in the UM and UIM coverage areas. The term \textit{family auto exclusion} is more aptly applied in its original setting: it serves as an exclusion from the liability coverage of an automobile policy. The excluded risks are usually associated with other vehicles owned or regularly used by the named insured or by other family members. In most instances, the automobile liability insurance is written for a specific vehicle.

Most policies extend to the named insured, including family members, liability insurance protection when operating other vehicles, as long as doing so does not extend the vehicle-based liability insurance from one owned vehicle to another owned vehicle. From that premise, it has been only a short reach to exclude liability coverage for other vehicles owned by family members of the named insured and also other vehicles not owned by, but furnished or available for regular use of, those same parties. The purpose of the exclusion “is to prevent coverage of two or more automobiles when only a single automobile is insured.”\textsuperscript{136}

\subsection*{c. The “Family Auto Exclusion” in Uninsured and Underinsured Motorist Coverage}

Almost every standard automobile policy contains provisions

\textsuperscript{135} See \textit{id.}

\textsuperscript{136} Boedigheimer v. Taylor, 287 Minn. 323, 327, 178 N.W.2d 610, 613 (1970).
that are designed to prevent the improper conversion of the relatively inexpensive first-party UM and UIM coverages into additional liability protection for the benefit of the vehicle owner or tortfeasor. One such provision, commonly referred to as the "family auto exclusion" specifically defines an uninsured or underinsured motor vehicle to exclude any vehicle owned by, furnished, or available for the regular use of the named insured or any family member.

The family auto exclusion has accounted for much litigation in the UM and UIM contexts largely because the exclusion applies to two separate situations. First of all, the exclusion prevents the insured vehicle from being considered an underinsured motor vehicle under the same policy. For example, in a one-car accident a passenger has a claim against the negligent driver, triggering the BI coverage written for that risk. If the passenger could also collect under the policy's UIM coverage, the inexpensive UIM coverage would be converted into extra BI coverage for the protection of the negligent owner. The owner would receive twice the BI coverage for little more than one BI premium. An improved version of the exclusion would simply state that the term "underinsured motor vehicle" does not include the insured vehicle; instead, some other vehicle must be involved in order to trigger the UIM risk.

Second, the family auto exclusion prevents the extension of one policy's BI coverage from the insured vehicle to another vehicle which should have been separately insured by the policyholder or one of his or her family members. UIM coverage is cheaper than comparable limits of BI coverage. The Minnesota system contemplates that each owner should insure each vehicle with liability coverage. If the named insured could recover the UIM coverage from one policy on vehicle A so that it became, in effect, "BI coverage" on a second vehicle owned by the named insured, the owner would have insured vehicle B with extra liability coverage without paying for it. Without the exclusion, inexpensive UIM coverage could be converted into BI coverage.

The family auto exclusion is most often litigated when the insured seeks to collect UIM coverage which should have been purchased as BI coverage by a member of the insured's family. At some point, it is inequitable to allow the family-owned vehicle to be treated as an "underinsured motor vehicle." Just where the line should be drawn has been influenced heavily by prevailing public policy factors.
Wintz v. Colonial Insurance Company of California\textsuperscript{137} directly addressed the question of whether exclusionary clauses, such as the family auto exclusion, were valid or void. Wintz involved a claim for uninsured (UM) motorist coverage by Linda Wintz.\textsuperscript{138} Wintz was injured while riding on an uninsured motorcycle driven by her husband but owned by her son (who did not live with them).\textsuperscript{139} Emphasizing the "rule that coverage follows the person" but not the vehicle, the court of appeals had refused to deny Linda Wintz UM coverage under her and her husband's automobile policy despite a provision that the UM/UIM coverage did not apply to vehicles which were "owned by or furnished or available for the regular use" of the named insured or a relative.\textsuperscript{140} The Minnesota Supreme Court reversed, and in so doing articulated the pre-1985 and post-1985 dichotomy as follows:

Before 1984, Minnesota courts relied on Nygaard v. State Farm Mutual Automobile Insurance Company, 301 Minn. 10, 221 N.W.2d 151 (1974), to determine the outcome of such cases. This court held in Nygaard that "uninsured motorist protection is not coverage for vehicles but for persons . . . ." \textit{Id.}, 221 N.W.2d at 157.

In 1985, the legislature amended Minn. Stat. section 65B.49, subd. 3a(7) (Supp.1985) to allow insurance companies to exclude certain vehicles from uninsured motorist coverage if the vehicle was owned by the policyholder, but not insured by the policyholder. \textit{See} Act of May 21, 1985, ch. 168, § 11, 1985 Minn. Laws 459, codified at Minn. Stat. section 65B.49, subd. 3a(7) (Supp.1985).

After that amendment, this court heard Petrich v. Hartford Fire Insurance Company, 427 N.W.2d 244 (1988). Relying on Myers, we said: "Myers . . . rests on the principle that vehicle owners may not purchase first party coverage and expect it to function as liability protection. The concern is not the creation of additional liability coverage, but the conversion of one type of insurance into another." \textit{Petrich}, 427 N.W.2d at 246.

To void an exclusionary clause where the vehicle was "owned by or furnished or available for the regular use of" the first-party beneficiary would allow a policyholder to in-

\begin{footnotes}
\item[137.] 542 N.W.2d 625, 626 (Minn. 1996).
\item[138.] \textit{See id.}
\item[139.] \textit{See id.}
\item[140.] \textit{Id.} at 627.
\end{footnotes}
sure only one vehicle, and gain coverage on any/all other uninsured vehicles. This would convert first-party benefits of an insurance policy into third-party liability benefits.\footnote{Id. at 626-27.}

In \textit{Myers v. State Farm Mutual Automobile Insurance Company},\footnote{336 N.W.2d 288, 289 (Minn. 1983).} a seminal case in this area, a passenger was killed in a vehicle owned by Stein and driven by another.\footnote{See id.} The car ran off the side of the road and struck a tree.\footnote{Id. at 290.} After collecting the liability coverage on the car, the decedent’s heirs sought UIM coverage under the same policy for the same negligent conduct.\footnote{Id. at 291.} The policy excluded the insured vehicle from the definition of an underinsured motor vehicle by providing that an underinsured motor vehicle would not include any vehicle “owned by or furnished or made available for the regular use of you [i.e., Stein] or any family member.”\footnote{Id. at 290.} The Minnesota Supreme Court upheld the provision and denied benefits, stating:

Underinsured motorist coverage is a first-party coverage and, in that sense, the coverage follows the person not the vehicle. Here, however, the decedent passenger’s heirs have already collected under the liability coverage of the insurer of the Stein car. To now collect further under the same insurer’s underinsured motorist coverage would be to convert the underinsured motorist coverage into third-party insurance, treating it essentially the same as third-party liability coverage. The policy [exclusion] . . . prevents this conversion of first-party coverage into third-party liability coverage.\footnote{See id. at 536.}

The same result was reached in claims involving UIM coverage that was imposed by operation of law under the 1975 to 1980 mandatory offer statute.\footnote{See Meyer v. Illinois Farmers Ins. Group, 371 N.W.2d 535, 537 (Minn. 1985); cf. Eisenschenk v. Millers Mut. Ins. Ass’n of Illinois, 353 N.W.2d 662, 665 (Minn. Ct. App. 1984), \textit{rev. denied}, (Minn. 1985).} In \textit{Meyer v. Illinois Farmers Insurance Group},\footnote{371 N.W.2d 535, 536 (Minn. 1985).} even in the absence of any contractual language, the “exclusion” was applied.\footnote{See id. at 536.} As a matter of public policy, the concept of under-
insured motorist coverage could not be extended to the owned vehicle or to others which fit within the scope of a family auto exclusion.\textsuperscript{151}

The 1985 legislation created a statutory priority or "source" system for payment of UM and UIM claims whereby the first level of priority is the coverage insuring the "occupied" vehicle.\textsuperscript{152} In Synstelien v. State Farm Automobile Insurance Company,\textsuperscript{153} for example, the court of appeals erroneously concluded that Meyer and Myers (the case relied on by Meyer) were no longer valid because their continued application would prevent an "occupant" from recovering UIM benefits.\textsuperscript{154} In Thommen v. Illinois Farmers Insurance Company,\textsuperscript{155} on the other hand, the supreme court held that 1985 amendments did not affect the validity of Myers and rejected the Synstelien analysis.\textsuperscript{156}

In Thommen, the policy on the occupied vehicle excluded the insured vehicle from becoming an "underinsured motor vehicle."\textsuperscript{157} Several passengers sought UIM coverage under that policy after collecting its BI coverage.\textsuperscript{158} The court noted that the 1985 amendment did "not change the fundamental character of UIM coverage [and therefore] the rationale for the Myers decision is equally valid today . . . ."\textsuperscript{159}

In Linder v. State Farm Mutual Automobile Insurance Company,\textsuperscript{160} Jennifer Linder, a minor, was struck by a pickup truck owned by her father which was driven by her brother.\textsuperscript{161} All were residents of the same household.\textsuperscript{162} Linder collected the liability coverage on the policy insuring the truck and conceded that Myers prevented her from collecting the UIM coverage of that same policy.\textsuperscript{163} Instead, she made claim for UIM benefits under separate policies is-

\textsuperscript{151} See id.
\textsuperscript{152} See MINN. STAT. § 65B.49, subd. 3a(5) (1996).
\textsuperscript{153} 418 N.W.2d 530 (Minn. Ct. App.), rev. granted, (Minn. 1988). See Broten v. Western Nat'l Mut. Ins. Co., 428 N.W.2d 85, 86 (Minn. 1988) (disposing of issue that was the basis of the review granted in Synstelien v. State Farm Auto. Ins. Co.).
\textsuperscript{154} See Synstelien, 418 N.W.2d at 532.
\textsuperscript{155} 437 N.W.2d 651, 652 (Minn. 1989).
\textsuperscript{156} See id. at 654.
\textsuperscript{157} See id. at 653.
\textsuperscript{158} See id. at 652.
\textsuperscript{159} Id. at 654.
\textsuperscript{160} 364 N.W.2d 481 (Minn. Ct. App.), rev. denied, (Minn. 1985).
\textsuperscript{162} See id.
\textsuperscript{163} See id. at 483.
sued to her father which insured other vehicles. These policies, however, provided that UIM coverage would not apply to injury "through being struck by a land motor vehicle owned by the named insured or any resident of the same household."

Although Linder was not seeking UIM benefits from the same policy that had afforded the BI coverage, the court of appeals enforced the exclusion. To invalidate the exclusion would convert the UIM coverage into additional liability protection for the family, and "underinsured motorist coverage is not designed to relieve an insured or his family from the failure to purchase adequate liability coverage."

In Petrich by Lee v. Hartford Fire Insurance Company, the Minnesota Supreme Court applied the "family auto exclusion" in the context of a UM claim. Gary Lee's stepson, Paul Petrich, was injured while riding in an uninsured pickup truck owned by Lee. Lee had two other vehicles which were both insured by Hartford. Petrich sought UM benefits under that policy. The policy excluded UM coverage if the accident arose out of an uninsured vehicle which was "owned by or furnished or available for the regular use of... [Gary Lee] or any family member."

Petrich argued that the Myers line of cases were inapplicable because in Myers and its progeny, the plaintiff had first collected liability coverage and then attempted to collect UIM benefits on the same policy or additional policies carried by the tortfeasor. In essence, Petrich argued that the courts that applied Myers were only prohibiting a doubling of the liability limits, a situation which could only occur where the claimant first collects under the third party liability coverage; not where the only vehicle involved was uninsured. The supreme court disagreed and held the exclusion was enforceable:

The Myers rule arises out of a fact pattern where the same

164. See id. at 482.
165. Id.
166. See id. at 483.
168. 427 N.W.2d 244, 245 (Minn. 1988).
169. See Petrich, 427 N.W.2d at 245.
170. See id.
171. Id.
172. See id. at 246.
173. See id. at 246.
person owns the at-fault vehicle and the policy under which the injured claimant seeks first-party coverage. Recovery in this situation inevitably compensates the owner who failed to adequately insure one of his vehicles. Such is the case for Gary Lee, who owns and declined to insure the car that caused his stepson’s injury, and also owns the uninsured motorist policy covering his stepson . . .

\textit{Myers} . . . rests on the principle that vehicle owners may not purchase first party coverage and expect it to function as liability coverage. . . . If anything, the prohibition against conversion established in \textit{Myers}, an uninsured case, is even more complete here where the car owner has purchased no liability coverage at all on the vehicle involved in the accident.\textsuperscript{174}

1. The “Family Auto Exclusion” In Separate Insurance Policies Not Issued to the Tortfeasor

In \textit{Great American Insurance Company v. Sticha},\textsuperscript{175} two tortfeasors caused an accident in which Sticha was injured.\textsuperscript{176} The accident occurred in 1983 at a time when the injured party was allowed to collect “jointly and severally” from either of the two tortfeasors. Sticha’s wife, one of the tortfeasors, was eighty percent at fault. Meyers, the second tortfeasor, was twenty percent at fault.\textsuperscript{177} The \textit{Sticha} court focused upon the “family” auto and allowed the UIM claim. The court quoted with approval “[i]t is well-established that first party coverages for which an insured pays a premium follow the person, not the vehicle. Policy exclusions which attempt to prevent the coverage from following the person are inconsistent with purposes of the Minnesota No-Fault Act.”\textsuperscript{178}

In \textit{DeVille v. State Farm Mutual Automobile Insurance Company},\textsuperscript{179} Mrs. DeVille was injured while a passenger on her husband’s mo-

\textsuperscript{174} See id. See also Vieths v. Illinois Farmers Ins. Co., 441 N.W.2d 575 (Minn. Ct. App.), \textit{rev. denied}, (Minn. 1989) (holding that children injured while on their father’s uninsured motorcycles when the motorcycles collided with each other were not entitled to UM coverage under their father’s policies insuring non-involved automobiles).

\textsuperscript{175} 374 N.W.2d 556 (Minn. Ct. App. 1985).

\textsuperscript{176} See \textit{Sticha}, 374 N.W.2d at 557.

\textsuperscript{177} See \textit{id}.

\textsuperscript{178} See \textit{id}. at 558 (quoting American Motorist Ins. Co. v. Saravela, 327 N.W.2d 77 (Minn. 1982)).

\textsuperscript{179} 367 N.W.2d 574 (Minn. Ct. App. 1985).
torcycle. Her husband was solely responsible for the accident. Mrs. DeVille had a separate policy of insurance on her cars. That policy excluded a vehicle "furnished for the regular use of you, your spouse or any relative" from becoming an uninsured motor vehicle. Mr. DeVille's motorcycle fell within that exclusion. The court of appeals refused to enforce the exclusion. The court limited Myers to situations "where the passenger had first collected the liability limits from the tortfeasor and then attempted to collect UIM coverage on the same or additional policies carried by the tortfeasor himself." UIM benefits were therefore payable.

Perfetti v. Fidelity & Casualty Company reached a similar result. In this case, Theresa Perfetti was injured while riding in an uninsured automobile driven by her brother, Steven. Both Theresa and Steven lived with their father, who had a separate Fidelity policy insuring his vehicle. The Fidelity policy contained an exclusion which provided that its UM coverage would not apply to "bodily injury sustained by any person while occupying any motor vehicle owned by [the policyholder] or any family member which is not insured for this coverage under this policy." The court invalidated the exclusion and distinguished Myers by stating:

Perfetti is not attempting to collect first-party benefits under the policy of the person who owned or insured the "at-fault" vehicle. She was injured in a vehicle owned by, but left uninsured by, her brother when he swerved to avoid an oncoming vehicle and struck a telephone pole. She has no third-party liability claim against her father, but merely claims uninsured motorist benefits under his policy. The exception based on prohibiting the conversion of first-party coverage into third-party coverage is therefore inapplicable.

180. See DeVille, 367 N.W.2d at 575.
181. See id.
182. See id.
183. See id.
184. See id.
185. See id. at 559.
186. Id. at 577.
188. See Perfetti, 486 N.W.2d at 441.
189. See id.
190. See id.
191. See id. at 443.
In *Linder v. State Farm Mutual Automobile Insurance Company*, (a 1977 accident) and *American Family Mutual Insurance Company v. Luhman*, (a 1983 accident) the injured parties were, similarly, seeking underinsured motorist coverage under separate policies. Neither were allowed to recover under the policies at issue.

In *Linder*, a minor was injured when struck by a pickup truck driven by her brother and owned by her father. All were residents of the same household. Linder recovered the liability coverage of the separately insured pickup truck and then sought to recover UIM benefits from two other policies issued to her father. She was denied UIM coverage on the basis of the family auto exclusion despite the fact that she was seeking coverage under a different policy.

In *American Family Mutual Insurance Company v. Luhman*, Luhman was injured when the car in which he was a passenger collided with a train. The car was driven by his mother, but it was insured by his step-father, Christensen.

Luhman, the injured person, lived with his mother and step-father. Luhman had his own insurance policy on his own car. Luhman sought to recover UIM benefits for the 1983 accident under his own insurance policy. The court of appeals denied his

See id.
claim of entitlement stating: "As this court explained in *Linder*, if the named insured wants substantial coverage when family members are injured while occupying... the named insured's vehicle, it is incumbent on the named insured to purchase sufficient *liability* insurance to cover such injuries." But what of the fact that his mother, and not the policyholder step-father, owned the vehicle? The court replied: "[w]hether Christensen or his wife owned the vehicle, the fact remains that Luhman is attempting to recover first party benefits from policies covering the person at fault where his appropriate remedy is to seek third party benefits from those parties."

2. Multiple Tortfeasors

If there is another motoring tortfeasor, unrelated to the claimant, there is no obstacle to collecting both the liability coverage and the underinsured motorist coverage under one single policy because there are then two distinct, separately insured "risks." One such risk involves the liability claim. If there is a second, unrelated vehicle which is also at fault, that other unrelated vehicle involves a separate risk. If that other vehicle were uninsured, UM coverage would be triggered. If the other vehicle were inadequately insured, it would trigger precisely the underinsured motorist "risk" for which the UIM coverage was issued.

*Lahr v. American Family Mutual Insurance Company,* 201 (*Lahr I*) held that a passenger injured in a multi-vehicle accident may recover underinsured motorist benefits from the insurer of the occupied vehicle if that other driver was underinsured. *Lahr I* seemed to recognize that there would be two separate tortfeasors, one triggering the BI coverage and one potentially triggering the underinsured (UIM) coverage.

After remand, fault percentages were assigned to both motorists. 202 The court of appeals in *Lahr II* qualified *Lahr I* by concluding that the determination of whether that other motorist is underinsured must be based upon that other vehicle's percentage of

---

199. See *Luhman*, 438 N.W.2d at 456 (quoting *Linder*, 364 N.W.2d at 483).
200. Id.
202. See *Lahr II*, 551 N.W.2d at 732.
fault.\(^\text{203}\) \text{Lahr II} agreed that the UIM could apply but refused to allow the application of joint and several liability principles to determine the UIM exposure.\(^\text{204}\)

\text{Jensen v. United Fire and Casualty Company}\(^\text{205}\) involved a claim for underinsured motorist coverage by a passenger in a one-car (pickup) accident. It might seem an unlikely case to discuss under the heading of “Multiple Tortfeasors,” but the case essentially raises the question of whether the owner is a separate tortfeasor.

In \text{Jensen}, the tortfeasor-driver was the claimant’s sister.\(^\text{206}\) The claimant and her sister lived with their father, Roger Jensen.\(^\text{207}\) The pickup truck was owned by the driver’s boyfriend.\(^\text{208}\) The boyfriend’s liability insurer and the father’s liability insurer paid their BI limits.\(^\text{209}\) The driver was an “omnibus insured” entitled to liability coverage under father’s policy when driving “non-owned” vehicles such as the pickup truck. The claimant passenger sought to recover UIM benefits on the father’s policy.\(^\text{210}\) That recovery was denied on the basis of a “reducing clause” which provided that “[a]ny [UIM] amounts payable will be reduced by: . . . any payment under the Liability Coverage of this policy.”\(^\text{211}\) Citing to \text{Myers v. State Farm Mutual Automobile Insurance Company},\(^\text{212}\) the court of appeals affirmed the denial of UIM benefits on the theory that allowing recovery would permit “conversion” of the policy’s UIM coverage into liability protection.\(^\text{213}\)

\text{Jensen} presented an unusual fact pattern. The at-fault vehicle was not owned by, furnished, nor available for the regular use by either father or daughter. However, the daughter drove the vehi-
The claimant thus argued that recovering UIM benefits should be allowed because the owner was not trying to convert inexpensive UIM into additional BI coverage. To that the court of appeals responded “[b]ut Jensen [father] did control the amount of liability insurance that policy provided for the driver of the pickup truck, Shanna Jensen [daughter-driver], and he could have increased that coverage by purchasing a larger policy.”

The inappropriate “conversion” was barred there not by the “family auto exclusion” but by a separate “reducing clause.” Nonetheless the essence of the court’s decision focuses upon avoiding “conversion” in much the same way as the court has applied the “family auto” exclusion.

2. “Geographic Exclusions:” Operating or Occupying an Owned but Uninsured Motor Vehicle or Motorcycle

What is the difference between a “family auto” exclusion and a “geographic” exclusion? The court sometimes uses the two terms to apply to the same exclusion. In both, the focus is upon delineating the scope of the underlying risk. Just as the family auto exclusion applied to a range of fact patterns, so too does the geographic exclusion. For example, the geographic exclusion is like the family auto exclusion in that it prevents an insured vehicle from also being considered uninsured or underinsured in other policies covering the injured person. It is unlike the family auto exclusion in that the at-fault vehicle need not be the “insured” vehicle. Thus, where the at-fault vehicle is owned by, furnished or available for the regular use of the insured, either exclusion applies. If the at-fault vehicle is some other vehicle, one neither owned by nor furnished for regular use by the insured or a family member, the family auto exclusion would not apply but a geographic exclusion may.

In a simple case of a one car accident injuring a passenger, the family auto exclusion operates to prevent the negligent use of one single vehicle from triggering both the liability and the UIM coverage. In that sense, there is one single risk which should be insured under liability coverage. The family auto exclusion prevents recovering both where such a restriction is consistent with the automobile insurance system in effect.

214. See id. at 537.
215. See id. at 538.
216. Id. at 539 (emphasis in original).
A geographic exclusion is only partially concerned with preventing an owned vehicle from being covered under the family's liability and its UM/UIM coverage. In its pure form, the geographic exclusion attempts to restrict the scope of coverage to injuries which occur only while occupying an insured vehicle. In a more moderate sense, the geographic exclusion operates only to deny access to a policy's UM or UIM coverage if the insured is operating another owned vehicle for which he should have purchased separate UM or UIM coverage. Thus, the most common application of a geographic exclusion is to prevent the extension of UM or UIM coverage from a policy covering specific vehicles so as to cover injuries sustained while the insured is using another owned vehicle for which UM or UIM coverage has not been purchased when the injury is caused by some other motorist. Geographic exclusions prevent the insurance from "following the person."

Nygaard v. State Farm Mutual Automobile Insurance Company discusses the geographic exclusion. In Nygaard, a consolidated case, two minors were injured by uninsured motorists while driving family owned motorbikes. The parties stipulated that the collision in each case gave rise to tort liability on the other uninsured motorist. That some other motorist would be uninsured is precisely the kind if risk which is covered under uninsured motorist policies unless there is an applicable exclusion. One such exclusion provided that the UM coverage did not apply: "(b) to bodily injury to an insured while occupying or through being struck by a land motor vehicle owned by the named insured or any resident of the same household, if such vehicle is not an 'insured automobile.'"

The Minnesota Supreme Court refused to enforce the exclusion. The court declared it invalid, reasoning that enforcing the exclusion would be inconsistent with the policies embodied in what was then the uninsured motorist statutes. The court stated:

The statute places no geographical limits on coverage and does not purport to tie protection against uninsured motorists to occupancy of the insured vehicle. Since our statute requires this broad coverage 'for the protection of persons,' we must leave to the legislature the sanctioning

217. 301 Minn. 10, 221 N.W.2d 151 (1974).
218. See Nygaard, 301 Minn. at 12-13, 221 N.W.2d at 152-53.
219. See id.
220. Id. at 12, 221 N.W.2d at 153.
of any exceptions dependent on the location of an insured.

As we held in *Northland Ins. Company v. West*, 294 Minn. 368, 373, 201 N.W.2d 133, 135, "uninsured motorist protection is not coverage for vehicles but for persons, even though it is contained in an insurance policy otherwise insuring an automobile. "If our interpretation of the intent of the uninsured-motorist statute is correct, little room is left for an insurer unilaterally to narrow the geographic scope of the statutorily required coverage. We therefore conclude that the trial court properly invalidated the exclusions in question as inconsistent with the requirements of the uninsured-motorist statute."^{221}

Minnesota's subsequent UM/UIM history dealt with geographic exclusions in the light of the then-existing UM and UIM laws. The following summarizes treatment of geographic exclusions leading up to the 1985 statutory change. The 1985 change effectively reversed the *Nygaard* rule that UM/UIM coverage primarily followed the person. Instead, post-1985 UM and UIM coverage may be said to primarily follow the vehicle. Further, the legislature in 1985 enacted two specific geographic exclusions to the statutory system which, by their terms, prevent the UM or UIM coverage from applying to injuries if the insured is occupying or using other owned vehicles.

a. **Pre-October 1, 1985 Law "Geographic Exclusions"**

Before October 1, 1985, Minnesota courts consistently refused to enforce policy exclusions which prevented UM and UIM coverages from following the person rather than the vehicle.^{222}

b. **Post-October 1, 1985 Law: Statutory Geographic "Exclusions"**

The 1985 law placed limits on the UM and UIM coverages when applied to (1) other motor vehicles owned by the insured

---

^{221} *Id. at 19, 221 N.W.2d at 156-57.*

and (2) motorcycles. These two statutory prohibitions against recovering UM or UIM benefits based upon occupancy of other owned vehicles accomplish a legislative "geographic" limitation upon the coverage. Before the 1985 legislative changes which enacted these provisions, courts tended to emphasize that the UM and UIM coverage "followed the person" with the result that such geographic limitations were void as against public policy. The 1985 statute not only validated the application of such previously-void policy exclusions and limitations but went one step further: the statute provided that the contractual UM or UIM coverage simply "does not apply" to injuries incurred while occupying such vehicles.

1. Motor Vehicle Owners

Section 65B.49, subdivision 3a(7) of the 1985 amendments imposes a geographical restriction on the scope of UM and UIM coverages. The statute is "designed to encourage motor vehicle owners to secure insurance on all of their vehicles."223 The provision became effective on October 1, 1985. It provides: "The uninsured and underinsured motorist coverages required by this subdivision do not apply to bodily injury of the insured while occupying a motor vehicle owned by the insured, unless the occupied vehicle is an insured motor vehicle."224

Subpart (7) effectively overruled Nygaard as to the "owner" of the uninsured vehicle.225 As the supreme court noted in Hanson v. American Family Mutual Insurance Company,226 the 1985 amendments "reflect a broad policy decision to tie uninsured motorist and other coverage to the particular vehicle involved in an accident."227 The plaintiff in Hanson, who was operating his own uninsured motorcycle, was, therefore, denied UM coverage under his auto policy.228

As noted above, this provision only applies to the "owner" of the occupied vehicle. Whether having legal title to the vehicle in one spouse's name would prevent the statute from applying when the vehicle is driven by the other is an open issue. Certainly, "in-

224. MINN. STAT. § 65B.49, subd. 3a(7) (1996).
226. 417 N.W.2d 94 (Minn. 1987).
227. Hanson, 417 N.W.2d at 96.
228. See id. at 95.
nocent passengers should not be denied coverage [as the] thrust of the statute is to encourage owners to insure all of their vehicles, which has nothing to do with passengers." 229

The 1985 statute does not prohibit resident relatives from collecting UM or UIM coverage under their own policies if they sustain injury while occupying the uninsured vehicle. 230 Resident relatives of the owner of an uninsured motor vehicle may, however, be prohibited from recovering UM or UIM benefits under policies insuring the owner's other vehicles under the "Family Auto Exclusion."

2. Motorcycle Owners

The No-Fault Act's definition of "motor vehicle" has always excluded motorcycles. 231 Motorcycles pose separate risks of injury; motorcycle owners are required to purchase liability insurance but not No-Fault, UM or UIM coverage. 232 Thus it is often the case that motorcycle owners would seek recovery for their injuries after the fact, seeking to collect on other policies where they were "insured." As noted above, prior to 1985, because the UM and UIM coverage was deemed to follow the person, the UM and UIM coverage from an automobile policy could be accessed by the injured motorcycle owner. That rule changed over time.

In Hanson v. American Family Mutual Insurance Company, 233 the plaintiff was injured by an uninsured motorist while operating his uninsured motorcycle. 234 He had no coverage on his motorcycle and looked to his American Family auto policy for UM benefits. 235 Hanson argued that section 65B.49, subdivision 3a(7) (which made the UM/UIM coverage inapplicable to motorcycle accidents) only applied to owners of "motor vehicles," and thus he could collect UM coverage from his car policy. 236 In essence, Hanson claimed that the legislature intended to exempt motorcycle owners

231. See MINN. STAT. § 65B.43, subd. 2 (1996) (defining "motor vehicle" as "every vehicle, other than a motorcycle . . . ") (emphasis added).
233. 417 N.W.2d 94 (Minn. 1987).
234. See Hanson, 417 N.W.2d at 95.
235. See id.
236. See id.
from the statutory exclusion. The court rejected Hanson's argument and held that the statute applied to motorcycle owners as well. The court found the legislative intent to be controlling over the literal terms of the statute.

The Hanson decision left open one important question: whether a motorcycle owner who procured liability insurance for the involved motorcycle but not UM or UIM coverages would be entitled to collect UM or UIM benefits under policies insuring non-involved cars.

The question was answered in Roering v. Grinnell Mutual Reinsurance Company, a 4-3 decision of the supreme court. In Roering, the court held that subpart (7) did not prohibit a motorcycle owner from recovering UIM benefits under an automobile policy because he had carried the mandatory liability coverage on the motorcycle. The court distinguished Hanson by noting that in Hanson the motorcyclist had failed to carry liability insurance.

For accidents occurring on or after August 1, 1990, the Roering rule has been legislatively overruled. Minnesota Statutes section 65B.49, subdivision 3a(8) now provides that “uninsured and underinsured motorist coverages . . . do not apply to bodily injury of the insured while occupying a motorcycle owned by the insured.” As a result, motorcycle owners cannot collect UM/UIM coverages on their auto policies. They must either purchase the coverage on their motorcycle policy or run the risk of suffering uncompensated damages.

3. Motorcycle Passengers

Section 65B.49, subdivision 3a(7) does not bar UM/UIM claims of motorcycle passengers. In Milwaukee Mutual Insurance Company v. Willey, Mathew Willey was injured by an underinsured

237. See id. at 96.
238. See id.
239. 444 N.W.2d 829 (Minn. 1989).
240. See Roering, 444 N.W.2d at 32-33.
241. See id. See also Johnson v. Western Nat. Mut. Ins. Co., 540 N.W.2d 78 (Minn. Ct. App. 1995). Under the law in effect in 1988, if at the time of an accident the injured person was occupying a fully insured motorcycle, the injured person was entitled to select any one limit of uninsured motorist coverage afforded by a policy under which the injured person was an insured. See id. at 80-81.
244. 481 N.W.2d 146, 147 (Minn. Ct. App. 1992).
motorist while a passenger on an uninsured motorcycle driven by his father.245 After recovering from the tortfeasor, he sought UIM benefits under his father’s auto policy with Milwaukee.246 The court of appeals held that Minnesota Statutes section 65B.49, subdivision 3a(7) did not bar the claim by noting that “innocent passengers should not be denied coverage . . . [as the] thrust of the statute is to encourage owners to insure all of their vehicles, which has nothing to do with passengers.”247 The court further stated in dictum that “any exclusion under the policy [which would prevent coverage] would be inconsistent with the statute . . . and therefore invalid.”248

Whether an auto policy must afford UM/UIM coverage for motorcycle passengers involved in accidents occurring on or after August 1, 1990 is an open question. Several insurers have amended their policy forms to specifically exclude coverage for injuries sustained while on motorcycles. Although subdivision 3(a) (7) will not bar the UM/UIM claims of passengers under the Willey case, the 1990 legislature also amended section 65B.49, subdivision 3a(5), the UM/UIM priority statute. The statute provides: “If at the time of the accident the injured person is not occupying a motor vehicle or motorcycle, the injured person is entitled to select any one limit of liability afforded for any vehicle by a policy under which the injured person is insured.”249

The history of the treatment of “family auto exclusions” and “geographic exclusions” in the UIM area shows the impact of different public policies. Even under the pre-1985 era, when UIM coverage was deemed to follow the person and not the vehicle, courts nonetheless applied and enforced the exclusions to avoid converting the UIM coverage into additional BI coverage for certain vehicles. Applying the pre-1985 accident cases to modern claims must be done with care to recognize that the post-1985 public policy links UIM coverage more heavily to the vehicle even, in some instances, to the point of simply declaring the UM/UIM coverage may not be claimed as a matter of statute.

245. See Willey, 481 N.W.2d at 147.
246. See id.
247. Id.
248. Id. at 148.
249. See MINN. STAT. §65B.49, subd. 3a(5) (1996) (emphasis added).
IV. CONDITIONS PRECEDENT TO MAKING A UIM CLAIM: TIMING, EXHAUSTION, NOTICE OF SETTLEMENT AND OTHER REQUIREMENTS

Understanding the concept underlying the state's underinsured motorist system in terms of what is compensable is only the beginning. UIM coverage is a supplement to the primary automobile liability insurance. That, in turn, applies to the tort obligation of an insured motorist. There are really three parties affected by any UIM claim: the injured motorist, the UIM insurer and the tortfeasor. All three have interests which exist, at one time or another, in relationship to one another. The process of resolving the underlying BI claim has an impact upon the UIM claim.

For example, if the injured party fails to recognize the contingent subrogation right of their UIM insurer, the UIM coverage may be forfeited as a result of how the underlying claim is resolved. The UIM insurer may forfeit its rights against the tortfeasor if it does not act to protect those rights, either by advancing payment under the UIM before the settlement stage is reached or by failing to respond to a Schmidt v. Clothier notice. If the UIM insurer does pursue subrogation against the tortfeasor, the process which has been followed between the UIM insurer and the injured person may, in turn, bear upon the ultimate tort liability of the at-fault motorist. All three players are involved, in one way or another, in a complex dance. Each party has certain rights and risks. Some of those rights and risks are affected by how the case is handled, the procedure followed or ignored.

Although certain of the UIM procedural aspects have been rather definitively pronounced, there remain certain areas of uncertainty and tension within the system. At least one such area of tension has its origins in the change from the "old" UIM law to the "new" UIM law. That has to do with the "gap" which results from below-limits settlements with the tortfeasor. Yet another, one which is just starting to emerge, has nothing to do with actual settlements but instead arises because the underlying tort claim may be resolved so as to produce a judgment—a judgment which does not seem to easily fit into the UIM doctrine.

250. 338 N.W.2d 256 (Minn. 1983).
251. As elsewhere in this paper, "old" refers to the UIM law in effect in 1983, the time the Schmidt v. Clothier case was decided. "New" refers to the current, post-1989 UIM law.
A. Timing of the UIM Claim: The Nordstrom Doctrine

Although there was considerable dispute over this issue for several years, it is now clear that a UIM claim cannot be pursued until after the liability claim has been resolved, either by way of tentative settlement (accompanied by notice to the UIM insurer in advance of the intention to settle) or by way of proceeding to tort judgment. In Employers Mutual Insurance Company v. Nordstrom,252 the supreme court held that until there has been a recovery from the tortfeasor, the UIM claim has simply not matured; a condition precedent to bringing a UIM claim has not been met before one of those two events. In order to preserve and initiate a UIM claim, the claimant must either (1) pursue the tort claim to conclusion in a district court action, and then, if the judgment exceeds the liability limits, pursue UIM benefits; or (2) settle the tort claim, give a Schmidt v. Clothier notice to the UIM carrier and then maintain a claim for UIM benefits.253

The Nordstrom rule is entirely consistent with the nature of UIM coverage as “excess” to any BI coverage. If a UIM claim could be pursued first, UIM coverage would become primary liability coverage, which “would be contrary to the designed role of underinsurance and to the underwriting principles on which it is written.”254

As far as the early stages of the UIM claim, at the point at which the claimant contemplates settlement of the claim with the insured tortfeasor, the law has become clear in terms of the procedures to be followed by both the UIM claimant and the UIM insurer. This paper will later address the lack of guidelines for the subsequent dealings between the UIM insurer, the tortfeasor, and the insured. There is a duty to proceed with the BI claim prior to bringing a UIM claim but also a duty to notify the UIM carrier of a tentative settlement, a right of a UIM carrier to “substitute its draft” in order to preserve its subrogation right, and various other rights and duties, all of which are interrelated. Several of those various aspects of the UIM procedures are discussed more fully in the sections which follow.

252. 495 N.W.2d 855 (Minn. 1993).
253. Nordstrom, 495 N.W.2d at 857.
254. Id. at 858; see also Johnson v. American Family Mut. Ins. Co., 426 N.W.2d 419, 422 (Minn. 1988) (“Underinsured motorist coverage is not an alternative to liability coverage.”).
The Nordstrom rule would provide that a tort judgment is binding upon the UIM insurer. However, providing that the underlying tort claim must first proceed to either tentative settlement or to judgment may assume too much. Is every "judgment" equally binding? What if the "judgment" lacks some of the protection which had earlier been afforded a UIM insurer? Those are the areas where some further testing of the limits may be expected.

The Nordstrom case represented the first serious question about whether the underlying tort judgment was binding upon the UIM insurer. Justice Simonett observed:

The typical underinsured contract provides, "We will pay damages which an insured is legally entitled to recover from the owner or operator of an [underinsured motor vehicle]." (Emphasis added.) See also Minn. Stat. section 65B.43, subd. 19 (1992). The tort judgment establishes conclusively the damages to which the claimant is "legally entitled"; if such damages exceed the tort insurance limits, the excess is payable by the underinsurer to the extent of its coverage without the need for arbitration. The underinsurer pays, not because it is estopped by the judgment, but because it has contractually agreed to pay the judgment less the tort liability insurance recovery.

This was initially challenged as dicta despite the fact that UIM coverage is intended to supplement the inadequate tort liability insurance of an at-fault motorist. If the amount of damages for which that motorist is legally obligated has been fixed, there would be no need (or opportunity) to relitigate or arbitrate the damages issue after a tort judgment.

Some of the reasons for the challenge to the new Nordstrom approach were aired in the subsequent case of Malmin v. Minnesota Mutual Fire & Casualty Company, as follows:

First, Minnesota Mutual asserts that an insurer would oth-

255. See Nordstrom, 495 N.W.2d at 858-59.
256. "'Underinsured motorist coverage' means coverage for the protection of persons insured under that coverage who are legally entitled to recover damages for bodily injury from owners or operators of underinsured motor vehicles." Minn. Stat. § 65B.43, subd. 19 (1996) (emphasis added). See also Minn. Stat. § 65B.49, subd. 4a (1996) (stating, "With respect to underinsured motorist coverage, the maximum liability of an insurer is the amount of damages sustained but not recovered from the insurance policy of the driver or owner of any underinsured at fault vehicle.") (emphasis added).
257. Nordstrom, 495 N.W.2d at 858-59.
258. 552 N.W.2d 723 (Minn. 1996).
erwise have to pay any judgment obtained by its insured, including default or consent judgments, even though the insurer was unaware of the pending lawsuit. Second, the tortfeasor's insurance carrier may have far less interest in defending against the injured party's suit than the UIM carrier. For example, if the tortfeasor has low liability insurance limits, the defending insurer has less incentive to vigorously defend the case, while the UIM carrier's financial exposure is increased. Thus, Minnesota Mutual contends that the UIM carrier should have the right to intervene and protect its financial interests. Third, Minnesota Mutual argues that it has a due process right to notice of the lawsuit under the United States Supreme Court's holding in *Fuentes v. Shevin*, 407 U.S. 67, 80 (1972). In short, Minnesota Mutual insists that it should not be required to pay Malmin's UIM claim because it was not allowed to participate in Malmin's lawsuit, it never expected that Malmin's injuries would result in such a large damages award, and it was never notified that Malmin intended to claim UIM benefits.\(^{259}\)

The court concluded:

Although Minnesota Mutual's arguments have some merit, a consent to sue provision is not a valid means of protecting the insurer's interests. While we agree that the insurer should receive notice of, and an opportunity to participate in, the insured's personal injury claim, we do not agree that the insurer can require its insured to seek written consent to sue before the insurer will be bound by the judgment.\(^{260}\)

After *Malmin* it would appear that the *Nordstrom* rule has, indeed, become the rule by which tort judgments will bind UIM insurers. Such a rule is comparatively simple and may apply where the tort judgment is the kind which follows full, fair litigation of the bodily injury claim and defense by the insured motorist. The UIM insurer in *Malmin* protested that it not be responsible for default or consent judgments.\(^{261}\) Even then, *Malmin* suggests that notice to the UIM insurer and opportunity to intervene would eliminate many of the concerns.\(^{262}\) Perhaps that is the message from the

---

259. *Malmin*, 552 N.W.2d at 726 (footnote omitted).
260. *Id.* at 728.
261. *See id.*
262. *See id.* at 728 n.4 (stating that providing a UIM carrier with notice of commencement of a liability suit "would permit the insurer to consider the nature
One of the increasingly common devices being used to resolve the underlying bodily injury claims is a form of “high-low arbitration.” That is an alternative dispute resolution device by which the parties (the BI claimant and the tortfeasor/BI insurer) agree to bracket the damages which might be awarded. The eventual award can be no less than the “low” amount nor any higher than the “high” figure. At that, the high-low arbitration agreement sounds like (and probably is) nothing more than a settlement device. However, most such high-low agreements are entered into in the context of a lawsuit and provide that the resulting arbitration award, somewhere within the bracketed range, may be reduced to “judgment.” That is done in order to make the resolution binding and secure payment. Would such a “binding” high-low arbitration agreement which provided that the resulting arbitration award would be reduced to “judgment” satisfy the Nordstrom rule? Or is that a situation where the label “judgment” presumes too much?

Consider what such a device does to the concerns of the UIM insurer. The moment the injured party signs the binding high-low arbitration agreement, the upper limit of the tortfeasor’s liability has been capped. (Usually that is set at or below the BI limits.) Is the resulting stipulated award figure binding upon the injured party? If so, then if it is “capped” at a dollar sum at or below the BI limits, perhaps the injured party has effectively waived UIM claims. If the underlying resolution (via such an ADR device) is not binding upon the injured party but if the injured party may instead claim that his or her damages exceed the capped amount, how can that be reconciled with the obligation of the UIM claimant to do nothing to prejudice the UIM insurer’s subrogation rights? Would it be consistent with the UIM system to ignore such a “judgment” altogether? Even if the award was considered of no force and effect in terms of binding the UIM insurer to pay, what about the fact that such high-low agreements provide a “binding” defense to the tortfeasor? Doesn’t the unilateral action of an injured party, to give the tortfeasor such a defense, amount to the

263. The UIM insurer’s subrogation rights were a prime concern in the delicate balancing performed by the Minnesota Supreme Court in Schmidt v. Clothier, 338 N.W.2d 256 (Minn. 1983). See supra notes 51-66 and accompanying text.
same as signing a release?

The high-low arbitration agreement is but one of the current devices being used, oftentimes with active pressure from the trial courts, to resolve the tort claim. That pressure, and the current acceptance of ADR procedures generally, contributes to some tension in the UIM system. How the courts treat them will have to be determined by the same balancing the Minnesota Supreme Court undertook in *Schmidt v. Clothier.*264 The tortfeasor has interests and expectations, usually relating to whether that tortfeasor will be released from further exposure (either to the injured party or to that party’s subrogated UIM insurer). The injured claimant wants to be able to process his or her bodily injury claim.

To a great extent, the high-low arbitration agreement is much like a “tentative settlement.” Perhaps, then, the court will apply the *Schmidt v. Clothier* concepts at the time of the making of the high-low agreement, reasoning that once the agreement is signed, subrogation rights have been waived irrespective of the dollar amount fixed by the arbitrator. In *Schmidt v. Clothier,* the UIM insurer’s interest in subrogation was considered an important right.265 All of those factors were juggled by the *Schmidt v. Clothier* court; the interests all remain with the result that further review of the impact of a high-low arbitration agreement upon UIM entitlement will have to consider all of the interests.

B. The Insured’s Failure to Exhaust the Liability Coverage is not an Absolute Bar to Maintaining a UIM Claim: The Schmidt v. Clothier Requirement

In order to recover UIM benefits, the tortfeasor must, of course, be underinsured, meaning that the damages the insured is legally entitled to recover from the tortfeasor must exceed the tortfeasor’s BI limits.266 However, an insured need not exhaust the BI limits in order to preserve a UIM claim. In 1983, the supreme

---

264. *See supra* notes 51-66 and accompanying text.

265. *See Schmidt,* 338 N.W.2d at 261-62. In many cases it is “important” as a principle without regard to the exact dollar significance. Gradually, the focus has shifted to whether the UIM insurer has suffered actual “prejudice” as a result of the injured party’s actions. *See American Family Mut. Ins. Co. v. Baumann,* 459 N.W.2d 923, 926-27 (Minn. 1990) (explaining that failure to provide notice will not result in forfeiture of UIM coverage if the settling claimant can overcome the presumption that UIM coverage will be forfeited by showing that UIM insurer has not been prejudiced).

court in *Schmidt v. Clothier* held void UIM policy provisions which indicated that the insured could not collect UIM coverage if the tortfeasor’s BI limits were not first exhausted. 267

In 1985, the Minnesota State Legislature tinkered with the idea of incorporating a statutory exhaustion clause which would have provided that:

The uninsured and underinsured coverages required by this subdivision do not apply to any bodily injury until the limits of bodily injury liability policies applicable to all insured motor vehicles causing the injury have been exhausted by payment of judgments or settlements and proof of such is submitted to the insurer providing the uninsured and underinsured motorist coverages. 268

This exhaustion provision was, however, eliminated during a 1985 Special Session. 269 As a result, the fact that the insured settles with the tortfeasor for an amount below the tortfeasor’s limits will not constitute an automatic bar to bringing a UIM claim.

Another question is whether UIM claims will be allowed in every case where the insured settles for an amount below the tortfeasor’s BI limits. Some below-limits liability settlements may be so far below the BI limits that no reasonable person could consider the tortfeasor to be underinsured. The supreme court’s opinion in *Employers Mutual Insurance Company v. Nordstrom*, discussed below, suggests that the determination of whether a UIM claim can be made, and the extent to which benefits would be payable, may be dependent upon whether the insured has made the “best possible settlement” with the tortfeasor’s insurer. 270 What constitutes the “best possible settlement” within the meaning of the *Nordstrom* case is also discussed below.

C. The “Best Possible Settlement” and Responsibility for “the Gap” in Below-Limits Liability Settlements

In *Schmidt v. Clothier*, the court held that exhaustion clauses were invalid. 271 At the same time, however, the court held that the UIM carrier would be entitled to deduct the full BI limits from the


269. *See id.*

270. 495 N.W.2d 855, 858 (Minn. 1993).

271. 338 N.W.2d 256, 261 (Minn. 1983).
insured's damages, regardless of the amount recovered in the liability settlement. The insured could not recoup the difference or "gap" between the tortfeasor's BI limits and the liability settlement from the UIM carrier. The Schmidt holding was consistent with the excess nature of UIM coverage; the UIM carrier only had to pay the damages which were above the tortfeasor's limits. That, in any event, was the UIM system in place in 1983 when the court balanced the competing and legitimate interests of the UIM claimant and the UIM insurer. The rationale for this rule was explained by the Schmidt majority as follows:

Practically, the insured would have no incentive to obtain the best settlement if he or she [were] assured of recovering the "gap" from the underinsurer. Use of underinsured benefits in this way runs counter to the agreement of the parties . . . [and] might also lessen the incentive of the liability carrier to make its best offer to the claimant. Three justices dissented. They suggested that these risks could be avoided without imposing any hardship upon the UIM carrier by simply requiring the insured to "negotiate the best possible settlement" and inform the UIM carrier of the proposed settlement. If the UIM carrier was not satisfied with the proposal, "the offer should be rejected, the underinsured carrier should immediately pay the amount of the offer to the injured party, and they should immediately proceed to arbitration."

In 1985, the legislature changed the calculation of UIM benefits from the old "add-on" (damages less BI limits) basis to a "limits less paid" basis. In Broton v. Western National Mutual Insurance Company, the court felt that this change, coupled with the legislature's rejection of an exhaustion provision, had "effectively codified the position of the Schmidt dissenters, who had argued that an insured who communicates the tortfeasor's settlement offer to the UIM insurer should be entitled to recover the gap from the UIM in-

272. See Schmidt, 338 N.W.2d at 261.
273. See id.
274. See id.
275. Id. at 261.
276. See id. at 264.
277. Id. (Todd, J., joined by Amdahl, C.J., & Scott, J., concurring and dissenting).
278. Id.
279. 428 N.W.2d 85, 90 (Minn. 1988).
As a result, responsibility for the “gap” was shifted to the UIM carrier for all policies issued or renewed on or after October 1, 1985. If the tortfeasor was “underinsured,” (i.e., the damages that the insured was legally entitled to recover from the tortfeasor exceeded the tortfeasor’s BI liability limits), the insured could attempt to recover the “gap” between the liability settlement and the tortfeasor’s BI liability limits from the UIM carrier. The 1989 laws did not alter responsibility for the “gap.” As a result, primary responsibility for the “gap” still rests with the UIM carrier.

In Onasch v. Auto-Owners Insurance Company, the court noted that while an insured need not exhaust the tortfeasor’s liability limits, “the injured party [nevertheless] retains the primary responsibility of negotiating a reasonable settlement with the tortfeasor’s insurer before turning to his or her own UIM coverage.” The court noted that this negotiation requirement was mandated by Broton: “Indeed, the dissenters in Schmidt, whose position the 1985 legislature and the Broton court adopted, stressed that ‘[t]he injured party should negotiate the best possible settlement’ with the tortfeasor’s insurer before seeking the available UIM coverage.”

What will constitute the “best possible settlement” within the meaning of Nordstrom has not been resolved by the appellate courts. The holding of Schmidt v. Clothier was that a UIM claimant could, in some cases, make a below limits settlement while preserving a UIM claim. However, in Schmidt and the Hoag case, which was consolidated with Schmidt, it was apparent that each injury not only exceeded the BI limits but that the tortfeasor(s) had already paid sums in excess of the BI limits. The damages in Schmidt were admittedly in excess of $250,000 while the BI limits of $100,000 had been tendered. In Hoag, one tortfeasor had paid $22,000 out of the $25,000 BI limits while another jointly liable tortfeasor had paid $4,000 out of its limits. The total of $26,000 illustrated that even in Hoag the situation presented an underinsured motorist scenario. The supreme court approved the settlement technique when it had

280. Broton, 428 N.W.2d at 90.
282. Onasch, 444 N.W.2d at 590.
283. Id. (citations omitted).
284. 338 N.W.2d 256, 261 (Minn. 1983).
285. See Schmidt, 338 N.W.2d at 259-60.
286. See id. at 259.
287. See id.
before it clearly underinsured situations. But, are there liability settle-
mements which do not involve multiple claimants and which are so far below the tortfeasor's liability limits that the courts will not even permit a UIM claim to be made? Can an insured, for example, settle with the tortfeasor's liability insurer for fifty percent of the available liability coverage where liability is not disputed and still maintain that the tortfeasor was underinsured?

In Nordstrom, the court noted that it had previously suggested in Broton v. Western National Mutual Insurance Company,288 that "some of the circumstances under which a claimant with a tort claim worth more than the tort insurance limits might settle with the tortfeasor's insurer for less than the policy limits," and still pursue a UIM claim.289 The relevant language from Broton is as follows:

An injured claimant does not always receive the full limit of the tortfeasor's liability insurance even though the claimant's damages exceed the policy limits. The insurance may be exhausted by the claims of other persons injured in the same accident. Or the limits of the tortfeasor's liability insurance may be distributed among multiple claimants in such fashion that no one claimant receives the full per person limit. Questionable liability may make settlement for the full amount of the tortfeasor's insurance impossible although the parties might be able to reach a suitable compromise.290

As the "gaps" grew after the 1985 UIM law took effect, underinsured motorist insurers were presented with UIM claims where the amount of BI insurance "left on the table" was rather significant. United States Automobile Association v. Morgan,291 an unpublished case, spotlights but does not resolve the tension caused by such below limits settlements.

In Morgan, Morgan's husband was killed by a truck which was insured with liability limits of $500,000 per person/$1,000,000 per accident.292 There was $500,000 of liability insurance available to respond to a tort judgment.293 However Morgan chose to settle for

288. 428 N.W.2d 85 (Minn. 1988).
292. See id.
293. See id.
50% of that amount, $250,000. Morgan then made claim to her UIM insurer. USAA had $500,000 of UIM limits. USAA’s objection was that, if the motorist was truly underinsured, USAA was being asked to begin paying at $250,000 which was one half of the BI insurance available.

USAA commenced a declaratory judgment action, arguing that Morgan’s settlement for half the liability limits was not the “best possible settlement” required to trigger its UIM obligation. The issue presented a question of law to be reviewed de novo. Two of the judges on the court of appeals panel relied heavily upon the purely mechanical application of the prior Schmidt v. Clothier rule, stating:

If United Services determined that the settlement was not representative of Morgan’s damages, it should have substituted its payment to preserve its subrogation rights. We believe the procedures and limits for UIM claims, as currently set out in the statutes, Schmidt, Nordstrom, and other cases provide adequate protection for United Services’ interests in under insurance claims.

Judge Davies took a more philosophical view of the dilemma faced by the UIM insurer in such a case. He agreed that the issues of UIM entitlement should, pursuant to Washington v. Milbank Insurance, be decided in arbitration as opposed to declaratory judgment. He commented further, in part, as follows:

I write separately, however, because precedent cases may suggest that appellant should, in the UIM proceeding that lies ahead in this case, be precluded from challenging the reasonableness of respondent’s tort settlement. I do not believe that to be the case, for such result is wholly impractical and substantively wrong... I believe it to be implicit in our rejection of this declaratory judgment pro-

---

294. See id.
295. See id.
296. See id.
297. See id.
298. See id. The court’s footnote in Morgan reads as follows: “The phrase ‘best possible settlement’ comes from the requirement that ‘[t]he injured party should negotiate the best possible settlement’ with the liability carrier before proceeding with a claim for under insurance benefits. Schmidt v. Clothier, 338 N.W.2d 256, 264 (Minn. 1983) (Todd, J., concurring and dissenting).” Id. at *1 n.1.
299. See id. at *3.
300. See id. (Davies concurring).
301. 562 N.W.2d 801, 802 (Minn. 1997).
302. See Morgan, 1997 WL 360595, at *3 (Davies concurring).
ceeding—and implicit, too, in the supreme court decision in Washington—that an insurer must be able to challenge a UIM claimant's improvident Schmidt v. Clothier tort settlement by some means other than by declaratory judgment.\(^{303}\)

In musing upon the subject of the UIM insurer's dilemma regarding settlements which are substantially below limits, Judge Davies also addressed the change in UIM law following Schmidt v. Clothier. The legislature responded in 1985 to the problems of multiple claimants and insurer insolvency, stating that UIM insurance covered the difference between the loss and the amount the claimant actually realized from the tort claim.\(^{304}\)

In the post-1985 UIM system, Judge Davies considered that, "[f]ailing to give UIM insurers the ability to question Schmidt v. Clothier settlements puts into the hands of UIM claimants an intolerable weapon; claimants are permitted to settle tort claims at a discount (small or substantial) and, by doing so, impose a dilemma on the claimant's UIM carrier."\(^{305}\) Seemingly the majority concluded differently, suggesting that "substitution" was the only alternative.\(^{306}\) In the wake of this unpublished, and divided, court of appeals decision, what is an UIM insurer to do? Is the door open for challenge to the "best settlement" in front of the arbitrators? Or, if the policy does not compel arbitration, is that an issue for the jury which decides the UIM case? These are some of the unresolved pressures, often vented by UIM insurers, which arise because of substantially below limits settlements occurring in Minnesota's current UIM system, where the "gap" is presumably shifted to the UIM insurer.\(^{307}\)

\(^{303}\) Id.

\(^{304}\) Id. at *4 (footnote omitted).

\(^{305}\) Id.

\(^{306}\) See id. at *3.

\(^{307}\) Judge Davies' concurrence goes further and suggests that there ought to be two different types of "gaps," either "coverage gaps" or "liability-based gaps." See id. at *4. In his view:

Gaps created because of exhausted coverage or insurer insolvency are legitimate "coverage gaps" resulting from a best settlement. But gaps created by settlements founded on uncertain liability or comparative fault are "liability-based gaps" and represent settlements that do not meet the best-settlement standard. A UIM insurer must compensate its insured for a "coverage gap"—one that falls within its contractual obligation. But the insurer has no obligation to cover a "liability-based gap;" those gaps are outside the insurance contract.

Id.
The alternative view, of course, is that the "best settlement" is whatever the injured person believes it to be. In that case, the future significance of the "best settlement" as a precondition to making a UIM claim will be nonexistent.

More than anything else, the change which "shifted the gap" from the insured (under the old law) to the UIM insurer (under the new law) fuels the drive for clear guidelines. Whether and to what extent UIM benefits are payable following a below-limits settlement will be the subject of appellate decisions over the next few years. Hopefully, the appellate courts will fashion some guidelines. Yet, uncertainty in the law weighs against the establishment of any hard and fast rules. The very fact that the law is in a state of flux serves a purpose: it creates an incentive on the part of the insured to obtain the full liability limits or risk losing the UIM coverage. This, in turn, reduces the likelihood that UIM coverage will become a form of primary coverage, contrary to its designed role and the underwriting principles on which it is based.

V. SUBSTITUTION BY A UIM INSURER: IS IT A MEANINGFUL RIGHT?

Schmidt v. Clothier\(^ {308} \) balanced the competing interests of the injured claimant, the tortfeasor and the UIM insurer. In doing so, the supreme court emphasized a key element: a UIM insurer may "substitute" an amount equal to the tentative BI settlement in order to preserve subrogation rights.\(^ {309} \)

At the time Schmidt v. Clothier was decided, the right to substitute was not intended to prevent the UIM insurer from paying amounts of damages which were within the tortfeasor's BI limits. Substitution in 1983 was not necessary to shift back to the BI insurer exposure for the dollar sum of the damages less than the BI limits. The Schmidt-era UIM system provided that the UIM insurance started at the point where the BI limits left off. If there was a below-limits settlement, that "gap" was "eaten by the settling plaintiff." The UIM exposure was, in the event of a below-limits settlement, less than is the UIM exposure under Minnesota's current UIM system. The difference lies in the amount of the gap. The gap amount was, in effect, another deduction available to the UIM insurer at the time of Schmidt. Today, the gap is an element which the claimant seeks from the UIM insurer. What the UIM substitu-

\(^{308}\) 338 N.W.2d 256, 258 (Minn. 1983).

\(^{309}\) Id. at 263.
tion provided, at the time of *Schmidt*, was a method by which the UIM insurer could pursue recovery of the UIM payment, that amount by which the damages exceeded the tortfeasor’s BI limit, thereby reducing net exposure by recovering some amount of the UIM payment.

Currently, UIM insurers are increasingly presented with tentative BI settlements which are substantially less than the BI limits as a precursor to a UIM claim. The same dynamic which allows a claimant to settle for substantially less than the BI limits has a corollary impact upon the UIM insurer. Specifically, the UIM insurer protests that, to the extent the UIM insurer is expected to pay the “gap,” such settlements are unfair to the UIM insurer because the UIM insurer must pay amounts which are the responsibility of the BI insurer. The primary, if not the exclusive, response of the courts is that if the UIM insurer does not want to be responsible for the gap, then it ought to substitute. 310 Presumably the thinking of the courts is that if the UIM insurer substitutes, somehow the ultimate responsibility for the gap will be shifted back to the BI insurer so that the UIM insurer is not, ultimately, responsible for sums which are less than the BI limits. 311

But just what is the right of subrogation of a UIM insurer after substitution? Is it truly an effective means by which the UIM insurer may “square accounts?” Or is it, under the current UIM system, more illusory than real? This section, while not a comprehensive analysis of all UIM substitution/subrogation issues, raises some practical concerns about the feasibility of UIM subrogation after substitution. The conclusion is that, practically speaking, subrogation by a UIM insurer after contesting the validity of a UIM claim is a comparatively hollow right.

What is UIM substitution? The UIM substitution is basically a payment made by the UIM insurer in the amount of the BI offer. The payment made by the UIM insurer is to preserve a subrogation right; it is not a payment out of the UIM coverage. The full UIM coverage remains intact to respond to the UIM claim. Some practical problems exist for UIM insurers when it comes to funding a


311. Minnesota law, even during the current UIM era, still provides that UIM coverage is intended to supplement inadequate BI coverage. If there is sufficient BI coverage to compensate the injured person, resort to UIM coverage is not allowed. But should these rules apply where the result is to shift responsibility for large portions of the damages which were within the BI limits to the UIM insurer?
substitution: most insurance payments must be reserved against specific coverages. Substitution requires a bit of creativity on the part of the insurer to justify a payment which could be many thousands of dollars.

Beyond the requirement that the UIM insurer must make payment in kind, matching the offer, the cases offer little guidance as to the rights of the UIM insurer and the claimant after the payment. If the offer to settle the BI claim is not the offer of money but instead is a structured settlement, the UIM insurer would have to match that offer in kind.

As UIM insurers began to receive notice of UIM claims and saw the insureds contemplating settling for substantially less than the BI limits, they looked to ways to prevent paying. One theory was that if the UIM insurer substituted there would be no “settlement” of the underlying BI claim, rendering the UIM claim premature. Put another way, some argued that if the UIM insurer would only “match the offer,” then the injured party and the tortfeasor/BI insurer would have to litigate the underlying tort claim to judgment. This interpretation arose in response to the insurer’s frustration in being forced to “drop down” so as to begin paying at the point where the tentative settlement left off. It did not survive appellate review. Essentially, substitution by the UIM insurer amounted to substitute performance. The result was that the underlying claim of the injured person against the tortfeasor was settled. What substitution preserved was the right of the UIM insurer to subrogate. But before there is subrogation, the UIM claim must proceed between the UIM insurer and the injured person.

Can the UIM insurer join the tortfeasor in that proceeding? On the one hand, doing so brings all interests into the case. That would result in a single determination as to liability and the amount of damages which would be binding upon the injured person, the tortfeasor and the UIM insurer. Theoretically, the UIM exposure is measured by the same factors. If the tortfeasor is a party, there will be one single determination reached—avoiding the risk that the same case, the same liability and damages factors, may be weighed differently by two separate tribunals. Joinder of

312. A structured settlement is a settlement where the consideration is not a payment of money to the injured party immediately but instead a contractual commitment to make payments over time, typically secured by the purchase of an annuity.
the motorist to the UIM claim also avoids duplication of effort.

On the other hand, a frequent objection to joining the tortfeasor to the UIM claim is that a defendant is entitled to trial without the jurors knowing, directly, that he or she had liability insurance. And, too, the UIM claim is a contract claim despite being measured by the same factors as the tort claim. Joinder poses some challenge to all concerned. No clear rules have emerged to provide a uniform method of handling the divergent interests.

What of the risk of divergent outcomes, one in the contest between the injured person and the UIM insurer and another in the subrogation claim by the UIM insurer? Is that a real risk? If two separate trials produce roughly the same outcome, there is less justification for "joinder" of the tortfeasor. But is it realistic to predict that the outcome of the UIM trial and a subsequent subrogation trial of the UIM subrogation will bear any resemblance? There are some practical concerns which cast serious doubt on that assumption, to the point where one must ask whether UIM subrogation is, under the current UIM system, a meaningful remedy for the UIM insurer which has paid "the gap" amounts.

The practical difficulties start with the issue of who is the "real party in interest" in a UIM subrogation suit? Washington v. Milbank Insurance Company effectively held that in any UIM subrogation effort the UIM insurer is the real party in interest. Just what must

314. 562 N.W.2d 801 (Minn. 1997).
315. See Washington, 562 N.W.2d at 805-06. Determination of the real party in interest is a function of whether the UIM insurer has responded to a tentative BI settlement or whether, on the other hand, the UIM insurer has made a pre-settlement payment to the injured party. See O'Donnell v. Brodehl, 435 N.W.2d 68, 70 (Minn. Ct. App.), rev. denied, (Minn. 1989). In O'Donnell the UIM insurer anticipated that O'Donnell's damages would exceed the tortfeasor's BI limits and decided to make a payment of the $25,000 UIM limits before the BI claim was made. See id. at 69. In exchange for the early tender of the UIM limits, O'Donnell executed an agreement assigning to Westfield, the UIM insurer, his potential claims arising from the accident. See id. O'Donnell then commenced suit against tortfeasor Brodehl. See id. Brodehl's BI insurer eventually offered $90,000 out of its $100,000 BI limit in settlement. See id. When O'Donnell sought court approval of the BI settlement, UIM insurer Westfield moved to intervene. See id. The trial court applied what it thought to be the rule of Schmidt v. Clothier and insisted that Westfield match the $90,000 offer or waive its subrogation rights. See id. at 70. The court of appeals reversed, indicating that a UIM insurer need not substitute for a settlement amount to protect its subrogation right if it has paid UIM benefits before settlement with the specific purpose of preserving those subrogation rights. See id. at 70-71. Westfield, the UIM insurer, thus continued to have a right against the tortfeasor. See id. And, since its insured was willing to settle his personal claim for $10,000 less than the BI limits, presumably Westfield could thereafter assert its
the UIM insurer prove in its subrogation claim? Presumably, the UIM insurer would have to prove all of the elements of the tort claim against the defendant, both liability and damages. Presumably that means the UIM insurer cannot prove its UIM payment but instead must prove the damages which the injured party sustained. Doing so poses some interesting challenges. The UIM insurer in such a situation will be put to the task of proving each and every element of the very injury claim the UIM insurer likely challenged in the context of the UIM claim. The defendant tortfeasor, in such a case, would relish the prospect of using all of the UIM defense ammunition (such as an independent medical examination obtained and used by the UIM insurer) in its defense. By attributing the source of the defense material to the very UIM insurer which makes claim against the tortfeasor, the BI defendant gains significant leverage in the contest of persuading the jury as to liability or damages.

The UIM insurer contemplating substitution and then subrogation finds itself in a dilemma. If the UIM insurer defends against the UIM claimant, the risk is that all of the defense efforts will be used to impeach the subsequent UIM subrogation claim. And if the UIM insurer does not defend against the UIM claim, the risk is that the UIM recovery will be greater than it would be if the UIM insurer defended itself.

Nor is there much solace for a UIM insurer who substitutes and then prevails in the UIM defense. Consider the practical problems of subrogating to recover the amount of the UIM substitution in the following hypothetical:

Assume the injured party presses a BI claim against a tortfeasor with $50,000 of BI coverage limits. Assume the injured party reaches a tentative BI settlement of $35,000 and gives the requisite Schmidt v. Clothier notice to the UIM insurer who, to preserve subrogation rights, substitutes its payment for a matching $35,000 payment. Assume further that the UIM insurer "succeeds" in defending itself against the UIM claim as a result of which the claim against the tortfeasor and hope to recover the $10,000 which was "left on the table." The process followed, prior to the settlement, involved the injured party, O'Donnell, as the real party in interest for all practical concerns.

In Washington v. Milbank, the UIM insurer used a "loan receipt agreement" but did so as the instrument to document its post-BI settlement substitution. See 562 N.W.2d at 806. In that case, the court was not willing to ignore that the "loan" took place after the tentative BI settlement rather than before. See id.
jury fixes the damages at $30,000. In such a case, the motorist would not be underinsured and the UIM insurer would pay nothing. But would the UIM insurer be able to recover its $35,000 payment?

The hypothetical illustrates some of the problems of having different dollar figures assessed to a single case in two separate forums. In this hypothetical, the $30,000 figure which was fixed by the jury in the UIM claim may well prevent the UIM insurer from claiming that its insured sustained losses in excess of $30,000.316 Nor is it likely that the UIM insurer could recover the $35,000 from its insured.317

To the extent that fairness is measured by the proposition that both the UIM and BI determinations would always be measured in the same way and with the same results, there are practical problems to obtaining such symmetry in the system. Some imbalance is to be expected. It is not realistic to assume an identical outcome if the "same case" is tried twice with two different "real parties in interest," one the injured party and the other the subrogated UIM insurer. The issue is whether subrogation actions following UIM substitutions provide a meaningful opportunity for UIM insurers to recover for the amounts of the UIM payments which are payments for the "gap" amounts. Practically speaking, the difficulties faced by UIM insurers in pursuing direct subrogation make recovery very problematic. And, if the UIM insurer must pursue subrogation in its own name against the tortfeasor in a setting where the tortfeasor may use all of the UIM insurer's efforts to defend the subrogation claim, it is not hard to predict that the UIM insurer will often fail in its subrogation recovery efforts. Because of that reality, the question remains whether the "right" to subrogate in an effort at shifting the "gap" back to the BI insurer is more than illusory.

316. "Collateral estoppel precludes the relitigation of issues which are both identical to those issues already litigated by the parties in a prior action and necessary and essential to the resulting judgment." Ellis v. Minneapolis Comm'n on Civil Rights, 319 N.W.2d 702, 704 (Minn. 1982).

317. Gusk v. Farm Bureau Mut. Ins. Co., 559 N.W.2d 421 (Minn. 1977) was a combined UM and UIM claim. The facts made it somewhat unique, but the supreme court held that after a jury verdict, a UIM insurer may not demand a "refund" of substitute drafts paid out pursuant to Schmidt v. Clothier. Id. at 424.
VI. THE SOURCE OF PAYMENT OF UM/UIM COVERAGE: OLD AND NEW COMPARED

There is no secret that the 1985 legislative changes to the UM/UIM statute radically altered the prior rules by which Minnesota law determined which policy and what dollar amount was available to an injured person. Professor Michael Steenson, commenting on the 1985 amendments, explained:

The statutory priority scheme now applicable to uninsured and underinsured motorist insurance claims substantially restricts the availability of multiple uninsured motorist insurance coverages. Stacking has been curtailed, and the statute now provides precise guidance in determining the source of coverage for the payment of uninsured and underinsured motorist insurance benefits.\(^{318}\)

In addition, the Minnesota Court of Appeals observed near the time of the change:

Before 1985, an insured in Minnesota was permitted to add together the coverage limits of two or more policies when the insured’s losses were not fully covered by one policy (citation omitted). Commonly called ‘stacking,’ this process of adding coverages together occurs when a court orders the ‘pyramiding of separate first party coverages attributable to two or more vehicles despite policy language prohibiting stacking.’\(^{319}\)

Chapter ten of the 1985 special session laws became the 1985 changes to the UM/UIM statute. With only minor changes over

---

318. MICHAEL K. STEENSON, 1 MINNESOTA NO-FAULT AUTOMOBILE INSURANCE 231 (2d ed. 1996).
319. Austin Mut. Ins. Co. v. Templin, 435 N.W.2d 584, 586 (Minn. Ct. App. 1989). Templin involved a short-lived form of “multiplied limits” or “contractual stacking.” That odd variant, not involved here, depended upon language in commercial automobile insurance policies which was not silent or neutral on “stacking” nor did the language attempt to prevent stacking. Id. at 587. Instead, the particular language found there provided a form of contractual multiplication of the UM or UIM limits. Id. At issue in Templin was whether the “multiplied limits” language became instantly void when the 1985 “anti-stacking” law became effective. The court of appeals stated that “We agree that In Re State Farm held that Chapter 10 outlawed stacking. Nevertheless, even if Chapter 10 outlawed judicially imposed stacking, it did not outlaw contracting for the right to add together underinsured motorist coverages.” Id. (emphasis in original.) The court there concluded that “The 1985 Legislature outlawed the practice in which courts order stacking despite policy language prohibiting it, but permitted stacking by agreement of policyholder and insurance company.” Id.
the next twelve years, chapter ten is the UM/UIM statute with which we deal at the present. Access to underinsured and uninsured motorist coverage is controlled by the same statutory system. Thus any cases dealing with UM access or UIM access flow from the same statutory system and, with rare exceptions not pertinent here, may be used interchangeably.

What is worth noting, in the context of this paper and its attempt to identify areas where the "rules" have been changed, is how the pre-1985 cases laid down "rules" or interpreted policy provisions in ways which are at odds with the new statutory system. The key philosophical change that occurred was discussed above: prior to 1985, the UM and UIM coverages were considered to "follow the person." After the 1985 changes, the risk (and thus the source of the UM or UIM coverage) essentially "followed the vehicle." In addition, there were other more subtle, but nonetheless important, effects of the 1985 changes.

"Stacking" of all potentially available UM and UIM coverage was abolished. Moreover, its underlying assumptions no longer operated. It was no longer dispositive that a person was an "insured" under several policies (once as occupant/omnibus insured, once as named insured and again by virtue of being a "resident relative" with another insured person). After 1985, the legislature linked UM/UIM entitlement and the source more closely to specific vehicles, and insurance limits decisions made by the vehicle owners for themselves and their families.

Instead of aggregating all available UM or UIM insurance (such that the total available was the total of all similar UM/UIM insurance) the statute specifically linked recovery to the dollar sums elected by the owner/insured. If recovery was allowed under more than one policy, a different form of aggregation was specified, one whose goal is usually to bring the total available UM or UIM coverage up to the total limit chosen by or for the injured per-

320. Chapter ten was later codified as Minn. Stat. § 65B.49 (1996).
321. See Minn. Stat. § 65B.49, subd. 3a (1996).
322. See id. subd. 3a(6):

Regardless of the number of policies involved, vehicles involved, persons covered, claims made, vehicles or premiums shown on the policy, or premiums paid, in no event shall the limit of liability for uninsured and underinsured motorist coverages for two or more motor vehicles be added together to determine the limit of insurance coverage available to an injured person for any one accident.

Id.
son on their own policy. For example, if a person selected $50,000 per person of UM coverage, in most instances that sum was available. If the person were riding in someone else’s automobile when struck by a phantom/uninsured motorist, the injured person would first collect the UM coverage on the occupied vehicle. If that was less than the limit the injured person had selected on his or her own policy, the person was allowed to supplement the primary UM coverage in order to bring the total up to the amount which had been selected by the injured party. This was a lesser result, and a very different result, than the pre-1985 “stacking” of UM (or UIM) coverage.

“Geographical limitations” were also imposed through the statute. These statutory limitations reversed a body of law which had allowed injured persons to access other policies even though they were occupying or using a vehicle they owned but did not insure.

How does this set of 1985 changes play into any difficulties faced in resolving UM or UIM entitlement questions? Although the changes took effect years ago, there remains a large body of UM and UIM case law which is based entirely upon the pre-1985 philosophy. The insurance policy forms in use today are somewhat different from those in use before the 1985 changes. However many of the same terms, definitions, and exclusions remain. Those terms have radically different meanings when interpreted with the pre-1985 and post-1985 concepts in mind. Nonetheless for the casual researcher (or the advocate) there remains a body of law which seems to interpret the same terms today for claims arising after the 1985 changes. In seeking to apply any of those cases to current fact situations, it is important to note the philosophical (and even the mechanical) rule changes since 1985. Some of the specific changes wrought by the 1985 changes to the “source” rules for both UM and UIM coverage are discussed below.

A. Source Rules for UM and UIM Coverages

1. Pre-October 1, 1985 Law

During the UIM “add-on” era of 1975 to 1985, the source of coverage for both UM and UIM benefits flowed from the very broad definition of a “covered person” or “insured” person in the insurance policy. Not only was a person covered under the policy
insuring the vehicle they were occupying but, in addition, they were often insured by name in their own policy and quite possibly as a "resident relative" under the policy of family members with whom they lived. An injured claimant could generally aggregate or "stack" the UM or UIM coverages under any insurance policy in which the claimant was identified as a "covered person" or "insured."\(^{323}\)

Because of the potential for overlapping coverages, it was often necessary to determine the order of priority among the various coverages. In *Holman v. All Nation Insurance Company*, the supreme court followed its decision in *Integrity Mutual Insurance Company v. State Automobile & Casualty Underwriters Insurance Company*,\(^{324}\) and held that UIM coverages, like UM coverage, would be stacked "in order of their closeness to the risk."\(^{325}\) The "closeness to the risk" doctrine was summarized by the *Integrity Mutual* court as follows:

The nub of the Minnesota doctrine is that coverages of a given risk shall be "stacked" for payment in the order of their closeness to the risk. That is, the insurer whose coverage was effected for the primary purpose of insuring that risk will be liable first for payment, and the insurer whose coverage of the risk was the most incidental to the basic purpose of its insuring intent will be liable last. If two coverages contemplate the risk equally, then the two companies providing those coverages will prorate the liability between themselves on the basis of their respective limits of liability.\(^{326}\)

Minnesota courts have applied the *Integrity Mutual* rule in a number of subsequent decisions.\(^{327}\) The general rule which emerged was that the UM and UIM coverage on the involved motor vehicle would provide primary coverage. If the damages exceeded the limits of liability on the occupied host vehicle, additional cover-

\(^{323}\) See *Holman v. All Nation Ins. Co.*, 288 N.W.2d 244 (Minn. 1980).

\(^{324}\) 307 Minn. 173, 239 N.W.2d 445 (1976).

\(^{325}\) *Holman*, 288 N.W.2d at 251.

\(^{326}\) *Integrity Mut. Ins. Co.*, 307 Minn. at 175-76, 239 N.W.2d at 447.

age could then be “stacked” to compensate the injured claimant in the following order: coverage where the injured claimant was a named insured was second in line for payment and coverage where injured claimant was identified as an additional insured by virtue of resident relative or spousal status was last in line for payment. In this manner, the insurer whose coverage was affected for the primary purpose of insuring the risk was liable first for payment, and the insurer whose coverage was most incidental to the risk was last in line for payment.

2. Post-October 1, 1985 Law

The 1985 amendments created Minnesota Statutes section 65B.49, subdivision 3a(5), which established a two-tier priority system that governs access to, and order of payment for, UM and UIM coverages. For the first time the statutes provided a formula-like approach to determining the source of UM/UIM coverage. Minnesota Statutes section 65B.49, subdivision 3a also plays a role in specifying which insurance is, or is not, applicable to a given situation. The essence of the statutory source system is that every injured person must make their UM or UIM claim to the insurer of the vehicle they are occupying. If UM or UIM coverage is available to the occupant of that vehicle, and if that limit is less than the limits which the injured person would otherwise have available, then the injured person may make claim for the difference, the amount by which the excess policy limit exceeds that which was available on the occupied vehicle. For those who are not occupying a vehicle (or those who occupy a vehicle which is the uninsured or underinsured motor vehicle) the statute allows the injured person to select any one policy where they are insured.

The priority system was designed to accomplish two legislative goals:

1. The system attempted to assign liability for UIM and UM coverage to the insurance carrier which more closely contemplated the risk of injury. In this regard, the legislation codifies prior case law which imposed liability upon the insurer who was “closest to the risk,” in other words, the insurer of the host vehicle in which the injured person was riding when struck by an uninsured or underinsured motorist.

328. MINN. STAT. § 65B.49, subd. 3a(5) (1996).
329. Id. subd. 3a(6) - (8).
tortfeasor. The Minnesota Supreme Court has noted that the 1985 amendments have codified the Integrity Mutual doctrine. \(^{330}\)

2. The system attempted to ensure that the *minimum* level of coverage that would be available would be the limit of UM or UIM coverage purchased by the policyholder. This intention is evidenced by the fact that a host passenger is able to look to his or her own personal policy for excess coverage when the coverage on the occupied vehicle is issued in an amount less than the insured’s UM or UIM coverage limits.

The statutory source system encompasses situations where the insured is in his or her own vehicle, riding in another insured vehicle or even is a pedestrian.

*a. Primary Coverage for Occupants of Motor Vehicles*

Following prior case law, the UM/UIM priority system creates a distinction based upon the relationship, or absence thereof, of the claimant to a motor vehicle. Primary UM or UIM coverage for occupants of motor vehicles is generally provided by the insurance policy covering the occupied vehicle. The principal priority statute, Minnesota Statutes section 65B.49, subdivision 3a(5), reads, in part, as follows:

> If at the time of the accident the insured person is occupying a motor vehicle, the limit of liability for uninsured and underinsured motorist coverages available to the injured person is the limit specified for that motor vehicle. \(^{331}\)

This statute requires that occupants of motor vehicles first look to the insurance coverage afforded by the policy insuring the host vehicle. \(^{332}\) Then, if the injured person’s damages are not fully compensated by the UM/UIM coverage on that occupied vehicle, the injured person may, in certain cases, be entitled to “surplus” insurance protection under one of their own insurance policies. \(^{333}\)

If the injured person is an “insured” of the policy covering the occupied vehicle, that policy will, with one exception, afford the sole and exclusive source of UM/UIM coverage. No surplus cover-

\(^{330}\) Thommen v. Illinois Farmers Ins. Co., 437 N.W.2d 651, 653 (Minn. 1989).
\(^{331}\) MINN. STAT. § 65B.49, subd. 3a(5) (1996).
\(^{333}\) MINN. STAT. § 65B.49, subd. 3a(5) (1996).
age can be sought. This follows from one of the principal purposes of the 1985 legislative changes—to allow individuals to select their own level of available insurance protection, (protection which was tied to the vehicle) and to prevent the shifting of insurance from one vehicle to another. Thus if an insured owned two vehicles, insuring one for minimum UM/UIM limits only but insuring the second for higher limits, the use of the specific vehicle will determine which UM/UIM policy applies. If the insured uses the vehicle for which he or she chose the minimum limits, then that selection is respected: only that UM/UIM limit applies. The insured injured while riding in a vehicle they own may not tap into UM/UIM on any other vehicle. This is also closely related to the purpose behind the statute—that UM/UIM coverages do not apply if the insured sustains bodily injury while occupying a motor vehicle owned by the insured, unless the occupied vehicle is an insured vehicle and do not apply if the insured sustains bodily injury while occupying a motorcycle owned by the insured.

The principle is the same: the insuring selection made by the insured for that particular vehicle will be enforced. If the insured selected no coverage, he or she will not be allowed to shift the UM/UIM risk to another policy on a non-involved vehicle. Unless the insured chose to purchase UM/UIM coverage for a motorcycle owned by the insured, the owner may not shift that risk to the insurance on a non-involved automobile. These rules are consistent with the Minnesota legislature's 1985 action forbidding the "stacking" of UM/UIM coverages. It is consistent with the elimination of stacking that the insurance selection for the particular owned vehicle is enforced.

b. Surplus Coverage for Occupants of Motor Vehicles

In LaFave v. State Farm Mutual Automobile Insurance Company, Mrs. LaFave was injured by an uninsured motorist while a passenger in her husband's vehicle. Mr. LaFave was also injured. The

---

334. Id. subd. 3a(7) & (8) (emphasis added)
335. Id. subd. 3a(8) (emphasis added).
336. Id. subd. 3a(6). The court of appeals noted that the statute which became the current "source" system "is an absolute prohibition on stacking of uninsured and underinsured motorist coverage . . . ." In re State Farm Mut. Auto Ins. Co., 392 N.W.2d 558, 566 (Minn. Ct. App. 1986).
337. 510 N.W.2d 16 (Minn. Ct. App. 1993).
338. LaFave, 510 N.W.2d at 17.
339. See id.
vehicle was insured by St. Paul Fire & Marine under a policy issued to Mr. LaFave that afforded a single UM limit of $100,000. Mrs. LaFave was not a named insured under that policy but qualified as an insured because she was a resident spouse and because she was occupying the vehicle. The LaFaves settled the UM claim with St. Paul Fire for $81,250 and Mrs. LaFave then sought surplus UM coverage from State Farm under a policy issued to her which afforded $50,000 of UM coverage. The court of appeals held that Mrs. LaFave could not recover surplus coverage under section 65B.49, subdivision 3a(5) because she qualified as an insured under the St. Paul Fire policy insuring the occupied vehicle. Why could Mrs. LaFave not recover under her own policy? The answer lies in the rules governing "surplus" UM/UIM coverage.

It is important to note that the statute only requires the injured "claimant to look first to the [UM/UIM] coverage" on the occupied vehicle. The statute does not mandate that the policy covering the host vehicle will always provide coverage. Coverage under the policy insuring the host vehicle may not be available if an enforceable exclusion, such as the family auto exclusion, bars coverage for the claim. In such a case, the injured person may be entitled to look to his or her own automobile policy for UM or UIM benefits because there is no like coverage which is available on the occupied vehicle.

The 1985 statute allowed passengers in host vehicles to recover some amount of surplus insurance protection under their own insurance policies. The ability to seek surplus UM/UIM coverage was designed to allow policyholders to pre-select the minimum level of insurance coverage that would be available for any given accident. Without such a provision, an insured's ability to protect and safeguard his or her destiny would be subject to the insuring responsibility of other motor vehicle owners and operators over

340. See id.
341. See id.
342. See id. at 17-18.
343. See id. at 19.
345. See id. at 654.
346. See id.
whom the injured person has no control. Minnesota Statutes section 65B.49, subdivision 3a(5) states, in part:

However, if the injured claimant is occupying a motor vehicle of which the injured person is not an insured, the injured person may be entitled to excess insurance protection afforded by a policy in which the injured party is otherwise insured. The excess insurance protection is limited to the extent of the covered damages sustained, and further is available only to the extent by which the limit of liability for like coverage applicable to any one motor vehicle listed on the automobile insurance policy of which the injured person is an insured exceeds the limit of liability of the coverage available to the injured person from the occupied motor vehicle.349

The statutory system allows access to an insured’s own policy limit in certain circumstances. However access is limited to the extent that the insured’s own policy limit exceeds the primary policy limit. The full policy limit of the “excess” policy is not available except in the limited case where there is no UM/UIM available on the occupied vehicle. If the full UM/UIM limits of the secondary policy were laid on top of the limits of the host/primary UM/UIM policy, the result would be stacking. The 1985 statutes prohibited stacking of UM/UIM.350

Minnesota allows the insured to “supplement” the amount of UM/UIM available on the host/primary policy in order to bring the total amount of UM/UIM up to the level selected by the insured. Such a system respects the selection made by the insured while also recognizing that the UM/UIM coverage follows the vehicle with the result that “primary” UM/UIM coverage is that written for the occupied vehicle. For example, if an individual selects and pays for $50,000/$100,000 of UM or UIM coverage, that amount should usually be available. If that individual were injured while occupying a friend’s car (which friend insured for UM/UIM coverage only to the minimum amount of $25,000/$50,000) when struck by a phantom or uninsured motorist, the statute determines the source(s) of UM coverage as follows:

1. First the insured collects the host vehicle’s $25,000 as the “primary” UM policy.
2. Second, if the injuries exceed that sum, the insured may turn to his/her own pre-selected limit of

349. Id. § 65B.49, subd. 3a(5) (emphasis added).
350. See id. subd. 3a(6).
$50,000/$100,000. Because that insured selected $50,000 of UM coverage per person, and because he or she has available $25,000 per person on the host vehicle, there is a maximum of $25,000 more of UM coverage available from the injured person's own policy. ($50,000 surplus limit reduced by the limit on the host/primary policy.) The net effect of "supplementing" the host vehicle's UM/UIM limit is to bring the total up to the selected level.

To this extent, then, UM and UIM coverage may be described as a form of "limits less limits" coverage. That term originally referred to reducing the UIM limits by the BI limits. That is not Minnesota's current system. However, it is an apt description of the working of Minnesota's UM/UIM "surplus" system.

Surplus coverage is generally available only when the limit of UM or UIM coverage on the host vehicle is less than the limits afforded to the occupant under a separate insurance policy. It is not available where the occupant's per person UM/UIM limits are equal to or less than the per person limits on the occupied vehicle.

If the full per person UM/UIM limits of the primary coverage are available to indemnify the injured person, the injured person should not be able to collect excess UM or UIM coverage unless his or her damages exceed the primary UM/UIM carrier's maximum exposure. The statute also makes it clear that if the injured person settles with the primary UM or UIM carrier for an amount less than the available limits, the injured person will not be entitled to recover the "gap" between the primary UM/UIM limits and the settlement amount from the surplus UM/UIM carrier. Excess coverage is available only to the extent its limit exceeds the limit of liability of the coverage available to the injured person from the oc-

352. See id.
354. "Gap" here is different from that which results from an injured person's electing to settle for less than the full BI limits. The "gap" here results from the statute's specifying that the surplus UM or UIM is available to the extent that the surplus "limit" exceeds the primary "limit." The gap is not created by policy language or by the decisions of the claimant when settling. The "gap" exists, if at all, only because the serendipitous coverage on the occupied vehicle is less than the pre-selected UM/UIM limit of the injured person's own (surplus) policy.
occupied motor vehicle. The insured will have to "eat the gap" between the primary coverage limits and the amount of the settlement.

The statute does not, however, necessarily require that the full UM or UIM limits on the occupied vehicle be set off against the surplus limits in all cases. The statute only authorizes the reduction of the excess coverage limits by the amount of coverage which was actually "available" on the occupied vehicle. The statute expressly states that an injured person may look to his own UIM or UM protection if its limit "exceeds the limit of liability of the coverage available to the injured person from the occupied motor vehicle." The UM/UIM limits on the occupied vehicle may not be "available" to the injured person for a number of reasons:

1. The primary limits may be non-existent as a result of an enforceable exclusion to coverage. For example, the host vehicle's UIM coverage will not be "available" if the host vehicle is the underinsured motor vehicle.

2. The primary UM/UIM limits may be exhausted or depleted by other persons injured in the same accident.

The surplus coverage provision was designed to allow policyholders the opportunity to pre-select the minimum level of insurance coverage that would be available for any given accident. In order to ensure that this purpose is not defeated, the excess carrier should only be entitled to set-off the amount of primary UM/UIM coverage that was actually available to the injured person.

It would seem that the Minnesota UM/UIM system is preserved if the surplus UM/UIM carrier is given credit for the amount of the host/primary UM/UIM which was legitimately "available" to the insured. In other words, if the insured was one of several injured in a vehicle, and if the host vehicle's UM limits were fairly divided, then the surplus UM/UIM insurer is responsible for a maximum of its limit less the amount that was "available" to the insured from the host vehicle. It is unfair to the insured who selected and paid for a policy limit to eliminate that coverage.

355. MINN. STAT. § 65B.49, subd. 3a(5) (1996) (emphasis added).
356. See, e.g., Thommen v. Illinois Farmers Ins. Co., 437 N.W.2d 651, 654 (Minn. 1989) (finding that the policy definition of "underinsured motor vehicle" did not include a vehicle furnished for the use of a third party); Davis v. American Family Mut. Ins. Co., 521 N.W.2d 366 (Minn. Ct. App. 1994) (holding that allowing an injured person "to recover both liability and UIM under the same policy... would, in essence, be allowing an individual to increase liability coverage by purchasing less expensive underinsured coverage").
At the same time, however, the same sense of fairness would prohibit the insured from "gerrymandering" the host vehicle's UM or UIM coverage so as to unfairly prejudice the secondary UM or UIM insurer. For example, it would seem improper for the multiple occupants of an insured vehicle to divide the primary UM/UIM limits so as to unfairly reduce the credit due to certain surplus insurers. In such a case, it is entirely possible that the court would follow the "limits less limits" approach. In that event, the gerrymandering insured could end up with nothing from the surplus carrier as a result of overreaching.

Any allocation of the primary UM/UIM limits among multiple claimants must not be done to the prejudice of the surplus insurance carrier. Although there is no case law which so provides, wisdom (and extension of the Schmidt v. Clothier reasoning) suggests that the excess carrier should be provided with notice of the tentative allocation prior to releasing the primary carrier so as not to prejudice the excess carrier's rights.

c. **Primary Coverage for Pedestrians (those not occupying a motor vehicle)**

If the injured person was not "occupying" a motor vehicle or motorcycle at the time of the accident, the injured person will seek benefits under a different source rule. In that event, the injured person is entitled to claim against one policy limit amount under any one policy wherein he or she "is insured." Minnesota Statutes section 65B.49, subdivision 3a(5) states, in part:

> If at the time of the accident the injured person is not occupying a motor vehicle or motorcycle, the injured person is entitled to select any one limit of liability for any one vehicle afforded by a policy under which the injured person is insured.

By incorporating the statutory definition of "insured" into

357. See generally Eckblad v. Farm Bureau Mut. Ins. Co., 371 N.W.2d 78, 81 (Minn. Ct. App.) (holding that "[t]he remaining nonsettling parties are still entitled to pay uninsured motorist coverage in the proportion they would have paid had [the primary insurer] not settled."); rev. denied, (Minn. 1985); see also Liberty Mut. Ins. Co. v. Crow, 451 N.W.2d 898, 901 (Minn. Ct. App. 1990) (stating that "[w]here a plaintiff settles with a defendant who may be liable for the plaintiff's damages, the settlement cannot be done to the prejudice of the remaining nonsettling defendants.").

358. 338 N.W.2d 256, 261 (Minn. 1983).

359. MINN. STAT. § 65B.49, subd. 3a(5) (1996).
subpart (5), the legislature probably intended the term to serve as a means of identifying the policy which will provide UM/UIM coverage when there is more than one policy of insurance covering members of the same family unit. The statutory definition serves the identical function under the economic loss benefits priority system of Minnesota Statutes section 65B.47. 360 The comments of the Uniform Motor Vehicle Accident Reparations Act (UMVARA), upon which the No-Fault Act was modeled, are illustrative:

This qualification [of not being named as an insured under another policy] serves to ameliorate the problems of identifying the policy which provides coverage where there is more than one basic plan of reparation security covering members of the same family unit. 361

The Minnesota Supreme Court used the UMVARA rationale in a case where the injured claimant sought economic loss coverage as an additional insured while identified by name in his own plan of reparation security. In Bock v. Mutual Service Casualty Company, the case consolidated with and reported in Wasche v. Milbank Mutual Insurance Company, 362 the court held that the statutory definition of “insured” precluded Clark Bock from collecting basic economic loss benefits under his father’s policy because Clark was identified as a named insured in his own policy. 363 The court, therefore, refused to consider Clark an “insured” under his father’s policy within the meaning of section 65B.47, subdivision 4(a) which provided that the “security for payment of basic economic loss benefits applicable to injury to an insured is the security under which the injured person is an insured.” 364

Bock may provide sufficient support for interpreting the term “insured” in the UIM and UM priorities system to serve as a means of identifying and assigning UM and UIM coverage to the appropriate insurer under subdivision 3a(5). Although Bock involved a different priority system, the need for consistency between the various types of benefits mandated by the Act has been a continuing focus of Minnesota courts. Applying Bock would promote the legislative purpose of assigning liability to the insurance carrier

360. Id. § 65B.47.
361. UNIF. MOTOR VEH. ACCIDENT REPARATIONS ACT § 1, 14 U.L.A. 41, commentary at 45 (1990).
362. 268 N.W.2d 913, 920 (Minn. 1978).
363. See Wasche, 268 N.W.2d at 917 n.4.
364. MINN. STAT. § 65B.47, subd. 4(a) (1996) (emphasis added).
which more closely contemplated the risk of injury.

The injured resident relative wishing to forego his/her own policy, on the other hand, would argue that the insurer could have clearly avoided coverage by excluding resident relatives who are named as insureds under their own insurance policies. However, this argument begs the issue of whether the term “insured” in the priority statute was intended to refer to the statutory definition or a policy definition. If the former, as appears to be the case, it should not matter whether the policy definition would cover the resident relative: the question is whether the resident relative is even entitled to access that policy. At the same time, however, for some of the same reasons underlying the “family auto exclusion,” there may be circumstances when the relationship was so close that the decision to insure at a certain dollar limit may be considered jointly made. In such a case, it is possible that the spouse may not be able to access his/her own policy as a result of the interplay of the definitions of “insured,” “underinsured motor vehicle” and possibly policy language setting out the scope of the policy’s application.

The “source” system accomplishes several significant changes by which the “source” of UM/UIM coverage is determined in Minnesota. Applying pre-1985 cases to post-1985 accidents should be done with some care to avoid confusion because the philosophical underpinnings of the state’s UM/UIM system were modified in 1985.

VII. CONCLUSION

Understanding the working of Minnesota’s underinsured motorist system must begin with realization that there have been several underinsured motorist systems in effect in the state, each one with different philosophical objectives. Although certain principles have remained constant, some of the fundamentals have been radically changed over time. The result is that many precedents, and the rules they embody, cannot be meaningfully applied in today’s underinsured motorist system. The careful balancing of rights which led to the Schmidt v. Clothier procedure for the beginnings of a UIM claim may have to be considered anew with some questions in mind for the latter stages of a UIM claim. For example, is substi-

365. See generally Burgraff v. Aetna Life & Cas. Co., 346 N.W.2d 627, 630 n.2 (Minn. 1984) (defining insured to include “any relative or relatives of the named insured who is a resident of the same household”).
tution a meaningful option for a UIM insurer when the underlying claim has been settled for a substantial discount? Should the UIM insurer have some defenses to paying the “gap” in any case? As the parties and the courts work to define rules by which the injured person, the underinsured motorist insurer, the liability insurer and even the at-fault motorist must relate to one another within today's UIM system, they must recognize just what system was in place when those earlier cases were decided. The challenge will be to balance the legitimate rights and obligations of all affected parties with the current system's philosophical objectives in mind to articulate rules which relate, meaningfully, to the behavior and dynamics which the current UIM system creates.