St. John's Law Review

Volume 54
Number 3 *Volume 54, Spring 1980, Number 3*

Article 13

Carrier's Release from Future Liability Effected by Employee's Third Party Recovery Held Not a Benefit for Consideration in Apportioning Litigation Expenses

Paul R. Williams

WORKER'S COMPENSATION LAW

Carrier's release from future liability effected by employee's third party recovery held not a benefit for consideration in apportioning litigation expenses

Section 29(1) of the Worker's Compensation Law (WCL) provides that an employee injured in the course of his employment through the fault of one other than his employer or fellow employee may pursue a third party action for damages without compromising his statutory entitlement to compensation.[285] In order to ensure the continued viability of the compensation system, however, the compensation carrier is afforded a lien upon the proceeds of any recovery to the extent of the benefits previously paid to the employee.[286] Where the carrier seeks to satisfy such lien out of the proceeds of a judgment or settlement procured through the efforts

---

tisement. *See id.* It is submitted that the vagueness of these rules detract from their value as purported standards to be followed by the advertising attorney.

It should be noted that proposed rule 9.3 permits solicitation on a limited basis. It provides, in part, that "a lawyer may initiate contact with a prospective client . . . [b]y a letter concerning a specific event or transaction if the letter is followed up only upon positive response by the addressee . . . ." ABA MODEL RULES OF PROFESSIONAL CONDUCT § 9.3 (1980). This provision apparently would sanction the type of letter sent by the defendants in *Koffler*.

[285] N.Y. WORK. COMP. LAW § 29(1) (McKinney Supp. 1979-1980). Originally, an employee had to choose between bringing his action against the third party or receiving payments from the compensation carrier. Ch. 816, § 29, [1913] N.Y. Laws 2293. The employee's election to receive compensation benefits constituted an automatic assignment of the tort cause of action of the carrier. *Id.*; Curtin v. City of New York, 287 N.Y. 338, 340, 39 N.E.2d 903, 904 (1942). The practical consequence of this election was that injured employees, financially unable to await the uncertain outcome of litigation, would "choose" to receive the compensation payments. *See* Gegan, *The Compensation Carrier's Right to Restitution for Medical Expenses Through a Lien on the Employee's Tort Recovery*, 52 ST. JOHN'S L. REV. 395, 401 (1978); 7 FORDHAM L. REV. 282, 282 (1938). The abolition of this forced election allowed the employee to collect his benefits without surrendering his right to bring a third party suit. Ch. 684, § 29, [1937] N.Y. Laws 1556 (McKinney). *See also* Gegan, *supra*, at 401.

[286] *See* N.Y. WORK. COMP. LAW § 29(1) (McKinney Supp. 1979-1980). The compensation carrier's lien was an outgrowth of the 1937 amendment to section 29(1) of the WCL designed to prevent a double recovery by the employee and to provide the carrier with an opportunity to recoup payments already made to the employee. *See* Granger v. Urda, 44 N.Y.2d 91, 97, 375 N.E.2d 380, 382, 404 N.Y.S.2d 319, 321 (1978); Becker v. Huss Co., 43 N.Y.2d 527, 538, 373 N.E.2d 1205, 1207, 402 N.Y.S.2d 980, 982-83 (1978); Curtin v. City of New York, 287 N.Y. 338, 342-43, 39 N.E.2d 903, 905 (1942); Gegan, *supra* note 284, at 401-02. The lien attaches to any recovery, whether by judgment or settlement, arising from the injury which originally generated the compensation payments. *See* Ryan v. General Elec. Co., 26 N.Y.2d 6, 9, 256 N.E.2d 188, 189, 307 N.Y.S.2d 880, 881 (1970); Petterson v. Daystrom Corp., 17 N.Y.2d 32, 39, 215 N.E.2d 329, 332, 268 N.Y.S.2d 1, 3 (1966).

of the injured employee, a 1975 amendment to the statute requires that the expenses incurred in the prosecution of the action, including attorneys' fees, be "equitably apportioned" between the employee and the carrier.[287] Despite the simplicity of the statutory mandate, however, no clear guidelines have been established to govern either the manner of the apportionment or, more importantly, the relative benefits upon which the apportionment is to be based.[288] Recently, however, in *Castleberry v. Hudson Valley*

---

[287] Ch. 190, § 29(1), [1975] N.Y. Laws 293-94 (McKinney) added to the statute the following:

> Should the employee or his dependents secure a recovery from such other, whether by judgment, settlement or otherwise, such employee or dependents may apply on notice to such lienor to the court in which the third party action was instituted . . . for an order apportioning the reasonable and necessary expenditures, including attorneys' fees, incurred in effecting such recovery. Such expenditures shall be equitably apportioned by the court between the employee or his dependents and the lienor.

N.Y. WORK. COMP. LAW § 227(1) (McKinney Supp. 1979-1980)(disability benefits), was similarly amended to provide for apportionment of legal expenses. Ch. 190, § 227, [1975] N.Y. Laws 294 (McKinney).

The 1975 Amendment was designed to eliminate two basic inequities which existed in the WCL. *See* Memorandum of the Law Revision Commission Relating to the Apportionment of Attorneys' Fees in Third-Party Actions Under the Workmen's Compensation Law §§ 29 and 227, [1975] N.Y. LAW REV. COMM'N REP., *reprinted in* [1975] N.Y. Laws 1551, 1552 (McKinney) [hereinafter cited as 1975 Memorandum]. First, compensation liens were being fully satisfied without the carrier sharing the costs of the recovery. *Id.* at 1552. Second, where the third party recoveries were modest in amount, employees were left with little, if any of the proceeds after the attorney's lien and the compensation lien were paid. *Id.*

The amendment of section 29(1) of the WCL brought New York in line with an increasing number of states favoring apportionment of legal expenses incurred in a third party suit between the employee and the employer's compensation carrier. *Id.* at 1553; 2A A. LARSON, WORKMEN'S COMPENSATION LAW § 74.32 (1976 & Supp. 1979); Atleson, *Workmen's Compensation: Third Party Actions and the Apportionment of Attorney's Fees*, 19 BUFFALO L. REV. 515, 539 (1970).

[288] By wording the statute to provide for "equitable" apportionment, the legislature avoided the adoption of a fixed formula to be applied in each case, opting instead for a more flexible scheme to be utilized by the trial court which is entertaining the third-party action. *See* 1975 Memorandum, *supra*, note 287, at 1553. Indeed, in Becker v. Huss Co., 43 N.Y.2d 527, 373 N.E.2d 1205, 402 N.Y.S.2d 980 (1978), it was noted that since the statute was designed to allow trial court discretion, it would be the rare case where the trial court's determination would be subject to review on appeal. *Id.* at 544, 373 N.E.2d at 1211, 402 N.Y.S.2d at 986. The *Becker* Court enumerated several factors to be weighed in determining the carrier's equitable share of the expenses, including the reasonableness of the lawyer's retainer, whether the retainer was influenced by the knowledge that the carrier would be shouldering part of the costs, the overall difficulty or ease of the case, and any other equitable circumstances. *Id.* at 543, 373 N.E.2d at 1211, 402 N.Y.S. 2d at 986.

Two formulas for computing the carrier's share of the attorneys' fees have evolved in the lower courts. Under one approach, the carrier's proportionate share is equal to the

Asphalt Corp.,[289] the Appellate Division, Second Department, had occasion to construe the apportionment provision, holding that the carrier's release from future liability effected by the recovery in the third party action is not a benefit upon which the apportionment of attorneys' fees may be based.[290]

Plaintiff Castleberry had been injured in the course of his employment and was receiving weekly payments from his employer's compensation carrier.[291] Subsequently, he brought a third-party action against the defendant for his injuries, which was ultimately settled for $75,000 without the carrier's consent or a judicial compromise order.[292] Pursuant to the apportionment of costs provision of section 29(1), the plaintiff thereupon petitioned the Supreme Court, Orange County to extinguish the full amount of the carrier's lien.[293] The plaintiff argued that since all of the recovery inured to the carrier's benefit by discharging its liability for future payments, the carriers should absorb the entire $25,000 in legal fees incurred in settling the third party suit.[294] The lower court, agreeing with the plaintiff's contention, granted the motion, but limited the carrier's equitable share of the expenses to the amount of its lien.[295]

---

amount of the carrier's lien multiplied by the ratio of the attorney's fee to the total recovery. Rice v. Bankers Trust Co., 83 Misc. 2d 797, 798, 374 N.Y.S.2d 87, 88 (Sup. Ct. Kings County 1975). The alternative computation method is to multiply the amount of the total legal fees by the ratio of the lien to the total recovery. Wargo v. Longo, 85 Misc. 2d 898, 900, 380 N.Y.S.2d 1009, 1012 (Sup. Ct. Albany County 1976). Under either method, however, the result is the same. *See* Castleberry v. Hudson Valley Asphalt Corp., 70 App. Div. 2d 228, 245 n.4, 420 N.Y.S.2d 911, 923 n.4 (2d Dep't 1979) (Shapiro, J., dissenting).

[289] 70 App. Div. 2d 228, 420 N.Y.S.2d 911 (2d Dep't 1979).

[290] *Id.* at 238, 420 N.Y.S.2d at 918.

[291] *Id.* at 239, 420 N.Y.S.2d at 919 (Shapiro, J., dissenting).

If Castleberry's condition remained the same, the compensation payments would continue indefinitely. *Id.* at 237-38, 420 N.Y.S.2d at 917. Based on his life expenctancy, the recovery from the carrier would, therefore, have totalled over $100,000. *Id.*

[292] *Id.* at 230, 420 N.Y.S.2d at 912; *see id.* at 239, 420 N.Y.S.2d at 919 (Shapiro, J., dissenting). *See* note 306 *infra*.

[293] *Id.* at 230, 420 N.Y.S.2d at 913.

[294] *Id.*

[295] 97 Misc. 2d 578, 580-81, 412 N.Y.S.2d 89, 91 (Sup. Ct. Orange County 1978). Since the carrier's lien will apply "to [the] extent such recovery shall be deemed for the benefit of such . . . carrier," N.Y. WORK. COMP. LAW § 29(1) (McKinney Supp. 1979-1980), the court viewed the release of "estimated future compensation" as constituting a benefit to the carrier. 97 Misc. 2d at 580, 412 N.Y.S.2d at 91. The court, however, did not explain why it limited the amount of the carrier's contribution to the amount of its lien without requiring the carrier to fully reimburse the attorney. While no case has been found in which the carrier was required to make an additional disbursement, the language of the statute apparently does not rule out such a result.

A divided appellate division reversed, stating that it was error to compromise completely the statutory lien of the carrier "under the guise of an apportionment of attorneys' fees."[296] Writing for the majority, Justice Margett stated that by sanctioning such an apportionment, the lower court had circumvented not only the objectives of the compensation scheme in general by ignoring the "inviolable" nature of the carrier's lien,[297] but had contravened the legislative intent underlying the 1975 amendment as well.[298] Conceding that the amendment was intended to assess proportionately the costs of procuring a judgment among the parties benefitting therefrom,[299] the *Castleberry* majority found no evidence that the legislature contemplated the impostion of all costs on the lienor, where, in the third party action, the plaintiff recovered "less than 'the sum of the lien plus the estimated liability of the carrier extinguished by the recovery.' "[300] Indeed, the court noted, nullifying a carrier's lien in such circumstances would afford the injured employee the "double satisfaction" of both statutory and common law recovery, a result which the existence of the lien was intended to obviate.[301] Hence, the court concluded, a proper application of the equitable apportionment provision required that the injured employee bear "that proportion of the attorneys' fees which his 'share' of the recovery (*i.e.*, the total settlement less the compensa-

---

[296] 70 App. Div. 2d at 230, 420 N.Y.S.2d at 913. Justices Cohalan and Martuscello joined Justice Margett in the majority. Concurring only in the reversal, Justice Shapiro dissented in a separate opinion.

[297] *Id.* at 230-31, 420 N.Y.S.2d at 913; *see* Granger v. Urda, 44 N.Y.2d 91, 96, 375 N.E.2d 380, 381, 404 N.Y.S.2d 319, 320 (1978). Noting the broad reach of the statute, the Court of Appeals in *Granger* found that the lien attaches "whenever a recovery is obtained in tort for the same injury that was a predicate for the payment of compensation benefits." *Id.* at 97, 375 N.E.2d at 381, 404 N.Y.S.2d at 321 (quoting Petterson v. Daystrom Corp., 17 N.Y.2d 32, 39, 215 N.E.2d 329, 332, 268 N.Y.S.2d 1, 5 (1966)).

[298] 70 App. Div. 2d at 230, 420 N.Y.S.2d at 913. *See* note 300 *infra*. *See generally id.* at 234, 420 N.Y.S.2d at 915 (citing 1975 Memorandum, *supra* note 287, at 1552-53). Justice Margett observed that the 1975 amendment sought to charge the carrier with a proportionate share of the litigation expenses and prevent recoveries from being fully exhausted by the lien and the attorneys' fees. *Id.* at 235, 420 N.Y.S.2d at 916.

[299] *Id.* at 235, 420 N.Y.S.2d at 916; *see* 1975 Memorandum, *supra* note 287 at 1552.

[300] 70 App. Div. 2d at 235, 420 N.Y.S.2d at 916. The *Castleberry* court asserted that it was "nothing short of incredible" to apply the 1975 amendment as a legislative "emasculation" of the carrier's lien. *Id.* at 232, 420 N.Y.S.2d at 914. The court reasoned that the carrier's future liability was too indefinite to be viewed as an amount benefitting the carrier, since a compensation award is subject to modification based on changed conditions. *Id.* at 235 & n.2, 420 N.Y.S.2d at 916 & n.2.

[301] *Id.* at 236, 420 N.Y.S.2d at 917. *See* note 286, *supra*.

tion lien, if any) bears to the total recovery."[302]

In a lengthy dissent, Justice Shapiro endorsed the conclusion reached by special term that the carrier's release from future liability is a benefit against which a proportionate share of the expenses should be assessed.[303] Maintaining that the recovery in the third-party suit takes the place of compensation benefits, the dissent contended that legal expenses should not be assessed against the plaintiff where the amount of the recovery does not exceed the carrier's lien plus its future liability, since to do so would "dilute" the recovery guaranteed by the WCL.[304] Justice Shapiro concurred in the reversal, however, because the lower court's apportionment of the attorneys' fees was not based on the present value of the carrier's discharge from future obligations.[305]

It is submitted that the *Castleberry* court's refusal to extinguish the carrier's lien to the extent of his liability for deficiency payments overemphasizes the importance of the lien in maintaining the viability of the compensation scheme. Assuming compliance with the statutory notice requirements,[306] when the third

---

[302] 70 App. Div. 2d at 238, 420 N.Y.S.2d at 918. As the attorneys' fees in the settlement were one-third of the recovery, the court allocated $6801 of the fees to the carrier, which was equivalent to one third of the amount of its lien. *Id.* at 238-39, 420 N.Y.S.2d at 918.

[303] *Id.* at 239, 420 N.Y.S.2d at 918-19 (Shapiro, J., dissenting).

[304] *Id.* at 247, 420 N.Y.S.2d at 923 (Shapiro, J., dissenting). The dissent noted that if the employee chose only to receive his compensation benefits, he would not have been required to pay any attorneys' fees in order to receive them. *Id.* (Shapiro, J., dissenting). Since a third party recovery effectively replaces compensation payments, Justice Shapiro reasoned that if the recovery was less than the amount already paid by the carrier plus its future liability, allowing further reduction of the proceeds through payments of litigation expenses would undercut the employee's statutorily guaranteed compensation. *Id.* at 247, 420 N.Y.S.2d at 923-24 (Shapiro, J., dissenting). Indeed, the dissent pointed out, most other states faced with the same issue have held that the release from future liability is a benefit which must be considered in apportioning attorneys' fees. *Id.* at 248-50, 420 N.Y.S.2d at 924-25 (Shapiro, J., dissenting).

[305] *Id.* at 250-51, 420 N.Y.S.2d at 926 (Shapiro, J., dissenting). Justice Shapiro pointed out that by failing to reduce the carrier's future obligation to present value, Special Term overstated the amount of the benefit inuring to the insurer, and as a result, incorrectly apportioned the costs of attorneys' fees. *Id.* (Shapiro, J., dissenting). For a discussion of the concept of present value, see K. BOUDREAUX & H. LONG, THE BASIC THEORY OF CORPORATE FINANCE, 15-18 (1977); H. OLECK, DAMAGES TO PERSONS AND PROPERTY, § 95 (1961).

[306] *Id.* at 237, 420 N.Y.S.2d at 917. Section 29(5) of the WCL provides that where the proposed settlement of the third-party action is less than the amount of the carrier's lien, the employee must either obtain written approval from the carrier or a judicial compromise order. N.Y. WORK. COMP. LAW § 29 (5) (McKinney Supp. 1979-1980). Failure to comply with these requirements automatically discharge any remaining future liability of the carrier. *See* Kusiak v. Commercial Union Assurance Co., 49 App. Div. 2d 122, 124, 373 N.Y.S.2d 714, 716 (4th Dep't 1975); O'Brien v. Lodi, 246 N.Y. 46, 51, 157 N.E. 925, 926 (1927). The purpose of

party recovery is less than the carrier's future liability plus its lien, the apportionment provision does not affect the amount of the benefits ultimately to be paid to the employee.[307] In such a case, the carrier remains liable for deficiency payments to the extent that its future obligation under the compensation claim exceeds the employee's *net* recovery from the third party action.[308] Hence, where the third party recovery does not discharge the carrier's future obligation, an apportionment of costs such as that granted by special term affects the timing but not the amount of the carrier's aggregate liability.[309] Such a result cannot logically be viewed as imperiling the integrity of the compensation scheme.[310]

By incorrectly assessing the implications of imposing most, if not all, of the litigation expenses upon the carrier in a *Castleberry* situation, it is suggested that the majority reached a result inconsistent with the policy of encouraging employees to pursue their claims against third party tortfeasors.[311]Since the potential for an

---

requiring either carrier approval or judicial consent is to prevent the "imprudent settlement" of third party claims which may adversely affect the carrier's rights. *See* Meachem v. New York Cent. R.R., 8 N.Y.2d 293, 297, 169 N.E.2d 913, 916, 206 N.Y.S.2d 569, 573 (1960); Kusiak v. Commercial Union Assurance Co., 49 App. Div. 2d 122, 124, 373 N.Y.S.2d 714, 716 (4th Dep't 1975); Clark v. Oakes & Burger Co., 16 App. Div. 2d 490, 491-92, 229 N.Y.S.2d 513, 515 (3d Dep't 1962).

[307] *Id.* at 238, 420 N.Y.S.2d at 917-18. Where a recovery in a third party action is less than the future obligation of the compensation carrier, the carrier must pay the employee any deficiency. N.Y. WORK. COMP. LAW § 29(4) (McKinney Supp. 1979-1980). The carrier in effect shoulders the total costs of attorneys' fees in such a case, since what he does not pay in the apportionment of attorneys' fees will ultimately be made up in deficiency payments. *See id.;* Curtin v. City of New York, 287 N.Y. 338, 341-44, 39 N.E.2d 903, 904-06 (1942); Kussack v. Ring Constr. Corp., 1 App. Div. 2d 634, 635, 153 N.Y.S.2d 646, 647 (3d Dep't 1956), *aff'd,* 4 N.Y.2d 1011, 177 N.Y.S.2d 522 (1958).

[308] N.Y. WORK. COMP. LAW § 29(4) (McKinney Supp. 1979-1980). *See* Castleberry, 70 App. Div. 2d at 236-37, 420 N.Y.S.2d at 917 (citing Curtin v. City of New York, 287 N.Y. 338, 39 N.E.2d 903 (1942)).

[309] *See* note 307 *supra.*

[310] The *Castleberry* court's conclusion, however, appears to be correct where the employee settles without complying with the statutory notice requirements. In such a case, the aggregate liability of the carrier would not be the same under either apportionment, since the employee is not entitled to recoup his legal expenses in the form of increased deficiency payments.

[311] Viewed in conjunction with the statutory lien afforded the carrier, *see* N.Y. WORK. COMP. LAW § 29(1) (McKinney Supp. 1979-1980), the purpose of encouraging an injured employee to pursue his common-law remedy against a third party tortfeasor is to keep the costs of coverage within practical limits, thus insuring the continued viability of the compensation system. *See* Granger v. Urda, 44 N.Y.2d 91, 97, 375 N.E.2d 380, 382, 404 N.Y.S.2d 319, 321 (1978); Becker v. Huss Co., 43 N.Y.2d 527, 537-38, 373 N.E.2d 1205, 1207, 402 N.Y.S.2d 980, 982-83 (1978); Curtin v. City of New York, 287 N.Y. 338, 342-43, 39 N.E.2d 903, 905 (1942). An additional, more fundamental consideration, is to assure the protection

earlier realization of his benefits operates as an inducement to the employee to seek such a recovery,[312] an incentive enhanced by the recent amendment to Section 29(1),[313] it appears incongruous to reject an apportionment which depletes the employee's share of the judgment but then allows him to recoup the costs assessed against him in the form of periodic future payments from the carrier.[314] It is submitted, therefore, that where the third party recovery does not exceed the sum of the lien and the carrier's future obligation, the objectives of the WCL could best be met if future courts, in equitably apportioning the litigation expenses, strive to maximize the residuum of the judgment.

Paul R. Williams

DEVELOPMENTS IN NEW YORK LAW

Court of Appeals prohibits insurer's indemnification of municipal employee for punitive damages arising out of federal civil rights action as contrary to public policy

Under a policy of liability insurance, an insurer is obligated to indemnify its insured for an award of compensatory damages rendered in a suit within the purview of the policy's provisions.[315]

---

of the worker and his family through preservation of any rights he may have which are not inconsistent with the compensation system. *See* McCoid, *The Third Person in the Compensation Picture: A Study of the Liabilities and Rights of Non-Employers*, 37 TEXAS L. REV. 389, 401 (1959).

[312] In the 1975 Memorandum, note 287 *supra*, the Law Revision Commission implicitly recognized that a reduction, or elimination of the proceeds inuring to the employee from the third party action would detract from the policy of encouraging employees to pursue their common-law remedies. *See id.* at 1552.

[313] *See id.* at 1552-53.

[314] *See generally* N.Y. WORK. COMP. LAW § 29(4)(McKinney Supp. 1979-1980); note 287 *supra*.

[315] *See* 1 COUCH, CYCLOPEDIA OF INSURANCE LAW §§ 1:2, 1:4, 1:5 (2d ed. 1959). Insurance is a voluntary contract between an insurer and its insured. The rights and obligations of the parties, absent contravention of public policy or statute, are governed by the policy's terms. *Id.*; W. PROSSER, LAW OF TORTS 542 (4th ed. 1971). *See* Kronfeld v. Fidelity & Cas. Co., 81 Misc. 2d 557, 562, 365 N.Y.S.2d 416, 422 (Sup. Ct. N.Y. County 1975), *aff'd*, 53 App. Div. 2d 190, 385 N.Y.S.2d 552 (1st Dep't 1976). The duty of an insurer to defend a lawsuit brought against its insured arises when the pleadings disclose facts which describe a risk covered under the policy. Sucrest Corp. v. Fisher Governor Co., 83 Misc. 2d 394, 399, 371 N.Y.S.2d 927, 934 (Sup. Ct. N.Y. County 1975).

Liability insurance is designed to reduce an insured's risk of loss and protect him against the deleterious effects of large damage awards. *See* R. MEHR & E. CAMMACK, PRINCI-