MONTANA STATE SENATE
JUDICIARY COMMITTEE
MINUTES OF THE MEETING

January 14, 1987

The sixth meeting of the Senate Judiciary Committee was called to order at 10:00 a.m. on January 14, 1987 by Chairman Joe Mazurek in Room 325 of the Capitol Building.

ROLL CALL: All committee members present.

CONSIDERATION OF SB 50: Senator Bob Brown of Senate District #2 sponsored SB 50. He explained the bill provides reasonable attorney fees must be awarded to the prevailing party in civil liability actions. He said it will adopt the English rule and that means the prevailing party has their legal fees paid by the loser in the civil action. He stated the idea would discourage frivolous suits.

PROPONENTS: Kathy Irigoin, State Auditor's Office, supported the bill because the State Auditor felt it is a tort reform measure that would cause more insurance companies to do their business here in Montana.

OPPONENTS: Karl Englund, Montana Trial Lawyers Association, felt the bill will have an effect on the filing of bona fide claims. He said that no lawyer should tell his client that he has a 100 percent chance of winning his case for him, so the client should know that he might have to pay tremendous attorney fees. Mr. Englund suggested the poor that are judgment proof have nothing to lose and the rich have the money to pay, so they have nothing to lose either. He said the middle class will be hard hit and probably won't have access to the court. Mr. Englund said the Supreme Court has a rule dealing with frivolous law suits, Rule 11, which states that any party that files anything that is not well grounded, will then pay the other side's cost. Mr. Englund felt this rule was enough to handle the problem. He explained that most of his associates handled their cases on a contingency fee arrangement where the client can't pay, but will give a percentage of the settlement to the attorney. He said many lawyers paid like this would not take a frivolous case because they would probably lose and then they would not get paid.

Glen Drake, an attorney representing American Insurance Association, suggested there would be an increase of all claims that were justifiable by 1/3 amount because most costs are on a contingency fee basis, so one will see a cost increase in all liability insurance coverage.

DISCUSSION ON SB 50: Senator Pinsoneault asked how often Rule 11 was

used by the Supreme Court. Mr. Englund did not know on the state level because it is quite new.

Senator Crippen inquired about how much a lawyer's time is expended on a bad faith case. Mr. Englund could not answer because he said he has never taken a bad faith case. Senator Crippen asked what defense counsel gets on an hourly bases on the average. Mr. Englund said around a $100 an hour. Senator Crippen asked if a plaintiff is told of this amount, which is pending against him, becasue it looks like a bad faith case. Mr. Englund said that is his point, that you have to tell a client that he might lose and have to pay for it. Mr. Englund said it will deter people from going to court unless they have a iron clad case. He also said he really had no idea what it would exactly cost to do a bad faith case.

Senator Yellowtail asked Kathy Irigoin if it would increase the cost of liability claims by one third. Kathy let Mr. Drake answer by saying there will be a one third value in all litigation claims and an increase in liability rates. Kathy Irigoin said she would get more information on this matter to the committee.

Senator Mazurek questioned Senator Brown on how an attorney's fees would be calculated. Senator Brown said the judge would decide according to the bill. Senator Mazurek asked if it would be calculated on contingency fees or hourly basis. Senator Brown responded by saying he was not sure. Senator Crippen asked about the language on line 13, "not arise from contract". Mr. Englund said it obligates one to conduct oneself in a reasonable manner and if one doesn't, there is a claim against that person which is based on an obligation not found in a contract. Senator Crippen asked if one can sue now in tort law for a breach of contract. Mr. Englund said there are torts that arise out of a contractual relationship, and a "bad faith" case would be covered because it could be an obligation that is not under the contract. Mr. Englund said you and I can make an agreement and if there is a suit in that agreement then the prevailing party gets attorney's fees. Senator Crippen felt the bill did not say that.

Senator Blaylock inquired if the subcommittee found there would be less law suits and a decrease in insurance rates if this bill was passed. Senator Brown said the idea is to decrease frivolous law suits, which will cause a decrease in insurance rates. Senator Blaylock asked if the subcommittee in their study found a substantial amount of frivolous law suits. Senator Brown answered that because of this bill a lawyer might not advise someone to sue, or the person, himself, might not carry a law suit through unless he really thought he could win.

Senator Crippen asked if lawyers had input into the subcommittee. Senator Brown felt they did not take this bill seriously. Senator Crippen remarked they should have taken it seriously.

Senator Bishop asked Mr. Englund if this bill would address the problem of attorney fees being more expensive than the settlement of the suit. Mr. Englund said it will cover this situation. Senator Bishop asked will it cause lawyers not to take good cases because the settlement is not a high sum, which would cover the expenses. Mr. Englund said we try to direct those cases to small claims court or to the justice court where it is not important to have counsel, but this bill would deal with that problem. Senator Bishop believed that a lot of young lawyers file a lot of law suits and if one files enough of those things, one can make a living filing and settling these suits. He asked if this bill will stop that. Mr. Englund did not know.

Senator Crippen asked Mr. Englund how many times he has taken a case that had a 100 percent chance to win in court. Mr. Englund said there is no such thing.

Senator Brown closed by stating if this bill has not done anything else it has brought the insurance casualty people and the Montana Trial Lawyers Association together.

CONSIDERATION ON SB 49: Senator Gene Thayer of Senate District #19 of Great Falls introduced SB 49, which is the only bill to pass unanimously by the special committee, set up to study all liability issues in the June Special Session of 1986. He explained the bill will amend 35-2-411 (MCA), which provides immunity for all directors, officers, employees and volunteers of nonprofit corporations from court suits, except for intentional torts or illegal acts. He pointed out three reasons for having the bill:

1. The cost of buying this insurance for a nonprofit organization is astronomical. He said some organization have paid up to 25 percent of their donations for liability insurance.

2. Directors and officers liability insurance is difficult to get.

3. Because of lack of liability insurance, people will not serve on the boards of nonprofit organizations.

PROPONENTS: Steve Waldron, Mental Health Association and Montana Residential Child Care Association, supported the bill because of the burden liability insurance costs put on small organizations' budgets. He stated that the organizations he represents do not condon protecting officers, directors, employees or volunteers from gross negligence but want to protect their regular duties.

Representative Kelly Addy from House District #94 of Billings stated he was on the special committee that drafted this bill. He stated that no director has ever been sued that was with any of these groups and the premium still rose steadily.

Joy Sterlingson of Helena, representing United Way of Cascade County, supported SB 49 (see Exhibit 1, written testimony). She gave additional information to the committee on the liability insurance problem, (see Exhibits 2 and 3).

Kathy Carp, representing herself, supported the bill because she states she is a professional volunteer. She said it was her job in her non-profit organizations to find insurance policies for them. She said she could wall paper her office with all the rejection notices she has received. She felt volunteers do a tremendous amount of work for a community and; thus, they should be protected.

Ken Hoovestal, a member of the Board of Directors for Regent II Child and Family Services in Great Falls and the Montana Snowmobile Association member, told the committee he was told there was insurance coverage on the Child and Family Services Program and then the next meeting the coverage was cancelled. He said the Snowmobile Association has many volunteers in their association and now those people are running scared because of the liability insurance problem.

Jerry Loendorf, Montana Medical Association, stated his concern is to get qualified people for director's positions and with insurance coverage the way it is, one can't get qualified people for these positions. He explained the deductable in today's coverages covers the defense costs but one has to pay one's own attorney's fees up to $10,000 to $25,000, that is why it is so difficult to get anyone to serve in these positions.

R.A. Ellis, Montana Water Development Association and Irrigation District member, said his groups supported SB 49.

George Allen, Montana Retail Association, said his group supported SB 49.

Bob Helding, Motor Carriers, also supported the bill.

Christin Volinkaty, Developmentally Disabled People of Montana, said that in the last year corporations' coverages went from $800 to $3,500; thus, services can't be given like her group would like to give them.

Wallace Melchar, Executive Director of Region II Child and Family Services of Great Falls, said since their coverage cancellation they have been told if they do find insurance coverage, it will be 500 to 600 percent higher than it was before. He commented that his group can't afford to have it, or not to have it. He stated his group had a recommendation on the two exemptions of intentional torts and illegal acts, which gives just officers and directors that right, because officers and directors can become liable for an employees' action under this bill.

Ron Waterman, representing himself and the United Way of Montana, stated that United Way raises money for 20 social agencies and insurance costs takes quite a bit of this money, so attracting people to director positions is difficult. He said the defense costs now can consume thousands of dollars and that is why insurance is a must.

Karl Englund, Montana Trial Lawyers Association, stated his support for SB 49 and gave amendments to the committee (see Exhibit 4). He said amendment number five states volunteers and employees should be in different groups because one is paid and one isn't. He said amendment number three tries to get to the point of a bona fide charitable organization because of the involvement of the IRS in tax exempt organizations (see Exhibit 5, page 2 through page 6). He commented on amendment number four by saying it deals with some of the questions the groups have asked today about intentional torts and illegal acts and who is covered under that. He said amendment number one takes "debits" out of the insurance coverage of officers and directors because this bill is about tort liability cases.

Shelia Sullivan, President of United Way for Lewis and Clark County, supported SB 49 because volunteers should not be afraid to serve. She said their policy for last year's cost $950, where as before they had a three year policy that only cost $1,100. She felt this amount of money should go to the services and not insurance.

Tom Harrison, Sheriffs and Peace Officers Association, Montana Automobile Association and Montana Certified Public Accounants, stated that there should be more peer advise about insurance and he felt this was a good bill.

Bob Pyfer, Montana Credit Unions League, supported SB 49 because it includes volunteers, which credit unions are a nonprofit member owned cooperative, which makes the small loans that other financial entities are not interested in. He said the credit unions by law have to have volunteer directors and officers. He said the rural areas are being hit the hardest as far as volunteers. He pointing out Congressmen John Porter from Illinois is presenting federal legislation, which calls for the Volunteer Protection Act that would mandate the states to inact legislation like his act. Mr. Pyfer said SB 49 should clarify what is a volunteer and what is a nonprofit organization and the committee should use the definitions in the Federal Volunteer Act to define these terms because it will clarify the terms and comply with the federal act. He supports the bill but feels it needs amendments.

Betti Christie Hill, representing the Montana Association for Homes of the Aging, supported the bill.

Carol Mosher, Montana Cattle Women, supported SB 49 and she turned in

Mr. Mons Teigen's testimony, who represents the Montana Stockgrowers Association in support of SB 49 (see witness sheet on Mons Teigen).

Pat Seiler, representing the Helena Mental Health Association, stated they do not carry liability insurance because the budget is only $5,000 a year.

Kathy Irigoin, State Auditor's Office, said the Complaints Division of the Insurance Department has gotten so many complaints from nonprofit organizations that they have now one full time person just handling the complaints.

Fred Boyce, MWWDA, said he supports the bill, but he felt the word "employee" should be left in the bill.

Karen Northey, the Program Director for the Florence Crittenton Home and Services, supports SB 49 (see Exhibit 6, written testimony).

Micheal Fieldrum, representing District #4 Human Resource Development Council in Havre, stated he has a board of 21 members and he has lost 6 members this year because of liability insurance fear. He explained if they do not get volunteers, the council can not legally exist.

Vicki Everson representing herself and Paris Gibson Square in Great Falls told the committee the art groups are in the same situation as the rest of the groups represented here. She felt that if it continues as it is there will be no more volunteers and the paid staff will have to take up all the slack.

Joe Upshaw of Helena, representing himself, stated he does quite a bit of volunteer work and has found that many good people will not voluteer because of this situation and urges support of SB 49.

Bill Leary of the Montana Hospital Association supported SB 49.

Jerry Brokist, Flathead County Electric Coop, said rural america can't afford increases in liability insurance.

Debi Brammer representing the Association of Conservation Districts supported the bill (see Exhibit 7, written testimony).

OPPONENTS: None

DISCUSSION ON SB 49: Senator Halligan asked if Senator Thayer had looked at the amendments presented by Karl Englund. Senator Thayer had looked at them and had also received amendments by the Montana Liability Coalition (see Exhibt 8). He felt the bill did need work and he was sure the committee would be able to make it workable. He also stated he

saw no problem in dropping the word "employee" from the bill. Senator Halligan asked Jim Robischon of the Montana Liability Coalition if he would respond to the idea of taking "employee" out of the bill. Mr. Robischon said his group felt the immunity should not extend to employees. He pointed out his third amendment changes the language because he felt it did not specially define the conduct that is and is not immuned with this bill (see Exhibit 8). He felt nonprofit organization was adequately identified in section 35-2-102 of the MCA. He said the Montana Liability Coalition does not believe that is appropriate to tie the definition of the nonprofit organization to the Internal Revenue Code or any other federal act. Senator Halligan asked if he is still allowing gross neligence to be covered by the bill. Mr. Robischon answered yes.

Senator Crippen asked Mr. Robischon if Mr. Englund's amendment number 4 on (3) was in any way dealing with a profit making entity. Senator Crippen said Junior Leagues have their "Next To New" shops and they are profit making and the money goes into their organization. Senator Crippen asked if the Leagues would be eliminated from the bill if amended this way. Mr. Robischon said it is possible. Senator Crippen asked Mr. Englund if that was his intent to exclude those groups like the Junior League from this bill. He responded it was not. Mr. Englund said his concern dealt with a religious organization that is tax exempt; owns property; takes over a community and runs a profit making business.

Senator Mazurek asked Mr. Englund what the definition of an illegal act is because he thought it was too broad. Mr. England replied it meant criminal conduct. Senator Mazurek asked what the effective day ought to be. Senator Thayer said it should be effective upon passage. Senator Mazurek inquired if the bill is only talking about directors' and officers' policies. Senator Thayer said it is specifically for officers, directors, volunteers and employees policies. Senator Mazurek asked the audience how many claims had been brought against their directors or officers. Bob Pyfer said they have had, but not a significant amount. Another person said there were 200 nationwide claims against Boy Scouts.

Senator Beck asked about the fourth amendment, (2) of Karl Englund's amendments, if mileage is included in the compensation part of it. Mr. Englund told the committee it was the intent of the amendment to distinguish a paid person from a volunteer.

Pat Seiler stated that some volunteers do get a little bit of money for their work, so they should not be excluded from the bill.

Senator Thayer closed on SB 49 by saying Representative Joan Miles of Helena would like to go on record as supporting this bill and he handed the committee a leaflet called "Legal Issues: Background Information for Liability" (see Exhibit 9).

CONSIDERATION OF SB 58: Senator Pinsoneault of St. Ignatius, Senate District #27, introduced SB 58. He said it provides another vechical in a trial; it is an option to take. He said SB 58 will allow plaintiffs and defendants in a civil action after liability has been determined to provide the jury proposed damage award amounts, from which the jury must choose one as the damage award. He asked the audience how many have sat on a jury. The response was little. He felt the jury's time on a trial would be less if they could choose from two amounts for damages. He commented that he polled the district judges and out of 30 percent response, 50 percent thought it was a good idea.

PROPRONENTS: Glen Drake, American Insurers Association, felt it was a good bill because it was not a mandatory procedure one has to do.

OPPONENTS: Karl Englund of the Montana Trial Lawyers Association felt if it is not mandatory, who will use it. He also felt it was not up to the lawyers to make the decisions, but the community should make the decision, which is the jury.

DISCUSSION ON SB 58: Senator Halligan questioned if one would settle for the amount while still in litigation procedures. Senator Pinsoneault felt it should be done before going to trial.

Senator Crippen asked what point and time do the parties decided to use this. Senator Pinsoneault said it could arise early on. Senator Crippen questioned if they were bound by any method in determining damages until after the liability has been determined. Senator Pinsoneault stated they would access any damage if there were any. Senator Crippen asked the plaintiff had proved his damages, what would the incentive be to enter into this kind of damage determination. Senator Pinsoneault said it is a question of value that has been put on the case. Senator Crippen asked if this decision can be reversed. Senator Pinsoneault said no.

Senator Mazurek felt it will be critical when the parties agree, because if they agree before the trial then the court might not take evidence on all issues. He said if they agree after liability has been determined, and if the plaintiff prevails on liability, then the court might take evidence on damages. He didn't feel the bill is clear when this decision should be made. Senator Mazurek asked if it should be done in advance of the trial. Senator Pinsoneault felt this would be the time to do it. Mr. Robischon of the Montana Liability Coalition felt this was a very good idea because it is a new option before or during the trial. He felt this helps the plaintiff when the two attorneys can figure out what the case is worth, instead of the two attorneys having different amounts and then the jury comes up with a new amount. He stated the Montana Liability Coalition did not take a stand on this. He felt cases dealing with liability should be left to the court, while the damages be left to the jury. He said before going into the trial, it should be requested

that the liability and damages be separated, which would probably enter into the agreement to determine damages. Senator Mazurek asked why this bill only pertains to general damages. Mr. Robischon said punitive damages would be more difficult to deal with because of the nature of the damages.

Senator Pinsoneault closed on SB 58.

The meeting was adjourned at 12:00 p.m.

Chairman

ROLL CALL

Judiciary COMMITTEE

50th LEGISLATIVE SESSION -- 1987 Date Jan. 14th

NAME	PRESENT	ABSENT	EXCUSED
Senator Joe Mazurek, Chairman	X		
Senator Bruce Crippen, Vice Chairman	X		
Senator Tom Beck	X		
Senator Al Bishop	X		
Senator Chet Blaylock	X		
Senator Bob Brown	X	-	
Senator Jack Galt	X		
Senator Mike Halligan	X		
Senator Dick Pinsoneault	X		
Senator Bill Yellowtail	X		

Each day attach to minutes.

DATE Jan 14, 1987

COMMITTEE ON

VISITORS' REGISTER

NAME	REPRESENTING	BILL #	Check One Support	Check One Oppose
Kathy Karp	Self	SB49	✓	
Bill Fleiner	Big Brothers & Sisters - Hln	SB 49	X	
Pat Grose	YWCA	SB49	X	
Chris Volinkaty	DD	SB49	X	
Brenda Schye	Montana Cultural Advocacy	SB49	X	
Bob Helding	Mt. Motor Carriers	SB 49	X	
Rose Christie Hill	Mt. Assoc. for Homes of the Aging	SB49	X	
Robert H[illegible]	Mt. State Pharmaceutical Assn	SB49	X	
Debi Brammer	Mt Assoc of Conservation Districts	SB49	X	
Mons Teigen	Mt Stockgrowers Assn	49	X	
Michael Feldman	Dist. 4 HRDC	SB49	X	
Sheila Sullivan	L & Clark United Way	SB49	X	
Art Wittich	MPC	SB 49		
Doug Davis	MWWDA	SB 49	X	
Fred J Boyce	MWWDA	SB49	X	
Lloyd Meland	Sun River Ditch Co	SB 49	X	
Tim Robischon	Mont. Liability Coalition	SB49	X	
RALPH F. WYMAN	SDA Denomination	"		
Karen Northey	Cuttenton Home	SB49	X	
Joy Sterlingson	United Way	SB49	X	
Mary Englund	Girl Scouts	SB 49	✓	
Vicki Emerson	Paris Gibson Sq	SB49	✓	
Jerry Brobst	Flathead Elec Co-op	SB 49	X	
Dan Skadura	Hill County Elec	" "	X	
Jeff Lutgrad	State Library	SB49	X	
Kathy M. Irigoin	State Auditor	SB49	X	
Bonnie Tippy	Alliance of Am Ins	SB49	X	X

(Please leave prepared statement with Secretary)

DATE Jan 21 1987

COMMITTEE ON ______________________

VISITORS' REGISTER

NAME	REPRESENTING	BILL #	Check One: Support	Check One: Oppose
Glen Drake	American Ins Assn	49 50	✓	✓
Don Thomas	Sen Bob Williams		✓	
Bob Ryser	Mont. Credit Unions League	49	✓	
Leta Livoti	Tri County Board of Directors DD. Svcs	49	✓	
Steve Waldron	Mental Health & MRCCA	49	X	
Carol Mosher	Mt. Cattle Women	49	X	
George Allen	Mt. Retail Assn	49	X	
Jack Zink	AFL-CIO	49 58	X	
[illegible] A. Duncan	U-Way - Helena	49	X	
Kathy Ward	United Way	49	✓	
Phil P[illegible]	Thurston [illegible], United Way	49	✓	
[illegible]	Gov's Council on Ec. Dev.	49		
[illegible]	providers of services to developmentally disabled			
[illegible]	Montana Oil & Gas	50	✓	
Dave [illegible]	Montana [illegible]	49	✓	
[illegible]	Mt [illegible]	49	✓	
Roger McGlenn	Independent Ins Agent Assoc. of MT	49	✓	
Roland D Pratt	Mt Optometric Assoc	49	✓	
William Leary	Mt. Hosp. Assn.	49	✓	
Wallace A Melcher	Region II Child & Family Services	49	✓	
Karen Malisani	American Cancer Society	49	✓	
Bob Anderson	Mt. Sch. Bds Assoc.	49	X	
Tom Harrison	MT. Soc. of CPAs	49	x	
Lorna Frank	Mt. Farm Bureau	49	X	
R.A. Ellis	Mont Water Development Assn	49	X	
Ken Hoovestol	Reg. II Child & Fam Services MT Snowmobile Assn	49	X	

(Please leave prepared statement with Secretary)

DATE (Jan 31 1985)

COMMITTEE ON (Fin)

VISITORS' REGISTER

NAME	REPRESENTING	BILL #	Check One: Support	Check One: Oppose
Dan Waterman	Self	SB 49	✓	
[illegible]	AFAF & others in opp's	SB 49	✓	
KARL ENGLUND	MTCA	SB 49	✓	
"	"	SB 50	✓	✓
"	"	SB 54		✓
Thomas W Maddox	MT Assn. of Tobacco & Candy	SB49	✓	
Mr. Delimata	Flathead Elect. Coop, Kalispell	SB49	✓	
Karl Schrade	Flathead Elect cooperative	SB49	✓	

(Please leave prepared statement with Secretary)

United Way
of Cascade County

P. O. Box 1343
Great Falls, Montana 59403
Phone 406-727-3400

January 13, 1987

SENATE JUDICIARY
EXHIBIT NO. 1
DATE Jan. 14, 1987
BILL NO. SB 49

To: Senate Judiciary Committee

From: Joy Stevlingson, Executive Director
United Way of Cascade County

The Great Falls, Montana, United Way Agency Directors Council, sponsored a community forum on December 3, 1986, in order to focus on problems faced by community non-profit agencies regarding the cost and availability of liability insurance.

Prior to the meeting, a questionnaire was distributed to non-profit agencies asking for information relative to the organizations ability to obtain liability insurance coverage for their operations and Boards of Directors. Of the questionnaires received, it was found that 33% of the organizations currently had no liability insurance for their Boards and officers. In almost all cases, the reason given for this was that coverage was too expensive or became unavailable as of the past several months. Of those able to secure and afford coverage, 83% had experienced increases of 100% or more since 1984.

Organizations serving youth groups and special populations appeared to have had the most difficulty and indicated that certain services could be in jeopardy. In addition, fears were expressed that people would be increasingly reluctant to serve on volunteer boards of directors because of vulnerability to law suits. Additionally, since non-profits cannot pass costs

on to clients, and since they are facing declining public funding coupled with current difficult economic difficulties, the increased costs of liability insurance have been difficult, if not impossible, to absorb within their already austere budgets.

Although we as a group cannot support specific legislation without Board of Director approval, we strongly support the intent of this bill. We feel without some relief, critical services to children and families in need could be in jeopardy. Many of the human services in our community are dependent upon the efforts of volunteers serving on boards and providing assistance to agencies in innumerable ways. Their personal assets should not be at risk as they offer their time and talent to improve the quality of life in our communities.

EXAMPLES

Boy Scouts - Liability insurance is obtained through the national office. Currently the national office spends 25% of its budget on liability insurance. (Both bodily injury and Directors and Officers liability) Each unit and council is assessed to cover this cost. Cost has increased 400% in the past two years.

Neighborhood Housing Services - Cost has increased from $513 in 1984 to $6700 in 1987 and is 5% of operating budget just for Directors and Officers.
Nancy Stephenson, director, states they are down to one choice and fear that at any moment they will be canceled or the premium will be so high they cannot afford it. NHS's Board and staff has a number of people who might not be able to

afford to be involved if the risk to their personal assets was not covered. The key to the success of NHS is the willingness of these business and City leaders to be involved and donate their expertise to help 'fix' the neighborhood. It is too much to expect them to also put their families' financial security at risk.

Children's Receiving Home - Directors and Officers insurance is not available because they serve children who have been sexually abused. Their mission is to provide temporary shelter for children who have been abused, neglected or abandoned.

JTS/lh
cc

NAME: Jay Sterlingson DATE: Jan. 14, 1987

ADDRESS: 913 Buena

PHONE: 727-3400

REPRESENTING WHOM? United Way of Cascade County

APPEARING ON WHICH PROPOSAL: SB 49

DO YOU: SUPPORT? X AMEND? _____ OPPOSE? _____

COMMENTS: _____

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

SENATE JUDICIARY
EXHIBIT NO. 2
DATE Jan. 14, 1987
BILL NO. SB 49

Specter of liability must not hinder spirit of voluntarism

A multitude of issues awaits the 1987 Montana Legislature when it convenes in January. Not least among those issues is that of liability.

With the November passage of Constitutional Initiative 30, voters gave the Legislature power to place ceilings on liability, limiting the amount of damages that can be awarded in a lawsuit.

Among those groups and people in desperate need of some kind of liability relief are the large number of nonprofit organizations and community volunteers. They are in jeopardy.

Nonprofit organizations, ranging from the Girl Scouts to the United Way to the Neighborhood Housing Service, are currently faced with skyrocketing insurance premiums.

During a meeting in Great Falls last week, representatives of such organizations said they are scrambling to find any kind of liability insurance — at rates that can be hundreds of times higher than the same coverage cost a year or two ago. In some instances, the community groups have been forced to curtail services or programs because they cannot find affordable insurance.

Volunteers in this community and throughout Montana have traditionally served the public well, stepping in to help those in need of everything from food and shelter to counseling, recreation and cultural enrichment.

"That type of volunteer activity is being hindered," said State Rep. Ron Miller, R-Great Falls. "Volunteers are open to all kind of (liability) actions as it stands now. It defeats the very purpose of voluntarism," he said.

Two bills are currently being drafted to exempt volunteers from liability, Miller said. Such legislation should be passed. Volunteers should not have to place their personal assets on the line when they participate in nonprofit organizations.

Any such legislation must be carefully worded, however, to clearly define the liability of the group itself, as opposed to the liability of the individual members of that group.

A hearing of the Legislature's Joint Interim Subcommittee on Liability Issues is set for Friday in Room 104 of the Capitol Building in Helena. The ball will start rolling there. We hope it clears the way for volunteers and nonprofit groups to continue their good work, either limiting or exempting them from liability.

We aren't suggesting that such legislation will be easy to pass. Those who oppose liability limits have strong concerns. They feel that injured parties must have full redress through the courts. What happens, for instance, if someone drowns at a Scout camp because of poor supervision?

Even so, the specter of liability should not be allowed to destroy the good work that nonprofit agencies in Montana are doing. Legislation is clearly needed.

12/4/86

Cost of insurance is endangering volunteer programs, workers fear

By FRED MILLER III
Tribune Staff Writer

Officials from six Cascade County nonprofit agencies Wednesday sounded an alarm also being heard from government and private sectors: Soaring insurance costs are squeezing the life out of them.

The insurance bind has agencies trimming services to pay skyrocketing costs and endangers recruiting because volunteers are reluctant to serve for fear they could be sued.

The comments were made at forum on the problems of liability insurance. It was sponsored by the United Way of Cascade County's Directors Council.

Jovanna Wooden, executive director of Big Sky Girl Scouts, said parts of that agency's coverage cost between 250 percent and 800 percent more this year and it was not able to find liability coverage.

"Failure for us to find liability insurance...will jeopardize a program which literally reaches thousands of children," Wooden said.

Nancy Stephenson, executive director of Neighborhod Housing Service, said its insurance has "just gone out of sight," from $1,000 a year to $7,500 a year.

"One more year like that would obviously take us out of having insurance coverage," she said. Nationwide, NHSs in California, Michigan and Montana "are having the most severe insurance crisis in the country."

Ilene Casey of the Junior League of Great Falls said the League asked 14 companies for a bid, but was told premiums would increase 600 percent. This "will break us if it continues to climb 600 percent a year."

"The whole camping progam of all our youth organizations is in jeopardy" because no company is willing to insure groups which sponsor outdoor activities, according to Dub Findley of the Community Help Line.

"Probably our society has not been aware of all the services it's been getting through volunteers' services" which, Findley said, which "we're in danger of losing...What happens to a society when we can no longer afford to serve ourselves?"

Robert Reiquam, First Bank president, said some volunteers are concerned about agencies not finding coverage, because "there's always that threat out there for a suit for what you really believe is right."

He cited the tremendous cost of defending a suit, starting at $10,000. "All of these things add up to prevent people from serving" as directors and volunteers. He said boards of directors should be exempt from any kind of suit and that legislation along those lines is "a step in the right direction."

With the authority granted with the passge of Constitutional Initiative 30 in the last election, Reiquam said he hoped the 1987 Legislature will limit the amount of damages that can be awarded in a suit, but not just for nonprofit groups.

"I don't think it's enough to eliminate boards of directors of nonprofit concerns from having damages filed against them," he said. If they are protected, others would be more vulnerable to suits.

Rep. John Phillips and Rep. Ron Miller, both Great Falls Republicans, encouraged those present to attend a Joint Interim Subcommittee on Liability Issues meeting in Helena Dec. 12 at the state Capitol to comment on bills to abolish liability actions against officers, directors and employees of nonprofit corporations.

SENATE JUDICIARY
EXHIBIT NO. 2
DATE Jan. 14, 1987
BILL NO. SB 49

SENATE JUDICIARY
EXHIBIT NO. 3
DATE Jan. 14, 1987
BILL NO. SB 49

CHICAGO TRIBUNE, Chicago, IL
August 24, 1986

Voice of the people

End the liability of volunteering

WASHINGTON—When your wife or husband tells you they're volunteering to serve on the board of the local United Way or park district, YMCA or school, the first thing you'd better ask is whether they have liability coverage for volunteers. Unfortunately, many organizations are having a tough time keeping volunteers protected. Either they can't get coverage at any cost or, if coverage is available, they can't justify the huge outlays.

Volunteers are the backbone of social progress and community life in America and run many of our local governments from townships to libraries to volunteer fire departments. Like it or not, they are increasingly being exposed to lawsuits which conceivably could cost them their homes or farms. While it is true that few have been successfully sued, the proclivity of trial lawyers to name everyone in sight as a party defendant and the increasingly unpredictable nature of our tort system have led insurance companies to withdraw from the market. The consequence is less and less liability insurance protection and fewer and fewer people coming forward to volunteer.

The solution: Exempt unpaid volunteers from personal civil liability, except for willful and wanton misconduct. Why should the assets of board members of the Junior League be jeopardized for a slip-and-fall injury in the local thrift shop? That judgment should be paid out of Junior League assets or its liability coverage, not by its volunteers. Otherwise, how can we expect volunteers to continue to come forward?

Who should implement such a solution? The states. It's here where jurisdiction over almost all personal injury litigation has resided for all 200 years of our republic. The Illinois General Assembly has just adopted such a provision in its insurance crisis package. All states should do so.

The role of the federal government? To prod the states to adopt this and other reforms to keep the liability crisis from destroying the competitiveness of American products, undermining the availability and quality of our doctors and hospitals, and withdrawing local government services—from paramedics to picnic grounds and toboggan hills.

To encourage the states, I have introduced legislation in the House of Representatives to redistribute a small amount of federal funds for social service programs to states which have acted by 1988 to exempt unpaid volunteers from civil liability. The money would come from the allocations to states that have not yet done so. State legislatures should be made to focus on the problem now, before the volunteer spirit is permanently crippled.

Eleven states already have enacted some legal immunity for volunteers without controversy. My bill [H.R. 5196] is based on the best of these state laws and has been developed in cooperation with the national councils representing the major private and public non-profit organizations served by volunteers.

Who are the volunteers of America? You and me and our families, friends and next-door neighbors. We should not have to fear placing family assets at risk when we donate our time and talent without compensation to serve our communities and charitable organizations.

U.S. Rep. John Porter
10th Congressional District, Illinois

SENATE JUDICIARY
EXHIBIT NO. 4
DATE Jan. 14th
BILL NO. SB 49

AMENDMENTS TO SB 49, INTRODUCED COPY,
PROPOSED BY THE MONTANA TRIAL LAWYERS ASSOCIATION

1) Title, line 9
Following: "27-1-701"
Strike : "AND 35-2-411"

2) Page 1, line 13
Following: "director,"
Strike : "employee,"

3) Page 1, line 13
Following: "volunteer of a"
Insert : "tax-exempt"

4) Page 1, line 17
Following: "section does not apply to"
Strike : "liability for intentional torts or illegal acts"
Insert : ":
(1) Liability for intentional torts, misconduct, illegal acts, or gross negligence;

(2) Officers or directors who receive compensation for the services provided to the corporation; or,

(3) Officers, directors or volunteers of a tax-exempt non-profit corporation that is in any way affiliated with a profit making entity."

5) Page 2, lines 6 and 7
Strike : All of lines 6 and 7

THE CODE OF THE LAWS

OF THE

UNITED STATES OF AMERICA

TITLE 26—INTERNAL REVENUE CODE

(Act Aug. 16, 1954, ch. 736, 68A Stat. 3 as amended)

Subchapter F.—Exempt Organizations

Part
I. General rule.
II. Private foundations.
III. Taxation of business income of certain exempt organizations.
IV. Farmers' cooperatives.
V. Shipowners' protection and indemnity associations.

HISTORY; ANCILLARY LAWS AND DIRECTIVES

In '69, P. L. 91-172, Sec. 101(j)(58), redesignated former parts II, III, and IV as parts III, IV, and V respectively and added new part II.

CROSS REFERENCES

This subchapter is referred to in 26 USCS §§ 532, 542, 552 [26 USCS §§ 501–526]

PART I.—GENERAL RULE

Sec.
501. Exemption from tax on corporations, certain trusts, etc.
502. Feeder organizations.
503. Requirements for exemption.

In '69, P. L. 91-172, Sec. 101(j)(61), repealed item 504 relating to denial of exemption.

---

§ 501. Exemption from tax on corporations, certain trusts, etc.

(a) Exemption from taxation. An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

(b) Tax on unrelated business income and certain other activities. An organization exempt from taxation under subsection (a) shall be subject to tax to the extent provided in parts II and III of this subchapter, but (notwithstanding parts II and III of this subchapter) shall be considered an organization exempt from income taxes for the purpose of any law which refers to organizations exempt from income taxes.

(c) List of exempt organizations. The following organizations are referred to in subsection (a):

(1) Corporations organized under Act of Congress, if such corporations are instrumentalities of the United States and if, under such Act, as amended and supplemented, such corporations are exempt from Federal income taxes.

(2) Corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt under this section.

(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

(4) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

(5) Labor, agricultural, or horticultural organizations.

(6) Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(7) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.

(8) Fraternal beneficiary societies, orders, or associations—

(A) operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and

(B) providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents.

(9) Voluntary employees' beneficiary associations providing for the payment of life, sick, accident, or other benefits to the members of such association or their dependents or designated beneficiaries, if no part of the net earnings of such association inures (other than through such payments) to the benefit of any private shareholder or individual.

(10) Domestic fraternal societies, orders, or associations, operating under the lodge system—

(A) the net earnings of which are devoted exclusively to religious, charitable, scientific, literary, educational, and fraternal purposes, and

(B) which do not provide for the payment of life, sick, accident, or other benefits.

(11) Teachers' retirement fund associations of a purely local character, if—

(A) no part of their net earnings inures (other than through payment of retirement benefits) to the benefit of any private shareholder or individual, and

(B) the income consists solely of amounts received from public taxation, amounts received from assessments on the teaching salaries of members, and income in respect of investments.

(12) Benevolent life insurance associations of a purely local character, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations; but only if 85 percent or more of the income consists of amounts collected from members for the sole purpose of meeting losses and expenses.

(13) Cemetery companies owned and operated exclusively for the benefit of their members or which are not operated for profit; and any corporation chartered solely for the purpose of the disposal of bodies by burial or cremation which is not permitted by its charter to engage in any business not necessarily incident to that purpose and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(14)(A) Credit unions without capital stock organized and operated for mutual purposes and without profit.

(B) Corporations or associations without capital stock organized before September 1, 1957, and operated for mutual purposes and without profit for the purpose of providing reserve funds for, and insurance of shares or deposits in—

(i) domestic building and loan associations,

(ii) cooperative banks without capital stock organized and operated for mutual purposes and without profit, or

(iii) mutual savings banks not having capital stock represented by shares.

(C) Corporations or associations organized before September 1, 1957, and operated for mutual purposes and without profit for the purpose of providing reserve funds for associations or banks described in clause (i), (ii), or (iii) of subparagraph (B); but only if 85 percent or more of the income is attributable to providing such reserve funds and to investments. This subparagraph shall not apply to any corporation or association entitled to exemption under subparagraph (B).

(15) Mutual insurance companies or associations other than life or marine (including interinsurers and reciprocal underwriters) if the gross amount received during the taxable year from the items described in section 822(b) (other than paragraph (1)(D) thereof) and premiums (including deposits and assessments) does not exceed $150,000.

(16) Corporations organized by an association subject to part IV of this subchapter or members thereof, for the purpose of financing the ordinary crop operations of such members or other producers, and operated in conjunction with such association. Exemption shall not be denied any such corporation because it has capital stock, if the dividend rate of such stock is fixed at not to exceed the legal rate of interest in the State of incorporation or 8 percent per annum, whichever is greater, on the value of the consideration for which the stock was issued, and if substantially all such stock (other than nonvoting preferred stock, the owners of which are not entitled or permitted to participate, directly or indirectly, in the profits of the corporation, on dissolution or otherwise, beyond the fixed dividends) is owned by such association, or members thereof; nor shall exemption be denied any such corporation because there is accumulated and maintained by it a reserve required by State law or a reasonable reserve for any necessary purpose.

(17)(A) A trust or trusts forming part of a plan providing for the payment of supplemental unemployment compensation benefits, if—

(i) under the plan, it is impossible, at any time prior to the satisfaction of all liabilities, with respect to employees under the plan, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of supplemental unemployment compensation benefits,

(ii) such benefits are payable to employees under a classification which is set forth in the plan and which is found by the Secretary or his delegate not to be discriminatory in favor of employees who are officers, shareholders, persons whose principal duties consist of supervising the work of other employees, or highly compensated employees, and

(iii) such benefits do not discriminate in favor of employees who are officers, shareholders, persons whose principal duties consist of supervising the work of other employees, or highly compensated employees. A plan shall not be considered discriminatory within

the meaning of this clause merely because the benefits received under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of the employees covered by the plan.

(B) In determining whether a plan meets the requirements of subparagraph (A), any benefits provided under any other plan shall not be taken into consideration, except that a plan shall not be considered discriminatory—

(i) merely because the benefits under the plan which are first determined in a nondiscriminatory manner within the meaning of subparagraph (A) are then reduced by any sick, accident, or unemployment compensation benefits received under State or Federal law (or reduced by a portion of such benefits if determined in a nondiscriminatory manner), or

(ii) merely because the plan provides only for employees who are not eligible to receive sick, accident, or unemployment compensation benefits under State or Federal law the same benefits (or a portion of such benefits if determined in a nondiscriminatory manner) which such employees would receive under such laws if such employees were eligible for such benefits, or

(iii) merely because the plan provides only for employees who are not eligible under another plan (which meets the requirements of subparagraph (A)) of supplemental unemployment compensation benefits provided wholly by the employer the same benefits (or a portion of such benefits if determined in a nondiscriminatory manner) which such employees would receive under such other plan if such employees were eligible under such other plan, but only if the employees eligible under both plans would make a classification which would be nondiscriminatory within the meaning of subparagraph (A).

(C) A plan shall be considered to meet the requirements of subparagraph (A) during the whole of any year of the plan if on one day in each quarter it satisfies such requirements.

(D) the term "supplemental unemployment compensation benefits" means only—

(i) benefits which are paid to an employee because of his involuntary separation from the employment of the employer (whether or not such separation is temporary) resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions, and

(ii) sick and accident benefits subordinate to the benefits described in clause (i).

(E) Exemption shall not be denied under subsection (a) to any organization entitled to such exemption as an association described in paragraph (9) of this subsection merely because such organization

provides for the payment of supplemental unemployment benefits (as defined in subparagraph (D)(i)).

(18) A trust or trusts created before June 25, 1959, forming part of a plan providing for the payment of benefits under a pension plan funded only by contributions of employees, if—

(A) under the plan, it is impossible, at any time prior to the satisfaction of all liabilities with respect to employees under the plan, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of benefits under the plan,

(B) such benefits are payable to employees under a classification which is set forth in the plan and which is found by the Secretary or his delegate not to be discriminatory in favor of employees who are officers, shareholders, persons whose principal duties consist of supervising the work of other employees, or highly compensated employees, and

(C) such benefits do not discriminate in favor of employees who are officers, shareholders, persons whose principal duties consist of supervising the work of other employees, or highly compensated employees. A plan shall not be considered discriminatory within the meaning of this subparagraph merely because the benefits received under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of the employees covered by the plan.

(19) A post or organization of war veterans, or an auxiliary unit or society of, or a trust or foundation for, any such post or organization—

(A) organized in the United States or any of its possessions.

(B) at least 75 percent of the members of which are war veterans and substantially all of the other members of which are individuals who are veterans (but not war veterans), or are cadets, or are spouses, widows, or widowers of war veterans or such individuals, and

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(d) Religious and Apostolic organizations. The following organizations are referred to in subsection (a): Religious or Apostolic associations or corporations, if such associations or corporations have a common treasury or community treasury, even if such associations or corporations engage in business for the common benefit of the members, but only if the members thereof include (at the time of filing their returns) in their gross income their entire pro rata shares, whether distributed or not, of the taxable income of the association or corporation for such year. Any amount so included in the gross income of a member shall be treated as a dividend received.

(e) Cooperative hospital service organizations. For purposes of this title, an organization shall be treated as an organization organized and operated exclusively for charitable purposes, if—

(1) such organization is organized and operated solely—

(A) to perform, on a centralized basis, one or more of the following services which, if performed in its own behalf by a hospital which is an organization described in subsection (c)(3) and exempt from taxation under subsection (a), would constitute activities in exercising or performing the purpose or function constituting the basis for its exemption: data processing, purchasing, warehousing, billing and collection, food, industrial engineering, laboratory, printing, communications, record center, and personnel (including selection, testing, training, and education of personnel) services; and

(B) to perform such services solely for two or more hospitals each of which is—

(i) an organization described in subsection (c)(3) which is exempt from taxation under subsection (a),

(ii) a constituent part of an organization described in subsection (c)(3) which is exempt from taxation under subsection (a) and which, if organized and operated as a separate entity, would constitute an organization described in subsection (c)(3), or

(iii) owned and operated by the United States, a State, the District of Columbia, or a possession of the United States, or a political subdivision or an agency or instrumentality of any of the foregoing;

(2) such organization is organized and operated on a cooperative basis and allocates or pays, within 8½ months after the close of its taxable year, all net earnings to patrons on the basis of services performed for them; and

(3) if such organization has capital stock, all of such stock outstanding is owned by its patrons.

For purposes of this title, any organization which, by reason of the preceding sentence, is an organization described in subsection (c)(3) and exempt from taxation under subsection (a), shall be treated as a hospital and as an organization referred to in section 170(b)(1)(A)(iii).

(f) Cross reference. For nonexemption of Communist-controlled organizations, see section 11(b) of the Internal Security Act of 1950 (64 Stat. 997; 50 U.S.C. 790(b)).

(Aug. 16, 1954, Ch. 736, 68A Stat. 163; Mar. 13, 1956, Ch. 83, § 5(2), 70 Stat. 49; Apr. 22, 1960, P. L. 86-428, § 1, 74 Stat. 54; July 14, 1960, P. L. 87-834, § 8(a), 76 Stat. 997; Feb. 2, 1966, P. L. 89-352, § 1, 80 Stat. 4; Nov. 8, 1966, P. L. 89-800, § 6(a), 80 Stat. 1515; June 28, 1968, P. L. 90-364, Title I, § 109(a), 82 Stat. 269; Dec. 30, 1969, P. L. 91-172, Title I, §§ 101(j)(3)–(6), 121(b)(5)(A), (6)(A), 83 Stat. 526, 527, 541; Dec. 31, 1970, P. L. 91-618, § 1, 84 Stat. 1855; Aug. 29, 1972, P. L. 92-418, § 1(a), (c)(19), 86 Stat. 656.

HISTORY; ANCILLARY LAWS AND DIRECTIVES

Prior law:

IRC 1939, §§ 101 except (12) and last paragraph, 165(a), 421.

Florence Crittenton Home and Services

Maternity Home **Mother/Baby Program** **Counseling & Classes** **Out-Patient Services**

846 FIFTH AVENUE
HELENA, MONTANA 59601
TELEPHONE (406)442-6950
A United Way Member Agency

KAREN E. NORTHEY, PROGRAM DIRECTOR

SENATE JUDICIARY
EXHIBIT NO. 6
DATE Jan 14, 1987
BILL NO. SB49

January 14, 1987

Senator Joe Mazurek, Chairman
Judiciary Committee

Dear Senator Mazurek:

The Crittenton Home supports Senate Bill number 49 concerning liability insurance for volunteers of non-profit agencies. We have a voluntary Board of Directors, big sisters, tutors, auxillary and other miscellaneous volunteers. The Home could not exist without these generous people giving of their time, yet holding them liable for non-malicious accidental incidents makes it difficult to recruit concientious volunteers as well as making the cost of our liability insurance extremely high. We would appreciate you support of Senate Bill 49.

Sincerely,

Karen E. Northey
Program Director

KEN/tk

cc: Committee Members
Steve Waldron

SENATE JUDICIARY
EXHIBIT NO. 7
DATE Jan. 14
BILL NO. SB 49

SB 49 (Thayer)

Mr. Chairman, members of the committee, for the record my name is Debi Brammer and I represent the Montana Association of Conservation Districts. Our association has monitored and has been very involved with the liability problems and discussions. We fully support the concept of SB 49 but understand that there are a few problems with it. We understand the problems are being looked at and hope that this committee does pass the bill.

(total agreement with United Way testimony)

Senate Bill No. 49

Introduced Copy

SENATE JUDICIARY
EXHIBIT NO. 8
DATE Jan. 14, 1987
BILL NO. SB 49

1. Title, line 7.
Following: "DIRECTORS,"
Strike: "EMPLOYEES,"

2. Page 1, line 13.
Following: "director,"
Strike: "employee,"

3. Page 1, line 16
Following: "This"
Strike: lines 17 and 18 in their entirety
Insert: "immunity does not extend to any wilful action intended to cause injury."

SENATE JUDICIARY
EXHIBIT NO. 9
DATE Jan. 14
BILL NO. SB 49

Legal Issues:

Background Information for

Liability Issues Study

Legal Memorandum

Prepared by
MONTANA LEGISLATIVE COUNCIL
Room 138
State Capitol
Helena, Montana 59620
(406) 444-3064

LEGAL ISSUES:
BACKGROUND INFORMATION
FOR LIABILITY ISSUES STUDY

PREPARED FOR

JOINT INTERIM SUBCOMMITTEE
ON LIABILITY ISSUES

by

Legal Division

Montana Legislative Council

June 1986

Table of Contents

I. INTRODUCTION

This report was prepared through the joint efforts of the Legislative Council legal staff and is designed to present a background of legal issues that may come before the Committee during its consideration of liability problems. The report is not intended to be an exhaustive treatment of the matters discussed but simply to provide committee members with a basic explanation of the legal issues involved in the study and the status of current Montana law in these areas.

This report addresses the following areas:

-- collateral source rule
-- joint and several liability
-- caps on damage awards, including punitive damages
-- structured settlements
-- contingent fee arrangements, including shifting of attorney fees to the losing party
-- termination of employment
-- sanctions for filing frivolous suits
-- statutes of limitation
-- simultaneous pursuit of a bad faith claim with the underlying claim
-- reinsurance and a state reinsurance fund
-- insurance marketing assistance plans (MAPs).

II. COLLATERAL SOURCE RULE

The "collateral source rule" is a principle of law relating to the recovery of damages in a lawsuit, "damages" being the compensation awarded for the injury or damage suffered by an injured party. The collateral source rule provides that benefits received by a plaintiff from a source wholly independent of and collateral to the wrongdoer, or defendant, will not diminish the damages otherwise recoverable from the defendant. 22 Am. Jur. 2d, Damages, § 206. Such benefits from collateral sources may include gratuitous medical care, continued salary or wage payments, proceeds from insurance policies, or welfare and pension benefits. Although benefits received by a plaintiff from collateral sources have the effect of reducing a plaintiff's financial losses, it is generally considered by the courts that reducing a plaintiff's recovery against a defendant would result in a windfall to the defendant. Thus, the courts have developed the collateral source rule to prohibit the reduction of damages that may be awarded in a trial. Damages, supra, at § 206.

The collateral source rule should not be confused with the rule that evidence that a defendant paid compensation to the plaintiff or that defendant is insured is not admissible to prove that defendant is liable to the plaintiff, a rule of evidence that is codified in Montana Rules of Evidence, Rules 409 and 411, Title 26, Chapter 10, MCA.

The collateral source rule has not been adopted by statute in Montana. However, the rule has been adopted

SENATE JUDICIARY
EXHIBIT NO. 9
DATE 1-14-87
BILL NO S.B. 49

by the Montana Supreme Court. In Benner v. B.F. Goodrich Co., 150 Mont. 97, 430 P2d 648 (1967), the Court acknowledged the existence of the collateral source rule, though the rule was not an issue in that case. In Goggans v. Winkley, 159 Mont. 85, 495 P2d 594 (1972), and Tribby v. N.W. Bank of Great Falls, ____Mont.____, 704 P2d 409, 42 St. Rep. 1133 (1985), the Court says it is applying the rule, but under the facts of each case the applicability of the rule is not an issue because in each case the compensation already paid plaintiff and sought to be used to reduce damages awarded was compensation for an occurrence wholly unrelated to the occurrence for which plaintiff was seeking damages. The rule applies only when the damages sought from defendant and the prior compensation that defendant seeks to use to reduce the damages that defendant must pay plaintiff are both for the same occurrence. The fact remains, however, that the Montana Supreme Court has recognized the collateral source rule.

Abolition or modification of the collateral source rule is one of the more popular forms of suggested tort reform in the United States today. The rule has been abolished or modified in at least 15 states, under the theory that a plaintiff should not be twice reimbursed for the same personal injury or property damage and that the rule contributes to higher insurance premiums. However, it has been argued to the contrary that there is no unfairness, and no windfall to plaintiff, when plaintiff's prior compensation is from a source that plaintiff maintained at his own expense, such as medical, property, or disability insurance. If plaintiff had the foresight to maintain insurance and paid premiums for years, why should he be penalized by

deducting from his recovery against defendant the amount of plaintiff's insurance award? Would this result in defendant's unjustly benefiting from plaintiff's going to the expense of maintaining insurance? For this reason it has been argued that after deducting the prior compensation from the damages awarded plaintiff, any money plaintiff paid to maintain the source of the prior compensation should be added to the damages, but not to exceed the amount of the prior compensation.

On the other hand, suppose plaintiff received prior compensation from a source he did not pay to maintain, such as employer-paid insurance and benefits or a rich parent. Would it not be more fair to provide that damages plaintiff recovers from defendant should be turned over to the source of the prior compensation in the amount of the prior compensation than to provide that the damages recovered from defendant must be reduced by the amount of the prior compensation?

The following are methods of abolishing the collateral source rule:

-- Evidence of compensation that has been or may be received is admissible and the trier of fact (judge or jury) may do what it wishes with the evidence, ignoring it or reducing damages by all or part of the compensation.

-- Evidence of compensation that has been or may be received is admissible and the trier of fact must reduce the damages by the amount of the compensation.

-- Evidence of compensation that has been or may be received is not admissible, but the judge must reduce damages awarded by the jury (or by the judge if there is no jury trial) by the amount of the compensation.

III. JOINT AND SEVERAL LIABILITY

"Joint and several liability" refers to the concept that if the acts of two or more wrongdoers, even though not acting in concert, combine to produce one injury, either wrongdoer, or tortfeasor, may be held liable for the entire damage. An injured person may pursue recovery for his damages from any or all the wrongdoers, and any one wrongdoer may be required to pay the full amount of the plaintiff's damages, despite his degree of responsibility for the harm. An injured person is entitled to only one full recovery, whether from one defendant or several. In Montana, joint and several liability is established by statute in section 27-1-703, MCA, which also provides that the defendants have a right of contribution from the other defendants.

Section 27-1-703, MCA, provides as follows:

> 27-1-703. Multiple defendants jointly and severally liable -- right of contribution.
>
> (1) Whenever the negligence of any party in any action is an issue, each party against whom recovery may be allowed is jointly and severally liable for the amount that may be awarded to the claimant but has the right of contribution from any other person whose negligence may have contributed as a proximate cause to the injury complained of.

(2) On motion of any party against whom a claim is asserted for negligence resulting in death or injury to person or property, any other person whose negligence may have contributed as a proximate cause to the injury complained of may be joined as an additional party to the action. Whenever more than one person is found to have contributed as a proximate cause to the injury complained of, the trier of fact shall apportion the degree of fault among such persons. Contribution shall be proportional to the negligence of the parties against whom recovery is allowed. Nothing contained in this section shall make any party indispensable pursuant to Rule 19, M.R.Civ.P.

(3) If for any reason all or part of the contribution from a party liable for contribution cannot be obtained, each of the other parties against whom recovery is allowed is liable to contribute a proportional part of the unpaid portion of the noncontributing party's share and may obtain judgment in a pending or subsequent action for contribution from the noncontributing party.

Other code areas that should be looked at in addressing joint and several liability are:

-- 25-13-104, pertaining to compelling contribution or repayment from joint debtors or sureties

-- Title 25, Chapter 15, pertaining to the liability of joint debtors

-- Title 25, Chapter 20, Rules 18 and 19, Montana Rules of Civil Procedure, pertaining to joinder of claims, remedies, and parties

-- Title 28, Chapter 1, part 3, pertaining to joint obligations

-- 28-1-1102 and 28-1-1103, pertaining to performance by one of several joint debtors or joint creditors

-- 28-3-703, pertaining to joint and several promises

-- 28-11-311, pertaining to joint and several liability of person indemnifying another

-- 28-11-417, pertaining to surety's right to reimbursement and contribution

-- 31-2-208, relating to joint and separate debts.

IV. DAMAGE LIMITATIONS

A. Constitutional Provisions

The provisions of the Montana Constitution which limit the authority of the Legislature to limit the amount of damages that may be recovered in a given type of action are:

1. Article II, Section 4, which reads:

> Individual dignity. The dignity of the human being is inviolable. No person shall be denied the equal protection of the laws. Neither the state nor any person, firm, corporation, or institution shall discriminate against any person in the exercise of his civil or political rights on account of race, color, sex, culture, social origin or condition, or political or religious ideas.

2. Article II, Section 16, which reads:

> The administration of justice. Courts of justice shall be open to every person, and speedy remedy afforded for every injury of person, property, or character. No person shall be deprived of this full legal redress for injury incurred in employment for which another person may be liable except as to fellow employees and his immediate employer who hired him if such immediate employer provides coverage under the Workmen's Compensation Laws of this state. Right and justice shall be administered without sale, denial, or delay.

3. Article II, Section 18, which reads:

> State subject to suit. The state, counties, cities, towns, and all other local governmental entities shall have no immunity from suit for injury to a person or property, except as may be specifically provided by law by a 2/3 vote of each house of the legislature.

B. General Damage Limitations

The Montana Supreme Court in Pfost v. State of Montana, ____ M ____, ____ P2d ____, 42 St. Rep. 1957, 1967 (1985), held that Article II, Section 16 of the Montana Constitution:

> . . . provides a speedy judicial remedy for every injury of person, property or character, and that such speedy remedy includes a full legal redress as a fundamental interest.

The court went on to state that:

> Any statute that restricts, limits, or modifies full legal redress for injury to person, property or character therefore affects a fundamental right and the state must show a compelling interest if it is to sustain the constitutional validity of the statute. Pfost at 1966.

Pfost struck down section 2-9-107, MCA, which imposed limitations on the amount of damages recoverable against governmental entities as violating the equal protection clause of the Montana Constitution found in Article II, Section 4. The court found that because the fundamental right to full legal redress found in Article II, Section 16, was involved, the strict scrutiny analysis for classifications was applicable and the statute declared unconstitutional. It appears to be virtually impossible to demonstrate a compelling state interest that would satisfy the strict scrutiny test in light of the supreme court's cursory treatment of the legislative findings contained in section 2-9-106, MCA, which were made in a good faith response to White v. State, ____ M ____, 661 P2d 1272, 40 St. Rep. 507 (1983).

C. Economic vs. Noneconomic Damages

In White (supra), the court struck down section 2-9-104, MCA, which limited governmental liability and distinguished between economic and noneconomic damages. The court used the same equal

protection, strict scrutiny analysis to strike down both limitations and held as to noneconomic damages that the language "every injury" contained in Article II, Section 16, of the Montana Constitution includes:

> . . . all recognized compensable components of injury, including the right to be compensated for physical pain and mental anguish and the loss of enjoyment of living. White at 510.

The most recent case in which limitations on the liability of a private group for noneconomic damages were challenged and upheld is Fein v. Permanente Medical Group, 211 Cal. Rptr. 368, 695 P2d 665 (1985). California Civil Code Section 333.2 limits the recovery for noneconomic loss in medical malpractice actions to $250,000. An attorney for the Legislative Counsel Bureau of the California State Legislature suffered a heart attack which was originally diagnosed as a muscle problem. He fully recovered physically and was able to attain his former lifestyle but had a diminished life expectancy. In addition to his economic damages he was awarded $500,000 for pain, suffering, and inconvenience. In a challenge to the statutory limitation, the California Supreme Court held that:

> It is well established that a plaintiff has no vested right in a particular measure of damages and the Legislature possessed broad authority to modify the scope and nature of such damages. So long as the measure is rationally related to a legitimate state interest, policy determinations as to the need for, and the desirability of, the enactment are for the legislature. Fein at 382.

The California statute was enacted in response to the rising cost for medical malpractice insurance, which was posing serious problems for the health care system in the state, was threatening to curtail the availability of medical care in some parts of the state, and creating the very real possibility that many doctors would practice without insurance, leaving patients who might be injured with the prospect of uncollectible judgments. The California court notes that a number of states have invalidated statutory provisions limiting damages in medical malpractice actions while others have upheld such limitations. The court points out that with only one exception, all of the invalidated statutes contained a ceiling on both pecuniary and nonpecuniary damages. The court states:

> In any event, as we have explained, we know of no principle of California -- or federal -- constitutional law which prohibits the Legislature from limiting the recovery of damages in a particular setting in order to further a legitimate state interest. Fein at 385.

Fein was appealed to the U.S. Supreme Court and dismissed for want of a substantial federal question.

The Montana Supreme Court has taken a different view than the California court with respect to limitations on noneconomic damages (see White supra.),

D. Workers' Compensation

The Workers' Compensation Act, codified as Title 39, Chapter 71, MCA, is an area of limitation on the right of recovery that has withstood constitutional challenge. In a case decided on the same day as Pfost (supra), the court analyzed the Workers' Compensation Act under both of the constitutional provisions used to find section 2-9-107, MCA, unconstitutional. In Raisler v. Burlington Northern Railroad Co., ____ M ____, P2d____, 42 St. Rep. 1997 (1985), Burlington Northern as the employer sought indemnity from Farmers Insurance Company for amounts paid to plaintiff. Section 39-7-411, MCA, precludes such indemnity, and Burlington Northern challenged the validity of the statute. In dealing with the Equal Protection challenge the court said:

> Because an employer's immunity from tort liability in a workers' compensation case is constitutionally recognized in Article II, Section 16, Mont. Const., we conclude no analysis of 39-71-411, MCA, on a strict scrutiny theory is required. Raisler at 2003.

The court specifically stated that White and Pfost were not applicable.

The court went on to analyze the section under Art. II, Sec. 16, guaranteeing full legal redress to injured parties. The court said:

> In our analysis of Art. II, Sec. 16, Mont. Const., we conclude that in workers' compensation cases, the second sentence affords a limitation upon the

> broad provisions in the first sentence. We conclude that where an employer has provided workers' compensation coverage, an employee constitutionally may be deprived of full legal redress for injury against his employer, both directly and indirectly. Raisler at 2003.

Raisler indicates that in order to deprive a person of full legal redress, constitutional grounds must be found for so doing. The constitutionality of the Workers' Compensation Act under the 1889 Montana Constitution was upheld in Shea v. North-Butte Mining Co., 55 M 522, 179 P 499 (1919).

E. Punitive Damages

In White (supra), the court did uphold the prohibition on recovering punitive damages from governmental entities. The prohibition is contained in section 2-9-105, MCA, which provides:

> State or other governmental entity immune from exemplary and punitive damages. The state and other governmental entities are immune from exemplary and punitive damages.

The court in White applied a "rational basis" rather than a "strict scrutiny" test. The court found that assessing punitive damages against the government would have little deterrent effect and would in effect punish innocent taxpayers. There is a statement in White at p. 511 that:

> Plaintiff has a constitutional right to redress for all her injuries but she does not have a constitutional right to recover punitive damages.

Taken on its face, this statement allows statutory limitations on punitive damages whether recoverable against a governmental entity or a private party.

The 1985 Legislature limited the right to recover punitive damages by enacting section 27-1-220 and amending section 27-1-221, MCA. Those provisions now provide:

> 27-1-220. Purpose -- factual basis for punitive or exemplary damages. The purpose of 27-1-221 is to deter claims for punitive or exemplary damages that are not clearly based in fact, and to that end, the legislature intends for 27-1-221 to be used in combination with early and ready application and granting of motions for summary judgment pursuant to Rule 56 of the Montana Rules of Civil Procedure where such claims are not based in fact, and the application of the sanctions provided for in Rule 11 of the Montana Rules of Civil Procedure against those parties responsible for making such claims.
>
> 27-1-221. When exemplary damages allowed. (1) Subject to subsection (2), in any action for a breach of an obligation not arising from contract where the defendant has been guilty of oppression, fraud, or malice, actual or presumed, the jury, in addition to the actual damages, may give damages for the sake of example and by way of punishing the defendant.
>
> (2) The jury may not award exemplary or punitive damages unless the plaintiff has proved all elements of the claim for exemplary or punitive damages by clear and convincing evidence. Clear and convincing evidence means evidence in which there is no serious or substantial doubt about the correctness of the conclusions drawn from the

evidence. It is more than a preponderance of evidence, but less than beyond a reasonable doubt.

(3) Presumed malice exists when a person has knowledge of facts, intentionally avoids learning of facts, or recklessly disregards facts, knowledge of which may be proven by direct or circumstantial evidence, which creates a high degree of risk of harm to the substantial interests of another, and either deliberately proceeds to act in conscious disregard of or indifference to that risk or recklessly proceeds in unreasonable disregard of or indifference to that risk.

(4) The plaintiff may not present, with respect to the issue of exemplary or punitive damages, any evidence to the jury regarding the defendant's financial affairs or net worth unless the judge first rules, outside the presence of the jury, that the plaintiff has presented a prima facie claim for exemplary or punitive damages.

(5) A defendant is guilty of oppression if he intentionally causes cruel and unjust hardship by:

(a) misuse or abuse of authority or power; or

(b) taking advantage of some weakness, disability, or misfortune of another person.

(6) (a) In cases of actual fraud or actual malice, the jury may award reasonable punitive damages after considering the circumstances of the case.

(b) In all other cases where punitive damages are awarded, punitive damages may be in an amount up to but no greater than $25,000 or 1% of the defendant's net worth, whichever is greater.

(7) In cases where punitive damages may be awarded, the jury shall not be instructed, informed, or advised in any manner as to the limitations on the amount of exemplary or punitive damages as set forth in subsection (6)(b).

F. Conclusions on Damages

In light of the White and Pfost decisions, it is difficult to envision any statute placing liability limits for economic or noneconomic damages on private groups which would pass constitutional muster. This is particularly true because the Legislature was acting pursuant to the authority granted to it by Article II, Section 18 of the Montana Constitution, authorizing it by a 2/3 vote of each house to limit the waiver of sovereign immunity contained therein. The court said:

> We reject out of hand that the Legislature has the power, under Art. II, Sec. 18, as amended, to act under that amended clause without regard to other provisions of the State Constitution. Pfost at 1970.

Damage limitations on an injured worker's right to recover under the Workers' Compensation Act are permissible because the authority of the Legislature to limit recovery is constitutionally recognized in Article II, Section 16 of the Montana Constitution.

The Legislature may limit the right to recover punitive damages in any manner it chooses because

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there is no constitutional right to recover punitive damages. Any law restricting punitive damage awards would be subject to a rational basis analysis under Article II, Section 4 of the Montana Constitution.

V. STRUCTURED SETTLEMENTS

Tort judgments are most often paid in a lump sum payment. Increasingly, the alternative of periodic payment of damages is being examined and used. In the most advantageous situation, under a structured award or settlement, the defendant will ultimately pay less and the injured party will receive more than under the lump sum payment approach.

The method of periodic payment of damages is generally used in two instances: first, when the parties agree to it, and second, when it is required by statute. Periodic payment of damages by agreement of the parties is usually called a "structured settlement". A structured settlement has been defined as "a negotiated settlement of a personal injury claim prior to trial, whereby the defendant agrees to make certain payments, both lump-sum and periodic, to the plaintiff, in exchange for a release of all present and future liability by the plaintiff and his or her heirs."[1]

FOOTNOTES

[1]Gehring, "Everyone Can Win With Structured Settlements," 28 Risk Mgmt. No. 7, 18, and 19 (July 1981).

A typical structured settlement agreement might provide for the following: (1) a lump sum payment for damages incurred prior to settlement; (2) a lump sum payment to the plaintiff to be used as the plaintiff chooses; (3) payment of plaintiff's attorney fees and legal costs; and (4) periodic payments to cover lost wages, medical and rehabilitation expenses, and living expenses. Each structured settlement is different and contains provisions of concern to the parties involved.

Periodic payment of damages under statute varies according to the particular statute, but generally follows the same approach as do structured settlements. For example, in 1985 the New York State Legislature enacted a law that requires the court in medical and dental malpractice cases to enter a judgment for payment of part of the award in a lump sum and for payment of the remainder of the award in periodic payments. A lump sum payment must be made for: past damages, future damages up to $250,000, certain attorney fees and costs, and future damages allocable to payments previously made by another party, such as a workers' compensation insurer. The New York law provides that the remainder of the judgment is equal to the amount of "the present value of an annuity contract that will provide for the payment of the remaining amounts of future damages in periodic installments."[2]

In recent years, several states have enacted legislation providing for structured awards of this type.

FOOTNOTES

[2]New York CPLR 5031, Ch. 294, L. 1985.

The National Conference of Commissioners on Uniform State Laws approved a Model Periodic Payment of Judgments Act in 1980.

Several arguments have been advanced in support of the periodic payment of damages rather than lump sum payment in tort actions. First, an injured party may lack experience in the management and investment of large sums of money and thus may prefer to receive regular periodic payments for the rest of his or her life. Second, a structured settlement may allow for a more accurate determination of the actual damages sustained by the injured party. For example, rather than agreeing to a specific payment amount, the parties could agree to gear the exact amount of the periodic payments to the future rate of inflation, as measured by the consumer price index. Third, there are tax advantages to a structured settlement agreement drafted in accordance with the federal Internal Revenue Code. A lump sum settlement is tax-free to the plaintiff, but interest earned on the recovery is taxable as ordinary income. In contrast, the IRS generally treats structured settlement payments as entirely tax-free. (This will be a factor in the parties' determination of the size of the payments.)

The major objections of those who see problems in the structured award approach are the approach's failure to compensate fully for those who do not live to their full life expectancy and the problem of the solvency of the entity from whom the responsible party has purchased an annuity to fund the periodic payments. When the amount of the periodic payments is based on the injured party's earning capacity and life expectancy

and the injured party lives for only half of his or her life expectancy, the party's dependents do not receive full compensation for the injuries. This problem can be prevented by providing for payments for a fixed number of years even if the injured party dies. The future solvency of the entity from which an annuity has been purchased is important when the injured party has a long life expectancy and payments are to be made for many years. This concern can be alleviated somewhat by careful choice of an annuity carrier and by requiring the defendant's insurer to guarantee the payments if the primary carrier defaults.

Although Montana law does not specifically provide for periodic payment of damage claims except in the area of workers' compensation, the structured settlement agreement is commonly used in Montana tort lawsuits. Under Workers' Compensation law, Section 39-71-741, MCA, most awards must be paid in periodic payments. Lump sum workers' compensation awards are permitted only in limited circumstances.

VI. CONTINGENT FEE ARRANGEMENTS

This portion of this memo will examine two aspects of attorney fees: first, the "American rule" of attorney fees, and second, contingency fees.

A. Fee-Shifting

Under what is known in the United States as the American rule, each party to a lawsuit pays his own costs of bringing or defending the lawsuit,

including attorney fees. In contrast, under what we call the English rule, the prevailing party in a lawsuit is usually awarded his or her attorney fees. The general rule in Montana is, absent a contractual agreement or an applicable statutes specifying otherwise, that each party is responsible for the costs and attorney fees each incurred in the lawsuit.

Among other concerns, critics of the American rule believe that it is a cause of the contemporary increase in litigation and that it discourages small but meritorious claims. Those who support the American rule argue that because litigation is uncertain, parties should not be penalized for merely defending or bringing a lawsuit, that requiring the losing party to pay the prevailing party's attorney fees might limit low-income persons' access to the courts, and that the complexities of litigation on the question of reasonable attorney fees would impose a burden on judicial administration.

Many exceptions to the American rule now exist both in federal and state laws. Under what are known as "fee-shifting" statutes, the American rule has been altered by one-way fee-shifting statutes and two-way or reciprocal fee-shifting statutes. When a statute provides for one-way fee shifting, an award of attorney fees can be made against a particular losing party only. For example, the federal Equal Access to Justice Act provides for the award of attorney fees against a losing governmental party only, not against a nongovernmental party even if that party loses.

Another type of one-way fee-shifting statute provides for the award of attorney fees against a defendant only, or a plaintiff only. Section 25-31-1005, MCA, provides for the plaintiff to pay the attorney fees incurred by the defendant in certain proceedings to change venue. When a statute provides for two-way fee shifting, ordinarily fees will be awarded against the losing party regardless of the identity of that party. Section 22-1-1111, MCA, of the Montana Library Records Confidentiality Act is an example of a two-way fee-shifting statute. Under that section a person identified in a library record that is disclosed in violation of the Act may sue the person responsible for the disclosure. Reasonable attorney fees may be awarded to the prevailing party.

Some fee-shifting statutes provide for the mandatory award of attorney fees to the party or parties specified in the statute. Others provide for award of attorney fees in the discretion of the court.

Montana has enacted a number of fee-shifting statutes that apply in a variety of situations. For example, the prevailing party in actions brought under a residential property rental agreement or under the Montana Residential Landlord and Tenant Act of 1977 may be awarded attorney fees. Also, a Montana court must award attorney fees to the prevailing party in a wage claim action. A third example, section 50-23-106, MCA, is a one-way fee-shifting statute. Under this section, if the State Department of

Health and Environmental Sciences prevails in an action to enjoin a party from keeping a nondomesticated animal known to be capable of transmitting rabies, such as a skunk, the defendant must pay the Department's attorney fees. If the Department loses, it is not liable to pay the defendant's attorney fees. Numerous other Montana statutes provide for some type of attorney fee-shifting.

B. Contingency Fees

Even though more and more fee-shifting statutes are being enacted, the general rule in the United States continues to be that each party is responsible for his own attorney fees. Contingency fees represent an accommodation of the American legal system to this rule. Under a contingency fee arrangement a lawyer agrees to represent a person in a lawsuit in return for a percentage of the judgment awarded to that person, if that person prevails in the lawsuit. If the lawyer's client loses, the lawyer is paid nothing. In some types of lawsuits, such as personal injury tort cases, contingent fees are the accepted method of pricing for legal services.

The contingency fee system has been defended in the following ways: first, the system gives the lawyer an incentive to work in the client's interest because the earnings of the lawyer will depend on the size of the client's award; second, the system allows the client to shift some of the risk of litigation to the lawyer; and third, the system allows the client to borrow the lawyer's services in advance of the lawsuit's resolution.

However, there are problems with the contingency fee system, as stated by its critics. First, because the system makes the lawyer financially interested in the result of the litigation, the lawyer's best interests may not parallel those of the client. Thus, a lawyer may have difficulty deciding whether to settle a case or to go to trial in the hope of receiving a larger recovery. Second, the contingency fee system is said to encourage what is often called "ambulance chasing". Third, it has been suggested that the vast majority of personal injury tort cases involve no uncertainty that the lawyer is going to be paid something; the only question is how much. Thus, the question has been raised as to whether a mere uncertainty about the amount of compensation justifies a lawyer taking a large percentage of the recovery.[3]

With the exception of provisions of the Montana Workers' Compensation Act, contingency fees in tort cases are not regulated by state statute in Montana. Contingency fees are commonly used in this state as a method of financing lawsuits.

VII. TERMINATION OF EMPLOYMENT

A. Wrongful Discharge and the Implied Covenant of Good Faith and Fair Dealing

Historically, the employment at will doctrine allowed an employer to discharge an employee for a

FOOTNOTES

[3]Grady, "Some Ethical Questions About Percentage Fees," Litigation, Summer 1976, at 20.

good reason, a bad reason, or no reason at all if the employee was not hired for a specific length of time. This doctrine was in force in all states until the early 1970s, when many states began to develop exceptions to the doctrine. Montana is one of those states. Montana's employment (or termination) at will doctrine is set out in the following code section:

> 39-2-503. Termination at will. An employment having no specified term may be terminated at the will of either party on notice to the other, except where otherwise provided by this chapter, 28-10-301 through 28-10-303, 28-10-502, 30-11-601 through 30-11-605, and 39-2-302.

The Montana Supreme Court has developed two exceptions to this doctrine. They are known as the wrongful discharge exception and the exception arising from breach of an implied covenant of good faith and fair dealing.

A wrongful discharge is an unfair or unjustified discharge in violation of a public policy. The following are examples of such discharges:

-- Discharge for refusal to commit perjury or some other crime

-- Discharge for asserting some statutory right, such as the right to workers' compensation

-- Discharge for refusing the unwanted advances of a superior.

Basically, the term "public policy" refers to the purpose of a law.

The Montana Supreme Court has also held that in certain employments there is an "implied covenant of good faith and fair dealing" and that an employer who breaches the covenant when discharging an employee is liable for damages. This means that the employer has by implication agreed to deal fairly and in good faith with the employee. The implied covenant is based on objective manifestations or actions by the employer which give rise to the employee's reasonable belief that he has job security and will be fairly treated. For example, if the employer has written an employee handbook setting forth the rights and duties of the employer and employees, including disciplinary procedure, our court has held that the handbook becomes a part of the employment contract and the employer has the duty to follow it. The actions of the employer leading to the employee's belief that he will be fairly treated may also consist of oral pronouncements or simply the employer's way of doing things.

It is reasonable to assume that these two exceptions to the employment at will doctrine also apply to such things as a demotion or a transfer to another location or job, meant to punish an employee.

B. Termination for Good Cause

The following code sections allow termination of employment by either the employer or the employee for breach of a duty:

> 39-2-504. Termination by employer for fault. An employment, even for a specified term, may be terminated at any time by the employer in case of any willful breach of duty by the employee in the course of his employment or in case of his habitual neglect of his duty or continued incapacity to perform it.
>
> 39-2-505. Termination by employee for fault. An employment, even for a specified term, may be terminated by the employee at any time in case of any willful or permanent breach of the obligations of his employer to him as an employee.

C. Blacklisting and Statement of Reasons for Discharge

The following code sections prevent an employer from blacklisting a discharged employee and require the employer to give the employee a written statement of the reasons for the discharge if the employee requests the statement:

> 39-2-801. Employee to be furnished on demand with reason for discharge. It is the duty of any person after having discharged any employee from his service, upon demand by such discharged employee, to furnish him in writing a full, succinct, and complete statement of the reason of his discharge and if such person refuses so to do within a reasonable time after such demand, it is unlawful thereafter for such person to

furnish any statement of the reason of such discharge to any person or in any way to blacklist or to prevent such discharged person from procuring employment elsewhere, subject to the penalties and damages prescribed in this part.

39-2-802. Protection of discharged employees. If any person, after having discharged an employee from his service, prevents or attempts to prevent by word or writing of any kind such discharged employee from obtaining employment with any other person, such person is punishable as provided in 39-2-804 and is liable in punitive damages to such discharged person, to be recovered by civil action. No person is prohibited from informing by word or writing any person to whom such discharged person or employee has applied for employment a truthful statement of the reason for such discharge.

39-2-803. Blacklisting prohibited. If any company or corporation in this state authorizes or allows any of its agents to blacklist or any person does blacklist any discharged employee or attempts by word or writing or any other means whatever to prevent any discharged employee or any employee who may have voluntarily left the company's service from obtaining employment with another person, except as provided for in 39-2-802, such company or corporation or person is liable in punitive damages to such employee so prevented from obtaining employment, to be recovered by him in a civil action, and is also punishable as provided in 39-2-804.

39-2-804. Violation of part a misdemeanor. Every person who violates any of the provisions of this part relating to the protection of discharged employees and the prevention of blacklisting is guilty of a misdemeanor.

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D. Statutes Prohibiting Discharge for Specific Reasons

Various code sections prohibit discharge of an employee for certain specific reasons. They include discharges because:

-- The employee's wages have been garnished or attached, 39-2-302

-- The employee refused to take a lie detector test requested by the employer, 39-2-304

-- The employee signed or filed an affidavit, petition, or complaint in regard to a public employer, or gave information or testimony, under Title 39, Chapter 31, Collective Bargaining for Public Employees

-- The Department of Revenue has ordered the employer to withhold the employee's income in the amount necessary to pay child support past due and send it to the department, or proceedings have been instituted under the "Child Support Enforcement Act of 1985", contained in Title 40, Chapter 5, part 4

-- The employee is pregnant, 49-2-310(1)

-- The employee has exercised his rights, testified, or assisted others in exercising their rights or duties under the "Employee and Community Hazardous Chemical Information Act", contained in Title 50, Chapter 78.

E. Further Reading

The following materials may be consulted for further reading on this subject:

-- Employment At Will, Wrongful Discharge, and the Covenant of Good Faith and Fair Dealing in Montana, Past, Present, and Future, Hopkins & Robinson, 46 Mont.L.Rev. 1 (1985).

-- Montana Association of Defense Counsel Seminar Materials, Mont. State Bar C.L.E. publication, June 1985.

-- The Demise of At-Will Employment, Mont. State Bar C.L.E. publication, May 1985.

-- Employment Discrimination, Mont. State Bar C.L.E. publication, Nov. 1984.

VIII. SANCTIONS AGAINST FRIVOLOUS LITIGATION

A. Traditional common-law remedies

1. Malicious prosecution

a. Developed in response to criminal actions brought without probable cause; extended to include unwarranted civil actions

b. Plaintiff usually required to prove 4 elements in a separate proceeding:

(1) Termination of proceeding in favor of plaintiff

(2) Malice

(3) Absence of probable cause

(4) Actual damages above costs recoverable in original action

c. English vs. American rule

(1) English: plaintiff must prove all 4 elements

(2) American: plaintiff not required to show actual damages, only material harm or violation of a legal right

2. Abuse of process

a. Lies against one who misuses or misapplies judicial process for collateral objective

b. Plaintiff must prove 3 elements:

(1) An ulterior purpose

(2) A willful act in the use of process not proper in the regular prosecution of the proceeding

(3) Actual damage

3. Both torts judicially created

4. Share common element of an improper purpose in use of legal process

5. Share common element with numerous statutory remedies: malice

6. Both remedies available to Montana party

B. Other antidotes for frivolous litigation

1. By statute, tax party who advances frivolous claim or defense with opponent's costs, attorney fees

   a. Inherent difficulty in finding practicable mechanism for determining what is "frivolous"

   b. Provision that seeks to prevent frivolous behavior may chill principle of free access to courts (Montana Supreme Court, in Pfost v. St. of Montana, held that Art. II, sec. 16, of the Montana Constitution gives a constitutional right to full legal redress for injury. Any statute that restricts, limits, or modifies full legal redress affects a fundamental right and thus the state must show a compelling state interest to sustain the constitutional validity of the provision.)

2. Give court discretion to determine reasonable costs and attorney fees

3. Allow judge to throw out any claim, defense, or motion, he determines frivolous on its face

4. Subject attorney to civil and professional sanctions for bringing a groundless claim

C. Montana remedies

1. Section 37-61-421, MCA (Ch. 533, L. 1985):

"Attorney's or litigant's liability for excess costs. An attorney or party to any court proceeding who, in the determination of the court, multiplies the proceedings in any case unreasonably and vexatiously may be required by the court to satisfy personally the excess costs, expenses, and attorney fees reasonably incurred because of such conduct."

2. Judicially created exception to general rule that, absent a contrary contractual agreement or statutory provision, prevailing party in civil action is not entitled to recover attorney fees

a. Foy v. Anderson, 176 Mont. 507 (1978): court, on case-by-case basis, may exercise its equity power to grant complete relief to the prevailing party, including award of attorney fees

b. Foy doctrine applied in limited situations

(1) Holmstrom Land Co. v. Hunter, 182 Mont. 43 (1979): where a party, through no fault of its own, is forced to defend frivolous action

(2) State ex rel. Wilson v. Dept. of Nat. Resources and Conserv., 648 P2d 766 (1982): where party finds it necessary to intervene in frivolous action, although not technically forced to become a party

(3) Thompkins v. Fuller, 667 P2d 944 (1983): Foy doctrine applies only where prevailing party forced into action that is frivolous and without merit

3. Numerous statutory provisions allowing prevailing party in certain civil actions to recover attorney fees (See comment, ". . . And Attorney Fees To The Prevailing Party": Recovering Attorney Fees Under Montana Statutory Law, Williams, 46 Mont. L. Rev. 119 (1985), for detailed enumeration and discussion of Montana statutory provisions that allow prevailing party in certain actions to recover attorney fees.)

4. Professional sanctions: attorney's legal and ethical responsibility to refrain from engaging in frivolous litigation

a. Rules of Professional Conduct (adopted by Montana Supreme Court effective July 1, 1985, to replace Canons of Professional Ethics):

(1) Rule 3.1: prohibits any claim unless it is "not frivolous"

(2) Rule 3.2: lawyer shall make reasonable efforts to expedite litigation consistent with the interests of the client

(3) Rule 3.4: lawyer shall not make a frivolous discovery request, or in trial, allude to any matter lawyer does not reasonably believe is relevant

(4) Rule 4.4: lawyer shall not use means that have no substantial purpose other than to embarrass, delay, or burden a third person

D. Examples of frivolous claim statutes

1. Wisconsin Wis. Stat. § 814.025

a. Allows victim to pursue remedy in original proceeding

b. Applies to frivolous actions, defenses, counterclaims, cross-claims

c. Requires finding of malice, i.e., brought or continued "in bad faith, solely for purposes of harassing or maliciously injuring another" or "party or partys' attorney knew or should have known that the action . . . was without any reasonable basis in law or equity and could not be supported by a good faith argument for an extension, modification or reversal of existing law."

d. Authorizes assessment of costs, fees against either attorney or party

(1) Requires assessment on finding of frivolous action

(2) Court has discretion to determine "reasonable" costs, fees

2. Oregon

a. ORS 20.105 authorizes attorney fees to a prevailing party when an opponent acts in bad faith, wantonly, or solely for oppressive reasons

b. ORCP 21 E provides for striking of a frivolous claim; allows a court, on its own or on motion of any party, to strike "any sham, frivolous, or irrelevant pleading or defense"

IX. STATUTES OF LIMITATIONS

Statutes of limitations, or time limits on when a legal cause of action may be filed, are set forth in Title 27, Chapter 2, part 2, MCA, for specific kinds of actions. The kinds of actions most frequently involved in liability insurance issues are tort actions (3-year statute of limitations), contract actions (3-, 5-, and 8-year statutes of limitations), and two specific tort actions: medical malpractice and legal malpractice (3 years from date of discovery of cause of action).

These statutes of limitations have varied little in Montana for many years. Therefore, they would appear to bear little responsibility for the recent liability insurance crisis. It is possible, however, to reduce the present exposure of insurance companies to liability for conduct of their insureds by decreasing the statutes of limitations to a very short period, expecting claims to decrease proportionately. This may backfire, though, forcing claimants to file actions for fear of having claims barred that might otherwise be dropped because of recovery from injury, disinterest in pursuing litigation as time passes, etc.

Another consideration that deserves serious attention before revising statutes of limitations is the question of what is fair to the litigants. What is the point at which a plaintiff's interest in having adequate time to discover and pursue a claim is fairly balanced against the defendant's interest in having a claim barred because the plaintiff sat on his rights and allowed the evidence to become difficult for the defendant to obtain?

X. SIMULTANEOUS PURSUIT OF A BAD FAITH CLAIM WITH AN UNDERLYING CLAIM

The term "bad faith claim" generally refers to a lawsuit against an insurance company for failure to make prompt and full payment for damages for which it is liable. A bad faith claim can be brought by an insured or by a third-party plaintiff who has been injured by the insurance company's insured.

Generally, under common law, a third party plaintiff has no right to sue a wrongdoer's insurance company for dealing in bad faith. However, in Klaudt v. Flink, ____ Mont. ____, 658 P2d 1065, 40 St. Rep. 64 (1983), the Montana Supreme Court recognized that section 33-18-201, MCA, a part of the Unfair Trade Practices Act of the Montana Insurance Code, creates the right of a third party to bring a lawsuit against another's insurance company for dealing in bad faith i.e., for wrongfully refusing to pay claims for which it is clearly liable. This obligation of the insurance company to a third party who is injured by the insurance company's insured is an obligation created statutorily by the Legislature. Section 33-18-201, MCA, is limited to situations where the insurance company engages in prohibited conduct as a "general business practice", which can be shown by multiple acts by the insurance company in the handling of a single claim.

Before the Montana Supreme Court decided Klaudt v. Flink, supra, the law in Montana and most jurisdictions did not permit a bad faith claim against an insurer to proceed until the underlying action, i.e., the action against the wrongdoer by the injured party, was

concluded. In the Klaudt decision, the Supreme Court overruled this rule and held that a bad faith claim against an insurer may be filed and tried before, concurrent with, or after liability in the underlying case has been determined. In the recent case of Fode v. Farmers Insurance Exchange, ____ Mont. ____,____ P2d ____ 43 St. Rep. 814 (1986), the Court overruled the Klaudt decision based on the experience in the field in the three years since the Klaudt decision. In the Fode decision, the Court recognized that the Klaudt decision unfairly works a prejudice to insurers by allowing undue leverage to be exerted by forcing the insurer to face the prospect of two lawsuits, with the additional costs incurred for defense, and by raising difficult discovery problems involving work product and attorney-client problems affecting the underlying case.

In the Fode decision, the Montana Supreme Court held that a bad faith case may be filed to toll the statute of limitations and to expedite ultimate disposition, but that no discovery can be made and that all proceedings in the bad faith case are suspended until the liability issues of the underlying case have been determined by settlement or judgment.

Therefore, the problems for insurance companies in Montana caused by the Klaudt decision have been largely taken care of by the Fode decision and further action by the Legislature should not be required, except perhaps to codify the Fode decision in statute to limit further judicial interpretations.

XI. REINSURANCE

Reinsurance refers to an undertaking whereby one insurer agrees to assume all or part of the risk of the other, the reinsured, for a fee. Both the underlying insurance policy, between the reinsured and the original insured, and the reinsurance policy are in effect at the same time, and the original insured has no interest in the reinsurance. The contracts of insurance and reinsurance are distinct and unconnected. Insurance companies regularly reinsure all or part of their risks with reinsurance companies such as Lloyd's of London and other domestic and foreign companies.

Traditionally, reinsurance has been a matter of private enterprise between the insurance companies. Government has generally not been involved in reinsurance, except as a regulator. However, in the 1960s, the federal government established a federal reinsurance program designed to encourage insurance companies to provide property insurance in inner cities that were experiencing racial turmoil. Under prescribed guidelines, the federal program provided reinsurance to companies writing insurance in the riot-torn areas. The guidelines required each participating insurer to reinsure a certain percentage of all its business with the federal program, not just insurance written in the distressed areas. According to Mr. Bob Hunter, who administered the program, it was successful in making insurance available as intended and made a profit of $125 million.

In the March 1986 Special Session, a state reinsurance bill, HB 21, was proposed. It would have established a state program to provide reinsurance to insurers

writing "distressed" lines of insurance in Montana, i.e., types of insurance not obtainable or affordable because of the insurance crisis. The bill provided for a startup loan to be paid back with interest from the Montana in-state investment fund, and it was intended that the fund would be self-sustaining over time, through reinsurance premiums, a premium surcharge of ½ of 1%, and one-half of punitive damages awarded in the state. The bill was generally opposed by the insurance industry and was tabled by the House Business and Labor Committee. A similar bill was introduced in the Alaska Legislature this year and died in committee. Staff is not aware of any other state that has adopted a state reinsurance program.

XII. INSURANCE MARKETING ASSISTANCE PLANS

In the March 1986 Special Session, the Legislature passed HB 16 (Ch. 11, Sp. L. March 1986), creating the Montana Insurance Assistance Plan. This market assistance program is designed to assist insurance consumers in this state in obtaining liability insurance by acting as a clearinghouse for hard-to-get insurance. The plan is authorized to provide assistance for political subdivisions, day-care centers, and sellers of alcohol. The Commissioner can expand the plan to other types of insurance found to be experiencing an availability problem.

The plan creates three committees appointed by the Insurance Commissioner. The Advisory Committee oversees the plan; it receives and reviews applications for insurance and forwards the applications to the Agents

Committee. To be eligible for the program, an applicant must have been previously refused insurance by three insurance companies. The Agents Committee attempts to find insurance for each applicant through known sources of insurance, including the excess and surplus lines markets. If the Agents Committee is unable to procure insurance for an applicant through these sources, the committee refers the application to the Underwriting Committee. The Underwriting Committee sends each application referred to it to participating insurers, who must offer insurance on one out of every five applications received from the Underwriting Committee. Each liability insurer licensed to do business in Montana must participate in this voluntary plan unless it requests and receives a waiver from the Commissioner. If it is determined that the voluntary plan is ineffective in making insurance available, the Commissioner has the authority to create a joint underwriting association (JUA) which would operate in a manner similar to the voluntary plan, except that participation by insurance companies would be mandatory.

The plan is currently being implemented by the Commissioner, who is required to report to the 50th Legislature on the effectiveness of the plan. The Commissioner's authority to create a JUA is not effective until July 1, 1987, and the plan and JUA authority terminate on July 1, 1989.

6156b:LANE:jj

SENATE JUDICIARY
EXHIBIT NO. 9
DATE 1-14-87
BILL NO. S.B. 49

NAME: Steve Walker DATE: 1-14-87

ADDRESS: 512 LOGAN

PHONE: 6142-7802

REPRESENTING WHOM? MRCCA & Mental Health

APPEARING ON WHICH PROPOSAL: SD49

DO YOU: SUPPORT? X AMEND? _____ OPPOSE? _____

COMMENTS: _____

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

NAME: Ken Hoovestol DATE: 1/14/97

ADDRESS: #33 Division Rd, Great Falls 59404

PHONE: 761-3578

REPRESENTING WHOM? MT. Snowmobile Assn.

APPEARING ON WHICH PROPOSAL: SB-49

DO YOU: SUPPORT? X AMEND? _____ OPPOSE? _____

COMMENTS: _____

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

NAME: B & R Fishing DATE: 1-15-87

ADDRESS: 2225 Chinook Dr Kasilof 99603

PHONE: 251-2891

REPRESENTING WHOM? Alt Motor Carriers Assn

APPEARING ON WHICH PROPOSAL: SR 49

DO YOU: SUPPORT? X AMEND? _____ OPPOSE? _____

COMMENTS: We must support in getting good people to serve on boards of State Corporations that will serve the public good

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

NAME: Nicki Tayon DATE: 1/14/93

ADDRESS: Helena

PHONE: 442-3420

REPRESENTING WHOM? Mont Stockgrowers Association

APPEARING ON WHICH PROPOSAL: SB 49

DO YOU: SUPPORT? X AMEND? _____ OPPOSE? _____

COMMENTS: The potential for costly lawsuits against officers & directors of organizations such as the Montana Stockgrowers and other similar non-profit organizations is growing alarmingly. This bill is sorely needed to insure that we can continue to get the dedicated leadership we now have.

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.