COURT OF APPEALS
DECISION
DATED AND FILED

July 16, 2015

Diane M. Fremgen
Clerk of Court of Appeals

Appeal No. 2014AP157 **Cir. Ct. No. 2011CV874**

STATE OF WISCONSIN **IN COURT OF APPEALS**
DISTRICT IV

DENNIS D. DUFOUR,

PLAINTIFF-APPELLANT-CROSS-RESPONDENT,

V.

PROGRESSIVE CLASSIC INSURANCE COMPANY AND MILWAUKEE PAINTERS LOCAL UNION 781 HEALTH FUND,

DEFENDANTS,

DAIRYLAND INSURANCE COMPANY,

DEFENDANT-RESPONDENT-CROSS-APPELLANT.

APPEAL and CROSS-APPEAL from an order of the circuit court for Dodge County: BRIAN A. PFITZINGER, Judge. *Affirmed in part; reversed in part and cause remanded with directions*.

Before Lundsten, Higginbotham and Kloppenburg, JJ.

¶1 PER CURIAM. This case involves property damage funds received in subrogation by Dennis Dufour's insurer, Dairyland Insurance Company, from the tortfeasor's insurer, American Standard Insurance Company. At the circuit court, Dufour sought recovery of the subrogated funds from Dairyland and also alleged that Dairyland acted in bad faith in refusing to turn over the funds to him. Both Dufour and Dairyland filed motions for summary judgment. The circuit court granted Dufour's motion as to the subrogated property damage funds, and granted Dairyland's motion on the bad faith claim. Dufour appeals and Dairyland cross-appeals.

¶2 We first consider the issue presented by the cross-appeal in which Dairyland argues that Dufour is not entitled to the property damage subrogation funds it received from American Standard, the tortfeasor's insurance company. We then address the appeal, which concerns Dufour's argument that the circuit court erred when it dismissed his bad faith claims.

¶3 Based on the undisputed facts presented on summary judgment, we first conclude that Dairyland has no subrogation rights under ***Valley Forge Ins. Co. v. Home Mut. Ins. Co.***, 133 Wis. 2d 364, 396 N.W.2d 348 (Ct. App. 1986), because Dufour has not been made whole considering his total loss. We further conclude that Dairyland acted in bad faith when it denied Dufour's claim to the funds at issue. Accordingly, Dufour is entitled to summary judgment in his favor on both his claim to the subrogated property damage funds and his bad faith claim. Therefore, we affirm the circuit court's order in part and reverse it in part, and remand for proceedings on Dufour's damages, including punitive damages, in regard to his bad faith claim.

BACKGROUND

¶4 There are no disputed material facts. Dufour was involved in a motorcycle accident caused by Steven Lucero. Lucero's insurer, American Standard, paid Dufour its $100,000 policy limit for bodily injuries. Dufour's insurer, Dairyland, also paid Dufour its $100,000 policy limit for bodily injuries. In addition, pursuant to a settlement agreement, Dairyland paid Dufour $15,589.85 for his property damage. Dufour's bodily injuries exceed the total amount of insurance proceeds that he received.

¶5 Under a subrogation clause in its policy, Dairyland sought and received the property damage funds in subrogation from American Standard. Dufour submitted a claim to Dairyland in which he asserted that he was entitled to the subrogated funds under ***Valley Forge***. Dairyland denied Dufour's claim.

¶6 When Dairyland refused to turn over the subrogated funds, Dufour amended his complaint to include breach of contract, bad faith, and punitive damages claims against Dairyland. Dairyland and Dufour filed cross-motions for summary judgment. The circuit court granted Dufour's motion, in part, and awarded him the subrogated property damage funds plus interest. The court also granted Dairyland's motion in part and dismissed Dufour's bad faith and punitive damage claims. Dufour appeals and Dairyland cross-appeals.

DISCUSSION

¶7 We first address the issue raised by Dairyland's cross-appeal—whether Dufour is entitled to the property damage subrogation funds received by Dairyland. We then turn our attention to Dufour's appeal concerning whether the circuit court erred when it denied his bad faith claims.

¶8 Both issues were decided by the circuit court on cross-motions for summary judgment. We review a grant of summary judgment de novo, applying the same methodology as the circuit court. ***State v. Bobby G.***, 2007 WI 77, ¶36, 301 Wis. 2d 531, 734 N.W.2d 81. Summary judgment is appropriate when the affidavits and other submissions show that no genuine issue of material fact exists and the moving party is entitled to judgment as a matter of law. WIS. STAT. § 802.08(2) (2013-14).[1] "We draw all reasonable inferences from the evidence in the light most favorable to the non-moving party." ***Burbank Grease Servs., LLC v. Sokolowski***, 2006 WI 103, ¶40, 294 Wis. 2d 274, 717 N.W.2d 781 (citation omitted).

I. *Subrogated Property Damage Funds*

¶9 Dufour's automobile insurance policy contains the following subrogation clause: "After we have made payment under this policy and, *where allowed by law*, we have the right to recover the payment from anyone who may be held responsible." (Emphasis added.) Under the terms of this clause, whether Dairyland has a right to retain the subrogated property damage funds depends on whether recovery of such payment is allowed under Wisconsin law. In order to answer the question whether Dairyland has a right to recover under Wisconsin law, we must decide whether our decision in ***Valley Forge*** precludes Dairyland from recovering here. Dairyland argues first that ***Valley Forge*** is distinguishable and second that subsequent case law has rendered it inapplicable. For the reasons that follow, we reject both arguments.

[1] All references to the Wisconsin Statutes are to the 2013-14 version unless otherwise noted.

A. *Subrogation and the made whole doctrine in general*

¶10 Subrogation in the insurance context allows "an insurer who has been contractually obligated to satisfy a loss created by a third party to step into the shoes of its insured and to pursue recovery from the responsible wrongdoer." ***Muller v. Society Ins.***, 2008 WI 50, ¶22, 309 Wis. 2d 410, 750 N.W.2d 1. Subrogation is based on equitable principles, one of which is to prevent an insured from recovering in excess of his or her loss. ***Id.***, ¶23. It follows then, generally speaking, that in circumstances where the insured is unable to fully recover his or her loss an insurer has no rights in subrogation. ***Rimes v. State Farm Mut. Auto. Ins. Co.***, 106 Wis. 2d 263, 271-72, 316 N.W.2d 348 (1982); ***Garrity v. Rural Mut. Ins. Co.***, 77 Wis. 2d 537, 541, 253 N.W.2d 512 (1977). This concept—that an insurer has no subrogation rights until its insured has been fully compensated for his or her loss—is known as the made whole doctrine. *See* ***Rimes***, 106 Wis. 2d at 271-72; *see also* ***Garrity***, 77 Wis. 2d at 541. Whether the made whole doctrine applies is dependent on the facts of each case. ***Muller***, 309 Wis. 2d 410, ¶60.

B. ***Valley Forge***

¶11 In ***Valley Forge***, 133 Wis. 2d 364, 367-70, we held that the made whole doctrine applied and prohibited the insurer of a plaintiff from obtaining, under subrogation principles, money that the plaintiff/insured had received from a tortfeasor's insurer. We first describe ***Valley Forge*** in detail, and reject Dairyland's attempts to distinguish it. We then address Dairyland's argument that, despite language in ***Valley Forge*** to the contrary, allowing Dufour to recover the property damage subrogated funds would result in an impermissible double recovery.

¶12 In ***Valley Forge***, the injured party, Samuel McIlrath, received the bodily injury policy limit from the tortfeasor's insurance company, Home Mutual, following a vehicle accident. ***Valley Forge***, 133 Wis. 2d at 365. McIlrath's injuries exceeded Home Mutual's payment to McIlrath. ***Id.*** at 367. McIlrath also received full compensation for the damage to his vehicle from his insurance company, Valley Forge. ***Id.*** at 366. Valley Forge then requested that Home Mutual pay it the property damage funds in subrogation. ***Id.*** Home Mutual subsequently paid the subrogated property damage funds *directly* to McIlrath. ***Id.*** at 367. Valley Forge argued that it, not McIlrath, was entitled to the property damage funds because of Valley Forge's subrogation rights with respect to the property damage part of the action. Valley Forge argued that permitting McIlrath to retain both the full property damage compensation Valley Forge paid and the property damage funds from Home Mutual resulted in double recovery in violation of ***Rimes***. ***Id.*** at 367.

¶13 We disagreed and held that Valley Forge was not entitled to the subrogated funds that Home Mutual paid to McIlrath because he had not been fully compensated for all of his injuries. ***Id.*** at 365. We explained that "there is no 'double recovery' within the meaning of the ***Rimes*** rule. McIlrath had only one cause of action that included both his property damage and his injuries." ***Id.*** at 367-68 (footnote omitted). In other words, we determined that although Valley Forge fully compensated McIlrath for his property damage, it had no right in subrogation to the property damage funds from the tortfeasor's insurer because McIlrath had not been fully compensated for his bodily injuries, which arose from the same accident that caused the vehicle damage.

¶14 In determining that Valley Forge had no subrogation rights, we applied the made whole doctrine from ***Rimes*** and ***Garrity***. ***Id.*** at 368. We stated

that '"Under Wisconsin law the test of wholeness depends upon whether the insured has been completely compensated for all the elements of damages, not merely those damages for which the insurer has indemnified the insured.'" ***Id.*** (quoting ***Rimes***, 106 Wis. 2d at 275). We further explained that '"it is only when there has been full compensation for all the damage elements of the entire cause of action, that the insured is made whole.'" ***Id.***

¶15 Finally, we determined that prohibiting Valley Forge from receiving the property damage funds in subrogation produced an equitable result. ***Valley Forge***, 133 Wis. 2d at 369. We explained, "the present decision produces a just result. Although McIlrath has been paid twice for his auto loss, the wrongdoer and his insured have paid him less than his total loss." ***Id.*** Our decision concluded that when a situation arises in which the insured and insurer cannot both be made whole, the insurer must bear the loss. ***Id.*** at 369-70.

1. *Not distinguishable*

¶16 Dairyland argues that ***Valley Forge*** is distinguishable because in that case the tortfeasor's insurer paid the subrogated funds directly to the injured party whereas here the subrogated funds were paid to Dairyland. We disagree that this factual difference should lead to a different result here.

¶17 To be clear, in both cases: (1) the injured party sustained bodily injury and his property was damaged following a vehicle accident, (2) the injured party had bodily injuries that exceeded the available insurance proceeds, (3) the injured party was fully compensated for its property damages from its insurer, and (4) the insurer asserted that it had a right in subrogation to the property damage funds from the tortfeasor's insurer. While Dairyland hones in on a factual difference—that the disputed money was paid directly to the insured/plaintiff—

Dairyland does not point to any language in ***Valley Forge*** suggesting that the result in that case was affected by the fact that the subrogated funds were paid directly to the insured. Moreover, Dairyland fails to explain why this factual difference should matter. In other words, Dairyland fails to identify any reason why ***Valley Forge*** is distinguishable in a way that should produce a different result here.

2. *No double recovery*

¶18 Dairyland also argues that allowing Dufour to recover the subrogated property damage funds results in an impermissible double recovery. Dufour's position is that ***Valley Forge*** got it right when it stated that property damage and bodily injury must be considered together to determine whether an insured has been made whole. In other words, Dufour argues that his receipt of the subrogated property damage funds will not result in double recovery because we are required to determine whether he has been compensated for his total loss, rather than to compartmentalize his damages. We agree with Dufour's position.

¶19 The test for wholeness depends on whether an insured has been compensated for his or her total losses. ***Rimes***, 106 Wis. 2d at 275. In ***Rimes***, our supreme court stated,

> Under Wisconsin law the test of wholeness depends upon whether the insured has been completely compensated for all the elements of damages, not merely those damages for which the insurer has indemnified the insured.... The injured or aggrieved party is not made whole unless *all* his damages arising out of the tort have been fully compensated.

Id.

¶20 We relied on this language in ***Valley Forge*** and we are aware of no subsequently decided cases, including ***Muller***, which we discuss below, that call this language into question. In sum, ***Valley Forge*** and ***Rimes*** make clear that we are to look to all damages that Dufour incurred as a result of the motorcycle accident to determine whether he has been made whole.

C. *Case law subsequent to* ***Valley Forge***

¶21 Following our decision in ***Valley Forge***, the Wisconsin Supreme Court discussed the made whole doctrine at length in ***Muller***. Dairyland relies on ***Muller*** to argue that it rendered ***Valley Forge***'s discussion of the made whole doctrine inapplicable.[2] We disagree.

¶22 In ***Muller***, our supreme court held that the made whole doctrine does not apply when an insured voluntarily settles with the tortfeasor's insurer for an amount less than the policy limit even if that means that the insured is not fully compensated. ***Muller***, 309 Wis. 2d 410, ¶4. The court explained that

> [T]he [made whole] doctrine does not apply when an insurer has fully satisfied its obligations under an insurance contract, given its insureds the opportunity to settle their claim with the tortfeasor and the tortfeasor's insurer, the pool of settlement funds available to the insureds exceeds the total claims of both the insureds and the insurer, and the insureds settle their claim, even though the insureds' settlement, together with the insurer's policy payments, does not satisfy the insureds' total claim. *In these circumstances, the inequitable prospect of an insurer*

[2] It is evident from Dairyland's briefing that it also believes that ***Valley Forge*** should be overruled. An amicus brief filed by the Wisconsin Insurance Alliance and the Property Casualty Insurers Association of American agrees with this position. The amici, and to some extent Dairyland, recognize that we cannot overrule ***Valley Forge***. *See* ***Cook v. Cook***, 208 Wis. 2d 166, ¶53-55, 560 N.W.2d 246 (1997). Accordingly, to the extent that Dairyland argues that ***Valley Forge*** was wrongly decided, we do not address those arguments.

> *competing with its insureds for an inadequate pool of funds is not present, and the equities favor the insurer.*

Id. (emphasis added).

¶23 Dairyland focuses on the above emphasized language in ***Muller*** to argue, as we understand it, that this case also presents a situation in which there is no competition for an inadequate pool of funds between an insurer and an insured because Dufour pursued and received all of the insurance proceeds available to him. We are not persuaded.

¶24 We acknowledge that in ***Muller*** the court explained that the made whole doctrine does not apply in all circumstances. However, the exception carved out in ***Muller*** does not help Dairyland here. The reason the ***Muller*** court declined to apply the made whole doctrine hinged on the fact that the tortfeasor's policy limit was "sufficient to cover all claims, including those of both the insureds and the insurer," and on the insured's decision to settle for less than the policy limits with the tortfeasor's insurer. ***Id.***, ¶¶2, 77, 87. This situation led the ***Muller*** court to conclude that the insured and insurer had not competed for a limited pool of funds. In contrast, here, the tortfeasor's policy limits were *not sufficient* to cover all claims and Dufour did not agree to accept an amount less than the policy limits.

¶25 Furthermore, we see no language in ***Muller*** that leads us to believe that the court intended to fashion a more general rule that covered situations beyond the one addressed in that case. Thus, we see nothing in ***Muller*** that purports to modify the ***Valley Forge*** decision in any way. If anything, ***Muller*** confirms that whether the made whole doctrine applies depends on the facts of

each case. ***Id.***, ¶46. And, the facts before us here, for all relevant purposes, are identical to those in ***Valley Forge*** and very different from those in ***Muller***.

¶26 In conclusion, there are no genuine disputes of material fact as to the issue of the subrogated property damage funds. It is undisputed that Dufour's bodily injury and property damage arose from the same tort, the motorcycle accident. Furthermore, it is undisputed that Dufour has not been fully compensated for his bodily injuries. Thus, as our above discussion indicates, Dufour has not been made whole for his total loss resulting from the motorcycle accident, as a matter of law. Consequently, Dairyland has no subrogation rights and Dufour is entitled to summary judgment on his claim to the subrogated property damage funds. This produces an equitable result consistent with the principle that "where either the insurer or the insured must to some extent go unpaid, the loss should be borne by the insurer for that is a risk the insured has paid it to assume."[3] ***Garrity***, 77 Wis. 2d at 542.

II. *Cross-Appeal: Bad Faith Claim*

¶27 Dufour argues that the circuit court erred when it granted Dairyland's motion for summary judgment in regard to his bad faith claim because he established the elements of bad faith as a matter of law. For the reasons that follow, we agree with Dufour.[4] Accordingly, we reverse the circuit court and

[3] Dairyland also argues that when Dufour settled his property damage claim his claim to the subrogated funds at issue evaporated; therefore, it, not Dufour, possesses the right to the subrogation claim of action. However, our conclusion that Dairyland has no rights in subrogation because Dufour has not been made whole considering his total loss necessarily disposes of this argument as well.

[4] Because we conclude that Dufour is entitled to summary judgment on his bad faith claim, we need not address his alternate argument that he presented sufficient facts and evidence to survive Dairyland's motion for summary judgment.

remand for proceedings to determine Dufour's damages, including punitive damages.

¶28 An insured may bring a first-party bad faith claim against his or her insurer by alleging that the insurer has unreasonably withheld payment in bad faith. *See* ***Roehl Transp. Inc. v. Liberty Mut. Ins. Co.***, 2010 WI 49, ¶27, 325 Wis. 2d 56, 784 N.W.2d 542. As a prerequisite to bringing a first-party bad faith claim, an insured must establish that a breach of contract occurred. ***Brethorst v. Allstate Prop. & Cas. Ins. Co.***, 2011 WI 41, ¶65, 334 Wis. 2d 23, 798 N.W.2d 467. Here, Dairyland does not dispute that if we conclude that Dufour is entitled to the subrogated property damage funds under ***Valley Forge***, then Dairyland breached the contract and this prerequisite is met. Having confirmed the existence of the prerequisite breach of contract, we turn to the two elements that Dufour must establish to prevail on his bad faith claim.

A. *First element: no reasonable basis to deny claim*

¶29 The first element that Dufour must show is that Dairyland had no reasonable basis to deny his claim to the subrogated property damage funds. *See* ***Id.***, ¶26. "In other words, the insurer did not possess information that would lead a reasonable insurer to conclude that an [insured's] claim is fairly debatable and that therefore payment need not be made on the claim." ***Brown v. LIRC***, 2003 WI 142, ¶24, 267 Wis. 2d 31, 671 N.W.2d 279. This presents an objective question of whether a reasonable insurer under similar circumstances would have denied Dufour's claim. ***Id.*** Furthermore, under this first element we look to "whether the insurer properly investigated the claim and whether the results of the investigation were subject to a reasonable evaluation and review." ***Id.***, ¶25.

¶30 Dufour asserts that implicit in a decision that he is entitled to the subrogated property funds as a matter of law under ***Valley Forge***, is a determination that Dairyland's denial of his claim is not fairly debatable. Dufour's argument is that there is no legitimate uncertainty that ***Valley Forge*** is good law that applies to his case and establishes that Dairyland has no right to the subrogated funds at issue. Dairyland counters that it engaged in a thorough investigation of Dufour's claim and that it analyzed case law, including ***Valley Forge***, before determining that Wisconsin case law supports its denial of the claim and its position that ***Valley Forge*** is distinguishable. We disagree with Dairyland and conclude that a reasonable insurer in Dairyland's position would not have denied Dufour's claim under similar circumstances.

¶31 There is no dispute that Dairyland investigated Dufour's claim to the subrogated property damage funds. However, while Dairyland raised several defenses when it denied Dufour's claim, none of these defenses are reasonable because, as we have demonstrated, they do not square with ***Valley Forge*** or subsequently decided case law. Dairyland's attempts to distinguish ***Valley Forge*** badly miss the mark. We conclude that it is not fairly debatable that ***Valley Forge*** does not control here. A reasonable insurer in Dairyland's position would not have denied Dufour's claim.

B. *Second element: insurer knew it had no reasonable basis to deny claim*

¶32 The second element that Dufour must show is that Dairyland "knew or recklessly disregarded that there was no reasonable basis for denying benefits." ***Brown***, 267 Wis. 2d 31, ¶26. This portion of the test is subjective and depends on the strength of the insurer's reasoning for denying the claim. ***Id.*** Therefore, in

analyzing this element we turn to Dairyland's stated reasons for denying Dufour's claim.

¶33 Dairyland was aware that Dufour based his claim to the subrogated property funds on ***Valley Forge*** as evidenced by the correspondence between the parties. In its letter denying Dufour's claim, Dairyland stated, "*Valley Forge* is inconsistent with Wisconsin law and with the made-whole doctrine the court purported to apply." Specifically, its letter made the following points:

- The insured in ***Valley Forge*** was allowed to double recover his property damages, which is not consistent with Wisconsin law;
- ***Valley Forge*** improperly allowed the insured to retain the subrogation cause of action after he settled his property damages, which contradicts settled law;
- ***Valley Forge*** runs counter to insurance law and practice in that bodily injury and property damage are viewed as separate and distinct risks and are injured as such;
- Dufour has "exhausted the pool of funds to which he is entitled" because he received the policy limit for his bodily injuries and under Wisconsin law, Dairyland, not Dufour, possesses the cause of action for the subrogated funds.

¶34 Dufour then sent a second letter to Dairyland in which he reiterated his position that ***Valley Forge*** required Dairyland to turn over the subrogated property damage funds to him. Shortly thereafter, Dairyland denied Dufour's claim without further explanation.

¶35 Dufour argues that Dairyland's letter denying Dufour's claim indicates, as a matter of law, that Dairyland knew about the legal basis underlying Dufour's claim, but that it "intentionally disregarded the law when it denied the claim." Dairyland asserts that its letter denying Dufour's claim clearly indicates that it believed that "*Valley Forge* departs from the law." We agree with Dufour.

¶36 Dairyland's denial letter to Dufour makes plain that Dairyland strongly disagrees with our decision in ***Valley Forge***. However, that disagreement does not give Dairyland a good faith basis to ignore our holding. Accordingly, having established the necessary elements of a bad faith claim, Dufour is entitled to summary judgment as a matter of law. Therefore, we remand for proceedings on Dufour's damages, including punitive damages, in regard to his bad faith claim.

CONCLUSION

¶37 For the reasons stated, we affirm the circuit court in part, reverse in part, and cause remanded with instructions.

By the Court.—Order affirmed in part; reversed in part and cause remanded with directions.

This opinion will not be published. *See* WIS. STAT. RULE 809.23(1)(b)5.