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The Louisiana Direct Action Statute

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that if insurers are allowed subrogation by operation of law to its insureds' collateral causes of action they will be receiving premiums without furnishing a *quid pro quo*, its obvious fallacy is that in many instances the remedy will be hollow and in others the prosecution of the cause will be costly even if successful. Finally, should the courts of Louisiana deny subrogation by operation of law to insurers, the simple cause of action for reimbursement, based on Article 2134 of the Civil Code, is logically undeniable to insurers, who, in distributing proceeds under casualty policies, effectively discharge to the extent of payment obligations for which others were liable.

There is unfortunately no better indication of the future course of Louisiana jurisprudence than a review of the decisions already rendered. Such a review has revealed that the problem of recourse for insurers who have paid has proved sufficiently troublesome to produce a confusing collection of cases. It has been submitted that many of these cases are unsound in theory as well as in result, and that the doctrine of subrogation by operation of law offers a solution which is not only workable but is also on solid ground theoretically. There appears to be a growing disapproval of the tort remedy. As this route was the only fairly sure way to recovery open to the insurer, possibly this awareness of its several shortcomings augurs favorably for the adoption of the suggested approach.

George M. Snellings III

The Louisiana Direct Action Statute

This Comment presents a review and discussion of the Louisiana Direct Action Statute as it relates to modern automobile liability insurance. The statute will be considered as a measure designed to afford financial protection both to individuals and to the public at large in the assertion of claims arising out of automobile accident cases. Primary emphasis will be placed upon the manner in which the statute implements this purpose by providing ready procedural access to the insurer.

Utility to Injured Party

(1) *The purpose of the Direct Action Statute.* Automobile liability insurance contracts commonly contain "no action"

clauses providing that "no action shall lie against the company . . . until the amount of the insured's obligation to pay shall have been determined either by judgment or settlement against the insured after actual trial or by written agreement of the insured, the claimant and the company," or to like effect.[1] The Louisiana Direct Action Statute overcomes the effect of such policy provisions by providing that an injured person shall have a right of action directly against the insurer *prior* to determination of the amount of the insured's obligation to pay.[2] Thus, what might be

1. Louisiana's Direct Action Statute, as presently written, represents the culmination of a long developmental process which began with the passage of Act 253 of 1918. The 1918 act was designed solely to overcome in part the effect of "no action" clauses, as a result of which insurers had been able to avoid liability where the insured became insolvent or bankrupt before an injured party could obtain or enforce judgment against him. It was to avoid this result that the 1918 act provided, in essence, that the insolvency or bankruptcy of the insured would not release the insurer from liability, but rather would give the injured party a right of direct action against the insurer. By Act 55 of 1930, the scope of the 1918 act was significantly broadened to provide an injured party an action directly against the insurer "within the terms and limits of the policy"; this phrase was interpreted not to allow an insurer to insert policy terms which would deny an injured party the right of direct action given him by the statute. Rambin v. Southern Sales Co., 145 So. 46 (La. App. 2d Cir. 1932).

With the adoption of the Insurance Code of 1948, the Direct Action Statute became Section 14.45 thereof, and in 1950, enactment of the Revised Statutes found the statute given its present designation as Section 655 of Title 22. In 1950 important amendments to R.S. 22:655 were adopted, with the passage of Acts 541 and 542. Further amendment of the statute occurred by Act 475 of 1956, with the addition of a second paragraph explaining the intent and purpose of the section, and with a revision of the first paragraph, which was further revised by Act 125 of 1958, the last amendment to the section.

2. The full text of the Direct Action Statute is as follows:

"No policy or contract of liability insurance shall be issued or delivered in this state, unless it contains provisions to the effect that the insolvency or bankruptcy of the insured shall not release the insurer from the payment of damages for injuries sustained or loss occasioned during the existence of the policy, and any judgment which may be rendered against the insured for which the insurer is liable which shall have become executory, shall be deemed prima facie evidence of the insolvency of the insured, and an action against the insurer may thereafter be maintained within the terms and limits of the policy by the injured person, or his or her survivors or heirs mentioned in Revised Civil Code Article 2315. The injured person or his or her survivors or heirs hereinabove referred to at their option, shall have a right of direct action against the insurer within the terms and limits of the policy in the parish where the accident or injury occurred or in the parish where the insured or insurer is domiciled, and said action may be brought against the insurer alone or against both the insured and insurer jointly and in solido, at the domicile of either of their principal place of business in Louisiana. This right of direct action shall exist whether the policy of insurance sued upon was written or delivered in the state of Louisiana or not and whether or not such policy contains a provision forbidding such direct action, provided the accident or injury occurred within the state of Louisiana. Nothing contained in this Section shall be construed to affect the provisions of the policy or contract if the same are not in violation of the laws of this state. It is the intent of this Section that any action brought hereunder shall be subject to all of the lawful conditions of the policy or contract and the defenses which could be urged by the insurer to a direct action brought by the insured, provided the terms and conditions of such policy or contracts are not in violation of the laws

a policy of indemnity against loss to the insured, were the "no action" clause enforced, is converted, by the statute's operation, into a true policy of insurance against liability.

While most states have adopted remedial statutes, in one form or another, allowing suit by an injured party against an insurer, they generally allow such suits only *after* a determination of the insured's liability.[3] This requirement that an insured's liability be fixed before recourse can be had against his insurer probably stems from an apprehension that to allow a suit against the insurer prior to such time would result in inflated jury verdicts, with juries influenced more by the insurer's solvency than by the insured's liability.[4] The reason behind such an assumption would seem to be fast disappearing in view of the prevalence of automobile liability insurance today. In fact, it seems probable that juries would assume that a defendant is insured if not told otherwise.[5]

Louisiana's Direct Action Statute, then, is unique in the extent to which it provides recourse by injured parties against insurers.[6] As a result, automobile liability insurance in Louisiana tends to protect the public at large by providing a fund

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of this state.

It is also the intent of this Section that all liability policies within their terms and limits are executed for the benefit of all injured persons, his or her survivors or heirs, to whom the insured is liable; and that it is the purpose of all liability policies to give protection and coverage to all insureds, whether they are named insureds or additionals insureds under the omnibus clause, for any legal liability said insured may have as or for a tort feasor within the terms and limits of said policy. Amended and reenacted Acts 1958, No. 125."

3. VANCE, INSURANCE 803-04, § 135 (3d ed. 1951); Leigh, *Direct Actions Against Liability Insurers*, 1949 INS. L.J. 633, 637.

4. See 2 HARPER & JAMES, TORTS 765-71, § 13.4 (1956); James, *Accident Liability Reconsidered: The Impact of Liability Insurance*, 57 YALE L.J. 549 (1948); James & Thornton, *The Impact of Insurance on the Law of Torts*, 15 LAW & CONTEMP. PROB. 431 (1950).

5. Some states bar mention of the fact of insurance before juries, violation of which rule might be reversible error. New York is one such state. See Morton v. Maryland Cas. Co., 4 N.Y.2d 488, 176 N.Y.S.2d 329, 151 N.E.2d 881 (1958); Green, *Blindfolding the Jury*, 33 TEXAS L. REV. 157, 273 (1955).

6. In most states, the right of an injured party to recover on an automobile liability policy is determined solely by reference to the terms of the policy itself. See VANCE, INSURANCE 800-06, § 135 (3d ed. 1951). Wisconsin is the only other state which has gone so far as to allow direct actions against insurers *before* determination of tortfeasors' liability. WIS. STAT. ANN. §§ 85.93, 260.11 (1951). The statement has been made: "The Louisiana statute seems to have paved the way for a real liberalization of the old immunities. Edwards v. Royal Ind. Co., 182 La. 171, 161 So. 191 (1935); Lusk v. United States Fidelity and Guaranty Co., 199 So. 666 (La. App. 1941). The Wisconsin statute has not. Lasecki v. Kabara, 235 Wis. 645, 294 N.W. 33 (1940); Fehr v. General Accident Fire & Life Assurance Corp., 246 Wis. 228, 16 N.W.2d 787 (1944)." James & Thornton *The Impact of Insurance on the Law of Torts*, 15 LAW & CONTEMP. PROB. 431, 437, n. 28 (1950).

which can be reached by an injured party, rather than being available only to the insured as a barrier against his actual loss.[7] It is submitted that the following are advantages which result from allowing suit against an insurer prior to determination of the insured's liability. First, from a purely procedural point of view, provision for direct actions eliminates circuity in the settlement of claims in that a determination of both the insured's and the insurer's liability is made in the same proceeding. Second, allowing suit directly against an insurer permits a realistic conception of the role played by liability insurance, thus furthering the public policy of providing protection for those injured in automobile accidents by permitting the fact of insurance to be considered by the courts and juries.

(2) *Defenses against the direct action.* Since an insurer is subject to a direct suit by an injured party, it becomes important to determine to what extent the defenses which would be available to the insured against the plaintiff will be available to the insurer. It is a well-established rule that, in a direct action against an insurer, only the general defenses of the insured can be urged by the insurer.[8] Thus, an insurer cannot successfully rely upon any defense which is purely personal to the insured.[9] One example of this is found in cases denying to an insurer the right to rely upon the defense of interspousal immunity in an action by a spouse against the other spouse's insurer.[10] Nor may an insurer assert the defense of sovereign immunity available to governmental units or their agencies. This has been held to be a defense personal to the governmental unit or agency, so that it will not avail the insurer.[11] Similarly, the defense of charitable immunity is not available to an insurer in a direct action.[12] On

7. See Leigh, *Direct Actions Against Liability Insurers*, 1949 INS. L.J. 633, 680.

8. McDowell v. National Sur. Corp., 68 So.2d 189 (La. App. 1st Cir. 1953), *appeal dismissed*, 347 U.S. 995 (1954).

9. Ruiz v. Clancy, 182 La. 935, 162 So. 734 (1935); Edwards v. Royal Indemnity Co., 182 La. 171, 161 So. 191 (1935); Harvey v. New Amsterdam Casualty Co., 6 So.2d 774 (La. App. Orl. Cir. 1942).

10. Edwards v. Royal Indemnity Co., 182 La. 171, 161 So. 191 (1935); Harvey v. New Amsterdam Casualty Co., 6 So.2d 774 (La. App. Orl. Cir. 1942). Similarly, a suit by a wife against her husband's employer's liability insurer for injuries sustained by her through his negligent operation of an automobile while in the scope of his employment has been held maintainable as against the insurer's plea of the defense of interspousal immunity. LeBlanc v. New Amsterdam Casualty Co., 202 La. 857, 13 So.2d 245 (1943).

11. Brooks v. Bass, 184 So. 222 (La. App. Orl. Cir. 1938); Rome v. London & Lancashire Indemnity Co., 169 So. 132 (La. App. Orl. Cir. 1936).

12. Lusk v. United States Fidelity & Guaranty Co., 199 So. 666 (La. App. Orl. Cir. 1941).

the other hand, the insurer may assert such general defenses as contributory negligence[13] and prescription.[14]

The Direct Action Statute provides that "an action against the insurer may . . . be maintained *within the terms and limits of the policy.*"[15] (Emphasis added.) It is thus important to determine the legal effects of a failure by the insured to comply with certain conditions found generally in automobile liability insurance policies. The Louisiana Supreme Court, in *West v. Monroe Bakery*,[16] held that the insured's failure to comply with a policy requirement that the insurer be given notice of an accident "as soon as practicable"[17] would not prevent recovery by the injured party under the Direct Action Statute. The court reasoned that the right of direct action conferred on an injured third party by the statute vests in him immediately upon the occurrence of an accident, and is not contingent upon any stipulation between the insurer and the insured, contained in the policy contract. The court cited with favor an earlier decision[18] in which a notice clause had been interpreted as relating only to cases where the insured has paid a damage claim and seeks to be reimbursed by his insurer. The court in *West* relied upon the same case as to the meaning of the provision in the statute granting a direct action "within the terms and limits of the policy,"[19] holding that it was not intended to include the requirement of notice, but referred only to the amount which might be recovered and to those other warranties and conditions with which it was within the power of the injured party to comply. As to the possibility that such an interpretation might work a hardship upon an insurer, the court stated that the insurer's obvious relief was through legislative action. Further, the benefit of the doubt should be given the innocent injured party as against the insurer, who has entered into the contract with full knowledge of the statute and for a monetary consideration. The court did, however, expressly recognize the possibility of an action over

13. See Rome v. London & Lancashire Indemnity Co., 169 So. 132 (La. App. Orl. Cir. 1936).

14. See Hidalgo v. Dupuy, 122 So.2d 639 (La. App. 1st Cir. 1960).

15. LA. R.S. 22:655 (1950), amended and re-enacted, La.Acts 1958, No. 125.

16. 217 La. 189, 46 So.2d 122 (1950).

17. 217 La. 189, 202, 46 So.2d 122, 127 (1950). The disputed policy provision read in full: "When an accident occurs written notice shall be given by or on behalf of the insured to the company or any of its authorized agents as soon as practicable."

18. Edwards v. Fidelity & Casualty Co., 11 La. App. 176, 123 So. 162 (Orl. Cir. 1929).

19. La. Acts 1930, No. 55, amended and re-enacted, La. Acts 1958, No. 125.

against the insured by the insurer, for breach of policy provisions.[20]

The holding of the *West* decision, that the rights of an injured third party to maintain a direct action become fixed at the time of an accident, would seem sufficiently broad to eliminate, as a defense to the insurer, the insured's failure to comply with *any* policy provision subsequent to the occurrence of an accident.[21] Thus, it would appear that non-cooperation of the insured would be no defense against an injured third party's direct action, despite the fact that virtually all automobile liability policies require that the insured assist the insurer in the defense of any action covered by the policy.[22] A like result should obtain in the event that the insured ceases to pay policy premiums after the occurrence of an accident, though in violation of policy provisions.

In Section 900 of the Louisiana Safety Responsibility Law,[23] it is provided in part:

> "F. Every motor vehicle liability policy shall be subject to the following provisions which need not be contained therein: (1) The liability of the insurance carrier with respect to the insurance required by this Chapter shall become absolute whenever injury or damage covered by said motor vehicle liability policy occurs; said policy may not be cancelled or annulled as to such liability by an agreement between the insurance carrier and the insured after the occurrence of the injury or damage; no statement made by the insured or on his behalf and no violation of said policy shall defeat or void said policy . . . . H. Any motor vehicle liability policy may provide that the insured shall reimburse the insurance carrier for any payment the insurance carrier would not have been obligated to make under the terms of the policy except for the provisions of this Chapter."

The insurance policy with which the court was concerned in

20. 217 La. 189, 202, 46 So.2d 122, 127 (1950): "It would seem that the rule of common sense is that this is a matter entirely between the assured and its insurer, and that the insurer has a cause of action for the contract breaching against the insured."

21. For a case involving an admission of liability by the insured, in violation of policy provisions, see U-Drive-It Car Co. v. Freidman, 153 So. 500 (La. App. Orl. Cir. 1934).

22. See American Fire & Cas. Co. v. Gresham, 195 F.2d 616 (5th Cir. 1952).

23. LA. R.S. 32:851-1043 (Supp. 1960), enacted La. Acts 1952, No. 52, § 41. R.S. 32:900 defines with particularity a "Motor Vehicle Liability Policy."

West was an ordinary automobile liability policy, as distinguished from a "motor vehicle liability policy," the latter being a policy certified in accordance with the requirements of the Safety Responsibility Law as proof of financial responsibility against liability arising out of future automobile accidents. A person may be required to prove such financial responsibility for the future when he fails to satisfy a judgment arising out of a prior accident.[24] The clear purpose of this requirement is to provide effective recourse against such person to those who may sustain damage or injury as a result of his negligence in future accidents. The above-quoted language of the Safety Responsibility Law would seem to adopt the rule of the *West* decision, as to "motor vehicle liability policies," insofar as it denies to insurers the power to avoid liability to injured persons by reason of a breach of policy provisions by the insured *subsequent* to the occurrence of an accident. A further question, however, is whether these provisions might not deny the insurer the power to avoid liability under a "motor vehicle liability policy" even if its insured breached a condition of the policy *before* the occurrence of the accident out of which an injured party's claim arose. While no cases were found on this point, it is arguable that an insurer should not escape liability in such a situation unless it has taken proper steps to have the "motor vehicle liability policy" rescinded by reason of the breach.

Instances in Which a Direct Action Is Available

(1) *Accident must occur in Louisiana.* The Direct Action Statute provides that "This right of direct action shall exist whether the policy of insurance sued upon was written or delivered in the state of Louisiana and whether or not such policy contains a provision forbidding such direct action, *provided the accident or injury occurred within the state of Louisiana.*"[25] Although the above-quoted provision was not contained in the statute until added by a 1950 amendment,[26] the Louisiana Supreme Court had earlier ruled that no direct action was maintainable on an accident which had occurred in Mississippi.[27] In that decision, the court stated that the statute was procedural rather

24. *Id.* 32:892.
25. LA. R.S. 22:655 (1950), amended and re-enacted, La. Acts 1958, No. 125.
26. La. Acts 1950, No. 541.
27. Burke v. Massachusetts Bonding & Ins. Co., 209 La. 495, 24 So.2d 875 (1946).

than substantive,[28] viewing it as affecting the injured party's *means* of recovery rather than *right* to recover. On this basis, the court concluded that the statute could give the injured party no more rights than she had under Mississippi law; and since that state did not give plaintiff wife a cause of action against her husband, no action could be maintained in Louisiana courts directly against the husband's insurer.

(2) *Locus of the Insurance Contract.* (a) *Louisiana contracts.* Under the provisions of the Louisiana Insurance Code,[29] a foreign or alien liability insurer must, as a condition precedent to doing business in Louisiana, consent to be sued in a direct action "whether the policy of insurance sued upon was written or delivered in the state of Louisiana or not." Even prior to the enactment of this provision, the Direct Action Statute had been upheld when applied to insurance contracts issued or delivered within the state, by virtue of the provisions of the statute itself.[30] Greater difficulty, however, has been encountered in the application of the statute to out-of-state contracts.

(b) *Out-of-state contracts.* In *Robbins v. Short*,[31] a Louisiana court of appeal allowed a direct action where the accident had occurred in Louisiana, even though the policy was written in Missouri and contained a "no action" clause. The court's view was that the statute was merely remedial and procedural, and therefore that to allow the suit deprived the insurer of no substantial right under the Missouri contract. Subsequently, however, grave questions concerning the constitutionality of applying the statute to out-of-state insurance contracts were raised in the federal courts.[32] It was left to the United States Supreme

28. *Cf.* Vowell v. Manufacturers Cas. Ins. Co., 229 La. 798, 86 So.2d 909 (1956).

29. LA. R.S. 22:983 (1950), amended and re-enacted, La. Acts 1958, No. 125.

30. Gager v. Teche Transfer Co., 143 So. 62 (La. App. 1st Cir. 1932); Rossville Commercial Alcohol Corp. v. Dennis Sheen Transfer Co., 18 La. App. 725, 138 So. 183 (Orl. Cir. 1932).

31. 165 So. 512 (La. App. 1st Cir. 1936).

32. Shortly following the incorporation of the Direct Action Statute into Louisiana's Insurance Code of 1948, as Section 14.45, serious questions concerning the applicability of the statute to out-of-state insurance contracts were raised in Belanger v. Great American Indemnity Co., 89 F. Supp. 736 (E.D. La. 1950), in which it was held that the legislature did not intend the statute to apply to out-of-state contracts. The court also stated that it would be *unconstitutional* to apply the statute to such out-of-state contracts if they contained "no action" clauses valid in the state in which the contract was written. Acts 541 and 542 of 1950 appear to have been intended to accomplish a legislative overruling of the *Belanger* decision. Act 541 amended the Direct Action Statute so as to provide that a right of direct action exists whether or not the insurance policy was written or delivered in Louisiana, and regardless of whether or not

Court, in *Watson v. Employers' Liability Assurance Corp.*,[33] to resolve the questions by sustaining the application of the statute to out-of-state contracts where the accidents occur in Louisiana. The Court in *Watson* rejected contentions that application of the statute to an out-of-state policy was violative of the equal protection,[34] due process,[35] contract,[36] and full faith and credit[37] clauses of the United States Constitution.

Procedural Considerations

(1) *Is the Direct Action Statute procedural or substantive?*

(a) *State courts.* In *West v. Monroe Bakery*,[38] the Louisiana Supreme Court characterized the Direct Action Statute as being

the policy's provisions forbid a direct action against the insurer, provided the accident or injury occurred within the State of Louisiana. Act 542 was passed to avoid the objection raised in the *Belanger* decision that the application of the Direct Action Statute in a case involving an out-of-state policy containing a "no action" clause would constitute an unconstitutional deprivation of property without due process of law. That act amended the statute so as to require that foreign or alien insurers consent to be sued directly by an injured party as a condition precedent to doing business in the state. In Bouis v. Aetna Casualty & Surety Co., 91 F. Supp. 954 (W.D. La. 1950), Act 541 was given retrospective effect in the application of the Direct Action Statute to an out-of-state insurance contract which contained a "no action" clause. By characterizing Acts 541 and 542 as remedial and procedural, the court justified their retrospective application to the policy in question. Bayard v. Traders and General Ins. Co., 104 F. Supp. 7 (W.D. La. 1952), however, specifically held the Direct Action Statute to be substantive, with the result that it could not constitutionally be applied to an out-of-state insurance policy. The court stated that the consent to be sued filed by the defendant insurance company "was exacted as a condition to the defendant's doing business in the state, and to that extent was coerced and should be strictly construed as in derogation of a common right." *Id.* at 7.

33. 348 U.S. 66 (1954).

34. As to the contention that the Direct Action Statute constituted a denial of equal protection, the Court answered: "The State's direct action provisions fall with equal force upon all liability insurance companies, foreign and domestic. Employers point to no other provisions of the Louisiana law or to facts of any nature which give the slightest support to any charge of discriminatory application of the direct action statute." 348 U.S. 66, 70 (1954).

35. The Court concluded that the Direct Action Statute did not violate due process, in light of "Louisiana's legitimate interest in safeguarding the rights of persons injured there." 348 U.S. 66, 73 (1954). Neither did Louisiana's compelling foreign insurers to consent to direct actions violate due process; "Louisiana has a constitutional right to subject foreign liability insurance companies to the direct action provisions of its laws whether they consent or not." *Id.* at 74.

36. *Id.* at 70: "[S]ince the direct action provisions became effective before this insurance contract was made, there is a similar lack of substantiality in the suggestion that Louisiana has violated Art. I, section 10, of the United States Constitution which forbids states to impair the obligation of contracts."

37. *Id.* at 73: The Court stated that the Full Faith and Credit Clause "does not automatically compel a state to subordinate its own contract laws to the laws of another state in which a contract happens to have been executed. Where, as here, a contract affects the people of several states, each may have interests that leave it free to enforce its own contract policies."

38. 217 La. 189, 46 So.2d 122 (1950).

substantive in the sense that substantive rights to proceed directly against an insurer vest immediately upon the occurrence of an accident. The question involved in that case, however, related to the failure of the insured to give timely notice to the insurer that an accident had occurred. Thus, it might be argued that the question whether the Louisiana courts will treat the statute as substantive for other purposes, such as whether or not it can be applied to accidents occurring in other states, or to insurance contracts written and delivered in other states, was not touched upon in *West*.[39] These latter questions, however, have been dealt with by the specific language of the statute.[40]

Applicability of the Direct Action Statute to actions brought in other states on accidents which occurred in Louisiana has been considered in the courts of Texas and New York. In a recent Texas Supreme Court decision,[41] the statute was construed as being procedural "in so far as it provides for joinder of a liability or indemnity insurance company with the insured in tort cases."[42] The court stated that it was compelled to reach that conclusion because the Texas Supreme Court rules treat the subject matter of joinder of parties as procedural, and further, because the Texas Rules of Civil Procedure prohibit the joinder in tort cases of a liability insurer, in the absence of specific authorization by Texas statute. The New York Court of Appeals reached the same result,[43] but based its determination solely upon the provision of the Direct Action Statute authorizing a direct action "in the parish where the accident or injury occurred or in the parish where the insured has his domicile,"[44] concluding that this language restricted the bringing of direct

39. In Vowell v. Manufacturers Casualty Insurance Co., 229 La. 798, 812, 86 So.2d 909, 914 (1956), the court said that the Direct Action Statute is "purely remedial and does not affect substantial rights under the insurance contract nor impair its obligations." In Home Insurance Co. v. Highway Insurance Underwriters, 222 La. 540, 62 So.2d 828 (1952), the court held that the statute is remedial in that it avoids the necessity for recovery from an insured and then subsequently from an insurer. See Robbins v. Short, 165 So. 512 (La. App. 1st Cir. 1936); Lowery v. Zorn, 157 So. 826 (La. App. 2d Cir. 1934); Rossville Commercial Alcohol Corp. v. Dennis Sheen Transfer Co., 18 La. App. 725, 138 So. 183 (Orl. Cir. 1932).

40. LA. R.S. 22:655 (Supp. 1960): "This right of direct action shall exist whether the policy of insurance sued upon was written or delivered in the state of Louisiana or not and whether or not such policy contains a provision forbidding such direct action, provided the accident or injury occurred within the state of Louisiana."

41. Penny v. Powell, 347 S.W.2d 601 (Tex. 1961).

42. *Id.* at 603.

43. Morton v. Maryland Cas. Co., 4 N.Y.2d 488, 176 N.Y.S.2d 329, 151 N.E.2d 881 (1958).

44. LA. R.S. 22:655 (Supp. 1960).

actions against the insurer to the appropriate Louisiana parishes only. The court observed that the lower court had also considered the fact that a direct action opposes New York's public policy of eliminating the fact of insurance from the jury's consideration, but emphasized that this consideration played no part in its determination.[45]

(b) *Federal courts.* In *Lumbermen's Mutual Casualty Co. v. Elbert*,[46] the United States Supreme Court sustained the diversity jurisdiction of a United States District Court sitting in Louisiana over a plaintiff and a defendant insurer of diverse residences, despite the fact that the plaintiff and the insured were both Louisiana residents. The Court, in reaching its conclusion that defendant insurer, an Illinois corporation, was the "real party at interest,"[47] followed the lead taken by the Louisiana Supreme Court, which had "characterized the statute as creating a separate and distinct cause of action against the insurer."[48] To defendant's contention that the tortfeasor was an indispensable party to the litigation, whose presence would destroy diversity of citizenship, the Court replied that "the state has created an optional right to proceed directly against the insurer; by bringing the action against petitioner [the insurer], respondent has apparently abandoned her action against the tortfeasor."[49] Fi-

45. Federal courts in both Texas and New York had previously reached results contrary to those reached by the state courts. Chambless v. National Industrial Laundries, 149 F. Supp. 504 (E.D. Tex. 1957); Collins v. American Automobile Insurance Co., 230 F.2d 416 (2d Cir. 1956).

46. 348 U.S. 48 (1954).

47. *Id.* at 51.

48. *Ibid.*

49. *Id.* at 52. The statement that "by bringing the action against petitioner [the insurer], respondent has apparently abandoned her action against the tortfeasor" seems open to question. Although an extended discussion of the point is beyond the scope of this Comment, it has been indicated that to obtain judgment against the *insured* alone will not result in an abandonment of the injured party's rights against the insurer. In Sewell v. Newton, 152 So. 389 (La. App. Orl. Cir. 1934), a defendant obtained judgment in reconvention against an insured. The court said: "[Defendant] needs no reservation of its rights against the insurance carrier of [plaintiff]. Under the statute referred to [the Direct Action Statute], its right is to proceed directly against either the principal or the insurer, or both, and to seek solidary judgments. *So long as the claim is not paid by one* [either the insured or the insurer], *the right to sue the other exists.*" (Emphasis added.) *Id.* at 393.

On the other hand, it has been indicated that *dismissal on the merits* of an injured party's direct action against an insurer *will* bar a subsequent action against the insured. In Emmco Insurance Co. v. Globe Indemnity Co., 237 La. 286, 290, 111 So.2d 115, 117 (1959), the court said in dictum: "[O]n a dismissal of the suit of plaintiff against the insurer alone, following a finding that he was solely responsible for the accident, unquestionably he would be barred from instituting an action against the insured."

It appears that three problems must be distinguished: (1) Will merely *obtaining* a judgment against either the insured or the insurer alone, without

nally, the Court refused to decline, as a matter of discretion, to exercise its jurisdiction over suits against an insurer alone. Defendant had urged that the federal courts should do so upon the basis that Louisiana civil cases are normally tried without a jury. The Court held that the case fell squarely within the language of the congressional grant of jurisdiction to the lower federal courts. Thus, as a result of the decision in *Elbert*, it is settled that an injured Louisiana resident will have access to the federal courts sitting in Louisiana against an out-of-state insurer, regardless of the fact that the tortfeasor may himself be a Louisiana resident. This being so, it is submitted that, although the Court did not deal specifically with the question, the *Elbert* decision must necessarily be read as having characterized the Direct Action Statute as being "substantive" rather than "procedural" for purposes of characterization under *Erie Railroad v. Tompkins*.[50]

(2) *Third party practice under the direct action statute.*

(a) *In Louisiana courts.* Article 1111 of the Louisiana Code of Civil Procedure allows the defendant in a principal action to call in any person, including a co-defendant, "who is or may be liable to him for all or part of the principal demand." By this means, a defendant insurer may call its insured, the alleged tortfeasor, into a direct action, but *only* by asserting that the insured is or may be liable to it for all or part of the principal demand. This being so, the availability of this aspect of third party practice to insurers is severely limited. It would appear that an insurer will be allowed to call in its insured as a third party defendant only in situations such as those involving a breach of the policy provisions by the insured, which might give rise to an action against the insured. Even so, however, Article 1111 is useful in that the insurer having a claim against its insured is not required to assert it in a subsequent action.[51]

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having satisfaction on it, bar a subsequent suit against the other? (2) Will both obtaining *and* satisfying a judgment against either the insured or the insurer alone bar a subsequent suit against the other? (3) Will dismissal on the merits of a suit against either the insured or the insurer bar a subsequent suit against the other?

50. 304 U.S. 64 (1938). The federal courts are to apply the substantive law of the state of the forum in all matters other than those governed by the Federal Constitution or by Acts of Congress. Matters strictly procedural, on the other hand, are governed in the federal courts by the Federal Rules of Civil Procedure.

51. LA. CODE OF CIVIL PROCEDURE art. 1091 (1960) would allow an insured to intervene in a direct action suit, originally brought against his insurer.

(*b*) *In federal courts.* Under Rule 14(a) of the Federal Rules of Civil Procedure, a defendant may, within the discretion of the trial judge,[52] call in as third party defendant, a person not a party to the action,[53] who is or may be liable to him for all or part of plaintiff's claim against him. Thus, under the federal rule, as under the Louisiana rule, an insurer desiring to call in its insured as third party defendant would be limited by the requirement that it assert that the insured is or may be liable to it in whole or in part. When, however, the insured is able and allowed to assert a third party demand against its insured in federal court, the fact that the insured may be a resident of the same state as the plaintiff will not destroy the court's diversity jurisdiction; in such a situation, the court is considered as having ancillary jurisdiction over the third party defendant.[54]

In *Pucheu v. National Sur. Corp.*,[55] defendant insurer availed itself of the provisions of Rule 14(a) to call as third party defendants the driver and insurer of the automobile in which plaintiff was a passenger at the time of its collision with its insured's automobile. This, of course, amounted to a double direct action — one by the injured party against defendant insurer, and another by defendant insurer against the third party defendant insurer of the other automobile. By this means, defendant insurer was able to assert that ultimate liability should fall elsewhere than on it, without having to institute a subsequent suit to do so.

(3) *Subrogation of insurer to rights of insured.*

The question arises whether an insurer, which has been subrogated to the rights of its insured by the payment of the insured's claim, can itself maintain a subsequent direct action against the alleged tortfeasor's insurer, without first obtaining judgment against the tortfeasor himself.[56] The Louisiana Court of Appeal for the Second Circuit, in *World Fire & Marine Ins. Co. v. American Automobile Ins. Co.*,[57] appears to have answered

52. Under *id.* art. 1111, the trial judge does not have the discretion to refuse to allow a defendant to call in a third party.

53. *Ibid.* A third party defendant may be "*any* person, including a codefendant." (Emphasis added.)

54. BENDER, FEDERAL PRACTICE MANUAL 97-98 (1948). A minority view is to the contrary. Federal Rule 24 sets out the federal rule as to intervention, as by an insured whose insurer is the defendant in a direct action.

55. 87 F. Supp. 558 (W.D. La. 1949).

56. See Comment, 22 LOUISIANA LAW REVIEW 225 (1961), dealing extensively with the subject of insurer's subrogation.

57. 42 So.2d 565 (La. App. 2d Cir. 1949).

in the negative. The court there relied upon the language of the Direct Action Statute that "the injured party or his or her heirs, at their option, shall have a right of direct action against the insurance company."[58] The court reasoned that the statute, being in derogation of a common right, must be strictly construed, and that its provisions granting a right of direct action thus cannot be extended to include any class, group, or individual not comprehended under the definition "the injured party or his . . . heirs." Subsequently, however, in *Motors Ins. Corp. v. Employers' Liability Assur. Corp.*,[59] the First Circuit Court of Appeal *did* allow a direct action by an insurer against an alleged tortfeasor's insurer. The court there, while noting the result reached in the *World Fire* case, apparently purported to distinguish it by saying: "In the case at bar, we are dealing with a conventional subrogation,"[60] implying that the *World Fire* case did *not* involve conventional subrogation. The court went on to say that the subrogee was not exercising a right by virtue of the Direct Action Statute, which gives him no such right, but rather "by virtue of the articles of the Civil Code and the established jurisprudence of this state which hold that he is substituted for the subrogor in all of the latter's rights, actions and remedies."[61] This language seems in direct conflict with the decision reached in the *World Fire* case. If, however, the latter decision has any vitality, it would appear that it will not limit to any significant degree the maintenance of direct actions by the insurer, in light of the fact that automobile liability insurance policies generally do contain conventional subrogation provisions.

Conclusion

Through the enactment of its Direct Action Statute, Louisiana has taken a significant step in recognizing the social importance of modern automobile liability insurance as a means by which persons injured as a result of automobile accidents may obtain financial relief for their losses. This recognition involves a basic determination that the obligation assumed by the liability insurer is undertaken not only to indemnify the insured against

58. La. Acts 1930, No. 55, incorporated as LA. R.S. 22:655 (1950), amended and re-enacted by La. Acts 1958, No. 125. This portion of the statute was amended by La. Acts 1956, No. 475, to include "survivors."

59. 52 So.2d 311 (La. App. 1st Cir. 1951).

60. *Id.* at 313.

61. *Id.* at 315. The court's decision was predicated on LA. CIVIL CODE arts. 2159 and 2160 (1870).

losses he may actually sustain, but also to provide a fund directly available to one injured as a result of acts of the named insured or of additional insureds under the expanded coverage currently afforded by liability policies. The approach taken by Louisiana towards a solution of the problems engendered by today's widespread use of automobiles, with all their potential for causing damage, is a realistic evaluation of the role played by automobile liability insurance. The courts have liberally construed the provisions of the statute so as best to serve the purposes it was designed to fulfill.

John Schwab II

Free Enterprise—Cost of Capital Rate Determination: "Rolled In" Costs

A public utility rate proceeding is of interest to the general public only in that the final result of it may be an increase or decrease in the prices paid by the public for the service they receive from that particular utility. The price paid by the consumer for service, however, is fixed only after consideration of many factors which bear both on the interest of the public in lower rates, and the interest of the utility in maintaining a financially sound enterprise. It would seem that a fair rate determination should arrive at the best balance between the interests of the consumer and the interests of the utility and its investors. In order for a utility to be financially sound, it must receive revenues in excess of its operating expenses that will enable it to retire its fixed indebtedness and to pay a fair return to its investors.[1] This excess is usually expressed as a percentage of the total capital investment of the utility, known as the composite rate of return.

1. This is basically a statement of the rule announced in the case of Federal Power Commission v. Hope Gas Co., 320 U.S. 591, 603 (1944), wherein the Court stated: "[T]he fixing of 'just and reasonable' rates involves a balancing of the investor and the consumer interests. . . . From the investor or company point of view, it is important that there be enough revenues not only for operating expenses, but also for the capital costs of the business. These include service on the debt and dividends on the stock. . . . By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital."