HOUSE BILL REPORT
ESSB 5726

As Passed House - Amended:
April 5, 2007

Title: An act relating to creating the insurance fair conduct act.

Brief Description: Creating the insurance fair conduct act.

Sponsors: By Senate Committee on Consumer Protection & Housing (originally sponsored by Senators Weinstein, Kline and Franklin).

Brief History:
Committee Activity:
Insurance, Financial Services & Consumer Protection: 3/22/07, 3/29/07 [DPA].
Floor Activity:
Passed House - Amended: 4/5/07, 59-38.

Brief Summary of Engrossed Substitute Bill
(As Amended by House)

- Prohibits the unfair practice of an insurer unreasonably denying a claim for coverage or payment of benefits to a first party claimant.
- Requires a court to award actual damages sustained, together with the costs of the action, including reasonable attorneys' fees and litigation costs if an insurer: (1) unreasonably denied a claim; (2) violated one of five specific unfair practice rules; or (3) violated an unfair practice rule adopted under unfair practice rule-making authority by the Insurance Commissioner intended to implement this act.
- Allows a court to award up to triple the amount of actual damages if an insurer: (1) unreasonably denied a claim; (2) violated one of five specific unfair practice rules; or (3) violated an unfair practice rule adopted under unfair practice rule-making authority by the Insurance Commissioner intended to implement this act.

HOUSE COMMITTEE ON INSURANCE, FINANCIAL SERVICES & CONSUMER PROTECTION

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Majority Report: Do pass as amended. Signed by 5 members: Representatives Kirby, Chair; Kelley, Vice Chair; Hurst, Santos and Simpson.

Minority Report: Do not pass. Signed by 3 members: Representatives Roach, Ranking Minority Member; Strow, Assistant Ranking Minority Member and Rodne.

Staff: Jon Hedegard (786-7127).

Background:

The Insurance Commissioner (Commissioner) oversees the insurance business in this state. The Commissioner reviews rates and policy forms. The Commissioner conducts financial examinations and reviews fiscal information to ensure solvency. The Commissioner performs market conduct examinations to ensure compliance with laws regarding claims practices, marketing, sales, rates, forms, and underwriting.

Consumer Protection Act
The Washington Consumer Protection Act (CPA) declares that unfair and deceptive practices in trade or commerce that harm the public interest are illegal. The CPA gives the Office of the Attorney General the authority to bring lawsuits against businesses, and to ask the court for injunctions and restitution for consumers. It also allows individuals to hire their own attorneys to bring consumer protection lawsuits. If the consumer wins in court, the law allows the court to award up to triple the amount of actual damages, up to $10,000, as well as attorneys' fees.

Unfair Insurance Practices
Chapter 48.30 RCW includes specific practices that the Legislature has determined to be unfair or deceptive practices. The Commissioner has the authority in RCW 48.30.010 to adopt rules to prohibit unfair or deceptive practices. These rules are primarily found in Chapter 284-30 WAC and are generally categorized as either unfair claims settlement practices or unfair trade practices.

Violations of the statutes and rules can be punished by fine by the Commissioner. The Commissioner may also issue a cease and desist order.

Violations of provisions of the unfair practice statutes and rules have been held to be violations of the CPA.

Summary of Amended Bill:

"First party claimant" means an individual, corporation, association, partnership or other legal entity asserting a right to payment as a covered person under an insurance policy or insurance contract arising out of the occurrence of the contingency or loss covered by such policy or contract.

An insurer may not unreasonably deny a claim for coverage or payment of benefits to any first party claimant.

Any first party claimant who is unreasonably denied a claim for coverage or payment of benefits by an insurer may bring an action in the superior court to recover the actual damages sustained, together with the costs of the action, including reasonable attorneys' fees and litigation costs.

The superior court must award reasonable attorneys' fees and actual and statutory litigation costs, including expert witness fees, to a first party claimant if their insurer has:
- acted unreasonably in denying a claim for coverage or payment of benefits;
- violated one of five specific unfair practice rules; or
- violated an unfair claims settlement practice rule adopted by the Commissioner that is intended to implement the act and is codified in chapter 284-30 of the Washington Administrative Code.

The superior court may increase the total award of damages to an amount not to exceed three times the actual damages if the insurer has:
- acted unreasonably in denying a claim for coverage or payment of benefits;
- violated one of five specific unfair practice rules; or
- violated an unfair claims settlement practice rule adopted by the Commissioner that is intended to implement the act and is codified in chapter 284-30 of the Washington Administrative Code.

The existing ability of a court to make any other determination regarding an unfair practice by an insurer or provide for any other remedy that is available at law is specifically not limited by the bill.

A first party claimant must give written notice to the insurer and the Insurance Commissioner 20 days before filing suit. Notice is deemed to be received three business days after it is mailed. The statute of limitation is tolled for the 20-day period.

The remedies are not available in an action against a health plan offered by a health carrier.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Amended Bill: The bill takes effect 90 days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony:

(In support) Many people are happy with their insurer until they file a claim. An insurer has no incentive to treat an insured fairly. The worst outcome for an insurer is to be sued for the amount they owe plus up to $10,000 under the Consumer Protection Act. The bill was narrowed to exclude third-party liability. Negligence is also removed as a cause of action. This bill brings Washington into line with other states. Not all states have treble damages but many have punitive damages. I am an attorney and have been concerned about this subject

since I became aware of the law in Washington. I worked on this subject with the Washington State Trial Lawyers Association. I know the Attorney General received a number of complaints by insureds but I do not have the number of complaints or percentages.

Washington places greater burdens on insureds than most states. The anti-fraud laws mean a misstatement by an insured could lead to a claim denial. If an insured files a suit, all they can get is what they are originally owed. That is not much of a disincentive if you treat people unfairly. The treble damages apply if there was harm or damage to an insured. Insurers say there isn't a problem. Even if this only applies to 4,000 people, isn't that enough? Many people don't file complaints with the Office of the Insurance Commissioner, the real figure may be much higher. In California, the situation is different. Voters also passed Proposition 103 in 1988. Those types of protections don't exist in Washington. Insurers made similar claims when the Patient Bill of Rights was passed. The increased liability would lead to an explosion of suits and increased premiums. That has not happened. In states that have unlimited punitive damages, trial lawyers have supported split-recovery provisions. There aren't punitive damages in the bill. Insurers in the 1990s began to work with consulting firms to try to figure out how to reduce claims. If the goal is to reduce claims or to investigate a certain percentage of claims, a conflict is created. The insurers use the judicial system to depress claims payment. They routinely shave claims. This bill could lead to an initial increase in claims but then insurers' behavior will be corrected to avoid violations. The market will also adjust. If some insurers have to pay more in damages because they are cheating claimants, they will be at a competitive disadvantage.

The bill is designed to address unreasonable actions. The OIC will look at complaints but doesn't have the resources to do anything about violations. Insurers can take an excessive amount of time to resolve claims. The treble damages provision is the most significant part of the bill. Washington doesn't have punitive dames. An increase in claims is unlikely in some areas. We don't see many cases involving life insurance or health insurance. The bulk of the claims issues is related to property and casualty insurance. I have claims related to the windstorm.

(Opposed) We oppose the bill. The Senate bill was worked on and has changed. The negligence provision was removed. On the floor a striker added an additional cause of action that made the bill worse. Fortunately, that was also removed. There was also a definition of "claimant" that broadened liability that was removed. These are steps in the right direction but we oppose this bill. This bill is one of the most damaging bills that the insurance industry has seen in a number of years. There are already a number of remedies available under Washington law. The damages available under this bill are greater than almost anywhere else. A vast majority of complaints are resolved quickly and fairly. Only a small minority of the claims filed with insurers has problems. California's experience is instructive even with the third-party liability element removed. The California courts issued a report that noted an explosion in litigation and stated that the reason for that was that the economics around litigation had changed. Suits were easier to file and the potential return was greater. We think this bill changes the economics of litigation regarding insurance claims. Ultimately, the taxpayers and policyholders pay more. To be specific, the bill allows a person who can show

an unreasonable denial or a single violation of a rule to get mandatory attorney fees and up to treble the actual damages. The CPA allows for only economic damages. There is no similar limit here. The bill increases the length and breadth of liability. It will change claims practices and suits. It will have unintended consequences. The fiscal note states that there will be more suits. More suits means more public funding of the courts. An analogy is the practice of defensive medicine due to fear of litigation. It increases costs for very little return. That is likely to happen where insurers settle claims where they are not liable to avoid lawsuits. California also had fraud skyrocket. The voters of California rejected this type of measure. They understood that increased litigation does not improve claims handling. The decade when California had this type of system experienced a tremendous increase in costs. There are CPA remedies available today. There are bad remedies. The Commissioner also can take action. The protections available in Washington are greater than in most states. Some look at this bill and see a greater reason to settle; we see a greater incentive to sue. Insurers are obligated to pay claims. Under current law, a person can file a complaint or sue if their insurer denies their claim. If they sue, they can receive contractual damages and also tort damages. This bill goes further. Few claims end up in court. Under this bill, the lawyers will have every incentive and, perhaps even, an obligation to sue. I am a taxpayer who lost his house in a fire. My insurer sent a claims representative immediately. I was told that they wouldn't pay me a dollar more or a dollar less than I was due. They explained my claim and my policy. My agent worked with me. A contractor that they helped me find responded to me and worked for me. My family lost everything. They took care of us.

When you talk about the reasons for a bad faith bill, you assume that there are patterns and a history of misconduct. Insurers make promises to policyholders. A bad faith claim asserts that the insurer does not fulfill their promises. The industry has a good record in Washington and does a terrific job of paying claims. The recent windstorm resulted in thousands of claims by individuals and businesses. Industry responded well to those claims. Forty two thousand, five hundred claims were settled and $170 million was paid in claims. Out of the 42,500 claims, the Commissioner received just 339 telephone inquiries and only 23 people filed written inquiries. The OIC opened just three files. One of those is settled and two remain open. In the wake of that performance, there is a bill that somehow says that we don't fulfill our obligations. That just is not based on the facts. The fiscal note asserts that the standard for breach of contract is lowered and more suits will follow. The existing standard seems to be working. Industry does not like the lower standard for a breach of contract. It does not like the treble damages provision. It does not like the single violation of a rule provision. If an insurer receives a claim and does not pay immediately, it may face a suit. The state would never subject itself to this kind of a standard for the Department of Labor & Industries to the Health Care Authority. The defense bar opposes punitive damages in any setting. The unreasonable standard is particularly difficult. I personally defended a case where the trial court held that an insurer's denial was unreasonable and the appellate court reserved that decision and state that the denial was correct. It is not a clear and easily applied standard. Washington is one of only five states that allows a private CPA action. We do see cases where the claim was properly denied. A jury is going to be asked if the action was unreasonable, not if the denial was correct. This bill will not help consumers. Most cases

don't go to court, they are settled. This bill will increase the number and the acrimoniousness of suits. I don't know of anyone who intends to wrong a consumer. There are a number of case law remedies today. Any harm that may be incurred has a remedy. Courts will allow a number of actions, including possible damages flowing from a wrongful denial. Lawyers get compensation and attorneys fees today. CPA remedies are available today. People want more affordable insurance, not windfall legal remedies. The benefits are going to accrue to lawyers, not claimants.

We oppose the bill. The single violation of a rule is problematic. There are over 50 rules in Chapter 284-30 WAC that address our behavior. Many of those are unrelated to claims. We are currently subject to OIC enforcement action if we violate those rules. If the bill passes, the OIC may say we acted appropriately but we may still lose in court. Or one court may say we acted appropriately and another may hold the opposite. This increase in liability is a concern.

We agree with earlier testimony. The claims submitted to health carriers usually are from providers which will lead to even more potential liability. The treble damage provisions are onerous. There has been considerable talk about how the bill relates to property and casualty insurance. It also applies to life insurance and annuities. The bill is unnecessary. There are tools available today for a policyholder. The bill is just as troubling to health carriers as other insurers. We have prompt pay laws which include strict time-lines. If we miss a half of a day, we risk treble damages and attorneys' fees. Already, we pay claims where we think we are not liable because we think it is cheaper than winning the suit.

There was testimony from the proponents that there is no incentive to treat a policyholder fairly in Washington. That statement is just false. An unreasonable action may lead to a bad faith tort claim. There are many remedies and many types of damages that can be awarded today. This bill doesn't fill a need. It merely tacks on treble damages to existing remedies. The increased costs will lead to increased premiums. This will impact lower income people disproportionately. They may be priced out of the market. The very premise of the bill is wrong. We have brought bills to you where we say that the Legislature needs to address industry's practices. There is no outcry today for this measure. Agents are not receiving complaints and customers aren't asking for this remedy. This bill increases the incentives to sue.

Persons Testifying: (In support) Senator Weinstein, prime sponsor; Larry Shannon and Pat LePley, Washington State Trial Lawyers Association; and Rob Dietz.

(Opposed) Jean Leonard, State Farm, Washington Insurers; Ken Cooley, State Farm; Joe McDaniel; Mel Sorensen, Property Casualty Insurers Association, American Council of Life Insurers, America's Health Insurance Plans, Allstate, American Family Insurance, Contractors Bonding and Insurance Company; Doug Foley, Allstate; Emilia Sweeney, Washington Defense Trial Bar; Jody Pucell, SAFECO, American Insurance Association; Carrie Tellefson, Symmetra Financial Corp., Progressive Insurance; Anne Bryant, Physicians' Insurance; Nancee Wildermuth, Regence Blue Shield, PacifiCare, Aetna; Ken Bertrand, Group Health; Karen Weaver; and Bill Stauffacher, Independent Insurance Agents and Brokers of Washington.

Persons Signed In To Testify But Not Testifying: None.