



Insurance Claims Practices. Civil Remedies. Referendum.

Official Title and Summary Prepared by the Attorney General

INSURANCE CLAIMS PRACTICES. CIVIL REMEDIES. REFERENDUM.

A “Yes” vote approves, a “No” vote rejects legislation that:

- restores right to sue another person’s insurer for insurer’s unfair claims settlement practices;
- allows such lawsuits only if insurer rejects a settlement demand and injured party obtains a larger judgment or award against insured party;
- bars such lawsuits against public entities; workers’ compensation insurers; and professional liability insurers under certain circumstances; or if convicted of driving under the influence;
- authorizes requests for consensual binding arbitration of claims under \$50,001 against parties covered by insurance. Insurers agreeing to arbitration cannot be sued for unfair practices.

Summary of Legislative Analyst’s Estimate of Net State and Local Government Fiscal Impact:

- Increase in state insurance gross premiums tax revenue, potentially several millions of dollars each year.
- Unknown net impact on state court costs.

Analysis by the Legislative Analyst

BACKGROUND

Insurance Claims

Under current law, an insurance company must handle claims from a policyholder in a fair manner. It is illegal for an insurance company to engage in “unfair” claims practices, such as:

- Failing to promptly explain the reason for denying a claim or offering a compromise settlement.
- Failing to act in “good faith” to settle a claim in which liability is reasonably clear.

If an insurance company unfairly handles a claim (typically referred to as the “underlying claim”), the policyholder has two ways to respond: (1) file a complaint with the Department of Insurance (DOI), which is responsible for enforcing state law regarding unfair claims practices; and/or (2) sue his or her insurance company in civil court. These lawsuits by individuals against their own insurance companies are referred to as “first-party” actions.

There are many insurance claims—especially those involving auto accidents—that involve two individuals. For instance:

Driver X runs a red light and hits Driver Y, causing both bodily injury to Driver Y and damage to her car. Driver X’s insurance company is willing to pay Driver Y \$20,000 for her injury and damages, but not the \$30,000 Driver Y feels is reasonable. Driver Y can either accept the \$20,000 or reject it and sue Driver X in court.

If Driver Y feels that Driver X’s insurance company did not deal with her fairly throughout the process, Driver Y—as a “third-party” claimant—has only one way to respond. She can file a complaint with DOI for an investigation. She cannot sue Driver X’s insurance company for unfairly handling the claim (a so-called third-party lawsuit). These third-party lawsuits were possible in California during the 1980s but are not now. See nearby box for a brief legal history.

Legal History on Third-Party Lawsuits in California

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| Prior to 1979 | Third-party lawsuits were not allowed. |
| March 1979 | The California Supreme Court ruled in <i>Royal Globe Ins. Co. v. Superior Court</i> that a third party could sue an insurance company for unfair claims practices. |
| August 1988 | In <i>Moradi-Shalal v. Fireman’s Fund Ins. Co.</i> , the California Supreme Court overturned its <i>Royal Globe</i> decision. The court held that state law did <i>not</i> include a right for a third-party claimant to sue an insurance company for unfair claims practices. |
| October 1999 | The Governor signed two laws specifically allowing third-party lawsuits in certain situations. These measures were to have gone into effect January 1, 2000. In December 1999, however, referenda on the two laws qualified for the March 2000 ballot (Propositions 30 and 31). Thus, the provisions of the two laws are “on hold” until after the vote on the propositions. |

Recent Legislation

In the fall of 1999, the Legislature approved and the Governor signed SB 1237 (Chapter 720) and AB 1309 (Chapter 721). These laws allow third-party claimants to sue insurance companies under certain conditions. The two laws would have gone into effect January 1, 2000. In December 1999, however, referenda on the two laws qualified for the March 2000 ballot (Propositions 30 and 31). Once these propositions qualified, SB 1237 and AB 1309 were put “on hold” until the vote at the March 2000 election.

PROPOSAL

If approved, this proposition would allow the provisions of SB 1237 to go into effect. Senate Bill 1237 (1) gives third-party claimants the right to sue an insurance company for unfair claim practices in certain liability cases and (2) creates an alternative, binding arbitration system for settling these liability cases.

Third-Party Lawsuits

This proposition allows an individual or a business to file a third-party lawsuit against an insurance company for unfair claims practices in handling liability claims. (Liability insurance provides financial protection to individuals and businesses for harm that occurs to others.) This insurance generally provides compensation for bodily harm, wrongful death, and economic losses. A third-party lawsuit could be filed, however, only if:

- The third party was not driving under the influence of alcohol or drugs at the time of the accident that caused injury.
- The third party sends a written final request to the insurance company to settle the claim for an amount within the insurance policy limits.
- The third party is awarded an amount larger than the final written request.

If the lawsuit goes forward, the third-party claimant needs to prove in court that the insurance company unfairly handled the claim. If the third party wins the lawsuit, the claimant could receive an amount that is higher than the insurance policy limits.

An Example. In the earlier example, Driver Y had one way of responding to the insurance company’s handling of her case—filing a complaint with DOI. Under this proposition, she could also pursue a third-party lawsuit against Driver X’s insurance company. To do so, an award in the underlying claim would have to exceed her final written request. (For instance, if her final request was the \$30,000 she thought was reasonable, the award would have to be more than that amount.)

Arbitration

This proposition also creates a binding arbitration system to settle certain disputed underlying claims

(generally those of \$50,000 or less where the claimant is represented by a lawyer). Either a third-party claimant or an insurance company can request arbitration, but both sides must agree before the case goes to arbitration. If a case goes to arbitration, the third-party claimant cannot sue the company. In all cases, an arbitration award cannot exceed policy limits or include damages not covered by the policy.

Interaction With Proposition 31

Proposition 31 would modify portions of this proposition *if* both are approved by the voters. In general, Proposition 31 would place some limits on when a third-party lawsuit could be filed. Please see the analysis of Proposition 31 for more details.

FISCAL EFFECT

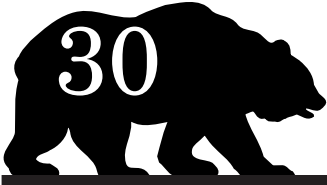
The fiscal impact of this proposition on state and local governments would depend on the future behavior of individuals, insurance companies, and other businesses in response to its provisions. The proposition, however, would likely increase liability insurance costs in California. These higher costs would occur because (1) in many cases, insurance companies will settle or arbitrate claims for somewhat higher amounts to avoid third-party lawsuits; and (2) when there are such lawsuits, insurance companies will incur greater costs. These higher costs could be offset in part by savings from other provisions in the proposition. For instance, some arbitration awards might be *lower* than what the insurance companies otherwise would have paid.

The net increase in liability insurance costs, however, presumably would result in insurance premiums that were higher than they otherwise would have been. In order for an insurance company to increase premiums, DOI must review and approve proposed premium increases.

Insurance Gross Premiums Tax. The state currently taxes insurance companies on the basis of gross premiums. (This tax is instead of the corporate income tax.) The current tax is 2.35 percent of gross premiums. Any increase in insurance premiums would increase state revenue from this tax. We estimate, for example, that for each 1 percent increase in liability premiums, state tax revenues would increase by about \$2 million each year.

State Court Costs. The proposition could affect the number of civil cases taken to court. On the one hand, some provisions of the proposition could *reduce* court costs (by shifting cases to arbitration). Other provisions, however, could *increase* court costs (by allowing third-party lawsuits). We cannot estimate the net effect of these provisions on state costs.

For Text of Proposition 30 see Page 12



Insurance Claims Practices. Civil Remedies. Referendum.

Argument in Favor of Proposition 30

Governor Gray Davis and *both* Houses of the Legislature enacted the Fair Insurance Responsibility Act—restoring your right to sue a bad driver’s insurance company if it illegally delays paying what they owe you and making your life miserable.

Here’s one example of thousands of cases:

A reckless driver talking on a cell phone runs through a red light and smashes into a woman driving her child to school. The reckless driver’s insurance company delays paying her medical bills for years. The innocent driver does not have the right to sue the reckless driver’s insurance company—unless voters approve the Fair Insurance Responsibility Act.

To protect your newly restored right to hold insurance companies responsible, *voters must approve* the Fair Insurance Responsibility Act.

Seven out-of-state and foreign insurance companies oppose this law. The *Los Angeles Times* calls their campaign “a \$50 million corporate effort . . . playing a complicated game with voters . . . hiding behind a consumer veil.”

Proposition 30 *prohibits drunk drivers* from suing and does *not* give uninsured motorists the right to sue you. In fact, if you’re injured by a drunk driver, Proposition 30 requires the drunk driver’s insurance company to pay your claim on time.

The insurance companies’ campaign ads falsely accuse Governor Gray Davis and the Legislature of giving drunk drivers the right to sue under this new law.

Governor Davis’ office responded: “That’s certainly not what the legislation does. Governor Davis signed measures that are good public policy and protect individuals from being treated unfairly.”

And Proposition 30 does not change Proposition 213 which *prohibits uninsured drivers* from suing for pain and suffering.

Proposition 30 will *reduce* the number of lawsuits in

California: *If an insurance company agrees to resolve your claim through arbitration or simply decides to treat your valid claim fairly, there is no lawsuit.*

Insurance companies are falsely accusing Governor Gray Davis of signing a law that allows insurance companies to raise your premiums.

Under California law, insurance companies penalized for violating this law *cannot* pass on those penalties to consumers by raising your premiums. The California Code of Regulations says: “*Bad faith judgments and associated loss adjustment expenses*” are “*excluded expenses*” for setting insurance company premiums.

The *Sacramento Bee* editorial summarized the issue: “On balance, SB 1237 (the Fair Insurance Responsibility Act) offers fair and needed protections to injured innocent victims and reasonable incentives for insurance companies to do the right and lawful thing.”

You pay your premiums on time. The bad driver’s insurance company should pay *your* valid claim on time.

Consumers Union (the publishers of *Consumer Reports*), the Congress of California Seniors and the Consumer Federation support the Fair Insurance Responsibility Act enacted by both Houses of the Legislature and signed by Governor Davis. Give yourself a fighting chance. Protect your rights. Vote “Yes” on Proposition 30.

SENATOR MARTHA ESCUTIA

KAY McVAY, RN

President, California Nurses Association

LOIS WELLINGTON

President, Congress of California Seniors

Rebuttal to Argument in Favor of Proposition 30

Ask yourself: If Propositions 30 and 31 are such good laws, why did the personal injury lawyers who wrote them specifically exempt their own insurance companies from their provisions?

They did it to protect themselves against higher insurance rates, pure and simple. Even though they created these proposals, they don’t want to pay the price. *And that says it all.*

Their so-called “Fair Insurance Responsibility Act” is neither fair nor responsible. It’s simply a way for them to file more lawsuits and make more money at your expense.

California’s retired Legislative Analyst warns that measures like Propositions 30 and 31 will increase insurance rates up to 15% and, “could cost taxpayers millions.” The California Organization of Police and Sheriffs says, “insurance fraud will thrive.”

The facts are: Propositions 30 and 31 will drive insurance rates significantly higher, double the number of lawsuits in accident cases and cost taxpayers millions—which is why these propositions are opposed by so many respected taxpayer,

consumer, senior, business and public safety groups in California.

Proponents claim these Propositions don’t give drunk drivers new power to sue. But after careful analysis, Mothers Against Drunk Driving concluded “because these measures do not exclude all drunk drivers, many will get new rights to sue . . . even when drunk at the time of the collision.”

Don’t reward drunk drivers and uninsured motorists for breaking the law. Say NO to higher insurance costs and personal injury lawyers who want to profit at your expense. Vote NO on 30 and 31.

REBECCA M. BEARDEN

Mothers Against Drunk Driving (MADD),

Chairperson, California Public Policy Committee

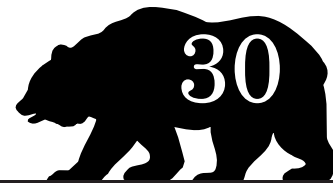
MICHAEL JOHNSON

Executive Director, Voter Revolt

JIM CONRAN

President, Consumers First

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Argument Against Proposition 30

DON'T BE FOOLED

Proposition 30 (and its companion, Proposition 31), sponsored by personal injury lawyers, is a trick to allow two lawsuits for the same accident. That means billions in higher lawyer fees, but consumers pay. No wonder the personal injury lawyers' association president told the *LA Times* that Proposition 30 (with Prop. 31) was, "our biggest victory in 40 or 50 years."

This "victory" for personal injury lawyers will dramatically increase insurance premiums for all Californians. Respected former Legislative Analyst William Hamm estimates *Proposition 30 could cost consumers up to 15% more for auto insurance*, over \$1 billion more each year. Small businesses also pay millions more.

Under Proposition 30, if your insurer refuses to pay an unreasonable settlement demand made against you, it risks a separate multi-million dollar lawsuit.

PROPOSITION 30 MEANS:

- Insurance rates for average consumers increase \$200–300 per year.
- Personal injury lawyers can file thousands of frivolous lawsuits aimed at you and your insurer.
- *Drunk drivers can sue and collect punitive damages that current law prevents.*
- *Lawbreakers who drive without insurance can sue for huge punitive damages.*
- Taxpayers pay tens of millions more in court costs for frivolous lawsuits.
- Insurance fraud skyrockets.

THE LESSONS OF RECENT HISTORY ARE CLEAR!

During the 1980s, the California Supreme Court allowed second lawsuits if an inflated settlement demand was not met. According to California Judicial Council records, auto injury lawsuits filed every year almost doubled. Settlements from insurers zoomed. Since personal injury lawyers often receive 40%, they made millions. As a result, consumer's insurance rates skyrocketed. Finally, the Supreme Court outlawed these second lawsuits. Since then, the number of auto injury lawsuits is back to normal. According to the Department of Insurance, insurance rates are down over 20%.

PROP. 30 IS COMPLETELY UNNECESSARY.

If someone thinks a settlement offer is too low, they can already take the dispute to court. They can also file a complaint with the state Department of Insurance.

Proposition 30 invites more frivolous lawsuits, more fraudulent claims and higher insurance rates.

HERE'S WHAT SOME OF THE MANY RESPECTED GROUPS OPPOSING PROP. 30 SAY:

"Proposition 30 would give drunk drivers new rights to sue and recover financial rewards against an insurance company, even if they are drunk at the time of the collision. Drunk drivers should be forced to pay, not BE PAID by their willful disregard for the law. MADD is vigorously opposed to Prop. 30."

—Mothers Against Drunk Driving

"Proposition 30 will cost taxpayers millions because hard-earned tax dollars will be diverted as government agencies are forced to pay for frivolous lawsuits and high insurance costs."

—California Taxpayers' Association

"Insurance fraud will thrive under Prop. 30."

—California Organization of Police and Sheriffs

"If Prop. 30 takes effect, money needed for classroom instruction will instead have to pay for higher school insurance costs."

—Marian Bergeson, Member, State Board of Education

JOIN TAXPAYERS, SENIORS, CONSUMERS, INSURERS, SMALL BUSINESS GROUPS, EDUCATORS AND LAW ENFORCEMENT.

VOTE NO ON PROPOSITION 30.

REBECCA M. BEARDEN

*Chairperson, California Public Policy Committee,
Mothers Against Drunk Driving (MADD)*

LARRY McCARTHY

President, California Taxpayers Association

SHIRLEY KNIGHT

*Deputy State Director, National Federation of
Independent Business*

Rebuttal to Argument Against Proposition 30

The insurance companies claim that Proposition 30 will double the number of lawsuits. That's false.

Ralph Nader says: "*Proposition 30 discourages lawsuits by requiring insurance companies to pay your claims fairly.*"

Insurance companies claim Proposition 30 will raise your premiums. That's false.

The California Department of Insurance rules *prohibit insurance companies from raising your premiums to pay their penalties for violating the law.*

The insurance companies accuse Governor Davis of signing a law that raises your premiums by giving new rights to drunk drivers and uninsured motorists. That's outrageous!

Governor Davis' office responded: "*That's certainly not what the legislation does.*"

Candace Lightner, the Founder of MADD: "I am the founder of Mothers Against Drunk Driving and a supporter of Proposition 30 because it helps victims of drunk drivers."

The insurance companies even falsely claim that Proposition 30 will take money from our schools!

State Superintendent of Public Instruction Delaine Eastin:

"Proposition 30 exempts public schools, police and fire departments and other public entities."

Seven out-of-state and foreign insurance companies are trying to kill Proposition 30 because they make more money every time they low-ball or stonewall paying your valid claim.

Proposition 30 restores a good driver's right to sue a bad driver's insurance company if it *illegally* delays paying *what they owe you.*

The California Department of Justice describes Proposition 30 as "*legislation restoring rights to sue insurers for unfair practices.*"

Ralph Nader says: "A 'Yes' vote protects your rights against insurance companies."

SENATOR MARTHA ESCUTIA

KAY McVAY, R.N.

President, California Nurses Association

LOIS WELLINGTON

President, Congress of California Seniors