contracts to provide services to that group, the method and data used in calculating the rates of payment. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

LITIGATION:

The unprecedented proliferation of litigation by injured investors and all types and levels of government agencies— several of which permitted the harm to occur—continues to swirl around Charles H. Keating, the now-bankrupt American Continental Corporation (ACC) owned by Keating, and the Irvine-based Lincoln Savings and Loan Association, an ACC subsidiary. In 1983-84, former Department of Savings and Loan Commissioner Larry Taggart approved Keating's original application to acquire Lincoln, despite the fact that Keating had been cited by the Securities and Exchange Commission in 1979 for receiving illegal loans and using corporate funds for the personal benefit of insiders; and, in late 1984, approved Lincoln's request to transfer $900 million to a subsidiary a few days before a new federal rule went into effect forcing S&Ls to limit direct investments to 10% of their assets. Further, the Department of Corporations twice authorized the sale of junk bonds by Lincoln employees to Lincoln depositors. (See CRLR Vol. 10, No. 4 (Fall 1990) pp. 117-19 and 128-29; Vol. 10, Nos. 2 & 3 (Spring/Summer 1990) pp. 135-38 and 149-50; and Vol. 10, No. 1 (Winter 1990) pp. 103 and 113-14 for extensive background information.)

People of the State of California v. ACC, the Department's civil fraud action against Keating, ACC, and two of ACC's top officers, is still pending in federal court in Arizona under U.S. District Court Judge Richard Bilby. The Department, which authorized ACC to sell junk bonds from branch offices of Lincoln Savings and Loan, charges defendants with securities fraud, fraud in application for qualification, offer/sale of unauthorized securities, and unauthorized advertising.

Although the Department's case was filed in Los Angeles County Superior Court in March 1990, the defendants removed the case to federal court; it was then transferred to Judge Bilby along with numerous other civil actions concerning Keating, ACC, and Lincoln. Although the case is technically stayed due to ACC's bankruptcy, the Department has been permitted to file a motion for summary judgment in the case; defendants have not yet responded because they have yet to complete discovery. The Department has also filed a motion to default Charles Keating, due to Keating's failure to file a responsive pleading to the Department's complaint since he was served in May 1990. Both motions are scheduled for an April 19 hearing before Judge Bilby.

Keating recently spent a month in jail as a result of the filing of related state criminal charges by the Los Angeles County District Attorney's Office; he was released on October 18 after a federal judge reduced his bail from $5 million to $300,000. On November 9, Los Angeles County Superior Court Judge Lance Ito set aside 22 of the 42 criminal counts, on grounds they were too vague or failed to state a violation of law. On November 19, prosecutors filed an amended indictment containing 46 counts. Judge Ito was scheduled to hold a hearing on the sufficiency of the amended indictment on January 11. The federal grand jury in Los Angeles is expected to hand down a federal indictment against Keating in the near future.

In Re American Continental Corporation/Lincoln Savings and Loan Association, No. 589302 (Orange County Superior Court), the class action filed on behalf of 23,000 investors who lost approximately $300 million in the collapse of Lincoln/ACC through their purchase of now-worthless junk bonds, has also been transferred to Judge Bilby. The Department was dismissed as a named defendant in this action in May 1990. Plaintiffs' objection to the transfer to federal court (triggered by defendants' filing of cross-complaints alleging federal questions) is now on appeal in the U.S. Court of Appeals for the Ninth Circuit.

The March 1991 trial date in the class action has been postponed until at least January 1992. The court in which trial will be held is unclear; Judge Bilby may try the federal claims, with the state law claims severed for state court trial. At this writing, partial settlements totalling $40 million have been negotiated and approved by the court.

DEPARTMENT OF INSURANCE

Commissioner: John Garamendi
(415) 557-3848
Toll-Free Complaint Number:
1-800-233-9045

Insurance is the only interstate business wholly regulated by the several states, rather than by the federal government. In California, this responsibility rests with the Department of Insurance (DOI), organized in 1868 and headed by the Insurance Commissioner. Insurance Code sections 12919 through 12931 set forth the Commissioner's powers and duties. Authorization for DOI is found in section 12906 of the 800-page Insurance Code; the Department's regulations are codified in Chapter 5, Title 10 of the California Code of Regulations (CCR).

The Department's designated purpose is to regulate the insurance industry in order to protect policyholders. Such regulation includes the licensing of agents and brokers, and the admission of insurers to sell in the state.

In California, the Insurance Commissioner licenses approximately 1,450 insurance companies which carry premiums of approximately $53 billion annually. Of these, 650 specialize in writing life and/or accident and health policies.

In addition to its licensing function, DOI is the principal agency involved in the collection of annual taxes paid by the insurance industry. The Department also collects more than 170 different fees levied against insurance producers and companies.

The Department also performs the following functions:

(1) regulates insurance companies for solvency by tri-annually auditing all domestic insurance companies and by selectively participating in the auditing of other companies licensed in California but organized in another state or foreign country;

(2) grants or denies security permits and other types of formal authorizations to applying insurance and title companies;

(3) reviews formally and approves or disapproves tens of thousands of insurance policies and related forms annually as required by statute, principally related to accident and health, workers' compensation, and group life insurance;

(4) establishes rates and rules for workers' compensation insurance;

(5) regulates compliance with the general rating law. Rates generally are not set by the Department, but through open competition under the provisions of Insurance Code sections 1850 *et seq.*; and

(6) becomes the receiver of an insurance company in financial or other significant difficulties.

The Insurance Code empowers the Commissioner to hold hearings to determine whether brokers or carriers are complying with state law, and to order an insurer to stop doing business within the state. However, the Commissioner may not force an insurer to pay a claim—that power is reserved to the courts.

DOI has over 800 employees and is headquartered in San Francisco. Branch offices are located in San Diego, Sacramento, and Los Angeles. The Commissioner directs ten functional divisions and bureaus.

The Underwriting Services Bureau (USB) is part of the Consumer Services Division, and handles daily consumer inquiries. It receives more than 900 telephone calls each day. Almost 50% of the calls result in the mailing of a complaint form to the consumer. Depending on the nature of the returned complaint, it is then referred to Claims Services, Investigations, or other sections of the USB.

Since 1979, the Department has maintained the Bureau of Fraudulent Claims, charged with investigation of suspected fraud by claimants. The California insurance industry asserts that it loses more than $100 million annually to such claims. Licensees currently pay an annual assessment of $1,000 to fund the Bureau's activities.

A Consumer Advisory Panel (CAP) has been named by the Commissioner as an internal advisor to DOI. CAP members are appointed by the Commissioner. The Panel's function is to advise the Department on methods of improving existing services as well as the creation of new services. Additionally, the CAP aids in the development and distribution of consumer educational and informational materials.

MAJOR PROJECTS:

Election of New Insurance Commissioner. On November 6, California voters had a chance to elect the Insurance Commissioner for the first time in state history. The change from an appointed to an elected commissioner is one of the most significant reforms accomplished by Proposition 103, enacted by the voters in 1988. While the implementation of most other Proposition 103 provisions remains bogged down and may never be carried out as intended by the voters over two years ago, the election of the Insurance Commissioner has the potential for triggering important insurance reforms.

Former state senator John Garamendi was elected as the state's new Insurance Commissioner. During his campaign, Garamendi stated that he wants to change the focus of the auto insurance debate from no-fault insurance to a concentration on efforts to create fair claims practices and the elimination of fraud. While these thoughts are laudable, the actual agenda of the new Commissioner remains to be seen. Garamendi, a heavy favorite in the race for the post, did not run an issue-specific campaign, for which he was heavily criticized by consumer groups. Therefore, it is still unclear exactly where he intends to lead the Department.

Gillespie Lifts Freeze, Approves 83 Rate Increase Applications. On December 13, lame-duck Commissioner Roxani Gillespie lifted the fourteen-month-old auto insurance rate freeze and began approving rate increase applications. By the time she left office in early January, she had approved rate increases for 83 companies.

The freeze had been in effect since October 2, 1989, when Gillespie imposed it and announced the commencement of two administrative hearings to fashion rules to implement Proposition 103, in settlement of a September 1989 lawsuit filed by consumer groups. (See CRLR Vol. 9, No. 4 (Fall 1989) pp. 92-94 for background information.) In lifting the freeze and allowing the rate increases, Gillespie warned companies that, although her initial auto rating criteria regulations had been invalidated by the Los Angeles County Superior Court (see CRLR Vol. 10, No. 4 (Fall 1990) p. 122 for background information), the issue is on appeal and insurers will be required to refund the rate increases if her rules are eventually upheld.

Gillespie's action was immediately blasted by consumer groups and Commissioner-elect Garamendi. Consumers Union criticized Gillespie for failing to defend her own regulations. Garamendi announced that he might reimpose the freeze once he takes office, especially since no companies have yet complied with Proposition 103's rollback requirement.

CSAA/SAFECO Rollback Hearings Conclude. In late November, DOI Administrative Law Judge Paul M. Geary concluded the Department's administrative hearings on the appropriate Proposition 103-mandated rate rollback/rebates for California State Automobile Association (CSAA) and SAFECO. (See CRLR Vol. 10, No. 4 (Fall 1990) pp. 120-21 for extensive background information.) ALJ Geary was expected to release his proposed decision in late January; thus, his recommendation will be reviewed by Commissioner-elect Garamendi instead of Roxani Gillespie. Garamendi has the authority to accept the ALJ's recommendation, modify it based on the hearing record, or to reject it. ALJ Geary's recommendation will be based on the "fair rate of return" regulations adopted by Gillespie; to the extent that Garamendi modifies those regulations once he takes office, the ALJ's decision may be rendered obsolete.

DOI Rulemaking. As detailed in CRLR Vol. 10, No. 4 (Fall 1990) at pages 121-22, the Department commenced a number of rulemaking proceedings shortly before Commissioner Gillespie left office. Most of these proceedings resulted in the adoption or readoption of emergency regulations, which are effective for only 120 days unless adopted in the normal course during that time period or properly readopted as emergency rules. The extent to which Commissioner-elect Garamendi will allow these rules to expire or propose the adoption of new rules in these areas is unclear at this writing. The following is a status update on several DOI rulemaking proceedings:

-Preapproval of Policy and Bond Forms. On November 19, DOI held a public hearing on its proposal to adopt regulatory sections 2195-2199, which would establish the procedure for the Commissioner's required preapproval of policy and bond forms developed by advisory organizations. Among other things, these proposed regulations would specifically allow consumer group participation in the process of prior approval of policy forms. Following the receipt of public comment the Department released a slightly modified version of these proposed regulations on December 28.

-Unfair Claims Settlement Practices Regulations. On November 13 and 15, the Department held public hearings on the proposed adoption of regulatory sections 2695.1-.10. Among other things, these wide-ranging rules would flesh out claims settlement practices which are unfair under Insurance Code section 790.03(h), and grounds for disciplinary action by DOI against the licensee. The need for these rules and their enforcement by DOI is enhanced by recent court rulings striking down third- and first-party bad faith actions. (See CRLR Vol. 10, No. 4 (Fall 1990) p. 124; Vol. 9, No. 4 (Fall 1989) p. 97; and Vol. 8, No. 4 (Fall 1988) p. 87 for background information on the *Tricor, Zephyr Park*, and *Moradi-Shalal* cases, respectively.) At the hearings, there appeared to be little opposition to the proposed rules, except as they may apply to title insurers. At this writing, the Department has taken no action to adopt the proposed rules.

-Auto Rating Factors. On November 16 and 20, DOI held public hearings on the permanent adoption of regulatory sections 2632.1-.18, which would implement Proposition 103 by defining automobile rating factors, good driver discount policies, collection of historical

loss data, and rates for private passenger automobile insurance. These regulations were adopted as emergency regulations in August 1990 in response to a court order invalidating Commissioner Gillespie's first set of auto rating criteria (*see supra "Gillespie Lifts Freeze, Approves 83 Rate Increase Applications"*). These regulations, which more or less preserve the insurance industry's territorial rating system sought to be eliminated in Proposition 103, were readopted as emergency regulations on December 12.

-Prior Approval of Property/Casualty Rates. On November 26, DOI held a public hearing on the proposed permanent adoption of numerous provisions in Subchapter 4.9, Chapter 5, Title 10 of the CCR, concerning the Proposition 103-mandated prior approval by the Insurance Commissioner of property and casualty insurance rates. These regulations were adopted as emergency regulations in August 1990; and, following the public hearing, were readopted as emergency regulations on December 21. However, Commissioner-elect Garamendi has indicated that once he takes office, no rate increases for any company will be approved until that company's liability for rollbacks is determined and paid.

LEGISLATION:

SB 35 (Robbins). Existing law requires the driver of a motor vehicle to maintain proof of financial responsibility and requires the Department of Motor Vehicles (DMV) to suspend the driver's license of a person who violates certain requirements relating to proof of financial responsibility. With specified exceptions, the DMV may not accept as proof of financial responsibility an insurer's certificate which does not cover all vehicles registered to the licensee. As introduced December 3, SB 35 would authorize the DMV to accept an insurer's certificate which does not cover all vehicles registered to the licensee for purposes of reinstating the driver's license of a person who is deemed to be a negligent driver on the basis of his/her violation point count. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 110 (Robbins). SB 2642 (Robbins) (Chapter 1420, Statutes of 1990) requires that, as of January 1, 1992, DOI must require all new applicants for licensure as fire and casualty broker-agents or as life agents to meet prelicensing education standards. SB 2642 also established various requirements and standards in connection with continuing education programs for persons licensed as fire and casualty broker-agents and life agents. (See CRLR Vol. 10, No. 4 (Fall 1990) p. 123 for background information.) SB 110, as introduced December 18, would delay the operative date of those provisions to January 1, 1993. This bill is pending in Senate Committee on Insurance, Claims and Corporations.

SB 122 (Robbins). Existing law requires certain law enforcement agencies to assist DOI's Bureau of Fraudulent Claims, and imposes a fee which is used, in part, to finance the Bureau. As introduced December 19, this bill would authorize the Bureau to impose an additional assessment on insurers. The money would be deposited in a separate account in the Insurance Fund, and would be available upon appropriation for purposes of a program that this bill would establish to reward persons whose information leads to the arrest and prosecution of vehicle thieves or the issuance of a warrant for suspected theft ring members or chop shop operators, or the arrest and filing of an indictment or information against suspected theft ring members or chop shop operators. However, the bill would provide that no reward shall be given if the suspected criminal is found to be not guilty, as specified. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

LITIGATION:

In *Allstate Insurance Co. v. Gillespie*, No. B047071 (Nov. 27, 1990), the Second District Court of Appeal overturned a Los Angeles County Superior Court decision compelling Insurance Commissioner Gillespie to grant Allstate Insurance Company a 40% increase in its rates under the California Automobile Assigned Risk Program (CAARP). (See CRLR Vol. 10, No. 1 (Winter 1990) pp. 107-10 for background information.) On December 18, 1989, then- Superior Court Judge Miriam Vogel interrupted a DOI administrative proceeding considering a requested 112% CAARP rate increase with her order to Gillespie to increase Allstate's CAARP rates only (Allstate is one of a large number of companies required to write CAARP policies).

The appellate court cited Allstate's failure to exhaust administrative remedies as its primary reason for reversing the lower court's decision; further, the majority noted that Allstate would not face irreparable harm because it could recoup any losses incurred during the pendency of the administrative hearing through future rate increases. The decision has little practical effect because, subsequent to her refusal to grant Allstate's CAARP rate increase request, Commissioner Gillespie granted an 85% increase to all companies writing CAARP policies (see CRLR Vol. 10, No. 4 (Fall 1990) p. 121 for background information). However, it is considered legally significant in that it analyzes in detail and lends strong support to the doctrine of exhaustion of administrative remedies.

In *Barnes v. State Farm Mutual Automobile*, No. CA001131 (Dec. 10, 1990), Los Angeles County Superior Court Judge Barnet M. Cooperman largely dismissed plaintiffs' complaint against State Farm. The action was filed by State Farm policyholders—who technically own the mutual insurance company—claiming that State Farm methodically deprives them of dividends by accumulating and retaining a surplus reserve well in excess of industry standards. Plaintiffs argued that other insurance companies pay out dividends that are 660% larger per $100 of premium income than State Farm's, and that the industry average of paying out 11.6% of surplus as dividends is 1,160% higher than returned by State Farm; they sought an order compelling State Farm to return $7 billion of its $20 billion in reserves to more than 51 million policyholders in the United States. (See CRLR Vol. 10, No. 1 (Winter 1990) p. 110 for background information.)

Judge Cooperman dismissed the majority of the complaint, applying the "business judgment rule" and declining to interfere with the insurer's dividend and surplus policies in the absence of fraud. The court also ruled that plaintiffs have an administrative remedy with the Insurance Commissioner if they believe State Farm's rates are excessive. Finally, Judge Cooperman gave plaintiffs 45 days to amend the portion of their complaint in which they allege that State Farm wrongfully used corporate funds to help finance campaigns for public office. Plaintiffs' counsel William Shernoff announced his intent to file an amended complaint on the political spending issue; appeal the dismissal of the other claims in the complaint; and request Commissioner-elect Garamendi to review State Farm's rates.

The dispute between FGS Insurance Agency, Inc. and the Department escalated during late 1990. As reported previously, DOI has initiated an administrative proceeding to revoke the license of the Irvine-based company; on August 13, the Department filed a multimillion-dollar racketeering/fraud case against FGS in Los Angeles County Superior Court. (See CRLR Vol. 10, No. 4 (Fall 1990) p. 124 for background information.) In conjunction with these actions,

DOI also set up a toll-free hotline to assist consumers with questions about FGS.

On October 5, FGS filed an administrative damage claim with the Department against DOI, Roxani Gillespie, and four DOI employees, alleging that the Department's actions in setting up the hotline, disseminating "false and misleading" press releases, seeking to revoke FGS' license, and making unauthorized and improper inspections of FGS' premises are unlawful, unethical, a waste of taxpayer funds, and a violation of the anti-racketeering statutes. Such an administrative claim is required prior to the filing of a damages lawsuit against a state agency, which is expected. At this writing, DOI's lawsuit and its revocation proceeding are still pending.

On November 5, then-Commissioner Roxani Gillespie announced that the liquidation companies of the now-defunct Mission Insurance Companies had reached a settlement of all pending litigation with Underwriters Reinsurance Company, subject to court approval. (See CRLR Vol. 10, No. 4 (Fall 1990) pp. 123-24 and Vol. 10, Nos. 2 & 3 (Spring/Summer 1990) p. 144 for background information.) Under the settlement, the parties will "run off" facultative business between the companies—that is, Underwriters would continue to make payments under its facultative certificates with Mission in the ordinary course of business, as policyholder claims are reported in the future within certain limits. Underwriters has also agreed to pay a cash commutation of its obligations under its reinsurance treaties with Mission; according to Gillespie, the overall settlement has a potential minimum value of $42.2 million and a maximum of $50.7 million.

Mission's reinsurers had sought removal of the pending litigation from Los Angeles County Superior Court to federal district court in New York. On November 16, Gillespie announced that the district court rejected those efforts, finding that the reinsurers' claims are receiving adequate consideration in the California proceedings.

In *AIU Insurance Co. v. Superior Court*, No. S012525, the California Supreme Court was asked to decide whether, under comprehensive general liability (CGL) insurance policies issued by insurers to FMC Corporation, the insurers are obligated to provide coverage to FMC for clean-up and other "response" costs incurred pursuant to the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), 42 U.S.C. section 9601 *et seq.*, and related state and federal environmental laws. On November 15, a unanimous court declared that the cost of government-ordered clean-up of toxic wastes does constitute "damages" that are covered under the CGL policies issued to thousands of businesses over the past fifty years.

The insurance industry argued that CGL policies do not cover costs incurred pursuant to a governmental clean-up injunction; that is, the standard CGL policy—which covers "all sums which the insured becomes legally obligated to pay *as damages* because of bodily injury or property damage"—does not cover costs incurred due to injunctions issued in equity. Applying traditional rules of interpretation to the insurance policies, and using the "ordinary and popular sense" of words to resolve any ambiguities in favor of the policyholder, the court determined that some of the adverse orders issued in CERCLA suits will "legally obligate" FMC to pay such costs; the costs will constitute "damages" or "ultimate net loss," and such costs will be incurred because of "property damage."

DEPARTMENT OF REAL ESTATE

Commissioner: James A. Edmonds, Jr.
(916) 739-3684

The Real Estate Commissioner is appointed by the Governor and is the chief officer of the Department of Real Estate (DRE). DRE was established pursuant to Business and Professions Code section 10000 *et seq.*; its regulations appear in Chapter 6, Title 10 of the California Code of Regulations (CCR). The commissioner's principal duties include determining administrative policy and enforcing the Real Estate Law in a manner which achieves maximum protection for purchasers of real property and those persons dealing with a real estate licensee. The commissioner is assisted by the Real Estate Advisory Commission, which is comprised of six brokers and four public members who serve at the commissioner's pleasure. The Real Estate Advisory Commission must conduct at least four public meetings each year. The commissioner receives additional advice from specialized committees in areas of education and research, mortgage lending, subdivisions and commercial and business brokerage. Various subcommittees also provide advisory input.

The Department primarily regulates two aspects of the real estate industry: licensees (as of July 1990, 202,408 salespersons and 98,891 brokers, including corporate officers) and subdivisions.

License examinations require a fee of $25 per salesperson applicant and $50 per broker applicant. Exam passage rates average 67% for both salespersons and brokers (including retakes). License fees for salespersons and brokers are $120 and $165, respectively. Original licensees are fingerprinted and license renewal is required every four years.

In sales or leases of most residential subdivisions, the Department protects the public by requiring that a prospective buyer be given a copy of the "public report." The public report serves two functions aimed at protecting buyers of subdivision interests: (1) the report requires disclosure of material facts relating to title, encumbrances, and similar information; and (2) it ensures adherence to applicable standards for creating, operating, financing, and documenting the project. The commissioner will not issue the public report if the subdivider fails to comply with any provision of the Subdivided Lands Act.

The Department publishes three major publications. The *Real Estate Bulletin* is circulated quarterly as an educational service to all real estate licensees. It contains legislative and regulatory changes, commentaries and advice. In addition, it lists names of licensees against whom disciplinary action, such as license revocation or suspension, is pending. Funding for the *Bulletin* is supplied from a $2 share of license renewal fees. The paper is mailed to valid license holders.

Two industry handbooks are published by the Department. *Real Estate Law* provides relevant portions of codes affecting real estate practice. The *Reference Book* is an overview of real estate licensing, examination, requirements and practice. Both books are frequently revised and supplemented as needed. Each book sells for $15.

The California Association of Realtors (CAR), the industry's trade association, is the largest such organization in the state. As of November 1990, approximately 144,500 licensed agents are members. CAR is often the sponsor of legislation affecting the Department of Real Estate. The four public meetings required to be held by the Real Estate Advisory Commission are usually on the same day and in the same location as CAR meetings.

MAJOR PROJECTS:

DRE Rulemaking. On October 25, Real Estate Commissioner James Edmonds held a public hearing on numerous proposed changes to DRE's