(Winter 1990) at page 105:

AB 2259 (Bentley), as amended on January 24 to authorize a parent company to merge into its subsidiary corporation, is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 503 (Stirling), as amended August 21, 1989, would permit the director of a corporation to consider and act in the best interests of the public as well as in the best interests of the corporation and its shareholders. This bill is still pending in the Assembly Judiciary Committee.

AB 1666 (Wright), which exempts specified transactions from qualification under the Corporate Securities Law of 1968, was signed by the Governor on April 5 (Chapter 40, Statutes of 1990).

LITIGATION:

In *In Re American Continental Corporation/Lincoln Savings and Loan Association*, No. 589302 (Orange County Superior Court), the Department has been dismissed as a named defendant. The case is a class action filed on behalf of 23,000 investors who lost upwards of $200 million in the collapse of Lincoln Savings and its now-bankrupt parent company, American Continental Corporation (ACC). Plaintiffs sued ACC, Lincoln, and its owner Charles H. Keating, Jr., both the law and accounting firms of ACC/Lincoln, and the state of California and its Department of Corporations. The Department approved the issuance and sale to the public of $350 million in high-risk, uninsured junk bonds at the branch offices of Lincoln. (See CRLR Vol. 10, No. 1 (Winter 1990) pp. 103 and 113-14; and Vol. 9, No. 4 (Fall 1989) p. 100 for background information on the Lincoln scandal.)

Other defendants include Karl Samuelian and former Corporations Commissioner Franklin Tom. In 1983, Samuelian—one of Governor Deukmejian's chief fundraisers—recommended that the Governor appoint Tom, a member of Samuelian's law firm, as Commissioner of the Department of Corporations. When Tom resigned in 1987 to return to Samuelian's law firm, Deukmejian replaced him with Christine Bender, another former member of Samuelian's firm.

Samuelian was hired by ACC's owner, Charles Keating, to represent the company before California state regulators. At one meeting in March 1988, Samuelian and Tom lobbied Bender and her staff to approve a second ACC junk bond issue for $150 million. The first request, for the public sale of $200 million worth of high-risk bonds, was approved by Tom in 1986. Bender eventually approved the second request, despite questions about ACC's worsening financial condition that were raised by federal banking regulators and the state Department of Savings and Loan (DSL).

Commissioner Bender testified before the Assembly Finance and Insurance Subcommittee in November 1989. Bender stated that no application had ever received greater scrutiny by the Department, that the Department had thoroughly reviewed ACC's financial position, and that the Department consulted with many state and federal agencies regarding ACC. Bender admitted that DSL had informed the Department of Corporations of its concerns about Lincoln and ACC in 1988. She concluded, however, that "...in the course of [DSL's] review of ACC's securities applications and its contacts with savings and loan regulators, [they] were unable to uncover any concrete evidence that ACC would not be able to continue to make payments on its debentures as scheduled."

The state of California and the Department were dismissed as defendants in the class action on May 3. Superior Court Judge David Sills ruled that the state enjoys statutory immunity from prosecution "for acts of its employees...where the act or omission was the result of the exercise of discretion...whether or not such discretion is abused."

Recently, Samuelian and Tom announced a tentative agreement to pay up to $14.3 million to resolve claims by investors. Over $4 million would be paid up front, and if the investors are unable to recover an additional $10 million from "other sources", the law firm's insurer will make up the difference. It is still unknown when investors will start recouping any of their losses.

DEPARTMENT OF INSURANCE

Commissioner: Roxani Gillespie
(415) 557-3245
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 Codes 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 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:

Commissioner Adopts "Fair Rate of Return" Standard. On June 13, Commissioner Gillespie finally approved a fair rate of return standard, the measuring stick to be used by the Department of Insurance in evaluating the exemption applications of over 450 insurance companies trying to dodge the rate rollback requirements of Proposition 103, and the companies' future applications for rate adjustments—which must now be pre-approved by the Commissioner under Proposition 103. (See CRLR Vol. 10, No. 1 (Winter 1990) pp. 106-08; Vol. 9, No. 4 (Fall 1989) pp. 92-94; and Vol. 9, No. 3 (Summer 1989) pp. 82-87 for extensive background information on Proposition 103, the insurance reform initiative enacted by California voters in November 1988.)

The Commissioner's decision ended a six-month adjudicatory proceeding conducted by DOI Administrative Law Judge William Fernandez in San Bruno, and—as with everything else connected with Proposition 103—ended one round of controversy and sparked others.

The "fair rate of return" standard was imposed by the California Supreme Court in its May 4, 1989 decision in *Calfarm v. Deukmejian*, 48 Cal. 3d 805 (1989). The court largely upheld Proposition 103, but substituted the "fair rate of return" standard for the initiative's "insolvency" standard as the benchmark for insurance company profit. At first, the Commissioner attempted to define fair rate of return herself, setting the rate at 11.2% at a press conference. However, under pressure from a consumer lawsuit alleging that she was ignoring the procedures set forth in the state Administrative Procedure Act, Gillespie commenced the "generic" adjudicatory hearing in San Bruno on October 2, 1989.

Fernandez, a retired Superior Court judge, presided over the San Bruno hearing. He often came under fire from consumer groups for allowing duplicative testimony favoring the insurance industry and for refusing to allow testimony regarding insurance executive salaries, lack of competition in the industry, and redlining practices in poor neighborhoods. After months of testimony, an agreement between counsel ended the parade of witnesses in the adjudicatory hearing aimed at creating factors for the implementation of Proposition 103. The agreement, reached by attorneys for the Department of Insurance and the insurance industry, required insurers and consumer groups to submit written testimony until April 9. Then the record was to be closed, with the ALJ's proposed decision to be submitted by Commissioner Gillespie by April 30.

Meanwhile, in mid-April, Attorney General John Van de Kamp, Proposition 103 author Harvey Rosenfield, and Consumers Union demanded the ouster of Fernandez, alleging that he had a conflict of interest through his wife's professional involvement with insurance companies. In the April 13 letter to Gillespie, at a time when all oral and written testimony had been concluded and Fernandez' recommendation was pending, Van de Kamp claimed a conflict of interest existed because Fernandez' wife, Judith Fielding, is a lawyer with a Redwood City firm which represents many major insurance companies. The letter also charged that Fernandez had been socializing with insurance industry representatives. (*See supra* reports on CONSUMERS UNION and ACCESS TO JUSTICE FOUNDATION for related information.)

Gillespie suggested that Van de Kamp's involvement was politically motivated, since the Democratic primary for governor was nearing. She suggested that further evidence of the questionable motives of the Attorney General and consumer groups was their acceptance of the "generic hearing" approach and of Fernandez' involvement until the time had come for a decision by the administrative law judge. "Some people obviously want the litigation on Proposition 103 to drag on for ten years, but I want this job done," Gillespie said. "Now that the Department of Insurance has had several months of hearings and is close to reaching decisions and implementation, the Attorney General and those groups seek to derail the process with their motions. However, the Department will persevere and not be swayed by political rhetoric." Two weeks later, Gillespie referred the written request to Judge Fernandez himself, as required by California law; Fernandez denied the motion.

On May 3, Judge Fernandez issued his proposed decision in the generic proceeding. Under his recommended decision, Proposition 103's rollback requirement would be applied to the point where an insurance firm makes less than a 13.2% rate of return from its 1989 operations. Each California insurance company must take its total insurance operations in California (with the California share apportioned by formulae for multi- state companies) and calculate a total investment amount (in rate regulation terminology, called a "rate base"). This amount is to be the long-term industry average of one-half of the total premiums for insurance policies collected in 1989. The company is allowed to charge rates to meet its claims paid and other expenses, and to then leave sufficient profit to return 13.2% of that invested amount. Thus, under the ALJ's recommended decision, rollbacks of up to 20% of premiums charged in 1988 would be sent to those paying premiums in 1989, up to the point of this 13.2% return for each company.

In calculating the return the company is assured, the proposed decision on rollbacks also included as income the investment income generated from the invested capital comprising the rate base. Expenses for political contributions, bad faith denial of claims, legal costs for unsuccessful employee discrimination, fines and penalties, and institutional advertising were all disallowed for purposes of calculating the rate of return.

The proposed decision separately addressed prior approval ratemaking more generally, contending that the industry is too complex to posit a single methodology and generally leaving pro-

cedures to the insurance companies. Here, contrary to the "whole company" approach used in rollbacks, Judge Fernandez required a profitable rate as to each line and subline of insurance. Similar expense disallowances were suggested. However, since ratemaking is by nature prospective, the companies should be allowed to suggest their needs and rationales for suggested rates as they find appropriate, with the burden on the Commissioner to demonstrate illegality. The companies may suggest their own formulae for calculating an appropriate rate base. Under the ALJ's proposed decision, the rate of return should be within a range of 11.2-19%, based on historical industry data. The Commissioner may develop "efficiency standards" by type of insurance to use to write down expenses for ratemaking purposes.

On June 13, Commissioner Gillespie issued a ruling which partially disagreed with Judge Fernandez' recommendations. Gillespie said that insurers must give their policyholders some or all of the 20% rollback called for by Proposition 103 if the companies' profits exceeded 11.2% in 1989, whereas Judge Fernandez would have allowed a 13.2% rate of return. However, the Commissioner agreed that future rates would be set by the DOI based on a range of return between 11.2-19%, largely adopting the insurance industry's position. The Commissioner's June 13 decision will no doubt be challenged, further engulfing Proposition 103 in litigation and further delaying any rollbacks for consumers.

Judge Strikes Down Proposition 103-Mandated Auto Insurance Rating Factors. Less than a month after the first permanent regulations were adopted to implement key provisions of Proposition 103, a Los Angeles County Superior Court judge struck down the ratemaking guidelines as "unfairly discriminatory" toward rural drivers.

In mid-April, DOI finally adopted regulations which eliminated the use of ZIP codes as the primary criteria upon which auto insurance rates are based and required companies to make available good driver discount plans. Proposition 103 requires insurers to base their rates on, in decreasing order: (1) a driver's safety record, (2) annual mileage driven, (3) years of driving experience, and (4) "such other factors as the commissioner may adopt by regulation that have a substantial relationship to the risk of loss." Emergency regulations adopted by Commissioner Gillespie in December 1989 replaced Factor No. 4 with 22 optional rating factors, including both non-territorial (type of vehicle, use of vehicle, etc.) and territorial (population density, vehicle density, theft rates, etc.) factors. The emergency regulations were amended by the Office of Administrative Law to specify that the "22 optional factors cannot collectively outweigh the three mandated factors." (See CRLR Vol. 10, No. 1 (Winter 1990) pp. 106-07 for detailed background information on the emergency regulations and the 22 factors.)

On May 4, however, Commissioner Gillespie was enjoined from enforcing the regulations by Los Angeles Superior Court Judge Miriam Vogel. The Commissioner had announced a plan that would allow insurers to raise rates no more than 4.5% in rural (and many urban) areas, in order to decrease rates by approximately 20% in Los Angeles County and allow smaller decreases in other highly populated counties. But Judge Vogel, ruling in favor of the insurance industry, issued an injunction blocking implementation of the new rules. The judge indicated that eliminating a driver's ZIP code as the primary consideration in determining his/her premium rate ignores the fact that urban drivers are greater risks than those in rural areas. For this reason, she found it was unacceptable to increase rural rates to give relief to urban drivers. The Commissioner appealed Vogel's ruling in late May.

This was not the first time that Vogel had issued a ruling that had greatly damaged Proposition 103, and it was also not the first time that Vogel had sent the Commissioner and consumer groups to the appellate courts in search of relief. In December, Vogel ruled that two of the state's largest insurers—Farmers and Allstate—could substantially increases their rates in defiance of Gillespie's order temporarily limiting increases to the Consumer Price Index (4.5%). When, a month later, all of the state's insurance industry suits were consolidated in the courtroom of Vogel, the Department of Insurance and consumer groups petitioned for her removal, but Vogel herself denied the motion. A writ challenging Vogel's denial of the petition was filed in the Third District Court of Appeal on March 8, but the writ was denied and Vogel continued to preside over the insurance cases. Only the Governor's subsequent elevation of Judge Vogel to the Second District Court of Appeal removed her from the consolidated Proposition 103 lawsuits; Judge Dzintra Janavs is now presiding over them.

Proposition 103 Author Abandons "Son of 103" Initiative Efforts. With a month remaining before the deadline to submit petitions for a spot on the November 1990 ballot, Harvey Rosenfield and Voter Revolt gave up on their efforts to qualify the Proposition 103 Enforcement Act for the ballot. (See CRLR Vol. 10, No. 1 (Winter 1990) p. 108 for background information.)

The new initiative would have been an ultimatum to the insurance industry, giving insurers one year to fully implement Proposition 103's rate rollback provisions and to reduce the number of uninsured motorists to no more than 15% of the state's licensed drivers. If the goals had not been met, the measure would have ousted private insurance companies from the state and would have replaced them with a state insurance agency.

The radical proposal would have required one million signatures by May 18 to qualify for the ballot. But, by April 13, the proposed initiative had gained just under 600,000 signatures and was abandoned.

Garamendi and Bannister Win Nominations for Insurance Commissioner. At the June 5 election, Democratic Senator John Garamendi and Republican Wes Bannister took their parties' nominations for the now-elective position of Insurance Commissioner.

Garamendi, a late entrant into the race, prevailed over television commentator Bill Press, who had captured the endorsement of his party at its state convention; State Board of Equalization member Conway Collis, who had promised to be the insurance industry's "worst nightmare" and to be "punitive and unfair" to insurers if elected; San Francisco attorney Ray Bourhis, who recently won a major case against DOI; and consumer advocate Walter Zelman, former executive director of California Common Cause. Zelman, who quit the CCC job he held for thirteen years in order to run, led in the early polls, due to his ballot listing as "Director, Common Cause." That designation was formally approved by the Secretary of State, but CCC later filed a lawsuit to compel Zelman to remove the reference to Common Cause. On March 29, Sacramento County Superior Court Judge James T. Ford barred the designation, based on his interpretation of the Elections Code. Zelman later plummeted in the polls and finished a distant fourth.

The race for the Republican nomination was wide open after the withdrawal of Insurance Commissioner Roxani Gillespie in December. (See CRLR Vol. 10, No. 1 (Winter 1990) p. 109 for background information.) Huntington Beach

city council member Bannister, the owner of a small independent insurance agency, defeated attorney Tom Skornia and several others.

Assigned Risk Auto Insurance. On April 6, the governing board of the California Automobile Assigned Risk Plan (CAARP) announced that it will again ask Commissioner Gillespie for a rate increase for assigned risk auto insurance. The request asks for an increase of 160.5% in premiums and comes on the heels of the Commissioner's recent rejection of a 112.3% increase. (See CRLR Vol. 10, No. 1 (Winter 1990) p. 108; Vol. 9, No. 4 (Fall 1989) p. 94; and Vol. 9, No. 2 (Spring 1989) p. 85 for background information.) In another move to cut costs, the board stated that it would drop all "good" drivers from the plan. This would result in as many as 400,000 of the plan's 800,000 drivers being dropped. Commissioner Gillespie stated that the move would deprive low-income drivers with good driving records of the ability to obtain insurance coverage that is mandated by state law. She vowed that legal action would be taken; the CAARP board countered by appealing the Commissioner's denial of its rate increase request *(see infra* LITIGATION).

In an additional response to CAARP's plan to drop good drivers, Commissioner Gillespie began rulemaking procedures that would require CAARP to cover low-income drivers even if they have good driving records. The rulemaking proposal, named the Insurance Affordability Method (IAM), contemplates adding sections 2409 through 2419 to Title 10 of the CCR. The regulations are designed to ensure that all Californians are able to obtain statutory limits of auto insurance. In addition, the rules are also designed to bar drivers who can easily afford insurance in the voluntary market but seek to obtain the lower CAARP rates. Finally, the rules will promote the availability of assigned risk insurance to eligible drivers in a manner that is neither arbitrary or capricious.

Commissioner Reconsiders And Readjusts Workers' Compensation Rates. On February 13, Commissioner Gillespie adopted the proposed decision of Deputy Insurance Commissioner Peter Groom, approving a 1% increase in workers' compensation insurance rates. The approval has the effect of amending section 2350, Title 10 of the CCR, which deals with premium rates charged to employers for workers' compensation insurance.

This approval modifies a ruling by the Commissioner made last year, which rejected a proposal by the Workers' Compensation Insurance Rating Bureau of California (Bureau) to increase rates by 5.9%. DOI's previous decision rejected the Bureau's rate request and ordered the Bureau to recompute its rates based on an increase of 4.9%. (See CRLR Vol. 10, No. 1 (Winter 1990) pp. 108-09 for background information.)

In this latest ruling, the Commissioner reconsidered and granted the additional 1% increase. The result is that the Bureau's original rate request of 5.9% has been approved. The Commissioner cited her erroneous rejection of the Bureau's analysis in the former proceeding as its basis for approving the current increase. The increase was effective March 1 as to all policies with anniversary dates of January 1, 1990 or thereafter.

Insurer Abuses Alleged In Child Cancer Cases. Recently, a coalition consisting of families of child cancer victims and consumer groups filed a petition with DOI, alleging that insurers have delayed or refused to pay clearly legitimate claims submitted by the families. The petition claimed that the insurers consistently failed to pay claims within the statutorily required period of thirty days, or completely refused to pay legitimate claims. Commissioner Gillespie stated that DOI would work with and support the coalition.

Homeowners Insurance. On March 13, DOI issued the results of a survey of comparative rates of homeowners insurance for dwellings throughout the state. Commissioner Gillespie noted that the "survey underscores the need to shop around...as rates varying greatly by area and insurer." Thirty insurers writing approximately 80% of all homeowner policies were surveyed. Free copies of the report are available by writing to DOI.

DOI Denies Acquisition Application. On April 9, DOI rejected a French takeover of the Farmers Insurance Group, jeopardizing the proposed $21 billion hostile buyout of Britain's BAT Industries. BAT owns Farmers, and bidder Sir James Goldsmith had proposed to sell Farmers to Axa-Midi Assurances of France upon acquiring BAT, Britain's biggest conglomerate.

DOI ruled that policyholders' interests would not be served by either a takeover of BAT by Goldsmith's Hoylake Investments, Ltd. or the sale of Farmers to Axa-Midi. Chief among DOI's objections was that Axa-Midi was putting no cash behind its $4.5 billion offer. Commissioner Gillespie stated that "[w]hile Axa Midi has an outstanding European record, the leverage of this deal is such that it would endanger the Farmers group of insurance companies." The Commissioner said Axa-Midi "basically looked to the financial performance of Farmers companies to repay the acquisition debt. However, insurance companies cannot be relied upon to repay this type of sizeable debt as it would be dangerous to policyholders and claimants."

LEGISLATION:

AB 2650 (Peace), as amended June 12, would make a number of changes regarding motor vehicle insurance, including requiring motor vehicle insurers to report specified information to the Commissioner, and requiring the Commissioner to make the information available to the public and local law enforcement officials. This bill would also provide that it is a felony to knowingly present or cause to be presented, under a contract of insurance, a bill in support of a claim for medical or other treatment of a physical injury if the treatment was not given or was obtained with the knowledge that it was unnecessary; to knowingly encourage a claimant to obtain medical or other treatment of a physical injury, or to obtain bills for that treatment where the treatment was not necessary or not performed with the intent that a claim would be made for the cost of the treatment; to knowingly give perjured testimony or make false affidavits in support of a false or fraudulent claim; or for an attorney to require a person to use a particular health care provider as a condition of accepting that person as a client or agreeing to prosecute a case.

This bill would require every admitted insurer selling automobile insurance to offer and sell a basic automobile insurance policy to owners and operators of private passenger motor vehicles who would qualify to purchase voluntary market coverage from that insurer. Under this bill, the policy of basic automobile insurance would only provide liability coverage in minimum amounts, and coverage for personal injury or death would be limited to economic losses. The bill would require the Commissioner to set a specified maximum rate for a policy of basic automobile insurance, and would require every admitted insurer to offer additional coverage.

Also, AB 2650 would require the Commissioner to approve or issue a reasonable plan, to be known as the California Auto Plan, for the equitable apportionment among insurers of applicants for basic automobile insurance

who are good drivers.

This bill would provide that every automobile insurer is required to act in good faith toward, and to deal fairly with, policyholders and others, as specified. This bill would provide that a policyholder or other person may bring an action for a violation of statutory provisions that prohibit unfair and deceptive practices, and may recover damages, but would limit the award of exemplary damages to $500,000. However, the bill would provide that with respect to motor vehicle liability claims, an automobile insurer is not liable for an alleged failure to comply with the duty of good faith if certain specified procedures are complied with.

This bill would also require motor vehicle comprehensive or collision insurers to provide coverage without deductible or minimum amount for repair or replacement of damaged safety equipment. This bill is pending in the Senate Judiciary Committee.

AB 2701 (Areias), as amended June 14, would require certification, on and after July 1, 1991, of all persons selling policies or certificates of disability insurance to persons eligible for Medicare by reason of age. The bill would impose certification requirements consisting of completion of a course, continuing education, and signing a code of ethics. The bill would also require the maintenance of a permanent place of business, records of activities, and liability insurance. The bill would require the Insurance Commissioner to establish an advisory committee to recommend approval of accredited courses of education. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

AB 3641 (Johnston). Existing law requires the Commissioner to approve or issue a reasonable plan for the equitable apportionment among liability insurers of applicants for automobile bodily injury and property damage liability insurance who are entitled but unable to obtain that insurance through ordinary methods. Existing law authorizes the subscribing insurers to form their own organization to operate that plan, which is known as the assigned risk plan (*see supra* MAJOR PROJECTS).

As amended June 18, this bill would authorize groups of insurers not under common ownership or management to form a limited assignment distribution arrangement, that would have one servicing carrier that writes assigned risk business on behalf of the members of the arrangement in return for consideration from the other participating carriers for not writing the business. The servicing carrier would be subject to the approval of the Commissioner.

This bill would also authorize the Commissioner to require insurers to report various loss and expense ratios and, if the insurers combined ratio exceeds the mean by 10%, a statement of the reason and a plan for reducing the ratio. The information would be a public record, and would be reported by the Commissioner to certain policy committees of the legislature. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

AB 3683 (Hauser) would prohibit motor vehicle liability insurers from refusing applications or issuance of insurance or from cancelling insurance solely for the reason that the applicant is on active duty service in the Armed Forces of the United States. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 2569 (Rosenthal) would require the Commissioner to establish a program on or before July 1, 1991, for the handling of insurance complaints registered with DOI, for responding to inquiries and, where warranted, for bringing enforcement actions against insurers. This bill, which would also require the DOI to develop a complaint handling evaluation form, is pending in the Assembly Finance and Insurance Committee.

AB 4282 (Johnston) would impose several restrictions on the advertisement, solicitation, and issuance of Medicare supplement policies, such as requiring a copy of every Medicare supplement policy advertisement to be filed with the Commissioner thirty days before its use. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 2136 (Robbins) would require member insurers to disclose the amount of any California Insurance Guarantee Association surcharge on billings or declarations sent to those insured under policies of automobile insurance and certain property insurance. This bill is pending in the Assembly Finance and Insurance Committee.

SB 2163 (Hart) would require the Insurance Commissioner, among others, to adopt regulations governing ex parte communications, as defined, with respect to his/her department. In general, these regulations would require a copy of written ex parte presentations and a memorandum of ex parte oral presentations to decisionmakers, as defined, to be placed in the public file or record of the affected proceeding. This bill is pending in the Assembly Finance and Insurance Committee.

SB 2179 (Robbins) would, among other things, require the Commissioner to report to the legislature on or before January 1, 1992, on the effectiveness of his/her monitoring and regulation of the financial condition of insurers, as specified. This bill is pending in the Assembly Finance and Insurance Committee.

SB 2299 (Davis) would require owners of private passenger vehicles registered in the state to have either liability insurance or compensation insurance. Owners of other vehicles would generally be required to have liability insurance. According to this bill, the compensation insurance would provide first-party benefits for specified losses, and would prohibit the recovery of noneconomic losses in actions for personal injury arising out of the use of a motor vehicle as a motor vehicle by or on behalf of or against a person who was insured under a policy of motor vehicle compensation insurance unless the injury giving rise to the noneconomic loss is a serious injury, as defined. This bill is pending in the Senate Judiciary Committee.

SB 2618 (Robbins) would require disability insurers and certain health care providers to pay an annual fee in order to fund increased investigation and prosecution of fraudulent health insurance claims and the compilation of health insurance claims data. This bill is pending in the Assembly Finance and Insurance Committee.

SB 2642 (Robbins) would require licensed insurance agents and brokers to annually and satisfactorily complete certain specified courses and programs as may be approved by the Commissioner. This bill would also provide for prelicense education, and would require the Commissioner to appoint a curriculum board, as specified. This bill is pending in the Assembly Finance and Insurance Committee.

SB 2682 (Hart) would require, on and after July 1, 1991, insurers engaged in writing policies of homeowner's insurance to also offer liability coverage in specified coverage amounts for licensed family day care homes, as specified. This bill is pending in the Assembly Finance and Insurance Committee.

SB 2777 (Robbins) would provide that CAARP shall not refuse to accept and assign applications from persons who are eligible for a good driver discount policy, and would prohibit CAARP from requiring rejection by an insurer as a precondition to obtaining insurance through the plan. This bill is

pending in the Assembly Finance and Insurance Committee.

SB 2851 (Hill) would delete the existing requirement that every driver and owner of a motor vehicle maintain a form of financial responsibility, and would instead require each owner of a private passenger motor vehicle, other than a motorcycle, to provide insurance that would provide personal injury protection benefits. Owners of other motor vehicles and of motorcycles would be required to provide insurance providing personal injury protection benefits to persons other than operators and occupants of the vehicles, and to provide liability coverage. The personal injury protection benefits would provide benefits for basic economic loss of up to $15,000 actual payout per person for health care expenses, for loss of earnings up to $1,000 per month, and other benefits, as specified. Persons injured in a motor vehicle accident would generally be entitled to receive those benefits regardless of fault. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

AB 4144 (Epple) would prohibit the Commissioner from making or participating in, or using his/her official position to influence, any of various specified governmental decisions, if he/she knows or has reason to know that he/she has a financial interest. This bill is pending in the Senate Governmental Organization Committee.

AB 3014 (Lancaster) would require the Commissioner to adopt regulations governing administrative hearings within specified time limits and provide that the sole remedy for failure to adopt those regulations within prescribed time periods or to abide by the regulations once adopted is a writ of mandate to compel the Commissioner to adopt the regulations or commence or resume hearings. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 2135 (Robbins) would prohibit an insurer from engaging in any marketing action, as defined, that would have the effect of discouraging or limiting the right of a person to purchase a good-driver discount policy. A violation of the provision would be subject to administrative sanctions by the Commissioner. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SB 2396 (Roberti) would provide that political contributions, as defined, are not to be included in determining the expenses of an insurer, and would require insurers to file a list of political contributions. This bill is pending in the Assembly Finance and Insurance Committee.

AB 4035 (Nolan) would have required insurers to reduce premium rates on January 1, 1991, for private passenger automobile insurance by 20% below corresponding rates in effect April 30, 1989, and prohibited rate increases for auto insurance until January 1, 1992, except for a change in risk or if the Commissioner determines the rate threatens the financial condition of the insurer. This bill was dropped by its author.

The following is a status update on bills reported in detail in CRLR Vol. 10, No. 1 (Winter 1990) at pages 109-10:

AB 451 (Johnston), regarding the qualifications that must be met in order to qualify for a good driver discount policy, was signed by the Governor on May 16 (Chapter 93, Statutes of 1990).

ACA 46 (M. Waters). Existing law imposes an annual tax, based on the insurer's gross premiums, on all insurers transacting insurance business in California, other than ocean marine insurance. This gross premiums tax is in lieu of all other taxes, state and local, upon those insurers and their property, with specified exceptions. This bill, as amended May 7, would have created an additional exception for any county or municipal taxes upon insurers' activities, and any personal property used in connection therewith, which are not involved in the production of premiums or the adjustment of claims. This bill was dropped by its author.

SB 3 (Roberti), which would create the Insurance Consumer Advocate's Office in the state Department of Justice, is pending in the Assembly Finance and Insurance Committee.

SB 207 (Boatwright), which would require insurers subject to Proposition 103 ratesetting regulations to submit a quarterly report to the Commissioner relating to the Commissioner's ratesetting procedures, is pending in the Assembly Finance and Insurance Committee.

SB 464 (Robbins) would provide that the ownership or financial control, in part, of an insurer by any other state, the United States, or by a foreign government, or by any political subdivision or agency thereof, shall not restrict the Commissioner from issuing or renewing or continuing in effect the license of that insurer to transact insurance business in this state, under specified conditions. This bill was enrolled to the Governor, but was returned to the desk of the Chief Clerk of the Assembly.

SB 604 (Green), which would require the Commissioner to annually report to the legislature on defined property/casualty insurance lines, is pending in the Assembly Finance and Insurance Committee.

SB 1518 (Nielsen), which would prohibit the Insurance Commissioner from being employed in the insurance industry for two years after leaving office, is pending in the Assembly Finance and Insurance Committee.

SB 1695 (Keene), which would enact changes in DOI's Bureau of Fraudulent Claims, is pending in the Assembly Finance and Insurance Committee.

AB 1721 (Friedman), as amended June 25, would prohibit life and disability insurers from discriminating, as to eligibility or rates, on the basis of sexual orientation. This bill is pending in the Senate Committee on Insurance, Claims and Corporations.

SCR 22 (Robbins), which would have requested a freeze in CAARP premium rates until January 1, 1990, or until DOI has received certain cost data, was dropped by its author.

AB 37 (Bane), as amended June 7, would provide that a person guilty of insurance fraud or filing false claims would be liable for a penalty of ten times the amount of the claims, plus reasonable attorneys' fees, in addition to any other penalty already provided by law. This bill is pending in the Assembly inactive file.

LITIGATION:

In *The Travelers Indemnity Co. v. Gillespie*, No. S008962 (Jan. 9, 1990), the California Supreme Court held that auto insurance companies may refuse to renew policies and withdraw from California without finding another insurer to serve its customers. Proposition 103 prohibits insurers from cancelling or failing to renew policies except for cases of fraud, failure to pay premiums, or a "substantial increase" in the insured risk. Commissioner Gillespie contended that the clause in the measure would require four Travelers companies to ensure "continuous coverage" through other companies before leaving the state.

But, in a 4-3 decision, the Supreme Court held that the measure itself had envisioned that its passage might send companies out of the state. And "since nonrenewal and cancellation are the only methods by which a withdrawing insurer can terminate its existing automobile policies, the conclusion is inescapable that the mandatory renewal provision does not apply to insurers who withdraw from the California market," wrote Justice Marcus M. Kaufman.

In order to resolve a split of authority

on the issue of whether a city may tax an insurer's business activities not directly related to insurance, the California Supreme Court has agreed to review a Second District Court of Appeal ruling. The Second District case, *Mutual Life Insurance Co. of New York v. Los Angeles*, No. S008824, held that Article 13, Section 28 of the California Constitution exempts insurers from Los Angeles utility user, parking lot, and general business taxes assessed against two office buildings owned and operated by Mutual Life. This holding directly conflicts with a previous appellate decision involving a San Francisco tax on furnishings of the Hyatt Union Square Hotel, then owned by an insurance company. In *Massachusetts Mutual Life Insurance Co. v. City and County of San Francisco*, 129 Cal. App. 3d 876 (1982), the court held that the property could be taxed because it was not directly related to the business of insurance.

On December 27, the Second District Court of Appeal, in *Prudential Reinsurance Co. v. Superior Court*, No. B041978, ordered that an order issued by Superior Court Judge Kurt J. Lewin be vacated. In the liquidation proceeding of Mission Insurance Companies (Mission) by DOI, Judge Lewin had ruled in favor of DOI with respect to reinsurers' rights to debt-credit set-offs. The appellate court's writ of mandate directed the Superior Court to vacate its previous ruling and issue a new order conforming to the appellate opinion.

The issue before Judge Lewin was whether DOI, as liquidator of Mission, could require Prudential Reinsurance Company (Prudential) to pay the full amount of reinsurance proceeds owed to Mission by Prudential, without any set-off credit for debts owed by Mission to Prudential. Prudential claimed that it was allowed set-offs by Insurance Code section 1031. Judge Lewin disagreed, and ruled that Prudential must pay the full amount due without any set-off of Mission's debt.

The Second District vacated Judge Lewin's order, holding that section 1031 allows Prudential to subtract from any amount due to Mission any Mission debts due to Prudential. DOI argued, but the court rejected, the proposition that public policy dictates that policyholders should be paid before insurers. The court held that "strong public policy...may not override the unequivocal language of the...statute." On April 23, the California Supreme Court granted review of this case.

In several related cases consolidated under the title of *Insurance Commissioner of the State of California v. Mission Insurance Companies*, No. C572724, Judge Lewin approved a rehabilitation agreement regarding the liquidation of Mission Insurance Companies. The agreement provides for the transfer of the assets and liabilities of Mission to the Commissioner as trustee. Mission will be released from delinquency proceedings and, subject to certain conditions, will be reorganized.

In an appeal from a ruling in these consolidated cases, the Second District Court of Appeal affirmed a ruling giving the Commissioner the right to sue reinsurers of Mission for bad faith. The court upheld DOI's right to sue reinsurers who refused to make payments in bad faith, thus driving Mission into insolvency.

Judge Lewin also ruled that DOI, as liquidator of Mission, may be awarded damages for future losses flowing from reinsurers' breaches of reinsurance agreements. The court held that future losses were recoverable as long as they are proven with sufficient certainty at trial. Trial is scheduled to begin on November 1.

In *Henry v. Associated Indemnity Corp.*, No. D009427, the Fourth District Court of Appeal recently held that a first-party insured's claim against a homeowner insurer for bad faith under Insurance Code section 790.03(h) is not barred by *Moradi-Shalal v. Fireman's Fund, Inc.* or *Zephyr Park v. Superior Court*. (See CRLR Vol. 9, No. 4 (Fall 1989) p. 97 and Vol. 8, No. 4 (Fall 1988) p. 87 for background information on these cases.) The court held that an insured may pursue traditional common law remedies notwithstanding the running of one-year statute of limitations contained in insurance policies if the true extent of the damage to the home was not known until after the running of the period.

The Second District Court of Appeal recently held that Business and Professions Code section 17200 does not provide a plaintiff with a cause of action for alleged unfair settlement practices. In *Safeco Insurance Co. of America v. Superior Court*, No. B045042, the court held that *Moradi-Shalal v. Fireman's Fund, Inc.* abolished the private cause of action for damages based on unfair claims settlement practices under either Insurance Code section 790.03(h) or the Business and Professions Code. In this case, plaintiff had an auto accident with an insured of Safeco. Safeco refused to pay plaintiff certain amounts claimed by plaintiff. Plaintiff sued under section 17200 of the Business and Professions Code, claiming that Safeco's failure to pay amounted to unfair competition, prohibited by the section. Plaintiff also contended that, although *Moradi-Shalal* barred an action under the Insurance Code, such an action could be maintained under the Business and Professions Code. The court rejected the argument, stating that the Business and Professions Code provided "no toehold for scaling the barrier of *Moradi-Shalal*." In addition, the court reasoned that accepting the plaintiff's proposition would render *Moradi-Shalal* "meaningless."

In December 1989, Commissioner Gillespie reversed an administrative law judge's decision and denied a request by the CAARP board to raise assigned risk auto insurance rates by 112.3%. The CAARP board asked the state Supreme Court to hear an appeal but the court refused, saying that the appeal had to go through the lower courts first. CAARP refiled in Los Angeles County Superior Court, in *California Automobile Assigned Risk Plan v. Gillespie*, No. C728295, where it sought to overturn Commissioner Gillespie's rate increase denial, and to drop "good" drivers from the plan. Judge Miriam Vogel overruled the Commissioner's decision and granted the rate increase. However, Vogel ordered CAARP to continue to insure good drivers as long as the drivers completed forms under penalty of perjury giving proof they were denied coverage in the voluntary market by one company for reasons other than their driving records, such as ethnicity or area of residence. DOI said it would appeal the decision regarding the rate increase.

In *California State Automobile Ass'n Inter-Insurance Bureau v. Superior Court*, No. S009171, the California Supreme Court held that a stipulated judgment of liability is a final judicial determination for the purpose of maintaining a *Royal Globe* third-party bad faith action against an insurer. Although *Moradi-Shalal v. Fireman's Fund, Inc.* abolished *Royal Globe* Insurance Code section 790.03(h) bad faith lawsuits by third parties, *Moradi-Shalal's* holding was applied prospectively. Thus, third-party bad faith claims preexisting *Moradi-Shalal* survived. However, *Moradi-Shalal* required that the surviving lawsuits must have a final judicial determination of the insured's liability as a prerequisite to maintenance of the cause of action. The issue before the Supreme Court in *California State Automobile Ass'n Inter-Insurance Bureau* was whether a stipulated judgment of liability was a final judicial determination within the meaning of *Moradi-Shalal*. The court concluded that the stipulated judgment was a final

judicial determination and vacated a lower court ruling to the contrary.

In *United States v. Stites*, No. 90-0391-K, fourteen attorneys were indicted by a San Diego federal grand jury on April 24 on racketeering and mail fraud charges. The group, known as "The Alliance," is charged with bilking insurance companies out of up to $50 million. The scheme was based on a 1984 appellate decision, *San Diego Navy Federal Credit Union v. Cumis Insurance Society Inc.*, which held that an insured who is sued and then becomes involved in a coverage dispute with the insurer is entitled to separate counsel at the insurer's expense. The Alliance used this ruling to create lawsuits with sham conflicts between the insured and insurer. The manufactured lawsuits were then prolonged by the attorneys for long periods of time while generating huge charges for attorneys' fees. The defendants face twenty-year prison terms, forfeiture of illegally gotten gains or fines of twice the amount of the gains if convicted on the RICO counts, as well as a $250,000 fine if found guilty of mail fraud.

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 September 1989, 234,979 salespersons, 91,365 brokers, 18,272 corporations) and subdivisions.

License examinations require a fee of $25 per salesperson applicant and $50 per broker applicant. Exam passage rates average 53% for salespersons and 43% for brokers. 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. Approximately 130,000 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 May 9, the Office of Administrative Law approved several regulatory changes adopted by DRE in recent months. The affected sections include sections 2785 (conduct justifying license denial), 2792.20 (executive sessions of common interest subdivision associations), 2792.22 (operating budget of common interest subdivision associations), and 2792.30 (alternatives to the "reasonable arrangements" required in governing instruments of common interest subdivision associations). (See CRLR Vol. 10, No. 1 (Winter 1990) p. 111 and Vol. 9, No. 4 (Fall 1989) for details on these changes.)

However, OAL rejected DRE's addition of sections 3050-3059, which would have established minority and women business participation goals for DRE's contracts, pursuant to Public Contract Code sections 10115-10115.10. OAL found that the proposed sections failed to satisfy the clarity, nonduplication, consistency, necessity, authority, and reference requirements of Government Code section 11349.1. DRE plans to hold a public hearing on the proposed regulations in October, and resubmit them to OAL following the hearing.

On March 19, OAL approved DRE's amendment to regulatory section 2746, which requires reporting of criminal convictions and of prior real or other business or professional licenses during the ten years prior to the application for a corporate real estate broker license and for reinstatement of a license. It also requests the person's social security number on a voluntary basis.

Broker Supervision Task Force. The Commissioner recently created a task force to study and make recommendations on ways to reduce causes of action against licensees. The task force concluded that many disciplinary actions can be avoided if brokers exercise adequate supervision over their salespersons. The task force made suggestions in the following areas:

-Staff Reports. The broker should require monthly reports from sales staff covering (1) trust funds received; (2) listing agreements; (3) transactions closed; (4) escrows opened; and (5) compensation received.

-Broker Availability. The broker or someone qualified to review and initial documents pursuant to regulatory section 2725 (failure of broker to review and initial agreements) should be reasonably available in the office to answer questions and resolve problems relating to ongoing transactions, as needed.

-File Review. The broker may want to install a regular system of reviewing files to ensure that appropriate documents are being reviewed and initialed per section 2725.