DONABEDIAN V. MERCURY: A COURT DECISION THAT THREATENS THE

STABILITY OF THE STATE'S INSURANCE MARKETS

If after 16 years of off-and-on court cases attempting to interpret the ambiguous and contradictory language of Proposition 103 isn't enough, this month, another interpretation came down from the Second District Court of Appeal in a case known as *Donabedian v. Mercury.* The ruling states that under Proposition 103, any citizen has the right to act as a "private citizen attorney general" and directly sue any insurance company if he or she disagrees with the company's California Insurance Department (CDI) approved rates, rules, or underwriting plans.

Donabedian, a private citizen, filed a lawsuit against Mercury Insurance Company in the Superior Court, claiming that under Proposition 103, it was illegal for the company to use a prior insurance record – approved by the (CDI) -- as part of its underwriting and pricing practices. Judge Carolyn Kuhl agreed with Mercury's argument that only the Insurance Commissioner, not the courts, can hear consumers' complaints. The judge cited a 1947 law giving the State Insurance Department regulatory authority over the insurance industry. The case was then taken to the appellate court. Interestingly, two friends-of-the-court briefs were filed. One by Harvey Rosenfield, author of Proposition 103 and counsel to the Foundation for Taxpayers and Consumer Rights, and the second by the CDI.

In his brief, Insurance Commissioner John Garamendi threw a bombshell into the scenario. He urged the court to approve citizen lawsuits against insurance companies, explaining that the Department of Insurance "simply lacks sufficient resources to pursue every allegation." The Court reversed the lower court decision and concluded that consumers have the right to enforce Proposition 103 through the state's Unfair Competition Law (UCL).

The CDI told the court that it did not have the "resources" to check every single activity of the insurance industry in California, but welcomed private citizen lawsuits to help it do its job. The (CDI), has more than 1350 employees, making it the second largest insurance department in the United States. The CDI also has the largest budget of any insurance department in the United States -- $170 million for fiscal year 2004.

Here is a direct quote from the California Insurance Commissioner's website stating what he believes the duties of the CDI are:

"Insurance is a $106 billion-a-year industry in California. Overseeing the industry and protecting the state's insurance consumers is the responsibility of the California Department of Insurance (CDI). The CDI regulates, investigates and audits insurance

business to ensure that companies remain solvent and meet their obligations to insurance policyholders.

As administrator, the Commissioner enforces the laws of the California Insurance Code and promulgates regulations to implement these laws.

That seems pretty clear. Now here is what the insurance law states:

The Insurance Commissioner is elected by the voters. Ins. Code § 12900. The reason for this is to ensure that the Commissioner is ***accountable*** *to the people for his actions as Insurance Commissioner. JA p. 569 (Ballot Pamphlet).".*

If the Appellate Court ruling allows private citizen lawsuits against insurance companies for rating plans approved by the commissioner, and Proposition 103 implicitly states*: "Insurance Code section 1860.1 grants to the Commissioner original and exclusive jurisdiction over insurance ratemaking matters." Id. p. 4.No insurance rate may be charged unless approved by the Commissioner. (Ins. Code, § 1861.01, subd. (c).),"* then why would the Commissioner or CDI need help to regulate the industry?

The law also states: "***The Commissioner is charged with enforcement of the Insurance Code, and in particular with the review and approval of proposed rates and class plans to ensure that rates are not "excessive, inadequate, unfairly discriminatory, or otherwise in violation of" Chapter 9 of Division 1, Part 2 of the Insurance Code*** *("Chapter 9"). Ins. Code §§ 12921(a); 1861.01(c); 1861.05(a).*

These provisions give the California Insurance Commissioner exclusive original jurisdiction over the rate making process." Therefore, **Harvey Rosenfield, author of Proposition 103, violates the very initiative he claims to have written by allowing the 36 million citizens of California the right to sue an insurance company that has lawfully, under Proposition 103, received approval for its rates from the Insurance Commissioner of California through the California Department of Insurance. Plus, the Insurance Commissioner, under Proposition 103, is now in violation of the law which requires him to regulate the industry by allowing 36 million citizens to regulate the insurance industry under Proposition 103.**

It gets even better. There is also a "double-enrichment" aspect to the new court ruling. Let me explain. First, under the Appellate Court ruling, any insurance company that wants to raise or lower its rates, would, under Proposition 103, proceed with a filing request to the (CDI which, could take up to 18 months or longer for approval, amendment, or denial. **But wait.** Didn't the author of Proposition 103 also write a section into the initiative that allows consumer groups, like the author's group -- Foundation for Taxpayers and Consumers

Rights -- to *intervene* on any insurance filing or procedure by any insurance company before the CDI? Yes. So, not only can his group or any qualified group under the Proposition 103 definition, intervene in proceedings. All intervenors get hourly wages for their intervention, paid for by insurance companies appearing before the CDI. In addition, the intervenors get expenses, including hotels, taxi's and meals while participating in the proceedings. Since Proposition 103 narrowly passed by 51 percent in 1988, the author's groups have collected more than $2 million in intervenor fees through the CDI, and paid for by insurance companies – even when some of those companies wanted rate reductions!.

Now comes the double-enrichment. If and when the filing for a rate change is granted to an insurance company, under the Appellate Court ruling, the author of Proposition 103 and his partners can sue the company a second time stating they believe the rate that was approved is illegal. It's a double lottery windfall for the so-called consumer groups, and a giant bite out of the wallets of consumers who eventually will have to pay all of the exorbitant, unnecessary costs.

Auto Insurance Report, publisher Brian Sullivan, in his weekly report offers another scenario

An insurance company uses territory as its most important rating factor. Under rules promulgated by the insurance department, this is allowed. But a consumer believes that Proposition 103 forbids this practice, and earlier court rulings supporting the regulation are wrong. So they sue personally to try and overturn the rules." It means that the insurance industry in California now has 36 million regulators who can sue and 1400 insurance department employees who scrutinize every filing, setting the insurance companies up for law suits under this appellate court ruling.

The Mercury Insurance Company has asked the Appellate Court for a rehearing on the *Donabedian* case. If denied, the company will take the case to the California Supreme Court. Meanwhile, Mr. Rosenfield has also filed a similar brief in another similar lawsuit, *Poirer v. State Farm Mutual Auto Insurance Company.* Although the case is similar, there are some differences. Vanessa Wells, State Farm's legal counsel in the *Poirer* case, is confident that at some point the courts will realize the damage a plaintiff's verdict would bring to the highly regulated insurance business. "As a matter of both law and public policy, there is no question that a decision that would allow every Department of Insurance-approved rate filing to be challenged in front of a jury would be as much anti-consumer as it would be anti-insurer," she said. "We are confident the courts will recognize that consumers need a healthy and competitive insurance industry in the state and a decision that creates regulatory gridlock by the courts will lead to neither industry health nor competition."