

DEVELOPMENTS IN CALIFORNIA INSURANCE LAW – 2008

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This article reviews last year's developments in three areas of California insurance law: legislation, case law decisions, and insurance regulatory initiatives.

1. LEGISLATION

The following are a few of the key bills signed into law in 2008 affecting property and casualty insurance, life, and disability insurance. All are effective January 1, 2009 unless otherwise specified in the statute.

A. Property and Casualty Insurance

Assembly Bill (AB) 1874, 2008-2009 (Cal. 2008) (Coto) State Compensation Insurance Fund. Part of a set of reforms aimed at California's workers compensation insurer of last resort, AB 1874, 2008-2009 (Cal. 2008) increases the number of members on the board of directors of the State Compensation Insurance Fund from five to 11.

AB 2143, 2008-2009 (Cal. 2008) (De Leon) Insurance: Fraud Assessment Fees. AB 2143 extends the repeal date on the statute, which authorizes a 50-cent annual per vehicle assessment to fund the Department of Insurance Fraud Division and the Organized Automobile Fraud Interdiction Program from January 1, 2010, to January 1, 2015.

AB 2654, 2008-2009 (Cal. 2008) (Laird) Discrimination. AB 2654, 2008-2009 (Cal. 2008) adds references to characteristics listed in the Unruh Civil Rights Act to Insurance Code statutes relating to discrimination in auto insurance and property insurance.

AB 2956, 2008-2009 (Cal. 2008) (Coto) Insurance: Agents and Brokers. Resolving a key subject discussed in last year's *Annual Review*, AB 2956, 2008-2009 (Cal. 2008) revises the statutory definitions relating to producer licenses to distinguish between the acts of an insurance agent and the acts of a broker. The bill provides for a presumption of broker status under specified conditions where a person on behalf of another person transacts insurance with, but not on behalf of, an admitted insurer. The bill further provides that the presumption may be rebutted if any one of certain factors (e.g. the licensee is appointed as an agent of the insurer for that class of insurance) is present or if the "totality of the circumstances" indicates that the licensee is acting on behalf of the insurer.

Senate Bill (SB) 28, 2008-2009 (Cal. 2008) (Simitian) Motor Vehicles: Mobile Service Device. SB 28, 2008-2009 (Cal. 2008) prohibits a person from driving a motor vehicle while using an electronic wireless communication device to write, send, or read a text-based communication.

SB 33, 2008-2009 (Cal. 2008) (Simitian) Vehicles: Wireless Telephones and Mobile. SB 33, 2008-2009 (Cal. 2008) prohibits a person possessing a valid instruction permit, student license, or provisional license from driving a motor vehicle while using a wireless telephone, including hands-free devices, except for emergency purposes.

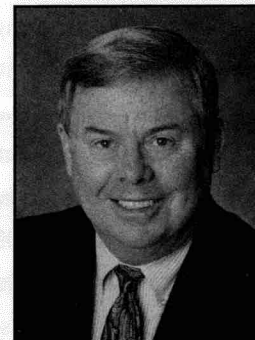
SB 1145, 2008-2009 (Cal. 2008) (Machado) State Compensation Insurance Fund. Adding to the reforms of AB 1874 discussed above, SB 1145, 2008-2009 (Cal. 2008) makes the board of directors of State Compensation Insurance Fund ("SCIF") subject to the Open Meetings Act and the California Public Records Act with a number of exceptions. The bill also requires the board of directors of SCIF to appoint a president, a chief financial officer, a chief operating officer, a chief information technology officer, a chief investment officer, a chief risk officer, and a general counsel. Effective Sept. 26, 2008.



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SB 1279, 2008-2009 (Cal. 2008) (Maldonado) Insurance: Electronic Records. SB 1279, 2008-2009 (Cal. 2008) provides that the Department of Insurance may maintain records in electronic form and handle transactions electronically to the extent not prohibited by law.

SB 1388, 2008-2009 (Cal. 2008) (Torlakson) Vehicles: DUI: Ignition Interlock. SB 1388, 2008-2009 (Cal. 2008) requires that specified persons immediately install an ignition interlock device on all owned vehicles for one to three years under specified circumstances (e.g. being convicted of driving a vehicle when his or her license has been suspended or revoked for conviction of DUI within a 10-year period). Effective July 1, 2009.

SB 1608, 2008-2009 (Cal. 2008) (Corbett) Disabled Persons: Equal Access: Civil Actions. SB 1608, 2008-2009 (Cal. 2008) requires a licensed architect, as a condition of license renewal, to complete courses regarding disability access requirements. SB 1608 will also allow a defendant in a disability access lawsuit to obtain a temporary stay in the action in order to resolve the complaint. SB 1608 also requires that building sites be inspected by certified access specialists.

B. Life and Disability Insurance

AB 2149 and 2150, 2008-2009 (Cal. 2008) (Berg) Annuities and Financial Product Sales. Prohibits an investment advisor or broker-dealer from using specific credentials or designations in such a way as to mislead. AB 2150 adds section 787.1 to the Insurance Code prohibiting, among other things, the use of a "senior designation" or credential, except as specifically approved for use in the sale of an insurance product.

AB 2465, 2008-2009 (Cal. 2008) (Duvall) Life Policy Replacements/Conversions: Disclosures. Extends the exemption from the replacement disclosure statute to those circumstances where an individual is simply converting a term life policy to a whole life policy when it is done within an insurer "group." Unless exempted, the disclosure provides warning of the potential costs of the replacement of a life insurance policy with another such policy from a different insurer.

SB 1168, 2008-2009 (Cal. 2008) (Runner) Medical Coverage. Allows adult students to continue on parents' medical coverage when an illness makes them unable to maintain full-time student status.

AB 1150, 2008-2009 (Cal. 2008) (Lieu) Health Insurance; Rescissions. Prohibits compensation agreements that might encourage health policy rescissions. The bill prevents compensation of a person employed by a health care service plan or insurer from being based in any way on the number of policies or cer-

tificates that the person has recommended be rescinded, cancelled, limited, or based on the resulting savings to the health care service plan or insurer. This bill is intended to address perceived causes of rescissions by health plans or insurers and is related to regulatory actions by the Department of Managed Health Care and the Department of Insurance.

2. CASE DECISIONS

A. California Supreme Court

In 2008, the California Supreme Court published opinions in the following two cases that are of interest to attorneys practicing insurance law, especially those attorneys who arbitrate insurance claims:

1. *Cable Connection, Inc. v. DIRECTV, Inc.*, 44 Cal. 4th 1334, 190 P.3d 586, 82 Cal. Rptr. 3d 229 (2008). Under the California Arbitration Act ("CAA"), parties may agree to expanded judicial review of an arbitration award for legal error where the arbitration agreement expressly requires the arbitrator to act in conformity with the law and provides that the arbitration award is reviewable for legal error.

In *Cable Connection*, DIRECTV's sales agency agreement with retail dealers contained an arbitration provision that provided for review by the courts. DIRECTV successfully moved for arbitration. A majority of the three-member arbitration panel concluded that class-wide arbitration was authorized under the arbitration agreement even though the agreement was silent about class arbitrations. The trial court vacated the award, concluding the panel erred as a matter of law. The court of appeal reversed, concluding the trial court erred by reviewing the merits of the arbitrators' decision in the first instance.

The California Supreme Court reversed again in an opinion filed August 25, 2008. The Supreme Court concluded that, under the CAA, the parties to an arbitration agreement may agree to judicial review of arbitration awards for legal error. In reaching this conclusion, the California Supreme Court departed from the United States Supreme Court, which, in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 128 S. Ct. 1396, 1404-1405 (2008), held that the Federal Arbitration Act ("FAA") does not permit the parties to agree to expanded judicial review. This seemingly inconsistent result is possible because (a) the U.S. Supreme Court indicated that that expanded review might be available under state law, and (b) the California Supreme Court concluded that the FAA is not preemptive and therefore does not require state law to conform to federal law with respect to judicial review of arbitration awards.

Continued on Page 44

See also the discussion of the *Cable Connection* case in this issue's articles by the Franchise Law standing committee and Paul J. Dubow's update on ADR cases.

2. *Bouton v. USAA Casualty Insurance Co.*, 43 Cal. 4th 1190, 186 P.3d 1, 78 Cal. Rptr. 3d 519 (2008). Insurance Code section 11580.2, subdivision (f), requires an insurer and insured to arbitrate disputes regarding the underinsured motorist's liability and the insured's damages, including the binding effect on the insurer of the insured's default judgment against the uninsured motorist, but it does not require arbitration of the claimant's status as an insured.

On June 9, 2008, the California Supreme Court filed a single opinion deciding two cases: *Bouton v. USAA Casualty Insurance Co.*, S149847 (Cal. 2008), and *Hanesian v. State Farm Mutual Automobile Insurance Co.*, S149851 (Cal. 2008). In these consolidated cases, the Supreme Court explained and applied Insurance Code section 11580.2, subdivision (f), which requires that, absent an agreement between insurer and insured, they must arbitrate the underinsured motorist's liability and the insured's damages.

The Supreme Court's two main holdings were: (a) whether a person claiming underinsured motorist policy benefits is an insured under the policy is a coverage question outside the scope of the statutory arbitration mandate and thus must be decided by the court, not by an arbitrator (this holding overruled the Supreme Court's contrary decision in *Van Tassel v. Super. Ct.*, 12 Cal. 3d 624 (1974)); and (b) whether the insured's default judgment against the underinsured motorist binds the underinsured motorist insurer is a question that falls within the scope of the statutory arbitration mandate and thus must be decided by an arbitrator, not by the court.

There are seven more insurance cases pending in the California Supreme Court: *State v. Underwriters at Lloyd's London*, S149988 (Cal.); *Ameron Intern. Corp. v. Insurance Co. of State of Pa.*, S153852 (Cal.); *21st Century Ins. Co. v. Super. Ct. (Quintana)*, S154790 (Cal.); *Delgado v. Interinsurance Exchange of Auto Club of Southern California*, S155129 (Cal.); *Fairbanks v. Super. Ct. (Farmers New World Life Ins.)*, S157001 (Cal.); *Village Northridge Homeowners Ass'n v. State Farm Fire and Casualty Co.*, S161008 (Cal.); and *Sentry Select Ins. Co. v. Fidelity & Guaranty Ins. Co.*, S145087 (Cal.). Two more insurance cases, *Allstate Ins. Co. v. Super. Ct. (Delanzo)*, S154815 (Cal.) and *Jafari v. EMI Ins. Companies*, S157924 (Cal.), are being held by the Supreme Court pending its decision in related lead cases.

At least the following two Supreme Court insurance cases are scheduled for decision in 2009:

State v. Underwriters at Lloyd's London, review granted April 18, 2007 (S149988). This case includes the following issues: (1) Does application of the pollution exclusion clause of the comprehensive general liability excess insurance policies at issue in this case turn on: a) when waste material was discharged from the Stringfellow Acid Pits waste disposal site; or b) when the waste was initially deposited into the site? (2) If pollution is caused by both uncovered intentional actions and covered accidents, does the insured have the burden at trial to prove that all of the damages it seeks to recover were caused by a covered event, or is there a duty to indemnify when two concurrent causes are responsible for an injury even if one of the causes is an uncovered act?

Sentry Select Ins. Co. v. Fidelity & Guaranty Ins. Co., request for certification granted August 23, 2006 (S145087). This case presents the following issue: What is the appropriate test for determining whether an insured is 'engaged in the business of renting or leasing motor vehicles without operators' under California Insurance Code section 11580.9(b)?

B. California Courts of Appeal

The California courts of appeal published numerous insurance decisions in 2008. Among the most significant court of appeal insurance decisions are the following:

Troyk v. Farmers Group, Inc., 168 Cal. App. 4th 1337 (2008) (service charge assessed for the payment in full of the stated insurance premium is itself a premium that must be stated in the policy under Insurance Code section 381).

Hill v. State Farm Mutual Auto. Ins. Co., 166 Cal. App. 4th 1438 (2008) (insurer's decision to maintain high reserves rather than pay billions of dollars in dividends to policyholders is protected by the business judgment rule).

Devonwood Condominium Owners Ass'n v. Farmers Ins. Exchange, 162 Cal. App. 4th 1498 (2008) (judgment confirming binding appraisal of amount of loss cannot be a money judgment against insurer where the appraisal award did not resolve coverage issues).

Everett v. State Farm General Ins. Co., 162 Cal. App. 4th 649 (2008) (insurer is not responsible for inadequate homeowners policy coverage limits where it provided the insured with adequate notice that it was discontinuing guaranteed replacement cost coverage and that it was the insured's responsibility to accurately assess the amount of coverage needed).

Qualcomm, Inc. v. Certain Underwriters at Lloyd's, London, 161 Cal. App. 4th 184, 73 Cal. Rptr. 3d 770 (2008) (insured who

settles a coverage dispute with its primary insurer for less than the limits of its primary policy and releases its primary insurer is not entitled to indemnification from its excess insurer for the unreimbursed litigation defense expenses and settlement costs in excess of the amount paid by the primary insurer).

Fogel v. Farmers Group, Inc., 160 Cal. App. 4th 1403, 74 Cal. Rptr. 3d 61 (2008) (Subscribers of reciprocal insurance exchanges may sue the exchanges' attorneys-in-fact to recover allegedly excessive fees under a breach of fiduciary duty theory).

De Bruyn v. Super. Ct. (Farmers Group, Inc.), 158 Cal. App. 4th 1213, 70 Cal. Rptr. 3d 652 (2008) ("absolute" mold exclusion bars coverage for mold losses regardless of Insurance Code section 530 and the efficient proximate cause doctrine).

2. INSURANCE REGULATION

As the business of insurance is regulated by the states, the actions and initiatives of the California Insurance Commissioner and the Department of Insurance have a significant impact on the practice of California insurance law. Insurance Commissioner Steve Poizner was inaugurated on January 8, 2007, succeeding John Garamendi. In 2008, Commissioner Poizner took action in a number of areas, including catastrophe response and mitigation, increased use of electronic records within the California Department of Insurance (CDI), and investigation and enforcement of insurance fraud and disciplinary actions. Also in 2008, the CDI's Financial Analysis Division was focused on the ramifications of the worldwide financial crisis on insurance institutions. Below are several of the regulatory actions and developments of interest in the past year:

Health Care Settlements. In the area of health care, the CDI is responsible for regulating provider-preferred organization (PPO) health products issued by insurance companies, and the Department of Managed Health Care (DMHC) is responsible for health maintenance organizations (HMOs). In 2008 and into early 2009, the two regulatory bodies investigated and obtained settlements involving major PPOs and HMOs regarding allegations of improper rescissions of coverage, as well as other aspects of improper claims handling practices. Significant administrative actions and settlements in 2008 involved PacifiCare Companies and HealthNet, followed by Blue Shield in January 2009.

Annuity Sales. The practices of insurers and agents in connection with the sales of annuity policies to senior citizens continues to be a significant regulatory focus. Common allegations include misrepresentations of annuity benefits and restrictions, as well as sales to seniors with diminished mental capacity. In 2008, the Commissioner announced a significant administrative settlement

with Allianz Insurance Company of North America regarding alleged improper annuity sales, and he also announced a number of enforcement actions against individual life insurance agents.

Automobile Insurance Rates. In August 2008, the CDI completed the implementation of 2006 revisions to the "Territorial" Rating Factor regulations. Cal. Code Regs., tit. 10, § 2632.5. This amendment reduced the weight that insurers may assign to the insured's geographical location in calculating rates for automobile insurance, thereby placing more emphasis on driving record, driving experience, and annual miles driven.

Insurance Rates. The continuing "soft" market combined with the CDI's prior approval authority over property and casualty insurance rates contributed to a number of significant insurance rate reductions in 2008. These included rate reductions in homeowners insurance by Allstate, as well as several other decreases in automobile insurance, medical malpractice, and other lines of business. The Workers Compensation Insurance rating Bureau and the Insurance Commissioner recommended modest increases.

The Insurance Law Standing Committee welcomes questions and comments regarding these and other insurance law topics. ■

Continued from page 16 . . . Update on California LLCs and Limited Partnerships

void." There are exceptions for sale or dissolution of corporations (section 16601); partnerships (section 16602); and limited liability companies (section 16602.5).

The court held that Andersen's non-competition agreement was unenforceable because it restrained his ability to practice his profession. The court rejected Andersen's contention that it should adopt a narrow-restraint exception to Business and Professions Code section 16600 discussed in *Campbell v. Trustees of Leland Stanford Jr. Univ.*, 817 F.2d 499 (9th Cir. 1987). The court concluded that non-competition agreements are invalid unless they fall within the statutory exceptions of sections 16601, 16602, and 16602.5.

Indemnification Obligations

In *Focal Point, LLC v. CNA Insurance Company, Inc. and Continental Casualty Company*, 2008 LEXIS 53952 (N.D. Cal. 2008), four members of Focal Point LLC voted to expel Brian Ward as a member. Two days later, Ward disputed his expulsion claiming that the other members had breached their fiduciary duty