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## Review of Selected 1998 California Legislation Addendum - Insurance

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# Insurance

## Insurance; Proposition 103—rates, regulation, commissioner

Insurance Code §§ 750, 750.1, 751, 752, 753, 754, 755, 755.2, 755.5, 755.6, 755.7, 756, 757, 758, 759, 760, 760.5, 761, 763, 763.5, 764, 765, 766, 767, 1643, 1850, 1850.1, 1850.2, 1850.3, 1852, 1853, 1853.6, 1853.7, 1854, 1854.1, 1854.2, 1854.25, 1854.3, 1854.4, 1854.5, 1857.5 (repealed), 1861.01, 1861.02, 1861.03, 1861.04, 1861.05, 1861.06, 1861.07, 1861.08, 1861.09, 1861.10, 1861.11, 1861.12, 1861.13, 1861.14, 12900, 12979 (new); Revenue and Taxation Code § 12202.1 (new).

1988 CAL. STAT. PROP. 103

(Effective November 9, 1988)\*

Proposition 103's purpose is "to protect consumers from arbitrary insurance rates and practices," to encourage competition, "to provide for an accountable Insurance Commissioner" (Commissioner), "and to ensure that insurance is fair, available, and affordable for all Californians".<sup>1</sup>

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\* Insurance Code sections 1861.01(c) and 1861.02 are effective November 8, 1989. CAL. INS. CODE §§ 1861.01 (c), 1861.02(d). All other provisions of Proposition 103 were to be effective November 8, 1988; however, the California Supreme Court enjoined enforcement of the statute pending review until December 7, 1988 at which point they lifted the injunction on all of the provisions except for the rate rollback in Insurance Code section 1861.01. *California Insurance Co. v. Deukmejian*, 88 Daily Journal D.A.R. 15354 (Ca. 1989).

1. 1988 Cal. Stat. prop. 103, sec. 2, at \_\_\_\_\_. Proposition 103 finds that insurance reform is necessary because insurance is unaffordable and unavailable to millions of Californians due to enormous increases in insurance costs and existing laws failed to protect consumers adequately and allowed insurance companies to charge excessive, unjustified, and arbitrary rates. *See id.* State regulation of business is constitutional providing there is a rational relationship between the regulation and the legitimate state interest. *See Williamson v. Lee Optical of Oklahoma*, 348 U.S. 483, 491 (1955) (Court upheld state statute requiring ophthalmologist prescription for any fitting or duplicating of lenses by an optometrist as long as there was a rational relationship between the means and the goal of the statute). *See generally* Note, *Constitutional Constraints on Initiative & Referendum*, 32 VAND. L. REV. 1143 (1979) (arguing for heightened standard of due process and equal protection scrutiny when reviewing popular initiative).

Proposition 103 requires all insurers to roll back rates to 20% below November 8, 1987 rates, and to use the rolled back rates when issuing or renewing policies effective on or after November 8, 1988.<sup>2</sup>

For the period preceding November 8, 1989, an insurer may increase rates only if the Commissioner determines, after a hearing, that the insurer is faced with a substantial threat of insolvency.<sup>3</sup> After November 8, 1989, insurers do not need to demonstrate a substantial threat of insolvency but they must still obtain the Commissioner's approval before implementing rate increases.<sup>4</sup> The Commissioner must notify the public of a rate change application and hold a hearing on timely request by a consumer or consumer representative if the requested rate increase exceeds 7% on policies for personal coverage or 15% on policies for commercial coverage.<sup>5</sup> If

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2. CAL. INS. CODE § 1861.01(a). Proposition 103 applies to all insurance except reinsurance, life, ocean marine, title, disability, workers compensation, mortgage, and insurance transacted by county mutual fire insurers. *Id.* § 1861.13. All new insurance issued on or after November 8, 1988 must be priced at 20% less than what comparable risks were priced on November 8, 1987. *Id.* § 1861.01(d). In addition, separate affiliates of the insurers must also comply with the rate reduction. *Id.* § 1861.01(e).

3. *Id.* § 1861.01(b). *Cf.* *Fisher v. City of Berkeley*, 37 Cal. 3d 644, 684, 693 P.2d 261, 269, 209 Cal. Rptr. 682, 690 (1984) (upholding rent control ordinance as facially constitutional under the federal and state due process clauses when the landlord was guaranteed a fair return on investment and adjustment procedures provided prompt access for approval of rent increases), *aff'd*, 475 U.S. 260 (1986), *reh'g denied*, 475 U.S. 1150 (1986). *But see* *Birkenfeld v. City of Berkeley*, 17 Cal. 3d 129, 550 P.2d 1001, 130 Cal. Rptr. 465 (1976) (invalidating rent rollback initiative when procedures for adjustment inherently and unnecessarily precluded prompt action).

4. CAL. INS. CODE § 1861.01(c). The burden of justifying a rate increase is on the applicant. *Id.* § 1861.05(b). The Commissioner must consider investment income but not the degree of competition in determining if the rates are excessive, inadequate, unfairly discriminatory, or otherwise in violation of Proposition 103. *Id.* § 1861.05(a). Prior law defined excessive, inadequate, and unfairly discriminatory, but Proposition 103 omits any definition. *See* 1947 Cal. Stat. ch. 805, sec. 1, at 1897 (enacting CAL. INS. CODE § 1852(a)). The Board of Equalization must adjust the gross premium tax rate assessed against insurers in order to offset any reduction in income which would result to the State from the rate decreases. CAL. REV. & TAX. CODE § 12202.1 (this provision will be in effect until January 1, 1991).

5. CAL. INS. CODE § 1861.05(c). If the rate increase requested does not exceed 7% for personal lines, or 15% for commercial lines, the Commissioner may determine not to hold a hearing and must issue written findings in support of that decision. Applications for rate increases which do not require a hearing are deemed approved 60 days after public notice. *Id.* Public notices of pending rate increase applications will be given to the media and to individuals who request placement on a mailing list. *Id.* § 1861.06. Furthermore, all records must be available for public inspection. *Id.* § 1861.07. Hearing procedures are outlined in Government Code sections 11500-11528 with the following exceptions: (1) an administrative law judge may be appointed by the Commissioner; (2) hearings are triggered by Commissioner request; (3) a decision by Commissioner to adopt, amend, or reject the findings must be based solely on the record; (4) ex parte communication with any party or interested person is prohibited, including communication by and with the Commissioner; and (5) discovery will be liberally construed and disputes determined by an administrative law judge. *Id.* Finally, judicial review of the hearing will be in accordance with Insurance Code section 1858.6. In determining the appropriateness of judicial review, the Commissioner's decision to hold a hearing is not a final order, but a decision not to hold a hearing is a final order. *Id.*

the Commissioner finds that insurers substantially withdraw from any covered insurance market, and that a market assistance plan would not be sufficient to make insurance available,<sup>6</sup> the Commissioner may establish a joint underwriting association<sup>7</sup> without first creating a market assistance plan.<sup>8</sup>

For auto insurance plans, insurers must rate the insured's risk by using the following rating factors applied in decreasing order of importance: (1) The insured's driving safety record; (2) the number of miles driven annually; (3) the number of years of driving experience the insured has had; and (4) other factors approved by the Commissioner that have a substantial relationship to the risk of loss.<sup>9</sup> Auto insurers must also provide a 20% good driver discount to drivers who have been licensed for at least three years and who have had no more than one moving violation.<sup>10</sup>

Proposition 103 also requires the Commissioner to provide consumers with a rate comparison for each personal line of insurance for every insurer.<sup>11</sup> In addition, consumers may participate in the rate-setting process.<sup>12</sup> First, any individual may initiate or intervene in any proceeding, challenge any action of the Commissioner, and enforce any provision of Proposition 103.<sup>13</sup> Second, Proposition 103 provides for payment of advocacy and witness fees to a qualified advocate representing the interest of consumers.<sup>14</sup> Finally, insurers must notify policyholders in every policy or renewal premium bill of the opportunity to join a non-profit corporation which will advocate the interests of insurance consumers.<sup>15</sup>

6. Not readily available means a significant decrease in the number of insurers or a total withdrawal of insurers from a market. *See id.* § 11891.

7. *See id.* § 11891 (authority for establishing joint underwriting association).

8. *Id.* § 1861.11. All insurers authorized and engaged in writing liability insurance on a direct basis in the state must be members of an association to provide a market on a self supporting basis. *Id.* § 11891. Section 11891 does not apply, however, to insurers who write coverages under Insurance Code sections 660 and 675 which are automobile and personal residential and property coverages that do not carry a commercial liability rider. *Id.*

9. *Id.* § 1861.02(a). The Commissioner's regulations will set forth the weight to be given each factor. Furthermore, the use of criterion without prior approval constitute unfair discrimination. *Id.*

10. *Id.* § 1861.02(b). The absence of prior automobile insurance does not preclude eligibility for insurance or the good driver discount. *Id.* § 1861.02(c).

11. *Id.* § 1861.04.

12. *Id.* § 1861.10.

13. *Id.* § 1861.10(a).

14. *Id.* § 1861.10(b). The advocate must have made a substantial contribution to the adoption of any order, regulation or decision by the Commissioner or a court. *Id.* If the advocacy is in response to a rate application, the applicant must pay the advocate's expenses. *Id.*

15. *Id.* § 1861.10(c) (the Commissioner will determine the wording of the notification and

Prior law prohibited property or casualty insurance activity by banks,<sup>16</sup> rebating of insurance premiums,<sup>17</sup> and exempted the insurance business from antitrust regulation.<sup>18</sup> Proposition 103 removes these prohibitions and subjects the insurance business to state antitrust regulation.<sup>19</sup> Proposition 103, however, allows insurers to continue sharing historical data and participating in joint underwriting associations.<sup>20</sup> Furthermore, Proposition 103 restricts an insurer's right to cancel or not renew any insurance policy for any reason except for non-payment of premium, fraud, or a substantial increase in the risk.<sup>21</sup>

Prior law also required the Governor to appoint the Commissioner.<sup>22</sup> Proposition 103 calls for the general election of the Commissioner every four years contemporaneously with the Governor.<sup>23</sup>

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the necessary procedures to implement this provision). The non-profit corporation will be established by an interim board of public members designated by the Commissioner and will be operated by democratically elected members. The corporation must reimburse insurers for increased costs attributable to the mailing of the notification. *Id.*

16. 1984 Cal. stat. ch. 922, sec. 1, at 3088-89 (amending CAL. INS. CODE § 1643) (banks were prohibited from selling insurance). Proposition 103 does not address other provisions of current law restricting insurance activity by banks. See CAL. FIN. CODE §§ 772(b) (prohibiting state banks from acting as insurance company, agent, or broker), 1208 (restricting state banks ability to sell insurance). The state banking department has interpreted Proposition 103 as impliedly repealing Financial Code sections 772(b) and 1208. See State Banking Department, *Interpretive Opinion - Proposition 103, Financial Code Sections 772(b) and 1208*, Jan. 4, 1989 (on file at the *Pacific Law Journal*).

17. 1935 Cal. Stat. ch. 145, sec. 750 at 515-16 (enacting CAL. INS. CODE § 750-767) (rebates were prohibited).

18. 1947 Cal. Stat. ch. 805, sec. 1, at 1898 (enacting CAL. INS. CODE § 1853-1857.5) (companies were permitted to act in concert for the purposes of joint underwriting, joint reinsurance, sharing of experience, forms, and underwriting rules).

19. CAL. INS. CODE § 1861.03(a). See CAL. BUS. & PROF. CODE §§ 16700-16770 (restraint of trade).

20. CAL. INS. CODE § 1861.03(b).

21. CAL. INS. CODE § 1861.03(c). This restriction on insurers may unconstitutionally impair a contractual obligation. See U.S. CONST. art. I, § 10 (no state shall impair the obligation of contracts); CAL. CONST. art. I, § 9 (a law impairing obligation of contracts may not be passed); *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 244-251 (1978) (state statute imposing retroactive vesting requirements on employee pension plan violates the contract clause when the employer's plan gave the employer an unqualified right to terminate and provided no rights to the employee until length of service and age conditions were met). *But see* *Energy Reserve Group, Inc. v. Kansas Power and Light*, 459 U.S. 400, 410-419 (1983) (state statute subjecting seller of natural gas to retroactive price ceiling did not substantially impair contractual rights and therefore did not violate the contract clause of the federal constitution).

22. See 1975 Cal. Stat. ch. 678, sec. 51, at 1489 (amending CAL. INS. CODE § 12900).

23. *Id.* § 12900. This provision may violate the single subject rule. See CAL. CONST., art. II, § 8(d) (an initiative measure embracing more than one subject may not be submitted to the electorate or have any effect). See generally Eastman, *Squelching Vox Populi: Judicial Review of the Initiative in California*, 25 SANTA CLARA L. REV. 529 (1985) (discussion of preelection and postelection judicial review or initiative procedures); Comment, *The California Initiative Process: The Demise of the Single Subject Rule*, 14 PAC. L.J. 1095 (1983) (argument for stricter interpretation of single subject rule based on purpose and history of the clause).

Violators are subject to penalties set forth in the Insurance Code as well as suspension or revocation of their certificate of authority.<sup>24</sup> Additionally, the legislature may not amend proposition 103 except by a two-thirds roll call vote to further the purpose of the chapter.<sup>25</sup> Finally, any provisions or applications of the act that are held invalid will be severed from the act.<sup>26</sup>

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24. *Id.* § 1861.14. The maximum penalty for a negligent violation is \$50,000; the maximum penalty for a willful violation is \$250,000. *Id.* § 1859.1. A willful violator is guilty of a misdemeanor.

25. 1988 Cal. stat. prop. 103, sec. 8, at \_\_\_\_.

26. *Id.*

