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Recent Ninth Circuit Rulings Uphold Plaintiffs' Efforts to Predicate Claims on Alleged Insurance Code Violations — Likely More to Come

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Recent rulings suggest insurers face increased risk of suits predicating breach of contract and state unfair trade practices claims on alleged violation of state insurance laws, notwithstanding the lack of an express private right of action. In no jurisdiction is this more a concern than California, as illustrated by two recent Ninth Circuit opinions involving claims under California's Unfair Competition Law (UCL). Most recently, in May, the Ninth Circuit reversed a California federal district court's dismissal of putative class action UCL claims in *Friedman v. AARP, Inc.*, an action by a Medicare beneficiary and purchaser of UnitedHealth supplemental health insurance coverage bought through a group Medigap policy, for which AARP was the policyholder. The suit names as defendants multiple affiliated AARP and UnitedHealth entities but, for ease of reference, those sets of defendants are referred to collectively as "AARP" and "UnitedHealth." The plaintiff alleges that, by soliciting insurance and accepting a commission, AARP unlawfully transacted insurance business without a license in violation of California Insurance Code § 1631, which prohibits persons subject to the Code from "solicit[ing], negotiat[ing], or effect[ing] contracts of insurance" without "a valid license from the commissioner." At the heart of the dispute is AARP's and UnitedHealth's Medigap arrangement, which the Ninth Circuit describes as governed by a joint agreement requiring, *inter alia*, that purchases of UnitedHealth's Medigap coverage be made through AARP's group policy, and that AARP manage certain program elements, including a requirement that AARP solicit its members' participation in the Medigap plan. In connection with the same, AARP is allowed to collect insurance premiums from members and, after first investing the collected payments and deducting and retaining 4.95 percent of each dollar paid by the enrollees, forwarding the appropriate payment to

UnitedHealth. While AARP argued the 4.95 percent retention is a permissible "royalty," the plaintiff contends it is an undisclosed commission on the sale of insurance, resulting in the payment by insureds of "an artificially inflated insurance price." For the Ninth Circuit, the inquiry was straightforward: "At issue therefore is whether Friedman has adequately pled that AARP has engaged in any of those … activities [listed in § 1631]. … We conclude that he has." Along the way, the court rejected AARP's effort to rely on the method of calculation of the fee it receives — calculated as a percentage of all premiums paid in connection with the program, regardless of the source — as evidence the fee does not qualify as a "commission." As the court explained, "[r]egardless of the nominal form of the arrangement called for by the AARP-United Agreement, the complaint alleges that AARP receives a 4.95% fee for every member that enrolls in UnitedHealth's Medigap program." Also key to the court's analysis were AARP's marketing materials. The court noted, for example, pieces that "expressly state in bold font: **'This is a solicitation of insurance.'"** Indeed, the Ninth Circuit also found that the plaintiff adequately pled that AARP violated the UCL's other two prongs, the "unfair" and "fraudulent" prongs, which claims are based on allegations of misrepresentation as to the nature of the payments. *Friedman*, though, is not the first action to allow a plaintiff to state a UCL claim based on an alleged violation of § 1631's licensing requirements. It is a reaffirmation of the ability. Two months before issuing *Friedman*, however, in *Walker v. Life Insurance Company of the Southwest*, a certified class action involving the sale of indexed universal life insurance policies, the Ninth Circuit issued a ruling representing an *expansion* of the recognition of a plaintiff's ability to pursue certain California Insurance Code violations via the UCL. In particular, the court reversed a California federal district court's May 2011 dismissal of claims that the defendant insurer violated the UCL's unlawful prong, which had been predicated on the insurer's alleged violation of California's illustration statute, California Insurance Code § 10509.950 et seq. As we previously discussed (*see Expect Focus*, Vol. I, 2017), in *Walker*, which also featured a jury verdict for the insurer on the plaintiff's fraudulent concealment claim and the district court judge's subsequent ruling for the insurer on the plaintiff's remaining UCL claims, the dismissal of the illustration statute-based UCL claim was but one of several elements of the Ninth Circuit's review of the trial court proceedings. Given the potential exposure, however, this aspect of the ruling is worth revisiting. As set forth in the code itself, California's illustration statute was enacted to "ensure that illustrations do not mislead purchasers of life insurance and to make illustrations more understandable by providing illustration formats, prescribing standards to be followed when illustrations are used, and specifying the disclosures that are required in connection with illustrations." According to the plaintiff, *inter alia*, the insurer failed to "specifically disclose and identify the cost of buying and maintaining the policies" and, instead, embedded them in the illustrations so policyholders could not make informed decisions. After noting there is no private right of action under California Insurance Code § 10509.950, the district court ruled that the plaintiff's claims under California's UCL could not be based on the illustration statute because claims under the UCL's "unlawful" prong cannot be based on violations of any statute lacking a private cause of action. In its March 2017 reversal of this aspect of the trial court proceedings, however, the Ninth Circuit found that the lack of a private right of action *was not* in fact dispositive. Instead, citing the California Supreme Court, the federal appellate

court ruled that "private UCL claims are barred only when the underlying statute either actually bars private rights of action or provides a 'safe harbor' that renders the alleged conduct lawful." These circumstances are not present as to the illustration statute. While these rulings might portend the *furtherance* of a trend, the use of state insurance laws as a predicate for claims in civil litigation is far from a new phenomenon. Consider plaintiffs' continued focus on California's senior notice statutes, California Insurance Code §§ 10127.13 and 10127.10, which, collectively, are intended to protect seniors through mandatory language regarding the surrender charge period as well as what are termed "associated penalties." A California federal district court's September 2010 ruling in *Rand v. American National* remains an instructive illustration of a plaintiff's effort to predicate UCL claims on an alleged failure to comply with these statutes, in part because the opinion continues to stand as one of the strictest readings by a court of these provisions. More specifically, the *Rand* court read the senior notice provisions strictly to require disclosure about policy elements the company — and perhaps the regulator — clearly never contemplated to be covered by the statutes, forcing companies to think critically about the real possibility that disclosures that appear consistent with the statutes' requirements may nevertheless fail to satisfy the stricter obligations a court might impose in its interpretation of those provisions. Of course, plaintiffs' efforts in this regard are not limited to suits that assert UCL claims. Plaintiffs also continue to point to alleged violations of insurance code provisions to bolster breach of express and implied contractual requirements. For example, in recent suits, policyholders have brought contract and UCL claims based on alleged noncompliance with California Insurance Code §§ 10113.71 and 10113.72 — enacted in 2013 — which, generally, require that insurers notify insureds of their right to designate a third party to whom notice of a nonpayment of premium or potential policy lapse or termination may be sent, prior to any termination.

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