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June 27, 2001

Honorable Ronald M. George, Chief Justice
and the Associate Justices
California Supreme Court
350 McAllister Street, Room 1295
San Francisco, California 94102

Re: Letter in Support of Petition for Review of Patricia Patrick in *Patricia Patrick v. Unum Life Insurance Company of America et al.*, No. S098602; (Cal. Rules of Court, Rule 14(b))

Dear Chief Justice George and Associate Justices of the Supreme Court:

Attorney General Bill Lockyer respectfully submits this letter pursuant to Rule 14(b) of the California Rules of Court in support of the Petition for Review of Patricia Patrick. The State of California has a vital interest in ensuring that the scope of preemption by the Employee Retirement Income Security Act of 1974 (ERISA) is not extended beyond Congress's intent. In view of the United States Supreme Court's recent decision in *Unum Life Insurance Company of America v. Ward* (1999) 526 U.S. 358 (*Ward*),[1] upholding California's notice-prejudice rule against a claim of ERISA preemption, the Attorney General urges this Court to revisit its prior decision in *Commercial Life Ins. Co. v. Superior Court* (1988) 47 Cal.3d 473 (*Commercial Life*). *Commercial Life* and its progeny[2] conclude that ERISA preempts first party insurer bad faith tort claims. The Attorney General believes the rationale of the majority opinion in that case was faulty and has been undermined by the United States Supreme Court's analysis in *Ward.*

The Issue Presented

The case at bar squarely presents the issue of whether ERISA's judicial remedies provision (29 U.S.C. § 1132 [remedies provision]) trumps ERISA's "saving clause" which

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[1] Attorney General Lockyer joined 40 other state Attorneys General and the Attorney General of Puerto Rico in filing an amicus brief in support of the position against preemption of California's notice-prejudice rule in *Ward.* (See Lexis 1997 U.S. Briefs 1868 (1999).)

[2] *E.g., Marshall v. Bankers Life & Casualty Co.* (1992) 2 Cal.4th 1045, 1051; *Dearth v. Great Republic Ins. Co.* (1992) 9 Cal.App.4th 1256, 1266-1267.)

precludes preemption of state laws regulating insurance (29 U.S.C. § 1144 [saving clause]) with respect to state insurance bad faith tort claims. Here plaintiff Patrick, after having been denied the right to pursue a state law bad faith tort claim against an insurance company, successfully pursued the ERISA cause of action under 29 U.S.C. section 1132. The Court of Appeal's decision quotes the trial court's findings that the conduct of Unum in handling the claim was "unprincipled" and "could only be termed bad faith under state law." (Slip Opn. at 3.) Yet, neither the trial court nor the Court of Appeal believed Patrick could pursue such a state law claim because of ERISA preemption. The Court of Appeal found itself compelled by *stare decisis* to follow this Court's holding in *Commercial Life* and the United States Supreme Court's decision in *Pilot Life Ins. Co. v. Dedeaux* (*Pilot Life*) (1987) 481 U.S. 41 as interpreted by this court in *Commercial Life.* (Slip Opn. at 15.) Thus, Patrick was denied compensation for injuries related to the tortious conduct of Unum and was limited to a recovery of the benefits to which she was entitled under the plan, even had there been no bad faith.

The Public Interest and Significance of the Issue

The result of the application of the majority's holding in *Commercial Life* is that in California all policyholders who suffer bad faith tortious conduct at the hands of their insurers in the processing and settlement of claims may fully recover for their injuries and losses -- except for policyholders covered by an ERISA plan. Those unfortunate claimants, such as plaintiff Patrick in this case, are limited to recovering their entitlements under the policy and their attorney fees--no matter how outrageous or damaging their insurers' conduct may be. This inequitable result is not mandated by the language of ERISA. In fact, a common sense reading of the words of ERISA indicates Congress intended exactly the opposite result. In Patrick's view, and in our view, the United States Supreme Court's holding in *Ward* provides this Court with the means to restore to California members of ERISA plans, the full protection of California law regulating insurance companies' bad faith conduct.

The Important Question of Law.

ERISA provides in 29 U.S.C. section 1144(a) that except as provided by section 1144(b), ERISA supersedes all state laws insofar as they may relate to any employee benefit plan. Section 1144(b) contains the saving clause which provides that "except as provided in subparagraph (B) [[3]], *nothing in this subchapter* shall be construed to exempt or relieve any person from any law of any State which regulates insurance. (29 U.S.C. § 1144(b)(2)(A); emphasis added.) This language makes clear that an "ERISA plan is . . . bound by state insurance regulations *insofar as they apply to the plan's insurer.*" (*FMC Corp. v. Holliday* (1990) 498 U.S. 52, 61 [Emphasis added].)

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[3] Subparagraph B, 29 U.S.C. section 1144(b)(2)(B), provides that an employee benefit plan governed by ERISA shall not be deemed an insurance company, an insurer, or engaged in the business of insurance for the purposes of any state law purporting to regulate insurance companies or insurance contracts. It has no applicability to the issue in this case.

Under ERISA, state decisional law, as well as statutory law regulating insurance, is deemed state law regulating insurance for purposes of the saving clause. (29 U.S.C. §1144(c)(1); *Ward* at 867, n. 1.) In California, the tort of bad faith conduct toward an insured by an insurer in settling a claim is well-established as a cause of action by an insured against his or her insurer. (*Kransco v. Empire Surplus Lines Ins. Co.* (2000) 23 Cal.4th 390, 400.)

Included in the subchapter with section 1144(a)'s saving clause is 29 U.S.C. § 1132 which provides for civil remedies under ERISA. In *Pilot Life* the United States Supreme Court considered the question of whether a Mississippi common law action in contract and tort for bad faith was preempted by ERISA. Noting that the cause of action *was not limited to insurance bad faith claims*, the United States Supreme Court found that the state law did not regulate insurance within the meaning of ERISA's saving clause and therefore was preempted. (*Id.* at 50-51.) The Court went further to opine that the civil remedies under ERISA were exclusive and thus any state common law bad faith tort or contractual remedy would be preempted under the remedies provision of ERISA which constituted an exclusive civil enforcement scheme. (*Id.* at 56-57.)

This Court in *Commercial Life*[4], found that the remedies provision of ERISA precluded any civil actions against ERISA insurers arising from the handling of ERISA claims. (*Commercial Life* at 484.) This Court further found that ERISA's "saving clause" for insurance regulations, while permitting the states to regulate the *substantive* provisions of insurance policies, did not permit the state to provide conflicting *procedural* remedies. (*Id.*) The Court relied on the holding in *Pilot Life* as being "directly on point regarding the exclusivity issue, and its conclusion inescapable." (*Id.*)

Justice Mosk in his dissent in *Commercial Life,* in which Justice Broussard joined, strongly disagreed with the majority's conclusion. He stated that there could be no serious dispute that the statute in question, Insurance Code section 790.03, regulated insurance and thus fell within the "saving clause" of ERISA. He concluded that ERISA does not purport to regulate the civil enforcement scheme *imposed by California law* on insurers for bad faith breach of duties to the insured. (*Id.* at 489.)

In decisions pre-dating the United States Supreme Court's decision in *Ward*, the federal circuit courts of appeal have split in their interpretation of *Pilot Life* as applied to state laws

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[4] *Commercial Life* involved a claim that a first party claimant's civil action under the Unfair Trade Practices Act, specifically, Insurance Code section 790.03(h) was not preempted by ERISA. The plaintiff conceded that *Pilot Life* precluded a non-statutory claim. Civil actions under section 790.03(h) were previously ruled to not exist under state law by the Court in *Moradi-Shalal v. Fireman's Fund Ins. Co.* (1988) 46 Cal.3d 287. *Commercial Life* addressed only those claims that remained by virtue of the prospective effect of this Court's holding in *Moradi-Shalal. (Commercial Life* at 484-485.)

regulating insurance. The Ninth Circuit has interpreted the case in a similar fashion as the majority in *Commercial Life.* (See *Kanne v. Connecticut General Life Ins. Co.* (9th Cir. 1988) 867 F.2d 489, cert. den. (1989) 492 U.S. 906; see also, *Ramirez v. Intercontinental Hotels* (5th Cir. 1989) 890 F.2d 760, 763-64; *In re Life Ins. Co. N. Am.* (8th Cir. 1988) 857 F.2d 1190, 1194.) The Second Circuit Court of Appeals in *Franklin H. Williams Ins. Trust v. Travelers Ins. Co.* (2nd Cir. 1995) 50 F.3d 144, 151, upheld a New York law against a claim of ERISA preemption noting that it would make no sense to interpret ERISA's saving clause to preclude preemption of a state law, but then to preclude its enforcement under the enforcement provision.

In *Ward*, the United States Supreme Court rejected Unum Life Insurance Company's assertion that California's judicially-established notice-prejudice rule was preempted by ERISA. The court found that the rule was a state law regulating insurance and was thus saved from preemption under ERISA's saving clause. The court also rejected Unum's argument that the law was preempted by ERISA's remedies provision. The court found the provision was not implicated since Ward only sought relief under ERISA. In so holding however, the court declined to affirm the precedential effect of the language in *Pilot Life* which appears to hold that the remedies provision preempts even state law that is saved from preemption by the saving clause. Instead, the court described the holding in *Pilot Life* as concerning "Mississippi common law creating a cause of action for bad-faith breach of contract, law not specifically directed to insurance industry and *therefore* not saved from ERISA preemption." *(Ward* at 376, n. 7; emphasis added.) With respect to the second "ground" in *Pilot Life,* the court in *Ward* noted that it was merely agreeing with a position of the Solicitor General, which has now changed, and that the issue of the applicability of the remedies provision did not need to be addressed in that case. (Id.)

The court in *Ward* recognized that state's varying insurance regulations created "disuniformities" for national plans such as ERISA, but that such "disuniformities" were the inevitable result of the congressional decision to save local insurance regulation. (*Ward* at 376, n. 6.) It is also apparent the court in *Ward* recognized that the *Pilot Life* case did not deal with a state law that was saved by preemption by the saving clause and the discussion of the clause was in the context of an otherwise preempted state law.

As the Court of Appeal in this case noted, federal court cases subsequent to the decision in *Ward* have split on the question of whether *Ward* in effect limited the holding in *Pilot Life* to its facts – a state law that was not directed specifically and solely to insurance. (Slip Opn. at 15.)

The Reason for Reconsidering *Commercial Life.*

Obviously, regardless of the significance of the issue and the merit of the petitioner's argument, this Court is faced with the question of whether it can and should reconsider *Commercial Life* in the absence of a decision by the United States Supreme Court expressly overruling *Pilot Life* to the extent it suggests ERISA's remedies provision trumps its saving clause. The Attorney General submits this Court can and should reconsider *Commercial Life.*

We recognize that the decisions of the United States Supreme Court are binding on this Court and even dicta in such decisions should be considered as controlling absent unusual circumstances. However, as to the holding in *Pilot Life*, a number of lower courts have construed the discussion of the remedies provision as being limited to state laws not squarely falling within the saving clause. The Second Circuit Court of Appeal squarely rejected extending the exclusive remedy discussion in *Pilot Life* to preempt a New York law regulating insurance. (*Franklin H. Williams Ins. Trust v. Travelers Ins. Co., supra,* 50 F.3d 144, 151.) Two justices of this Court, in dissenting in *Commercial Life,* implicitly found *Pilot Life* did not apply to state laws falling within the saving clause. Now, a unanimous decision of the United States Supreme Court suggests that the *Pilot Life* case is limited to its facts. (*Ward* at 376, fn. 7.) Finally, in *Commercial Life* this Court itself stated that *"Pilot Life* provide[d] helpful *guidance*, but the [U.S.] Supreme Court has not addressed the precise issued posed here." (*Commercial Life* at 481 [emphasis added].) The United States Supreme Court likewise has not addressed the issue presented in this case. Accordingly, we submit that this Court can take another look at the "guidance" provided by *Pilot Life* in view of the more recent decision in *Ward* and reassess its holding in *Commercial Life.*

Since this Court *can* reconsider its holding in *Commercial Life*, it *should* do so. From a legal standpoint, the conclusion that the remedies provision trumps the saving clause makes no sense in view of the language of the statute. In the McCarran-Ferguson Act, Congress expressly mandated that state laws regulating the business of insurance are in the public interest (15 U.S.C. § 1011), and that "[n]o Act of Congress *shall be construed* to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance" (15 U.S.C. § 1012). (Emphasis added.) As noted above, ERISA's saving clause, with one exception not applicable here, provides "nothing in this subchapter *shall be construed* to exempt or relieve any person from any law of any State which regulates insurance. (29 U.S.C. § 1144(b)(2)(A); emphasis added.) Since, not one, but two federal laws unequivocally bar construing the provisions of the subchapter of ERISA containing the remedies provision as preempting state law regulating insurance, it is illogical to conclude that the remedies provision trumps the saving clause. This is no doubt one reason why the Solicitor General in *Ward* maintained that *Pilot Life* should not be construed to apply to insurance specific state law remedies and that the "savings clause, on its face, saves state law conferring causes of action or affecting remedies that regulate insurance, just as it does mandated-benefits laws." (*Ward* at 376, fn. 7 [quoting from Solicitor General's brief].)

The Court should reconsider *Commercial Life* for public policy reasons as well. Determination of whether an insurer should escape, or be subject to, civil liability for tortious conduct in the handling of a policyholder's claim should not depend upon whether the insurance policy is pursuant to an ERISA plan. That the policy is covered by ERISA makes the insurer's conduct no less reprehensible and the injuries and losses to the insured no less significant. The social policy of safeguarding an insured articulated by the Court in *Kransco v. American Empire Surplus Lines Ins. Co., supra,* 23 Cal.4th 390, 400, applies equally to insureds under an ERISA plan as to other insured.

Justice Mosk in his dissent in *Commercial Life* warned of the "growing and ominous trend toward federal preemption of issues that belong within the sphere of control by the individual states." (*Id.* at 490.) It would be unfortunate if the social policy of safeguarding insureds promoted by California's law of bad faith insurance torts, were preempted by ERISA by means of Congressional fiat or United States Supreme Court precedent. We submit there is neither such fiat nor such precedent. What defeats this social policy in the realm of ERISA is this Court's decision in *Commercial Life*. This Court has the authority and, we submit, the duty overrule that decision.

For these reasons, the Attorney General urges this Court to grant the petition for review.

Respectfully submitted,

PAUL H. DOBSON
Deputy Attorney General

For BILL LOCKYER
Attorney General

DECLARATION OF SERVICE
(AG Mailroom)

Case Name: **Patricia Patrick v. Unum Life Insurance Company of America; No.: S098602**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar at which member's direction this service is made. I am 18 years of age or older and not a party to this matter. I am familiar with the business practice at the Office of the Attorney General for collection and processing of correspondence for mailing with the United States Postal Service. In accordance with that practice, correspondence placed in the internal mail collection system at the Office of the Attorney General is deposited with the United States Postal Service that same day in the ordinary course of business.

On June 27, 2001, I served the attached **Letter in Support of Petition for Review of Patricia Patrick** by placing a true copy thereof enclosed in a sealed envelope with postage thereon fully prepaid, in the internal mail collection system at the Office of the Attorney General at 1300 I Street, P.O. Box 944255, Sacramento, CA 94244-2550, addressed as follows:

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I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on June 27, 2001, at Sacramento, California.

Catherine F. Cordova

Typed Name

Catherine F. Cordova

Signature

Court of Appeal, First Appellate District, Division Four - No. A088190
S098602

IN THE SUPREME COURT OF CALIFORNIA

En Banc

PATRICIA E. PATRICK, Plaintiff and Appellant,

v.

UNUM LIFE INSURANCE COMPANY OF AMERICA et al.,
Defendants and Appellants.

Petition for review DENIED.
Kennard, J., is of the opinion the petition should be granted.
Werdegar, J., was absent and did not participate.

GEORGE

Chief Justice