

## First Supplement to Memorandum 95-58

### Administrative Adjudication by State Agencies: Followup Legislation (Comments of Proposition 103 Enforcement Project)

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One of the provisions to be included in the administrative adjudication followup legislation is an amendment of Insurance Code Section 1861.08. This provision is part of Proposition 103 (automobile insurance initiative measure), and requires conforming revisions for the new administrative adjudication law. We did not include these conforming revisions in the original administrative adjudication bill because we did not want to burden the bill with a two-thirds vote requirement, which is necessary for an amendment to Proposition 103.

The proposed conforming amendments are:

#### **Ins. Code § 1861.08 (amended). Conduct of hearings**

SEC. . Section 1861.08 of the Insurance Code is amended to read:

1861.08. Hearings shall be conducted pursuant to Sections 11500 through 11528 Chapter 5 (commencing with Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code, except that: (a) hearings

(a) Hearings shall be conducted by administrative law judges for purposes of Sections 11512 and 11517, chosen under Section 11502 or appointed by the commissioner; ~~(b) hearings .~~

(b) Hearings are commenced by a filing of a Notice in lieu of Sections 11503 and 11504; ~~(c) the .~~

(c) The commissioner shall adopt, amend or reject a decision only under Section 11517 (c) and (e) and solely on the basis of the record; (d) Section 11513.5 shall apply to the commissioner; (e) discovery Section 11518.5.

(d) Discovery shall be liberally construed and ~~disputes determined by the administrative law judge.~~

**Comment.** Section 1861.08 is amended to reflect revision of the Administrative Procedure Act by 1995 Cal. Stat. ch 938.

The introductory portion of the section is amended to refer to the entire formal hearing chapter. That chapter is supplemented by Chapter 4.5 (commencing with Section 11400) of the same part, containing general provisions on administrative adjudication applicable to all state agency hearings. See Gov't Code § 11410.10 (application of chapter).

The reference in subdivision (c) to the procedure for adoption, amendment, or rejection of a decision is supplemented by a reference to the new procedure for correction of mistakes and clerical errors in the decision. See Gov't Code § 11518.5. The reference to a decision "solely on the basis of the record" in subdivision (c) is deleted as surplus. All decisions under the Administrative Procedure Act must be based exclusively on the record. Gov't Code § 11425.50 (decision).

The reference to former Government Code Section 11513.5 is deleted as obsolete. It is superseded by Government Code Sections 11430.10-11430.80 (ex parte communications), which apply to all hearings under the Administrative Procedure Act.

The reference in subdivision (d) to determination of discovery disputes by the administrative law judge is deleted as surplus. All discovery disputes under the formal hearing procedure are now determined by the administrative law judge. Gov't Code § 11507.7.

We sent the proposed amendments to the Proposition 103 Enforcement Project for review. Their comments are attached as Exhibit pp. 1-6. (Their letter also includes comments directed to the Commission's unfair competition project. These we will deal with separately.)

#### **Subdivision (c) — Adoption, Amendment, or Rejection of Proposed ALJ Decision by Insurance Commissioner**

The existing reference in subdivision (c) to the Commissioner adopting a decision under Government Code Section 11517 (c) and (e) is obscure, so we asked the Proposition 103 Enforcement Project to clarify the intent of the provision. Their letter indicates that the intent is to require a proposed decision by an ALJ, followed by an affirmative act by the Insurance Commissioner. They suggest that for this reason, subdivision (c) should be revised to refer to subdivision (b) of Section 11517 as well as to subdivisions (c) and (e). **The staff sees no problem with this, and would implement the change:**

(c) The commissioner shall adopt, amend or reject a decision only under Section 11517 (e) (b), (c), and (e) and Section 11518.5.

**Comment.** Subdivision (c) is amended to add a reference to Section 11517(b), which includes expanded procedures for agency adoption of a proposed administrative law judge decision.

The reference in this provision to Section 11518.5 picks up the new procedure for correction of mistakes and clerical errors in the decision. The Proposition 103 Enforcement Project notes that this procedure requires notice to the parties, but

suggests it could be improved by allowing parties an opportunity to respond to an application for correction. As originally developed, we included provisions for a response, but ultimately deleted the response provisions in order to make the correction procedure limited, technical, and expeditious. The notice is sufficient to enable the parties to raise any problems on administrative (or judicial) review.

#### **Subdivision (d) — Application of Ex Parte Communication Rules to Insurance Commissioner**

Our draft would delete the reference in subdivision (d) to Government Code Section 11513.5 (ex parte communications) on the basis that this provision is superseded by general ex parte communications provisions in the revised Administrative Procedure Act. The Proposition 103 Enforcement Project points out that the effort to apply the general ex parte communications provisions in all state agency hearings has resulted in a weakening of existing prohibitions as they apply to Insurance Commissioner proceedings. Specifically, Government Code Section 11430.30 allows some communications between agency personnel and the presiding officer (designed for small agencies), and Section 11430.70(b) allows ex parte communications in individualized ratemaking proceedings (designed for the Public Utilities Commission). **The staff has no problem with excepting these provisions in order to preserve existing law as it applies to Proposition 103 hearings:**

(d) Section 11513.5 shall apply to the commissioner; Notwithstanding Section 11501, Section 11430.30 and subdivision (b) of Section 11430.70 shall not apply in these hearings.

Comment. The reference in subdivision (d) to former Government Code Section 11513.5 is deleted as obsolete. It That section is superseded by Government Code Sections 11430.10-11430.80 (ex parte communications), which apply to all hearings under the Administrative Procedure Act. However, subdivision (d) makes clear that Government Code Sections 11430.30 (permissible ex parte communications from agency personnel) and 11430.70(b) (ex parte communications in individualized ratemaking proceeding) do not apply in hearings under this article; this preserves the effect of existing law under former Government Code Section 11513.5.

If these changes are acceptable to the Commission, we will add them to the administrative adjudication followup bill.

Respectfully submitted,

Nathaniel Sterling  
Executive Secretary

**PROPOSITION  
103  
ENFORCEMENT  
PROJECT**

October 30, 1995

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BY FACSIMILE AND US MAIL

RE: Proposed amendments to Insurance Code Section 1861.08 and  
the Unfair Competition Act (Business & Professions Code Sections  
17200, et seq.)

Dear Mr. Sterling:

Thank you for asking the Proposition 103 Enforcement Project (the Project) for our comments regarding whether the proposed changes to Insurance Code Section 1861.08 -- the procedural provisions of Proposition 103 -- would further the consumer protection purposes of the initiative. As we discussed last month, the Law Revision Commission is proposing these amendments to conform Section 1861.08 with SB 523's amendments to the Administrative Procedures Act. We would also like to comment at this time regarding the Commission's proposal to amend Business and Professions Code Sections 17200 et seq. These sections were incorporated in Proposition 103 to enable consumers to sue insurers for unfair business practices.

Proposition 103 is a comprehensive insurance reform package. As provided in the purposes section of the initiative,

The purpose of this chapter is to protect consumers from arbitrary insurance rates and practices, to encourage a competitive insurance marketplace, to provide for an accountable insurance commissioner, and to ensure that insurance is fair, available, and affordable for all Californians. (Proposition 103, Section 2).

To meet those purposes, Proposition 103 incorporated many procedural and consumer protection sections from other laws, including the Government Code and the Business and Professions Code. As described in detail below, the Project believes that some of the Commission's proposed amendments may hinder those purposes.

**A. Proposed Amendments To The Insurance Code**

**1. Amendments to the first paragraph of section 1861.08.**

This amendment changes the reference in section 1861.08 from the administrative hearing provisions of the current APA to the formal hearing provisions of the APA as amended by SB 523. Essentially, the same hearing procedures are adopted, merely the numbering of the code sections is altered.

Upon a first reading, this proposed change does not make any notable substantive changes to the formal hearing provisions of Section 1861.08 -- with the exception of the addition of a settlement conference procedure (Section

1511.7). Therefore, it would not hinder the purposes of Section 1861.08 of Proposition 103.

**2. Amendments to section 1861.08 (a).**

This amendment is minor and technical in nature. It merely changes the placement of the term "hearings" from the end of the paragraph to the beginning of the same paragraph. Based upon my review of the amended APA, this amendment does not make any substantive changes to Section 1861.08, and would not, therefore, hinder the purposes of Section 1861.08 of Proposition 103.

**3. Amendments to section 1861.08 (b).**

This amendment is minor and technical in nature. It merely adds the term "hearings" to the beginning of the paragraph. Based upon my review of the amended APA, it does not appear to make any substantive changes to Section 1861.08, and would not, therefore, hinder the purposes of Section 1861.08 of Proposition 103.

**4. Amendments to section 1861.08(c).**

**a. Your comment regarding Section 11517(c) and (e).**

In your letter, you noted that "the existing reference to Government Code Section 11517(c) and (e) appears to be erroneous, but we cannot tell what was intended. This may be an opportunity to correct the error, if you can ascertain the true intent of the provision."

Regarding the intent of this section of Proposition 103, this provision was meant to ensure two things. First, that administrative law judges alone, as opposed to in conjunction with the Commissioner, are to hear Proposition 103 cases that are heard pursuant to section 11517. (Ins. Code § 1861.08(a)). Therefore, subdivision (a) of section 11517 is not applicable to Proposition 103 hearings.

Second, proposed Administrative Law Judge (ALJ) decisions regarding Proposition 103 proceedings shall not be automatically deemed approved. Such decisions must be affirmatively adopted, amended, or rejected by the Commissioner. (Ins. Code § 1861.08(c)). Therefore, subdivision (d) of section 11517 is not applicable to Proposition 103 hearings.

All of the other provisions of Section 11517 seem to be applicable and are currently in force in Proposition 103 proceedings. Further, Section 11517(c) refers the reader to section 11517(b). Therefore, under the numerical system of the revised APA, the intent of Proposition 103 may be met by amending Section 1861.08 as follows:

(c) The Commissioner shall adopt, amend or reject a decision only under Section 11517(b), (c), and (e)....

**b. The elimination of the language that the decision shall be "solely on the basis of the record" from Section 1861.08.**

The comments provide that this provision is eliminated as surplusage because all decisions must be based solely upon the record pursuant to section 11425.50 of the amended APA. Based upon my initial review of that section, it does not appear that this amendment would hinder the purposes of Section 1861.08 of Proposition 103.

**c. The elimination of the language that "Section 11513.5 shall apply to the Commissioner."**

The comments provide that "the reference to Government Code Section 11513.5 is deleted as obsolete. It is superseded by Government Code Sections 11430.10-11430.80 (ex parte communications), which apply to all hearings under the Administrative Procedures Act."

The Project believes that many of the current protections afforded to consumers from "behind closed door" meetings between the insurance industry and the Insurance Department, which are currently provided by Government Code section 11513.5, are eliminated under the amended APA sections 11430.10 - 11430.80. The weakening of Proposition 103's "ex parte" provisions as proposed by the Commission would seriously undermine the purposes of Proposition 103.

For instance, Section 11430.30 provides certain circumstances wherein agency representatives may engage in ex parte communications with the presiding officer of a hearing. Further, Section 11430.70 explicitly provides for ex parte communications with the agency head or presiding officer in ratemaking hearings -- exactly the sort of communications Section 1861.08 is intended to prevent.

These provisions are directly contrary to the ex parte sections of the APA which Section 1861.08(c) specifically incorporated for Proposition 103 proceedings and applied to the Commissioner and the Commissioner's staff as well as to ALJ's. Government Code Section 11513.5 forbids direct or indirect ex parte communications regarding the merits of a contested matter with the ALJ serving in an adjudicative proceeding while the proceeding is pending with either a party, an agency employee, an interested third party, or with any person who presided at a previous stage of the proceeding.

Section 1861.08 of Proposition 103 incorporated those provisions to ensure that decisions in Proposition 103 proceedings are based exclusively upon the record after a full and open hearing in which no ex parte communications unfairly influence the ALJ hearing the case or the Insurance Commissioner who ultimately decides the case. (Ins. Code § 1861.08).

This mandate is not subtle. It is a fundamental part of the overall scheme of Proposition 103 which envisions that an elected insurance commissioner will be subject to the will of the voters, but, not unfairly influenced by ex parte communications with the insurance industry. Prior to Proposition 103, much of California's insurance public policy was made in secret meetings between insurance industry executives and the Department of Insurance. Proposition 103

mandated that these decisions be made in a fair and open context where insurance consumers would have a voice in crafting the policies affecting them.

Similarly, the ALJ initially hearing Proposition 103 cases should not be influenced by communications which are not on the record. An ALJ who is in need of further expert testimony may request that information either on his or her own behalf or from the parties to the proceeding -- on the record. The ALJ should not be influenced by communications with outside parties, the Commissioner, or the Commissioner's staff. Otherwise, the decision may not ultimately be "solely on the basis of the record." Such a result would also hinder the appeal of improper decisions.

Therefore, the inclusion of either of these provisions in Section 1861.08 would unlawfully hinder the purposes of Proposition 103. The following amendment, however, would adopt the good aspects of the new ex parte provisions while avoiding these pitfalls:

(d) Sections 11430.30 and 11430.70 shall not apply to these hearings....

- d. The addition of Section 11518.5 as one means whereby the Commissioner may adopt, amend, or reject a decision.**

The proposed amendment adds Section 11518.5 as one means whereby the Commissioner may adopt a decision. This section provides a procedure whereby a party may apply to a regulatory agency to correct a mistake or clerical error in a decision and further provides that notice of the application for such a change must be provided to all parties to the proceeding. Although it would be wise to amend the provision to provide other parties an opportunity to respond to the application, the addition of this section to Section 1861.08(c) would not hinder the purposes of Proposition 103.

- 5. The elimination of the language that "discovery disputes be determined by the administrative law judge."**

The comments provide that this provision is eliminated as surplusage because all discovery disputes under the formal hearing provisions of the amended APA are determined by the ALJ. Based upon my review of Section 11507.7, it appears that this amendment would not hinder the purposes of Proposition 103.

## **B. Proposed Amendments To The Business and Professions Code**

The Project also wishes to express its grave concerns regarding the direction taken by the Commission in its Study (B-700) regarding the Unfair Competition Act (Business and Professions Code Section 17200, et seq) which is incorporated into Proposition 103 by Insurance Code Section 1861.03. The Project believes that the solutions proposed in the most recent Draft Tentative Recommendation (Memorandum 95-43) go far beyond the scope of the problems which are alleged in the Study and that major change in this area is unnecessary. Further, the Project believes that any application of these proposed amendments to Proposition 103 would require the approval of the voters because such application would not further the purposes of Proposition 103.



Prior to the passage of Proposition 103, the Insurance industry was exempted from the consumer protection and unfair competition laws which applied to every other business in the State. (Ins. Code § 1860.1). Proposition 103 halted the unfair and collusive activities of the industry by providing that:

The business of insurance shall be subject to the laws of California applicable to any other business, including, but not limited to, the Unruh Civil Rights Act (Civil Code Sections 51 through 53), and the antitrust and unfair business practices laws (Parts 2 and 3, commencing with section 16600 of Division 7, of the Business and Professions Code). (Insurance Code Section 1861.03(a)).

Proposition 103 thereby intended to protect insurance consumers from civil rights violations and unfair business practices as well as to encourage a competitive insurance marketplace in California. The ability of consumers to enforce the Unfair Competition Act through Section 17200 actions on behalf of the general public is an extremely important tool for the Project as well as other consumer representatives in California.

In Section 17200 cases that we are aware of, many of the problems identified in the Study simply do not exist. In fact, not enough Section 17200 actions are brought, particularly by public prosecutors, leaving the burden on public interest organizations -- such as the Project -- as well as private attorneys to enforce state laws.

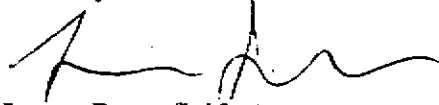
Because of the lack of empirical evidence of major abuses of Section 17200 cases, we cannot support any changes that would place greater burdens on private parties bringing such actions. Further, we believe that existing means can be used to address the few problem cases. If any further action need be taken, it would more appropriately be dealt with in the legal ethics arena, rather than through major procedural changes in Section 17200 which will only serve to hinder consumers from suing to halt unfair business practices.

In addition, there are other problem areas that the Commission has not addressed that should be included if any legislation to improve section 17200 litigation is proposed. One such improvement, which was passed by the legislature but vetoed by the Governor, is a prohibition on secrecy agreements for settlements in actions brought on behalf of the general public. There is simply no justification for confidentiality in public actions such as these.

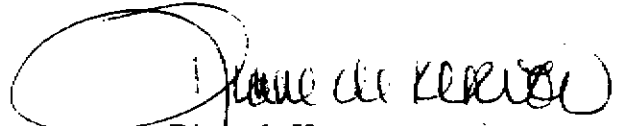
Because we believe that some of the Commission's proposed amendments to the Business and Professions Code and the Insurance Code will seriously undermine the purposes of Proposition 103, we wish to play an active role in your consideration process on these proposals. Please add the Project to your mailing list for these proposals and keep us advised of any further developments.

Once again, thank you for requesting our views regarding the proposed amendments to Section 1861.08 of Proposition 103 and the amendments to the Unfair Competition Act, which is incorporated into Proposition 103. If you have any questions regarding our remarks, please don't hesitate to call us.

Sincerely,

A handwritten signature in dark ink, appearing to read 'Harvey Rosenfield', with a stylized, flowing script.

Harvey Rosenfield  
Executive Director of the Project

A handwritten signature in dark ink, appearing to read 'Diane de Kervor', with a large, circular flourish at the beginning.

Diane de Kervor  
Staff Attorney for the Project