
SENATE COMMITTEE ON INSURANCE

Senator Susan Rubio, Chair

2021 - 2022 Regular

Bill No:	SB 1040	Hearing Date:	March 31, 2022
Author:	Rubio		
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Urgency:	No	Fiscal:	Yes
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SUBJECT: Insurance: restitution

DIGEST: Authorizes the California Department of Insurance (CDI) to issue restitution on behalf of insurance consumers, as an ancillary order to an administrative action for insurance code or standards of conduct violations where the commissioner issues a cease and desist order, financial penalty, or other sanction. If facts and equity permit, authorizes the commissioner to order rescission, or cancellation, of the insurance contract.

ANALYSIS:

Existing law:

- 1) Generally regulates insurance and creates the Department of Insurance, headed by the Insurance Commissioner.
- 2) Subject to exemption, requires that persons soliciting, negotiating, or effecting contracts of insurance hold a valid license from the commissioner that authorizes them to act in that capacity, and generally regulates these agents and brokers according to their field.
- 3) Authorizes the commissioner to bring a superior court action to enjoin a person who is violating or about to violate the Insurance Code.
- 4) Authorizes the commissioner to apply to the clerk of the superior court for a judgment to enforce an order requiring a person to pay a monetary penalty or reimburse the department for costs incurred by the department in prosecuting the matter.
- 5) Authorizes the commissioner to issue a cease and desist order and impose a monetary penalty on a person, or someone who aided and abetted a person in acting in a capacity for which a license or certificate of authority from the commissioner was required but not possessed. Requires the order show cause in order for monetary penalty to attach, and allows the penalty to be calculated as the greater of \$5,000 per day of violation or five times the amount of money the person received for acting in the capacity for which a license was required but not possessed.
- 6) Exempts generally surplus lines brokers, among others, from licensing requirements and provides for separate regulation of surplus lines activities.

- 7) Provides that all fines, forfeitures, taxes, assessments, and penalties provided for in the insurance code shall be due and payable on the demand of the commissioner. If payment is not made within ten days after the demand, requires the commissioner institute an action in the name of the people of the State of California for the purpose of recovering the moneys due.

This bill:

- 1) Authorizes the commissioner to seek a judgment to enforce an order for restitution. Specifically:
 - a) Authorizes the commissioner to order a respondent to an ancillary administrative action authorized by the insurance code, if certain requirements are met, to provide restitution for a loss arising from the respondent's conduct.
 - b) Requires the commissioner to first determine the respondent violated the insurance code or the standards of conduct applicable to persons acting in the capacity the respondent was acting in or purporting to act in when the loss occurred, and in this ancillary proceeding impose a cease and desist order, an order for monetary penalties, or another sanction.
 - c) The restitution order:
 - i) Must cite a factual basis for the order;
 - ii) Must state the persons, or classes of persons, who suffered a loss;
 - iii) Must state the amount to be paid or property to be returned; and
 - iv) May be judicially enforced in an action brought by the commissioner, the Attorney General, a district attorney, a city attorney, or any person owed restitution pursuant to the order. In that action, the court may award attorney's fees and court costs to a prevailing plaintiff.
- 2) Authorizes the commissioner to issue with a restitution order, if the facts and equity permit, an order of rescission enforceable on any person subject to the commissioner's jurisdiction. The order of rescission:
 - a) Must be subject to judicial review in the same manner and time as the order to which it is ancillary; and
 - b) May be judicially enforced in an action brought by the commissioner, the Attorney General, a district attorney, a city attorney, or any person owed restitution pursuant to the order. In that action, the court may award attorney's fees and court costs to a prevailing plaintiff.
- 3) Authorizes the commissioner to order a respondent to reimburse the commissioner for the commissioner's costs of implementing and enforcing this section, including attorney's fees along with an order requiring restitution.

- 4) Defines “restitution” to mean the full amount that will compensate each person for their direct and indirect financial and nonfinancial losses proximately caused by the respondent’s violations.
- 5) Exempts surplus lines brokers.
- 6) Makes restitution payable on the demand of the commissioner, and requires the commissioner institute an action in the name of the people of the State of California for the purpose of recovering restitution if payment is not made within ten days after the commissioner’s demand.

Background

Under current law, anyone who sells insurance must be licensed with the California Department of Insurance (CDI). California consumers benefit from licensing requirements by being able to trust the agents and brokers that sell them insurance products meet minimum standards and are trained on California practices. In order to maintain this trust, CDI maintains significant enforcement operations to ensure unlicensed individuals are denied access to, and do not harm, California consumers. Currently, the Insurance Commissioner may issue a cease-and-desist order and assess a monetary penalty of \$5,000 per day against an unlicensed seller of insurance, among other sanctions.

One well-known insurance scam CDI notes fits this bill is a pre-recorded phone message that many people have received. It typically starts with a phrase along the lines of, “We have been trying to reach you about your car’s extended warranty.” Extended auto warranties, or vehicle service contracts, are not illegal in California, but they may only be sold at dealers. This is intended to limit consumer confusion about whether a telephone solicitation may be legitimate, but has not stopped unscrupulous individuals from trying to sell real and faulty auto warranties to unsuspecting consumers over the phone.

The commissioner may spend many months and significant resources to stop one operation. During this time, a person selling insurance without a license may have defrauded hundreds or thousands of Californians of millions of dollars of premium. Despite having the authority to issue cease and desist orders, and issue penalties, the commissioner does not have authority to order restitution for the victims CDI identifies as part of these investigations. This requires victims of fraud to file individual lawsuits to obtain restitution. Obstacles to litigation including getting time off from work, the inability to afford a lawyer for larger cases, the uncertainty of collecting a judgment, mobility issues, and language barriers often deter victims from suing regardless of their socioeconomic status. A sly scammer can “fly under the radar” by defrauding many consumers of relatively small amounts, betting that it’s unlikely many will have the interest or means to devote significant resources to recover a small sum.

CDI notes that due to the length of time of some of these operations, the penalties that do accrue can be far above whatever CDI is able to collect. The stated reason is that often times an entity can have a civil judgment forgiven in a bankruptcy reorganization. When the committee inquired, CDI was not able to pinpoint exactly how much potential revenue from unpaid penalties is lost in this manner, but notes the ease at which

predatory organizations are able to dissolve and reform through bankruptcy or other means to avoid meaningful oversight.

Precedent

Many California regulators and insurance regulators in other states possess the authority to obtain restitution orders when an unlicensed person harms a consumer. These include:

- California agencies:
 - Bureau of Automobile Repair,
 - Contractors State License Board,
 - Dental Hygiene Board,
 - Bureau of Security and Investigative Services,
 - the State Bar,
 - Department of Financial Protection and Innovation, and
 - Department of Real Estate.

- Other state insurance regulators, including: AR, CT, IA, KS, KY, ME, VA, and WV.

Regulatory Activity

CDI claims the commissioner issues cease and desist orders to unlicensed sellers of insurance, including unlicensed automobile warranty companies, unlicensed insurers, and unlicensed individuals acting as agents or brokers, annually. These sales defraud Californians of millions of dollars every year and the typical case involves multiple victims. Losses include stolen premium and the placement of fraudulent policies that lead to uninsured claims.

Unlicensed sellers target vulnerable communities and small businesses, among others. Unlicensed auto warranty companies have left countless consumers with unpaid claims. Examples provided by CDI of unlicensed conduct and its victims include:

- An unlicensed seller was sentenced to four years in prison in 2022 after being convicted of defrauding three victims of over \$1.4 million. The unlicensed seller gave the victims with fraudulent certificates of insurance, leading them to believe they had valid coverage.

- In 2020, CDI issued a cease and desist order to an unlicensed auto warranty company. Over 1,000 Californians paid more than \$2 million in illicit premium.

- An unlicensed seller stole \$174,000 in premium payments from individual truck drivers and charter bus companies in 2017 and 2018. Truck drivers who thought they were insured and were not temporarily lost their authority to operate and had to decline jobs while securing actual coverage.

Suggested Amendments

The Committee may wish to require the following amendments:

1. Considering CDI's stated oft-encountered struggle to obtain recoveries that match what the commissioner has levied in penalties, the Committee may wish to require the Insurance Commissioner allocate any monies collected to restitution

on behalf of consumers before the Commissioner may apply it to the penalties the Commissioner has assessed.

2. Due to the fact that this bill specifically targets people that are unlicensed but acting as agents and brokers selling insurance inside California, and the state has significant interest in maintaining a strong surplus lines market – the sale of out of state products inside California when a domestic product is unavailable– special care should be taken to ensure these activities are not erroneously swept up into the classification of activities this bill intends to stifle. The Committee may therefore wish to consider an amendment to clarify the surplus lines broker exemption.

Related/Prior Legislation

AB 989 (Block, 2009) For the regulations regarding protection of persons 65 years of age and older, would have given any person harmed as a result of a violation of those provisions the right to bring a civil action for compensatory damages and any other remedies.

ARGUMENTS IN SUPPORT:

In support of the measure the commissioner writes, “Every year, Californians are victimized by unscrupulous individuals who sell insurance without a license. Unlicensed sellers include unlicensed automobile warranty companies, unlicensed insurers, and unlicensed pseudo-agents and pseudo-brokers, who have defrauded California residents out of millions of dollars in recent years. The California Department of Insurance (Department) has discovered numerous instances of insurance premium theft, embezzlement, and fraud by unlicensed insurance sellers who specifically target vulnerable communities such as seniors, immigrants, and historically underrepresented communities. In many cases, small businesses are left without insurance coverage, and business owners’ livelihoods are put at risk.”

SUPPORT:

California Department of Insurance (Sponsor)
California Advocates for Nursing Home Reform
City of Rosemead
City of South El Monte
City of West Covina
Consumer Attorneys of California
Paradise Association of Realtors
Rosemead Chamber of Commerce and Visitor Information Center
The LGBTQ Center Long Beach

OPPOSITION:

None.

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