California Uninsured Motorist Coverage—A Promise to the Ear Broken to the Hope[1]

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Uninsured and underinsured vehicles present challenging public policy and public health issues. UM/UIM coverage is designed to compensate those injured by vehicles which carry less than adequate coverage. To the extent UM/UIM coverage compensates innocent victims and accommodates their reasonable expectations, one may count the coverage a success. To the extent it fails to compensate those injured or falls short of reasonable expectations, it is less so. California's underinsured motorist coverage, adopted in 1984, falls into the latter category. It is outdated and strays in many significant ways from sound policy and best practices followed in many sister states.[3]

California has between 2,600,000 and 3,950,000 uninsured vehicles on the road (Between 9.89% and 15%, depending on which survey one credits), and many more carry only 15/30 coverage. This compulsory limit has not been revised since 1967 and, when adjusted for inflation, is currently worth $2,143/$4,286. One can expect, therefore, that between 1 in 6 and 1 in 7 California accidents will be with an uninsured motorist, and many more (estimated at 50% in staff comments to AB 3984 in 1984) will carry a liability policy with little value.

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[1] "And be these juggling fiends no more believed,
That palter with us in a double sense;
That keep the word of promise to our ear,
And break it to our hope."
Macbeth thought his life was covered by an insurance policy he carried with The Three Weird Sisters Insurance Company. He speaks these lines when he finds that two of the improbable exclusions – moving forests and death at the hands of one (Macduff) born by cesarean section -- apply to him. W. Shakespeare, Macbeth, act 5, sc. viii.

[2] Opinions expressed are those of the author and not necessarily those of the Center or the University of Santa Clara.

[3] UM/UIM is complex, and this brief essay will not do it justice. Although occupying perhaps 3 pages of a standard 33 page auto policy, Robert C. Clifford's treatise on California Uninsured Motorist Law stretches to two loose-leaf volumes. See: Robert C. Clifford, *California Uninsured Motorist Law* (2008).

Attempts to reduce this number of uninsured vehicles have been remarkably unsuccessful. Some attempts include (1) requiring proof of insurance to register an automobile, (2) attaching penalties to driving without insurance and (3) barring uninsured plaintiffs from recovering for noneconomic damages (Proposition 213, Civ. Code § 3333.4).

California also adopted a Low Cost Automobile Insurance program to address this issue. According to the Department of Insurance's 2014 report to the legislature, at the end of 2013 there were only 11,521 low cost policies in force. If each 10,000 uninsured cars were a rung on a ladder, one would have to insure between 260 and 395 rungs to eliminate the uninsured motorists from California roads. The Low Cost Automobile Insurance Program has barely reached the first rung. Although there have been recent modifications both with respect to those who may qualify for the policy (See SB 1273, effective January 01, 2015) and those who may acquire valid driver's licenses (thus making insurance more easily available), the results of these changes are yet to be seen.

As a result, through no fault of their own, many of those injured by uninsured or underinsured motorists are unnecessarily denied adequate compensation in California. This is unnecessary because California can deliver more adequate coverage consistent with affordability, availability and profitability. Better coverage can also be delivered consistent with sound insurance principles such as avoiding moral hazard, adverse selection and arbitrary outcomes.

Uninsured motorist (UM) coverage was created by insurers in the 1950s to forestall either compulsory automobile insurance or the takeover of coverage by states (e.g., with an unsatisfied claim fund). Jennifer B. Wriggins, *Mandates, Markets, and Risk: Auto Insurance and the Affordable Care Act,* 19 Conn. Insurance Law J., pp. 295, 313 (2012-2013). The basic law (it has been amended a number of times) went into effect in California in 1961. By 1984 inflation and the rising cost of medical care had substantially eroded the value of California's minimum 15/30 coverage (adopted in 1967). The many drivers insured for the minimum, therefore, offered little protection to those they injured. Because of this

erosion in coverage, in 1984 many California insurers, including CSAA and State Farm, offered underinsured (UIM) coverage in one form or another.

Supported by the California Trial Lawyers Association (CTLA), in 1984 AB 3984 (Connelly) was introduced to mandate the offer (although not the purchase) of UIM insurance. Although initially opposed by insurers, after several amendments, insurers and CTLA made common cause and both supported the bill. The law went into effect in 1985. Today, 49 states require that insurers offer UM coverage, and 21 states mandate that insureds purchase UM coverage. *Id.* at 313, n. 159.[4] Thirteen of those states also mandate the purchase of UIM coverage,[5] and seventeen states offer or require the purchase of "no-fault" insurance (PIP).[6]

UM/UIM coverage is broader than many people may think. For example, when an automobile carries UM/UIM coverage, the coverage extends to resident relatives, domestic partners, unemancipated children who are away at school, and anyone occupying the insured vehicle. In addition, UM/UIM coverage extends to injuries that do not arise from use or occupancy of the insured vehicle. (Ins. Code § 11580.2(b) – "while occupants of (the insured) vehicle or otherwise"). [Emphasis added]. For example, if an uninsured or underinsured vehicles strikes a child of the insured in a crosswalk, the UM/UIM coverage on the family vehicle extends to the accident even though at the time of the accident the insured vehicle may have been in the garage at home. *Lopez v. State Farm Fire & Casualty Co.*, 250 Cal. App.2d 210, 58 Cal. Rptr 243 (1967). These are substantial benefits under UM/UIM coverage.

When an insured makes a claim under their UM/UIM insurance against their company, questions related to fault and damages are decided by arbitration. There is no right to jury trial. This procedure can be more expeditious than court proceedings, and it also lowers insurers' concerns about possible "runaway juries."

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[4] The Insurance Information Institute lists the jurisdictions at: http://www.iii.org/issue-update/compulsory-auto-uninsured-motorists

[5] Id.

[6] Id.

Nevertheless, there is ample room for improving California's UM/UIM coverage. In 1984 the Enrolled Bill Report for AB 3984 stated that

> "Underinsured Motorist coverage is designed to allow a prudent individual to protect himself in case of accident involvement with an at-fault insured motorist, but one whose insurance coverage limits are at or only slightly above the minimum financial responsibility limits." (Enrolled Bill Report, 9.20.84)

A few fact patterns may test how well the design of this coverage protects a prudent insured who wants to protect herself and her family from inadequately insured motorists. The following fact pattern, with some modifications, will be used to illustrate the issues and to suggest some solutions.

Fact pattern:

Prudence suffered $200,000 in injuries and carried $100,000 in UM/UIM coverage. Dan injured her with his vehicle and was entirely at fault. Dan carried liability insurance as indicated in the fact patterns.

1. <u>To Setoff or not to Setoff?—That is the Question.</u>

Unlike a number of states, California is a "setoff" state rather than a "nonsetoff" state.

> When bodily injury is caused by one or more motor vehicles, whether insured, underinsured, or uninsured, the maximum liability of the insurer providing the underinsured motorist coverage <u>shall not exceed</u> the insured's underinsured motorist coverage limits, less the amount paid to the insured by or for any person or organization that may be held legally liable for the injury." Calif. Ins. Code § 11580.2(p)(4)(A)(Emphasis added).

Standard policy provisions track this language. This means that, whenever the tortfeasor has insurance triggering UIM coverage, the carrier NEVER pays the limits of the UIM policy regardless of the gravity of the insured's injuries. *Mercury Insurance Co v. Vanwanseele-Walker* (1996) 41 Cal. App. 4th 1093, 1102, 49 Cal. Rptr 2d 28, 31 ("[A] carrier providing underinsured motorist benefits *never* pays the full amount. . . .").

In the hypothetical, if Dan carried $15,000 in liability coverage, Prudence would recover only $85,000 from her UIM carrier and $15,000 from Dan's liability carrier – total of

$100,000 against a $200,000 injury. Indeed, if both Patricia and Dan carry minimum UIM and liability coverage (15/30), the UIM insurer will never pay anything. This is for two reasons: (1) when UIM coverage is equal to the liability coverage, the UIM coverage is not triggered (see discussion below) and (2) because when Dan's insurer pays the $15,000 policy limits, it is deducted from the UIM limit ($15,000), leaving zero on the UIM limit. When both parties carry minimum insurance the UIM carrier pays nothing. One dissenting justice suggested that this was to "perpetuate a statewide fraud of historical magnitude against low-end insureds." *Schweiterman v. Mercury Cas. Co.* (1991) 229 Cal. App 3d 1044, 1049, 280 Cal. Rptr 804, 807 (Crosby, J. dissenting).

Auto insurance rates are regulated and are subject to prior approval in California. Cal. Ins. Codes §§ 1861.01(c), 1861.05. Significant elements in setting rates are loss experience and projected loss experience. Since no UIM claims payments would be expected from a 15/30 UM/UIM policy, one would expect that the policyholder will have paid no premium for the UIM portion of the policy. Any claims payments, presumably, would be on the UM side of the policy. This, though, will be small comfort to a policyholder who paid a premium for UM/UIM coverage only to find that the $15,000 UIM side was illusory. Compare *Sweeney v. General Casualty Co. of Wisconsin* (1998) 582 N.W.2d 735, 736 (Wis. Ct. of App.)(Applying a reducing clause would render the UIM coverage "illusory"). It is a little like purchasing a dozen eggs, only to find 8 when you open the carton. The grocer's explanation that he charged for only 8 is of small consolation when you needed a dozen.

Many states, including Nevada, are nonsetoff states. Applying the above fact pattern in a nonsetoff state, Prudence would recover $100,000 from her UIM carrier and $15,000 from Dan's liability carrier – a total of $115,000 against her $200,000 injury.

Here is some typical statutory language in nonsetoff states:

Ark. Code §§ 23-89-209(a)(3), (a)(5) (2012).

> 23-89-209(a)(3) The coverage shall enable the insured or the insured's legal representative to recover from the insurer the amount of damages for bodily injuries to or death of an insured which the insured is legally entitled to recover from the owner or operator of another motor vehicle whenever the liability **insurance limits of**

the other owner or operator are less than the amount of the damages incurred by the insured.

23-89-209(a)(5) Coverage of the insured pursuant to underinsured motorist coverage **shall not be reduced by the tortfeasor's insurance** coverage except to the extent that the injured party would receive compensation in excess of his or her damages. [Emphasis added]

Nev. Rev. Statute § 687B.145(2):

Uninsured and underinsured vehicle coverage must include a provision which enables the insured to recover **up to the limits of the insured's own coverage** any amount of damages for bodily injury from the insured's insurer which the insured is legally entitled to recover from the owner or operator of the other vehicle **to the extent that those damages exceed the limits of the coverage for bodily injury carried by the owner or operator.** [Emphasis added]

Utah Code Ann. § 31A-22-305.3 (2013)(i)(ii).

Underinsured motorist coverage **may not be set off** against the liability coverage of the owner or operator of an underinsured motor vehicle, but shall be added to, combined with, or stacked upon the liability coverage of the owner or operator of the underinsured motor vehicle to determine the limit of coverage available to the injured person. [Emphasis added]

Some states enforce the setoff only when Prudence would be OVER compensated. See Alan I. Widiss, *Uninsured and Underinsured Motorist Insurance* (2001) sec. 41.7, n. 8 (listing 8 jurisdictions).[7] When there is no statutory authorization for the setoff, courts frequently invalidate policy terms providing for it. *Id.* at n. 9 (listing 17 jurisdictions).[8] Others invalidate setoff provisions because they are inconsistent with the reasonable expectations of insureds. *Id.* at n. 13 (listing 2 jurisdictions).[9]

[7] Arkansas, Connecticut, Florida, Indiana, Iowa, New Hampshire, Oregon, West Virginia.
[8] Delaware, Idaho, Illinois, Maine, Minnesota, Missouri, Montana, Nevada (setoff is currently banned by statute), New York, Ohio, Pennsylvania, South Carolina, Texas, Virginia, Washington, West Virginia, Wisconsin.
[9] Missouri, Wisconsin.

This author asked his faculty, all law professors, whether, with a $200,000 injury, $100,000 in UIM coverage, and $15,000 of liability coverage for the tortfeasor, they could recover a total of $100,000 ($85,000 from their insurer and $15,000 from the tortfeasor) or a total of $115,000 ($100,000 from their UIM insurer and $15,000 from the tortfeasor.) Twenty responded. Two said they had no reasonable expectation. Of the remaining 18 responses, 13 were incorrect. Eleven thought there was no setoff compared with 5 who thought there was a setoff. It is not surprising that, even among those sophisticated in legal matters, these nuances are not understood.[10]

This confusion among trained lawyers is consistent with confusion at large. To explore awareness of car insurance coverage, the NAIC conducted a survey of 1,000 people. The survey revealed that "some of the basics of auto insurance are not well understood, even though it is one of the most commonly purchased types of insurance by people of all ages and demographics." *New NAIC Insurance IQ Study Reveals Americans Lacking in Confidence, Knowledge of Insurance Choice,* Nat'l Ass'n of Ins. Comm'rs (Apr. 6, 2010).[11] An earlier report of the Arizona Department of Transportation concluded that "many people do not understand the difference between liability coverage and uninsured motorist coverage." Lisa Markkula, *Uninsured and Underinsured Motorists: Trends in Policy and Enforcement,* Ariz. Dep't of Transp., (June 2004).[12]

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[10] This is the question posed to the law faculty:

Would you be kind enough to email me your answer to the following question? If you have read your policy and know the answer, that is fine. You are in the sample pool. If you have not read your policy, please do not do so to answer this question. I want what you think, not the truth. This is not a test.

1. A sustains injuries of $200,000 in an auto accident and carries $100,000 in uninsured/underinsured insurance with A's own auto insurer. B negligently injures A with B's car. B is entirely at fault. B has $15,000 in liability insurance (the minimum required by California's Financial Responsibility Law) and no other assets. How much may A recover?

a. $15,000 from B's insurer and nothing from A's own insurer because B complied with California's Financial Responsibility Law

b. $100,000 ($15,000 from B's insurer and $85,000 from A's own insurer).

c. $115,000 ($15,000 from B's insurer and $100,000 from A's own insurer).

d. I have no reasonable expectation as to what the answer is.

There were 20 responses: a—2, b—5, c—11, d—2.

[11] http://www.naic.org/Releases/2010_doc/iiq_new.htm.

[12] http://www.azdot.gov/tpd/atrc/publications/project_reports/pdt/az548.pdf.

In addition to being more consistent with the reasonable expectations of insureds, moving to a nonsetoff rule also reduces issues associated with the exhaustion rule (see below). That rule requires judgments or settlements in order to trigger UIM coverage. A nonsetoff rule allows immediate recourse to the UIM coverage if the injuries justify it and they exceed the available liability coverage. The UIM claim would be the actual damages net of available liability coverage.

It is a well settled rule in California that an insurer may offer broader coverage than mandated by statute. In *Utah Property & Casualty Ins. V. United Services Auto. Assn. (1991)* 230 Cal.App.3d 1010 and *Lumberman's Mut. Cas. Co v. Wyman (1976)* 64 Cal.App.3d 252 the courts held that where a policy includes greater coverage than required under the law, the insurer may not rely on statutory restrictions on coverage that were not incorporated in the policy. It could be argued that the setoff rule may be an exception to this principle because Calif. Ins. Code § 11580.2(p)(4)(A) speaks in mandatory language ("shall not exceed"). The statute outlines a "statutory policy" – i.e., one whose terms may not vary from the statute. Read literally, the statute would have the unusual effect of forbidding an insurer from offering the more generous nonsetoff UIM coverage.

In 2013 there was a bill addressing the setoff question - AB 862 (Wieckowski). AB 862 addressed this issue by proposing a modest change with respect to California's setoff rule. This bill would ALLOW, but not require, insurers to offer policies of the "nonsetoff" kind. In the earlier hypothetical, if Prudence had purchased a nonsetoff policy and sustained $200,000 in injuries, carried a $100,000 UIM limit, and Dan carried a $15,000 limit, Prudence could recover $15,000 from Dan and $100,000 from her own company under the UIM insurance - a total of $115,000 against the $200,000 in injuries. She is $15,000 closer to being fully compensated.

While addressing part of this problem, AB 862 included a major defect – it did not go far enough. It modified the setoff rule when underinsured motorist coverage is triggered, but it did not alter the trigger – the definition of an underinsured motor vehicle. This would have led to an unacceptable anomaly. Subdivision (p) governs underinsured motorist coverage.

The subdivision provides that the section applies only when bodily injury is caused by an "underinsured motor vehicle." "Underinsured motor vehicle" is defined as one where the limits are "less than the uninsured motorist limits carried on the motor vehicle of the injured person." Subsection (p)(2).

Applying this definition of "underinsured motor vehicle," the court in *State Farm Mut. Auto. Ins. Co. v. Messinger* (1991) 232 Cal. App. 3d 508, 283 Cal.Rptr. 493 denied UIM benefits when the tortfeasor's limits were equal to the UIM claimant's limits. The court concluded that no UIM benefits were triggered: "[The tortfeasor's] car was insured for an amount equal to the uninsured/underinsured coverage the [victims] carried, and therefore not 'an amount less than the uninsured/[underinsured] motorist limits carried' by the [victims]." 232 Cal. App. 3d at 514.

Returning to the hypothetical, again assume Prudence sustained $200,000 in injuries. She carried nonsetoff UIM coverage of $100,000, and Dan carried liability coverage on his vehicle of $15,000. Prudence could recover $115,000 under AB 862.

Assume nonsetoff UIM coverage of $100,000 and liability coverage of $75,000. Now Prudence recovers $175,000.

Assume UIM coverage of $100,000 and liability coverage of $100,000. Now Prudence recovers only $100,000 (from Dan) and NOTHING under the UIM coverage because the tortfeasor's vehicle is not an "underinsured motor vehicle." Thus, by increasing the liability coverage by $25,000, Prudence loses $75,000 in coverage for her $200,000 injury. In this roulette game, the "winner" is one who is injured by an automobile with anything less than $100,000 in liability coverage, and the loser is one injured by an automobile with $100,000 or more in coverage (but less than $200,000). Make sense of that, if you can.

An earlier Bill (AB 1063, 2011)(Bradford) also addressed this definitional issue, but AB 862 did not. Utah solved the problem by adopting the common sense meaning of "underinsured motor vehicle." An underinsured motor vehicle as one with "insufficient

liability coverage to compensate fully the injured party for all special and general damages." Utah Code Ann § 31A-22-305.3 (2013). This is a "damages-to-limit" trigger rather than a "limit-to-limit" trigger. California should consider following Utah's lead.

The limit-to-limit trigger can have truly perverse consequences. Assume again that Prudence suffers $200,000 in damages and carries $100,000 in UM/UIM. Assume that Dan also carries a $100,000/$200,000 liability limit. Unfortunately, Dan also killed Pat and gravely injured Paul in the same accident. In compromising these two claims, Dan's insurer pays Pat's heirs $100,000 and Paul $90,000. Clearly, Dan was grossly underinsured for this accident, but he is not an "underinsured" within the meaning of California's statute because Dan's liability insurance was not less than Prudence's UM/UIM coverage. See subsection 11580.2(p). Thus, Prudence's UM/UIM coverage is not triggered, and Prudence is left with only the remaining $10,000 on Dan's liability policy and nothing from her own UM/UIM coverage. Indeed, if all of Dan's coverage had been used to compromise other claims, Prudence would recover nothing from her $100,000 in underinsured coverage. *State Farm Mut. Auto. Ins. Co. v. Messinger* (1991) 232 Cal. App.3d 508, 283 Cal. Rptr. 493. The *Messinger* Court suggested that the problem could only be solved in the legislature. Citing the multiple injuries scenario, the dissenting judge in *Schweiterman v. Mercury Cas. Co.* (1991) 229 Cal. App.3d 1044, 280 Cal. Rptr 804 compared the result to fraud.

It is also not clear whether authorizing insurers to offer nonsetoff policies would have the desired effect. Arguable, and despite the apparent statutory language mandating setoff "uninsured motorist coverage," insurers could offer nonsetoff coverage now. It could take the form of an endorsement, perhaps with a name such as the "make whole" endorsement. Since the endorsement is not "uninsured motorist coverage," but, rather, is separate from and in addition to uninsured motorist coverage, it would not be forbidden by the statute. If the endorsement were approved by the Department of Insurance, it could be offered. Despite this potential avenue, the author is aware of no insurer offering such an endorsement.

2. Exhaustion

Ins. Code § 11580.2(p)(3) provides that UIM coverage does not apply "until the limits of bodily injury liability policies applicable to ALL insured motor vehicles causing the injury have been EXHAUSTED by payment of judgments or settlements . . . ."[Emphasis added].

A typical clause in a policy reads:

> "[W]e will pay only if the full amount of all available limits of all motor vehicle bodily injury liability insurance, self-insurance, or cash deposits or bonds posted to satisfy a financial responsibility law that apply to the insured's bodily injury have been exhausted by payment of judgments or settlements, and proof of the payment is submitted to us."

This provision is designed to insure that the UIM carrier is credited with any recovery or potential recovery from the insurance of the tortfeasor. Unfortunately, as drafted and applied, it leads to anomalous and unacceptable results.

In the hypothetical, assume that Dan carries $15,000 in liability insurance, but his insurer will offer Prudence only $14,000 in settlement (set aside, for now, issues of possible bad faith towards Dan on the part of Dan's insurer). To protect Prudence's UIM claim (recall, Prudence suffered $200,000 in damages) she is forced to the expense and risk of going to trial in pursuit of the remaining $1,000 in coverage in order to protect her $100,000 UIM claim (or $85,000 UIM claim under California's setoff rule). This "Tail Wags the Dog" rule is a waste of her money and the state's judicial resources. Many states have rejected it, but it is the law in California. *Farmer's Insurance Exchange v. Hurley* (1999) 76 Cal. App. 4th 797, 806-07, 90 Cal. Rptr.2d 697, 703-04. The *Hurley* court encouraged the legislature to address this issue. The court included a discussion of the numerous jurisdictions that required only that the insurer be credited for the full policy limits.

It is far more sensible to allow Prudence to accept the $14,000 settlement and CREDIT THE UIM insurer with the $15,000 liability limit. Indeed, two of the justices in

Hurley, supra, suggested just that approach. *Id.* at 808, 90 Cal. Rptr. at 705 (Gaut and Ward, J. concurring). Numerous states do not require exhaustion so long as the UIM carrier is credited with the liability insurer's policy limits. See cases listed in Robert C. Clifford, *California Uninsured Motorist Law* (2008) § 11.51.5. Many courts invalidate exhaustion clauses as contrary to public policy. See cases collected in the Idaho Supreme Court's opinion in *Hill v. American Family Mutual Insurance Co.*, 150 Idaho 619, 624-25, 249 P.3d 812, 817-818 (2011). Nevada's UIM statute does not mention an exhaustion clause. In the absence of statutory authorization, the Nevada Supreme Court also struck down as contrary to public policy an exhaustion clause included in an insurer's policy. *Mann v. Farmers Insurance Exchange*, 108 Nev. 648, 836 P.2d 620 (1992), *overruled in part on other grounds by White v. Cont'l Ins. Co.*, 119 Nev. 114, 65 P.3d 1090 (Nev. 2003). But "an underinsured motorist coverage provider should only pay for whatever damages the insured suffered *beyond* the tortfeasor's policy limit" [Emphasis in original]. *Mann, supra.* at 651, 836 P.2d at 622, *White, supra* at 118, 65 P.3d 1090, 1092 (2003). Fair enough.

If multiple tortfeasors contribute to Prudence's injuries, California's exhaustion rule (at least as drafted) presents yet another unacceptable anomaly. The code requires that the LIMITS of ALL insured vehicles causing injury be exhausted. California's UIM law was adopted in 1984. In June, 1986 the California voters adopted Proposition 51 (Civ. Code § 1431.2) which apportions noneconomic harm among concurrent tortfeasors according to their share of fault. Thus, prior to the adoption of Proposition 51 Prudence could recover for all of her injuries from any among the tortfeasors until she was fully compensated or the various policies were exhausted. After the adoption of Proposition 51, that may no longer be possible. See discussion in Robert C. Clifford, *California Uninsured Motorist Law* (2008) § 11.51.5.

Assume noneconomic injuries of $200,000 and UIM coverage of $100,000. Dan, who is 95% responsible for the injuries, carries $15,000 in liability coverage. Doug, who is 5% responsible, carries $1,000,000 in coverage. Dan pays the policy limits, and Doug (because of Proposition 51) pays $10,000 (5% of $200,000). Prudence is grossly undercompensated, yet she can never exhaust ALL of the policy LIMITS. If exhaustion

under these circumstances is a precondition to triggering the UIM coverage, it is a nonsensical result and clearly violates any reasonable expectation on the part of Prudence when she purchased her UIM coverage. Contrast *Wedemeyer v. Safeco Ins. Co.*, 160 Cal. App.4th 1297, 73 Cal. Rptr. 3d 415 (2008)(after exhausting driver's $15,000 policy, insured need not also exhaust employer's $1,000,000 business policy because exhaustion requirement applies only to automobile policies and not to policies that incidentally also cover automobiles).

Since Proposition 51 will make it impossible to exhaust all policy limits in many circumstances, it seems at least plausible that "policy limits" should be given a broad interpretation. In practice, there are two relevant limits to coverage: (1) the express limit on the declaration page of the policy and (2) the limit imposed by the phrase in the insuring agreement that the insurer will pay damages for which any covered person becomes "legally liable." Proposition 51 may leave the UIM insured inadequately compensated by limiting the legal liability of one or more of the tortfeasors. Thus, the second "limit" may be reached short of the policy limits on the declaration page of the policy. When this limit is reached, coverage is exhausted. Perhaps the exhaustion requirement will be interpreted in this manner, but if the exhaustion requirement is to remain, the statute should be amended to clarify how the exhaustion requirement is to be applied under these circumstances.

If it appears that due to Proposition 51 or otherwise, exhaustion of all relevant policies may not be possible or practical, it is advisable to consult with the UIM insurer early in the process. Perhaps they will agree in writing that using best efforts to exhaust as much as possible of the relevant policies is sufficient. This approach, however, relies on the willingness of the UM/UIM insurer to agree, and the UM/UIM insurer is in the position of an adversary with respect to the insured's claims against the insured's own insurer.

Should there be an issue whether the $10,000 settlement with Doug is reasonable, one might put in place a procedure similar to the one used to protect joint tortfeasors who lose their right of contribution when another joint tortfeasor settles. In these cases, the settling torfeasor may apply to the court for a declaration that the settlement is in good faith.

3. UM or UIM?

Although procedural requirements for UM and UIM differ in a number of details, whether UM or UIM coverage is triggered can compel stunningly arbitrary results. This is especially so when there are multiple tortfeasors, and one tortfeasor is uninsured while the other has some insurance. Consider these two examples.

Dan and Doug are equally responsible for Prudence's injuries. Again, Prudence carries $100,000 UM/UIM and suffers $200,000 in injuries. Dan has NO insurance, and Doug carries a $75,000 liability limit. Since Prudence's UM/UIM limit is higher than Doug's liability limit, this triggers Prudence's UIM coverage. Thus, under Section 11580.2(p)(4), the UIM insurer is entitled to a credit for Doug's $75,000 in coverage. Prudence's total recovery is $100,000 ($75,000 from Doug, $25,000 from her UIM insurer and $0 from uninsured Dan).

Assume the same constellation of injuries and insurance, except that Doug now carries $100,000 in liability coverage instead of $75,000. This no longer triggers UIM coverage because Doug's liability coverage is not less than Prudence's UIM coverage. Doug is no longer "underinsured." UM coverage, however, IS triggered because Dan has NO insurance. The offset provision applicable to UIM coverage under Section 11580.2(p)(4) does not apply to UM coverage. Moreover, the subrogation provision of UM coverage (Section 11580.2(g)) does not apply until Prudence is fully compensated. *Holcomb v. Hartford Casualty Insurance Co* (1991) 230 Cal. App.3d 1000, 281 Cal. Rptr. 651.

> "An insured who is injured by both an insured and an uninsured motor vehicle can recover for his damages up to the limits of his uninsured motor vehicle coverage without reduction for recovery from the insured motorist. However, an insured who is injured by both an underinsured and an uninsured motor vehicle, by virtue of section 11580.2, subdivision (p)(4), can recover no more than the limits of his underinsured motorist coverage reduced by the amount paid on behalf of the underinsured motorist." *Id.* at 1006, 281 Cal. Rptr at 654.

Thus, when Patricia's UM coverage is triggered, she may recover $100,000 from Doug's liability insurer and $100,000 from her own UM insurer (assuming Dan is

responsible for at least that much of Patricia's injuries) for a total of $200,000. Patricia is fully compensated.

This result is nonsense. A $25,000 increase in Doug's liability coverage increased Patricia's recovery by $100,000. In the new math of UM/UIM insurance, 2 plus 2 no longer equals 4. This nonsense ("anomaly," in the gentler words of the *Holcomb* Court, *id.* at 1006, 281 Cal. Rptr at 654), is, again, a product of the setoff rule. If California were a nonsetoff state, Patricia's recovery under the first scenario would be $175,000 and under the second $200,000 -- consistent with compensating her and exactly what a reasonable consumer would expect.

Compare this with the opposite "anomaly" under AB 862 discussed above. If there is only one tortfeasor with a $75,000 limit, and his liability coverage is increased by $25,000, Patricia loses $100,000 in coverage! Add an equally responsible UNinsured tortfeasor, and Patricia's recovery increases by $100,000! Enough exclamation points!

4. Physical Contact

The California Insurance Code includes in the definition of uninsured or underinsured drivers those who are "unknown" provided that there is "physical contact" between the uninsured automobile and the "insured or with an automobile that the insured is occupying." Calif. Ins. Code § 11580.2(b)(1). Thus, California insurers need not afford coverage for injuries caused by an unknown "Miss-and-Run" driver. This limitation was in the 1961 UM law and was carried forward into the 1984 UIM additions.

A typical clause in a policy reads:

> "Uninsured Motor Vehicle means: . . . a "hit-and-run" land motor vehicle whose owner or operator remains unknown and which has physical contact with: (a) an insured; or (b) the vehicle an insured is occupying."

When a policy includes this restriction, recovery under UM/UIM coverage is no longer congruent with accidents for which the tortfeasor is "legally responsible."

Uninsured motorist property damage claims, which are typically limited to $3,500, require both physical contact and the identity of the hit-and-run driver or the hit-and-run vehicle (at least by license number). Calif. Ins. Code § 11580.26(b). A typical clause reads:

> "Uninsured Motor Vehicle means a land motor vehicle which involves actual, direct physical contact with your car. . . . A land motor vehicle is an uninsured motor vehicle only if the owner or operator of the vehicle is identified, or if the vehicle is identified by its license number."

Although the physical contact rule is intended to avoid fraud, experience suggests that the restriction can spawn as much mischief as it avoids. Keep in mind that the restriction applies even when the injured party, who has the burden of proof in any event, can prove beyond any doubt that the accident was caused by the negligence of the unknown or unidentified driver.

Let's look at a concrete example. As reported in the news, on November 1, 2014 there was a 5 car pileup on Highway 80 outside Sacramento. A white car struck a Kia, causing the Kia to spin out in the middle of the highway. The white car fled and had not, at the time of the report, been identified. Another driver, in attempting to avoid a collision with the Kia, lost control of his car and hit a tree. The collision with the tree killed one passenger (let's call her Prudence) and caused minor injuries to others in his car.

Assuming there was no fault on the part of the driver, but the driver carried the standard UM/UIM policy in California, can the family of Prudence recover on the driver's (or, indeed, Prudence's) UM/UIM policy? No. Despite the fact that the unknown hit-and-run driver collided with the Kia, and there was a total of 5 automobiles involved in the collision, and doubtless numerous witness, there was no physical contact between the hit-and-run vehicle and our driver's automobile. Nor did the hit-and-run vehicle propel the Kia into the driver's car. Thus, none of the UM/UIM coverages is triggered. See examples discussed in *Inter-Insurance Exchange of the Automobile Club of Southern California v. Lopez*, (1965) 238 Cal. App.2d 441, 443-444, 47 Cal. Rptr. 834, 835-836.

This incident was more newsworthy because Prudence was a passenger in an automobile driven by a Lyft driver. The news reports stated that Lyft carries $1,000,000 in

UM/UIM coverage "in cases where an uninsured or underinsured motorist causes damage to a Lyft or Uber vehicle, including hit-and-run cases."[13] The author has not seen the commercial Lyft policy, but if it contains the same limitations as your policy and the author's policy, this statement is incorrect. There must be physical contact with the uninsured automobile (the white hit-and-run vehicle) to trigger the UM/UIM coverage.

Many jurisdictions find the "physical contact" restriction unnecessary, contrary to public policy, or both. Where no statute authorizes it, many courts have invalidated "physical contact" provisions as contrary to public policy. Courts in approximately one-half of the states have invalidated the "physical contact" requirement. Widiss, *supra* at sec. 9.7.

Some examples are *Lowing v. Allstate Insurance Co*, 176 Ariz. 101, 859 P.2d 724 (1993)(en banc)(reversing previous rulings to the contrary), and *Simpson v. Farmers Insurance Company, Inc.*, 225 Kan 508, 592 P.2d 445 (Sup. Ct. Kan 1979)(apparent majority holds physical contact requirement impermissible). The statute in *Lowing* required uninsured motorist coverage. Since the purpose was to "close the gap in protection under the Safety Responsibility Act," the statute was remedial in nature and should be liberally construed. Since it was impossible to tell whether the unidentified driver was or was not insured, the court presumed that the driver was uninsured. The policy provided coverage only for those who were "hit" or had "physical contact" with the unknown driver. The purpose of this provision was to avoid fraud. It was not, however, authorized by the statute and, in the Court's view, it was both too broad (there could be 20 witnesses) and too narrow (the insured could easily manufacturer contact.) The Court, therefore, invalidated the clause.

Still, there are some limits. *Mayor v. Wedding*, 2003 Ohio 6695; 2003 Ohio App. LEXIS 5947 (Cow not uninsured vehicle because not a "land motor vehicle"). What, however, if the cow had just jumped or fallen from a cattle truck? Jumped or fallen one-half

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[13] http://www.theaggie.org/2014/11/11/ridesharing-service-lyfts-first-fatal-accident-occurs-in-sacramento/

hour before? [14] It may depend on whether the object (the cow) was still in motion due to the motion of the unidentified vehicle, or was the cow either stationary or moving under its own power. Compare *Lopez, supra*, and *Pham v. Allstate Insurance Co.*, 206 Cal. App.3d 1193, 1198, 254 Cal. Rptr. 152, 155 (1988)(physical contact requirement satisfied when rock which fell from the unknown vehicle, bounced once, then struck the motorist's car) with *Barnes v. Nationwide Mut. Ins. Co*, 186 Cal. App.3d 541, 543-544, 230 Cal. Rptr. 800, 801 (1986)(no physical contact with unidentified vehicle when the injured party collided with a box of dinette chairs lying in the freeway.)

Some statutes moderate the physical contact requirement by requiring either physical contact or corroboration. For a statute requiring physical contact or a disinterested witness, see Georgia statute O.C.G.A. § 33-7-11 (b) (2):

> "A motor vehicle shall be deemed to be uninsured if the owner or operator of the motor vehicle is unknown. In those cases . . . in order for the insured to recover under the endorsement where the owner or operator of any motor vehicle which causes bodily injury or property damage to the insured is unknown, actual physical contact must have occurred between the motor vehicle owned or operated by the unknown person and the person or property of the insured. **Such physical contact shall not be required if the description by the claimant of how the occurrence occurred is corroborated by an eyewitness to the occurrence other than the claimant.**" (Emphasis added).

A number of other states arrive at a similar conclusion either through statute or judicial decision. See Widiss, *supra* sec. 9.8, n. 10 (listing 10 states, 6 with statutes). In the absence of physical contact, Tennessee's statute requires "clear and convincing evidence." Tenn. Ann. Code § 56-7-1201(e). Following the invalidation of the physical contact requirement in *Simpson v. Farmers Insurance Co., supra*, the Kansas legislature adopted a corroboration rule. K.S.A. 40-284(e)(3) now permits an exclusion or limitation

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[14] For a dashcam video of a truck decanting cattle into the roadway, see: https://www.youtube.com/watch?v=nBYRihfVboY Since the truck overturned, it likely was a known, rather than unknown, driver.

"when there is no physical contact with the uninsured motor vehicle and when there is no **reliable competent evidence** to prove the facts of the accident from a **disinterested witness not making claim under the policy**." (Emphasis added)

Today there are far more surveillance cameras in many places than there were when this rule was adopted by California in 1961. There are now dashcams and phones with video recorders. Even if these offer irrefutable evidence, California's "physical contact" rule would deny recovery to Prudence. It should also be noted that newer cars have recording devices that make accident reconstruction far more reliable. According to the Department of Transportation, approximately 96% of 2013 model cars include event data recorders that preserve helpful information related to a crash.[15] Self-driving cars in both California and Nevada are required to preserve all the recorded information for 30 seconds preceding an accident. See, *e.g.*, Cal. Motor Veh. Code § 38750(c)(1)(G), Nev. Automobile Code § 482A.110(2)(b). When a virtual video of the accident exists, the physical contact requirement makes no sense.

The "physical contact" requirement also invites perverse results or incentives. It tends to punish the nimble driver who avoids the more serious collision with the miss-and-run driver and lands in a ditch or hits a tree, but it "rewards" the poorer driver who fails to avoid the oncoming vehicle. Indeed, when writing an algorithm to control a self-driving car, all things being equal, the physical contact rule might suggest programming the car to select a glancing blow with the oncoming vehicle rather than a similar collision with a tree or roadside embankment!

5. Raise the Compulsory Coverage Limit

California's 15/30 limit has not been revised since 1967 (with the exception of Low Cost Insurance, which lowers the limits for qualifying drivers to 10/20). If 15/30 was the appropriate amount when originally adopted, it cannot possible be the appropriate amount now. Indeed, the ravages of inflation and the cost of medical care make the limit seem derisory. A major reason for the 1984 legislation mandating the offer of UIM coverage was

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http://www.nhtsa.gov/About+NHTSA/Press+Releases/U.S.+DOT+Proposes+Broader+Use+of+Event+Data+Recorders+to+Help+Improve+Vehicle+Safety

the inadequacy, at that time, of the 15/30 limit. Today the value of that limit has eroded to just $2,143/$4,286 when compared to 1967 dollars. Indeed, to reflect the value of 1967 dollars, the $15,000 limit would have to be raised to $104,958.[16] The author is aware of no state that has limits lower than California.[17] Even Mississippi, the "Thank God for . . . ." state has higher limits (although if is fair to state that it also has a higher percentage of uninsured drivers – estimated at 22.9%[18]). Raising this limit will not only afford better primary protection to those injured, but it will also reduce the number and amount of UM/UIM claims because more drivers will carry adequate coverage. The legislature should consider revising this limit upward.

Raising the minimum limit would likely have greater impact on premiums than reforming UM/UIM coverage, so there may be no political will to do it. Indeed, like a 1967 home that has been neglected for almost 50 years, perhaps these 1967 rates are no better than a tear-down. One may wonder why we keep in place this elaborate structure (at considerable direct and indirect cost to the public) when its value has deteriorated from $104, 958 to $2,243 (or perhaps less, since medical costs have inflated even faster than inflation).

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[16] http://data.bls.gov/cgi-bin/cpicalc.pl?cost1=15%2C000.00&year1=2015&year2=1967

[17] The Insurance Information Institute list (as of Feb., 2015) only 4 other non-PIP states with the same limit. State financial responsibility limits are listed at: http://www.iii.org/issue-update/compulsory-auto-uninsured-motorists

15/30 – AZ, CA, DE, LA, NV
20/40 – CT, IA
25/40 - WV
25/50 – AL, CO, GA, , ID, IL(raised from 20/40 as of 1.1.15), IN, MS, MO, MT, NE, NH (not compulsory), NM, OH, OK, RI, SC, SD, TN, VT, VA, WA, WI (With a change of administration, in 2011 Wisconsin lowered its mandatory minimum from 50/100 to 25/50), WY
30/60 – NC, TX
50/100 – AK, ME
PIP Jurisdictions – AR, DE, DC, FL, HI, KS, KY, MD, MA, MI, MN, NJ, NY, ND, OR. PA, UT

[18] Id.

6. Wedding UIM to Liability Limits – a Match Not Made in Heaven

Insurers may argue that California's "setoff" rule is justified because UIM insureds may purchase higher coverage if they desire it. This is not completely true. Cal. Ins. Code § 11580.2(m) provides that insurers must offer UM insurance equal to the liability limits for bodily injury in the underlying policy, but need not offer UM limits in excess of 30/60. Cal. Ins. Code § 11580.2(n) provides that insurers must offer UIM at least in the amount of UM coverage, but may offer higher limits.

Insurers uniformly refuse to offer a UIM limit in excess of the liability limit in the underlying policy. In order to purchase the more moderately priced UIM coverage, the insured must also purchase the matching, but much more expensive, liability coverage. Thus, in order for Prudence to protect herself and her family from personal injury she must purchase coverage to protect her financial assets that she does not want and may not need. This tie-in is not required by the statute, and there is no logical connection between personal assets and physical wellbeing (unless one were to embrace the obnoxious notion that pain and net worth rise in unison).

Insurers defending this practice argue that one should not be permitted to protect oneself in an amount greater than one is willing to protect others. This "insure unto others as you would have them insure unto you" has an appealing cadence, but unless it is based on a solid concern about moral hazard or adverse selection, it is a meaningless limitation on an innocent person's ability to protect against the serious hazards presented by automobiles. There is no similar limit on the purchase of life insurance nor on the purchase of one automobile that may be safer than another (or, like heavy mini vans and SUVs, of greater hazard to others). Moreover, many who benefit from UM/UIM are not in a position to make the decision with respect to purchasing liability coverage (e.g., relatives resident in the insured's household).

The Golden Rule, however, becomes a bronze rule when applied to insurers. They need not, and some do not, offer UM/UIM in the same limits as the liability limits purchased by the insured. Thus, one may purchase $500,000 in liability coverage, but be restricted to much less in UM/UIM coverage despite the willingness to purchase it. The author's own

experience is an example – the author carries $500,000 liability coverage for a single injury on his 1993 Toyota pickup truck, but the carrier would write no more than $250,000 in UM/UIM coverage for a single injury. The author has not canvassed umbrella policies, but the author's own umbrella policy does not cover

> "excess uninsured motorist coverage, except in a few states. Uninisured Motorist coverage is only available with the Umbrella policy if you live in the following states: FL, LA, NH, OH, TN, and VT."

California's draconian application of the exhaustion requirement also undermines the industry's Golden Rule argument. The exhaustion requirement forces injured parties to expend their own time, money and risk to exhaust the tortfeasors' policies by settlement or judgment for the benefit of the UIM insurer. All sums recovered in the exhaustion process reduce the victim's recovery under the UIM coverage.

This issue is more difficult to address, though, because compelling an insurer to write insurance in whatever amount an insured may desire is alien to the marketing of insurance. Perhaps a reminder that coupling UIM limits with liability limits is not required would encourage more insureds to ask for higher UIM limits. Competition may do the rest. If insurers oppose moving California to a "nonsetoff" state, and they argue that there is no need to make the move because insureds may purchase the UIM coverage they want, perhaps they will de-couple the two limits on their own to forestall legislation they oppose. At a minimum, if the Golden Rule is to be applied to policyholders, it should also apply to insurers.

Since California highways are rife with uninsured and underinsured vehicles, perhaps mandatory UIM and higher limits are in order. Careful consideration must be given to potential impact on rates and on how any change might affect affordability and availability. In a letter supporting the earlier Bradford Bill (AB 1063) the CDI estimated that eliminating the setoff rule would raise the UM/UIM premium by about 10%. A 2013 filing from a major

carrier suggested that the UM/UIM premium accounts for only about 7% of the total premium volume. On these facts, one would expect an overall increase of about 0.7%.[19]

7. Conclusion

For Prudence and large numbers of Californians, UM/UIM coverage is more important than their liability coverage. Injured passengers, pedestrians and innocent drivers have little other recourse. If insurers can market profitable policies at a modest increase in cost while fulfilling the reasonable expectations of Prudence and others who purchase this coverage, they should be encouraged to do so. Since many drivers are uninsured, and even more carry only minimum coverage, UM/UIM is the best hope for many – if we get it right.

If Arkansas, Utah, Idaho, Nevada and so many other states can deliver better coverage, so can California.

8. Where Do We Go from Here? - Some Modest Proposals

A. Follow the lead of many other states. Deliver what consumers reasonably expect.

--Eliminate the "setoff" rule. Failing that, offer a choice to insureds of a setoff or nonsetoff policy and allow the market place to make the choice.

Insurers have argued that this is confusing. More confusing than now?[20] As a comparison, look at a homeowners policy. As required by Calif. Ins. Code § 10102, the

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[19] The author also carries policies on a 1996 Saturn and a 2013 Honda Fit. The author carries collision on the Honda, but not the Saturn. The total 6 mo. premium for both is $996.62. The total 6 mo. UM/UIM premium for bodily injury for both is $94.67, or 9.5% of the total premium. In any individual case, the ratio of the UM/UIM premium to the total premium will vary considerably depending on whether the insured also carries the relatively expensive collision coverage on one or more vehicles. Looking only at the premium for the fully insured Honda, the bodily injury portion of the UM/UIM coverage for the Honda comes to 7.1% of the total premium.

[20] It may be that even the legislature was confused about the setoff rule, the definition of "underinsured motorist," or both. In a letter memo to the Senate Insurance, Claims and Corporations Committee dated August 28, 1984, Chief Consultant Sheldon Davidow characterized underinsured coverage in this way: "Such coverages would cover the buyer for liability in excess of the policy limits of a driver who causes damages up to the uninsured motorist limits of his/her own policy." There is no suggestion that the driver's coverage should be deducted from the underinsured limits.

In the Senate Republican Caucus bill digest dated 8/29/84, the digest author states that "This bill expands the definition of 'uninsured motor vehicle' to include an 'underinsured motor vehicle'

disclosure page will list 5 different kinds of homeowners policies with a brief explanation of how each kind of policy works. There will be check marks next to the kind of policy you are purchasing. If there is a palpable risk of confusion, auto insurers could use a similar approach.

--Use a "damages-to-limit" trigger rather that the current "limit-to-limit" trigger. Compare Utah Code Ann § 31A-22-305.3 (2013). ("[U]nderinsured motor vehicle" includes vehicle with "insufficient liability coverage to compensate fully the injured party for all special and general damages."

--Exhaustion - When it is difficult or impossible to exhaust other policies, give credit to the UIM insurer for the policy limit and "good faith" settlements if Proposition 51 makes exhaustion impossible.

--Modify the "physical contact" requirement. Either eliminate it or allow reasonable corroboration as a substitute.

--Encourage UM/UIM coverage to be offered at least at the limits of the liability coverage or higher than liability coverage.

--Decouple the ability to recover under UM/UIM from the legal responsibility of the other driver. As cars become more like rolling computers rather than manually driven vehicles, the need to compensate for injuries without regard to the other driver's fault will likely increase. One could still reduce recovery by the claimant's fault, if any.

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which is defined as a vehicle that is insured in an amount that is less than the liability injury limits carried on the vehicle of the injured person." [Emphasis added]. This is simply incorrect. Under the bill an underinsured vehicle is one whose liability limits are less than the underinsured limits carried by the injured person.

Of course, these are only thumbnail descriptions, and the bill says what it says. But, if those advancing the bill seem confused as to its effect, what hope does Prudence have? The BI portions of the author's UM/UIM policy occupies only 3 pages out of a 33 page policy, yet Robert Clifford's treatise explaining these 3 pages extends to 2 loose-leaf volumes and several pounds of paper. Much of it is devoted to sorting the problems presented by the issues outlined in this essay.

B. Many unprotected people fall within the group deserving protection, including pedestrians, passengers, and those taking public transportation. They may neither own a car nor reside in a family with a car. When struck by an underinsured vehicle, they fall outside the present constellation of those protected by UM/UIM insurance. This group includes the snowy haired little old lady who long ago surrendered her license as well as Little Orphan Annie.

One might address this problem in several ways.

--UM/UIM could be uncoupled from auto liability insurance. Those who own no car and/or take public transportation should be able to protect themselves even though they carry no vehicle liability insurance.

--Offer UM/UIM endorsements on homeowners and renters policies to protect those who do not have cars in their resident family.

--Offer a stand-alone UM/UIM policy? There may be insufficient premium or commission to justify the product, but this might be worth considering.

--Protect those who have no other insurance policy to which they might attach the UM/UIM endorsement. An uncompensated victim fund, as used in a few states, may be an appropriate model.

C. Looking further into the crystal ball: Health coverage may soon become nearly universal. To reduce litigation costs and the cost of UM/UIM coverage, one might offer a product covering only other losses, plus, perhaps, deductibles and co-pays. Indeed, one might consider such a system for personal injury claims in general. As with MICRA today, health insurers would no longer have a subrogation claim for the medical portion of judgments or settlements because there would be none.

Model Legislation

Coverage for Californians injured by uninsured and underinsured motorists can be improved in a number of ways. Substantial improvement would flow from improving only four policy provisions -- moving from a setoff to a nonsetoff policy; relaxing the physical

contact requirement; changing to a damages-to-limit trigger, and modifying the exhaustion rule to a credit for collectible insurance rule.

It is likely that these changes will have some impact on rates and premium. The impact may be modest, but nevertheless insurers must account for it. It is likely that since all rates, whether raised or lowered, are subject to prior approval in California, these changes would invite an application for rate approval. Proposition 103, as incorporated in Cal. Ins. Code § 1861.05(b), provides that "every insurer which desires to change any rate shall file a complete rate application with the commissioner."

A complete rate application in California is complex, expensive, and subject to substantial delay. In contrast to Nevada, where approval averages 20 days or fewer, in California approval may take from 6 months to over a year. Insurance is a business, and it would not be unreasonable for California insurers to resist modest policy changes that primarily benefit their insureds if the changes require a complete rate application in order to effect them. If would also be perverse if Proposition 103, which was promoted as benefiting consumers, created unreasonable impediments to enhancing coverage.

By nature, insurers are conservative. Their business is predicting future losses and expenses based on past experience. As Yogi Bara may or may not have said, "Predictions are difficult, especially about the future." For automobile insurance, actuaries will typically begin with the previous three years' experience and attempt to develop an "indication" for the next policy period or periods. When a benefit changes, the previous years' experience is no longer as predictive, and adjustments must be made to account for the change in benefits. In these circumstances, actuaries may try to incorporate "similar" experience into the calculation. Since many states have the reforms suggested above, and many of the insurers in California also write in those states, there is similar experience on which actuaries may call. This is not to say it is easy, but it is clearly doable.

Issues of cost and delay in rate approval may be addressed in several ways. Enabling legislation, if passed by a 2/3 majority, could permit a rate application addressing only the rate change, if any, attributable to these policy changes. Since the purpose of the legislation

would be to enhance coverage for consumers, it would also satisfy the requirement that legislative changes to Proposition 103 "further" the purposes of the proposition. At present, rates are changed without filing a complete rate application with respect to previously approved rates when new vehicle models are introduced, so it does no violence to the prior approval process to permit incremental rate changes when enhancing coverage. For example, Nevada, which is also a prior approval state, allows partial rate applications addressing changes in policy coverage.

An insurer might also adjust the rates by filing an "amendment" to the most recent complete rate application.

In addition, the legislation could provide that an insurer need not introduce these changes until the insurer files a complete rate application in the ordinary course of its business. If an insurer wanted to delay introduction, they could introduce the changes at the time most consistent with their business plan. Since a complete rate application is, by its nature, subject to all of the rigor of Proposition 103 in any event, adding these changes should be manageable with the least additional burden. Perhaps the legislation should adopt an outside time limit of 3 or 4 years for introduction.

CONSUMER ATTORNEYS OF CALIFORNIA

Seeking Justice for All

President Brian D. Chase | CEO • Chief Lobbyist Nancy Drabble | Legislative Director Nancy Peverini | Legislative Counsel Jacqueline Serna Anguiano | Associate Staff Counsel Saveena K. Takhar | Political Director Lea-Ann Tratten

March 18, 2015

TO: MEMBERS, SENATE INSURANCE COMMITTEE

FR: CONSUMER ATTORNEYS OF CALIFORNIA

RE: SENATE INSURANCE OVERSIGHT HEARING (March 25, 2015)
Does Uninsured and Underinsured Motorist Coverage Meet Consumer Needs?

Thank you for inviting Consumer Attorneys of California to participate in this important hearing. This issue is one that must be addressed by the California legislature because uninsured and underinsured motorist coverage does not meet consumer needs or expectations under the current system.

Uninsured and Underinsured Insurance Issues

Uninsured and underinsured motorist coverage is complex and raises a number of issues for consumers. "Uninsured motorist" coverage ("UM") refers to protection in the event that a negligent vehicle operator without *any* insurance at all causes injury to the person who owns that coverage. "Underinsured motorist" coverage ("UIM") provides the same type of protection in cases where a negligent person does not have *enough* of their own auto insurance coverage to pay for all of the damages sustained by the insured person who owns the UIM coverage. (Ins. Code § 11580.2).

UM/UIM motorist coverage is mandatory for any policy purchased in California, unless an insured declines it in writing (§ 11580.2(a)(1) and (2)). Therefore, it is imperative from a consumer protection standpoint that consumers can completely access the insurance that they have purchased and from which they expect protection. *Unfortunately, our current UM/UIM laws apply in a way that make the coverage illusory.*

UM/UIM is insurance coverage that a consumer can buy to protect herself when she is injured by another driver whose insurance is not adequate to cover her injuries. However, under the current law, consumers very often are unable to collect the full value of the UIM coverage, even when their injuries are not fully compensated.

Under current law, an "underinsured motor vehicle" is a vehicle that is covered by an insurance policy, but only if the policy is for a lower amount than the UM/UIM policy in effect for the injured party. (Ins. Code § 11580.2(p)(2)). Thus, when the person causing the accident has total liability limits that are *greater than or equal to* an accident victim's underinsured coverage, no coverage exists. For example, if you have purchased underinsured coverage in the amount of $100,000, but the person who injures you also has coverage of $100,000, and even if your damages (medical bills, etc.) are well over $100,000, you can never claim coverage under your underinsured policy.

Additionally, in UM, the insured assigns subrogation rights to the carrier making UM payments, so the carrier can attempt to collect up to the statutory minimum. In UIM, there are no subrogation rights beyond the statutory minimums. Often, this leaves tax payer provided social safety net to help the injured party recover.

- The majority of UIM policies purchased by consumers are completely illusory. An overwhelming majority of UIM policies purchased are for the minimum limits of $15,000; this means the consumer will never be able to access the UIM policy when they need it most because an underinsured driver is determined by comparing the at-fault driver's policy to the UIM policy the consumer.
- UIM coverage is meant to cover the monetary difference that results when the costs of an accident exceed the available coverage from the at fault party's insurer.
- UM/ UIM coverage is the ONLY coverage that a consumer can purchase that is solely for his or own benefit.
- UM/UIM coverage is OPTIONAL. Unlike liability coverage, the state of California does not require a consumer to purchase UIM coverage.
- UM/UIM coverage is cheap and on average, it accounts for only about 10 percent of a consumer's premium.
- Twenty states already successfully sell "true" UIM policies, where a consumer can access their own policy if their injuries warrant it. It is ironic that states such as Alabama, Arkansas and Kentucky provide more protection for their drivers than California.
- Any potential rate increase to a UIM policy must be approved by the Department of Insurance. The Department must approve rates that are justified, meaning the insurer is entitled to a reasonable rate of return. However, the Department cannot approve a rate that is excessive. Both consumers and insurers are protected by this prior approval system.

Californians are adversely affected every day.

- A man in his late 70's was on driving to a local golf course when he was rear-ended by a commercial truck with a $1 million policy. He suffered severe spinal injuries and was rendered a paraplegic with damages totaling well over $1 million but was unable to tap his $100,000 UIM policy because the commercial truck was not considered "underinsured" under current law.
- A laborer who performed small contracting jobs was involved in a collision that resulted in several rotator cuff surgeries and an early retirement, with damages totaling $150,000. However, he was unable to access his UIM policy because the at-fault driver carried a liability policy of $50,000 and was not "underinsured" compared to the $30,000 UIM policy. However, accessing the underinsured policy would have gone a long way in compensating the laborer's damages.
- The trailer unhinged from a truck headed uphill and striking the vehicle below which carried a couple headed to their Valentine's Day dinner. This horrific crash killed the wife and caused serious fractures along the entire left side of the husband. Although no amount of money will ever compensate the husband for the loss of his wife and life-altering injuries he was unable to access his $500,000 UIM policy because the truck also had a liability policy of $500,000.

A consumer's recovery should not be contingent by luck of the draw of an at-fault driver's motorist policy limits.

Past CAOC Legislative Attempts on UM/UIM

In 2011 CAOC worked with consumer groups and Department of Insurance Commissioner Dave Jones and introduced AB 1063 (Bradford), which would have given insureds the value of what they paid for and guaranteed that if another driver's liability insurance is inadequate to pay for the policyholder's injuries, the policyholder could collect up to the full amount of the UIM policy purchased if needed to cover her damages. This bill was modeled after the majority of states that allow consumers to get true UIM coverage so that they may be fully compensated for their damages. Even Texas and Arkansas have more consumer friendly laws than California on this issue!

Underinsured Motorist (UIM) Coverage is an optional coverage that a consumer can buy to protect herself when she is injured by another driver whose insurance is not adequate to cover her injuries. However, under current law consumers very often are unable to collect the full value of the UIM coverage, even when their injuries are not fully compensated. Unfortunately, a statutory offset exists against any amount that the consumer is able to recover from her UIM policy. That offset is whatever the consumer is able to recover from the Insurer of the at fault party, regardless of what the consumer's injuries are. Additionally, if a consumer chooses to collect from the UIM policy she has paid premiums for she must first sign a release of liability waiving his or her rights to pursue any additional recovery against the actual at fault party. This leaves tax payer provided social safety nets to help the injured party recover.

Then Assembly Insurance Committee Chair Jose Solorio held the bill despite strong support from consumers, insureds and seniors. The bill was later significantly narrowed to allow consumers to be given an option to either purchase UIM coverage that would allow full coverage or to purchase UIM coverage that would be offset by the third party insurance contribution, a provision modeled on Georgia's UIM law. (Ga. Code Ann., Sec. 33-7-11). Even this narrow and moderate attempt faced stiff industry opposition and did not proceed.

In 2012, CAOC introduced a bill to simply allow insurers to offer, should they choose, a UM/UIM policy without an offset. Consumers are unaware that when they purchase a UIM policy that their recovery will actually be offset by the at-fault driver's insurance coverage and typically don't learn about the set-offs until after they have been injured. This can be very distressing to learn at a time he or she is suffering from catastrophic injuries and sky-high medical bills. Although this was a modest bill which had no mandate, AB 862 (Wieckowski) received heavy insurer opposition in the Assembly Insurance Committee and stalled.

Key Insurance Issues for Consumers

In addition to the issues identified above, there are other priority issues for California's insureds.

- ***Requiring the same amount of UM/UIM coverage as liability coverage***

Currently, many insureds have absolutely no idea that they are underinsured because when they purchase or renew policies, the focus is on personal liability insurance and often there is no discussion of UM-UIM limits. It is very common for drivers to purchase a high level of liability protection (protecting the driver if she causes an accident), but to have much lower UM-UIM

limits. In fact, we urge you to go check your own policy! Insurers are not allowed to sell consumers higher UM/UIM limits than what they sell in liability limits, but they are able to sell them *less* than they do in liability insurance. Ins. Code § 11580.2(a)(3). A driver's effective amount of UM/UIM coverage hinges upon the other driver's liability coverage. Consumers may allow an agent to sell them this type of insurance to "save money" without understanding the implications. They effect is that the consumer actually ends up with less protection and usually it costs very little to have the same level of UM-UIM limits as personal liability coverage. This can be fixed by requiring insurers to sell the same amount of UM/UIM insurance as liability coverage

- ***Outdated Financial Responsibility Limits (or, where were you in 1967?)***

California's current minimum motor vehicle liability insurance limits were first established in 1967 and have never been adjusted. (AB 1010, Chapter 862 of 1967). At that time, the mandatory minimum that an insured must have was adjusted from 10/20 to 15/30/5 which is precisely how it still stands today, 47 years later. California ranks near the bottom when comparing auto limits in the other 49 states. An increase in California's limits would make us more in line with national averages.

Our current minimum limits are dangerously low given the changed conditions since 1967. An increase in the minimum liability limits would provide all California residents with a much better and safer level of protection. And, California recently enacted legislation to allow undocumented immigrants to apply for a state driver's license. The influx of new licensed driver's as of January 1st 2015 will be an important factor to consider.

Although there is no current legislation proposed to increase these limits, such low limits directly relate to UM/UIM issues as there is a significant chance a person will be hit by someone with these low limits, which then impacts the availability (or lack thereof) of UIM coverage. Further, an overwhelming majority of UIM policies purchased are for the minimum limits of $15,000, this means the consumer will never be able to access the UIM policy when they need it most because an underinsured driver is determined by comparing the at-fault driver's policy to the UIM policy the consumer.

Thank you for your attention to these important consumer issues.