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THREAT TO STATE REGULATION FROM TRIAL BAR,

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In *BMW of North America, Inc. v. Gore*, the U. S. Supreme Court said:

No one doubts that a State may protect its citizens by prohibiting deceptive trade practices . . . But the States need not, and in fact do not, provide such protection in a uniform manner. Some States rely on the judicial process to formulate and enforce an appropriate disclosure requirement . . . Other States have enacted various forms of legislation that define the disclosure obligations of automobile manufacturers, distributors, and dealers. The result is a patchwork of rules representing the diverse policy judgments of lawmakers in 50 States.¹

This is or appears to be a good law today, but, as a class action lawsuit in downstate Illinois moves forward to trial, change may be coming — change that could disrupt the current state-based insurance regulatory system, bring chaos to insurance company claims settlement practices, and produce millions of dollars for class action attorneys.

In July 1997, a class action lawsuit, *Snider, et al. v. State Farm Mutual Automobile Insurance Company*, was filed in downstate Marion, Illinois on behalf of policyholders in 48 states. The suit alleges that because non-Original Equipment Manufacture ("non-OEM") parts are per se defective and inferior to Original Equipment Manufactured ("OEM") parts, State Farm breached its obligation to restore the insured's vehicle to its pre-loss condition by using non-OEM parts. The suit was later amended to also allege that such action violated the Illinois Consumer Fraud Act ("CFA").²

This broad construction of a class of policyholders from 48 states with varying policy language in jurisdictions with varying regulations, statutes and case law concerning non-OEM parts makes this case far different than the run-of-the-mill class action. This action also creates the potential to render state-based regulation a legal impossibility.

On December 5, 1997, the court certified the class to include:

All persons in the United States, except those residing in Arkansas and Tennessee, who (1) were insured by a vehicle casualty insurance policy issued by Defendant State Farm and (2) made a claim for vehicle repairs pursuant to their policy and had imitation, that is, non-factory-authorized and/or non-OEM parts installed in their vehicles or else received monetary compensation determined in relation to the cost of imitation parts. Excluded from the class are employees of Defendant State Farm, its officers, its directors, its subsidiaries, or its affiliates.

In addition, the following persons are excluded from the class: (1) persons who resided in Illinois and whose policies were issued/executed prior to April 16, 1994, and (2) persons who resided in California and whose policies were issued/executed prior to September 26, 1996.³

26, 1996.³

This Certification was subsequently narrowed on February 11, 1997 to apply only to repair involving "crash parts."⁴

In determining that there was a common question of law, the court acknowledged that State Farm "designed policies specific to each state . . ." but found the contractual obligation to repair, restore, replace, etc. was substantially identical in policies nationwide.

The court dismissed State Farm's objection that the difference in policy language created different questions of law by finding, "the policy's specific form is immaterial provided the operation contractual language contained in each policy is susceptible to uniform interpretation." (Emphasis added.)⁵

Apparently, this uniform interpretation can be done without regard to the laws governing non-OEM parts in the state in which the policy is issued. Indeed, the court went further and decided substantive Illinois law would control in interpreting the State Farm policies issued in the 48 various states.

Citing *Martin v. Heinold Commodities, Inc.* the court held:

There can be no doubt that the claim of each member of the plaintiff class implicates the legitimate interests of Illinois in applying its law to adjudicate a dispute involving a business principally situated in its jurisdiction and which, by its own efforts, insistently has sought to avail itself of both the courts and the laws of the forum State.⁶

In concluding that Illinois law should control, the court stated, ". . . given the fact that State Farm is situated and headquartered in Illinois and affirmatively used Illinois courts and law, this Court could apply Illinois substantive laws including the CFA to the entire class."⁷

This ruling, as well as the ruling on notice to the class, was unsuccessfully appealed to the Illinois Supreme Court⁸ and to the U.S. Supreme Court on a writ of certiorari.⁹ The writ of certiorari was denied without comment on October 5, 1998 despite a chorus of amicus briefs from NAIC, NCOIL, New York, Texas, Nevada, Massachusetts and others.

While the notice issues were of some importance, the issues raised here will focus on the impact of applying Illinois substantive law on policyholders in other states. This application is without the approval, express or implied, of the state affected and it can be safely said with the expectation of the policyholder.

According to the amicus curiae filed by NCOIL:

Thirty-six states have taken seven different approaches to insurer specification of non-OEM parts. One state, Massachusetts, requires use of non-OEM parts. Another state, Hawaii, strongly encourages such use by requiring policyholders to pay the price differential if they insist on receiving OEM parts. Twenty-five states permit use of non-OEM parts upon disclosure to the policyholder. Three states permit use without disclosure. Two states permit use with the policyholder's consent. Three states require consent during a limited time period. One state requires consent for certain types of non-OEM parts. There are even subcategories of different treatment within these seven categories.

A similar but diverse situation exists with the consumer fraud statutes of the various states as to whether they apply, or not, to insurance policies.¹⁰

The NAIC in its amicus curiae stated:

Use of non-OEM parts is only one of literally hundreds of examples of significant matters on which insurance regulations vary between the states. Each of the differing

matters on which insurance regulations vary between the states. Each of the differing regulations reflects that state's view of the best interests of insurance consumers within its own borders, taking into account all relevant factors, including the specific needs of the state's insured population as well as the cost and availability of insurance.¹¹

As an example of this diversity of state regulation, the NAIC brief sites the fact that Illinois mandates health coverage for reconstructive surgery after mastectomies while neighboring Indiana does not. Applying the logic of *Snider* to this example, Indiana policyholders would be legally entitled to Illinois mandated benefits if purchasing a policy from an Illinois domiciled company and any denial of these benefits could be litigated in Illinois.

Apparently, the resolution of controversial issues such as OEM and non-OEM parts or mandated benefits by regulation, legislation or the courts in the individual state are of no importance to the Illinois courts.

Where could the progeny of *Snider* end? Where could it logically end except a cry for federal intervention to sort out the confusion? The plea would be from companies, consumers and regulators alike.

How would an Illinois company handle future auto claims in Massachusetts? To use non-OEM parts violates Illinois law while not using them violates Massachusetts law. How would a Massachusetts company handle the claim of an Illinois policyholder?

How would a company determine rates? How would a Commissioner set them? That point leads to some interesting results for those who advocate competitive rating. Take Illinois and New Jersey as an example. Will State Farm's New Jersey policyholders be able to claim their rates should be set under Illinois open competition law while Prudential's Illinois insureds would be subject to prior approval rates or can they choose the lesser of the two? More perversely, would New Jersey drivers be able to claim the same Illinois rate as Illinois drivers enjoy and sue for overcharges?

For those who want to move toward federal regulation, the industry may as well have been thrown into the "briar patch" by the *Snider* court. For those who want to keep state regulation, they should heed the words of former Illinois State Senator John Grotberg who was fond of saying about bad legislation, "Let's kill this thing before it has little ones."

Endnotes

1. *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559 (1996).

2. 815 ILCS 505/1 et seq.

3. *Snider, et al. v. State Farm Mut. Auto. Ins. Co.*, No 97-L-114 (1st Jud. Cir., IL Dec. 5, 1997).

4. *See Id.* at Amended Order entered Feb. 11, 1998.

5. *Id.*

6. *Id.*

7. *Id.*

8. *State Farm Mut. Auto. Ins. Co. v. Speroni, et al.*, No. 85008 (IL. S. Ct. March 24, 1998).

9. *State Farm Mut. Auto. Ins. Co. v. Speroni, et al.*, 119 S. Ct. 276 (1998).

10. Amicus Curiae Brief of NCOIL on Behalf of Appellant at 8, *State Farm Mut. Auto. Ins. Co. v. Speroni, et al.*, 119 S. Ct. 276 (1998).

et al., 119 S. Ct. 276 (1998).

11. Amicus Curiae Brief of NAIC on Behalf of Appellant at 7, *State Farm Mut. Auto. Ins. Co. v. Speroni, et al.*, 119 S. Ct. 276 (1998).