

PUBLIC RECORDS, BAD FAITH, AND THE ARIZONA DEPARTMENT OF INSURANCE

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1. Introduction

To carry out its statutory responsibilities, the Arizona Department of Insurance conducts both targeted and full scale examinations of insurers, reviews financial documents filed with the Department of Insurance, collects rate and policy form information from insurers, investigates consumer complaints filed against insurers and other regulated entities, and investigates insurance fraud through a dedicated Fraud Unit whose investigators are licensed peace officers under Arizona law.¹ The Department is funded by a legislative appropriation but also makes extensive use of outside independent contractor examiners for the purpose of conducting financial and market conduct examinations.²

The Director may conduct examinations and investigations of insurance matters, investigate adjusters, agents and brokers, hold hearings for any purpose deemed by him or her to be necessary, and take depositions, subpoena witnesses for documentary evidence, administer oaths, and examine any person relative to the subject of any hearing or investigation.³ In some cases the Director may even obtain access to the records of entities over which the Department has no direct regulatory authority.⁴

2. Public Records

Arizona's public record laws require that the permanent public records of the State be maintained in a manner which conforms to the standards established by the Director of the Arizona State Library, Archives and Public Records.⁵ All state public records are, as a general rule, open to inspection by any person at all times during office hours.⁶ The public records laws provide the framework pursuant to which public documents must be maintained, the manner in which requests for access to public records must be accommodated and the method for redress should such a request be denied.⁷ Although the public records laws create a presumption in favor of disclosure, this presumption is rebuttable.⁸

In addition to the general public records laws, the insurance laws contain specific provisions regarding the maintenance of those records in the possession of the Department of Insurance. All public records maintained by the Department of Insurance are open to public inspection in accordance with A.R.S. § 39-121, except as otherwise provided.⁹ That same provision also specifically states that the Director *may* destroy records pursuant to §§ 41-1347 and 41-1351.¹⁰ These provisions of the library, archives and public records laws provide in essence that public records shall not be destroyed or disposed of unless it is determined that the records have no further administrative, legal, fiscal, research or historical value.¹¹ The Department of Insurance has interpreted this provision to allow it to make record destruction decisions on a case by case basis and to use a "common sense" approach to determine whether or not a document has further "administrative, legal, fiscal, research or historical value." Since no formal record retention or destruction policy or rule has been promulgated by the Department of Insurance, whether or not a particular document is in the possession of the Department must generally be determined by means of a public records request or inquiry. A copy of the Department's Public Record Request Form can be found on the Department's website.¹²

Notwithstanding the very broad scope of the Arizona public records laws, and the corresponding provisions of the insurance laws, the insurance statutes contain a number of exceptions and modifications to the general disclosure provision, some of which are statutory and some of which are regulatory in nature. For example:

1. All documents, materials or other information which are obtained by the Department in the course of a filing, examination or investigation made pursuant to certain provisions of the Arizona insurance holding company system statutes are confidential, privileged, not subject to the public records law and not subject to subpoena.¹³ These filings, examinations and investigations include:

- (a) A “Form A” made by a person seeking to obtain control of an Arizona domestic insurer;¹⁴
- (b) Request for approval of transactions between an Arizona domestic insurer and one of its affiliates;
- (c) a request for approval of an extraordinary dividend by a domestic insurer;
- (d) the examination of a registered insurer¹⁵ or its affiliate.¹⁶

The Director may nonetheless make these records public if it is determined that the interest of policyholders, shareholders or the public would be served by publication.¹⁷ The Director also has the authority to share non-public documents with other regulatory agencies which warrant similar authority to maintain the confidentiality of the protected documents.

2. The Department must treat as confidential or privileged those documents it receives from the NAIC, its affiliates and subsidiaries, or from regulatory or law enforcement officials in other jurisdictions which are confidential or privileged under the laws of the jurisdiction from which the documents are received.¹⁸

3. As a general proposition, documents which the Director obtains as a result of an investigation conducted by the Fraud Unit are privileged and confidential during the pendency of the investigation.¹⁹ Similarly, the identity of a Fraud Unit informant is considered to be confidential, as is the information that might identify the informant, unless that information is requested by a law enforcement agency, the Attorney General or a county attorney for purposes of a criminal investigation or prosecution.²⁰ The Director must notify an insurer of any public record request or subpoena related to documents the insurer referred to the Fraud Unit in order that the insurer may have the opportunity to assert any applicable privileges in an appropriate judicial proceeding.²¹ This requirement does not apply to a subpoena issued by the Attorney General or a county attorney.²²

4. The policy effective dates of surplus lines coverages procured by a surplus lines broker and reported to the Department of Insurance are not subject to public inspection.²³

5. Any information which is disclosed by an insurer to certain authorized agencies conducting an investigation into automobile theft, fire or arson must be held in confidence until such time as the information is released as required by law or used pursuant to a criminal or civil proceeding.²⁴

6. In addition to these statutory grants of confidentiality, the Department also treats a number of other types of documents and information as being beyond the scope of the Public Records Act. These include, for example:

- financial, medical or personal information in the possession of the Department of Insurance, such as Social Security numbers, dates of birth, medical records, checking account numbers, and similar records which would be considered personal records or information;
- Department work papers reflecting internal policy deliberations;
- any material subject to the attorney-client privilege.

3. *Litigation*

Needless to say, litigation in its various forms often involves some aspect of insurance coverage or insurer conduct. While information in the possession of an insurer or that which has been filed with the Department of Insurance, or obtained by the Department of Insurance from an insurer during an investigation or examination, may be of value in a particular lawsuit, obtaining that information from the Department of Insurance is one thing – using it in litigation involving an insurer is, of course, often quite another. In addition to insurance bad faith and related causes of action,²⁵ insurers are often called to respond to a variety of different kinds of cases including:

- reinsurance coverage litigation;
- rescission claims;

- uninsured and underinsured motorists coverage claims;
- subrogation claims;
- coverage questions;
- utilization review decisions;
- lien related litigation;
- suits involving non-insurers which are regulated by the Department of Insurance;
- suits arising out of or related to Fraud Unit Investigations;
- cases relating to the cancellation or non-renewal of insurance;
- claims relating to the Health Insurance Portability and Accountability Act (HIPAA);
- claims relating to healthcare insurer liability for alleged failure to authorize medically necessary healthcare services or denial of payment of benefits.

In many of the cases described above, it could be beneficial for a party to a lawsuit to obtain information in the possession of the Department of Insurance relating to a particular insurer or another entity regulated by the Department of Insurance. While there is considerable information in the possession of the Arizona Department of Insurance which might be useful in the course of litigation, whether that information is in fact available to the litigant depends upon several factors, including whether it remains in the possession of the Department, whether it was destroyed as a result of the Department's public record destruction practices, whether it falls within one of the exceptions to the public records laws, and whether the litigant's request is sufficiently refined to result in the location and disclosure of the document by the Department of Insurance. And of course, whether the document ultimately obtained from the Department is admissible in the proceeding for which it is sought is another question altogether. While these evidentiary issues are beyond the scope of this article, it might be useful to discuss one particularly significant case addressing an issue common to most states which have adopted the Model Uniform Claim Practices Act.

As discussed above, although the Department conducts many types of examinations and investigations, market conduct examination results have always been of particular interest to litigants in bad faith cases. Arizona law has recognized the tort of bad faith since 1981 when the Arizona Supreme Court, concluded that bad faith occurs "when the insurance company intentionally denies, fails to process or pay a claim without a reasonable basis for such action."²⁶ During market conduct examinations of insurers, Department examiners often look very closely at information directly related to the manner in which an insurer underwrites its coverages, deals with its policyholders generally and, perhaps most importantly, administers its claims.

The standards which the Department employs in addressing these issues include several provisions of the Arizona insurance laws, but often focus on the unfair claims settlement practices act ("UCSPA") and the corresponding regulation.²⁷ The UCSPA is based upon – but not identical to – the NAIC model Unfair Claims Settlement Practices Act. The law imposes a *regulatory* standard of conduct required of insurers and provides specifically that a person shall not commit or perform certain prohibited acts with such a frequency to indicate a general business practice.

While the results of the Department's market conduct examinations would obviously provide potentially valuable information for counsel seeking redress against an insurer in a bad faith case, the use of that information in a civil lawsuit in Arizona has proven problematic. Arizona law provides that:

Nothing contained in this section is intended to provide any private right or cause of action to or on behalf of an insured or uninsured resident or non-resident of the State. It is, however, the specific intent of this section to provide solely an administrative remedy to the Director for any violation of this section or rule related thereto.²⁸

This language reflects an intent consistent with that of the NAIC Model Law, to provide solely a *regulatory* remedy for insurer conduct not in compliance with the USCPA.

This issue was addressed in Arizona in the case of *Melancon v. USAA Casualty Insurance Company*.²⁹ In that 1992 case, after a jury trial, the Plaintiff insureds, Ralph and Kristin Melancon, were awarded damages, including punitive damages, against their insurer USAA Casualty Insurance Company, for breach

of contract and breach of the duty of good faith and fair dealing. On appeal, USAA argued that the court's instructions to the jury regarding the breach of the duty of good faith claim erroneously characterized Arizona law by quoting regulation R4-14-801 (now A.A.C.R. 20-6-801), the regulation promulgated by the Arizona Department of Insurance to implement the provisions of the UCSPA. The jury instructions stated that “under Arizona law” an insurer must respond to a Claimant within a certain time period if a response is reasonably expected and an insurer cannot deny a claim on the grounds of a specific policy provision unless that provision is identified in the insurer’s denial, quoting verbatim from the regulation.³⁰ The court noted that both A.R.S. § 20-461 and the regulation adopted to effectuate that law provided “solely an administrative remedy to the Director...” and that the “clear and unambiguous language” of the law does not create a private right or cause of action.³¹ The court pointed out that the law was intended to provide the Department with “guidelines for determining whether an insurer’s procedures and practices occur with such frequency as to indicate an unacceptable general business practice [and the] provisions of R4-14-801 are expressly not a standard of conduct against which an insurer’s conduct in handling an individual claim is to be measured [for judicially] creating a claim for relief.”³² The court reversed the jury’s verdict, including the associated punitive damages, by virtue of the fact that the “trial court erred in instructing the jury based on language taken directly from rule R4-14-801, thereby serving to create a private right of action in direct contravention of the act....”³³

It is clear, therefore, that under the current state of the law in Arizona, findings by the Department of Insurance that an insurance company violated the provisions of the UCSPA or the corresponding regulation cannot be used to establish a standard of conduct against which an insurer may be measured in determining whether or not its handling of a specific individual claim constituted bad faith. However, there have been no similar decisions with respect to the treatment of bad faith claims under the workers’ compensation laws.

A.R.S. § 23-930 grants to the Industrial Commission of Arizona exclusive jurisdiction over complaints involving bad faith by an employer, self-insured employer, insurer or claims processing representative regarding the administration of workers’ compensation claims.³⁴ That same statute gives the Industrial Commission the authority to assess penalties for violations and to adopt rules defining unfair claims practices and bad faith. Interestingly, Subsection F of that statute provides that the law is not to be construed as “limiting or interfering” with the authority of the Department of Insurance to regulate insurers including specifically the jurisdiction of the Department over unfair claims settlement practices as provided in A.R.S. § 20-461.³⁵ Since the adoption of this law, the Arizona Supreme Court has held A.R.S. § 23-930 does not result in exclusive jurisdiction over bad faith claims being granted to the Industrial Commission. At this point, therefore, the question of whether or not a violation of the Industrial Commission’s standards of insurer conduct would provide a standard against which an insurer’s conduct could be measured in an appropriate bad faith case has not yet been answered by the courts.³⁶

End Notes

¹ A.R.S. § 20-466.

² A.R.S. § 20-156.

³ A.R.S. §§ 20-142, 20-156, 20-161.

⁴ A.R.S. § 20-481.20(A).

⁵ A.R.S. § 39-101(A).

⁶ A.R.S. § 39-121.

⁷ A.R.S. § 39-121.01 et seq.

⁸ *Scottsdale Unified Sch. Dist. No. 48 v. KPNX Broad. Co.*, 191 Ariz. 297, 301, 955 P.2d 534,538 (1998).

⁹ A.R.S. § 20-153

¹⁰ A.R.S. § 20-153(B).

¹¹ A.R.S. § 41-1347.

¹² <http://www.id.state.az.us>

¹³ A.R.S. § 20-481.21(A).

¹⁴ A.R.S. § 20-481.02 et seq.

¹⁵ Every insurer authorized to do business in Arizona which is a member of an insurance holding company system, i.e. which has affiliated non-insurance entities, must register with the Director after it becomes subject to registration and again by March 31 of each year.

¹⁶ The Department's examination authority under A.R.S. § 20-481.20 extends to the records of non-insurance affiliates of a registered insurer and the Department has the authority to require the production of documents from the affiliate if the insurer fails to comply with an order for production. *See*, A.R.S. § 20-481.20(A).

¹⁷ A.R.S. § 20-481.21(A).

¹⁸ A.R.S. § 20-481.21(B)(2).

¹⁹ A.R.S. § 20-466(E).

²⁰ *Id.*

²¹ *Id.*

²² *Id.*

²³ A.R.S. § 20-408.

²⁴ A.R.S. § 20-466.

²⁵ For an excellent analysis of causes of action related to insurance bad faith, see *Bad Faith Litigation in Arizona*, National Business Institute (2004).

²⁶ *Noble v. National American Life Insurance Co.*, 128 Arizona 188, 624 P.2d at 866 (1981).

²⁷ *See* A.R.S. § 20-461; *See also* A.A.C.R. 20-6-801.

²⁸ A.R.S. § 20-461(D).

²⁹ 174 Arizona 344, 849 P. 2d 1374 (Ariz. App. 1992)

³⁰ *Melancon*, 174 Arizona at 346, 849 P.2d at 1376.

³¹ *Id.*, at 348, 849 P.2d at 1378.

³² *Id.*, at 347, 849 P.2d at 1377.

³³ *Id.*, at 348, 849 P.2d at 1378.

³⁴ A.R.S. § 23-960

³⁵ A.R.S. § 23-930(F)

³⁶ *Hayes* 178 Ariz. at 264,872 P.2d at 668.