Chapter X—Closing Continuum Actions

The process for continuum actions from inception to closing may be divided into four phases: (1) a "Fact Finding Phase" in which insurance department personnel are gathering facts[1] from the regulated entity and other sources[2]; (2) a "Violation Analysis Phase" in which the insurance department is applying the law to the facts in an effort to determine if any violations of the law have occurred; (3) a "Remedial Phase" in which the insurance department seeks appropriate remedies for any violations of the law; and (4) a "Reporting Phase" in which the insurance department reports the resolution of the continuum action to interested parties.

A. The Fact Finding Phase

Continuum actions involving the gathering of information from regulated entities regarding their activities can be divided into continuum actions that are undertaken pursuant to the insurance department's investigation authority and those that are undertaken pursuant to the insurance department's examination authority.

1. Continuum Actions under Investigation Authority

Chapter 2—Continuum of Regulatory Responses of this handbook lists a number of actions in the section titled "Contact with the Regulated Entity" that may be undertaken by an insurance department under its investigation authority[3]. Continuum actions under the investigation authority may be initiated on an informal basis (e.g., writing a letter to a company requesting information about an activity) or they may be part of a formal market regulation investigation as described in Chapter 7—Market Regulation Investigation Guidelines of this handbook. Regardless of whether the investigation is informal or formal, the end product of the Fact Finding Phase is generally a summary of findings from which a determination may be made in the next phase of the continuum action process. Depending upon the type of continuum action, the summary of findings may be as informal as a verbal discussion with a supervisor or may involve a more formal written memorandum or investigation report.

2. Continuum Actions under Examination Authority

Market conduct examinations are the continuum actions undertaken pursuant to an insurance department's examination authority. The types of market conduct examinations and the procedures used are discussed in great detail in other chapters of this handbook, so they will not be described in detail here. While variations in the market conduct examination process may occur due to variations in state law, the Fact Finding Phase generally concludes with a draft examination report being filed with the insurance department by the exam team conducting the examination along with a response to the draft examination report being filed by the entity examined.

[1] Facts may be gathered through the entire continuum process beginning with market analysis and extending to examinations.
[2] Some states may also utilize market regulation continuum actions to investigate entities operating illegally in a state. In such cases, fact finding may also extend to such illegally operating entities.
[3] Some states may take the position that all continuum activities from market analysis through examinations are conducted under their examination authority. For such states, the discussion of "Continuum Actions under Investigation Authority" in this chapter is intended to describe any continuum actions that these states may initiate under their examination authority other than actual market conduct examinations.

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B. The Violation Analysis Phase

Once the Fact Finding Phase is completed, the results are referred to insurance department personnel with the requisite authority to determine whether violations have occurred[4], which may vary depending upon the department's organizational structure. These insurance department personnel review the facts and apply the relevant laws to those facts in an effort to analyze whether or not the facts demonstrate a violation of the insurance laws. In performing this analysis, the insurance department personnel must apply the standards imposed by the language of the state's laws.

1. Laws Requiring Intent vs. Laws without Intent Language

In a legal context, "intent" is "[a] state of mind in which a person seeks to accomplish a given result through a course of action." *Black's Law Dictionary, Sixth Edition*, p. 810 (1990). Some laws have as a component of the violation that the prohibited action must be done with some level of intent. Laws that describe the prohibited action as being done "knowingly," "willfully" or "in conscious disregard" are laws that require the facts to demonstrate some intent on the part of the regulated entity in order for the entity's action to be considered a violation. Intent "can seldom be proved by direct evidence, but must ordinarily be proved by circumstances from which it may be inferred." Id. For example, evidence that behavior contrary to the law had previously been brought to the regulated entity's attention but it had done nothing to change its behavior would be circumstantial evidence that it acted with intent. Where intent is a necessary element of the prohibited conduct in the law, there is no violation if no evidence is found indicating intent on the part of the regulated entity.

By contrast, some laws contain no language indicating a requirement for intent on the part of the violator. In applying such laws to the facts, all that need be shown in order to show a violation of the law is that the regulated entity engaged in the prohibited conduct.

2. Frequency Based Violations vs. Non-Frequency Based Violations

For some insurance laws, the question of whether a violation has occurred is dependent upon whether the regulated entity committed the prohibited conduct with sufficient frequency. Two examples of this type of law are the *Unfair Trade Practices Act* (#880) and the *Unfair Claims Settlement Practices Act* (#900). Both of these model laws indicate that a violation may be found if the regulated entity commits any of the actions defined in the laws "with such frequency to indicate a general business practice to engage in that type of conduct." When conducting compliance testing for activities regulated by these two model laws, states frequently utilize benchmark error rates. The presumption of a business practice violation is created when the ratio of errors to the total number of files tested exceeds these benchmark error rates. States vary in the benchmark error rates they use.

When analyzing the facts for the existence of a business practice, however, the reviewer should be careful not to slavishly rely upon the benchmark error rates. A business practice may be shown by other evidence. For example, a test for claims practices may uncover only one error out of a field of 100. The resulting error rate of 1% may be less than the state's benchmark error rate for claims practices, but a review of the company's claims processing manual shows that all claims of the type that was noted as an error will be processed in this way. Therefore, the combination of the claims processing manual and the single found error demonstrate that it is the company's business practice to incorrectly process all claims of that type in violation of the law despite the test error rate of only 1%.

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[4] Some states will initiate a continuum action where a substantive error occurs even though a statute or regulation does not actually address the conduct. In such cases, the analysis phase may only involve a consideration of what actions, if any, the insurance department may be able to take.

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Many other insurance laws are not based upon the frequency of committing the prohibited conduct. For these laws, a single instance of the prohibited conduct would constitute a violation. Such laws are the type of laws with which the average person is most familiar. For example, the laws against exceeding the speed limit do not say that one must exceed the speed limit a certain number of times before the law is violated; you will receive a ticket for a violation each time a policeman catches you speeding.

Similarly, some states have not included the "business practice" language when enacting the *Unfair Trade Practices Act* (#880) and/or the *Unfair Claims Settlement Practices Act* (#900). In these states, a violation occurs each time the regulated entity commits any of the acts prohibited by the statute regardless of whether it occurred once or one hundred times.

3. Violations of Prior Orders or Agreements

Some state laws make it a separate violation to fail to comply with an order or agreement not to behave in a certain way. For example, an insurance company may have entered into a settlement agreement with an insurance department not to process claims in a way that violated insurance law due to a finding of such violations in a market conduct examination. In a subsequent market conduct examination, it was discovered that the insurance company had continued to process claims in this way despite its agreement not to do so. If the state has a law making the company's failure to comply with the settlement agreement a violation, the company in this instance would be guilty of violating both the claims practices law it had previously violated as well as the law against failing to comply with a settlement agreement.

C. The Remedial Phase

The actions taken in this phase of the process are a function of what was determined in the Violation Analysis Phase.

1. No Violations Found

Where no violations are found, there is nothing to remedy, and the continuum action is usually closed without further action. How this occurs is a function of the type of continuum action. Actions under the investigation authority may or may not have prescribed processes under the state's laws, so closing may or may not involve communication of the resolution to the regulated entity. The market conduct examination process is usually more formalized. While the exact process depends upon a state's law, it usually involves something similar to the *Model Law on Examinations* (#390): (1) finalizing the exam report; (2) adoption of the exam report; and (3) forwarding of the adoption order and finalized exam report to the regulated entity examined.

Alternatively, if the regulator conducting the Violation Analysis Phase determines there is insufficient evidence of a violation, but there is reason to believe that it would be appropriate to gather additional facts, he or she could reopen the Fact Finding Phase. The degree of formality with which the Fact Finding Phase is reopened is a function of the state's law and the insurance department's procedures. The *Model Law on Examinations* (#390)specifically provides two options for reopening the Fact Finding Phase for market conduct examinations by authorizing the insurance commissioner to (1) reject the examination report with instructions to the examiners to reopen the examination to gather additional information or (2) call for an investigatory hearing for the same purpose.

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2. Violations Found

Actions taken when violations are found depend upon the nature of the violations and the circumstances of the continuum action.

a. Resolution with Instructions to Cure any Violations Found

If violations are found that do not rise to a level requiring disciplinary action, a continuum action may be closed with instructions to the regulated entity to take action to bring itself into compliance with the law. Depending upon a state's laws, this directive to comply for continuum actions under an insurance department's investigation authority could be as informal as a verbal instruction or letter or as formal as a department order. Market conduct examinations usually have more formal procedures that may vary by state. For example, the *Model Law on Examinations* (#390) provides that "the commissioner may order the company to take any action the commissioner considers necessary and appropriate to cure the violation" in those states that have enacted it.

b. Voluntary Settlement

The majority of continuum actions where violations are found and disciplinary action is deemed appropriate are resolved through a voluntary settlement. Voluntary settlements allow the insurance department and the regulated entity to avoid the time, trouble and expense of litigation. While state laws may vary as to the process, voluntary settlements usually involve a negotiated settlement agreement and/or appropriate departmental orders, such as consent orders, encompassing one or more of the following remedial measures.

(1) Retrospective Remediation

To address past violations, a voluntary settlement may require the regulated entity to take steps to remedy its past practices, including the payment of restitution where appropriate. For example, a company that had been improperly denying claims may be required to reprocess and pay previously denied claims, including applicable interest, in order to make affected consumers whole.

(2) Prospective Remediation

To ensure that violations do not continue to occur, a voluntary settlement may require the regulated entity to cease and desist from engaging in the prohibited conduct and to develop a plan to ensure future compliance. The voluntary settlement may also require the regulated entity to perform self-audits of its compliance measures.

(3) Monetary Fines

A voluntary settlement may include a requirement for the regulated entity to pay a fine for the violations of law. The calculation of a fine should be based upon the provisions of state law, which may allow for the consideration of various aggravating and mitigating circumstances.

(a) <u>Intent as an aggravating or mitigating factor</u>: While intent may be an element of determining whether or not a violation has occurred for some laws, other laws may utilize intent as a mechanism to enhance or reduce the fine. In such instances, evidence showing that the regulated entity acted with intent (e.g. "knowingly," "willfully" or "in conscious disregard") would involve the imposition of a higher fine and lack of a showing of intent would lead to a lesser fine.

(b) <u>Business practice violations</u>: For laws that are not frequency based, the fining provision of state laws usually regard each instance of conduct contrary to the law as being subject to a separate fine. Frequency based business practice laws, however, may vary in how a fine is calculated. Some state laws may regard the business practice as a single violation subject to a single fine. Other state laws may regard the business practice standard as merely a threshold. Once a

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business practice is established under this threshold view, each act making up the business practice is considered a separate violation subject to a separate fine.

(c) Violation of prior agreements or orders as an aggravating factor: As noted above, a regulated entity's failure to comply with a prior agreement or order may be regarded as a separate violation subject to a separate fine under some state's laws. Additionally, this failure to comply may also be regarded as evidence of intent and an aggravating factor leading to increased fines for the underlying conduct that is contrary to the prior agreement or order.

(d) Behavior of the regulated entity as a mitigating or aggravating factor: Where the insurance department has some discretion to calculate fines within a range, the behavior of the regulated entity both before and during the continuum action may act as either a mitigating or aggravating factor. Cooperation with the continuum action, efforts to identify and correct problems prior to the continuum action being initiated or self-reporting of a violation are examples of behavior that may justify a lower fine within the range. Lack of cooperation, obstruction or evasion by the regulated entity are types of behavior that may justify increases of the fine within the range.

(e) Level of harm as an aggravating factor: The severity of financial or other harm to affected persons caused by the violations may act as an aggravating factor in calculating a fine, as opposed to technical violations that cause no apparent harm. Some state laws specifically recognize the amount or type of harm as an aggravating factor allowing an enhancement to the amount of fine imposed.

(4) Suspension or Revocation of License

Where violations are particularly egregious, a voluntary settlement may include the suspension or revocation of the regulated entity's license. Some state laws may allow a voluntary settlement to include a period of probation in lieu of a suspension or revocation of the license.

(5) Monitoring and Reporting

A voluntary settlement will likely include a requirement that the regulated entity provide the insurance department with reports on its retrospective and prospective remedial activities. Such reports may be at the completion of the remediation or may be required periodically if the voluntary settlement includes a monitoring period. After remedial measures are completed and any monitoring period has ended, the insurance department may determine that a follow-up investigation or examination is appropriate to audit compliance with the terms of the voluntary settlement.

c. Initiate an Administrative or Court Proceeding

Where the insurance department and the regulated entity cannot resolve a continuum action through a voluntary settlement, the insurance department may decide to initiate a formal proceeding. This may be either an administrative proceeding or a court proceeding depending upon the state's laws. In either case, it is important to realize the Fact Finding Phase starts anew given that either side may seek to do discovery (e.g., depositions, interrogatories or requests for production of documents) and the administrative hearing officer or judge will make his or her own findings of fact based upon the evidence presented at a hearing. After the hearing, the administrative hearing officer or judge will enter an order setting forth findings of fact and conclusions of law as to whether violations exist. This order may also impose some of the same kinds of disciplinary actions discussed above for voluntary settlements if the administrative hearing officer or judge agrees that violations exist, but if the administrative hearing officer or judge does not agree that violations exist, no discipline will be imposed. Either party may appeal the order through the court system if they are not happy with the result. This may lead to a protracted period before the continuum action is resolved unless the parties decide to negotiate a voluntary settlement at some point during the process.

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d. Referral to the Market Actions (D) Working Group

If the findings of the continuum action indicate issues affecting multiple states, the insurance department may wish to refer the matter to the Market Actions (D) Working Group for collaborative action. A detailed discussion of this process may be found in Chapter 6—Collaborative Actions.

D. The Reporting Phase

Where appropriate, the results of a continuum action should be reported in accordance with the state's law and in the applicable NAIC database.

1. Publication of the Resolution as Authorized by State Law

The extent to which the resolution of a continuum action becomes a public record under a state's law may be dependent upon the type of continuum action.

a. Continuum Actions under Investigation Authority

Continuum actions under the investigation authority may not be considered public records under many state's laws unless some form of disciplinary action is imposed. Where disciplinary action is imposed, the settlement agreement and/or order for a voluntary settlement or the order entered pursuant to an administrative or court proceeding are frequently considered public documents[5]. Many insurance departments may wish to increase the dissemination of this information by posting the information on its website and issuing press releases.

b. Continuum Actions under Examination Authority

Finalized market conduct examination reports are generally considered public documents under state examination laws regardless of whether any violations were found or any disciplinary action was imposed. The "Continuum Core Competencies" for market conduct examinations in Appendix D of this handbook indicate that the publication of the final examination report should include the regulated entity's response to the examination report where allowed by state law. If disciplinary action is imposed, this will also likely include the settlement agreement and/or order for a voluntary settlement or the order entered pursuant to an administrative or court proceeding. As discussed above, dissemination of the final examination report and related documents to the public may occur through posting the information on the insurance department's website and the issuance of press releases.

2. Report the Resolution in the Market Actions Tracking System

The Market Actions Tracking System (MATS) was developed by the NAIC for tracking and reporting information regarding continuum actions to the other states. The resolution of any continuum action recorded in MATS should be entered into the system to share with other states.

3. Report any Disciplinary Action in the Regulatory Information Retrieval System

The Regulatory Information Retrieval System (RIRS) was developed by the NAIC to document and share information regarding disciplinary actions taken against regulated entities. If a continuum action results in disciplinary action, this information should be recorded in RIRS to share with the other states.

[5] While settlement agreements and orders may be considered public documents, any other information in the continuum action file (e.g., work papers, information received, communications, etc.) may still be accorded confidential status under the laws of many states. In particular, this is likely to be the case where a state conducts all of its continuum activities under its examination authority.

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4. Other Reporting Activities

The section titled "Closure" of Chapter 2—Continuum of Regulatory Responses of this handbook mentions other means of reporting on issues uncovered in a continuum action to interested parties, such as insurance department bulletins, consumer outreach and referrals to other law enforcement agencies. Where appropriate, these may be considered and implemented.

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