

**IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA**

JOEL ROSENBAUM	:	CIVIL ACTION
	:	
Plaintiff	:	
	:	
v.	:	
	:	
UNUM LIFE INSURANCE CO. OF	:	
AMERICA	:	NO. 01-6758
	:	
Defendant	:	
	:	

NEWCOMER, S.J. July , 2002

O P I N I O N

Presently before the Court is Defendant's Motion to Dismiss and Plaintiff's Answer. For the reasons outlined below, this Court will grant Defendant's motion, in part.

BACKGROUND

Plaintiff brought suit after being denied long-term disability insurance benefits under the Defendant's employee benefit plan, which is governed by the Employee Retirement Income Security Act (ERISA). Defendant moves to dismiss Plaintiff's state law claims by arguing ERISA preemption. With the exception of Count X, a bad faith claim brought under 42 Pa.C.S. § 8371 (Pennsylvania's bad faith statute for insurance claims), the

parties agree that Plaintiff's state law claims under the employee benefit plan are preempted.

DISCUSSION

In his Answer to Defendant's Motion to Dismiss, Plaintiff concedes that, with the exception of his bad faith claim (Count X), his state law claims (Counts I, III, V, VII, IX) are preempted by ERISA. I, therefore, dismiss these claims without further discussion and turn to the key issue before this Court, that is, whether Pennsylvania's bad faith statute for insurance claims, 42 Pa.C.S. § 8371, is preempted by ERISA. While this issue has not been addressed by the Third Circuit, this Court has, in the past, consistently answered this question in the affirmative. In fact, no court has yet found to the contrary. However, a new trend in the federal law, led by the United States Supreme Court's decision in Unum Life Insurance Co. of America v. Ward, 526 U.S. 358 (1999), and its recent decision in Rush Prudential HMO, Inc. v. Moran, 122 S.Ct. 2151 (2002), warrants a re-examination of this important question.

At the heart of this issue is ERISA's saving clause, which exempts from preemption "any law of any State which regulates insurance." ERISA § 514(b)(2)(A), 29 U.S.C. § 1144(b)(2)(A). The Supreme Court has applied the following two

prong approach in determining whether a statute “regulates insurance.” First, the Court considers whether from a “common-sense view of the matter,” the state statute in question regulates insurance. UNUM, 526 U.S. at 367. Second, the Court considers the following three factors in determining whether “the regulation fits within the ‘business of insurance’ as that phrase is used in the McCarran-Ferguson Act,” 59 Stat. 33, as amended, 15 U.S.C. § 1011 et seq.:

- (1) Whether the practice has the effect of transferring or spreading a policyholder’s risk;
- (2) Whether the practice is an integral part of the policy relationship between the insurer and the insured;
- (3) Whether the practice is limited to entities within the insurance industry.

UNUM, 526 U.S. at 367. UNUM marked a significant change in the application of the Common-sense/McCarran-Ferguson Test. For the first time, the Court explained that a state statute need not meet each of the McCarran-Ferguson factors in order to qualify for ERISA’s saving clause.¹ Id. at 373 (“[W]e reject UNUM’s assertion that a state regulation must satisfy all three

¹ Despite the guidance offered by UNUM and Rush, it is not clear whether a statute must satisfy more than one of the McCarran-Ferguson factors in order to be covered by ERISA’s savings clause. Further, the Third Circuit has not ruled on this issue.

McCarran-Ferguson factors in order to 'regulate insurance.'") Rather, the UNUM Court found that the McCarran-Ferguson factors are "'considerations to be weighed' in determining whether a state law regulates insurance." Id. This decision clarified the Court's previous rulings (i.e., Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41 (1987); Metropolitan Life Ins. Co. v. Massachusetts, 471 U.S. 724 (1985)), which have been solely interpreted to require compliance with each of the McCarran-Ferguson factors. UNUM, 526 U.S. at 373. Most recently, in Rush, the Supreme Court reaffirmed UNUM's holding by finding an Illinois State statute qualified under ERISA's saving clause by meeting two of the McCarran-Ferguson factors. Rush, 122 S.Ct. at 2163. We turn now to an application of the Common-sense/McCarran-Ferguson Test with regard to § 8371.

I. Common-sense View

A common-sense view of ERISA's saving clause clearly establishes that Pennsylvania's bad faith statute "regulates insurance" and is specific to the insurance industry. In fact, one need look no further than the statute's title, "Actions on insurance policies," in discerning its scope. Furthermore, the statute limits its application to "action[s] arising under an insurance policy...." Finally, the Pennsylvania Supreme Court has recognized a distinction between those remedies available at

common law and those available through the instant statute with regard to bad faith claims. The Birth Center v. St. Paul Companies, Inc., 787 A.2d 376, 403 2001 Pa. Lexis 2759 (Pa. 2001). The Court's holding in Birth Center emphasizes the particular focus of this statute concerning the insurance industry. Thus, it is clear that the legislative intent behind § 8371 was to "regulate insurance."

II. McCarran-Ferguson Test

A. Spreading Policyholder's Risk

Because it serves solely as a special damages section, it is doubtful that the provisions of § 8371 spread a policyholder's risk. Since the McCarran-Ferguson factors are mere guideposts and need not be unanimously met, we shall move on to a consideration of the second factor. Rush, 122 S.Ct. at 2163.

B. Integral Part of the Policy Relationship

This Court is mindful of its previous finding that § 8371 did not play an integral part in the policy relationship between the insurer and the insured. Zimnoch v. ITT Hartford, et al., 2000 U.S. Dist. LEXIS 2846, Civ.A. No. 99-6594 at *18 (E.D.Pa. March 14, 2000) (Newcomer, J.). However, in light of the Supreme Court's recent holding in Rush and this Court's

subsequent re-examination of UNUM, this Court concludes that its previous finding is no longer suitable.

In UNUM, the Supreme Court found that a California statute requiring an insurer to "prove prejudice before enforcing a timeliness-of-claim provision" created a mandatory contract term between the two parties. UNUM, 526 U.S. at 375. In Rush, the Court examined an Illinois statute requiring HMOs to provide independent review of disputes with primary care physicians, and to cover any costs deemed medically necessary by the independent reviewer. The Court found that the statute provided a "legal right to the insured" and an "obvious" contractual requirement which was "an integral part of the policy relationship." Rush, 122 S.Ct. at 2164. These cases suggest that a statute plays an integral part in the policy where it affords the parties rights or remedies other than those originally bargained for, in effect creating a new mandatory contract term.

Just as the statutory provisions in UNUM and Rush afford the parties rights or remedies other than those originally bargained for, § 8371 creates mandatory contract terms providing for special damages. Here, the insured gain the right to pursue the following remedies: punitive damages, attorney fees and a specified amount of interest. Therefore, the Court finds that the statute clearly plays an integral role in the policy

relationship.

Although other Supreme Court cases, such as Pilot Life, address preemption of bad faith claim law, this Court cautions the reader not to confuse the case at hand with cases like Pilot Life. In Pilot Life the Supreme Court found that the Mississippi law of bad faith did not satisfy the second factor of the McCarran-Ferguson Test. Pilot Life, 481 U.S. at 51. However, Pilot Life dealt with common law claims of bad faith unspecific to the insurance industry, while the bad faith claim before this Court is derived from a statute specific to the insurance industry. Id. Consequently, the Pilot Life Court found the bad faith law's connection to the policy relationship to be "attenuated at best" based on the fact that it was "developed from general principles of tort and contract law available in any Mississippi breach of contract case." Id. In addition, "the common law of bad faith does not define the terms of the relationship ... it declares only that, whatever terms have been agreed upon in the insurance contract, a breach of that contract may in certain circumstances allow the policyholder to obtain punitive damages." Id. In contrast, § 8371 provides particular remedies for incidents of bad faith and was designed exclusively for use in the insurance industry. Specifically, it allows the court to award a particular amount of interest, assess attorney's

fees and award punitive damages where breaches of insurance contracts are concerned.

C. Limited to Entities within the Insurance Industry

The third factor, which requires the statute to be limited to entities within the insurance industry, is satisfied for many of the same reasons that the statute satisfies the requirements of the common-sense test. Rush, 122 S.Ct. at 2164.

CONCLUSION

In conclusion, this Court finds that the Common-sense View Test is easily satisfied by § 8371. Furthermore, factors two and three of the McCarran-Ferguson Test are also satisfied. Therefore, this Court holds that § 8371 is not preempted by ERISA as it falls under ERISA's saving clause.

AN APPROPRIATE ORDER WILL FOLLOW.

Clarence C. Newcomer, S.J.

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Plaintiff	:	
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v.	:	
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UNUM LIFE INSURANCE CO. OF	:	
AMERICA	:	NO. 01-6758
	:	
Defendant	:	
	:	

O R D E R

AND NOW, this day of July, 2002, upon consideration of Defendant's Motion to Dismiss (Document 2) and Plaintiff's Answer, it is hereby ORDERED that said motion is GRANTED, in part, and DENIED, in part. Specifically, Counts II, IV, VI and VIII are DISMISSED.

AND SO IT IS ORDERED.

Clarence C. Newcomer, S.J.