

State Laws Regulating Arbitration in Insurance Contracts

The following summary describes current state regulation of arbitration in insurance contracts as best as could be determined by a cursory electronic database search. This summary is not a substitute for research by a licensed member of an individual state's bar. Also, some state insurance regulators may use their discretion to strike arbitration clauses during policy form approval processes. But this does illustrate the deficiency in most states' insurance laws, as well as the interplay among state statutes, the Federal Arbitration Act (FAA), and the McCarran-Ferguson Act.

- **Twenty-four** states appear to have *no statute or regulation* in force prohibiting or restricting the use of arbitration in insurance contracts. **AZ, AK, CO, CT, FL, ID, IN, IA, ME, MI, MN, NV, NH, NJ, NM, NY, NC, ND, OH, OR, TN, TX, WI, WV**
- **Sixteen** states have statutes that seem to *prohibit any* enforcement of arbitration clauses by insurers. In those states, matters are complicated by the interplay among the Federal Arbitration Act, the McCarran-Ferguson Act, and the common law.

In **thirteen** of those states, the statute has either been upheld by the courts, or has not been challenged as pre-empted by FAA. **AR, HI, KS, KY, LA, MO, NE, OK, SC, SD, WA, VA**

In **three** of those states, **AL, MA, VT**, courts have found the statutes insufficient to prevent enforcement of the arbitration clauses against insurance consumers.

- **Seven** states' laws or courts have *restricted* the application of arbitration clauses. Disclosure for arbitration in HMO contracts: **CA**

No arbitration of bad faith claims: **IL, MT, PA**

No arbitration of uninsured motorist claims: **MS**

No arbitration for life insurance policies: **RI**

Non-binding arbitration only: **DE**

- **Three** states have regulations *restricting* the use of arbitration in insurance contracts: **MD, UT, WY**

NOTES:

Alabama:

Alabama statute, Section 8-1-41, Ala. Code 1975, provides that an agreement to submit a controversy to arbitration cannot be specifically enforced. In 1999, the Alabama Supreme Court held this statute does not "reverse preempt" Federal Arbitration Act (FAA) under provisions of McCarran-Ferguson Act as the Alabama Statute was not enacted for purpose of regulating the business of insurance and was not incorporated into law of insurance by statute deeming all contracts of insurance to have been made within state. *American Bankers Insurance Company of Florida v. Crawford*, 757 So.2d 1125 (1999). Also see *Southern United Fire Insurance Company v. Pierce*, 775 So.2d 194 (2000).

Arkansas:

Arkansas' version of the Uniform Arbitration Act (UAA) provides that its provision enforcing pre-dispute agreements to arbitrate shall have no application to personal injury or tort matters, employer-employee disputes, nor to any insured or beneficiary under any insurance policy or annuity contract. (ACA 16-108-201) The courts have not decided whether this statute will survive a claim of preemption pursuant to the FAA.

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California:

California has a statute making agreements to arbitrate medical malpractice disputes with HMOs invalid only if certain notice requirements are not complied with. October 25, 2001, the California Court of Appeals, 2d Appellate District, Division 3, ruled that the

McCarren-Ferguson Act overrides the FAA and precludes FAA's preemptive impact on the California statute requiring clear specific disclosures in the arbitration agreement in order to be enforceable. After examination of the relevant authorities, the Court concluded that the notice requirement constitutes a regulation of the business of insurance within the meaning of McCarran-Ferguson, not preempted by FAA, and therefore the failure of the Defendant to provide the required notice renders the arbitration agreement unenforceable. (*Smith v. Pacificare Behavioral Health of California, Inc.*, 93 Cal. App. 4th 139; 113 Cal. Rptr. 2d 140 (2001)).

Connecticut:

Connecticut has a broad version of the UAA, which provides for enforcement of pre-dispute agreements to arbitrate. (CGSA 52-408) In *Hutchinson v. Farm Family Casualty*, 2000 WL 435443, a United States District Court Judge enforced an agreement to arbitrate an uninsured motorist claim and held plaintiff's bad faith claim is an issue to be decided by the arbitrator.

Delaware:

Regulation 10 requires non-binding arbitration of claims against insurers. An adverse determination may be appealed to the Superior Court. Filing fees are limited to \$30.

Georgia:

Georgia Code 9-9-2 prohibits enforcement of arbitration clauses in any contract of insurance.

Hawaii:

HRS 431:10-221 prohibits any insurance policy from "depriving the courts of this state of the jurisdiction of actions against the insurer."

Illinois:

Illinois has a broad version of the UAA, which provides for enforcement of pre-dispute agreements to arbitrate. (IL ST CH 10, paragraph 101). The only exception is that this section is subject to the Health Care Arbitration Act. Illinois' statute on bad faith insurance claims practices appears to require that courts, not arbitrators, determine such matters. *American Service Insurance v. Passerelli*

Iowa:

Iowa's version of the UAA provides that its provision enforcing agreements to arbitrate "future controversies" shall not apply to contracts of adhesion, contracts between employers and employees, or, unless otherwise provided in a separate writing executed by all parties to the contract, any claim sounding in tort whether or not involving a breach of contract. (ICA 679A.1) A separate section of Iowa's Insurance Code provides, in part, that no recovery on a policy or contract of insurance shall be defeated for failure of the insured to comply, after a loss occurs, with any arbitration or appraisal stipulation as to fixing the value of property. (ICA 518A.26) The courts have not decided whether either statute will survive a claim of preemption pursuant to the FAA.

Kansas:

Kansas adopted the UAA with exceptions regarding pre-dispute agreements to arbitrate. (KSA 5-401) The Kansas statute says that provisions regarding arbitration of controversies "thereafter arising" shall not apply to: (1) Contracts of insurance, except for those contracts between insurance companies, including reinsurance contracts; (2) contracts between an employer and employees, or their respective representatives; or (3) any provision of a contract providing for arbitration of a claim in tort.

In *Friday v. Trinity Universal of Kansas*, 939 P.2d 869 (1997), the Kansas Supreme Court held that: (1) appraisal clause was arbitration clause and, therefore, unenforceable under statute making written agreement requiring submission of controversy to arbitration inapplicable to insurance contracts; and (2) McCarran-Ferguson Act prevented FAA from preempting the statute. The Court reasoned that the Kansas statute regulated the business of insurance even though it was not in the insurance code or in an act relating only to insurance, and, thus, the McCarran-Ferguson Act precluded application of the FAA.

Kentucky:

Kentucky's version of the UAA recognizes the validity of agreements to arbitrate controversies thereafter arising with two exceptions. (1) Arbitration agreements between employers and employees or between their respective representatives; and (2) Insurance contracts. (Excluding agreements to arbitrate between insurers, including reinsurers.) (KRS 417.050)

Although no court has specifically decided whether the "insurance contract" exception of this Kentucky statute survives a claim of preemption pursuant to the FAA, the United States Court of Appeals, 2d Circuit, held that a similar anti-arbitration provision in the Kentucky Liquidation Act was protected from preemption by the FAA under the McCarran-Ferguson Act. Because the Kentucky Liquidation Act is a state statute enacted "for the purpose of regulating the business of insurance" and is "designed to protect policyholders" under the McCarran-Ferguson Act, it is not preempted by the FAA. *Stephens v. American International Ins. Co., et al*, 66 F.3d 41 (1995)

Louisiana:

La. Revised States 22:629 prohibits any insurance policy from "depriving the courts of this state of jurisdiction of action against the insurer." In *Doucet v. Dental Health Plans*, 412 So.2d 1383 (1982) this provision was held to prohibit compulsory arbitration.

Maryland:

MD Insur. Admin. 31.11.10.07 ? bans arbitration in health insurance contracts:

- ✍ C. Arbitration. (1) A carrier may include a provision in a group health insurance contract or blanket health insurance contract giving the insured or the group policyholder the option of entering binding arbitration to settle a dispute with the carrier.
- (2) If the carrier includes the provision described in ?C(1) of this regulation, the provision may not require the insured or the group policyholder to enter binding arbitration.

Massachusetts:

M.G.L.A. 175 ? 22, prohibiting a policy of insurance from "depriving the courts of the commonwealth of jurisdiction of actions" against the insurer, was pre-empted by FAA. *DiMercurio v. Sphere Drake Ins.*, 202 F.3d 71 (2000)

Missouri:

Missouri's version of the UAA recognizes the validity of agreements to arbitrate controversies thereafter arising with two exceptions, contracts of insurance and contracts of adhesion. (V.A.M.S. 435.350) In *Standard Sec. Life Ins. Co. v. West* (WD Mo. 2001) 127 F. Supp.2d 1064, the 8thCircuit Court of Appeals decided that this Missouri statute rendering an arbitration clause in an insurance contract unenforceable fell within the protection of the McCarran-Ferguson Act, and thus, was not preempted by the FAA. According to the Court, common sense suggested that the statute regulated the business of insurance because it only exempted arbitration clauses of insurance contracts from enforceability.

20 Mo. Code of State Regulations 500-1.600

This regulation precludes insurers from issuing property and casualty insurance policies containing compulsory arbitration provisions. This regulation was adopted pursuant to the provisions of [sections 374.045, 379.203](#) and [435.010, RSMo](#).

- (1) Any contract or agreement entered into containing any clause or provision providing for an adjustment by arbitration shall not preclude any party or beneficiary under the contract or agreement from instituting suit or legal action on the contract at any time and the compliance with the clause or provision shall not be a condition precedent to the right to bring or recover in the action. A party is bound by an arbitration provision only when s/he elects to arbitrate and a lawful and binding arbitration follows.
- (2) No automobile policy written shall contain an arbitration clause applicable to disputed claims under uninsured motorist coverage and any provision to the contrary shall be void and of no effect as of August 22, 1974.

Montana:

Montana's version of the UAA authorizes enforcement of agreements to arbitrate arising between the parties after the agreement is made, but provides that this provision does not apply to: (a) claims arising out of personal injury; (b) any contract by individual for the acquisition of real or personal property, services, or money or credit where the total consideration is \$5,000 or less; (c) any agreement

concerning or relating to insurance policies or annuity contracts except for those contracts between insurance companies; or (d) claims for workers' compensation. (MCA 27-5-114)

In *Garretson v. Mtn. W. Farm Bureau Mut. Ins. Co.*, 234 M 103, 761 P2d 1288, 45 St. Rep. 1764 (1988), the Supreme Court of Montana decided that enforcement of an insurance contract providing for arbitration of disputes *concerning the value of the lost property* was specifically excluded from subsection (c) of their UAA. As a result, the Court then looked to Montana's common law for resolution of the issue. Pursuant to Montana's common law, agreements to arbitrate factual questions relating to value or quantity are enforceable, and, therefore, Farm Bureau's request for summary judgment is granted. The court's rationale would not apply to issues such as whether an insurer acted in bad faith.

Nebraska:

Section f (4) of Nebraska's UAA provides that the subsection making agreements to submit to arbitration any controversy thereafter arising valid and enforceable does not apply to any agreement concerning or relating to an insurance policy other than a contract between insurance companies including reinsurance contract. (Neb. Rev. St. 25-2602.01)

On December 13, 1991, the Nebraska Supreme Court held that the statute (Neb. Rev. St. 25-2601 et seq.) which authorizes binding arbitration of future disputes was unconstitutional. The Court said that the statute violates the open courts provision of the State Constitution. (The interesting question is whether the FAA trumps Nebraska's Constitution?)

Oklahoma:

Section 802 of Oklahoma's UAA provides that although agreements to submit to arbitration any controversy thereafter arising between the parties are valid and enforceable, this act shall not apply to collective bargaining agreements or contracts with reference to insurance except for those contracts between insurance companies.

In *Towe, et al v. Kansas City Fire & Marine Insurance Co.*, 947 P.2d 594 (1997), the Court of Civil Appeals, in dicta, recognized that pursuant to the McCarran-Ferguson Act, Oklahoma has the exclusive right to regulate "the business of insurance" in Oklahoma. It said that a state may, therefore, decide in its arbitration statute whether insurance matters are subject to arbitration. However, the Court concluded that the contract between this insurer and its employees or independent contractors was not a contract "with reference to insurance" and arbitration clauses in those contracts was enforceable.

In a related, recent case of *Conover v. Aetna US Healthcare, Inc.*, 2001 WL 1219481 (U.S. Dist. Ct., N.D. Okla., Aug. 2, 2001), the Court decided that an employee's state common law cause of action for bad faith against the insurance company does not sufficiently regulate insurance such that it falls within ERISA's savings clause and is, therefore, pre-empted by ERISA. The Court said the cause of action did not transfer policyholder's risk, was not integral part of the policy relationship, and had its origins in general principles of tort and contract law, and thus did not regulate insurance.

Pennsylvania:

Pennsylvania's version of the UAA contains no provision preventing the enforcement of arbitration agreements in insurance contracts. (PA ST 42 Pa. C.S.A. sect. 7301 et seq.) Pennsylvania's Superior Court held that claims pursuant to the state's bad faith insurance claims practices (42 Pa. C.S.A. section 8371) are required to be determined by the courts, not arbitrators. *Nealy v. State Farm*, 695 A.2d 790 (Pa. Super. 1997). But a federal court has held that the arbitrator could decide issues of bad faith. *Central Reserve Life v. Marelo*, 2000 WL 1474106 (E.D. Pa., Oct. 4, 2000)

Puerto Rico:

26 L.P.R.A. 1119 prohibits any insurance policy from "depriving the courts of Puerto Rico of jurisdiction of action against the insurer," applied to prohibit binding arbitration in *Berrocales v. Superior Court*, 102 D.P.R. 224 (1974).

South Carolina:

South Carolina's version of the UAA provides, in part, subsection (b) This chapter however shall not apply to: "(4) Any claim arising out of personal injury, based on contract or tort, or to any insured or beneficiary under any insurance policy or annuity contract." (SC ST Section 15-48-10)

In a recent decision, the Court of Appeals of South Carolina took up the question of whether this provision of the South Carolina Arbitration Act was saved from preemption by the McCarran-Ferguson Act. After reviewing many decisions from around the country on this issue, the Court concluded the "insurance exception" is an integral part of the policy relationship between the insurer and the insured because it expressly invalidates a provision contained in an insurance policy and sets forth the method for resolving disputes between the insured and the insurer. Through the exception, the legislature placed limits on the enforceability of an agreement to spread risk. Furthermore, this section is a specific exemption limited to entities within the insurance industry. Accordingly, the Court concluded, section 15-48-10(b)(4) "reverse pre-empts the FAA through application of the McCarran-Ferguson Act. (The Court also found that the arbitration exception is not applicable to fraternal benefits associations such as the Defendant. Thus, as the Defendant's contract provides for arbitration, the current dispute is subject to arbitration pursuant to the FAA.) Cox v. Woodmen of the World Ins. Co. 2001 WL 1007453.

South Dakota

SDCL 21-25A-3 provides that any insurance policy provision requiring arbitration or restricting enforcement of the policy by legal proceedings is "void and unenforceable." The Director of Insurance has held this to invalidate any clauses which require binding arbitration. Bulletin 98-5.

Texas:

In 1995, Texas amended its version of the UAA to delete, among other things, from the statute the exception that excluded insurance contracts and controversies arising thereunder from its coverage. (TX CIV PRAC & REM s 171.001 et seq.)

Utah:

Utah Code 31A-21-314 prohibits any insurance policy from "depriving Utah courts of jurisdiction over an action against the insurer, except as provided in permissible arbitration provisions."

U.A.C. R590-122, Utah Admin. R. 590-122

R590-122-4. Rule.

1. Compulsory non-binding arbitration is contrary to the public interest and is not a "permissible arbitration provision."
2. Optional binding arbitration at the exclusive election of an insured party is a "permissible arbitration provision," in which case the disclosure provisions in paragraph 5 below may not be applicable.
3. Both compulsory and optional binding arbitration at the election of either the insured or the insurer are "permissible arbitration provisions."
4. Policy forms containing optional binding arbitration provisions for the exclusive election of an insurer will be disapproved under Section 31A-21- 201(3)(a)(iv). Such provisions in previously approved forms are declared not enforceable. They will be construed under Section 31A-21-107 and applied as if in compliance with the Insurance Code.
5. Except as excluded in paragraph 2 above, each application or binder pertaining to an insurance policy which contains a permissible arbitration provision must include or have attached a prominent statement substantially as follows:
ANY MATTER IN DISPUTE BETWEEN YOU AND THE COMPANY MAY BE SUBJECT TO ARBITRATION AS AN ALTERNATIVE TO COURT ACTION PURSUANT TO THE RULES OF (THE AMERICAN ARBITRATION ASSOCIATION OR OTHER RECOGNIZED ARBITRATOR), A COPY OF WHICH IS AVAILABLE ON REQUEST FROM THE COMPANY. ANY DECISION REACHED BY ARBITRATION SHALL BE BINDING UPON BOTH YOU AND THE COMPANY. THE ARBITRATION AWARD MAY INCLUDE ATTORNEY'S FEES IF ALLOWED BY STATE LAW AND MAY BE ENTERED AS A JUDGEMENT IN ANY COURT OF PROPER JURISDICTION.
Such statement must be disclosed prior to the execution of the insurance contract between the insurer and the policy holder and, in the case of group insurance, shall be contained in the certificate of insurance or other disclosure of benefits.
6. Both compulsory binding arbitration provisions and optional binding arbitration provisions may not be construed to preclude any dispute resolution by any small claims court having jurisdiction.
7. All arbitration provisions contained in insurance policies shall be in compliance with the "Utah Arbitration Act" (Title 78, Chapter 31a).
8. Any such agreement for arbitration may not obligate any insured to pay more than 50% of the advance payments required to begin the arbitration process.
9. No arbitration provision may require that arbitration be held at a place further from the residence of the insured than the nearest location of a State Court of General Jurisdiction

Vermont:

12 V.S.A. Section 5653 Limitations, says, in part: "This chapter applies to all arbitration agreements to the extent not inconsistent with the laws of the United States. However, this chapter does not apply to labor interest arbitration, nor to arbitration agreements contained in a contract of insurance, ****"

October 10, 1997, the Vermont Supreme Court held that the FAA pre-empts VAA and makes irrevocable an agreement to arbitrate an UM coverage dispute. *Little v. Allstate Insurance Co.*, 167 Vt. 171, 705 A.2d 538). The Court said that the effect of the provision excluding from the VAA agreements contained in insurance contracts is to leave the law governing such arbitration agreements to the common law, which allows revocation of such an agreement at any time up to the publication of an award. However, as the Court said, the FAA prevails over Vermont common law as the supreme law of the land, unless reverse pre-empted by McCarran-Ferguson. The problem, according to the Court, is that Vermont's common-law rule making arbitration agreements revocable up to the time of award is not a **state law** regulating the business of insurance. So, the Vermont Legislature has not acted to make insurance arbitration agreements revocable. Therefore, the VAA provides no protection from enforcement of arbitration agreements in insurance contracts.

Virginia:

Va. Code Ann. 38.2-312 prohibits any insurance policy from "depriving the courts of this Commonwealth of jurisdiction in actions against the insurer," which the Virginia Insurance Commissioner, in Administrative Letter 1998-12, has ruled prohibits binding arbitration or appraisals.

Washington:

RCWA 48.18.200 prohibits any insurance policy from "depriving the courts of this state of the jurisdiction of actions against the insurer."

Wisconsin:

Arbitration clauses are reviewed as part of the form review process. OCI disapproves

arbitration clauses in health insurance products but they are permitted

in some other insurance products. Per Fred Nepple, General Counsel, Office of the Commissioner of Insurance.

Wyoming:

WY Rules and Regulations INS GEN Ch 23 s 9

Section 9. Mandatory Arbitration Clause

In no instance shall any uninsured motorists coverage circulated within the State of Wyoming contain a mandatory arbitration clause by which the insured is required to arbitrate an insurance claim in the event of disagreement with his insurer, nor shall any such clause require that the results of arbitration are binding on the parties without the right of appeal unless the parties themselves agree to be so bound by a separate agreement.