Approved _____
Date

MINUTES OF THE House COMMITTEE ON Insurance.

The meeting was called to order by Rep. Rex B. Hoy at
Chairperson

3:30 XX a.m./p.m. on February 27, 1986 in room 521-S of the Capitol.

All members were present except:
Rep. Gjerstad, excused
Rep. King, excused
Rep. Lowther, excused
Rep. Weaver, excused

Committee staff present:

Ms. Emalene Correll, Research Department
Ms. Melinda Hanson, Research Department
Mr. Gordon Self, Revisor's Office
Ms. Deanna Willard, Committee Secretary

Conferees appearing before the committee:

Ms. Margaret Angle, National Car Rental System, Inc.
Mr. Wayne Morris, Security Benefit Life
Mr. Richard Harmon, Kansas Life Association

The Chairman called the meeting to order.

Hearing on: HB 2719 - collision damage waiver contracts

Ms. Margaret Angle, appeared before the committee on behalf of the Ad-Hoc Committee on the Collision Damage Waiver Option. She said that all courts and attorneys general which have considered the issue have concluded that collision damage waiver options are not insurance. She distributed a presentation of the Ad-Hoc Committee prepared for a task force of the National Association of Insurance Commissioners which sets forth the aforementioned court and regulatory decisions. She contended that there was no need to regulate these options. (Attachment 1.)

She was informed that the bill was an effort to define the collision damage waiver options as insurance so they could be regulated.

She discussed the typical bailment contract; the renter is not responsible for normal wear and tear, only damage beyond a specified amount. The rental company waives its right to collect from the renter when a collision damage waiver is purchased. The renter has an option; he doesn't have to purchase the option; he could assume responsibility to pay for the car, if necessary. She said that in the event of a loss, the rental company incurs the loss if the option has been purchased, and she contended that a basic requirement of insurance is indemnification.

She said that this was enabling legislation to allow rental companies to sell collision insurance but that they did not wish to be in the business of selling insurance and were requesting that Subsection (m) be deleted. (Attachment 2.)

She was asked to explain how the rates for the options were set. Committee members expressed concern that rates were much higher than would be considered reasonable and that the rental companies are benefitting by the confusion of the consumer. She stated that there is a good consumer

protection act in Kansas that could be applied if one felt he had been unfairly dealt with concerning collision damage waivers.

She was asked by the Chairman if limiting the deductible to $500 might be an acceptable solution. She spoke of two freestanding bills that suggest that collision damage waivers be regulated, but she reiterated that they are not insurance and should not be treated as such. In response to a question as to what has triggered the paper, she stated that there had been some concerns from the vacation states.

Hearing on: HB 3007 - deposit of securities by life insurance companies

Mr. Wayne Morris, Security Benefit Life, spoke for this bill. He explained that Kansas law requires that all Kansas life insurance companies deposit securities and other assets with the Commissioner of Insurance sufficient to cover the entire amount of its net reserves in a vault in the State Office Building. This bill would permit companies to get a credit for investment income due and accrued on investments which are on deposit when calculating the deposit requirement. Also, the procedure for appraising real estate would be updated, and companies would be given the option of depositing real estate at its book value and avoiding the time and expense of obtaining an appraisal. (Attachment 3.)

He clarified for the committee that the life insurance company would still retain interest income. The bill would simply allow that it be considered part of the reserve and kept by the company rather than in the vault. The same level of deposits must still be maintained.

There was concern from the committee that this was a fairly significant change. Mr. Dick Brock, Kansas Insurance Department, said that it might dilute protection slightly.

There was discussion of the provision of Line 0210 that the Commissioner has authority to say that book value (defined on Lines 144-146) is not accurate and that a current appraisal must be obtained. (Such appraisals are paid for by the company.) In most instances the book value is the more conservative amount and is what would be shown on the annual statement.

Mr. Richard Harmon, Kansas Life Association, said that the bill has the support of the 18 domestic life insurance companies in the organization which he represents.

The minutes of the previous meeting were approved.

The meeting was adjourned at 4:50 p.m. by the Chairman.

GUEST LIST

COMMITTEE: Insurance DATE: 2-27-86

NAME	ADDRESS	COMPANY/ORGANIZATION
Dick Brock	Topeka	Fire Dept.
Wayne Morris	"	Security Benefit
Jane Tedder	"	"
Richard Harmon	"	KS Life Assn.
William W Sneed	"	KS Ass of Def. Counsel
Margaret S. Ayde	Nat'l Car Rental System Inc 7700 France Ave So, Mpls, MN 55435	AD HOC COMMITTEE ON CDW
Ron Clarke	St Louis	Household Intl Inc

National Car Rental System, Inc.
Law Department
7700 France Avenue South
Minneapolis, Minnesota 55435
612-830-2554

National Car Rental

A HOUSEHOLD INTERNATIONAL COMPANY

February 27, 1986

HAND DELIVERED

The Honorable Rex Hoy
Chairman
House Insurance Committee
Kansas Legislature

RE: Kansas House Bill No. 2719

Dear Chairman Hoy:

This letter in opposition to Kansas House Bill No. 2719 is written on behalf of the Ad-Hoc Committee on the Collision Damage Waiver Option, which includes the American Car Rental Association and the following companies:

Avis, Inc.
Budget Rent A Car Corporation
The Hertz Corporation
National Car Rental System, Inc.
Thrifty Rent-A-Car System, Inc.

Kansas House Bill No. 2719, if enacted, would define collision damage waiver contracts as insurance.

Collision damage waiver options are not insurance. All courts and attorneys general which have considered the issue have concluded that collision damage waiver options are not insurance. In addition, a committee of The National Association of Insurance Commissioners has determined that collision damage waiver options are not insurance. (Report to the Market Conduct Surveillance [EX3] Task Force, June 11, 1985).

Attached is the Presentation of the Ad-Hoc Committee on the Collision Damage Waiver Option which is being presented to the Market Conduct Surveillance [EX3] Task Force of the National Association of Insurance Commissioners. This Presentation fully sets forth the court and regulatory decisions which have concluded that collision damage waiver options are not insurance. The Presentation further demonstrates that collision damage waiver options are not insurance, and that there is no need to regulate these options.

The Ad-Hoc Committee on the Collision Damage Waiver Option and

Attachment 1
House Insurance
2-27-86

National Car Rental System, Inc. respectfully urge your committee to amend Kansas House Bill No. 2719 to delete Subsection 1(m) for all of the reasons set forth in the attached Presentation.

Sincerely,

NATIONAL CAR RENTAL SYSTEM, INC.

Margaret S. Angle
Senior Attorney
Law Department

MSA:bkd
Presentation w/attachments
cc: Ron Clarke (Presentation w/attachments)

THE COLLISION DAMAGE WAIVER OPTION

A Presentation

To

The Market Conduct Surveillance [Ex 3] Task Force

of

The National Association Of Insurance Commissioners.

Prepared by:

LeBoeuf, Lamb, Leiby & MacRae
on behalf of the Ad Hoc
Committee on the Collision
Damage Waiver Option
520 Madison Avenue
New York, New York 10022
(212) 715-8000

February 25, 1986

INTRODUCTION

The following statement is presented on behalf of the Ad-Hoc Committee on the Collision Damage Waiver Option, which includes the American Car Rental Association and the following companies:

Avis Rent A Car System, Inc.
Budget Rent A Car Corporation
The Hertz Corporation
National Car Rental System, Inc.
Thrifty Rent-A-Car System, Inc.

This statement is presented with the intention of providing comprehensive information to demonstrate that the collision damage waiver option is not insurance, and that there is no need to regulate further this option as federal and state statutes, regulations and court decisions exist which provide sufficient protection to consumers.

Respectfully submitted,

LeBoeuf, Lamb, Leiby & MacRae
on behalf of the Ad Hoc
Committee on the Collision
Damage Waiver Option
520 Madison Avenue
New York, New York 10022
(212) 715-8000

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PRELIMINARY STATEMENT

A large number of companies are engaged in the business of renting cars to the general public. Most, if not all, of these companies make available to the person renting the car an option which is commonly referred to in the car rental industry as a "collision damage waiver option" (hereinafter referred to as the "CDW option"). In accordance with long-standing industry practice, this option, if the renter elects to take it, provides that for an additional charge the rental company will waive its right to hold the renter responsible for collision damage to the rented vehicle.

The question of whether the CDW option is insurance was considered last year by the Advisory Committee to the Market Conduct and Consumer Affairs [Ex 3] Subcommittee. In its report, submitted to the Market Conduct Surveillance [Ex 3] Task Force, in Kansas City, Missouri, on June 11, 1985, the Advisory Committee concluded not only that the CDW option is not insurance, but also that the policy reasons for regulating insurance do not apply in the case of the CDW option.

In concluding that the CDW option is not insurance, the Advisory Committee noted that the CDW option lacks

both an indemnity element and a risk-spreading element. The relevant portions of this Report follow:

> The concensus [sic] of the majority of the Advisory Committee is that there is a real danger in calling something insurance simply because it is "insurance-like". Overall legal research by members of the Advisory Committee would indicate the genesis of various innovative products and services has often raised the issue as to whether they constitute insurance. A state insurance department's authority to regulate a given entity depends on whether it is carrying on the business of insurance. Thus, frequently the courts have been called on to decide whether a particular contract constitutes insurance.
>
> The nature of a contract as one of insurance depends upon its contents and the true character of the agreement itself. Insurance is a contract by which one party, for consideration, assumes particular risks of the other party and promises to pay a certain ascertainable sum on the happening of a specified contingency. It consists of a personal contract to pay another sum by way of indemnity to protect the interest of the insured. Insurance is a system for reducing risks through the transfer of that risk and the pooling of losses. It is a device in which the losses of a few are paid by many. Insurance transfers risk for a premium from one party to another. For an activity to constitute insurance it must combine a large number of independent exposure units with a common risk into an interrelated group.
>
> A number of states have statutorily defined the term insurance. Most follow California in sum and substance:

"Insurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown event." CAL.INS.CODE section 22.

The essence of insurance is the transfer of risk by a person to an insurer which reimburses the insured for covered losses. The existence of a risk and the transference of that risk and sharing of ensuing losses are vital elements of insurance. The critical inquiry as to whether a contract is one of insurance depends on whether the practice has the effect of transferring or spreading policyholders' risks. Union Labor Life Ins. Co. v. Pireno, 458 U.S. 119 (1982). The practice at issue must spread or transfer risk throughout the pool. It is this crucial element of risk spreading which is lacking in [the] collision damage waiver scenario. The collision damage waiver does not spread risk in the insurance sense.

The risk of loss of property is actually the risk of the rental company. Through contractual provisions it transfers the risk of loss to the renter. Through the operation of the CDW, the risk of economic loss remains with the rental car company. Through the operation of this rental agreement provision, the risk of loss never passes to the renter. In its most basic form, insurance is a contract where one party agrees to indemnify another for losses sustained. The concept of indemnification does not appear to be present in the collision damage waiver. Through the CDW the rental company does not agree to pay anything over to the renter. It merely agrees not to pursue its legal claim against the renter for the renter's failure to return the vehicle undamaged.

There is one additional approach to the review of insurance-like concepts such as CDW. Under that analysis one reviews the need for regulation presented by the product. Are the needs for regulation of the CDW the same as the needs for the regulation of typical insurance products? The primary need for regulation presented by the typical insurance product is the need to assure that the company will remain solvent in order to meet its financial obligations to indemnify the policyholders. There is no need for solvency regulation presented by the CDW. The car rental company will not be required in any situation to pay money over to the renter. The economic loss sustained is to the property of the rental company.

This lack of need for solvency regulation serves to highlight the most significant difference between the CDW and an insurance contract. Only the fact that the CDW is an intangible product, the economic value of which is not readily determinable at the time of the sale, makes it similar to insurance and different from most other consumer products. This fact does not seem sufficient to justify a finding that . . . CDW is an insurance product in need of insurance-type regulation.

Based on the above review of legal and insurance authorities, the Advisory Committee concludes that CDWs are not insurance, and therefore does not believe it is appropriate to convert what is only marginally an insurance-like product into insurance to solve suspected consumer abuse. (pp 2-3) (Emphasis added)

This position paper will demonstrate that the Advisory Committee's June 11, 1985 Report is correct. The CDW option is not insurance. Furthermore, this position paper will show that the CDW option and the companies which make it available are already sufficiently regulated by federal and state statutes, regulations and case law.

SUMMARY

The CDW option is not insurance, as demonstrated both by the statutory and common law definitions of the term. The CDW option is not insurance because (i) it is only an incidental and ancillary part of the rental contract, (ii) it is not aleatory and executory in nature, and (iii) it is not a contract of indemnity. Instead, the car rental contract is a bailment contract and the CDW option merely allocates risks inherent in the bailment contract, an allocation which does not give rise to insurance. All courts which have addressed this issue have held that the CDW option is not insurance.

There are public policy considerations which argue against the regulation of the CDW option, including the fact that it would be necessary for similar contracts to be regulated, which would consume limited insurance department resources. Finally, it is not necessary to regulate the CDW

option as federal and state laws and regulations already exist which are sufficient to protect consumers against alleged abuses.

ARGUMENT

POINT I

THE COLLISION DAMAGE WAIVER OPTION IS NOT INSURANCE

Proponents of regulation have argued that by offering the CDW option to car renters, car rental companies are engaged in the business of insurance and, being unlicensed to do so, are in violation of law. Point I of this position paper will demonstrate that car rental companies which offer the CDW option are not engaged in the insurance business.

(A) The Collision Damage Waiver Option Does Not Meet The Statutory Definition Of Insurance. All states which define insurance require that the following two essential elements be present for a contract to constitute a contract of insurance - (i) indemnification against a loss, and (ii) that a contingent event give rise to the indemnity.

One example, California, which is cited in the Advisory Committee's June 11, 1985 Report as being an example followed by other states in "sum and substance", is as follows:

> Insurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown event.

Cal. Ins. Code §22 (NILS 1983 & Supp. 1985).

A second typical example is Delaware. It defines "insurance", in relevant part, as:

> [A] contract whereby one undertakes to pay or indemnify another as to loss from certain specified contingencies or perils, called "risks," or pay or grant a specified amount or determinable benefit in connection with ascertainable risk contingencies . . . .

Del. Ins. Code §102(2)(NILS 1983 & Supp. 1985).

A third typical example is Arizona, which defines "insurance", in relevant part, as:

> [A] contract by which one undertakes to indemnify another or to pay a specified amount upon determinable contingencies.

Ariz. Ins. Code §20-103 (NILS 1983 & Supp. 1985).

A fourth typical example is Oregon, which defines "insurance", in relevant part, as:

> [A] contract whereby one undertakes to indemnify another or pay or allow a specified or ascertainable amount or benefit upon determinable risk contingencies.

Ore. Ins. Code §731.102 (NILS 1983 & Supp. 1985).

All these statutes clearly require the presence of (i) indemnification against a loss, and (ii) that a contin-

gent event give rise to the indemnity. As demonstrated in Point I(B) which follows, the CDW option contains neither of these elements.

(B) The Collision Damage Waiver Option Does Not Meet The Common Law Definition Of Insurance. According to the common law definition of insurance, there are a number of distinctive contractual features which, when they are present, signal the existence of an insurance contract. These distinctive contractual features, summaries of which follow, are absent in the case of the CDW option.

(1) The collision damage waiver option is only an incidental and ancillary part of the rental contract. As a general rule, in determining whether an insurance contract exists, one must first look to the essential nature and purpose of the entire agreement. Huff v. St. Joseph's Mercy Hosp., 261 N.W.2d 695 (Iowa 1978). When risk allocation is ancillary to the purpose of a contract, neither the contract nor its ancillary risk allocation provisions become contracts of insurance.

> [I]nsurance regulatory laws are not properly construed as aimed at an absolute prohibition against the inclusion of any risk-transferring-and-distributing provisions in contracts for services or for the sale or rental of goods . . . [with regard, for example, to contracts for the rental of motor vehicles], [e]ven if one finds an ele-

> ment of what he regards as insurance in such transactions as these, he may yet find that, because it is relatively insubstantial and is closely tied in with and incidental to the main objective of the transaction, it does not bring the transaction within the scope of the insurance regulatory laws as properly construed.

Keeton, Insurance Law 552 (West 1971). Accord Jordan v. Group Health Association, 107 F.2d 239, 245 (D.C. Cir. 1939).

The principal purpose of the contracts in question and the primary business in which the car rental companies are engaged is, obviously, the rental of automobiles. Korn v. Avis Rent A Car Sys., Inc., No. 1670, slip op. at 7 (C.P. Pa. February 10, 1977). The amount charged pursuant to the CDW option by no means constitutes the principal purpose of the rental contract, or even a major purpose of the transaction. Korn, at 7. The portion of the contract relating to the condition of the car upon its return is but of incidental and subordinate importance to the contract as a whole, Korn, at 7; Kramer v. Avis Car Leasing, Inc., No. 23344/82, slip op. (Sup. Ct. 1983), aff'd, No. 19118-19-19A-19B, slip op. (App. Div. N.Y. 1984). Inclusion of the CDW option is entirely voluntary. The car rental companies will rent cars whether or not the CDW option is exercised. Further, the CDW option cannot be offered independent of the

rental of the car because it is a waiver offered by the owner/car rental company to the renter.

(2) The collision damage waiver option is not aleatory and executory. All insurance contracts, as to an insurer, are executory and aleatory in nature. 12 Appleman, Insurance Law and Practice §7001 (1981 & Supp. 1984). The insurer's obligations are incomplete because they depend upon the occurrence of a future contingency. The CDW option, however, is unambiguous and certain. The instant the contract is entered into performance is completed and the parties' rights and responsibilities concerning the condition of the property at the time of its return have been fully defined. The responsibility for damage is not contingent upon any future event, nor is it in any way affected by what might occur to the vehicle.

(3) The collision damage waiver option is not a contract of indemnity. Another essential element of insurance contracts is the principle of indemnity. "A contract of insurance is a contract to indemnify the person or persons secured thereby, and is considered an indemnity contract." 12 Appleman, Insurance Law and Practice §7001 (1981 & Supp. 1984). A second leading treatise on the subject explains:

> Insurance, other than that of life or accident where the result is death, is a contract of indemnity, by which is meant that the party insured is entitled to compensation for such loss as has been occasioned by the perils insured against . . . .

1 Couch on Insurance 2d (Rev. ed.) §1:9 (1984 & Supp. 1985). The case law also makes clear that the element of indemnity must be present in order for insurance to exist. Haynes v. United States, 353 U.S. 81 (1957); Candell v. United States, 189 F.2d 442, 444 (10th Cir. 1951); State v. Timmer, 260 Iowa 993, 999, 151 N.W.2d 558, 561 (1967); Huff v. St. Joseph Mercy Hosp., 261 N.W.2d 695 (Iowa 1978); 1983 Op. Ins. Comm. Iowa (January 5, 1983)(Declaratory Ruling 1983-1). The CDW option, however, does not require any indemnification payment from the car rental company to the consumer or to anyone else. The CDW option merely provides that if the car is returned in a damaged condition the car rental company has waived its right to proceed against the renter, regardless of the extent of the collision damage sustained.

(C) The Car Rental Contract Is A Bailment Contract. The relationship between car rental companies and their customers is that of bailor and bailee. 8 C.J.S. Bailments §2 (1938 & Supp. 1985); 8 Am. Jur. 2d Bailments §33 (1980 & Supp. 1985).

At least two courts have concluded that the nature of the bailor-bailee relationship is not eliminated by the existence of a CDW option in the car rental contract. Korn v. Avis Rent A Car Sys., Inc., No. 1670, slip op. (C.P. Phila Co., February 10, 1977); Russell v. The Hertz Corp., 82 CH 6632, slip op. (Cir. Ct. Ill., February 28, 1983). In Korn the court reasoned:

> The overall transaction involved in the instant suit is the renting of automobiles. The CDW provision is an intricate part of the rental agreement and is offered merely to relieve the lessee from some potential liability. The arrangement is nothing more than a simple bailment.

Slip op. at 6-7.

Similarly, the Court in Russell summarily dismissed the complaint, holding that "[t]he collision damage waiver provisions contained in the standard rental agreements . . . constitute terms of a bailment agreement and not a contract of insurance." Opinions rendered by the Insurance Departments of Iowa and Texas are to the same effect.

(1) The collision damage waiver option merely allocates risks inherent in the bailment contract. In a letter dated January 4, 1977, the Office of General Counsel to the New York Department of Insurance described the obligations of the parties to a rental contract as follows:

> The parties to a rental agreement bear a relationship of bailor and bailee to each other. In the absence of an express contract, the law imposes an implied agreement to return the property in as good condition as when received by the bailee, ordinary wear excepted. If not returned in the same condition, the bailee has the burden of establishing that the damages to the bailed property were not caused by his negligence. The obligation of the bailee in this regard, however, may be enlarged or diminished by contract.
>
> By the terms of the typical rental agreement, the lessee is responsible for damage, but he may be relieved of this responsibility upon payment to the bailor of a specified consideration. If this is done, the lessor agrees to waive liability for collision damage to the vehicle. As such, the rental company does not enter into an insurance contract, but has merely effected a modification of the bailee's obligations.

In other words, in every bailment contract there exists a risk of loss that must be allocated as between the bailor and bailee. 8 C.J.S. Bailments §22 (1938 & Supp. 1985). The parties are legally free to allocate or divide the risk between them by agreement, or they may rely upon the allocation provided by common law, which makes the bailee liable to the bailor for damage to the bailed article caused by the bailee's negligence. Klar v. H & M Parcel Room, Inc., 270 A.D. 538, 541 (App. Div. 1946), aff'd, 296 N.Y. 1044, 73 N.E.2d 912 (1947); Gramore Stores, Inc. v.

Bankers Trust Co., 93 Misc. 2d 112, 402 N.Y.S.2d 326 (Sup. Ct. 1978); 8 C.J.S. Bailments §26(c) at 264, §27 (1938 & Supp. 1985).

The CDW option provides for an allocation of the risk of collision damage to the car. Under the rental agreements, without the CDW option, car rental companies either assume no risk or assume the risk of loss to the car in excess of a specified amount. The risk of loss to the car up to that specified amount, if there is a maximum, is assumed by the renter. The renter, however, has the option to elect the collision damage waiver under which he may, for an additional charge, relieve himself of some or all of his responsibility to the car rental company for collision damage to the vehicle. This has been held by the New York courts to "represent an entirely legal apportionment or shifting of that one risk [damage to the rented car] to one of the parties to the rental agreement from the other, for a consideration." Kramer v. Avis Car Leasing, Inc., No. 23344/82, slip op. (Sup. Ct. N.Y. 1983), aff'd, No. 19118-19-19A-19B, slip op. (App. Div. N.Y. 1984).

(2) Allocating risks in a bailment contract does not give rise to insurance. One argument commonly raised to "prove" that the CDW option is insurance is that because it

constitutes an agreement whereby a given risk is shifted, it must be insurance. This is patently incorrect.

Keeton, in his Insurance Law, makes clear that an element of risk transference in a transaction, unless "central and relatively important" to the underlying transactions (the rental of the car), does not give rise to insurance:

> All insurance contracts concern risk transference, but not all contracts concerning risk transference are insurance. The complex bundle of risks from a venture gives rise to a variety of kinds of legal risk transference, some of which are not regarded as insurance for any purpose, and some of which are regarded as insurance for one purpose but not for another. Even in states having the broadest statutory or decisional definitions of insurance, which if literally applied would include all or nearly all contracts transferring risk, many arrangements literally within such definitions are not treated as insurance transactions in legal contexts.

Keeton, at 6 (Emphasis added). As noted above, Keeton specifically cites "contracts for rental of vehicles" as one example in which the risk transference is "relatively insubstantial" and "incidental to the main objective of that transaction" and therefore not "within the scope of the insurance regulatory laws as properly construed." Keeton, Insurance Law at 552 (West 1971). See also In re Feinstein,

36 N.Y.2d 199, 203, 207-08, 366 N.Y.S.2d 613, 326 N.E.2d 288 (1975); Transportation Guar. Co. v. Jellins, 29 Cal. 2d 242, 174 P.2d 625 (1946); California Physician's Service v. Garrison, 28 Cal. 2d 790, 172 P.2d 4 (1946); Korn v. Avis, at 7.

The shifting of risk resulting from the renter's exercise of the CDW option is as unlike insurance as every other ordinary commercial transaction in which the parties contract with respect to risk. If the allocation of risk in this bailment is to be viewed as insurance, so too must any arrangements in which the parties agree to allocate between them the risk of loss to the subject matter of the transaction, or even the risk of consequential damage or liability to third parties. For example, sale of goods contracts often include provisions allocating risk of loss during shipment between seller and buyer. U.C.C. §§2-319, 2-320. Such contracts have not been considered contracts of insurance. See, e.g., Korn v. Avis.

The reason these examples are not contracts of insurance is that a transaction between two parties in which they must allocate a certain risk between them cannot give rise to the relationship of insurance with respect to that risk. It can give rise to the relationship of insurance if the risk is undertaken by a third party otherwise unin-

terested in the transaction, or it can give rise to the relationship of insurance with respect to a risk the parties need not allocate between them, such as the case where one party to a real estate or loan transaction assumes the risk of the other party's death as a material inducement to enter into the transaction. Simply put, a transaction requiring that a certain risk be allocated as between the parties does not, when the allocation is made, make one party an insurer of the other. This is equally true if the allocation is made by giving one party a choice.

Indeed, if risk transference is the factor determinating insurance, the concept of "insurance" would be hopelessly distorted:

> That an incidental element of risk distribution or assumption may be present should not outweigh all other factors. If attention is focused only on that feature, the line between insurance or indemnity and other types of legal arrangement and economic function becomes faint, if not extinct . . . . [O]bviously it was not the purpose of the insurance statutes to regulate all arrangements for assumption or distribution of risk. That view would cause them to engulf practically all contracts . . . . The fallacy is in looking only at the risk element, to the exclusion of all others present or their subordination to it.

Jordan v. Group Health Ass'n., 107 F.2d 239, 247-48 (D.C. Cir. 1939)

(D) All Courts Have Held That The Collision Damage Waiver Option Is Not Insurance. Every court and attorney general which has thus far addressed the issue has decided that the CDW option is not insurance. Following is a listing of all court decisions, attorney general decisions and insurance department rulings which have held that the CDW option is not insurance.

1. California.

a. Truta v. Avis Rent A Car System, Inc., Index No. 283922, slip op. (Super. Ct. Cal. December 10, 1984).

2. Colorado.

a. Davis v. M.L.G. Corp., No. 83SC219, slip op. (Colo. January 21, 1986).

3. Florida.

a. Op. Att'y Gen. Fla. (February 8, 1973)(The CDW option is the waiver of a contractual right, not insurance).

b. Burrell v. Avis Rent A Car Sys., Inc., No. 83-6162-7, slip op. (Cir. Ct. Fla., June 21, 1984)(trial court order dismissing complaint on ground that the CDW option is not insurance).

4. Illinois

a. Russell v. The Hertz Corp., No. 83 CH 6632, slip op. (Cir. Ct. Ill. 1983)(trial court ruling dismissing claims because the CDW option is part of bailment contract and not a separate contract of insurance).

5. Iowa

a. Op. Ins. Comm. Iowa (January 5, 1983)(The CDW option is not insurance as it lacks the element of indemnification).

6. New York

a. 1977 Op. Ass't Att'y Gen. N.Y. (January 4, 1977).

b. 1977 Op. Atty Gen. 63 (November 7, 1977)(The CDW option is not insurance).

c. Kramer v. Avis Car Leasing, Inc., No. 23344/82, slip op. (Sup. Ct. 1983), aff'd, No. 19118-19-19A-19B, slip op. (App. Div. N.Y. 1984).

d. Super Glue Corp. v. Avis Rent A Car Sys., Inc., No. 2084/84, slip op. (Sup. Ct. N.Y. May 11, 1984).

7. North Carolina

a. Op. Ins. Comm. N.C. (August 31, 1956)(rental agreement is a bailment, the CDW option does not meet the statutory definition of insurance).

8. Pennsylvania

a. Korn v. Avis Rent A Car System, Inc., No. 1670, slip op. (Pa. Ct. of Common Pleas, February 10, 1977)(trial court ruling dismissing claims that the CDW option involves the unauthorized sale of insurance because the CDW option is an ancillary part of the rental agreement and lacks the element of indemnity).

9. Texas

a. Op. Ass't. Ins. Comm. Tex. (March 30, 1967)(the CDW option is part of a bailment agreement and is not insurance).

The only contrary pronouncements are from the states of Louisiana and New Mexico. In Louisiana, an Insurance Department hearing officer recently opined that the CDW option is insurance. His views have been challenged in court, Commissioner of Insurance v. The Hertz Corporation, and enforcement of this opinion has been stayed pending a final decision of the Louisiana courts. In New Mexico, the Superintendent of Insurance in an informal letter dated August 22, 1985, expressed his view that the CDW option is insurance. We believe that both these expressions of opinion were made in contravention of the applicable law and are incorrect.

(E) Public Policy Objectives Which Require Insurance Regulation Are Irrelevant To The Collision Damage Waiver Option. The basic reason for regulating insurance is to guarantee that insurance companies will remain financially solvent and be able to pay out money to their insureds when they are obligated to do so. 2A Couch on Insurance 2d (Rev. ed.) §§21:32 - 21:35 (1984 & Supp. 1985). This rationale was stated more fully in Korn v. Avis as follows:

> The security of policyholders requires, first, permanency in the custodian of the funds gathered from them, and on which their indemnity in case of loss depends; second, an honest and competent administration of these funds; third, restraint against the division of the profits of the business whenever such division would injuriously affect the security of policyholders. How are these safeguards to be obtained? There is but one way in which they can be obtained and that is by means of general laws regulating the insurance business.

Korn at 9-10.

This rationale is not relevant to the offering of the CDW option by a car rental company. Where the CDW option is exercised, the car rental company does not pay money to the renter or to anyone else. Therefore, there is no need for a payment fund, capital account, surplus account and no need to monitor these assets to make sure they are not spent improperly. Indeed, even if a car rental company

became insolvent, no renter would be disadvantaged in any way, the renter would get exactly what he or she paid for - freedom from responsibility for collision damage. The Advisory Committee has recognized the illogic of applying insurance-like regulation to CDW:

> Are the needs for regulation of the CDW the same as the needs for the regulation of typical insurance products? The primary need for regulation presented by the typical insurance product is the need to assure that the company will remain solvent in order to meet its financial obligations to indemnify the policyholders. There is no need for solvency regulation presented by the CDW. The car rental company will not be required in any situation to pay money over to the renter. The economic loss sustained is to the property of the rental company.

Report of the Advisory Committee to the Market Conduct and Consumer Affairs [Ex 3] Subcommittee (June 11, 1985) presented at a meeting of the Market Conduct Surveillance [Ex 3] Task Force, National Association of Insurance Commissioners, Kansas City, Missouri (June 11, 1985).

In at least two states the fundamental weakness of applying insurance laws and regulations to the CDW option is well recognized. In Korn v. Avis, the Court held:

> the financial stability and management of [car rental companies] is obviously

> irrelevant to [renters] and therefore [there] is no need for the protection [of general laws regulating the insurance business]. Once the CDW [option] is accepted, [renters] agree not to seek any reimbursement for damages. This will be binding regardless of their fiancial condition. Regulation by the Insurance Commissioner would be unjustified and wasteful.

Id., at 10. In 1977 Op. Atty Gen. N.Y. 63 (Nov. 7, 1977), it was concluded:

> Moreover it is obvious that this type of agreement, involving a waiver of liability, does not pose the dangers that the Insurance Law was designed to meet, including inadequate coverage, excessive premiums and fiscal irresponsibility.

POINT II

PUBLIC POLICY ARGUES AGAINST INSURANCE DEPARTMENT REGULATION OF THE COLLISION DAMAGE WAIVER OPTION

Independent of the foregoing arguments, there are a number of public policy considerations which also argue strongly against Insurance Department regulation of the CDW option.

(A) Regulating The Collision Damage Waiver Option Would Necessitate Regulating Many Other Similar Contracts. The CDW option is not unique to the car rental business. A similar option, often known as the physical damage waiver option ("PDW option"), exists throughout the equipment

rental industry, which has been estimated to include 10,000 equipment rental outlets in the United States, with gross revenues in the billions of dollars. (Equipment Leasing and Rental Industries: Trade and Prospects, U.S. Department of Commerce, December, 1976). Should insurance departments thrust themselves into a regulatory role in regard to the car rental CDW option, it would eventually find itself compelled to regulate equivalent options contained in contracts which rent, for example, televisions, appliances, party supplies, construction machinery, medical equipment and devices, and exercise and recreational equipment.

(B) Regulating The Collision Damage Waiver Option Will Consume Limited Insurance Department Resources. To involve the states' insurance departments in regulating the CDW option would require, obviously, a substantial commitment of agency resources. In this era of limited, and often decreasing, governmental financial and manpower resources, Insurance Department involvement in regulating the CDW option could only result in its inability to regulate more important traditional insurance products.

POINT III

THERE IS NO NEED TO REGULATE THE COLLISION DAMAGE WAIVER OPTION AS LAWS AND REGULATIONS ALREADY EXIST WHICH PROTECT CONSUMERS

The CDW option has been made available to consumers for at least thirty years. Statutes and regulations already exist on the federal and state levels which are sufficient to protect the interests of consumers.

The Task Force and Advisory Committee have expressed concern over the following three issues: (A) rates, (B) deception of consumers, and (C) sales tactics. Each of these concerns is already addressed by existing federal and state laws and regulations.

(A) Rates. The Task Force and Advisory Committee have expressed concern that the amounts which are charged for the CDW option are "excessive". Even if true (which the Ad Hoc Committee denies) that fact alone cannot justify regulation of the CDW option by the state insurance departments. Only if the CDW option is "insurance" would the N.A.I.C. be the proper forum in which to draft a model act to respond to this complaint.* In light of the fact that the CDW option

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* See Constitution of the National Association of Insurance Commissioners, Article II; Bylaws of the National Association of Insurance Commissioners, Section 2(3)(c).

is not insurance (see the discussion under Point I, pp. 6-22, infra), the N.A.I.C. should not concern itself with the amount of the charges for exercise of the CDW option.

It must be noted that the charge for the CDW option is not the result of any cooperation or collusion between car rental companies. It is, as it must be, the result of competition in the marketplace. Indeed, any agreement or even discussion between car rental companies of the amount to charge for the CDW option would be a violation of the Sherman Anti-Trust Act, 15 U.S.C. §§1-7 (1973 & Supp. 1985), and various state anti-trust laws.

Furthermore, this Committee should realize that there exist both state and federal laws which already provide significant protection to renters with respect to these charges:

(1) Federal laws. The federal statute applicable to rates charged by automobile rental companies is the Federal Trade Commission Act, 15 U.S.C. §§41-77 (1976)(the "F.T.C. Act"). The operative portion of this Act is §45(a)(1) which provides in relevant part that "unfair or deceptive acts or practices in or affecting commerce, are declared unlawful." Since virtually all sales practices affect commerce, the F.T.C. has jurisdiction over almost all

forms of consumer fraud. The Commission implements its general mandate to prescribe unfair and deceptive acts by defining, in guides, rules and cases, specific prohibited practices.

(2) State laws. Since the 1960's, virtually every state has enacted consumer protection legislation designed to parallel and supplement the F.T.C. Act. M. Leaffer & M. Lipson, Consumer Actions Against Unfair or Deceptive Acts or Practices: The Private Uses of Federal Trade Commission Jurisprudence, 48 Geo. Wash. L. Rev. 521, n. 1 (1980). These state statutes, which generally make unlawful all "unfair or deceptive acts or practices", are based on one or all of three Acts - (i) the F.T.C. Act, (ii) the Uniform Deceptive Trade Practices Act, and (iii) the Uniform Consumer Sales Practices Act.

Although the wording of the state statutes vary from state to state, the operative language in each state is approximately the same - prohibited are "unfair or deceptive acts or practices," a phrase which is usually given an extremely broad interpretation.

Numerous state court decisions have used state consumer protection laws, whether based on any one or a hybrid of more than one of the three model statutes, to hold that a cause of action exists for the charging of excessive

prices. One example is Clayton v. McCary, 426 F. Supp. 248 (N.D. Ohio 1976). In that case, the United States District Court sitting in the Northern District of Ohio, which is one of the states which adopted the Uniform Consumer Sales Practices Act, acknowledged that excessive price was a circumstance which should be considered in determining the fairness of a transaction.

A second example is Kugler v. Romain, 58 N.J. 522, 279 A.2d 640 (1971) in which the court held excessive, pursuant to the state consumer fraud laws, the price charged by a seller of so-called "educational books" and related materials when the price was approximately 2-1/2 times the reasonable market price of the package.

(B) Deception of Consumers.

(1) Federal laws. The F.T.C. Act prohibition against "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce" have been held to apply to actions against companies which deceive consumers. The scope of the application of the F.T.C. Act as well as examples are described in detail in M. Leaffer & M. Lipson, Consumer Actions Against Unfair or Deceptive Acts of Practicers: The Private Uses of

Federal Trade Commission Jurisprudence, 48 Geo. Wash. L. Rev. 521, n.1 (1980).

(2) State laws. Regardless of the origin of any given state's consumer protection laws, considerable protection is afforded car renters against deceptive practices by car renters. The scope and exemptions of the state deceptive trade practice and consumer protection acts is laid out in detail in Annot. 89 A.L.R.3d 399 (1979 & Supp. 1985) and Annot. 89 A.L.R.3d 449 (1979 & Supp. 1985), copies of which are attached to this position paper as Appendix A and Appendix B.

(C) Sales Tactics. The third concern of the Task Force and Advisory Committee is that renters are being induced to accept the CDW option when they really do not want to do so. There exist both federal and state laws and regulations which provide significant protection to renters against such conduct.

(1) Federal law. The F.T.C. Act as described above, prohibits all "unfair or deceptive acts or practices." Again, there is no question that it is within the FTC's power to act in the event of the complaint in question. In individual cases the FTC has successfully challenged certain forms of particularly abusive "hard sell" sales tactics involving, for example, home solicitation sales. The FTC, in addition, has also established rules governing "hard sell" tactics. For examples, see J. Sheldon & G. Zweibel, Survey of Consumer Fraud Law, (1978).

(2) State laws. Regardless of which statute a state has based its consumer protection statute on, consumers are protected against high pressure sales tactics.

Virtually all states have prohibited through their own unfair and deceptive trade practices laws high-pressure sales tactics. See M. Leaffer & M. Lipson, Consumer Actions Against Unfair or Deceptive Acts or Practices: The Private Uses of Federal Trade Commission Jurisprudence, 48 Geo. Wash. L. Rev. 521, n.1 (1980); J. Sheldon & G. Zweibel, Survey of Consumer Fraud Law (1972).

Exhibit A

CONCLUSION

FOR THE FOREGOING REASONS, WE URGE THIS COMMITTEE NOT PROPOSE A MODEL REGULATION OF THE CAR RENTAL AGREEMENT COLLISION DAMAGE WAIVER OPTION.

Respectfully submitted,

LeBoeuf, Lamb, Leiby & MacRae
on behalf of the Ad Hoc
Committee on the Collision
Damage Waiver Option
520 Madison Avenue
New York, New York 10022
(212) 715-8000

February 25, 1986

Reference Materials

Security Benefit Life Insurance Company
A Member of The Security Benefit Group of Companies

February 27, 1986

TO: The Honorable Rex Hoy, Chairman, and Honorable Members,
House Committee on Insurance

FROM: Wayne Morris, Assistant Counsel

RE: H. B. 3007 -- Kansas Deposit Law

I am Wayne Morris, Assistant Counsel for Security Benefit Life Insurance Company. I appreciate the opportunity to review H.B. 3007, dealing with Kansas deposit laws.

Kansas law requires that all domestic (Kansas) life insurance companies deposit securities and other assets with the Commissioner of Insurance sufficient to cover the entire amount of its net reserves. To fulfill this obligation, the Commissioner employs staff and maintains a vault for these deposits in the State Office Building.

H.B. 3007 would amend two sections of the Kansas deposit law. Section one would amend KSA 40-404 to permit companies to get a credit, when calculating the deposit amount, for investment income due and accrued on investments which are on deposit and which are not in default. Companies would be required to file an annual form setting forth the amount of this credit. This income is virtually the same as cash, and would be readily available for the policyholders' benefit. It is currently reported on each company's annual statement, but it is not currently allowed as a deposit credit.

Section two would amend KSA 40-404a to both update the procedure for appraising real estate that is to be deposited with the Commissioner and to also give companies the option of merely depositing real estate at its book value, without the need to obtain an appraisal. The section currently requires that there be an "appraisement" of all such real estate, which is to be done by "three disinterested resident freeholders of the county where the land is situated", and such freeholders may not be paid more than $25.00 per day. The amendments would allow the real estate to be appraised by one appraiser approved by the Commissioner and the fee limitation (the fees are borne by the company) would be eliminated. At the same time, a company could deposit real estate at its book value, as reported in its annual statement, and avoid the time and expense of obtaining an appraisal. Regardless of which procedure might be followed, the Commissioner retains authority to require that the real estate be appraised or reappraised.

Attachment 3
House Insurance
2-27-86

We believe these changes are prudent and conservative improvements in the deposit law. They will allow companies to more easily and less expensively comply with the deposit requirement, but they do not reduce the policyholders' security. We have also worked with the Insurance Department on these proposals. Security Benefit, along with the other members of the Kansas Life Association, respectfully requests your favorable consideration of this bill.

Thank you for this opportunity to appear in support of this bill. Either I, or Ms. Jane Tedder, Security Benefit's Portfolio Manager, would be happy to attempt to answer any questions you may have.

vf

Wayne