Attorney General files lawsuit against six large insurance companies alleging price-fixing

Attorney General Charles Foti filed a lawsuit in Orleans Parish Civil District Court late Wednesday alleging collusion, price-fixing and anti-trust violations by six major insurance companies - including Allstate and State Farm - as well as the firms that manufacture their claims-processing software, and the companies that offer them advice or collect their data.

The suit, filed in conjunction with several outside law firms deep in Katrina litigation, is based on the work of an ongoing investigation by the Louisiana Attorney General, who lost his re-election bid in the October 20 primary.

Charles FotiIt says that these groups conspired to manipulate commerce for their own enrichment "by rigging the value of policyholder claims and raiding the premiums held in trust by their companies" and that companies "coerced their policyholders into settling their claims of damages for less than their value by editing engineering reports, by delaying payment and by forcing policyholders to litigate claims to receive full value."
Bob Hartwig, an economist who is president of the Insurance Information Institute trade group, said that Foti's accusations are baseless.

"To allege that insurers act collusively in the settlement of claims is an accusation that has no merit whatsoever," Hartwig said. "Insurers operate independently from each other in settling claims. They do not consult with one another, and they adjust those claims according to their individual contracts with their customers."

In Louisiana, insurers paid out $28 billion on 1.2 million claims of all types from Hurricanes Katrina and Rita. "Those are very substantial numbers. Much of the rebuilding that's going on in Louisiana today is being done with insurance money," Hartwig said.

The suit names State Farm Fire and Casualty Co. and Allstate Insurance Co., Louisiana's two largest residential insurers; Farmers Insurance Exchange, the state's fifth largest homeowners insurance company; Standard Fire Insurance Co, better known as Travelers, the state's seventh largest homeowners insurer; military insurer USAA Casualty Insurance Co., the eighth largest homeowners company and tiny Lafayette Insurance Co., a division of United Fire Group.

The suit also names Marshall & Swift/Boeckh LLC and Xactware Inc., companies that manufacture leading claims adjusting software; and Xactware's parent company, insurance data collector Insurance Services Office Inc. It also names McKinsey & Co., an international consulting firm which was the architect of claims handling practices used by many major insurance companies.

Many of the companies named in the suit could not be reached for comment Wednesday. McKinsey officials said the company doesn't comment on anything related to client work. Allstate and Travelers officials said they couldn't comment because they hadn't seen the suit, as did State Farm, which also said it stands by its claims-handling procedures.

"We haven't seen the suit. What I can say is that we handle each claim individually based on the merits of the claims based on our contracts with our policyholders," State Farm spokesman Fraser Engerman said. "We pay what we owe."

USAA spokesman David Snowden said that lawyers are reviewing the suit. "USAA's claims practices are based on a foundation of ethics, fairness and integrity. Since Hurricane Katrina, we've worked with our members to individually resolve more than 20,000 claims in Louisiana," Snowden said. USAA is owned by its members, who are military personnel and their families.

The sweeping suit says that many insurance companies used the same consulting firm, McKinsey, to devise a strategy for reducing claims, and the success of those companies created financial pressure for everyone else in the industry to follow.

By using claims processing software manufactured by Marshall & Swift/Boeckh and Xactware, the industry has been able to standardize its tactics for low-balling claims, and create a "tainted" database of claims settlements figures which the industry uses to further depress estimates for what people need to repair their homes, according to the lawsuit.. Meanwhile, all of this data is centralized by Xactware's parent company, Insurance Services Office, better known as ISO, allowing companies to collude.

By using these outside vendors to unify "power and control," insurers systematically reduced the percentage of premium dollars that companies return to policyholders in the form of claims payments "under a shroud of secrecy." While the industry has historically paid 70 cents on every premium dollar collected back to policyholders in claims payments, in Katrina, they paid 50 cents for every premium dollar, the suit says.

Foti's suit was filed in conjunction with Baton Rouge sole practitioner Joseph McKernan; New Orleans sole practitioner Mark Glago; and the New Orleans law firms of Herman, Herman, Katz & Cotlar and Capitelli & Wicker. Those firms are working with Jane Johnson, Louisiana's assistant attorney general for anti-trust issues, without any guarantees earning legal fees.

The lawsuit relies heavily on the theories of New Mexico attorney David Berardinelli, who wrote a book about the McKinsey company's work for Allstate called "From Good Hands to Boxing Gloves." The title of the book is taken from a McKinsey slide advising the company to don boxing gloves and pummel anyone who doesn't accept settlements for pennies on the dollar.

Prior to McKinsey's consulting work for the industry, insurance was viewed as a quasi-public trust in which insurance played a vital role in indemnifying the middle class against financial ruin. But McKinsey, in its quest to increase profits for its clients, ignored this unique function of the industry, and created a devastating strategy that rewards shareholders at the expense of policyholders that has spread throughout the industry, Berardinelli says.

Foti's suit says that insurance companies engaged in horizontal price-fixing "with the explicit approval of insurer management," and strategies to delay and deny claims. In the face of such strategies, homeowners are essentially buying insurance that will never adequately compensate them, meaning that they are overpaying on their premiums.

The suit takes note of the record profits achieved by the industry in 2005 and 2006, despite fielding the most expensive hurricane seasons ever in 2004 and 2005.

In alleging the conspiracy, Foti's suit notes the vast influence that the outside firms named in the suit have on insurance companies. McKinsey, for example, advises two-thirds of the nation's Fortune 1000 companies.

ISO brags in press releases that it has a searchable database of more than 500 million insurance claims, and its Xactware is used by 16 of the nation's top 20 property insurers. The company's software allows insurers to monitor what claims adjusters are doing through its XactAnalysis Quality Review and compare their work to the latest prices reported in the software's Industry Trend Reports, and allows insurers to assign reinspections.

Those trend reports allow insurers "to share the current prices being submitted by competitors, and thus, coordinate the horizontal price-fixing suppression, or attempted suppression, of the overall market in repair services at virtually every geographic level and price component," the suit says.

By December 2005, the cost of repairing a home had doubled since before the storm, and the cost of completely rebuilding a home had gone up by 50 percent, the suit says, yet the price lists of the insurers named in the suit had only increased by 15 percent to 20 percent by December 2005.

Once enough companies are onboard using a certain product others are under pressure to follow. Farmers, according to the suit, visited with a bunch of other leading insurance companies in 1998 and 1999, and when it saw the financial benefits of using the standard claims processing software, it started using Xactimate, too.

The suit cites quotes by Frank Coyne, chairman, chief executive and president of ISO, boasting that computerized claims software and aggregated data are changing how companies do business, while companies that don't follow are going out of business.

"In just a decade and a half, approximately a third of the insurers serving the United States vanished as escalating competition ate into top-line revenue growth and bottom-line profitability. But it isn't just the intensity of competition that's changing . . .The nature of the competition is changing, too, as advances in predictive modeling and other analytical techniques enable leading insurers of all sizes to target their marketing, underwriting and pricing as never before."

Claims adjusters, the suit says, are pressured or required to accept the pricing database information from the Xactware or Marshall & Swift/Boeckh software in the estimates they write if the adjuster wants to be able to close the claim and get paid for the work.

While these companies purport to be providing an independent and objective benchmark for pricing, the suit says, "they intentionally devalue the market price in order to underpay their policyholders and/or artificially deflate, or attempt to deflate construction and repair costs in the affected market."

Meanwhile, the suit says that State Farm has testified under oath that it can modify Xactimate's price lists before adjusting claims. A pricing specialist conducts surveys building material suppliers for the latest prices and updated its New Orleans prices several times per quarter between 2005 and 2007. However, the suit says, a State Farm price list containing 10,000 different items was exactly the same as a Travelers price list on Nov. 15, 2005, something that would be "a statistical impossibility without collusion."

"This continuous arrangement gave insurers an unjust advantage over policyholder, which they took advantage of before, during and after the greatest disaster this country has ever suffered, by reaping huge profits from the misfortunes of persons whom they pledged to protect from risk of loss. They raised insurmountable odds against policyholders' ability to recover," the suit says.

The suit asks for all damages, including but not limited to, treble damages, attorneys fees and costs, injunctive relief and all equitable, declaratory and general relief.

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