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LITIGATION ALERT

SUPREME COURT TO DETERMINE THE SCOPE OF SECTIONS 1681m(a) AND 1681n OF THE FAIR CREDIT REPORTING ACT

In recent years, a new trend of Fair Credit Reporting Act (FCRA) litigation has emerged. Consumers in a number of jurisdictions around the country have filed FCRA class actions against insurance companies arguing that the FCRA's § 1681m(a) mandates an adverse action notice when a premium charged for initial insurance policies is not the best rate the company can offer. In most cases, the plaintiffs have alleged violations under § 1681n of the FCRA, which allows for statutory as well as punitive damages, if the consumer can show a "willful" violation of the Act. Two 9th Circuit rulings on these issues are currently before the U.S. Supreme Court.

Among other things, the Fair Credit Reporting Act requires companies that use credit reports in their business decisions to notify consumers when adverse information in a credit report negatively impacts the price at which the company decides to offer the consumer a good or service. In the two cases currently before the U.S. Supreme Court, *GEICO General Insurance Company, et al. v. Edo*, No. 06-100, and *Safeco Insurance Company of America, et al. v. Burr*, No. 06-84, the 9th Circuit (i) expansively interpreted the circumstances in which companies must issue adverse action notices and (ii) held that plaintiff may prove a willful violation of the FCRA (thus entitling him to punitive damages) based on a mere reckless disregard for the adverse action notice rules rather than on an intentional disregard for the law, which is the standard applied in other circuits.

The plaintiffs in these cases applied for auto and renters insurance. None of them, however, received the best rate offered by the companies. In the *GEICO* case, the plaintiff was issued a policy from its standard risk, rather than its preferred risk, company. In the *Safeco* case, the plaintiffs were essentially offered standard, not preferred, rates. GEICO contends that its pricing decision was based on other underwriting factors and not any specific derogatory information in the plaintiff's credit report. Therefore, it had no duty to issue an adverse action notice. Safeco argues that its actions in offering an initial premium higher than the best possible rate did not trigger a notice requirement under the FCRA.

In the decisions below, the 9th Circuit held otherwise, finding that the failure to issue insurance at the best available rate, even upon the initial application of insurance, when that decision included a credit report review in consideration, constituted an adverse action under the statute. The 9th Circuit also held, contrary to the holdings of other circuits, that the plaintiffs could prove a willful violation merely by showing that the companies recklessly disregarded the law, even if the evidence did not show that the companies intentionally disregarded any known legal obligation.

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The Supreme Court heard oral arguments on these cases on January 16, 2007. During oral arguments, several justices seemed taken aback by the 9th Circuit's expansive reading of the FERA's adverse action notice requirements. While this seems to indicate that at least some of the justices may agree with the insurers' interpretation of the FCRA, it is too early to predict which interpretation the Court will adopt.

Companies that use consumer credit reports in their business decisions should closely follow these cases. In both cases, the 9th Circuit found that reliance on counsel may not be sufficient to defend the claim of willfulness because the Court found the company's interpretation of the rules to be so "implausible" that the plaintiff should be allowed to argue to the jury that even such reliance may amount to a reckless disregard of the FCRA's notice requirements. On the adverse action notice point, both companies argued that a failure to qualify for the best available rate upon an initial insurance application is not an adverse action under the statute. Further, GEICO argues that it should not be required to issue adverse action notices when a credit report did not impact the pricing decision, as other underwriting factors lead the company to offer standard rates rather than preferred rates.

The Court is likely to decide the cases by the end of June. The cases have the potential to fundamentally affect the way that many financial services companies and businesses, which use credit in their decision-making processes, issue adverse action notices. Most courts interpreting the FCRA have held that an adverse action occurs when negative information in a credit report causes a company to decline an application or when it increases the price for goods or services already offered. No court has previously held that an adverse action occurs simply because a company sets an initial insurance premium at a rate higher than the company's best available rate. As GEICO and Safeco have argued to the Supreme Court, the 9th Circuit's interpretation would require an adverse action notice issue in many cases in which the credit report is either not a factor at all, or in cases where positive information in a credit report causes the company to lower its price, but not all the way to its lowest available price.

The willfulness issue is tremendously significant as well. The 9th Circuit held that the district court, on remand, must engage in a subjective inquiry into the companies' motives behind their adverse action policies. That is, there should be an inquiry into specific evidence as to how the companies' decisions were reached, which includes obtaining testimony from the companies' executives and in-house counsel. According to the Court, even good-faith reliance on the advice of counsel would not be dispositive. Thus, even if a company's policy was based on good-faith advice from its in-house counsel, it may still be exposed to punitive damages even where the plaintiff could prove no actual harm. As GEICO has put it in its Supreme Court brief, the 9th Circuit holding means that a company can be found to have willfully violated the statute based on a good-faith interpretation of counsel that the court later determines to have been wrong. The term "willfulness" in the law connotes conduct far more culpable than that.

CONTACT INFORMATION

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