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Client Alert

Third Circuit Holds That The McCarran-Ferguson Act Does Not Preclude Private RICO Claim Against Insurer

On April 3, 2007, the Third Circuit Court of Appeals held that neither the McCarran-Ferguson Act nor the New Jersey Insurance Trade Practices Act (ITPA) precludes a private plaintiff from initiating a complaint against an insurer under the Federal Racketeer Influenced and Corrupt Organizations Act (RICO). After reviewing the relevant provisions of New Jersey's ITPA, the court decided that Richard Weiss' RICO claims against First Unum Life Insurance Company would not frustrate the operation of New Jersey's insurance laws.

As part of its review, the court applied the broad test set forth in *Humana Inc. v. Forsyth*, a 1996 case in which the Supreme Court held that the plaintiff's private RICO action was consistent with Nevada insurance law. The *Humana* test requires the court to evaluate a variety of factors – such as whether the state provides both statutory and common law remedies for insurance misconduct, the availability and scope of damages for such misconduct, and the existence of other state grounds for suit – to determine whether acceptance of the federal claim would interfere with the application of state insurance laws.

The U.S. District Court of New Jersey considered the *Humana* factors and concluded that the McCarran-Ferguson Act precluded Weiss' RICO claims. The court distinguished the case from *Humana* by noting that New Jersey law fails to create a private right of action for the non-payment of insurance benefits and also fails to provide for an award of punitive damages. Based on these differences, the district court held that Weiss' RICO claims would "impair" the operation of New Jersey's regulatory scheme.

On appeal, the Third Circuit acknowledged that New Jersey's ITPA fails to provide a private right of action, but decided that the balance of the other *Humana* factors favored allowing Weiss' federal claim. For example, the court noted that New Jersey recognizes a common law right of recoupment for wrongly withheld benefits and indicated that New Jersey's Consumer Fraud Act (CFA) might provide statutory recourse for non-payment of insurance benefits. The court also noted that the CFA provides for treble damages consistent with those available under RICO. Finally, the court indicated that a racketeering scheme might be sufficiently egregious to warrant punitive damages under New Jersey law. Based on these and other factors, the court concluded that acceptance of Weiss' federal claim would not frustrate New Jersey's insurance regime.

The Implications of the Third Circuit Decision

The primary implication of the Third Circuit decision is that it provides an alternative basis for private action against New Jersey insurance companies. The decision allows a private claimant to work around the New Jersey insurance law that specifically prohibits private actions against insurers. Based on the decision, an insurance company is now vulnerable to any federal claim that does not frustrate or impair the operation of New Jersey insurance law. Assuming that other circuits adopt a similar approach, the insurance companies conducting business in those circuits may also become susceptible to private claims under federal law. In this respect, the decision may prove to

be wide-reaching in scope, opening the door for private plaintiffs to advance federal claims even where state insurance laws prohibit private actions against insurers.

A secondary implication of the Third Circuit decision is that it reiterates the limited scope of the McCarran-Ferguson Act. The McCarran-Ferguson Act, 15 U.S.C. §§ 1011-15 (2000), was enacted in 1945 to preserve state regulation of the business of insurance. The Act affords insurers protection from federal antitrust laws where: (1) the challenged practice is part of the "business of insurance" and (2) the practice is "regulated by State law." Id. § 1012(b). Although the McCarran-Ferguson Act affords considerable protection to state insurance regimes, the Weiss decision demonstrates that the Act fails to operate as an absolute bar to federal suits against insurers. Instead, the Act only insulates state insurance regimes in cases in which state law directly conflicts with federal law or application of federal law would frustrate state policy. Thus, in addition to developing an extensive knowledge of state-specific insurance laws, insurers must remain mindful of the federal implications of their insurance activities. More importantly, insurers must appreciate that, even if the state insurance scheme prohibits private complaints against insurers, a private plaintiff may still find legal recourse in the form of a federal cause of action.

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