

CASE NOTE

The Notification Requirement of the Fair Credit Reporting Act in Insurance Underwriting: Clarifying the Willfulness Standard in Civil Actions

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I. Introduction

In the consolidated decision of *Safeco Insurance Company v. Charles Burr* and *GEICO General Insurance Company v. Ajene Edo*,¹ the U.S. Supreme Court clarified protection for consumers under the Fair Credit Reporting Act and the element of willfulness which is widely used in civil statutes. Although the cases at bar involved insurance companies, the holdings will have application beyond the insurance industry. The decision in *Safeco v. Burr* is also significant because it applies *federal* law to the insurance industry's use of consumer credit reports to set rates offered to customers.

The insurance industry is largely regulated by the states.² Generally, each state has a Department of Insurance that operates as an executive agency within the government. Much of the regulatory action occurs within the administrative regulatory machinery. The standards developed are not uniform throughout the United States because each state is free to make its own rules and create its own enforcement regime.

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1. *Safeco Ins. Co. of Am. v. Burr* (Safeco v. Burr), 127 S. Ct. 2201 (2007).

2. In *United States v. Se. Underwriters Ass'n.*, 322 U.S. 533 (1944), the U.S. Supreme Court held that the transfer of funds, information, and communication across state lines brought the transaction within the bounds of the commerce clause of the U.S. Constitution (U.S. CONST. art. I, § 8) and made the insurance transaction subject to federal regulation. In response to this ruling, Congress passed the McCarran Ferguson Act of 1945, 15 U.S.C.A. § 1011 (1997), which reserved the right to regulate insurance to the individual states.

The Fair Credit Reporting Act³ (hereinafter “FCRA”) was enacted in 1970 by Congress to “curb some of the abuses” of entities that compile or use credit information on consumers.⁴ The act contemplates use of consumer credit reports for various purposes, including the granting of credit to an individual, as well as insurance and employment uses.⁵ The stated purpose of FCRA is to ensure that consumers are treated in a fair and equitable manner and that the information in their credit report remains confidential, accurate and relevant.⁶ As a federal statute, FCRA supersedes state law.⁷ Therefore, in this particular area, the federal government regulates insurance companies and the federal courts hear all disputes.

The FCRA requires users of credit reports to notify the consumer when an “adverse action” is taken based upon the information in a credit report.⁸ An adverse action, as it relates to insurance, includes the denial, cancellation, increase in charge, reduction in coverage, or any other unfavorable change in the coverage or amount of insurance.⁹ The Act applies to existing coverage, new applications or changes in underwriting.¹⁰ The Act further provides that a consumer may receive actual damages, costs and attorneys fees if notification is not received when required.¹¹ If the violation is willful, the consumer can recover statutory and punitive damages.¹²

II. Factual Background

Safeco v. Burr consolidates review of two rulings by the Ninth Circuit Court of Appeals.¹³ The central issue is the willful disregard of a company’s obligation to send FCRA-required notice when, based on credit information, the company does not offer a customer its lowest possible rate.¹⁴

Safeco uses consumer credit scores as one of the factors in determining the initial insurance premium that it will offer to a new customer.¹⁵ Plaintiffs, Charles Burr and Shannon Massey, had separate but similar experiences with Safeco. Both applied for insurance and neither had been insured with Safeco immediately before requesting a quote. Both plaintiffs accepted the quoted premiums for new policies. Based partly on their credit

3. Fair Credit Reporting Act, 15 U.S.C. § 1681 (2000).

4. *Ackerley v. Credit Bureau of Sheridan, Inc.*, 385 F. Supp. 658, 659 (D. Wyo. 1974).

5. 15 U.S.C. § 1681b.

6. 15 U.S.C. § 1681.

7. U.S. CONST. art. VI.

8. 15 U.S.C. § 1681m.

9. 15 U.S.C. § 1681a.

10. 15 U.S.C. § 1681a(k)(1)(B)(i).

11. 15 U.S.C. § 1681o(a).

12. 15 U.S.C. § 1681n(a).

13. *Reynolds v. Hartford Fin. Servs. Group, Inc.*, 435 F.3d 1081 (9th Cir. 2006); *Spano v. Safeco Corp.*, 140 Fed. Appx. 746 (9th Cir. 2005).

14. *Safeco v. Burr*, 127 S. Ct. 2201, 2205 (2007).

15. *Id.* at 2207.

scores, neither was offered Safeco's lowest possible rate. However, the company did not send them adverse action notices.¹⁶

Burr and Massey joined in a proposed class action suit against Safeco.¹⁷ They claimed the insurer had taken an adverse action against them by using their credit scores in the decision to provide a less-than-best rate.¹⁸ They further claimed that the insurer willfully failed to notify them of the adverse action as required by FCRA.¹⁹

Safeco asserted that no adverse action had occurred and, therefore, FCRA did not require notification to the plaintiffs. The district court agreed with Safeco's reasoning that there could be no "rate increase" for new customers who had no history of a lower rate with the insurance company.²⁰ The trial court granted summary judgment for Safeco relying, in part, upon Safeco's definition of an "adverse action."²¹ Plaintiffs appealed and the Ninth Circuit reversed and remanded, based on its earlier ruling in a consolidated decision including GEICO.²²

The previous case against GEICO (Government Employees Insurance Companies) also involved the use of credit ratings in setting insurance rates. GEICO is a holding company with several different subsidiary companies.²³ Each subsidiary has different insurance rate structures and customers are placed with a particular subsidiary based on the insurer's evaluation of a customer's risk. For example, low-risk customers are directed to one subsidiary and offered "preferred" policies with the lowest rates; moderate-risk customers to another subsidiary which offers "standard" policies with moderate rates; high-risk customers are directed to yet another subsidiary which offers "nonstandard" policies at higher rates.²⁴ This placement is accomplished through the use of a model that takes several customer characteristics into account, including the customer's credit.²⁵ However, since not all customers have a credit score, the model can also set a default rate which GEICO refers to as a "neutral credit score."²⁶ GEICO interpreted "adverse action" to be a quote of any insurance rate that is higher than the

16. *Spano v. SAFECO Ins. Co. of Am.*, 215 F.R.D. 601, 607 (D. Or. 2003).

17. *Spano v. SAFECO Ins. Co. of Am.*, 215 F.R.D. 601 (D. Or. 2003) (other plaintiffs included Spano, Opoien, McGrath and Horton).

18. *Safeco v. Burr*, 127 S. Ct. 2201, 2207 (2007).

19. *Id.*

20. *Id.* at 2210-11.

21. *Spano v. SAFECO Ins. Co. of Am.*, 215 F.R.D. 601, 612 (D. Or. 2003). The greater part of the trial court's opinion dealt with pleading technicalities and the inability of the plaintiffs to penetrate the complex corporate structure of Safeco in order to name the correct Safeco subsidiary as defendant to the suit. However, these pleading difficulties are not germane to the later appellate decisions.

22. *Reynolds v. Hartford Fin. Servs. Group, Inc.*, 426 F.3d 1020, 1040 (9th Cir. 2005).

23. *Safeco v. Burr*, 127 S. Ct. 2201, 2206 (2007).

24. *Id.*

25. *Id.*

26. *Id.* at 2206-07.

price the customer would have been offered if no credit score were available.²⁷

Ajene Edo applied for insurance with GEICO. GEICO obtained Edo's credit score and used it in assigning him to GEICO Indemnity Company, the moderate-risk company.²⁸ Based on GEICO's model, Edo did not qualify for a policy from GEICO General, the subsidiary with the lowest premiums. However, Edo would have been assigned to GEICO Indemnity using the neutral credit score model, so GEICO did not send him a notice of adverse action.²⁹

Edo filed suit against GEICO claiming that the insurer had taken an adverse action against him and had willfully failed to send him the notice required by FCRA. The trial court granted summary judgment for GEICO holding that, because his rate would have been the same with or without the credit score, there was no adverse action.³⁰ On appeal, the Ninth Circuit disagreed. The court held that an adverse action requiring notification occurred whenever a customer would have received a better rate if the customer's credit score had been more favorable.³¹ The Ninth Circuit remanded the case to the district court to determine whether this failure by GEICO had been willful. The Ninth Circuit explained that a good faith attempt by a party to fulfill its statutory obligations would not be willful, but a deliberate failure to determine those obligations would be classed as willful.³²

The U.S. Supreme Court granted certiorari on the cases involving both insurers³³ and consolidated them.³⁴ The opinion in *Safeco v. Burr* answers two questions: 1) what constitutes an adverse action when using credit scores to determine insurance rates and 2) do willful violations comprehend only *knowing* violations of the statute, or do they include *reckless* violations as well.³⁵

III. Adverse Action in Pricing for First Time Insurance Customers

Both the *Safeco* and the *GEICO* actions involved the setting of initial insurance rates for new customers. FCRA enumerates several types of adverse actions,³⁶ however the only one applicable in these cases was "in-

27. *Id.* at 2207.

28. *Id.*

29. *Id.*

30. Edo v. GEICO Cas. Co., 2004 U.S. Dist. LEXIS 28522 (D. Or. Feb. 23, 2004).

31. *Safeco v. Burr*, 127 S. Ct. 2201, 2207 (2007).

32. *Reynolds v. Hartford Fin. Servs. Group, Inc.*, 416 F.3d 1097, 1116-17 (9th Cir. 2005).

33. *Reynolds v. Hartford Fin. Servs. Group, Inc.*, 435 F.3d 1081 (9th Cir. 2006); *Spano v. Safeco Corp.*, 140 Fed. Appx. 746 (9th Cir. 2005).

34. *Safeco v. Burr*, 127 S. Ct. 2201, 2208 (2007).

35. *Id.* at 2208.

36. 15 U.S.C. § 1681a(k)(1)(B)(i) (2000).

crease in charge.”³⁷ Therefore, if there was no price increase there was no adverse action.³⁸ Both plaintiffs argued that there *was* a price increase even though there were neither previous dealings with the insurance companies nor any previously established price.³⁹

A plain language reading of the statute could lead an insurer to believe that a price increase can only occur when a different and lower price had been previously established with a particular customer.⁴⁰ Safeco reasoned that a price increase, by definition, could not occur for a new customer in which there was no previous price with which to compare. The district court relied on this reasoning in granting summary judgment.⁴¹

The Supreme Court looked to the intent of Congress and the Act’s own statement of purpose in developing the notification requirement.⁴² Notification is intended to protect the public from unfair and inaccurate credit reporting that can gravely impact many aspects of a consumer’s life.⁴³ When a financial institution, including an insurance company, takes an action detrimental to the consumer based on information contained in the consumer’s credit report, the consumer must be notified so that the report can be checked for inaccuracies.⁴⁴

Writing for the majority, Justice Souter reasoned that this broad statement of purpose, as well as the legislative history of amendments to FCRA, indicated that Congress intended broad application of the notification requirement.⁴⁵ Consequently, a broad definition of adverse action was also required.⁴⁶ Nothing in the stated purpose or legislative history of the act suggested that its protections should be denied to first time victims of the adverse effect of a less than stellar credit report.⁴⁷ In a metaphor adopted from the U.S. Government’s amicus curiae brief, the opinion offered the example of a gas station customer who is offered a price for gas that is higher than the price posted on the sign just because the owner does not like the customer. This would be considered a price increase even if the customer had never been to that gas station in the past.⁴⁸

37. *Safeco v. Burr*, 127 S. Ct. 2201, 2210 (2007).

38. *Id.* at 2207.

39. *Id.*

40. *Id.* at 2210-11.

41. *Id.* at 2207.

42. 15 U.S.C. § 1681(a) (2000); *Safeco v. Burr*, 127 S. Ct. 2201, 2211 (2007).

43. *Safeco v. Burr*, 127 S. Ct. 2201, 2211 (2007).

44. 15 U.S.C. § 1681(m) (2000).

45. *Safeco v. Burr*, 127 S. Ct. 2201, 2211-12 (2007).

46. *Safeco v. Burr*, 127 S. Ct. 2201, 2205 (2007). Justice Scalia joined the majority opinion except for footnotes 11 and 15. Although he gave no reason for failing to join the majority in these footnotes, the two footnotes both use the legislative history of the FCRA to support the Court’s broad definition of an “adverse action.”

47. *Id.* at 2211.

48. *Id.* at 2211 n.10.

Therefore, the Court held that an “increase” is any disadvantageous rate, even for a first time customer.⁴⁹ Applying this holding to the cases at bar, the Court held that Safeco had, in fact, taken an adverse action based on a consumer credit report, thereby triggering the notification requirement of FCRA. Due to information in their credit reports, Safeco had offered the plaintiffs a higher rate than they would otherwise have received.⁵⁰

The GEICO situation was different. GEICO uses an underwriting model in which the company compares the price produced by the model using credit information with the price produced by a model that does not take credit into account—what GEICO calls a *neutral credit score*.⁵¹ When the price produced using the credit score model is higher than the price using the credit neutral model, GEICO considers it an adverse action and notifies the customer as required by FCRA. On the other hand, if the price is the same or better using the credit score than it would have been without, the company does not consider the result an adverse action and does not notify the customer.⁵² The majority approved of GEICO’s reasoning and methodology. They held that GEICO had not taken an adverse action in this case and was not required to notify the customer.⁵³

In a concurring opinion, Justices Stevens and Ginsberg disagreed with this portion of the majority opinion.⁵⁴ The justices argued that the *neutral credit score* which acted as the baseline was likely to be equivalent to a very low credit score, thus rarely triggering the notification requirement. As a result, a majority of consumers would be deprived of the notification that FCRA was intended to give them.⁵⁵

IV. Interpretation of “Willful” in Federal Civil Statutes

The more wide-reaching holding of *Safeco v. Burr* is that a willful violation of a civil statute encompasses both knowing and reckless violations.⁵⁶ Violations of both criminal and civil statutes may have an element of intent, knowledge, willfulness or recklessness which is a consideration in the degree of the offense and the remedies available. Despite the frequent use of these terms, they are not well defined and are sometimes used interchangeably, especially when applied to civil cases.⁵⁷ *Safeco v. Burr* addressed whether violations in *reckless disregard* of the requirements of a

49. *Id.* at 2211-12.

50. *Id.*

51. *Id.* at 2206.

52. *Id.*

53. *Id.* at 2212.

54. *Id.* at 2216-17.

55. *Id.* at 2217 (Stevens, J., concurring).

56. *Id.* at 2216 (majority opinion).

57. *Id.* at 2208-09.

federal civil statute are *willful*.⁵⁸ Such a determination would affect the types of damages available to the plaintiffs.

The preamble sentence of § 1681n(a) of FCRA uses the terms “willfully fails to comply.”⁵⁹ Quoting *Bryan v. United States*, the Court initially noted that the term “‘willfully’ is a ‘word of many meanings whose construction is often dependent on the context in which it appears.’”⁶⁰ In the civil context, where willful violations are included in a statute, the term has generally been construed to encompass both *knowing* and *reckless* violations.⁶¹ Under the common law, the terms “reckless,” “reckless disregard,” “willful,” and “wanton” have typically been treated as having the same meaning, or at least as having the same legal effect on civil liability.⁶² However, in criminal law, when intent is an essential element, the terms “willful” or “willfully” in criminal statutes have typically been construed to include only *knowing* violations of the law.⁶³

Relying on the legislative history of § 1681n(a), GEICO and Safeco argued that Congress intended that civil liability would only be imposed for *knowing* violations of the notice requirement.⁶⁴ The original version of the Senate Bill which ultimately became FCRA included two standards of liability: (1) a lower standard of grossly negligent violation and (2) a higher standard of willful violation.⁶⁵ Under the gross negligence standard, only actual damages were applicable.⁶⁶ However, under the willful standard, actual, statutory and punitive damages were available.⁶⁷ In later versions of the bill, the lower standard was changed to simple negligence; however, there was no change to the willful standard.⁶⁸

GEICO and Safeco argued that the lower standard of gross negligence was equivalent to “reckless disregard.” They reasoned the differentiation between the two standards in the original version of the bill indicated that Congress intended a higher degree of culpability, i.e., knowing violation, be required for a willful violation.⁶⁹ Thus, the companies argued, the original, higher standard should still apply.⁷⁰

58. *Id.* at 2208.

59. Fair Credit Reporting Act, 15 U.S.C. § 1681n(a) (2000); *Safeco v. Burr*, 127 S. Ct. 2201, 2210 (2007).

60. *Safeco v. Burr*, 127 S. Ct. 2201, 2208 (2007) (quoting *Bryan v. United States*, 524 U.S. 184, 191 (1998)).

61. *Safeco v. Burr*, 127 S. Ct. 2201, 2208 (2007).

62. *Id.* at 2209.

63. *Id.* at 2209 n.9.

64. *Id.* at 2209.

65. *Id.*

66. *Id.*

67. *Id.*

68. *Id.*

69. *Id.*

70. *Id.*

A long-held rule of construction is to “give effect, if possible, to every clause and word of a statute.”⁷¹ The Court rejected Safeco and GEICO’s proposition regarding a higher standard, noting that the use of the term “knowingly” in describing damages in § 1681n(a)(1)(B)⁷² would be “superfluous and incongruous” if Congress had intended that only knowing violations be classified as willful.⁷³ By construing both reckless and knowing violations as “willful” violations of varying degrees, the Court reasoned that both the preamble and subsections (1)(A) and (1)(B) could fulfill their purposes.⁷⁴

Other arguments advanced by Safeco and GEICO regarding the detrimental effect of construing both reckless and knowing violations as willful were also rejected by the Court. The Court indicated that reckless and knowing are “alternative[s]” and that conduct would not be both at the same time.⁷⁵ The Court also rejected the companies’ argument that reckless and willful violations are different because the wording in *another* section of the Act related to criminal violations refers to “acting knowingly and willfully.” The Court noted that “paired modifiers” are frequently used in the criminal context to further define intent, but are not significant in construing language in the civil arena.⁷⁶

Having decided that GEICO’s action did not constitute an adverse action, and having construed “willful” as including both knowing and reckless violations, the Court returned to whether Safeco’s conduct constituted a willful violation. In the civil law context, the common law has typically used an objective standard in evaluating recklessness which requires “an unjustifiably high risk of harm that is either known or so obvious that it should be known.”⁷⁷ The Court noted that there is no indication that, for FCRA, Congress intended a different meaning than the accepted common law one.⁷⁸ In applying this definition, the Court reasoned that a company would not be in violation of the notice provision if the reading of the statute was not objectively unreasonable and was merely careless.⁷⁹

71. *Safeco v. Burr*, 127 S. Ct. 2201, 2210 (2007) (quoting *Montclair v. Ramsdell*, 107 U.S. 147, 152 (1883)).

72. The measures of damages for violation are described in § 1681n(a)(1)(A) and (1)(B). Paragraph (1)(A) permits the consumer to seek either actual damages or damages between \$100 and \$1000. Paragraph (1)(B) provides for actual damages or \$1000, whichever is greater, “for obtaining a consumer report under false pretenses or knowingly without a permissible purpose.”

73. *Safeco v. Burr*, 127 S. Ct. 2201, 2210 (2007).

74. *Id.*

75. *Id.*

76. 15 U.S.C. § 1681q, r (2000); *Safeco v. Burr*, 127 S. Ct. 2201, 2210 (2007).

77. *Safeco v. Burr*, 127 S. Ct. 2201, 2215 (2007) (quoting *Farmer v. Brennan*, 511 U.S. 825, 836 (1994)).

78. *Safeco v. Burr*, 127 S. Ct. 2201, 2215 (2007).

79. *Safeco v. Burr*, 127 S. Ct. 2201, 2215 (2007). (There would be a violation of the notice requirement if “the action is not only a violation under a reasonable reading of the statute’s terms, but shows that the company ran a risk of violating the law substantially greater than the risk associated with a reading that was merely careless.”).

The Court declined to define the line between negligence and recklessness because Safeco's interpretation of the Act was not objectively unreasonable.⁸⁰ Thus, this issue is left to a future case where it is central to the controversy.

Safeco's conclusion that the adverse action and increase provisions did not apply to new customers and initial rate offerings was not an unreasonable reading of the Act.⁸¹ The Court noted that there was little guidance from the courts or the Federal Trade Commission (hereinafter "FTC") to guide interpretation of the statute.⁸² The plaintiffs argued that a letter from an FTC staff member should have put Safeco on alert that its conduct was illegal. However, the court noted that the letter was not comprehensive and was merely an "informal staff opinion."⁸³ Furthermore, the Court rejected as contrary to "history and current thinking" that "evidence of subjective bad faith can support a willfulness finding even when the company's reading of the statute is objectively reasonable."⁸⁴ Therefore, so long as Safeco's interpretation of the Act was objectively reasonable, the issue of the willfulness of its conduct would not even be raised.

As a result, the Court found that the Ninth Circuit correctly held that the term "willful" in FCRA *does* encompass reckless violations.⁸⁵ However, holding that Safeco's interpretation of the statute was not reckless, the Court reversed the Ninth Circuit's decision.⁸⁶

V. Conclusion

In *Safeco v. Burr*, the Court provided important guidance regarding the notice requirement of the Fair Credit Reporting Act and interpretation of the term "willful" in federal civil statutes. The Court held that the notice requirement of the Act applies to new customers when their credit information is used to establish initial price or rate offerings. The Court also held that an "increase" is any disadvantageous rate, even for a first time customer.⁸⁷ By adopting this broad reading of the language in the statute, the Court demonstrated its commitment to supporting the Act's purpose of giving consumers expansive protections. The holding signals to insurers and other financial institutions that where the statutory language of FCRA is

80. *Safeco v. Burr*, 127 S. Ct. 2201, 2215 (2007).

81. *Id.*

82. *Id.* at 2216.

83. *Id.* at 2216 n.19.

84. *Id.* at 2216 n.20.

85. *Id.* at 2216.

86. *Safeco v. Burr*, 127 S. Ct. 2201, 2216 (2007). *But see* *Safeco v. Burr*, 127 S. Ct. 2201, 2217-18 (2007) (Thomas, J., concurring) (commenting that he would have refrained from evaluating the merits of Safeco's interpretation since it was not critical to the decision nor argued in the briefs of the parties).

87. *Id.* at 2211-12.

susceptible to multiple interpretations, the reading that provides the maximum protection to the consumer is likely to be the correct one.

The Court also held that willfulness in the civil context includes both knowing and reckless violations.⁸⁸ This important clarification of a common law concept may have broad applicability beyond the specific facts of this case to any federal civil action in which willfulness is an element. In contrast to criminal law, where a willful violation generally requires scienter, willful violation of a federal civil statute may be found for merely reckless conduct. However, the Court reaffirmed a long-held principle that subjective bad faith is not sufficient and the inquiry into the willfulness of conduct will not be initiated if the party's reading of the statute was not objectively unreasonable.⁸⁹

88. *Id.* at 2216.

89. *Id.*