SHEAHAN et.al. v. STATE FARM, VERISK, ISO, and XACTWARE *3:18-cv-06186-EMC*

BACKGROUND

by Julia Donoho and Rebecca Mc Williams

1990's: After the Oakland Hills fire in 1991, insurers suffered big losses when contractors who rebuilt homes after disaster took advantage of the "Guaranteed Replacement Cost" coverage to charge premium rates. The moral hazard of that coverage invited excessive market escalation and insurers became determined to control post-disaster construction costs and claims payments. By 1997, "Guaranteed Replacement Cost" went away in California.

MCKINSEY: "Allstate and other insurers hired the megaconsulting firm McKinsey & Company to develop new strategies for handling claims."[1] They advised insurers to control risks and drive profits using software. McKinsey wrote reports and consulted with insurers including State Farm, Allstate, Farmers, Liberty Mutual, etc. From 1994, they advised making the claims process into a profit center by undergoing Claims Core Process Redesign (CCPR).[2]

ISO: Insurance Services Office (ISO) "was formed as an association of insurance companies to gather statistical data and other information from insurers and report to regulators, as required by law."[3] Since 1971, ISO has provided advisory services and information to many insurance companies, and provided standard forms and policies to insurers. They now offer many tools for insurance companies, including software provided to agents to create reports of property values that facilitate underwriting and speed up policy issuance. Reports are generated without owner input or agent visits to sites, despite the huge financial importance.

IPO FLIP: Insurers that used these tools were able to issue more policies, faster, and grow in the marketplace. ISO was created by the insurance companies, served insurance companies, and grew with them. ISO reorganized from non-profit to an IPO with an independent board after a six-year antitrust challenge from 20 AG's.[4] "On May 23, 2008, in contemplation of our initial public offering, or IPO, ISO formed Verisk Analytics, Inc., … to be the holding company for our business. Verisk was initially formed as a wholly-owned subsidiary of ISO. On Oct. 6, 2009, in connection with our IPO, the Company effected a reorganization

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[1] Jay M. Feinman, *Delay, Deny, Defend: Why Insurance Companies Don't Pay Claims and What You Can Do About it"* (Delden Press, 2010)

[2] Ibid., 61.

[3] *2013 Annual Report Verisk Analytics, Inc.,* SEC Form 10-K, p. 67.

[4] https://law.justia.com/cases/federal/district-courts/FSupp/723/464/1630284/

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galgadot@policyholderpros.com

whereby ISO became a wholly-owned subsidiary of Verisk."[5] The IPO of Verisk was essentially a tax play and reorganization. As well as a valve by which the owners could cash in some equity.[6] The insurers profited largely by their investment in data and continue to do so in big ways.

VERISK: Verisk's goals became more comprehensive. "The mission of Verisk Analytics is to help our customers see, understand, and manage risk — and to profit from the risks they assume."[7] In addition to analytics and catastrophe modeling, Verisk moved beyond risk and loss prediction into a more complete suite of products that are utilized for valuation, policy issuance, claims management, predictive modeling, underwriting, construction costs, etc.

XACTWARE: In 2006, before the IPO, ISO acquired Xactware Solutions, Inc., purveyor of Xactimate, a construction estimating tool that is now being used by the adjusters for most major insurers, primarily during the claims process. This is a tool designed to control claims payments using data developed from the manufactured home industry, and discounted labor and materials form insurance companies preferred providers, applying a kit of parts approach that is not reflective of market conditions. The homeowner is mostly excluded from this process, and it is a hidden activity which has tremendous effects on their net worth.

MORAL HAZARD SHIFT: The moral hazard of over or under estimating property values and construction costs shifted over to the insurance companies when insurers started using these tools because the reports are now dictating property values, policy limits, and/or controlling the cost of rebuilding whole communities without serious input of local real estate appraisers, general contractors, and the actual property owners. These are "fake" reports.

NATION-WIDE PROBLEM: This invasion of homeowner's financial privacy and personal rights with fake reports, is a nation-wide problem designed to ensure that the industry profits from disasters. The reports mine data that is personal and don't verify their sources with legitimate local resources. Agents don't know what they are selling, homeowners don't know what they are buying, and adjusters don't understand the impact of their work on the homeowners nor the communities. There is no "Truth in Insurance." The whole system is in

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[5] Ibid, SEC Form 10-K, p. 4.

[6] See: https://www.reuters.com/article/verisk-idUSN0533161120091007
" All 85.25 million shares in the IPO were being sold by Verisk's existing shareholders " Who were the existing shareholders? Principal: ESOP, Chubb, Berkshire Hathaway, AIG, CNA, Travelers, Hartford Great American, and execs from ISO/Verisk. Other Stockholders: 30 Insurance companies, and 34 affiliated industry individuals. https://www.sec.gov/Archives/edgar/data/1442145/000095012309049069/y78574b4e424b4.htm#112

[7] Ibid., *2013 Annual Report,* p. 15.

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galgadot@policyholderpros.com

trouble. Software competitors are falling away and the growth of insurance companies using Verisk tools have outpaced the rest of the market and become ubiquitous.

United Policyholders, a non-profit that helps homeowners states, "After every wildfire UP has worked since 1991, over <u>50% of the victims who thought they were fully insured turned out to be insured for less</u> - often far less - than they needed to cover repairs and rebuilding. We refer to this as **"the underinsurance crisis."** Solving it remains one of our top priorities. The vast majority of people are underinsured through no fault of their own. When they bought their insurance, an agent or insurer set the dollar amounts of coverage on their home and assured them those dollar amounts would be adequate for replacing the home,"[8] but were not.

<u>BUCK STOP</u>: Verisk is not selling insurance or software to consumers. They are creating tools for insurers that create report products that are elements and expenses of their insurance package. The reports generated by Verisk software are eviscerating the life savings of good Americans. Verisk feigns a lack of responsibility and hides behind an ephemeral screen of "economic loss doctrine," pointing back at the insurance companies and how they use the tools. Insurance companies sidestep their responsibility with assertions that they have only a general duty to sell insurance. Both are hiding from antitrust and trying to cloak themselves with McCarran Ferguson Act. But, without recourse or accountability, the buck does not stop. The goal of CCPR recommended by McKinsey was to monopolize the market and drive profits regardless of the effect on homeowners. They have succeeded. Verisk is now advertising that their software helps insurers develop obscene profits in the face of major calamities, $34 billion in profits in the first half of 2018.[9] Verisk has grown to be a multi-national data analytics company, in 32 countries, with no competition or control. The pendulum of moral hazard has swung to the profiteers.

<u>KATRINA</u>: The first big challenge of the McKinsey Report ,"CCPR," and Xactware software came after Katrina when Attorney General Foti, a New Orleans resident, worked with five local law firms to file a horizontal antitrust suit alleging conspiracy, collusion and price fixing against eight major insurers, with Xactware, Marshall and Swift, and McKinsey &

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[8] *Association of California Insurance Companies et al. v. Dave Jones, in his capacity as Insurance Commissioner for the State of California,* 2016, B248622/S226529, California Supreme Court

[9] "Property/Casualty Insurance Industry's Net Income More Than Doubles to $34 Billion in First-Half 2018," Verisk Analytics Press Release, Jersey City, N.J., October 15, 2018.

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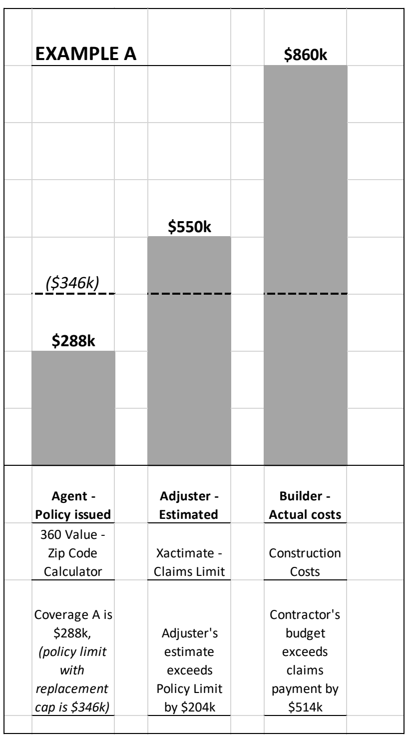
galgadot@policyholderpros.com

Company[10]. One year into the case, the Attorney General lost his re-election to a local district attorney from Shreveport who refused to prosecute the case, and it did not survive a Rule 12 motion that was resisted pro bono, making it impossible for the case to progress.

<u>FINANCIAL TECHNOLOGY</u>: The President of Verisk, claims that Insur-Tech is the way of the future in this YouTube video <u>https://www.youtube.com/watch?v=ckq0E8QNMRY</u>. Verisk may have a whole host of insurance technology tools, but the two software systems that are addressed in this suit are not insurance tools. These financial technology instruments are using big data without accurate verification to predict individual asset values, with little inquiry, controls, consistency or communication. Verisk's objectives are to "simplify consumer's interaction and dramatically reduce the time to acquisition to **<u>1 minute or less</u>**."[11] Insurance companies are invading a person's financial assets and playing games with their personal wealth, and the system has no checks and balances. Net worth is "Gone in 60 Seconds."



<u>SHAVING DRIVES HUGE PROFITS</u>: We live in a bold new age of big data and analytics. Rapidly understanding the impact of new applications of big data and schemes of monopoly that disadvantage the consumer are essential. As insurers use these tools, they drive down their own prices to be competitive and gain market share by minimizing the risk and the obligations to their bottom line, without concern for the real impact they are causing to homeowners (Example A) They are shaving a few dollars off their policy to monopolize the market, but causing homeowners in the same instant to lose **hundreds of thousands of dollars** from net worth. The disparity of shaving a policy, and the huge losses homeowners suffer from this activity is staggering.

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[10] *State of Louisiana, Ex Rel, Charles C. Foti, Jr. v. Allstate Insurance Company, Lafayette Insurance Company, Xactware, Inc., Marshall & Swift/Boeckh, LLC, Insurance Services Office, Inc., State Farm Fire And Casualty Company, USAA Casualty Insurance Company, Farmers Insurance Exchange, Standard Fire Insurance Company, McKinsey & Company.* Parish of Orleans Division L-6, Case #07-14595.

[11] *Verisk Underwriting Report 2015*, John F. Petricelli, VP Verisk Analytics, and Bill Ayscue, Sr. Product Manager, March 10, 2015.

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galgadot@policyholderpros.com

<u>HUB AND SPOKE CARTEL</u>: Verisk is the hub of a larger anticompetitive scheme and each insurer is its own spoke. State Farm is the largest offender, because they use the tools more harshly to seize a greater market share, and that is why they are named in this suit. State Farm's application of these tools fails to provide values or estimates within a 10% window of consistency one to the next, or with the market. We call on the court to now look into this whole system and find a pathway that respects the privacy and the values of the consumer first and creates a reliable, reasonable, and predictable system.

<u>MCCARRAN FERGUSON:</u> Passed in 1945**,** with a narrow exception for insurance, the McCarran Ferguson Act (15 U.S.C.A. § 1011 et seq.) did not intend to create antitrust protections for financial technology products that invade personal financial assets. Mortgages are regulated by the Financial Industry Regulatory Authority (FINRA). Financial data is protected by the Fair Credit Reporting Act (FCRA). Offering financial tools in the insurance arena does not take Verisk out of federal oversight for antitrust, FCRA and FINRA responsibility nor absolve of responsibility under state laws for practicing appraising and contracting without a license.

Verisk sells their software tools in various industries, not just to insurance companies. They strive for complete market dominance. State Farm's use of these tools with promises to provide better insurance coverage by use of the tools does not shield them with the McCarran Ferguson protections. Software is not insurance. Reports generated from software are products of the moment in time when they are created, and are intended to limit net worth rather than protect assets. If they are inaccurate, homeowners lose their life savings. Therefore, the McCarran Ferguson Act does not apply here. In addition, State Farm is specifically using the big data software tools in a way that makes the insurance policies fail, thereby epically failing to protect the assets of the consumers who are looking to these particular policies for protection.

The #EPICFAILURE of the system is not something to be protected. #FAKEREPORTS cannot hide under a 1945 act. These activities are unregulated, unlicensed, and out of control. In *<u>Spectrum Sports, Inc. v. McQuillan</u>* 506 U.S. 447 (1993) the Supreme Court said:

> "The purpose of the [Sherman] Act is not to protect businesses from the working of the market; it is to protect the public **from the failure of the market**."

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