Special Investigations Unit

Report to the Legislature

Pursuant to RCW 48.135.090

June 30, 2010

Washington State
Office of the
Insurance Commissioner

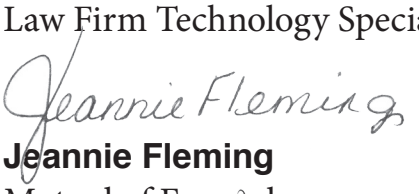
Mike Kreidler - State Insurance Commissioner

www.insurance.wa.gov

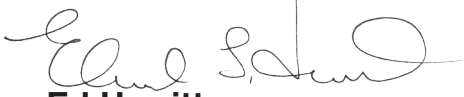
Special Investigations Unit Advisory Board

Bill Baldwin
Independent Insurance Agents & Brokers of Washington

Kent Davis
Law Firm Technology Specialists



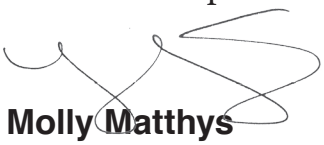
Jeannie Fleming
Mutual of Enumclaw



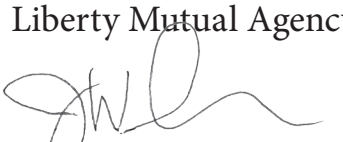
Ed Hewitt
Premera Blue Cross

David Lyons
State Farm Insurance

Dana MacDonald
Director of Operations, Area 2, National Insurance Crime Bureau



Molly Matthys
Liberty Mutual Agency Markets



Joe Wheeler
Thurston County Prosecutor's Office

Executive Summary

Four years ago, the Legislature filled a critical void in the state's ability to investigate insurance fraud by authorizing the establishment of a Special Investigations Unit (SIU) under the state Office of the Insurance Commissioner. The SIU's goal is to investigate, prosecute, and deter insurance fraud.

Insurance fraud cases, as with white collar crime in general, are often complex cases that end up as a low priority for prosecutors contending with crowded dockets and violent crime. However, if insurance fraud is not addressed, the substantial additional costs of fraudulent claims end up being paid – in the form of higher premiums – by innocent drivers, homeowners, businesses and other policyholders throughout Washington.

This report describes the effectiveness of the program, its resources and funding. It includes two legislative recommendations:

- Allow the current staffing level restriction for the unit (8 FTEs) sunset as planned on June 30, 2010,
- And maintain the unit's appropriation, which is funded from the insurance commissioner's regulatory account. The account is funded by a surcharge paid by insurers, who benefit from the unit's fraud-fighting work.

Report

The insurance commissioner and the SIU Advisory Board combine their required reports to the Legislature in this document.

The commissioner is tasked to periodically report the fraud program's activities to the Legislature, and did so last in 2008[1]. (See http://www.insurance.wa.gov/fraud/documents/report-final-2008.pdf.)

The SIU Advisory Board is specifically required to advise the commissioner and Legislature on the four key areas of staffing, effectiveness, resources and long term funding of the unit in 2010[2]; those recommendations are included in this report as well.

Effectiveness: Although still a relatively new unit, the SIU has honed its ability to triage the very large number of referrals it receives into a manageable number of high-priority cases. Organized insurance fraud can be extremely complex, with enterprising individuals fabricating incidents and hundreds or thousands of documents over the course of years.

In calendar year 2009, the unit's successful investigations resulted in $846,222 in prevented losses and restitution.

The year-to-date total for 2010 (January through June 15th) is $681,402 in prevented losses and restitution.

Major cases in progress as of the writing of this report include:

Construction fraud (2010)

SIU investigators documented dozens of cases of apparent fraud by a Seattle construction company. The fraud, totalling $470,000, was related to tree removal and repairs in the wake of a major windstorm.

- A fraudulent medical claims case totalling $860,000 in claims to three different insurers.
- An auto glass case in King County involving an estimated $1.6 million in fraudulent bills to several insurance companies.
- Another medical fraud case involving $108,000 in claims for health care that never occurred.

1 RCW 48.135.100 "The Commissioner shall prepare a periodic report of the activities of the fraud program. The report shall, at a minimum, include information as to the number of cases reported to the commissioner, the number of cases referred for prosecution, the number of convictions obtained, the amount of money recovered and any recommendations of the insurance advisory board."

2 RCW 48.135.090 "… The board shall advise the commissioner and the legislature with respect to the effectiveness, resources allocated to the fraud program, the source of the funding of the program, and before June 30, 2010, if the staffing level restriction in RCW 48.135.020(5) should be renewed."

From January 2007 through June 15, 2010, the unit's caseload has been as follows:

Cases opened	93
Cases closed	40
Cases referred for prosecution	34

Resources: The commissioner and the SIU Advisory Board are not requesting additional resources at this time. From the unit's inception, the biggest roadblock to filing criminal charges was the difficulty of getting local prosecutors to take these white-collar-crime cases. To address that issue, the SIU works closely with a half-time assistant attorney general and, recently, a half-time prosecutor in King County.

Long Term Funding of the Unit: The commissioner and the SIU Advisory Board respectfully recommend continued appropriation for the unit, even in these tight economic times. The SIU performs valuable work well. Insurers benefit, and they fund the regulatory account that provides the budget for the unit.

Staffing Level Restriction: The commissioner and the SIU Advisory Board recommend that the staffing level restriction, limiting SIU staff levels to 8.0 full-time equivalent employees (FTEs), be permitted to sunset as planned on June 30, 2010.

Background and history of the unit

The National Insurance Crime Bureau estimates that 10 percent of all insurance claims are fraudulent, adding an average of $200 to $1000 a year in higher premiums. In Washington state alone, this would mean that insurance fraud costs about $1.6 billion annually.

This translates into at least $80 billion a year nationwide, or about $950 per family. National data on health insurance fraud indicates that every dollar spent investigating health insurance fraud returns eleven dollars to the health care sector. (Please see http://www.insurancefraud.org/fraud_backgrounder.htm)

In operation since 2007, the SIU investigates insurance fraud and forwards evidence to prosecuting attorneys. It is one of 41 such "fraud bureaus" across the country.

Washington is one of eight states whose multi-line fraud bureau does not include workers' compensation. A separate fraud bureau is operated by the Department of Labor and Industries (L&I) to address workers' compensation fraud.

Our SIU refers cases to the workers' compensation fraud bureau and cooperates with them where investigations overlap.

As a region, the Northwest has a patchwork infrastructure in terms of efforts to fight insurance fraud. Washington, Alaska, Montana and Idaho all have multi-line fraud bureaus or SIUs in place, while Oregon and Wyoming do not. This makes it more challenging to address fraud cases occurring across state lines.

The SIU focuses on insurance fraud as it is defined in RCW 48.135.010:

> "(1) "Insurance fraud" means an act or omission committed by a person who, knowingly, and with intent to defraud, commits, or conceals any material information concerning, one or more of the following:
>
> (a) Presenting, causing to be presented, or preparing with knowledge or belief that it will be presented to or by an insurer, insurance producer, or surplus line broker, false information as part of, in support of, or concerning a fact material to one or more of the following:
>
> (i) An application for the issuance or renewal of an insurance policy;
>
> (ii) The rating of an insurance policy or contract;
>
> (iii) A claim for payment or benefit pursuant to an insurance policy;
>
> (iv) Premiums paid on an insurance policy;
>
> (v) Payments made in accordance with the terms of an insurance policy; or
>
> (vi) The reinstatement of an insurance policy;
>
> (b) Willful embezzlement, abstracting, purloining, or conversion of moneys, funds, premiums, credits, or other property of an insurer or person engaged in the business of insurance; or
>
> (c) Attempting to commit, aiding or abetting in the commission of, or conspiracy to commit the acts or omissions specified in this subsection.

False medical claims (2010)

A Kelso woman filed 96 claims from eight alleged family accidents. These included: severe fireworks burns, a tractor accident resulting in amputation, and a major car accident. All were fictitious. She pleaded guilty to attempted insurance fraud and has repaid nearly $215,000 in false claims.

> The definition of insurance fraud is for illustrative purposes only under this chapter to describe the nature of the behavior to be reported and investigated, and is not intended in any manner to create or modify the definition of any existing criminal acts nor to create or modify the burdens of proof in any criminal prosecution brought as a result of an investigation under this chapter."

In summary, insurance fraud consists of fraudulent activities committed by applicants for insurance, policyholders, third-party claimants, vendors paid by insurance or professionals who provide insurance services.

Categories of fraud and penalties

Insurance fraud can be "hard" or "soft."

Hard Fraud: When a criminal fakes an accident, injury, theft, arson or other loss, or takes out a life insurance policy intending to kill the insured, intending to collect money illegally from insurance companies, the criminal commits hard fraud. Increasingly, organized crime rings stage a series of events that steal millions of dollars.

Soft Fraud: Policyholders commit fraud by telling small lies as well, such as inflating the value of an item stolen from their home, or claiming that a bumper was damaged in an accident when it was damaged beforehand. These are generally "opportunistic" crimes.

When prosecutors succeed, the court may order that the perpetrator reimburse the insurance company, reducing overhead and the claims paid ratio for the company, which in turn supports lower premiums.

Moving van fraud (2010)

A Lewis County couple claimed that nearly $17,000 in property was damaged by rain leaking into a rental truck. But water tests on the truck found no leak, and weather reports that day showed little or no rain. The Lewis County prosecutor has charged the couple with insurance fraud.

In addition, in Washington the court may impose fines of between $1,000 and $250,000, with average jail time of between 10 and 16 months, and probation terms of between 3 and 20 years. (RCW 10.93.020.) Successful prosecutions also help deter future fraud.

Work and staffing of the Special Investigations Unit

Referrals and tips come to the SIU from several sources:

- Insurance company special investigations units
- National Association of Insurance Commissioners referrals
- National Insurance Crime Bureau referrals (operated by ISO)
- Prosecutorial or law enforcement referrals, and
- Individual tips.

Supervised by an executive director, the SIU staff includes:

- Three criminal investigators
- One criminal analyst specializing in high level analysis of fraud-related data and maintaining evidence
- One administrative assistant, and
- A Washington State Patrol detective sergeant.

In addition, the National Insurance Crime Bureau provides an agent, paid by the NICB, to provide expert advice and act as a conduit between the SIU and insurance companies' own fraud investigators.

This cohort does not exceed the restriction limiting staff to not more than 8 FTEs, imposed by the Legislature in the SIU's authorizing statutes. RCW 48.135.020(5). That restriction expires June 30, 2010.

This staffing level is somewhat low compared to other states' anti-fraud units, although apples-to-apples comparisons are difficult since workers' compensation fraud in Washington is handled by a separate agency, the Department of Labor and Industries.

Auto glass fraud (2010)

A Battle Ground auto glass installer pleaded guilty in February 2010 to a billing scheme in which he submitted bogus, inflated invoices for repairs. An SIU search found more than 100 such cases. The installer pleaded guilty to first-degree theft and agreed to repay $100,000.

According to the Coalition Against Insurance Fraud's 2007 report on state insurance fraud bureaus, the average number of fraud unit employees in 2006 was

33. Some states, like California and New York, have anti-fraud units with hundreds of employees.

In most state anti-fraud units, 40 percent to 60 percent of staff are devoted to workers' compensation issues. In Washington state, the state workers' compensation fraud unit numbers 63 people[3]. The SIU, as noted above, is comprised of 8 FTEs.

In most state fraud units, investigators comprise most of the staff. This is also true in Washington. In Washington, SIU investigators are commissioned law enforcement officers with arrest authority. A criminal analyst provides support on cases.

Referrals and Tips

All work begins with a referral to the SIU. For insurance fraud, there is always an insurer involved as the victim of the alleged fraud, and typically also as the holder of critical evidence needed to evaluate and investigate the case. As required by a statutory mandate, insurers report cases of suspected fraud by flagging those claims in an insurance industry database, which is checked daily by an SIU analyst.

Disability insurance fraud (2010)

A West Seattle man was paid more than $26,000 in medical expenses and disability benefits after a back injury allegedly left him unable to work. His doctors reversed their opinion when shown videotape of him vigorously sanding, painting, climbing and moving machinery while working on his sailboat at a Seattle marina. He pleaded guilty to first-degree theft.

Referrals received by the SIU vary dramatically in terms of usefulness for building a criminal case. Some are multi-page reports with excellent documentation. Others are little more than tips, or are cases in which the statute of limitations has expired. Although the information provided by insurers is sufficient for them to make a determination of whether or not to pay a claim, a majority of these referrals do not include documentation to support a charge of criminal insurance fraud, which requires proof beyond a reasonable doubt.

To meet that standard, the SIU must triage the incoming information and be selective about which cases to devote resources to. The unit must determine what evidence exists, its sufficiency, and the likelihood that further investigation will develop the neccesary proof of fraud.

3 Coalition Against Insurance Fraud, "State Insurance Fraud Bureau Report 2001-2006" (February 2007) at 10.

Once the SIU has determined that a case should be prepared for prosecution, the team uses its subpoena authority to obtain records and interview witnesses. Most SIU cases require substantial, detailed investigation before meeting the standards of a criminal prosecution.

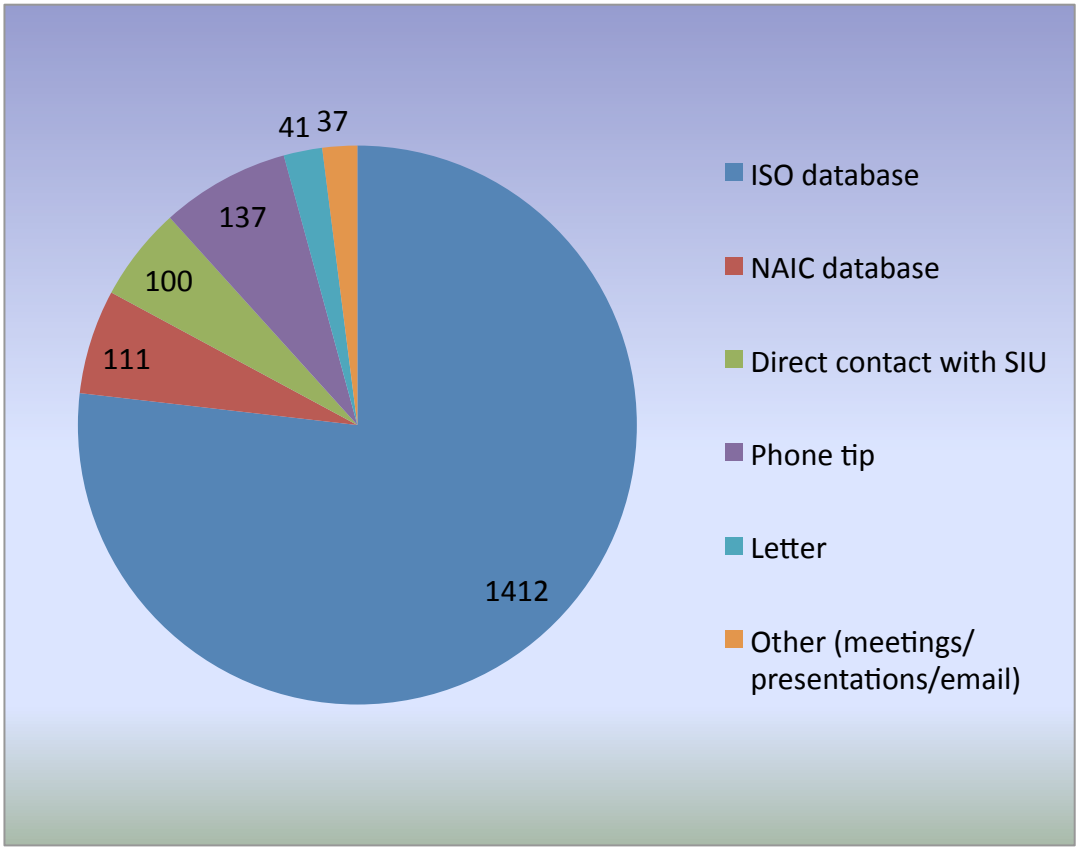
Sources of referrals and tips

Most referrals come to the SIU through the National Insurance Crime Bureau (NICB). Insurers and other participating organizations report claims data and information to the Insurance Services Office (ISO); the NICB does the referrals. This data is available to the SIU; the referrals through ISO relate to property, casualty and auto claims.

The National Association of Insurance Commissioners (NAIC) is another source of referrals. The NAIC maintains an online fraud reporting system that consumers and the insurance industry may use to report fraud. When a report is made through the system, the NAIC forwards it to the appropriate state regulator for assessment and follow-up.

Beginning this year, insurers have been able to file a single report to multiple state insurance departments, which means there will not be separate streams of referrals from the NICB and the NAIC in the future. All reports will stream through the NAIC system. This will help identify possible fraud occurring across state lines because states will share a single report where the fraudulent activity is identified in more than one state. The only states not participating are New York, New Jersey, Rhode Island, Kentucky, Pennsylvania and Wisconsin.

Here's a breakdown of referrals, by source, in 2010:

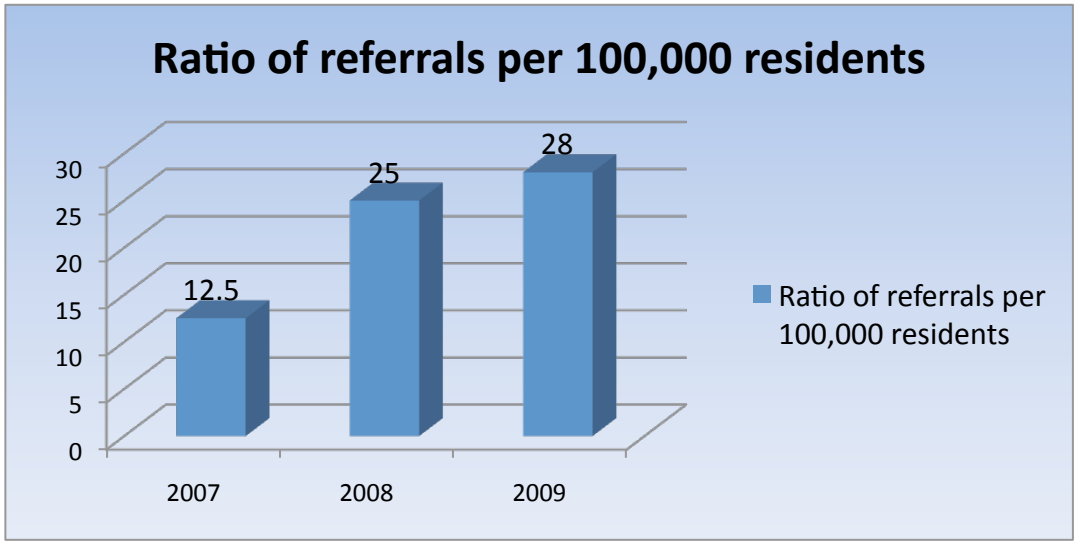


The total number of referrals and tips is growing, a fact we attribute to increased reporting by the major databases, as well as increased awareness of the unit and its role.

Referral Source	2007	2008	2009
NICB database	575	1230	1412
NAIC database	112	122	111
Direct Contact- SIU	51	124	100
Phone	30	146	137
Letter	19	15	41
Other (meetings, presentations, email)	23	15	37
TOTAL	**810**	**1651**	**1838**

2009 data from Special Investigations Unit, Office of the Insurance Commissioner

The referral data shows an initial doubling of referrals from year one to year two of operation, and a 15 percent increase in referrals between years two and three.



While the SIU has enjoyed significant growth in referrals, however, it does not approach the national average. In 2006, the national average of referrals was 43 per 100,000 residents. In Washington, in 2009, the average of referrals was 28 per 100,000 residents. This is most likely because other states with anti-fraud units can typically accept more referrals due to larger staff size, and a broader scope of authority, as their referral ratios typically include workers' compensation fraud in addition to the lines of business our SIU addresses.

From January through June 15th, 2010 the SIU received 767 referrals. Thus far, 11 have been opened as cases, with nine of those referred for prosecution.

Statistical data, restitution and loss prevention

Required Reporting Area (RCW 48.135.100)	Number
Number of referrals and tips reported to the insurance commissioner in 2009	1,838
Number of cases opened	29
Number of cases referred for prosecution	10
Number of convictions obtained	10
Restitution	$80,979
Additional information	
Immediate loss prevented	$193,000
Projected loss prevented	$572,243
Total restitution and loss prevented	$846,222

2009 Data from Special Investigations Unit, Office of the Insurance Commissioner

As previously mentioned, only a small number of the referrals are opened as cases. A significant number of referrals involve areas over which the unit has no jurisdiction, such as consumer complaints about health care providers or concerns about the high cost of health care. Over the past three years, the SIU has developed criteria for opening a referral as a case that is limiting, based on both available staff capacity and the potential beneficial impact pursuing the matter may have.

The Legislature's intended focus for the SIU was organized fraud against insurance companies. (RCW 48.135.005[4].) Insurance company reporting primarily occurs through the now-consolidated NICB – NAIC channel. A key focus of the SIU staff is community outreach to help educate consumers and service providers about fraud indicators, so that possible fraud can be reported, investigated and addressed even before companies note a claim payment or request pattern.

Prosecution

Prosecutors in Washington state's 39 counties are committed public servants with overwhelming dockets. The Legislature empowered the SIU to:

> " (g) Report incidents of alleged insurance fraud disclosed by its investigations to the appropriate prosecutorial authority, including but not limited to the attorney general and to any other appropriate law enforcement, administrative, regulatory or licensing agency; (h) Assemble evidence, prepare charges, and work closely with any prosecutorial authority having jurisdiction to pursue prosecution of insurance fraud;"
> (RCW 48.135.040(1)(g) and (h).)

In the first three years of operation, cases sent to prosecutors ranged between six and 10 per year. In just the first six months of 2010, the unit has already referred nine cases to prosecutors.

As a relatively new unit, the SIU's approach to preparing matters for prosecutors focuses on referring cases that are significant in terms of frequency or severity of the fraud. The ability to properly work up a case is limited to the number of staff available. When the SIU was proposed, the Legislature was told that "a program similarly structured to the one proposed for Washington, Utah produced 82 criminal prosecutions, 12 civil actions and $7.8 million in ordered restitution

4 RCW 48.135.005 states: The purpose of this chapter and sections 14 through 17, chapter 284, Laws of 2006 is to confront the problem of insurance fraud in this state by making a concerted effort to detect insurance fraud, reduce the occurrence of fraud through criminal enforcement and deterrence, require restitution of fraudulently obtained insurance benefits and expenses incurred by an insurer in investigating fraudulent claims, and reduce the amount of premium dollars used to pay fraudulent claims. The primary focus of the insurance fraud program is on organized fraudulent activities committed against insurance companies.

in 2002." [5] A 2009 audit of the Utah Insurance Fraud Division[6] determined that 20 percent of those cases did not involve insurance, bringing Utah's results into alignment with those of Washington's SIU in terms of prosecution results for its first three years of operation. On average, a third of all cases opened for full investigation by the SIU are referred to a prosecutor.

As mentioned earlier, a key variable in the number of cases being prosecuted is the willingness of prosecutors to accept the cases. In Washington, most referrals fitting the profile of "organized insurance fraud" – a priority category for the SIU – occur in King County. Insurance fraud falls under the purview of the county prosecutor's economic crimes unit, which the King County Prosecutor's Office describes as having the following focus:

"Cases handled by the Economic Crimes Unit cover a wide range of crimes from simple thefts and narcotics cases to complex organized criminal activity, including: public corruption, abuse of office, employee thefts, insurance frauds, environmental crimes, investment frauds, mortgage frauds, aggravated consumer frauds, frauds against the elderly and vulnerable victims, frauds against government, and technology crimes. They also maintain a focus on prosecuting the top identity theft offenders in the county."[7]

The SIU has a policy of not referring a case for prosecution unless the receiving prosecutor's office is prepared to handle it. Otherwise, statutes of limitation may expire or other technical barriers to success may undercut a well-developed fraud case. Due in large part to the broad charge to King County's Economic Crimes Unit and an already full docket for the prosecutors assigned to this unit, it was often difficult for the SIU to find open space for its cases on the docket. The same is true in some other counties, due to budget limitations and lack of expertise with insurance fraud.

Stolen property fraud (2010)

A Snohomish County woman forged and altered thousands of dollars in receipts as part of a claim for stolen property. As part of a diversion agreement, she admitted the fraud and paid back $66,610 in restitution.

The Legislature wisely authorized the SIU to make grants to or reimburse the local prosecuting attorneys that assist in the prosecution of insurance fraud. (RCW 48.135.020(4))

5 Office of the Insurance Commissioner Fact Sheet, Fraud Investigation Units (2006)

6 Report to the Utah Legislature, Number 2009-09 A Performance Audit of the Insurance Fraud Division (June 2009)

7 http://www.kingcounty.gov/prosecutor/criminaloverview.aspx#economic

Faced with the realities of trying to bring a case to closure in the state's most populous county, the SIU recently launched an approach in King County that is working well for both the county and the SIU. Specifically, the Insurance Commissioner's Office agreed to pay for a half-time prosecutor and associated support staff to handle insurance fraud prosecutions in King County. The contract, not to exceed a total of $131,750 over a 16-month period, runs from Feb. 1, 2010 through June 30, 2011.

In addition, the Attorney General's Office may prosecute insurance fraud matters. The SIU has an assistant attorney general assigned to the unit, primarily to handle prosecutions in the state's other 38 counties. (RCW 48.135.020(3) One challenge has been the fact that since launching operations in 2007, the SIU has had three different assistant attorneys general assigned to it. Early on, turnover and each new assistant attorney general's understandable need to learn both the SIU and the types of cases limited the effectiveness of this resource to increase prosecution. Currently, the assistant attorney general assigned has been in place for over a year, and is an effective member of the SIU team.

Restitution and Return on Investment

The actual restitution ordered by a court or agreed to by the defendant in SIU-referred cases has varied:

Year/ Amount	2007	2008	2009	2010 (YTD)
Actual dollars	$139,254	$14,386	$80,979	$131,402

Figure 2: Office of the Insurance Commissioner data from Special Investigations Unit, May, 2010.

During calendar year 2009, the SIU began tracking the "immediate loss" prevented by its efforts. Immediate loss means the identifiable amount of claims that the insurer would have paid if the fraud had not been successfully detected and prosecuted. In 2009, the unit identified $193,000 in immediate loss prevented, with an additional $572,243 in projected savings from activity that the unit knows the criminals had planned, but were not able to accomplish.

From January 2010 through June 15, 2010, the unit's cases resulted in $131,402 in restitution and $550,000 in immediate loss prevention.

Recommendations

Effectiveness Assessment: The Special Investigations Unit is effective at identifying the most significant cases in terms of frequency of fraud or severity of fraud, and preparing those cases for referral to prosecutors.

Resources Assessment: There are five key resources for the Special Investigations Unit. They are:

1. **Qualified Staff:** Current staff is qualified and skilled at performing their work, based both on the outcomes of cases referred to prosecutors and the report of the SIU's executive director. Four investigators are the minimum number to triage and follow up on almost 2,000 referrals each year.

2. **Prosecutorial Will and Capacity:** This is the most challenging aspect of delivering measurable outcomes. Prosecutors have been slow to encourage case referral, because they have limited resources. The SIU is committed to using the tools the Legislature provided in RCW 48.135.020 to encourage county prosecutors to move these cases forward. The new contract with the King County Prosecutor's Office is helping the unit address this issue.

3. **Continuing Referrals:** With the advent of the combined reporting system from NAIC and NICB, the SIU anticipates receiving more referrals with the ability to identify multi-state opportunities for investigation and prosecution. The industry is clearly aware of the benefits of the SIU, and is committed in reporting claims identified as potentially fraudulent to the unit.

   The SIU also has an ongoing effort to educate the public about insurance fraud, through speakers and by publicizing the unit and its efforts. This remains an integral part of the unit's ongoing business activity, to encourage increased public reporting of potential fraud and to deter fraudulent activity.

4. **Quality and Availability of Information:** At times, insurers are reluctant or do not understand their ability to provide the SIU with necessary original evidence relating to an investigation. This can delay an investigation or compromise the SIU's ability to refer the matter to a prosecutor. Insurers may refer a matter believing their work-up is sufficient for a criminal prosecution, when in actuality it only supports the exercise of their discretion to deny a claim. If the claim is denied, vital information and evidence is often sent to storage or archives, and insurer cooperation to retrieve it is essential. Part of the unit's ongoing business plan includes insurer education about the work of the SIU, and the higher burden of proof

in criminal cases that requires their cooperation in producing original evidence to support a case.

5. **Time:** The unit must refer cases to a prosecutor that can be prepared and charged within the applicable statute of limitations. Depending on when the case is received by SIU, some matters are not even investigated because the fraud occurred too far in the past to prosecute.

Source of Funding for the SIU: The current source of funding is the insurance commissioner's regulatory account, which is funded through a surcharge paid by insurers. This continues to be the appropriate source of funding for the activities of the SIU. That said, additional funds for dedicated prosecution capacity in the future would help the state leverage its investment in fraud prevention.

Staffing Limitation: The limitation on staffing should be permitted to expire, and not be renewed after June 30, 2010.

Conclusions

Although still relatively new, the Special Investigations Unit, continues to build on its efforts to combat fraud. The SIU staff has gained valuable expertise in handling these specialized cases, and the recent addition of the half-time King County prosecutor will help move additional cases to trial or pleas.

As a result of the SIU's work, we look forward to increased restitution and lower loss ratios arising from fraud-related claims. We are particularly encouraged by the unit's 2010 data to date, and believe that the unit is gaining respect among the law enforcement, insurance, and prosecution communities.

In short, the unit serves a valuable role for Washingtonians by investigating and deterring fraudulent claims, which helps keep auto, health, property and casualty insurance premiums low. Without the state's involvement and growing investigative expertise in this arena of financial crime, these cases would, in many instances, go unprosecuted.