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INSURANCE

Halted health coverage suit may be far-reaching

An appeals court will weigh Blue Shield's retroactive cancellation of a car-crash patient.

By Lisa Girion

Times Staff Writer

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A 2001 car accident that left Steven Hailey badly injured was the beginning of his continuing medical and financial calamity.

While Hailey was still recovering in his Cypress home and with medical bills topping \$450,000, Blue Shield of California suddenly canceled his coverage. That forced the former self-employed machinist to wait so long for surgery to repair an injured urethra, he says in a lawsuit against Blue Shield, that his bladder stopped working. Since then, he has depended on an implanted catheter that drains his urine into a bag strapped to his body.

Now, Hailey says, he and his wife, Cindy, can't afford the care he needs because Blue Shield began garnisheeing her wages to recoup more than \$104,000 it had paid for Steven's medical care before canceling him.

The outcome of the Haileys' case against Blue Shield could change the way insurers do business in California and influence reform efforts by state regulators and lawmakers. As the first case of its kind to reach an appellate court in California, it will test the legality of retroactive health policy cancellations, a controversial industrywide practice that has driven canceled consumers into debt and forced them to forgo needed medical treatment.

Blue Shield contends it was within its rights to cancel the Haileys because they failed to disclose Steven's true weight and full medical history when the couple applied for coverage nearly seven years ago.

Blue Shield says it would not have covered Steven in the first place had it known that his weight was 285 pounds, not the 240 listed on the application, or that he had been treated for headaches, hypertension and other conditions.

The Haileys say that Cindy made an honest mistake when she filled out the application

and that state law bans the rescission of health coverage without evidence that the policyholder intentionally misrepresented his or her medical history. Blue Shield disagrees, saying the law allows it to cancel policies for any misrepresentation, even inadvertent ones.

Whatever the 4th District Court of Appeal in Santa Ana decides could affect hundreds of suits challenging such cancellations as illegal and unfair.

Such retroactive rescissions have come under scrutiny in recent months because of the hardships they create for patients. A Los Angeles Times article detailed the turmoil of a Murrieta family whose daughter had an aggressive cancer-like tumor, a Riverside couple who sold their home to pay off medical debts and a Van Nuys small-business owner who was maxing out credit cards to get therapy for his disabled infant twins.

State regulators recently levied a \$1-million fine against Blue Cross of California, the state's biggest health insurer, over retroactive cancellations. Regulators say they are investigating other carriers, including Blue Shield.

But regulatory actions have failed to stop the cancellations, and none of the lawsuits has resolved the dispute over whether such actions violate the law. The Orange County court is poised to do that.

Noting the "broad public interest" in the test case, the appellate court invited consumer advocates, regulators and industry representatives to weigh in, an unusual move suggesting that the panel sees more at stake than just the case at hand. The court asked for briefs on the law and public policy "against improper health policy cancellations and post-claims underwriting."

"They want to know: How big is this problem?" said Amy Bach, executive director of United Policyholders, a nonprofit organization based in San Francisco, which plans to submit a brief. "Clearly, the court is smelling something bigger."

Blue Shield is one of the state's largest sellers of individual policies, the type of coverage at issue. Unlike with employment-based group coverage, which is issued to all group members regardless of health, carriers in California and some other states are allowed to reject applicants for individual policies based on their medical histories.

Blue Shield says it was conducting a routine and legal claims review when it discovered that the couple's application had purportedly shaved 45 pounds off Steven's weight and failed to disclose his health history. The health plan says it immediately mailed the couple a letter rescinding coverage.

But the letter didn't reach the Haileys before a vendor showed up at their Cypress home and repossessed Steven's wheelchair and adjustable hospital bed.

The Haileys, both now 45, declined to discuss the case on a lawyer's advice. But in court

documents, they accuse Blue Shield of launching a secret investigation while Steven was hospitalized to search for an excuse to dump them and avoid paying his bills.

The Haileys say they never tried to conceal anything. In a sworn deposition, Cindy testified that she was confused by the application and mistakenly thought it was seeking only her medical history.

Consumer advocates say the forms routinely trip up people such as Cindy because they use a single set of medical history questions for all family members.

"I've seen that happen repeatedly," said William Shernoff, a Claremont lawyer who represents policyholders but not the Haileys.

The error is so common, Shernoff said, that he is trying to persuade insurers to use separate medical questionnaires for each member of a family seeking coverage.

The Haileys don't fit the profile of people who insurers typically say have an incentive to lie about preexisting conditions to obtain coverage. They could have gotten guaranteed group coverage through Cindy's employer.

They said they turned to Blue Shield because a physician Cindy wanted to continue seeing was not in her employer's health plan. The physician was in Blue Shield's network, so, in November 2000, she filled out the application, listing only her treatment for a digestive condition.

Blue Shield issued coverage in December. Steven was injured in March 2001. The carrier rescinded coverage in June.

Blue Shield says its application's request for information on all applicants was clear. The carrier also says the law allows insurers to take applications at face value. Anything else would be unworkable, said John LeBlanc, a lawyer for Blue Shield.

"If the company were required to investigate every response on an application, despite what the applicant says ... the burden would be placed on the insurance company to investigate everything," he said.

Cindy Ehnes, director of the California Department of Managed Health Care, which regulates health plans, recently sided with consumers, saying a 1993 state law clearly bars insurers from rescinding policies unless they can prove a policyholder engaged in "willful misrepresentation" on an application.

Ehnes' office plans to file a friend-of-the-court brief at the Haileys' request and is drafting regulations aimed at curbing cancellations. Her proposal is expected to require carriers, among other things, to develop clear and simple applications and to limit how much medical history they ask applicants to accurately remember.

Ruling without trial in the Haileys' lawsuit against Blue Shield, Orange County Superior Court Judge Corey Cramin upheld the cancellation in 2005 and ordered the couple to repay the carrier \$104,192 — the amount the carrier says it spent on Steven's care before dropping him.

Before the accident, Steven owned and operated a small plant that made hydraulic presses for the ceramics industry. The disruption in coverage forced him to wait several months longer than his physician desired for the operation to repair his urethra, the Haileys say.

Often in pain and unable to work, Steven and his wife moved to Broken Arrow, Okla., to be closer to relatives who help care for him.

Blue Shield obtained an order from an Oklahoma judge to garnishee Cindy's wages from her job as a staffing manager for a temporary employment agency. Blue Shield's cut — \$680 a month — reduced her monthly take-home pay to \$1,714 and, the Haileys say, made it impossible to pay for all the medical care and therapy that Steven needs.

They "are barely hanging on," Michael Nutter, one of their lawyers, wrote, urging the Orange County appellate court to stop the garnishment. Blue Shield argued that if the couple was so hard up, they could file for bankruptcy.

The appellate court sided with the Haileys in December, issuing a temporary halt to the garnishment.

lisa.girion@latimes.com