NO. 91494

IN THE SUPREME COURT OF ILLINOIS

MICHAEL E. AVERY, et al., on behalf of themselves and all others similarly situated,

Plaintiffs-Appellees-Respondents.

vs.

STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY,

Defendant-Appellant-Petitioner.

On Appeal from the Appellate Court of Illinois Fifth District No. 5-99-0830

There Heard on Appeal from the Circuit Court for the First Judicial Circuit Williamson County

No. 97 L-114

John Speroni,
Judge Presiding

AMICUS CURIAE BRIEF OF UNITED POLICYHOLDERS IN SUPPORT OF THE POSITION OF CLASS PLAINTIFFS-APPELLEES-RESPONDENTS

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INTEREST OF AMICUS CURIAE

United Policyholders was founded in 1991 as a non-profit organization dedicated to educating the public on insurance issues and consumer rights. The organization is tax-exempt under Internal Revenue Code §501(c)(3). UP is funded by donations and grants from individuals, businesses, and foundations.

In addition to serving as a resource on insurance claims for individuals and commercial insureds, UP monitors legal and marketplace developments affecting the interests of all policyholders. UP receives frequent invitations to testify at legislative and other public hearings, and to participate in regulatory oversight proceedings.

A diverse range of policyholders throughout the United States communicate on a regular basis with UP regarding the insurance claims process. Because UP monitors both marketplace developments and policyholders' real life experiences, the organization is qualified to provide topical information to courts throughout the country via the submission of *amicus curiae* briefs in cases involving insurance principles that are likely to impact large segments of the public. Class action proceedings are of particular interest to our organization because they provide an important remedy for policyholders who are victimized by unfair insurance practices but cannot seek redress because of the economic realities that make it impossible to pursue small dollar disputes in court.

United Policyholders' *amicus curiae* briefs have been accepted by courts throughout the country. *See, e.g., Humana, Inc. v. Forsyth*, 525 U.S. 299, 313-14 (1999) (citing to pages 19-23 of Brief for United Policyholders as *Amicus Curiae*); *Vandenberg v. Superior Court*, 88 Cal. Rptr. 2d 366 (Cal. 1999); *Western Alliance Ins. Co. v. Gill*,

686 N.E. 2d 997 (Mass. 1997).[1] UP has filed *amicus* briefs on behalf of policyholders in over one hundred cases throughout the United States since 1992.

SUMMARY OF ARGUMENT

1. A class action proceeding was the correct vehicle for remedying the fraudulent practices adjudicated in the trial court.

As a practical matter, the policyholders affected by the State Farm practices at issue in this case could not have brought individual suits to vindicate their rights under their automobile insurance policies. The dollar amounts in controversy were far too small, ($51 on average), to permit anyone -- consumer or attorney, to have filed suit without spending far in excess of the actual damages sustained. Insureds frequently find themselves in this position. Yet, the practices were fraudulent, affected a defined class of policyholders, and warranted a remedy. A class action proceeding was the appropriate vehicle to provide that remedy. The trial court determined that in each policy sold to class members, State Farm made the identical promise to pay for parts "of like kind and quality" that would restore the vehicle to its "original pre-loss condition". The trial court further determined that State Farm breached that promise as a matter of course both in and outside Illinois, and was unjustly enriched as a result. It fashioned a remedy that was consistent with the evidence and tailored to deprive the defendant of unjust profits and deter future misconduct.

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[1] *See also, Fleming v. United Services Auto. Assoc.*, 988 P.2d 378 (Or. 1999); *Peace v. Northwestern Nat'l Ins. Co.*, 596 N.W. 2d 429 (Wis. 1999); *United States v. Brennan*, 183 F.3d 139 (2d Cir. 1999); *Board of Ed. of Township High School Dist. No. 211 v. International Ins. Co.*, 720 N.E.2d 622 (Ill. App. Ct. 1999), *appeal denied*, 729 N.E. 2d 494 (Ill. 2000); *Carter-Wallace, Inc. v. Admiral Ins. Co.*, 712 A.2d 1116 (N.J. 1998); *Guaranty Nat'l Ins. Co. v. George*, 953 S.W.2d 946 (Ky. 1997).

2. **The trial court correctly applied the law of the state where the defendant chose to be domiciled.**

Logic and well-established law dictates that Illinois may police its own resident corporations with regard to their conduct. Because State Farm operates on a national scale, issuing standardized policies to consumers throughout the United States and engaging in standardized claims practices from state to state, State Farm's conduct in Illinois naturally affects residents of other states. It is logical therefore to regulate its conduct both in and outside Illinois with regard to a well-defined class of policyholders by applying the laws of the state where State Farm is domiciled. The McCarran-Ferguson Act does not disturb this logic. The Act is not and should not be made an issue in this case.

3. **All major insurers operate nationally and are *de facto* regulated through coordinated efforts by states and the federal government, the National Association of Insurance Commissioners and a host of national trade associations.**

Applying the law of the state in which an insurer is domiciled is consistent with the coordinated modern approach to insurance industry regulation.

ARGUMENT

1. **A class action proceeding was the correct vehicle for remedying the fraudulent practices adjudicated by the trial court.**

Insurance policyholders are very frequently subjected to unfair business practices like those adjudicated in this case where it is not economically feasible for them to bring suit as an individual to stop the practice but where the practice is affecting large numbers of other insureds and is unjustly enriching an insurer. Because of the small amount of actual damages sustained by the policyholders affected by State Farm's fraudulent use of non-OEM parts, this case presents a classic example of one suited for a class action

proceeding. The policy objective behind class actions is to encourage individuals, who may otherwise lack incentive to file individual actions because their damages are limited, to join with others to vindicate their rights in a single action. *Hansberry v. Lee*, 311 U.S. 32, 41, 85 L. Ed. 22, 27, 61 S. Ct. 115, 118 (1940).

Class actions are particularly important in consumer protection cases because individual suits are often not economically feasible. *Hoover v. May Department Stores Co.*, 62 Ill. App. 3d 106, 112, 378 N.E.2d 762, 768 (1978), *rev'd on other grounds*, 77 Ill. 2d 93, 395 N.E.2d 541 (1979). The slight loss to the individual, when aggregated in the coffers of the wrongdoer, results in recovery that is worthy of an attorney's time and costs of litigation and that provides some measure of restitution to the injured party and deterrence to the wrongdoer. See *Hoover*, 62 Ill. App. 3d at 112, 378 N.E.2d at 768; *Gordon v. Boden*, 224 Ill. App. 3d 195, 204, 586 N.E.2d 461, 467 (1991).

As the Court of Appeal aptly stated, "Based upon even a cursory review of this record, there is little doubt that any individual cases would be defended as vigorously as the case at bar. The costs of pursing the case on an individual basis would greatly exceed any recovery." Citing to *Gordon*, 224 Ill. App. 3d at 203-04, 586 N.E.2d at 467. The remedy of a class action suit was therefore appropriate.

During a pretrial hearing conducted to determine class certification the trial court considered documents and testimony from several witnesses then certified a narrowly defined class. The trial court reviewed State Farm auto policies issued to class members who resided in states other than Illinois. It found variations in the form of the policy from state to state, but concluded that they were immaterial because the *operative policy language in each policy was susceptible to uniform interpretation.* The court determined

that in each policy State Farm made the identical promise to pay for parts "of like kind and quality" that would restore the vehicle to its "original pre-loss condition".

As a business that chose to domicile itself in Illinois and avail itself of the protection of Illinois law, and as a defendant who has been adjudged by the lower courts to have engaged in wrongful conduct that was directed and controlled by executives in Illinois, State Farm cannot justifiably complain about the application of Illinois law to its conduct, regardless of where its customers ultimately suffered the consequences.

2. The McCarran-Ferguson Act does not bar Illinois from applying its laws to police State Farm's conduct emanating from within its borders but affecting in and out-of-state residents.

The McCarran-Ferguson Act's primary purpose was to restore to the states broad authority to tax and regulate the insurance industry. *United States Department of Treasury v. Fabe*, 508 U.S. 491 (1993). It sets forth a special insurance-related anti-pre-emption rule. That rule provides that a federal law will not pre-empt a state law enacted "for the purpose of regulating the business of insurance" - unless the federal statute "specifically relates to the business of insurance." 15 U.S.C. 1012(b) There is no federal law or preemption issue in this case, therefore the McCarran-Ferguson Act is irrelevant.

State Farm argues that the Act bars Illinois from applying its laws to regulate auto claims practices that affect both Illinois and non-Illinois residents. Neither the Act nor cases interpreting the Act impose such a ban. State Farm cites the case of *FTC v. Traveller's Health Assoc.* 362 U.S. 293 (1960) in support of its position, but to no avail. This Court in *FTC v. Traveller's* examined the preemption issue and held that an insurer could be simultaneously subject to the laws of its domicile state with regard to

advertising materials sent out of state and subject to regulation by the Federal Trade Commission. The three Justices who objected to upholding the FTC's jurisdiction specifically highlighted in their dissent that nothing in the majority's decision undermined the law that states have the right to police their own insurance company domiciliaries with respect to activities affecting citizens of other states. *FTC v. Traveller's* 392 U.S. at 305, citing *Hammond Packing Co. v. Arkansas*, 212 U.S. 322 (1909) *Sligh v. Kirkwood*, 237 U.S. 52 (1913). The trial court here correctly applied the law of the state where the defendant chose to be domiciled.

3. **Because all major insurers operate nationally, they are regulated through coordination by state and federal government, the National Association of Insurance Commissioners and a host of national trade associations.**

The idea that insurance companies operate on a state by state basis and the idea that insurance companies are regulated on a state by state basis are as moribund as the "state's rights" cries of 50 years ago. The National Association of Insurance Commissioners ("NAIC"), administers much of the regulation of insurance in a coordinated fashion. State insurance laws are promulgated through coordination among state legislators who serve on the insurance committees of their respective legislatures under the aegis of the National Conference of Insurance Legislators ("NCOIL"). For generations the Federal Bureau of Investigation (FBI) has provided more investigative services and criminal prosecution to the insurance industry than to the banking industry.

Insurers influence public policy and legal developments in Washington, D.C. and in legislatures throughout the United States through national organizations including the American Insurance Association and the Alliance of American Insurers. The Securities

and Exchange Commission regulates publicly held insurance companies. The Federal Trade Commission regulates insurance industry mergers.

Robert W. Klein, Director of Research for the National Association of Insurance Commissioners (NAIC), addressed the current state of coordinated regulation of insurance companies in the well-respected trade publication, The Journal of Risk and Insurance, Volume 62, No. 3, (September 1995):

> -Insurance markets have increasingly become national and international in scope, as insurers have widened the boundaries of their operations.[2]
>
> -Insurers are required to file uniform annual financial statements for the previous calendar year by March 1 with their domiciliary state, every state in which they are licensed to do business, and the NAIC. *Id at 3.*
>
> -State regulators operate on a multi-state basis: States generally prioritize the review of their domiciliary companies and any other companies which require expedited scrutiny. Most departments utilize some system of financial ratios or other tools to screen and prioritize insurers for analysis. Regulators also use NAIC financial information systems including the Insurance Regulatory Information System (IRIS) which includes the Financial Analysis and Surveillance Tracking (FAST) system, and other reports. *Id. at 3-4.*
>
> -Solvency examinations are done on a multi-state basis. The NAIC encourages the use of "association" or "zone" examinations in which various states participate to consolidate efforts and avoid duplicative and

redundant examinations of the same company. The NAIC's Financial Condition (EX4) Subcommittee also may encourage non-domiciliary states to call a special association examination if an examination conducted by a company's domiciliary is inadequate or if the domiciliary state fails to conduct an examination when financial ratio results or other information indicate the need. *Id. at 4.*

-The National Association of Insurance Commissioners, ("NAIC") serves as a national coordinating agency for state insurance regulators. Policing a large and diverse insurance industry, operating on an interstate bases, has been a particular challenge for the individual states. Insurance commissioners have used their national association extensively in coordinating their regulatory activities. The NAIC is a private, non-profit association of the chief insurance regulatory officials of the 50 states, the District of Columbia, and the four territories. It was established in 1871 to coordinate the supervision of multistate companies within a state regulatory framework, with special emphasis on insurers' financial condition. The NAIC functions in an advisory capacity, as well as a service corporation for state insurance departments.

-State regulators are able to achieve considerable efficiencies by pooling resources through the centralized facilities provided by the NAIC. For example, it is much more efficient to have one central repository of insurer financial data than for every department to capture the same data from the

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[2] Robert W. Klein, Structural Change And Regulatory Response In The Insurance Industry, Insurance Regulation in Transition, June 19, 1995, at 1. *Journal of Risk and Insurance*, Vol. 62,

same insurer. The objective is to allow states to focus their resources on regulation of their markets and the solvency of their domiciliary companies, relying on support services from the NAIC.

-The NAIC supports state regulatory efforts in a number of ways, including: 1) maintaining an extensive insurance database and computer network linking all insurance departments; 2) analyzing and informing regulators as to the financial condition of insurance companies; 3) coordinating examinations and regulatory actions with respect to troubled companies; 4) establishing and certifying states' compliance with minimum financial regulation standards; 5) providing financial, reinsurance, actuarial, legal, computer and economic expertise to insurance departments; 6) valuing securities held by insurers; 7) analyzing and listing non-admitted alien insurers; 8) developing uniform statutory financial statements and accounting rules for insurers; 9) conducting education and training programs for insurance department staff; 10) developing model laws and coordinating regulatory policy on significant insurance issues; and 11) conducting research and providing information on insurance and its regulation to state and federal officials and the general public. *Id at 7.*

-The NAIC's risk based capital requirements are designed to be uniform among states. *Id. at 9.*

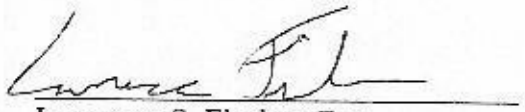
CONCLUSION

No.3, Sept. 1995.

For the reasons enumerated above, United Policyholders respectfully submits that this matter was properly adjudicated in the trial court and the result was appropriately upheld in the Court of Appeal.

DATED: February 14, 2003

Respectfully submitted,



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CERTIFICATE OF SERVICE

I, Lawrence Fischer, an attorney, on oath state that I filed 20 copies of the foregoing Brief and Argument of *Amicus Curiae* United Policyholders in support of Michael Avery, et al., Plaintiffs-Appellees-Respondents, by U.S. Mail, postage prepaid, to the Office of the Clerk of the Illinois Supreme Court, Supreme Court Building, 200 E. Capitol Ave., Springfield, IL 62701 on February 14, 2003. I further state that I have served 3 copies of the foregoing Brief and Argument of *Amicus Curiae* United Policyholders in support of Michael Avery, et al., Plaintiffs-Appellees-Respondents to each counsel on the attached service list by U.S. Mail, postage prepaid, on February 14, 2003.

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