

Nos. A04-2088 and A04-2054

STATE OF MINNESOTA

SUPREME COURT

Christopher P. Schermer, Jon V. Smith, Marjorie B. Smith, Reverend Albert
Gallmon, on behalf of themselves and all other similarly situated,

Petitioners,

vs.

State Farm Fire and Casualty Company, State Farm General Insurance Company,

Respondents.

BRIEF OF *AMICUS CURIAE*
STATE OF MINNESOTA

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TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES.....	ii
STATEMENT OF AMICUS CURIAE.....	1
LEGAL ISSUE.....	1
INTRODUCTION.....	2
ARGUMENT	3
I. THE FILED RATE DOCTRINE IS INAPPLICABLE.....	4
A. The Filed Rate Doctrine Is Inapplicable To Minnesota’s File-And-Use Insurance Ratemaking Scheme Because Insurers Set Their Own Rates.....	5
B. The Filed Rate Doctrine Is Inapplicable Because This Is Not A Rate Case And To Adopt The Doctrine Here Would Violate Public Policy.....	8
II. INSURERS ARE PROHIBITED FROM CHARGING HIGHER HOMEOWNER’S INSURANCE PREMIUMS BASED UPON THE AGE OF THE PROPERTY’S STRUCTURAL ELEMENT, SUCH AS ITS WIRING, UNLESS THE AGE OF THE STRUCTURAL ELEMENT ACTUALLY INCREASES THE INSURER’S RISK OF LOSS.	9
CONCLUSION	14

TABLE OF AUTHORITIES

	Page
FEDERAL CASES	
<i>Arkansas Louisiana Gas Co. v. Hall</i> , 453 U.S. 571 (1981)	4
<i>H.J., Inc. v. Nw. Bell Tel. Co.</i> , 954 F.2d 485 (8th Cir. 1992).....	7
<i>Hanson v. Acceleration Life Ins. Co.</i> , 1999 WL 33283345 (D. N.D. Mar. 16, 1999).....	7
<i>Keogh v. Chicago & Nw. Ry. Co.</i> , 260 U.S. 156 (1922)	4, 7
<i>Square D. Co. v. Niagra Frontier Tariff Bureau, Inc.</i> , 476 U.S. 409 (1988)	4
<i>Wegoland, Ltd. v. NYNEX Corp.</i> , 806 F. Supp. 1112 (S.D.N.Y. 1992).....	5
STATE CASES	
<i>Current Tech. Concepts, Inc. v. Irie Enters., Inc.</i> , 530 N.W.2d 539 (Minn. 1995).....	10
<i>Hatch v. Am. Family Mut. Ins. Co.</i> , 609 N.W.2d 1 (Minn. Ct. App. 2000)	2
<i>Heim v. Am. Alliance Inc. Co.</i> , 147 Minn. 283, 180 N.W. 225 (Minn. 1920)	10
<i>Hince v. O'Keefe</i> , 632 N.W.2d 577 (Minn. 2001)	12
<i>Mitchell v. Chicago Title Ins. Co.</i> , No. 02-17299, 2004 WL 2137815 (Minn. Dist. Ct. Aug 13, 2004).....	7
<i>State by Humphrey v. Alpine Air Prod., Inc.</i> , 490 N.W.2d 888 (Minn. Ct. App. 1992)	10

<i>Illinois Farmers Ins. Co. v. Glass Serv. Co., Inc.</i> , 683 N.W.2d 792 (Minn. 2004).....	12
<i>Kersten v. Minn. Mut. Life Ins. Co.</i> , 608 N.W.2d 869 (Minn. 2000).....	12
<i>In the Matter of Sentry Ins. Payback Program Filing</i> , 447 N.W.2d 454 (Minn. Ct. App. 1989)	6
<i>In the Matter of State Farm Mut. Auto. Ins. Co.</i> , 392 N.W.2d 558 (Minn. Ct. App. 1986)	12
<i>Schermer v. State Farm Fire & Cas. Co.</i> , 702 N.W.2d 898 (Minn. Ct. App. 2005)	4
<i>Shank v. Fidelity Mut. Life Ins. Co.</i> , 221 Minn. 124, 21 N.W.2d 235 (Minn. 1945)	10, 13
<i>Streich v. Am. Family Mut. Ins. Co.</i> , 358 N.W.2d 396 (Minn. 1984).....	12

STATE STATUTES

Minn. Stat. § 8.01 (2004)	2
Minn. Stat. § 8.31, subd. 1 (2004).....	2
Minn. Stat. § 14.69 (2004)	6
Minn. Stat. § 70A.01, subd. 2(b), (d) (2004).....	7
Minn. Stat. § 70A.04 (2004).....	5
Minn. Stat. § 70A.04, subd. 1 (2004)	6
Minn. Stat. § 70A.04, subd. 2(a) (2004).....	1, 6
Minn. Stat. § 70A.06 (2004).....	1, 5, 6
Minn. Stat. § 70A.07 (2004).....	7
Minn. Stat. § 70A.10 (2004).....	5
Minn. Stat. § 70A.11 (2004).....	1, 6

Minn. Stat. § 72A.20, subd. 13 (2004)..... passim

Minn. Stat. § 645.16 (2004) 13

Minn. Stat. § 645.17(1) (2004)..... 12

STATE RULES

Minn. R. Civ. App. 129.03 2

OTHER AUTHORITIES

Black's Law Dictionary, p. 1320 (8th ed. 2004) 10

STATEMENT OF AMICUS CURIAE

The Minnesota Supreme Court has never adopted the federal “filed rate doctrine,” and it should not do so in this case involving the insurance industry. Under Minnesota law, homeowner’s insurance rates are set by insurers and subject only to minimal supervision by the Commissioner of the Minnesota Department of Commerce (“Commissioner”). The lower courts improperly adopted and applied the federal filed rate doctrine, rendering useless State law that prohibits a discriminatory insurance underwriting practice known as redlining.¹ Minn. Stat. § 72A.20, subd. 13 (2004).

LEGAL ISSUE

Under Minn. Stat. § 70A.06, an insurer must file homeowner’s insurance rates with the Commissioner no later than the effective date of the rate. These rates are statutorily presumed not to be excessive if a reasonable degree of competition exists in the market. Minn. Stat. § 70A.04, subd. 2(a) (2004). In other words, as long as a minimum degree of competition exists, State law presumes that the marketplace will efficiently establish the appropriate rates. As such, the insurer “files and uses” rates without any further action, review, or approval by the Commissioner. Instead of a legally-required rate review and approval process, the Commissioner *may* request supporting actuarial data from the insurer and *may* initiate a contested case proceeding to disapprove rates as excessive, inadequate or unfairly discriminatory. *See* Minn. Stat. §§ 70A.06 and 70A.11 (2004). The insurer, however, continues to use such rates unless and until the Commissioner finds, after a hearing, that the rates violate Minnesota law.

Petitioners brought this action claiming that a State Farm surcharge constituted illegal redlining under Minn. Stat. § 72A.20, subd. 13. The lower courts dismissed Petitioners’ claims by adopting the filed rate doctrine, a judge-made federal doctrine that prohibits claimants from challenging the reasonableness of rates approved by a regulator. Under these circumstances, should the filed rate doctrine be extended into state insurance law and foreclose policyholders from challenging an age-based utilities surcharge that constitutes redlining in violation of Minn. Stat. § 72A.20, subd. 13?

¹ Redlining refers to insurers using underwriting factors to achieve the goals of the prohibited “red-lined” map (*e.g.*, artificially increasing the cost of insurance in older communities deemed “undesirable” because of the predominance of the low-income, elderly, and racial minority persons). *See, e.g.*, Petitioners’ Appendix (“PA”) at 152-53.

INTRODUCTION

The State of Minnesota, by its Attorney General, respectfully submits this brief in support of the Petitioners and in the public interest.² The Attorney General may appear in court whenever the interests of the State require it. Minn. Stat. § 8.01 (2004). The Attorney General is charged with enforcement of Minnesota's consumer protection laws. Minn. Stat. § 8.31, subd. 1 (2004). The Attorney General has authority to enforce the principal statute at issue, Minn. Stat. § 72A.20, subd. 13. *See* Minn. Stat. § 8.31, subd. 1 (2004); *Hatch v. Am. Family Mut. Ins. Co.*, 609 N.W.2d 1, 4 (Minn. Ct. App. 2000), *review denied* June 13, 2000 (Minn. Stat. § 8.31 grants the Attorney General authority to enforce violations under chapter 72A).

This *amicus* brief addresses why this Court should not adopt the lower courts' reasoning, which would adversely affect the ability of low-income, elderly, and minority citizens of Minnesota to obtain affordable homeowners' insurance, a necessity to secure a mortgage and protect a home. Indeed, those most affected by the inaccessibility of homeowner's insurance generally have older homes in older neighborhoods, which are typically composed of higher home ownership rates by racial minorities.

The Legislature enacted Minn. Stat. § 72A.20, subd. 13 to prohibit discrimination against minority homeowners in regard to homeowner's insurance. The lower courts' decision sets poor public policy because it permits insurers to charge consumers in older

² Pursuant to Minn. R. Civ. App. 129.03, the Minnesota Attorney General's Office states that it solely prepared and paid for this brief.

communities higher rates for homeowner's insurance, notwithstanding an explicit statutory prohibition. *See* Minn. Stat. § 72A.20, subd. 13 (2004).

The facts supporting Petitioners' lawsuit demonstrate the reality behind these concerns. Respondents instituted large homeowner's insurance premium swings based on the age of electrical utilities, even though the actual losses due to faulty electrical wiring were small, at best. Petitioners assert that these premium swings had much greater negative consequences for Minnesota policyholders living in communities comprised of high percentages of minorities.³ Indeed, Petitioners state that Minnesota's minority policyholders were 28 percent more likely than non-minority policyholders to pay a surcharge.⁴ This is precisely the mischief that the Legislature sought to remedy when it enacted Minn. Stat. § 72A.20, subd. 13.

ARGUMENT

Minnesota Statute § 72A.20, subdivision 13 prohibits insurers from engaging in a specific form of discrimination known as "redlining." An insurer commits redlining when it refuses to renew, declines to offer, or charges different rates for, homeowner's insurance based solely on "the age of the primary structure sought to be insured." Minn. Stat. § 72A.20, subd. 13 (2004). The statute does not "prohibit the use of rating standards based upon the age of the insured structure's plumbing, electrical, heating or cooling

³ Petitioners' Br., p. 8; PA at 118-27.

⁴ Petitioners' Br., p. 8; PA at 124.

system or other part of the structure, *the age of which affects the risk of loss.*” *Id.* (emphasis added).

This appeal hinges on the construction of the phrase “*the age of which affects the risk of loss.*” Specifically, does this phrase limit surcharges to the degree that the particular utility actually causes an increased risk (as Petitioners and the Attorney General believe), or should this phrase be declared superfluous (as implemented by Respondents)? The lower courts avoid this analysis, deciding the case by adopting the federal filed rate doctrine. *Schermer v. State Farm Fire & Cas. Co.*, 702 N.W.2d 898, 905-908 (Minn. Ct. App. 2005), *review granted* Dec. 13, 2005.⁵

I. THE FILED RATE DOCTRINE IS INAPPLICABLE.

The filed rate doctrine is a judge-made federal law initially created to preclude shippers from recovering antitrust damages from carriers based on allegedly excessive rates which had been filed with and approved by the Interstate Commerce Commissioner. *See, e.g., Keogh v. Chicago & Nw. Ry. Co.*, 260 U.S. 156 (1922). Since its inception, the filed rate doctrine “has been extended across the spectrum of regulated utilities.” *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 (1981).

Application of the filed rate doctrine is typically justified by two principles: “first, that legislative bodies design agencies for the specific purpose of setting uniform rates,

⁵ This brief only relates to the application of the filed rate doctrine to a private class action lawsuit in the homeowner’s insurance context. It is well-settled that the filed rate doctrine does not apply to actions by the government. *See, e.g., Keogh v. Chicago & Nw. Ry. Co.*, 260 U.S. 156 (1922); *Square D. Co. v. Niagra Frontier Tariff Bureau, Inc.*, 476 U.S. 409, 422 (1988) (government antitrust action not subject to filed rate doctrine).

and second, that courts are not institutionally well suited to engage in retroactive rate-setting.” *Wegoland, Ltd. v. NYNEX Corp.*, 806 F. Supp. 1112, 1115 (S.D.N.Y. 1992), *aff’d* 27 F.3d 17 (2d Cir. 1994) (applying filed rate doctrine to telephone rates).

These principles are inapplicable to this case. First, insurance companies -- not the Commissioner -- set their own rates under Minnesota law, which presumes the marketplace to be an efficient regulator of rates. The absence of active supervision by the Commissioner precludes the application of the filed rate doctrine. Second, this is not a rate case. Petitioners do not ask the courts to become enmeshed in actuarial analysis to determine whether the surcharge was reasonable. Rather, Petitioners merely seek an adjudication that Respondents violated the underlying statutory provision prohibiting discriminatory redlining.

The Legislature has not codified the filed rate doctrine into Minnesota statutes, and the filed rate doctrine should not be adopted by this Court as a bar to claims that an insurer engaged in redlining.

A. The Filed Rate Doctrine Is Inapplicable To Minnesota’s File-And-Use Insurance Ratemaking Scheme Because Insurers Set Their Own Rates.

The lower courts misconstrue the Commissioner’s role as it relates to homeowner’s insurance rates. The Legislature established a ratemaking scheme in the insurance arena whereby competition is presumed to be an effective regulator. *See* Minn. Stat. §§ 70A.04, 70A.06 and 70A.10 (2004). Under the State’s “file-and-use” procedures, insurers set their own rates, which may be used as soon as they are filed with the Commissioner. Minn. Stat. § 70A.06 (2004).

Under Minn. Stat. § 70A.04, subd. 2(a), rates are presumed not to be excessive if a reasonable degree of price competition exists in the marketplace.⁶ Insurers are not required to file “supporting data and explanatory data” with their rate-filing. Minn. Stat. § 70A.06 (2004). Since rates are statutorily deemed approved upon filing, the Commissioner is not required to “approve” any filed rate. For these reasons, as well as budgetary and staffing reasons, the Minnesota Department of Commerce has generally not subjected homeowners’ insurance rate filings to meaningful actuarial review.⁷

If the Commissioner wishes to disapprove a rate, a contested case hearing under chapter 14 must occur. Minn. Stat. § 70A.11 (2004). If the Commissioner disapproves any rate after a hearing, the insurer may seek judicial review with the Court of Appeals. *See, e.g.,* Minn. Stat. § 14.69 (2004); *In the Matter of Sentry Ins. Payback Program Filing*, 447 N.W.2d 454 (Minn. Ct. App. 1989) (insurance company appealing Commissioner’s order to disapprove insurance filing following chapter 14 hearing). The Commissioner may not order that any filed rate “be discontinued” unless, after a hearing, the Commissioner finds that the rate is excessive, inadequate or unfairly discriminatory. Minn. Stat. § 70A.11 (2004); *see also* Minn. Stat. § 70A.04, subd. 1 (2004).

This ratemaking scheme does not require notice to policyholders before an insurer files rates with the Commissioner. Similarly, any ratemaking materials filed with the Commissioner are not “open to public inspection” until *after* the “[C]ommissioner’s

⁶ This statute does not, of course, mean that those rates are not, in fact, excessive.

⁷ PA at 85.

review has been completed.” Minn. Stat. § 70A.07 (2004). Accordingly, any review by the Commissioner lacks policyholder input. As such, unlike the insurer which is entitled to judicial review after a chapter 14 hearing, policyholders are excluded from the process.

In short, insurance rate-filings are not even subject to modest regulatory scrutiny under chapter 70A in most cases. Indeed, two overriding purposes of chapter 70A are to encourage “independent action by and reasonable price competition among insurers” and “to authorize cooperative action among insurers in the ratemaking process”. Minn. Stat. § 70A.01, subd. 2(b), (d) (2004). Because of the Commissioner’s limited and modest role, the filed rate doctrine is inapplicable to insurance rates in Minnesota. *See Hanson v. Acceleration Life Ins. Co.*, 1999 WL 33283345, *4 (D. N.D. Mar. 16, 1999) (declining to apply the filed rate doctrine in the context of long term care insurance); *see also Mitchell v. Chicago Title Ins. Co.*, No. 02-17299, 2004 WL 2137815 (Minn. Dist. Ct. Aug 13, 2004) (“In Minnesota, the filed rate doctrine has only been applied to common carriers and their shipping rates, often within the context of the federal Interstate Commerce Commission”).⁸

Moreover, extending the filed rate doctrine to this case would leave policyholders without a forum to redress their injuries. The ability to assert claims in another forum has been pivotal to the development of the filed rate doctrine. *See, e.g., Keogh*, 260 U.S. at 162 (claimants could recover damages by filing claim with Interstate Commerce Commission); *H.J., Inc. v. Nw. Bell Tel. Co.*, 954 F.2d 485, 492-93 (8th Cir. 1992)

⁸ Located in “Appellants’ Appendix” at 569-571.

(“Moreover, here, another forum exists for telephone customers to recover the alleged overcharges.”). Applying the filed rate doctrine in this case would eliminate any recourse for policyholders to challenge discriminatory underwriting factors.

B. The Filed Rate Doctrine Is Inapplicable Because This Is Not A Rate Case And To Adopt The Doctrine Here Would Violate Public Policy.

The filed rate doctrine also does not apply to Petitioners’ claims because this is not a rate case under chapter 70A. Petitioners’ allegations relate to whether an insurer may use an impermissible underwriting factor under chapter 72A. The existence of the illegal surcharge -- not its reasonableness -- is at issue in this case. In other words, Petitioners are not challenging the reasonableness of the rate. Instead, they assert that the rate is illegal because it violates a specific statutory provision, and they seek a return of the illegal surcharge. In essence, Petitioners ask for a declaration that the law was violated. The return of an illegal surcharge does not obligate the Court to set a rate or evaluate whether the rate is reasonable.

Public policy considerations also weigh heavily in favor of rejecting the filed rate doctrine in this context. If the Court, for the first time in Minnesota history, applies the filed rate doctrine to insurance, the far-reaching consequences could be perverse, to say the least. Taken to its logical extreme, the filed rate doctrine could severely undermine private enforcement of Minnesota’s consumer protection statutes. For instance, assume there were “smoking gun” documents proving that competing insurers had unlawfully conspired to fix policy rates. A private cause of action could be blocked because the defendants would likely argue that, because the rates were filed with the Commissioner,

the filed rate doctrine should protect them from private antitrust liability. Assume an insurance company whistleblower came forward and reported that the actuarial figures used to support certain rates were rigged or “cooked,” and that the actuarially-justified rates were actually 20 percent lower than the filed rate. A private cause of action could be blocked because the defendants would likely argue that, because the rates were filed with the Commissioner, the filed rate doctrine would shield them from private liability. Assume an insurance company insider produced internal memoranda from high ranking executives to actuarial staff directing that actuarial criteria be manipulated specifically to discriminate against minorities. A private cause of action could be blocked because the defendants would likely attempt to hide behind the filed rate doctrine. These results makes no sense, particularly against the backdrop of Minnesota’s laws that are designed, in part, to remedy abuses and discrimination in the market place.

Potentially eliminating such private causes of action would be a drastic measure which should require a more direct pronouncement from the Legislature, versus this Court relying on a judge-made doctrine from another jurisdiction to effect such a sweeping change. In short, the filed rate doctrine should not be adopted in this case.

II. INSURERS ARE PROHIBITED FROM CHARGING HIGHER HOMEOWNER’S INSURANCE PREMIUMS BASED UPON THE AGE OF THE PROPERTY’S STRUCTURAL ELEMENT, SUCH AS ITS WIRING, UNLESS THE AGE OF THE STRUCTURAL ELEMENT ACTUALLY INCREASES THE INSURER’S RISK OF LOSS.

The prohibition against redlining advances public policy by protecting consumers from unfair and discriminatory insurance practices. *See* Minn. Stat. § 72A.20, subd. 13 (2004). Passage of modern consumer protection laws resulted from the failure of the

common law to protect consumers in a position of unequal bargaining power. “Consumer protection laws are remedial in nature and are to be liberally construed in favor of protecting consumers.” *State by Humphrey v. Alpine Air Prod., Inc.*, 490 N.W.2d 888, 892 (Minn. Ct. App. 1992). Courts interpret remedial legislation broadly to better effectuate its purpose and apply exceptions within remedial legislation narrowly. *Current Tech. Concepts, Inc. v. Irie Enters., Inc.*, 530 N.W.2d 539, 543 (Minn. 1995).

Insurance laws founded on public policy are remedial. *See, e.g., Heim v. Am. Alliance Inc. Co.*, 147 Minn. 283, 288, 180 N.W. 225, 226 (Minn. 1920); *Shank v. Fidelity Mut. Life Ins. Co.*, 221 Minn. 124, 130, 21 N.W.2d 235, 238 (Minn. 1945) (“When the legislature has spoken on the form which a policy of insurance must take, such enactments declare the public policy of the state.”). A remedial insurance law must be “construed liberally for the suppression of the mischief it was designed to do away with.” *Heim*, 147 Minn. at 288, 180 N.W. at 226.

Statutory construction and legislative history establish that Minn. Stat. § 72A.20, subd. 13 is a remedial statute.⁹ The legislative author, Senator Robert Tennesen, indicated that the intent and purpose of the anti-redlining legislation was to require insurers “to demonstrate the relationship between the risks of loss arising from the

⁹ “Remedial law” is defined by *Black’s Law Dictionary* as: “1. A law providing a means to enforce rights or redress injuries. 2. A law passed to correct or modify an existing law; esp., a law that gives a party a new or different remedy when the existing remedy, if any, is inadequate.” *Black’s Law Dictionary*, p. 1320 (8th ed. 2004).

structural element before it could use age-based data for the structural element.”¹⁰ That relationship has not been demonstrated here.

In 1979 the Midwest Advisory Committee to the United States Commission on Civil Rights issued a report directed specifically to state legislators in the Midwest and state insurance commissioners. The report emphasized that insurance companies were limiting the availability of insurance to the degree that it was, effectively, unavailable. The report outlined several proposals to address redlining, including the legislation adopted in Minn. Stat. § 72A.20, subd. 13.¹¹ Subdivision 13 was included among other statutory provisions regulating unfair and deceptive acts and practices in the business of insurance, further establishing that the statute was intended to prevent unlawful discrimination in the underwriting of such policies. Notably, subdivision 13 was *not* included in chapter 70A, which contains the ratemaking provisions of the insurance laws.

Minnesota Statute § 72A.20, subd. 13 provides that: “Clause (b) shall not prohibit the use of rating standards based upon the age of the insured structure’s plumbing, electrical, heating or cooling system or other part of the structure, *the age of which affects the risk of loss.*” The plain meaning of the phrase is that a homeowner’s insurer may only impose a surcharge based upon the age of a particular utility system to the degree it actually causes an increased risk.

¹⁰ Affidavit of Robert J. Tennessen, ¶ 18 (located in “Appellants’ Appendix” at 335).

¹¹ PA at 205-10.

The trial court, however, suggested that an undefined *correlation* between losses unrelated to the age of electrical utilities permitted the underwriting factor. Under this interpretation, causation is not required to establish a correlation. This is flawed because it subverts the legislative purpose and intent to prohibit redlining. Indeed, applying the law in this manner could lead to absurd results (as it did in this case) harmful to policyholders by thwarting the consumer protection purposes of Minn. Stat. § 72A.20, subd. 13. Courts must construe statutes to avoid absurd or unjust consequences. Minn. Stat. § 645.17(1) (2004); *Hince v. O'Keefe*, 632 N.W.2d 577, 582 (Minn. 2001).

The interpretation of this statute is a question of law. *See, e.g., Kersten v. Minn. Mut. Life Ins. Co.*, 608 N.W.2d 869, 872-74 (Minn. 2000) (“[T]his case deals primarily with the interpretation of a statute, a duty we cannot shift to the [Commerce] commissioner.”); *In the Matter of State Farm Mut. Auto. Ins. Co.*, 392 N.W.2d 558, 565 (Minn. Ct. App. 1986) (“The [Commerce] commissioner’s decision . . . is a question of law, and this court therefore need give no deference to the [Commerce] commissioner’s decision on the issue.”).

An insurance policy provision that conflicts with State law is invalid, “even if the commissioner approved it.” *Id.*; *see also Illinois Farmers Ins. Co. v. Glass Serv. Co., Inc.*, 683 N.W.2d 792, 802 (Minn. 2004) (“If a term in an insurance contract conflicts with Minnesota statutes, the contract term becomes unenforceable.”); *Streich v. Am. Family Mut. Ins. Co.*, 358 N.W.2d 396, 399 (Minn. 1984) (“The extent of an insurer’s liability is governed by the contract between the parties only as long as . . . policy

provisions do not contravene applicable statutes.”); *Shank*, 221 Minn. at 130, 21 N.W.2d at 238 (Minn. 1945) (“The commissioner lacked the power to change or waive the plain provisions of the statute.”). Thus, regardless of the Commissioner’s statutory construction, the surcharge is unenforceable since it violates State law by subjecting consumers to a discriminatory, illegal surcharge.

The Legislature intended to prohibit insurers from using underwriting factors which artificially increased the cost of insurance of older, impoverished, and minority communities. Any construction that allows an insurer to use the age of a utility to increase rates in an amount in excess of the amount by which the age of the utility actually increases the risk of loss negates the mischief sought to be remedied and makes the phrase “*the age of which affects the risk of loss*” completely superfluous. *See also* Minn. Stat. § 645.16 (2004) (“Every law shall be construed, if possible, to give effect to all its provisions.”).

The lower courts’ failure to enforce Minn. Stat. § 72A.20, subd. 13 effectively eviscerates the “broad” and “aggressive” consumer protection law, creating an opportunity for widespread abuse by insurers. A plain reading of Minn. Stat. § 72A.20, subd. 13 allows an insurer to charge higher homeowner’s insurance premiums based upon the age of a property’s structural element, such as its wiring, only to the extent that the age of the structural element actually increases the risk of loss.

In sum, a rating plan which allows premium swings of up to 30 percent or more of the overall premium based upon the age of an electrical system is unlawful unless the

insurer can demonstrate that the risk of loss is actually 30 percent or greater *as a result of the age of the electrical system*.¹² Any other result renders the statute meaningless and contravenes the rights of policyholders.¹³

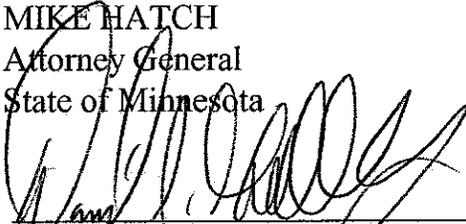
CONCLUSION

Amicus Curiae State of Minnesota respectfully requests that this Court issue an opinion reversing the lower courts. Specifically, the Court should not adopt the filed rate doctrine in the context of homeowner's insurance. Further, the Court should interpret the redlining statute to permit homeowner's insurers to use the age of utilities as an underwriting factor only to the extent that the age of utilities actually increase the risk of loss.

Dated: January 19, 2006

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¹² PA at 84.

¹³ PA at 86.

CERTIFICATE OF COMPLIANCE

WITH MINN. R. APP. P 132.01, Subd. 3

The undersigned certifies that the Brief submitted herein contains 4,481 words and complies with the type/volume limitations of the Minnesota Rules of Appellate Procedure 132. This Brief was prepared using a proportional spaced font size of 13 pt. The word count is stated in reliance on Microsoft Word 2002, the word processing system used to prepare this Brief.


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