

NO. A10-2090

State of Minnesota
In Court of Appeals

Tammy Pepper,

Appellant,

v.

State Farm Mut. Auto. Ins. Co. a/k/a State Farm Fire and
Casualty Company, a/k/a State Farm Insurance Companies,

Respondent.

**BRIEF AND APPENDIX OF RESPONDENT
STATE FARM MUT. AUTO. INS. CO.**

Karen R. Cote (#219824)
Brett W. Olander (#164793)
BRETT W. OLANDER & ASSOCIATES
Wells Fargo Place
30 East Seventh Street
Suite 3100
St. Paul, MN 55101
(651) 229-5072
(651) 229-5070

*Attorneys for Respondent
State Farm Mut. Auto. Ins. Co.*

Alan B. Fish (#238120)
ALAN B. FISH, P.A.
102 Second Avenue N.W.
Roseau, MN 56751
(218) 463-2088

*Attorneys for Appellant
Tammy Pepper*

The appendix to this brief is not available for online viewing as specified in the *Minnesota Rules of Public Access to the Records of the Judicial Branch*, Rule 8, Subd. 2(e)(2).

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LEGAL ISSUES

- I. Can an insured collect underinsured motorist coverage under a policy that insured the alleged underinsured motor vehicle?

The trial court held in the negative.

- II. Does Appellant's status as a pedestrian change the outcome?

The trial court held in the negative.

STATEMENT OF CASE

Appellant commenced this action against Respondent alleging that she was an insured under the Respondent's policy issued to Frank Matlachowski and that she was entitled to underinsured motorist coverage under the policy. Respondent asserted Appellant was not an insured under the policy and even if she was an insured, she was not entitled to underinsured motorist coverage due to an exclusion that prohibits converting underinsured coverage into excess liability coverage. Respondent brought a motion for summary judgment to dismiss Appellant's Complaint in its entirety based on the exclusion and specifically preserved the issue of whether Appellant qualified as an insured under the policy. (R.A.1-13)

Respondent's motion for summary judgment was heard before the Honorable Donna Dixon on September 21, 2010. The court granted Respondent's motion for summary judgment and dismissed Plaintiff's Complaint with prejudice.

In granting Respondent's motion, the court looked at the policy language and noted that underinsured motorist coverage provided that Respondent "will pay damages for bodily injury the insured is legally entitled to collect from the owner or driver of an

underinsured motor vehicle.” (A.A. 5) (citing policy section III, p. 19) (R.A. 40). The court then cited the definition of an “underinsured motor vehicle” which specifically stated that an underinsured motor vehicle does not include:

“another vehicle or motorcycle: (1) insured under the liability coverage of this policy{.}” (A.A. 5) (citing policy section III, p. 19, R.A.40).

The court held that since the vehicle was insured under the liability coverage of the same policy from which Appellant sought underinsured motorist benefits, it was excluded from the policy definition of underinsured motor vehicle. Therefore, Appellant’s claim was barred. (A.A. 6)

The court rejected Appellant’s argument that she was entitled to underinsured motorist (hereinafter “UIM”) benefits under the policy that did not pay out the liability limits because Matlachoski owned and insured two vehicles under separate policies. *Id.* The court explained that the plain language of the policy excluded all vehicles that are insured under the liability coverage and not just vehicles for which liability payments were made. The court cited well-established case law that supported its decision. (A.A.5-7)

The court also rejected Appellant’s argument that the exclusion did not apply in this case because she alleged negligence of the at-fault vehicle’s owner for failure to maintain the vehicle and/or warn about an alleged defect. The court rejected this argument because the exception to the exclusion only applied when there was another “at-fault vehicle”. (A.A. 6). In this case, there was only one alleged at-fault underinsured motor vehicle. Thus, the exception to the exclusion did not apply.

Finally, the court rejected Appellant's argument that since she was a pedestrian, she could still collect underinsured motorist benefits. The court noted that Appellant's status as a pedestrian removed the limitations regarding the priority of coverage. However, the valid exclusion still applied. (A.A. 7)

Since the trial court's analysis was correct, this court should affirm the trial court's decision.

STATEMENT OF THE FACTS

On September 3, 2009, while a pedestrian, Appellant was struck by a vehicle driven by Frank Matlachowski and owned by Tracie Drew. The vehicle was insured by Tracie Drew as the owner through State Farm Mutual Automobile Insurance Company with \$100,000 in liability limits. (R.A.101) Appellant made a claim to State Farm under this policy and State Farm paid the policy limits. Appellant then made a claim against Frank Matlachowski for his negligent operation of the vehicle and submitted that claim to State Farm. Frank Matlachowski had two insurance policies on vehicles that were not involved in the accident through State Farm. Both policies provided \$100,000 in liability coverage and \$100,000 for underinsured motorist coverage. Frank Matlachowski was the named insured under both policies and both policies covered the vehicle operated by Frank Matlachowski as a non-owned vehicle operated by an insured with permission. (R.A. 16, 59). State Farm paid the liability limits of \$100,000 under one of the policies issued to Frank Matlachowski. (R.A.102)

Appellant submitted a claim for underinsured coverage under the same policies that covered Frank Matlachowski for liability coverage. Both of the policies issued by

State Farm to Frank Matlachowski contain identical provisions regarding underinsured motorist coverage. The policy language reads as follows:

We will pay damages for **bodily injury** an **insured** is legally entitled to collect from the owner or driver of an **underinsured motor vehicle**. The **bodily injury** must be sustained by an **insured** and caused by accident arising out of the operation, maintenance or use of an **underinsured motor vehicle**.

(R.A. 40)(emphasis in original)

An underinsured motor vehicle means:

A **motor vehicle** or **motorcycle**, the ownership, maintenance or use of which is insured or bonded for bodily injury liability in amounts that:

1. meet the requirements of the laws of the state where **your car** is mainly garaged; and
2. are less than the amount needed to compensate the **insured** for damages.

An **underinsured motor vehicle** does not include a **motor vehicle** or **motorcycle**

1. insured under the liability coverage of this policy;
2. furnished for the regular use of **you, your spouse** or any **relative**;
3. while located for use as a premises; or
4. that is an **uninsured motor vehicle**.

(R.A. 40)(emphasis in original)

State Farm denied Appellant's claim for UIM benefits because an underinsured motor vehicle does not include a motor vehicle insured under the liability coverage of this policy. Appellant commenced an action against State Farm. Appellant's action against State Farm was captioned naming State Farm Mutual Automobile Insurance Company

a/k/a State Farm Fire and Casualty Company, a/k/a State Farm Insurance Companies. Since State Farm Mutual Automobile Insurance Company is the only insurer that issued the policies to Frank Matlachowski, State Farm affirmatively pled that State Farm Fire and Casualty Company and State Farm Insurance Companies were improperly named. State Farm repeatedly requested that Appellant dismiss State Farm Fire and Casualty Company and State Farm Insurance Companies and even served Request for Admissions in that effort. Because Appellant refused to amend the Complaint, State Farm's motion for summary judgment also requested that the caption be amended to reflect only State Farm Mutual Automobile Insurance Company. (R.A.2, 12-13) Since the court dismissed the entire action, this issue was not resolved by the court.

STANDARD OF REVIEW

On appeal from summary judgment, the appellate court must determine whether there are any genuine issues of material fact and whether the district court erred in its application of the law. *Wallin v. Letourneau*, 534 N.W.2d 712, 715 (Minn. 1995). In this case there are no disputed issues of material fact pertaining to the policy exclusion. The interpretation of an insurance contract involves a question of law for the court to decide. *See Auto-Owners Ins. Co. v. Forstrom*, 684 N.W.2d 494, 497 (Minn. 2004); *Dohney v. Allstate Ins. Co.*, 632 N.W.2d 598, 600 (Minn. 2001). The appellate court reviews issues of law *de novo*. Similarly, statutory interpretation presents a question of law that this court will review *de novo* on appeal. *Hibbing Educ. Ass'n v. Public Employment Relation Board*, 369 N.W.2d 527, 529 (Minn. 1985).

ARGUMENTS

I. REGARDLESS OF THE NUMBER OF ALLEGED NEGLIGENT PARTIES AND NEGLIGENCE THEORIES, THE OUTCOME IS THE SAME: APPELLANT CANNOT CONVERT UNDERINSURED MOTORIST COVERAGE INTO EXCESS LIABILITY COVERAGE.

The purpose of liability coverage is to pay damages the insured is legally obligated to pay another person, a third party, for bodily injury arising out of the insured's ownership, maintenance or use of a vehicle. *See* Minn. Stat. §65B.49, subd.3(2) (2000); *Lynch ex rel. Lynch v. American Family Mutual Automobile Ins. Co.*, 626 N.W2d 182 (Minn. 2001). The purpose of underinsured motorist coverage is to compensate an insured under her own policy for a third party's negligence when the third party does not have adequate insurance. *Id.* Because the UIM coverage mandated by the No-Fault Act is not intended to supplement an insured for inadequate liability coverage under the insured's policy, an insurer may issue a policy with an exclusion that prohibits an insured from converting UIM coverage into excess liability coverage. *Id.*

Minnesota courts have long upheld exclusions that prohibit providing both underinsured and liability coverage for the same accident. *See e.g. Kelly v. State Farm Mut. Auto. Ins. Co.*, 666 N.W.2d 328, 332 (Minn. 2003); *Thommen v. Illinois Farmers Insurance Co.* 427 N.W.2d 244, 246 (Minn. 1988), *reh'g denied* (Minn. Sept. 14, 1988); *Petrich by Lee v. Hartford Fire Ins. Co.*, 427 N.W.2d 244 (Minn. 1988); *Myers v. State Farm Mut. Auto. Ins. Co.*, 336 N.W.2d 288 (Minn. 1983); *Stewart v. Illinois Farmers Ins. Co.*, 727 N.W.2d 679 (Minn. Ct. App. 2007); *Staley v. Metropolitan Property & Casualty Co.*, 576 N.W.2d 175 (Minn. Ct. App. 1998), *rev. denied* (Minn. June 17, 1998).

“Coverage conversion” refers to an insured attempting to use first-party benefits to substitute for inadequate third-party liability coverage. *See Kelly*, 666 N.W.2d at 331. The exclusion operates to prevent a vehicle from becoming an underinsured vehicle by definition under a policy that covers the same vehicle for liability coverage. The exclusion applies irrespective of the number of insurance policies available. *See e.g. Kelly v. State Farm Mut. Auto. Ins. Co.*, 666 N.W.2d 328, 332 (Minn. 2003); *Staley v. Metropolitan Property & Casualty Co.*, 576 N.W.2d 175 (Minn. Ct. App. 1998), *rev. denied* (Minn. June 17, 1998); *Barton v. American Intern’l Adjustment Co., Inc.*, unpublished decision, No. CX-93-1737 (Minn. Ct. App. Jan. 18, 1994). (R.A.103)

In *Kelly*, Kelly’s husband was driving a Dodge Intrepid with the Plaintiff Kelly riding as a passenger. At the time of the accident, Kelly’s husband was the sole owner of the Intrepid and was insured by State Farm. In addition, both Kelly and her husband were listed as owners of a Pontiac Grand Am which was also insured by State Farm. As a result of the accident, Kelly brought a claim against her husband which State Farm settled by paying the \$100,000.00 liability limit on the policy insuring the Intrepid. Because her damages exceeded the \$100,000.00 liability limits, Kelly filed a claim with State Farm seeking underinsured motorist benefits under the separate policy covering the Grand Am. State Farm denied her UIM claim contending that under the Grand Am policy, the Intrepid was not an “underinsured motor vehicle.” Furthermore, allowing Kelly to recover UIM benefits under the Grand Am policy which also provided liability coverage to her husband, the tortfeasor, would result in coverage conversion because the

UIM policy would be used to supplement her husband's inadequate liability insurance. *See Kelly*, 666 N.W.2d at 329.

Following State Farm's denial of the UIM claim, Kelly commenced a lawsuit. Both parties filed cross-motions for summary judgment. Initially, the district court denied State Farm's motion and granted Kelly's motion reasoning that Kelly had no ownership interest in the Intrepid (the at-fault vehicle) and it did not appear that Kelly was working with her husband to convert her UIM coverage into additional liability coverage. *Id.* at 329. Approximately one month later, the court of appeals decided *Johnson v. St. Paul Guardian Insurance Co*, 627 N.W.2d 731 (Minn. Ct. App. 2001), *rev. denied* (Minn. Sept. 11, 2001). In *Johnson*, the Court of Appeals held that "an injured individual, whose injuries exceeded the tortfeasor's liability coverage, could not look to a separate policy providing UIM coverage for the tortfeasor because this would result in impermissibly converting that UIM coverage into more expensive liability coverage to make up for the tortfeasor's inadequate liability coverage." *Id.* at 733 – 34.

As a result of the *Johnson* decision, State Farm moved the district court to reconsider the grant of partial summary judgment in favor of Kelly. The district court reversed its earlier order and entered judgment in favor of State Farm, finding that under *Johnson*, Kelly was not entitled to UIM benefits. The court of appeals affirmed.

On appeal to the Minnesota Supreme Court, Kelly argued that the court should conclude that she is entitled to coverage under the Grand Am policy because the policy exclusion contravened the underlying purpose of the No-Fault Act. Kelly argued that her UIM claim should not be denied simply because her husband was listed as an insured on

the Grand Am policy. Kelly argued that her claim was under a different policy than the one that paid liability coverage.

State Farm contended that exclusions such as the one contained in the Grand Am policy were appropriate and consistent with Minnesota law. State Farm argued that to allow Kelly to recover UIM benefits under the Grand Am policy would permit the conversion of less expensive underinsured motorist coverage into more expensive liability coverage.

The court considered both arguments and acknowledged the distinction made by Kelly but rejected Kelly's argument. The court stated:

[w]hen a liability claim is made on one policy and a UIM claim is made on a second policy, both of which list the tortfeasor as an insured, allowing the UIM claim would result in the payment of additional benefits for injuries caused by the negligence of the insured tortfeasor, which is, as we stated in *Lynch*, the 'essence of liability coverage.'

Id. at 331, (emphasis added).

Thus, although the liability payment was made under the State Farm policy covering the Intrepid, the Plaintiff could not seek UIM coverage under the State Farm policy covering the Grand Am. "To allow Kelly's husband to benefit from providing inadequate liability coverage on the Intrepid by supplementing that coverage with cheaper UIM coverage on a separate policy that also names him as an insured resulted in coverage conversion" which the court stated insurance companies could exclude. *Id.* at 332. (emphasis added)

As explained by the court in *Lynch*, the fact that the vehicle driven by the tortfeasor was a non-owned vehicle insured by a different company than the one

providing UIM coverage does not change the fact that the tortfeasor's negligence was the exclusive cause of the damages and to claim coverage under a policy insuring another vehicle makes no difference because the policy already issued payment under its liability coverage for the same negligent act. The court explained that "[t]o now collect further under the same insurer's underinsured motorist coverage would be to convert the underinsured motorist coverage into third-party insurance, treating it essentially the same as third-party liability coverage." *Id.* at 188 citing *Myers v. State Farm Mut. Auto. Ins. Co.*, 336 N.W.2d 288 (Minn. 1983).

The holdings in *Kelly* and *Lynch* are consistent with the court's holdings in *Myers v. State Farm Mut. Auto. Ins. Co.*, 336 N.W.2d 288 (Minn. 1983); *Petrich v. Hartford Fire Ins. Co.*, 427 N.W.2d 244, 246 (Minn. 1988); *Barton v. American Intern'l Adjustment Co., Inc.*, unpublished decision, No. CX-93-1737 (Minn. Ct. App. Jan. 18, 1994) (R.A. 103); *Steele v. American Nat'l Property & Cas. Co.*, unpublished decision, No. A07-1411 (Minn. Ct. App. 2008) (R.A. 106)

In *Myers v. State Farm Mut. Auto. Ins. Co.*, *supra*, Lawrence Myers was a passenger in a car that struck a tree. He was fatally injured. The car was owned by Allison Stein and driven by another person. Allison Stein was insured with State Farm. The driver was insured with Iowa Kemper Ins. Co. Gay Myers, as trustee for the deceased collected \$25,000 liability limits from the car owner's policy (State Farm) and \$25,000 from the driver's policy (Iowa Kemper). *Id.* at 289. The trustee then sought UIM coverage from the occupied vehicle, State Farm. State Farm denied coverage based upon the exclusion within policy's definition of "underinsured motor vehicle". This

exclusion provided that an “underinsured motor vehicle” does not include any vehicle owned by or furnished or available for the regular use of you [the named insured] or any family member. Since the named insured owned the car that hit the tree, it did not qualify for UIM coverage. The court held that the exclusion applied. In so holding, the court stated that this exclusion within the policy definition of “underinsured motor vehicle” “properly prevents this conversion of first-party coverage into third-party coverage.” *Id.* at 291. As the court explained, the owner’s policy is “not designed to compensate Stein [the owner] or his additional insureds from Stein’s failure to purchase sufficient liability insurance.” *Id.*

In *Petrich by Lee v. Hartford Fire Ins. Co*, 427 N.W.2d 244 (Minn. 1988), Petrich brought a declaratory judgment action seeking a determination that Hartford owed uninsured motorist benefits. Hartford denied uninsured motorist coverage based on a policy exclusion that excluded coverage if the uninsured vehicle is owned by the insured or family member. The court cited the reasoning of *Myers* explaining that the purpose of the exclusion is to prevent the conversion of one type of insurance into another, here, uninsured coverage under one policy for liability coverage for an uninsured vehicle.

In the case at hand, Appellant sought underinsured motorist coverage under a separate policy that insured Frank Matlachowski and the at-fault vehicle as a non-owned vehicle. Frank Matlachowski was the named insured under both State Farm policies. The Drew vehicle was a non-owned vehicle operated by Frank Matlachowski at the time of the accident that qualified for liability coverage under both policies. Both policies specifically excluded from the definition of “underinsured motor vehicle” vehicles

insured under the liability coverage. Since the exclusion is a valid exclusion, the trial court's decision should be affirmed.

The only exception to this exclusion is when there is another underinsured at fault vehicle. See *Lahr v. Am. Family Mut. Ins. Co.*, 528 N.W.2d 257 (Minn. Ct. App. 1995); In *Lahr*, the court noted that Lahr conceded that case law prohibited Lahr from obtaining UIM benefits from a driver's insurer if the driver is the only vehicle involved in the accident or the only at-fault 'underinsured' vehicle. *Lahr v. Am. Family Mut. Ins. Co.*, 528 N.W.2d 257, 258 (Minn. Ct. App. 1975). The issue was whether Lahr could collect UIM coverage based upon the fault of another underinsured motor vehicle. The court held that in this situation, the insured could collect UIM benefits. See also *Mitsch v. American Nat. Property and Cas. Co.*, 736 N.W.2d 355 (Minn. Ct. App. 2007) (followed *Lahr* and held that a reducing clause that prevented recovery of UIM benefits based upon the fault of another involved vehicle was unenforceable.)

The case at hand involved a single-vehicle accident. Thus, the exception did not apply. To get around the fact that there was not another at-fault vehicle, Appellant argued that she could collect UIM coverage under a separate policy based upon the fault of another person (Tracie Drew). There is no authority for extending *Lahr* to situations where a party can claim another party as a tortfeasor without another at-fault vehicle.

The Minnesota No-Fault Act provides for underinsured motorist coverage and defines underinsured motorist coverage as "coverage for the protection of persons insured under that coverage who are legally entitled to recover damages for bodily injury from owners or operators of underinsured motor vehicles." See Minn. Stat. § 65B.43, subd. 17

and 19. (emphasis added) Subd. 17 defines an “underinsured motor vehicle” as “a motor vehicle or motorcycle to which a bodily injury liability policy applies at the time of the accident but its limits of bodily injury liability is less than the amount needed to compensate the insured for accidents.” *Id.* (emphasis added)

In underinsured motorist claims, the focus is on the involved motor vehicle; not whether the Plaintiff can create multiple tortfeasors. If Plaintiff’s theory was correct, every product liability claim involving a motor vehicle would include a liability payment for negligence of the driver and underinsured motorist coverage payments for the negligence of the manufacturer. This is not the case. The question is simply whether the vehicle (including the owner or the operator) had adequate liability coverage to compensate the insured for damages sustained. (R.A. 112-115)

In this case, there was only one at-fault vehicle. Appellant already recovered liability coverage from the owner and the driver’s policies. She was prohibited from collecting underinsured motorist coverage from the same policy or policies that provided liability coverage. Thus, this court should affirm the trial court.

II. APPELLANT’S STATUS AS PEDESTRIAN DOES NOT CHANGE THE OUTCOME.

Appellant’s status as a pedestrian struck by a motor vehicle means that the priority provisions do not limit the Appellant to the occupied vehicle policy. Rather, the pedestrian is permitted to turn to any policy under which the pedestrian qualifies as an insured. This principle, however, does not allow an injured pedestrian to convert

underinsured motorist coverage into excess liability coverage. The valid exclusion still applies.

The exclusion in the policy applies under both policies. Under both policies, the exclusion is the same. Under both policies, an underinsured motor vehicle does not include a motor vehicle that is insured under the liability coverage of the policy. The non-owned vehicle operated with permission by Frank Matlachowski qualifies as an insured motor vehicle under the liability coverage of both policies. The fact that only one policy paid out the liability limits does not mean that the Appellant avoids the exclusion. The intent of the exclusion is to prohibit conversion of underinsured motorist coverage into excess liability coverage.

III. STATE FARM FIRE AND CASUALTY COMPANY AND STATE FARM INSURANCE COMPANIES ARE IMPROPERLY NAMED AND SHOULD BE DISMISSED.

Appellant captioned the Complaint naming State Farm Mutual Automobile Insurance Company a/k/a State Farm Fire and Casualty Company a/k/a State Farm Insurance Company. For clarity, "State Farm" moved to dismiss State Farm Fire and Casualty Company and State Farm Insurance Company. First, service of process was never made upon either entity. (R.A. 110-111). Second, neither State Farm Fire and Casualty Company or State Farm Insurance Company issued the policies at issue. *See* Certificates of Coverage, *Ex. A*. The certificate of coverage clearly states that the insurance company that issued the policies is State Farm Mutual Automobile Insurance Company. (R.A. 16). Since neither company has been served and neither company is a

proper party, both should be dismissed and the caption should be amended with State Farm Mutual Automobile Insurance Company listed as the only Defendant.

CONCLUSION

The trial court properly applied the valid exclusion based upon well established case law. Appellant's attempt to create an exception is not supported by any cases and violates the purpose of the valid exclusion. Therefore, this court should affirm the trial court's grant of summary judgment.

Dated: 1-26-11

BRETT W. OLANDER & ASSOCIATES



Karen Cote

Attorney Registration #219824
Brett W. Olander,
Attorney Registration #164793
Wells Fargo Place
30 East 7th Street, Suite 3100
St. Paul, MN 55101
Attorneys for Respondent

CERTIFICATION OF BRIEF LENGTH

I hereby certify that this brief conforms to the requirements of Minn. R. Civ. App. P. 132.01, subds. 1 and 3, for a brief produced with a proportional font. The length of this brief does not exceed 45 pages and contains 3,869 words. This brief was prepared using Microsoft Word 2007.

Dated: 1-26-11

BRETT W. OLANDER & ASSOCIATES



Karen Cote

Attorney Registration #219824

Wells Fargo Place

30 East 7th Street, Suite 3100

St. Paul, MN 55101

Attorneys for Respondent