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9 ALLSTATE INSURANCE COMPANY  
10 and ALLSTATE INDEMNITY COMPANY

11 **BEFORE THE INSURANCE COMMISSIONER**  
12 **OF THE STATE OF CALIFORNIA**

13 In the Matter of the Rates, Rating Plans, or Rating ) FILE NO.: PA-2007-00011  
14 Systems of )  
15 ALLSTATE INSURANCE COMPANY and ) **NOTICE OF DEFENSE**  
16 ALLSTATE INDEMNITY COMPANY )  
17 Respondents. )

18 Pursuant to California Government Code (the "Government Code") § 11506, Respondents  
19 Allstate Insurance Company and Allstate Indemnity Company ("Respondents" or "Allstate") hereby file  
20 this Notice of Defense to the Notice of Noncompliance and Order to Show Cause (the "OSC"), issued  
21 by the California Department of Insurance ("CDI") on May 23, 2007<sup>1</sup>:

22 **PRELIMINARY STATEMENT**

23 In the OSC, the CDI claims that Allstate's current rates for homeowners' insurance ("Current  
24 Rates") are "excessive" and therefore in violation of Section 1861.05 of the California Insurance Code  
25 (the "Insurance Code"). By reason of this alleged "excessiveness," the CDI proposes not merely to  
26 order Allstate to reduce its Current Rates, but to order Allstate to extend refunds or credits to  
27 policyholders on account of premiums billed and collected in the past, notwithstanding the fact that  
28 those premiums were based upon approved rates.

<sup>1</sup> The OSC was served upon Allstate at its corporate headquarters in Northbrook, Illinois by overnight mail. The OSC was deposited with the overnight mail on May 23, 2007 and physically received by Allstate on May 24, 2007. Accordingly, the time within which Allstate is required to file its notice of defense has been extended by two court days, to and including June 11, 2007. See Cal. Gov. Code § 11506 and Cal. Civ. Proc. Code § 1013(c).

1 The OSC does not specify the dates upon which the Current Rates allegedly became excessive or  
2 after which the alleged right of policyholders to refunds began to accrue. While the OSC indicates that  
3 the Commissioner has determined the amount of the alleged excessiveness with great precision and  
4 accuracy (it claims that the “excessiveness” factor is 43.88%), the CDI apparently does not know, or  
5 feels that Allstate should be required to guess at, the date upon which this huge, alleged liability began  
6 to accrue.

7 Significantly, the CDI does not and cannot contest the facts that (1) the Current Rates were  
8 approved by the Commissioner more than three years ago, (2) the Commissioner has never ordered that  
9 such rates be reduced or otherwise modified, and (3) the Current Rates have been consistently applied  
10 by Allstate in strict compliance with the law.

11 The Commissioner freely admits that, in seeking to issue a Refund Order, he is proposing to  
12 exercise alleged “rights” that neither he nor any prior Commissioner of Insurance has ever before sought  
13 to exercise; he recognizes that his actions are unprecedented. The May 23, 2007 “News Release” issued  
14 by the Commissioner at the time of issuance of the OSC contains this acknowledgement:

15 Commissioner Poizner also announced his intent to seek refunds for  
16 Allstate customers if the Department of Insurance determines that their  
17 rates are excessive. **This would be the first time in California history**  
18 **that a retroactive refund is ordered following a rate hearing.** “I am  
drawing a line in the sand,” said Commissioner Poizner. (Emphasis  
added.)

19 The reason this action is unprecedented is that the Commissioner has absolutely no legal authority to  
20 issue a Refund Order. The measures the OSC proposes to invoke are not merely unprecedented, they  
21 are unlawful. The issuance of a Refund Order by the Commissioner is proscribed by both the applicable  
22 statutes and long-established, and utterly consistent, case law. The Commissioner is wrongfully seeking  
23 to confer upon himself and his department powers that the California State Legislature and the citizens  
24 of California (through Proposition 103) did not see fit to grant them.

25 Chapter 9 of the California Insurance Code and the regulations promulgated thereunder establish  
26 “a comprehensive administrative scheme” for the regulation of rates charged by insurance companies for  
27 certain types of insurance. *Farmers Ins. Exch. v. Superior Court*, 137 Cal. App. 4th 842, 855 (2006).  
28 Among other things, the regulatory scheme, which is embodied in dozens of pages of statutes and

1 regulations, (1) provides for the prior approval by the CDI of all rates charged by insurers in connection  
2 with certain enumerated lines of insurance, including but not limited to homeowners' insurance,  
3 (2) absolutely mandates that insurers charge only those rates that have previously been approved by the  
4 CDI, and (3) contains a mechanism by which either policyholders or the CDI (on its own initiative) may  
5 initiate action to correct insurance company conduct that is allegedly not in compliance with this rate-  
6 setting scheme.

7         Significantly, while this detailed and "comprehensive administrative scheme" provides a  
8 mechanism by which the Commissioner may seek to reduce, on a prospective basis, the approved rates  
9 of an insurer if the Commissioner has good cause to believe such rates have become "excessive," the  
10 regulatory scheme does not allow him to issue a Refund Order. To the contrary, the issuance of a  
11 Refund Order is prohibited, for good reason: to compel insurers to refund premiums collected pursuant  
12 to previously approved rates would undermine the prior approval process itself and infuse dangerous  
13 uncertainty in the insurance industry. If insurance companies may not rely upon previously approved  
14 rates, and must constantly face the risk and uncertainty that their rates will retroactively be reduced, they  
15 will be unable to create and abide by meaningful budgets, make appropriate prospective business  
16 decisions involving the evaluation of profitability and investment of capital, and attract necessary capital  
17 at reasonable rates of return.

18         Finally, as Respondents shall demonstrate at the Hearing on the OSC, Respondents' rates are not  
19 excessive. On or before June 15, 2007, in a prior approval rate case that is currently pending in this  
20 court (designated File No.: PA-2006-00006), Allstate will be filing an amended rate application  
21 demonstrating through the consistent application of sound actuarial principles that, if anything, its  
22 current homeowners' insurance rates do not fully and adequately cover their projected losses, expenses,  
23 and reasonable costs of capital.

#### 24                                   **ADDITIONAL PREFATORY STATEMENT**

25         Respondents are concerned by the fact that the Commissioner has apparently made the  
26 determination, or somehow come to believe, that Allstate's rates are excessive by a factor of 43.88%.  
27 On September 1, 2006, Respondents filed an application ("Rate Application") for an increase in their  
28 homeowners' insurance rates. The resulting "prior approval proceeding" (the "Rate Case") which has

1 been designated File No.: PA-2006-00006, has been pending since that time. On or about September 28,  
2 2006, the FTCCR intervened in the Rate Case. In early January, the CDI issued a Notice of Hearing in  
3 the Rate Case. On April 26, 2007, Chief Administrative Law Judge Marjorie Rasmussen scheduled a  
4 full adjudicative hearing date in the Rate Case. The hearing is scheduled to commence in September of  
5 2007.

6 Under Cal. Gov. Code § 11517(c), the Commissioner will be the ultimate administrative  
7 decisionmaker regarding the Rate Application. It appears, from the assertion within the OSC that  
8 Allstate's rates are excessive by 43.88% and that the Commissioner has pre-judged and already made a  
9 determination not to grant the rate increase being considered in the Rate Case, without providing  
10 Respondents with any of their Due Process Rights. In addition, Respondents do not understand how the  
11 Commissioner could make a determination regarding "excessiveness," much less the amount of the  
12 alleged excessiveness, without violating statutory prohibitions on *ex parte* communications and staff  
13 contact by communicating with either the FTCCR or the CDI regarding the Rate Case.

14 "While the proceeding is pending there shall be no communication, direct or indirect, regarding  
15 any issue in the proceeding, to **the presiding officer from an employee or representative of an**  
16 **agency that is a party or from an interested person outside the agency**, without notice and  
17 opportunity for all parties to participate in the communication." Cal. Gov. Code § 11430.10(a)  
18 (emphasis added). The California Supreme Court has held that the **APA does not "permit prosecutors**  
19 **and other adversarial agency employees to have off-the-record contact about substantive issues**  
20 **with the agency head, or anyone to whom the agency head delegates decisionmaking authority,**  
21 **during the pendency of an adjudicative proceeding."** *Department of Alcoholic Beverage Control v.*  
22 *Alcoholic Beverage Control Appeals Bd.*, 40 Cal. 4th 1, 10 (2006) ("Quintanar") (emphasis added).  
23 Neither the CDI nor the Commissioner are exempt from the protections afforded by this statute and the  
24 cases decided thereunder.

25 The Commissioner has apparently received information or evidence pertinent to the Rate Case in  
26 an *ex parte* context or manner. Whether the information came from CDI employees or the FTCCR is  
27 irrelevant. Respondents have had no opportunity to review this "evidence," cross-examine witnesses, or  
28 rebut this evidence. "The decision of the agency head should be based on the record and not on off-the-

1 record discussions from which the parties are excluded.” *Quintanar*, 40 Cal. 4th at 11 (quoting West's  
2 Annotated Cal. Gov. Code § 11430.80, Law Revision Comm'n cmt. 32D).

3 Administrative tribunals which are required to make a determination after a hearing cannot act  
4 upon their own information, and nothing can be considered as evidence that was not introduced at a  
5 hearing of which the parties had notice or at which they were present. The fact that there may be  
6 substantial and properly introduced evidence which supports the board's ruling is immaterial. A contrary  
7 conclusion would be tantamount to requiring a hearing in form but not in substance, for the right of a  
8 hearing before an administrative tribunal would be meaningless if the tribunal were permitted to base its  
9 determination upon information received without the knowledge of the parties. *English v. City of Long*  
10 *Beach*, 35 Cal. 2d 155, 158-59 (1950) (internal citations omitted). If the Commissioner has violated the  
11 statutory protections designed to ensure due process and a fair hearing, courts have concluded that no  
12 harm must be shown and “reversal of the Department’s orders is required.” *Quintanar*, 40 Cal. 4th at  
13 17.

14 Respondents hereby expressly reserve any and all rights they may have as a result of the matters  
15 addressed and the issues raised in this “Additional Prefatory Statement.”

### 16 I. NOTICE AND GENERAL ALLEGATIONS

17 1. **Paragraph 1 of OSC<sup>2</sup>:** Pursuant to Cal. Ins. Code section 1858.1 unless Respondents  
18 can show cause as to why the noncompliance alleged herein does not exist by establishing compliance to  
19 the satisfaction of the Commissioner, Respondents are ordered to correct the noncompliance within 10  
20 days of the date of this Notice.

21 **Answer:** The allegations of paragraph 1 of the OSC constitute characterizations of law,  
22 legal conclusions, and a purported order to which no response is required. To the extent an admission or  
23 denial is for some reason otherwise required, Allstate denies each and every allegation of paragraph 1 of  
24 the OSC. Allstate further affirmatively alleges that it is currently charging a rate that was previously  
25 approved by the Commissioner, and that, under California law, Allstate is prohibited from charging a  
26 rate other than the approved rate. Allstate further affirmatively alleges that the OSC improperly orders  
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28 <sup>2</sup> The allegations of the OSC are set forth in their entirety herein for the convenience of the reader.

1 Allstate to violate California law by directing it to charge a rate different from the rate that was  
2 previously approved by the Commissioner. Allstate further affirmatively alleges that, in accordance  
3 with California law, Allstate filed a rate application on September 1, 2006 in an effort to obtain approval  
4 to charge a different rate than that previously approved by the Commissioner. Allstate further  
5 affirmatively alleges that a hearing on that rate application is scheduled for September of 2007. Allstate  
6 further affirmatively alleges that the OSC represents an improper attempt by the Commissioner to  
7 invoke his enforcement power to interfere with Allstate's right to a hearing on its previously filed rate  
8 application.

9       2.       **Paragraph 2 of OSC:** Pursuant to Cal. Ins. Code section 1858.2, if within 10 days of the  
10 date of this notice Respondents do not make those changes as may be necessary to correct the  
11 noncompliance alleged herein or Respondents fail to show cause as to why the noncompliance alleged  
12 herein does not exist a notice of public hearing will issue and a public hearing will commence 30 days  
13 after the date of that notice of public hearing.

14               **Answer:** The allegations of paragraph 2 of the OSC constitute characterizations of law,  
15 legal conclusions, and purported predictions regarding future events to which no response is required.  
16 To the extent an admission or denial is for some reason otherwise required, Respondents deny each and  
17 every allegation of paragraph 2 of the OSC.

18       3.       **Paragraph 3 of OSC:** Pursuant to Cal. Ins. Code section 1858.3 if, after the hearing  
19 held pursuant to Cal. Ins. Code section 1858.2, the Commissioner finds that the rates being charged by  
20 Respondents for policies of Homeowners Multi-Peril insurance are excessive and being charged in  
21 violation of the provisions of Cal. Ins. Code section 1861.05, the continued charging of those rates shall  
22 be prohibited.

23               **Answer:** The allegations of paragraph 3 of the OSC constitute characterizations of law,  
24 legal conclusions, and purported predictions regarding future events to which no response is required.  
25 To the extent an admission or denial is for some reason otherwise required, Respondents deny each and  
26 every allegation of paragraph 3 of the OSC.

27       4.       **Paragraph 4 of OSC:** Pursuant to Cal. Ins. Code section 1858.3 if, after the hearing  
28 held pursuant to Cal. Ins. Code section 1858.2, the Commissioner finds that the rates being charged by

1 Respondents for policies of Homeowners Multi-Peril insurance are excessive and being charged in  
2 violation of the provisions of Cal. Ins. Code section 1861.05, the Commissioner will take any and all  
3 corrective action as may be deemed necessary and proper, including but not limited to, the ordering of  
4 premium credit to policyholders to offset excessive premium already paid and/or monetary assessments  
5 to facilitate the refunding to policyholders of excessive premium dollars collected pursuant to the  
6 charging of excessive rates in violation of Cal. Ins. Code section 1861.05.

7           **Answer:** The allegations of paragraph 4 of the OSC constitute characterizations of law  
8 and legal conclusions to which no response is required. To the extent an admission or denial is for some  
9 reason otherwise required, Respondents deny each and every allegation of paragraph 4 of the OSC.  
10 Respondents further affirmatively allege that the Commissioner lacks the legal authority to order the  
11 Respondents to issue any credits or refunds to policyholders on account of premiums charged and paid  
12 pursuant to rates previously and duly approved by the Commissioner.

13           5.       **Paragraph 5 of OSC:** To respond to this Notice of Noncompliance and Order to Show  
14 Cause Respondents shall submit an original and four (4) copies of the responsive document to Donald P.  
15 Hilla, Senior Litigation Counsel, 45 Fremont Street, 21st Floor, San Francisco, CA 94105 within 10  
16 days of the date of this notice.

17           **Answer:** The allegations of paragraph 5 of the OSC constitute characterizations of law  
18 and legal conclusions to which no response is required. To the extent an admission or denial is for some  
19 reason otherwise required, Respondents deny each and every allegation of paragraph 5 of the OSC.  
20 Respondents further affirmatively allege that, under Cal. Gov. Code § 11506 and Cal. Code Civ. Proc. §  
21 1013(a), the time within which Respondents must file their Notice of Defense is 15 days from the date  
22 of service of the OSC, plus two additional court days on account of service by overnight mail (not ten  
23 days from the date of issuance of the OSC, as alleged by the Commissioner).

24           6.       **Paragraph 6 of OSC:** Respondents are and were at all relevant times insurers licensed to  
25 transact and did transact the business of insurance in the State of California including the sale of policies  
26 of Homeowners Multi-Peril insurance and did market and sell said policies.

27           **Answer:** Respondents admit the allegations of Paragraph 6 of the OSC.  
28

1           7.     **Paragraph 7 of OSC:** Pursuant to Cal. Ins. Code section 700(c) all insurers engaged in  
2 the business of insurance in this state are required to comply with all statutory requirements of the  
3 insurance laws of this state.

4                     **Answer:** The allegations of paragraph 7 of the OSC constitute characterizations of law  
5 and legal conclusions to which no response is required.

6           8.     **Paragraph 8 of OSC:** Pursuant to Cal. Ins. Code section 1861.05, no rate charged for a  
7 policy of insurance in those lines subject to Cal. Ins. Code section 1861.05 shall remain in effect where  
8 those rates are excessive. Homeowners Multi-Peril insurance is a line of insurance subject to California  
9 Insurance Code section 1861.05. The Commissioner hereby notifies Respondents that he has  
10 determined and has good cause to believe the rates being charged by Respondents for policies of  
11 Homeowners Multi-Peril are excessive, are being charged in noncompliance with the law and that  
12 Respondents knew or should have known the rates being charged were excessive and in violation of the  
13 law.

14                     **Answer:** The allegations of the first sentence of paragraph 8 of the OSC constitute  
15 characterizations of law and legal conclusions to which no response is required. Respondents admit  
16 that their homeowners' multi-peril line of insurance is subject to California Insurance Code section  
17 1861.05. The statement that "[t]he Commissioner hereby notifies Respondents that he has determined  
18 and has good cause to believe the rates being charged by Respondents for policies of Homeowners  
19 multi-peril are excessive, are being charged in noncompliance with the law and that Respondents knew  
20 or should have known the rates being charged were excessive and in violation of the law," is a purported  
21 "notification," that can be neither admitted nor denied. To the extent that the statement represents an  
22 allegation that the Commissioner has made a determination regarding the alleged presence of "good  
23 cause to believe," the Respondents lack sufficient information to form a belief regarding the truth or  
24 falsity of the allegation that the Commissioner has made a determination, and therefore deny that  
25 allegation. To the extent that it represents an allegation or allegations that there is "good cause to  
26 believe the rates being charged by Respondents for policies of Homeowners multi-peril are excessive,  
27 are being charged in noncompliance with the law and that Respondents knew or should have known the  
28 rates being charged were excessive and in violation of the law," Respondents deny those allegations.



1 **II. RESPONDENTS' ALLEGED NONCOMPLIANCE**

2 9. **Paragraph 9 of OSC:** Pursuant to Cal. Ins. Code section 1858.1, upon the basis of  
3 information obtained from Respondents, the Commissioner has determined that good cause exists to  
4 believe that the rates being charged by Respondents for policies of Homeowners Multi-peril insurance  
5 do not comply with the requirements of the law, specifically, the rates being charged by Respondents for  
6 policies of Homeowners Multi-peril insurance are excessive, within the meaning and in violation of  
7 California Insurance Code section 1861.05. (See attached calculation and supporting documentation  
8 designated Exhibit 1.)

9 **Answer:** Respondents lack sufficient information to determine the truth or falsity of the  
10 allegation contained in Paragraph 9 of the OSC that “upon the basis of information obtained from  
11 Respondents, the Commissioner has determined that good cause exists . . .,” and therefore deny that  
12 allegation. To the extent that Paragraph 9 of the OSC contains allegations that Respondents’  
13 homeowners’ multi-peril insurance rates are excessive and in violation of the law, Respondents deny  
14 those allegations.

15 10. **Paragraph 10 of OSC:** The Commissioner has determined that good cause exists to  
16 believe that the rates being charged by Respondents for policies of Homeowners Multi-peril insurance  
17 do not comply with the requirements of the law, specifically, that the rates being charged by  
18 Respondents for policies of Homeowners Multi-peril insurance are excessive, within the meaning of  
19 California Insurance Code section 1861.05. Specifically, application of California Code of Regulations  
20 (Cal. Code Regs.) sections 2641.1 *et seq.* which are designed to implement and make specific the  
21 requirements of Cal. Ins. Code section 1861.05, provides evidence that Respondents rates are excessive  
22 and should be reduced 43.88% in order to be in compliance with the law. (See attached calculation and  
23 supporting documentation designated Exhibit 1.)

24 **Answer:** Respondents lack sufficient information to determine the truth or falsity of the  
25 allegation contained in Paragraph 10 of the OSC that “the Commissioner has determined that good cause  
26 exists . . .,” and therefore deny that allegation. To the extent that Paragraph 10 of the OSC contains  
27 allegations that Respondents’ homeowners’ multi-peril insurance rates are excessive and not in  
28 compliance with the law, Respondents deny those allegations. Respondents deny the allegations that

1 “application of California Code of Regulations (Cal. Code Regs.) sections 2641.1 *et seq.* which are  
2 designed to implement and make specific the requirements of Cal. Ins. Code section 1861.05, provides  
3 evidence that Respondents rates are excessive and should be reduced 43.88% in order to be in  
4 compliance with the law.”

### 5 III. PRAYER FOR RELIEF

6 11. **Paragraph 11 of OSC:** Pursuant to Cal. Ins. Code section 1861.05, as implemented and  
7 made specific by Cal. Code Regs, sections 2641.1 *et seq.*, in order to correct the noncompliance herein  
8 alleged, Respondents must reduce the rates charged for policies of Homeowners Multi-Peril insurance  
9 by 43.88%.

10 **Answer:** Respondents deny the allegations that they have failed to comply in any respect  
11 with the applicable law and that they must reduce their homeowners’ insurance rates by 43.88% in order  
12 to correct the alleged noncompliance. The remaining allegations of paragraph 11 of the OSC constitute  
13 characterizations of law and legal conclusions to which no response is required. Allstate further  
14 affirmatively alleges that it is currently charging a rate approved by the Commissioner and, under  
15 California law, Allstate is prohibited from charging a rate other than the approved rate. Allstate further  
16 affirmatively alleges that the OSC improperly directs Allstate to violate California by directing it to  
17 charge a different rate than that approved by the Commissioner. Allstate further affirmatively alleges  
18 that the Commissioner’s attempt to require Allstate to reduce its rates prior to a hearing violates  
19 Allstate’s right to due process. Allstate further affirmatively alleges that, from a practical standpoint, it  
20 would be impossible for Allstate to roll back its rates by any amount, let alone 43.88%, within 10 days.

21 12. **Paragraph 12 of OSC:** Pursuant to Cal. Ins. Code section 1858.1 unless Respondents  
22 can show cause as to why the noncompliance alleged herein does not exist Respondents are ordered to  
23 correct this noncompliance by reducing the rates charged for policies of Homeowners Multi-Peril  
24 insurance by 43.88% within 10 days of the date of this Notice.

25 **Answer:** Paragraph 12 of the OSC constitutes a purported “order” to which no response  
26 is required. To the extent that Paragraph 12 can be read to contain an implicit allegation that  
27 Respondents’ rates are in violation of applicable law (much less, in violation by a factor of 43.88%),  
28 Respondents deny those allegations.

1           13.     **Paragraph 13 of OSC:** Pursuant to Cal. Ins. Code section 1858.2, Respondents are  
2 ordered to, within 10 days of the date of this notice, make those changes as may be necessary to correct  
3 the noncompliance alleged herein or show cause as to why the noncompliance alleged herein does not  
4 exist.

5                     **Answer:** Paragraph 13 of the OSC constitutes a purported “order” to which no response  
6 is required. To the extent that Paragraph 13 can be read to contain an implicit allegation that  
7 Respondents’ rates are in violation of applicable law, Respondents deny those allegations.

8           14.     **Paragraph 14 of OSC:** Pursuant to Cal. Ins. Code section 1861.05, the Commissioner is  
9 charged with protecting the citizens of this state from excessive insurance rates. Respondents are on  
10 notice that the Commissioner has determined and has good cause to believe the rates being charged by  
11 Respondents are now and have been excessive and in order to correct the noncompliance Respondents  
12 should cease and desist charging excessive rates for policies of Homeowners Multi-Peril insurance as  
13 excessive rates may not lawfully be charged in this state.

14                     **Answer:** The allegations of the first sentence of paragraph 14 of the OSC constitute  
15 characterizations of law and legal conclusions to which no response is required. The second sentence of  
16 paragraph 14 of the OSC constitutes a purported “notification” to the Respondents regarding a  
17 determination that has allegedly been made by the Commissioner to which no response is required. To  
18 the extent that Paragraph 14 can be read to contain implicit allegations that Respondents’ homeowners’  
19 insurance rates are excessive or that there is good cause to believe that such rates are excessive,  
20 Respondents deny those allegations.

21           15.     **Paragraph 15 of OSC:** If after the hearing held pursuant to Cal. Ins. Code section  
22 1858.2, the Commissioner finds that the rates being charged by Respondents for policies of  
23 Homeowners Multi-Peril insurance are excessive and have been and are being charged in violation of  
24 the provisions of Cal. Ins. Code section 1861.05, pursuant to Cal. Ins. Code 1858.3 the Commissioner  
25 will take any and all corrective action as may be deemed necessary and proper, including but not limited  
26 to, credit to policyholders for excessive premium already paid or monetary assessments to facilitate the  
27 refunding to policyholders of excessive premium paid resultant from the charging of excessive rates in  
28 violation of Cal. Ins. Code section 1861.05.

1           **Answer:** Paragraph 15 of the OSC constitutes a purported prediction regarding the  
2 future actions of the Commissioner to which no response is required. To the extent that Paragraph 15  
3 can be read to contain implicit allegations that Allstate's homeowners' insurance rates are excessive,  
4 Allstate denies those allegations. Allstate further affirmatively alleges that the Commissioner lacks legal  
5 authority to order Allstate to issue any credits or refunds to policyholders on account of premiums  
6 charged and paid pursuant to rates previously and duly approved by the Commissioner. Allstate further  
7 affirmatively alleges that, in accordance with California law, Allstate filed a rate application on  
8 September 1, 2006 in an effort to obtain authority charge a rate different than that rate that had  
9 previously been approved by the Commissioner. Allstate further affirmatively alleges that a hearing on  
10 that rate application is scheduled for September of 2008. Allstate further affirmatively alleges that the  
11 OSC represents an improper attempt by the Commissioner to invoke his enforcement power to interfere  
12 with Allstate's right to a hearing on its previously filed rate application.

#### 13                                       **IV. APPLICABLE LAW AND PROCEDURE**

14           16.   **Paragraph 16 of OSC:** If, pursuant to Cal. Ins. Code section 1858.1, Respondents  
15 cannot show cause as to why the noncompliance alleged herein does not exist by establishing to the  
16 satisfaction of the Commissioner that the noncompliance does not exist, or if pursuant to Cal. Ins. Code  
17 section 1858.2, within 10 days of the date of this notice Respondents do not make those changes as may  
18 be necessary to correct the noncompliance alleged herein and if a notice of public hearing issues and a  
19 public hearing commences 30 days after the date of this notice, the purpose of that public hearing will be  
20 to ascertain whether Respondent's current rates comply with the requirements of Cal. Ins. Code section  
21 1861.05.

22           **Answer:** The allegations of paragraph 16 of the OSC constitute characterizations of  
23 law and legal conclusions to which no response is required. To the extent that Paragraph 16 can be read  
24 to contain implicit allegations that Respondents' homeowners' insurance rates are excessive,  
25 Respondents deny those allegations. Respondents further affirmatively allege that the OSC represents  
26 an improper attempt by the Commissioner to engage in underground rulemaking.

27           17.   **Paragraph 17 of OSC:** Specifically the hearing will be held for the purpose of  
28 determining whether the current rates being charged by Respondents are excessive and being charged in

1 violation of Cal. Ins. Code section 1861.05 by application of the pertinent portions of Cal. Code Regs.  
2 sections 2644.1 *et seq.*

3 **Answer:** The allegations of paragraph 17 of the OSC constitute characterizations of law,  
4 legal conclusions, and purported predictions regarding future events to which no response is required.  
5 To the extent that Paragraph 17 can be read to contain implicit allegations that Respondents'  
6 homeowners' insurance rates are excessive, Respondents deny those allegations.

7 18. **Paragraph 18 of OSC:** The hearing shall be conducted pursuant to the requirements set  
8 forth in Cal. Ins. Code section 1861.08 which requires the hearing be conducted pursuant to Chapter 5,  
9 commencing with Section 11150 of Part I of Division 3 of title 2 of the Californian Government Code  
10 with the exception that the hearing be conducted by the California Department of Insurance  
11 Administrative Law Judges.

12 **Answer:** The allegations of paragraph 18 of the OSC constitute characterizations of law,  
13 legal conclusions, and purported predictions regarding future events to which no response is required.  
14 To the extent that Paragraph 18 can be read to contain implicit allegations that Respondents'  
15 homeowners' insurance rates are excessive, Respondents deny those allegations. Respondents further  
16 affirmatively allege that there exist no California statutes or regulations authorizing or establishing  
17 procedures for the ordered refund or credit of premiums previously charged to policyholders pursuant to  
18 duly authorized and approved rates on the ground that such rates were allegedly excessive.

19 19. **Paragraph 19 of OSC:** The hearing shall also be conducted pursuant to Cal. Code Regs.  
20 section 2646.4 and pursuant to all the instructions contained herein. Specifically, as the Commissioner  
21 has determined and has good cause to believe the rates in effect and being charged by Respondents are  
22 excessive, and as the Commissioner has alleged so herein, pursuant to Cal. Code Regs section 2646.4  
23 subsection (a)(2) the hearing will be for the purpose of determining whether the rates are excessive.

24 **Answer:** Respondents lack sufficient information to determine the truth or falsity of the  
25 allegation contained in Paragraph 19 of the OSC that the "Commissioner has determined . . .," and  
26 therefore deny that allegation. Respondents deny the allegation that the Commissioner "has good cause  
27 to believe the rates in effect and being charged by Respondents are excessive." The remaining  
28 allegations of paragraph 19 of the OSC constitute characterizations of law and legal conclusions as to

1 which no response is required. Respondents further affirmatively allege that, contrary to the allegations  
2 of the Commissioner, Cal. Code Regs. § 2646.4 is inapplicable to this proceeding. The procedures that  
3 govern the conduct of non-compliance proceedings are set forth in Cal. Code Regs. § 2614, *et seq.*  
4 Respondents further affirmatively allege that there exist no California statutes or regulations authorizing  
5 or establishing procedures for the ordered refund or credit of premiums previously charged to  
6 policyholders pursuant to duly authorized and approved rates on the ground that such rates were  
7 allegedly excessive.

8       **20. Paragraph 20 of OSC:** In order to determine whether the rates are excessive the law  
9 governing is Cal. Ins. Code section 1861.05 as implemented and made specific in Cal. Code Regs  
10 sections 2641.1 *et seq.* Those regulatory sections shall be applied to Respondents' historical data to  
11 determine, through application of the ratemaking formula, other formulae, and applicable calculations,  
12 according to the procedures and instructions contained therein, whether the rates in effect and currently  
13 being charged by Respondents are excessive.

14       **Answer:** The allegations of paragraph 20 of the OSC constitute characterizations of law,  
15 legal conclusions, and predictions as to future events to which no response is required. To the extent a  
16 response is required, Respondents deny the allegations of paragraph 20 of the OSC. Respondents  
17 further affirmatively allege that Cal. Code Regs sections 2641.1 *et seq.* is inapplicable to the OSC.

18       **21. Paragraph 21 of OSC:** Pursuant to Government Code section 11507.3(b) it is hereby  
19 ordered that in furtherance of convenience and to expedite the proceeding this hearing shall be held in  
20 two separate parts.

21       **Answer:** The allegations of paragraph 21 of the OSC constitute characterizations of law,  
22 legal conclusions, and a purported order to which no response is required. Respondents further  
23 affirmatively allege that the Commissioner lacks legal authority to order that the hearing be conducted in  
24 two separate parts under Government Code section 11507.3(b).

25       **22. Paragraph 22 of OSC:** Part one will be commenced for the sole purpose of determining  
26 whether the rates currently being charged by Respondents for policies of Homeowners Multi-Peril  
27 insurance are excessive and being charged in noncompliance with the law. Only in the case where  
28

1 Respondents fail to meet their burden and the rates are found to be excessive and it is so ordered by the  
2 Commissioner will the second part of the hearing be required.

3           **Answer:** The allegations of paragraph 22 of the OSC constitute characterizations of law,  
4 legal conclusions, predictions regarding possible future events, and statements regarding the manner in  
5 which the Commissioner would like the hearing to be conducted to which no response is required. To  
6 the extent a response is required, Respondents deny the allegations of paragraph 22 of the OSC.  
7 Respondents further affirmatively allege that the Commissioner lacks legal authority to order that the  
8 hearing be conducted in two separate parts under California Government Code section 11507.3(b).  
9 Respondents further affirmatively allege that, under Cal. Code Regs. § 2614.6, the Commissioner, not  
10 the Respondents, bears the burden of proof on the allegation that the Respondent's rates are excessive.

11           **23. Paragraph 23 of OSC:** At the conclusion of part one of the hearing the Administrative  
12 Law Judge will issue a proposed decision on the issue of whether the rates in effect and being charged  
13 by Respondents are excessive and being charged in noncompliance with the law. In the event the  
14 Administrative Law Judge finds the rates to be excessive, pursuant to Cal. Code Regs. section 2644.1,  
15 the proposed decision will include an indication as to the highest rate that may be charged that would not  
16 be excessive. Pursuant to Government Code section 11517(c)(1) the proposed decision shall be  
17 delivered to the Commissioner no later than 30 days after the case is submitted to the Administrative  
18 Law Judge.

19           **Answer:** The allegations of paragraph 22 of the OSC constitute characterizations of law,  
20 legal conclusions, predictions regarding possible future events, and statements regarding the manner in  
21 which the Commissioner would like the hearing to be conducted to which no response is required. To  
22 the extent that a response is for some reason required, Respondents deny the allegations of paragraph 23  
23 of the OSC.

24           **24. Paragraph 24 of OSC:** The Commissioner will then issue an Order as to whether  
25 Respondents' current rates are excessive and if the Commissioner finds Respondents' current rates to be  
26 excessive, pursuant to Cal. Code Regs. section 2644.1, the Order will include an indication as to the  
27 highest rate that may be charged that would not be excessive. Pursuant to Cal. Ins. Code section 1858.3  
28

1 the Commissioner may also order Respondents to take such corrective action as he may deem necessary  
2 and proper.

3           **Answer:** The allegations of paragraph 24 of the OSC constitute characterizations of law,  
4 legal conclusions, and predictions regarding possible future events to which no response is required. To  
5 the extent a response is for some reason required, Respondents deny the allegations of paragraph 24 of  
6 the OSC.

7           **25. Paragraph 25 of OSC:** If, and only if, after part one of the hearing the Commissioner  
8 finds the current rates being charged by Respondents are excessive within the meaning of and in  
9 noncompliance with Cal. Ins. Code section 1861.05, and pursuant to Cal. Ins. Code section 1858.3 the  
10 Commissioner orders credit to policyholders on excessive premium already paid or monetary  
11 assessments to facilitate the refunding to policyholders of excessive premium collected, the second part  
12 of the hearing will be held for the purposes of determining the amount of such monetary assessments or  
13 premium credits and to ascertain the proper actuarial procedure to be used to calculate such refunds or  
14 credits.

15           **Answer:** The allegations of paragraph 25 of the OSC constitute characterizations of law,  
16 legal conclusions, and predictions regarding possible future events to which no response is required. To  
17 the extent a response is for some reason required, Respondents deny the allegations of paragraph 25 of  
18 the OSC. Respondents further affirmatively allege that the Commissioner lacks the legal authority to  
19 order the Respondents to issue any credits or refunds to policyholders on account of premiums charged  
20 and paid pursuant to rates previously and duly approved by the Commissioner. Respondents further  
21 affirmatively allege that the OSC represents an improper attempt by the Commissioner to engage in  
22 underground rulemaking.

23           **26. Paragraph 26 of OSC:** If the second part of the hearing is required to be held and the  
24 Commissioner has ordered credits to policyholders on excessive premium already paid or monetary  
25 assessments to facilitate the refunding to policyholders of excessive premium collected, at the  
26 conclusion of part two of the hearing the Administrative Law Judge will issue a proposed decision on  
27 the issue of the amount of monetary assessments or premium credits and the proper actuarial procedure  
28 to be used to calculate such refunds or credits. Pursuant to Cal. Gov. Code section 11517(c)(1) the



1 proposed decision shall be delivered to the Commissioner no later than 30 days after the case is  
2 submitted to the Administrative Law Judge.

3           **Answer:** The allegations of paragraph 26 of the OSC constitute characterizations of law,  
4 legal conclusions, and predictions regarding possible future events to which no response is required. To  
5 the extent a response is for some reason required, Respondents deny the allegations of paragraph 26 of  
6 the OSC. Respondents further affirmatively allege that the Commissioner lacks the legal authority to  
7 order the Respondents to issue any credits or refunds to policyholders on account of premiums charged  
8 and paid pursuant to rates previously and duly approved by the Commissioner. The Respondents further  
9 affirmatively allege that the Commissioner lacks legal authority to order that the hearing be conducted in  
10 two separate parts under Government Code section 11507.3(b).

11           **27. Paragraph 27 of OSC:** If a proposed decision as described in paragraph 25 is delivered  
12 to the Commissioner, the Commissioner will subsequently issue a final Order relating to premium  
13 credits, monetary assessments, or other corrective action the Commissioner may deem necessary and  
14 proper pursuant to Cal. Ins. Code section 1858.3.

15           **Answer:** The allegations of paragraph 27 of the OSC constitute characterizations of law,  
16 legal conclusions, and predictions regarding possible future events to which no response is required. To  
17 the extent a response is for some reason required, Respondents deny the allegations of paragraph 27 of  
18 the OSC. Respondents further affirmatively allege that the Commissioner lacks the legal authority to  
19 order the Respondents to issue any credits or refunds to policyholders on account of premiums charged  
20 and paid pursuant to rates previously and duly approved by the Commissioner. Respondents further  
21 affirmatively allege that the Commissioner lacks legal authority to order that the hearing be conducted in  
22 two separate parts under Government Code section 11507.3(b).

23           **28. Paragraph 28 of OSC:** Pursuant to Cal. Code Regs. section 2646.5, Respondents shall  
24 have the burden of proving, by a preponderance of the evidence, that the rates are not excessive.

25           **Answer:** The allegations of paragraph 28 of the OSC constitute characterizations of law  
26 and legal conclusions as to which no response is required. To the extent a response is for some reason  
27 required, Respondents deny the allegations of paragraph 28 of the OSC. Respondents further  
28 affirmatively allege that Cal. Code Regs. § 2646.5 is inapplicable to this OSC proceeding. Respondents

1 further affirmatively allege that, pursuant to Cal. Code Regs. § 2614.6, the Commissioner, not  
2 Respondents, bears the burden of proof with respect to the allegation that Respondents' homeowners'  
3 insurance rates are excessive.

4 29. Respondents deny each and every allegation of the OSC that they do not expressly admit  
5 herein.

6 **AFFIRMATIVE DEFENSES**

7 30. The OSC is defective, and should be quashed, on the ground that it is so indefinite and  
8 uncertain that Respondents cannot adequately prepare their case.

9 31. The OSC is defective, and should be quashed, on the ground that the Commissioner's  
10 attempt to seek refunds of premium already paid to Respondents pursuant to rates previously approved  
11 by the Commissioner is inappropriate and contrary to applicable law.

12 32. The OSC is defective, and should be quashed, on the ground that the Commissioner has  
13 failed to establish good cause for the issuance of the OSC.

14 33. The OSC is defective, and should be quashed, on the ground that it seeks to impose an  
15 unjust, unreasonable and confiscatory rate standard, in a discriminatory and punitive fashion, in  
16 violation of the Fifth and Fourteenth Amendments of the United States Constitution.

17 34. The OSC is defective, and should be quashed, because it represents a wrongful attempt  
18 by the Commissioner both to circumvent established procedures for challenging approved rates and  
19 unlawfully to shift the burden of proof to the insurer.

20 35. The OSC is defective, and should be quashed, on the ground that it fails to follow the  
21 governing procedures for noncompliance hearings set forth in Cal. Code Regs. § 2614.24.

22 36. The OSC is defective, and should be quashed, on the ground that it represents an  
23 improper attempt by the Commissioner to engage in underground rulemaking.

24 37. The OSC is defective, and should be quashed, on the ground that the Commissioner's  
25 claims may be barred by the doctrine of laches.

26 38. Discovery may reveal the existence of additional affirmative defenses. The Respondents  
27 reserve the right to seek leave to amend their Notice of Defense to assert such additional affirmative  
28 defenses in the future.

1 **PRAYER FOR RELIEF**

2 For the foregoing reasons, Respondents respectfully request that the Judge of the Administrative  
3 Hearing Bureau (i) quash the OSC, (ii) strike those portions of the OSC seeking a refund of premiums  
4 previously paid by policyholders to the extent the OSC is not quashed, (iii) find that Respondents' rating  
5 plans, rating systems and rates for its Homeowners' multi-peril insurance lines are not in violation of  
6 Insurance Code § 1861.05, and (iv) grant Respondents such other and further relief as she or he deems  
7 just and appropriate.

8  
9 Dated: June 4, 2007

Respectfully submitted,

10 **LEBOEUF, LAMB, GREENE & MACRAE LLP**

11  
12  
13 By: 

Brett J. Kitei

*Attorneys for Allstate Insurance Company and  
Allstate Indemnity Company*

1 **PROOF OF SERVICE**

2 At the time of service, I was over 18 years of age and not a party to this action. My business  
3 address is LeBoeuf, Lamb, Greene & MacRae LLP, One Embarcadero Center, Suite 400, San Francisco,  
4 California 94111.

5 On the date hereinbelow listed, I served the foregoing document(s) described as:

6 **NOTICE OF DEFENSE**

7 on the interested parties in this action as follows:

8 **SERVICE LIST: (SEE ATTACHED)**

9  **By United States mail.** I enclosed the documents in sealed envelope(s) or package(s) addressed to  
10 the person(s) at the address(es) in the **Service List** and placed them for collection and mailing,  
11 following our ordinary business practices. I am readily familiar with this business's practice for  
12 collection and mailing. On the same day that correspondence is placed for collection and mailing, it  
13 is deposited in the ordinary course of business with the United States Postal Service, in envelope(s)  
14 or package(s) with postage fully prepaid. I am employed in the county where the mailing occurred.  
15 The envelope(s) or package(s) was placed in the mail at San Francisco, California.

16  **By messenger service.** I served the documents by placing them in sealed envelope(s) or package(s)  
17 addressed to the person(s) at the address(es) listed on the **Service List** and providing them to a  
18 professional messenger service for service.

19  **By electronic mail.** I served the documents via electronic mail, addressed to the person(s) at the  
20 email address(es) listed on the **Service List**.

21 I declare under penalty of perjury under the laws of the State of California that the foregoing is true  
22 and correct.

23 Executed on June 4, 2007 at San Francisco, California.

24 

25 \_\_\_\_\_  
26 Tracy Boothe

**SERVICE LIST**

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**Persons(s) Served**

**Phone/Fax Numbers**

**Method of Service**

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