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SUPERIOR COURT OF THE STATE OF CALIFORNIA

COUNTY OF LOS ANGELES

ASSOCIATION OF CALIFORNIA INSURANCE COMPANIES and PERSONAL INSURANCE FEDERATION OF CALIFORNIA, Plaintiffs, **v.** **DAVE JONES in his capacity as Commissioner of the California Department of Insurance,** Defendant.	Case No. BC463124 **CALIFORNIA DEPARTMENT OF INSURANCE'S OPPOSITION TO PLAINTIFFS' MOTION FOR JUDGMENT ON THE PLEADINGS** Date: January 6, 201 Time: 8:30 a.m. Dept: 36 Judge: The Honorable Gregory W. Alarcon Trial Date: Action Filed: June 8, 2011

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SUMMARY OF ARGUMENTS IN OPPOSITION TO MOTION FOR JUDGMENT ON THE PLEADINGS

Plaintiffs, trade organizations, Association of California Insurance Companies and Personal Insurance Federation of California, (hereinafter referred to as "plaintiffs"), have filed a motion for judgment on the pleadings against Dave Jones, in his capacity as Insurance Commissioner (hereinafter referred to as "Commissioner"). Plaintiffs' summary motion attempts to invalidate regulation 10 CCR Section 2695.183, by contending that the uniform definition contained in the regulation for the term "estimate of replacement cost" constitutes "underwriting", that the Commissioner lacked authority to enact the regulation, and that the regulation violates plaintiffs' First Amendment rights.

The Commissioner contends that the questioned regulation has nothing to do with "underwriting" since it does not mandate which risks of loss insurance carriers should insure against or what factors they should consider when providing coverage. The uniform definition contained in the regulation for the term "estimate of replacement cost" is merely interpretive and only requires that whenever an insurance carrier voluntarily decides to communicate such an estimate to a consumer or insured, that it contain certain information, thereby avoiding false, misleading and deceptive practices from occurring. The regulation does not require licensees (carriers, agents, and brokers) to provide an "estimate of replacement cost" to consumers or insureds.

In enacting the regulation the Commissioner was acting pursuant Insurance Code sections 790, 790.03(b), 790.10, 1749.7, as well as the general police powers enabling him to protect the public from deceptive, false and misleading practices regarding insurance. The Commissioner has complied with all First Amendment requirements in enacting the regulations at issue.

INTRODUCTION

Plaintiffs' motion requests that this court invalidate Insurance Regulation 10 CCR Section 2695.183. The motion fails, both on factual and legal grounds. It is based upon a partial administrative record carefully crafted to prevent the court from having access to the full record, thus lacking 'adequate disclosure" of the extensive hearings which occurred prior to enactment of

the regulation.

Even a cursory review of the arguments posed by plaintiffs shows that, stripped of its rhetoric and posturing, their motion for judgment on the pleadings is deficient as a matter of fact and law. The motion, replete with carefully crafted but faulty legal conclusions and factual contentions, is short on analysis, and evidentiarily deficient. Plaintiffs ask this court to scour through an incomplete record to make a determination as to the merits of a regulation based upon partial evidence, implications, and an absence of citation to the record. From this plaintiffs attempt to draw their ill-founded conclusions. Plaintiffs' motion and request for judicial notice asks the court to determine the merits of the underlying controversy by reverting to section 438 of the Code of Civil Procedure. A determination of the underlying merits of the controversy by the utilization of a motion for judgment on the pleadings is improper and not authorized by section 438.

The proper method to determine the validity of the subject regulation is not by employing the deficient summary method envisioned by plaintiffs but rather by presenting a complete administrative record to the court along with briefs citing to those portions of the record supporting their respective contentions.

This court should deny plaintiffs' motion for judgment on the pleadings because: (1) as a matter of law the court is not required to grant a motion for judgment on the pleadings; (2) plaintiffs have tendered only a partial administrative record to this court and on that basis expect the court to rule on their motion; (3) plaintiffs' motion does not cite to any portion of the administrative record to support the allegations contended; (4) the complete administrative record is voluminous and it would be a waste of this court's time to scour the entire record in order to assist plaintiffs in establishing a factual and legal basis for their contentions;[1] (5) plaintiffs arguments are not supported by either fact or law and therefore their motion must be denied.

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[1] Defendant will be providing the court with a complete administrative record, which exceeds 1,700 pages. A copy of the complete record will be served upon plaintiffs.

ARGUMENT

I. A MOTION FOR JUDGMENT ON THE PLEADINGS IS NOT THE PROPER MECHANISM FOR RESOLVING THIS DISPUTE AND PLAINTIFFS' MOTION MUST BE DENIED

A motion for judgment on the pleadings is in the nature of a general demurrer and must be denied if the answer raises material issues of fact or sets up a defense. (*Barasch v. Epstein* (1957) 147 Cal.App.2d 439-440, 442-443; *MacIssac v. Pozzo* (1945) 26 Cal.2d 809, 812-813). Thus, it is well settled that if an answer puts in issue a material allegation, or sets up an affirmative defense, a motion for judgment on the pleadings cannot be granted. (*Richter v. United Cal. Theaters, Inc.* (1960) 177 Cal.App.2d 126, 128).

When the moving party is the plaintiff a motion for judgment on the pleadings can only be granted if: (1) the complaint states facts sufficient to constitute a cause of action, and, (2) the answer does not state facts sufficient to constitute a defense to the complaint. (Code of Civ. Proc., § 438(c)(1)(A).) Plaintiffs' motion for judgment on the pleadings fails to comply with the requirements of section 438(c)(1)(A) since it does not show, either factually, or legally, that the Commissioner's answer does not constitute a defense to the allegations of plaintiffs' complaint. The portions of the administrative record supplied by plaintiffs do not assist them in their endeavor.

The Commissioner's answer contests all of the grounds of invalidity asserted against the questioned regulation via plaintiffs' complaint. In a motion for judgment on the pleadings, the court will consider all material facts pled to be true. (*Parnell v. Adventist Health Systems West* (2005) 35 Cal.4th 595, 598). It must do so with respect to the Commissioner's answer. It is not and never has been the function of a motion for judgment on the pleadings to test the truthfulness of the allegations contained in the respective pleadings under examination, thereby determining the controversy on its merits. Case law clearly demonstrates otherwise.

Plaintiffs are attempting to subvert the purpose of Code of Civil Procedure section 438 by turning it into something for which it was never intended. Plaintiffs are requesting this court to determine this controversy on the merits and not upon the pleadings filed by the respective parties. Plaintiffs expect the court to scour through an incomplete record in order to

resolve the controversy. Plaintiffs proceed with this ploy by requesting the court to take judicial notice of the partial record. This ploy must also fail.

The determination of the sufficiency of an answer requires an examination of the complaint because its adequacy is with reference to the complaint it purports to answer. (*Miller & Lux, Inc. v. San Joaquin Light & Power Corp.*, 120 Cal.App. 589, 600). Therefore, as with a general demurrer, a motion for judgment on the pleadings cannot be used to adjudicate the underlying merits of the action because the factual truth of the allegations are not at issue. (*Diamond Multimedia Systems, Inc. v. Superior Court* (1999) 19 Cal.4th 1036, 1041, fn. 4). A motion for judgment on the pleadings is not the appropriate procedure for determining the truth of disputed facts. (*Cross Talk Productions, Inc. v. Jacobson* (1996) 65 Cal.App.4th, 631, 635; *Ramsden v. Western Union* (1977) 71 Cal.App.3d 873, 879). Based upon a reading of the Commissioner's answers the facts are disputed.

In order for judicial notice to support a motion for judgment on the pleadings, the noticed evidence must be something that cannot reasonably be controverted. (2 Jefferson, Cal. Evidence Benchbook (2nd ed. 1982) Judicial Notice § 1747-1754 (1990) Supp. at § 47.2 p. 638; 1 Witkin, Cal. Evidence (3rd. ed 1986) Judicial Notice § 80, p. 75). Plaintiffs have not established that the partial record, which they request this court to take judicial notice of, contains items that cannot be reasonably controverted. Therefore, plaintiffs' request for judicial notice is deficient and should be rejected. Additionally, the partial nature of the administrative record makes it irrelevant for purposes of ruling on plaintiffs' motion contending that the Commissioner's answer does not provide a proper defense to the action.

II. PLAINTIFFS MOTION FAILS TO PROVIDE EVIDENTIARY OR LEGAL SUPPORT TO INVALIDATE THE QUESTIONED REGULATION ON THE MERITS OF THE CONTROVERSY

The promulgation of regulations is an exercise of an agency's quasi-legislative authority. (*California School Boards Association v. State Board of Education* (2010) 191 Cal.App.4th 530, 543-544). The agency's action comes before the court with a presumption of correctness and regularity, which places the burden of demonstrating invalidity upon the assailants. (Evid Code § 664; *Ralph's Grocery Co. v. Reimel* (1968) 69 Cal.2d 172, 175).

The burden is on the party challenging the regulation to establish its invalidity. (*Geftakys v. State Personnel Board (1982) 138 Cal.App.3d 844. 867*). The issue of whether a regulation is reasonably necessary implicates an agency's expertise. (*Yamaha Corp. of America v. State Board of Equalization* (1998) 19 Cal.4th 1, 11). "A facial challenge is '"the most difficult challenge to mount successfully, since the challenger must establish that *no set of circumstances exists under which the* [*law*] *would be valid.*'" The moving party must show that the challenged statutes or regulations 'inevitably pose a present total and fatal conflict with applicable prohibitions." (*T.H. v. San Diego Unified School Dist.* (2004) 122 Cal.App.4th 1267, 1281). Courts ordinarily defer to an agency's interpretation of a regulation with its area of expertise, "unless the interpretation flies in the face of the clear language and purpose of the provision." (*County of Sacramento v. State Water Resources Control Board* (2006) 145 Cal.App.4th 246, 252; *Stolman v. City of Los Angeles* (2003) 114 Cal.App.4th 916, 928). In considering the validity of a regulation, the court's "function is to inquire into the legality of the regulations, not their wisdom." (*Morris v. Williams* (1967) 67 Cal.2d 733, 737).

One of the grounds asserted for attempting to invalidate the questioned regulation is that there is no authority for the Commissioner to promulgate the regulation. In fact, as will be discussed herein, there is ample authority. Further, even if there was an absence of any specific statutory provision regarding a regulation, that does not mean that such regulation exceeds statutory authority. The Commissioner has broad discretion to adopt regulations as necessary to promote the public welfare. (*Calfarm Ins. Co. v. Deukmejian* (1989) 48 Cal.3d 805, 824). The Commissioner's powers are not limited to those expressly conferred by statute, but also include, "'such additional powers as are necessary for the due and efficient administration of powers expressly granted by statute, or as may fairly be implied from the statute granting the powers.'" (*20th Century Ins. Co. v. Garamendi* (1994) 8 Cal.4th 216, 245. The agency is authorized to "fill in the details of the statutory scheme." (*Mineral Association Coalition v. State Mining & Geology Board* (2006) 138 Cal.App.4th 574, 589; *Marshall v. McMahon* (1993) 17 Cal.App.4th 1841, 1848). The prevention of deceit and transmission of misleading information promotes the public welfare. The Commissioner has thus acted properly in enacting the regulation.

> "Government Code section 11342.2 provides the general standard of review for determining the validity of administrative regulations. That section state that [w]henever by the express or implied terms of any statute a state agency has authority to adopt regulations to implement, interpret, make specific or otherwise carry out the provisions of the statute, no regulation adopted is valid or effective unless [1] consistent and not in conflict with the statute and [2] reasonably necessary to effectuate the purpose of the statute.'" (*Communities for a Better Environment v. California Resources Agency* (2002) 103 Cal.App.4th 98, 108).

When a regulation is challenged, the task of the court is to determine whether the questioned regulation: (1) is within the scope of authority conferred, (Gov. Code § 11373) and (2) is reasonably necessary to effectuate the purpose of the statute. (Gov. Code § 11374). In enacting the regulation, the Commissioner was acting pursuant to Insurance Code sections 790, 790.10, 790.30, to prevent the misleading and deceptive practices of licensees providing differing and self-serving definitions for the term "estimate of replacement cost" to insureds and consumers. The regulation itself states that failure to comply with the "estimate of replacement cost" definition contained with the regulation is a misleading and deceptive practice violative of Insurance Code section 790.03(b). (3) The regulation is merely interpretive of the concepts of false misleading or deceptive practices which the Insurance Code prohibits.

Without providing a uniform definition of the term "estimate of replacement cost," consumers have no way of determining what the licensee means when the term is communicated to them. By providing a uniform definition for the term, the regulation ensures that insureds and consumers are placed on a level playing field and can understand what a communicated "estimate of replacement cost" includes. It permits them the opportunity to better evaluate the potential risk of loss, which the insurance was meant to cover. It is important to note that the regulation does not require insurance carriers to communicate an "estimate of replacement cost". The regulation merely provides that when an "estimate of replacement cost" is communicated, it contains certain essential items.

Stripped of its rhetoric, plaintiffs' motion fails to meet its burden of proving that the questioned regulation is invalid. Other than broad sweeping allegations, plaintiffs' motion does not cite to any specific evidence to support its conclusory analysis. Issues relating to providing a uniform definition of the term "estimate of replacement cost" and its impact on insurers' inability

to engage in free speech, and other ill conceived notions, are far-fetched fantasies. The law is clear. The Commissioner has broad discretion to adopt rules and regulations necessary to promote the public welfare. (*Credit Ins. Gen. Agents Assn. v. Payne* (1976) 16 Cal.3d 651, 656). The regulation at issue falls within these criteria.

Even though the regulation specifically states that providing "an estimate of replacement cost" is not required, plaintiffs challenge subdivision (g)(2) of the regulation because it mandates the inclusion of certain items as set forth in subdivision (a)(1)-(4). (PPA[2] p. 6, lines 11-22).

At no time did plaintiffs, or anyone else who offered comments in the protracted and thorough rulemaking process, suggest that a replacement cost estimate that did not contain all the ingredients was not inherently misleading. This is true despite the fact that the Initial Statement of Reasons stated categorically that such an incomplete estimate necessary is misleading:

> If all of the relevant elements and components necessary to calculate an estimate of replacement cost are not considered, the use of the term "replacement" is inherently misleading. It leads an applicant or insured to expect that the estimate was based on all of the necessary components to effectuate a true "replacement" cost estimate when, in reality, the estimate may, in fact, be low because certain components necessary to rebuild or replace have not been factored into the estimate. (Initial Statement of Reasons, p. 18.)

The rulemaking process provided plaintiffs with an adequate opportunity to voice their objections. The fact that nowhere in their exhaustive objections as expressed in their comments to the noticed regulation did plaintiffs contest this statement constitutes a tacit admission by the industry that expressing to a consumer such an incomplete estimate of replacement value does, in fact, constitute a misleading statement, and that the insurance industry knows or should know that this is the case.

To the extent that the questioned regulation is applicable, plaintiffs incorrectly contend that mandated information "goes well beyond avoiding misleading information" and is therefore beyond the scope of the Commissioners authority. (PPA p. 6, lines 18-22). Plaintiffs' allegation is based on pure conjecture.

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[2] The designation "PPA" refers to plaintiff's points and authorities filed in support of their motion.

Regulation 10 CCR Section 2695.183 is remedial in nature because it enables consumers to make informed decisions about what is and is not within the definition of "an estimate of replacement cost." By contrast, plaintiffs seek to provide self-serving definitions of "an estimate of replacement cost," thereby leading consumers to guess what an "estimate of replacement cost" means, and what components of rebuilding a structure includes. The definition of "estimate of replacement cost" should not be determined thorough litigation initiated by insureds. The Commissioner's enactment of section 2695.183 avoids this situation. The regulation prevents a potentially unfair and deceptive practice from taking place and interprets acts constituting fraud, deceipt and misleading statements.

Plaintiffs' moving papers fail to show that the Commissioner lacks the authority to promulgate and enact the questioned regulation or, that the Commissioner has exceeded his authority in promulgating the questioned regulation.

III. THE COMMISSIONER HAD THE AUTHORITY TO PROMULGATE THE QUESTIONED REGULATION

The administrative record is clear. Section 2695.183 requires that if the licensee communicates an estimate of replacement cost, that it will be complete and include consideration of those components enumerated in the regulation. To communicate an estimate that is missing components results in consumer confusion and is misleading.

California Insurance Code Section 790.03 states that: "The following are hereby defined as unfair methods of competition and unfair and deceptive acts or practices in the business of insurance...(b) Making or disseminating or causing to be made or disseminated before the public in this state, in any newspaper or other publication, or any advertising device, or by public outcry or proclamation, or in any other manner or means whatsoever, any statement containing any assertion, representation or statement with respect to the business of insurance or with respect to any person in the conduct of his or her insurance business, which is untrue, deceptive, or misleading, and which is known, or which by the exercise of reasonable care should be known, to be untrue, deceptive, or misleading."

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California Insurance Code Section 790.10 states: "The commissioner shall, from time to time as conditions warrant, after notice and public hearing, promulgate reasonable rules and regulations, and amendments and additions thereto, as are necessary to administer this article."

The regulation states that it is misleading under Insurance Code Section 790.03 to characterize that an estimate is complete by communicating an estimate that does not include all of the components required to be considered in estimating replacement cost. Section 2695.183 (j): "To communicate an estimate of replacement value not comporting with subdivisions (a) through (e) of this Section 2695.183 to an applicant or insured in connection with an application for or renewal of a homeowners' insurance policy that provides coverage on a replacement cost basis constitutes making a statement with respect to the business of insurance which is misleading and which by the exercise of reasonable care should be known to be misleading, pursuant to Insurance Code section 790.03."

Insurance Code Section 1749.7 states: "The commissioner may, pursuant to Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code, adopt reasonable rules and regulations necessary for the convenient administration of this article." The article contains section 1749.85: "(a) The curriculum committee shall, in 2006, make recommendations to the commissioner to instruct fire and casualty broker-agents and personal lines broker-agents and applicants for fire and casualty broker-agent and personal lines broker-agent licenses in proper methods of estimating the replacement value of structures, and of explaining various levels of coverage under a homeowners' insurance policy. Each provider of courses based upon this curriculum shall submit its course content to the commissioner for approval. (b) A person who is not an insurer underwriter or actuary or other person identified by the insurer, or a licensed fire and casualty broker-agent, personal lines broker-agent, contractor, or architect shall not estimate the replacement value of a structure, or explain various levels of coverage under a homeowners' insurance policy. (c) This section shall not be construed to preclude licensed appraisers, contractors and architects from estimating replacement value of a structure. (d) However, if the Department of Insurance, by adopting a regulation, establishes standards for the calculation of estimates of replacement value of a structure by appraisers, then

on and after the effective date of the regulation a real estate appraiser's estimate of replacement value shall be calculated in accordance with the regulation."

The section anticipates the Department adopting regulations establishing standards for the calculation of estimates of replacement value. Regulation 2695.183 establishes those standards.

There is nothing new about the prohibition of misleading statements made by licensees. The proposed regulations do nothing more than identify one particular variety of misleading statement which licensees know or should know is misleading: to describe as a replacement cost estimate an estimate that fails to consider all of the elements which no one disputes may in fact need to be paid for in the event of a total loss.

The requirements for a replacement cost estimate that are set forth in Section 2995.183 are quite modest: The regulations do not require of replacement cost estimates any particular degree of accuracy; instead, all the regulation does is require that any estimate of replacement cost be complete and must not ignore any of the basic cost components that figure into replacement cost. As mentioned above, during the rulemaking process neither the plaintiffs, nor any other commenter, called into question the fact that each of the elements listed in Subdivision (a) of Section 2695.183 may be required to be paid for in the event of a total loss, because each in fact could be. Thus, to describe as a "replacement cost estimate" an estimate that does not factor in each of these potential cost elements is inherently a misleading statement that is or should to be known to be misleading.

The regulation imposes no substantive requirement to the effect that the estimate must turn out to be accurate. Inaccurate estimates of replacement cost, in and of themselves, are not violations of the regulation unless it turns out that when the licensee estimated replacement cost he failed to consider one or more of the cost elements known to be part of the cost of replacing the structure in question in the event of a total loss.

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IV. THE QUESTIONED REGULATION DOES NOT CONSTITUTE INSURANCE UNDERWRITING AND DOES NOT REQUIRE INSURERS TO PROVIDE ESTIMATES OF REPLACEMENT COST

One basis tendered by plaintiffs for contending that the questioned regulation is invalid is that it purports to regulate the process of insurance underwriting. This contention is without merit. "Underwriting" is a label commonly applied to the process, and fundamental to the concept of insurance and of deciding which risks to insure and which to reject in order to spread losses over risks in an economically feasible way." (*Smith v. State Farm Mutual Automobile Ins. Co.* (2001) 93 Cal.App.4th 700, 726).

The regulation does not specify, require, or otherwise mandate how insurers underwrite homeowner policies or which risks they decide to insure against and therefore does not constitute "underwriting". The regulation does not require licensees to communicate an "estimate of replacement cost" to either consumers or insureds. The regulation simply requires that if licensees communicate an "estimate of replacement cost", it will be complete and include those components and requirements as enumerated in the regulation. Therefore to the extent that the information is communicated, it will not be misleading or deceptive.

Subsection (m) of section 2695.183 of the regulation reads: "No provision of this article shall be construed as requiring a licensee to estimate replacement cost or to set, or recommend a policy limit to an applicant or insured. No provision of this article shall be construed as requiring a licensee to advise the applicant or insured as to the sufficiency of an estimate of replacement cost."

Section 2695.183 (n) states: "No provision of this article shall limit or preclude a licensee from providing and explaining the California Residential Property Insurance Disclosure, as cited in Insurance Code section 10102, explaining the various forms of replacement cost coverage available to an applicant or insured, or explaining how replacement cost basis policies operate to pay claims."

Section 2695.183 (o) states: "No provision of this article shall limit or preclude an applicant or insured from obtaining his or her own estimate of replacement cost from an entity permitted to make such an estimate by Insurance Code section 1749.85."

Section 2695.183 (p) states: "For purposes of this subdivision (p), "minimum amount of insurance" shall mean the lowest amount of insurance that an insurer requires to be purchased in order for the insurer to underwrite the coverage on a particular property, based upon an insurer's eligibility guidelines, underwriting practices and/or actuarial analysis. An insurer may communicate to an applicant or insured that an applicant or insured must purchase a minimum amount of insurance that does not comport with subdivisions (a) through (e) of this Section 2695.183; however, if the minimum amount of insurance that is communicated is based in whole or in part on an estimate of replacement value, the estimate of replacement value shall also be provided to the applicant or insured and shall comply with all applicable provisions of this article. Nothing in this article shall limit or preclude an insurer from agreeing to provide coverage for a policy limit that is greater than or less than an estimate of replacement cost provided pursuant to this article."

Since, according to the language of the regulation itself, licensees (insurance carriers, brokers and agents) are not required to tender information relating to an "estimate of replacement cost," the regulation cannot be said to implicate insurance underwriting.

During the rulemaking process, the plaintiffs, in comments, asserted that the Department cannot adopt regulations that have an impact upon homeowners' insurance underwriting practices. As previously discussed, the regulations do not have an impact on underwriting practices. The regulations do not specify, require, or otherwise mandate how insurers underwrite homeowner policies. Insofar as the comment references Section 2695.183, this section requires that if the licensee states that it has calculated an estimate of "replacement cost," it will include those components listed in the regulation, simply. The plaintiffs' argument that the proposed regulations act to impose "restrictions on estimating replacement costs – a fundamental component of any underwriting decision" ignores Section 2595.183 (m), which explicitly provides that the regulation does not require a licensee to estimate replacement cost. The regulation does not require a licensee to set or recommend a policy limit. The regulation does not require a licensee to advise a consumer or insured as to the sufficiency of an estimate of replacement cost.

In spite of the protestations that the proposed regulations act to impose restrictions on how an insurer underwrites its insurance business, the regulations explicitly do not impose any such limitations or restrictions.

V. THE SUBJECT REGULATION DOES NOT ESTABLISH A NEW CATEGORY OF UNFAIR METHODS OF COMPETITION OR UNFAIR OR DECEPTIVE ACTS OR PRACTICES

Plaintiffs argue that the Commissioner, by enacting regulation 2995.183, is establishing a new category of unfair methods of competition and unfair and deceptive acts and practices in the business of insurance as defined by Insurance Code section 790.03. Plaintiffs also argue that regulatory authority for this does not exist and that rather Insurance Code section 790.06 establishes the method for taking action if the Commissioner believes that a person is engaged in any method of competition or in any act or practice in the conduct of the business that is not covered by Section 790.03.

Plaintiffs' argument fails. By providing a uniform definition for the term "estimate of cost of replacement" the regulation is merely interpretative of the underlying statues; Insurance Code sections 790 and 790.03. It merely provides clarification as to what a false, misleading or deceptive practice consists of. The regulation is not inconsistent with either the purpose or the intent of the underlying statute and is therefore valid. (*Slocum v. State Board of Equalization* (2005) 134 Cal.App.4th 969, 974.) The regulation applies with equal force to all licensees who decide to communicate an "estimate of replacement" cost. In turn, 10 CCR Section 2595.183 specifically provides that when applicable, the failure to use the term "estimate of replacement cost" as defined within the regulation is a violation of section 790.03(b) of the Insurance Code. The regulation, by citing to Insurance Code section 790.03(b), clarifies that failure to comply with the provision of the regulation defining "estimate of replacement cost" is a misleading and deceptive practice unlawful under section 790.03(b) of the Code.

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VI. THE REGULATION DOES NOT VIOLATE PLAINTIFFS' FIRST AMENDMENT RIGHTS UNDER EITHER THE STATE OR FEDERAL CONSTITUTIONS

The business of insurance is clothed with a public interest and is therefore subject to be controlled by the public for the common good. (*20th Century Ins. Co. v. Superior Court* (2001) 90 Cal.App.4th 1247). The Insurance Commissioner has broad discretion in adopting rules and regulations necessary to promote the public welfare. (*State Farm Mutual Ins. Co. v. Garamendi* (2004) 32 Cal.4th 1029).

Courts presume the constitutionality of a legislative act and resolve all doubts in its favor; courts uphold the act unless it clearly and unquestionably conflicts with a provision of the state or federal Constitution. (*Rains v. Belshe* (1995) 32 Cal.App.4th 157, 160.) "[All] presumptions and intendments favor the validity of a statute and mere doubt does not afford sufficient reason for a judicial declaration of invalidity. Statutes must be upheld unless their constitutionality clearly, positively, and unmistakably appears." (*Lockheed Aircraft Corp. v. Superior Court* (1946) 28 Cal.2d 481, 484).

The Supreme Court has recognized that the government may regulate commercial speech in ways that it may not regulate protected noncommercial speech. (*Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc.* (1976) 425 U.S. 738). Government may regulate commercial speech to ensure that it is not false, deceptive, or misleading and to ensure that it is not coercive. (*Ohralik v. Ohio State Bar Assn.* (1978) 436 U.S. 447). The government may also prohibit commercial speech proposing unlawful activities. (*Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations* (1973) 413 U.S. 376, 388).

It is the government's interest in protecting consumers from "commercial harms" that provides "the typical reason why commercial speech can be subject to greater governmental regulation than noncommercial speech." (*Cincinnati v. Discovery Network, Inc.* (1993) 507 U.S. 410, 426.) The government's power to regulate commercial transactions justifies its concomitant power to regulate commercial speech that is "linked inextricably "to those transactions. (*Friedman v. Rogers* (1979) 440 U.S. 1, 10, n. 9.)

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State regulation of the insurance business has been upheld against constitutional challenges in a wide variety of circumstances. The police power of the state legitimately extends to the activity of regulating the practices of the insurance industry. (*California State Auto Association Inter-Insurance Bureau v. Maloney*, (1951) 341 U.S. 105, 109 n. 2, 110). Legislation will be upheld if it bears a rational relationship to a legitimate state interest. (*Williamson v. Lee Optical Co.*, (1955) 348 U.S. 483, 488). A state does not lose its power to regulate commercial activity harmful to the public merely because speech is a component of that activity. (*Ohralik v. Ohio State Bar Association* (1978) 436 U.S. 447, 456-457).

The standard to be applied in determining whether a regulation violates the First Amendment depends upon whether the expression allegedly being suppressed is "commercial speech" and therefore accorded a lesser protection. (*Central Hudson Gas Co. v. Public Service Common of New York* (1980) 447 U.S. 557, 562-563). With respect to commercial speech the speech can be constitutionally regulated if the government has a substantial interest in regulating the speech; the regulation advances a governmental interest; and the regulation is not more extensive then necessary to serve the interest. (*Board of Trustees v. Fox* (1989) 492 U.S. 469, 480).

The Commissioner has met all requirements articulated in the *Central Hudson* and *Board of Trustees* cases. He is acting in the public interest by promulgating the questioned regulation to insure that consumers and insureds make informed decisions with respect to coverage based upon being supplied with "adequate information." In this case the "adequate information" is a uniform definition of what is contained in an "estimate of replacement cost."

The State has a substantial interest in policing a regulated industry – insurance - to make sure that no false, misleading, or deceptive practices take place in determining the scope of coverage and what is being insured. All insurance carriers providing information relating to "estimate of replace cost" are acting on a level playing field by requiring that certain items be included within that term. The regulation is reasonable because it specifically does not require that any insurance carrier provide an "estimate of replacement cost." The regulation merely provides a uniform definition for the term "estimate of replacement cost" when such an estimate

is provided.

Plaintiffs consider the requirement that they supply "adequate information" to insureds and consumers as a First Amendment impediment. Plaintiffs believe that it is the industry itself which should define "estimate of replacement cost" and decide what information consumers and insureds should receive with respect to what is included in the definition of a communicated "estimate of replacement cost." It is, however, within the power of the Commissioner of a regulated industry to determine the adequacy of the information provided to consumers and insureds and to make sure that such compliance is within the scope of Insurance Code section 790 thereby avoiding deceptive practices.

Plaintiffs' motion argues that the regulation bans all communications not in accordance with section 2695.183 and that a ban on communications, save one, is impermissible if disclaimers accompanying the communication can prevent them from being misleading. The plaintiffs then go on to suggest potential disclaimers. This argument is fallacious. There is nothing in the regulation that prevents licensees from communicating any information they wish to consumers and insureds. Rather, the regulation simply defines a term: "estimate of replacement cost". If a licensee communicates an "estimate of replacement cost," the regulation requires that the estimate include the elements which no one disputes may in fact need to be paid for in the event of a total loss. When the regulation is stripped to its core, it defines a term, a term that benefits all sides of the insurance transaction, for all concerned know what it means when one refers to an "estimate of replacement cost."

The "disclaimers" plaintiffs suggest are the following: "this is an estimate, your actual cost for replacement may be more or less depending on future circumstances," or "you're responsible for choosing the coverage amount, this estimate is provided solely as a tool for use to select a coverage amount, you may wish to consult other sources or consider other information." (PPA p. 6 and 11)

The text of the regulation strategically ignored in Plaintiffs' Motion, provides the information that Plaintiffs suggest in their proposed disclaimers. This is the theme of the Plaintiffs' argument, to overstate and misrepresent what the regulation actually says. The

regulation, quoted elsewhere in this Opposition in responding to Plaintiffs' overreaching arguments, establishes that the regulation is, in fact, narrowly drawn.

Subsection (m) of section 2695.183 states that there is no requirement that a licensee estimate replacement cost or set, or recommend a policy limit and further that the licensee is not required to advise as to the sufficiency of an estimate of replacement cost.

Subsection (n) provides that nothing precludes a licensee from providing and explaining various forms of replacement cost coverage or explaining how replacement cost basis polices operate to pay claims.

Subsection (o) provides that the regulation does not preclude an applicant or insured from obtaining his or her own estimate of replacement cost pursuant to Insurance Code section 1749.85.

Subsection (p) states that an insurer may communicate to an applicant or insured that an applicant or insured must purchase a minimum amount of insurance. Further, that nothing in the regulation limits or precludes an insurer from agreeing to provide coverage for a policy limit that is greater than or less than an estimate of replacement cost.

The plaintiffs are well aware that the regulation does not require that the replacement cost estimates be accurate, or that they be generated or communicated at all. Simply, the regulation requires that the communication of what is represented to be an estimate of replacement cost be complete and must not ignore any of the basic cost components that figure into replacement cost. It bears repeating that during the rulemaking process the plaintiffs never called into question the fact that each of the elements listed in Subdivision (a) of Section 2695.183 may be required to be paid for in the event of a total loss, because each in fact could be.

The plaintiffs' citation to *Pearson v. Shalala*, 164 F. 3d 650 (D.C. Circuit 1999) is not helpful to their arguments and it is not authoritative. The court, in remanding the case, required that the FDA explain what it meant by "significant scientific agreement." The questioned regulation does just this in the context of an "estimate of replacement cost," it defines what that term means and it refers to applicable statutes.

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The requirement that a uniform definition be provided for the term "estimate of replacement cost" does not provide either a factual or legal basis for legitimately contending that the free speech rights of the regulated insurance industry have been violated. Plaintiffs' contentions with respect to this issue must fail.

When communications occur between licensees and consumers, there can be no confusion over what is meant by an "estimate of replacement cost." This requirement provides for a full and open discussion, not an interference with commercial free speech. Requiring licensees to identify something as an estimate of replacement cost only when it, is in fact, an estimate of replacement cost, cannot be deemed an interference with commercial free speech. It creates a better environment for commercial free speech, one where both licensees and consumers understand the concepts and the context of the discussion.

CONCLUSION

For the reasons stated herein, plaintiffs' motion for judgment on the pleadings must be denied. The motion is factually and legally deficient. This court, on its own motion, is requested to grant judgment on the pleadings in favor of the Commissioner because all of plaintiffs' arguments have now been rejected.

Dated: December 12, 2011

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DECLARATION OF PERSONAL SERVICE

Case Name: **ASSOCIATION OF CALIFORNIA INSURANCE COMPANIES and PERSONAL INSURANCE FEDERATION OF CALIFORNIA v. DAVE JONES in his capacity as Commissioner of the California Department of Insurance**

Case No.: **BC463124**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar, at which member's direction this service is made. I am 18 years of age or older and not a party to this matter; my business address is: 300 South Spring Street, Suite 1702, Los Angeles, CA 90013.

On December 12, 2011, I caused a true and correct copy of the following document described as:

CALIFORNIA DEPARTMENT OF INSURANCE'S OPPOSITION TO PLAINTIFFS' MOTION FOR JUDGMENT ON THE PLEADINGS

to be personally delivered to:

Gene Livingston, Esq.
Greenberg Traurig, LLP
1201 "K" Street, Suite 1100
Sacramento, California 95814-3938

I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on December 12, 2011, at Los Angeles, California.

ROSITA EDUARDO
Declarant


Signature

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