No. GV2-02501

THE STATE OF TEXAS AND THE TEXAS COMMISSIONER OF INSURANCE, *Plaintiffs*, V. FARMERS GROUP, INC., FARMERS UNDERWRITERS ASSOCIATION, FIRE UNDERWRITERS ASSOCIATION, FARMERS INSURANCE EXCHANGE, AND FIRE INSURANCE EXCHANGE, *Defendants*.	§ § § § § § § § § § § § § § §	IN THE DISTRICT COURT OF TRAVIS COUNTY, TEXAS 353RD JUDICIAL DISTRICT

GILBERTO VILLANUEVA AND MICHAEL PALADINO'S ORIGINAL PLEA IN INTERVENTION AND OBJECTIONS TO PROPOSED SETTLEMENT

TO THE HONORABLE JUDGE OF THIS COURT:

Gilberto Villanueva and Michael Paladino, individually and on behalf of all others similarly situated, file this Original Plea in Intervention. In support thereof, Gilberto Villanueva and Michael Paladino respectfully show as follows:

PARTIES

Intervenor Gilberto Villanueva is an individual residing Dimmit County, Texas.

Intervenor Michael Paladino is an individual residing in Kerr County, Texas.

Plaintiffs the State of Texas and the Texas Department of Insurance ("TDI") have appeared in this action. A copy of this plea will be forwarded to their attorney of record, David C. Mattax, Chief, Financial Litigation Division of the Office of the Attorney General of Texas, P.O. Box 12548, Austin, Texas 78711-2548, by facsimile and certified mail, return receipt requested.

Defendants Farmers Group, Inc., Farmers Underwriters Association, Fire Underwriters Association, Farmers Insurance Exchange, and Fire Insurance Exchange have appeared in this action. A copy of this plea will be forwarded to their attorneys of record, M. Scott Incerto, Fulbright & Jaworski, L.L.P., 600 Congress Ave., Suite 2400, Austin, TX 78701 and Layne Kruse, Fulbright & Jaworski, L.L.P., 1301 McKinney, Suite 5100, Houston, Texas 77010-3096, by facsimile and certified mail, return receipt requested.

ORIGINAL PLEA IN INTERVENTION

A. Intervenors filed suits Against the Farmers Companies.

On or about May 8, 2000, Intervenor Villanueva, for himself and others similarly situated, initiated an action against Texas Farmers Insurance Company, Mid-Century Insurance Company of Texas, and Farmers Texas County Mutual Insurance Company in Cause No. GN0-01347 in the 53rd Judicial District Court of Travis County, Texas. In that action, Intervenor Villanueva asserted claims for damages arising out of, *inter alia*, the defendants' violations of the Texas Insurance Code in the placement of automobile insurance in the State of Texas.

On or about January 23, 2002, Intervenor Paladino, for himself and others similarly situated, initiated an action against Mid-Century Insurance Company of Texas, Texas Farmers Insurance Company, and Farmers Texas County Mutual Insurance Company in Cause No. GN2-00207 in the 250th Judicial District Court of Travis County, Texas. On that same day, Intervenor Paladino, for himself and others similarly situated, also initiated an action against Farmers Insurance Exchange and Fire Insurance Exchange in Cause No. GN2-00208 in the 261st Judicial District Court of Travis County, Texas. In those actions, Intervenor Paladino asserted claims for damages and injunctive

relief arising out of the defendants' violations of the Texas Insurance Code in the placement of automobile and homeowners insurance in the State of Texas.

B. The State of Texas and the Texas Department of Insurance Initiate Proceedings Against the Farmers Companies

On or about August 5, 2002, the Office of the Attorney General, on behalf of the State of Texas and the TDI, initated an action against Farmers Group, Inc., Farmers Underwriters Association, Fire Underwriters Association, Farmers Insurance Exchange, and Fire Insurance Exchange, in Cause No. GV2-02501 in the 261st Judicial District Court of Travis County, Texas (the "AG Action"). In the AG Action, the State of Texas and the TDI asserted claims against the defendants for damages and injunctive relief arising out of the defendants' violations of the Texas Insurance Code in the placement of homeowners insurance in the State of Texas.

On or about August 13, 2002, the TDI presented the Commissioner of Insurance with a verified application for an *ex parte* Emergency Cease and Desist Order against Farmers Insurance Exchange and Fire Insurance Exchange. In that application, the TDI alleged that Farmers Insurance Exchange and Fire Insurance Exchange "are or have been engaging in unfair methods of competition or unfair or deceptive acts or practices in the business of insurance in Texas by overcharging Texas policyholders" in violation of the Texas Insurance Code.

On that same day, Montemayor issued Cease and Desist Order No. 02-0844 against Farmers Insurance Exchange and Fire Insurance Exchange (the "Cease and Desist Order"). In the Cease and Desist Order, Montemayor made numerous findings of fact, including but not limited to the following:

> Farmers Insurance Exchange and Fire Insurance Exchange' are . . . engaging in unfair methods of competition or unfair or deceptive acts or practices in the business of insurance in violation of TEX. INS. CODE ANN. art. 21.21 §§ 3 and 5 and 28 TEX. ADMIN. CODE §§ 21.1-21.5. Such conduct by Farmers Insurance Exchange and Fire Insurance Exchange is unfair, creates an immediate danger to public safety, and is causing or can be reasonably expected to cause public injury that is likely to occur at any moment, is incapable of being repaired or rectified, and has or is likely to have influence or effect.
>
> Fire Insurance Exchange is using unfair rates which unfairly cause its Texas HO-A policyholders to overpay by more than 50 percent in violation of TEX. INS. CODE ANN. art. 2121 § 3 and 28 TEX. ADMIN. CODE §§ 21.1-21.5. This includes condominium owners and tenants.
>
> Farmers Insurance Exchange is using unfair rates which unfairly cause its Texas HO-A policyholders to overpay by more than 17 percent in violation of TEX. INS. CODE ANN. art.21.21 § 3 and 28 TEX. ADMIN. CODE §§ 21.1-21.5.
>
> Farmers' own data shows that Farmers is overcharging thousands of Texas HO-A policyholders, including house owners, condominium owners and renters. Complaints received by TDI demonstrate the anguish and distress experienced by Texas HO-A policyholders as a result of Farmers unfair Texas HO-A rates.
>
> Unless [Farmers Insurance Exchange and Fire Insurance Exchange] are immediately ordered to cease and desist, [they] will continue to engage in unfair methods of competition or unfair acts or practices in the business of insurance in Texas by overcharging Texas HO-A policyholders.

On or about August 30, 2002, Farmers Insurance Exchange and Fire Insurance Exchange brought the present action against Montemayor and TDI appealing from Order No. 02-0844 and also seeking a declaratory judgment.

On or about September 24, 2002, Farmers Insurance Exchange and Fire Insurance Exchange gave notice to their Texas homeowners insureds that they would not be offering coverage or

renewing homeowners insurance policies. Farmers Insurance Exchange and Fire Insurance Exchange timed the effective date of such non-renewal action to begin November 11, 2002.

C. The State of Texas and the Texas Department of Insurance Reach a Settlement in Principle with the Farmers Companies Which is Inadequate and Unfair to Texas Policyholders

On November 13, 2002, the TDI agreed to extend the effective date of the Cease and Desist Order for thirty days through December 10, 2002, purportedly to allow an opportunity to negotiate a settlement. In return, Farmers Insurance Exchange and Fire Insurance Exchange purportedly agreed to continue offering coverage and renewing homeowners insurance policies until December 10, 2002 with a base rate reduction of 6.8% from the rate structure used in the period immediately prior to November 2002.

On November 30, 2002, the State of Texas, Montemayor, and the Farmers Companies reached a settlement in principal. As announced to the public, that settlement involved the following terms:

Prospective Consumer Relief: effective 01/01/03	VALUE▪
Rate reduction of 6.8% effective until 09/01/03. ▪ **Adjusted discounts for Credit Scoring/Age of Home**; move to indicated discounts and freeze upper discount range at 47% for credit score and 40% for age of home. ▪ Territory relativities adjusted with TDI approval ▪ Credit Scoring disclosures acceptable to AG (homeowner and auto)	$35,000,000
Consumer Restitution:	▪
Refund or premium credit for overcharges due to unfunded CAT load and management fee for policies written 12/28/01 through 11/10/02; payable at end of policy period by premium credit on renewal statement, premium refund due within 45 days if policyholder does not renew with Farmers	$35,000,000▪
Refund or premium credit for overcharges due to improper Credit Scoring/Age of Home discounts and territory relativities for policies written beginning 12/28/01; payable at end of policy period by premium	$25,000,000*▪

credit on renewal statement, premium refund due within 45 days if policyholder does not renew with Farmers	
Refunds for incorrect credit scores and payment of credit reports, for homeowner and auto customers whose credit scores were incorrect due to errors on credit reports, which they were unable to correct due to inadequate notice by Farmers; funds to be transferred to an escrow account for stated purpose, to be supplemented by Farmers if necessary. Also includes reimbursement for state's investigative and attorneys' fees.	$5,000,000+
TOTAL:	$100,000,000+

*If necessary refunds are less than stipulated amount, balance is payable to the state's General Revenue Fund.

In light of the acts committed by the Farmers Companies (as evidenced by the findings of the TDI in the Cease and Desist Order) and the hundreds of millions of dollars in damages the Farmers Companies have caused Texas policyholders, the proposed settlement is inadequate and unfair to Texas policyholders, including Intervenors Villanueva and Paladino. However, through a Memorandum of Understanding ("MOU") setting forth the terms of the proposed settlement, the State of Texas, Montemayor and the Farmers Companies attempt to prevent <u>anyone</u> (including persons such as Intervenors Villanueva and Paladino who are currently pursuing claims against the Farmers Companies as well as consumers who do not currently have counsel and are not parties to ongoing lawsuits) from seeking the full amount of damage and penalties owed by the Farmers Companies.

For example, the MOU provides that the parties will effectuate a "global settlement" through a "broad form release" which "shall include a release of all existing, <u>known and unknown claims</u>, demands and causes of action against the [Farmers companies], <u>whether pending or threatened, suspected or unsuspected</u>, contingent or non-contingent, for all existing, <u>known and unknown</u>

damages and remedies that arise out of or relate to the acts and/or occurrences" alleged by the State of Texas and/or Montemayor in the AG Lawsuit, the Cease and Desist Order, and certain other proceedings.

The MOU also provides that the intent of the settlement is:

> to the full extent permitted by law to fully resolve all claims against the Farmers Parties and their affiliates in the homeowners markets in Texas that could be brought by the State of Texas, the OAG, or the TDI, Montemayor, either individually or on behalf of policyholders, including such claims under the Texas Insurance Code, the Texas Deceptive Trade Practices Act, Fair Credit Reporting Act, common law and the antitrust laws, that arise out of or relate to the issues raised in or that could have been raised in the AG Lawsuit, the Cease and Desist Order, and [other] Proceedings, including but not limited to issues concerning or related to the management fee, the placement of policyholders in a particular insuring entity, the use of Farmers Auto Risk Assessment, age of home discount, the Unfunded Catastrophe load, the decision to no longer offer HO-B policies (including HO-Protector Plus, HO-CON-B, HO380 endorsement, TDP-2, TDP-3, DF-Builder's Risk (collectively referred to herein as HO-B)), the offering of HO-A policies in place of HO-B policies, territorial discounts, credit scoring, the use of the Farmers Property Risk Assessment, or the rates that the Farmers Parties or their affiliates have charged for homeowners policies and endorsements and all notices and statements that the Farmers Parties or their affiliates have made or issued in connection with the above, including but not limited to the notices of nonrenewal of the HO-B polices and notices issued pursuant to the Fair Credit Reporting Act as to home and auto insurance.

The MOU further provides that the settlement "contemplates (in addition to the resolution of claims brought to date by the [Office of the Attorney General], TDI, and Montemayor) the resolution of all claims that have been made or could have been made by the Exchanges' individual policyholders in the State of Texas arising out of or relating to issues raised" in the AG Lawsuit, the Cease and Desist Order, or certain other proceedings.

The procedure by which the State of Texas, Montemayor, and the Farmers companies intend to prevent Texas policyholders, including Intervenors Villanueva and Paladino, from seeking the full amount of damage and penalties owed by the Farmers companies is through the creation of a

Settlement Class. Specifically, the MOU contemplates the creation of a Settlement Class consisting of "all policyholders who have claims, demands, or causes of action arising out of or relating to issues that were or could have been brought" in the AG Lawsuit, the Cease and Desist Order, and certain other proceedings and the participation of all such policyholders in a limited Settlement Fund.

The proposed settlement is inadequate and inequitable to Texas policyholders. The inadequacies and inequities include, but are not limited to:

a. The requirement that the Farmers companies (at best) compensate policyholders for less than half of the amount they were overcharged in violation of Texas law.

b. The attempted abolition of claims against the Farmers companies by certain damaged policyholders with no compensation whatsoever;

c. The waiver of any and all penalties for the Farmers companies' unfair and deceptive conduct in violation of Texas law;

d. The failure to immediately compensate damaged policyholders with no requirement that the Farmers companies pay interest.

e. The inadequate prospective rate reduction; and

f. The placement of improper and illegal restrictions on the ability of the Texas Commissioner of Insurance to establish benchmark rates, including the automobile benchmark rate.

D. Intervenors Seek to Protect Their Interests and Those of Others Similarly Situated

For the reasons set forth above, Intervenors Villanueva and Paladino file this Plea in Intervention to protect their rights and remedies and those of others similarly situated. As alleged in the petitions filed by Intervenors in the lawsuits described above, Intervenors are entitled to damages and injunctive relief arising out of the Farmers companies' violations of the Texas Insurance Code. Intervenors have a justiciable interest in the matters at issue in this case because

the settlement proposed in the MOU (1) directly impacts and determines their rights and remedies relating to homeowners policies purchased from the Farmers Companies, (2) directly affects the manner in which the Commissioner of Insurance can set the automobile benchmark rate in the future, and (3) directly affects the permissible amount the Farmers companies may charge for automobile coverage in the future.

OBJECTIONS TO PROPOSED SETTLEMENT

Intervenors, on behalf of themselves and all other similarly situated, submit the following list of objections to the proposed settlement. This list is not a comprehensive list of all objections, nor is it a complete recitation of all facts supporting each objection. Intervenors reserve the right to supplement this list with further objections, and to expand, both orally and in writing, on the objections stated herein. The objections are as follows:

A. The proposed settlement is inadequate and inequitable to Texas policyholders. The inadequacies and inequities include, but are not limited to:

i) The requirement that the Farmers companies (at best) compensate policyholders for less than half of the amount they were overcharged in violation of Texas law.

ii) The attempted abolition of claims against the Farmers companies by certain damaged policyholders with no compensation whatsoever;

iii) The waiver of any and all penalties for the Farmers companies' unfair and deceptive conduct in violation of Texas law;

iv) The failure to immediately compensate damaged policyholders with no requirement that the Farmers companies pay interest.

v) The inadequate prospective rate reduction; and

vi) The placement of improper and illegal restrictions on the ability of the Texas Commissioner of Insurance to establish benchmark rates, including the automobile benchmark rate.

B. The settlement is not fair because the case has not been certified as a class action, and cannot be appropriately maintained as a class action. The fairness of any proposed settlement is necessarily dependent upon a threshold finding that the matter is appropriately maintained as a class action. *Northrup v. Southwestern Bell Telephone Co.*, 72 S.W.3d 1, 12 (Tex. App.--Corpus Christi 2001, no pet.). Without a proper ruling on the question of certification, no settlement can be fair. *Id.*; *Southwestern Refining Co., Inc. v. Bernal*, 22 S.W.3d 425, 439 (Tex.2000).

C. Assuming this is intended to be viewed as a "settlement class" the class and the settlement are both objectionable because of insufficient notice. Both the U.S. Supreme Court and the Texas Supreme Court have expressly cautioned against allowing the settlement class device to collapse the protections for unnamed class members incorporated into the rules. *See Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617, 117 S.Ct. 2231, 138 L.Ed.2d 689 (1997); *Bloyed v. General Motors Corp.*, 881 S.W.2d 422, 429 (Tex. 1994). In non-settlement class cases, the class is certified prior to settlement, and the class representatives are required by the rules to send out notice to the class. TEX. R. CIV. P. 42(c)(2). The class members are thereby put on notice that a class action is pending, and have a clear opportunity to challenge the adequacy of the named representative by appealing the class certification or by filing an intervention. See TEX. REV. CIV. PRAC. & REM. CODE ANN. §§ 51.014(a) (interlocutory appeal of class certification); TEX. R. CIV. P. 60 (any party may intervene, subject to a motion to strike). Later, if a settlement is reached, notice of the settlement given to the class members would, ostensibly, be the second notice advising class members that their substantive rights are likely to be affected by the pending class action. This approach, obviously, better protects the interests of the unnamed class members than the settlement class approach. *Northrup*, 72 S.W.3d at 13. Here none of the members of the potential class are protected at all, and therefore this settlement class is objectionable, there has been no adequate notice of the class certification, settlement, terms of settlement, or of the hearing on the settlement.

D. This settlement does not pass the smell test. The State of Texas, as the ostensible representative of the class members cannot and has not adequately

protected the interests of the potential class members. The timelines and events occurring throughout the history of this lawsuit raise an inference that the parties and their counsel may have colluded with each other in reaching this settlement. This appears to be a settlement borne out of a desire on the one hand to use the homeowners insurance issue to benefit the political campaigns of certain candidates, while at the same time protect the insurance industry from being forced to pay the multi millions of dollars that it is obligated to repay its customers, the class members. Where there is evidence of fraud, collusion, or gross unfairness in the settlement, the court should substitute its judgment for that of the parties and their counsel, and refuse to approve such a settlement. *See, e.g., Bloyed v. General Motors Corp.*, 881 S.W.2d 422, 429 (Tex. 1994). The Court should permit the parties additional time to conduct discovery to determine what has occurred to result in this settlement being reached. If this Court is unwilling to permit the Intervenors time and leave to conduct discovery to obtain evidence of fraud or collusion, under this heightened *Bloyed* standard which this Court should apply to this settlement class proposed here, the settlement class must not be approved.

E. The settlement is unfair because there was insufficient notice for the hearing on this settlement. In fact, there has never been any notice to interested parties regarding this hearing. The lack of notice is inadequate to protect the class, and violates due process of all class members. There has not been adequate time for the class members to be notified of the existence of the proposed settlement, consult with counsel or otherwise attempt to understand the meaning and consequences of the settlement, and to determine whether or not to intervene and object. Moreover, there has not been adequate time for intervening and objecting parties to accumulate the evidence that can best prove how inadequate, improper and unfair this proposed settlement is.

F. As indicated in the Memorandum of Understanding, the parties to this suit purport to use this inadequate, unjust and facially defective settlement class proceeding to defeat the rights of thousands of Texans to pursue many claims against the Defendants herein that are not even subject of this lawsuit. The settlement would eradicate essentially any possible or potential claim that could arise out of a consumer engaging in business with the Defendants, and as such, this settlement is far too broad. It seeks to disenfranchise and defeat the claims of thousands, without clearly saying so, and providing only a pittance as remuneration compared to the damages suffered by the class members.

G. The settlement class is also objectionable because there are far too many different varieties of class members lumped together in one class-including homeowners insurance and auto insurance, but not identifying specifically

which claims for each are covered, how the damages can or will be apportioned to each type of claimant, and providing settlement damages that are exceedingly small, and wholly inadequate to rectify the damages and injuries suffered by the consumers harmed by the Defendants.

H. The settlement is objectionable because it is unfair, unreasonable and inadequate under the circumstances because the measure and determination of the amount of an award is inadequate.

I. The settlement is objectionable because it is unfair, unreasonable and inadequate under the circumstances because the value of the award of damages is insignificant.

J. The settlement is unfair unreasonable and inadequate because it appears to be the product of collusion.

K. The settlement is unfair unreasonable and inadequate because the notice given was improper, inadequate and violated due process. No attempt was made to give notice to the individual proposed class members, and the notice period provided in general was itself extremely limited, providing almost no time at all for intervention and objection. A notice that does not meet the requirements of Texas Rule of Civil Procedure 42 violates due process and fails to provide a meaningful right to be heard.

L. The settlement is unfair unreasonable and inadequate because the release is ambiguous and overbroad.

M. The settlement is unfair unreasonable and inadequate because the proposed "blow" provision is contrary to law and inadequate as it is not truly a "blow" provision, but allows the class settlement to stay intact regardless of how many opt-outs there are-whether two percent or 100 percent.

N. The settlement, despite its overreaching nature, is proposed as an "opt-out" class versus an "opt-in" class. The opt-in class would better protect the consumers in the State of Texas. The State has an obligation to protect the consumers from unwittingly having their rights taken away. If the State will not stand for the consumer, the Court must. The best way to protect the consumer is an opt-in class. This gives the consumer the ultimate power to decide if the consumer likes the way the State has handled the matter.

O. The settlement proposes a global release of all claims, known and unknown. The amount of money to be paid is inadequate to support a global release. In class actions, the Court should review the amount paid to see if it could even

support the release. The Farmers parties should not get a global release of claims known and unknown for such little compensation. The Court should only approve a specific, delineated release that only requires a release of those issues for which compensation is actually paid.

P. The settlement contains a release for any auto policyholders. The auto defendants in the *Villanueva* action were not even defendants in the either lawsuit involving the State. The State never looked at or investigated the auto issues. Regardless, the Farmers entities included the auto insurers in the settlement by including the *Villanueva* auto defendants (Mid-Century Insurance Company, Mid-Century Insurance Company of Texas, Texas Farmers Insurance Company, and Farmers Texas County Mutual Insurance Company) as "Affiliates" in Para. 1, Global Settlement, of the MOU. While never addressing auto claims directly, the acts complained of in *Villanueva* are slipped into the laundry list of released items (management fee, placement of policy holders in a particular insuring entity, the use of Farmers Auto Risk Assessment, credit scoring, notices issued pursuant to the Fair Credit Reporting Act as to home and auto insurance) in Para. 3(iii) of the MOU. Finally, despite never directly addressing or investigating it, the entire MOU contemplates a full release of all auto policyholders claims in exchange for payment only under Para. 5(d) (FCRA Adjustment Fund), with a total pool of $3,000,000 allocated. When Intervenors reviewed the numbers, violations in for auto policyholders alone (without $25,000 penalty) could exceed $50,000,000. In exchange for a total release of all claims, Farmers agrees to a total of $3,000,000, but only to be paid for FCRA violations. This is too little compensation to support a global release. Auto policyholder issues should not be anywhere addressed in the MOU because the State never dealt with it.

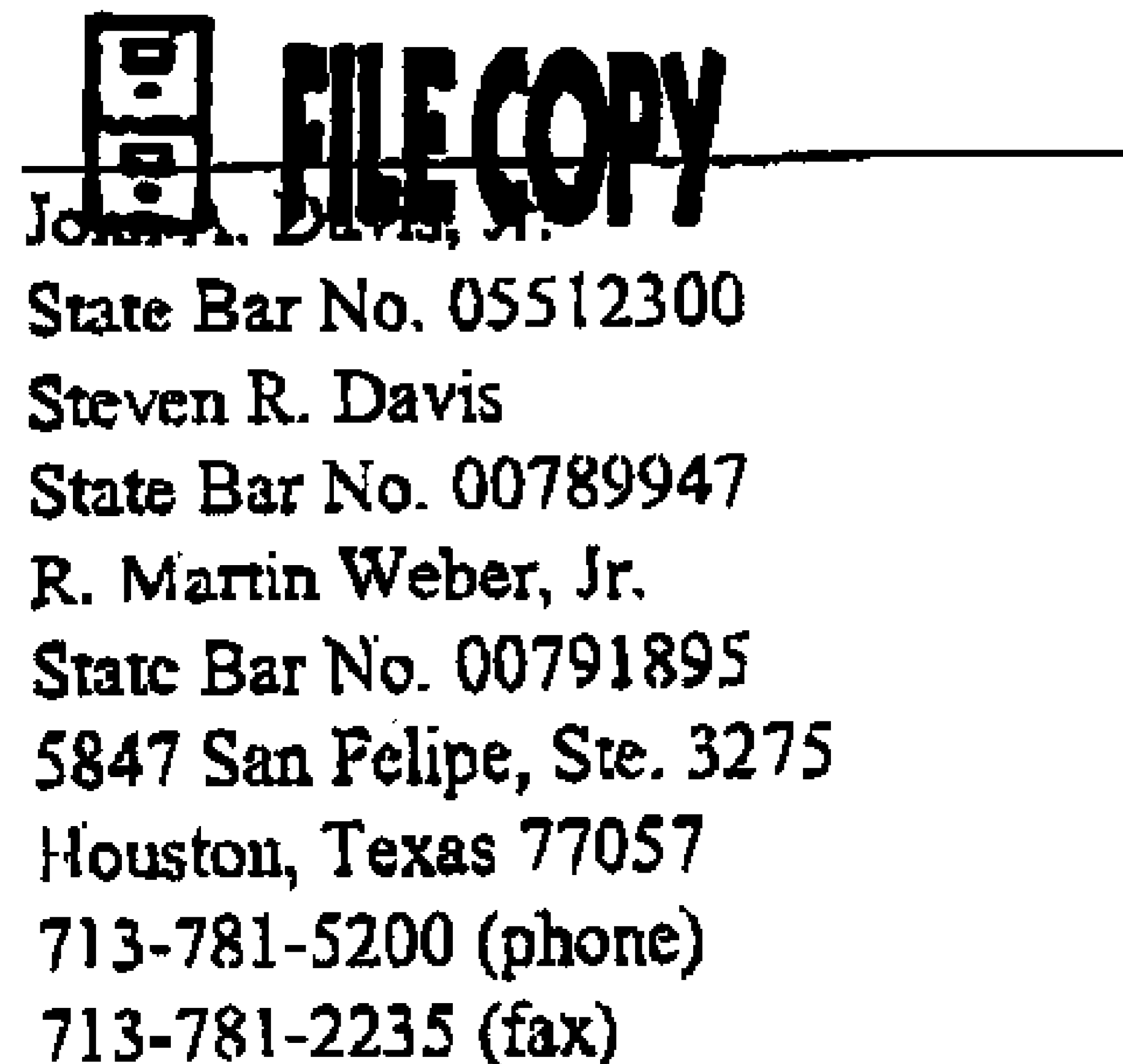
Q. The settlement should not require the State to change its administrative practices on how the State views and calculates management fees, and how much of a reduction in rates it will require. Such a settlement permits the Farmers Companies to achieve an insurance coup which benefits all insurers to the detriment of consumers. By violating the laws of the State of Texas, the Farmers Companies were able to extract concessions from the State which would not otherwise be obtained. Rewarding wrongdoers is contrary to public policy and cannot be tolerated, particularly given the consumer issues involved.

WHEREFORE, Intervenors Gilberto Villanueva and Michael Paladino pray that they be given the opportunity to appear in this action; to assert claims and causes of action for damages and

injunctive relief arising out of the Farmers companies' violations of the Texas Insurance Code; to oppose any certification of a Settlement Class as proposed in the MOU and assert objections thereto; to oppose the entry of the Judgment proposed in the MOU; and to seek all other relief both at law and in equity to which they, on behalf of themselves and all others similarly situated, are entitled.

Respectfully submitted,

DAVIS & DAVIS

By: 

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CERTIFICATE OF SERVICE

I hereby certify that on this 11th day of December, 2002, a true and correct copy of the foregoing document has been served upon the parties below by facsimile and certified mail/RRR:

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