S232322

IN THE
SUPREME COURT
OF THE STATE OF CALIFORNIA

SAMUEL HECKART,
Plaintiff & Appellant,

vs.

A-1 SELF STORAGE, *INC. et al.*
Defendants & Respondents.

AFTER A DECISION BY COURT OF APPEAL, FOURTH APPELLATE DISTRICT, DIV. ONE, APPEAL NO. D066831, APPEAL FROM JUDGMENT OF THE SAN DIEGO COUNTY SUPERIOR COURT; CASE NO. 37-2013-00042315 CU-BT-CTL, HON. JOHN S. MEYER
SERVICE ON ATTORNEY GENERAL & SAN DIEGO DISTRICT ATTORNEY REQUIRED BY BUS. & PROF. CODE § 17209

RESPONDENT DEANS & HOMER'S ANSWER TO THE AMICUS CURIAE BRIEF OF INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA

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INTRODUCTION

On what is now understood to be *four* separate occasions, Deans & Homer presented its program for providing coverage to self-storage facilities to the Department of Insurance ("DOI") and sought approval related to the program. In two instances, Deans & Homer sought specific approval, to make sure it was in compliance with its legal obligations and that its program, including the Lease Agreement A-1 ultimately entered into with Heckart – would not be considered insurance. (2 CT 320-24; 331, ¶ 5.) The initial approval was obtained in advance of Deans & Homer implementing the program.

In two other instances, Deans & Homer sought the required approval from the DOI for the Storage Liability Policy it offered to self-storage operators such as A-1. (*See* Declaration of Scott Lancaster filed concurrently herewith ("Lancaster Decl."), ¶¶ Cal. Ins. Code § 1861.05.) In each instance, the DOI approved the program.

In a remarkable reversal, the DOI in its amicus brief now seeks to disown its prior opinions and approvals, and asserts for the first time that the Lease Agreement utilized by A-1 is insurance. The DOI's new, remarkably inconsistent and vacillating stance is not entitled to any deference and should not be considered. It would be remarkably unfair to Deans & Homer (as well as to A-1), and it would be a violation of due process, if the DOI was permitted to radically alter its interpretation of the law fourteen years after it approved Deans & Homer's program.

In addition, the DOI's new stance should be rejected on its merits. The DOI essentially (with a few exceptions) adopts Heckart's arguments. Those arguments were properly rejected by the trial court and the Court of

Appeal, as they are inconsistent with the past seventy years of precedent under the principal object test.

LEGAL DISCUSSION

I. The DOI's Current Vacillating Stance Is Not Entitled To Deference And Should Be Given No Weight

The DOI's argument in its amicus brief contradicts the position the DOI has consistently taken since 2003. As such, the DOI's new position is not entitled to deference, and should be rejected.[1]

A. Consistent, Long-standing Agency Interpretations Are Entitled To Deference, Whereas Vacillating Interpretations Are Entitled To None

The deference to be accorded to an agency's viewpoint is "fundamentally *situational*." (*Yamaha Corp. v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 12 (emphasis in original).) Judicial deference to an agency's position "turns on a legally informed, commonsense assessment of [the position's] contextual merit." (*Id.* at 14.) An agency's interpretation of a statute is entitled to more deference if the interpretation was contemporaneous with the statute's enactment. (*See id.* at 13.) Further, the agency's interpretation may be entitled to deference if the agency has "consistently" maintained that interpretation, and particularly if the agency has stuck with that interpretation for a lengthy period of time. *(Id.)*

One reason for giving deference to a consistent and long-standing agency interpretation is the fact that over time, members of the public rely on the agency's view. It would be unfair and disruptive to those who have

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[1] Deans & Homer also joins in, and incorporates by reference, the arguments made by A-1 in its separate answer to the DOI's amicus brief.

relied on an agency's long-standing position if that stance suddenly is invalidated. (*See Ste. Marie v. Riverside County Reg'l Park and Open-Space Dist.* (2009) 46 Cal.4th 282, 293 ("When an administrative interpretation is of long standing and has remained uniform, it is likely that numerous transactions have been entered into in reliance thereon, and it could be invalidated only at the cost of major readjustments and extensive litigation") (quoting *Whitcomb Hotel, Inc. v. California Employment Comm'n* (1944) 24 Cal.2d 753, 757).)

On the other hand, this Court has held that a "*vacillating position . . . is entitled to no deference.*" (*Id.* (emphasis added).) A common-sense reason for not deferring to a vacillating agency interpretation is the fact that such vacillation calls into question whether the agency's new view, rather than its prior position, is the correct one.

B. The DOI's History Of Approvals Related To Deans & Homer's Program

1. Summary of the Two Separate Contracts Relevant to the Case

There are two separate transactions relevant to this case. The first is the Lease Agreement between A-1 and Heckart. Through the Lease Agreement, A-1 leased storage space to Heckart, and A-1 also agreed to retain liability for certain risks that could cause damage to Heckart's property stored at A-1's facility. (1 CT 49-53.) A-1's Lease Agreement, and particularly the Lease Addendum (or "Protection Plan") portion of the agreement through which A-1 retained liability, stemmed from Deans & Homer's proposed new program to provide insurance coverage to self-storage facilities that assumed liability under the lease agreement (Deans & Homer's program is referred to herein as the "Alternative Lease Program")

The second contract is the insurance policy Deans & Homer offered to A-1 and other self-storage operators to cover some of the risks they retained in their Lease Agreements with tenants. Deans & Homer's insurance policy offered to self-storage companies including A-1 is titled the Storage Operator's Contract Liability Policy (referred to herein as the "Storage Liability Policy"). (1 CT 106-113.)

2. The 2003 and 2008 DOI Opinion Letters

Beginning in 2003 and continuing until the DOI filed its amicus brief, the DOI consistently took the position that the Alternative Lease Program, was not insurance. During that fourteen-year period, the DOI provided approvals related to Deans & Homer's program on four occasions.

Two of those approvals are the opinion letters – one in August 2003 and a second one in July 2008 – addressed by the Court of Appeals, (Opn. at 12-13) and in Deans & Homer's Answer Brief on the Merits filed with this Court ("Answer Brief" or "ABOM"). (Deans & Homer ABOM at 13-14.) Both opinion letters were issued by the DOI after Deans & Homer voluntarily contacted the DOI to ensure the Alternative Lease Program would be in compliance with the insurance code.

Deans & Homer first sought the DOI's approval for the Alternative Lease Program in 2003. Deans & Homer intentionally reached out to the DOI *before* enacting the program, with the intent of proceeding only if the DOI agreed the contracts between the self-storage operators and their tenants would not be insurance. (2 CT 320-324 [Deans & Homer letter discussing the proposed program, and noting it would only be implemented "[a]ssuming the [DOI] agrees . . . the elements of the proposed program between tenants and owners will not constitute insurance"].) The DOI responded on August 29, 2003. The DOI informed Deans & Homer that

the DOI did not view the contract between the self-storage operator and its tenant as a contract for insurance. (2 CT 326.)

After Article 16.3 was enacted, Deans & Homer again reached out to the DOI on a voluntary basis to confirm that the enactment of Article 16.3 did not cause the DOI's opinion to change. (2 CT 331, ¶ 5.) In July 2008, the DOI responded with another opinion letter assuring Deans & Homer that its opinion expressed in the 2003 letter was unchanged. (2 CT 328.)

3. The 2003 and 2014 DOI Approvals of Deans & Homer's Storage Liability Policy

In addition to these two DOI opinion letters, Deans & Homer also received the DOI's approval for its Storage Operator's Contract Liability Policy on two other occasions – in November 2003, and in August 2014.[2]

a. The DOI's November 2003 Approval

The first DOI approval of the Storage Liability Policy occurred soon after the DOI issued its August 29, 2003 opinion letter stating that the Alternative Lease Program would not constitute insurance. (2 CT 326.) Ten days later, on September 8, 2003, in reliance on the DOI's opinion letter, Deans & Homer submitted its application for the DOI to approve its Storage Liability Policy to be offered to self-storage operators that assumed

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[2] In response to the DOI's amicus brief reversing its interpretation of the relevant law and disclaiming any evidence in the DOI's records regarding what, if anything, the DOI reviewed about Deans & Homer's program in 2003 and 2008, Deans & Homer is responding with materials relating to the DOI's approval in November 2003 of the Storage Liability Policy and its 2014 approval of revisions to the program. (*See* Deans & Homer's Motion for Judicial Notice filed concurrently herewith; Lancaster Decl., MJN Exhibits 1 and 2; *see also* Deans & Homer ABOM at 17 n.10 [discussing that such approval from the DOI would have occurred].)

risk under their lease agreements. (*See* Lancaster Decl., ¶ 3 and MJN Exhibit 1, at 1.)

Deans & Homer's application to the DOI expressly laid out the program and the risk to be covered by the Storage Liability Policy. (*See* Lancaster Decl., MJN Exhibit 1, at 1, 6, 7.) The Deans & Homer submission included a detailed "General Program Description" and "Coverage" description that set out the underlying Alternative Lease Program, explaining that under the program, self-storage companies would retain liability in their lease agreement for damage to their tenants' property – in other words, Deans & Homer specifically explained to the DOI in its application the exact issue giving rise to this case.

Significantly, on November 4, 2003, the department within the DOI reviewing the application identified certain items that needed to be addressed before a recommendation could be made about the new program. (*See* Lancaster Decl., MJN Exhibit 1, at 12.)

On November 6, 2003, Deans & Homer responded to the DOI's questions, (*See* Lancaster Decl., MJN Exhibit 1, at 11.), and pointed out that Senior Staff Counsel from the DOI recently approved the program. Deans & Homer attached a copy of the August 29, 2003 DOI opinion letter with its response. (*See id.,* MJN Exhibit 1, at 13.) Finally, Deans & Homer invited the DOI to contact them if there were any further questions. (*See id.,* MJN Exhibit 1, at 11.)

The DOI did not raise additional questions or concerns. Instead, after receiving Deans & Homer's response, the DOI approved Deans & Homer's application for the new Storage Liability Policy. (*See id.,* MJN Exhibit 1, at 14.)

In short, in the Fall of 2003, yet another department within the DOI was informed of the Alternative Lease Program and Storage Liability Policy, and after specific consideration of the new program, gave the necessary approval of the application. (*See id.*) In reliance on the DOI's August 2003 and November 2003 approvals, Deans & Homer implemented the authorized program and began offering the Storage Liability Policy.

b. The DOI's August 2014 Approval

In 2014, Deans & Homer filed an application for a revision to the Storage Operator Contract Liability Policy with the DOI. (*See id.*, MJN Exhibit 2.) Deans & Homer did so because it was seeking to revise the product form and rates for the Storage Liability Policy. (*See id.*, MJN Exhibit 2, at 16.) As part of its 2014 application, Deans & Homer once again provided a "General Program Description" and "Coverage" description that set out the underlying Alternative Lease Program, as it had done in its 2003 application.[3] (*See id.*, MJN Exhibit 2, at 19.) Thus, the DOI again had the opportunity to review this issue and to raise additional questions or withhold approval. Instead, in August 2014, the DOI once again approved the program. (*See id.*, MJN Exhibit 2, at 18.)

In addition to the DOI's approvals for the Alternative Lease Program, the DOI has not initiated any enforcement proceeding against Deans & Homer or A-1, and the DOI does not mention any such enforcement proceedings in its brief. The DOI's four approvals demonstrate the DOI always was fully informed of the Alternate Lease

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[3] The application also noted the DOI had previously approved the Storage Liability Policy, and included a reference to the DOI's file number for that application and subsequent approval (referred to as "CDI 03-6207"). (*See id.*, MJN Exhibit 2, at 16.) Thus, the DOI could access the 2003 application.

Program it now claims violated the law. If the DOI believed the program constituted the unlicensed sale of insurance in violation of California's insurance code, as the DOI now asserts, the DOI could have initiated an enforcement proceeding at any time. The DOI chose not to do so – because until now, the DOI has consistently maintained that the program was not insurance.

C. The Court Should Give Weight To The DOI's Prior Approvals, Not To The DOI's New, Inconsistent Stance

This Court should give weight to the DOI's consistent stance it has taken since 2003: that the Alternative Lease Program is not insurance. This prior stance of the DOI contains a number of hallmarks of the type of agency interpretations that are entitled to some weight.[4] First, unlike the DOI's new stance, the DOI applied its prior interpretation for a lengthy time period – for the past fourteen years. This Court has said an agency's interpretation is entitled to more weight when it is long-standing. (*See Yamaha Corp. v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 13.)

Second, this Court has stated that an agency's interpretation also is entitled to more weight when the agency's interpretation is consistently applied. (*See id.*) Again, the DOI applied its prior interpretation consistently for fourteen years. During that time, the DOI repeatedly and

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[4] There are, of course, other types of agency interpretations that are entitled to even greater weight than the prior DOI approvals at issue here. For example, this Court has stated it would give greater weight to an agency's interpretation of its own regulation than to an interpretation of a statute. (*See Yamaha Corp. v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 12.) Nonetheless, the DOI's repeated, consistent, and long-standing stance related to the Alternative Lease Program, from multiple divisions within the DOI, is entitled to some weight here. (*See id.* at 13 (discussing factors, such as whether the interpretation was consistent and long-standing, and contemporaneous with the statute's enactment).)

consistently concluded the Alternative Lease Program is not insurance. The DOI also never initiated any enforcement proceeding against Deans & Homer or the self-storage companies participating in the program, including A-1, even though the DOI was fully informed of the program.

Third, this Court has held that an agency interpretation is entitled to greater weight when that interpretation is contemporaneous with the enactment of the statute being interpreted. (*See id.*) Here, the DOI's interpretation that the Alternative Lease Program would not constitute insurance was contemporaneous with the enactment of Article 16.3. As Deans & Homer discussed in its Answer Brief, (Deans & Homer ABOM at 31), the legislative history of Article 16.3 notes that the statute was being enacted in response to efforts by the DOI to stop self-storage companies from selling insurance policies as agents for insurance carriers. (Senate Committee on Insurance Report on AB 2520, hearing date June 16, 2004 at 3[http//www.leginfo.ca.gov/pub/03-04/bill/asm/ab_2501-2505/ab_2520_cfa_20040616_081436_sen_comm.ht ml].) In fact, the legislative history also notes that the DOI had issued several cease-and-desist orders against self-storage companies acting in this manner. (*See id.*) Thus, Article 16.3 was designed to address a circumstance the DOI viewed as a violation of the *existing* Insurance Code, as it existed even prior to Article 16.3 being enacted (namely, self-storage companies selling insurance policies as agents for insurance carriers).

Yet around the same time the DOI was issuing cease-and-desist letters to self-storage operators for the circumstance Article 16.3 was enacted to address, the DOI issued the 2003 opinion letter concluding the Alternative Lease Program was not insurance. (2 CT 326.) Soon thereafter, a separate division within the DOI issued its approval for the Storage Liability Policy. (Lancaster Decl., MJN Ex. 1, at 14.) After

Article 16.3 was enacted, and Deans & Homer asked the DOI to confirm Article 16.3 did not change the DOI's conclusion, the DOI issued the 2008 opinion letter affirming its prior view.[5] (2 CT 328.)

Thus, the DOI's prior position that the storage companies' contracts under the Alternative Lease Program did not involve insurance was contemporaneous with the passage of Article 16.3 and is entitled to greater weight as a result. (*See Yamaha Corp.*, 19 Cal.4th at 13.)

While there are numerous reasons why the DOI's prior interpretation of the law is entitled to deference and considerable weight, the DOI's sudden new stance, that the contracts under the Alternative Lease Program *do* constitute insurance, is entitled to no deference at all. The DOI's new position is directly contrary to the DOI's consistent interpretation of the law and its application of that law since 2003. As such, the DOI's current view is a "vacillating position" to which there should be no deference.[6] (*Yamaha Corp. v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 13.)

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[5] The 2003 and 2008 opinion letters were issued by the DOI's Compliance/Enforcement Bureau, (2 CT 326, 328.) which is the same division within the DOI responsible for enforcement actions (including issuing cease-and-desist letters) against those selling insurance without a license. Thus, the same division that was issuing cease-and-desist against self-storage operators for the type of conduct Article 16.3 was designed to address was, at the same time, informing Deans & Homer that its program would not violate the law. This further demonstrates the 2003 and 2008 opinion letters should be given considerable weight.

[6] In fact, whenever an agency issues an opinion that is not based on a long-standing interpretation of the statute, unless that opinion is a formally adopted regulation, courts have expressed a reluctance to defer to it at all. For example, in *Interinsurance Exchange of Automobile Club v. Superior Court* (2007) 148 Cal.App4th 1218, the trial court asked the DOI to opine on an important statutory interpretation issue. (*See Interinsurance Exchange*, 148 Cal.App.4th at 1223.) After the DOI provided its opinion,

Giving any weight to the DOI's current view also would be stunningly unfair to Deans & Homer, and would set a precedent that would result in regulated parties being unable to rely on opinions from the agencies that regulate them. Here, Deans & Homer acted responsibly and fairly, voluntarily seeking the DOI's input both before proceeding with its program and again after it was implemented. When the DOI issued legal interpretations giving its approval to Deans & Homer to continue, Deans & Homer was entitled to rely on the DOI's position, and Deans & Homer did in fact expressly rely on it. (Lancaster Decl. ¶ 3.)

As an insurance underwriter and agent licensed under the Insurance Code, (1 CT 204, ¶ 19), Deans & Homer must be able to rely in confidence on the DOI's statements regarding how the insurance laws are to be interpreted and enforced. (*See Ste. Marie v. Riverside County Reg'l Park and Open-Space Dist.* (2009) 46 Cal.4th 282, 293.) It would be grossly unfair to allow the DOI to abandon its prior approvals and to pull the rug out from under Deans & Homer fourteen years later.

Deans & Homer and A-1 are not the only ones to have relied on the DOI's prior view. Reversing the decision below on a retroactive basis would have significant negative consequences for California's 2,204 storage facilities. (*See* CSAA Amicus Br., at 4.) Those facilities and their

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the trial court deferred to the DOI's view. On appeal, the Court of Appeal held the trial court erred in deferring to the DOI's stance. The court held that when an "agency does not have a long-standing interpretation of the statute and has not adopted a formal regulation interpreting the statute, courts may simply disregard the opinion offered by the agency." (*See id.* at 1236 (quoting *State of Calif. Ex rel. Nee v. Unumprovident Corp.* (2006) 140 Cal.App.4th 442, 451.) In the present case, the DOI's interpretation is not just devoid of support from a long-standing agency position, it is directly counter to the DOI's long-standing view. As such, the DOI's current opinion cannot receive any deference.

tenants that have used the mutually-beneficial protection plan at issue here have operated in good-faith reliance for over a decade on the DOI's view that such plans are not insurance. Those protection plans remain in full effect even though the DOI has now changed its stance. If upheld, the DOI's new position would require a wholesale, unwarranted restructuring of how those transactions are consummated, with no ability for storage operators or even tenants who prefer the status quo ante to opt out.

The extensive reliance on the DOI's own view makes it even more inappropriate to give deference to its newly-minted position. It would be one thing if the DOI had been pursuing enforcement actions against regulated entities over the years and had staked out a clear and consistent position. But it makes no sense to have a regime where the DOI's amicus brief is treated as the key input when that input comes long after the decisions relying on the DOI's prior interpretation were made. This Court should reject the DOI's attempt to impose significant liability on storage operators who have done nothing more than sell a pre-approved product in conformity with long-settled industry practice.[7]

Perhaps even more concerning is that the DOI's brief implies Deans & Homer somehow acted nefariously in marketing its program for self-storage operators. The DOI now claims that the Lease Agreement A-1 sold to Heckart "appears to be designed to avoid regulation under the Insurance Code," (DOI Amicus Br. at 18), and that the Lease Agreement "implicates the evils at which the regulatory insurance statutes were aimed." (*Id.* at 26.) But the time for the DOI to have raised these concerns was back in

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[7] Because of this extensive reliance on the DOI's former position, considerations of fairness and public policy require any change in the law only to apply prospectively, not retroactively. (*See Claxton v. Waters* (2004) 34 Cal.4th 367, 378-79; *see also* Deans & Homer ABOM at 43-46.)

2003, when Deans & Homer initially sought the agency's approval, or at least back in 2008, when Deans & Homer inquired as to whether the DOI's position had changed.

In light of the multiple efforts Deans & Homer made to ensure the DOI approved of the program, it is difficult to see how Deans & Homer could have been any more transparent. Deans & Homer acted precisely in the manner one would want a good corporate citizen to behave – seeking regulatory approval before implementing its program, repeatedly disclosing the details of its program in a transparent manner, and following up with the regulator to confirm its opinion was unchanged when a potentially relevant statute was enacted later on.

Given Deans & Homer's transparency with its regulator, the DOI's criticism is not warranted. Instead, deference should be given to the repeated regulatory approvals on which Deans & Homer expressly relied.

D. The DOI's Criticisms Of Its Own 2003 and 2008 Opinion Letters Lack Merit

Because the DOI 's current opinion is utterly divergent from the opinion letters the DOI provided to Deans & Homer in 2003 and 2008, the DOI criticizes its own 2003 and 2008 opinions and attempts to minimize their importance. First, the DOI suggests the 2003 and 2008 DOI opinion letters should be ignored because it is unclear what materials the DOI reviewed before issuing them.

As for the 2003 letter, the DOI notes "[t]here is no evidence in the record that the Department received any other materials with the original letter [from Deans & Homer]." (DOI Amicus Br. at 11.) But the DOI's brief ignores the details of the lengthy 2003 letter from Deans & Homer,

which *is* in the record. (2 CT 320-324.) That letter described the Deans & Homer program in specific detail. (*See id.*) The Court of Appeal specifically found that this letter accurately described the Alternative Lease Program to the DOI, and rejected Heckart's argument that the letter failed to disclose key aspects of the program. (Opn. at 12-13.)

Thus, the DOI's 2003 opinion letter was issued only after it received a complete and accurate description of the Alternative Lease Program. There is no basis for discarding the opinion letter because of any alleged potential inadequacy in the materials the DOI received.

As for the 2008 letter, the DOI claims "there is no allegation that Deans & Homer sent any additional written materials to the Department at that time [in 2008]." (DOI Amicus Br. at 11-12.)

That is not accurate. The DOI's 2008 opinion letter expressly acknowledges that it did receive additional materials. The 2008 letter from the DOI states, "We thank you for providing the requested materials relating to the Deans & Homer program." (2 CT 328.)

This sentence from the 2008 DOI letter is significant because it reveals the DOI's 2008 opinion letter was based on a review of the specific materials the DOI requested, which the DOI itself believed were needed to conduct a proper analysis. This demonstrates that as much as the DOI now wants to paint its 2008 approval as ad-hoc and potentially without the benefit of adequately understanding Deans & Homer's program, its approval was the result of a considered process, and was based on the information the DOI believed was necessary to reach an informed opinion on which Deans & Homer could rely.

Next, the DOI seeks to downplay its 2003 and 2008 opinion letters by noting they were not the result of careful consideration by senior agency officials, but rather were prepared by a single staff member. (DOI Amicus Br. at 18 n.3 (quoting *Yamaha Corp.*, 19 Cal.4th at 13).) As an initial matter, the 2003 and 2008 opinion letters indicate they were written by Bruce Weiner, who is identified as a "Senior Staff Counsel," implying he was a senior attorney within the DOI's legal department. (2 CT 326, 328.) In 2003, Mr. Weiner's letterhead listed him in the Legal Division's Compliance Bureau, and in 2008 he is identified as Senior Staff Counsel in the Enforcement Bureau, (*see id.*) – the very department within the DOI that is responsible for enforcing the insurance laws against those who engage in the unlicensed sale of insurance. Thus, the record suggests he was a senior attorney within the very department at the DOI with particular knowledge regarding whether Deans & Homer's program for self-storage operators would constitute insurance under existing law.

In addition, while the DOI notes its 2003 and 2008 opinion letters were prepared by a single staff member, the DOI says nothing about the fact that a separate department within the DOI approved the new insurance program application. Deans & Homer's Answer Brief pointed out that under California law, it was required to obtain the DOI's authorization for issuance of the Storage Liability Policy. (Deans & Homer ABOM at 17 n.10.) Although Deans & Homer specifically discussed this required DOI approval in its brief, the DOI's amicus brief ignored that approval and its impact on the DOI's stance. As discussed above, in response to the DOI's amicus brief and the DOI's newly provided evidence, Deans & Homer is responding with evidence showing the Rate Regulation Division of the DOI did provide such approvals for Deans & Homer's insurance policy sold to self-storage operators, once in November 2003, and again in August 2014.

(*See* Lancaster Decl., Ex. 1 at MJN 14, Ex. 2 at MJN 18.) Consequently, contrary to the DOI's argument, Deans & Homer's program was reviewed and approved by two separate divisions within the DOI. Its approval was not limited to a single staff attorney within one department.[8]

II. The Lease Agreement Is Not Insurance Under The Principal Object Test and Article 16.3

In addition to the unfairness inherent in the DOI's new vacillating position, the DOI's position should be rejected for another reason: it is unsupportable on the merits. Although the DOI has drastically altered its own position, it has not added new substantive arguments beyond those Heckart previously posed, and which were addressed by the Court of Appeal. The DOI essentially just adopts Heckart's position and repeats his substantive points.

A. The DOI's Argument that "Whether Something is Insurance does not Depend on Who is Offering it" is Deeply Flawed

One of the DOI's primary arguments is that the Lease Agreement between A-1 and Heckart must be insurance because it is very similar to actual insurance policies that insurance carriers are selling to customers to protect their property stored in rented storage facilities. Adopting Heckart's argument, the DOI argues it would exalt form over substance to

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[8] The DOI also notes that the 2003 and 2008 letters did not benefit from input from other interested parties "as would have occurred in a quasi-adjudicatory proceeding or in a rulemaking that is subject to notice and comment." (DOI Amicus Br. at 18 n.3.) Of course, the same is true of the new position the DOI asserts in its amicus brief. The DOI's brief was not subject to input from the industry or other interested parties, nor was it subject to notice and comment. Thus, in this regard, the DOI's new stance is open to the same criticism to which the DOI subjects its own 2003 and 2008 opinion letters.

conclude that a contract is insurance if sold by an insurance carrier, but is not insurance if it is sold by a self-storage company. (DOI Amicus Br. at 24; *see* Heckart OBOM at 13-14.)

Actually, under the principal object test, whether something is insurance can depend a great deal on who is offering it. While that may seem counter-intuitive at first blush, it actually makes an extraordinary amount of sense. This is because the principal object test recognizes there is a critical difference between (1) a contract with an insurance carrier who agrees to take on a risk *to which it otherwise would face no possibility of exposure*, versus (2) a contract with a primary purpose other than indemnity, that also allocates between the parties the risks arising under that contract *to which the parties already face exposure*. Under the principal object test, the former is a contract for insurance, whereas the latter is not. (*See* Deans & Homer ABOM at 20-22.)

The reason for this distinction is that the Courts have recognized the parties to a contract should be able (or even encouraged) to resolve liability issues related to their contractual relationship before a dispute arises. This allows the parties to create certainty regarding their potential liability under the agreement, and allows both sides to reduce the risk of litigation related to the contract.

When an insurance carrier signs a contract to assume liability to which it otherwise has no exposure, however, it is not resolving existing questions of liability. Instead, the insurance carrier is being paid to take on a new risk it otherwise could not be forced to bear. The principal object of such a contract is indemnity, and thus it is a contract for insurance.

Here, the principal object of the contract between A-1 and Heckart is not indemnity. Instead, the principal object, as even Heckart admits, was

the rental of storage space. (Heckart OBOM at 21 [acknowledging the protection plan was "incidental" to the lease agreement between A-1 and Heckart].) The purpose of the specific risk-shifting provisions in the contract is for the parties to resolve potential liability for various risks that could arise under the agreement.

The DOI also asserts A-1 is agreeing to pay for its tenant's cost to repair or replace property damaged by various hazards, which the DOI claims is "directly comparable to property or casualty insurance policies offered by licensed insurers." (DOI Amicus Br. at 17.) As a result, the DOI concludes A-1's Lease Agreement must be treated the same as such property or casualty insurance policies. (*See id.*) But this argument ignores the critical distinction discussed above – that, unlike insurance carriers who offer property or casualty insurance, A-1 already faces exposure for the liability it is agreeing to retain. Thus, whereas a property or casualty insurer is being paid to take on a new risk of liability for which it otherwise could not be responsible, A-1 is simply negotiating with the other contractual party to determine which party will bear the risks inherent in their contract. As such, the DOI's argument that A-1's situation is comparable to that of a property or casualty insurer is incorrect.

As the court in *Automotive Funding Group* stated "[o]ffering an alternative to insurance does not mean that the alternative *is* insurance." (*Automotive Funding Group, Inc. v. Garamendi* (2003) 114 Cal.App.4th 846, 854.)

B. Through the Protection Plan, A-1 is Retaining Liability to which it Already Faces Exposure

Relatedly, the DOI disputes that A-1 is truly "retaining" liability in the Lease Agreement, as opposed to "assuming" liability that it does not

otherwise have. The DOI argues A-1 would not actually have any liability for damage to a tenant's property "unless and until a court of law so ruled." (DOI Amicus Br. at 17.) Thus, the DOI argues A-1 is not truly "retaining" liability, it is acting more like an insurer.

Obviously, a self-storage operator faces a real risk of liability to its tenants for damage to their stored property. Under the Lease Agreement A-1 entered into with Heckart, A-1 agreed to retain liability for damage to the tenant's property caused, for example, by fire, roof leak or water damage, theft, or vandalism. (1 CT 52.) As a lessor, A-1 faces a very real risk of liability for damage to its lessee's property from each of these causes, particularly if A-1 was negligent in failing to maintain, repair, or secure its premises. (*See* A-1 ABOM at 12 [listing cases in which liability was imposed on self-storage companies and other lessors for theft, vandalism, fire, and water damage].)

Because A-1 faced the possible exposure to such liability, it was entitled to negotiate with Heckart to allocate such liability to Heckart, or conversely, to retain such liability for itself. (*See* 2 CT 261 [A-1 expressly noting the areas in which it was "retaining" liability].)[9] Either way, A-1 was not simply "assuming" liability in the Lease Agreement to which it otherwise would not be exposed, as an insurance carrier would do. A-1 was allocating liability for risks to which it already was exposed.

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[9] Moreover, the addendum to the Lease Agreement also carved out a number of other areas in which A-1 was not agreeing to retain liability. This is significant because many of the items listed generally are "force majeure" events outside the control of a landlord, such as acts of war earthquakes, or nuclear/biological/chemical contamination. (2 CT 262.) A-1 generally would not face liability for these risks. The fact that A-1 carved out such risks from its acceptance of liability demonstrates A-1 was not "assuming" risks it otherwise would not face, it was only "retaining" risks to which it is more likely to be exposed.

C. As the DOI Acknowledges, the Purpose of Article 16.3 was to Create a Streamlined Licensing Scheme for Self-Storage Companies Acting as Agents for Insurers

The DOI now believes that A-1's Lease Agreement is insurance under Article 16.3 of the Insurance Code. (DOI Amicus Br. at 17-18.) Of course, that stance directly contradicts the DOI's interpretation of that statute as reflected in its 2008 opinion letter to Deans & Homer. (2 CT 328.) Putting that aside, the DOI's current view is at odds with the DOI's own understanding of the purpose of Article 16.3.

In its Answer Brief, Deans & Homer discussed that both the statutory language and legislative history of Article 16.3 show it is intended to govern the situation in which a self-storage facility acts as an *agent* for an insurance carrier, selling the *insurance carrier's* policy directly to its tenant. (Deans & Homer ABOM at 29-33.) Of course, Heckart disagrees – he argues Article 16.3 was intended to create a definition of insurance within the context of self-storage companies, and that the statute thus directly governs this case. (Heckart OBOM at 13; *see id.* at 10-17.)

The DOI agrees with Deans & Homer in this respect, not Heckart. The DOI agrees that the purpose of Article 16.3 was not to define a new category of "insurance," as Heckart argues, but rather to "provide a streamlined licensing scheme under which self-storage facilities, acting as *agents* for authorized insurers, may offer or sell" certain types of insurance incidental to self-storage rental agreements. (DOI Amicus Br. at 8 (emphasis added).) In other words, the DOI agrees the statute's purpose was to create a limited agent license when self-storage operators are acting as the *agent* for an insurance carrier.

Despite this acknowledgment, the DOI nonetheless argues Article 16.3 still governs this case. (DOI Amicus Br. at 17.) The DOI argues:

> If the Protection Plan sold by A-1 is not "hazard insurance" because it may be considered incidental to the Rental Agreement, then it is unclear what transactions *would* be subject to licensing under Insurance Code section 1758.7 et seq. [i.e. Article 16.3], given that every transaction other than the Rental Agreement is in a sense subsidiary or secondary to the Rental Agreement."

(*Id.* (emphasis in original).) But the answer to the DOI's question – when would Article 16.3 apply, if it does not apply to the present case – is simple.

The answer is contained within the DOI's own acknowledged statement of the purpose for the statute. Article 16.3 applies when a self-storage company is acting as an *agent* for an insurance carrier, and is selling the insurance carrier's insurance policy directly to the self-storage company's tenant. In that instance, the tenant would be forming a contractual relationship directly with the insurer, and would hold an insurance policy issued under the carrier's name. The insurance carrier would be assuming liability directly for the tenant's stored property, which the liability the carrier otherwise would not be exposed. Stated differently, Article 16.3 would apply to situations such as that addressed in *Wayne v. Staples* (2006) 135 Cal.App.4th 466, where a separate insurance policy issued by an insurance carrier was being sold through an agent to the customer. (*See id.* at 471-472 [Staples sold insurance policy on behalf of, and

in the name of, an insurance carrier, to its customers, who became additional insureds under the policy.])

Here, A-1 is not acting as the agent for any insurance carrier, nor is A-1 selling an insurance carrier's policy to its tenants on the carrier's behalf. Instead, A-1 has merely agreed with its tenant regarding the allocation of risks under the Lease Agreement. Heckart's contractual relationship remains solely with A-1, not with an insurance carrier. Consequently, Article 16.3 does not apply to the circumstances in this case.

D. A-1's Alleged Profit From the Protection Plan does not Demonstrate that the Lease Agreement should be Regulated as Insurance

The DOI argues A-1's Lease Agreement should be regulated as insurance because the rate A-1 charged on the Protection Plan portion of the Lease Agreement allegedly is excessive. The DOI argues the rate A-1 charged, compared to the rate A-1 paid for the Storage Liability Policy, shows the Protection Plan implicates the evils at which the insurance code is aimed. (DOI Amicus Br. at 26.)

As an initial matter, as discussed in detail in Deans & Homer's Answer Brief, the so-called "evils" prong is not part of the principal object test, and thus is not relevant here. (*See* Deans & Homer ABOM at 25-27).

In addition, the DOI's argument is flawed because it ignores allegations in Heckart's own complaint that show A-1 would make virtually the same profit even if A-1 was regulated as an insurer.

Specifically, the DOI points to a portion of Heckart's First Amended Complaint, which alleges A-1 netted about $1.6 million per year in Protection Plan Premiums, while paying out only about $25,000 in Protection Plan claims per year. (DOI Amicus Br. at 26 (citing 1 CT 213, ¶¶ 49-51).) The DOI also points out that A-1 only pays a premium of 74 cents per month for the Storage Liability Policy, while tenants pay $10 per month under the Protection Plan. The DOI concludes that tenants are paying a rate that is more than thirteen and a half times higher than the amount A-1 is paying. As a result, the DOI asserts the rate A-1 is charging, if proven, would be excessive. (DOI Amicus Br. at 26-27.)

The problem with this argument is that it makes the wrong comparison. The DOI is comparing the amount A-1 receives from its tenant ($10 per month) to the amount A-1 allegedly is paying in premiums under the Storage Liability Policy (74 cents per month).

But to make this argument, what the DOI *actually* needs to compare is the amount A-1 receives under its lease ($10) versus what licensed insurance carriers are charging to self-storage tenants under their insurance policies. After all, the alleged "evil" here is that A-1 is charging a rate to tenants that has not been approved by the DOI and that is excessive compared to DOI-approved insurance policies. Thus, the proper comparison is to policies with rates approved by the DOI.

Heckart's complaint alleges that the rate Deans & Homer charges to self-storage tenants for a policy comparable to A-1's Protection Plan is $9.66 per month, whereas A-1's protection plan costs $10 per month. (1 CT 209-210, at ¶ 40.) Thus, under the

proper comparison, A-1's protection plan is only thirty-four cents more per month for relatively similar coverage, and the difference is offset by the lack of a deductible.[10] That is, if anything, a nominal difference in rate. Moreover, the option of contracting directly with the storage company rather than with an insurer provides additional benefits for the consumer. (*See* CSSA Amicus Br. at 9.)

Based on this *accurate* comparison, the DOI's argument that the alleged rate A-1 charged was excessive, and warrants regulation under the insurance laws, falls apart.[11]

III. Adoption of the DOI's New Interpretation would Violate Deans & Homer's Federal Due Process Rights

In addition to the lack of deference to be accorded the DOI's new position under California law, deferring to the DOI's new interpretation of the law and applying it to Deans & Homer retroactively would create federal due process concerns.

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[10] Heckart claims A-1's Protection Plan covers $2,500 in losses, with no deductible, whereas Deans & Homer's similar policy covers $3,000 in losses and has a $100 deductible.

[11] The DOI also argues the so-called "evils" are implicated, mandating regulation of the Protection Plan as insurance, because A-1 employees are not given sales practice instruction, nor does A-1 inform tenants that the Protection Plan may duplicate coverage. (DOI Amicus Br. at 27.) But as the Court of Appeal found, and as Deans & Homer addressed in its Answer Brief, that argument is utterly circular. (Opn. at 11-12; Deans & Homer ABOM at 26.) The requirements of the Insurance Code, including those mentioned by the DOI, do not apply unless and until A-1's Lease Agreement is found to be insurance.

A. The Federal Constitutional Limits Governing Retroactive Lawmaking Preclude Retroactive Agency Decisions.

The United States Constitution limits the ability to apply agency decisions retroactively. The Due Process Clause of the United States Constitution prevents the courts from achieving, through a legal interpretation both unexpected and indefensible by reference to the law previously expressed, that which the legislative branch may not achieve under the Ex Post Facto Clause. (*Bouie v. City of Columbia* (1964) 378 U.S. 347, 354; *Rogers v. Tennessee* (2001) 532 U.S. 451, 461.) As a general matter, the principles that disfavor retroactive enforcement of legal change also apply to administrative agencies. (*See, e.g., Bowen v. Georgetown Univ. Hospital* (1988) 488 U.S. 204, 208 [because "[r]etroactivity is not favored in the law," "congressional enactments and administrative rules will not be construed to have retroactive effect unless their language requires this result"].)

There is no basis for concluding, based on precedent or otherwise, that federal due process limits on retroactivity constrain legislatures and judges but somehow leave the executive branch completely unfettered. Administrative decisions and rules can give rise to private expectations protected by the Fourteenth Amendment. (*See, e.g., Perry v. Sindermann* (1972) 408 U.S. 593, 602-603 [noting that "rules and understandings, promulgated and fostered by state officials" may even create a property interest protected by the Due Process Clause].) Accordingly, the various constitutional principles that limit the power of legislatures to disrupt settled expectations must limit less-democratically accountable administrative agencies as well. Otherwise, it would make little sense for the Court to enforce limits on legislative retroactivity, but to give agencies

carte blanche to change their legal interpretations retroactively, regardless of justification or circumstance.

Applying these basic principles, the Supreme Court has thus rejected claims that would have exposed settled industry practices to potentially significant retroactive liability. (*See, e.g.*, *Integrity Staffing Solutions, Inc. v. Busk* (2014) 135 S.Ct. 513, 518-519 [rejecting novel attempt to impose FLSA liability for time spent in security screenings].) The Court has likewise explained that where an agency's change in an interpretation of its own regulation creates "unfair surprise," the change can present a ground for disregarding the agency's new interpretation advanced in litigation. (*See Long Island Care at Home, Ltd. v. Coke* (2007) 551 U.S. 158, 170-171.) As explained herein, that is precisely the case here.

B. The DOI Has Failed to Justify Its Adoption of an Interpretation That Upsets Long-Settled Expectations.

The DOI's startling decision to change its prior view upends an area of law that had been settled for nearly a decade and a half. Having formally conferred its blessing on the Alternative Lease Program, the DOI lulled both Deans and Homer and the storage operators to perform their conduct in a particular way. Consequently, the DOI cannot simply change its mind and dash the reasonable expectations of the contracting parties.

In sum, the DOI's radical change in position does not merit judicial deference because its novel interpretation of the law, an about-face interpretation expressed only in an *ad hoc* amicus filing, raises grave retroactivity problems. (*See Edward J. DeBartolo v. Florida Building Trades* (1988) 485 U.S. 568, 574-575 [deference inapplicable where agency interpretation raised serious constitutional concerns].) While storage operators have presumably made massive investments in reliance on the

DOI's approval of the subject protection plan, the DOI claims the ability to make those investments "worthless" with the stroke of a pen. (*Bowen, supra,* 488 U.S. at p. 220 (conc. opn. of Scalia, J.).)

This Court should, therefore, be highly skeptical of the DOI's arguments seeking to impose significant retroactive liability for settled industry practices that had long been viewed by the DOI itself as lawful. "It is one thing to expect regulated parties to conform their conduct to an agency's interpretations once the agency announces them; it is quite another to require regulated parties to divine the agency's interpretations in advance or else be held liable when the agency announces its interpretations for the first time in an enforcement proceeding and demands deference." (*Christopher v. SmithKline Beecham Corp.* (2012) 567 U.S. 142, 158-159.)

Here, of course, the danger is even more acute because the agency has articulated its new position in an amicus brief. This type of "drive-by" interpretation ill serves both the regulated community and the public at large by promoting unpredictability and a lack of transparency while undermining the sense of procedural fairness that engenders public confidence in agency action.[12] The DOI's justification for discarding its

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[12] Of course, the Supreme Court has deferred to an agency interpretation advanced for the first time in an amicus brief. (*See Auer v. Robbins* (1997) 519 U.S. 452, 461-462.) The *Auer* doctrine has arguably created a world in which businesses must scour court dockets, amicus briefs, agency websites, letters sent to other companies, and other agencies' policies to understand the regulatory regime that might be enforced against them. (*See, e.g., Chase Bank USA, N.A. v. McCoy* (2011) 562 U.S. 195, 208 [applying *Auer* doctrine].) Several justices, however, have confirmed that the *Auer* doctrine should be reconsidered and overruled. (*See, e.g., Perez v. Mortg. Bankers Ass'n* (2015) 135 S.Ct. 1199, 1211-1213 (conc. opn. of Scalia, J.); *Decker v. Nw. Envtl. Def. Ctr.* (2013) 568 U.S. 597, 616-626 (conc. & dis. opn. of Scalia, J.).) "The issue is a basic one going to the heart of administrative law." (*Decker*, at p. 616 (conc. opn. of Roberts, C.J.).)

own counsel's prior view, relegated to a single footnote (Amicus Br., p. 18, fn. 3), allows "[a]ny government lawyer with a laptop [to] create a new" cause of action "by adding a footnote to a friend-of-the-court brief." (*Carter v. Welles-Bowen Realty, Inc.*, 736 F.3d 722, 733 (6th Cir. 2013) (conc. opn. of Sutton, J.).) In short, this is a classic case where the position taken in the government's brief "departs markedly from the [agency's] understanding at all times relevant to this case." (*Wyeth v. Levine* (2009) 555 U.S. 555, 580 n.13 [deeming the government's position in its amicus brief "undeserving of deference" for this reason].)

To be sure, the DOI's new stance here *is not quasi-legislative*. It is merely a change in the agency's long-standing interpretation of statutory law. However, there remain federal due process concerns in applying that new interpretation retroactively.

CONCLUSION

The decisions of the trial court and the appellate court should be affirmed.

Respectfully submitted,

DATED: October 2, 2017

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Because the *Auer* doctrine "is on its last gasp" (*United Student Aid Funds, Inc. v. Bible* (2016) 136 S.Ct. 1607, 1608 (Thomas, J., dissenting from denial of certiorari)), it does not govern this case, given its inherent flaws.

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PROOF OF SERVICE

Samuel Heckart v. A-1 Self Storage, Inc., et al.
Supreme Court of California, Case No. S232322
Court of Appeal, Fourth Appellate District, Div. One, Case No. D066831
San Diego Superior Court Case No. 37-2013-00042315-CU-BT-CTL

I, the undersigned, declare as follows: I am employed with the law firm of Wilson, Elser, Moskowitz, Edelman & Dicker LLP, whose address is 401 West A Street, Suite 1900, San Diego, California 92101. I am over the age of eighteen years, and am not a party to this action. On **October 2, 2017**, I served the foregoing documents described as:

RESPONDENT DEANS & HOMER'S ANSWER TO AMICUS CURIAE BRIEF OF INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA

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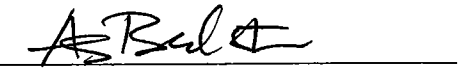

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