

IN THE SUPERIOR COURT FOR THE DISTRICT OF COLUMBIA
CIVIL DIVISION

NATIONAL ASSOCIATION OF)
STATE FARM AGENTS, INC.,)

RECEIVED
SEP 02 2005
Clerk's Office
Superior Court of the
District of Columbia
Washington, D.C.

Plaintiff,

v.

STATE FARM MUTUAL)
AUTOMOBILE INSURANCE)
COMPANY, *et al.*)

Defendants.)

C.A. No. 02ca004089
Calendar 7

Senior Judge Leonard Braman

DEFENDANTS' POST-TRIAL MEMORANDUM

Paul S. Reichler, D.C. Bar No. 185116
Lawrence H. Martin, D.C. Bar No. 476639
Sarah A. Altschuller, DC Bar No. 489202
FOLEY HOAG LLP
1875 K Street, N.W., Suite 800
Washington, DC 20006
(202) 223-1200

September 2, 2005

TABLE OF CONTENTS

I.	The Partner Agent Program	1
II.	Select Agent Program	8
III.	Restrictions on the Submission of New Business.....	18
IV.	Brokering Business for Other Insurers	23
V.	Mandatory Attendance at Annual Ethics Meetings	27
	Conclusion	30

Pursuant to the Court's order at the close of trial on August 1, 2005, Defendant State Farm respectfully submits this Post-trial Memorandum. For the reasons articulated in Defendants' Proposed Findings of Fact and Conclusions of Law submitted simultaneously herewith, and elaborated below, State Farm respectfully submits that it is entitled to judgment in its favor on all remaining counts of Plaintiff's Complaint.

I. The Partner Agent Program

The uncontroverted facts adduced at trial show that the Partner Agent Program as originally conceived was discontinued as of August 2003. Each and every one of State Farm's trial witnesses testified that the Program was terminated or replaced as of that date. (Proposed Findings ¶¶ 61-62.) Plaintiff's deposition and trial witnesses testified to like effect. In each case, they acknowledged that the Partner Agent Program as initially devised had either been ended or was never implemented. (*Id.* ¶ 62; *see especially* Nazziola, July 26, Tr. 170:9-15 ("Q. So basically, the Program was? A. Stopped. Q. Stopped? A. Stopped."); Knapp, July 26, Tr. 119:9-22 (the Partner Agent Program was the "perfect program because everyone was happy and nothing happened.")) Indeed, Plaintiff claimed credit for the demise of the Partner Agent Program in a July 2003 communication sent to all State Farm Agents -- members and non-members alike -- in which it stated: "[A]lthough the Partner Agent Program may not be completely dead, it is clearly in a very deep coma and is not likely ever to be revived." (Def. Ex. 55.) The conclusion is thus unmistakable: the Partner Agent Program was over by August 2003.

The testimony is equally unanimous that the Partner Agent Program was replaced by the Registered Representative Referral Database ("RRRD") in August 2003. (Proposed Findings ¶ 61.) Plaintiff has offered nothing to contradict this fact because there is nothing. Court Exhibit 3 contains proof positive in the form of e-mails from Mr. Don Sikora to agency field leadership announcing the updating of the "Registered Representative Referral Database" used for

“referring securities customers to a local registered State Farm Agent.” (Ct. Ex. 3 at SFM NASFA 4721.) Similarly, Court Exhibit 3 also contains a model e-mail to AFEs with the subject line “Registered Representative Database” and states: “It is time to update the database with the names of non-registered agents and their selected registered agent.” (Ct. Ex. 3 at 4719.)

The record shows that Agents received and heard the information concerning the transition from the Partner Agent Program to the RRRD. AFEs were instructed to inform their Agents that the Partner Agent Program had been replaced and no longer existed. (Proposed Findings ¶ 61.) And when presented with the opportunity to select a registered referral Agent in connection with the introduction of the RRRD, fully 94% of all non-registered Agents elected to do so. (*Id.* ¶ 69.)

Participation by non-registered Agents in the RRRD was entirely voluntary. Although non-registered Agents were encouraged to select a registered referral Agent, they were not required to do so. Nor was a registered referral Agent selected for them if they declined to do so. (Proposed Findings ¶ 67.) Mr. Sikora’s August 6, 2003 e-mail to Agency field leadership states the voluntary nature of the program in emphatic terms. For instance, it states: “All non-registered agents will have the opportunity to **voluntarily** select a registered fellow agent for their referrals.” (Ct. Ex. 3 at SFM NASFA 4721 (emphasis in original).) In a like vein, it also states: “**The non-registered agent may choose NOT to select an agent for referrals.**” (*Id.* (emphasis and capitalization in original).) The voluntariness of participation in the RRRD is likewise echoed in a model e-mail Mr. Sikora sent out to the field on August 21, 2003: “If a non-registered agent elects NOT to select a registered agent for securities products referrals, no agent will be recorded on the database.” (Ct. Ex. 3 at SFM NASFA 4719 (capitalization in original).) This same fact is reflected throughout the record. Not only did Messrs. Sikora and

Fisher personally testify to it (Sikora, July 26, Tr. 244:17-22; Fisher, July 27, Tr. 80:18-20), but it is also reflected on the “Frequently Asked Questions” document posted on State Farm’s Agency intranet, which is available to all field leadership. (See Pl. Exs. 13 & 14 (Question 3: “If a non-registered agent does not submit a selection, the Securities Products department will handle inquiries on a rotation basis.”). Still further, the sample print-outs from the RRRD offered into evidence as Court Exhibit 4 reveal that when a non-registered Agent chose not to select a registered referral Agent, the database was left blank where the information concerning the referral Agent would otherwise be.

At trial, Plaintiff devoted attention to several of the July 2005 e-mails included in Plaintiff’s Exhibit 91 requesting updates to the RRRD, and tried to argue that they demonstrate that participation in the RRRD is required. The nominal basis for this argument is the fact that a small subset of these 20 e-mails state that if non-registered Agents do not select a referral Agent, one will be selected for them. In point of fact, however, there are only three (3) such e-mails from AFEs to Agents, representing a mere 0.6% of State Farm’s 500 AFEs nationwide. Fifteen of the other 17 e-mails offered in Exhibit 91 do nothing more than ask non-registered Agents to select a referral Agent without affirmatively stating that Agents have the choice to decline to do so; the last two are completely neutral.

Moreover, the testimonial and documentary proof shows that when these e-mails were brought to the attention of State Farm management in Bloomington, Illinois, the Company took immediate action to remedy any confusion and reiterate to AFEs that Agents’ participation in the RRRD is entirely optional. (Proposed Findings ¶¶ 74-75.) Specifically, State Farm made sure that instructions were sent to all of its 500+ AFEs reminding them that Agents were not required to appoint a referral Agent, and that if an Agent chose not to make such an appointment, no

referral Agent would be appointed for him. (*Id.* ¶¶ 74-75.) In these communications, the Company referred AFEs to the existing Agency intranet site for the correct information about the RRRD. (*Id.*)

State Farm management also sent e-mails directly to the particular AFEs who had given incorrect or incomplete information to Agents, and instructed them to advise the Agents that the RRRD was voluntary, that they were not required to appoint a referral Agent, and that if they chose not to do so none would be appointed for them by the Company. (Proposed Findings ¶ 75.) Conspicuously, Plaintiff offered absolutely no evidence that any referral Agent was in fact appointed by the Company when a non-registered Agent chose not to do so. (*Id.* ¶ 76.) The evidence thus remains unequivocal that participation in the RRRD is entirely voluntary.

There is no doctrine of contract law which prohibits one party to an agreement from requesting the voluntary cooperation of another party. To the contrary, a claim for breach can only lie where one party acts in contravention of a duty created by the terms of the contract. *See* 8 CORBIN ON CONTRACTS § 30.13 (1999) (“Breach of contract is always the non-performance of some duty created by a promise.”); *Martin v. State Farm Mut. Auto. Ins. Co.*, 2004 WL 594096, *5 (Ill. App. Ct. 2004) (“In stating a claim for breach of contract, only a duty imposed by the terms of the contract can give rise to the breach.”); *Dist. Cablevision Ltd. P’shp v. Bassin*, 828 A.2d 714, 729 (D.C. 2003) (“The hornbook definition of the term ‘breach of contract’ is ‘an unjustified failure to perform all or any part of what is promised in a contract.’”) (citing *Fowler v. A & A Co.*, 262 A.2d 344, 347 (D.C. 1970)). Accordingly, there is no serious argument that the RRRD violates the Agent’s Agreement.

Because participation in it, too, was voluntary, the original Partner Agent Program likewise did not violate the Agent’s Agreement. At closing argument, counsel for NASFA

invoked Sections I(B) and I(H) of the Agreement as textual bases for its breach of contract claim, but for the reasons more fully set out in Defendant's Proposed Findings of Fact and Conclusions of Law, neither provision can provide foundation for Plaintiff's claim. (*See generally* Proposed Findings ¶¶ 79-95.) For present purposes, it is sufficient to note that (1) there is no evidence that Agents' independence under Section I(B) was impinged in any way by the Partner Agent Program since participation in it was voluntary; and (2) non-registered Agents' interests in their "books of business" -- to the extent those interests are even protected by Section I(H) -- were at all times respected by the Company and by registered Agents.

Setting aside the absence of any formal grounds for NASFA's complaint, there is also no basis even for concluding that Plaintiff's inchoate concerns about the Partner Agent Program ever materialized in actuality. At trial, Plaintiff's President-elect, Mr. Knapp, testified that he considered the Partner Agent Program a violation of the Agent's Agreement because (1) "it opens the door wide to promote the raiding of [his] business by the partner agent" and (2) the Company's contemplated direct marketing of mutual funds to customers of non-registered Agents somehow made "it easy for [his] clients to be transferred to another Agent." (Knapp, July 26, Tr. 113:16-25.) Plaintiff's other witnesses expressed similar concerns. (*See* Swift, July 26, Tr. 144:20-25, 146:1-4; Nazziola, July 26, Tr. 164:10-165:1.)

With respect to the first concern, the undisputed facts demonstrate that the door to raiding was sealed shut. During the truncated life of the Partner Agent Program, State Farm never received even a single report of raiding in connection with the Program. (Proposed Findings ¶ 54.) Nor have any of Plaintiff's witnesses been able to identify even a single instance of raiding occasioned by the Program. (*Id.*)

The reason is simple -- State Farm took all reasonable steps to forestall raiding (a fact which by itself should conclusively demonstrate State Farm's good faith towards non-registered Agents). Indeed, the facts reveal that one of the very purposes of the Program was to prevent raiding by giving non-registered Agents control over the identity of their partner in order to give them comfort that their partner was someone they could trust to refrain from raiding. (Proposed Findings ¶ 33.) Additionally, State Farm required Partner Agents to confirm that they would not solicit other lines of insurance and charged local agency leadership with monitoring the situation to make sure no raiding occurred. (*See id.* ¶ 52.) Indeed, when Plaintiff's former President, Mr. Swift, contacted State Farm's former chief agency officer, Chuck Wright, to express his concerns about the program, Mr. Wright assured him that State Farm would make sure that no raiding occurred in connection with the Program. (*Id.* ¶ 53.)

With respect to Plaintiff's second concern, the evidence demonstrates that State Farm did nothing to make it easy for the clients of non-registered Agents to be transferred to registered Agents. Although some form of direct mail marketing to customers serviced by non-registered Agents was envisioned at the time the Partner Agent Program was conceived, State Farm never actually pursued any direct marketing efforts. (Proposed Findings ¶ 56; *see especially* Sikora, July 27, Tr. 57:4-9 ("THE COURT: Even if a non-registered agent appointed a registered agent, there would be no direct mailing by that registered agent? THE WITNESS: There would be no direct mail by the registered agent to the customers of that non-registered agent."); Knapp, July 26, Tr. 120:13-121:7, 139:21-24 ("Q. ... The company did not, in fact, conduct any direct mail solicitations to the customers of non-registered agents such as yourself; correct? A. Not that I am personally aware of.")) In fact, State Farm decided not to engage in direct marketing to customers of non-registered Agents after hearing the concern expressed by some non-registered

Agents, who were fearful that this might make them look bad to their customers. (Proposed Findings ¶¶ 51, 56.)

In the end, the record shows that participation in the Partner Agent Program was, like participation in the RRRD, voluntary. Although the Company did select Partners for non-registered Agents who declined to do so for themselves, 79% of all non-registered Agents voluntarily nominated their own Partners. (Proposed Findings ¶ 48.) Indeed, Plaintiff's incoming President did so. Mr. Knapp, the same man who testified at trial that the Partner Agent Program was a danger, also testified that he saw "no harm" in selecting his own Partner. (*Id.*)

Even in those cases where the Company selected a non-registered Agent's Partner, the "partnership" existed nowhere but in an electronic database maintained at State Farm's corporate headquarters. The key fact is that State Farm never *required* non-registered Agents to refer customers interested in mutual funds to their designated Partners. (Proposed Findings ¶ 35.) As Mr. Knapp himself testified: "[N]on-registered Agents were certainly encouraged to refer. They weren't required to refer, they were encouraged to refer." (Knapp, July 26, Tr. 135:11-13.) Thus, it is undisputed that State Farm took no action against Agents who refused to refer mutual fund business to their Partners. (Proposed Findings ¶ 35.) It is also undisputed that State Farm never required -- or even asked -- non-registered Agents to share any of their policyholder information with their Partner Agents. (*Id.* ¶ 36.) And State Farm never gave Partner Agents the names and addresses of the non-registered Agents' customers itself. (*Id.*; *see especially* Sikora, July 27, Tr. 57:16-19 ("THE COURT: But nevertheless, the company did not give the registered agent the names and addresses of the non-registered agent's customers? THE WITNESS: That is correct."))

The bottom line is simple: State Farm did not *require* non-registered Agents to deal with their Partner Agents in any way; their collaboration, if any, was entirely voluntary on the part of the Agents involved. (Proposed Findings ¶ 36.) Contrary to what Plaintiff would have the Court believe, this was no “shotgun marriage” between Agents. Agents were not forced or required to refer customers, share information or deal with other at all if they chose not to do so. In actual practice, the only purpose served by the Partner Agent Program was the same as that of the RRRD -- to provide customers who submitted an inquiry about mutual funds directly to the Company with the name of a local Agent licensed to solicit securities business, as the law required. (*See id.* ¶¶ 31, 35, 36, 56, 58, 61.)

Consequently, the Partner Agent Program, like the RRRD, did not violate the Agent’s Agreement. Moreover, even if, for the sake of argument, it did so in some theoretical way, it still would not constitute grounds for the declaratory relief Plaintiff has requested. The testimony and documentary proof showed that the Partner Agent Program was terminated and replaced in August 2003, more than two years ago, and both parties have asserted that it will not be revived. (Proposed Findings ¶¶ 61, 62.) Accordingly, because it is moot, Plaintiff’s request for a declaratory judgment should be denied.

II. Select Agent Program

The evidence proves that the Select Agent Program is a bonus and reward program that affords all Agents an opportunity to receive benefits beyond anything they are entitled to under their Agent’s Agreement. The Select Agent Program thus resembles an additional contract with terms and conditions beyond those set forth in the Agent’s Agreement. State Farm *offers* all Agents the extra rewards and benefits associated with being a Select Agent (co-op advertising monies, block assignments, *etc.*) in exchange for meeting additional criteria set by the Company (participation in the CRC, creation of a business plan, *etc.*). Agents who *accept* this offer by

meeting the criteria, thereby become entitled to receive the extra-contractual benefits. Agents who choose not to accept this offer do not receive these additional benefits, but neither do they assume any additional obligations. In all cases, they continue to receive all of the compensation and other benefits to which the Agent's Agreement entitles them.

* * *

By stipulation, the Parties agree that the benefits of being a Select Agent are: (1) eligibility to receive co-op advertising monies; (2) free designation in the Yellow Pages as a "Select Agent;" (3) eligibility to receive block assignments and internet leads concerning new customers; (4) eligibility to participate in additional bonus programs; and (5) registered Select Agents are eligible to receive mutual fund referrals. (Supp. Pretrial Statement (July 15, 2005).)¹ None of these benefits are promised to any Agent under the Agent's Agreement.

With respect to co-op advertising monies and free Yellow Pages designations, the Agent's Agreement is clear that any participation in the cost of an Agent's advertising will take place, if at all, at State Farm's sole discretion. Section I(F) states: "We will advertise, provide promotional materials, and participate in the cost of your advertising *in accordance with policies determined from time to time by us.*" (Emphasis added.) Thus, Agents have no contractually conferred right to receive either of these benefits. Even so, it is worth noting that State Farm does nonetheless participate in the cost of non-Select Agents' advertising in other ways. For instance, State Farm subsidizes the cost of non-Select Agents' participation in the Yellow Pages "display advertisement," and covers part of the cost associated with "trademark advertisements" also included in the Yellow Pages. (Proposed Findings ¶¶ 144-45.)

¹ In the Supplemental Pretrial Statement, Plaintiff also contended that there are two other benefits of the Select Agent Program; namely, that Select Agents are eligible to broker policies for Phoenix Life and AON insurance, and that Select Agents have greater underwriting flexibility than non-Select Agents. However, the evidence does not support either assertion. Indeed, the latter was directly refuted by Mr. Knapp on questioning from the Court. (See Knapp, July 26, Tr. 138:15-21.)

Similarly, the Agent's Agreement does not promise that all Agents will receive block assignments, internet leads or mutual fund referrals. Indeed, the Agreement is entirely silent on all three subjects. At trial, Clifford Mueller, one of Plaintiff's board members and a witness on the subject of Internet sales, admitted that the Company has discretion over whether or not to assign business to Agents, and over which Agents to assign it to. (Proposed Findings ¶ 141.) There is thus no contractual or other basis from which to conclude that State Farm is violating a promise made to non-Select Agents by declining to afford them these items.

Lastly, the portion of the Select Agent Program that makes eligibility to participate in additional bonus programs dependent on Select Agent status is directly authorized by the Agent's Agreement.² Section II(D) states: "Each of the Company reserves the right to fix and determine *the amount, extent, and conditions* of any bonuses, awards, prizes and allowances."³ (Emphasis added.) Accordingly, there is nothing in the contract which prohibits State Farm from providing the benefits of Select Agent status only to those Agents who choose to meet the criteria of the Program.

* * *

Plaintiff continues to advance its theoretical argument that there is something discriminatory about the Select Agent Program. But the evidence brought out at trial disproves Plaintiff's contention that the Program is not "reasonably available" to all Agents. Thus, even

² As the Court is well aware, it is State Farm's position that the entirety of the Select Agent Program is directly authorized by Section II(D) because it is a bonus designed to reward those Agents who go the extra mile and meet special incentive criteria set by the Company. For analytical completeness, however, State Farm notes that Section II(D) is a contractual truism. Even without it, State Farm would be free to institute whatever bonus and incentive programs it considered appropriate. There is no doctrine of contract law that prevents State Farm from giving *extra* benefits to Agents who do *extra* work. Thus, the particular benefits of the Select Agent program do not have to be semantically pigeon-holed within the "bonuses," "awards," "prizes," and "allowances" of Section II(D) for the Program to be permissible.

³ In the case of the AA3 and AA4, the same provision is found at Section II(C).

accepting *arguendo* Plaintiff's (false) premise that an incentive program has to be reasonably available to all to be permissible, Plaintiff's complaint fails.

At trial, Plaintiff offered just a single witness on the subject of the Select Agent Program, Mr. Knapp. Interestingly, Mr. Knapp made no allegation that he personally was unable to participate in the Select Agent Program. Quite the contrary, both at deposition and again at trial, he testified that he voluntarily made the considered business decision not to become a Select Agent. (Knapp Depo. 54:6-15 ("I have decided to pass on being a select agent. I didn't see any benefit to that to me, and I saw that it perhaps some significant costs to it."); *see also* Knapp, July 29, Tr. 520:14-20.) Mr. Knapp decided not to participate in the Program for just one reason: because he did not want to prepare a business plan. (Proposed Findings ¶ 140.) He did not testify that he was unable to prepare a business plan, or that the requirement was unreasonably onerous in some fashion. And for good reason; the undisputed evidence in the record demonstrates that the business plan requirement is readily achievable, and that no Agent has ever been denied participation in the Program simply for failure to prepare an adequate business plan. (*Id.* ¶¶ 138-39.) Plaintiff thus did not produce even a single witness to testify that the Select Agent Program was beyond his reach.

Although Plaintiff did not bother to offer the testimony of any of its members other than Mr. Knapp, several other board members were deposed during discovery. In no case did any of them claim that the Select Agent Program was not reasonably available to them. Quite the opposite in fact. Several testified that for one reason or another, they voluntarily chose not to become a Select Agent. For instance, Robert Lamphier, Plaintiff's President at the time this lawsuit was first brought, testified:

Q. You decided not to become a select agent because you did not want to participate in the Call [sic] Response Center; correct?

A. Yes.

Q. Again, that was your free choice; correct?

A. Yes.

Q. And you could have participated in the CRC if you wanted to?

A. Yes.

(Lamphier Depo. 56:19-57:5; Adams Depo. 22:15-23:22; Swift Depo. 222:13-22; Mueller Depo. 35:25-36:11.)

Struggling up this evidentiary hill, the best Plaintiff could do in its effort to show the Select Agent Program is not reasonably available to all Agents was resort to indirect, unsubstantiated testimony that Agents who service “inner city” areas have greater difficulty meeting the criteria for Select Agent status, in particular the now-eliminated profitability criteria, and the current life insurance production criteria. (See Proposed Findings ¶ 131.) To support this allegation, Plaintiff offered nothing more than the self-serving and entirely conclusory assertions of Mr. Knapp.⁴ It did not offer any data of any kind, nor did it even bother to call one of its members who could testify that he directly was unable to become a Select Agent for the reasons Plaintiff alleges.

Mr. Knapp’s testimony is thoroughly refuted by, among other things, itself. Unlike Mr. Swift who offered testimony to the same effect in connection with the Parties’ summary judgment papers, Mr. Knapp at least claimed to have some direct knowledge about the situation

⁴ Mr. Killingsworth, a former AFE with his own lawsuit against State Farm, offered similarly conclusory testimony on this point. (Killingsworth, July 26, Tr. 37:19-38:1.) Indeed, when the Court *sua sponte* noted the conclusory nature of Mr. Killingsworth’s statements, Plaintiff made no effort to remedy this failing. (*Id.* at 38:2-6.)

in inner city areas because his service area includes East St. Louis, Illinois. (Knapp, July 29, Tr. 499:13-18.) Yet, notwithstanding the fact that his service area includes precisely the demographic that supposedly makes Select Agent status unattainable, Mr. Knapp did not testify that this fact made it any more difficult for him personally to qualify as a Select Agent. As already stated, the only barrier to his becoming a Select Agent that Mr. Knapp mentioned was the business plan requirement, and even that barrier was entirely self-imposed.

Not only is there no serious evidence to support Plaintiff's allegations about the inaccessibility of the Select Agent Program to Agents serving inner city areas, the overwhelming body of evidence proves the contrary. Although State Farm does not keep statistics that specifically categorize "inner city" Agents, it does keep information that designates Agents by market area (*i.e.*, city, metro, suburban, rural) and by race. This uncontroverted evidence shows that Agent participation in the Select Agent Program does not vary significantly no matter how you slice the demographics. (*See* Def. Ex. 78.) Whether the Agent is in a city or rural area, whether he is White or Black, Select Agent participation rates do not vary materially. (*Id.*) For instance, in 2004, 81% of "City" Agents were Select, as compared to 75% of "Suburban" Agents, while 79.4% of Black Agents were Select as compared to 75.6% of White Agents. (*Id.*) The data thus unambiguously demonstrate exactly what State Farm has long argued -- that the Select Agent Program is (by design) an inclusive program and that there are no structural impediments to participation by any identifiable group or subgroup of Agents.

In effect, Plaintiff is asking this Court to issue an order denying the 76% of State Farm Agents who have chosen to become Select Agents the benefits and rewards they have earned by deciding voluntarily to meet the criteria State Farm has established for the Program, above and beyond the call of the Agent's Agreement. Alternatively, Plaintiff is asking the Court to make

State Farm treat the 24% of Agents who have opted not to participate in the Select Agent Program exactly the same as those Agents who did, and accord them benefits that they not only have not earned, but are stated nowhere in the Agent's Agreement.

When the issue is framed in this fashion, one is forced to ask for whom Plaintiff really speaks? Who are its members? Plainly, they are not the more than 12,000 State Farm Agents who have chosen to be Select Agents; nor are they the 94% of non-registered State Farm Agents who voluntarily selected a referral Agent under in the RRRD. Although Plaintiff grandly calls itself the "National Association of State Farm Agents," all indicators suggest it is anything but that. The question of who Plaintiff represents is significant because NASFA is before the Court asking for declaratory relief that will potentially affect all 17,000 State Farm Agents nationwide.

Throughout the course of this litigation, Plaintiff has studiously avoided answering this question. At trial, it offered absolutely no evidence bearing on how truly representative it is of State Farm Agents as a whole. Indeed, earlier in the life history of this lawsuit, and in response to Defendants' motion to compel its membership information, Plaintiff dropped its prayer for injunctive relief rather than disclose even the number of members it has to either to Defendant or to the Court. (*See* Pl.'s Supp. Opp'n to State Farm's Mot. to Compel Pl.'s Membership Info. (July 15, 2003).) The only evidence in the record as to the size of Plaintiff's membership suggests that only a tiny percentage of the Company's Agents are actually members of Plaintiff's organization. Defendants' Exhibit 19, a document produced to State Farm by Plaintiff in discovery, reflects the results of a survey that NASFA sent to all 16,000+ State Farm Agents, not just its members, in September 2002. Out of more than 16,000 questionnaires, how many

responses did the National Association of State Farm Agents get? Exactly 215, that is, from approximately 1.3% of State Farm's Agents.⁵

The issue of Plaintiff's (non-)representativeness is also germane because there are times when NASFA seemed intent on transforming this into a labor law matter in which State Farm was cast as the employer and Plaintiff played the role of a union speaking on behalf of all Agents. But the analogy is thoroughly inapt. As Plaintiff itself is so fond of insisting, each State Farm Agent is an independent contractor. They are not employees. The relationship between State Farm and its Agents is governed not by a single collective bargaining agreement, but rather by more than 16,000 individual agreements which, at least in the case of Agents operating under the AA3 and AA4 Agreements, are governed by the law of the particular state in which the Agent does business and by the common law of agency. The rules governing labor disputes thus do not apply even by analogy to this case.

The importance of the distinction is acute in the context of the Select Agent Program. Whatever the labor law consequences of treating unionized employees disparately, the law governing non-employee agents is clear that State Farm is privileged to treat them differently. The RESTATEMENT (SECOND) OF AGENCY makes the point clear. According to Comment (b) to Section 434, although a principal's "contract may prohibit[] him from interfering otherwise with the success" of one of its agents, the principal "is *privileged* to assist another of them in making a sale, and *has no duty to act impartially among them.*" (Emphasis added.)

The case law bears the point out. For instance, in *Bertera Chrysler Plymouth, Inc. v. Chrysler Corp.*, 992 F. Supp. 64 (D. Mass. 1998), the Court found there was no breach of contract or violation of the implied covenant of good faith where the Chrysler Corporation

⁵ In reply to a survey of retired State Farm Agents sent out at the same time, NASFA received only a total of 60 responses. (Def. Ex. 19.)

granted a particular request by one dealership, but summarily denied an identical request from a second dealership in the same area.

It must be said that among the conspicuous gaps in Plaintiff's case is the fact that it has never identified any authority standing even remotely for the "non-discrimination" principle among agents for which it now advocates.⁶ This three-year silence is more telling than any memorandum of law could be.

Of course, State Farm rejects the notion that it is behaving partially or discriminating among its Agents. On the contrary, the evidence shows that State Farm is acting impartially by giving them an equal opportunity to participate in the Program and enjoy its benefits. As Plaintiff's own witnesses testified, the choice of whether or not to participate in the Program lies squarely with the Agents themselves. If anything, the Agents who make the voluntary choice not to participate are themselves creating the distinction about which Plaintiff is complaining.

Because it has no serious contractual argument that the Select Agent Program violates the Agent's Agreement, Plaintiff's challenge then is to demonstrate that State Farm either adopted or implemented the Program in bad faith and thus violated an implied duty of good faith. The trouble for Plaintiff is that any such argument is foreclosed by the facts.⁷ There is not the

⁶ It is worth also considering just what the term "discrimination" means. According to BLACK'S LAW DICTIONARY, it means: "A failure to treat all persons equally *where no reasonable distinction can be found* between those favored and those not favored." 322 BLACK'S LAW DICTIONARY (emphasis added); *see also* 377 WEBSTER'S COLLEGE DICTIONARY (defining discriminate as "to make a distinction in favor of or against a person on the basis of the group or class to which the person belongs, *rather than according to merit.*") (emphasis added). Viewed literally, there is thus nothing discriminatory about the Select Agent Program. To the extent it can be said to distinguish among Agents, it does so according to merit. There is thus an eminently reasonable basis for the distinction and thus no "discrimination."

⁷ Facts aside, Plaintiff's good faith attack on the Select Agent Program also has serious legal problems. Indeed, not all states would even recognize it. Under New York law, for example, where (as here) a contract reserves to one party complete discretion over bonuses and rewards, a good faith claim will not lie even if that discretion is exercised arbitrarily and capriciously. *Sathe v. Bank of N.Y.*, 1990 U.S. Dist. Lexis 5012, at *11-12 (S.D.N.Y. 1990).

The point is key because there are substantial choice of law issues imbedded in any good faith claim in this case. Although the AA97 Agreement contains a choice of law provision in favor of Illinois law, neither the AA3 nor AA4 Agreement contain any such provision. The good faith claims of Plaintiff's members who continue to operate under

slightest hint in the record that State Farm acted in bad faith in connection with the Select Agent Program. Indeed, the overwhelming weight of the evidence points in precisely the opposite direction -- to a conclusion that State Farm acted in a manner consistent with sound business judgment and with a view to making the Program as accessible as possible to all Agents.

The record demonstrates that the Company adopted the Select Agent Program for legitimate and rational reasons; *i.e.*, in good faith. Mr. Wright offered unchallenged testimony articulating the reasons the Company considered each of the criteria for becoming a Select Agent to be in the best interests of the Company and of the Agents. (Proposed Findings ¶ 124 (CRC), ¶ 127 (licensed staff), ¶ 129-30 (quality), ¶¶ 135 (product availability), ¶ 137 (business plan).)

The record is just as conclusive that each of these criteria is readily achievable by the vast majority, if not all, Agents. Indeed, Plaintiff did not offer any evidence (or even argument) suggesting that the CRC, licensed staff or product availability criteria were unattainable by Agents who chose to meet them. Instead, Plaintiff focused its attack on the quality and business plan requirements. As already set forth above, State Farm has amply demonstrated the fallacy of Plaintiff's argument that Agents serving "inner city" areas were disabled from becoming Select Agents because of the quality criteria. In reality, the actual facts demonstrate that all Agents enjoyed an equal opportunity to participate in the Program regardless of the underlying demographics. The quality criteria thus did not disadvantage any group or subgroup of Agents.

With respect to the business plan, Plaintiff's bad faith argument turns on the contention that it was administered arbitrarily. Yet, the record shows, without contradiction, that the business plan requirement was exceedingly easy to meet. State Farm provided detailed guidelines, templates, instructions and models for Agents to follow on the Agent's intranet.

the AA3 and AA4 Agreements would have to be evaluated under the individual laws of the 47 states where Plaintiff has at least one member.

(Proposed Findings ¶ 138.) Mr. Knapp, Plaintiff's lone witness, complained about the alleged arbitrariness of the business plan requirement, but then was forced to admit that he had never even bothered to look at these materials. (*Id.* ¶ 140.) Of course, Agents were not obligated to follow the models that State Farm made available to them. They were still free to submit any kind of business plan that they saw fit. (*Id.* ¶ 138.) And most significantly, the evidence demonstrates that there is not a single case in which an Agent failed to qualify as a Select Agent because his business plan was deemed unacceptable. (*Id.* ¶ 139.) Accordingly, there is no basis to conclude that business plan requirement operated in an arbitrary manner to the detriment of Agents.

The conclusion is unmistakable: there is nothing arbitrary or capricious about any aspect of the Select Agent Program. Plaintiff's good faith claim must be rejected right along with its contract claim.

III. Restrictions on the Submission of New Business

Plaintiff's argument that State Farm's restrictions on the submission of new business violated the Agent's Agreement and/or the implied covenant of good faith is similarly based on faulty premises of both fact and law. As it did in connection with the Select Agent Program, Plaintiff offered the testimony of only a single trial witness on the subject, this time Mr. Swift. On direct examination, Mr. Swift testified that throughout his tenure as a State Farm Agent, he was encouraged to write as much new business as he could. (Swift, July 28, Tr. 264:2-17.) Contradicting himself, he then testified that there were occasions when he was not permitted to write as much new business as he could following "natural disasters, like hurricanes or earthquakes." (Swift, July 28, Tr. 18-24.) On cross-examination, Mr. Swift also testified that in the 1990s, State Farm stopped him from soliciting selling commercial insurance policies

covering apartment buildings, because, in the Company's view, such business was no longer profitable. (Proposed Findings ¶ 163.)

Mr. Swift's statements are not only internally inconsistent, they are also contradicted by the stipulated facts. According to the stipulations agreed upon in the Joint Pretrial Statement: (1) unlike many other enterprises, volume and profitability are sometimes at odds with each other in the insurance industry (JPTS, Stip. No. 41); (2) from time to time in the past, State Farm has imposed specific limitations on the number of new applications Agents may submit in order to minimize the Company's risk exposure (JPTS, Stip. No. 42; *see also* PR ¶¶ 178-187); and (3) historically, these previous limitations were occasioned by unforeseen or unforeseeable events like natural catastrophes *or economic downturns*. (JPTS, Stip. No. 43) (emphasis added.)

The record establishes without contradiction that the restrictions challenged by Plaintiff in this case were implemented in 2002 in response to unprecedented operating losses of over eight billion dollars in 2000 and 2001, including billions of dollars of losses on the sale of new insurance policies. (Proposed Findings ¶ 167.) The losses were occasioned by a convergence of several negative trends: unprecedented claim severity, rate inadequacy, reduced investment income, and rapid growth. (*Id.* ¶ 168.) Significantly, on cross-examination, and consistent with the Preamble to the Agent's Agreement, Mr. Swift agreed that it is in the mutual interest of State Farm and of the Agents to maintain the operations of the Company on a profitable basis in order assure that the Company remains sufficiently strong financially to protect policyholders' interests. (*Id.* ¶ 160.) The factual basis of, and business rationale behind, the restrictions imposed in 2002 are thus either unchallenged or admitted.⁸

⁸ In any event, the restrictions have now been lifted in all but three jurisdictions: Louisiana, Florida, and Texas. (Proposed Findings ¶ 172.) And of these remaining three, Texas is out of the case because the entity that has imposed restrictions in that state, State Farm Lloyd's, is not a party to this lawsuit. (*Id.* ¶ 181 n.4.)

Legally, the Courts are unanimous that the Agent's Agreement specifically gives State Farm the right to restrict or limit Agents' submission of new business. The relevant sections of the Agreement, Sections I(L) and I(M), have been analyzed in at least three separate jurisdictions: Florida, Louisiana, and California. In each case, one or more State Farm Agents challenged Company programs limiting the amount of new business they could produce. In *Hartman v. State Farm Mut. Auto. Ins. Co.*, Case No. 93-8084 (S.D. Fla. 1993), *aff'd*, 77 F.3d 496 (11th Cir. 1996), for example, a State Farm Agent sought relief from State Farm programs enacted after Hurricane Andrew that, among other things, limited the amount of new homeowner's insurance applications Agents could submit. On State Farm's motion to dismiss for failure to state a claim, the District Court held that "according to the plain and ordinary meaning of the contract," State Farm may place restrictions on the amount of home or fire applications its agents may solicit. Final Order of Dismissal With Prejudice at 8.⁹ Citing the language of Section I(L) and I(M) of the AA3 Agreement, the Court reasoned: "This language clearly and unambiguously reserves to State Farm the right to control the amount of risk assumed by its companies through their intermediary agents." *Id.* at 9.

Similarly, in *Hemmans v. State Farm Ins. Co.*, 653 So. 2d 69 (La. Ct. App. 1995), a State Farm Agent challenged restrictions on his ability to submit new automobile insurance applications under the AA3 and AA4 Agreements. Although the jury returned a verdict in plaintiff's favor, the Court of Appeals threw out the verdict. It found the limitations "within the authority of State Farm under the contract." *Id.* at 74. The appellate court's reasoning was straightforward: "In Section I, Paragraph L, State Farm specifically retains the right to prescribe all rules governing the acceptance of all risks and the adjustment of losses. Paragraph M limits

⁹ Submitted with the Joint Pretrial Statement.

the agent's authority to obligate State Farm except as authorized in the agreement or by the rules adopted by the Company." *Id.* As a result, the Court of Appeals held that "according to the plain and ordinary terms of the contract," State Farm may place a restriction on the type and amount of applications Agents may solicit." *Id.* at 75.

In *Appling v. State Farm Mut. Auto. Ins. Co.*, No. C97-1569 MJJ (N.D. Cal. 1999), *aff'd* 340 F.3d 769 (9th Cir. 2003), a multi-state group of 73 State Farm Agents (who had signed the AA3 and AA4 Agreements) challenged restrictions adopted in response to losses occasioned by Hurricane Andrew and then compounded by the Northridge (California) Earthquake. The District Court granted State Farm's motion for summary judgment holding:

Section I(L) of the contracts clearly and unambiguously reserves to State Farm the right not only to control the amount of risk assumed by its companies through their intermediary agents, it expressly permits State Farm to enact, without limitation, any "rules" governing the "acceptance, renewal, rejection, or cancellation" of such risks and to prescribe "all premiums, fees, and charges for insurance." Moreover, section I(M) clearly precludes the agents from binding State Farm in any manner not expressly authorized by the company in writing.

Slip. op. at 7-8.¹⁰ The ruling was upheld by the 9th Circuit Court of Appeals which stated: "This provision is patently clear: State Farm has the right to prescribe rules governing risks. Because the exposure management program is a program governing risks, it is permissible under the Risk Provision." 340 F.3d at 779.¹¹ There is no material difference between these cases and the case at bar. The contract provisions at issue are identical. The facts are equivalent. And the result should be the same. Plaintiff's breach of contract claim must be rejected.

¹⁰ Submitted with the Joint Pretrial Statement.

¹¹ The language of Section I(L) differs somewhat between the AA3/4 Agreements and the AA97 Agreement. The *Appling* case specifically held the difference irrelevant in determining whether or not State Farm has the right to impose restrictions. *Slip. op.* at 9-11.

Having no sustainable claim under the Agent's Agreement itself, Plaintiff is once again forced to argue vague notions of bad faith. Rather than take issue with the general decision to institute limitations, Plaintiff seems to be arguing that the way the limitations were implemented was arbitrary or capricious, and thus a violation of good faith. Faced with unimpeached testimony from Mr. Wright concerning the process and criteria by which the restrictions were implemented, Plaintiff turns to the deposition testimony of Mary Bitzer, State Farm's Regional Vice President for the Central Zone, in search of support. As Plaintiff would have it, the fact that Ms. Bitzer supposedly testified that State Farm followed no "set standard or criterion" in establishing the limitations somehow shows that they were *per se* capricious. (See Garner, Aug. 1, Tr. 695:4-23.) The trouble for Plaintiff is that, under very general questioning from Mr. Garner, Ms. Bitzer actually testified that the limitations in her zone, which varied from state to state, were decided upon after thorough consultation among all the responsible people in her zone and at corporate headquarters, and after taking account of all relevant information, *including the interests of Agents*. (Bitzer Depo. 11/25-12/13, 27/9-23.) The fact that no pre-codified procedures were followed, or that there was no rigid set of pre-ordained criteria, cannot make the Company's conduct arbitrary. Rather, Ms. Bitzer and the rest of State Farm's top management did what insurance executives necessarily do -- they relied on the reports of the underwriting and actuarial experts on State Farm's staff and their own knowledge of the particular markets within their jurisdiction, and they used their informed business judgment to determine what level of new business the Company could profitably sustain in each of the affected markets. There is thus no genuine evidence to support Plaintiff's assertion that the limitations were in any way unreasonable, or imposed arbitrarily.

IV. Brokering Business for Other Insurers

The starting point for evaluating Plaintiff's prayer for a declaration that State Farm must permit Agents to broker business for other insurers is, of course, the Agent's Agreement. Under Section I(G)

[Agents] *will not* directly or indirectly write or service insurance for any other company, other than a State Farm subsidiary or affiliate or through any governmental or insurance industry plan of facility, or for any agent or broker, *except in accordance with the terms of any written consent we may give you.* (Emphasis added.)

The Agreement thus provides that Agents must solicit business *exclusively* for State Farm, unless the Company gives them written permission to produce business for another insurer.

Plaintiff does not dispute this point. Indeed, it concedes the fact. (*See Proposed Findings ¶ 184.*) Plaintiff argues instead that State Farm has exercised its contractual authority capriciously in violation of the implied covenant of good faith. The record, however, does not contain any evidence of bad faith on State Farm's part. Rather, the evidence reveals that State Farm has a policy concerning brokering that is reasonable, supported by legitimate business concerns, and consistently applied; *viz.* Agents are not permitted to compete with State Farm by brokering business for the Company's competitors. Indeed, Agent exclusivity lies at the heart of the business model around which State Farm has built itself for more than 50 years. (*Proposed Findings ¶ 182; see also Lamphier Depo. 18:2-9 (admitting that agent exclusivity gives State Farm a "marketplace advantage").*)

The justification for State Farm's policy prohibiting brokering in these circumstances is self-evident. Why would any company make one of its principal assets -- in this case, its highly-skilled, highly trained corps of independent contractor Agents -- freely available to a competitor? In any event, the rationale behind the policy is amply set out in the record. At trial, Mr. Fisher testified concerning the business reasons for the policy at some length, including State Farm's

considerable investment in its exclusive Agents, the potential for policyholder confusion, the possibility of divided Agent loyalty, the difficulty protecting trade secrets, *etc.* (Proposed Findings ¶¶ 185-88.) Plaintiff has not challenged these reasons, nor has it identified a single instance in which State Farm has deviated from this policy. The evidence is plain: every time State Farm Agents have been authorized to write products for other insurers, whether in the case of Baldwin Mutual or Phoenix life or any of the others, State Farm was not selling, and had no plans to sell, similar products to the public at the time or in the foreseeable future. (*Id.* ¶¶ 193-98.) Still more, in the cases of Phoenix Life, Assurant (formerly Fortis), and Aon, State Farm entered a strategic business alliance with these companies and thus was in a position to put whatever safeguards it deemed necessary in place to protect its interests. (*See id.* ¶ 197-98; *see also* Fisher, July 27, Tr. 223:8-17.)

Not only has Plaintiff not challenged the rationale behind State Farm policy, its witnesses have expressly admitted that it is reasonable for State Farm to deny Agents' requests to broker business for competing insurers. At trial, for example, Mr. Mueller testified that it would be reasonable for State Farm to deny requests to broker for "direct multiliner competitor[s]." (Mueller, July 27, Tr. 159:3-8.) At deposition, another of Plaintiff's board members, Mr. Stephen Adams agreed. (Adams Depo. 86:14-20.) Of course, Plaintiffs quibble about what kind of insurers really constitute "competition" and argue that smaller, single-line companies do not count. The trouble for Plaintiff is that at deposition, and wholly unprompted by the question, Mr. Swift stated: "Well, State Farm is in direct competition with *any other insurance company.*" (Swift, July 27, Tr. 145:21-146:3 (emphasis added).) To this effect, Mr. Fisher testified that the size of the competitor is immaterial because State Farm competes for customers on a policy-by-

policy basis. Hence, every policy that a competitor, regardless of size, is able to sell, is a policy that State Farm has potentially lost. (Proposed Findings ¶ 188.)

Setting aside the Parties' generalized dispute about State Farm's policy against brokering, the fact is that there are only two specific brokering requests in the record. The first is Mr. Swift's written request to State Farm in November 2002 nominally written on behalf of all State Farm Agents, not just NASFA members. (Def. Ex. 79.) Mr. Swift admitted at trial that his letter requested permission to broker for all other insurance companies, including direct multi-line competitors of State Farm. (Proposed Findings ¶ 205.) Thus, by Plaintiff's own admission it was perfectly reasonable for State Farm to deny this request.

The only other request in the record is Mr. Mueller's October 2002 e-mail asking for permission to write fire insurance for "a company other than State Farm." (Pl. Ex. 92.) On cross-examination, Mr. Mueller admitted that if State Farm had responded to his e-mail with a "simple yes," he "would have been free to place fire insurance with any company other than State Farm." (Mueller, July 27 Tr. 171:2-8.) To be sure, on direct examination, Mr. Mueller testified that during a phone conversation with Mr. Bill Whitney, he limited his request to two regional companies, Northern Neck and Loudon Mutual. (Mueller, July 27, Tr. 155:13-18.) But this testimony is not only inconsistent with the wording of his e-mail, it was directly contradicted by Mr. Whitney himself. (Whitney, July 27, Tr. 192:18-25.) In any event, on redirect by his own counsel, Mr. Mueller testified that he told Mr. Whitney he wanted to broker business for other companies "such as" Northern Neck and Loudon Mutual; *i.e.*, his request was not limited to just those two or any other specifically identified companies. (Mueller, July 27, Tr. 182:8-14.)

However these disputed facts are viewed, the undisputed record proves that State Farm did not act in bad faith in denying Mr. Mueller's request. Mr. Whitney testified without

contradiction that at the time he denied Mr. Mueller's request in October 2002, he was aware, based on existing trends, that State Farm was very likely to resume selling fire insurance in Virginia "as early as the end of the year." (Proposed Findings ¶ 201.) Thus, when he denied Mr. Mueller's request, Mr. Whitney knew State Farm was going to be competing for these same customers within two months.

In addition, the record shows that upon receiving Mr. Mueller's request, Mr. Whitney did not simply reject it out of hand. He took the time to call agency personnel at corporate headquarters in Bloomington to make sure that the Company's policy was still what he remembered; *i.e.*, no brokering for competitors. (Proposed Findings ¶ 202.) Only then did he reply to Mr. Mueller. To the extent Mr. Whitney went out of his way to make sure he was doing the right thing, he cannot be guilty of bad faith.

At the end of the day, Mr. Mueller's e-mail is the only individual brokering request in the record. Thus, setting aside the facts for a moment, even if Mr. Whitney were guilty of bad faith towards Mueller, it still would not form a proper basis for the declaratory relief Plaintiff is seeking. Simply put, Mr. Mueller's isolated, individual experience is irrelevant to this associational standing case. NASFA is the Plaintiff here, not Mr. Mueller. And NASFA has no standing to press claims which turn on the particular experiences of its individual members. Such claims turn on individualized proof of just the sort that is inconsistent with associational standing. *See* Order Denying Defendants' Motion to Dismiss Complaint at 10 (Oct. 22, 2002) (citing *Dupont Circle Citizens Ass'n v. Barry*, 455 A.2d 417 (D.C. 1983)). Furthermore, in a case seeking broad declaratory relief, it would not be reasonable to treat a single incident involving just one of State Farm's more than 16,000 Agents as evidence of systematic bad faith

in the application of the Company's policy on brokering of business for other insurers -- even if the incident involved bad faith, which the denial of Mr. Mueller's request did not.

For each and every one of these reasons, Plaintiff's prayer for declaratory relief on this count must be denied.¹²

V. Mandatory Attendance at Annual Ethics Meetings

Plaintiff's last claim, challenging State Farm's requirement that Agents attend an annual meeting on matters of ethics and legal compliance, must fail along with all its other complaints.

The material facts are not in dispute. State Farm requires its Agents to attend a half-day session on ethical and legal obligations once every year. The meeting lasts for half a day and takes place in an Agent's AFO. If an Agent cannot attend the meeting on the date scheduled for his AFO, he can attend the meeting at any of the other AFOs in his state. And if an Agent is unable to participate due to illness or like circumstance, State Farm works with that Agent to find a solution. (Proposed Findings ¶¶ 231-33.)

The reasonableness of this minimal requirement is self-evident, and is underscored by the undisputed facts of record. State Farm's former chief agency officer, Mr. Wright, offered unimpeached testimony as to the origin and rationale of the requirement and showed how and why it advances the interests of the Company, the Agents and the policyholders. (Wright, July 29, Tr. 631:2-635:17.) And Plaintiff's lone witness on the subject, Mr. Knapp, readily agreed that (1) "insurance is a closely regulated business;" (2) "State Farm and the agents must deal equitably with policyholders as to rates and claims, be trustworthy in handling money, avoid false advertising and unfair practices and refrain from any action that would result in violation by

¹² In both the *Appling* and *Hartman* cases, Plaintiffs similarly argued that State Farm wrongfully denied their request to broker business for other insurers even as restrictions were pending. In both cases, the courts rejected Plaintiffs' arguments. *Appling*, *slip. op.* at 5, 11; *Hartman*, *slip. op.* at 23.

State Farm or any agent of any applicable law or regulation;” (3) “an agent needs to be aware of the applicable laws and regulations and applicable ethical standards;” and (4) “[a]ll of the agents need to be aware of any changes in the applicable laws, regulations or standards.” (Knapp, July 29, Tr. 620:24-621:16.)

Nonetheless, Plaintiff continues to object to the requirement that Agents attend a meeting designed specifically to further the goals Plaintiff readily agrees are unobjectionable. Indeed, when pressed about the logic of Plaintiff’s position, Mr. Knapp even went so far as to say that while State Farm could send him information on matters of ethics and legal compliance that it considers important, he would have no obligation whatsoever to actually read it. (Knapp, July 29, Tr. 628:17-21.) Mr. Knapp thus effectively admitted that the only way State Farm can be certain that its Agents have read or heard the information the Company provides them regarding their ethical and legal obligations is by requiring their attendance at the annual meeting.

The Agent’s Agreement and the applicable law authorize State Farm to require such attendance. The Agent’s Agreement plainly underscores the importance of matters of ethics and legal compliance. The very first paragraph of the Preamble, for example, states: “It is in our mutual interest to serve the insuring public [and] to comply with all applicable laws” The second paragraph is even more explicit:

Insurance is a closely regulated business. The Companies and agents must deal equitably with policyholders as to rates and claims, be trustworthy in handling money, avoid false advertising and unfair practices, and otherwise act in a lawful manner.

The first operative provision of the Agent’s Agreement echoes the the Preamble. Among Agents’ duties, Section I(A) states that they must “comply with all laws and regulations, and cooperate with and advance the interests of the Companies, the agents, and the policyholders”

Section I(B) of the Agent's Agreement, invoked by Plaintiff, does not change the result suggested by these provisions. The promise that, as independent contractors, Agents have "full control" over their "daily activities" does not mean that they have absolute control over every second of every work day. To the contrary, understood in its ordinary sense, the phrase "daily activities" refers to the types of conduct Agents are engaged in on a daily basis; *i.e.*, soliciting insurance, servicing policyholders, *etc.* This conclusion is supported by the case law. In *Samson v. Harvey's Lake Borough*, 881 F. Supp. 138 (M.D. Penn. 1995), the U.S. District Court specifically held that required attendance at meetings does not constitute control over one's "daily work activity" so as to violate one's independent contractor status. 881 F. Supp. at 143.

The result is the same here. Agents remain free to decide when to open their doors, when and how to solicit business, when to take a day off, and when to close at night. In other words they retain "full control over [their] daily activities."

Even if the express terms of the Agent's Agreement did not specifically authorize State Farm to require Agents' attendance at the annual ethics/compliance meeting, the requirement is nonetheless fully within State Farm's rights under the common law of agency. Governing precepts of agency law provide that principals are privileged to issue reasonable directions to agents, and agents must obey, whether or not there is a written contract between the parties. Indeed, when there is a written agency agreement, the common law rule is actually deemed part of the contract. RESTATEMENT (SECOND) OF AGENCY, Intro. Note, Ch. 13., Topic 1.

Comment b to Section 14 of the RESTATEMENT reinforces this point.

If it is otherwise clear that there is an agency relation ... the principal, although he has contracted with the agent not to exercise control and to permit the agent the free exercise of his discretion, nevertheless has the power to give lawful directions which the agent is under a duty to obey if he continues to act as such.

RESTATEMENT (SECOND) OF AGENCY § 14, cmt. b; *see also* AM. JUR. § 213 (“An agent has a duty to obey all reasonable instructions and directions....”) Under these rules, principals may issue instructions to agents that *go beyond the terms of preexisting agreements* without breaching the contract. *See, e.g., Hanover Insurance Co. v. St. Paul Fire & Marine Insurance*, 359 F. Supp. 591 (W.D. La. 1973); *Walker v. John Hancock Mut. Life Ins. Co.*, 80 N.J.L. 342 (N.J. 1911).


Under the RESTATEMENT and the case law, the touchstone is the reasonableness of the principal’s instruction to the agent. Based on the evidence presented in this case, State Farm’s instruction to its Agents -- that they attend one meeting a year, for half a day, on the ethical and legal obligations with which the law, and the Company, demand compliance -- is eminently reasonable. There is thus no breach of contract.

Conclusion

For the reasons stated in this memorandum, as well as those set forth in Defendants’ Proposed Findings of Fact and Conclusion of Law, Plaintiff’s request for a declaratory judgment should be denied in its entirety.

Respectfully submitted,

By its attorneys,



Paul S. Reichler, DC Bar No. 185116
Lawrence H. Martin, DC Bar No. 476639
Sarah A. Altschuller, DC Bar No. 489202
FOLEY HOAG LLP
1875 K Street, N.W., Suite 800
Washington, DC 20006
(202) 223-1200

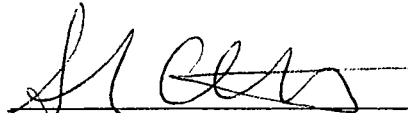
Dated: September 2, 2005

CERTIFICATE OF SERVICE

I hereby certify that on this the 2nd day of September, 2005, a true and correct copy of (1) **Defendants' Proposed Findings of Fact and Conclusion of Law**; and (2) **Defendants' Post-trial Memorandum** were served upon the following attorneys of record for Plaintiff herein, by Federal Express:

Allan P. Hillman, Esq.
NEUBERGER, QUINN, GIELEN,
RUBIN & GIBBER, P.A.
One South Street, 27th Floor
Baltimore, MD 21202-3282

W. Michael Garner, Esq.
DADY & GARNER, P.A.
4000 IDS Center
80 South Eighth Street
Minneapolis, MN 55402-2204


Sarah A. Altschuller