Insurance Law Update

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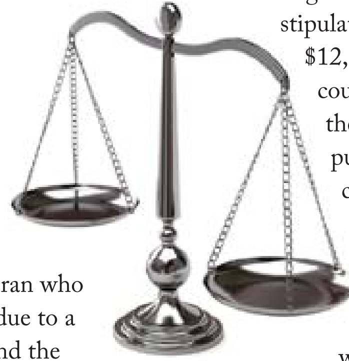
The past few months have seen both state and federal opinions addressing the scope of Brandt fees, the limitations imposed upon automobile insurers to consider diminution when covering a claim, the reliance by insurers upon the genuine dispute doctrine, reaffirmation that triable issues of fact will preclude an insurer's motion for summary judgment regarding its duty to provide coverage, inter-insurance disputes among primary and excess insurers, and reaffirmation that intentional conduct by an insured precludes coverage.

BRANDT ATTORNEY FEES AWARDED BY A TRIAL COURT AS COMPENSATORY DAMAGES IN AN INSURANCE BAD FAITH CASE MAY BE CONSIDERED IN DETERMINING WHETHER THE DISPARITY BETWEEN COMPENSATORY DAMAGES AND PUNITIVE DAMAGES RENDERS THE PUNITIVE DAMAGES AWARD UNCONSTITUTIONALLY EXCESSIVE

In the case styled Nickerson v. Stonebridge Life Ins. Co. (2016) 63 Cal.4th 363, 203 Cal. Rptr.3d 23, the California Supreme Court held on June 9, 2016, that in determining whether a punitive damages award is unconstitutionally excessive, Brandt fees may be included in the calculation of the ratio of punitive to compensatory damages, regardless of whether the fees are awarded by the trier of fact as part of its verdict or are determined by the trial court after the verdict has been rendered.

In this case, the issue before the Supreme Court concerned the proper calculation of the punitive-compensatory ratio when the parties agreed to have the trial court determine a component of the plaintiff's compensatory damages—here, the attorney fees plaintiff was compelled to expend to obtain the insurance benefits to which he was entitled to receive pursuant to the Brandt doctrine—after, rather than before, the jury rendered its punitive damages verdict. The Court of Appeal held that Brandt fees awarded in this manner must be excluded from the calculation in determining whether, and to what extent, the jury's punitive damages award exceeds constitutional limits. The Supreme Court conclude that the Court of Appeal erred.



Plaintiff was a disabled veteran who was confined to a wheelchair due to a spinal cord injury. While he and the wheelchair were being lowered from a van, plaintiff fell to the pavement, suffering a broken leg. He was taken by ambulance to the emergency room and then moved to a unit in a Veterans Administration hospital. At the time of the accident, plaintiff was insured under a policy issued by Stonebridge Life Ins. Co. and which paid plaintiff a daily benefit for medically necessary hospital stays. The insurer paid benefits for plaintiff's first 19 days in the hospital, but denied benefits for the remaining 90 days while Plaintiff was in the hospital. The insurer maintained that only the first 19 days qualified as "necessary treatment" within the meaning of the policy.

Plaintiff sued the insurer for breach of contract and bad faith. Finding that the policy clause limiting coverage to medically necessary treatment was unclear and inconspicuous and thus unenforceable, the trial court entered a directed verdict for Plaintiff in the amount of $31,500 in unpaid benefits on the breach of contract claim. A jury found for Plaintiff on the bad faith claim and awarded $35,000 in emotional distress damages and $19 million in punitive damages. Neither party presented evidence to the jury on the attorney fees Plaintiff incurred in recovering contract damages.

In California, such fees are recoverable as an element of compensatory damages for insurer bad faith under the California Supreme Court's landmark decision in Brandt v. Superior Court (1985) 37 Cal.3d 813, 817, 210 Cal.Rptr. 211. In Brandt, the California Supreme Court held that when an insurance company withholds policy benefits in bad faith, attorney fees reasonably incurred to compel payment of the benefits are recoverable as an element of a plaintiff's damages. Brandt fees, as they are known in California, do not include those attributable to the bringing of the bad faith action itself.

The parties stipulated before trial that if Plaintiff should prevail, the trial court could determine the amount of Brandt fees. Following trial, Plaintiff and the insurer stipulated that Plaintiff was entitled to $12,500 under Brandt, and the trial court awarded that amount. After the jury awarded $19 million in punitive damages, the trial court conditionally granted a new trial unless the Plaintiff accepted a reduction in the punitive award to $350,000—which, at ten times the bad faith damages, was the maximum that the trial court believed would pass constitutional boundaries. In calculating the 10 to 1 ratio, the court included in the compensatory damages denominator only the $35,000 in emotional distress damages awarded on the bad faith claim. The court rejected Plaintiff's contention that the denominator also should include the $12,500 in Brandt fees. Plaintiff refused to accept the reduced award and appealed. The insurer also appealed.

In our judicial system, compensatory damages are intended to redress the concrete loss that the Plaintiff has suffered by reason of the defendant's wrongful conduct, while punitive damages operate as "private fines" intended to punish the defendant and to deter future wrongdoing. When a punitive damages award is grossly excessive in violation of the due process clause, the appropriate order is for an absolute reduction in the award, rather than a conditional reduction with the alternative of a new trial, *i.e.*, a remittitur, since once a maximum constitutional award has been determined, a new trial on punitive damages would be futile.

To determine whether a jury's award of punitive damages is grossly excessive in violation of the due process clause, reviewing courts must consider, among other factors, whether the "measure of punishment is both reasonable and proportionate to the amount of harm to the plaintiff" by comparing the amount of compensatory damages to the amount of punitive damages, and absent special justification, ratios of punitive damages to compensatory damages that greatly exceed nine or 10 to one are presumed to be excessive and therefore unconstitutional.

The Supreme Court, for the first time, found that a plaintiff's compensatory damages may include the Brandt fees the plaintiff was compelled to expend to obtain the insurance benefits to which he was entitled, and that such attorney fees may be included

in the calculation of the ratio of punitive to compensatory damages to determine whether the punitive damages award is "grossly excessive" in violation of the due process clause, even when the fees are awarded by the trial court after the jury has rendered its verdict.

The Supreme Court found no reason to exclude the amount of Brandt fees from the constitutional calculation merely because they were determined, pursuant to the parties' stipulation, by the trial court after the jury rendered its punitive damages verdict. On the contrary, to exclude the fees from consideration would mean overlooking a substantial and mutually acknowledged component of the insured's harm. The effect would be to skew the proper calculation of the punitive-compensatory ratio, and thus to impair reviewing courts' full consideration of whether, and to what extent, the punitive damages award exceeds constitutional bounds.

MOTOR VEHICLE INSURER DID NOT BREACH ITS INSURANCE POLICY WHEN IT ELECTED TO REPAIR AN INSURED DAMAGED VEHICLE, SINCE THE POLICY CONTAINED NO PROVISION REQUIRING IT TO PURSUE ITS INSURED'S DIMINISHED VALUE CLAIM

In the case styled James B. Copelan and Brian M. Lowenthal v. Infinity Insurance Company and Liberty Mutual Fire Insurance Company (2016) -- F.Supp.3d --, 2016 WL 3398408, the United States District Court for the Central District of California held on June 14, 2016, that a motor vehicle insurer did not breach its insurance policy, under California law, when it elected to repair an insured damaged vehicle, since the policy contained no provision requiring it to pursue its insured's diminished value claim.

Plaintiffs contended that their auto insurance policies entitled them to diminished value or stigma damages, rather than simply repair of their damaged automobiles. They alleged in their suit causes of action against their insurers for failing to provide diminished value damages.

Plaintiffs' entire case was premised on the idea that they were entitled to diminished value or stigma damages. However, Plaintiffs were unable to point to anywhere in their individual policies with their insurers that provided such an entitlement. Plaintiffs failed to cite any case law that established that diminished value or stigma damages were encompassed in the policies' insuring clause for "physical damage to tangible property." Rather, the Ninth Circuit has specifically held that the insertion of the word "physical" into the definition of "property damage" eliminated any possibility that intangible economic losses could constitute "property damage." Because neither insurers' policies covered third-party diminished value claims, the insurers' coverage was limited to repairing the damages to the vehicles.

A GENUINE DISPUTE REGARDING THE EXTENT OF DAMAGE TO A HOME AND REQUIRED REPAIRS PRECLUDED BAD FAITH LIABILITY ON PART OF THE INSURER

In the case styled Paslay v. State Farm General Insurance Company (2016) 248 Cal. App.4th 639, 203 Cal.Rptr.3d 785, the Court of Appeal, Second District, Division 4 held on June 27, 2016, that although triable issues of fact existed regarding whether the insurer breached the insurance contract by refusing to pay for repairs, a genuine dispute about coverage entitled the insurer to summary judgment on the insured's bad faith and elder abuse claims where the insureds prematurely commenced repairs precluding their insurer from adequately investigating the nature and cause of the loss.

The insureds, Clayton and Traute Paslay, sought coverage under their homeowners property insurance policy for water infiltration damage resulting from the failure of a roof drain during a rain storm. The insurer, State Farm, did not contest coverage for water infiltration damage, but for damage to the master bathroom and ceiling drywall that the insurer contended did not result from water infiltration related to the storm. The Paslays sued State Farm for breach of contract, insurance bad faith, and, since Traute Paslay was 80-years-old, elder abuse under the California Elder Abuse Act.

In general, the obligation imposed on an insurer under the covenant of good faith and fair dealing is not the requirement mandated by the terms of the policy itself; it is the obligation under which the insurer must act fairly and in good faith in discharging its contractual responsibilities. In the context of a bad faith claim, an insurer's denial of or delay in paying benefits gives rise to tort damages only if the insured shows the denial or delay was unreasonable. An insurer denying or delaying the payment of policy benefits due to the existence of a genuine dispute with its insured as to the existence of coverage liability or the amount of the insured's coverage claim is not liable in bad faith, even though it might be liable for breach of contract, because when there is a genuine issue as to the insurer's liability under the policy for the claim asserted by the insured, there can be no bad faith liability imposed on the insurer for advancing its side of that dispute. An insurer may obtain summary adjudication of a bad faith cause of action by establishing that its denial of coverage, even if ultimately erroneous and a breach of contract, was due to a genuine dispute with its insured. However, the genuine dispute doctrine does not relieve an insurer of its obligation to thoroughly and fairly investigate, process and evaluate the insured's claim. A genuine dispute, precluding a finding of bad faith, exists only where the insurer's position is maintained in good faith and on reasonable grounds. Reasonable grounds for an insurer's position, precluding a bad faith claim under the genuine dispute doctrine, include reasonable reliance on experts hired to estimate repair benefits owed under the policy.

In this case, the Court found that the insurer had a genuine dispute regarding the extent of damage to Plaintiffs' home and required repairs because the insurer's expert promptly examined the master bathroom and drywall ceilings, assessed the extent and type of damage, and provided an estimate of cost of the appropriate repairs, but the Plaintiffs curtailed their insurer's ability to further investigate the damage by removing the damaged property before their insurer had an opportunity to conduct a full assessment.

AN EXCESS CARRIER WHO FUNDS AN EXCESS PRIMARY LIMITS SETTLEMENT MAY ASSERT A CLAIM FOR EQUITABLE SUBROGATION AND BAD FAITH AGAINST A PRIMARY INSURER WHO PREVIOUSLY UNREASONABLY REFUSED TO ACCEPT AND FUND A POLICY LIMITS SETTLEMENT DEMAND

In the case styled Ace American Insurance Company v. Fireman's Fund Insurance Company (2016) 2 Cal.App.5th 159, 206 Cal. Rptr.3d 176, the Court of Appeal, Second District, Division 4, held on August 5, 2016 that in an action between an excess and primary insurer alleging equitable subrogation

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and breach of the duty of good faith and fair dealing, an excess insurer which has settled and discharged the insured's liability may recover from the primary insurer an amount in excess of the primary insurer's policy limits if the excess insurer can prove the primary insurer's unreasonable refusal to settle within its policy limits resulted in loss to the excess insurer in an amount in excess of the policy limits of the primary insurer it would not otherwise have had.

A movie industry worker was seriously injured on a movie set. His employer had two primary insurance policies with Fireman's Fund Insurance Company, and an excess insurance policy with Ace American Insurance Company. The injured worker sued, Fireman's Fund defended the case, and the case eventually settled with the participation of and contributions from both insurers.

Ace American then sued Fireman's Fund for equitable subrogation, alleging that the injured worker initially offered to settle his case within the limits of the Fireman's Fund policies, and that Fireman's Fund unreasonably rejected those settlement offers. Ace American alleged that as a result, it was required to contribute to the eventual settlement, which exceeded the limits of the Fireman's Fund policies.

The question before the appellate court was whether Ace American stated viable causes of action for equitable subrogation and breach of the duty of good faith and fair dealing, or whether the lack of a judgment in the employment injury case bared Ace American's claims. The trial court concluded that because Ace American, the excess insurer, alleged it was required to contribute to the settlement of the underlying case due to the primary insurer's failure to reasonably settle the case within policy limits, the lack of an excess judgment against the insured in the underlying case did not bar an action for equitable subrogation and breach of the duty of good faith and fair dealing.

Parenthetically, the United States District Court for the Eastern District of California reached the same conclusion relative to the equitable subrogation claim between and excess and primary insured on May 3, 2016 in the unpublished decision styled RSUI Indemnity Company v. Discover P & C Insurance Co. (2016 WL 1745119).

AS A MATTER OF LAW, THE EXISTENCE OF TRIABLE ISSUES OF FACT AS TO JUST WHAT OCCURRED PRECLUDES AN INSURER'S MOTION FOR SUMMARY JUDGMENT REGARDING ITS DUTY TO PROVIDE COVERAGE

In the case styled Public Service Mutual Insurance Co. v. Liberty Surplus Insurance Corporation (2016), -- F.Supp.3d --, 2016 WL 4474603, the United States District Court for the Eastern District of California held on August 25, 2016, that the as a matter of law, the existence of triable issues of fact as to just what occurred precluded an insurer's Motion for Summary Judgment regarding its duty to provide coverage.

Plaintiff Public Service Mutual Insurance Company sought equitable indemnification from another insurance carrier, Liberty Surplus Insurance Corporation for amounts paid by Plaintiff for the defense and indemnification of its insureds, Fair Oaks Fountains, LLC ("FOF") and FPI Management Company ("FPI"). According to Plaintiff's complaint, Defendant was obligated to pay those amounts under its own policy, issued to Gala Construction, on grounds that both FOF and FPI were specifically designated as additional insureds under the Defendant's policy because, according to Plaintiff's complaint, the Defendant's policy was primary as to the underlying loss. That loss occurred when an injury occurred, allegedly as a result of Gala Construction's negligence, while Gala Construction effectuated repairs on an apartment complex owned by FOF and managed by FPI. Defendant filed a Motion for Summary Judgment.

In denying the motion, the District Court explained that the basis for Defendant's motion was that it owed no obligation whatsoever under its policy. According to Defendant, neither FOF nor FPI could qualify as insureds because any liability on their part could not have arisen from the "work," of Gala Construction so as to trigger coverage under Defendant's policy. In the absence of any such qualifying activity, Defendant maintained that it had no duty to defend or indemnify either entity. Given the many triable issues of fact as to just what occurred and what role Gala Construction played, however, the District Court concluded that no such determination could be made as a matter of law on summary judgment.

WHEN THERE IS NO CONTRACTUAL DUTY TO INDEMNIFY AN INSURED BECAUSE OF AN INSURED'S INTENTIONAL CONDUCT, THE INSURER CANNOT BE FOUND TO HAVE BREACHED THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALINGS

In the ***unpublished*** case styled Douglas Bilyeu *et al.* v. State Farm General Insurance Company (2016), 2016 WL 4547658, the Court of Appeal, Second District, Division 2, held on September 1, 2016, that where there is no contractual duty to indemnify an insured arising from the insured's intentional conduct, the insurer cannot be found to have breached the implied covenant of good faith and fair dealings.

A homeowner struck his neighbor in the face, knocking him to the ground, breaking one of his ribs and causing a traumatic brain injury that resulted in permanent brain damage. The homeowner claimed he was acting in self-defense, but two juries—one criminal and one civil—rejected this defense. The homeowner's insurer agreed to defend him in the civil suit brought by the neighbor, but ultimately refused to indemnify him for the $6.3 million verdict. The homeowner assigned his rights against his insurer to the injured neighbor, who then sued the insurer for breach of the duty to indemnify, for bad faith denial of coverage, and for relief as a judgment creditor. The trial court granted summary judgment for the insurer.

In affirming the trial court, the Court of Appeal noted that the insured homeowner's conduct was not an "accident." The homeowner frankly admitted that he did precisely what he intended to do: he struck his neighbor in the face. This act was intentional. Although the homeowner asserted that he undertook this intentional act in self-defense or in defense of his daughter, two juries—the criminal jury that heard the assault charges against him and the civil jury that awarded the neighbor $6.3 million—specifically and necessarily found that the homeowner did not reasonably act in self-defense. These jury findings, said the appellate court, were binding upon it. And although neither jury made a finding as to whether the homeowner acted in self-defense unreasonably, the California Supreme Court has previously held that "an

Bottom Line

Title of Case: Robert Notman v. Millers Towing, Inc.

Court and Case Number: SDSC Case No. 37-2011-00071034-CU-BC-EC

Judge: Hon. Kevin Enright

Plaintiff's Counsel: Joseph Sciarretta and Anthony Sciarretta of Sciarretta Law

Defense Counsel: Colin Walshok of Wingert Grebing Brubaker & Juskie, LLP and Rob Mackey of Veatch Carlson, LLP

Type of Case/Causes of Action: Business Dispute/Breach of Contract

Plaintiff's Settlement Demand: $2,300,000

Defendant's Settlement Offer: $50,000

Trial Type: Jury/Bench

Trial Length: 8 days

Verdict: $139,342 ◆

insured's unreasonable belief in the need for self-defense does not turn the resulting purposeful and intentional act of assault and battery into 'an accident' within [a] policy's coverage clause."

To prevail on a claim that an insurance company has breached the implied covenant of good faith and fair dealings, an insured must show (1) that benefits were due under the policy, and (2) that these benefits were withheld without proper cause. The threshold requirement that benefits be due under the policy reflects the fact that breach of the implied covenant is an "auxiliary" and "supplemental" claim that flows from a breach of the insured's primary right to receive the benefits of his insurance contract."

Based upon the above factual and legal analysis, the Court of Appeal concluded that State Farm had no contractual duty to indemnify the homeowner and that the neighbor's auxiliary bad faith denial of the claim under the implied covenant of good faith and fair dealings necessarily failed. It is well settled that where a breach of contract cannot be shown, there is no basis for a finding of breach of the covenant of good faith and fair dealings and without coverage there can be no liability for bad faith on the part of the insurer. ◆

COVER STORY CONTINUED FROM PAGE 1

"work product" of attorneys acting on a client's behalf. [CCP § 2018.010 et seq.] Work product includes *attorney's agents and consultants*: However, "work product" of an attorney's employees or agents (investigators, researchers, etc.) is treated as the "work product" of the attorney. [*See Rodriguez v. McDonnell Douglas Corp.* (1978) 87 CA3d 626, 647-648 (disapproved on other grounds in *Coito v. Sup.Ct.* (State of Calif.) (2012) 54 C4th 480, 499)].

The "work product" of experts consulted by the attorney and who will not testify at trial is likewise treated as the attorney's "work product." [*Scotsman Mfg. v. Sup.Ct.* (1966) 242 CA2d 527, 530] (Compare: Experts who testify may be compelled to disclose all reports they have prepared; *see* ¶8:255 ff.)

While the waters are murky when it comes to an attorney retaining an investigator, California courts have made it clear if the surveillance was obtained prior to the retaining of counsel. A party's or insurer's consultations with an expert before hiring counsel are not protectable as "attorney work product." Nor can an attorney later "by retroactive adoption convert the independent work of another, already performed, into his own." (*Jasper Construction, Inc. v. Foothill Junior College Dist. of Santa Clara County* (1979) 91 CA3d 1, 16 (internal quotes omitted) (disapproved on other grounds in *Los Angeles Unified School Dist. v. Great American Ins. Co.* (2010) 49 C4th 739, 753)]

CCP section 2018.030 separates the two privileges writings are subject to, absolute and qualified. A writing that reflects an attorney's impressions, conclusions, opinions, or legal research or theories is not discoverable under any circumstances. (CCP section 2018.030.) All other work product of an attorney "…is not discoverable unless the court determines that denial of discovery will unfairly prejudice the party seeking discovery in preparing that party's claim or defense or will result in an injustice." (Code Civ. Proc., § 2018.030(b).)

Surveillance

Under California Law, surveillance alone does not warrant absolute protection. (*Suezaki v. Superior Court*, (1962) 58 Cal. 2d 166, 177.) The *Suezaki* court reasoned that simply because the subject matter sought to be discovered is the 'work product' of the attorney, it is not privileged…but that is a factor that the trial court should consider, in its discretion, together with other relevant factors, in determining whether to deny or to grant discovery in whole or in part. Id. Therefore, surveillance falls under the qualified privilege, whose protection depends on the court's determination of whether the plaintiff will be unfairly prejudiced in preparing his or her claim or will suffer an injustice if the surveillance is not disclosed. (Code Civ. Proc, § 2018.030(b).)

Disclosure Required?

As to the specific question of whether failing to disclose surveillance materials unfairly prejudices or causes plaintiff to suffer injustice, the water is still murky. There is no bright line rule on when a party must disclose surveillance footage. However, in the example mentioned in the introduction, if surveillance is obtained by the carrier prior to being assigned to an attorney, the surveillance is not covered by the work product doctrine under *Rodriguez*.

An attorney who does not disclose the surveillance runs the risk of the surveillance not being permitted by the judge and prohibiting the footage being introduced as evidence at trial. Surveillance may also facilitate an early settlement if some particular footage is obtained which significantly damages plaintiff's case. Therefore, attorneys must weigh the advantages and disadvantages of producing the surveillance, under the circumstances of each case. ◆