No. E039995

In the Court of Appeal of the State of California
Fourth Appellate District, Division Two

OLD UNITED INSURANCE COMPANY, dba
VANTAGE CASUALTY COMPANY
Plaintiff, Cross-Defendant and Appellant,

vs.

DON BUHRMAN,
Defendant, Cross-Complainant and Respondent, and

WESTERN MARINE INSURANCE SERVICES, INC.
dba WESTMAR INSURANCE,
Cross-Defendant and Appellant

BRIEF OF UNITED POLICYHOLDERS
as *AMICUS CURIAE* IN SUPPORT OF DON BUHRMAN

Appeal from Riverside Superior Court Number RIC349816
Honorable Gloria Connor-Trask

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MISCELLANEOUS

STATEMENT OF INTEREST OF *AMICUS CURIAE*

United Policyholders is a non-profit organization founded in 1991 and dedicated to education on insurance issues and consumer rights. The organization is tax-exempt under §501(c)(3) of the Internal Revenue Code. United Policyholders is funded by donations and grants from individuals, businesses, and foundations.

While much of its work is aimed at individuals and businesses affected by disasters, United Policyholders actively monitors legal and marketplace developments affecting the interests of all policyholders. United Policyholders receives frequent invitations to testify at legislative and other public hearings and to participate in regulatory proceedings on rate and policy issues.

A diverse range of personal and commercial line policyholders throughout the United States communicate their insurance concerns on a regular basis to United Policyholders. United Policyholders advances policyholders' interests in courts throughout the country by filing *amicus curiae* briefs in cases involving important insurance principles.

United Policyholders' *amicus* brief was cited in the U.S. Supreme Court's opinion in *Humana, Inc. v. Forsyth*, (1999) 525 U.S. 299 [119 S.Ct. 710, 142 L.Ed.2d 753]. United Policyholders has filed *amicus curiae* briefs on behalf of policyholders in over one hundred and twenty cases throughout the United States in the past six years. These activities are limited only to the extent that United Policyholders exists exclusively on donated labor and contributions of services and funds. No party to this case has contributed directly or indirectly to the preparation of this brief.

United Policyholders has a vital interest in seeing that insurance companies do not attempt to shift risk assumed in insurance policies back to their policyholders through schemes unsupported by insurance policies or public policy. United Policyholders has an interest in ensuring that insurance companies live up to their promises to their policyholders.

United Policyholders seeks to appear as *amicus curiae* to address certain issues presented in this case that are of significance

well beyond the application of law to the specific facts of this case. These important issues will affect policyholders nationwide.

I. STANDARD OF REVIEW

Trials are not perfect. If this were a criminal case it would be affirmed post haste. *Delaware v. Van Arsdall*, (1986) 475 U.S. 673 [106 S.Ct. 1431, 89 L.Ed.2d 674].

Reversal of this case would invite disrespect for the judicial process and encourage abuse of the litigation process. Justice Robert Traynor wrote many years ago:

> Like all too easy affirmance, all too ready reversal is also inimical to the judicial process. Again, nothing is gained from such an extreme, and much is lost. Reversal for error, regardless of its effect on the judgment, encourages litigants to abuse the judicial process and bestirs the public to ridicule it.
>
> Robert J. Traynor, "The Riddle of Harmless Error," Ohio State University Press, Columbus, Ohio (1970) at 50

The decision of the trial court should be summarily affirmed.

II. INADEQUACY OF BREACH OF CONTRACT REMEDIES

Policyholders who prevail in breach of contract cases are entitled to money damages sufficient to restore them to their position had there been no breach and no more. E. Allan Farnsworth, Farnsworth on Contracts, Section 12.8 (Aspen 2001). E. Allan Farnsworth, *Legal Remedies for Breach of Contract*, 70 Colum. L. Rev. 1145 (Nov. 1970). Breach of contract damages are thus inadequate, grossly inadequate.

The decision of the trial court recognizes that contractual damages need to be amplified to provide justice to insurance policyholders.

III. LITIGATION SLEDGE HAMMER

A. Arbitration

The insurance policy in this case contained an arbitration provision – not optional arbitration but mandatory.

For reasons not apparent from the record, Old United Insurance Company chose not to ask for arbitration. (If one is to

believe the advocates for arbitration it is cheaper, quicker and more efficacious.)

The insurance company sued in court. Instead of arbitration the policyholder in this case got a long drawn-out contentious and expensive court battle. It is no wonder the policyholder missed time from work to help battle the litigation Godzilla.

B. Wrongful Litigation

First, if this case had been arbitrated there would be, and there would have been, no wrongful litigation claim against the insurance company. Donald P. Wagner & John C. Lautsch, *Malicious Prosecution and Contractual Arbitration*, 43-AUG Orange County Law. 30 (2001) discussing *Brennan v. Tremco*, (2001) 25 Cal.4th 310 [105 Cal.Rptr.2d 790, 20 P.3d 1086].

Second, the case falls well within the ambit of a number of leading California cases, in particular *Slaney v. Ranger Ins. Co.*, (2d Dist. 2004) 115 Cal.App.4th 306 [8 Cal.Rptr.3d 915]. See also: *Zamos v. Stroud*, (2004) 32 Cal.4th 958 [12 Cal.Rptr.3d 54, 87 P.3d

802], *George F. Hillenbrand, Inc. v. Insurance Co. of N. Am.*, (3d Dist. 2002) 104 Cal.App.4th 784 [128 Cal.Rptr.2d 586] and *Shafer v. Berger, Kahn, Shafton, Moss, Figler, Simon & Gladstone*, (2d. Dist. 2003) 107 Cal.App.4th 54 [131 Cal.Rptr.2d 777].

As a case akin to malicious prosecution this case should be affirmed.[1]

IV. FIRST PARTY BAD FAITH

A. Background

Within the last fifty years, courts have come to look upon the insurance policy as a different type of contract, a contract that occupies a "unique institutional role" in modern society.[2]

An insurance policy is designed to transfer economic risk. The policyholder pays a premium to protect against the risk.

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1 The "leading" malicious prosecution case in the United States is *TXO*. *TXO Production Corp. v. Alliance Resources Corp.*, (1993) 509 U.S. 443 [113 S.Ct. 2711, 125 L.Ed.2d 366].

2 Roger C. Henderson, *The Tort of Bad Faith in First Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Statute*, 26 U. Mich. J.L. Reform 1 (Fall 1992). Professor Henderson has written extensively and insightfully on the development of first-party bad faith claims. *See also*, Roger C. Henderson, *The Tort of Bad Faith in First Party Insurance Transactions After Two Decades*, 37 Ariz. L. Rev. 1153 (1995).

However, if the risk materializes, the insurance company will pay the policyholder far more than the policyholder has ever paid the insurance company. The payment is due at a time of emotional, personal and financial disaster for the policyholder. This disparity in financial consequences is only possible because the risk of loss is spread over many policyholders who fear, but will not suffer, the same disaster. The broad distribution of risk across society is a "perceived social significance"[3] distinguishing insurance policies from private contracts, which, if breached, impact only the parties to the contract.

B. Third Party Bad Faith

The origin of the tort of bad faith in first-party insurance policy cases is to be found in third-party insurance policies, that is, liability insurance.[4]

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[3] Roger C. Henderson, *The Tort of Bad Faith in First Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Statute*, 26 U. Mich. J.L. Reform 1 (Fall 1992).

[4] *Id.*

Only the policyholder and the insurance company are involved in first-party insurance, which is marketed as protecting the policyholder and the policyholder's property. First-party insurance includes uninsured motorist coverage; property insurance; health, life and disability insurance; fidelity bonds; and business interruption insurance.

In a third-party case, *Communale v. Traders and General Ins. Co.*,[5] the California Supreme Court held that the implied covenant of good faith and fair dealing in every contract is applicable to insurance contracts. Parties to a contract inherently promise that neither will do anything to injure the right of the other party to receive the benefits of the agreement. In *Communale*, the insurance company wrongfully refused to defend its policyholder and wrongfully refused to settle the liability claim against the policyholder within the policy limits. The Court held that the consequences of a judgment in excess

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5 *Communale v. Traders and General Ins. Co.*, (1958) 50 Cal.2d 654 [328 P.2d 198].

of policy limits against the policyholder should be shifted from the policyholder to the insurance company.

In *Opsal v. United Services Automobile Assn.*,[6] the court held that an insurance company's erroneous failure to pay policy benefits does not necessarily constitute bad faith entitling the policyholder to recover tort damages. The ultimate test according to the court is whether the refusal was unreasonable. In other words, drawing a distinction between claim decisions that are erroneous or wrong, constituting a breach of contact, and those that are unreasonable and *wrongful*, which may constitute bad faith. Being fed into the litigation "maw," as happened in this case, is hardly a benefit policyholders contemplated.[7]

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6 *Opsal v. United Services Automobile Assn.*, (4th Dist.1991) 2 Cal.App. 4th 1197 [10 Cal.Rptr.2d 352].

7 John D. Cross, *Returning to 'Go' (But Not Collecting $200); Re-examining Insurance Bad Faith in Light of Modern California Law on Summary Judgment, and the Genuine Dispute Doctrine*, 40 Tort Trial & Ins. Prac. L.J. 1051 (Summer 2005). Cross explains that California policyholders are victims of summary judgment justice. This does not speak well for the California judiciary and has, in effect, nullified the right to jury trial in California.

The California Supreme Court again considered third-party bad faith in *Crisci v. Security Ins. Co. of New Haven.*[8] Significantly, *Crisci* held, in a clear departure from traditional contract law, that the policyholder's damages for the insurance company's bad faith could include the emotional distress suffered by the policyholder.

C. First Party Bad Faith

In *Gruenberg v. Aetna Ins. Co.*[9] the California Supreme Court applied *Crisci* to a first-party insurance claim. The insurance company wrongfully denied benefits under a fire insurance policy. The policyholder recovered damages for emotional distress because the court recognized that when an insurance company, ". . .fails to deal fairly and in good faith with its insured by refusing, without proper cause, to compensate its insured for a loss covered by the policy, such conduct may give rise to a *cause of action in tort* for

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8 *Crisci v. Security Ins. Co. of New Haven, Conn.* (1967) 66 Cal.2d 425 [58 Cal.Rptr. 13, 426 P.2d 173].

9 *Gruenberg v. Aetna Ins. Co.*, (1973) 9 Cal.3d 566 [108 Cal.Rptr.480, 510 P.2d 1032].

breach of an implied covenant of good faith and fair dealing."[10] The court did not require the policyholder to establish that the insurance company committed the separate and distinct tort of intentional infliction of emotional distress.

According to Professor Henderson,[11] ten of the thirty jurisdictions that permit extra-contractual damages in first-party bad faith cases follow the "reckless conduct test," two jurisdictions follow the "gross negligence test," and three jurisdictions have "expanded the tort to encompass "mere negligence." Two states have statutory definitions for first-party bad faith and other jurisdictions adhere to the outrageous conduct requirement. The law continues to evolve, and it appears to be evolving in favor of policyholders.

As to any action against an insurance company, whatever the theory, the insurance company's defense will be its 'right to be wrong' – i.e., there is no bad faith liability if the insurance company

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10 Id. At 574.

11 Roger C. Henderson, *The Tort of Bad Faith in First Party Insurance Transactions After Two Decades*, 37 Ariz. L. Rev. 1153 (1995).

reasonably, even if incorrectly, denied coverage.[12] If there is a *reasonable basis* for denying or delaying the policyholder's benefits, the insurance company will contend that it cannot be guilty of bad faith. No other product purveyor would dare make this anti-consumer claim.

According to insurance companies, the California genuine dispute doctrine applies to both legal and factual disputes, i.e., a court can conclude as a matter of law that an insurance company's denial of a claim is not unreasonable, so long as there existed a genuine issue as to the insurance company's liability.[13]

V. ADVICE OF COUNSEL

Reliance on advice of counsel as a defense requires waiving the attorney client privilege. *See Clausen v. National Grange*

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12 Douglas G. Houser, *Good Faith As A Matter of Law: The Insurance Company's Right to Be Wrong*, 27 Tort & Ins. L.J. 665 (Spring 1992); Douglas G. Houser, et al., *Good Faith As A Matter of Law – An Update on The Insurance Company's 'Right to Be Wrong*, 39 Tort Trial & Ins. Prac. L.J. 1045 (Summer 2004); and Edward Zampino & M. Farrett Coleman, *Turning the Other Cheek: Can Insurers' Defense of Coverage Suits Constitute Grounds for 'Bad Faith Litigation'?*, 38 Tort Trial & Ins. L.J. 103 (2002).

13 *Morris v. Paul Revere Life Ins. Co.*, (4th Dist. 2003) 109 Cal.App.4th 966 [135 Cal.Rptr. 2d 718].

Mutual Ins. Co., (Del. 1997) 730 A.2d 133. In this case the insurance company waived the "advice of counsel" defense.

VI. CONCLUSION

The law pertaining to first-party bad faith claims has rapidly evolved. Within fifty years, more than half of the states have recognized what is, essentially, a *new* cause of action. Remarkably, the courts have applied classic tort considerations to resolve disputes arising from contracts. This migration of legal principles has been justified by recognition that a first-party insurance policy is not an "ordinary" contract. The policyholder enters into the policy seeking peace of mind and financial protection from calamity. The insurance policy provides a mechanism to spread the policyholder's financial risks among many others. Therefore, society has an interest in the faithful, reliable performance of the insurance company's obligations. When calamity does strike, the policyholder is vulnerable and dependent upon the insurance company to fulfill its promises. If the insurance company denies benefits to the policyholder, the policyholder may suffer consequences much greater than the loss of

the anticipated financial assistance. Under the law as it presently stands, when the insurance company is merely wrong, the policyholder will ultimately obtain the relief provided by the policy inadequate though that may be. But, when the insurance company's denial of benefits is outrageous or reckless or unreasonable, only a tort rationale will provide compensation for the consequential damages suffered by the policyholder.

As the law of first party bad faith continues to morph from contract to tort, insurance companies will be encouraged to raise the level of their claims handling and policyholders will be able to recover appropriate damages if the insurance company's wrongful conduct causes harm.

The judgment below should be affirmed.

Dated: September , 2006
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VII. CERTIFICATE OF COMPLIANCE WITH CAL. R. CT. 14(C)(1)

Pursuant to California Rule of Court 14(c)(1), the foregoing *Amicus* Brief is double-spaced and was printed in proportionately-spaced 14 point Times New Roman type. It contains 1,973 words (including footnotes, but excluding tables and this Certificate). In preparing this certificate, I relied on the word count generated by Microsoft Word.

Executed on September _____ 2006 at

_____

_____

Amy Bach

Old United Insurance Company v. Don Buhrman,
and Related Cross Actions,

Cal. App. 4/2 No. E039995
(Riverside Superior Court No. RIC 349816)

AFFIDAVIT OF SERVICE

Amy Bach, being duly sworn, deposes and says that she is not a party to this action and is over 18 years of age. On the _____ day of September 2006, deponent served the annexed Brief of United Policyholders as *Amicus Curiae* in Support of Don Buhrman upon the following named parties at the addresses indicated via UNITED STATES MAIL, postpaid:

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