A093437

COURT OF APPEAL
STATE OF CALIFORNIA
FIRST APPELLATE DISTRICT
DIVISION THREE

NGOC M. TRAN, dba SHING FAT SUPERMARKET,

Plaintiff and Appellant,

vs.

FARMERS GROUP, INC., TRUCK INSURANCE EXCHANGE, ET AL.

Defendants and Respondents.

Application by United Policyholders for leave to file brief as amicus curiae; Brief of United Policyholders

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Appeal from the Superior Court of Alameda County
Honorable Patrick J. Zika, Judge

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APPLICATION FOR PERMISSION TO FILE BRIEF AS AMICUS CURIAE

Pursuant to Rule 15(b) of the California Rules of Court, United Policyholders ("UP") seeks leave to file a brief in this action as amicus curiae. UP was founded in 1991 as a non-profit organization dedicated to educating the public on insurance issues and consumer rights. The organization is tax-exempt under Internal Revenue Code §501(c)(3). UP is funded by donations and grants from individuals, businesses, and foundations.

In addition to serving as a resource on insurance claims for disaster victims and commercial insureds, UP actively monitors legal and marketplace developments affecting the interests of all policyholders. UP 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 policyholders throughout the United States communicate on a regular basis with UP, which allows it to provide important and topical information to courts throughout the country via the submission of *amicus curiae* briefs in cases involving insurance principles that are likely to impact large segments of the public.

UP's *amicus* brief was cited in the U.S. Supreme Court's opinion in *Humana, Inc. v. Forsythe* (1999) 525 U.S. 299, and its arguments were adopted by the California Supreme Court in *Vandenberg v. Sup. Ct.* (1999) 21 Cal.4th 815. UP has filed *amicus* briefs on behalf of policyholders in over ninety cases throughout the United States.

By virtue of its network of attorneys who represent policyholders, UP is aware of facts that pertain to the key issue presented in this appeal that might not otherwise be presented to this Court. It does not present these facts as a basis to decide this case; only to show the Court that plaintiffs in other cases could plead and prove these facts, and if they did, could establish liability against the entities within the Farmers Group of Companies and particularly against Farmers Group, Inc. UP's concern is that unless this Court is made aware of these facts and the legal theories that they support, it could decide

this case in a way that might foreclose legitimate claims by other insureds in other cases against Farmers and Group, Inc.

PRELIMINARY STATEMENT

This appeal raises a recurrent issue — what are the rights of an insured who has purchased coverage from "the Farmers Group of Companies"? As explained below, "the Farmers Group of Companies" ("Farmers") is not a collection of autonomous individual companies. Rather, it is a single business enterprise operating as an unincorporated association and as a joint venture, which exists to sell insurance under its service mark, the "Farmers Insurance Group of Companies."

Farmers has adopted a Byzantine structure of interlocking affiliates with similar names that defies easy understanding or explanation. Prospective customers purchase insurance from their "Farmers" agent, but the actual policy will be issued by an insurance exchange or a company that the insured has never heard of or dealt with, and the claim will be adjusted by another Farmers entity. The entire enterprise is controlled by Farmers Group, Inc. ("Group Inc.")

When a dispute with an insured develops into litigation, Farmers argues that only the entity that actually issued the policy is a proper defendant, even where that entity has no employees, no physical assets, and is entirely controlled and directed by Group Inc. These are the arguments that Farmers has made here.

Unfortunately, the record developed below may not allow this Court to evaluate Farmers' true structure or the full range of legal theories that should be available to a Farmers insured. In this brief UP will set forth the facts that could be asserted against Farmers, which have been developed in the course of many lawsuits against Farmers of which UP is aware, but which most individual plaintiffs are not.

These facts would support liability against the Farmers as an unincorporated association or as a joint venture. Additionally, liability against Group Inc. could be proper on an alter ego theory. UP is not suggesting that these findings could necessarily

be made in this case. But it is important for the Court to know that these theories could be available when the facts supporting them are alleged and developed, so that it does not issue a decision that inadvertently forecloses other litigants from proceeding on these theories in other cases.

FACTS THAT ESTABLISH FARMERS' POTENTIAL LIABILITY

Based on its network of counsel who represent insureds, UP has obtained information that would allow a Farmers insured bringing a lawsuit against Farmers to plead the following facts in good faith, with every expectation that they could be fully proven at trial.

The Farmers Insurance Group of Companies ("Farmers") is an unincorporated association carrying on a single business enterprise of marketing and selling various forms of property and casualty insurance, is comprised of, *inter alia*, the following entities. Group Inc. does business as "Farmer's Underwriting Association."

Group Inc. is the sole owner of Truck Underwriters Association, Fire Underwriters Association, Farmer's Ins. of Columbus, Inc., Illinois Farmers Ins. Co., Farmers New World Life Ins. Co., F.I.G. Holding Co., and F.I.G. Leasing Co.

The entities within Farmers share the same or substantially the same corporate officers and boards of directors, and have the same principal place of business — 4680 Wilshire Boulevard, Los Angeles, California. Group Inc. controls, manages, and supervises the other members of Farmers. These members are simply instrumentalities or conduits for Farmers and Group Inc. to pursue a single business enterprise of an insurance company.

Truck Insurance Exchange, Truck Underwriters Association, Fire Insurance Exchange, Fire Underwriters Association, Farmers Texas County Mutual Ins. Co., and Mid-Century Ins. Co. (the reciprocal or inter-insurance exchanges), are the entities within Farmers that actually sell insurance policies to the public. Each is a mere shell entity, having no employees, no tangible property, no real property assets, and is capitalized only to the extent necessary to meet minimum capital requirements.

Group Inc., together with the "P&C Group" (for property and casualty group), which consists of Farmers Ins. Exchange, Fire Insurance Exchange, Truck Insurance Exchange, and Mid-Century Ins. Co., form an insurance company holding system. Group Inc. operates as the attorney-in-fact for the P&C Group. As attorney-in-fact, Group Inc. appointed itself to provide management services to the ensuring entities, at a rate it sets, which averages more than $1 billion yearly.

All claims handling for the reciprocal or inter-insurance exchanges is performed by Farmers Insurance Exchange. All other functions, including, but not limited to management services, underwriting, accounting, actuarial services, investment advice and services, real estate management and maintenance, computer services, facilities and equipment procurement, are provided for the reciprocal or inter-insurance exchange by Group Inc. The cost of providing these services is "allocated" to the various entities in accordance to various "pooling agreements" between the entities.

Group Inc. follows a corporate policy of maintaining the reciprocal or inter-insurance exchanges in an inadequately capitalized condition in light of the business they conduct and the risks they face. Group Inc. and its wholly-owned subsidiaries loaned hundreds of millions of dollars to the reciprocal or inter-insurance exchanges to bolster their statutorily required surpluses after the 1994 Northridge earthquake. Group Inc. also maintains credit lines with financial institutions through which it meets the unanticipated short-term cash needs of other entities within Farmers.

Group Inc. has expropriated "the lion's share" of Farmers' policyholders' premiums and investment proceeds through the management fees it charged the other entities within Farmers, and a percentage of earned premiums, and has disbursed these payments to its own corporate parents in the form of dividends, and to high-ranking corporate executives in the form of bonuses and profit-sharing.

Group Inc. has purchased assets, including real estate, equipment, and other fixed assets, in its own name or through its wholly-owned subsidiaries, but these assets were used by, or on behalf of, all entities within Farmers.

Group Inc. determines premium rates for the entities within Farmers, based on Farmers' collective experience. Farmers files consolidated federal and state tax returns, and combined annual statements with state insurance regulators describing its business as "Farmers Insurance Group of Companies and its affiliated property and casualty insurers."

Group Inc. creates, develops and implements all marketing materials for Farmers' insurance-related products, and emphasizes Farmers to the public as a single business entity. Group Inc. owns the service mark, "Farmers Insurance Group of Companies." All the Farmers entities use the same logo on all advertising, forms, signage, vehicles, and agencies. Through its unified marketing efforts, Farmers leads those who purchase insurance from the entities within it to believe the policies are based on the strength and backing of the entire Farmers enterprise, not the single entity within Farmers named on the policy sold.

Farmers uses a single agency network of 14,447 writing agents that sells all of the insurance-related products of each of the entities within Farmers. Farmers operates two pension plans, the "regular plan," for which almost all employees of all entities within Farmers are eligible, and the "restoration plan," which covers key employees of various Farmers entities.

The boards of governors for the P&C Group share personnel. All the Farmers entities share the same agent for service of process. Group Inc.'s SEC filings explain that the P&C Group operates under a common trade name and logo, and distribute their insurance products through a common agency network In its SEC filings, Group Inc. says that as manager and attorney-in-fact for the P&C Group, it selects risks, issues policies, prepares and mails policy forms and invoices, and collects premiums.

Group, Inc. and other Farmers entities share in any profits earned by the various exchanges. Group, Inc. has implemented employee review and bonus programs that created incentives for Farmers Insurance Exchange employees to deny or minimize claims.

LEGAL ARGUMENT

A. Farmers, and the entities that comprise Farmers, are subject to suit as an unincorporated association

Section 369.5 of the Code of Civil Procedure expressly allows an unincorporated association be sued in the name it has assumed and by which it is known. Here, that would be "the Farmers Group of Companies. An unincorporated association is defined by Corporations Code § 24000, subd. (a) as "any partnership or other unincorporated organization of two or more persons, whether organized for profit or not." Subdivision (b) of the same section makes clear that the term "person" refers to a natural person, corporation, or any other unincorporated organization. The Law Review Commission comment to § 24000 confirms the breadth of the definition, explaining that it applies to "all private unincorporated associations of any kind."

The test for whether an entity is an unincorporated association is simple, and was explained in *Barr v. United Methodist Church*:[1]

> The criteria applied to determine whether an entity is an unincorporated association are no more complicated than (1) a group whose members share a common purpose, and (2) who function under a common name under circumstances where fairness requires the group be recognized as a legal entity. Fairness includes those situations where persons dealing with the association contend their legal rights have been violated. . . . Formalities of quasi-corporate organization are not required.

A complaint that stated all the foregoing allegations against Farmers would meet these criteria. The entities that make up Farmers share a common purpose — selling insurance as a single business enterprise — and function under a common name, representing to all who do business with them that they are all part of a single organization. Farmers assigns different parts of its whole to perform various tasks, but collectively it functions as a unified insuring entity.

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[1] *Barr v. United Methodist Church* (1979) 90 Cal.App.3d 259, 266-267.

These facts caused the Oklahoma Supreme Court in 1997 to conclude that Farmers could be liable as an unincorporated association. In *Oliver v. Farmers Ins. Group of Companies*,[2] it affirmed a summary judgment allowing suit against "the Farmers Insurance Group of Companies."

Group Inc. has suggested in other litigation that *Oliver* turned on the particular wording of the Oklahoma statute allowing suit against unincorporated associations. But the statute in question, 13 Title 12 O.S.1991, Section 182, is little more than an amalgam of Cal. Corporations Code § 24000, subd. (a) (which defines unincorporated associations) and Code Civ. Proc. 369.5 (which allows suit against them.) The Oklahoma statute does both in the same provision, stating, "When any two or more persons associate themselves together and transact business for gain or speculation under a particular appellation, not being incorporated, they may be sued by such appellation."[3]

B. Farmers and the entities that comprise it are subject to suit on a joint venture theory

A joint venture is "an association of two or more persons who combine their property, skill or knowledge to carry out a single business enterprise for profit."[4] To show a joint venture exists, the evidence must show a community of interest in the enterprise, a sharing of profits and losses, and joint participation in the conduct of the business.[5] A substantial contribution can be made to a joint venture by the furnishing of knowledge, skill, and services, as well as by money. The contributions of the respective parties to a joint venture need not be equal or of the same character.[6]

Joint venturers are, like partners, jointly and severally liable for the activities of the joint venture.[7] Because each joint venturer is the agent for the other members of the

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[2] *Oliver v. Farmers Ins. Group of Companies* (Ok. 1997) 941 P.2d 985, 988.
[3] *Id.*, 941 P.2d at 988.
[4] *Precision Fabricators, Inc. v. Levant* (1960) 182 Cal.App.2d 637, 640.
[5] *Ibid.*
[6] *Epstein v. Stahl* (1960) 176 Cal.App.2d 53, 57.
[7] *Ohio Cas. Ins. Co. v. Harbor Ins. Co*. (1968) 259 Cal.App.2d 207, 213, 214.

venture, all members are liable for the torts committed by any venturer while acting in connection with the venture.[8] The existence of a joint venture is a question of fact.[9]

Based on the facts stated above, a plaintiff could allege that each entity within Farmers acted as, *inter alia*, an agent and joint venturer of the other entities, and that Farmers carried on "a single business enterprise" of marketing and selling property and casualty insurance. The factual allegations would support these contentions:

- The sharing of profits and shifting of assets within the venture through payment of fees, dividends, loans, and pooling agreements;
- The unified marketing strategy and sales structure;
- The contributions of various skills and services by various entities within the venture, e.g., the exchanges issue the policies that generate the premium income; Farmers Insurance Exchange adjusts all claims for all the entities; Group Inc. provides management services and overall direction;
- The creation and use of employee incentive programs to increase venture profits through the denial of claims;
- The use of property purchased and held by Group Inc. by all Farmers entities.

Plainly, the various entities within Farmers, including Group Inc., have a community of interest in the enterprise. They each make different types of contributions, including skills, services and money, all in service of the ultimate purpose of the venture — selling insurance. If the facts stated above were alleged in a complaint and were established at trial, Farmers could be found liable on a joint venture theory.

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[8] *Grant v. Weatherholt* (1954) 123 Cal.App.2d 34, 45 (imputing liability for fraud to all joint venturers).

[9] *Holtz v. United Plumbing & Heating Company* (1958) 49 Cal.2d 501, 506.

C. Group Inc. could be held liable on an alter-ego theory

1. *The other Farmers entities are merely instrumentalities or conduits of Group Inc.*

Under the joint venture theory discussed above, Group Inc. faces liability based on agency. But given the structure of Farmers, and Group Inc.'s role within that structure, it could also be held liable on an alter ego theory of liability. There is no litmus test to determine when the alter ego theory will allow the corporate veil will be pierced; rather the result will depend on the circumstances of each particular case.[10] The determination of whether an alter ego relationship exists is a question of fact.[11]

The California Supreme Court explained in *Mesler v. Bragg Management Co.*,[12] that there are two general requirements for application of the alter ego doctrine: (1) a unity of interest and ownership so that the separate personalities of the parent corporation and its subsidiaries no longer exists and (2) that, if the acts are treated as those of the parent corporation alone, an inequitable result will follow.

With respect to the first factor, a plaintiff can establish a unity of interest by showing manipulative conduct by the parent toward the subsidiary that relegates the sub to the status of merely an instrumentality, agency, conduit or adjunct of the parent.[13] Examples of conduct that will justify an alter ego finding include "the manipulation of assets and liabilities between entities so as to concentrate the assets in one and the liabilities in another";[14] overlap in management between the parent and the sub, the commingling of funds and other assets of the two entities, or the holding out by one entity that it is liable for the debts of the other.[15]

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[10] *Mesler v. Bragg Management Co.*(1985) 39 Cal.3d 290, 300.
[11] *Las Palmas Associates v. Las Palmas Center Associates* (1991) 235 Cal.App.3d 1220, 1248.
[12] *Ibid*.
[13] *Institute of Veterinary Pathology, Inc. v. California Health Laboratories, Inc.* (1981) 116 Cal.App.3d 111, 119-120.
[14] *Associated Vendors, Inc. v. Oakland Meat Co.* (1963) 210 Cal.App.2d 825, 840.
[15] *Roman Catholic Archbishop v. Superior Court* (1971)15 Cal.App.3d 405, 411; *Sonora Diamond Corp. v. Superior Court* (2000) 83 Cal.App.4th 523, 539.

The facts alleged above are more than sufficient to satisfy these factors. Funds between the entities are transferred and then loaned back, amounting to commingling or diversion of assets. Assets purchased by Group Inc. are used by other entities. Group Inc. owns many of the other entities outright, and manages and controls entities it does not own. Management is interlocking. Some entities are mere shells, with no employees or tangible assets, except those provided by Group Inc. Group Inc. procures and provides labor, services and merchandise for other entities. Given its unified marketing system, purchasers of insurance believe they are buying protection from Farmers, a massive insurer, not just a smaller entity within the group.

Ultimately, a court could conclude if the facts alleged above were established that Group Inc. controls Farmers, using the smaller entities as mere conduits or instrumentalities for the conduct of its business. The first *Mesler v. Bragg Management* factor is therefore amply satisfied.

2. *The facts alleged show that treating Group Inc. as a distinct entity would sanction an abuse of corporate immunity*

Group, Inc's response to this showing is typically that the second part of the *Mesler* test is not met, because the various exchanges meet the minimum statutory requirements for capitalization, and therefore have adequate assets to respond in damages to a plaintiffs' claims. Group Inc. cites *Tomaselli v. Transamerica Ins. Co.,*[16] to argue that the potential of a lower punitive damages award that could result from basing punitive damages on the net worth of, say Truck standing alone, cannot provide the requisite injustice necessary to pierce the corporate veil.

Tomaselli does not, however, establish the blanket rule Group Inc. suggests. The relevant passage in *Tomaselli* says, "Here, alter ego was not litigated or decided, nor is there any significant showing of unity of interest. More importantly, there is nothing to

[16] *Tomaselli v. Transamerica Ins. Co.* (1994) 25 Cal.App.4th 1269, 1282-86

suggest how an 'injustice' would befall Tomasellis if the punitive damage award were limited to a percentage of appellant's value rather than that of the parent company."[17]

Since the alter ego issue was not even litigated in *Tomaselli,* it is unsurprising that no showing of injustice was made. Had the facts there been similar to those alleged above, the court's comments would not have been accurate. On the facts stated above, there would be demonstrable injustice in allowing Group Inc. to control Farmers and yet escape liability for its own wrongful conduct.

First, Group Inc. touts Farmers collective size and financial strength in selling its insurance products to the public. It would be unjust to allow it to sell its products based on the financial wherewithal of the entire Farmers entity, but restrict its insured's right of recovery to a single part of the entity with only a fraction of the entity's assets.

Second, the purpose of punitive damages is to punish wrongdoing and thereby to protect the public from future misconduct, either by the same defendant or other potential wrongdoers.[18] There is injustice in allowing Group Inc. to engage in wrongful conduct through its control and domination of the various Farmers entities, and to siphon capital from those entities for its own benefit, while shielding itself from any potential liability for that wrongdoing.

The Court of Appeal in *Delos v. Farmers Insurance Group, Inc*.[19] recognized these points, explaining that allowing Group Inc. to avoid liability in that case "would deprive plaintiff of redress against the party primarily responsible for its injuries."[20] Here, the facts alleged above demonstrate this injustice. Group Inc. could therefore properly be held liable on an alter ego theory.

3. *Group Inc. has litigated this issue and lost*

Two decisions of the California Court of Appeal, one published, and one unpublished, have held that Group Inc. can be liable for bad faith, even though it did not

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[17] *Tomaselli,* 25 Cal.App.4th at 1285, 1286.
[18] *Adams v. Murakami* (1991) 54 Cal.3d 105,110.
[19] *Delos v. Farmers Insurance Group, Inc.* (1979) 93 Cal.App.3rd 642, 652.
[20] *Ibid*.

issue the policy in question. In *Delos*, the published decision, found that Group, Inc's role as attorney-in-fact for the insurance exchange that issued the policy required a departure from the normal rule that only the entity issuing the insurance policy can be liable to an insured for bad faith.[21] *Delos* based this finding on the role that Group Inc. played in controlling the insurer, and affirmed a punitive damages award against Group Inc.

Group Inc. will argue that *Delos* was based on violations of Ins. Code § 790.03, which no longer affords a private right of action, and that it applies only when an insured would be wholly without redress unless the claim against Group Inc. was permitted. These point are drawn from *Fillipo Industries Inc. v. Sun Ins. Co*.[22] A closer reading of *Fillipo* shows its observations about *Delos* were off-target.

First, *Delos* affirmed a bad-faith claim against Group Inc. based on the common-law claim of breach of the implied covenant of good faith and fair dealing.[23] While violations of Ins. Code § 790.03 may have been used to prove that breach, the underlying claim was based on the common law.

Second, plaintiffs in *Filippo* sought to use *Delos* for the general proposition that a non-party to the insurance contract could be liable for bad faith. As the *Filippo* court noted, there was no showing that the insurer there was part of a reciprocal exchange.[24] The considerations of Farmers's structure that underlie *Delos* therefore did not apply.

Third, Group Inc. and the *Fillipo Industries* misread *Delos* when they suggest that Group Inc. was held liable in that case because there was no other entity from which plaintiffs could obtain redress. Rather, the *Delos* court emphasized that to allow Group Inc. to escape liability would deprive plaintiff of "redress *against the party primarily responsible for damages*."[25] (Emphasis added.) There was no suggestion in *Delos* that the other Farmers defendant, Farmers Insurance Exchange, which had issued the policy,

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[21] *Delos*, 93 Cal.App.3rd at 652.
[22] *Fillipo Industries Inc. v. Sun Ins. Co*. (1999) 74 Cal.App.4th 1429, 1443.
[23] *Delos*, 93 Cal.App.3rd at 650, 651, 658.
[24] *Fillipo Industries*, 74 Cal.App.4th at 1443.
[25] *Delos*, 93 Cal.App.3rd at 652.

could not respond in damages. Rather, the Court was explaining that it was unfair to allow Group Inc. to escape liability when it was the primary wrongdoer. This argument would apply here, with equal force.

This issue was also decided against Group Inc. by the Second Appellate District, in 1993 in *Cleveland v. Fire Insurance Exchange, Farmers Group, Inc.*,[26] an unpublished opinion. (UP's Request for Judicial Notice, Exhibit "1.") In that case, the insurance policy was "issued" by Fire Insurance Exchange and Group Inc. was named as a defendant to the breach of contract and bad faith causes of action. (*Cleveland, supra,* at 12.) The court affirmed a bad-faith verdict, including punitive damages, against Group Inc.

Given *Delos* and *Cleveland*, Group Inc. should be collaterally estopped to continue to litigate this issue. A party is collaterally estopped from relitigating an issue already decided in a prior case if: (1) the issue decided in the previous litigation is identical with that presented in the instant action, (2) there was a final judgment on the merits in the first action, and (3) the party against whom the plea of collateral estoppel is asserted was a party to the first action.[27] The party asserting collateral estoppel need not have been a party to the action; nor is there any bar to its affirmative use. [28]

While the doctrine should not be applied mechanically or blindly, the purpose of collateral estoppel is to prevent vexatious litigation with its attendant expense both to the parties and the public.[29] Here, Group Inc. brings the same arguments over, and over again, in cases that have come to UP's attention. Attached hereto as Exhibits 2 - 9 to UP's request for judicial notice are orders and minute orders from in other actions against

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[26] *Cleveland v. Fire Insurance Exchange, Farmers Group, Inc.* (1993) 2nd District, Div. 3, No. B 062941. Pursuant to California Rules of Court, an "[unpublished] opinion may be cited or relied on: (1) when the opinion is relevant under the doctrines of law of the case, res judicata, or collateral estoppel . . ." (Cal. Rules of Court, Rule 977(b)(1).)
[27] *Mountain Home Properties v. Pine Mountain Lake Assn.* (1982) 135 Cal.App.3d 959, 964, citing, *Bernhard v. Bank of America* (1942) 19 Cal.2d 807, 810-813.
[28] *Ibid*.
[29] *Ibid*.

Group Inc. in the Superior Courts, denying its demurrers and motions for summary judgment, which raise the same issue.

CONCLUSION

If a plaintiff obtained the proper information, it could plead and prove a set of facts that would allow a judgment to be entered against Farmers as an entity, and against Group, Inc., for controlling the entity. This Court should therefore not decide this case in a manner that would foreclose other Farmers insureds in other cases from pleading these facts and proceeding on the legal theories discussed above.

Dated: February 5, 2002.

Respectfully submitted,

SHERNOFF, BIDART & DARRAS,

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