IN THE COURT OF APPEAL FOR THE STATE OF CALIFORNIA
FIRST APPELLATE DISTRICT, DIVISION THREE

Randall Chapman,

Plaintiff and Respondent/Cross-Appellant,

vs.

UnumProvident Corporation; The Paul Revere Life Insurance Company; Provident Life and Accident Insurance Company; David W. Hover; and Does 1-20,

Defendants and Appellants/Cross-Respondents.

Appeal from the Superior Court of Marin County
Case No. CV012323
The Honorable Lynn O'Malley Taylor

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INTRODUCTION

This should have been a straightforward case about whether, and to what extent, an ophthalmologist was unable to perform the important duties of his occupation as a result of a "specific phobia" of performing eye surgery and hence was entitled to benefits under two disability policies he owned. The insurers investigated his claim for over a year, paying it in full for much of that period. In the process, they uncovered a substantial number of red flags—including, for example, the facts that (i) though claiming that he had this phobia throughout his career, he never brought it to the attention of anyone until he went to a psychiatrist who was a med-school classmate of his and asked about whether he could qualify for disability benefits and (ii) he then refused to undertake either of the psychiatrist's two treatment recommendations. After several in-house psychiatric, psychological, and medical consultants reviewed his medical records, the insurers concluded that he was not disabled under his policies and denied his claim.

Out of this basic corpus of facts arose a bad-faith claim, accompanied by a request for ***$335,000,000*** in punitive damages. The allegation of bad faith barely touched on the actual handling of plaintiff's claim. Instead, plaintiff regaled the jury with stories of corporate greed and misconduct told by three former employees who had no involvement in or knowledge of the handling of his claim and never connected their "bad company" testimony to anything that took place in the resolution of that claim.

Evidently, the strategy worked. After hearing the "bad company" testimony and being exhorted by plaintiff's counsel to return a nine-digit punitive award, the jury found defendants liable for breach of contract and bad faith, awarding $1,676,301 in compensatory damages and $30,000,000 in

punitive damages, which the trial court ordered remitted to $1,127,405 and $5,000,000 respectively.

Under both California law and the U.S. Supreme Court's decision in *State Farm Mutual Automobile Insurance Co. v. Campbell* (2003), 123 S.Ct. 1513, which post-dated the trial court's resolution of the post-trial motions, the remitted judgment is unsustainable.

First, because the testimony of the three former employees lacked any nexus to the handling of plaintiff's claim, it was irrelevant to any issue in the case. Accordingly, the trial court erred in admitting it, necessitating, at minimum, a new trial. Moreover, because, in the absence of that distracting testimony, there is no evidence to support a finding of bad faith, the more appropriate remedy is j.n.o.v.

Second, even if there were a basis for sustaining the finding of bad faith, the evidence comes nowhere near meeting California's strict standard for the imposition of punitive damages—clear and convincing evidence that the defendant's conduct was so contemptible that it would be despised by ordinary decent people.

Third, at minimum, a new trial on punitive damages is necessary because the trial court committed prejudicial error by failing to prohibit manifestly improper arguments of counsel (including blatant appeals to bias against out-of-state corporations and the outlandish request for a nine-digit punitive award) and then compounded the error by refusing to instruct the jury on two critical constitutional limitations on punitive damages that were expressly recognized by the U.S. Supreme Court in *State Farm*.

Finally, *State Farm* establishes that the $5,000,000 remitted punitive award remains unconstitutionally excessive. Under *State Farm*, no more than a $1,000,000 punishment is permissible.

STATEMENT OF THE CASE

After The Paul Revere Life Insurance Company ("Paul Revere") and Provident Life and Accident Insurance Company ("Provident") terminated his disability benefits payments, plaintiff Randall Chapman sued them and their ultimate corporate parent, UnumProvident Corporation, in Marin County Superior Court. In a trifurcated trial, the jury found defendants liable for breach of contract, breach of the covenant of good faith and fair dealing, and punitive damages. The jury awarded the full amount of total disability benefits that were unpaid as of the date of trial, the present value of the benefits that would be owed to Chapman were he to remain totally disabled until age 65, emotional distress damages of $125,000, and punitive damages of $30,000,000. On post-trial motions, the trial court held that there was insufficient evidence to support the jury's finding of total disability and that the emotional distress and punitive awards were excessive. The court ordered a new trial unless Chapman agreed to remit the economic damages to $1,112,405 (the stipulated value of past and future residual disability benefits), the emotional distress damages to $15,000, and the punitive damages to $5,000,000. After Chapman did so, the trial court entered a modified final judgment on April 25. Defendants timely filed a notice of appeal on May 19, 2003.

STATEMENT OF FACTS

1. The Policies.

In November 1983, Provident issued Dr. Chapman an individual noncancellable disability insurance policy, and, in July 1987, Paul Revere issued him a similar policy. Although Provident's parent company would later acquire Paul Revere's parent and the two companies' claim-handling functions would be consolidated, when the policies were issued, Provident and Paul

Revere were rivals in the disability insurance industry. Nevertheless, Chapman's policies provided substantially similar benefits: In the event that he suffered a "total" disability that prevented him from performing his important duties as an ophthalmologist, each would afford Chapman a specified monthly benefit for as long as he remained disabled, through age 65. And in the event that he suffered a "residual" disability that limited but did not absolutely preclude him from working as an ophthalmologist, each would provide benefits to make up for the resulting monthly shortfall in his income.

The Paul Revere policy defined "Total Disability" to mean that, because of injury or sickness:

a. You are unable to perform the important duties of Your Occupation; and

b. You are under the regular and personal care of a Physician.

Plaintiff's Trial Exhibit 14, at § 1.9. The Provident policy similarly defined "Total Disability" to mean that, because of injuries or sickness:

1. you are not able to perform the substantial and material duties of your occupation; and,

2. you are under the care and attendance of a Physician.

Plaintiff's Trial Exhibit 13, at 4. Meanwhile, the Paul Revere policy defined "Residual Disability" to mean that, because of injury or sickness:

a. (1) You are unable to perform one or more of the important duties of Your Occupation; or

(2) You are unable to perform the important duties of Your Occupation for more than 80% of the time normally required to perform them; and

b. Your Loss of Earnings is equal to at least 20% of Your Prior Earnings while You are engaged in Your Occupation or another occupation; and

c. You are under the regular and personal care of a Physician.

Plaintiff's Trial Exhibit 14, at § 1.10. And the Provident policy similarly defined "Residual Disability" to mean that, because of injuries or sickness:

> 1. you are not able to do one or more of your substantial and material daily business duties or you are not able to do your usual daily business duties for as much time as it would normally take you to do them;
> 2. you have a Loss of Monthly Income of at least 20%; and
> 3. you are under the care and attendance of a Physician.

Plaintiff's Trial Exhibit 13, at 7.

Chapman also received a "specialty letter" clarifying that Paul Revere would determine his occupation for purposes of the policy it issued to him by comparing the "important duties" he was performing "immediately prior to the time disability begins" with those he continued to be able to perform after the onset of disability. PRLCL00447.[1/]

2. Chapman's Disability Claim and Defendants' Investigation.

For over two decades, Chapman practiced ophthalmology, providing general eye care and performing conventional and laser ophthalmic surgery. In June 1999, however, he contacted Dr. Harvey Lerchin—an old medical school classmate who was now practicing psychiatry—and scheduled an appointment. RT40-41. During his initial session with Dr. Lerchin, Chapman reported suffering "the gradual onset & escalation of anxiety features (dread, worry, mental preoccupation, sleep disturbance, tremor, apprehension, depressed mood) relative to having to perform eye surgery." PRLCL00040. Chapman explained to Lerchin that he had stopped performing surgery and that his "non-surgery office practice [was] going well (although reportedly far less lucrative for him)." *Id.* According to Lerchin's notes, Chapman also

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[1/] References to "PRLCL___" are to the claim file, which was admitted into evidence as Plaintiff's Exhibit 18.

used the first visit to "raise[] questions as to whether or not he [could] claim disability insurance benefits on a pro-rata basis." *Id*.

Just a few weeks later—in July 1999—Chapman submitted claims for total disability benefits under both of his policies.[2/] PRLCL00007-10. Describing the duties of his occupation as including "ophthalmic surgery and preparation," "pre-post surgical care," and "general eye care" (*i.e.*, eye exams, treatment of eye diseases, etc.), Chapman premised his phobia-related disability claim on an "[e]motional disorder on going [sic] for years that became intolerable to do surgery." PRLCL00009; *see also* PRLCL00133 (Chapman reported to Lerchin that "[h]e has since childhood been prone to anxiety episodes, performance anxiety and 'high strung' demeanor").[3/] In response, defendants (who, by that time, were commonly owned and had consolidated their claim handling) began an investigation of Chapman's claim.

Despite having doubts about the validity of that claim no later than November 1999, defendants continued to investigate the claim for almost a year—and paid him more than $50,000 (PRLCL00432)—before deciding to deny further benefits (PRLCL00424).

Specifically, after Chapman filed his notice of claim in July 1999, defendants obtained from him a completed claim form, as well as an Attending Physician Statement from Dr. Lerchin. PRLCL00007-11. Upon receiving that information, defendants requested and obtained medical records from the

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[2/] He did not then, or at any later point, file a claim seeking residual disability benefits.

[3/] Chapman did not explain either in his claim form or at any later point in the investigation of his claim why a condition that he had "since childhood" suddenly prevented him entirely from doing what he had done so many times for so many years (RT17 (pre-disability, Chapman had performed some 175-200 ophthalmic surgeries annually)).

treating physicians Chapman identified, namely, Drs. Lerchin, Lambert (a nephrologist treating Chapman for a chronic kidney condition), and Hoke. PRLCL00009, 00015-43. Jean-Marie Merritt, who has a Master's degree in rehabilitation counseling and over 20 years experience in the mental health field, then called Lerchin on defendant's behalf to obtain additional information about Chapman's condition. PRLCL00054. She followed up on November 23 with a letter confirming that discussion and a Psychiatric Assessment Form ("PAF") for Lerchin to prepare. PRLCL00053-61.

Lerchin returned the completed PAF as well as a corrected copy of Merritt's letter, on which he noted that "Dr. Chapman has no compelling reason to resume his surgical practice beyond his obvious loss of status and partial loss of income" (PRLCL00097)—thus suggesting that Chapman lacked interest in continuing that part of his former practice, especially if he received income replacement benefits from defendants. Lerchin reported on the PAF that Chapman did not have any current symptoms beyond his baseline social inhibition/withdrawal/anxiety—with which Chapman had lived, and worked, all his life. PRLCL00086-90. Lerchin assigned Chapman a Global Assessment of Functioning ("GAF") score of 75 (PRLCL00086), which defendants' consulting psychologist, Dr. Alex Ursprung, explained at trial denotes a high level of functioning that "would describe most of us in this room" (RT875; *accord* RT352 (Lerchin testimony)).

Lerchin also detailed his treatment recommendations of behavior modification (a series of therapy sessions tailored to ameliorate or extinguish the symptoms of a specific phobia such as the one he diagnosed in Chapman (RT501-504)) and Inderal (a prescription medication shown in clinical trials

to be effective in controlling surgeons' hand tremors (RT152-54)).[4/] Lerchin specifically reported that Chapman refused to try Inderal. PRLCL00089. More generally, Lerchin recorded that Chapman had no symptoms and that his response to treatment to date was "[e]xcellent." *Id.*

Defendants then assigned Dr. Frederic Schwartz, a consulting specialist in internal medicine, to assess the merits of Chapman's claim that he could not take Inderal because it posed a danger to his kidneys. PRLCL00072. Schwartz concluded that Lerchin's prescription of Inderal was "clinically appropriate" and would not have a negative impact on Chapman's kidney condition (*id.*)—a conclusion that was consistent with the medical opinion of Chapman's treating nephrologist, Dr. Mark Lambert (RT563, 566).

Defendants also asked Dr. Ursprung to review Chapman's file. PRLCL00085. After a thorough review of Lerchin's treatment notes, Ursprung expressed "serious concerns" about the validity of Chapman's claim, including (1) Chapman reported a long history of anxiety yet had never sought treatment for it before; (2) Chapman raised the question of filing a disability claim during his first session with Lerchin; (3) Chapman refused a reasonable recommendation of Inderal; (4) Chapman's symptoms of hand tremors were purely self-reported; and (5) Chapman had not engaged fully in treatment. PRLCL00100-01.

In February-March 2000, defendants obtained updated psychiatric records from Lerchin, which reported that Chapman's "[m]ental status is

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[4/] At trial, Lerchin testified that he "eventually came to the conclusion that [Inderal] was not appropriate treatment." RT297. But he also clarified that this change of heart followed his consultations with plaintiff's counsel in October 2001 (long after defendants had made their final claim determination), that it reflected a legal rather than a medical judgment, and that he never included it in his treatment notes or otherwise communicated it to defendants. RT297, 368-69.

normal in all parameters." PRLCL00135. The records also showed that, on Lerchin's advice, Chapman had attended two sessions with a behavioral therapist, Dr. Corey Bercun, but reported that Chapman had informed Lerchin—inaccurately—that Bercun had not recommended further treatment. PRLCL00137.[5/]

Because of these red flags, defendants dispatched a field representative to collect additional information from Chapman. PRLCL00160. Chapman's attorney informed the field representative that Chapman had initially sustained his prior level of net income despite his supposedly disabling condition (PRLCL00161)—a factor directly relevant under the policies to his eligibility for residual disability benefits (Plaintiff's Trial Exhibit 14 (Paul Revere Policy), at § 1.10; Plaintiff's Trial Exhibit 13 (Provident Policy), at 7). And Chapman's tax accountant explained that, although Chapman's income later dropped by $60,000, the change resulted from insurance cost caps on patient billings and not a decreasing workload. PRLCL00163. The field representative specifically indicated defendants' concerns about certain aspects of the claim, and, in particular, questioned Chapman directly about his refusal to take Inderal and about the fact that he was attending only infrequent psychiatric sessions with Lerchin. PRLCL00161-62; RT1782.

On May 25, defendants requested, and subsequently obtained, records from kidney tests that Chapman had undergone. PRLCL00269-73. Dr. Schwartz reviewed those records—which reported "[n]o significant abnormality" (PRLCL00273)—and concluded, once again, both that Lerchin's

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[5/] Dr. Lerchin's notes indicated skepticism about what Chapman had told him. PRLCL00137 ("No further treatment recommended, it seems. * * * I will need to confer with Dr. Bercun."). In fact, Dr. Bercun testified at trial that he continued to believe that behavior modification therapy could help Chapman yet Chapman had unilaterally abandoned treatment. RT515-18.

prescription of Inderal would be an appropriate treatment and that Chapman had no medical condition preventing him from performing his occupational duties. PRLCL00297-98. Next, on September 8, Laurie Ghiz, a psychiatric consultant, reviewed the claim file and concluded that the information in it reflected that Chapman had chosen to stop doing surgery and did not support a finding of psychiatric impairment. PRLCL00340-42. On September 11, Ghiz spoke with Lerchin and confirmed that Chapman's status had not changed from what Lerchin had previously reported to defendants and what he had detailed in his treatment notes running through March 2000. PRLCL00343. Later that month, defendants requested and received an updated PAF and additional treatment records from Lerchin (PRLCL00378-87), which Ghiz found to confirm the conclusion that Chapman did not have a disabling condition (PRLCL00388). On September 26, Dr. Ursprung conducted a second review of the claim file and made the same determination. PRLCL00389-90.

On the basis of this medical consensus, defendants denied Chapman's total disability claim by letter dated October 4, 2000. PRLCL00417-24. Four months later, after Chapman provided additional information, Schwartz and Ghiz again reviewed the claim, but came to the same conclusions. PRLCL00473-76. Then, Steven Carlson, an appeals consultant in defendants' Quality Support Department, reviewed Chapman's entire file before upholding the denial of benefits in April 2001. Carlson's denial letter provided a detailed analysis of the claim and spelled out the reasons for the denial, supported by, among other things, the opinions of Drs. Ursprung and Schwartz. PRLCL00618-23.

Meanwhile, throughout this extensive and prolonged investigation into Chapman's medical claims, defendants made numerous requests for proper

documentation of his financial condition (*see, e.g.*, PRLCL00050-51; PRLCL00104-14; PRLCL00125-26; PRLCL00160-63; PRLCL00240-41; PRLCL00268; PRLCL00274; PRLCL00278; PRLCL00336-37; PRLCL00355-58), which Chapman knowingly failed to provide (PRLCL00314) despite express policy provisions stating that such information was a prerequisite to receiving benefits (*see* Plaintiff's Trial Exhibit 14 (Paul Revere Policy), at § 9.4; Plaintiff's Trial Exhibit 13 (Provident Policy) at 8). Nevertheless, defendants paid him benefits until March 3, 2000, when they informed him that they could no longer pay him without documentation of his financial condition. PRLCL00240.

3. Proceedings Below.

a. *The trial.*

Chapman sued defendants, alleging breach of contract and bad faith, and seeking punitive damages. The Superior Court conducted a trifurcated trial, with the jury considering the breach of contract claims in the first phase, the bad faith claim and liability for punitive damages in the second, and the amount of punitive damages in the third.

Phase I. Although Chapman had never filed an insurance claim seeking residual disability benefits, and had never submitted the monthly financial information required under the terms of his policy to establish the amount of such benefits, his breach of contract action included claims for residual as well as total disability benefits. In his trial testimony, he conceded that: (a) at the time that he submitted his notice of claim for total disability benefits, he was working as an ophthalmologist "doing general eye care" on a part-time basis (RT123); (b) although no longer performing surgery, he continued to perform all the other tasks of an ophthalmologist that he had performed prior to the date he identified on his claim form as the onset of his disability (RT93, 123); and

(c) in the period after he stopped doing surgery, he was able to both increase his gross billings and reduce his overhead by examining patients himself instead of hiring an optometrist to do so. RT92-93. When asked whether it was true that his alleged disability was at best residual under the terms of his policies because office ophthalmology was an important duty of his practice both before and after filing his claim, Chapman agreed, responding: "You could say that." RT121. And his counsel acknowledged during Phase I closing arguments that a finding of residual rather than total disability would be "fair and reasonable" and "the right thing to do," and that a finding of anything more than residual disability would allow Chapman to "make money and get ahead of the game by getting disability benefits," which was "not what he's here for." RT1231-32. The trial court nonetheless submitted both the total and residual disability claims to the jury.

After extensive deliberations, the jury deadlocked as to whether Chapman was totally disabled. RT1319. But following an unorthodox procedure in which the jury was allowed to skip the total disability question, then, after resolving the residual disability claim in Chapman's favor, go back and redeliberate on total disability and then choose between its verdicts on the two questions (RT1341-42, 1359-61, 1453, 1463-65), the jury ultimately found Chapman totally as well as residually disabled—despite his judicial admissions that he was not totally disabled. The jury was not asked to find a specific amount of contract damages because the parties had stipulated that, in the event of a finding of liability, past benefits would be computed using formulas prescribed by the policies.

Phase II. In support of his claims of bad faith and punitive liability, Chapman relied primarily on the testimony of Mary Fuller (a former employee of UnumProvident and a predecessor company not involved with Chapman's

claims, whom the trial court permitted to testify as both a percipient witness and a paid expert), the videotaped deposition testimony of Dr. Fergal McSharry (a former in-house medical consultant at UnumProvident), and the deposition transcript from another case of Dr. William Feist (a former in-house medical consultant at Provident who left the company in 1996). Chapman offered their testimony to support his allegation that the handling of his claim was part of a corporate policy of improperly denying valid insurance claims. Although Fuller and McSharry each gave generalized testimony regarding defendants claim-handling practices, and Feist had given testimony in the earlier case regarding Provident's practices prior to the acquisition of Paul Revere's parent by Provident's parent, none of the three tied the handling of Chapman's claim to any of the practices of which they were critical.

Despite the lack of nexus between the "bad company" evidence and the handling of Chapman's claim, the trial court submitted the bad faith claim and the question of punitive liability to the jury, which awarded Chapman $1,109,093 in future benefits and $125,000 in emotional distress damages on the bad faith claim, and also found punitive liability.

Phase III. Finally, Chapman offered voluminous data on defendants' net worth and cash reserves (which each state requires insurers to maintain for payment of future claims), and argued that the jury would need to impose punitive damages of as much as 10% of defendants' corporate wealth if it wished defendants even to notice the sanction. In support of this pitch, Chapman's counsel drummed up bias against defendants as wealthy corporations from "back East" (RT2889), urging the jurors to apply an us-against-them mentality in setting a punishment. Counsel also made *ad hominem* attacks on defendants, including likening their corporate

management to the perpetrators of atrocities in Nazi Germany. RT2764. In response, the jury imposed a massive punitive exaction of $30,000,000.

b. The post-trial proceedings.

The Superior Court did not take the same view of the evidence that the jury did. Following extensive briefing and a hearing on defendants' post-trial motions, the court found sufficient evidence to support the jury's finding of residual disability but no basis for the finding of total disability.[6/] It also found both the emotional distress and the punitive damages to be excessive. Accordingly, the court ordered a new trial unless Chapman agreed to remittiturs of the award of past benefits to $247,657, the award of future benefits to $864,748, the emotional distress damages to $15,000, and the punitive damages to $5,000,000.

Chapman immediately accepted the remittiturs of the past and future benefits but deferred decision on the remittiturs of the emotional distress and punitive awards. After the U.S. Supreme Court issued its ruling in *State Farm Mutual Automobile Insurance Co. v. Campbell* (2003) 123 S.Ct. 1513, clarifying the law governing several key aspects of this case, Chapman immediately accepted the remaining remittiturs.

ARGUMENT

I. DEFENDANTS ARE ENTITLED TO JUDGMENT NOTWITHSTANDING THE VERDICT OR, AT MINIMUM, A NEW TRIAL ON PLAINTIFF'S BAD-FAITH CLAIM.

To prevail on a bad-faith claim, an insured must prove that the insurer "fail[ed] or refus[ed] to discharge contractual responsibilities, prompted not by an honest mistake, bad judgment or negligence but rather by a ***conscious and***

[6/] Defendants in their post-trial motions did not challenge the jury's finding of contract liability for residual disability benefits, and we do not do so now.

deliberate act." *Careau & Co. v. Sec. Pac. Bus. Credit, Inc.* (1990) 222 Cal.App.3d 1371, 1395 (emphasis added). A mere finding that the insurer breached its contract is insufficient because bad faith involves "unfair dealing rather than mistaken judgment." *Congleton v. Nat'l Union Fire Ins. Co.* (1987) 189 Cal.App.3d 51, 59 (internal quotation marks omitted). If there was a genuine dispute over the insurer's liability for coverage, ***as a matter of law*** the insurer cannot be held liable for bad faith unless the plaintiff proves that the insurer conducted a biased investigation. *See, e.g.*, *Chateau Chamberay Homeowners Ass'n v. Associated Int'l Ins. Co.* (2001), 90 Cal.App.4th 335, 347.

In this case, Chapman did not offer sufficient evidence to support a finding that defendants consciously and deliberately denied his claim in bad faith, and the trial court so held. Order After Hearing at 5 ("[t]here is no evidence of a deliberate intent to deny plaintiff's legitimate claim"). Nor did he offer sufficient evidence of a biased investigation. Instead, he focused the jury's attention on a patchwork of trial and deposition testimony from three of defendants' former employees concerning allegedly improper claim-handling practices. Because he never showed that those practices were employed in, or had any bearing on, the handling of his own claim, however, the testimony was irrelevant to the issues in the case. And because Chapman relied heavily on this evidence in arguing that he had met the standards for bad faith and punitive liability and then in arguing for a nine-digit punitive award, this "bad company" evidence was self-evidently prejudicial. At minimum, therefore, defendants are entitled to a new trial in which this highly prejudicial and irrelevant testimony is excluded. But because no other evidence in the record can support the finding of bad faith, the more appropriate remedy is j.n.o.v.

A. Because The Trial Court Improperly Admitted The Evidence Upon Which The Finding Of Bad Faith Was Predicated, The Court Should, At Minimum, Grant Defendants An Unconditional New Trial.

To prevail on a bad-faith claim under California law, a plaintiff must prove, *inter alia*, that whatever allegedly improper conduct he attributes to the defendant was the cause of his injury—*i.e.*, that any allegedly wrongful practices on the part of the insurer were employed in handling ***his*** claim. As a federal court recently explained in granting Provident summary judgment on bad faith, notwithstanding the plaintiff's invocation of much the same evidence that Chapman elicited here:

> Even if this Court accepted Plaintiff's evidence, Plaintiff fails to establish any link between Provident's actions with respect to this specific claim and the alleged plan attributed to Provident. For example, Plaintiff fails to show how the "practice" of denying claims affected and influenced the denial of his specific claim in particular. * * * Plaintiff's claim was individually examined, and Plaintiff's proffered evidence of a change in Provident's "goals" does not create a genuine issue for trial.

Cardiner v. Provident Life & Accident Ins. Co. (C.D. Cal. 2001) 158 F.Supp.2d 1088, 1106. Similarly, in *State Farm*, the Supreme Court held that "[a] defendant's dissimilar acts, independent from the acts upon which liability was premised, may not serve as the basis for punitive damages. A defendant should be punished for the conduct that harmed the plaintiff, not for being an unsavory individual or business." 123 S.Ct. at 1520, 1523. Accordingly, defendants in this case can be held liable only if, and only to the extent that, the misconduct alleged at trial was "direct[ed] toward" Chapman himself. *Id.* at 1521.

Chapman modeled his litigation strategy in this case on the one that had worked so well before the jury in *State Farm* (producing a $145,000,000 punitive verdict) and, as a result, committed the very transgression that the

Supreme Court has since condemned. Specifically, through Fuller's testimony and the McSharry and Feist depositions, Chapman presented a litany of supposedly improper claim-handling practices that the various defendants allegedly employed at different times over the course of almost a decade, including charges that defendants pressured claim handlers, implemented improper economic incentives, and orchestrated roundtable reviews to deny valid claims. But, as in *State Farm*, Chapman adduced ***no*** smoking-gun document, ***no*** testimony by any past or present employee of any of the defendants, ***no*** medical evidence, and indeed ***no*** evidence of any kind to establish the required nexus between his "bad company" evidence and the handling of his claim.

Fuller, whom the trial court permitted to appear over defendants' objection as both a percipient witness (though she had no involvement in the handling of Chapman's claim (RT1697)) and a paid expert, testified at length regarding "claims initiatives" instituted in the wake of the acquisition of Paul Revere's parent by Provident's parent, and what she viewed as inappropriate post-acquisition claim-handling procedures. RT1603-79; 1689-1835. But Chapman offered no evidence, whether through Fuller's testimony or otherwise, that the "claims initiatives" and "procedures" Fuller criticized had any impact on the handling of his specific claim, much less that his claim would have been paid but for those initiatives. *Cf. Cardiner*, 158 F.Supp.2d at 1106 (evidence of insurer's "goals" and "practice" of denying claims does not create jury question on bad faith absent evidence that such practices "affected and influenced the denial of [the plaintiff's] specific claim in particular"). To the contrary, in some instances, Fuller affirmatively acknowledged that "procedures" she disparaged were inapplicable to Chapman's claim. RT1779, 1819-20, 1824, 1834. And during cross-

examination she was forced to withdraw several other factually baseless criticisms of defendants' handling of the claim. *See, e.g.*, RT1785-86, 1790-94, 1826-27.[7/]

Indeed, Fuller specifically testified both in her deposition and at trial that defendants followed appropriate procedures in investigating Chapman's claim. *See* Fuller Dep. 17:7-20; 18:20-20:7; RT1630 ("[t]he procedures as they were initially developed appeared to be appropriate to me"). She further testified that defendants' claim-handling procedures were not set up for the purpose of denying legitimate claims (RT1735)—thus repudiating the fiction at the core of Chapman's theory of liability. Although Fuller insinuated that defendants' employees felt subtle pressure to deny legitimate claims (*see, e.g.*, RT1631, 1651-52, 1820), she also stated both that, as the head of one of defendants' "impairment units," she never instructed anyone to deny a valid claim (RT1717) and that, to her knowledge, no one else ever did either (RT1720). And although Fuller made generalized attacks on defendants' use of roundtable reviews—meetings during which claim handlers, medical consultants, and sometimes in-house lawyers would discuss particular claims and develop plans of action for investigating or processing those claims—she

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[7/] The closest Fuller came to criticizing the handling of Chapman's claim was when she opined that the timing of the denial in September 2000 could be explained only by the fact that September is the end of a financial quarter, when, according to Fuller, defendants put pressure on their employees to resolve claims. RT1664-66. But Fuller subsequently admitted that the determination of Chapman's claim followed hard on the heels of an entirely different kind of pressure—namely, pressure from Chapman's attorney to resolve the matter. And she went on to explain that such expedited claim handling "oftentimes" results when an insured gets an attorney involved and to conclude that the pressure brought to bear by Chapman's attorney "was a driver for" defendants' expedited review and coverage determination (RT1820-24), thereby entirely undermining the result-oriented speculation in which she engaged during direct examination.

acknowledged that the roundtable review of Chapman's own claim was not a mechanism to generate a denial but instead led to a field investigation in which Chapman was specifically informed of and questioned about the matters that remained of concern to defendants. RT1820. Moreover, Fuller stated that she did not know how other impairment heads at other locations—such as the one with responsibility for Chapman's claim—conducted their roundtable reviews. RT1819.

Taken all together, Fuller's vague, generalized criticisms of defendants' procedures not only had no connection to the denial of benefits in this case; as supposedly general company practices, they also had no basis whatsoever in her personal knowledge or experience. And although she testified as an expert on claim-handling practices, Fuller did not support her criticisms of defendants with reference to any California law or regulation or any insurance industry standard.

Accordingly, Fuller's recitation of defendants' supposed abuses was not merely insufficient to create a triable issue of fact as to the reasonableness of their conduct (*see Adams v. Allstate Ins. Co.* (C.D. Cal. 2002) 187 F.Supp.2d 1207, 1217-18; *Cardiner*, 158 F.Supp.2d at 1105); it was irrelevant to any issue in the case (*id.* at 1106).

The portions of McSharry's videotaped deposition that Chapman played at trial are, if anything, even less relevant. McSharry testified about UnumProvident's claim-handling practices in broad terms based solely on his experience as an employee during the 13-month period from November 2000 to January 2002—when he was fired for poor performance. McSharry testified that he worked only in UnumProvident's General Medical impairment unit in Chattanooga, Tennessee. McSharry Dep. 102:20-103:2. For this reason, he had little or no knowledge concerning the approximately 90 other doctors, 325

nurses, and 2,500 customer care specialists who worked in other impairment units or at other UnumProvident sites. Furthermore, McSharry admitted to a complete lack of any factual knowledge regarding any case for which he did not personally perform a review. *See id.* at 757:20-759:25, 760:5-11, 762:7-763:8. In short, McSharry had no knowledge concerning Chapman's claim; the procedures employed in the Worcester, Massachusetts facility where the claim was handled; the psychiatric impairment unit in Worcester with responsibility for the claim; or the doctors, consultants, and claim representatives who participated in the handling of the claim. *See id.* at 756:8-9. Indeed, the only pertinent thing McSharry did know is that, in his experience, the medical and claims professionals with whom he dealt in defendants' Appeals Unit made fair and valid assessments (*see id.* at 887:6-19)—testimony that goes a long way toward establishing defendants' good faith as a matter of law.

Feist's deposition testimony was the most tangential of all. In the first place, the deposition came from an entirely different lawsuit and therefore necessarily did not address the specifics of the handling of Chapman's claim. Beyond that, the deposition dealt with a different company and a different time period. Feist worked only for Provident, and his employment there terminated in 1996 (RT2018)—before Provident's parent acquired Paul Revere's parent and the companies conducted a best-practices review to develop unified claim-handling procedures (RT1616, 1629-30, 1759-60 (testimony of Mary Fuller)). He left Provident was fully three years before Chapman filed his claim in 1999 and more than four years before the claim was denied. Thus, though asserting in this deposition from an unrelated case that the "tenor" of roundtable reviews during his time at Provident in Chattanooga, Tennessee, had been to find ways to deny claims (RT2018, 2029), Feist did not purport to know about roundtable

reviews (or any other practices) at Paul Revere in Worcester, Massachusetts, either before or after the acquisition. RT2049. Finally, even if there were a basis for equating Paul Revere with pre-acquisition Provident, Feist admitted that, during his tenure at Provident, he was never involved in any decision to terminate a claim (RT2037) and that he could not remember ever seeing a claim file that he thought was mishandled (RT2038). That concession should have precluded admission of his dated deposition transcript. *See Yumukoglu v. Provident Life & Accident Ins. Co.* (D.N.M. 2001) 131 F.Supp.2d 1215, 1227-28 (finding Feist's general testimony about roundtables insufficient to raise a genuine question about whether Provident committed bad faith because Feist conceded "both that he has no personal knowledge of [the plaintiff's] claim and that he could not recall a single instance in which a decision to deny a disability claim was made at a Round Table session"), *aff'd* (10th Cir. 2002) 36 Fed.Appx. 378.

At trial, Chapman tried to tie the generalized Fuller/McSharry/Feist mudslinging to the handling of his claim by introducing into evidence documents regarding claim-handling initiatives and claim resolution rates that were prepared at Provident when it was still a competitor of Paul Revere. Chapman wove these documents into a tale of corporate malfeasance, in which Provident's senior management developed improper claim termination goals, infected Paul Revere with them after the merger, and then used them to inflict on claim handlers an aggressive program of denying valid claims. RT2678-82, 2695-712, 2756-62, 2885-89. But he offered no evidence that anyone involved in the handling of his claim was even aware of the alleged claim termination goals that he contended the documents had established, much less that the

investigation or resolution of his claim was the product of them.[8/] Thus, far from establishing the required nexus between the Fuller, McSharry, and Feist testimony and the handling of Chapman's own claim, the Provident documents suffered from precisely the same defect and tainted the trial in precisely the same way. *See Cardiner*, 158 F.Supp.2d at 1106 (granting summary judgment on bad faith because "Plaintiff fail[ed] to show how the 'practice' of denying claims affected and influenced the denial of his specific claim in particular").

Moreover, the trial court's errors in admitting the Fuller/McSharry/Feist testimony and the Provident documents were manifestly prejudicial. This evidence was the centerpiece of Chapman's argument that defendants committed bad faith and engaged in the kind of despicable conduct necessary for the imposition of punitive damages.[9/] RT2695-712, 2756-62. It also played a key role in his argument for a multimillion dollar punitive award.

[8/] Chapman's spin on the the documents was predicated on the false assumption that "termination" of a claim is a synonym for "denial." As both Ralph Mohney and Mary Fuller testified without contradiction, however, "termination" refers to closure of a claim ***for any reason***, including (most frequently) a return to work, the end of the benefit period, failure to meet the elimination period, the death of the insured, or a determination that the claim is not compensable. RT1715-16, 1718-19, 2283-85.

[9/] The prejudicial effect of the Feist testimony was compounded, moreover, by the fact that Feist had conveniently declared himself unavailable. Thus, Chapman's counsel were able to stage a dramatic reading of his deposition transcript, casting one of their own number in the role of Feist. RT2015-30. By doing so, they were able to dictate the tone and demeanor of the "witness," deprive defendants of the ability to cross-examine Feist about his lack of knowledge of the relevant facts of ***this*** case, and prevent the jury from judging Feist's credibility.

RT2885-89. Accordingly, at minimum, a new trial on bad faith and punitive damages is required.[10/]

B. The Evidence Does Not Support A Finding That Defendants Conducted A Biased Investigation.

Having found that "[t]here is no evidence of a deliberate intent to deny plaintiff's legitimate claim" (Order After Hearing at 5), the trial court nonetheless concluded that evidence of unreasonable investigative practices supports the finding of bad faith (*id.* at 3). But most of what the trial judge had in mind appears to have been the improperly admitted Fuller, McSharry, and Feist testimony. *See id.* at 2 ("taken as a whole [defendants'] procedures appeared to be designed to place defendants' interest ahead of the insured's and to avoid affording the insured a thorough investigation of his claim"). While, at minimum, admission of that highly prejudicial testimony requires a new trial, once it is discarded, no substantial evidence of bad faith remains. And hence, j.n.o.v. is the more appropriate remedy.

1. The handling of Chapman's claim was not inherently unreasonable in light of the overwhelming number of red flags in the claim file.

Although bad faith can be established if the insured proves that the insurer conducted an inadequate or biased investigation (*Chateau*, 90 Cal.App.4th at 348-49), "the reasonableness of the insurer's decisions and actions must be evaluated as of the time that they were made; the evaluation cannot fairly be made in the light of subsequent events that may provide evidence of the insurer's errors" (*id.* at 347). In other words, this Court's task in reviewing the investigation of Chapman's claim is to put itself in

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[10/] It should go without saying that the trial court's remittiturs did not and could not remedy its evidentiary errors. *See generally* C.C.P. § 662.5 (remittitur available only to correct excessive damage awards).

defendants' shoes and consider whether their actions were reasonable in light of what ***they*** knew at the time.[11/] When viewed from this standpoint, and taken all together, the claim form, medical records, and other information that Chapman, his treating physicians, and his accountant supplied added up to a decidedly questionable claim; and the more that defendants investigated, the more suspicious things looked. Specifically, the thorough and searching investigation that defendants conducted—which we describe above (*see* pages 5-11, *supra*)—produced the following information, all of which remained undisputed at trial:

a. Although supposedly suffering from "lifelong" anxiety and hand tremors (PRLCL00040; RT127-28), Chapman's very first documented appointment with a medical professional—and indeed, the first evidence that he had ever told anybody about his condition—was the June 1999 visit with Dr. Lerchin, during which Chapman asked his former classmate about whether he might be able to obtain disability benefits (PRLCL00040); he never mentioned his condition to his patients, his malpractice insurer, or the hospitals or chiefs of staff where he had surgical privileges (RT66-67, 100-06).[12/]

[11/] On appeal from the denial of a motion for j.n.o.v. on the ground of insufficiency of the evidence, this Court reviews *de novo* "whether any substantial evidence—contradicted or uncontradicted—supports the jury's conclusion." *See Sweatman v. Dep't of Veterans Affairs* (2001) 25 Cal.4th 62, 68.

[12/] Before that, the only suggestion that anything was amiss was Chapman's unilateral decision in February 1999 to remove himself from the hospital scrub schedule. RT66. He did so without first consulting any medical professional and without ever giving the hospital or anybody else an explanation (RT66-67); and he then waited nearly 5 months before contacting Lerchin. Even after ceasing to perform hospital procedures, Chapman continued to conduct office surgeries until after his first session with Lerchin (when, not coincidentally, Chapman was preparing his disability claim).

b. Although Chapman self-reported to Lerchin, and reported to defendants, that he suffered from debilitating hand tremors, sleeplessness, diarrhea, vomiting before surgery, and other substantial physical manifestations of a severe anxiety disorder, there is not a word in the claim file to suggest that Lerchin ever witnessed any of these symptoms firsthand.

c. Although Chapman reported pre-surgery vomiting, pacing the operating room, rushing through procedures, and hand tremors (PRLCL00040, RT100-03), from all appearances none of the trained medical personnel present in the operating room with him during any of the 175-200 surgeries he performed each year had ever witnessed any of these symptoms; and not one patient ever noticed any of them during operations performed quite literally before the patients' very eyes. RT103-06.

d. Chapman never identified a single person who could confirm the existence of any physical manifestation of his condition—not even his wife, who was in the best position to know whether he in fact suffered from such things as sleeplessness and night sweats before surgeries.

e. Chapman never gave any explanation—to Lerchin or anybody else—why, after performing 175-200 surgeries annually with a severe lifelong anxiety disorder, he awoke one day to discover that his condition now absolutely prevented him from operating ever again.

f. Although Lerchin made two reasonable treatment recommendations—Inderal and behavior modification—Chapman dismissed the first out of hand and made only a token gesture to try the second before electing to cease the treatments. Notably Chapman's own expert, Mary Fuller, testified that, in her capacity as a former overseer of claim handling, she would have expected an insured to follow his own physician's treatment recommendations (RT1797-99), thus confirming the reasonableness of the

suspicions that arose from Chapman's refusal to try Lerchin's prescribed treatment regimens.[13/]

g. According to Lerchin's treatment notes, Chapman explained his cessation of behavior modification therapy by reporting—improbably (and, as it turned out, inaccurately)— that Dr. Bercun had concluded after just two visits that no further sessions were appropriate. PRLCL00137.[14/]

[13/] Chapman explained to defendants' field representative that he would not take Inderal out of concern that it would exacerbate his kidney condition (PRLCL00162), and then, in response to the denial of his claim in October 2000, he obtained a letter from his treating nephrologist, Dr. Lambert, supporting his refusal to take the medication (PRLCL00444) and a letter from Dr. Lerchin stating that "[t]here is certainly no guarantee that [Inderal] will prove itself to be efficacious in the treatment of a specific tremor condition" (PRLCL00445). Because both letters post-dated the denial of the claim, they could not serve to allay the legitimate suspicion that had been aroused by Chapman's refusal to follow either of Lerchin's recommendations. And while the letters were available by the time of Carlson's appellate review, it is manifest from his letter denying the appeal that the refusal to follow Lerchin's recommendations was not a basis for his decision. PRLCL00618-23 In any event, both in deposition and at trial, Lambert opined that Inderal posed ***no*** danger whatsoever to Chapman's kidneys and was not contraindicated from a nephrological standpoint. RT563, 566. He further testified that Chapman had never revealed that the Inderal prescription had come from his psychiatrist and instead had represented that it was his insurance company that wanted him to take the medication. RT155-56, 557-59. As for Lerchin, he merely indicated that there were no guarantees, not that the medication wasn't worth trying.

[14/] At trial, Bercun confirmed that he had scheduled a third session with Chapman and expected the treatment to continue for several months, but that Chapman canceled the appointment and never made another. RT515-16. Bercun also testified that, with only two sessions under Chapman's belt, "I don't think we ever started behavior modification or really cognitive behavior therapy"; and Bercun explained that he had the "intent and the hope that I could have helped him, and if I couldn't, we would have evaluated that together to see if it made sense to continue or if he should pursue some other avenue." RT517-18.

h. After refusing to try Inderal and quitting behavior modification therapy, Chapman never asked Lerchin, Lambert, or anyone else for other treatment alternatives that might allow him to resume surgery. RT177-78, 358.[15/]

[15/] This fact alone should foreclose a finding of bad faith. As a matter of law in California:

> A disability policy that requires an insured claiming benefits to be "under the care and attendance" of a physician cannot reflect an intent of the parties that the insurer will be obligated to pay benefits even if the insured stubbornly refuses the only appropriate "care" recommended. * * * If, for instance, a patient's doctors urge surgical intervention as the only appropriate course of medical care, and the patient refuses to so submit, it is hard to see how that patient could, in any meaningful sense, still be "under the care and attendance" of a physician.

Provident Life & Accident Ins. Co. v. Van Gemert (C.D. Cal. 2003) 262 F.Supp.2d 1047, 1051.

Here, Chapman never started behavior modification therapy. RT517-18. He refused to try Inderal. PRLCL00089. He only sporadically attended psychiatric sessions with Lerchin. RT1782. And even when he saw Lerchin, he did not seek treatment designed to get him back into the operating room. *See, e.g.*, PRLCL00089 (care was palliative and not therapeutic); RT671-72 (same); PRLCL00382-85 (Chapman scheduled sessions not for anxiety disorder but for help dealing with unrelated issues of his mother's death and a dispute with his sisters). *Cf. Rosenberg v. Guardian Life Ins. Co. of Am.* (S.D.N.Y. Dec. 27, 2002, No. 00 Civ. 8198) [2002 WL 31885930, at *7] ("The plain meaning of the condition that Rosenberg be under the *regular* care of a doctor for the *cause* of the disability required, at a minimum, that Rosenberg consult with a physician more than sporadically and that the consultations seek care for the cause of the condition which Rosenberg claims disabled him."). Under *Van Gemert*, Chapman's refusal to pursue any of his doctors' reasonable treatment recommendations would preclude as a matter of California law not just a bad faith claim but probably even a breach of contract claim. *See* 262 F.Supp.2d at 1051. Moreover, even if this Court were to

i. Lerchin assigned Chapman a GAF score of 75 (PRLCL00086), which indicates essentially normal functioning (RT352, 875).

j. Chapman refused to provide defendants with monthly profit-and-loss statements or other proof of financial condition as required by his policies (PRLCL00314), thus preventing them from investigating whether he had sustained the 20% loss of income that might entitle him to residual disability benefits.

k. Chapman informed defendants' field representative that his net income initially remained the same after he ceased performing surgery. PRLCL00161.

l. Although Chapman's income later declined by $60,000, he attributed the decrease not to the cessation of surgery but to insurer cost-capping that had made the practice of ophthalmology less lucrative. PRLCL00163.

m. According to Lerchin's reports, Chapman did not miss surgery and did not appear to regret the fact that he would never again engage in it. PRLCL00135.

n. Chapman made no attempt to expand the non-surgical side of his ophthalmology practice, but instead remained content to work part-time while joining a golf club, traveling abroad, and generally participating in activities more consistent with a person enjoying the fruits of an early retirement than with one forced by illness to give up on the investment of years of study, training, and effort to build a medical practice and a professional reputation. PRLCL00040, PRLCL00385.

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disagree with the federal court's statement of California law, it certainly was not "inherently unreasonable" (*see Congleton*, 189 Cal.App.3d at 59) for Provident to have applied the same interpretation here that it did, with the court's blessing, in *Van Gemert*.

Taken all together and viewed from defendants' perspective at the time that they investigated and eventually denied Chapman's claim, this evidence in the file was sufficient to raise reasonable doubts in the minds of defendants' medical consultants and claim handlers about the validity of that claim. And that, in turn was sufficient to give rise to a genuine dispute over whether defendants were obligated to pay the claim. *Chateau*, 90 Cal.App.4th at 348-50. Indeed, we submit that ***anyone*** who stood in defendants' shoes would have had grave doubts about the claim. But all that matters here is that, to the extent that coverage was unclear, defendants cannot as a matter of California law be held liable for bad faith. *Id.* at 348 (a "genuine dispute" over the facts of the claim, like a genuine legal dispute, may bar recovery for bad faith as a matter of law); *accord Feldman v. Allstate Ins. Co.* (9th Cir. 2003) 322 F.3d 660, 669, *petition for cert. filed* (Oct. 6, 2003, No. 03-56) 72 U.S.L.W. 3093.

2. The trial court's bases for finding a biased investigation are patently inadequate.

Without addressing the numerous red flags that popped up during defendants' investigation of Chapman's claim, the trial court identified three bases for finding defendants' investigation to be biased. None amounts to bad faith.

First, the trial court pointed to defendants' failure to send Chapman for an Independent Medical Examination ("IME"). Order After Hearing at 3. Although, in his initial review of the file, Dr. Ursprung suggested a psychiatric IME to fill in some gaps in Chapman's file, he later concluded that an IME was unnecessary because Lerchin's supplemental treatment notes and Chapman's other medical records provided a full picture of his condition. RT851-53. In other words, in resolving Chapman's claim defendants effectively accepted the medical opinions and conclusions of his treating physician and concluded that they did not add up to a compensable psychiatric

impairment under the terms of the policies. It cannot be bad faith to accept the diagnosis of the insured's treating physician rather than requiring the insured to undergo an unnecessary IME. More broadly, at trial Chapman could point to no statute, rule, or other standard (nor are we aware of any) requiring an insurer to administer an IME under any circumstance at all.

Second, the trial court found the evidence sufficient to support a finding that one of the numerous individuals involved in handling the claim, Steven Carlson (who conducted the in-house "appellate" review), was unqualified, and that the procedure he employed did not result in an "objective, independent and thorough review of the denial of plaintiff's claim." Order After Hearing at 3. The only evidence about Carlson's training and the appropriateness of his review came, however, in the form of Fuller's bald assertion that he lacked sufficient experience to perform an appellate review. RT1673-74. But Fuller did not indicate the minimum experience required to conduct an appellate review, the source of that supposed standard, or the respects in which she viewed Carlson's experience to have fallen short. Moreover, her condemnation of Carlson's experience must be viewed in light of several salient facts: (a) by the time Carlson was in the picture, a thorough and searching investigation had ***already*** been performed by a host of undeniably qualified people, including Schwartz, Ursprung, Merritt, and Ghiz, all of whom brought medical or psychiatric experience and expertise to bear (*see* pages 6-10, *supra*); (b) Chapman had, months before, received a thorough and detailed eight-page, single-spaced denial letter from claim handler Elaine Neeser, and the trial court found no fault with that (PRLCL00417-24); (c) the additional information Chapman supplied after receiving Neeser's denial letter was reviewed by Schwartz and Ghiz; (d) Carlson's own six-page, single-spaced letter reporting the results of his final review of the file was thorough,

detailed, and clearly supported with reference to Schwartz's and Ursprung's medical opinions (PRLCL00618-23); and (e) as the trial court held, "[t]here is no evidence of a deliberate intent to deny plaintiff's legitimate claim" (Order After Hearing at 5), a conclusion that applies just as much to Carlson as to the rest of defendants' staff. In any event, we have found no California case holding that the mere employment of an unqualified or under-qualified claim handler is enough to support a finding of bad faith. Indeed, such a proposition is irreconcilable with the rule that bad faith exists only if the insurer's conduct was "prompted not by an honest mistake, bad judgment or negligence but rather by a conscious and deliberate act."[16/] *Careau*, 222 Cal.App.3d at 1395.

Third, the trial court held that defendants "applied an unreasonably restrictive interpretation of the policy language when they concluded that plaintiff was not performing his occupation as an eye surgeon immediately prior to the onset of his disability." Order After Hearing at 3. The trial court's conclusion appears to be based on a mistake of fact. The court evidently believed that, because Chapman had stopped performing in-hospital surgeries four months before the date he identified as the onset of disability (RT122-23), defendants did not consider surgery to be among his pre-disability duties. In fact, however, the denial letter makes clear that defendants compared his post-disability duties with the duties he performed over the entire 18-month period pre-dating his claim. PRLCL00417-24.

And even if they had taken a literal approach and focused solely on the duties Chapman had performed "immediately" prior to the date he identified

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[16/] Application of that principle here makes perfect sense because an inadequately trained claim handler may be just as apt to recommend payment of an invalid claim as denial of a valid one—making it impossible to infer improper intent from the mere decision to entrust that person with claim decisions.

as the onset of his disability, that would have been fully consistent with the plain language of his policies, both of which defined his pre-disability occupation as the one in which he was "regularly engaged at the time [he] bec[a]me disabled." Plaintiff's Trial Exhibit 13 (Provident Policy), at 4; Plaintiff's Trial Exhibit 14 (Paul Revere Policy), at § 1.8.[17/] Moreover, prior case law endorsed this approach. *See Brumer v. Nat'l Life of Vermont* (E.D.N.Y. 1995) 874 F.Supp. 60, 65 (granting summary judgment on claim for total disability where, although plaintiff was a podiatric surgeon at time he purchased disability policy, his "actual duties" at "the time [his] disability beg[a]n" had not involved surgery for at least 13 months) (alterations in original), *aff'd* (2d Cir. 1998) 133 F.3d 906. As a matter of law, it cannot be "inherently unreasonable" to interpret policy language in the same way that a federal district court had four years earlier. *See Congleton*, 189 Cal.App.3d at 59. And that is so even if this Court ultimately disagrees with that reading. *See, e.g.*, *Tomaselli v. Transamerica Ins. Co.* (1994) 25 Cal.App.4th 1269, 1280-81.

In sum, the "problem" with defendants' investigation wasn't that pieces of the jigsaw puzzle were missing or that defendants tried to force them into the wrong spaces. Rather, when all the pieces came together, the picture that was revealed was simply not one of a valid claim. Instead of a hardworking physician with a medically verifiable disability who was actively engaged in

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[17/] Although Chapman argued at trial that his specialty letter amended his policies to establish conclusively that his occupation was that of an ophthalmic surgeon (RT2695-96), it in fact merely confirmed that Paul Revere would determine his occupation by comparing the "important duties" he was performing "immediately prior to the time disability beings" with those he continued to be able to perform after the onset of disability. PRLCL00447. Indeed, it was Chapman's own expert—Fuller—who explained that at trial. RT1713-14.

treatment and wanted to get back to work, defendants saw an insured whose business was becoming less profitable because of economic forces beyond his control and whose outside interests were taking up ever more of his time. So, not seeing what they would have expected from a genuinely disabled ophthalmologist, defendants denied the claim. Whether or not that conclusion was the right one in hindsight, from where defendants stood it was not inherently unreasonable and certainly did not evidence the conscious and deliberate unfair dealing that bad faith requires. *Careau*, 222 Cal.App.3d at 1395; *Congleton*, 189 Cal.App.3d at 59.

II. DEFENDANTS ARE ENTITLED TO J.N.O.V. OR, AT MINIMUM, A NEW TRIAL ON CHAPMAN'S CLAIM FOR FUTURE BENEFITS.

The trial court instructed the jurors that, if they found defendants to have committed the tort of bad faith, they were entitled to award Chapman the policy benefits that he would be owed if he were to remain disabled until age 65. *See* RT2673-74. The trial court's ruling was based on a mistaken understanding of California law.

In a short footnote written some 25 years ago, the California Supreme Court indicated that the measure of damages for bad faith is governed by "the general rule for fixing tort damages" and that cases holding that future benefits may not be awarded for breach of contract are therefore beside the point. *Egan v. Mut. of Omaha Ins. Co.* (1979) 24 Cal.3d 809, 824 n.7. In so stating, the Court did not purport to address whether tort principles actually do authorize future benefits merely upon a showing that benefits have been denied in bad faith in the past.[18/] Were it confronted with that question, the

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[18/] The *Egan* court did indicate that, "applying to ***these*** facts the general rule for fixing tort damages," the jury was entitled to award the plaintiff future benefits that it reasonably concluded the plaintiff would have been entitled to

Court surely would conclude that allowing future benefits whenever there is a finding of bad faith is irreconcilable with two fundamental principles of tort law.

First, in California (as elsewhere) tort plaintiffs may recover damages only for injuries arising out of the tort. For example, the statute invoked by the *Egan* Court specifies that "the measure of damages, except where otherwise expressly provided by this code, is the amount which will compensate for ***all the detriment proximately caused thereby***, whether it could have been anticipated or not." Civ. Code § 3333 (emphasis added). *See generally* Restatement (Second) of Torts, § 910 ("One injured by the tort of another is entitled to recover damages from the other for all harm, past present and prospective, ***legally caused*** by the tort.") (emphasis added).

Under this fundamental principle, if the plaintiff seeks damages that arise from and are proximately caused by the tortious conduct, he may recover their present value so long as the future damage is reasonably certain to occur, a point we discuss below. The paradigmatic example is a personal injury case: If a person has been rendered quadriplegic by a defective product, the

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receive had the contract been honored by the insurer. 24 Cal.3d 824 n.7 (emphasis added). That is a case-specific holding that does not establish a general rule that future benefits are routinely awardable upon a finding of bad faith. Indeed, as we discuss below, *Egan* involved facts not present here that warranted the conclusion that the insurer would continue to look for ways to avoid paying the claim even in the face of a final judicial determination of liability and thus justified awarding future benefits under traditional tort and remedial principles.

We acknowledge that the Third District has construed *Egan* to allow for an award of future benefits whenever there is a finding of bad faith. *See Pistorius v. Prudential Ins. Co. of Am.* (1981) 123 Cal.App.3d 541, 551. For the reasons just discussed, however, we submit that *Pistorius* misinterpreted *Egan* and that this Court therefore ought not follow it.

expenses she incurs in the future for medical care undeniably arise out of the tort, and she therefore is entitled to recover their present value. Indeed, because our legal system does not permit injured persons to file successive lawsuits to recover damages for the same delict, the only opportunity a personal-injury plaintiff has to recover her future damages is at the time she seeks her past damages.

The typical bad-faith case is nothing like the personal-injury paradigm. When an insurer denies a claim in bad faith, the compensable injuries arising out of that denial may include unpaid past benefits, consequential damages proximately caused by the unavailability of the benefits, and the plaintiff's emotional distress. But the delict of denying a claim in bad faith ***in the past*** cannot be said to be the cause (let alone the "proximate cause") of any ***future*** failure to pay benefits. Rather, failure to pay benefits in the face of a final judicial determination that the insured is entitled to them would constitute a new delict that could form the basis for a new lawsuit.

In this regard, insurance bad faith is comparable to trespass. When a person drives across a neighbor's farm to save the time it would take to drive around it, the landowner is entitled to recover the full amount of the resulting crop damage. But the law does not afford her a right to presume that the defendant will continue trespassing (even if the defendant had been doing so for years) and therefore to recover the present value of future crop damage. Instead, because future crop damage would be the result of entirely new delicts, the law protects the landowner by affording her the right to bring new lawsuits in the future (and to seek punitive damages for the obstinate refusal to recognize her property rights). *See* Dobbs, The Law of Torts (2000) § 57, at 116.

In sum, the law draws a distinction between situations in which there is a single delict that has future consequences, for which future damages are recoverable, and those in which any future injuries would be the result of new delicts, for which future damages are unavailable. Because insurance bad faith fits squarely within the latter category, a mere finding of bad faith is insufficient to authorize an award of future benefits.

Moreover, the belief that future benefits are routinely available upon a showing of bad faith conflicts with a second fundamental proposition of tort law—that, to be recoverable, future damages must be "reasonably certain" to occur. *See, e.g.*, *Roedder v. Rowley* (1946) 28 Cal.2d 820, 822. This precondition is satisfied with respect to many of the categories of future damages that a personal-injury plaintiff might seek. And it is even satisfied in some categories of trespass cases—those in which the invasion is "relatively enduring in character and not readily alterable so as to avoid future injury" (Restatement (Second) of Torts, § 930, com. b). But it is not satisfied in many bad-faith cases, and certainly not in ***this one***.

When there has been a final judicial determination that an insurer denied a valid claim in bad faith, there ordinarily is no reason to suppose that the insurer will continue to refuse to pay the claim. Indeed, given the probability that a recalcitrant refusal to abide by such a ruling and pay the claim would result in a substantial award of punitive damages in a subsequent bad-faith suit, it is reasonably certain that the insurer will ***not*** deny benefits in the future and hence that the insured will suffer ***no*** future loss of benefits. *See Doe v. Provident Life & Accident Ins. Co.* (E.D. Pa. 1996) 936 F.Supp. 302, 308 (holding that Pennsylvania law does not permit award of future benefits absent showing of "complete repudiation" by insurer, and explaining that allegations sufficient to support finding of bad faith "do not show that once a

judgment has been entered against it [the] defendant will continue to improperly deny the benefits owed to [the] plaintiff, especially in the face of possible punitive damages").

This is not to say that future benefits may never be awarded in a bad-faith case. That, of course, ***would*** be inconsistent with *Egan*. Future damages would be warranted if, for example, there is evidence that the defendant has completely repudiated its obligations under the policy. *Id.*[19/] Such an award might also be justified if there is evidence either that the insurer failed to pay the claims of other insureds even after those insureds had secured judicial findings of entitlement to benefits, or that the plaintiff himself "personally has had to bring * * * previous suits to enforce his rights under the specific insurance policies at issue." *Id.* Finally, as in *Egan* itself, it would be permissible to award future benefits upon proof that the defendant had ***serially*** denied past claims of the plaintiff without adequate investigation, accused the plaintiff of fraud, and tendered an inadequate amount for the insured's claims coupled with an offer of a "larger check" if the insured would agree to surrender his policy (24 Cal.3d at 815-17, 821-22), thus warranting the inference that it would look for ways to avoid paying the plaintiff's claims in the future.

Here, there is no evidence to support a finding that defendants repudiated their contract with Chapman. Nor is there any evidence that defendants have ever failed to pay benefits to an insured after a final judicial

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[19/] Repudiation entails a "renunciation or abandonment of the contract as a whole." *New York Life Ins. Co. v. Viglas* (1936) 297 U.S. 672, 677. Importantly, "an insurer's refusal to continue total disability benefits, upon the ground that the insured was not in fact totally disabled, does not amount to a repudiation of the entire contract." *Aetna Life Ins. Co. v. Smith* (Fla. Dist. Ct. App. 1977) 345 So.2d 784, 787.

determination that the insured was disabled. And, of course, there is no evidence that defendants denied claims by Chapman on more than one occasion, accused him of fraud, or tried to use the leverage of an inadequate benefits payment to induce him to surrender his policy in exchange for a more substantial payment. Hence, there is no basis under either *Egan* or established tort principles to award future benefits in this case. Accordingly, the Court should excise from the judgment the award of $864,748 in future benefits. At minimum, because the trial court failed to instruct the jury on the proper prerequisites for an award of future benefits, a new trial is necessary on this issue. And "because the jury was misled about the amount of compensatory damages it could award, its punitive damage award is suspect," and must be vacated, as well. *Auerbach v. Great W. Bank* (1999) 74 Cal.App.4th 1172, 1190.

Even if an award of future benefits could otherwise be reconciled with these fundamental principles of tort law, moreover, it still would not make any sense ***here*** in light of the trial court's ruling that Chapman was residually, but not totally, disabled. His policies make clear that residual disability benefits must be determined on a month-to-month basis depending on his actual income for the month in question. Plaintiff's Trial Exhibit 13 (Provident Policy), at 8; Plaintiff's Trial Exhibit 14 (Paul Revere Policy), at § 2.2. And his own expert, Constance Cardamone, explained that this means that Chapman's residual disability benefits cannot be projected into the future but must instead be calculated by comparing his actual income on a going-forward basis to his pre-disability income. RT426-30. An award of future benefits would freeze in perpetuity the level of residual disability that Chapman had at the moment of judgment, thus divesting him of the right to collect a larger benefit if his monthly income were to fall, while depriving defendants of the

right to pay a smaller benefit if his monthly income were to increase either because of a return to surgical duties or because of an increase in the frequency or profitability of his other duties. *Egan*, of course, involved a policy that included only a total disability provision. Accordingly, whatever the Court meant in its short footnote in that case, it surely did not hold that future benefits are awardable when the claim is for residual, rather than total, disability.

III. DEFENDANTS ARE ENTITLED TO J.N.O.V. ON PUNITIVE LIABILITY.

Although evidence relevant to a finding of bad faith is also relevant to the imposition of punitive damages, the conduct required for the latter is "'of a different dimension.'" *Shade Foods, Inc. v. Innovative Prods. Sales & Mktg. Inc.* (2000) 78 Cal.App.4th 847, 890 (quoting *Tomaselli*, 25 Cal.App.4th at 1286). Specifically, to recover punitive damages, the plaintiff must prove "by clear and convincing evidence" that "the defendant has been guilty of oppression, fraud, or malice" (Civ. Code § 3294(a))—in other words, that the defendant "engaged in despicable conduct with a conscious disregard of the rights or safety of others" (*Kransco v. Am. Empire Surplus Lines Ins. Co.* (2000) 23 Cal.4th 390, 410). Despicable conduct is "'conduct which is so vile, base, contemptible, miserable, wretched, or loathsome that it would be looked down upon and despised by ordinary decent people.'" *Tomaselli*, 25 Cal.App.4th at 1287 (citation omitted).

The requirement that a plaintiff prove entitlement to punitive damages by clear and convincing evidence "assuredly emphasize[s] the greater and more convincing proof desired at the trial level." *Id.* This level of proof requires that "the evidence be so clear as to leave no substantial doubt; sufficiently strong to command the unhesitating assent of every reasonable mind." *In re Angelia P.* (1981) 28 Cal.3d 908, 919 (internal quotation marks

omitted). Application of this heightened standard—which is required in testing the sufficiency of the evidence every bit as much as in instructing the jury (*see Shade Foods*, 78 Cal.App.4th at 891)—leaves no doubt that defendants are entitled to j.n.o.v.[20/]

"Since the facts of this case do not give rise to a breach of the duty of good faith and fair dealing, this Court cannot find that these same facts establish clear and convincing evidence of oppression, fraud or malice."[21/] *Phelps v. Provident Life & Accident Ins. Co.* (C.D. Cal. 1999) 60 F.Supp.2d 1014, 1026; *see also* Civ. Code § 3294(a); *Taylor v. Superior Court* (1979) 24 Cal.3d 890, 894-95; *Tomaselli*, 25 Cal.App.4th at 1287. But even if there were a sufficient basis for finding under the ***preponderance*** standard that defendants acted wrongfully in handling Chapman's claim, the evidence that their conduct

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[20/] This Court reviews a denial of a j.n.o.v. motion *de novo*. *See Sweatman*, 25 Cal.4th at 68.

[21/] We note in passing that, although the jury found malice and fraud (but not oppression), the trial court's Order After Hearing (at 5) makes reference to malice but omits any discussion of fraud. That is unsurprising. Chapman based his charge of fraud on the allegation that defendants "[sold] a policy and then when it turn[ed] out to be not such a good deal[,] * * * decide[d] not to pay the benefits on it." RT2691. California law is clear, however, that intent to defraud must exist at the time that the contract is formed; making an agreement and subsequently deciding not to adhere to it is nothing more than ordinary breach of contract. *Muraoka v. Budget Rent-A- Car, Inc.* (1984) 160 Cal.App.3d 107, 119 (promissory fraud requires "a promise made regarding a material fact without any intention of performing it" and "the existence of the intent at the time of making the promise"). Simply put, a claim of fraud arises out of misconduct in the sale of an insurance policy; a claim of bad faith has to do with conduct occurring after the policy has already issued. That no doubt explains why "[p]unitive damages for failure to pay or properly administer an insurance claim are ordinarily * * * based on 'malice' or 'oppression,' rather than on the third possible ground for the award, 'fraud'" (25 Cal.App.4th at 1286).

went beyond bad faith and instead was "'so vile, base, contemptible, miserable, wretched, or loathsome that it would be looked down upon and despised by ordinary decent people'" was non-existent, much less "sufficiently strong to command the unhesitating assent of every reasonable mind." Accordingly, the finding of punitive liability is unsustainable. *See Shade Foods*, 78 Cal.App.4th at 892 (although jury reasonably could conclude that insurer evinced "a careless disregard for the rights of its insured and an obstinate persistence in an ill-advised initial position," its conduct was "within the common experience of human affairs" and, accordingly, plaintiff had fallen "well short of establishing by clear and convincing evidence the sort of contemptible conduct that could be described by the term 'despicable'"); *Tomaselli*, 25 Cal.App.4th at 1288 (reversing award of punitive damages because defendant's conduct, though "overzealous," "legally erroneous," "slipshod," and "callous," was not "evil, criminal, recklessly indifferent to the rights of the insured, or [undertaken] with a vexatious intention to injure").

IV. A NEW TRIAL ON PUNITIVE DAMAGES IS NECESSARY BECAUSE THE TRIAL COURT FAILED TO PROHIBIT PLAINTIFF'S COUNSEL FROM MAKING IMPROPER ARGUMENTS TO THE JURY AND FAILED TO INSTRUCT THE JURY IN ACCORDANCE WITH CONSTITUTIONAL LIMITATIONS ON PUNITIVE DAMAGES.

In *State Farm*, the Supreme Court observed that "punitive damages pose an acute danger of arbitrary deprivation of property" and that "the presentation of evidence of a defendant's net worth creates the potential that juries will use their verdicts to express biases against big businesses, particularly those without strong local presences." 123 S.Ct. at 1520 (internal quotation marks and alterations omitted). It also expressed "increase[d]" "concerns over the imprecise manner in which punitive damages systems are administered"—concerns that "are heightened when the decisionmaker is

presented * * * with evidence that has little bearing as to the amount of punitive damages that should be awarded." *Id*. And it lamented that "[v]ague instructions * * * do little to aid the decisionmaker in its task of assigning appropriate weight to evidence that is relevant and evidence that is tangential or only inflammatory." *Id*.

The clear import of these statements is that trial courts must take a greater role in ameliorating the prejudicial effects of tangential and/or inflammatory evidence through the instructions they give juries and the limitations they place on efforts by plaintiffs' counsel to inflate punitive awards through improper argumentation. Having been victimized by such tactics in the past, defendants sought the very kinds of safeguards that the Supreme Court endorsed in *State Farm*. Specifically, defendants requested the trial court to instruct the jury that (i) it could not punish them for harms to non-parties and (ii) it could not punish them more severely because of their substantial net worth. Defendants also asked the trial court to prohibit Chapman's counsel from (i) making inflammatory references to their out-of-state location and corporate status; (ii) urging the jury to base punishment on their sizeable wealth; and (iii) asking for an amount of punitive damages that, if imposed, would be unconstitutionally excessive. The trial court's denial of these requests was reversible error.

A. The Trial Court Erred In Refusing To Instruct The Jury Not To Punish Defendants For Harms To Non-Parties.

As with the bad-faith count, the centerpiece of Chapman's case for punitive damages was the Fuller/McSharry/Feist testimony concerning defendants' allegedly improper claims practices, none of which figured into the handling or disposition of Chapman's own claim. *See* Section I.B., *supra*. Because this testimony conjured up the specter of countless other injured policyholders, defendants sought the following instruction:

> You are not to impose punishment for harms suffered by persons other than the plaintiff before you. Such individuals may bring their own lawsuits, in which other juries can resolve those non-parties' claims.

Appellants' Appendix, vol. 8, at 1837. Defendants had an absolute right to that instruction.

In *State Farm*, the Supreme Court held excessive a punitive award for insurance bad faith that had been based in part on evidence of "unsavory" claim-handling practices analogous to the evidence on which Chapman relied here. In the course of so holding, it explained:

> Due process does not permit courts, in the calculation of punitive damages, to adjudicate the merits of other parties' hypothetical claims against a defendant under the guise of the reprehensibility analysis * * *. Punishment on these bases creates the possibility of multiple punitive damages awards for the same conduct; for in the usual case nonparties are not bound by the judgment some other plaintiff obtains.

123 S.Ct. at 1523. Because defendants' proposed instruction would have told the jury precisely that, it correctly stated the law, and it was error not to give it—error that is of constitutional magnitude in light of the Supreme Court's expression of concern about "[v]ague instructions" that "do little to aid the decisionmaker in its task of assigning appropriate weight to evidence that is relevant and evidence that is tangential or only inflammatory" (*id*. at 1520), like the Fuller/McSharry/Feist testimony here. And because the trial court's refusal to give the proposed instruction was based "exclusively upon an erroneous concept of legal principles applicable to the cause," a new trial is warranted without the need for inquiry into whether the error was prejudicial. *Conner v. S. Pac. Co.* (1952) 38 Cal.2d 633, 637; *accord Maher v. Saad* (2000) 82 Cal.App.4th 1317, 1323.

B. The Trial Court Erred In Failing To Instruct The Jury That It Could Not Punish Defendants More Severely Based Upon Their Wealth.

The evidence that Chapman presented in Phase III of the trial consisted of detailed financial data about defendants' substantial assets and cash reserves. Defendants therefore sought the following instruction:

> You may consider the defendants' financial condition in order to satisfy yourselves that the defendants are capable of paying the punitive award. You may not, however, punish the defendants more severely simply because they are large and therefore have substantial net worth or income.

Appellants' Appendix, vol. 8, at 1834. *State Farm* confirms that defendants were entitled to this instruction.

The Supreme Court there held unequivocally that "[t]he wealth of a defendant cannot justify an otherwise unconstitutional punitive damages award." 123 S.Ct. at 1525. And it further observed that arguments based on a defendant's "enormous wealth" "bear no relation to [a punitive] award's reasonableness or proportionality to the harm," but rather "seek to defend a departure from well-established constraints on punitive damages." *Id.* at 1525; *see also Lane v. Hughes Aircraft Co.* (2000) 22 Cal.4th 405, 427 (Brown, J., joined by Chin, J., concurring) ("Many of the wealthiest defendants are corporations, and the size of a corporate defendant is not an additional evil that in itself warrants an enhanced penalty."). Accordingly, although before *State Farm* was decided, evidence of a defendant's financial condition was a prerequisite to an award of punitive damages under California law (*see Adams v. Murakami* (1991) 54 Cal.3d 105, 110), this Court has now explained that "the constitutional soundness of the * * * consideration [of a defendant's financial condition] has been rendered uncertain by *Campbell*'s seemingly categorical rejection of the Utah Supreme Court's reliance on the defendant's

''massive wealth'' as one justification for the award there." *Henley v. Philip Morris Inc.* (Sept. 25, 2003, No. A086991) ___ Cal.App.4th ___ [2003 WL 22211589, at *32].

The requested instruction limiting the use of evidence of defendants' financial condition was the bare minimum that the trial court should have done to ensure the jury's adherence to the dictates of due process.[22/] Because the court's refusal to give the instruction was based on the legally erroneous belief that juries are entitled to increase their punitive awards on account of the defendant's wealth, a new trial is required. *See Conner*, 38 Cal.2d at 637; *Maher*, 82 Cal.App.4th at 1323.[23/]

[22/] The *Adams* Court held that evidence of financial condition must be adduced at trial because "[t]he absence of this evidence thwarts effective appellate review of a claim that punitive damages are excessive" (*Adams*, 54 Cal.3d at 109; *see also id.* at 114, 118), a rationale that derives principally from the concern that punishment not be disproportionate to the defendant's ability to pay (*id.* at 112-14). It may well be that *State Farm* does not preclude California from continuing to use evidence of financial condition as a ***check*** against excessive awards. But that is not, of course, the purpose for which it was used here. Rather, the evidence was used for the undeniably impermissible purpose of launching an argument for a nine-digit punishment. *State Farm* establishes that the trial court erred in admitting this financial evidence, erred in refusing to prohibit Chapman from arguing to the jury that the punitive damages needed to be a significant percentage of defendant's financial resources, and erred in refusing to instruct the jury that the amount of defendants' resources is not a valid basis for enhancing punishment.

[23/] In *Henley*, this Court suggested that any error in failing to instruct the jury that it could not set punishment on the basis of the defendant's wealth was harmless because it was unlikely that a properly instructed jury would have returned a verdict lower than the amount to which the Court had reduced the award. 2003 WL 22211589, at *32. No similar conclusion can be reached here. As we explain below (*see* Section IV.C.2-3), plaintiff's wealth-based closing arguments skewed the jury's reasoning by establishing a scale on which $167,000,000 marked the smallest supposedly reasonable punitive award that might be assessed against defendants, while $667,000,000 marked

C. The Trial Court Erred In Allowing Chapman's Counsel To Engage In Improper Closing Arguments Over Objection.

In a case such as this one, it is a virtual certainty that the plaintiff will seek to inflate the punitive award beyond what is constitutionally permissible or supported by the evidence by making inflammatory references to the defendants' out-of-state residence and corporate status and by asking the jury to base the punitive damages on the defendants' wealth. Because the trial court indicated that it did not want counsel to interrupt each other during closing arguments (RT2677), and anticipating that plaintiff's counsel would employ these improper tactics here, defendants moved for orders in limine barring him from (i) making inflammatory references to defendants' corporate status and out-of-state location; (ii) asking the jury to base the punishment on defendants' wealth; and (iii) asking for an amount of punitive damages that, if actually imposed, would be unconstitutionally excessive. The trial court denied those motions, and plaintiff's counsel proceeded to engage in each of these improper kinds of arguments. Because the grossly improper arguments made by plaintiff's counsel had the purpose and effect of causing the jury to return an unsupported and unconstitutionally excessive punitive award, the trial court's failure to stop those arguments when it had the chance was prejudicial error necessitating a new trial.

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the top end of the range. RT2888-89. Thus, there can be no basis to assume that the jury meant to impose the very largest punitive award that the Constitution might permit in the most extreme case—nor would the evidence support such an award. And, for that reason, there similarly is nothing on which to ground the assumption made in *Henley* about how a properly instructed jury would likely have behaved.

1. Counsel's attacks on defendants' out-of-state residence and corporate status were grossly improper.

Plaintiff's counsel set the tone for his closing arguments by pitting "corporate greed" against "the most vulnerable among us, the sick, the injured, and the disabled." RT2678. From the get-go, he sketched a picture of a corporate philosophy in which those who seek to injure disabled individuals "go up the corporate ladder," while "[t]hose people who don't fall out of the corporation. That is generally the way corporations work." RT2885. He harped on the fact that the jury was the watchdog for California (*see, e.g.*, RT2717, 2764), inviting the jurors to send a message from "San Rafael, California" (RT2717) to the corporate executives from the big, bad insurance company "back East" (RT2889), who would then ask, "What's the matter with those people out in California?" RT2889-90. And, most egregiously, counsel made the following attack:

> The greatest evil is not now done in those sordid dens of crime that Dickens loved to paint. It is not done even in concentration camps and labor camps. In those we see its final results. But it is conceived and ordered[,] moved, seconded, carried and minuted in clear carpeted, warmed, and well-lighted offices, by quiet men with white collars and cut fingernails and smooth shaven cheeks who do not need to raise their voices.

RT2764 (quotation marks omitted).

The only possible purpose that plaintiff's counsel might have had for attacking defendants based on their corporate status, and for juxtaposing defendants' executives "back East" with the jurors in San Rafael, was to inflame the jury's prejudice against corporations and non-Californians.

The U.S. Supreme Court and the courts of this state have long recognized, however, that attempts by counsel to evoke jurors' anti-corporate or sectional biases are wholly inappropriate. *See, e.g.*, *New York Cent. R. Co. v. Johnson* (1929) 279 U.S. 310, 319 ("remarks of counsel * * * tending to

create an atmosphere of hostility toward petitioner as a railroad corporation located in another section of the country, have been so often condemned as an appeal to sectional or local prejudice as to require no comment"); *Brokopp v. Ford Motor Co.* (1977) 71 Cal.App.3d 841, 860 ("Appeals to the sympathy of the jury based on the size or corporate status of a defendant are improper.").

That is particularly so when, as in this case, counsel encourages the jurors to send a message about what their community will or won't tolerate from outsiders. *See, e.g.*, *Smith v. Travelers Ins. Co.* (6th Cir. 1971) 438 F.2d 373, 375 & n.2 (plaintiff's exhortation to "send them back up to Hartford and let them know how we feel about it in Tennessee" was "obviously designed to prejudice the jurors"); *Clement Bros. Co. v. Everett* (Ky. 1967) 414 S.W.2d 576, 577 (reversal of compensatory award required because jury arguments picturing defendant as "a rich, grasping, foreign corporation running ruthlessly roughshod over the poor, honest, long-suffering citizens of Barren County" were "designed specifically to appeal to and arouse the passions and prejudices of the jury"); *Rockwell Int'l Corp. v. Wilhite* (Ky. Ct. App. Aug. 8, 2003, No. 1997-CA-000188-MR) ___ S.W.3d ___ [2003 WL 21826306, at *18, *21] (noting impropriety of plaintiff's reference to defendants' location in Seal Beach, California, "where everybody has got a tan and a $60 haircut and life is good").

And while caricatures of corporate defendants as men with "white collars and cut fingernails and smooth shaven cheeks" are improper in and of themselves (*see Rockwell*, 2003 WL 21826306, at *18, *21), plaintiff's depiction of defendants' corporate management as being worse than the Nazis was the utmost in impropriety, "clearly transgress[ing] the bounds of legitimate advocacy." *United States v. Thiel* (8th Cir. 1980) 619 F.2d 778, 782 (prosecutor analogized defendant's conduct to Holocaust and Jonestown

massacre); *see also, e.g.*, *Martin v. Parker* (6th Cir. 1993) 11 F.3d 613, 616 (granting habeas corpus based on "deplorable" comparison drawn between defendant and Adolf Hitler); *Pennsylvania v. Baranyai* (Pa. Super. Ct. 1982) 442 A.2d 800, 803 (new trial ordered after prosecutor attempted to "stigmatize" defendant as, *inter alia*, someone who used "Gestapo tactics").

2. Counsel's request for excessive punitive damages based on defendants' wealth was grossly improper.

Using as a springboard the voluminous evidence of defendants' corporate wealth and cash reserves that he offered during Phase III of the trial, plaintiff's counsel suggested in closing arguments that the jury might award punitive damages in the amount of ***$670,000,000***, or 10% of defendants' corporate wealth as calculated by Chapman's expert. RT2888. Then, counsel offered that the jury might halve that number and award $335,000,000, or 5% of defendants' wealth (*id.*)—which counsel identified as, in his view, "the appropriate number" (RT2888-89). Counsel next suggested that the jury might even halve that number again, yielding a $167,000,000 million verdict, although he indicated that such an amount would be insufficient to punish and deter. *Id.* And he argued that a punitive award on the order of $25,000,000 "would have absolutely no impact on [defendants] whatsoever." RT2889. In other words, counsel set a scale for punitive damages on which an award of $167,000,000 was at the very bottom end of the range of reasonable punishment, while $667,000,000 marked the top end. This despite the fact that counsel was proposing awards of ***between 99 and 395 times*** the compensatory damages that the jury had awarded and 2.5% to 10% of defendants' net worth.

In view of the Supreme Court's admonition that trial courts must do more to rectify the arbitrariness that has been common in the administration of punitive damages and its specific holding that reliance on evidence of financial condition is "a departure from well-established constraints on punitive

damages" (*State Farm*, 123 S.Ct. at 1520, 1525), it was error to deny defendants' twin requests to prohibit Chapman's counsel from exhorting the jury to punish defendants on the basis of wealth and from suggesting an amount, that, if actually awarded, would be manifestly excessive.

3. The improper arguments were manifestly prejudicial.

Both individually and collectively, the trial court's errors in failing to rein in Chapman's counsel were manifestly prejudicial. To begin with, given the size of the jury's punitive award ($30,000,000), its disproportionality to the compensatory damages (18:1), and the comparatively modest reprehensibility of defendants' conduct toward Chapman, it hardly can be denied that counsel's improper appeals to bias against out-of-state corporations had their intended effect.

Moreover, the prejudicial impact of arguments based on the defendant's financial condition has been repeatedly acknowledged by the Supreme Court. *See State Farm*, 123 S.Ct. at 1520 ("'the presentation of evidence of a defendant's net worth creates the potential that juries will use their verdicts to express biases against big businesses, particularly those without strong local presences'") (quoting *Honda Motor Co. v. Oberg* (1994) 512 U.S. 415, 432); *TXO Prod. Corp. v. Alliance Res. Corp.* (1993) 509 U.S. 443, 464 (agreeing with respondent that "the emphasis on the wealth of the wrongdoer increased the risk that the award may have been influenced by prejudice against large corporations, a risk that is of special concern when the defendant is a nonresident").

Finally, juror studies consistently show that allowing counsel to suggest a specific damage amount significantly skews jurors' ultimate damages awards. *See* Viscusi, *The Challenge of Punitive Damages Mathematics* (June 2001) 30 J. Legal Stud. 313 (subjects in juror study "base[d] their judgments largely on

the anchoring influence [of counsel's suggested amounts]."); Hastie *et al.*, *Juror Judgments in Civil Cases: Effects of Plaintiff's Requests and Plaintiff's Identity on Punitive Damage Awards* (Aug. 1999) 23 Law & Hum. Behav. 445 (study results demonstrate "anchor-and-adjust" phenomenon whereby jurors use counsel's suggested awards as starting point and set punitive awards at some discounted compromise figure relative to the suggested amount); Marti & Wissler, *Be Careful What You Ask For: The Effect of Anchors on Personal Injury Damages Awards* (June 2001) 6 J. Experimental Psychol. 91 (describing mock juror study in which exaggerated plaintiff requests for pain and suffering damages produced exaggerated awards and concluding that counsel's award recommendations alter jurors' beliefs about what constitutes an acceptable award).

For this reason, numerous courts have held that allowing arguments like the ones made by Chapman's counsel here is prejudicial error. *See, e.g.*, *Henne v. Balick* (Del. 1958) 146 A.2d 394, 398 ("the purpose [of suggesting a specific sum as damages] is solely to introduce and keep before the jury figures out of all proportion to those which the jury would otherwise have had in mind, with the view of securing from the jury a verdict much larger than that warranted by the evidence"); *Bechard v. Eisinger* (App. Div. 1984) 481 N.Y.S.2d 906, 908 (prohibiting counsel from asking jury for specific sum is appropriate in order "to curb the effect of exaggerated demands for damages which could * * * bias [the jury] towards making excessive awards"); *Kusisto v. McLean* (App. Div. 1976) 382 N.Y.S.2d 146, 147-48 (request for specific amount was prejudicial despite curative instruction and fact that jury returned verdict for less than amount requested); *Purpura v. Pub. Serv. Elec. & Gas Co.* (N.J. App. Div. 1959) 147 A.2d 591, 595 ("statements such as these are made by counsel with the intent to influence the jury"; "the prejudice arises not from the acceptance

by the jury of the suggested figures, but from the influences upon the minds of the jurors").

Because the trial court committed prejudicial error in failing to prohibit improper arguments of counsel, which was then compounded by its legally erroneous refusal to instruct the jury on two critical constitutional limitations on punitive damages, a new trial is required.

V. THE REMITTED PUNITIVE DAMAGES REMAIN UNCONSTITUTIONALLY EXCESSIVE.

Seven years ago, the Supreme Court instructed lower courts to review punitive awards for excessiveness in light of three "guideposts"—(l) the degree of reprehensibility of the defendant's conduct; (2) the ratio of punitive to compensatory damages; and (3) the civil penalties applicable to comparable conduct. *BMW of N. Am., Inc. v. Gore* (1996) 517 U.S. 559, 575-76. Applying these guideposts, the Superior Court concluded that the very largest punitive award that the evidence in this case could support was $5,000,000—4.4 times Chapman's compensatory damages. Shortly thereafter, the Supreme Court decided *State Farm* in which it provided substantial guidance for the proper application of the *BMW* guideposts in the specific context of insurance bad faith cases such as this one. *State Farm* makes crystal clear not only that the court below correctly rejected the jury's extravagant $30,000,000 exaction, but also that the remitted award remains grossly excessive.[24/] And this Court's recent ruling in *Henley*, *supra*, underscores that conclusion.

1. *Reprehensibility.* The reprehensibility guidepost embodies the age-old principle that "punitive damages may not be grossly out of proportion to the severity of the offense." *BMW*, 517 U.S. at 576 (internal quotation marks

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[24/] This Court reviews the trial court's excessiveness determination *de novo*. *State Farm*, 123 S.Ct. at 1520.

omitted). As *State Farm* demonstrates, the mere fact that an insurer has been found to have committed the tort of bad faith—even when accompanied by intentional fraud—is insufficient to support a multimillion dollar punitive award.

State Farm involved a bad-faith claim arising out of a dispute between a State Farm insured and third-party claimants under the insured's automobile policy. Accepting the findings of the lower courts, the Supreme Court observed that, in defending its insured (a financially vulnerable senior citizen) against the third-party claimants, State Farm altered the claim file, ignored the advice of its investigator, refused to settle within policy limits, and took the case to trial, all the while assuring its insured that he ran no risk of liability, that his assets were safe, and that he did not need separate counsel. 123 S.Ct. at 1518. State Farm did all of this despite the "overwhelming likelihood of liability and the near-certain probability that, by taking the case to trial, a judgment in excess of the policy limits would be awarded." *Id.* at 1521. When the jury returned a verdict in excess of policy limits, State Farm "amplified the harm" by refusing to pay the excess (*id.*) and callously telling its insured and his wife that they should put their house up for sale to pay the remaining portion of the judgment. *Id.* at 1518, 1521. State Farm then refused even to post a supersedeas bond to give its insured the chance to appeal the verdict. *Id.* at 1518.

With such malfeasance firmly in mind, the Supreme Court acknowledged that "State Farm's handling of the claims against the Campbells merits no praise." *Id.* at 1521. Yet the Court reversed the $145,000,000 punitive award—which the Court regarded as an attempt to punish "the perceived deficiencies of State Farm's operations throughout the country"—holding that "a more modest punishment for this reprehensible conduct could have satisfied the State's legitimate objectives, and the Utah

courts should have gone no further." *Id.* The Court later suggested that, all things considered, State Farm's conduct toward the plaintiff "likely would justify a punitive damages award at or near the amount of compensatory damages"—$1,000,000. *Id.* at 1526.

The conclusion that State Farm's conduct did not warrant punishment in excess of $l,000,000 is dispositive here. As in *State Farm*, Chapman sought punishment for an alleged scheme to terminate claims improperly. But as the Supreme Court held in *State Farm*, "[a] defendant should be punished for the conduct that harmed the plaintiff, not for being an unsavory individual or business." 123 S.Ct. at 1523. "The reprehensibility guidepost does not permit courts to expand the scope of the case so that a defendant may be punished for any malfeasance * * *." *Id.* at 1524. Absent proof—and there was none here—that defendants engaged in substantially similar conduct with regard to other policyholders, "the conduct that harmed [plaintiff] is the only conduct relevant to the reprehensibility analysis." *Id.*

And defendants' conduct here is undeniably ***far less culpable*** than the conduct at issue in *State Farm*, which involved doctoring a claim file, lying to the insured, and exposing financially vulnerable senior citizens to the risk of losing their home. For, as the trial court held:

> Here, there was no physical injury caused by defendants' actions. Plaintiff was not totally disabled. There is no evidence of a deliberate intent to deny plaintiff's legitimate claim, even though plaintiff's claim was not processed in good faith. Defendants paid residual benefits early on. Additionally, there is no evidence of oppression or equally reprehensible conduct inflicted upon a sick, old, destitute or an otherwise particularly vulnerable plaintiff * * *.

Order After Hearing at 5. Hence, the very largest punishment here would be $1,000,000.

Indeed, nothing beyond $1,000,000 would be permissible even if Chapman had demonstrated the required nexus between the "unsavory" practices about which Fuller, Feist, and McSharry testified and the "specific harm" that he suffered. *State Farm*, 123 S.Ct. at 1522. For even in that event, an award in excess of $1,000,000 would punish defendants for a entire course of conduct affecting multiple individuals, thus creating an unacceptable risk of "multiple punitive damages awards for the same conduct." *Id.* at 1523.[25/]

But if any hope for the viability of the punitive award could be thought to have survived *State Farm*, this Court's recent decision in *Henley* puts still another nail in the coffin. In that case, this Court found the evidence sufficient to support a finding that the defendant tobacco manufacturer:

> touted to children what it knew to be a cumulatively toxic substance, while doing everything it could to prevent them and other addicts and prospective addicts from appreciating the true nature and effects of that product. The result of this conduct was that millions of youngsters,

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[25/] Moreover, the unrefuted testimony of defendants' consulting psychologist Dr. Ursprung and their Vice President Jeffrey McCall establishes that, since the time when Chapman's claim was denied, defendants have implemented numerous changes to improve their claim handling with regard to precisely the practices about which Fuller, McSharry, and Feist testified. *See, e.g.*, RT1853, 2483, 2486-87, 2495-96. As the Supreme Court has emphasized, a multimillion dollar award "cannot be justified on the ground that it was necessary to deter future misconduct without considering whether less drastic remedies could be expected to achieve that goal." *BMW*, 517 U.S. at 584. And, in conducting that inquiry in a case involving an automobile manufacturer's policy of not disclosing certain pre-sale repairs to new automobiles, the Supreme Court deemed it highly significant that the defendant abandoned its policy shortly ***after*** the verdict in question. *Id*. at 579 n.31. If a $2,000,000 punitive award—characterized by the Supreme Court as "tantamount to a severe criminal penalty" (*id*. at 585)—cannot be justified when the defendant changes its policy ***in response*** to that award, it follows inexorably that nothing close to that is permissible when the undisputed evidence is that the defendants altered their conduct even ***before*** the case came to trial.

> including plaintiff, were persuaded to participate in a habit that was likely to, and did, bring many of them to early illness and death.

2003 WL 22211589, at *29. Having found sufficient evidence that the defendant "consciously exploited the known vulnerabilities of *children*" (*id.* at *30 (emphasis in original)), this Court reasoned that the defendant had committed "a quintessential 'mass tort,' i.e., a course of more-or-less uniform conduct *directed at the entire public* [that] maliciously injur[ed], through a system of interconnected devices, an entire category of persons to which plaintiff squarely belongs" (*id.* at 31), in the process causing the plaintiff "severe *bodily* injury in the form of lung cancer" (*id.* at *29 (emphasis in original)).

Because "[t]he gist of plaintiff's claim [in *Henley*] was not that defendant inflicted an economic harm but that its conduct caused her severe *bodily* injury," this Court concluded that the "[d]efendant's malicious infliction of such an injury is * * * ***substantially more reprehensible*** than the conduct at issue in *Campbell*," namely, "bad faith denial of [an] insurance claim." *Id.* (first emphasis in original; second emphasis added). The same conclusion applies here as well. Thus, if $9,000,000 is the maximum permissible punishment for what this Court regarded as "extraordinarily reprehensible conduct of which plaintiff was a direct victim" (*id.* at *32), it follows that a $5,000,000 punishment is grossly excessive for the "substantially" less reprehensible conduct involved here.

2. *Ratio*. The ratio of remitted punitive to compensatory damages is more than 4.4:1—concededly, an improvement over the 18:1 ratio of the jury verdicts.[26/] But that does not immunize the award from constitutional challenge. In *State Farm*, the Supreme Court pointed to the 700-year history

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[26/] If the award of future benefits is excised, however, the ratio increases to 19:1.

of legislative imposition of double (1:1), treble (2:1), and quadruple (3:1) damages as the hallmark of reasonable punishments, and reiterated its observation in *Pacific Mutual Life Insurance Co. v. Haslip* (1991) 499 U.S. 1, 23-24, that an award of more than four times the amount of compensatory damages "might be close to the line of constitutional impropriety" irrespective of the egregiousness of the conduct or the severity of the resulting harm. 123 S.Ct. at 1524. The Supreme Court also explained that, just as "low awards of compensatory damages may properly support a higher ratio than high compensatory awards, if, for example, a particularly egregious act has resulted in only a small amount of economic damages" (*BMW*, 517 U.S. at 582), "[t]he converse is also true" (*State Farm*, 123 S.Ct. at 1524). "***When compensatory damages are substantial, then a lesser ratio, perhaps only equal to compensatory damages, can reach the outermost limit of the due process guarantee***." *Id.* (emphasis added); *see also Lane*, 22 Cal.4th at 423 (Brown, J., concurring) ("three times compensatory damages" is "*an uppermost limit*, and most punitive damage awards should fall well *below* that limit") (emphasis in original).

Here, the remitted compensatory damages are some 11% greater than the $1,000,000 compensatory award in *State Farm*—an amount that the Supreme Court held sufficiently large to merit only a 1:1 ratio. And just like in *State Farm*, there is no basis for any greater ratio because "[t]he harm arose from a transaction in the economic realm, not from some physical assault or trauma [and] there were no physical injures" (*id*. at 1524-25); instead, Chapman suffered "only minor economic injuries" for the period during which defendants declined to pay his claim (*id.*).[27/] Thus, like *State Farm*, this case is one in

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[27/] Additionally, because the future benefits that the jury awarded are highly speculative and do not reflect harm that is substantially likely to occur (*see* Part II, *supra*), they are, from defendants' perspective, punitive in nature.

which application of the *BMW* guideposts dictates, at the very most, "a punitive award at or near the amount of compensatory damages." *Id*. at 1526.

Again, *Henley* underscores this conclusion. Having set a scale in which a 6:1 ratio marks the outermost constitutional limit for conduct that this Court placed at the very top end of the reprehensibility spectrum (2003 WL 22211589, at *32), *Henley* compels the conclusion that a 4.4:1 ratio on a similarly-sized compensatory award must similarly be reserved for cases involving truly egregious misconduct; and nothing even approaching that ratio can be sustained when, as here, the defendants' conduct barely (if at all) crosses the threshold for punitive liability and hence is at the extreme low end of the reprehensibility spectrum.

3. *Penalties for Comparable Misconduct.* The third *BMW* guidepost requires a comparison between "the punitive damages award and the civil or criminal penalties that could be imposed for comparable misconduct." *BMW*, 517 U.S. at 583. In *State Farm*, the Supreme Court compared the punitive award with Utah's $10,000 fine for unfair claims practices. 123 S.Ct. at 1526. The comparable penalty in this state is found in Section 790 of the California Insurance Code, which prohibits as "unfair claims settlement practices" a variety of acts by insurers, including "[n]ot attempting in good faith to effectuate prompt, fair, and equitable settlement of claims in which liability has become reasonably clear." Ins. Code § 790.03(h)(1), (5). The California legislature has fixed the maximum civil penalty for a ***willful*** violation of the Insurance Code (of which defendants' conduct surely is not) at $10,000. *See*

Accordingly, if this Court does not reverse the award of those benefits, little more is needed to advance California's legitimate interests in punishment and deterrence. *See State Farm*, 123 S.Ct. at 1525 (observing that emotional distress damages have punitive component, making large punitive award less necessary).

id. § 790.035(a). Because the $5,000,000 punishment in this case is ***500 times*** the maximum civil penalty that would be allowed under California law for comparable (or, indeed, more egregious) insurer misconduct, the third guidepost points unambiguously toward a conclusion of excessiveness.

CONCLUSION

This Court should grant defendants j.n.o.v. on the bad faith and punitive damages claims. Alternatively, the Court should grant defendants an unconditional new trial on bad faith and punitive damages. Barring that, the Court should further remit the punitive damages to a nominal sum or, in all events, no more than $1,000,000.

Respectfully submitted,

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