

RAY OF SUNSHINE ON PUNITIVE DAMAGES

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A routine insurance premium collection case for premium due on a commercial automobile policy in California, issued by the California Assigned Risk Plan (“CAARP”), resulted in a punitive damage award to the insured by the trial court. The trial court decision was subsequently reversed by the California District Court of Appeals. The intermediate appellate court’s opinion regarding punitive damages is very revealing.¹

The facts in the above case were very simple. *Jonathan Neil* arose from a very simple collection action. The plaintiff was a collection agency that sued a trucking firm to recover premium which remained unpaid to an insurer who had assigned the account for collection. The commercial auto policy was issued to the insurer, Cal Eagle Insurance Company, through an assignment from CAARP. After several rulings by the trial court, which were favorable to the cross-defendant trucking company, the jury returned a verdict for the insured and awarded more than \$13 million in punitive damages. The trial court then reduced the award to \$7 million.

The District Court of Appeals reversed the award, finding that the insured had failed to exhaust its administrative remedies (in the unpublished portion of the opinion) and the imposition of tort liability was unwarranted by the facts of the case. First, the Court analyzed the California bad faith actions, generally, and the current status of appellate decisions relating to bad faith cases involving insurance policies. It then concluded the trend was toward limited tort recovery in both insurance and noninsurance cases.² The language of the Court was most revealing with the following statement by the Court, as to its interpretation of the current state of bad faith actions in California:

We are satisfied the “insurance case” exception preserved in *Freeman* and *Mills* does not extend to every breach of an insurance contract. As noted above, the covenant of good faith and fair dealing is reciprocal, binding both the insurer and the insured. (*Commercial Union Insurance Corp. Companies v. Safeway Stores, Inc.*, *supra*, 26 Cal. 3d at p. 918.) Nevertheless, an insured is not guilty of the tort of bad faith when the insured breaches the covenant; in those circumstances the insurer is limited to contract remedies. (*Kransco v. American Empire Surplus Line Ins. Co.*, *supra*, 23 Cal. 4th at pp. 404-405.) Accordingly, we must reject any interpretation of the preserved “insurance cases” exception in *Freeman* and *Mills* that would permit a tort action for every bad faith breach of an insurance contract.³

The Court went on further to state:

In addition however, the logic and language of *Foley* and other Supreme Court cases persuade us that not every instance of bad faith conduct by an insurer gives rise to a tort cause of action. In particular, we perceive that the general administration of an insurance policy “is not sufficiently similar” to the duties involved in investigating, defending, and settling cases to justify the imposition of tort liability of an insurer who acts in bad faith. (*See Foley v. Interactive Data corp.*, *supra*, 47 Cal. 3d at p. 693.) Rather, in performance of such contract administration duties, the obligations of an insurer are much closer to the normal contract duties of an insured – present in many policies – to pay premiums, provide information to the insurer and maintain adequate records to facilitate administration of a contract. (*See Kransco v. American Empire Surplus Line Insurance Co.*, *supra*, 23 Cal. 4th at pp. 404-405.)⁴

The Court went on to set forth three aspects of the relationship between an insured and insurer that are most distinctive in those cases supporting bad faith actions against an insurer. First, the insurer has virtually sole control of the proceedings, decisions, investigation and payment of claims by its insured. Second, the insured is subject to financial pressures that the insurance is intended to mitigate. Third, the insured must initiate acts against the insurer in order to obtain the benefits of the insurance policy. The insurer may simply refuse action unless the insured has the financial resources and the perseverance to force the insurer’s hand; the insured cannot just go out into the marketplace and purchase replacement coverage for the loss that has already occurred. Those facts were distinguished by the Appellate District Court of Appeals in reversing the award for punitive damages based upon the

collection of additional premium by the insured.⁵ The Court went on to state that none of the above factors are present in the case of a premium dispute as in this case. The insured can do nothing and make the insured prove its entitlement to additional premium in litigation initiated by the insurer.

The *Jonathan Neil* case may appear to be a collection case at first blush, but a reading of the language of the District Court of Appeals shows that the Court had analyzed all of the current trends by the California State Supreme Court and the intermediate appellate courts and determined the present trend in California was toward limiting tort recovery in both insurance and noninsurance cases.⁶ The Court agreed with the insurer that all breaches of the provisions of a contract of insurance will not support a bad faith claim, but rather only breaches of duties that relate to claims handling functions which threaten the peace of mind that the insured sought by purchasing the insurance coverage. A full and complete reading of the *Jonathan Neil* case is in order for anyone who seeks to fathom the present status of bad faith actions relating to insurance contracts in the state of California.

Endnotes

1. *Jonathan Neil & Associates v. Jones* (2002) 98 Cal. App. 4th 434, 119 Cal. Rptr. 2d 660.
2. California, until recently, has been in the forefront of cases allowing recovery against insurers on the implied covenant of good faith and fair dealing. See *Comunale v. Traders & General Ins. Co.* (1950) 50 Cal. 2d 654, 658, 328 P.2d 198; *Crisci v. Security Ins. Co.* (1967) 66 Cal. 2d 425, 430-431, 426 P.2d 173; *Egan v. Mutual of Omaha Ins. Co.* (1979) 24 Cal. 3d 809, 816-817, 598 P.2d 452; *Walker v. Truck Ins. Exchange, Inc.* (1995) 11 Cal. 4th 1, 900 P.2d 619; and *Greenberg v. Aetna Ins. Co.* (1973) 9 Cal. 3d 566, 510 P.2d 1032.
3. *Jonathan Neil* at p. 451.
4. *Jonathan Neil* at p. 451.
5. *Jonathan Neil* at pp. 451-452.
6. *Jonathan Neil* at pp. 448-449 *Foley v. Interactive Data Corp.* (1988) 47 Cal. 3d 654, 685-691, 765 P.2d 373; *Freeman & Mills, Inc. v. Belcher Oil Co.* (1995) 11 Cal. 4th 85, 88, 900 P.2d 669; *Cates Construction, Inc. v. Talbot Partners* (1999) 21 Cal. 4th 28, 46, 980 P.2d 407.