Nos. 07-15326, 07-15356, 07-15541

IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

AMERICAN COLOR GRAPHICS, INC.

Plaintiff-Appellee-Cross-Appellant

vs.

TRAVELERS PROPERTY CASUALTY INSURANCE COMPANY,

Defendant-Appellant-Cross-Appellee.

On Appeal from the United States District Court
for the Northern District of California, Oakland Division
Case No. CV-04-03518-SBA
Hon. Saundra Brown Armstrong, Presiding

ASSOCIATION OF CALIFORNIA INSURANCE COMPANIES' AMICUS CURIAE BRIEF IN SUPPORT OF APPELLANT TRAVELERS PROPERTY CASUALTY COMPANY OF AMERICA (SEEKING REVERSAL)

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CORPORATE DISCLOSURE STATEMENT
(FEDERAL RULE OF APPELLATE PROCEDURE 26.1)

The Association of California Insurance Companies ("ACIC"), is a non-profit corporation formed under the laws of the State of California. No individual or corporation owns 10% or more of the stock of the Association of California Insurance Companies.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

FEDERAL CASES

STATE CASES

STATE STATUTES

INTRODUCTION

The Association of California Insurance Companies ("ACIC") represents more than 300 property/casualty insurance companies doing business in California. ACIC member companies write 41.8 percent of all property and casualty insurance in California, including 57.3 percent of private passenger automobile insurance, 40 percent of homeowners insurance and 43.4 percent of private workers' compensation insurance. ACIC is affiliated with the Property Casualty Insurers Association of America ("PCI"). With more than 1,000 member companies, PCI represents the broadest cross-section of insurers of any national trade association.[1]

Among other things, ACIC and PCI strive to ensure that the laws and regulations affecting insurance companies are fair, rationally based and do not needlessly add to the cost of providing insurance to California's consumers. ACIC and PCI are also concerned with the appropriate operation of our courts and the workers' compensation system.

ACIC has filed numerous amicus briefs before California courts, including in connection with various pending California Supreme Court cases. ACIC does not file an amicus brief in connection with every appeal that may have some impact on the insurance industry. Rather, ACIC provides amicus support in only those instances where a particular judgment could have a tangible, deleterious

[1] Travelers Property Casualty Company of America ("Travelers") is not a member of ACIC or PCI.

impact on its member companies, the operation of the courts, or the operation of the workers' compensation system. ACIC joins as amicus here because the judgment on appeal has a potentially adverse impact on the workers' compensation system as well as individual insurers.

Specifically, insurers should not be subject to tort liability, let alone punitive damages, for providing coverage and paying claims against their insureds. But that is precisely what happened here. Travelers faces substantial compensatory and punitive damages ($1.4 million) for accepting liability and then ultimately settling a single workers' compensation claim against its insured with the insured's approval.

The egregious nature of an award of punitive damages based on the payment of a single claim is exacerbated by the fact that the punitive damages award here is ten times the amount of the compensatory damages awarded plaintiff. Such a high punitive to compensatory damages ratio is one that the United States Supreme Court has reserved for only the most reprehensible of conduct. As explained below, even where an insurer unreasonably fails to pay a claim against its insured, the Supreme Court has indicated that the proper ratio is no more than one to one; not ten to one. Indeed, the Supreme Court recently confirmed a one to one ratio in Exxon Shipping v. Grant Baker, 2008 U.S. LEXIS 5263 (June 25, 2008), citing "the need to protect against the possibility (and the disruptive cost to the legal

system) of awards that are unpredictable and unnecessary, either for deterrence or for measured retribution." Id. at 76. Such limits on punitive damages articulated by the Supreme Court are intended to prevent the type of unjust punitive damage award imposed against Travelers here.

ARGUMENT

I. PUNITIVE DAMAGES SERVE NO PURPOSE WHEN THE INSURER PAYS A CLAIM

As this Court is aware, it is not uncommon for policyholders to challenge the failure of an insurer to provide coverage for a third-party claim against the policyholder. When the insurer's failure to provide such coverage is unreasonable, the insurer may be found liable in tort. Indeed, when the denial of coverage is accompanied by "oppression, fraud or malice," punitive damages are an available remedy. In theory, such damages are intended to prevent insurers from unreasonably denying coverage where policyholders are faced with a significant claim for which they thought they had purchased insurance.

The judgment below against Travelers turns that paradigm on its head. Here, the insurer accepted coverage of the workers' compensation claim filed against its insured. While the insured did have a deductible, the ultimate responsibility for payment of that claim belonged to the insurer if the insured failed to reimburse the deductible or payments exceeded the deductible. Given that the

insurer accepted the claim, and had a direct stake in the claim's outcome, punitive damages seem wholly unwarranted.

Punitive damages are quasi-criminal in nature, are disfavored and "should be granted with the greatest of caution." Beck v. State Farm Mutual Auto., 54 Cal. App. 3d 347, 355 (1976). By statute, imposition of punitive damages requires clear and convincing proof that the defendant engaged in "oppression, fraud, or malice." Cal. Civ. Code § 3294(a). Moreover, it "should be presumed a plaintiff has been made whole for his injuries by compensatory damages, so punitive damages should only be awarded if the defendant's culpability, after having paid compensatory damages, is so reprehensible as to warrant the imposition of further sanctions to achieve punishment or deterrence." Jet Source Charter, Inc. v. Doherty, 148 Cal. App. 4th 1, 9 (2007) (citing State Farm Mutual Automobile Insurance Co. v. Campbell, 538 U.S. 408, 419 (U.S. 2003).

It is not entirely clear what purpose is furthered by "punishing" an insurer with punitive damages for accepting a single workers' compensation claim, even if the claim is considered to have no merit. Ironically, it appears that the insured here contends that Travelers should be punished not for its acceptance of the claim but, rather, for its alleged failure to fully investigate the claim it accepted. But, given that the record shows that Travelers did take steps to investigate the claim (even before the insured complained), a failure to "properly" investigate or in the

ultimate decision-making sounds of negligence and not "reprehensible conduct" that must be "punished" or "deterred." See Tomaselli v. Transamerica Ins. Co., 25 Cal. App. 4th 1269, 1288 (1996).

Perhaps most importantly, even if there was a failure to investigate, that failure did not violate the special duties of defense and indemnity. Those specific duties, defense and indemnity, are the special duties protected by bad faith tort liability and punitive damages. See Waller v. Truck Insurance Exchange, 11 Cal. 4th 1, 35 (1995); Jonathan Neil & Assoc., Inc. v. Jones, 33 Cal. 4th 917, 938 (2004) (withholding payment of a claim could subject insurer to tort liability). And even where those duties are breached in the context of claims handling, California courts are reluctant to award punitive damages. See Tomaselli, 25 Cal. App. 4th at 1288 (while failing to follow up on information provided by the insured and failing to communicate with the insured may be described as "negligent" or even "callous," it is not malicious or oppressive and does not support the imposition of punitive damages).

The context within which this claim was accepted is also important to understand. California law expressly encourages the payment of workers' compensation claims: "[T]he established legislative policy is that [the Workers' Compensation Act] must be liberally construed in the employee's favor and all reasonable doubts as to whether an injury arose out of employment are to be

resolved in favor of the employee." McLune v. Workers' Compensation Appeals Board, 62 Cal. App. 4th 1117, 1121 (1998) (citing Garza v. Workmen's Comp. App. Bd., 3 Cal. 3d 312 (1970); see Cal. Labor Code § 3600(a). The punitive damages award here stifles rather than encourages the payment of workers' compensation claims.

In sum, no legitimate "punishment" or "deterrent" objective is satisfied by awarding millions of dollars to punish California insurers who actually accept a workers' compensation claim. Even where the insured has a deductible, its insurer is still liable to the injured worker, whether or not the insured meets its contractual obligation to reimburse the insurer for the amount of that deductible. While punitive damages may be understood to be appropriate to prevent unreasonable and egregious insurer conduct in other contexts, e.g., failing to defend or indemnify the insured against a third-party claim, an award of punitive damages simply serves no recognized purpose here.

II. THE RATIO OF PUNITIVE TO COMPENSATORY DAMAGES HERE EXCEEDS THAT REQUIRED BY DUE PROCESS

In State Farm v. Campbell, the United States Supreme Court determined that the federal constitutional due process clause places important restrictions on punitive damage awards. Imposing excessive or arbitrary awards is unconstitutional because due process affords a defendant to "fair notice not only of

the conduct that will subject him to punishment but also of the severity of the penalty that a state may impose." 538 U.S. at 417.

Here, the District Court's judgment includes a punitive damages award which is ten times greater than the award of compensatory damages. This is a level that the Supreme Court has reserved for the most "reprehensible" conduct such as where purposeful discrimination is involved. See, e.g., Zhang v. American Gem Seafoods, 339 F. 3d 1020, 1044 (9th Cir. 2003) (intentional racial discrimination). Even in the typical "bad faith" case, where the insured was unreasonably denied defense and/or indemnity against a third-party claim, such "bad faith" fails to rise to the level of conduct of sufficient reprehensibility to support a higher ratio of punitive to compensatory damages. See, State Farm, 538 U.S. at 429 (endorsing a one to one ratio in bad faith case); Walker v. Farmers Insurance Exchange, 153 Cal. App. 4th 965, 974 (2007) (even where insured had to borrow money to defend herself against third party claim, insurer's unreasonable denial of claim did not support more than one to one ratio).

Thus, if the Court finds punitive damages are warranted here, ACIC agrees with Travelers that the ratio of punitive damages to compensatory damages should be no greater than one to one. This is an issue of importance to all types of business, not just insurers.

Indeed, any ratio greater than one to one here would be inconsistent with numerous decisions, including the United States Supreme Court's recent decision in Exxon Shipping Co., 2008 U.S. LEXIS 5263, addressing punitive damages against Exxon for the oil spill in Prince William Sound in 1989. Exxon spent some $2.1 billion in cleanup efforts, pleaded guilty to criminal violations occasioning major fines, settled a civil action by the United States and Alaska for at least $900 million, and paid another $303 million in voluntary payments to private parties. Other civil cases were consolidated into this one, and the jury awarded $287 million in compensatory damages to some of the plaintiffs; still others had settled earlier for $22.6 million. The jury subsequently awarded $5 billion in punitive damages against Exxon. The Ninth Circuit remitted the punitive damages award against Exxon to $2.5 billion or five to one. Recognizing that the relevant compensatory damages awarded were $507.5 million, the Supreme Court held that the actual correct ratio of punitive damages to compensatory damages was one to one.

While the specific issue in Exxon was "whether the award of $2.5 billion in this case is greater than maritime law should allow in the circumstances," the Supreme Court, relying on detailed studies, discussed the appropriate ratio of punitive damages to compensatory damages. As the Supreme Court explained, a

careful study of punitive damage cases fails to support a ratio greater than one to one in cases like this one:

> These studies cover cases of the most as well as the least blameworthy conduct triggering punitive liability, from malice and avarice, down to recklessness, and even gross negligence in some jurisdictions. The data put the median ratio for the entire gamut of circumstances at less than 1:1, see supra, at 25-26, and n. 14, meaning that the compensatory award exceeds the punitive award in most cases. In a well-functioning system, we would expect that awards at the median or lower would roughly express jurors' sense of reasonable penalties in cases with no earmarks of exceptional blameworthiness within the punishable spectrum (cases like this one, without intentional or malicious conduct, and without behavior driven primarily by desire for gain, for example) and cases (again like this one) without the modest economic harm or odds of detection that have opened the door to higher awards. It also seems fair to suppose that most of the unpredictable outlier cases that call the fairness of the system into question are above the median; in theory a factfinder's deliberation could go awry to produce a very low ratio, but we have no basis to assume that such a case would be more than a sport, and the cases with serious constitutional issues coming to us have naturally been on the high side, see, e.g., State Farm, 538 U.S., at 425 (ratio of 145:1); Gore, 517 U.S., at 582 (ratio of 500:1). On these assumptions, a median ratio of punitive to compensatory damages of about 0.65:1 [footnote omitted] probably marks the line near which cases like this one largely should be grouped. Accordingly, given the need to protect against the possibility (and the disruptive cost to the legal system) of awards that are unpredictable and unnecessary, either for deterrence or for measured retribution, we consider that a 1:1 ratio, which is above the median award, is a fair upper limit in such maritime cases.

Id. at 75 - 76 (emphasis added).

Thus, Exxon does not support a ratio greater than one to one here. It is apparent that the record here does not contain evidence of "exceptional blameworthiness." There is no evidence that Travelers' conduct was "driven primarily by desire for gain." Moreover, the alleged reprehensibility of Travelers' conduct here falls far below the criminal conduct held to justify only a one to one ratio in Exxon.

In fact, Travelers' alleged failure to investigate occurred in its administration of one of hundreds of claims it handled for ACG, without complaint, during the relevant time period. Travelers accepted the claim, and therefore accepted full responsibility for it, consistent with California's policy to encourage the payment of workers' compensation claims. For these reasons and those discussed in Travelers' briefing, a ten to one ratio of punitive damages to compensatory damages is particularly unfair and incompatible with due process.

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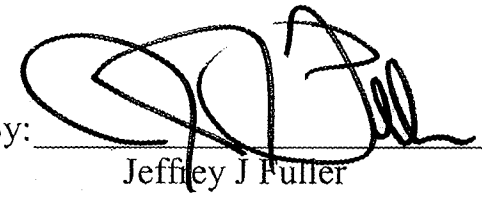
CONCLUSION

As explained above, there is simply no support for awarding punitive damages against an insurer for accepting a claim and, therefore, responsibility for that claim. Even if the Court somehow finds punitive damages are warranted here, given the lack of reprehensibility shown by Travelers' conduct, a ten to one ratio of punitive to compensatory damages is improper. The ratio should be no greater than one to one.

Dated: July 2, 2008

ASSOCIATION OF CALIFORNIA INSURANCE COMPANIES

By: 

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CERTIFICATE OF WORD COUNT

I certify that pursuant to Federal Rule of Appellate Procedure 32(a)(7)(C), the attached memorandum contains 2,406 words, excluding the Corporate Disclosure Statement, Table of Contents, Table of Authorities and this Certificate, in proportionately spaced typeface of 14 points as counted by the word-processing program used to generate the memorandum.

Dated: July 2, 2008

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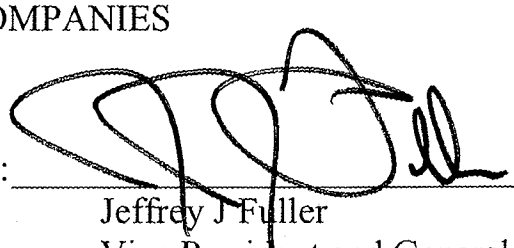

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PROOF OF SERVICE

I declare that I am employed with the Association of California Insurance Companies, whose address is 1415 L Street, Suite 670, Sacramento, CA 95814. I am not a party to the within cause, and I am over the age of eighteen years.

I further declare that on July 2, 2008, I served a copy of:

ASSOCIATION OF CALIFORNIA INSURANCE COMPANIES' AMICUS CURIAE BRIEF IN SUPPORT OF APPELLANT TRAVELERS PROPERTY CASUALTY COMPANY OF AMERICA (SEEKING REVERSAL)

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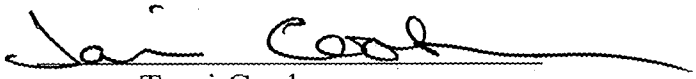

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