4th Civil Case No. G015482

IN THE COURT OF APPEAL

OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

SURGIN SURGICAL INSTRUMENTATION, INC.,

Plaintiff and Respondent,

vs.

TRUCK INSURANCE EXCHANGE,

Defendant and Appellant.

Appeal from the Orange County Superior Court
Honorable C. Robert Jameson, Judge
Case No. 66 22 16

APPELLANT'S REPLY BRIEF

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INTRODUCTION

Like a veteran sleight-of-hand artist, Surgin has repeatedly used distraction and misdirection in an attempt to create the illusion that it is a victim of insurance and discovery abuse and that Truck is an unrepentant abuser. A superficial review of Surgin's deceptive presentation might lead an uncritical reader to be fooled. But the truth is far different.

Setting the record straight in the face of such wholesale manipulation of the facts and law is a daunting prospect: Responding to every mischaracterization—disproving every inaccuracy—would expand this already sizeable brief well beyond readability and would ultimately detract from the core issues that truly merit attention. However, a few examples of Surgin's technique serve to illustrate why its presentation, however slick it might be, warrants careful scrutiny at every step of the way:

- Seeking to avoid over a century of statutory and decisional law establishing that the $57.2 million punitive damage award directly violates express jurisdictional limits that govern default proceedings, Surgin relies on recently-enacted Civil Code section 3295(e)'s mandate that no claim for punitive damages may state an amount. However, Surgin never mentions that section 3295(e) was enacted as part of a comprehensive legislative scheme *designed to curtail punitive damages*—even though this fact makes it unmistakably clear that there is no rational possibility the Legislature could have intended the legislation to *expand* potential punitive damage liability in default proceedings or to repeal, *sub silentio*, the long-established statutory mandate that a default judgment shall "not exceed[] the amount stated in the complaint." Code of Civil Procedure section 585(b) expressly so requires, yet *not once* in its 73-page brief does Surgin bother to cite or quote this controlling statute, let alone deal with its explicit language. (See discussion *infra*, pp. 8-12.)

- Faced with *Watercloud's* unequivocal preclusion of any duty to defend Alcon's patent infringement claims (which accounted for 98% of Surgin's claimed defense fees), Surgin concocts an alternate breach of promise theory premised mainly on *Travelers Ins. Co. v. Lesher* (1986) 187 Cal.App.3d 169. Surgin's portrayal of *Lesher's* supposed holding is pure fiction. Surgin fails to disclose that what it claims is *Lesher's* holding is actually something the *Lesher* court specifically described as merely the plaintiff's *contention*. Nor does Surgin disclose that the appellate court

never decided this contention because, as the court specifically noted, *the defendant conceded the point*. And beyond misrepresenting this irrelevant case, Surgin actually criticizes Truck for not citing it! (See discussion *infra*, pp. 39-41.)

- Surgin denies that the default judgment was based on claims that Surgin never pleaded, such as a purported pattern and practice of claims mishandling and supposed discovery abuse. Yet, in virtually the same breath, Surgin directly seeks to justify the $57.2 million punitive award by relying precisely on that evidence. (See discussion *infra*, pp. 24-26, 57-61.)

- Asserting there is substantial evidence to support the award of *Brandt* fees, Surgin relies on a few isolated snippets of testimony expressing conclusions that its attorney's billings covered only efforts to obtain policy benefits. Surgin never mentions that this testimony was *directly contradicted* by the very same billings, and it fails to cite the authorities holding that such conclusory testimony *cannot* constitute substantial evidence when it is refuted by the very documentary evidence to which it pertains. (See discussion *infra*, pp. 44-46.)

- Despite direct Supreme Court authority holding that modification of the compensatory award *requires* a redetermination of the punitive award—authority Surgin fails to cite—Surgin relies on a single decision that does not even purport to address that issue and that was decided years *before* the controlling Supreme Court authority. (See discussion *infra*, pp. 49-50.)

- Surgin relegates to a footnote its discussion of whether its complaint adequately pleaded facts sufficient to permit recovery of punitive damages under Civil Code section 3294(b), which provides that punitive damages cannot be recovered against a corporate employer unless the pertinent conduct was authorized or ratified by an *officer, director*, or *managing agent*. The complaint indisputably fails to allege the facts required by Civil Code section 3294(b). Instead of addressing this failing, Surgin—in a masterpiece of misdirection—responds to an argument Truck never made; cites nonexistent evidence; ignores section 3294(b)'s explicit requirements; relies on a decision that section 3294(b) was specifically enacted to limit; and does not even cite this Court's own precedent directly rejecting its position. (See discussion *infra*, pp. 33-35.)

- Surgin's misdirection metastasizes when it comes to the discovery dispute. For example:

- Surgin accuses Truck of lying by initially denying the existence of claims manuals and then "finally admit[ting] that claims manuals exist." But the only thing Truck ever denied was the existence of the type of manuals *Surgin specifically requested*: manuals "used," "referred to or relied upon" in handling advertising injury claims. There was *never* a discovery request that sought, and Truck *never* denied that it had, other types of claims manuals used in other contexts. (See discussion *infra*, pp. 65-66.)

- When Surgin was seeking terminating sanctions, it claimed that Truck had been required to produce "all . . . reports on this litigation by [Truck's then-trial counsel] Lichtman & Bruning and Greines, Martin, Stein & Richland". Yet *it disavowed that very same construction* when it resisted Truck's writ petition seeking this Court's protection from disclosure of such obviously privileged materials. At that time, Surgin conveniently proclaimed that "[a]bsolutely no such order was entered . . . . Judge Jameson never actually directed Truck to produce 'all . . . reports on this litigation by Lichtman & Bruning and Greines, Martin, Stein & Richland.'" Now, Surgin has come full circle, once again claiming that these materials had to be produced after all. (See discussion *infra*, pp. 69-70, 75-76.)

- In seeking to justify the severity of the penalty (i.e., terminating sanctions), Surgin claims that Truck's discovery abuse went to "the entirety of Surgin's claims." It supports this assertion by reference to a series of "contention" discovery requests that addressed the basis for Truck's denials of the complaint's allegations. The perception Surgin tries to create is utterly false. Surgin's brief *admits* that Truck produced documents responsive to the contention requests; it advances *no* argument that such production was inadequate. Thus, although Surgin tries mightily to have this Court think otherwise, it has not pointed to a single discovery defalcation that went to the entirety of the case. (See discussion *infra*, p. 81.)

We could go on and on, but doing so would only further Surgin's goal of diverting attention from the real issues. When the real issues are examined, there is only one permissible conclusion: The $57.8 million default judgment is an outrageous miscarriage of justice stemming from repeated violations of fundamental federal and state constitutional due process guarantees and California substantive law. The judgment must be reversed.

LEGAL DISCUSSION

I.

THE CONTROLLING STATUTORY PROCEDURE GOVERNING DEFAULT JUDGMENTS EXPRESSLY LIMITS SUCH JUDGMENTS TO THE AMOUNT PLEADED IN THE COMPLAINT—HERE NO MORE THAN $270,000.

One would never know from Surgin's brief that Code of Civil Procedure sections 580 and 585 place specific limits on compensatory and punitive damages. The statues unequivocally provide that no default judgment shall "exceed[] the amount stated in the complaint. . . ." (§ 585(b).)[1/] The Supreme Court holds this limit must be interpreted "in accordance with its plain language"; it "means what it says and says what it means: that a plaintiff cannot be granted more relief than is asked for *in the complaint.*" (*In re Marriage of Lippel* (1990) 51 Cal.3d 1160, 1166, emphasis added.) Under the law, the default judgment here may not exceed the $270,000 pleaded in Surgin's complaint.

Surgin asks this Court to disregard the law. But the limitation is *jurisdictional.* It cannot be disregarded. (AOB 12-13.)[2/]

A. The Jurisdictional Limitation That A Default Judgment May Not Exceed The Amount Pleaded In The Complaint Applies To All Compensatory Damages; There Is No Exception For *Brandt* Fees.

Surgin's rationale for recovering over double the compensatory damages pleaded in its complaint is that sections 580 and 585 should not apply to *Brandt* fees (see *Brandt v. Superior Court*

1/ Except as noted, all further statutory references are to the Code of Civil Procedure; however, references to "section 3295(e)" are to Civil Code section 3295(e).

2/ We use the following abbreviations: AOB: Appellant's Opening Brief; JA: Joint Appendix; RB: Respondent's Brief; RT: Reporter's Transcript; RJN: Appellant's Request For Judicial Notice; SRJN: Appellant's Supplemental Request For Judicial Notice (filed concurrently with this brief).

(1985) 37 Cal.3d 813, 817) because Surgin incurred those fees after filing its complaint and, thus, could not have known their exact amount.[3] (RB 50-51.) This argument fails for many compelling reasons:

1. Sections 580 and 585 provide for no such exception. If Surgin's view were correct, any plaintiff who suffered post-complaint or future damages would be free to obtain potentially limitless recovery on default; routinely-pleaded future damage claims, such as future economic losses (i.e., lost rents, wages, profits, etc.), future medical expenses and future pain and suffering, would suddenly fall outside the statute. That would nullify the statute.

2. Not surprisingly, California courts have rejected Surgin's exact argument.[4] In *Greenup v. Rodman* (1986) 42 Cal.3d 822, our Supreme Court specifically rejected the contention—identical to Surgin's here—that a plaintiff should not be bound on default by the amount pleaded in the complaint even though the dissent argued that "plaintiff could not realistically estimate the losses she suffered." (Compare *Greenup*, *supra*, 42 Cal.3d at p. 829, majority opn. with *id.* at p. 833, Bird, C.J., dissenting.)[5]

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[3] Even the non-*Brandt* fees portion of the compensatory damages award exceeds the $270,000 jurisdictional limit. (See JA 7481.) Surgin offers no rationale for this violation.

[4] E.g., *Becker v. S.P.V. Construction Co.* (1980) 27 Cal.3d 489 [striking award of attorney's fees because complaint failed to plead any amount]; *Brooks v. Forington* (1897) 117 Cal. 219 [failure of prayer to claim amount for attorney's fees precludes their award even though the pleaded agreement allowed for award of attorney's fees]; *Parrott v. Den* (1867) 34 Cal. 79 [although mortgage allowed plaintiff to recover all taxes plus interest on foreclosed property, default award for taxes and interest was improper as no specific amount was pleaded in complaint]; *Lee v. Ski Run Apartment Associates* (1967) 249 Cal.App.2d 293, 298 [although complaint alleged assignment of ongoing profits of $5,000 per month, no monetary amount could be recovered on default as no amount of damages was specified in complaint]; *Von Der Kuhlen v. Hegel* (1921) 51 Cal.App. 416, 417 [reversing award of interest in excess of amount pleaded in complaint].

[5] Against this avalanche of authority, Surgin cites but one case, *Ely v. Gray* (1990) 224 Cal.App.3d 1257, 1262-1263 (cited at RB 50). But *Ely* actually *supports* Truck's position. Unlike the present case, *Ely* was not an action for damages, but rather was an equitable action for an accounting. Even though section 425.10 applies only to actions for damages and even though no other statute requires a plaintiff in an accounting action to plead an amount sought, *Ely* nonetheless holds that a plaintiff in an accounting action still must give notice of the amount

(continued...)

3. Even if there were some unstated exception for post-complaint damages, it would not apply here because Surgin's complaint expressly pleaded *Brandt* fees *as a part of* the $270,000 sought in compensatory damages, repeatedly alleging that Surgin's $270,000 in losses *included* "Surgin's attorney's fees and costs incurred in compelling [Truck] to pay" its defense fees. (JA 160-161, 163-164, emphasis added; see *Hartke v. Abbott* (1931) 119 Cal.App. 439, 442 [rejecting award of $301 for attorney's fees in default judgment where complaint sought only $200 as attorney's fees].)

4. Section 425.10 requires that *all* amounts of damages be pleaded in the complaint in commercial cases, such as this one. Only actions seeking recovery of "actual or punitive damages for personal injury or wrongful death" are excepted; there is *no exception* for future damages. Indeed, plaintiffs routinely plead specific amounts for unincurred future damages. They do so by estimating the amount. That is exactly what Surgin did here: It estimated its compensatory damages, specifically including *Brandt* fees, at $270,000. If that estimate later proved too low, Surgin had a straightforward remedy—amend its complaint to increase its claim. (§§ 464, 472.) Surgin never availed itself of that remedy. It cannot now bootstrap its own pleading failure into a reason for discarding express jurisdictional limits on default recoveries. The statute—not Surgin's pleading oversight—must prevail.

5. The jurisdictional error is highlighted, not excused (as Surgin contends, RB 50), by the fact that $93,500 of Surgin's supposed *Brandt* fees were incurred over six months *after* the trial court entered Truck's default. (See JA 6691.) If accepted, Surgin's position would mean that after a default a plaintiff is free to run up limitless legal bills and charge them to a defaulted defendant, who cannot even contest them. Such a result is antithetical both to the default statutes and to basic

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[5/](...continued)
it seeks before the court can render a default judgment for that amount (224 Cal.App.3d at p. 1263). In *Ely*, the default judgment was reversed because the defaulted defendant received no notice at all (*id.* at p. 1264); therefore, *Ely* was not required to and did not consider what quantum of notice would suffice. (E.g., *Security Pacific National Bank v. Wozab* (1990) 51 Cal.3d 991, 1003-1004 [case cannot stand for proposition not considered]; *Brown v. Kelly Broadcasting Co.* (1989) 48 Cal.3d 711, 734-735 [same].)

notions of due process requiring "that defendants be told *exactly* what their exposure is." (*Pino v. Campo*, (1993) 15 Cal.App.4th.Supp. 1, 5, emphasis added, internal quotation marks omitted; see *Greenup, supra*, 42 Cal.3d at p. 829 ["due process requires notice to defendants . . . of the *potential consequences* of a refusal to pursue their defense"].)

The $574,284.72 compensatory damage award must be reversed. It cannot exceed $270,000.

B. The Same Jurisdictional Limitations On Default Compensatory Recoveries Apply With Equal Force To Claims For Punitive Damages.

It has long been settled that, under sections 580 and 585, the punitive damage portion of a default judgment may not exceed the amount pleaded in the complaint. (E.g., *Gudarov v. Harjieff* (1952) 38 Cal.2d 412, 416-417 [court struck punitive damages awarded on default because no amount of punitive damages was pleaded, even though total judgment was within amount of pleaded compensatory damages].) Surgin seeks to avoid this settled principle by relying on Civil Code section 3295(e), which provides that "[n]o claim for exemplary damages shall state an amount or amounts." (RB 47.)

The drafters of that statute would be astonished by Surgin's argument. The reason: they created section 3295(e) as one of a group of statutes uniformly designed to *limit* punitive damage awards. Nevertheless, according to Surgin, this *restrictive* legislation (which does not even refer to default procedures) *silently* upended over a century of settled default law, *silently* created a gaping exception to the explicit jurisdictional dollar limits on default judgments, and *silently* made it *easier* to obtain default recoveries of punitive damages than default recoveries of compensatory damages. Settled principles of statutory construction preclude such a nonsensical result.

Surgin expresses concern that, if the default judgment laws are enforced as written, defendants will simply default to escape punitive damage liability. (RB 47.) This simplistic assertion bears no relation to reality. As we demonstrate below, the purpose of section 3295(e) can be achieved fully in several ways without incurring any such risk and without destroying settled default procedure. But the result in this case is *not* one of those ways.

1. Civil Code Section 3295(e) Was Never Intended, And Cannot Properly Be Construed, To Expand The Jurisdictional Limitations On Default Judgments For Punitive Damages.

Civil Code section 3295 was part of the "napkin" agreement that led to the compromise tort reform legislation known as the Civil Liability Reform Act of 1987 (Stats 1987, ch. 1498). (See *American Tobacco Co. v. Superior Court* (1989) 208 Cal.App.3d 480, 487-488, fn. 3.) The Act imposed across-the-board *restrictions* on plaintiffs' ability to recover punitive damages. (See, e.g., Civ. Code, §§ 3294(a) [raised burden of proof from "preponderance of the evidence" to "clear and convincing evidence"]; 3294(c) [added requirement of "despicable" conduct]; 3295(d) [bifurcated trial of liability and punitive damages, so that punitive damages phase could not take place until after a verdict finding malice, oppression, or fraud]; Code Civ. Proc., § 425.13 [limited pleading and proof of punitive damages in claims against health care providers], all enacted by Stats. 1987, ch. 1498.) Its purpose was to "[a]ddress[] the problem of excessive punitive damage awards. . . ." (SRJN Exh. 5, Republican Assembly Caucus, Talking Points Explanation of S.B. 241, p. 2.)

Section 3295(e) fits perfectly into this restrictive scheme. Its limited purpose is "to curtail use of such [punitive damage] claims as a tactical ploy." (*College Hospital Inc. v. Superior Court* (1994) 8 Cal.4th 704, 712; see SRJN Exh. 5, Republican Assembly Caucus, Talking Points Explanation of S.B. 241, p. 2 [Civ. Code, § 3295(e) "prohibits claims for punitive damages from stating amounts to prevent use of it as a publicity tactic"].)

In enacting section 3295(e), the Legislature said nothing to suggest (or even hint) that it intended the statute to have any impact on default procedure. Nor can one rationally infer that, despite its goal of *restricting* punitive damage recoveries in all cases, the Legislature somehow harbored a secret intent to expand them in default cases by silently eliminating the strict jurisdictional limitations on default judgments that have governed default proceedings for 115 years. As the Supreme Court said in *Fuentes v. Workers' Comp. Appeals Bd.* (1976) 16 Cal.3d 1, 7, "Repeals by implication are not favored, and are recognized only when there is no rational basis for harmonizing two potentially conflicting laws." (See also *In re Christian S.* (1994) 7 Cal.4th 768, 776; *Theodor v. Superior Court* (1972) 8 Cal.3d 77, 92.) Here, the Legislature is presumed to have

known what sections 580 and 585 provide and to have understood that, under *Greenup*, "unless and until the Legislature *specifically* provides a separate procedure," sections 580 and 585 continue to govern default proceedings and judgments. (See *Greenup*, *supra*, 42 Cal.3d at p. 828, emphasis added; *Bailey v. Superior Court* (1977) 19 Cal.3d 970, 977-978, fn. 10 [Legislature is presumed to know and act in light of existing case law]; *Estate of McDill* (1975) 14 Cal.3d 831, 839 [same]; *Unzueta v. Ocean View School Dist.* (1992) 6 Cal.App.4th 1689, 1697-1698 [Legislature's failure to alter statutory scheme in light of intervening statutory developments reveals intent to keep scheme in place according to its original plain language].)

In Surgin's view, the enactment of section 3295(e) silently scuttled sections 580 and 585, thus entitling a defaulted defendant to *less* formal notice of its exposure to potentially ruinous punitive damages than of its exposure to compensatory damages, even though punitive damages are disfavored, inherently more open-ended and not objectively determinable. (See *Las Palmas Associates v. Las Palmas Center Associates* (1991) 235 Cal.App.3d 1220, 1258 [punitive damages disfavored].) This may be an acceptable result on the other side of the looking glass where everything is backwards, but not here. Section 3295(e) cannot be used to turn default procedure on its head, nor is it necessary to read section 3295(e) in that manner in order to achieve its purpose.

2. The Statutes At Issue Here May Easily Be Harmonized, Fulfilling The Purposes Of Each.

This Court must construe section 3295(e) in light of the fundamental principle that, whenever possible, statutory directives must be harmonized to give effect to the statutory purposes of all. (*Fuentes*, *supra*, 16 Cal.3d at p. 7.) The Court may not ignore the language and purpose of several statutes (e.g., §§ 425.10, 580, 585) in favor of the language of one (§ 3295(e)).

The narrow anti-tactical-advantage, anti-publicity goals of section 3295(e) are fully served by strictly applying the statute at the outset of an action, when the shock and tactical advantage of publicizing a huge punitive-damage claim (perhaps even before the complaint is served) is the greatest. After that, if the defendant fails to answer and the plaintiff desires to obtain a punitive damage recovery by default, the plaintiff can simply move the trial court for permission to file an

amended complaint pleading a specific amount of punitive damages. This suggested procedure, which is quite similar to that already recognized by section 425.13(a) in suits for professional negligence against a health care provider,[6] would satisfy all statutory goals:

- It would comport with section 425.10, which requires that, in a case not involving personal injury or wrongful death, the complaint must state the amount of punitive damages demanded.[7]

- It would satisfy sections 580 and 585, which permit entry of a default judgment only in an amount "not exceeding the amount stated in the complaint."

- It would achieve the goals of section 3295(e). To the extent it did not completely eliminate the "tactical ploy/publicity" aspects of punitive damage claims, any lingering effects could be ameliorated by appropriate protective orders, such as requiring amendments alleging punitive damages to be filed under seal. (§ 473 [amendment to complaint can be allowed "upon any terms as may be just"].)

The net result: if the defendant continued to default after the amendment, the plaintiff would be entitled to recover punitive damages on default because there would have been full compliance with sections 425.10, 580 and 585; and the defendant would have no legitimate objection to the amendment based on any purpose still served by section 3295(e). Unlike Surgin's approach, the purposes of *all* the statutes would be fully served without disregarding the purpose of any.

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[6] Under section 425.13(a), "no claim for punitive damages shall be included in a complaint or other pleading unless the court [upon motion] enters an order allowing an amended pleading that includes a claim for punitive damages to be filed."

[7] In relevant part, section 425.10 provides: "A complaint . . . shall contain . . . [a] demand for judgment for the relief to which the pleader claims he is entitled. If the recovery of money or damages be demanded, the amount thereof shall be stated, unless the action is brought in the superior court to recover actual or punitive damages for personal injury or wrongful death, in which case the amount thereof shall not be stated."

3. To The Extent Civil Code Section 3295(e) Somehow Cannot Be Reconciled With Sections 425.10, 580 And 585, The Latter Statutes Must Control.

Where statutes on the same subject irreconcilably conflict, the statute most specifically directed to the issue in question controls. (E.g., *Shoemaker v. Myers* (1990) 52 Cal.3d 1, 21-22.) Sections 580 and 585 specifically govern default judgment proceedings and their limitations; section 425.10 specifically governs what must be contained in a complaint. On the other hand, section 3295(e) says nothing about default proceedings and its language does not expressly refer to complaints. In the context of default proceedings, sections 580 and 585 are the only statutes that apply; they and section 425.10 are clearly more specific than section 3295(e) and must govern. (See *Shoemaker v. Myers*, *supra*, 52 Cal.3d at pp. 21-22.)

This was the express holding in one of Surgin's own authorities, *Cummings Medical Corp. v. Occupational Medical Corp.* (1992) 10 Cal.App.4th 1291, 1296-1298. (RB 47-48.) There, the court held that, notwithstanding section 3295(e), a plaintiff could recover a default judgment for punitive damages *because* it had complied with sections 580 and 585 by pleading an amount for punitive damages *in the complaint*. (10 Cal.App.4th at p. 1296.) The court rejected the defaulting defendant's argument that section 3295(e) governed the default proceedings. (*Id.* at pp. 1297-1298.)

Finally, to the extent there is a choice between a restrictive and an expansive approach to default proceedings, the restrictive approach (embodied in sections 425.10, 580, and 585) should be favored over the expansive because the law favors resolving matters on their merits, rather than by default. (*Elston v. City of Turlock* (1985) 38 Cal.3d 227, 233, 235.) Moreover, the procedures outlined in section 425.10, 580 and 585 are an embodiment of due process principles. (*Greenup*, *supra*, 42 Cal.3d at pp. 828-829; *Pino*, *supra*, 15 Cal.App.4thSupp. at p. 4 [a default judgment that exceeds the demand of the complaint is "a denial of the due process right to a fair hearing"].)

4. Since Surgin Did Not Comply With The Requirements Of Sections 580 And 585, Surgin Has No Right To A Default Judgment For Punitive Damages.

In precluding a defaulted defendant from any further participation in the case, California's statutory default procedure is unique. It contrasts sharply with the common law and with the rules

in both federal and other state courts, where a defaulted defendant is permitted to contest damages by presenting evidence and cross-examining the plaintiff's witnesses. (*Greenup, supra*, 42 Cal.3d at pp. 828-829 [distinguishing procedure of contested hearing on damages followed in federal courts on the basis that section 585 provides a different procedure in California]; *Devlin v. Kearney Mesa AMC/Jeep/Renault, Inc.* (1984) 155 Cal.App.3d 381, 387, fn. 2 [California's procedure diverges from that of every other state researched].)[8/]

This unique California limitation is embodied in section 585(b), which states that "the court shall hear the evidence *offered by the plaintiff.*" (Emphasis added.) "*[U]nder section 585* there is no contest whatever once a defendant defaults." (*Greenup, supra*, 42 Cal.3d at p. 829; *Devlin, supra,* 155 Cal.App.3d at pp. 386-387 [same].) Since the only authority for default judgments in California is statutory and since sections 580 and 585 are the only statutes that govern default procedures, our Supreme Court has uniformly held that compliance with these statutes is essential

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[8/] See *Cyrus v. Haveson* (1976) 65 Cal.App.3d 306, 318 [at common law, after default, court issued a writ of inquiry under which a jury was empaneled to determine the amount of damages to be awarded]; *Sony Corp. v. Elm State Electronics, Inc.* (2d Cir. 1986) 800 F.2d 317 [reversing default judgment where court refused to consider defendant's evidence]; *Sumpter v. J.E. Sieben Construction Co.* (Mo.Ct.App. 1973) 492 S.W.2d 150, 155 [under writ of inquiry procedure, defendant is entitled to appear, cross-examine plaintiff's witnesses and present evidence to contest amount of damages]; *Pan American World Airways v. Gregory* (Fla.App. 1957) 96 So.2d 669, 672 ["It has long been established that after default in a tort action, the defendant has a right to put in proof and to be heard on the question of damages"]; 6 J. Moore, et al., Moore's Federal Practice (1994) ¶ 55.07, p. 55-58 & fn. 9 ["A defaulting defendant is entitled to be heard at the hearing on the amount of damages"]; W. McKinney, Encyclopædia of Pleading and Practice (1896) p. 136 ["The defendant is entitled, on the hearing in damages, to controvert the allegations of amount or value set up by the plaintiff"]; 2 A. Will, Standard Encyclopædia of Procedure (1911) pp. 561-62 ["And after default (the defendant) may appear, and is entitled to be heard upon the question of damages"]; 3 Blackstone, Commentaries on the Laws of England (1780) pp. 397-398 [at common law, in the event of a default the court (by writ of inquiry) ordered sheriff to convene a jury, and damages were tried under nearly the same law and conditions as a jury trial in court].

to the legitimacy of any default judgment.[9] Here, the default judgment exceeds the $270,000 jurisdictional limit. The excess is void.

It was Surgin, not Truck, who sought imposition of terminating sanctions. It was Surgin, not Truck, who invoked section 585(b)'s unique procedure, thus prohibiting Truck from any further participation in the proceedings. (JA 5723 [Surgin files Judicial Counsel Form requesting "court judgment under CCP 585(b)"], 2476 [specifying default prove-up to be conducted pursuant to § 585, "no notice to (Truck) required"], 7970 [Truck's counsel barred from even observing proceedings in chambers]; RT 357 [trial court's view that in this case there was only one side to be heard].) Surgin, however, now denies that section 585 governs its punitive damage claim. (RB 46-50.) In doing so, it jettisons the solitary procedure supporting its default award. Surgin cannot have it both ways: Its default judgment is either supportable under section 585, or not at all.

Surgin proclaims that, if sections 580 and 585 really mean what they say and say what they mean, then punitive damages would never be recoverable on default and defendants would be able to avoid punitive damages simply by defaulting. (RB 47.) This is both highly unrealistic and wrong.[10] Even if a defendant were prepared to accept the certainty of pleaded compensatory damages in order to avoid the risk of punitive damages, the escape would be as brief as it is illusory.

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[9] *Burtnett v. King* (1949) 33 Cal.2d 805, 807 [a "court's jurisdiction to render default judgments can be *exercised only in the way authorized by statute*," original emphasis]; *In Re Marriage of Lippel, supra,* 51 Cal.3d at p. 1167 [same]; *Becker, supra,* 27 Cal.3d at p. 493 ["a court *has no power* to enter a default judgment *other than in conformity with [Code of Civil Procedure] section 580*," emphasis added); *Greenup, supra,* 42 Cal.3d at p. 828 ["sections (580 and 585) remain the sole statutory procedures for default judgments"].

[10] However, in light of the windfall nature of punitive damages (*Las Palmas Associates, supra,* 235 Cal.App.3d at p. 1258), their purely public purpose (*Adams v. Murakami* (1991) 54 Cal.3d 105, 110), and the markedly different procedures employed in federal and other state courts, it would not be surprising if the Legislature—particularly a Legislature bent on restricting punitive damage awards generally, as was the 1987 Legislature—did intend to limit a plaintiff's ability to obtain a default judgment for punitive damages, just as it has limited the availability of default procedure in other contexts. (See, e.g., §§ 116.520(b) [no default judgment in small claims proceedings]; 764.010 [same re quiet title actions]; 1088 [same re mandamus actions]; Family Code, § 2336 ["[n]o judgment of dissolution or of legal separation of the parties may be granted upon the default of one of the parties"].)

First, as demonstrated above, there are ways for a plaintiff to amend its complaint to state an amount of punitive damages without violating the purposes of section 3295(e).

Second, nothing requires a plaintiff to avail itself of the abbreviated procedural short-cut of default.[11/] A plaintiff who wants a punitive damage recovery against a defendant who has not answered can do what *any* other plaintiff can do: Proceed to trial in ordinary fashion and prove its case, including its punitive damages case, in a proceeding in which the defendant has an opportunity to appear and defend itself. (See *Wilson v. Goldman* (1969) 274 Cal.App.2d 573 [where § 585 does not apply because defendant initially answered but does not appear at trial, plaintiff is not entitled to default judgment but must prove its case]; *Warden v. Lamb* (1929) 98 Cal.App. 738 [same]; *Brown v. Pacific Tel. & Tel. Co.* (1980) 105 Cal.App.3d 482, 486 [a plaintiff who chooses to proceed on the merits of his claim waives any default]; *Oil Tool Exchange, Inc. v. Schuh* (1944) 67 Cal.App.2d 288, 297 [same as *Brown*].)

Third, in a case where a defendant obstructs discovery, a plaintiff seeking to preserve its ability to recover punitive damages (but who, for some reason, does not opt to amend the complaint, as suggested above) can exercise a simple option: Don't ask the court to strike the defendant's answer, but instead ask for severe issue-preclusion sanctions, including (in appropriate cases) that liability be deemed established, and then proceed to a contested trial on damages. (See *Johnson v. Pratt & Whitney Canada, Inc.* (1994) 28 Cal.App.4th 613, 623-625.)

Surgin could have elected to proceed along any of these paths, but it didn't. Instead, it voluntarily *chose* to have Truck's answer stricken and thereafter to seek an uncontested default judgment. It therefore elected to follow and be bound by section 585's procedure. Surgin should not now be allowed to disavow the very statute it invoked. It is limited to the relief available under section 585: the $270,000 *pleaded in the complaint*. The entire default-judgment system should not be scuttled just because Surgin didn't do it right.

11/ Section 585 provides that, if a defendant fails to answer, judgment "*may* be had" under the default statutes. Subdivision (b) provides that default shall be entered "upon written *application* of the plaintiff" and, once entered, "[t]he plaintiff thereafter *may apply* to the court for the relief demanded in the complaint. . . ." (Emphasis added.)

5. Contrary To Surgin's Contention, Code Of Civil Procedure Section 425.11 Does Not Provide An Appropriate Analogy By Which To Invent A Non-Statutory Means Of Obtaining Default Judgments.

Surgin invents a procedure of its own in attempting to construct an analogy to sections 425.10 and 425.11. (RB 48-49.) Section 425.10 prohibits pleading an amount of actual or punitive damages in personal injury and wrongful death complaints; in those types of cases, section 425.11 requires a separate statement of damages setting forth the amounts sought. Despite the absence of any comparable legislative directive in commercial cases, Surgin argues that the Court should manufacture a similar procedure in those cases. Surgin reasons that since section 3295(e), like section 425.10, prohibits pleading a specific amount, there should be a procedure comparable to section 425.11's statement of damages that allows a plaintiff to compensate for the inability to plead the amount of punitive damages claimed. (RB 48-49.) Aside from the fact that the courts have no power to create such legislation, there are several dispositive reasons why Surgin's analogy is inapt:

a. Both the courts and the Legislature have made it clear that the limitations of sections 580 and 585 cannot be relaxed by implication. Indeed, in 1993 (*after* the trial court ordered Truck's default), the Legislature found it necessary to amend those sections (effective January 1, 1994, *after* entry of the default judgment against Truck) in order to accommodate the section 425.11 statement of damages procedure. It did so by providing that a default judgment could not exceed the amount stated in the complaint "or in the statement required by Section 425.11."[12/] These amendments

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[12/] See, e.g., analysis of Assembly Bill 58 prepared for the Senate Committee on Judiciary (SRJN Exh. 6 p. 2) ["(pre-e)xisting law limits the amount of a default judgment to the amount demanded *in the complaint*. (The new, amended language of sections 580 and 585) would *instead* limit the amount of a default judgment to the amount demanded in the complaint or the amount specified in a statement of damages filed in a personal injury or wrongful death action"; emphasis added]; Consent Analysis of Assembly Bill 58 prepared by the Office of Senate Floor Analyses (SRJN Exh. 7 pp. 1-2) [same]; see also Sept. 2, 1993, letter from Assemblyman Peace to Governor Wilson and enclosed summary of provisions of A.B. 58 (SRJN Exh. 8 pp. 1-2) ["The separate statement provision as it exists has made it very difficult to default defendants who will not respond to the complaint in these actions. The problem results from the failure to integrate CCP 425.11 with the existing default and prayer provisions of CCP 580 and 585"]; Author's Analysis of A.B. 58 (SRJN Exh. 9, pp. SP 12, AP 5) ["the separate statement provision has caused all kinds of havoc when a default judgment is to be entered. The problems (continued...)

would have been an idle act if a statement of damages were, by implication, sufficient to satisfy the former, more narrow requirements of sections 580 and 585 limiting default judgments to the amount stated in the complaint. The courts have reached the same result. (*Engebretson & Co. v. Harrison* (1981) 125 Cal.App.3d 436, 439-441 [service of a section 425.11 statement of damages in a commercial case cannot cure a failure to plead an amount of damages in the complaint].) If neither the Legislature nor the courts considered section 425.11 (with its express, formal mechanism for providing explicit notice of the amount of damages sought) to be an implied exception to sections 580 and 585, *a fortiori* section 3295(e) cannot furnish the basis for such an implied result.

b. Section 425.11 was already in effect when the Legislature passed section 3295(e). If the Legislature had intended to utilize the section 425.11 statement-of-damages procedure as a means of satisfying sections 580, 585 and 3295(e), it could easily have done so. It did not. (See *Unzueta*, *supra*, 6 Cal.App.4th at pp. 1697-1698 [that Legislature did not amend statute to accommodate new procedure in a related area indicates intent not to accommodate that procedure].) Similarly, when the Legislature amended sections 580 and 585 in 1993 to include reference to a section 425.11 statement of damages, it could easily have made similar provision for punitive damages if it so desired, but—once again—it did not.

c. But even if section 425.11 afforded an implied procedure by analogy, it affords Surgin no relief here because Surgin did not follow the specific procedure that its own analogy would have required. If Surgin believed that a formal statement of damages would have solved its problem, then it should have served one. But it didn't. The last-minute settlement letters it relies upon simply do not satisfy section 425.11's explicit requirement of a separate, formal statement of damages. (E.g., *Debbie S. v. Ray* (1993) 16 Cal.App.4th 193, 199-200 [§ 998 demands, at-issue memorandum, and settlement negotiations do not satisfy § 425.11]; *Morgan v. Southern Cal. Rapid*

[12/](...continued)
all result from the failure of AB 4467—or subsequent legislation—to integrate CCP 425.11 with the existing default and prayer provisions of CCP 580 and 585"].

Transit Dist. (1987) 192 Cal.App.3d 976, 986-987 [same regarding written discovery responses and settlement negotiations], disapproved on other grounds in *Schwab*, *supra*, 53 Cal.3d at p. 434.)[13]

6. There Is No "Actual Notice" Exception To The Requirements Of Sections 580 And 585. The Isolated Instances Where Default Judgments Have Been Affirmed Based Upon "Actual Notice" Have Occurred Only Where The Plaintiff Did, In Fact, Comply With Sections 580 and 585 By Specifically Pleading An Amount Of Damages In The Complaint.

Surgin asserts that the amount of damages awarded here is proper because the trial court "found" that Truck had "actual notice" of the amounts Surgin demanded. (RB 51.) This so-called finding is irrelevant: By statutory mandate, a trial court has *no jurisdiction* to enter a default judgment that exceeds the amount pleaded in the complaint; it thus has *no power* to supplant the strict statutory pleading requirement with a relaxed "actual notice" standard.[14]

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[13] Surgin argues that the formal requirements of section 425.11 do not apply here because this is not a personal injury or wrongful death action. (RB 54.) But this is doubletalk—a classic have-your-cake-and-eat-it argument. Just as Surgin should not be allowed to rely on section 585's procedure for a default prove-up while ignoring its express limitations on recoverable damages, it should also not be able to rely on section 425.11 to manufacture an implied alternative procedure to section 585 while eschewing compliance with section 425.11's requirements for a statement of damages. (See RB 54.) As one court said in a slightly different context: "Insofar as judgments by default are concerned, . . . [t]he plaintiff cannot rely on the rules for the entry of its judgment and ignore the same rules when such judgment is contrary to any meaningful concept of justice. The rules giveth and the rules can taketh away." (*W. D. Haddock Construction Company v. D. H. Overmyer Co., Inc.* (Del. Super. Ct. 1969) 256 A.2d 760, 762.)

[14] In any event, the trial court's so-called "finding" is suspect. It first surfaced in the judgment prepared by Surgin (JA 7480), *having never previously been mentioned by the trial court or by Surgin.* This was *after* Truck's default, *after* the default prove-up and *after* the trial court had announced its decision and recited the basis for it, all without the court or Surgin breathing a word about the amount of damages pleaded in the complaint. After all this had transpired, Surgin apparently realized it had led the court to act wildly in excess of its jurisdictional limits, and it tried to cobble something together in its proposed judgment in an effort to protect the void result. (See discussion at pp. 20-23, *infra*.) This afterthought is not enough.

Our Supreme Court has squarely held that there is no "actual notice" exception to the requirements of sections 425.10, 580 and 585. As *Greenup* flatly declared: "[A]ctual notice may not substitute for service of an amended complaint." (43 Cal. 3d at p. 826.)

The handful of decisions purportedly applying an "actual notice" test are consistent with *Greenup*. They involve extremely narrow circumstances where a plaintiff is statutorily precluded from pleading an amount of damages in the complaint *but does so anyway*—thus giving the defendant "actual notice" exactly as the default statutes require, even though the notice violates *other* statutes. In these narrow circumstances, the courts have held that, *since the default requirements were met,* the default judgment could stand. For instance, in *Uva v. Evans* (1978) 83 Cal.App.3d 356, the plaintiff violated section 425.10 by pleading an amount of damages in a personal injury complaint. Although it reversed the damage award as excessive, the Court of Appeal affirmed the default judgment because it complied with the default statutes:

> "Right or wrong, the complaint filed and served herein did contain a recitation of the damages sought and the judgment did not exceed the amount requested. In this case, section 580 was fully complied with." (*Id.* at pp. 360-361, footnote omitted; accord *Cummings*, *supra*, 10 Cal.App.4th at p. 1297 [plaintiff pleaded amount of punitive damages in complaint, even though that was precluded by § 3295(e); held, since pleading complied with §§ 580 and 585, default judgment affirmed].)

In *Engebretson & Co.*, *supra*, 125 Cal.App.3d at pp. 439-441, the Court of Appeal rejected Surgin's position. The court held that even actual notice in the form of a formal section 425.11 statement of damages did not suffice to give the required notice in a non-personal injury case that is not subject to section 425.11. (125 Cal.App.3d at pp. 439-441.) *Engebretson* was specifically approved by the Supreme Court in *Greenup*, *supra*, 42 Cal.3d at pp. 826-827. (See also *Schwab*, *supra*, 53 Cal.3d at p. 433 ["*Greenup* cited and relied in large part on *Engebretson*"].)

None of the authorities relied upon by Surgin suggests or permits any different conclusion:

a. In *Wiley v. Rhodes* (1990) 223 Cal.App.3d 1470, 1473-1474, a personal injury action subject to section 425.11, the plaintiff obtained a default judgment for punitive damages despite failing to provide *any* notice of the amount of punitive damages sought. On appeal, the plaintiff asserted that the complaint's demand for an unspecified amount of punitive damages sufficed. The Court of Appeal reversed, holding that a judgment rendered with *no notice* of the *amount* of punitive damages was void. *Wiley's* footnote dictum speculating about how notice *might* have been accomplished (*id.* at pp. 1473-1474, fns. 3 & 4) is hardly a basis for concluding—contrary to sections 580, 585 and *Greenup*—that there is an "actual notice" exception. (See authorities cited at conclusion of footnote 5, *supra*.)

b. Surgin exaggerates when it says that *California Novelties, Inc. v. Sokoloff* (1992) 6 Cal.App.4th 936, "rejected any hard and fast rule regarding the timing and content of post-complaint notice." (RB 51.) In that case, which was also a personal injury action governed by section 425.11, *no issue ever was raised* regarding the *form* of notice necessary under section 425.11. The parties' briefs reveal that the *only* issues raised concerned the *method of service* (mail or personal) and the *timing* of service (17 days before entry of default) of the notice. (See SRJN Exhs. 1-3.) On these issues, this Court merely said that "there is no hard and fast rule regarding the precise *method* or *timing* of the section 425.11 statement of damages." (6 Cal.App.4th p. 945, emphasis added.) *California Novelties* says nothing about the *form* of notice; it never suggests that anything less than statutorily-prescribed notice will do.

C. In Addition To Surgin's Failure To Satisfy The Jurisdictional Requirements For A Default Judgment, Its Purported "Actual Notice" Also Fails To Satisfy The Separate, Additional Minimum Requirements Of Due Process.

Surgin's failure to satisfy the jurisdictional statutory requirements of sections 580 and 585 alone renders the default judgment void to the extent it exceeds $270,000. But even if the Court could somehow overlook the absence of proper statutory notice, there was still no sufficient notice

here. Surgin's settlement-demand letters—the only other possible form of notice—fall far short of the threshold due process requirements that any notice must be formal, timely, and clear.

1. *Form.* Surgin opts to ignore controlling precedent establishing that "due process requires *formal* notice of potential liability" and that "[i]t is precisely when there is no trial . . . that *formal* notice, and therefore the requirement of section 425.10, becomes critical." (*Greenup, supra,* 42 Cal.3d at pp. 826-827, emphasis added; *Parish v. Peters* (1991) 1 Cal.App.4th 202, 207-210 [same]; *Pino, supra,* 15 Cal.App.4thSupp. at p. 5 [constructive notice insufficient; due process "require(s) *formal* notice of potential liability"; emphasis added, internal quotation marks omitted]; see also 1 Weil & Brown, Civil Procedure Before Trial (Rutter Group 1994) ¶ 5:105 at p. 5-25 [suggesting notice needs to be formal], cited with approval in *Wiley, supra,* 223 Cal.App.3d at pp. 1473-1474, fn. 3.) This means that settlement demands—which is exactly what Surgin's letters were—are insufficient as a matter of law. (*Debbie S., supra,* 16 Cal.App.4th at p. 199; *Morgan, supra,* 192 Cal.App.3d at p. 986 ["(t)he possibility the defendant could divine the amount of damages claimed through collateral sources does not satisfy due process"].)[15/]

2. *Timing.* Under due process, Truck was entitled to notice at a time when *Truck*, and not just the trial court, knew unequivocally that it could avoid the entry of its default by complying with discovery and knew exactly what it had to do to comply. That was not the context of the "notice" Surgin claims Truck received. (RB 51-53.) The first letter came *after* Surgin had renewed its motion for terminating sanctions and a bare six days before the trial court heard and granted that motion—at a time when the choice whether to enter Truck's default rested solely in the hands of the trial court. That was a time when, as far as Truck was aware, the trial court could have been in *agreement* with Truck's interpretation of the court's prior orders. After all, the court did *deny* Surgin's first terminating sanctions motion, and only expert tea-leaf reading (if that) would have then revealed to Truck the court's later-disclosed, non-obvious reading that its prior "denial" order was

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[15/] Once again, Surgin's reliance on *California Novelties* affords it no assistance. (RB 53-54.) As just demonstrated, the decision says nothing about the *content* of notice, but only concerns the *timing* and *method* of its service.

really a "clear flag" that Truck had one more chance to comply with discovery before terminating sanctions would be imposed.

The whole premise of *Greenup* is that the notice must be timed so as to "enable[] the defendant to exercise his right *to choose* . . . between (1) giving up his right to defend in exchange for the *certainty* that he cannot be held liable for more than a known amount, and (2) exercising his right to defend at the cost of exposing himself to greater liability." (42 Cal.3d at p. 829, emphasis added.) In short, due process requires that the *defendant* must receive notice at a time when *the defendant*, by its own unilateral act, may *with certainty* avoid entry of its default. But when Truck received Surgin's first letter, the court had not even informed Truck that it viewed its supplemental responses as deficient or that its "denial" order really meant that Truck was required to do something more or had "one more chance."

Even Surgin argues that "[c]ompliance just before or following sanctions *does not absolve* prior willful misconduct" and that terminating sanctions are still appropriate in such circumstances. (RB 15, emphasis added.) But by the time Surgin sent its first letter, it had already requested Truck's default, and its second letter was not even sent until *after* Truck's default had already been ordered. So, under Surgin's own argument, neither letter was sent in time to enable Truck to choose to "cease its [claimed discovery] abuse and avoid the sanction." (RB 48 fn. 50.)

3. *Clarity*. Surgin's own explanation of its letters underscores their vagueness. Surgin says that, in its first letter, "[t]he $62 million figure was the relevant one." (RB 52-53.) That's easy for Surgin to say now. But what did the letter mean when it was sent? It was hardly clear. It demanded settlement for $825,000; it also stated that Surgin "believed" that a *$2-3 million* jury award was "a conservative estimate given the recent award against Truck in the amount of $62 million in *Waller v. Truck Ins. Exchange*" (a decision that is *still* not final, yet was damningly used

against Truck at the trial level).[16] (JA 7581.) Surgin's belated second letter presented a similar jumble of escalating numbers and demands. (JA 6573.)

Surgin seems to argue that its reference to $62 million (and to various numbers in its post-sanctions second letter) permitted Truck to *infer* that Surgin *might* be seeking those amounts against it and, thus, somehow satisfied the due process requirements that entitle defendants to "know *exactly* what risk they assume by not responding to the pleading" (*Pino v. Campo*, *supra*, 15 Cal.App.4thSupp. 1, 5, internal quotation marks omitted]) and that preclude notice by inference or "speculation" (*Greenup*, *supra*, 42 Cal.3d at p. 829; see also *Becker*, *supra*, 27 Cal.3d at p. 494). However, inferences much more obvious and direct than those Surgin advances here have been held insufficient. (*Schwab*, *supra*, 53 Cal.3d at pp. 433-434 [disapproving cases holding that a defendant can infer that a complaint in superior court seeks at least the jurisdictional minimum]; *Debbie S.*, *supra*, 16 Cal.App.4th at pp. 199-200 [amounts stated in § 998 offers, and demanded or referenced in settlement negotiations insufficient]; *Morgan*, *supra*, 192 Cal.App.3d at pp. 986-987 [discovery responses do not provide notice of damages sought because they *might* be open to interpretation]; *Ludka v. Memory Magnetics International* (1972) 25 Cal.App.3d 316, 322-323 [allegation that plaintiff suffered damage "equal to the present market value of (2500) shares" of stock, less plaintiff's pleaded cost, was insufficient to support default judgment because amount claimed is open to speculation].)

For all these reasons, the portion of the judgment that exceeds $270,000 is void and must be stricken.

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[16] Even if it were true that the letter clearly threatened a $62 million recovery, it was not clear that Truck was the only, or even the most direct, object of the threat. When Surgin sent its letters, Farmers Insurance Exchange was still a defendant. (See JA 5698.) In *Waller*, punitive damages were awarded $6 million against Truck and $50 million against Farmers Insurance Exchange, not $62 million against Truck as inaccurately stated in Surgin's first letter. (*Waller v. Truck Insurance Exchange* (1994) 27 Cal.App.4th 674, 675, 684, rev. granted.)

II.

SURGIN'S PROOF OF UNPLEADED CLAIMS—AN ASSERTED PATTERN AND PRACTICE OF WRONGDOING IN OTHER CASES AND DISCOVERY ABUSE IN THIS AND OTHER CASES—REQUIRES REVERSAL OF THE DEFAULT JUDGMENT BECAUSE THESE CLAIMS FALL SUBSTANTIALLY OUTSIDE THE ULTIMATE FACTS PLEADED IN THE COMPLAINT.

On default, "the complaint delimits the nature of the legal theories which plaintiff may pursue and the nature of the evidence which is admissible." (*Ostling v. Loring* (1994) 27 Cal.App.4th 1731, 1744.) If the plaintiff departs from what is alleged *in the complaint*, "the trial court should hew to the complaint." (*Id.* at p. 1745.)

Far from hewing to the complaint, Surgin introduced, and the trial court relied upon, evidence totally outside the complaint's allegations: (1) An unalleged pattern and practice of supposed misconduct relating to insureds in other cases, involving different circumstances, and allegedly occurring at far distant times, and (2) unalleged purported discovery abuse in this and other cases. Surgin attempts to justify these departures by characterizing its proof as merely "evidentiary facts" that added "detail" to the allegations of its complaint. (RB 55.) But this wasn't "detail"—it was major reconstructive surgery. Surgin fails to identify a single ultimate fact alleged in the complaint that its supposed "evidentiary facts" support or "detail." No wonder: The complaint does not even hint, much less allege, that Truck acted wrongfully in any other case, that Truck engaged in a pattern or practice of acting wrongfully, or that Truck engaged in discovery abuse in this or any other case.[17]

Significantly, neither the trial court nor Surgin ever attempted to justify the size of the $57.2 million punitive award on the basis of the narrow ultimate facts Surgin's complaint alleged—i.e.,

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[17] The asserted discovery abuse in this case did not even occur until long after Surgin filed its complaint. (*Jackson v. Bank of America* (1986) 188 Cal.App.3d 375, 390 [default judgment cannot be premised on facts occurring after filing of complaint]; *Lee v. Bank of America* (1994) 27 Cal.App.4th 197 [complaint cannot "relate back" to facts taking place *after* its filing].) Surgin never sought to amend its complaint, as it could have, to expand the scope of its allegations.

how Truck handled the four Alcon lawsuits that comprised Surgin's claim. Quite the opposite: The trial court expressly based its punitive award on the broader unalleged grounds, including—contrary to what Surgin says (RB 58)—Truck's supposed discovery abuse and its pattern and practice of wrongdoing. (RT 322.) And, despite its disclaimers, Surgin still seeks to justify the punitive award on the broader grounds.[18]

This is impermissible. A default admits "nothing more than was alleged in the complaint." (*Williams v. Foss* (1924) 69 Cal.App. 705, 707; see *Vasey v. California Dance Co.* (1977) 70 Cal.App.3d 742, 749 ["the defendant who fails to answer admits only facts which are well-pleaded"].) Facts *not* pleaded in the complaint are not admitted. "[D]ifferent acts allegedly leading to the same injuries are not part of the same general set of facts [pleaded in the complaint] even though the two different acts may, in context, have been part of the same story." (*Lee v. Bank of America*, *supra*, 27 Cal.App.4th at p. 208; *Hicks v. Murray* (1872) 43 Cal. 515, 522 ["(e)vidence of facts . . . cannot make the case broader than it appears by allegation"].) In the case of "an exemplary damage claim [like any other type of claim], fairness demands that [the defendant] receive adequate notice of the *kind of conduct* charged against him." (*Smith v. Superior Court* (1992) 10 Cal.App.4th 1033, 1041 [emphasis added, internal quotation marks omitted, quoting *G.D. Searle & Co. v. Superior Court* (1975) 49 Cal.App.3d 22, 29].)[19]

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[18] Consider, for example, the following: RB 64 ["When a defendant engages in such conduct *as a practice*, this justifies a larger award," emphasis added], 65 ["Surgin also presented evidence of Truck's *pattern and practice* of similar bad faith in responding to other policyholders," including "Truck's policy of *discovery abuse*, "and "Truck's misconduct directed at plaintiffs in *Waller*," emphasis added] & fn. 71 ["Truck fails to cite any case holding that discovery abuse cannot be considered in connection with punitive damages. In fact, abusive litigation tactics properly support a bad faith claim"], 67 ["There was ample evidence of Truck's *pattern and practice* of attempting to avoid its obligations to all its policyholders—not just Surgin," (emphasis added)]. In the trial court, Surgin opposed Truck's post-judgment motions by relying heavily on unpleaded matters to support the punitive damage award. (See, e.g., JA 8063-64, 8070-71.)

[19] *Beeman v. Burling* (1990) 216 Cal.App.3d 1586 is not contrary, as Surgin claims. Surgin's own quotation from *Beeman* (RB 56) verifies, as we have urged, that a defaulted defendant may not be exposed "to any greater or different liability than was presented by the complaint on file." (*Id.* at p. 1595.) Truck falls precisely within the *Beeman* rule, having been exposed both to drastically "greater" and fundamentally "different" liability than alleged in Surgin's complaint.

Surgin argues that the unpleaded matters merely addressed the "measure" of punitive damages. (RB 58.) But that was not what the evidence was all about. The evidence did not answer the question, "How much should Truck be punished for doing what the complaint alleges?" It addressed a very different question: "What else did Truck do that it should be punished for?" The judgment did not punish Truck just for failing to defend Surgin's claims, the solitary subject of the complaint. The trial court specifically said it was punishing Truck for a pattern and practice of claims and discovery misbehavior ranging far beyond anything alleged in the complaint, including Truck's supposed "pattern and practice within the industry" and discovery conduct "through the litigation which terminated a few weeks ago." (RT 322.)

Surgin suggests that Truck suffered no prejudice from the error. (RB 59.) But a $57.8 million default judgment based on facts materially different from those pleaded speaks volumes of prejudice. Truck was tried and convicted *in absentia* on claims it had never previously heard and that its default did not admit, with no opportunity to challenge any of the evidence or have any of the claims decided by a jury. No prejudice? Hardly.

The pertinent question is not whether Surgin's presentation of a default case that it never pleaded mandates reversal. It undeniably does. (*Jackson*, *supra*, 188 Cal.App.3d at p. 390; see *Ostling*, *supra*, 27 Cal.App.4th at pp. 1744, 1746 [plaintiff's "allegation and proof must agree"; if the judgment is premised on facts beyond the scope of the complaint, it must be reversed].) The real question concerns only the proper scope of the reversal. Surgin suggests the case should merely be remanded for a new prove-up, citing *Ostling*, *supra*, 27 Cal.App.4th 1731. (RB 59.) Although Surgin argues that *Ostling* sought to limit *Jackson*, *supra* (RB 59, fn. 65), both decisions support opening the default here. Where a plaintiff (as in *Ostling*) merely introduces evidence of damages *premised upon the facts alleged in the complaint* but in excess of the *amount* pleaded in the complaint, there is no reason to open the default because striking the excessive damages affords a complete remedy for the error. But where, as here and in *Jackson*, the plaintiff offers a completely different *factual basis* for its claims than alleged in the complaint, the plaintiff has *de facto* amended the complaint and the default must be opened.

III.

THE JUDGMENT MUST BE REVERSED BECAUSE THE COMPLAINT FAILS TO STATE A VIABLE CAUSE OF ACTION FOR COMPENSATORY OR PUNITIVE DAMAGES.

This Court's *Watercloud* decision (now supported by a swelling chorus of decisions from other courts)[20] has eliminated any shadow of a claim that Truck owed Surgin any defense obligation under its policy. However, without a duty *rooted in the policy*, there can be no *tortious* breach of the implied covenant of good faith and fair dealing and, therefore, no punitive damages. But even if there were such a duty here, there is an independent reason why Surgin would still not be entitled to recover punitive damages: The complaint fails to allege any of the *facts* required by Civil Code section 3294(b) as a prerequisite to recovering punitive damages.

Surgin's footnote response to the latter point merely avoids the issue. Its response to the first point is to attempt to invent a cause of action based on Truck's highly conditional promise to defend, a promise completely outside the policy. Surgin's theory has been rejected every time a court has ever considered it; moreover, no *tort* or punitive damage claim can arise from a breach of a purely contractual obligation. And because Surgin could not reasonably or detrimentally have relied on the highly conditional promise, the complaint does not state any cause of action at all.

A. Truck's Policy Never Obligated It To Defend Any Of the Alcon Actions. Neither Speculation About Unalleged Facts Nor Past Legal Uncertainty About Policy Construction Can Change That Fact.

Surgin presents no viable argument that its *policy* required Truck to afford a defense to any of the four separate Alcon lawsuits. (RB 43-46.)[21]

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[20] *Aetna Casualty & Surety Co. v. Superior Court* (1993) 19 Cal.App.4th 320; see, e.g., *Microtech Research Inc. v. Nationwide Mutual Ins. Co.* (9th Cir. 1994) 35 F.3d 571, and cases cited at AOB 25.

[21] Surgin implies that Truck owed a duty to defend all the separately-filed Alcon actions if it owed a duty to defend any of them. (RB at 43-45.) This is wrong. While carriers typically (continued...)

1. *The Patent Infringement Actions.* Surgin has not cited a single authority that would establish that its policy *required* Truck to defend the three Alcon actions that alleged only patent infringement. (JA 150-151, 206-26, 231-38.) Surgin grudgingly concedes these claims are not covered under *Watercloud.* (RB 45.)[22] Nevertheless, it asks this Court to find potential coverage by speculating that, "given the commercial rivalry between Surgin and Alcon," Alcon *might* have been able *to amend* its patent infringement complaints to allege some unidentified other facts that *might* have triggered coverage. (RB 45.)

Whether a complaint triggers coverage depends on the *facts* alleged; an insured may not demand coverage based on facts the plaintiff has *not* alleged. This was established in *Gray v. Zurich Insurance Co.* (1966) 65 Cal.2d 263, 276-277, where our Supreme Court held that "[a]n insurer, therefore, bears a duty to defend its insured whenever it ascertains *facts* which give rise to the potential of liability under the policy." (Emphasis added.) Appellate courts repeatedly have held that *Gray* does *not* apply to theories that *might* give rise to liability under the policy premised on facts *not* pleaded in complaint. "The duty to defend depends on whether there is potential liability based on facts pled in complaint." (*McLaughlin v. National Union Fire Ins. Co.* 23 Cal.App.4th 1132, 1152; *Cutler-Orosi Unified School Dist. v. Tulare County School etc. Authority* (1995) 31 Cal.App.4th 617, 633 ["Assertions of potential coverage based entirely on speculation do not give rise to a duty to defend"]; *Hurley Construction Co. v. State Farm Fire & Casualty Co.* (1992) 10 Cal.App.4th 533, 538 [no potential for coverage or duty to defend where "(t)he extraneous 'facts' regarding potential liability came from (the insured's) counsel who speculated about how (the plaintiff) might amend its complaint at some future date. . . . (T)he insured may not speculate about unpled third party claims to manufacture coverage"]; *Coit Drapery Cleaners, Inc. v. Sequoia Ins.*

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[21](...continued)
defend both covered and noncovered claims *in the same action*, there is no requirement that a carrier defend a separate lawsuit that indisputably is noncovered. (*United Pacific Ins. Co. v. Hall* (1988) 199 Cal.App.3d 551 [carrier has no duty to defend separate noncovered juvenile action against insureds' son, even though outcome of that action might have substantive impact on potentially covered suit for damages against parents arising out of son's arson].)

[22] Surgin asserts that *Watercloud* "counsels" that these plainly noncovered claims "may not be covered." (RB 45.) They aren't covered, plain and simple. (AOB 24-25.)

Co. (1993) 14 Cal.App.4th 1595, 1604 [same]; *Olympic Club v. Underwriters at Lloyd's London* (9th Cir. 1993) 991 F.2d 497, 503 [insured cannot rely upon unpleaded facts to create coverage].

Surgin contends this Court should ignore its own *Watercloud* decision and evaluate coverage based on the uncertain state of the law at the time of Surgin's tender. (RB 43.) This is impermissible. Since the duty to defend depends exclusively on whether there is potential liability based on *facts* pled in the complaint or known to the insurer, there is no such duty "'where the only potential for liability turns on resolution of a legal question. . . .'" (*McLaughlin v. National Union Fire Ins. Co.*, *supra*, 23 Cal.App.4th at p. 1152; accord, *State Farm Mut. Auto. Ins. Co. v. Longden* (1987) 197 Cal.App.3d 226, 233.) Here, the question whether Truck's advertising liability coverage applied to patent infringement claims was a legal question that was conclusively resolved by *Watercloud.*

"[T]he fundamental rule of 'retrospective operation' . . . has governed 'judicial decisions . . . for near a thousand years.'" (*Harper v. Virginia Dept. of Taxation* (1993) ___ U.S. ___ [113 S.Ct. 2510, 2516-2517, 125 L.Ed.2d 74, 84, 86]; see *Newman v. Emerson Radio Corp.* (1989) 48 Cal.3d 973, 978.) This rule has been applied uniformly in defining the existence and scope of a carrier's duty to defend.[23] Clearly, *Watercloud* pronounced *existing* law. It therefore applies squarely to this case.

Recently, Division One of this Court expressly held, contrary to the very argument Surgin makes here, that "a subsequent judicial determination [that] an insurance company has no duty to defend or liability under a policy . . . retroactively relieve[s] an insurance company of its obligation to conduct in good faith a defense it has voluntarily accepted." Holding that the carrier was "entitled to retroactive relief" from having to pay fees that it really never owed, the court *rejected* an argument that "once [the carrier] voluntarily accepted the tender of . . . defense, it was obligated

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[23] E.g., *McLaughlin*, *supra*, 23 Cal.App.4th at pp. 1151-1152 [1994 decision relying on 1992 appellate decision holding no duty to defend claim tendered in 1980s]; *Watercloud*, *supra*, 19 Cal.App.4th at pp. 327-328 [relying on Supreme Court's 1992 *Bank of the West* decision in determining no duty to defend in 1988]; *Coit Drapery Cleaners, Inc. v. Sequoia Ins. Co.*, *supra*, 14 Cal.App.4th at pp. 1608-1609 [no duty to defend based on numerous cases decided after carrier's refusal to defend].

to pay all defense costs and its withholding or delaying payments to the attorneys constituted bad faith . . . ." (*Richardson v. State Farm Fire & Cas. Co.* (Feb. 3, 1995) 95 Daily Journal D.A.R. 1659, 1662.)

2. *The Counterclaim Action.* Burying almost its entire discussion of the Alcon counterclaim in two footnotes (RB 44, 45 fns. 45, 46), Surgin tries to create an illusion of coverage by playing with labels. It doesn't work.

a. The *only* factual premise of the counterclaim is that Surgin misrepresented governmental approval and other attributes of its *own product.* (JA 197-199.) That kind of claim does not fall within the policy's "advertising liability" coverage because it does not qualify as "unfair competition" or otherwise qualify under any other definition or component of "advertising liability." (JA 179.) Both *Bank of the West* and *Watercloud* expressly limit coverage for "unfair competition" claims to those involving "the act of *passing off* one's goods as those of another," a claim Alcon *never* made. (*Bank of the West v. Superior Court* (1992) 2 Cal.4th 1254, 1263; *Watercloud*, *supra*, 19 Cal.App.4th at p. 327.) As this Court held in *Watercloud*, an insured's touting of its own products (the only allegedly-covered accusation here) is "far from passing off its goods as those of" another. (*Id.* at p. 328; see JA 198-199.) None of the cases cited by Surgin is to the contrary. (RB 44-45.)[24]

b. *Bank of the West*, *supra*, 2 Cal.4th at p. 1272, expressly rejects Surgin's assertion that the counterclaim should be covered because it contains a count labeled "unfair competition." (RB 44 fn. 45.) The label changes nothing. The *only* claim of "unfair competition" Alcon pleaded was that Surgin made deceptive statements "in violation of section 17500, et seq. of the California Business and Professions Code, which acts constitute unfair competition within the meaning of sections 17200 through 17206 of the Business and Professions Code." (JA 200.) *This*

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[24] See, e.g., *New Hampshire Ins. Co. v. Foxfire, Inc.* (N.D. Cal. 1993) 820 F.Supp. 489, 495-496 [acknowledging that coverage for unfair competition requires "passing off"; complaint arguably alleged insured "passed off" his services as those of another]; *Keating v. National Union Fire Ins.* (9th Cir. 1993) 995 F.2d 154, 155 [expressly refraining from deciding whether there are further restrictions on definition of covered unfair competition since plaintiffs alleged no competitive injury].

is the precise theory Bank of the West expressly held is not covered: "The policy term 'unfair competition' does not refer to conduct that violates the Unfair Business Practices Act. ([Bus. & Prof. Code,] § 17200, et seq.)" (2 Cal.4th at p. 1272; see *id.* at p. 1260 & fn. 2 [Bus. & Prof. Code, § 17200 defines action as for "unfair competition"].)

c. Surgin also asserts that the counterclaim triggered potential coverage for intentional interference with contractual relations and might be amended to allege defamation. (RB 44-45.) Again, more labels with no substance.

(1) Truck's policy affords no separate coverage (outside of "unfair competition") for intentional interference with contract. (JA 179 ["Advertising Liability means: (1) Libel, slander or defamation; (2) Infringement of copyright or of title or of slogan; (3) Piracy or unfair competition or idea misappropriation under an implied contract; (4) Invasion of right of privacy; committed or alleged to have been committed in any advertisement, publicity article, broadcast or telecast and arising out of the named insured's advertising activities"; no mention is made of interference with contract]; see *Atlantic Mutual Ins. Co. v. Badger Medical Supply Co.* (Wis. App. Jan. 19, 1995) 1995 Wis.App. LEXIS 50 [no advertising injury coverage for interference with contract if the facts alleged do not fall within one of the defined terms of such coverage].) Since the *facts* alleged in the *Alcon* actions do not qualify as unfair competition under *Bank of the West* and *Watercloud*, putting an "intentional interference with contract" label on them adds nothing.

Neither of the authorities cited by Surgin supports its position. (RB 45.) In *CNA Casualty of California v. Seaboard Surety Co.* (1986) 176 Cal.App.3d 598, the court held the complaint's "specific *factual* allegations" established potential claims of unfair competition and defamation (176 Cal.App.3d at p. 612, emphasis added); there, the *factual* allegations were that the insured stole trade secrets and made false representations about the property *of others*. Likewise, in *Foxfire, Inc.*, *supra*, 820 F.Supp. 489, the district court held the *facts* alleged (albeit under the rubric of interference with contract) potentially fell within the coverage for unfair competition where the *facts* pleaded were that the insured had *passed off his services as those of the plaintiff*. (*Id.* at pp. 495-496.) Both cases involve an asserted misappropriation of *others'* rights, *not* the mis-touting of one's own product, as alleged here.

(2) While Surgin's advertising liability coverage encompasses defamation, that coverage was not triggered here because the counterclaim does not allege a single fact that could potentially support such a claim. The counterclaim only describes Surgin's statements about its *own* product; there is no suggestion that Surgin ever maligned Alcon or its product. (*Nichols v. Great American Ins. Companies* (1985) 169 Cal.App.3d 766, 774 ["The (underlying) complaint contains no suggestion of the defamatory meaning that (the insureds) seek to infer. . . . (The insureds) cannot insert an essential allegation where none appears"].) As the Ninth Circuit cogently observed, advertising-injury coverage "plainly" does not apply to "misrepresentation, negligent or otherwise, of the unique attributes of *one's own products*." (*Standard Fire Ins. Co. v. Peoples Church of Fresno* (9th Cir. 1993) 985 F.2d 446, 450, emphasis added, footnote omitted.)

d. It is difficult to understand how Surgin can seriously maintain (RB 45 fn. 46) that Alcon's claim for "false, deceptive and misleading advertising" falls anywhere but squarely within the policy's exclusion for "incorrect description of any article or commodity" that occurs "with respect to advertising activities." (JA 182; see *New Hampshire Ins. Co. v. Power-O-Peat, Inc.* (8th Cir. 1990) 907 F.2d 58, 59.) Surgin seems to suggest that a facially-applicable exclusion somehow does not negate the duty to defend even though it negates the duty to indemnify. (RB 45 fn. 46.) Surgin is wrong. If the exclusion applies, there is no potential for coverage and therefore *no* duty to defend. (E.g., *Smyth v. USAA Property & Casualty Ins. Co.* (1992) 5 Cal.App.4th 1470; *Fire Ins. Exchange v. Jiminez* (1986) 184 Cal.App.3d 437; *State Farm Fire & Cas. Co. v. Geary* (N.D. Cal. 1987) 699 F.Supp. 756, 760-761.)

B. <u>There Can Be No Punitive Damage Recovery Here Because The Complaint Does Not Allege Facts Sufficient To Satisfy The Requirements Of Civil Code Section 3294. Since These Unalleged Facts Are Not Deemed Admitted For Purposes of Default, The Punitive Damage Portion Of the Judgment Must Be Vacated</u>.

The complaint's failure to plead facts sufficient to satisfy the requirements of Civil Code section 3294 is alone sufficient to void the $57.2 million punitive part of the judgment. (See AOB 27-28; *Cyrus*, *supra*, 65 Cal.App.3d at pp. 316-317 [striking punitive award because complaint

failed to allege requisite state of mind].) Surgin has utterly failed to respond to this point. (RB 46 fn. 47.)

1. Conclusory Allegations That A Corporate Entity Acted Maliciously—Unaccompanied By Essential Factual Allegations Of Malicious Conduct By An Officer, Director, Or Managing Agent—Are Insufficient To Satisfy The Explicit Requirements Of Civil Code Section 3294(b).

Surgin asserts it sufficiently pleaded a claim for punitive damages against Truck by generally alleging that Truck acted maliciously and with bad intent. (RB 46 fn. 47.) The Civil Liability Reform Act of 1987 specifically proscribes exactly this kind of pleading.

Although corporate employers can certainly act through employees and agents and be held vicariously liable for *compensatory* damages, they can only be held liable for *punitive* damages if their employees' conduct is authorized or ratified by *an officer, director, or managing agent.* (Civ. Code, § 3294(b).) Surgin's complaint contains no such factual allegation. This omission is fatal in the default judgment context because Truck's default admits *only* the facts Surgin alleged. (*Williams v. Foss, supra,* 69 Cal.App. at pp. 707-708.) The absence of crucial factual allegations—required by Civil Code section 3294(b) as a condition precedent to imposing punitive damages against Truck—requires reversal of that award.

In *Grieves v. Superior Court* (1984) 157 Cal.App.3d 159, 167-168, this Court directly rejected the exact argument Surgin has advanced here, squarely holding that a claim for punitive damages against a corporate defendant had to be stricken because "absent from the complaint is any assertion that an officer, director or managing agent of [the defendant] was *personally responsible* for any of the acts allegedly performed by [the defendant]." (Emphasis added; see also *College Hospital, supra,* 8 Cal.4th at pp. 725-726 [punitive damages not proper against corporation where officer only *might* have known about employee's wrongdoing]; *Hart v. National Mortgage & Land Co.* (1987) 189 Cal.App.3d 1420, 1432-1433 [punitive damages not properly pleaded where complaint did not allege action taken, ratified or approved by officer, director or managing agent]; *Fisher v. San Pedro Peninsula Hospital* (1989) 214 Cal.App.3d 590 [same]; cf. *Monge v. Superior*

Court (1986) 176 Cal.App.3d 503 [complaint sufficient where it alleged that tortious actions were undertaken and ratified by specifically-named corporate officers].)

Surgin's effort to plug this gaping hole in its punitive damage recovery falls hopelessly short of the mark:

a. Surgin claims the defect is cured because the complaint summarily alleges malice. (RB 46 fn. 47.) This is entirely beside the point. Truck's argument is not that the complaint fails to allege malice, but rather that it does not allege malice *by an officer, director or managing agent.* Under Civil Code section 3294(b), generic malicious intent is not enough to permit imposition of punitive damages against Truck.

b. Surgin next relies on *Egan v. Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d 809, 823, asserting that Truck should be liable for punitive damages because one of its employees, Mr. De Rivera, inferentially "managed the relationship" between Truck and Surgin. (RB 46 fn. 47.) There are two equally fatal defects with this argument:

(1) Mr. De Rivera's supposed management responsibility is not pleaded in the complaint and, therefore, Truck is not deemed to have admitted it for purposes of default. Indeed, Mr. De Rivera is not even mentioned in the charging allegations of the complaint either by name, title or other identification.[25/]

(2) In enacting Civil Code section 3294(b), the Legislature directly responded to *Egan*, rejecting *Egan's* effort to impose punitive damage liability for the acts of any corporate employee regardless of management responsibility. (See *College Hospital, supra*, 8 Cal.4th at pp. 712-713; *Palos Verdes Faculty Assn. v. Palos Verdes Peninsula Unified Sch. Dist.* (1978) 21 Cal.3d

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[25/] The complaint's sole reference to Mr. De Rivera is oblique, incorporating by reference a letter Mr. De Rivera signed agreeing to defend Surgin under a reservation of rights. (JA 247-252 [complaint Exhibit I].) That letter was hardly an act of bad faith. But even if it were, there is *no* allegation or suggestion that Mr. De Rivera was an officer, director or managing agent of Truck or that he even had general or final authority to handle or manage Surgin's claims. (Cf. JA 4616-4617, 4646-4654 [De Rivera reporting to *his* superior]; *Egan, supra*, 24 Cal.3d at p. 823 [only a person with *ultimate* supervisorial and policymaking decision acts in a managerial capacity].) Moreover, there is *no* allegation or suggestion that Mr. De Rivera acted in bad faith or maliciously in sending the reservation of rights letter, or that he ever possessed any particular state of mind or knowledge.

650, 659 [Legislature's enactment or amendment of statute immediately after recent judicial decision indicates intent to change the law].) The Legislature specifically rejected the broad "managerial capacity" language of *Egan* and adopted the more limited term "managing agent."[26] The Legislature then paired the term "managing agent" with the terms "officer" and "director," thus requiring that the person in question possess general powers and responsibilities of corporate management comparable to those of an officer or director. (See *Peralta Community College Dist. v. Fair Employment & Housing Com.* (1990) 52 Cal.3d 40, 50 [the doctrine of "ejusdem generis" requires that the definition of persons in a list be construed to be similar to the others listed].)[27] Here, the complaint never mentioned Mr. De Rivera or alleged that he had any general or specific managerial authority—either as a managing agent or in a managerial capacity—over Truck's affairs.

Since Surgin's complaint failed to satisfy the requirements of Civil Code section 3294(b), the default judgment for punitive damages must be reversed.

2. Civil Code Section 3294(c) Requires Despicable Conduct For An Award Of Punitive Damages; Surgin Furnishes No Justification For Its Failure To Satisfy This Essential Element.

In a footnote argument, Surgin contends that it alleged malice, and that is enough. (RB 46 fn. 47.) It is not.

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[26] Sen. Bill No. 1989 (1979-1980 Reg. Sess.) as passed by Senate on May 14, 1980 [original bill limited to "senior executive officer or officers"] (SRJN Exh. 11 p. 3); *id.* passed by Assembly on July 9, 1980 ["agent . . . employed in a managerial capacity] (SRJN Exh. 12 p. 3); Sen. Final Hist. (1979-1980 Reg. Sess.) p. 1135 [Senate refused to accept Assembly version] (SRJN Exh. 10 p. 2); Sen. Bill No. 1989 (1979-1980 Reg. Sess.) as passed by Assembly on August 27, 1980, and by Senate on August 31, 1980 [conference version and final bill limited to "officer, director or managing agent"] (SRJN Exh. 13 p. 3).

[27] In other contexts, the Legislature has used the term "managing agent" to refer to a person with general powers of management over the whole or a significant portion of a business. (E.g., § 531; Penal Code, §§ 1392, 1427; see R. Prof. Responsibility 2-100(B) [distinguishing between officers, directors, and managing agents, on the one hand, and employees whose acts bind the corporation on a particular occasion or in a limited realm, on the other hand].)

In the absence of an intent to injure or defraud (neither alleged here), Civil Code section 3294(c) requires that the defendant's *conduct* be "despicable" as a prerequisite to recovery of punitive damages.[28] (*College Hospital, supra*, 8 Cal.4th at p. 725 ["The additional component of 'despicable conduct' must be found"].)

In our opening brief, we demonstrated that Truck's failure to pay a claim it did not owe—i.e., reaching the right result, even if for the wrong reason or through the wrong process—cannot possibly qualify as "despicable." (AOB 28 & fn. 9.) Surgin has no response. Surgin's latest theory—that Truck failed to perform an entirely gratuitous "promise"—proves our point. The mere failure to perform a promise entirely outside the terms of an insurance policy is not even tortious, let alone despicable. (*Foley v. Interactive Data Corp.* (1988) 47 Cal.3d 654.) And, since any such promise necessarily arises out of contract, it cannot support a punitive damage award. (Civ. Code, § 3294(a) [punitive damages available only in "an action for the breach of an obligation not arising from contract"].) Nor can it be despicable where, as here, the defendant specifically warned the plaintiff, through a detailed reservation of rights, that it may owe no obligation at all.

C. Surgin Has No Cause Of Action—And Certainly No Tort Cause of Action—Based Solely On Truck's Bare Agreement To Defend, Accompanied by a Reservation of Rights To Contest Any Duty To Defend And To Recoup Defense Fees.

As we have shown, the theory expressly pleaded in the complaint—that Surgin's *policy* obligated Truck to defend each of the Alcon actions—is not viable. Shifting gears on appeal, Surgin now suggests an alternate theory of liability. It asserts that despite the lack of any *duty* to defend under the *policy*, the complaint might state a claim because Truck promised to defend Surgin and

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[28] In relevant part, Civil Code section 3294 provides: "(c) As used in this section, the following definitions shall apply: (1) 'Malice' means conduct which is intended by the defendant to cause injury to the plaintiff or *despicable conduct* which is carried on by the defendant with a willful conscious disregard of the rights or safety of others. (2) 'Oppression' means *despicable conduct* that subjects a person to cruel and unjust hardship in conscious disregard of that person's rights." (Emphasis added.)

failed to perform its promise. (RB 39-41.) Even if this could support some kind of claim, it cannot support Surgin's claim for *tortious* breach of the covenant of good faith and fair dealing—the only basis on which Surgin could recover punitive damages and *Brandt* fees. In fact, in the absence of *reasonable* reliance by Surgin—which is here negated on the face of the complaint—*no* authority supports *any* recovery by Surgin under its breach of promise theory.

1. There Can Be No Claim Against Truck For Tortious Breach Of The Implied Covenant Of Good Faith And Fair Dealing For Failing To Pay Defense Fees That Its Policy Did Not Obligate It To Pay.

Completely absent from this case is the quintessential element of a claim for tortious breach of the implied covenant of good faith and fair dealing: the existence and denial of some benefit actually owing under the policy. Without a duty owed under the insuring agreement, there can be no tort. "The terms and conditions of the policy define the duties and performance to which the insured is entitled." (*Western Polymer Technology, Inc. v. Reliance Ins. Co.* (1995) 32 Cal.App.4th 14, 15.) Obligations stemming from the implied covenant of good faith and fair dealing "depend on the existence of the contractual duty to pay. . . . [T]he obligation of good faith conduct does not exist independent of an express contractual obligation . . . ." (*Tomaselli v. Transamerica Ins. Co.* (1994) 25 Cal.App.4th 1766, 1770, fn. 4, 1771-1772; AOB 26-27.)

Consistent with these views, our Supreme Court in *Foley v. Interactive Data Corp., supra,* emphatically rejected the notion that the implied covenant is some abstract engine of social justice divorced from the obligations owed under the parties' agreement:

> "The covenant of good faith is read into contracts in order to protect the *express covenants or promises* of the contract, *not* to protect some general public policy interest not directly tied to the contract's purpose." (47 Cal.3d at p. 690, emphasis added.)

For these reasons, "an insured may not recover bad faith damages for an insurance company's delay relating to benefits which are not otherwise due under the policy." (*Richardson*

v. State Farm Fire & Cas. Co., *supra*, 95 Daily Journal D.A.R. at p. 1662.) Since no benefits were due under Truck's policy, whatever else Surgin's theory might be, it cannot be one for tortious breach of the covenant of good faith and fair dealing, which is the only theory on which punitive damages and *Brandt* fees could have been awarded. (See Civ. Code, § 3294(a); Code Civ. Proc., § 1021 [attorney's fees only awardable if provided by contract]; *Brandt*, *supra*, 37 Cal.3d at p. 817 ["When an insurer's *tortious* conduct reasonably compels the insured to retain an attorney to obtain the benefits *due* under a policy, it follows that the insurer should be liable in a tort action for that expense," emphasis added].)

2. Decisional Law Refutes Surgin's Argument That, In The Absence Of A Duty To Defend, A Carrier Is Liable Merely For Agreeing To Defend.

a. Surgin contends an insurer is liable for bad faith if it fails to pay defense fees once having agreed to pay such fees. (RB 39, 41.) The case law is contrary:

- In *Richardson v. State Farm Fire & Cas. Co.*, *supra*, 95 Daily Journal D.A.R. at p. 1662-1663, Division One of this Court rejected an insured's bad faith cause of action premised, as here, on a carrier's failure to honor its promise to pay certain defense fees incurred by the insured's counsel. There, after the carrier agreed to defend its insured, it failed to pay a portion of defense fees incurred and delayed in paying other fees. Since the carrier owed no duty to defend in the first place and had reserved its right to seek reimbursement of fees, the Court of Appeal held the carrier's refusal to pay as agreed was irrelevant.

- *State Farm Fire & Cas. Co. v. Geary* (N.D. Cal. 1987) 699 F.Supp. 756 directly rejects Surgin's precise claim that a carrier's *agreement* to defend, but refusal to provide *Cumis* counsel, may constitute bad faith even though the policy creates no duty to defend. Surgin attempts to distinguish *Geary* on the mistaken ground that the carrier there only had refused to defend under one policy, but not under another. (RB 41 fn. 42.) Not so. The court held the carrier had "no potential for coverage under *either* the homeowner's or personal liability policies, [and] . . . *[a]s a result*, it is not necessary to determine whether *Cumis* counsel was wrongfully *withdrawn*." (699

F.Supp. at pp. 761-762, emphasis added].) Contrary to Surgin's purported distinction, *Geary* involves a claimed failure to defend under *both* policies and an *actual refusal* to pay *Cumis* counsel.

- *California Union Ins. Co. v. Club Aquarius, Inc.* (1980) 113 Cal.App.3d 243 also categorically refutes Surgin's contention that, by agreeing to defend, a carrier "assume[s] an obligation to defend broader than the policy required." (*Id.* at p. 247.) There, the court held that, even though the carrier had promised to defend the "entire action," it was still *not* obligated to pay any defense fees indisputably attributable to noncovered claims. (*Id.* at pp. 247-248.) Significantly, *Club Aquarius* rejected an "agreement to defend" cause of action even though the carrier had *not* reserved its right to deny a duty to defend, to recoup defense fees, or to withdraw from the defense. Our case is much stronger because here Truck expressly reserved these rights.

b. None of the cases relied on by Surgin is to the contrary (see RB at 39):

(1) Two of Surgin's authorities (*McMillin Scripps North Partnership v. Royal Ins. Co.* (1993) 19 Cal.App.4th 1215, 1222; *Murray v. State Farm Fire & Casualty Co.* (1990) 219 Cal.App.3d 58, 65-66) support Truck, not Surgin. Each held that *the insured had no cause of action* for breach of the implied covenant *where no policy benefits were due.* (*McMillin, supra*, 19 Cal.App.4th at p. 1222 [no cause of action for breach of implied covenant for failure to investigate because there was no policy coverage]; *Murray, supra*, 219 Cal.App.3d at p. 66 [carrier not liable where it reached correct result even if its investigation was inadequate].)[29]

(2) The final case—the putative linchpin of Surgin's theory—is *Travelers Ins. Co. v. Lesher, supra*, 187 Cal.App.3d 169. *Lesher* does not even begin to stand for what Surgin claims.

According to Surgin, the *Lesher* court "*concurred with the insured* that once Travelers had agreed to defend, it 'was obligated to conduct that defense with the same duty of care as if there were no coverage dispute.'" (RB 39-40, emphasis added [purporting to quote *Lesher's* holding, 187

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[29] Surgin relies on *dicta* in each case suggesting that in "unusual" circumstances—nowhere comprehensively defined in either opinion—there *might* be a claim for breach of the implied covenant even though there is no obligation to pay policy benefits. The only hypothesized *potential* examples, however, have nothing to do with the present facts. (*McMillin, supra* 19 Cal.App.4th at p. 1222 [first party insurer hides critical facts from insured after inducing insured to rely solely on carrier's investigation]; *Murray, supra*, 219 Cal.App.3d at p. 66, fn. 5 [undefined "collateral" harm caused by insurer's delay in handling claim].)

Cal.App.3d at p. 187].) *No way.* The quoted language merely summarized the insured's *contention*. Far from "concurring," the court merely noted that Travelers *did not dispute* the point:

> "Neither party has cited any case in which liability has been imposed on an insurer under similar facts. Nevertheless, *Travelers does not contend that an insured has no cause of action under such circumstances.*" (*Id.* at p. 187, emphasis added.)

Since the precise point for which Surgin cites *Lesher was not in issue and was not decided*, that case is irrelevant. Moreover, *Lesher* arose from a unique factual situation not at all comparable to that here and presented only narrow appellate issues completely unrelated to whether a cause of action had been stated.[30/]

3. Even On Its Own Terms, Surgin's "Breach Of Promise" Theory Cannot Support Either The Compensatory Or Punitive Damages Awarded.

The essential premise of Surgin's theory is this: In reliance on Truck's agreement to defend, Surgin necessarily incurred defense costs. This does not support the damages Surgin seeks.

First, by its own evidence, Surgin incurred a significant portion, and maybe even most, of its asserted defense fees *before* the earliest possible date of any agreement to defend—indeed, before Surgin even tendered its claim. (JA 151 [Surgin first tendered three of the Alcon actions on March

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[30/] *Lesher's* holding was limited to the propriety of a jury instruction concerning the availability of a *statutory* cause of action under Insurance Code section 790.03 (187 Cal.App.3d at pp. 187-191), a cause of action repudiated in *Moradi-Shalal v. Fireman's Fund Ins. Companies* (1988) 46 Cal.3d 287, 304, and not asserted in this case. The core facts in *Lesher* were that the insured had *relied on counsel selected by the carrier* as its sole counsel, that the carrier had created a conflict of interest that required that counsel withdraw (for reasons unrelated to payment of fees), and that the carrier left the insured without counsel on the eve of trial, thus placing the insured in a worse position than if the carrier had never defended at all. (See *Richardson*, *supra*, 95 Daily Journal D.A.R. at p. 1662 ["*Lesher* involved actions by the insurance company which prejudiced the insured's defense"].) By sharp contrast, here Surgin was *always* represented by counsel of its own choosing, expressly refusing counsel proffered by Truck. (JA 155.) It could not have been placed in a worse position by Truck's failure to pay fees it never owed. (*Club Aquarius*, *supra*, 113 Cal.App.3d at pp. 248-249 [where the insured is defended by counsel of its own choosing, it is left in no worse position by having to pay such counsel itself in circumstances where the carrier owes no further obligation to defend].)

3, 1990, and the fourth Alcon action on April 25, 1990]; JA 152, 245-246 [Truck first suggested it might consider defending on May 2, 1990]; JA 152-153 [Truck agreed to defend Surgin, subject to the right to seek reimbursement of defense fees, on August 7, 1990]; JA 5918-5921, 5931-5942, 5946-5947, 5951-5954 [fees incurred well before Truck gave any indication that it might defend Surgin].) In incurring these fees, Surgin could not possibly have relied on an "agreement" that did not then even exist. (Compare JA 151.)

Second, Surgin could not *reasonably* have relied on the agreement as an unqualified commitment to pay defense fees because Truck specifically reserved its rights, including its right to recoup defense fees in the event there was no coverage. (*State Farm Fire & Casualty Co. v. Jioras* (1994) 24 Cal.App.4th 1619, 1626 [an insured can neither reasonably nor detrimentally rely on defense by carrier where carrier reserved its right on the issue in controversy]; *McLaughlin v. National Union Fire Ins. Co., supra,* 23 Cal.App.4th at pp. 1148-1149 [where carrier continues to dispute coverage, insured cannot justifiably rely on carrier's position]; *Richardson, supra,* 95 Daily Journal D.A.R. at pp. 1662-1663 [where carrier reserves right to seek reimbursement and it turns out there is no coverage, insured is not even entitled to use of money between time carrier might have paid and time carrier would have sought reimbursement].)

Third, a breach of promise, without more, cannot give rise to punitive damages. (Civ. Code, § 3294(a) [punitive damages may be recovered only "(i)n an action for breach of an obligation *not* arising from contract," emphasis added].) It also does not permit recovery of *Brandt* fees. (§ 1021 [no attorney's fees absent statute or agreement].)

D. Truck Has Never Admitted, Judicially Or Otherwise, That It Owed Defense Fees To Surgin .

By choosing to seek a default judgment, Surgin limited itself to the allegations of its complaint. The complaint, however, fails to state a viable cause of action. Now, Surgin attempts to persuade the Court to look beyond the complaint (and thus beyond the limited facts deemed admitted by Truck's default) to supposed "admissions" by Truck that it had a duty to pay Surgin's defense fees. (RB 41-42.) Surgin's position is unfounded.

First, on default, Surgin cannot supplement or expand the complaint's allegations by a different evidentiary presentation, including a claimed admission (judicial or otherwise) outside the complaint. (See Section II, *supra*, AOB 21-22.)

Second, the complaint expressly alleges that Truck repeatedly communicated to Surgin its doubt about the existence of any duty to defend and the conditional nature of any agreement to pay defense fees. (See RB 42; JA 152 [complaint alleges that Truck's initial response to tender included that "*if Farmers (Truck) later determined that there was coverage* under the Primary or Umbrella Policy that Farmers (Truck) would reimburse (Surgin's counsel)," emphasis added], 153 [complaint alleges that "In connection with Farmers' (i.e., Truck's) agreement to pay Surgin's costs of defense in the Alcon actions, Farmers (Truck) sent Surgin a letter wherein it reserved its rights: . . . [¶] d. To seek reimbursement of all sums paid on behalf of Surgin"].)

Third, there was no judicial admission. The claimed judicial admission supposedly arose in Truck's opposition to Surgin's motion for summary adjudication. In its memorandum, Truck argued that, although "there are substantial reasons why it may not have had a duty to defend," no purpose would be served by adjudicating the duty because Truck had agreed to defend. (JA 735, see also JA 732-733, 785-786.) Surgin contends Truck thereby *judicially admitted* that the *legal implication* of its conditional agreement to defend was that it owed an *obligation* to defend. Not so. Even if admissions that occur after the filing of a complaint could somehow be used to buttress a deficient default judgment (they can't), it is clear that legal arguments and conclusions are not judicial admissions. (E.g., *Do It Urself Moving & Storage, Inc. v. Brown, Leifer, Slatkin & Berns* (1992) 7 Cal.App.4th 27, 37 [an "unsworn statement made as part of the points and authorities supporting a motion" does not constitute "a judicial admission"]; *Osbourne v. Security Ins. Co.* (1957) 155 Cal.App.2d 201, 212 [court had to ascertain insurance coverage "independent() of any concessions of counsel as to the legal effect of the policy"]; *Valdez v. Taylor Automobile Co.* (1954)

129 Cal.App.2d 810, 821 [stipulation regarding policy limits not binding as one of law].) Numerous cases are in accord.[31/]

Fourth, at the time Truck's counsel advanced this argument, even Surgin did not assert it was an admission; indeed, it asserted just the opposite. In response to Truck's counsel's statements, Surgin argued that "Truck stubbornly refuses to concede this point [i.e., that there was a duty to defend]." (JA 803). Truck has never wavered from its position that it owed *no duty* to defend or to pay any amount of defense fees. (JA 755-756, 785-786; see JA 846-847; SRJN Exh. 4 p. 8.)

IV.

THE COMPENSATORY DAMAGE AWARD IS UNSUPPORTED BY SUBSTANTIAL EVIDENCE AND IS EXCESSIVE AS A MATTER OF LAW.

Surgin attempts to camouflage the *legal* insufficiency of its compensatory damage evidence by asserting that this is just a substantial evidence case and should essentially be given rubber-stamp approval. (RB 60.) Significantly, Surgin refuses to discuss the evidence. Surgin's wishful thinking notwithstanding, "[t]he Court of Appeal 'was not created . . . merely to echo the determinations of the trial court.'" (*Kuhn v. Department of General Services* (1994) 22 Cal.App.4th 1627, 1633.)

Even the case on which Surgin primarily relies (*Uva v. Evans*, *supra*, 83 Cal.App.3d 356) resoundingly refutes Surgin's position. Far from giving rubber-stamped approval, the appellate court in *Uva* reversed a $30,000 default judgment in a dog bite case because it resulted in a "gross

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[31/] See, e.g., *Swift & Co. v. Hocking Valley Ry. Co.* (1917) 243 U.S. 281, 289 [37 S.Ct. 287, 289-290, 61 L.Ed. 722, Brandeis, J.] ["If the stipulation is to be treated as an agreement concerning the legal effect of admitted facts, it is obviously inoperative, since the court cannot be controlled by agreement of counsel on a subsidiary question of law"]; *Desny v. Wilder* (1956) 46 Cal.2d 715, 729 ["(t)his court . . . is not bound to accept concessions of parties as establishing the law applicable to a case"]; *Adelstein v. Greenberg* (1926) 77 Cal.App. 548, 552 ["statement of counsel . . . during the course of the argument . . . is unimportant, being merely the statement of a legal conclusion, and even if it could be regarded as a matter of fact, was not binding . . . because it was not made during the trial of the action on the merits as an admission or stipulation of fact"]; *In Re Applin* (Bankr. E.D. Cal. 1989) 108 Bankr.R. 253, 258-259 [argumentative assertions in briefs are not judicial admissions].

injustice." (83 Cal.App.3d at p. 364.) It did so even though the judgment was entered by a respected trial jurist who later served with distinction on the Court of Appeal. Concluding that the judgment was so "grossly disproportionate as to be without evidentiary support and shocking to the conscience," Justice Kaus declared:

> "The requirement of proof of damages [on default] is meaningless if it can be fulfilled by *any* evidence . . . . We know of no statutory or constitutional barrier which requires an appellate court to ignore gross injustice in the award of damages simply because the judgment was procured by way of default." (*Id.* at pp. 364-365, emphasis in original.)

Here, exactly as in *Uva*, the compensatory damage award must be reversed. It is utterly without evidentiary justification.

1. The Award Of *Brandt* Fees Is Unsupported By Substantial Evidence.

Surgin argues the substantial evidence rule requires acceptance of isolated *ipse dixit*, conclusory statements that all of Surgin's attorney's fees were incurred solely in pursuit of policy benefits even though the hard evidence—*the actual attorney's bills* to which the testimony referred—incontrovertibly establish the contrary. (RB 61.)[32/]

[32/] The *entirety* of the evidence relied on by Surgin is as follows: (1) "These fees, of Callahan & Gauntlett, they were incurred to assist Surgin in obtaining the benefits it was due under its insurance policies with Truck" (RT 295 [Maskamp testimony, cited at RB 61]); and (2) "All of the costs and fees charged by Callahan & Gauntlett *as detailed in the Surgin billings* are directly attributable to Callahan & Gauntlett's efforts to obtain the rejected benefits due to Surgin under its policies of insurance issued by Truck" (RT 244-245 [Gauntlett testimony, cited at RB 61, emphasis added]).

There is also a declaration of Lloyd Stamp, Surgin's coverage counsel, pertaining to his fees of $4,916, which comprised only 1.6% of the total claim for *Brandt* fees. (RT 109-124, cited at AOB 32 and RB 61.) However, the few portions of Mr. Stamp's declaration that actually describe his activities concern work *predating* any possible refusal by Truck to pay policy benefits. (See, e.g., RT 112, 119, 123-124 [Stamp sent letters to Truck on July 10, July 24, and October 23, 1990; October 23, 1990, letter claimed, for the first time, that Truck was failing to live up to promise to pay Surgin's defense fees].) *Brandt* does not authorize recovery

(continued...)

The most telling feature of Surgin's argument is its *complete failure even to mention* the details of the "Surgin billings" to which the conclusory statements refer. The billings, however, categorically disprove the conclusory testimony. (See AOB 32 & fn. 10.) They reveal that substantial fees were incurred for pursuing Surgin's *tort* claims (e.g., to establish insurance bad faith and compensatory and punitive damages flowing from the claimed bad faith) or were incurred before Truck supposedly denied policy benefits. *Brandt* expressly precludes an award of such fees. (See AOB 31-33 & fn. 10; *Brandt, supra,* 37 Cal.3d at pp. 817-819.)

The witnesses' unsupported conclusions about what the billing statements disclosed cannot constitute substantial evidence where the billing statements themselves *refute* those conclusions. (See, e.g., *Fullerton Union High School Dist. v. Riles* (1983) 139 Cal.App.3d 369, 383 ["a trier of fact may not indulge in inferences rebutted by clear, positive and uncontradicted evidence"].)

Garcia v. Hyster Co. (1994) 28 Cal.App.4th 724, is directly on point. There, exactly as here, the trial court awarded every dollar requested on the basis of an attorney's conclusory declaration that all fees were attributable solely to certain matters. The Court of Appeal reversed because, exactly as here, the attached bills *contradicted* the attorney's naked assertion: "Nothing in the bare-bones showing made below, or in the lower court's award, reflects that any consideration was given to the fact that [the prevailing party's] trial preparation might extend beyond those areas" for which fees could legitimately be awarded. (*Id.* at p. 737.) Numerous cases echo *Garcia.*[33]

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[32](...continued)
of such fees. (See AOB 32-33.) But, in any event, $4,916 is a far cry from the $302,000 *Brandt* award in this case.

[33] See, e.g., *Banco Do Brasil, S.A. v. Latian, Inc.* (1991) 234 Cal.App.3d 973, 1012-1016 [reversing judgment for lack of substantial evidence because plaintiff's broad, conclusory testimony "defies belief" in light of the undisputed more specific facts]; *Foggy v. Ralph F. Clark & Associates, Inc.* (1987) 192 Cal.App.3d 1204, 1214-1215 [affirming JNOV for defendant because testimony as to value of property by real estate agent on behalf of plaintiff inherently incredible, and thus not substantial, in light of more specific testimony by defendant's expert]; *Crawford v. Continental Cas. Co.* (1968) 261 Cal.App.2d 98 [reversing judgment for lack of substantial evidence where plaintiff's testimony about interlineations on insurance policy inherently improbable in light of the document itself]; *Newhart v. Pierce* (1967) 254 Cal.App.2d 783, 788-792 [reversing judgment for lack of substantial evidence to support damages where owner's estimate of ranch's value not borne out by method of calculation he admitted was
(continued...)

At bottom, Surgin asks this Court to ignore *its own* detailed billing evidence and instead accept a few lines of facile conclusions about the very same billings, conclusions that the billing statements themselves directly *refute*. But a party cannot create substantial evidence by contradicting itself, as Surgin has done here. The tactic has long been rejected in the summary judgment context (*D'Amico v. Board of Medical Examiners* (1974) 11 Cal.3d 1, 21-22), and it must be rejected here as well.

Surgin had the burden of establishing that all of the attorney's fees it sought resulted from services compensable under *Brandt* (AOB 33) and were reasonable (*Fernandez v. Fernandez* (1961) 194 Cal.App.2d 782, 800). Its failure of proof on *Brandt* fees means the compensatory judgment cannot stand.

2. The Award Of Defense Fees Is Improper Because Truck Neither Owed Nor Undertook Any Obligation To Pay For The Defense Of Wholly Noncovered Claims.

Surgin fares no better with its argument regarding the award of $270,622 in defense fees. (RB 60.) Once again, Surgin completely ignores *its own evidence*. And again, the reason is obvious: Its own lawyers' bills—which are specifically separated by subject matter—conclusively reveal that over 98 percent of the claimed defense fees (i.e., $267,145.09) related to the *indisputably noncovered* patent infringement actions and the *noncovered* appeal from the preliminary injunction regarding the patent. (AOB 31; see also *Cutler-Orosi Unified School Dist.*, *supra*, 31 Cal.App.4th at p. 629 [no coverage or duty to defend injunction actions].) Nor does Surgin point to any evidentiary nexus between the remaining claimed fees—the $3,476.95 Hyman firm's bills—and any

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[33](...continued)
appropriate]; see also *People v. Johnson* (1980) 26 Cal.3d 557, 577 ["we must resolve the issue in light of the *whole record* . . . and may not limit our appraisal to isolated bits of evidence selected by the respondent"; "it is not enough for the respondent simply to point to . . . '*some*' evidence supporting the finding," internal quotations and citations omitted, first emphasis in original, second emphasis added]; *Kuhn v. Department of General Services*, *supra*, 22 Cal.App.4th 1627, 1633 ["'A decision supported by a mere scintilla of evidence need not be affirmed on review'"].

of the Alcon actions, or to any evidence that it expended any fees in defending the counterclaim action. (See AOB 30, 31.)

The question, then, is whether Surgin may recover defense fees that its *own uncontroverted evidence* reveals were *indisputably* expended *solely* in defending entirely *noncovered* actions. The answer is "no." *Hogan v. Midland National Ins. Co.* (1970) 3 Cal.3d 553, 564, holds that, even where a carrier wrongfully refuses to defend a single lawsuit involving some causes of action that are covered, it still owes no obligation to pay fees indisputably allocable to noncovered claims. Our case is much stronger. Here, the patent infringement actions were not merely separate causes of action, they were *separate lawsuits*. The legal billings were separately broken down by lawsuit, so there is no question about fee allocation among the separate suits. And since there wasn't a single arguably covered cause of action in *any* of the patent infringement lawsuits, there is no conceivable basis for awarding any fees for defending those suits. At a bare minimum, the compensatory damage award must be reduced by $267,145.09.

Surgin's predictable response is to draw attention elsewhere, this time by returning to its theme that Truck promised to pay. (RB 60.) But this claim ignores Surgin's *own allegation* that Truck offered to pay Surgin's defense fees *if* Truck owed a duty to defend and *subject to* a reservation of its right to recoup if it turned out it owed no duty to defend. So, even if there were some extra-policy promise to pay, that agreement—*according to the specific allegations of the complaint*—was expressly limited to covered claims.

California Union Ins. Co. v. Club Aquarius, Inc., *supra*, 113 Cal.App.3d at pp. 247-248, specifically rejects Surgin's argument. It holds that even a carrier's unqualified agreement to "assume the cost of the defense of the entire action" did *not* require the carrier to pay fees indisputably and wholly allocable to noncovered claims. (See also *Richardson*, *supra*, 95 Daily Journal D.A.R. at p. 1662-1663 [carrier had no obligation to pay fees for claims it had agreed to defend, where carrier reserved right to seek reimbursement of defense fees and there was no coverage]; see cases cited, *supra*, at pp. 38-39.)

V.

THE $57.2 MILLION PUNITIVE DAMAGE AWARD— A HUNDRED TIMES THE UNSUPPORTED AND EXCESSIVE COMPENSATORY DAMAGE AWARD—MUST BE REVERSED BECAUSE IT IS GROSSLY EXCESSIVE AND PLAINLY THE PRODUCT OF PASSION AND PREJUDICE.

In discussing the punitive damage award, Surgin again wants the court to look everywhere but where it matters, focusing on labels rather than substance. While it is true, as Surgin says, that punitive damage awards have been reviewed under a "passion or prejudice" standard (RB 61-62), the required review, regardless of label, is of constitutional dimension and is far more intense than the superficial standard Surgin would like this Court to employ.

Recent decisions provide a "clear constitutional mandate for *meaningful* judicial *scrutiny* of punitive damage awards." (*Adams*, *supra*, 54 Cal.3d at p. 118 [interpreting *Pacific Mut. Life Ins. Co. v. Haslip* (1991) 499 U.S. 1 [111 S. Ct. 1032, 113 L.Ed.2d 1], cited in *Honda Motor Co. Ltd. v. Oberg* (1994) ___ U.S. ___ [114 S.Ct. 2331, 2334, 129 L.Ed.2d 336].) The mandate requires that "[a]ppellate courts must *scrutinize* punitive damage verdicts" and conduct a *searching* review of the criteria governing the propriety of the award. (*Las Palmas Associates*, *supra*, 235 Cal.App.3d at p. 1258, emphasis added; *Pacific Mut. Life Ins. v. Haslip* (1991) 499 U.S. 1, 21, fn.10 [111 S.Ct. 1032, 1045, fn. 10, 113 L.Ed.2d 1] [review for mere "passion or prejudice" or "excessiveness" would be insufficient].) Since "[p]unitive damages pose an acute danger of arbitrary deprivation of property," reviewing courts must closely review punitive awards to ensure they do not exceed *substantive* constitutional limits. (*Oberg*, *supra* ___ U.S. ___ [114 S.Ct. at pp. 2335, 2341, 129 L.Ed.2d 336] ["we hold that Oregon's denial of judicial review of the size of punitive damage awards violates the Due Process Clause of the Fourteenth Amendment"].)

Given these strong constitutional underpinnings, it is not surprising that the United States Supreme Court has rejected Surgin's assertion (RB 62) that "[t]he substantial evidence rule controls" review of the *amount* of punitive damages. (*Oberg*, *supra*, ___ U.S. ___, [114 S.Ct. at pp. 2334, 2341] [as a matter of due process, appellate review of size of punitive damage award may not be

limited to a determination whether there is evidence to support the verdict].) Nor is Surgin correct when it asserts that a reviewing court should simply rubber-stamp a default award because it reflects a judge's, rather than a jury's, decision. (E.g., RB 62.) *Uva* is expressly to the contrary.

In fact, there is no legitimate basis for the massive punitive damage award in this case.

A. As A Matter Of Law, The Punitive Award Must Be Reversed Because It Is Premised On A Compensatory Award That Itself Must Be Reversed.

Under *Neal v. Farmers Ins. Exchange* (1978) 21 Cal.3d 910, 928, the relative size of the punitive and compensatory awards is one of the factors a court *must* consider in evaluating the propriety of a punitive damage award. Just as a court must tailor a punitive award to the defendant's net worth (*Adams, supra*, 54 Cal.3d 105), so, too, the court must tailor it to the compensatory award. If the compensatory award is reversed or reduced, the punitive award—which by law must bear a reasonable relationship to the compensatory award—necessarily must be reconsidered *by the trier of fact*. (AOB 35-36.) Our Supreme Court has expressly so held:

> "The trial court therefore properly granted a new trial on the issue of compensatory damages. Exemplary damages must be redetermined as well, as 'it would be improper and premature to assess such damages until or concurrently with the assessment of "actual damages"' [citation] and 'exemplary damages must bear a reasonable relation to actual damages' [citation] . . . ." (*Liodas v. Sahadi* (1977) 19 Cal.3d 278, 284.)[34]

Surgin argues that *Bertero v. National General Corp.* (1974) 13 Cal.3d 43, is contrary. (RB 69.) It is not. True, in *Bertero* the Supreme Court reduced a compensatory award without

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[34] In support of this proposition, the Supreme Court cited *Kuffel v. Seaside Oil Co.* (1970) 11 Cal.App.3d 354, 367 and *Foster v. Keating* (1953) 120 Cal.App.2d 435, 454-455, both of which explicitly require reversal of a punitive award when the compensatory award may change. (See also *Palmer v. Ted Stevens Honda, Inc.* (1987) 193 Cal.App.3d 530, 540-542 [punitive damages had to be reconsidered where jury not informed that compensatory award would be reduced because of payment by co-tortfeasor].)

reducing a punitive award. But *Bertero* was decided four years before *Neal* first identified the reasonable relationship test as a necessary prong of its tripartite standard. In any event, *Bertero* did not even consider whether the reduction of compensatory damages should have affected the punitive award and, therefore, it is not authority for that proposition. (See authorities discussed at conclusion of footnote 5, *supra*.)

Since the compensatory damage award in this case must be reversed as excessive (both in exceeding the $270,000 jurisdictional limit and for want of substantial evidence), the punitive damage award must fall in turn. While this alone is reason for reversal, the punitive award must also be vacated for other reasons as well, as we now demonstrate.

B. By Any Measure, The Punitive Award Is So Excessive That It Only Could Have Been Motivated By Passion Or Prejudice.

Even if there were no jurisdictional $270,000 limit and even if every penny of the $572,000 compensatory damage award were otherwise miraculously supportable, the punitive award would *still* be massively excessive. No other conclusion is possible when one considers the relevant questions: Is the punitive award disproportionate to the award of compensatory damages or to the defendant's net worth? Does the punitive award exceed the amount necessary to punish? How reprehensible was the conduct at issue when *compared to other conduct warranting punitive damages*? Was the fact-finder influenced by improper considerations? Is there any indication that the fact-finder might have been influenced by passion or prejudice?

1. The *Neal* Factors Cannot Be Viewed In Isolation. When Considered Together, They Compel The Conclusion That The Punitive Award Here Vastly Exceeds Any That Can Be Justified Rationally.

Surgin urges this Court to view the various *Neal* factors in isolation, picking a ratio here and a percentage there to justify its position. (RB 62-63, 67, 70-71.) The vice of such a simplistic analysis is that it can be used to prove almost anything and, thus, fails to address the "substantive limit" on punitive awards mandated by the United States Constitution. The vice is eliminated by

the "combined number" approach presented in the Opening Brief. (AOB 37-38.) Although Surgin disparages this analysis by name-calling ("pseudo-mathematical," whatever that means) (RB 62), Surgin's approach would perpetuate both meaningless and unconstitutional results.

For example—exactly as we predicted (AOB 37, fn. 12)—Surgin seeks to justify the punitive award by citing several cases adopting high ratios of punitive to compensatory damages, while ignoring the vital fact that the compensatory damage award in *each* of those cases was *less than $20,000* and represented infinitesimal percentages of the defendants' respective net worths. See RB 67.)[35/] There simply is no comparison between these cases and a 100:1 punitive-compensatory ratio where the compensatory damages exceed $570,000. The courts have recognized this distinction. For instance, in *Vossler v. Richards Manufacturing Co.* (1983) 143 Cal.App.3d 952, 969, the court affirmed a 20:1 ratio because "[t]he actual damages were limited [$25,000]," noting that "[a] ratio of 20:1 would be excessive in a case like *Grimshaw* [*v. Ford Motor Co.* (1981) 119 Cal.App.3d 757]" where the compensatory damages were $2.5 million, even though the $3.5 million punitive award represented only 0.45% of Ford's net worth.

35/ *Finney v. Lockhart* (1950) 35 Cal.2d 161 [2000:1 ratio, but compensatory damages of $1]; *Wetherbee v. United Ins. Co. of America* (1971) 18 Cal.App.3d 266 [190.5:1 ratio, but compensatory damages of $1,050; punitive award was 0.33% of net worth]; *Neal v. Farmers Ins. Exchange*, *supra*, 21 Cal.3d 910 [78:1 ratio, but compensatory damages no more than $10,000; punitive award was 0.73% of net worth]; *Chodos v. Insurance Co. of North America* (1981) 126 Cal.App.3d 86 [38.9:1 ratio, but compensatory damages of $5,146; punitive award no more than 0.2% of net worth]; *TXO Production Corp. v. Alliance Resources Corp.* (1993) ___ U.S.___ [113 S.Ct. 2711, 2714, 2716, fn. 9, 2721-2722, 125 L.Ed.2d 366] [526:1 ratio, but compensatory damages of $19,000; $10 million punitive award was only 0.45% of net worth of $2.2 billion company]. The *TXO* case applied only a "grossly excessive" standard, *expressly* leaving to state law enforcement of a "reasonable relationship" between punitive and compensatory damages. (___ U.S. ___ [113 S.Ct. at p. 2720, fn. 24]; see *Neal*, *supra*, 21 Cal.3d at p. 928 [requiring *reasonable* relationship between punitive and compensatory damages].)

Surgin's net worth comparisons are equally deficient. The cases it cites (RB 70-71) all involve relatively small punitive damage awards—none exceeding $150,000—and *significantly* smaller ratios of punitive to compensatory damages than here.[36/]

Contrary to Surgin's assertions (RB 62), we do *not* claim there is a mathematically precise way of evaluating the size of a punitive award, although we note that the U.S. Supreme Court has declared that a 4:1 ratio is close to the line (*Haslip*, *supra*, 499 U.S. at p. 23 [111 S.Ct. at p. 1046, 113 L.Ed.2d 1] and that California reviewing courts have suggested 10 percent as a net worth cap (e. g., *Michelson v. Hamada* (1994) 29 Cal.App.4th 1566, 1596). But comparisons must nonetheless be made because there is no other way to assess—as courts must—whether an award is excessive or approaches the "substantive limit" mandated by the U.S. Constitution. As the California Supreme Court has declared: "Deciding in the abstract whether an award is 'excessive' is like deciding whether it is 'bigger,' without asking 'Bigger than what?'" (*Adams*, *supra*, 54 Cal.3d at p. 110.)

There is no discernable pattern when the various mathematical measures are examined in isolation from each other. To eliminate individual distortions, we have suggested viewing the figures together, rather than individually, so that combined comparisons—utilizing *all* the

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36/ *Burnett v. National Enquirer, Inc.* (1983) 144 Cal.App.3d 991 [3:1 ratio, $150,000 punitive award]; *Zhadan v. Downtown Los Angeles Motor Distributors, Inc.* (1979) 100 Cal.App.3d 821 [17:1 ratio, $90,000 punitive award]; *Godfrey v. Steinpress* (1982) 128 Cal.App.3d 154 [3:1 ratio, $60,000 punitive award].

factors—can be made.[37] The combined-number approach directly answers the Supreme Court's "Bigger than what?" question. When viewed in this sensible manner, a pattern *does* emerge: (1) a large absolute punitive damage award is *only* approved when it represents (a) a small ratio of punitive to compensatory damages *and* (b) a small percentage of a defendant's net worth; (2) a large punitive-to-compensatory ratio is approved only where the compensatory award is small.

While the combined-number approach may not afford an infallible mechanical formula for precisely determining the permissible limits of a punitive award, and while more sophisticated approaches might be conceived, the approach at least directly addresses the substantive issues and it does define a ballpark—a range of court-approved results. Unlike Surgin's approach, it allows meaningful comparisons. (*Devlin*, *supra*, 155 Cal.App.3d 381, 391 [while "there is no *simple* formula for calculating punitive damages . . . . there is a range of reasonableness," emphasis added].) This is all our combined-number approach purports to do; but no more is needed to show that the punitive award here is not just dramatically out of the ballpark, it is off the planet.

The combined-number for this case is 1,420,000,000. That is a monstrous number. It means that when the punitive damage award in this case is compared on an equal basis with other punitive damage awards challenged as excessive and approved on appeal in California, the award here is many, many times the mean, median and highest award. This is far out of bounds. It is even dramatically out of kilter when compared to some of the largest punitive awards ever awarded

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[37] Surgin's methodological quibbles with Truck's analysis (RB 63-64, fn. 69) are unfair and unfounded:

1. Surgin complains about comparisons involving cases that reported the punitive award as a percentage of "net assets," rather than "net worth" (RB 63-64, fn. 69), but Black's Law Dictionary (6th ed., 1990) at pp. 1040, 1041, gives the same definition for both.

2. Surgin also complains that Truck's analysis omitted certain cases. (RB 64, fn. 69.) This criticism is unwarranted. Truck did not consider cases where the discussion concerning excessiveness of punitive damages was unpublished (*Leonardini v. Shell Oil Co.* (1989) 216 Cal.App.3d 547; see Cal.R.Ct. 976.1(b), 977(a)) or where the court did not decide the excessiveness issue (*Gagnon v. Continental Casualty Co.* (1989) 211 Cal.App.3d 1598) or where the size of the punitive award was not challenged on appeal (e.g., *Grimshaw v. Ford Motor Co.* (1981) 119 Cal.App.3d 757).

3. Truck did inadvertently overlook one case (*Wyatt v. Union Mortgage Co.* (1979) 24 Cal.3d 773), which was also overlooked in *Devlin's* appendix. However, adding that case to the data (and several other cases overlooked in *Devlin*) does not change the result in any appreciable manner; a revised chart incorporating these cases is attached as Appendix A to this brief.

in the *nation*. (E.g., *Texaco v. Pennzoil* (Tex.App. 1987) 729 S.W.2d 768 [approving *$2 billion* punitive award, compensatory damages of *$7.5 billion*, 0.27:1 ratio of punitive to compensatory damages; punitives represented 8.33% of $24 *billion* company's net worth; combined number is 45,000,000—merely 3.2% of the combined number here]; *TXO*, *supra*, ___ U.S. ___ [113 S.Ct. at p. 2714] [$10 million punitive award represented a 526:1 ratio to compensatory damages, but only 0.45% of $2.2 *billion* company's net worth; combined number is 23,900,000—only 1.7% of the combined number here].)

Despite its efforts to isolate a number here and there, Surgin points to *no* case that comes anywhere close to supporting its punitive award when all three of the governing factors—ratio to compensatory damages, percent of net worth, and absolute size of award—are considered together. That's why Surgin seeks to ridicule the significance of the immense disproportionality here. The effort fails.

First, Surgin claims the compensatory damages here do not reflect the true harm to Surgin because there were unspecified "other effects" on its business that should be considered. (RB 68.) Nonsense. As we have demonstrated, the compensatory award here is outrageously excessive, *not* understated. Also, the trial court specifically found that the only *pleaded* "other effects"—supposed lost profits—were *not* recoverable because they were speculative, both as to fact and amount. (RT 321.)[38/]

Second, implicitly conceding that an award of 25% of Truck's net worth would be reversible *per se* (see, e.g. *Michelson v. Hamada*, *supra*, 29 Cal.App.4th at p. 1596 [anything over 10 percent of net worth generally considered excessive as a matter of law]), Surgin again attempts to alter reality, arguing that the punitive damage award should be compared not to Truck's net worth, but rather to the net worth of the non-party entities with which Truck purportedly "pools" its insurance risks. (RB 70.)

[38/] Surgin has not even responded to Truck's argument that the asserted lost profits could not possibly have been caused by Truck's supposed failure to defend, but rather were caused at the outset by Alcon's filing its lawsuit and obtaining a preliminary injunction *before* Surgin even tendered the Alcon claims to Truck. (AOB 43, fn. 15.)

a. Surgin never pleaded this theory and therefore nothing about it was deemed admitted by Truck's default.

b. There was no evidence of "pooling" before the trial court at the time it decided the amount of the punitive award. The problem is not, as Surgin mischaracterizes it (RB 70, fn. 79), simply that the evidence was submitted after the default prove-up hearing. The problem is that the evidence was not submitted until *after* the trial court had already announced its *decision* on punitive damages. There is, of course, nothing extraordinary about taking further evidence on issues which have not yet been decided. But that didn't happen here. What happened here is that the trial court permitted the introduction of additional evidence long after it announced its decision. The evidence was offered for no discernible purpose other than to bolster the already-made decision. It was jurisprudence worthy of Lewis Carroll's Queen of Hearts: "Sentence first—verdict afterwards." (See *Wiler v. Firestone Tire & Rubber Co.* (1979) 95 Cal.App.3d 621, 627 ["The trial court's decision must be reviewed on the basis of the papers filed at the time the court considered the motion, not in light of documents filed subsequent to the trial court's resolution of the issue"].)

c. Surgin does not cite, and Truck has not found, any case anywhere in the nation that endorses Surgin's approach. That is not surprising. It is *at best* a "rich uncle" argument. According to Surgin, an individual defendant should be punished not according to its own net worth, but according to the resources of anyone who might agree to come to its aid. However, courts across the nation have uniformly rejected essentially the same argument where plaintiffs seeking punitive damages from a corporation have tried to enhance the award by basing it on the net worth of a non-party corporate parent. (E.g. *Tomaselli v. Transamerica Ins. Co.* (1994) 25 Cal.App.4th 1269, 1284-1286 [due process forbids use of parent company's financial status to prove net worth absent showing that parent controlled litigation]; *Institute of Veterinary Pathology, Inc. v. California Health Laboratories, Inc.* (1981) 116 Cal.App.3d 111, 120; *HCA Health Services of Midwest, Inc. v. National Bank of Commerce* (1988) 294 Ark. 525, 531-532 [745 S.W.2d 120, 124]; *Walker v. Dominick's Finer Foods, Inc.* (1980) 92 Ill.App.3d 645, 649 [415 N.E.2d 1213, 1216-1217, 47

Ill.Dec. 900, 903-904].)[39] As *Tomaselli* observed, 25 Cal.App.4th at pp. 1284-1286, it would offend due process to premise the size of a punitive damage award on the assets or worth of an absent (or in this case *dismissed*) entity which has not had an opportunity to participate in the proceedings. If Surgin's premise is that the judgment should be enlarged because of the net worth of another entity that ultimately would be paying, that other entity is entitled to an opportunity to be heard on the subject.

d. But even if Surgin's unprecedented pooling theory could somehow be accepted at face value, the punitive damage award must still be reversed as grossly excessive:

(1) The combined-number approach demonstrates that, even with "pooling," the award is massive. Surgin states that the $57.2 million punitive award represents 2.18% of the combined net worth of all pool members. (RB 70; JA 7454, 7461.) But 2.18% of net worth is *still* an immense number given the punitive-compensatory ratio and absolute size of the award. Even 2.18% of pooled net worth yields a combined number of 124,228,436—over three times the largest number ever approved in a published California decision, and almost eighteen times the largest number ever approved in a published California decision that reports a percentage of the defendant's net worth. (See Appendix A.)

(2) By narrowly focusing on a 1993 financial snapshot of the pool members, the pooling approach makes no allowance for the huge *losses* the entities collectively suffered in each of the preceding five years—over $940 million in pre-tax losses from 1988 to 1992, with losses in every year ranging from $25 million to $280 million. (JA 7461; see cases cited at AOB 38 [defendant's net income is relevant to punitive calculation].)

(3) Even allocating only 10.24% of the award ($5.9 million) to Truck, as Surgin advocates (RB 70), the punitive award would still *exceed* Truck's *entire* net pre-tax income for the

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[39] Even in states that, unlike California, allow insurance of punitive damage awards, the fact that the defendant is insured (which is essentially what pooling would accomplish from Surgin's perspective) may not be used to inflate the punitive award. (E.g., *Liberatore v. Thompson* (Ariz. App. 1988) 157 Ariz. 612, 621 [760 P.2d 612, 621] ["It is a defendant's own wealth, not his insurer's wealth, that bears on the proper level of punitive damages"]; see also Evid. Code, § 1155.)

only year in five in which Truck did not suffer a loss. (JA 6361, 7454, 7470; RT 179, 180.)[40] And, of course, the remaining $51.3 million in punitive damages doesn't just disappear; it still must be paid. If for any reason Truck could not obtain contribution from the other pool members (who would not be bound by the judgment), it would be in the unacceptable position of being subject to a punitive award based on a completely fictitious asset base.

The grossly excessive punitive damage judgment may not be saved by Surgin's "pooling" afterthought. It was not pleaded or before the Court at the time decision was made; it is not supported by any authority; it is contradicted by established precedent; and it is contrary to due process.

2. Surgin's Analysis Of The Reprehensibility Of Truck's Conduct Improperly Relies On Unpleaded Facts And Ignores The Requirement That, In Assessing Reprehensibility, A Defendant's Conduct Must Be Compared To Other Reprehensible Conduct.

Surgin's argument regarding reprehensibility amounts to nothing more than a bald statement that Truck behaved badly. (RB 64-67) This would not be enough even if the showing of bad behavior were properly limited only to the deemed-admitted allegations of the complaint. But, in fact, most of the factual predicates for Surgin's argument were never pleaded and were never deemed admitted by Truck's default.

The unpleaded "pattern and practice" evidence lies at the heart of the punitive award. To establish this "pattern and practice," Surgin relied heavily on the *Waller* judgment and on the testimony of a former employee of an entity affiliated with Truck, Mr. Conn. Although the

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[40] Surgin urges that the Court should disregard the testimony of *Surgin's* own expert that a $1.5 million award would have a material impact on Truck's financial statements and be reported to senior management. (RB 71; RT 178.) Surgin again overreaches. While the purpose of a punitive award is to deter and punish misconduct, "[a]n award should be *no larger* than the amount necessary to accomplish this purpose and therefore must be tailored to the defendant's financial status." (*Michelson, supra*, 29 Cal.App.4th at p. 1593, emphasis added.) Having an effect on the bottom line of financial statements is just what it takes to punish and deter. Having an effect *38 times larger than that* is patently excessive.

Supreme Court granted review in *Waller* after Truck filed its Opening Brief in the present case, it is significant in evaluating reprehensibility that three Court of Appeal justices *unanimously agreed* there was *no* basis for punitive damages in *Waller* and that Truck was entitled to judgment in its favor. That Truck was subjected to massive punishment based on an unpleaded "pattern and practice" theory whose cornerstone is the still-non-final *Waller* judgment that three appellate justices unanimously rejected speaks volumes about the shocking absence of due process in this case.

As for the unpleaded conduct of the former employee, Conn, his affiliation with Truck ended some five years before the earliest of the events at issue here (and some seven years before the discovery conduct at issue), so he had no basis for knowing Truck's practices after the *Alcon* actions were tendered. Besides, Conn's testimony pertained to his experience as an investigator working with counsel on behalf of Truck and other affiliated entities (RT 207, 208, 217-24), and it was therefore subject to attorney-client privileges (*Triple A Machine Shop, Inc. v. State of California* (1989) 213 Cal.App.3d 131, 141-42) which, in Truck's absence, the trial court was *required* to enforce *sua sponte* (Evid. Code, § 916).

Significantly, Surgin refuses even to acknowledge the recent, controlling Supreme Court authority requiring that the reprehensibility of the defendant's misconduct be judged "*in light of the types of misconduct that will support punitive damages . . . .*" (*Adams, supra*, 54 Cal.3d at p. 111, fn. 2, emphasis added.) In determining excessiveness, "[t]he nature of the inquiry is a comparative one." (*Adams, supra*, 54 Cal.3d at p. 110.) As *Adams* requires, the relevant inquiry is: How does the "despicable" misconduct at issue compare with other types of "despicable" misconduct. (See *Vossler, supra*, 143 Cal.App.3d 952 [continued sale of surgical implant knowing it would cause excruciating pain to hundreds of mostly elderly arthritic patients still less reprehensible than conduct in *Grimshaw* involving marketing of vehicle that management knew would result in fiery deaths].) Failure to pay, even wrongful and intentional failure to pay, a commercial insurance claim, while not excusable, is simply not as reprehensible as many other types of despicable misconduct for which punitive damages are and should be awarded.

Even if one were to ignore *Adams* and evaluate the conduct pleaded here in the abstract, it still would not reflect elevated reprehensibility. *Truck never deprived Surgin of any benefit to which*

Surgin was entitled under its policy. Rather, the *most* Surgin can complain about is Truck's failure to perform an entirely gratuitous promise to provide a benefit that, in fact, was not due under the policy. Failing to live up to a promise to provide something that was never owing, while perhaps not commendable, is not in the same world as the kind of egregious behavior that typically underlies sizeable punitive awards. Indeed, failure to honor a promise is exactly the type of conduct for which the Legislature has said punitive damages cannot be recovered. (Civ. Code, § 3294 (a).)

But even if Truck's policy somehow required a defense, Truck's breach pales in comparison to other conduct deserving of deterrence and punishment, such as severely beating people, abducting and hiding children, and marketing products knowing they are likely to kill, injure or cause excruciating pain. (See AOB 40; see also *Tomaselli, supra*, 25 Cal.App.4th at pp. 1287-1288 [a carrier's mishandling of one or a few claims does not justify punitive damages at all].)

3. The Punitive Award Must Be Reversed Because The Trial Court Expressly Based The Award On Improper Factors.

Determining the amount of punitive damages involves careful balancing. (*Devlin, supra*, 155 Cal.App.3d at p. 388.) When the fact-finder considers improper factors, as the trial court did here, the balance is upset and the fact-finder must revisit the issue. This is true even if the punitive award is otherwise supported by substantial evidence.

The Supreme Court made this clear in *Potter v. Firestone Tire & Rubber Co.* (1993) 6 Cal.4th 965, 1004, where, though it held that substantial evidence supported a punitive damage award, it nonetheless *reversed* the award because—exactly as in this case—the trial court misunderstood the degree or basis of the wrongfulness of the defendant's conduct. (See also *Don v. Cruz* (1982) 131 Cal.App.3d 695, 707 [in ferreting out passion, prejudice, or excessiveness of compensatory award, "the (reviewing) court may consider, in addition to the amount of the award, indications in the record that the fact finder was influenced by improper considerations"]; *Zhadan v. Downtown L.A. Motors* (1976) 66 Cal.App.3d 481, 500-501 [same re punitive damages].)

Here, the trial court indisputably considered numerous improper factors:

- At the prove-up, Surgin sought (and, even now, still seeks) to justify the punitive damage award on the basis of a purported pattern of misconduct in other cases and on purported discovery abuse in this and other cases. (RB 65, 67.) *But none of this was ever pleaded in the complaint* and, thus, was never deemed admitted on default. (AOB 22-23.)

- The trial court expressly refused to consider this Court's controlling decision in *Watercloud* (RT 340), and thus erroneously assumed Truck owed a duty to defend Surgin in the Alcon actions under the terms of its policy. Further, it believed, contrary to established law, that Truck owed a *fiduciary* duty to pay Surgin's defense costs. (See *Love v. Fire Ins. Exchange* (1990) 221 Cal.App.3d 1136, 1147-1150.) In short, the trial court misunderstood both the nature and degree of Truck's allegedly wrongful conduct, the precise circumstance that required reversal in *Potter*.

- The trial court *expressly* enhanced the punitive award "*to compensate* [Surgin] for the aggravation" caused "by this litigation and the trials and tribulations of litigation" and for the speculative "lost profits" that it refused to award as compensatory damages. (RT 323, emphasis added; AOB 42-43.)[41/]

- The trial court *said* it premised its award on Truck's supposed tactics in "the litigation that terminated a few weeks ago." (RT 322.) Under established law, this was improper. As one court said:

> "It may thus be reasonably said that the jury's punitive damage verdict was at least in part reflective of the jury's annoyance with [defendant's] conduct in court, as distinguished from his conduct in reference to [the matter in controversy]. To that extent, it was a result of passion and prejudice and was not based on those acts for which he should be punished." (*Goshgarian v. George* (1984) 161 Cal.App.3d 1214,

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41/ Although Surgin implicitly concedes it is improper to award speculative compensatory damages through the back door as punitive damages, it attempts to downplay the problem by mischaracterizing the trial court's actions as merely "consider[ing] this non-compensable harm, not compensating for it." (RB 68.) The trial court's express words belie Surgin's microscopic distinction.

1230; *Nie v. National Auto. & Casualty Ins. Co.* (1988) 199 Cal.App.3d 1192, 1201-1202 [insurer's litigation conduct in same action, other than settlement offers, is *inadmissible* in bad faith action]; see AOB 44-45].)

In this case, one need not speculate about whether the trial court was reacting to Truck's litigation conduct: The trial court *said* it was. In any event, it hardly lies in Surgin's mouth to claim that "it is not clear that the trial court relied on Truck's discovery misconduct in setting the punitive award" (RB 65, fn. 71), since Surgin itself elected to offer the evidence at the uncontested default hearing for the precise purpose of having the trial court rely on it. Why else would Surgin have offered the evidence? Indeed, Surgin opposed Truck's post-judgment motions by strenuously urging the unpleaded evidence as support for the huge punitive award. (See JA 8063-64, 8070-71; see also JA 8181 [Truck pointing out the impropriety of relying on such unpleaded evidence].)

4. The Punitive Award Reflects Passion Or Prejudice.

Surgin urges this Court to abdicate its constitutional responsibility to scrutinize the punitive damage award because the award was imposed by "a respected and cautious judge." (RB 72.) But judges are not immune from passion and prejudice. Just because a judge, rather than a jury, awards punitive damages does not mean there is some presumption against the existence of passion or prejudice. (*Uva*, *supra*, 83 Cal.App.3d at pp. 364-365 [held, reversed, default award "shocking to the conscience"].) The issue is not the trial judge's reputation, but what the trial judge *actually did on this occasion*. Even the most "respected and conservative" judges (see RB 1, 3) sometimes lose their temper, are swayed by pleas to passion, or are unwilling to admit they are wrong. That is why we have appellate courts; that is why the law requires judges to be disqualified or to disqualify themselves when they cannot be objective. (§ 170.1.)

A judge proceeding dispassionately does not ignore fundamental rules and procedures time and time again at each stage of the proceedings. But that is exactly what happened here. (AOB 46-47.) When a judge who repeatedly ignores the law and reaches an outrageously unjust result is "respected and conservative," then there is all the more reason to believe that the only conceivable

explanation for such conduct is that the judge was influenced by passion or prejudice. For this reason, too, the judgment must be reversed.

VI.

THE APPEARANCE OF IMPROPRIETY CREATED BY THE TRIAL COURT'S PRIVATE, UNREPORTED MEETING WITH SURGIN MANDATES REVERSAL.

The facts regarding the trial court's private, unreported meeting with Surgin's counsel immediately prior to the scheduled prove-up hearing are undisputed and were confirmed by both the trial court and by Surgin's counsel. Denying even the *appearance* of impropriety, Surgin argues that there is nothing wrong with a "harmless" social contact between the court and a party and that Truck must, but cannot, show prejudice from a meeting Truck was not permitted to witness or review by written transcript. (RB 72-73.)

Random contact in a social setting is one thing, but when the discussion admittedly involves the case in question, the contact moves from apparent innocence to apparent impropriety. (*Guadalupe A. v. Superior Court* (1991) 234 Cal.App.3d 100, 109 ["although a harmless communication with a party or a witness is not misconduct, it is generally considered misconduct to engage in serious discussion with those persons"].) And, as the contact moves from a social setting to the courtroom during court hours, the appearance of impropriety is further enhanced. (*Kennick v. Commission on Judicial Performance* (1990) 50 Cal.3d 297, 331-332 [innocent conversations between trial court and counsel representing one side constitute misconduct because undertaken during court hours in court chambers]; *Dubaldo v. Dubaldo* (1988) 14 Conn.App. 645 [542 A.2d 750] [mistrial required because of court's ex parte, in-chambers meeting with one side's witness, even though purpose of discussion was entirely innocent, i.e., to express sympathy at death of witness' wife].)

Surgin's meeting with the trial court was hardly a social encounter. It took place at the appointed hour for Surgin's default prove-up, in the trial court's chambers. It was supposed to involve official business. Truck was expressly excluded from participating or even observing; nor

was the meeting reported, as Truck had requested. At least a part of the time *admittedly* was spent discussing this case (with the rest of the time devoted to kibitzing about Michael Jordan). All the while, the defaulted defendant awaited its fate outside the court's chambers. The discussion concerning the case was hardly innocent or "harmless": Admittedly at issue was not some minor procedural nicety, but a critical decision by Surgin as to whether it would entrust the damage award to the judge instead of the jury it previously requested. *Immediately upon emerging from his ex parte meeting with the trial court*, the first thing Surgin's counsel expressed was his conversion: "our belief [is] that a jury would serve no other purpose, no better purpose than having the court hear it, [and] we've elected to do it just to the court." (RT 77.) The trial court then proceeded to render an astounding $57.8 million award, including $57.2 million for punitive damages, far exceeding even Surgin's demands.

No appearance of impropriety?

Surgin proclaims the judgment should not be reversed because there is no showing of prejudice. (RB 73.) But that misses the point of the error. Prejudice or not, a party is entitled to a trial that is fair in appearance as well as in fact. (*In re Marriage of Iverson* (1992) 11 Cal.App.4th 1495, 1500 ["the trial of a case should not only be fair in fact, but it should also appear to be fair"; citations and internal quotations omitted]; *id.* at p. 1504, Moore, J., concurring; *Webber v. Webber* (1948) 33 Cal.2d 153, 155; *Pratt v. Pratt* (1903) 141 Cal. 247, 252.) If a party had to show actual prejudice in these circumstances, there could never be a reversal for an appearance of impropriety: By definition, an *appearance* of impropriety means there is no direct evidence of an actual impropriety and therefore no direct evidence of prejudice. How can a party, excluded from a meeting between the court and one side that is not reported, ever show prejudice? That is exactly why the rules prohibit an *appearance* of impropriety.

It is not surprising that courts repeatedly have reversed judgments on the basis of an appearance of impropriety created by the trial court's actions, without addressing prejudice. (E.g. *In re Marriage of Iverson*, *supra*, 11 Cal.App.4th at p. 1501 [reversing for lack of *appearance* of impartial trial]; *id.* at p. 1504, Moore, J., concurring [explaining reversal mandated by *appearance* of partiality regardless of any actual bias]; *Gay v. Torrance* (1904) 145 Cal. 144, 149-150; *Dubaldo*,

supra, 14 Conn.App. 645 [542 A.2d 750].) As our Supreme Court long ago proclaimed, a new trial is necessary whenever the trial court's "acts were of such a nature, and done under such circumstances, as to afford *reasonable grounds* for the conclusion that by reason thereof the defeated party has not had a fair and impartial trial." (*Gay, supra,* 145 Cal. at pp. 149-150, emphasis added).[42/]

VII.

THE ORDER IMPOSING TERMINATING SANCTIONS MUST BE REVERSED. TRUCK COMPLIED WITH THE PLAIN MEANING OF SURGIN'S DISCOVERY REQUESTS AND THE TRIAL COURT'S DISCOVERY ORDERS. UNDER NO CIRCUMSTANCES DOES THE PUNISHMENT FIT THE CRIME.

We are well aware how much courts dislike discovery disputes. This is understandable. Resolving these disputes is time-consuming, requiring painstaking analysis of the language of discovery requests, responses, motions, orders and further responses. Boring, tedious stuff. Unfortunately, however, delving into the details of the discovery dispute here is the only way to determine whether Truck was lawfully deprived of its right to defend itself and whether the discovery punishment fit the discovery crime.

In arguing that the punishment is lawful, Surgin takes extensive liberties with the record and the law. But the truth is in the details.

We welcome a close and careful review of the *facts* underlying the discovery dispute. To facilitate that review, we submit two appendices with this brief: Appendix B presents a chronology of the events resulting in the imposition of terminating sanctions; Appendix C consists of three flow diagrams outlining the chronology and facts of each of the three disputed discovery areas. When

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42/ *In re Jonathan S.* (1979) 88 Cal.App.3d 468, cited by Surgin (RB 73), is not contrary. The contact in question there resulted in the trial court making the *sole* legal ruling the law allowed, so any possible unfairness or partiality could not have had any effect. Surgin can hardly make a similar showing here.

compared with the "factual" recitation in Surgin's brief, these appendices reveal the tortured paths Surgin travels in its effort to justify a finding that Truck deserved the civil death penalty.

A. Surgin Misstates The Standard Of Review For Determining Whether Discovery Misconduct Occurred.

Surgin simplistically urges that all aspects of the discovery dispute must be reviewed under an abuse of discretion standard. (RB 14.) The cases it cites, however, do *not* address the standard of review when, as here, the issue concerns the *meaning* of discovery requests and orders and the legal adequacy of responses; Surgin's cases concern only review of determinations of "wilfulness" and the selection of appropriate sanctions. (RB 14, fn. 12.)

Under the law, the *meaning* of Surgin's written discovery requests and the court's discovery orders and the *legal adequacy* of Truck's written discovery responses, like the interpretation of any other writings, are reviewed de novo. (See, e.g., *Beesley v. Superior Court* (1962) 58 Cal.2d 205, 208 [where facts are undisputed in discovery controversy, there is no room for trial court to exercise discretion]; *Greyhound Corp. v. Superior Court* (1961) 56 Cal.2d 355, 383-384 [same]; *Herman Feil, Inc. v. Design Center of Los Angeles* (1988) 204 Cal.App.3d 1406, 1414-1415 [interpretation of orders and writings "has long been held to be peculiarly an appellate function," rejecting contention that appellate court should apply substantial evidence rule to the trial court's interpretation of a minute order].)

B. Surgin's Overblown Claims Of Discovery Abuse Are Not Supported By The Record.

We cannot hope in this limited space to rebut all of Surgin's misrepresentations of the discovery record. Here, however, are some examples:

- Surgin would like this Court to believe that from the beginning it sought "all" claims-handling manuals, regardless of what they were used for. (E.g., RB 18-19, 24-25, 32.) The record is otherwise. The manuals requests only sought manuals "used," "referred to or relied upon" in handling or adjusting "claims under the 'advertising injury' provisions" of Surgin's policies. (JA 1042, 1092.) Surgin's motion to compel, specifically responding to an overbreadth objection,

argued that its requests narrowly sought "any claims procedure manuals and/or written guidelines *which are used* by Defendants in determining claims *under the 'advertising injury' provisions* of Defendant's policies." (JA 1020, emphasis added; accord, JA 1064-1065.) Not until Surgin's reply brief supporting its first unsuccessful motion for terminating sanctions did Surgin even hint at an "*all* manuals" construction (JA 1785); and it was not until its January 15, 1993 letter—sent after its initial terminating sanctions motion was denied—that Surgin directly claimed that the Court's discovery order required Truck to produce "*all* written claims handling guidelines [and] claims procedure manuals." (JA 2383, emphasis added; see RB 32.) But Surgin's exaggerated claim and the reality of its discovery requests are worlds apart. No matter how hard Surgin tries, it cannot alter the legal effect of what was *actually* sought and ordered.

- Surgin claims that a particular manual—the so-called Branch Claims Office Procedures Manual or "BCO Manual"—is a "smoking gun," a manual that was requested but not produced. (RB 18.) Far from it. Undeniably, the BCO Manual is a "manual," but the *uncontroverted evidence* is that the BCO Manual was not "used," "referred to or relied upon" by Truck in adjusting or handling advertising injury claims.[43] It therefore did not fall within Surgin's *own definition* of the documents it requested on the face of the court's order. (See JA 1042, 1092.) No matter how many times Surgin asserts the BCO manual must have been used, Truck's sworn testimony is the opposite.[44]

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[43] The sole, and hence unrefuted, evidence on this point is as follows: "Q: As a claims adjuster [i.e., if the questioner were a claims adjuster], would I ever refer to the Branch Claims Office Manual to determine how the claim that I'm handling should be processed? A: No." (JA 2396; accord, JA 2021M, 2021S & 2021T.) Surgin's assertion that this uncontradicted evidence is "not credible" (RB 23) has no basis in the record and affords no basis for disregarding Truck's sworn testimony.

[44] The supposed "contrary" testimony on which Surgin relies is not, in fact, contrary. That evidence revealed, without contradiction, that Truck's claims representatives did *not* have copies of the BCO Manual, that the BCO Manual *only* discussed the investigation and reporting of claims "*in generalities*" (i.e., not in reference to any specific type of claims such as advertising injury claims), and that the BCO Manual was only referred to at *training* sessions and *not* in the actual handling of claims. (JA 1806-1807, emphasis added.) When Truck was ordered to respond further to the manuals requests, it truthfully responded under oath that it *"is not presently aware of any documents that fall within this category."* (JA 4680, emphasis added.) This has never been disproved.

- Surgin impermissibly relies on testimony it introduced at the default prove-up—long after terminating sanctions had already been imposed—to assert that Truck possessed documents responsive to the manuals requests. (RB 23-24.) This bootstrap doesn't work. Due process precludes affirming terminating sanctions on the basis of evidence that was *not before the court* at the time terminating sanctions were imposed and that the sanctioned party had no opportunity to challenge or rebut. "The trial court's decision must be reviewed on the basis of the papers filed at the time the court considered the motion, not in the light of documents filed subsequent to the trial court's resolution of the issue." (*Wiler v. Firestone Tire & Rubber Co.*, *supra*, 95 Cal.App.3d at p. 627; *Munoz v. Kaiser Steel Corp.* (1984) 156 Cal.App.3d 965, 975 & fn. 2 [party cannot rely on document introduced at trial to urge that court previously erred in granting motion made at a time when the document was not before the court]; *In re Marriage of Quinlan* (1989) 209 Cal.App.3d 1417, 1421 [§ 128.5 sanctions may not be imposed without notice of the particular basis for sanctions and opportunity to be heard thereon].) Once again, while Surgin's tactic of "sanctions first, evidence later" might please the Queen of Hearts, it bears no relation to due process.[45/]

- Truck's sworn discovery responses on substantive issues cannot be disregarded simply because Surgin, or even the trial court, found them "not credible." (See RB 23, 28.) "Discovery sanctions . . . are meant to deter intentional abuse of the discovery process, not as a means to resolve the merits of a case." (*Ingalls Shipbuilding, Inc. v. United States* (Fed. Cir. 1988) 857 F.2d 1448, 1451.) For example, a trial court may not impose discovery sanctions on a driver in an

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[45/] Even if the belated evidence could somehow be considered, it was utterly incompetent, consisting of nothing but speculation. (JA 6629 [witness left non-claims employment with a Truck-affiliated entity more than five years before Surgin even tendered defense of the Alcon litigation], 6662-63 [witness speculated Truck must have had manual for advertising injury claims because, during his tenure more than five years before, it had manuals for all types of claims]; JA 6576-6622 [second witness opined that Truck had responsive manuals premised on her having "represented several clients in their bad-faith lawsuits against Farmers Group of Insurance Companies" in Texas, but she revealed *no* knowledge of what manuals Truck personnel used or relied upon in adjusting or determining advertising injury claims, and none of the documents she identified related to Truck's advertising injury policy provisions]; see *California Shoppers, Inc. v. Royal Globe Ins. Co.* (1985) 175 Cal.App.3d 1, 66 [attorney who regularly sues insurance carriers for bad faith is not an expert on insurance company procedures].)

automobile accident case simply because it does not believe the driver's sworn discovery response that the light was green; it may not do so even if a dozen other people at the scene testify the light was red. Just as with a motion for summary judgment or summary adjudication, a trial court cannot make such credibility calls on issues pertinent to the merits. Those are reserved exclusively for the jury at trial. Here, Truck had a right to a jury trial on the issue of what claims manuals and guidelines did or did not apply to the handling of Surgin's tenders.[46/]

- Truck's sworn supplemental discovery responses cannot be disproven by Truck's prior, overruled objections. Discovery objections are "legal conclusions interposed by counsel, not factual assertions by a party . . . ." (*Blue Ridge Ins. Co. v. Superior Court* (1988) 202 Cal.App.3d 339, 345; see §§ 2030(g), 2031(g).) The trial court overruled Truck's objections and imposed monetary sanctions for raising them. Once this happened, Truck was required to respond without objection. It did so under oath. The prior objections by its counsel did not purport to, nor did they, constitute its responses under oath. "[T]he appropriate focus for determining the propriety of the sanctions order is not [the party's] response to the [initial discovery], but its response to [the court's] order." (*Underwriters at Lloyd's London v. The Narrows* (Alaska 1993) 846 P.2d 118, 120 [reversing issue sanctions which resulted in $85 million judgment against carrier].)

Surgin's reliance on *Laguna Auto Body v. Farmers Ins. Exchange* (1991) 231 Cal.App.3d 481, is misplaced. (RB 23-24.) That case concerned a party's express continued assertion of objections after being ordered to respond without objection, its repeated admission that its responses were inadequate, and its failure to oppose a motion for terminating sanctions. This is not even close to what happened here. Here, in marked contrast, Truck (1) provided verified further responses *without objection* exactly as ordered, (2) consistently contended (and continues to contend) that its supplemental responses complied with the court's discovery orders, and (3) consistently opposed Surgin's motions for terminating sanctions, explaining both its understanding of the discovery and

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[46/] Truck does *not* contend, as Surgin asserts (RB 35), that a trial court's determination of discovery issues collateral to the merits of the action, such as a party's wilfulness in disobeying a discovery order, infringe on a party's right to a jury trial. Rather, the right to a jury trial is implicated where, as here, the trial court imposes sanctions premised on the disputed truthfulness of a party's *substantive* discovery response pertinent to the merits.

pointing to the evidence showing the responsiveness of its further responses. Contrary to Surgin's assertion (RB 24 & fn. 21), *Laguna Auto Body* did not use overruled initial objections to establish the inadequacy of subsequent verified responses submitted without objection.

● If it does nothing else, Surgin's continuing claim that it was entitled to invade the privileged domain of post-litigation communications between Truck and its counsel illustrates exactly how overreaching its discovery position has been. (See *Transamerica Title Ins. Co. v. Superior Court* (1987) 188 Cal.App.3d 1047, 1052-1053 [insurers entitled to assert attorney-client privilege in insurance bad faith suits].) Ironically, Surgin's claim is based entirely on Truck's protective *objection* that, if Surgin's discovery did seek privileged materials (as Surgin eventually claimed), the discovery was blatantly improper.[47/] Surgin, however, says that Truck's assertion of the objection proves there *must* have been responsive privileged documents, so Truck *must* have been lying—and violating a supposed order to produce clearly privileged material[48/]—when it said it had produced all responsive documents without including any privileged documents. (RB 26.)

What nonsense. As we have just demonstrated, a discovery objection is not the equivalent of a response under oath. Does Surgin seriously claim that a lawyer should not—indeed may not, on pain of terminating sanctions—assert a routine, prophylactic privilege objection (even though there are then no known documents) to avoid the potentially disastrous consequences of waiving the privilege if, for instance, a previously unknown privileged document happens to surface later? Maybe Surgin believes this, but no careful lawyer trying to protect his or her client's interests would

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[47/] Truck asserted the attorney-client privilege at the same time it *voluntarily agreed* to produce pre-litigation privileged correspondence. (JA 1043-1048.) The privilege objection made clear that, even though Truck was voluntarily waiving the privilege as to pre-litigation documents, it was not waiving the privilege across the board. (See *Owens v. Palos Verdes Monaco* (1983) 142 Cal.App.3d 855, 870 [disclosure of contents of one privileged communication does not waive privilege as to all communications on subject].) Proving exactly why such caution was necessary, Surgin is now quick to claim that Truck somehow waived the attorney-client privilege as to the *production* of communications from its counsel by failing to assert that privilege in its responses to a form *interrogatory* which, by definition, did not call for the production of anything. (RB 18, 28; see also discussion at page 71, *infra*.)

[48/] When resisting Truck's writ petition, Surgin apprised this Court that just the opposite was true, arguing that "[a]bsolutely no such order was entered." (RJN Exh. 2 p. 1.)

agree, and no court has ever so held. And even if a privilege objection were improperly interposed, the proper remedy (if any) would be the monetary sanctions that were, in fact, imposed here, *not* terminating sanctions.

- Surgin contends that, in response to the affirmative defense requests, Truck should have produced a privilege log of *privileged, post-litigation* documents. (RB 20, 26-27.) But Truck stated under oath that it had produced *all* responsive documents in response to the affirmative defense requests (JA 1664-66; RB 18); its counsel further stated that *there existed no privileged documents* responsive to such requests (JA 1749). Is it Surgin's idea that in order to avoid terminating sanctions, Truck was required to produce a privilege log listing documents that do not exist?

In any event, it is hard to imagine how post-litigation, unquestionably privileged documents could ever be responsive to requests that only seek production of documents supporting affirmative defenses. Even if such documents existed (contrary to Truck's repeated denials), a propounding party cannot reasonably expect—and a trial court cannot legitimately order—a privilege log of correspondence between a client and its trial counsel without first showing some colorable basis for intruding into an area so clearly private and presumptively off limits. (*Mitchell v. Superior Court* (1984) 37 Cal.3d 591, 600 [party may not be required to identify transmissions to it from its counsel since that might reveal litigation strategy]; *BP Alaska Exploration, Inc. v. Superior Court* (1988) 199 Cal.App.3d 1240, 1252 [no further showing necessary where party consistently asserts written reports are attorney work-product and opposing party makes no contrary showing]; *In re Couch* (Bankr. S.D. Cal. 1987) 80 Bankr.R. 512 [applying Evid. Code, § 917; held, no further factual showing necessary to establish attorney-client privilege where document request seeks correspondence and reports between insurer and its counsel in bad faith action against insurer].) But even if none of these insurmountable obstacles existed, a privilege is not waived by failure timely to provide a privilege log. (*Motown Record Corp. v. Superior Court* (1984) 155 Cal.App.3d 482, 492.)

- Surgin tries to twist a denial into admission by misquoting Truck. Surgin claims that Truck admitted the existence of responsive privileged documents by arguing in its Opening Brief

that "all withheld documents *responsive* to the defense request were 'indisputably' privileged." (RB 26, emphasis added, citing AOB 71.) Truck said no such thing. Instead, it merely said "there can be no possible prejudice from any failure to produce or identify indisputably privileged communications." (AOB 71.) The point Truck was making is that, even *if* there had been responsive privileged communications notwithstanding Truck's denial, Surgin still could never have been prejudiced by any failure to produce them because it would never have been entitled to get them in the first place. Not exactly an admission.

- Surgin claims that Truck failed "to *produce* 'privileged' documents in response to the report request" and "was *withholding* those reports in bad faith." (RB 28 & fn. 24, emphasis added.) This is disingenuous wordplay. What Surgin calls the "report *request*" was really a *form interrogatory*. (JA 1138.) "Interrogatories cannot be used, however, to force a party to produce documents or records in his or her possession for inspection or copying." (2 Weil & Brown, Civil Procedure Before Trial (Rutter Group 1994) § 8:993 at p. 8F-23.) Moreover, Surgin premised its renewed motion for terminating sanctions solely on a supposed failure to produce documents, not on any failure to respond to an interrogatory. (JA 2027.) Thus, terminating sanctions were not (and could not possibly have been) premised on any failure to respond adequately to the reports form interrogatory. (*Gonzales v. Superior Court* (1987) 189 Cal.App.3d 1542, 1545 ["Only the grounds specified in the notice of motion may be considered by the trial court"]; *Taliaferro v. Riddle* (1959) 167 Cal.App.2d 567, 570 [same].)[49/]

Although we could write volumes about other factual and legal liberties taken in the discovery portion of Surgin's brief, limitations of time and space constrain us to move on. Accordingly, we turn now to a detailed discussion of why—even assuming arguendo that Truck's

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[49/] In any event, there was no basis for a claim that Truck had not responded to the interrogatory. Truck's sworn response could not have been more direct: "No." (JA 5047.) Surgin's speculation that there *must* have been "reports" of the "incident" (RB 28) cannot overcome either Truck's sworn response or Truck's statement that any documents that might conceivably be called "reports" of the "incident" already had been produced as a part of Truck's production of its *entire* claims file. (JA 1747; see § 2030(f)(2).)

further responses were inadequate—the imposition of terminating sanctions was inappropriate, constituting a gross abuse of discretion.

C. The Trial Court's Discovery Orders Did Not Mean—And Certainly Did Not Unambiguously Mean—What The Trial Court And Surgin Later Said They Meant.

Even Surgin tacitly acknowledges the obvious—that due process does not permit punishment (much less terminating sanctions) without clear warning. (RB 29-31.) That is the problem here. The trial court's orders never said what Surgin and the trial court later claimed.

Surgin can say that "black" means "white" as much as it wants, but the meaning of the trial court's orders remains a question of law for this Court, not a matter of post-hoc discretion vested in Surgin or the trial court. (See discussion, *supra*, at p. 65.) As a matter of law, the discovery orders did not direct Truck to provide any discovery responses beyond the supplemental responses it made.

1. The Trial Court's Initial Minute Orders Did Not Create Any Discovery Obligations More Expansive Than Surgin's Formal Discovery Requests And Motions To Compel.

In moving to compel, Surgin narrowly construed its discovery requests. (See Appendix C; JA 1020, 1022, 1023, 1065, 1115.) The court granted *these* motions, not some other motions that were never made. (JA 1289, 1291, 1293, 1295.) Each of the trial court's discovery orders—issued without a hearing, and unaccompanied by any explanatory comment or discussion—consisted simply of checking a pre-printed "granted" box. (JA 1289, 1291, 1293, 1295, see JA 8612)

As a matter of law, the discovery orders could only have meant that Truck was required to produce those documents that Surgin's discovery and motions sought—for example, those manuals that Truck "used," "referred to or relied upon" in adjusting advertising injury claims. (E. g., *Cox v. Tyrone Power Enterprises* (1942) 49 Cal.App.2d 383, 389 ["the order granting (the motion) could be no more inclusive than such motion"; "the order must be construed within the limits set up in

the motion"]; *Western Greyhound v. Superior Court* (1958) 165 Cal.App.2d 216, 219 ["In construing an order, resort may be had to the notice of motion"].)

2. The Trial Court's Cryptic "Denial Without Prejudice" Cannot Properly Be Read As Requiring Further Discovery By Truck.

The trial court also held no hearing on Surgin's initial motion for terminating sanctions. The *entirety* of the trial court's order on that motion read: "The trial is continued to May 3, 1993 at 9:00 a.m. in Department 12. Discovery cut-offs shall be April 12, 1993. Motion is denied without prejudice as to terminating sanctions." (JA 2022.)

Although Surgin's motion had requested that issue and monetary sanctions be imposed (JA 1585-1586), the order said nothing about that request. The order also said nothing about (and suggested no resolution of) the conflicting discovery interpretations that had been advanced by Surgin and Truck. (Compare, e.g., JA 1785-1786 with JA 2021C.) Having *denied* Surgin's motion, albeit "without prejudice," the order cannot reasonably be read as holding that the motion was granted or that Truck's supplemental responses were found deficient.

Echoing the trial court (RT 72), Surgin claims that "denied without prejudice" was a "clear flag"—that it somehow meant that Truck's supplemental responses were deficient and implicitly warned that Truck "had another chance to comply." (RB 31.) But Truck was constitutionally entitled to more than semaphore or smoke signals from the trial court before the court forfeited Truck's constitutional right to defend itself. This Court has rightly criticized "attempts by judges, apropos of Carroll's Humpty Dumpty, to redefine words to mean what they wanted them to mean." (*ACL Technologies, Inc. v. Northbrook Property & Casualty Ins. Co.* (1993) 17 Cal.App.4th 1773, 1794, fn. 50.) Of course, "denied" cannot mean "granted." But, in the trial court's view, that's exactly what it meant. The problem is that the court never told Truck.

Surgin claims the trial court's continuance of the trial and discovery dates reflected an implicit endorsement of Surgin's position, since Surgin said it needed extra time to obtain the discovery that Truck was supposedly refusing. (RB 31.) What Surgin fails to mention is that Truck, while disagreeing with Surgin's reason (i.e., that Truck had obstructed discovery), *agreed*

to the requested continuance. (JA 1745.) That agreement, coupled with the court's "denied" order and its effective denial of Surgin's request for issue and monetary sanctions, suggests the opposite of Surgin's inference.[50] Hardly a "clear flag."

The task of explaining the parties' discovery obligations was the trial court's job. It was not Surgin's job or the clerk's job. (See footnote 50, *supra.*) If the court really wanted Truck to produce "all" its claims manuals, rather than the limited types of manuals requested by Surgin's discovery and discovery motion, or to produce or log all privileged attorney-client correspondence, then it should have said so in unmistakable terms. It never did—until it was too late.

3. Even The Death Knell Order Granting Terminating Sanctions Was Unilluminating As To What Was Required.

One of Surgin's more astonishing arguments is that the ultimate sanction was permissible because the *sanctions order itself* clarified Truck's discovery obligations. (RB 36-37.) According to Surgin, at the same time the trial judge was kicking Truck out of court, he was giving Truck clarification as to what was necessary to comply. (RB 36-37.) This is simply more law from the other side of the looking glass. To satisfy due process a party must be given clear notice of what has been ordered—affording it a *clear choice* between defined compliance and default. This must happen *before* sanctions are imposed, not after. (See *Greenup*, *supra*, 42 Cal.3d at p. 829.)

But even if after-the-fact clarification were somehow constitutionally permissible, that is not what happened here. When the trial court imposed terminating sanctions, it *still* did not provide Truck with a clear explanation of what had been expected or what Truck did that was wrong; and it gave no hint that, even though Truck's answer had been stricken, Truck could still do something to save itself from the civil death penalty that had just been imposed.

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[50] Surgin's January 15, 1993 demand letter advanced an expansive interpretation of the trial court's "denial without prejudice" order and purported to invoke the court clerk's authority to support its expansive interpretation. (JA 2384.) This confused things further. When Truck checked with the clerk, the clerk told Truck that Surgin's interpretation was "convoluted." (JA 2391-92.) And while Surgin chides Truck for contacting the court clerk to clarify the order (RB 31, fn. 28), it was *Surgin* who expressly invoked the clerk's authority in the first place.

Contrary to Surgin's contention (RB 37), the terminating sanctions order did not, in any meaningful sense, "end[] any confusion regarding Truck's discovery obligations." True, the trial court did finally hold a hearing, but its comments were limited at best. The most that could be gleaned was that Truck had done something wrong, that it had been given the maximum punishment, and that there had been a "gross misunderstanding." (RT 2-3, 10 [Feb. 9, 1993, hearing].)

Surgin argues that *the court's* order was adequately explained because *Truck* had an opportunity to argue its position and the matter had been fully briefed. (RB 32.) This is double-speak. The problem is not what the parties argued; their positions were clear (although Surgin's has proven ductile). The problem is that Truck was not informed of the *court's* views on the disputes at issue. For example, were terminating sanctions being imposed because Truck failed to furnish all the privileged communications with its trial counsel? Were Truck's supplemental responses found deficient? If so, how? The court never said. (See RT 1-10.)

The court's formal written order—issued later—provided no better clue. It simply stated that Truck failed to produce unspecified documents; it never explained how Truck went wrong. (JA 2476.) Truck asked for clarification (JA 2457-2460, 2469-2472), but at Surgin's urging, the trial court refused. (JA 2465-2468, 2474.)

4. The First Time The Trial Court Afforded Truck A Meaningful Revelation Of Its Intent Was At The Hearing On The Motion For Reconsideration.

It was not until several months later, at the May 4, 1993, hearing on Truck's motion for reconsideration, that the trial court finally said—*for the very first time*—that Surgin's January 15 letter was "exactly what the court meant." (RT 72.) This was the *first* meaningful indication of what the court expected—not one-word orders, not Surgin's interpretations, not the clerk's explanations.

Once Truck knew that the court had really meant to order production of "all written claims handling guidelines, claims procedure manuals and reports on this litigation by [trial counsel]," Truck's response was immediate. Even though its answer had already been stricken, within days Truck served Surgin with eight boxes of documents containing "all" its manuals. (JA 7577, see JA

7493-7497.) It also sought writ relief from this Court (RJN Exh. 1) with respect to the court's apparent adoption of that portion of the January 15 letter that demanded production of "all" privileged communications with Surgin's trial counsel (JA 2383-2384). In response to the writ petition, however, Surgin unabashedly and unconscionably changed its position, apprising this Court that "[a]bsolutely no such order [to produce attorney-client privileged documents] was entered" and that "Judge Jameson never 'actually directed Truck to produce "all reports on this litigation by Lichtman & Bruning and Greines, Martin, Stein & Richland."'" (RJN Exh. 2 pp. 1, 6.)

5. Surgin's Invention Of An Uncommunicated "Last Chance" Opportunity For Truck To Obtain A Rescission Of Sanctions Is A Hoax.

The trial court's supposed "finding" that "Truck still could have corrected its misconduct" and thus avoided the terminating sanctions (see RB 37) is another Surgin after-the-fact invention. The "finding" is something Surgin gratuitously inserted into its proposed judgment *without the trial court's ever having said a word about the issue.* The "finding" said that the court would have vacated Truck's default if Truck had simply complied with Surgin's and the court's interpretation of the discovery orders—if it provided "all" claims manuals plus a privilege log—at any time before September 1993. (JA 7480.) The problem is that this supposed "opportunity" *was never communicated to Truck* until Surgin submitted its proposed judgment—months after the supposed September deadline.

But even this invented "opportunity" was illusory, as Truck was soon to learn.

As soon as the court had clarified what it expected Truck to do (i.e., at the May 4, 1993 hearing), Truck immediately complied. As noted above, it produced eight boxes of documents containing every conceivable manual and written claims handling guideline (even though Truck continued to maintain that it did not use or rely on them in adjusting advertising injury claims), as well as a privilege log of *every* attorney-client communication between Truck and its counsel (accompanied by an explanation that none had ever been called for by or was responsive to *any* discovery request, just as Truck had always said). (JA 7493-7497, 7577, 7623-7644.) This

compliance occurred on May 11, 1993 (*ibid.*)—well before the September 1993 "deadline." Was this enough? No way.

When Truck established that it had complied with the September 1993 deadline in its post-judgment motions (JA 7576-77, 7623-50, 8022-8023 & fn. 6), Surgin realized the defect in its ploy and simply changed the rules. During the hearing on Truck's motions, Surgin, without affording any prior notice to Truck, simply whipped out an amended judgment which retroactively advanced the invented last-chance deadline from the September date (the date Truck had shown it had met) to an earlier date—the May 4, 1993, hearing date on the motion for reconsideration, a date that Truck could never have met because that was the *first date* on which Truck learned from the court what it really meant by its prior orders. (JA 8293). Once again, *the trial court had never said anything on the subject*. Nonetheless, the court signed the amended judgment minutes later, thus magically cutting four months off the last chance deadline. (RT 360-365.)

And, as if this weren't enough, the trial court, acting *sua sponte*, then struck from the record and ordered Truck to remove the eight boxes of documents Truck had produced and later lodged with the Court, thus depriving Truck—and this Court—of any record of Truck's compliance with the original last chance "deadline." (JA 8541.)

6. As A Matter Of Due Process, Terminating Sanctions May Not Be Imposed On The Basis Of Orders That Did Not Clearly Direct Truck To Produce The Documents Allegedly Withheld Or, At Most, Were Ambiguous On The Issue.

The meanings Surgin ascribes to the trial court's various orders—such as "denied without prejudice" really meaning "granted"—"take us from the world of reality into the wonderland of clairvoyance." (*Tarasoff v. Regents* (1976) 17 Cal.3d 425, 452, Mosk, J., dissenting.) The problem is not just that the trial court's orders did not say what the trial court and Surgin later claimed they did, but also that Truck *reasonably* understood them *clearly* to mean the exact opposite, and its counsel said so under oath.

While due process may not require a court to explain every "nuance" of its orders (RB 29, fn. 25), a court is obligated *before* imposing sanctions—especially terminating sanctions—to give

a party fair warning of what it must do and an opportunity to comply. No case has ever upheld such severe sanctions on anywhere near such an abbreviated, cryptic, or clouded record; whenever serious sanctions are affirmed, it is because the trial court gave *explicit* direction and an undeniable opportunity to comply.[51] That never happened here.

While Surgin—with ever-increasing bravado—was making ever-expanding claims about what the court's orders supposedly meant, the court itself never directly said what it expected until May 4, when it reimposed terminating sanctions immediately after granting Truck's motion for reconsideration. Whatever may have been the court's reasons for its uninformative approach, Delphic utterances interpreted by one's adversary are hardly enough to satisfy due process. (See AOB 60-61.)[52]

D. Truck Could Not Wilfully Have Failed To Comply With Discovery Orders That The Uncontradicted Evidence Demonstrated Were Not Understood. Section 473 Mandates That Truck Should Not Suffer For The Mistake Or Inadvertence Of Its Trial Counsel In Failing To Divine The Court's True Intent..

Surgin wants this Court to disregard the objective facts revealing Truck's understanding of the meaning of the trial court's orders and of its discovery obligations in favor of Surgin's speculation that Truck must have acted with subjective bad faith. In marked contrast to Surgin's speculation stands the sworn testimony of Truck's then trial counsel, Robert Bruning. He testified

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[51] E.g., *Johnson*, *supra*, 28 Cal.App.4th 613, 621, fn. 6 ["at least fifteen (15) court hearings," repeated warnings, and counsel's express acknowledgement of what was required]; *Manzetti v. Superior Court* (1993) 21 Cal.App.4th 373, 377-378 [*monetary* sanctions after two hearings; order to inspect property included videotaping and photographing]; *Morgan*, *supra*, 192 Cal.App.3d at pp. 981-983 [two hearings, *explicit* order that supplemental responses insufficient and allowance of additional time to comply]; *Founding Church of Scientology v. Webster* (D.C. Cir. 1986) 802 F.2d 1448, 1459, fn. 15 [trial court made "crystal clear" what was expected]; see also authorities discussed at AOB 60-61.

[52] Surgin's attempts to distinguish the authorities Truck cites are fanciful. (RB 29 & fn. 25.) For example, Surgin claims *R.W. Intern. Corp. v. Welch Foods, Inc.* (1st Cir. 1991) 937 F.2d 11, only addressed a "mere scheduling order." In fact, that case is directly on point. It concerned an "order[] [that] the plaintiffs . . . produce . . . all documents regarding their claimed damages." (*Id.* at p. 14.) Surgin's other attempted distinctions are equally unavailing.

that he alone interpreted Surgin's discovery requests and the trial court's orders and, therefore, that any mistaken or erroneous responses were his sole responsibility. (JA 2574-2589, 3082-90.) He testified he *never* understood either the discovery or the orders to mean what Surgin and the trial court later interpreted them to mean. (JA 2575-2589.) There is no evidence that contradicts his testimony.

In these circumstances, section 473 *mandates* relief from default. However, Surgin argues that "Truck's counsel could not, in good faith, have believed that Truck's conduct was an appropriate response to Truck's discovery obligations." (RB 36.) Once again, this is unsupported supposition contradicted by the record. But even if it were true, it would not change the result. At most, it is a claim of *inexcusable* neglect. However, section 473 "*require[s]* the court to grant relief if the attorney admits neglect, even if the neglect was *inexcusable*." (*Metropolitan Service Corp. v. Casa de Palms, Ltd.* (1995) 31 Cal.App.4th 1481, 1487, emphasis in original; see *Beeman, supra*, 216 Cal.App.3d at pp. 1604-1605 & fn. 14 [same].)

Surgin urges that the trial court could unilaterally reject the Bruning declaration as not credible. But Section 473 requires the trial court to vacate the default when presented with an attorney's declaration of fault "unless the court *finds* that the default or dismissal was not in fact caused by the attorney's mistake, inadvertence, surprise or neglect." (§ 473, emphasis added.) True, the trial court here did not accept Mr. Bruning's explanation. But findings require *evidence*, not mere disbelief of testimony. (See *Oldenburg v. Sears, Roebuck & Co.* (1957) 152 Cal.App.2d 733, 742 [a trier of fact's disbelief "of a witness who testifies to the negative of an issue does not of itself furnish any evidence in support of the affirmative of that issue, and does not warrant a finding in the affirmative thereof unless there is other evidence in the case to support such affirmative"], quoting *Marovich v. Central Calif. Traction Co.* (1923) 191 Cal. 295, 304.) There is no evidence here except the declaration of Truck's attorney regarding his exclusive responsibility for interpreting, and his understanding of, Surgin's discovery and the court's discovery orders.[53/]

[53/] For this reason, Surgin's reliance on *Johnson v. Pratt & Whitney Canada, Inc., supra*, 28 Cal.App.4th at pp. 622-623 (RB 36) is misplaced. There, the attorney's declaration was flatly contradicted by his own prior representations to the court that his client was responsible for the failure to comply with discovery.

Surgin's claim that trial counsel's acceptance of responsibility came "too late" (RB 35-36) is equally untenable. Although Surgin does not explain what it means by "too late," the record plainly shows that Truck's request for section 473 relief was timely. (JA 2575-2589 [counsel provides facts of his responsibility in connection with motion for reconsideration]; JA 8300 [Truck makes offer of proof of motion for mandatory relief on day amended judgment is entered]; § 473 [motion for mandatory relief from default based on attorney neglect may be made anytime within six months after *entry of judgment*]; *Metropolitan Service Corp.*, *supra*, 31 Cal.App.4th at p. 1488 [trial court required to afford mandatory relief whenever "moving papers contained all that was required to show defendants' entitlement to mandatory relief"; § 473's 6-month deadline for mandatory relief is not subject to any "diligence" requirement].)

E. The Terminating Sanction Was Totally Out Of Proportion To The Limited Discovery At Issue, Particularly Given Truck's Undisputed Record Of Compliance With Other Discovery.

The United States Supreme Court has recognized that, as a matter of due process, a discovery sanction "must be specifically related to the particular 'claim' which was at issue in the order to provide discovery." (*Insurance Corp. of Ireland v. Compagnie des Bauxites* (1982) 456 U.S. 694, 707 [102 S.Ct. 2099, 2107, 72 L.Ed.2d 492].) This rule was echoed by the Texas Supreme Court:

> "In our view, whether an imposition of sanctions is just is measured by two standards. First, a direct relationship must exist between the offensive conduct and the sanction imposed. This means that a just sanction must be directed against the abuse and toward remedying the prejudice caused the innocent party. . . . [¶] Second, just sanctions must not be excessive. The punishment should fit the crime." (*Transamerican Natural Gas Corp v. Powell* (Tex. 1991) 811 S.W.2d 913, 917.)

Here, the punishment dwarfs the perceived crime. While trial courts have substantial discretion in fashioning appropriate sanctions, striking Truck's answer was an abuse of discretion. It went far beyond remedying any perceived discovery abuses. It violated due process.

1. The Terminating Sanctions Did Not Bear A Reasonable Relationship To Any Supposed Discovery Abuse.

Surgin has no real response to the fact that the terminating sanctions vastly exceeded the scope of the discovery violation that the trial court found Truck to have committed. Instead, Surgin manufactures a response that is totally unsupported by the record.

Surgin attempts to justify terminating sanctions by asserting that "the *contention* and defense requests went to the *entirety of Surgin's claims*—Truck's *denial of* and defenses to the complaint." (RB 34, emphasis added.) This sounds reasonable enough at first blush. But it is false. *Surgin does not contest that Truck complied with the contention requests!* (See RB 18 [admitting Truck produced documents responsive to the contention requests]; 22-28 [Surgin's discussion of supposedly sanctionable conduct does not mention contention requests]; see JA 1750-1751.) In fact, not a single one of Truck's supposed discovery defalcations went to the whole of this case. The affirmative defense requests were, by definition, limited to Truck's affirmative defenses; Surgin concedes that the remaining disputed requests—the advertising injury manuals request and the reports form interrogatory—were directed to a *single issue*: "whether Truck properly handled Surgin's request for a defense and coverage." (RB 34.) Hardly "the entirety of Surgin's claims."

Even if Truck actually had engaged in all of the sanctionable conduct Surgin asserts (a gigantic "if"), due process requires that, at most, any sanction should have focused solely on the limited subjects of the disputed discovery: Truck's affirmative defenses, the reasonableness of Truck's claims-handling procedures, and Truck's compliance with those procedures in handling Surgin's claim. *None of these matters goes to the entirety of Surgin's case.* Far from it. They have nothing whatever to do with any of the numerous other issues discussed in the Opening Brief, such as the existence of a duty to defend; the appropriate amount of damages; the whole question of punitive damages; the unpleaded events Surgin proffered at the default prove-up; Surgin's own

failure to cooperate or to submit its defense bills; and so on. (See AOB 68.) Nor do they have anything to do with any issues implicated by the "agreement to defend" theory Surgin now relies on—what did Truck agree to do; how, if at all, did Surgin rely on any agreement; was any reliance reasonable or detrimental; et cetera.

With respect to each asserted discovery defalcation, sanctions far short of terminating sanctions could readily have been tailored to fit the crime. Consider, for example, the following:

- Since affirmative defenses never go to the heart of a plaintiff's case (rather, they involve the introduction of new matter that, if proved, would entitle defendant to win), there is no conceivable way that striking a party's answer could ever be considered appropriate punishment for violating discovery about affirmative defenses. Reasonable, properly tailored sanctions on the affirmative defense discovery might have precluded Truck from introducing any of the supposedly withheld documents in support of its affirmative defenses.[54/] Alternatively, the court might have stricken Truck's affirmative defenses.

- Reasonable, properly tailored sanctions on the claims-handling issues might have prevented Truck from offering evidence on the subject or, perhaps, might have established those specific issues against Truck—for instance, by establishing that Truck had specific procedures for adjusting advertising injury claims and that it violated those procedures.

Although these would be serious sanctions indeed, they would at least have satisfied due process. They would have borne a direct relationship to the asserted discovery violation, yet they would still be a far cry from taking away Truck's ability to defend itself on the many other important issues involved in the litigation—issues that had nothing to do with the discovery in question.

[54/] Truck did, of course, produce a substantial number of documents on which it premised its affirmative defenses.

2. Terminating Sanctions Were An Abuse Of Discretion Given The Record As A Whole.

Even if it were somehow appropriate to impose terminating sanctions for a limited failure to comply with discovery, they were an abuse of discretion here. Judicial discretion is "not unfettered"; it must be exercised "in a manner to subserve and not to impede or defeat the ends of substantial justice." (*Bettencourt v. Los Rios Community College Dist.* (1986) 42 Cal.3d 270, 275.) Like any other exercise of discretion, "sanctions must be guided by reasoned analysis of the purposes sanctions served and the means of accomplishing those purposes. . . . *Rendition of default judgment as a discovery sanction ought to be the exception rather than the rule.*" (*Transamerican Natural Gas Corp., supra*, 811 S.W.2d at p. 917 & fn. 6, 919, emphasis added; accord, *McGinty v. Superior Court* (1994) 26 Cal.App.4th 204, 210.)

Surgin cannot dispute that a party's compliance with substantial other discovery and the absence of prejudice to the propounding party are highly relevant factors in evaluating the propriety of terminating sanctions. (*Deyo v. Kilbourne* (1978) 84 Cal.App.3d 771, 796; *Fjelstad v. American Honda Motor Co.* (9th Cir. 1985) 762 F.2d 1334, 1342-1343; see also *City of Sacramento v. Drew* (1989) 207 Cal.App.3d 1287, 1297-1298 [in exercising judicial discretion court must consider all relevant factors].) Here, the *undisputed* record establishes:

- Truck voluntarily provided very substantial discovery to Surgin, including its *entire claims file*. It even provided something that most plaintiff's lawyers can only dream about getting: an indisputably privileged, pre-litigation coverage opinion advising Surgin to defend some of the Alcon actions. (JA 3265-4395, 3307-31.)
- The claimed discovery failures did not go to the whole of the case, but rather were limited to discrete issues.
- The materials that Truck supposedly withheld were at most only tangentially relevant (manuals *not* "used," "referred to or relied upon" in adjusting the advertising injury claims at issue here), or were protected by the attorney-client privilege. But boxes of these manuals were produced once Truck learned the court wanted them produced.

- Evidence or issue preclusion orders tailored to the allegedly withheld evidence would have eliminated even the remotest possibility of prejudice to Surgin.

Ignoring these significant considerations, the trial court imposed the civil death penalty. Surgin seeks to justify this unreasonable and unjust punishment as a deterrent to "unrepentant discovery abuser[s]." (RB 33.) But, as we have shown, the record belies this characterization, however slickly and deceptively Surgin has packaged it. Moreover, "[a]lthough punishment and deterrence are legitimate purposes for sanctions [citations], they do not justify trial by sanctions." (*Transamerican Natural Gas Corp.*, *supra*, 811 S.W.2d at p. 918.) In addition to the goal of deterrence, there is also a real need to ensure that the sanctioned party receives due process. (E.g., *National Hockey League v. Metropolitan Hockey Club, Inc.* (1976) 427 U.S. 639, 640-43 [96 S.Ct. 2778, 2779-2781, 49 L.Ed.2d 747] [court upholds terminating sanctions where crucial discovery *never* provided despite express discovery deadline, "several admonitions by the Court and promises and commitments by the plaintiffs," and "warnings that their failure to provide certain information could result in the imposition of sanctions"]; *Sauer v. Superior Court* (1987) 195 Cal.App.3d 213, 230 [affirming narrowly tailored evidentiary sanction]; *Morgan v. Southern California Rapid Transit Dist.*, *supra*, 192 Cal.App.3d at pp. 981-982 [upholding terminating sanctions where court held three hearings and twice imposed lesser sanctions].)

Affirmance in this case would validate *in terrorem* case management and deceptive and overreaching discovery. It would put responding parties at risk of terminating sanctions whenever they reasonably disputed the propriety of a discovery request or disputed their opponent's interpretation of a discovery request or order. It would reward propounding parties for overreaching and for exploiting and abusing the discovery process, a practice that should be deplored as much as obstructionist discovery responses. It would, in short, utterly compromise the entire discovery process.

CONCLUSION

The unprecedented parade of prejudicial errors on fundamental issues produced an astounding $57.8 million default judgment and an outrageous miscarriage of justice. The judgment is an abomination that tarnishes the meaning of justice. Individually and cumulatively, the errors overwhelmingly mandate reversal.

The reversal should be with directions to enter judgment for Truck because of Surgin's failure to plead any cognizable cause of action or to prove any recoverable damages. At a minimum, the case should be reversed and set at large for a contested trial on the merits before a different superior court judge. In no event may any default judgment exceed the $270,000

jurisdictional limit mandated by statute; in fact, any supportable judgment may not permissibly exceed even a small fraction of that amount.

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Respectfully submitted,

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