

2003

Gary Machan v. Unum Life Insurance Company of America : Brief of Appellant

Utah Supreme Court

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IN THE SUPREME COURT

STATE OF UTAH

GARY MACHAN,

Plaintiff/Appellant,

vs.

UNUM LIFE INSURANCE COMPANY
OF AMERICA,

Defendant/Appellee.

No. 20030789-SC

BRIEF OF PLAINTIFF/CO-APPELLANT GARY MACHAN

Certification Order from the Honorable Paul G. Cassell,
United States District Court, District of Utah, Central Division

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UTAH SUPREME COURT

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PAT BARTHOLOMEW
CLERK OF THE COURT

IN THE SUPREME COURT

STATE OF UTAH

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LIST OF PARTIES TO THE PROCEEDINGS

All parties to the proceedings are identified in the caption on appeal.

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JURISDICTION

This Court has jurisdiction over the certification from the United States District Court pursuant to Utah Code Ann. § 78-2-2(1) and Rule 41, Utah Rules of Appellate Procedure.

ISSUES PRESENTED

The issues certified by the United States District for the District of Utah are:

1. In a first party insurance situation, may an insured recover consequential damages, other than attorney's fees, for breach of the express terms of an insurance contract? If so, what are the consequential damages that are recoverable for breach of the express terms of an insurance contract and how are they distinguished from the consequential damages for breach of the implied covenant of good faith and fair dealing that are recoverable under *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 801 (Utah 1985)?

Standard of Review: Determining the scope of damages under a cause of action is a question of law. *Billings v. Union Bankers Ins. Co.*, 918 P.2d 461 (Utah 1996).

2. Did Utah Code Ann. § 31A-26-301, entitled "Timely Payment of Claims," allow a private cause of action by the insured against his or her insurer for violation of the statute in 2000?

Standard of Review: Whether a statute creates a private cause of action is a question of law. *Miller v. Weaver*, 2003 UT 12, 66 P.3d 592.

CONSTITUTIONAL PROVISIONS, STATUTES, AND RULES

U.C.A. § 31A-26-301 (effective in 2000), attached as Addendum 2

U.C.A. § 31A-26-301 (as amended in 2002), attached as Addendum 3

STATEMENT OF THE CASE

Nature of the Case, Course of Proceedings and Disposition in the Court Below

This case arises out of the failure of defendant UNUM Life Insurance Company of America to pay disability benefits to plaintiff Gary Machan pursuant to the terms of his disability income insurance policy.

In October 2000, Machan filed a Complaint against UNUM in the Third Judicial District Court in and for Salt Lake County, State of Utah. The case was later removed to the United States District Court, District of Utah, Central Division, pursuant to diversity jurisdiction.

UNUM filed a motion for summary judgment and, after briefing and oral argument, the Hon. Paul G. Cassell determined that the certified issues were unsettled questions under existing Utah law. Accordingly, Judge Cassell issued an Order of Certification on September 22, 2003. R. 149 (attached hereto as Addendum 1). This Court issued an Order of Acceptance on October 30, 2003.

Facts

Plaintiff Gary Machan (hereinafter “Machan”) received his MBA degree from Brigham Young University in 1969. R. Exh 17, bates UMAC173.¹ For more than twenty years, he was a CEO and corporate executive of various companies involved in development, construction and management of properties throughout several western states. Some of his more notable projects include developing and constructing Brickyard Plaza, Woodland Towers, Cottonwood Medical Center, and Lindberg Plaza at the International Center. R. Exh 26, pp. 19-20.

In 1988, Machan purchased a disability insurance policy from defendant UNUM. Unlike typical (“any occupation”) disability policies, Machan paid a higher premium for what is commonly referred to as an “Own Occupation” policy. Under this type of policy, an insured is entitled to benefits if he becomes unable to perform the material and substantial duties of his own occupation in the usual and customary way, even if he is able to engage in some other occupation. R. 49, bates UGIB 380.

Machan’s policy has a common provision where disability benefits are paid if the insured falls within either of the following definitions: (1) “total disability,” and/or (2) “residual disability.” “Total disability” is defined:

“Total disability” and “totally disabled” mean injury or sickness restricts [sic] the Insured’s ability to perform the material and substantial duties of

¹ The Record submitted to this Court by the federal court clerk does not specify a citation number for the exhibits that were attached to plaintiff’s pleadings. Rather, the exhibits were placed in three expanded folders entitled, “Exhibits # 1 of 3”, “Exhibits # 2 of 3”, and “Exhibits # 3 of 3”. Plaintiff will therefore cite to the original exhibit numbers in the record.

his regular occupation to an extent that prevents him from engaging in his regular occupation.

“Regular occupation” means the Insured’s occupation at the time the Elimination Period begins. If the Insured engages primarily in a professionally recognized specialty at that time, his occupation is that specialty.

R. Exh 3, bates PL00005-6.

UNUM marketed these “Cadillac” Own Occupation policies to highly paid professionals, such as corporate executives, doctors, and lawyers, to provide coverage for disability from their specific occupations (including their areas of specialty). For example, an orthopedic surgeon who could no longer perform surgery might be totally disabled under an “Own Occupation” policy, even though he or she could still work in some other area of health care. R. Exh 49.

Machan continued to pay the premiums on his Own Occupation policy for more than a decade. In early 1999, Machan was diagnosed with coronary artery disease and underwent coronary artery bypass grafting in March 1999. Until the surgery, Machan was engaged full-time in his occupation. R. Exh 6, pp. 100-103.

Unfortunately, Machan suffered serious complications as a result of the surgery, in particular mild vessel eschemic disease in his brain. Over a matter of months, the brain injury led to cognitive deficits and severe mental illnesses that UNUM now, after two years of litigation, acknowledges rendered Machan fully disabled.² R. Exh 31.

² The type of mental deficiencies and illnesses suffered by Machan are not uncommon after open heart surgery. His eschemic brain injury was verified objectively by MRI studies (R. Exh 14), by psychological testing, and by the professional judgment of his treating physicians and therapists. R. Exh 10, pp. 215-222; Exh 22, pp. 40-42, 65-66, 73-

After March 1999, Machan was never able to return to the work he did before. His prior annual earned income plummeted from \$200,000 or more to little or nothing after his surgery. R. Exh 6, pp. 55-57.

By the summer of 1999, Machan experienced obvious cognitive deficits and reduced executive function in his brain. R. Exhs 7, 8 and 9. He also suffered from psychological problems, including severe depression and anxiety. R. Exh 23, bates UMAC 137-138,161-162; and Exh 11 at 139-141, 155-156. From that time, his symptoms have worsened and he has never returned to productive work. *Id.*

In March 1999, Machan filed a notice of claim for disability benefits due to his heart condition. UNUM initially agreed to pay for two weeks of benefits beyond Machan's 120-day elimination (waiting) period. When Machan asserted that more was owed under the contract, UNUM offered to pay two additional months of benefits, but only if Machan fully and completely released all other claims for benefits, which Machan refused to do. R. Exh 16, pp. 156-164. UNUM denied any further benefits.

By the spring of 2000, Machan's cognitive and psychological deficits had become the predominant cause of his disability. As permitted by the Policy, Machan filed another Notice of Claim in April 2000 based upon his mental disabilities.³ R. Exh 17.

74, 83-88, 90-92, 98-104. His treating doctors, Drs. Traub and Lambert, and Dr. Linda Gummow, an expert neuropsychologist, unanimously agreed that plaintiff was not capable of returning to his prior occupation or any other meaningful occupation since his heart surgery. *See*, for example, R. Exh 10, pp. 155, 176-177 and 215-222; Exh 22, pp. 38-42; Exh 12; and Exh 13, p.155.

³ UNUM's Policy recognized mental incapacity as a legitimate basis for disability. "Sickness" that may form the basis of a covered disability is defined in the Policy as "a

At the time that Machan submitted his disability claims, certain duties applied to the handling of claims, including, among other duties: (1) thoroughly and promptly investigating the claims, which would include a proactive investigation, not just waiting for the insured to send information (R. Exh 4, bates UCCM 0008; Exh 20⁴, pp. 88-93), and (2) a thorough, fair, and objective evaluation of each claim, which would include resolving reasonable doubts in favor of the policy holder and “exploring reasonable theories which support payment of the benefits . . .” *Id.*

There is substantial evidence, including expert testimony, that UNUM breached these and many other duties, as described in detail in Plaintiff’s Opposition to Motion for Summary Judgment. R. 135, pp. xxvi - xxxvii. Despite UNUM’s extensive wrongful conduct, the trial court, though deferring a formal ruling, indicated that it was inclined to grant summary judgment on most of plaintiff’s causes of actions because UNUM had hired Dr. Peter Strang, an allegedly independent doctor.⁵ Apparently, the trial court felt

mental or physical illness or condition which has been diagnosed or treated.” R. Exh 3, bates PL 0005. UNUM’s claims manual defines “limitations” on an insured’s ability to perform the duties of his own occupation as “the mental or physical functions he cannot do.” R. Exh 4, bates UCCM0035.

⁴ Exh 20 is comprised of both the March 7, 2001 denial letter and the deposition of Chapman, UNUM’s claims person who handled plaintiff’s claim.

⁵ UNUM often uses Dr. Strang as a so-called “independent” doctor to perform “cold file” reviews. The evidence demonstrated that he is far from independent. Dr. Strang, who makes approximately \$250,000 a year from UNUM, spends at least one day a week in UNUM’s claims office doing cold file reviews, does very little clinical work, does 40% of his practice for UNUM, and has a bias against the claimant. He uses UNUM employees to prepare his report on UNUM stationary, keeps no notes or file on the patient, uses UNUM’s address, fax and telephone number for responses from third parties and uses UNUM’s acronyms in his report. R. Exh 45, pp. 5-27; Exh 46, pp. 8-14, 22-25,

compelled under *Prince v. Bear River Mutual Ins Co.*, 2002 UT 68, 56 P.3d 524, to rule that because of Dr. Strang's involvement, UNUM's position was fairly debatable and, accordingly, in spite of egregious conduct, that all claims except breach of contract and perhaps breach of section 31A-26-301, Utah Code Ann. (assuming there is a private cause of action under this statute), must therefore fail. R. Tr. 7/29/03, pp. 3-4. Referring specifically to the *Prince* case, the trial court concluded that if there is a fairly debatable issue, "these other kinds of causes of action that you're talking about topple over like a set of dominos, sort of all or nothing" *Id.* p. 26.

After issuing its denial letter on November 3, 2000, UNUM closed its file even though Machan's claim was still pending and he had commenced litigation. R. Exh 20, pp. 293-294. Closing a file has special significance to UNUM because it terminates the posted reserve amount and helps meet certain "reserve reduction" goals. Each new and pending claim has a reserve amount allocated to it. R. Exh 41, pp. 16-18, 24. When the claim is terminated, either by denial or some other resolution, the file is generally closed and the reserve amount allocated to that claim is subtracted from the collective total. *Id.* A denial of a new or pending claim was one way to meet improper reserve reduction expectations that UNUM imposed on claims personnel. *Id.* at 31-41.

As articulated by various UNUM witnesses, UNUM had, for many years, implemented arbitrary and wrongful reserve reduction goals, sometimes referred to as "expectations" or "targets." These goals were designed to increase the company profits

28-31, and Exh 47. Plaintiff also presented evidence from experts that Dr. Strang was a "hired gun" who gave predictable opinions for UNUM. R. Exh 39, p. 5.

by arbitrarily reducing reserves through closing files and terminating claims. (R. Exh 32 pp. 1603-1604, 1614-1621, 1625-1629, 1636-1660, 1714-1733, 1831; Exh 41, pp. 28-41.

Tremendous pressure is placed on claims personnel from upper management to meet these goals, including the employee's performance evaluations, pay, promotions, etc. In addition to creating conflicts of interest, these wrongful goals were foul because they require the reduction of claim payments or denial of claims for reasons of company profit and the adjuster's personal gain (bonus, etc.) rather than on the substance of any given claim. R. Exh 32, pp. 1603-1604, 1614-1621, 1625-1629, 1636-1660, 1714-1733, 1831; R. Exh 34; R. 135, pp. xxxvii-xlvii, and R. 139.

UNUM's closure goals were arbitrary and not dependent upon the merits of the pending claims. They were determined by a calculation nicknamed "the Arnold theory," in which claim termination goals were computed by taking the total number of new claims and subtracting the reopened reserve amounts. The balance was what Tim Arnold, head of the UNUM claims department, expected to be terminated or "recovered". R. Exh 32 at 1653. Even when a vice president over disability claims told Arnold there were no other claims to close, he instructed her to "go back to my unit and find the additional closures." *Id.* at 1652, 1714-20.

Meeting reserve reduction goals was particularly problematic in the area of non-cancellable ("noncan") individual disability policies like Machan's because in 1994, UNUM stopped selling them. R. Exh 41 at 18-20. After 1994, the number of existing noncan policies continued to decrease because policies would lapse each year for various reasons. *Id.* The number of new claims from these decreasing noncan policies was

correspondingly decreasing over the years since 1994. *Id.* Because of this decrease, the increasing expectations to reduce total reserve dollars on claims from these policies created even greater pressure to terminate otherwise valid claims.

Plaintiff's expert, Stephen Prater, confirms this scheme based on his extensive experience and research regarding UNUM and UNUMProvident, and addresses why these performance goals run afoul with the industry standards. R. 135, p. xlvii; Exh 33. Another expert, Barbara Paull, outlines in detail the violations of UNUM's internal and industry standards in her expert report and deposition through UNUM's inadequate and untimely investigation and a biased evaluation. R. Exh 39; and R. Exh 40. She further testifies that she could not find a reasonable basis, based on claims practices, for the denial of plaintiff's claim, and that any reliance on Dr. Strang was improper since he was not an "independent" nor unbiased doctor. R. Exh 39, pp. 5-7; Exh 40, pp. 190-93.

A more detailed description of UNUM's wrongful corporate scheme, together with quotes and citations, is set out in Plaintiff's Opposition to Motion for Summary Judgment, R. 135, pp. xxxvii – xlvii.

Partly from the financial stress caused by his disability, compounded by UNUM's refusal to pay any benefits and the distress from the resulting litigation, Machan's psychological conditions worsened. *See* R. Exh 10, p. 235; Exh 12 and Exh 15. He was forced to use his savings and consume his assets to exist. R. Exh 6, pp. 170-175.

Machan's treating doctors and expert agree that in all likelihood he will be unable to have any significant gainful employment for the rest of his life. R. Exh 13, pp. 155; Exh 10, pp. 217-222; Exh 12, pp. 19-20. They further agree that, had he not suffered the

financial stress from the lack of disability income, exacerbated by the emotional distress associated with having to fight with UNUM and to engage in protracted litigation, he would likely have been able to at least return to some form of gainful employment, though not his prior occupation. R. Exh 12, pp. 19-20.

In spite of all of the evidence available to UNUM regarding Machan's disability, UNUM continued to deny his claim, issuing a final denial letter on March 7, 2001. R. Exh 20. The specific basis for UNUM's denial of plaintiff's claim was tenuous and appeared to be a pretext.⁶

The case was set for trial September 9, 2002 (trial was later continued to September 2003). In August 2002, UNUM unexpectedly announced that it had decided to pay Machan's claim for benefits. In explaining this sudden reversal, UNUM stated that after a review of "recently submitted materials," it had determined that benefits were owing. UNUM wrote: "The recent information substantially supports Mr. Machan's claim" R. Exh 31. (Oddly, however, nothing had been submitted to UNUM recently. Machan had not submitted anything for many months, and virtually all information

⁶ For example, UNUM denied the entire claim because: (1) it couldn't determine the starting date of the disability, even though its claim file consistently refers to the start of disability as March 12, 1999 (the approximate time plaintiff's heart surgery); (2) there was no "objective data" to substantiate the mental illnesses, even though the policy does not require objective proof, nor is objective proof commonly available with mental illnesses; (3) it couldn't determine plaintiff's occupation, even though its own vocational consultant Robert Violetta concluded after researching the issue over a year before the denial letter, "it is my opinion that the preponderance of information on file indicates that Mr. Machan's occupation corresponds to construction manager," and (4) because Machan revoked his medical authorization to UNUM when he filed his lawsuit. R. 135 pp. xxxii-xxxv.

supporting Machan's claim had been submitted more than a year before UNUM's August 16, 2002 letter.)

UNUM paid the past benefits under a reservation of rights which not only reserved UNUM's right to revoke future benefits, but also allowed UNUM to recover back what it had paid to plaintiff. R. Exh 4, bates UCCM0073. Furthermore, UNUM did not pay the cost of living increases, reimbursement of premiums under the waiver of premium provision of the policy, interest, and other benefits owed under the policy. Shortly before filing its motion for summary judgment, however, UNUM finally paid most of those additional amounts (without interest).

The specific mechanisms of UNUM's breaches and wrongful conduct are not at issue in this appeal. This background, however, is important to understand the context of why these two issues were certified and how they relate to the certified issues.

SUMMARY OF THE ARGUMENT

1. The law in this state has always been that a defendant who breaches a contract is liable for damages that were reasonably foreseeable or within the contemplation of the contracting parties ("consequential damages"). That this basic principle extends to breaches of insurance contracts was expressly recognized by this Court nearly half a century ago.

UNUM argues, however, that this Court has now eliminated all claims for consequential damages in suits for breach of an insurance contract. UNUM's contention is that, when the Court earlier recognized a broader range of consequential damages for

breach of the covenant of good faith and fair dealing in an insurance contract (“first-party bad faith”), it thereby shrank the damages that could be recovered for ordinary breach of contract.

This argument is not supported by either of the two principle cases cited by UNUM, *Billings v. Union Bankers Insurance Co.*, 918 P.2d 461, 466 (Utah 1996), or *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 801 (Utah 1985). Instead, those cases upheld the principle that ordinary consequential damages are recoverable for breach of an insurance contract. It is only when the breach is accompanied by bad faith that “expanded,” tort-like damages may be sought. Nothing in *Billings* or elsewhere in this Court’s jurisprudence suggests that it ever intended to eliminate a longstanding element of contract damages merely because a defendant happens to be an insurance company.

2. A private right of action should be recognized when an insurer violates Utah Code Ann. § 31A-26-301, which requires timely payment of valid claims. Under Section 874A of the *Restatement (Second) of Torts*, the statute intends to protect an identifiable class of persons, of whom Machan is a member. The purpose of Section 31A-26-301, its wording, and legislative history all support the recognition of a cause of action for violation of the statute.

ARGUMENT

I. UTAH LAW RECOGNIZES CONSEQUENTIAL DAMAGES FOR BREACH OF AN INSURANCE CONTRACT.

Certified Question 1 is:

In a first party insurance situation, may an insured recover consequential damages, other than attorney’s fees, for breach of the express terms of an

insurance contract? If so, what are the consequential damages that are recoverable for breach of the express terms of an insurance contract and how are they distinguished from the consequential damages for breach of the implied covenant of good faith and fair dealing that are recoverable under *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 801 (Utah 1985)?

To understand the context in which this question arose, it is important to address the specific argument raised by UNUM in its motion for summary judgment before Judge Cassell. UNUM's motion argued that, in an action for breach of a first-party insurance contract, the only damages available to the plaintiff are the unpaid policy benefits. R. 126, p. 2.

According to UNUM, *Billings v. Union Bankers Insurance Co.*, 918 P.2d 461, 466 (Utah 1996) confirmed that consequential damages are only available in bad faith claims, not in claims for ordinary breach of an insurance contract. *Id.* at 2-3. And if *Billings* was not clear enough, UNUM says, *Campbell v. State Farm Mutual Automobile Ins. Co.*, 2001 UT 89, 65 P.3d 1134, rev'd on other grounds, 538 U.S. 408 (2003), "leaves no doubt that damages beyond the fixed dollar amount of coverage are only available for breach of the implied covenant of good faith." R. 141, p. 31⁷.

⁷ UNUM's phraseology suggests that *Campbell* addressed the issue of damages in breach of contract claims (it didn't), or that some new analysis was offered on the subject (it wasn't). *Campbell*, of course, involved third-party bad faith, not first-party bad faith or breach of contract. The only issue addressed in the section of *Campbell* quoted by UNUM was whether attorney fees are recoverable in third-party bad faith actions. Moreover, the quoted text from *Campbell* itself consists largely of quotes from *Billings* and *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 801 (Utah 1985). *Campbell* offered no new views on the issues raised in those cases. Accordingly, it is not addressed further herein.

As UNUM stated: “[I]t is UNUM’s position that the Utah Supreme Court elected to eliminate the potential for consequential damages for mere breach of contract in order to expand the litany of potential consequential damages available for breach of the implied covenant of good faith and fair dealing. . . . For pure breach of the insurance contract, Machan’s damages are limited to the Policy benefits.” R. 126 at 3, 4. UNUM then claimed that it had paid all Policy benefits to which Machan was entitled, and therefore Machan’s breach of contract claim should be dismissed. *Id.* at 4.

The suggestion that no consequential damages – indeed, no damages of any kind except unpaid policy benefits and fees – are available for breach of an insurance contract is remarkable in at least two major respects. First, the theory is not supported (and, in fact, is contradicted) by the cases upon which it purports to be based. Second, it would place plaintiffs who suffer the breach of an insurance contract in a worse position than plaintiffs in all other contract actions, which is inconsistent with the Court’s longstanding recognition of the special nature of insurance.

A. Basic damages principles in insurance-related cases.

Three causes of action are commonly asserted in connection with an insurer’s alleged mishandling of a claim. Each has different duties and elements of proof (not at issue here), and, more important, each has different recoverable damages:

1. Breach of contract. Damages for ordinary breach of contract “serve the important purpose of compensating an injured party for actual injury sustained so that she may have been restored, as nearly as possible, to the position she was in prior to the

injury.” *Mahmood v. Ross*, 1999 UT 104, ¶ 19, 990 P.2d 933, quoting *Castillo v. Atlanta Casualty Co.*, 939 P.2d 1204, 1209 (Utah App.), *cert. denied*, 945 P.2d 1118 (Utah 1997).

Such damages may include “general damages, which flow naturally from the breach” *Id.* Additionally, consequential damages are also recoverable, if (and only if) the plaintiff can establish that the damages claimed, “while not an invariable result of breach, were reasonably foreseeable by the parties at the time the contract was entered into.” *Id.* This limitation is sometimes characterized as requiring that consequential damages have been “reasonably within the contemplation of, or reasonably foreseeable by, the parties at the time the contract was made.” *Billings*, 918 P.2d at 466.

The availability of consequential damages in breach of contract actions involving insurance policies has been established in Utah since at least 1958. In *Pacific Coast Title Insurance Company v. Hartford Accident & Indemnity Company*, 7 Utah 2d 322, 325 P.2d 906 (1958), an insurer failed to pay laborers and materialmen as required by its contract, which led to lien foreclosure proceedings against the insured by those individuals. The trial court allowed recovery of legal expenses incurred in defense of the third-party suit, and the insurer appealed.

This Court began its analysis:

The rule as to what damages are recoverable for breach of contract is based upon the concept of reasonable foreseeability that loss of such general character would result from the breach. Therefore, to be compensable, the loss must result from the breach in the natural and usual course of events, so that it can fairly and reasonably be said that if the minds of the parties averted to breach when the contract was made, loss of such character would have been within their contemplation.

Id. at 907 (citations omitted). The Court concluded that, because it was reasonably foreseeable that the insurer's breach of contract would result in liens and legal proceedings, the plaintiff was entitled to recover its expenses in defending against those proceedings as consequential damages. *Id.*, citing *Hadley v. Baxendale*, 9 Exch. 341, 156 Eng. Rep. (1854), *et al.*⁸ See also, *Horton v. Gem State Mutual of Utah*, 794 P.2d 847 (Utah App. 1990) (affirming trial court's award of consequential damages for breach of health insurance contract).

2. Third-party bad faith. When insurers handle claims brought by third parties against their insureds (as contrasted with claims brought by the insured against the insurer), they owe fiduciary and other duties beyond those expressed or implied in the insurance contract itself. *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 801 (Utah 1985). Consequently, when a cause of action arises out of third-party bad faith, the full gamut of normal tort damages are available, including punitive damages. *Id.*; *Campbell v. State Farm Mutual Automobile Ins. Co.*, 840 P.2d 130 (Utah App.), *cert. denied*, 853 P.2d 897 (Utah 1992); *Ammerman v. Farmers Ins. Exch.*, 22 Utah 2d 187, 450 P.2d 460, 462 (1969).

3. Breach of the covenant of good faith and fair dealing in the first-party context ("first-party bad faith"). This cause of action is a hybrid in Utah: not quite contract, not quite tort. The liability analysis is contract-based. Rather than adopt a tort cause of action for first-party bad faith, this Court in *Beck v. Farmers Insurance*

⁸ *Pacific Coast's* articulation of consequential damages has been cited approvingly on numerous occasions, including by this Court in *Beck* and *Billings*. In spite of that fact,

Exchange, 701 P.2d 795, 798 (Utah 1985), held that “the good faith duty to bargain or settle under an insurance contract is only one aspect of the duty of good faith and fair dealing implied in all contracts and that a violation of that duty gives rise to a claim for breach of contract.”

Although the *Beck* court found a contract theory of liability more theoretically sound in first-party situations, the Court remained concerned about the vulnerability of insureds. It observed:

An insured who has suffered a loss and is pressed financially is at a marked disadvantage when bargaining with an insurer over payment of that loss. Failure to accept a proffered settlement, although less than fair, can lead to catastrophic consequences for an insured who, as a direct consequence of the loss, may be peculiarly vulnerable, both economically and emotionally. The temptation for an insurer to delay settlement while pressures build on the insured is great, especially if the insurer’s exposure cannot exceed the policy limits.

Id.

Because of the “unique nature and purpose of an insurance contract,” which includes “to provide peace of mind,” *id.* at 802, a “broad range” of consequential damages that may extend beyond those available in a normal contract action are recoverable for first-party bad faith. *Id.* As this Court recognized in *Billings*, the *Beck* court, while adopting a contract theory of liability, contemplated damages essentially adapted or borrowed from tort law. *Billings* began its analysis of this issue with a detailed discussion of *Beck*, particularly the Court’s approach to the question of damages in that case:

as discussed below, UNUM suggests that *Billings* effectively overruled *Pacific*.

We discussed the types of damages recoverable for the breach [of the covenant of good faith and fair dealing]. We began with the general rule that “damages recoverable for breach of contract include both general damages, *i.e.*, those flowing naturally from the breach, and consequential damages, *i.e.*, those reasonably within the contemplation of, or reasonably foreseeably by, the parties at the time the contract was made.” We recognized that in appropriate circumstances, “consequential damages for breach of contract may reach beyond the bare contract terms,” and therefore, that the monetary limits of an insurance policy do not invariably define the amount for which the insurer may be liable upon a breach. Under this framework, we proceeded to craft a damage measure for *Beck*’s rather unique contract approach to the implied covenant of good faith and fair dealing.

Id. at 466 (internal citations and brackets omitted).

The Court then indicated that, under its “unique” approach, damages recoverable for first-party bad faith would be more akin to those in tort than in contract:

The *Beck* court observed that although it had rejected the tort approach, the measure of damages that the law made available for breach of the implied covenant should not ignore the principal reason for other courts’ adoption of the otherwise theoretically unsound tort approach, *i.e.*, to remove any incentive for insurers to breach the duty of good faith by expanding their exposure to damages caused by such a breach beyond the predictable fixed dollar amount of coverage provided by the policy. In furtherance of this purpose, we departed from the restrictive contract damages approach and followed a course more closely aligned with a tort damages approach. The *Beck* court concluded that a first-party insurer who breaches the implied covenant by unreasonably denying the insured the benefits bargained for may be held liable for broad consequential damages foreseeably caused by the breach, damages which might include those for mental anguish and which would be closely analogous to those available in states taking a tort approach.

Id. (emphasis added).⁹

The *Billings* court held that this “expanded consequential damage measure should be available only for the breach of implied covenant, not, as the court instructed the jury,

for breach of the expressed terms of the contract.” *Id.* (emphasis added). “It would not further *Beck*’s purpose of encouraging insurers to act reasonably if we were to impose the broad consequential damages allowed in *Beck* on every insurer who is ultimately determined by a court to have incorrectly denied coverage, regardless of how reasonable the denial,” the Court wrote. “Such an insurer ought to incur no greater damage exposure than any other person breaching the expressed terms of a contract.” *Id.* at 466-67 (emphasis added).

B. Consequential damages are available for breach of an insurance contract.

UNUM’s argument would require this Court to rewrite the last-quoted portion of *Billings*: Instead of an insurer facing *no greater* damage exposure than an ordinary breach of contract defendant, an insurer would face *less* damage exposure than an ordinary breach of contract defendant. After all, “any other person breaching the express terms of a contract” would be liable for consequential damages, if proved. That has long been the law in Utah. *See, e.g., Wagner v. Anderson*, 122 Utah 403, 250 P.2d 577 (1952); *Bevan v. J. H. Construction Co., Inc.*, 669 P.2d 442 (Utah 1983); *Kraatz v. Heritage Imports*, 2003 UT App. 201 and n. 11.

UNUM contends, however, that when this Court held a broader range of consequential damages to be available in first-party bad faith claims against insurers, it must have intended to eliminate consequential damages altogether in ordinary breach of

⁹ The analogy to tort remedies, while close, is not complete. Punitive damages, for example, are not available in first-party bad faith cases.

contract claims against insurers. (UNUM does not explain why this Court would make such an abrupt departure from at least 40 years' worth of jurisprudence *sub silentio*.)

A similar argument was made – and rejected – in *Castillo v. Atlanta Casualty Co.*, 939 P.2d 1204 (Utah App.), *cert. denied*, 945 P.2d 1118 (Utah 1997). In *Castillo*, an insured brought suit for an insurer's failure to pay uninsured motorist property damage benefits. As part of his claim for breach of contract, the plaintiff sought consequential damages for loss of use of his vehicle. The trial court concluded that such damages would be recoverable, but denied them because the insured had not rented a replacement vehicle.

On appeal, the insurer argued that damages for breach of an insurance contract are limited to the policy benefits themselves, and that consequential damages may not be sought. *Id.* at 1208 (“In effect, the insurer appears to argue that the monetary limits of the policy invariably define the amount for which it is liable upon a breach of the insurance contract.”) The Court of Appeals rejected that contention, noting:

The insurer's position in this respect is incorrect. “Although the policy limits define the amount for which the insurer may be held responsible in performing the contract, they do not define the amount for which it may be liable upon a breach.” *Beck v. Farmers Ins. Exch.*, 701 P.2d 795, 801 (Utah 1985).

Id. at 1208 n. 1. See also *id.* at 1208 (“Thus, plaintiffs' consequential damages theory is based on general contract law, not the provisions of the insurance policy. They are

correct that the policy's provisions on loss of use coverage are irrelevant to their claim premised on the insurer's breach of another policy provision.")¹⁰

In this case, UNUM's position appears to be based upon an assumption that, if consequential damages remain viable in breach of contract claims against insurers, there will be no difference between the damages available in a breach of contract claim and those available in a first-party bad faith claim. There are two principal flaws in that reasoning:

First, if *Beck* did indeed create such a supposed anomaly, it would seem more appropriate to reevaluate *Beck*'s limitations than to strip protections from an entire class of breach of contract claimants.

Moreover, as made clear in the language from *Billings* quoted above, it simply is not accurate to say that recoverable damages are identical in first-party bad faith claims and ordinary breach of insurance contract claims. In *Billings*, this Court agreed that the same "broad" and "expanded" damages "more closely analogous to those available in states taking a tort approach" available for first-party bad faith are not recoverable for plain breach of contract. Nowhere did the Court ever suggest that, by expanding the damages available in bad-faith claims, it had decreased the damages available in ordinary contract claims.

For purposes of answering Certified Question 1, this Court need not – nor can it – delineate in advance each and every conceivable element of consequential damages that

¹⁰ The *Castillo* court ultimately concluded that the plaintiff was not entitled to the consequential damages that he claimed, but only because he had not established their

might be available in a breach of insurance contract claim. The type of damages that might qualify as consequential varies, depending upon the facts of a particular case. *See, e.g., Wagner*, 250 P.2d at 579-80 (plaintiffs could recover damages “occasioned by the delay which the appellants can prove”); *Bevan*, 669 P.2d at 444 (lost favorable mortgage rate recoverable if due to defendant’s breach of contract); *Horton*, 794 P.2d at 847-48 (affirming award of damages for deterioration of medical condition as consequential damage of breach of health insurance contract).

The requirement imposed upon contract claimants to prove that their consequential damages were within the parties’ contemplation or reasonably foreseeable (a requirement that does not appear to be imposed, at least to the same degree, in bad faith cases) creates appropriate and predictable limitations upon a defendant’s exposure. Whether the plaintiff has sufficient evidence to present a particular item of damages to the jury in a specific case is, obviously, best left for trial courts to address in the first instance.

For purposes of answering the certified questions, Machan requests the Court to issue a clarification that whatever consequential damages would be available in a normal breach of contract claim remain available in a breach of insurance contract claim. If, however, the Court is inclined to explore Machan’s factual situation, the Court should clarify that each of these elements (if proved) is recoverable as a consequential damage in Machan’s breach of contract claim:

amount. *Id.* at 1211.

1) Deterioration of Machan's psychological condition, including his resulting inability to engage in significant gainful employment as a result thereof, due to UNUM's breach of its obligation to pay disability benefits under the contract;

2) Economic losses caused by depletion of his assets and savings in order to meet basic living expenses as a result of UNUM's breach of the contract; and

3) Mental anguish/emotional disturbance. This element is recoverable if "the contract or the breach is of such a kind that serious emotional disturbance was a particularly likely result." *Restatement (Second) of Contracts* § 353. Comment a to this section offers an example particularly apropos to the present case: "Breach of other types of contracts, resulting for example in sudden impoverishment or bankruptcy, may by chance cause even more emotional disturbance..." *Id.*

The foreseeability of these damages is indisputable. UNUM representatives have admitted the (self-evident) fact that the very purpose of disability insurance is to alleviate financial stress at a time when it is expected due to a disability. In fact, UNUM's own sales material warns customers: "There's too much at stake to have inadequate disability coverage. You work hard to maintain a comfortable lifestyle. But if you're not completely covered, the things you've worked for could be in jeopardy: · Your home(s). · Your retirement savings. · Your vacation. · Your children's education." R. Exh 50, bates UGIB 843. *See also*, R. Exh 39, p. 7, ¶ 12 (reasonable insurers know that failing to pay benefits would likely result in financial and emotional distress, and other adverse consequences to the insured).

II. UNUM'S VIOLATION OF UTAH CODE ANN. § 31A-26-301 IS ACTIONABLE BY A PRIVATE CAUSE OF ACTION.

The second question that Judge Cassell found unsettled under Utah law is: “Did Utah Code Ann. § 31A-26-301, entitled ‘Timely Payment of Claims,’ allow a private cause of action by the insured against his or her insurer for violation of the statute in 2000?”

For purposes of answering this question, it must be presumed that UNUM violated Section 31A-26-301 (2000), which provides: “Unless otherwise provided by law an insurer shall timely pay every valid claim made by an insured.” The sole issue, accordingly, is whether an insured has a remedy if his insurer violates this statute.

In addressing this issue, Machan acknowledges this Court’s pronouncement that, “in the absence of a clear indication from the [statute] itself, we are ‘not generally in the habit of implying a private right of action’” *Young v. Salt Lake City School Dist.*, 2002 UT 64, ¶ 21, 52 P.3d 1230. Machan submits that, in this instance, the legislature has provided such an indication. Moreover, as the Court’s qualified language notes, the absence of an express provision affirmatively setting forth a private right of action does not automatically preclude the recognition of such a right if other considerations support such recognition.

Restatement (Second) Of Torts (1979) § 874A articulates the basic considerations in determining whether to find a private right of action in a legislative enactment:

When a legislative provision protects a class of persons by proscribing or requiring certain conduct but does not provide a civil remedy for the violation, the Court may, if it determines that the remedy is appropriate in furtherance of the purpose of the legislation and needed to assure the effectiveness of the provision, accord to an

injured member of the class a right of action, using a suitable existing tort action or an new cause of action analogous to an existing tort action.

This Court recently relied on Section 874A in deciding whether to allow damages for violations of the State constitution. In *Spackman v. Bd. of Ed. of Box Elder County School Dist.*, 16 P.3d 533, 538 (Utah 2000), the Court noted that “there is no express statutory right to damages for one who suffers a constitutional tort.” Quoting Section 874A, however, the Court determined that it had the authority under common law to “accord an appropriate remedy to one injured from the violation of a [legislative provision].” *Id.*¹¹

Machan asks this Court to accord him an appropriate remedy for a (presumed) violation of Section 31A-26-301. Section 874A references two primary considerations: Does the legislative provision “protect a class of persons”? Second, is the plaintiff an “injured member of the class”?

The purposes of Chapter 26 of Title 31A (the Utah Insurance Code) are set forth in Utah Code Ann. § 31A-26-101. One express purpose is “to protect claimants under insurance policies from unfair claims adjustment practices” *Id.* § 31A-26-101(3). Another is “to prevent compensation arrangements for insurance adjusters that endanger the fairness of claims settlements” *Id.* § 31A-26-101(4). The legislature intended to protect a class of insureds, including from insurers’ failure to pay claims timely. That conclusion is especially compelling in a case like Machan’s, where the evidence suggests

¹¹ The Court noted that, while Section 874A uses the term “legislative provision,” comment a explains that “legislative provision” includes constitutional provisions. *Id.* at 538 n. 9.

that nonpayment of the insured's benefits was not merely happenstance, but rather due to an insurer's unlawful profit-enhancing programs.

It also appears that the Utah legislature intended or contemplated a private cause of action for breach of this statute. Subsection 31A-26-301(3) provides, "This section applies only to claims made by claimants in direct privity of contract with the insurer," with no mention that there is no private cause of action intended. By contrast, only two sections later, Section 31A-26-303(5) states, "This section does not create any private cause of action." The notable absence of such limiting language in Section 301 suggests a legislative intent to allow an insured who is direct privity of contract (like Machan) to have a private cause of action for breach of the statute, or a recognition that such a right already exists.

Legislative history further supports this conclusion. When the section was first enacted in 1985, it contained limiting language in subparagraph 3, "This section applies only to claims made by claimants in direct privity of contract with the insurer." *See* a copy of § 31A-26-301, attached as Addendum 2. The Utah Trial Lawyers Association became concerned that the statute created inequity by allowing only the person in direct privity of contract to bring an action against an insurer for failing to timely pay benefits. Typically, only the person or entity that signs the application for insurance is considered in privity, yet the insurance is usually intended to provide benefits for other insureds. For example, an insurance policy for an automobile might be purchased by a husband or wife. The policy, however, is clearly intended to provide benefits for the spouse, the children, and other possible insureds. The statute as worded created a remedy for only the

applicant, not the other intended insureds. (See Affidavits of Brian S. King and L. Rich Humpherys regarding Section 31A-26-301 amendment process, R. Exh 53).

During the 2000 legislative session, UTLA attempted to submit an amendment to have Section 31A-26-301 apply to all insureds under a policy, not just those technically “in privity.” Because the proposed amendment was submitted too late, the legislature did not consider it that year. Thereafter, the amendment was prepared with input from the insurance department and insurance industry representatives, and was then introduced as First Substitute Senate Bill 126 in the 2001 legislative session. In the process, lobbyists on behalf of the insurance industry and UTLA representatives worked together in creating language that satisfied the concerns of both sides. See Attachments to R. Exh 53, Transcript of House Business, Labor and Economic Standing Committee, p. 2.

The insurance industry was concerned that the language be carefully restricted to apply only to insureds under the policy, to avoid an argument that a third-party claimant might be able to sue the defendant’s liability carrier directly. Under well-established Utah law, third-party claimants do not have a direct cause of action against a defendant’s liability carrier; only the insured can assert a claim. Representatives from the insurance department and insurance industry did not want this statute to create a new claim that has never existed. However, they conceded that all insureds under a policy should be entitled to file an action directly against their own insurance company, not just those in privity of contract. To address both sides’ concerns, the amendment was carefully crafted to use the words “claim for first party benefits,” with a clear description of those insureds who

would be entitled to make the claim. Third-party claims were carefully excluded. *See* Utah Code Ann. § 31A-21-301(3), as amended 2002, attached as Addendum 3.

During the senate committee hearing when Senate Bill 126 was addressed, extensive discussion ensued regarding the need to modify the statute to alleviate the inequity of having it apply only to persons in privity of contract. Brian S. King, a member of UTLA's Board of Governors, explained that the purpose of the amendment was to allow all insureds a direct cause of action against their insurers, not just those in privity, since all insureds who have been damaged by the failure of the insurer to pay timely benefits should have a right to recover for their damages, not just the person who signed the application. (*See* attachments to R. Exh 53, King Aff., Humpherys Aff., and transcripts of hearings before the House and Senate committees on February 13, 2001)¹².

After First Substitute Senate Bill 126 passed the committees, it was introduced on the floor of the Senate by Senator John Valentine. He explained the purpose of the bill and gave an example of its application:

What Senate Bill 126 does, is it allows those people who are named insureds to also make claims against the insurance company rather than have to go through the oddball situation of having to sue the person who is in privity, so that person can then sue their own insurance company.

Let me give an example in my own law firm. In my law firm we have health insurance, and we have a number of people who are named as the beneficiaries, like myself, my wife, my children, my employees, and all my other partners....

¹² Shortly after King began to explain the purpose and affect of § 31A-26-301 and the proposed amendment, the audio tape ended and there is no further record of that proceeding. Mr. King, however, has testified to the substance of the discussion. The missing portion is likewise explained in the affidavit of Humpherys, who also participated in the amendment process.

Everyone in the firm is covered by this insurance policy. However, the signator on the policy is my law firm, a professional corporation.

Literally, if I've got a problem with a claim...I have to sue my own company, the people at my company then sue my insurance company.

What Senate Bill 126 does, the First Substitute, is cuts through all that mess and says, okay, if you're a named insured you can go directly to the insurance company and say pay up. That's what it does.

See attachments to R. Exh 53, Transcript of the Senate Floor, February 15, 2001, pp. 3-4.

First Substitute Senate Bill 126 thereafter passed and became law. Section § 31A-26-301(3), as amended, now reads as follows:

This section applies only to a claim for first party benefits made by a person who is:

- (a) named or defined as an insured under the terms of an insurance policy;
- (b) described as a covered person under the terms of a policy of health care insurance as defined in Section 31A-1-301; or
- (c) named, defined, or described:
 - (i) as:
 - (A) an insured;
 - (B) a beneficiary;
 - (C) a policyholder; or
 - (D) otherwise covered person; and
 - (ii) under the terms of :
 - (A) a life insurance policy; or
 - (B) an annuity.

While the 2002 amendment is not directly applicable to Machan (because he is in direct privity of contract, and therefore has always been covered by the statute), the legislative history surrounding the amendments to Section 31A-26-301 clearly indicate an intention by the legislators that a direct cause of action would exist by insureds for violation of the statute.

CONCLUSION

For the reasons set forth above, plaintiff/co-appellant Gary Machan respectfully requests the Court to answer the certified questions in the following manner:

1. To clarify that plaintiffs in breach of insurance contract actions are entitled to seek the same types of consequential damages available to plaintiffs in other breach of contract claims.
2. To clarify that a private right of action for violation of Utah Code Ann. § 31A-21-301 exists for plaintiffs who are within the class of persons protected by the statute.

DATED this 17th day of February, 2004.

CHRISTENSEN & JENSEN, P.C.



L. Rich Humpherys
Karra J. Porter
Attorneys for Plaintiff/Co-Appellant/Gary Machan

INDEX TO ADDENDA

1. Order of Certification
2. Utah Code Ann. § 31A-26-301 (as applicable in 2000)
3. Utah Code Ann. § 31A-26-301 (as amended 2002)

CERTIFICATE OF SERVICE

I hereby certify that two true and correct copies of the foregoing Brief of Appellant was hand delivered on the 17th day of February, 2004, to the following:

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A handwritten signature in cursive script, reading "A. Rick Humphrey", written over a horizontal line.

Tab 1

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DISTRICT OF UTAH
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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF UTAH, CENTRAL DIVISION

GARY MACHAN,

Plaintiff,

vs.

UNUM LIFE INSURANCE COMPANY OF
AMERICA,

Defendant.

Civil No. 2:00-CV-00904PGC

ORDER OF CERTIFICATION

The United States District Court for the District of Utah, pursuant to Rule 41 of the Utah Rules of Appellate Procedure, hereby certifies the following questions of law which are controlling in the above-captioned matter now pending before this Court.

1. In a first party insurance situation, may an insured recover consequential damages, other than attorney's fees, for breach of the express terms of an insurance contract? If so, what are the consequential damages that are recoverable for breach of the express terms of an insurance contract and how are they distinguished from the consequential damages for breach of the implied covenant of good faith and fair dealing that are recoverable under *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 801 (Utah 1985)?

2. Did Utah Code Ann. § 31A-26-301, entitled "Timely Payment of Claims," allow a private cause of action by the insured against his or her insurer for violation of the statute in 2000?

FACTUAL BACKGROUND

1. This case arises out of the claimed failure of defendant UNUM Life Insurance Company of America ("UNUM") to pay disability benefits to plaintiff, Gary Machan, under the terms of a disability income insurance policy.

2. Mr. Machan submitted two claims to UNUM under his disability income policy: 1) in March, 1999, following cardiac bypass surgery; and 2) in April, 2000, asserting mental impairment as a result of the earlier bypass surgery. Very briefly, UNUM claimed that Mr. Machan was either not entitled to the benefits he was claiming, or that UNUM lacked sufficient information to determine whether benefits were owed.

3. This case was removed from the Third District Court, Salt Lake County, State of Utah, on November 17, 2000.

4. The complaint averred five claims for relief: (1) breach of the express terms of the insurance contract; (2) breach of the implied covenant of good faith and fair dealing; (3) intentional and/or negligent misrepresentation; (4) intentional infliction of emotional distress; and (5) breach of statutory duties. Mr. Machan has represented to the court that his bad faith claim relates solely to his second claim for benefits.

5. Mr. Machan claimed that as a consequence of UNUM's denial of benefits, he suffered consequential damages, including: (1) worsening of his psychological condition; (2) inability to afford psychological treatment for himself and his mentally ill son; (3) depletion of his assets and savings in order to meet basic living expenses; and (4) the inability to have any significant gainful employment due to his worsened psychological condition.

6. In September 2002, while this lawsuit was pending, UNUM made a determination to pay Mr. Machan his full monthly benefits under his disability policy retroactive to March 1999.

7. UNUM filed a motion for summary judgment in June, 2003, challenging each claim for relief in the complaint. The court has taken the motion for summary judgment under advisement.

8. UNUM'S motion for summary judgment raised the issue of whether an insured in a first party situation may recover consequential damages, other than attorney's fees (which UNUM concedes are recoverable under existing case law), for breach of the express terms of the insurance contract. UNUM's motion also raised the issue of whether a private cause of action exists under Utah Code Ann. § 31A-26-301 ("Timely Payment of Claims"). These issues have led to the certified question and are addressed in the Discussion below.

DISCUSSION

1. Consequential Damages

UNUM asserted in its summary judgment motion that under *Beck v. Farmers Insurance Exchange*, 701 P.2d 795 (Utah 1985) and *Billings v. Union Bankers Insurance Company*, 918 P.2d 461 (Utah 1996), the only damages available to Mr. Machan for breach of the express terms of his insurance contract are the insurance benefits under the policy (which have been paid to date), prejudgment interest assuming the criteria are met, and attorneys fees if Mr. Machan can prove that the fees were foreseeable at the time the parties entered into the insurance contract.

UNUM contends that consequential damages, other than attorney's fees, are not recoverable for bare breach of an insurance contract.

UNUM urged that according to *Beck* and *Billings*, consequential damages, other than attorney's fees, are recoverable only for breach of the implied covenant of good faith and fair dealing in order to remove any incentive for insurers to breach the duty of good faith by expanding their exposure beyond the predictable fixed dollar amount of coverage provided by the policy. UNUM argued that this incentive would be abrogated if these same consequential damages are made available for breach of the express covenants in an insurance contract. To allow an insured to recover damages beyond the policy coverage in the absence of bad faith would effectively deny any careful insurer the option of declining to pay a contested claim and awaiting the outcome of the dispute.

UNUM further argued that the consequential damages claimed by Mr. Machan, i.e., worsening of his psychological condition, inability to afford psychological treatment for himself and his mentally ill son, depletion of his assets and savings in order to meet basic living expenses, and the inability to have any significant gainful employment due to his worsened psychological condition, assuming that Mr. Machan can otherwise prove that these claimed losses meet the criteria for consequential damages, fall within the scope of consequential damages that *Beck* and *Billings* said are the remedy for breach of the covenant of good faith in order to remove any incentive for insurers to breach their implied covenant. Finally, UNUM argued that its position has been confirmed by statements made recently by the Utah Supreme Court in *Campbell v. State Farm Mutual Automobile Insurance Company*, 2001 UT 89, 432 Utah

Adv. Rep. 44, 2001 Utah LEXIS 170 (Utah 2001), *rev'd on other grounds*, __ U.S. ___, 123 S.Ct. 1513 (2003).

In response to UNUM's position, Mr. Machan cited, among other authorities, *Pacific Coast Title Insurance Co. v. Hartford Accident & Indemnity Co.*, 325 P.2d 906 (Utah 1958); *Cratz v. Heritage Imports*, 71 P.3d 188, ¶¶ 48-51 (Utah App. 2003); and Restatement (Second) of Contracts, § 351, and argued that under general contract law, damages which are reasonably foreseeable to the parties when the contract was made, have always been recoverable, indeed, since the days of *Hadley v. Baxendale*, 9 Exch. 341, 156 Emg. Rep. 145 (1854). Mr. Machan contends that when allowing a broad range of tort-like damages under a breach of implied covenants of good faith and fair dealing (as set forth in *Beck, supra*) that the Utah Supreme Court did not abrogate the recovery of well recognized consequential damages arising from a breach of contract. Instead, the Court simply expanded the remedies where the insurer has also breached the implied covenants of good faith and fair dealing.

Mr. Machan asserted that the "incentive" theory urged by UNUM to justify a partial abrogation of general contract law regarding damages, exists without eliminating historical damages, since insurers have adequate incentive to avoid liability for a much broader range of tort-like damages available under a breach of the implied covenant of good faith. Mr. Machan argued that *Billings*, instead of restricting historical contract damages, held only that without a violation of the implied covenants, this broad range of tort-like damages is not recoverable. To reach any other position, concluded Mr. Machan, would give unfair preferential treatment to insurance companies over all other non-insurance parties who breach contracts.

Mr. Machan proffered evidence that, based on the testimony of UNUM's representatives and based on UNUM's own marketing material, it was foreseeable to UNUM that if UNUM breaches the insurance contract, Mr. Machan would suffer consequential damages beyond the insurance benefits.

2. Utah Code Ann. § 31A-26-301

The applicable part of Utah Code Ann. § 31A-26-301(1), effective in 2000, stated:

Unless otherwise provided by law, an insurer shall timely pay every valid insurance claim made by an insured.

UNUM asserted in its summary judgment motion that § 31A-26-301(1) does not provide a private cause of action; that absent specific direction from the legislature, Utah Courts routinely decline to create private rights of action based on alleged violations of statutes. *See e.g., Milliner v. Elmer Fox & Co.*, 529 P.2d 806, 808 (Utah 1974); *Broadbent v. Bd. of Educ. of Cache Cty.*, 910 P.2d 1274, 1278 (Utah Ct. App. 1996), *cert. denied*, 917 P. 2d 556 (Utah 1996); *J.H. v. D.H. v. West Valley City*, 840 P.2d 115, 125 (Utah 1992); *Richards Irr. Co. v. Karren*, 880 P. 2d 6 (Utah Ct. App. 1994). No Utah decision has ever recognized a private cause of action under Utah Code Ann. § 31A-26-301.

In response to UNUM's position, Mr. Machan argued that he is a member of the class of persons which the statute was designated to protect and that the elements necessary to imply a private right of action are met, citing *Spackman v. B.D. of Ed. Box Elder County School District*, 16 P.3d 533, 538 (Utah 2000), and § 874A of the Restatement (Second) of Torts (1979). Mr. Machan further argued that the expressed purpose of the Utah Insurance Code, including Chapter 26, is to protect claimants under insurance policies from unfair claims adjustment practices.

Utah Code Ann. §§ 31A-102(2) and 31A-26-101(3). Mr. Machan also contends that the statutory language itself demonstrates a legislative intent to create a private cause of action. Finally, Mr. Machan argued that the legislative history of § 31A-26-301 demonstrates an intent to allow a private cause of action.

It appears to the court that the issue of whether Section 31A-26-301 provided a private cause of action in the year 2000 is closely related to the consequential damages issue, and that both questions overlap and are complimentary. For these reasons, the court seeks an answer as to whether Section 31A-26-301 provided a private cause of action in 2000.

The two questions that are certified are controlling in this case. Mr. Machan claims to have suffered consequential damage from the denial of disability benefits. The issue is neither trivial, nor is it collateral. Having found no controlling Utah law to resolve these issues, and upon the belief that the issue concerning Section 31A-26-301 is complimentary to the consequential damages question, and in the interest of cooperative federalism, the court believes that these questions of Utah law presented in this case are best answered by the Utah Supreme Court.

CONCLUSIONS

This Court concludes that the questions of law outlined above are unsettled under existing Utah law. Accordingly, the clerk of this Court shall transmit a copy of this Order of Certification to counsel for all parties to the proceedings in this Court. The clerk shall also submit to the Utah Supreme Court a certified copy of this Order of Certification, together with the parties' respective summary judgment memoranda, the hearing transcript for July 29, 2003, and any other portion of the record before this Court that may be required by the Utah Supreme

Court. Pursuant to Rule 41(f) of the Utah Rules of Appellate Procedure, this Court orders that each party shall bear its own fees and costs of this certification.

IT IS SO ORDERED this 22nd day of September, 2003.

BY THE COURT:



Honorable Paul G. Cassell
United States District Court

hereby certify that the annexed document is a true and correct copy of the original on file in this office.

ATTEST: MARKUS B. ZIMMER
Clerk, U.S. District Court
District of Utah

By: _____

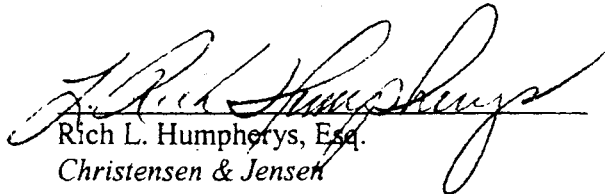


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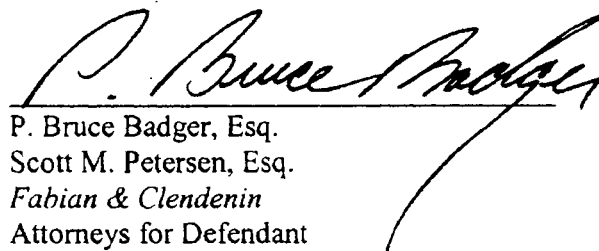
Date: _____

12-16-03

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United States District Court
for the
District of Utah
September 23, 2003

* * CERTIFICATE OF SERVICE OF CLERK * *

Re: 2:00-cv-00904

True and correct copies of the attached were either mailed, faxed or e-mailed by the clerk to the following:

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Tab 2

PART III

CLAIM PRACTICES

31A-26-301. Timely payment of claims.

(1) Unless otherwise provided by law, an insurer shall timely pay every valid insurance claim made by an insured. By rule the commissioner may prescribe the kinds of notice and proof of loss that will establish validity, the manner in which an insurer may make a bona fide denial of a claim, the periods of time within which payment is required to be made to be timely, and the reasonable interest rates to be charged upon late claim payments.

(2) Notwithstanding Subsection (1), the payment of a claim is not overdue during any period in which the insurer is unable to pay the claim because there is no recipient legally able to give a valid release for the payment, or in which the insurer is unable to determine who is entitled to receive the payment, provided that the insurer has promptly notified the claimant of the inability and has offered in good faith to pay the claim promptly when the inability is removed.

(3) This section applies only to claims made by claimants in direct privity of contract with the insurer.

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Tab 3

PART III

CLAIM PRACTICES

31A-26-301. Timely payment of claims.

- (1) (a) Unless otherwise provided by law, an insurer shall timely pay every valid insurance claim made by an insured.
- (b) By rule the commissioner may prescribe:
 - (i) the kinds of notice and proof of loss that will establish validity;
 - (ii) the manner in which an insurer may make a bona fide denial of a claim;
 - (iii) the periods of time within which payment is required to be made to be timely; and
 - (iv) the reasonable interest rates to be charged upon late claim payments.
- (2) (a) Notwithstanding Subsection (1) and subject to Subsection (2)(b), the payment of a claim is not overdue during any period in which:
 - (i) the insurer is unable to pay the claim because there is no recipient legally able to give a valid release for the payment; or
 - (ii) the insurer is unable to determine who is entitled to receive the payment.
- (b) Subsection (2)(a) applies only if the insurer:
 - (i) promptly notifies the claimant of the inability to pay the claim; and
 - (ii) offers in good faith to pay the claim promptly when the inability to pay the claim is removed.
- (3) This section applies only to a claim for first party benefits made by a person who is:
 - (a) named or defined as an insured under the terms of an insurance policy;
 - (b) described as a covered person under the terms of a policy of health care insurance as defined in Section 31A-1-301; or
 - (c) named, defined, or described:
 - (i) as:
 - (A) an insured;
 - (B) a beneficiary;
 - (C) a policyholder; or
 - (D) otherwise covered person; and
 - (ii) under the terms of:
 - (A) a life insurance policy; or
 - (B) an annuity.

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