

2003

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

Utah Supreme Court

Follow this and additional works at: [https://digitalcommons.law.byu.edu/byu\\_sc2](https://digitalcommons.law.byu.edu/byu_sc2)



Part of the [Law Commons](#)

Original Brief Submitted to the Utah Supreme Court; digitized by the Howard W. Hunter Law Library, J. Reuben Clark Law School, Brigham Young University, Provo, Utah; machine-generated OCR, may contain errors.

L. Rich Humphreys; Christensen and Jensen, P.C.; Attorney for Plaintiff.

Scott M. Petersen; P. Bruce Badger; Fabian and Clendenin; Attorneys for Defendant.

---

## Recommended Citation

Brief of Appellant, *Machan v. Unum Life Insurance*, No. 20030789.00 (Utah Supreme Court, 2003).  
[https://digitalcommons.law.byu.edu/byu\\_sc2/2462](https://digitalcommons.law.byu.edu/byu_sc2/2462)

This Brief of Appellant is brought to you for free and open access by BYU Law Digital Commons. It has been accepted for inclusion in Utah Supreme Court Briefs by an authorized administrator of BYU Law Digital Commons. Policies regarding these Utah briefs are available at [http://digitalcommons.law.byu.edu/utah\\_court\\_briefs/policies.html](http://digitalcommons.law.byu.edu/utah_court_briefs/policies.html). Please contact the Repository Manager at [hunterlawlibrary@byu.edu](mailto:hunterlawlibrary@byu.edu) with questions or feedback.

---

**BEFORE THE UTAH SUPREME COURT**

---

GARY MACHAN,

Plaintiff and Co-Appellant,

vs.

UNUM LIFE INSURANCE  
COMPANY OF AMERICA,

Defendant and Co-Appellant.

No. 20030789-SC

---

**BRIEF OF CO-APPELLANT UNUM LIFE INSURANCE  
COMPANY OF AMERICA**

---

Certification From the U.S. District Court for the District of Utah,  
Civil No. 2:00 CV 904PGC  
Honorable Paul G. Cassell, Presiding

---

L. Rich Humphreys (1582)  
CHRISTENSEN & JENSEN, P.C.  
50 South Main Street, Suite 1500  
Salt Lake City, Utah 84144  
Telephone: (801) 323-5000  
Facsimile: (801) 355-3472

Attorneys for Plaintiff and  
Co-Appellant Gary Machan

Scott M. Petersen (A7599)  
P. Bruce Badger (A4791)  
FABIAN & CLENDENIN,  
A Professional Corporation  
215 South State Street, 12<sup>th</sup> Floor  
P.O. Box 510210  
Salt Lake City, Utah 84151  
Telephone: (801) 531-8900  
Facsimile: (801) 531-1716

Attorneys for Defendant and Co-  
Appellant UNUM Life Insurance  
Company of America

EME COURT

FEB 17 2004

PATENT  
C.

---

**BEFORE THE UTAH SUPREME COURT**

---

GARY MACHAN,

Plaintiff and Co-Appellant,

vs.

UNUM LIFE INSURANCE  
COMPANY OF AMERICA,

Defendant and Co-Appellant.

No. 20030789-SC

---

**BRIEF OF CO-APPELLANT UNUM LIFE INSURANCE  
COMPANY OF AMERICA**

---

Certification From the U.S. District Court for the District of Utah,  
Civil No. 2:00 CV 904PGC  
Honorable Paul G. Cassell, Presiding

---

L. Rich Humphreys (1582)  
CHRISTENSEN & JENSEN, P.C.  
50 South Main Street, Suite 1500  
Salt Lake City, Utah 84144  
Telephone: (801) 323-5000  
Facsimile: (801) 355-3472

Attorneys for Plaintiff and  
Co-Appellant Gary Machan

Scott M. Petersen (A7599)  
P. Bruce Badger (A4791)  
FABIAN & CLENDENIN,  
A Professional Corporation  
215 South State Street, 12<sup>th</sup> Floor  
P.O. Box 510210  
Salt Lake City, Utah 84151  
Telephone: (801) 531-8900  
Facsimile: (801) 531-1716

Attorneys for Defendant and Co-  
Appellant UNUM Life Insurance  
Company of America

Pursuant to Rule 24(b) of the Utah Rules of Appellate Procedure, Co-Appellant UNUM Life Insurance Company of America hereby submits the following Brief of Co-Appellant.

### **LIST OF PARTIES**

Pursuant to Rule 24(a)(1) of the Utah Rules of Appellate Procedure, the caption of the case contains the names of all parties to the proceeding in the U.S. District Court for the District of Utah from which the Order of Certification was issued.

## TABLE OF CONTENTS

LIST OF PARTIES .....	i
TABLE OF AUTHORITIES .....	iv
STATEMENT OF JURISDICTION.....	1
STATEMENT OF THE ISSUES.....	1
STANDARD OF REVIEW .....	2
STATEMENT OF GROUNDS FOR SEEKING REVIEW.....	2
STATUTES .....	3
STATEMENT OF THE CASE.....	3
SUMMARY OF THE ARGUMENT .....	7
ARGUMENT .....	9
I. CONSEQUENTIAL DAMAGES SHOULD NOT BE RECOVERABLE FOR A BREACH OF THE EXPRESS TERMS OF AN INSURANCE CONTRACT .....	9
A. <i>Beck v. Farmers Insurance Exchange</i> Enlarged The Remedy For An Insurer's Breach Of The Implied Covenant Of Good Faith And Fair Dealing In A First-Party Situation .....	9
B. <i>Billings v. Union Bankers Insurance Company</i> Confirmed That Consequential Damages Are Not Recoverable In The Absence of Bad Faith.....	12
C. <i>Campbell v. State Farm Mutual Automobile Insurance Company</i> Leaves No Doubt That Damages Beyond The Fixed Dollar Amount of Coverage Are Only Available For Breach Of The Implied Covenant Of Good Faith.....	16
D. Allowing Attorney's Fees Without Proving Bad Faith Contravenes <i>Beck's</i> Objectives .....	18

II.	MUJI AGREES WITH UNUM.....	21
III.	THE UTAH INSURANCE CODE DID NOT PROVIDE A PRIVATE CAUSE OF ACTION IN 2000.....	23
	CONCLUSION .....	26

## ADDENDUM

Tab A:	Order of Certification
Tab B:	Utah Code Ann. § 31A-1-102 (2000) Utah Code Ann. § 31A-2-308 (2000) Utah Code Ann. § 31A-26-301 (2000)
Tab C:	<i>Billings v. Union Bankers Insurance Company</i> , 918 P.2d 461 (Utah 1996)
Tab D:	<i>Beck v. Farmers Insurance Exchange</i> , 701 P.2d 795 (Utah 1985)

## TABLE OF AUTHORITIES

### CASES

<i>Beck v. Farmers Insurance Exchange</i> , 701 P.2d 795 (Utah 1985).....	1, 7, 8, 9, 11
.....	12, 13, 14, 17, 21, 22
<i>Billings v. Union Bankers Insurance Company</i> , 918 P. 2d 461 (Utah 1996)...	6, 7, 8
.....	12, 13, 14, 17, 18, 20, 21
<i>Broadbent v. Bd. Of. Educ. Of Cache Cty.</i> , 910 P.2d 1274 (Utah Ct. App. 1996), <i>cert. denied</i> , 917 P.2d 556 (Utah 1996) .....	24
<i>Callioux v. Progressive Ins. Co.</i> , 745 P.2d 838 (Utah Ct. App. 1987).....	20
<i>Campbell v. State Farm Mutual Automobile Insurance Company</i> , 65 P.3d 1134 (Utah 2001).....	16, 17
<i>Cannon v. Travelers Indemnity Co.</i> , 994 P. 2d 824 (Ut. Ct. App. 2000) .....	24
<i>Canyon Country Store v. Bracey</i> , 781 P.2d 414 (Utah 1989).....	18
<i>Castillo v. Atlanta Casualty Co.</i> , 939 P.2d 1204 (Ut. Ct. App. 1997), <i>cert. denied</i> 945 P.2d 1118 (1997).....	18
<i>Gibbs M. Smith, Inc., v. U.S. Fidelity</i> , 949 P. 2d 337 (Utah 1997).....	20
<i>Grundberg v. The Upjohn Co.</i> , 813 P. 2d 89 (Utah 1991).....	2
<i>J.H. by D.H. v. West Valley City</i> , 840 P.2d 115 (Utah 1992).....	24
<i>Johnson v. Life Investors Insurance Company of America.</i> , 216 F. 3d 1087, 2000 WL 954840 (10 <sup>th</sup> Cir. 2000 ) .....	20
<i>Lyon v. Hartford Accident and Indemnity Co.</i> , 25 Utah 2d 311, 480 P. 2d 739 (1971).....	10, 11
<i>Milliner v. Elmer Fox &amp; Co.</i> , 529 P.2d 806 (Utah 1974) .....	24, 25
<i>Moore v. Energy Mutual Insurance Co.</i> , 814 P.2d 1141 (Ut. Ct. App. 1991).....	18
<i>Nielson v. Div. Of Peace Officer Standards &amp; Training</i> , 851 P.2d 1201 (Utah Ct. App. 1993).....	24
<i>Prince v. Bear River Mutual Ins. Co.</i> , 56 P. 3d 524 (Utah 2002).....	5, 19, 26

<i>Pugh v. North Am. Warranty Servs., Inc.</i> , 1 P.3d 570 (Ut. Ct. App. 2000).....	14, 20
<i>Richards Irr. Co. v. Karren</i> , 880 P.2d 6 (Utah Ct. App. 1994) .....	24
<i>Spackman v. Board of Education of Box Elder County School Dist.</i> 16 P.3d 533 (Utah 2000) .....	25
<i>Turtle Management, Inc. v. Haggis Management, Inc.</i> , 645 P.2d 667 (Utah 1982) .....	19
<i>Zions First National Bank v. National American Title Insurance Co.</i> , 749 P.2d 651 (Utah 1988) .....	18

## **STATUTES**

Utah Code Ann. § 31A-1-102 .....	23
Utah Code Ann. § 31A-2-308 (2000) .....	23
Utah Code Ann. § 31A-26-301 (2001) .....	2, 3, 4, 6, 23, 26, 27
Utah Code Ann. §78-2-2 .....	1

## **OTHER AUTHORITIES**

Theresa Viani Agee, Note, <i>Breach of an Insurer's Good Faith Duty to its Insured: Tort or Contract?</i> , 1988 Utah L. Rev. 135 .....	10
William Kevin Tanner, <i>Bad Faith Claims Against Insurers: The State of Utah Law Fifteen Years after Beck v. Farmers Insurance Exchange</i> , 15 B.Y.U. J. Pub. L. 53 .....	10

## **RULES**

Utah Rules of Appellate Procedure, 24(a)(1).....	i
Utah Rules of Appellate Procedure, Rule 24(b) .....	i
Utah Rules of Appellate Procedure, Rule 41(a).....	1, 2
Utah Rules of Appellate Procedure, Rule 41(b) .....	2



## STATEMENT OF JURISDICTION

This matter arises from an Order of Certification issued by the U.S. District Court for the District of Utah pursuant to Rule 41 of the Utah Rules of Appellate Procedure. The Utah Supreme Court has original jurisdiction, pursuant to Utah Code Ann. §78-2-2 (2001), to answer questions of state law certified by a court of the United States.

## STATEMENT OF THE ISSUES

The following questions of state law have been certified by the U.S. District Court for the District of Utah<sup>1</sup>:

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).

---

<sup>1</sup> A copy of the Order of Certification is included in the Addendum at Tab "A".

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**

Pursuant to Rule 41(a) of the Utah Rules of Appellate Procedure, both certified questions are questions of law “for original disposition” by this Court. *Grundberg v. The Upjohn Co.*, 813 P. 2d 89, 90 (Utah 1991).

### **STATEMENT OF GROUNDS FOR SEEKING REVIEW**

Pursuant to Rule 41(b) of the Utah Rules of Appellate Procedure, any court of the United States may invoke Rule 41 by entering an order of certification as described in the rule. When invoking the rule, the certifying court may act either *sua sponte* or upon a motion by any party. In the U.S. District Court, both the plaintiff and defendant orally moved the court to certify the first question presented above, and the plaintiff orally moved the court to certify the second question. Hearing Transcript, July 29, 2003, at pp. 13-19, 28-29, 48-49.

## STATUTES

With respect to the second question presented, Utah Code Ann. §31A-26-301 (2000)<sup>2</sup> reads:

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.

## STATEMENT OF THE CASE

This lawsuit was filed in the Third District Court in and for Salt Lake County and was removed to the U.S. District Court for the District of Utah on diversity grounds. The plaintiff, Gary Machan (“Machan”), averred that the defendant, UNUM Life Insurance Company of America (“UNUM”), owed him

---

<sup>2</sup> A copy of each insurance statute referred to in this brief is included in the Addendum at Tab “B”.

benefits under two disability income insurance policies. Machan averred that UNUM had failed to pay him his disability benefits after he underwent open heart surgery in March 1999. UNUM countered that Machan's physicians had certified that he was fit to return to work following a three month recuperation period and that UNUM had paid all of the disability benefits that were owed under the disability policies. Machan further averred that UNUM had failed to pay him disability benefits for a mental/psychiatric claim that Machan filed in 2000. UNUM countered that Machan's disability could not be determined based on the information provided by Machan's treating health care providers and that Machan filed suit and withdrew his consent to release of medical information before UNUM could complete its claims determination.

Machan raised numerous claims for relief including breach of the express terms of his insurance contracts with respect to both his cardiac and psychiatric claims, and breach of the implied covenant of good faith and fair dealing with respect to his psychiatric claim. He also averred that UNUM violated the Utah Insurance Code, Utah Code Ann. § 31A-26-301 (2000), which requires an insurance company to pay all claims in a timely manner.

UNUM filed a motion for summary judgment addressing each of Machan's claims for relief. With respect to Machan's claim for breach of the implied covenant of good faith and fair dealing, UNUM urged that Machan's claim was

fairly debatable according to *Prince v. Bear River Mutual Ins. Co.*, 56 P. 3d 524, 533 (Utah 2002). UNUM supported its motion with the testimony of its outside consulting psychiatrist who testified that the information provided by Machan's treating psychiatrist and psychologist was contradictory and that many of the medical records were illegible. UNUM's consulting psychiatrist had attempted on at least five separate occasions to engage in what are referred to in the insurance industry as "doc to doc calls" with Machan's health care providers, but before he was able to speak with Machan's psychiatrist or psychologist, Machan filed suit and withdrew his release of any further information and made it impossible for UNUM to gather needed information other than through the formal discovery process. During discovery UNUM asked Machan to submit to an examination by a neuropsychologist, who, even after an MRI of Machan's brain, was still unable to determine whether or not Machan was able to perform the material and substantial duties of his occupation, which is the contractually agreed upon threshold for payment of disability benefits under Machan's disability policies. Nevertheless, after being afforded the opportunity to evaluate Machan's MRI, UNUM began paying Machan disability benefits retroactively beginning in September 2002.

At the summary judgment hearing the court asked for additional briefing on whether Machan's expert witnesses created an issue of fact on the bad faith claim. UNUM addressed the court's concerns by filing two separate motions in limine

which have gone unopposed. In the meantime, the trial court, for administrative purposes, has denied UNUM's Motion for Summary Judgment, without prejudice, pending the resolution of the questions raised by this certification.

Machan asserted that, in addition to his attorney's fees, he suffered consequential damages from the following losses: (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.

Machan asserts that he can recover for these consequential losses for a breach of either the express terms of his policies, or for a breach of the implied covenant of good faith and fair dealing.

The issues that bring us to the Utah Supreme Court are whether there are any consequential damages, other than attorney's fees, that may be recoverable for breach of the express terms of an insurance contract, and whether the Utah Insurance Code, Utah Code Ann. § 31A-26-301, provided a private cause of action in 2000.

In this brief UNUM extends the first issue and also argues that *Billings v. Union Bankers Insurance Company*, 918 P. 2d 461 (Utah 1996)<sup>3</sup>, should be

---

<sup>3</sup> A copy of *Billings* is included in the Addendum at Tab "C".

overruled in part, and that attorney's fees should not be recoverable in a first party insurance situation unless the insured proves that the insurance company acted in bad faith.

### SUMMARY OF THE ARGUMENT

Although ordinarily damages recoverable for breach of contract include general and consequential damages, it is clear that the case law treats insurance contracts differently than other contracts. Prior to *Beck v. Farmers Insurance Exchange*, 701 P.2d 795 (Utah 1985)<sup>4</sup>, the only damages that could be recovered by an insured for breach of an insurance contract in a first-party context, including breach of the implied covenant of good faith and fair dealing, was the predictable fixed dollar amount of coverage provided by the policy. *Beck* changed the law to provide an insured with a remedy for its insurer's bad faith conduct, and to provide an incentive to insurance companies not to act unreasonably and in bad faith. To provide this incentive, *Beck* permits the recovery of consequential losses arising from a breach of the implied good faith covenant, including attorney's fees, the loss of a home or business, bankruptcy, and in unusual cases, mental anguish.

In a subsequent insurance case, *Billings v. Union Bankers Insurance Company*, *supra*, the Utah Supreme Court once again treated insurance contracts

---

<sup>4</sup> A copy of *Beck* is included in the Addendum at Tab "D".

differently than other contracts and allowed an award of attorney's fees for breach of the express terms of an insurance contract in a first-party context, even when the insurance contract failed to provide for an award of attorney's fees to the prevailing party. By its language, *Billings* confirmed that the purpose of the broad range of consequential damages available under *Beck* is to provide insurance companies with an incentive to act reasonably and in good faith, and that the incentive will be lost if consequential damages can be recovered by an insured for an insurer's breach of the express contract terms. Accordingly, *Billings* implies that no consequential damages can be recovered for a breach of the express terms of an insurance contract. For reasons that are not clear, *Billings* nevertheless allows an insured to recover his attorney's fees for breach of the express contract terms, even though this limited measure of consequential damages penalizes an insurance company that acts reasonably in denying a claim that a court or jury subsequently decides must be paid. Although *Billings* has never been overruled, Utah insurance cases subsequent to *Billings* have failed to award any consequential damages in a first party situation, including attorney's fees, unless there has been a breach of the implied good faith covenant.

It would not further *Beck*'s purpose of encouraging insurers to act reasonably if consequential damages can be recovered against an insurer who is ultimately determined by a court to have incorrectly denied coverage, regardless of



how reasonable the denial. Accordingly, consequential damages, including attorney's fees, should not be recoverable for breach of the express terms of an insurance contract.

With respect to the second question certified by the U.S. District Court, the Utah Insurance Code did not provide a private cause of action in 2000. If it did, the statute would say so. It is not for this Court, or any trial court, to imply a private cause of action when the statute is silent. This is a matter that should be left to the Utah legislature. Furthermore, to permit a private cause of action would vitiate the "fairly debatable" defense.

## ARGUMENT

### I

#### **CONSEQUENTIAL DAMAGES SHOULD NOT BE RECOVERABLE FOR A BREACH OF THE EXPRESS TERMS OF AN INSURANCE CONTRACT**

##### **A. *Beck v. Farmers Insurance Exchange* Enlarged The Remedy For An Insurer's Breach Of The Implied Covenant Of Good Faith And Fair Dealing In A First-Party Situation**

In *Beck v. Farmers Insurance Exchange*, *supra*, the Utah Supreme Court held that when an insurance company fails to bargain or settle a claim with its insured in good faith, the insured can recover damages beyond the maximum dollar amount of insurance provided by the policy. Until *Beck*, an insured's damages were limited to the policy coverage and the insured had no effective remedy

against an insurer that refused to bargain or settle in good faith in a first-party situation. *Id.* 701 P. 2d at 798; *see, Lyon v. Hartford Accident and Indemnity Co.*, 25 Utah 2d 311, 480 P. 2d 739 (1971); *See also*, William Kevin Tanner, *Bad Faith Claims Against Insurers: The State of Utah Law Fifteen Years after Beck v. Farmers Insurance Exchange*, 15 B.Y.U. J. Pub. L. 53. *Beck* confirmed that an insurer has an implied duty to bargain or settle in good faith, and that a breach of this duty gives rise to a claim in contract, not tort.

Other states, California among them, had adopted a tort approach in an effort to provide insurance companies selling insurance in their states with an incentive to honor their duty of good faith. *See*, Theresa Viani Agee, Note, *Breach of an Insurer's Good Faith Duty to its Insured: Tort or Contract?*, 1988 Utah L. Rev. 135, 137, fn 20. These states, so *Beck* observed, believed that existing contract principles would not allow recovery beyond policy limits, and had instead adopted a tort approach that *Beck* found to be theoretically unsound.

To provide the stated incentive to insurance companies to act in good faith, *Beck* expanded the remedy available to insureds and held that consequential damages, i.e., those reasonably within the contemplation of, or reasonably foreseeable by, the parties at the time the contract was made, can be recovered for breach of the implied covenant of good faith and fair dealing.

Although it rejected the tort approach, *Beck* observed that the objective of these other states was meritorious and that the measure of damages for breach of the implied covenant of good faith should “not ignore the principle 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. *Beck* at 802.

*Beck* recognized that in an action for breach of a duty to bargain in good faith, a broad range of recoverable consequential damages is conceivable, including damages stemming from bankruptcy, loss of peace of mind, loss of home or business, and in unusual cases, mental anguish. *Id.* Gary Machan claimed these very types of consequential losses in the present case, 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. Plaintiff’s Opposition To Motion For Summary Judgment at pp. 11-12, U.S. District Court Docket Entry 135.

*Beck* found a remedy for insureds whose insurance companies refuse to bargain or settle claims in good faith by acknowledging that in a first party insurance situation, the relationship between the insured and its insurer is purely

contractual. Earlier, in *Lyon v. Hartford Accident and Indemnity Co.*, supra, the Court had denied an insured a tort remedy for its insurance company's bad faith and until *Beck* it appeared that an insured had no effective remedy. Thus, by shifting the focus from tort to contract, *Beck* found a remedy.

The obvious corollary to *Beck*'s objective to provide an incentive to insurance companies to bargain and settle in good faith by penalizing them if they do not is that insurance companies should not be penalized for asserting valid defenses and denying questionable claims. The duty of good faith is a two way street and it would be unfair not to permit an insurer to have a legitimate dispute with an insured resolved before having to pay the claim. Subsequent case law addressed this precise issue.

**B. *Billings v. Union Bankers Insurance Company* Confirmed That Consequential Damages Are Not Recoverable In The Absence of Bad Faith**

In a case eleven years after *Beck*, the Third District Court gave an improper jury instruction suggesting that consequential damages were available to an insured if he could convince the jury that his insurance company had breached the express terms of his insurance contract. In *Billings v. Union Bankers Insurance Company*, supra, both the insured's claim that his insurance company had breached the express covenants of his insurance policy, and his claim that the implied good faith covenant had been breached, went to the jury. The insured demanded

consequential damages and the district court instructed the jury that if it found that Union Bankers had breached the express coverage provision of the policy it could award the insured the value of his policy benefits, and if the jury found Union Bankers breached either the express coverage provision or the implied covenant of good faith and fair dealing, the jury could award the insured consequential damages for emotional suffering and mental anguish, medical expenses, lost income and earning capacity, and the extent to which the insured had been limited in pursuing and enjoying the ordinary affairs of life. *Billings*, 918 P.2d at 464.

Union Bankers Insurance Company argued on appeal that the consequential damages allowed by *Beck* are available only for breach of the implied good faith covenant, not, as the district court had instructed the jury, for breach of the express terms of the insurance policy. The Utah Supreme Court agreed:

“[T]he implied covenant imposes a duty on first-party insurers to act in an objectively reasonable manner in handling an insured’s claim. 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.”...

*Id.* at 466.

*Billings* confirmed that *Beck* had departed from the “restrictive traditional contract damages approach” and had allowed consequential damages for breach of

an insurance contract beyond the bare contract terms.<sup>5</sup> *Billings* at 466. *Billings* explained that *Beck* did not intend to allow consequential damages for breach of the express terms of an insurance contract; rather, “We recognized that in appropriate circumstances, ‘consequential damages for breach of contract may reach beyond the bare contract terms’” (emphasis added). *Id.* Obviously, the “appropriate circumstance” to which *Billings* referred is a breach of the implied covenant of good faith and fair dealing.

*Billings* recognized that any time a claim is disputed by an insurance company there is likely to be a toll on the insured, but the insurance company should not be exposed beyond the limits of its coverage when it has not settled a fairly debatable claim and has elected to have the dispute resolved before having to pay the claim. *See, Billings* at 467. So, while *Beck* emphasized that an insurance company needs an incentive to act reasonably and in good faith, *Billings* explained that it would be unfair not to permit a careful insurer who has a legitimate dispute

---

<sup>5</sup> In a case four years after *Billings*, the Utah Court of Appeals recognized that *Beck* treats insurance contracts differently than other contracts when it said:

[O]ur Supreme Court in *Beck* stated that insurance contracts are to be treated differently than other contracts for the simple reason that an insured frequently faces catastrophic consequences if funds are not available within a reasonable period of time to cover an insured loss; damages for losses well in excess of the policy limit, such as for home or business, may therefore be foreseeable and provable.

*Pugh v. North Am. Warranty Servs., Inc.*, 1 P. 3d 570, 575 (Ut. Ct. App. 2000).

with an insured over a claim to have the dispute resolved before having to pay the claim. *Billings* explained:

“[I]t 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. Such an insurer ought to incur no greater damage exposure than any other person breaching the express terms of a contract. Indeed, it would be unfair not to permit an insurer who has a legitimate dispute with an insured over a claim to have the dispute resolved before having to pay the claim. Exposure to the sweeping measure of damages available for breach of the implied covenant would effectively deny any careful insurer the option of declining to pay a contested claim and awaiting the outcome of the dispute.

*Billings* at 466-467.

Although *Billings* allowed the plaintiff in that case to recover his attorney’s fees as consequential damages for breach of the express terms of the insurance contract, *Billings* otherwise made clear that the consequential damages the plaintiff was seeking for breach of the implied good faith covenant were not recoverable absent a breach of the implied covenant.

In spite of its restriction on *Beck*’s consequential damages to a breach of the implied good faith covenant, the present case with Gary Machan suggests that *Billings* may have raised more questions than it answered, including: (1) When *Billings* uses language like “broad consequential damages” and “the sweeping measure of damages available for breach of the implied covenant,” what did it

mean? Machan says that this language in *Billings* implies that there may still be consequential damages other than those specifically mentioned in *Beck* that may be recoverable in the absence of bad faith, even though his own consequential losses appear to be remarkably similar to the bad faith losses enumerated in *Beck*; (2) Why are attorney's fees recoverable as consequential damages for breach of the express terms of an insurance policy? This obviously penalizes an insurer who in good faith disputes a legitimate claim, and, when the insurance policy lacks an attorney's fees provision, this additional remedy affords an insured a greater measure of damages for breach of contract than he would otherwise be entitled to recover.

C. **Campbell v. State Farm Mutual Automobile Insurance Company Leaves No Doubt That Damages Beyond The Fixed Dollar Amount of Coverage Are Only Available For Breach Of The Implied Covenant Of Good Faith**

*Campbell v. State Farm Mutual Automobile Insurance Company*, 65 P.3d 1134 (Utah 2001), a case involving a third party insurance claim, seems to answer one of the questions raised by *Billings*. *Campbell* confirmed, although admittedly in *dicta*, that the purpose of allowing consequential damages in first-party bad faith actions beyond the predictable fixed dollar amount of coverage provided by the policy is to remove any incentive for an insurer to act in bad faith, thus suggesting that any damages beyond the policy limits are not recoverable absent a showing of bad faith:



“Under Utah law, plaintiffs may recover attorney fees if they are successful in pursuing a first-party bad faith suit against their insurer. *Billings v. Union Bankers Ins. Co.*, 918 P.2d 461, 468 (Utah 1996). Such actions fall within the rule that the damages available to plaintiffs “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 foreseeable by, the parties at the time the contract was made.” *Beck v. Farmers Ins. Exch.*, 701 P.2d 795, 801 (Utah 1985). **The rationale behind allowing recovery of both general and consequential damages in first-party, bad faith actions is “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.”** *Billings*, 918 P.2d at 466. Consequential damages in first-party bad faith actions can be awarded for such things as attorney fees, loss of a home or business, damages flowing from bankruptcy, and mental anguish, provided such damages are foreseeable. *Id.* at 468; *Beck*, 701 P.2d at 802. (bold and underline added).

*Campbell*, 65 P. 3d 1134, 1168, ¶ 120.

Utah law treats insurance contracts differently than other contracts.

Consequential damages are not available for every breach of an insurance contract.

By expanding the measure of “damages caused by such a breach [of the implied covenant] beyond the predictable fixed dollar amount of coverage provided by the policy,” Utah law provides an incentive for an insurance company to honor the

implied good faith covenant.<sup>6</sup> *Campbell* makes clear that there is not a broad array of consequential damages that may be available for breach of the implied covenant of good faith, and a more narrow array of consequential damages that may be available for breach of the express terms of the insurance policy.

**D. Allowing Attorney's Fees Without Proving Bad Faith Contravenes Beck's Objectives**

We have no good answer to the second question implicit in *Billings*.<sup>7</sup>

Allowing an insured to recover attorney's fees as consequential damages for

---

<sup>6</sup> We are aware of only one reported Utah decision, other than *Billings*, where an insured sought consequential damages above policy limits, other than attorney's fees, without specifically alleging bad faith. In *Castillo v. Atlanta Casualty Co.*, 939 P.2d 1204, 1211 (Ut. Ct. App. 1997), *cert. denied* 945 P.2d 1118 (1997), the insureds sought consequential damages for the lost use of their automobile when their insurer failed to promptly pay uninsured motorist coverage. Although the insureds failed the second required prong for an award of consequential damages (i.e., damages must be proved with a reasonable degree of certainty), the Court of Appeals suggested that consequential damages would otherwise have been recoverable. An obligation to promptly and reasonably bargain and settle a claim is precisely the duty of good faith that *Beck* says is inherent in all insurance contracts. Thus, it appears that the insurer's breach in *Castillo* amounted to a breach of the implied covenant of good faith, not a breach of the express terms of the insurance policy, even though bad faith was apparently not pleaded.

<sup>7</sup> The supposed genesis for allowing recovery of attorneys fees as consequential damages for breach of the express terms of an insurance contract is *Canyon Country Store v. Bracey*, 781 P.2d 414 (Utah 1989). However, the *Billings* dissent later pointed out that it was unclear whether the attorneys fees in *Canyon Country* were awarded for breach of the implied covenant or for breach of the express terms of the insurance contract. See, *Billings*, 918 P.2d at 469 (Howe, J., dissenting). Prior to *Billings*, the Utah Court of Appeals, basing its ruling on *Beck*, *Canyon Country*, and *Zions First National Bank v. National American Title Insurance Co.*, 749 P.2d 651 (Utah 1988), ruled in *Moore v. Energy Mutual Insurance Co.*, 814 P.2d 1141 (Ut. Ct. App. 1991), that attorneys fees were recoverable as consequential damages for breach of the express terms of an insurance contract. None of the three cases the Court of Appeals relied on supported *Moore*. *Beck*, of course, dealt only with a bad faith claim, and in *Zions First*

breach of the express terms of an insurance policy places an unfair hammer over the head of an insurer who legitimately disputes a questionable claim. This is precisely contrary to *Billings*' statement that "Such an insurer ought to incur no greater damage exposure than any other person breaching the express terms of a contract." Without *Billings*, the insured would not be awarded attorney's fees without an attorney's fees provision in the policy. See, *Turtle Management, Inc. v. Haggis Management, Inc.*, 645 P.2d 667, 671 (Utah 1982) (holding attorney's fees may be awarded only if authorized by statute or by contract).

Allowing attorney's fees as consequential damages absent a finding of bad faith also removes the "fairly debatable" shield that encourages insurance companies to contest unscrupulous claims. The Utah Supreme Court recently stated that, "The denial of a claim is reasonable if the insured's claim is fairly debatable. Under Utah law, if an insurer denies an 'insured's claim [that] is fairly debatable, [then] the insurer is entitled to debate it and cannot be held to have breached the implied covenant if it chooses to do so.'" *Prince v. Bear River Mutual Ins. Co.*, 56 P.3d 524, 533 (Utah 2002). "If the evidence presented creates a factual issue as to the claim's validity, there exists a debatable reason for denial, .

---

*National Bank* the Court of Appeals ruled that attorneys fees would have been recoverable had the insured made a bad faith claim, but that attorneys fees were specifically not recoverable for straight breach of contract in that case because there was no attorney's fees provision in the insurance contract. *Zions*, 749 P.2d 656.

.. eliminating the bad faith claim.” *Id.* at 535 (quoting *Callioux v. Progressive Ins. Co.*, 745 P.2d 838, 842 (Utah Ct. App. 1987)). The quite obvious purpose of the fairly debatable defense is to shield insurance companies from damages in excess of policy limits when they challenge questionable claims. *Billings* does injury to this defense.

Not surprisingly, *Billings* appears not to have been followed. No Utah state court decision subsequent to *Billings* allows attorney’s fees as consequential damages for breach of the express terms of an insurance policy.<sup>8</sup> A year after *Billings*, in *Gibbs M. Smith, Inc., v. U.S. Fidelity*, 949 P. 2d 337 (Utah 1997), the Court, without any mention of *Billings*, overturned the district court’s award of attorney’s fees for breach of an insurance contract in a first party situation and remanded for a determination as to whether the implied covenant of good faith and fair dealing had been breached and for an award of attorneys fees accordingly.

In *Pugh v. North American Warranty Services, supra.*, the Court of Appeals affirmed an award of attorney’s fees only after concluding that the insured had breached not the express policy terms, but the implied good faith covenant. The court stated:

---

<sup>8</sup> In an unpublished decision, the 10<sup>th</sup> Circuit Court of Appeals in *dicta* relied on *Billings* for the proposition that an insured can recover attorney’s fees as consequential damages for breach of the express terms of an insurance policy in a first party situation. *Johnson v. Life Investors Insurance Company of America.*, 216 F. 3d 1087, 2000 WL 954840 (10<sup>th</sup> Cir. 2000 ).

“Of course, to recover attorney’s fees for breach of an insurance contract, the insured must demonstrate that the insurer has breached the implied covenant to act in good faith in its performance of the insurance contract.

*Pugh*, 1 P.3d at 576.

*Beck’s* and *Billings’* stated objective to provide insurance companies with an incentive to act in good faith cannot be reconciled with allowing an award of attorney’s fees for breach of the express terms of the insurance policy. The dissent in *Billings* focused on this obvious inconsistency in logic and we suggest that the issue should now be revisited by the Court and this part of *Billings* should be overruled.

## II

### **MUJI AGREES WITH UNUM**

Because the Model Uniform Jury Instructions are in the process of being revised, we advise the Court of two MUJI instructions that support UNUM’s position, should the Court desire to provide confirmation or specific guidance to the committee charged with drafting new jury instructions.

#### **MUJI 21.4 Relationship Between Insurer and Insured.**

The relationship between insurer and insured is contractual. The insurance policy does not create a relationship of trust or reliance between the parties, it simply obligates the insurer to pay the covered claims submitted by the insured in accordance with the policy. Without more, a breach of the

terms of the policy can give rise only to a claim for damages under the policy.

*References:*

*Beck v. Farmers Ins. Exch.*, 701 P.2d 795 (Utah 1985)

**MUJI 21.9 General And Consequential Damages.**

If you find, by a preponderance of the evidence, that the insurer breached its contractual duty of good faith and fair dealing to the insured, you may award the insured compensatory damages. Damages recoverable for the breach of this duty are damages for those injuries or losses flowing naturally from the breach, and those losses or injuries which were reasonably within the contemplation of, or reasonably foreseeable by, the parties at the time the contract was made. *In awarding these damages, you may award an amount in excess of the policy limits specified in the insurance policy.* In determining the amount of damages to award, you may consider [the loss of the insured's property] [the insured's expenses and debt associated with the loss of the property] [the insured's bankruptcy] [the insured's loss of financial reputation and credit] [the insured's loss of income or profit] [the insured's past and future emotional suffering and mental anguish] [any other detriment naturally flowing from the insurer's breach]. However, only those factors that were reasonably foreseeable by the parties and that were proximately caused by the insurer's breach may be considered. (italics added)

*References:*

*Beck v. Farmers Ins. Exch.*, 701 P.2d 795 (Utah 1985)

### III

#### **THE UTAH INSURANCE CODE DID NOT PROVIDE A PRIVATE CAUSE OF ACTION IN 2000**

The U.S. District Court has asked whether Utah Code Ann. § 31A-26-301(1) (2000) provided a private right of action in 2000. The answer from this Court should be that it did not.

No Utah decision has ever recognized a private cause of action under Utah Code Ann. § 31A-26-301 (2000) which provides rather plainly that “Unless otherwise provided by law, an insurer shall timely pay every valid insurance claim made by an insured.”

The insurance code has been put in place as a regulatory scheme that governs the insurance industry. *See* Utah Code Ann. § 31A-1-102. Section 31A-26-301(1) (2000) demonstrates the regulatory nature of the statute:

“[B]y 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.”

As part of the regulatory scheme, the legislature specifically provided enforcement penalties and procedures for violations of Section 31A-26-301, as well as every other insurance statute, including fines, criminal penalties, and license suspension or revocation. *See* Utah Code Ann. § 31A-2-308 (2000). Not

surprisingly, the list of enforcement penalties and procedures does not include a private right of action.

The Utah appellate courts have consistently refused to create a private cause of action based on the violation of a statute when the statute itself does not specifically do so. *See, e.g., Cannon v. Travelers Indemnity Co.*, 994 P. 2d 824, 828 (Ut. Ct. App. 2000) (holding that the insurance unfair claims settlement practices statutes and rules do not give rise to a private right of action); *Milliner v. Elmer Fox & Co.*, 529 P.2d 806, 808 (Utah 1974). “The courts of this state are not generally in the habit of implying a private right of action based upon state law, absent some specific direction from the legislature.” *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); *see also J.H. by D.H. v. West Valley City*, 840 P.2d 115, 125 (Utah 1992) (declining to create private right of action to challenge city’s failure to follow statutory procedures in hiring officers); *Nielson v. Div. Of Peace Officer Standards & Training*, 851 P.2d 1201, 1204 (Utah Ct. App. 1993) (holding a private citizen had no right to compel agency to conduct disciplinary hearings); *Richards Irr. Co. v. Karren*, 880 P.2d 6 (Utah Ct. App. 1994) (the court refused to imply a private cause of action where statute provided for penalty, and there was no language regarding a private right of action in the statute).



In *Milliner, supra*, the Utah Supreme Court refused to create a private right of action based upon a statute defining certain actions as securities fraud. Though the statute made certain conduct criminal, “it [did] not provide for a private right of action for its violation.” Though the plaintiff urged the court to fashion a remedy, the court replied, “we are of the opinion that it is a matter best left to the legislature.” 529 P.2d at 809.

Disciplinary measures against an insurer for violations of the Insurance Code are enforced by the Insurance Commissioner, not private citizens. The Utah Insurance Code creates no private right of action, nor does it indicate any intent by the legislature to provide a private right of action.

In the U.S. District Court, Machan cited *Spackman v. Board of Education of Box Elder County School Dist.* 16 P.3d 533, 538 (Utah 2000) for the proposition that the Utah Supreme Court has adopted § 874A of the Restatement (Second) of Torts (1979) and that this Restatement section supports the proposition that a court may imply a private cause of action when a statute is silent on the issue. *See*, Plaintiff’s Opposition To Motion For Summary Judgment at pp. 37-38. In *Spackman*, however, the issue had absolutely nothing to do with state statutes. Rather, the issue was whether the Free and Equal Public Education Clause of the Utah Constitution (Art. X, § 1) and/or the Due Process Clause of the Utah Constitution (Art. I, § 7) are self-executing constitutional provisions that may be

directly enforced without implementing legislation. The Court's reliance on section 874A was limited solely to Constitutional provisions, not statutes, and *Spackman* does not aid Machan's position.

Finally, a judicially created private cause of action based on Utah Code Ann. § 31A-26-301 would completely eviscerate years of jurisprudence by removing the "fairly debatable" defense from insurance law. *See, Prince v. Bear River Mutual Ins. Co., supra*. Under current case law insurers are not subject to bad faith liability when a claim is fairly debatable. Creation of a private cause of action for Section 31A-26-301 would render the Court's bad faith jurisprudence meaningless.

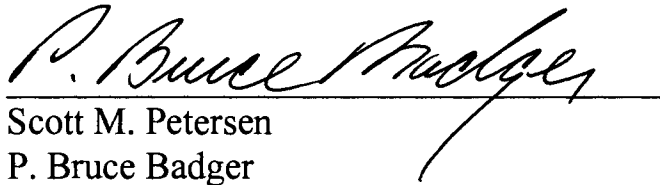
In summary, Utah Code Ann. § 31A-26-301 did not provide a private cause of action in 2000.

## CONCLUSION

The U.S. District Court should be advised that with respect to the first question certified, that the answer is "no". In a first party insurance situation an insured may not recover consequential damages, other than attorney's fees, for breach of the express terms of an insurance contract. We further suggest that the U.S. District Court should be advised that Utah law no longer allows an award of attorney's fees as consequential damages for breach of the express terms of an insurance policy.

With respect to the second question certified, the U.S. District court should again be advised that the answer is “no”. Utah Code Ann. §31A-26-301, entitled “Timely Payment of Claims” did not allow a private cause of action by the insured against his or her insurer for violation of the statute in 2000.

DATED this 17<sup>th</sup> day of February, 2004.



Scott M. Petersen

P. Bruce Badger

FABIAN & CLENDENIN

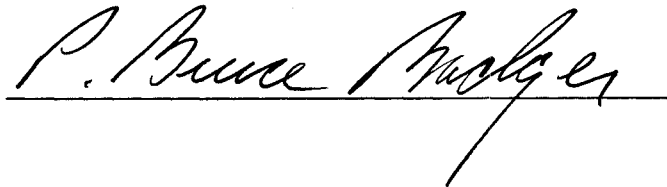
a Professional Corporation

Attorneys Co-Appellant UNUM Life  
Insurance Company of America

**CERTIFICATE OF HAND DELIVERY**

I hereby certify that on the 17<sup>th</sup> day of February, 2004, I caused to be hand delivered two (2) true and correct copies of **BRIEF OF CO-APPELLANT UNUM LIFE INSURANCE COMPANY OF AMERICA** to the following counsel of record:

L. Rich Humphreys  
CHRISTENSEN & JENSEN, P.C.  
50 South Main Street, Suite 1500  
Salt Lake City, Utah 84144

A handwritten signature in cursive script, reading "P. Bruce Hughes", is written over a horizontal line.

## ADDENDUM

- Tab A:      Order of Certification
- Tab B:      Utah Code Ann. § 31A-1-102 (2000)  
              Utah Code Ann. § 31A-2-308 (2000)  
              Utah Code Ann. § 31A-26-301 (2000)
- Tab C:      *Billings v. Union Bankers Insurance Company*, 918 P.2d 461  
              (Utah 1996)
- Tab D:      *Beck v. Farmers Insurance Exchange*, 701 P.2d 795 (Utah 1985)

Tab A

FILED  
CLERK, U.S. DISTRICT COURT  
22 SEP 03 PM 9:02  
DISTRICT OF UTAH  
DEPUTY CLERK

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); *Crutz 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.

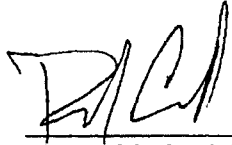
### **CONCLUSIONS**

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.

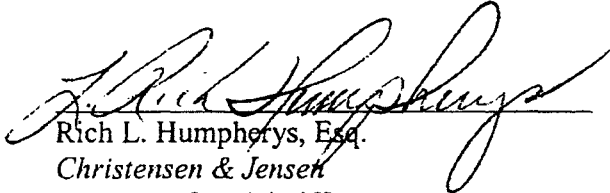
IT IS SO ORDERED this 22nd day of September, 2003.

BY THE COURT:

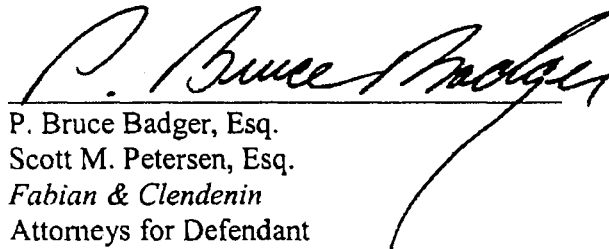
A handwritten signature in black ink, appearing to read 'P. G. Cassell', is written over a horizontal line.

Honorable Paul G. Cassell  
United States District Court

Approved as to form:



Rich L. Humpherys, Esq.  
*Christensen & Jensen*  
Attorneys for Plaintiff



P. Bruce Badger, Esq.  
Scott M. Petersen, Esq.  
*Fabian & Clendenin*  
Attorneys for Defendant

tsh

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:

Julianne R. Blanch, Esq.  
SNOW CHRISTENSEN & MARTINEAU  
10 EXCHANGE PLACE  
PO BOX 45000  
SALT LAKE CITY, UT 84145-5000  
JFAX 9,3630400

L. Rich Humpherys, Esq.  
CHRISTENSEN & JENSEN PC  
50 S MAIN STE 1500  
SALT LAKE CITY, UT 84144  
JFAX 9,3553472

Scott M. Petersen, Esq.  
FABIAN & CLENDENIN  
215 S STATE STE 1200  
PO BOX 510210  
SALT LAKE CITY, UT 84151  
EMAIL

Thomas J. Quinn, Esq.  
UNUM LIFE INSURANCE COMPANY  
2211 CONGRESS ST  
PORTLAND, ME 04122-0590

John Meagher, Esq.  
SHUTTS & BOWEN  
1500 MIAMI CENTER  
201 S BISCAYNE BLVD  
MIAMI, FL 33131



Tab B

the former licensee may not apply for a new license for five years without the express approval of the commissioner.

(6) Any person whose license is suspended or revoked under Subsection (2) shall, when the suspension ends or a new license is issued, pay all fees that would have been payable if the license had not been suspended or revoked, unless the commissioner by order waives the payment of the interim fees. If a new license is issued more than three years after the revocation of a similar license, this subsection applies only to the fees that would have accrued during the three years immediately following the revocation.

(7) The division shall promptly withhold, suspend, restrict, or reinstate the use of a license issued under this part if so ordered by a court. 1997

#### 31A-26-214. Probation.

(1) In any circumstances that would justify a suspension under Section 31A-26-213, the commissioner may instead, after a formal adjudicative proceeding, put the licensee on probation for a specified period no longer than 24 months.

(2) The probation order shall state the conditions for retention of the license, which shall be reasonable.

(3) Violation of the probation is grounds for revocation pursuant to any proceeding authorized under Title 63, Chapter 46b, Administrative Procedures Act. 1997

### 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. 1985

##### 31A-26-301.5. Health care claims practices.

(1) Except as provided in Section 31A-8-407, an insured retains ultimate responsibility for paying for health care services the insured receives. If a service is covered by one or more individual or group health insurance policies, all insurers covering the insured have the responsibility to pay valid health care claims in a timely manner according to the terms and limits specified in the policies.

(2) (a) Except as provided in Section 31A-22-610.1, a health care provider may bill and collect for any deductible, copayment, or uncovered service.

(b) A health care provider may bill an insured for services covered by health insurance policies or may otherwise notify the insured of the expenses covered by the policies. However, a provider may not make any report to a credit bureau, use the services of a collection agency, or use methods other than routine billing or notification until the later of:

(i) 15 days after the date all insurance companies covering the insured have paid their portion of the claim covered by the policies;

(ii) 60 days from the date all insurers covering the insured are billed for the covered service; or

(iii) in the case of medicare beneficiaries or retirees 65 years of age or older, 60 days from the date medicare determines its liability for the claim.

(c) Beginning October 31, 1992, all insurers covering the insured shall notify the insured of payment and the amount of payment made to the provider.

(3) The commissioner shall make rules consistent with this chapter governing disclosure to the insured of customary charges by health care providers on the explanation of benefits as part of the claims payment process. These rules shall be limited to the form and content of the disclosures on the explanation of benefits, and shall include:

(a) a requirement that the method of determination of any specifically referenced customary charges and the range of the customary charges be disclosed; and

(b) a prohibition against an implication that the provider is charging excessively if the provider is:

(i) a participating provider; and

(ii) prohibited from balance billing. 2000

##### 31A-26-302. Settlement of claims in credit life and disability insurance.

(1) The creditor shall promptly report all claims to the insurer or its designated claim representative. The insurer shall maintain adequate claims files. All claims shall be settled as soon as possible in accordance with the terms of the insurance contract.

(2) The insurer shall pay all claims either by draft drawn upon the insurer or by check of the insurer to the order of the claimant to whom payment of the claim is due pursuant to the policy provisions, or upon direction of that claimant to another.

(3) No person other than the insurer or its designated claim representative may settle or adjust claims. The creditor may not be designated as a claims representative. 1985

##### 31A-26-303. Unfair claim settlement practices.

(1) No insurer or person representing an insurer may engage in any unfair claim settlement practice under Subsections (2), (3), and (4).

(2) Each of the following acts is an unfair claim settlement practice:

(a) knowingly misrepresenting material facts or the contents of insurance policy provisions at issue in connection with a claim under an insurance contract; however, this provision does not include the failure to disclose information;

(b) attempting to use a policy application which was altered by the insurer without notice to, or knowledge, or consent of, the insured as the basis for settling or refusing to settle a claim; or

(c) failing to settle a claim promptly under one portion of the insurance policy coverage, where liability and the amount of loss are reasonably clear, in order to influence settlements under other portions of the insurance policy coverage, but this Subsection (2)(c) applies only to claims made by persons in direct privity of contract with the insurer.

(3) Each of the following is an unfair claim settlement practice if committed or performed with such frequency as to indicate a general business practice by an insurer or persons representing an insurer:

(a) failing to acknowledge and act promptly upon communications about claims under insurance policies;

(b) failing to adopt and implement reasonable standards for the prompt investigation and processing of claims under insurance policies;

is filed under Subsection (2). After the filing of the complaint, only the attorney general may compromise the forfeiture.

(2) When a person fails to comply with an order issued under Subsection 31A-2-201(4), including a forfeiture order, the commissioner may file an action in any court of competent jurisdiction or obtain a court order or judgment:

- (a) enforcing the commissioner's order;
- (b) (i) directing compliance with the commissioner's order and restraining further violation of the order; and

- (ii) subjecting the person ordered to the procedures and sanctions available to the court for punishing contempt if the failure to comply continues; or

- (c) imposing a forfeiture in an amount the court considers just, up to \$10,000 for each day the failure to comply continues after the filing of the complaint until judgment is rendered.

(3) The Utah Rules of Civil Procedure govern actions brought under Subsection (2), except that the commissioner may file a complaint seeking a court-ordered forfeiture under Subsection (2)(c) no sooner than two weeks after giving written notice of the commissioner's intention to proceed under Subsection (2)(c). The commissioner's order issued under Subsection 31A-2-201(4) may contain a notice of intention to seek a court-ordered forfeiture if the commissioner's order is disobeyed.

(4) If, after a court order is issued under Subsection (2), the person fails to comply with the commissioner's order or judgment:

- (a) the commissioner may certify the fact of the failure to the court by affidavit; and

- (b) the court may, after a hearing following at least five days written notice to the parties subject to the order or judgment, amend the order or judgment to add the forfeiture or forfeitures, as prescribed in Subsection (2)(c), until the person complies.

(5) (a) The proceeds of all forfeitures under this section, including collection expenses, shall be paid into the General Fund.

- (b) The expenses of collection shall be credited to the Insurance Department's budget.

- (c) The attorney general's budget shall be credited to the extent the Insurance Department reimburses the attorney general's office for its collection expenses under this section.

(6) (a) Forfeitures and judgments under this section bear interest at the rate charged by the United States Internal Revenue Service for past due taxes on the:

- (i) date of entry of the commissioner's order under Subsection (1); or

- (ii) date of judgment under Subsection (2).

- (b) Interest accrues from the later of the dates described in Subsection (6)(a) until the forfeiture and accrued interest are fully paid.

(7) A forfeiture may not be imposed under Subsection (2)(c) if:

- (a) at the time the forfeiture action is commenced, the person was in compliance with the commissioner's order; or

- (b) the violation of the order occurred during the order's suspension.

(8) The commissioner may seek an injunction as an alternative to issuing an order under Subsection 31A-2-201(4).

(9) (a) A person is guilty of a class B misdemeanor if that person:

- (i) intentionally violates:

- (A) an insurance statute or rule of this state;

- or

- (B) an order issued under Subsection 31A-2-201(4);

- (ii) intentionally permits a person over whom that person has authority to violate:

- (A) an insurance statute or rule of this state;

- or

- (B) an order issued under Subsection 31A-2-201(4); or

- (iii) intentionally aids any person in violating:

- (A) an insurance statute or rule of this state;

- or

- (B) an order issued under Subsection 31A-2-201(4).

- (b) Unless a specific criminal penalty is provided elsewhere in this title, the person may be fined not more than:

- (i) \$10,000 if a corporation; or

- (ii) \$5,000 if a person other than a corporation.

- (c) If the person is an individual, the person may, in addition, be imprisoned for up to one year.

- (d) As used in this Subsection (9), "intentionally" has the same meaning as under Subsection 76-2-103(1).

(10) (a) After a hearing, the commissioner may, in whole or in part, revoke, suspend, place on probation, limit, or refuse to renew the licensee's license or certificate of authority:

- (i) when a licensee of the department, other than a domestic insurer:

- (A) persistently or substantially violates the insurance law; or

- (B) violates an order of the commissioner under Subsection 31A-2-201(4);

- (ii) if there are grounds for delinquency proceedings against the licensee under Section 31A-27-301 or Section 31A-27-307; or

- (iii) if the licensee's methods and practices in the conduct of the licensee's business endanger, or the licensee's financial resources are inadequate to safeguard, the legitimate interests of the licensee's customers and the public.

- (b) Additional license termination or probation provisions for licensees other than insurers are set forth in Sections 31A-19a-303, 31A-19a-304, 31A-23-216, 31A-23-217, 31A-25-208, 31A-25-209, 31A-26-213, 31A-26-214, 31A-35-501, and 31A-35-503.

(11) The enforcement penalties and procedures set forth in this section are not exclusive, but are cumulative of other rights and remedies the commissioner has pursuant to applicable law.

1999

### 31A-2-309. Service of process through state officer.

(1) The commissioner, or the lieutenant governor when the subject proceeding is brought by the state, is the agent for receipt of service of any summons, notice, order, pleading, or any other legal process relating to a Utah court or administrative agency upon the following:

- (a) all insurers authorized to do business in this state, while authorized to do business in this state, and thereafter in any proceeding arising from or related to any transaction having a connection with this state;

- (b) all surplus lines insurers for any proceeding arising out of a contract of insurance that is subject to the surplus lines law, or out of a certificate, cover note, or other confirmation of that type of insurance;

- (c) all unauthorized insurers or other persons assisting unauthorized insurers under Subsection 31A-15-102(1) by doing an act specified in Subsection 31A-15-102(2), for a proceeding arising out of the transaction that is subject to the unauthorized insurance law;

- (d) any nonresident agent, broker, consultant, adjuster, and third party administrator, while authorized to do

(3) Subsections (1) and (2) do not apply to the extent that the law specifically provides otherwise. 1991

### 31A-2-303. Notice.

(1) If the commissioner determines that the number of persons affected by a proposed action is so great as to render it impracticable to serve each person affected with a copy of an order, notice of hearing, or other notice, the commissioner shall:

(a) provide a copy of the order, notice of hearing, or other notice to all persons who have filed with the department a general request to be informed of this type of action, or if fewer than ten persons have requested this type of notice, provide a copy to those who have and also to others affected by the notice or order so that at least ten persons receive the notice or order who are collectively representative of the class of persons whose legal status, pecuniary interests, or other substantial interests will be affected by the proposed action; and

(b) publish a copy of the order, notice of hearing, or other notice under Subsection (2).

(2) When this title requires the commissioner to publish an order, notice of hearing, or other document in newspapers, the commissioner shall cause the notice or order to be published at least once during each of the four weeks preceding the hearing, effective date, or other critical event, in at least two newspapers with sufficient circulation and appropriate location to best provide actual notice. 1987

### 31A-2-304. Auxiliary procedural powers.

The commissioner, or his delegate authorized for a particular matter over his handwritten signature, may administer oaths, take testimony, issue subpoenas, and take depositions in connection with any hearing, meeting, examination, investigation, or other proceeding that the commissioner may conduct. The subpoena shall have the same effect and shall be served in the same manner as if issued from a court of record. Sections 78-24-7 and 78-32-15 apply to the enforcement of the process issued by the commissioner or his delegate. 1985

### 31A-2-305. Immunity from prosecution.

(1) If a natural person declines to appear, testify, or produce any record or document in any proceeding instituted by the commissioner or in obedience to the subpoena of the commissioner, the commissioner may apply to a judge of the district court where the proceeding is held for an order to the person to attend, testify, or produce records or documents as requested by the commissioner. In the event a witness asserts a privilege against self-incrimination, testimony and evidence from the witness may be compelled pursuant to Title 77, Chapter 22b, Grants of Immunity.

(2) If a person claims the privilege against self-incrimination and refuses to appear, testify, or produce documents in response to probative evidence against him in a proceeding to revoke or suspend his license, and if the testimony or documents would have been admissible as evidence in a court of law except for the Fifth Amendment privilege, the refusal to appear, testify, or produce documents is, for noncriminal proceedings only, rebuttable evidence of the facts on which the proceeding is based. 1997

### 31A-2-306. Judicial review — Costs.

(1) A person aggrieved by a rule or order of the commissioner, or aggrieved by the commissioner's failure to act when he has a duty to act, may obtain judicial review.

(2) The court reviewing agency actions governed by this title shall give priority to those actions and shall hear and determine them promptly.

(3) Costs shall be awarded as in civil cases. If the court finds that the appeal from action or inaction stemmed from the bad faith or malice of the commissioner, the court may award

reasonable attorney's fees to the prevailing petitioner. Section 63-30-23 applies to the extent the attorney's fees awarded under this subsection exceed \$10,000 for any one appeal. 1987

### 31A-2-307. Declaratory interpretation of statutes — Procedure.

(1) The commissioner or any other person with a substantial interest in the result may petition the Third District Court for Salt Lake County for a declaratory judgment interpreting any provision of this title as applied to stipulated facts.

(2) The court may require that notice be given to persons that may be affected by the judgment. These persons may participate in the proceeding.

(3) The court in its discretion may require the commissioner and any other participating parties to provide testimony and documentary evidence necessary for a fair disposition of the case.

(4) The court may decline to proceed on the petition if it believes the petition is frivolous, or the declaratory relief is unnecessary or has the possibility of prejudicing persons who cannot practicably be made parties to the proceeding.

(5) The court may declare the meaning of the statute. The declaration has the effect of a final judgment or decree.

(6) Any participating party may obtain judicial review of the decision.

(7) The costs of the proceeding shall be paid by the petitioner unless the commissioner is the petitioner, in which case all parties shall bear their own costs. "Costs" means:

(a) fees of the clerk and marshal;

(b) fees of the court reporter or the transcriber of a tape of the proceedings for all or any part of the transcript necessarily obtained for use in the case;

(c) fees and disbursements for printing and witnesses;

(d) fees for exemplification and copies of papers necessarily obtained for use in the case; and

(e) compensation of court-appointed experts or interpreters. Reimbursements shall be made to the General Fund, and shall be added back to the department's budget, except to the extent the department forwards a reimbursement to the attorney general's office, in which case the attorney general's budget shall be credited with the reimbursement. 1988

### 31A-2-308. Enforcement penalties and procedures.

(1) (a) A person who violates any insurance statute or rule or any order issued under Subsection 31A-2-201(4) shall forfeit to the state twice the amount of any profit gained from the violation, in addition to any other forfeiture or penalty imposed.

(b) (i) The commissioner may order an individual agent, broker, adjuster, or insurance consultant who violates an insurance statute or rule to forfeit to the state not more than \$2,500 for each violation.

(ii) The commissioner may order any other person who violates an insurance statute or rule to forfeit to the state not more than \$5,000 for each violation.

(c) (i) The commissioner may order an individual agent, broker, adjuster, or insurance consultant who violates an order issued under Subsection 31A-2-201(4) to forfeit to the state not more than \$2,500 for each violation. Each day the violation continues is a separate violation.

(ii) The commissioner may order any other person who violates an order issued under Subsection 31A-2-201(4) to forfeit to the state not more than \$5,000 for each violation. Each day the violation continues is a separate violation.

(d) The commissioner may accept or compromise any forfeiture under this Subsection (1) until after a complaint



**30-8-8. Limitations of actions.**

Any statute of limitations applicable to an action asserting a claim for relief under a premarital agreement is tolled during the marriage of the parties to the agreement. 1994

**30-8-9. Application and construction.**

This act shall be applied and construed to effectuate its general purpose to make uniform the law with respect to the subject of this act among states enacting it. 1994

**TITLE 31****INSURANCE [REPEALED]****TITLE 31A****INSURANCE CODE****Chapter**

1. General Provisions.
2. Administration of the Insurance Laws.
3. Department Funding, Fees, and Taxes.
4. Insurers in General.
5. Domestic Stock and Mutual Insurance Corporations.
6. Service Insurance Corporations [Repealed].
- 6a. Service Contracts.
7. Nonprofit Health Service Insurance Corporations.
8. Health Maintenance Organizations and Limited Health Plans.
9. Insurance Fraternal.
10. Annuities.
11. Motor Clubs.
12. State Risk Management Fund.
13. Employee Welfare Funds and Plans.
14. Foreign Insurers.
15. Unauthorized Insurers, Surplus Lines, and Risk Retention Groups.
16. Insurance Holding Companies.
17. Determination of Financial Condition.
18. Investments.
19. Rate Regulation [Renumbered].
- 19a. Utah Rate Regulation Act.
20. Underwriting Restrictions.
21. Insurance Contracts in General.
22. Contracts in Specific Lines.
23. Insurance Marketing — Licensing Agents, Brokers, Consultants, and Reinsurance Intermediaries.
24. Regulation of Independent Escrows [Repealed].
25. Third Party Administrators.
26. Insurance Adjusters.
27. Insurers Rehabilitation and Liquidation.
28. Guaranty Associations.
29. Comprehensive Health Insurance Pool Act.
30. Individual and Small Employer Health Insurance Act.
31. Insurance Fraud Act.
32. Medical Care Savings Account Act [Repealed].
- 32a. Medical Care Savings Account Act.
33. Workers' Compensation Fund.
34. Voluntary Health Insurance Purchasing Alliance Act.
35. Bail Bond Sureties and Agents Act.

**CHAPTER 1****GENERAL PROVISIONS****Part I****Purposes, Scope, and Application****Section**

- 31A-1-101. Short title.  
31A-1-102. Purposes.

**Section**

- 31A-1-103. Scope and applicability of title.  
31A-1-104. Authorization to do insurance business.  
31A-1-105. Presumption of jurisdiction.  
31A-1-106. Residual unlicensed domestic insurers.  
31A-1-107. Licensees under former Title 31.  
31A-1-108. Corporations in the process of organizing.  
31A-1-109. Name of licensee.

**Part II****Construction and Interpretation**

- 31A-1-201. Construction.  
31A-1-202. Effect of repeal of former provisions.  
31A-1-203. Interpretive rules.  
31A-1-204. Repealed.  
31A-1-205. Severability.

**Part III****Definitions**

- 31A-1-301. Definitions.

**PART I****PURPOSES, SCOPE, AND APPLICATION****31A-1-101. Short title.**

This title is known as the "Insurance Code." 1985

**31A-1-102. Purposes.**

The purposes of the Insurance Code are to:

- (1) ensure the solidity of insurers doing business in Utah;
- (2) ensure that policyholders, claimants, and insurers are treated fairly and equitably;
- (3) ensure that Utah has an adequate and healthy insurance market, characterized by competitive conditions, the spirit of innovation, and the exercise of initiative;
- (4) provide for an insurance department that is expert in the field of insurance and able to enforce the Insurance Code effectively;
- (5) encourage cooperation between the Insurance Department and other Utah regulatory bodies, as well as other federal and state governmental entities;
- (6) preserve and improve state regulation of insurance;
- (7) maintain freedom of contract and enterprise;
- (8) encourage self regulation of the insurance industry;
- (9) encourage loss prevention as part of the insurance industry;
- (10) keep the public informed on insurance matters; and
- (11) achieve other purposes stated elsewhere in the Insurance Code. 1985

**31A-1-103. Scope and applicability of title.**

(1) This title does not apply to:

- (a) retainer contracts made by attorneys-at-law with individual clients with fees based on estimates of the nature and amount of services to be provided to the specific client, and similar contracts made with a group of clients involved in the same or closely related legal matters;
- (b) arrangements for providing benefits that do not exceed a limited amount of consultations, advice on simple legal matters, either alone or in combination with referral services, or the promise of fee discounts for handling other legal matters;

Tab C

Glen A. BILLINGS, as guardian ad litem  
for Stanley D. Billings, a protected per-  
son, Plaintiff, Appellee, and Cross-Appel-  
lant,

v.

UNION BANKERS INSURANCE COM-  
PANY, a Texas corporation, Defendant,  
Appellant, and Cross-Appellee.

No. 940098.

Supreme Court of Utah.

March 19, 1996.

Rehearing Denied July 1, 1996.

Insured sued catastrophic health insurer for breach of contract and bad faith in connection with denial of coverage for costs of transitional treatment for brain injuries sustained in motorcycle accident. Following jury trial after remand, 819 P.2d 803, the Third District Court, Salt Lake County, Leslie A. Lewis, J., awarded damages and attorney fees to insured. Insurer appealed and insured cross-appealed. The Supreme Court, Zimmerman, C.J., held that: (1) first-party insurer has "fairly debatable" defense to claim for breach of implied covenant of good faith and fair dealing; (2) insured's claim was not rendered fairly debatable as matter of law by existence of fact question about nature of treatment received; (3) broad measure of consequential damages awardable for first-party insurer's breach of implied covenant is not available for breach of contract's express terms; (4) evidence was sufficient to sustain verdict for insured under theory that he had suffered mental anguish as result of insurer's breach of implied covenant; and (5) no evidence supported trial court's finding that insured's contingency fee arrangement was not foreseeable.

Affirmed in part, vacated in part, and remanded.

Howe, J., filed concurring and dissenting opinion in which Russon, J., joined.

### 1. Appeal and Error ⇨181

Supreme Court declined to review challenges that appellant did not raise below, where appellant failed to show special circumstances warranting such review, as required for application of "interests of justice" exception to waiver principle. Rules Civ. Proc., Rule 51.

### 2. Appeal and Error ⇨842(2)

Interpretation of effect of prior judicial decision is conclusion of law which Supreme Court review for correctness.

### 3. Appeal and Error ⇨842(2)

Although Supreme Court will carefully review trial court's conclusion that insured's claim is or is not fairly debatable, within context of implied covenant of good faith and fair dealing, it will grant trial court's conclusion some deference.

### 4. Insurance ⇨124(1)

"First-party insurance contract" is insurance agreement where insurer agrees to pay claims submitted to it by insured for losses suffered by insured.

See publication Words and Phrases for other judicial constructions and definitions.

### 5. Insurance ⇨602.5

Under *Beck*, first-party insurer has "fairly debatable" defense to claim for breach of implied covenant of good faith and fair dealing in insurance contract; that is, first-party insurer may not be held liable for breaching implied covenant on ground that it wrongfully denied coverage if insured's claim, although later found to be proper, was fairly debatable at time it was denied.

### 6. Insurance ⇨602.2(1)

Whether first-party insurer has acted reasonably when confronted by insured's claim, so as to satisfy implied covenant of good faith and fair dealing in insurance contract, is objective question to be determined without considering insurer's subjective state of mind, although this standard is not to be construed as one of strict liability.

### 7. Insurance ⇨602.12(2)

Insured's claim for coverage under catastrophic health policy for costs of transitional

treatment for brain injuries sustained in motorcycle accident was not rendered fairly debatable as matter of law by existence of fact question about nature of treatment received, for purposes of "fairly debatable" defense to claim for breach of implied covenant of good faith and fair dealing in insurance contract, especially since there was no determination that insurance contract itself was sufficiently ambiguous to create fact question.

#### 8. Insurance ⇨602.10(1)

Broad measure of consequential damages awardable for first-party insurer's breach of implied covenant of good faith and fair dealing in insurance contract, which includes such things as mental anguish, is not available for breach of contract's express terms.

#### 9. Appeal and Error ⇨842(1)

Supreme Court reviews challenge to jury instructions for correctness, granting trial court no deference on its view of the law.

#### 10. Damages ⇨56.10

Evidence was sufficient to sustain verdict for insured under theory that he had suffered mental anguish as result of catastrophic health insurer's breach of implied covenant of good faith and fair dealing, even though it did not necessarily compel that conclusion.

#### 11. Appeal and Error ⇨1136

When civil case is submitted to jury on several alternative theories and jury does not identify which theory or theories it relied on in reaching its verdict, Supreme Court may affirm verdict if jury could have properly found for prevailing party on any one of theories presented.

#### 12. Appeal and Error ⇨1026

Under harmless error rule, Supreme Court will affirm verdict unless it concludes that likelihood of different outcome absent the error is sufficiently high as to undermine confidence in verdict.

#### 13. Appeal and Error ⇨930(1)

In reviewing jury verdict, Supreme Court views evidence in light most supportive

of verdict, and assumes that jury believed those aspects of evidence which sustain its findings and judgment.

#### 14. Appeal and Error ⇨1003(6)

Supreme Court will upset jury verdict only upon showing that evidence so clearly preponderates in favor of appellant that reasonable people would not differ on outcome of case.

#### 15. Insurance ⇨602.9

No evidence supported trial court's finding that insured's contingency fee arrangement was not foreseeable, for purposes of determining amount of attorney fees awardable to insured as consequential damages flowing from catastrophic health insurer's wrongful denial of coverage for costs of transitional treatment for brain injuries sustained in motorcycle accident.

#### 16. Insurance ⇨602.10(2)

Attorney fees may be recoverable as consequential damages flowing from insurer's breach of either express or implied terms of insurance contract, though only if they were reasonably within contemplation of, or reasonably foreseeable by, parties at time contract was made.

#### 17. Appeal and Error ⇨1003(6)

Supreme Court reverses trial court's findings of fact only if they are against clear weight of evidence, thus making them clearly erroneous.

L. Rich Humpherys, Mark L. Anderson, Stacy L. Hayden, Salt Lake City, for plaintiff.

Robert S. Campbell, Kevin Egan Anderson, Joann Shields, David W. Slagle, Salt Lake City, for defendant.

ZIMMERMAN, Chief Justice:

Glen A. Billings brought this action on behalf of his son Stanley D. Billings ("Billings") against Union Bankers Insurance Company ("Union Bankers"), alleging that Union Bankers breached both the express terms and the implied covenant of good faith and fair dealing contained in a catastrophic

healt  
tried  
the  
cont  
Billi  
awa  
of \$  
ers  
gen  
Uni  
Bill  
fee  
aw  
cul  
da

ca  
U:  
ag  
cr  
si  
tz  
sl  
b  
a  
t  
z  
c  
c  
:



health insurance contract. The case was tried to a jury, which found a breach of both the express and the implied terms of the contract and returned a \$1,800,000 verdict in Billings' favor. The district court also awarded Billings "reasonable" attorney fees of \$110,651 but refused to hold Union Bankers liable for the substantially higher contingency fee which Billings actually incurred. Union Bankers appeals the jury verdict, and Billings cross-appeals the award of attorney fees. We affirm the verdict but vacate the award of attorney fees and remand for recalculation of Billings' recoverable fees in accordance with his fee agreement.

In June of 1984, Billings entered into a catastrophic health insurance contract with Union Bankers in which Union Bankers agreed to pay certain medical expenses incurred by Billings as a result of injury or sickness. Covered expenses included hospital inpatient services, room, and board; skilled nursing facility services, room, and board; and home health care services. In addition, the policy contained a miscellaneous benefits rider in which Union Bankers agreed to pay, among other things, certain out-of-hospital medical expenses. Throughout the period of the policy, Billings paid the premiums and performed each act required to keep the policy in full force and effect.

On September 22, 1985, Billings was involved in a motorcycle accident in which he sustained serious injuries, including traumatic brain injury. He was hospitalized for several months following the accident, and pursuant to the insurance policy, Union Bankers paid Billings' hospitalization expenses.

In May of 1986, Dr. Goka, Billings' treating physician at Holy Cross Hospital, determined that Billings' recovery would be improved if he were transferred to Tangram Rehabilitation Network in San Marcos, Texas ("Tangram"). Tangram is a transitional treatment center for individuals who are medically stable but who have suffered loss of memory or basic functional skills due to traumatic brain injury. Billings was admitted to Tangram on May 9, 1986. However, Union Bankers denied coverage for Billings' treatment at Tangram, stating that the insurance policy did not cover such treatment.

Although his condition was improving, Billings discontinued his treatment at Tangram on November 25, 1986, due to a lack of funds.

Billings commenced this action on May 4, 1988, alleging that Union Bankers breached both the express coverage provision and the implied covenant of good faith and fair dealing contained in the insurance contract. Billings sought reimbursement of the expenses he incurred at Tangram and consequential damages resulting from the premature termination of treatment, which allegedly prevented Billings from ever achieving his full potential for recovery.

On April 10, 1990, Billings moved for partial summary judgment, seeking a ruling that Union Bankers had breached the express coverage provision by refusing to pay for Billings' treatment at Tangram. The trial judge denied Billings' motion "for the reason that differing interpretations of the insurance policy create genuine issues of material fact to be tried." Billings then petitioned this court for interlocutory review. We granted Billings' petition and affirmed the denial of Billings' motion because the "record before us . . . fail[ed] to adequately demonstrate the nature of the treatment received at Tangram." *Billings v. Union Bankers Ins. Co.*, 819 P.2d 803, 805 (Utah 1991) ("*Billings I*"). We remanded, and the case proceeded to trial.

Following closing arguments, Union Bankers moved for a directed verdict on Billings' claim for breach of the implied covenant of good faith and fair dealing. Union Bankers argued that it could not have breached the implied covenant as a matter of law because its liability under the insurance policy was fairly debatable. The district court denied Union Bankers' motion but instructed the jury that Union Bankers would not be liable for breaching the implied covenant if its liability under the insurance policy was "fairly debatable [and] a reasonable insurance company in similar circumstances [would have] den[ied] the claim." The district court also instructed the jury that if it found Union Bankers to have breached the express coverage provision of the insurance contract, it could award Billings the value of the insurance policy benefits to which he was entitled

and if it found Union Bankers to have breached *either* the express coverage provision *or* the implied covenant of good faith and fair dealing, it could award Billings consequential damages for emotional suffering and mental anguish, medical expenses, lost income and earning capacity, and the extent to which Billings had been limited in pursuing and enjoying the ordinary affairs of life. Although Billings also sought to recover his attorney's contingency fee as consequential damages, the parties agreed to reserve this issue until after the trial.

Following the trial, the jury returned a special verdict finding that Union Bankers had breached both the implied covenant of good faith and fair dealing and the express coverage provision of the insurance contract. It awarded Billings \$1,800,000. The district court subsequently addressed the attorney fee issue and awarded Billings what it determined to be a reasonable attorney fee of \$110,651.

[1] On appeal, Union Bankers argues that the district court erred in (i) denying Union Bankers' motion for a directed verdict on Billings' claim for breach of the implied covenant of good faith and fair dealing, and (ii) instructing the jury that it could award damages for mental anguish caused by Union Bankers' breach of the insurance contract's express coverage provision.<sup>1</sup> Billings cross-appeals the award of attorney fees. We address Union Bankers' arguments first and then consider Billings' cross-appeal.

Union Bankers first argues that the district court should have granted its motion for a directed verdict on Billings' claim for breach of the implied covenant of good faith and fair dealing. Union Bankers contends that under our decision in *Beck v. Farmers Insurance Exchange*, 701 P.2d 795 (Utah 1985), a first-party insurer may not be held

liable for breaching the implied covenant where the basis for the alleged breach is that it wrongfully denied coverage and where the insured's claim was fairly debatable. Union Bankers argues that Billings' claim was fairly debatable as a matter of law and therefore that it could not have breached the implied covenant of good faith and fair dealing. Although we agree that *Beck* established a "fairly debatable" defense to a claim for breach of the implied covenant of good faith and fair dealing, we do not think that Billings' claim was fairly debatable as a matter of law.

[2, 3] We first state the applicable standard of review. Whether *Beck* established a fairly debatable defense to a claim for breach of the implied covenant based on an insurer's wrongful denial of coverage is a question of law which we review for correctness. See *State v. Montoya*, 887 P.2d 857, 858 (Utah 1994) ("[T]he interpretation of the effect of a prior judicial decision ... constitutes a conclusion of law to which we accord no particular deference. Review is for correctness."); see also *State v. Pena*, 869 P.2d 932, 936 (Utah 1994). Whether an insured's claim is fairly debatable under a given set of facts is also a question of law. See *Pena*, 869 P.2d at 936 ("[T]he effect of a given set of facts is a question of law."). However, because of the complexity and variety of the facts upon which the fairly debatable determination depends, the legal standard under which this determination is made conveys some discretion to trial judges. See *id.* at 938-39. Therefore, although we will carefully review a trial court's conclusion that an insured's claim is or is not fairly debatable, we will grant the trial court's conclusion some deference. See *id.*

[4] Because our decision today turns heavily on our holding in *Beck*, we examine

1. Union Bankers also raises various other challenges to the jury instructions and to the special verdict form, none of which were raised below. Union Bankers' failure to object at trial precludes our consideration of these issues on appeal unless, in our discretion, we conclude that the "interests of justice" would be served by addressing the issues. Utah R.Civ.P. 51. We have held that before this exception to the waiver principle is available to a party, that party must

make a showing of "special circumstances warranting such a review." *Crookston v. Fire Ins. Exch.*, 817 P.2d 789, 799 (Utah 1991) (quoting *Hansen v. Stewart*, 761 P.2d 14, 17 (Utah 1988)). Like the appealing party in *Crookston*, Union Bankers has not begun to make this required showing. We therefore decline to consider its additional challenges to the jury instructions and special verdict form.

that case in detail here. Like the instant case, *Beck* involved an alleged breach of a first-party insurance contract, i.e., "an insurance agreement where the insurer agrees to pay claims submitted to it by the insured for losses suffered by the insured." *Beck*, 701 P.2d at 798 n. 2. In *Beck*, we held that the relationship between an insurer and its insured in the first-party context is contractual rather than fiduciary and that "as parties to a contract, the insured and the insurer have parallel obligations to perform the contract in good faith, obligations that inhere in every contractual relationship." *Id.* at 800-01. We then explained:

[T]he implied obligation of good faith performance contemplates, at the very least, that the insurer will diligently investigate the facts to enable it to determine whether a claim is valid, will fairly evaluate the claim, and will thereafter act promptly and reasonably in rejecting or settling the claim.

*Id.* at 801.

[5, 6] The first question presented is whether, under *Beck*, a first-party insurer may be held liable for breaching the implied covenant on the ground that it wrongfully denied coverage if the insured's claim, although later found to be proper, was fairly debatable at the time it was denied. The answer lies in the nature of the duties imposed by the covenant on an insurer: when confronted with a claim for benefits by a first-party insured, the insurer must "diligently investigate the facts . . . , fairly evaluate the claim, and . . . act promptly and reasonably in rejecting or settling the claim." *Id.* (emphasis added). The terms used to characterize these duties plainly indicate that the overriding requirement imposed by the implied covenant is that insurers act reasonably, as an objective matter, in dealing with

2. We emphasize that whether an insurer has acted reasonably is an objective question to be determined without considering the insurer's subjective state of mind. As we said in *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 800 (Utah 1985), the "state of mind of the insurer is irrelevant; even an inadvertent breach of the covenant of good faith implied in an insurance contract can substantially harm the insured and warrants a remedy." This statement could be read as suggesting that the covenant of good

their insureds.<sup>2</sup> It is entirely consistent with this overall approach to hold that when an insured's claim is fairly debatable, the insurer is entitled to debate it and cannot be held to have breached the implied covenant if it chooses to do so. *McLaughlin v. Alabama Farm Bureau Mut. Cas. Ins. Co.*, 437 So.2d 86, 90 (Ala.1983); cf. *Western Cas. & Sur. Co. v. Marchant*, 615 P.2d 423, 427 (Utah 1980) ("It would not comport with our ideas of either law or justice to prevent any party who entertains bona fide questions about his legal obligations from seeking adjudication thereon in the courts."). Therefore, we conclude that *Beck* established a fairly debatable defense to a claim for breach of the implied covenant of good faith and fair dealing.

[7] Having agreed with Union Bankers' construction of *Beck*, we next address its contention that the district court should have granted its motion for a directed verdict because Billings' claim was fairly debatable as a matter of law. Union Bankers argues that this court's conclusion in *Billings I* that a material issue of fact existed as to whether Union Bankers breached the express coverage provision was tantamount to a conclusion that Billings' claim for benefits was fairly debatable. We disagree.

In *Billings I*, Billings contended that the trial court erred in refusing to grant him partial summary judgment on the question of whether his treatment at Tangram was covered by the express terms of the insurance policy. We affirmed the trial court, reasoning that Billings had not adduced sufficient factual information regarding the nature of the treatment he received at Tangram to enable us to reach the legal question of whether that treatment was covered. *Billings I*, 819 P.2d at 805. In the present proceeding, Union Bankers assumes that it

faith and fair dealing imposes something akin to strict liability, i.e., if a claim is denied and a court later determines it should have been granted, the insurer is liable for breaching the implied covenant, regardless of how reasonable it was to deny coverage. On the contrary, this statement in *Beck* was intended only to disavow any implication that a "bad faith" state of mind is necessary to show a breach of the implied covenant, not to impose strict liability on insurers.



prevailed in *Billings I* because the contract provision in question was determined to be ambiguous, thus leaving the factual question of coverage for the jury to decide. However, this is a misreading of *Billings I*. We never reached the question of whether the insurance policy was sufficiently ambiguous to create a fact question. Had such a determination been made, there might well be merit to Union Bankers' assertion. However, because we made no such determination, we cannot conclude that Billings' claim was fairly debatable as a matter of law. Accordingly, we affirm the jury's finding that Union Bankers is liable for breaching the implied covenant of good faith and fair dealing.

[8,9] Union Bankers next contends that the district court erred in instructing the jury that it could award Billings the same broad types of consequential damages for breach of the insurance contract's express coverage provision as it could award under *Beck* for breach of the implied covenant. We review Union Bankers' challenge to the jury instructions for correctness, granting the trial court no deference on its view of the law. *Steffensen v. Smith's Management Corp.*, 862 P.2d 1342, 1346 (Utah 1993).

Again, because our decision on this issue revolves around our holding in *Beck*, we refer to that case in some detail. *Beck* did not deal with a breach of the underlying insurance contract's express provisions, but only with a breach of the implied covenant of good faith and fair dealing. After settling on a contract, as opposed to a tort, theory upon which to base the plaintiff's claim, we discussed the types of damages recoverable for the breach. We began with the general rule that "[d]amages 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 foreseeable by, the parties at the time the contract was made." *Beck*, 701 P.2d at 801. We recognized that in appropriate circumstances, "consequential damages for breach of contract may reach beyond the bare contract terms," *id.* at 801-02 (citing *Bevan v. J.H. Constr. Co.*, 669 P.2d 442, 444 (Utah 1983); *Pacific Coast Title Ins. Co. v. Hart-*

*ford Accident & Indem. Co.*, 7 Utah 2d 377, 325 P.2d 906, 908 (1958)), 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. *Id.* at 801. 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.

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 ignor[e] 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. *Id.* In furtherance of this purpose, we departed from the restrictive traditional 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.* at 802. Against this background, we consider Union Bankers' claim.

Union Bankers asserts that this expanded consequential damage measure should be available only for breach of the implied covenant, not, as the trial court instructed the jury, for breach of the express terms of the contract. We agree. As noted above, the implied covenant imposes a duty on first-party insurers to act in an objectively reasonable manner in handling an insured's claim. 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. Such an insurer

ought to incur no greater damage exposure than any other person breaching the express terms of a contract. Indeed, it would be unfair not to permit an insurer who has a legitimate dispute with an insured over a claim to have the dispute resolved before having to pay the claim. Exposure to the sweeping measure of damages available for breach of the implied covenant would effectively deny any careful insurer the option of declining to pay a contested claim and awaiting the outcome of the dispute. Therefore, we hold that the trial court erred in instructing the jury that it could award broad consequential damages for breach of either the implied covenant of good faith and fair dealing or the express terms of the insurance contract.

[10] We must now determine the consequences of this instructional error. Union Bankers asserts that because the jury's special verdict did not identify what portion, if any, of Billings' damages were awarded pursuant to the erroneous instruction, we must vacate the entire damage award and remand for a redetermination of Billings' recoverable damages under proper instructions. We disagree.

[11, 12] When a civil case is submitted to a jury on several alternative theories and the jury does not identify which theory or theories it relied on in reaching its verdict, we may affirm the verdict if the jury could have properly found for the prevailing party on any one of the theories presented. *See Cambelt Int'l Corp. v. Dalton*, 745 P.2d 1239, 1241-42 (Utah 1987) (citing *Barson v. E.R. Squibb & Sons, Inc.*, 682 P.2d 832, 835 (Utah 1984)).<sup>3</sup> Because the jury in the instant case was properly instructed that it could award broad consequential damages for breach of the implied covenant, we may affirm the verdict if the evidence presented at trial is sufficient to sustain the verdict under that alternative theory of recovery. We conclude that the evidence is sufficient to sustain the verdict.

3. This rule is essentially a refined version of the harmless error rule, under which we will affirm a verdict unless we conclude that "the likelihood

[13, 14] In reviewing a jury verdict, "we view the evidence in the light most supportive of the verdict, and assume that the jury believed those aspects of the evidence which sustain its findings and judgment." *E.A. Strout W. Realty Agency, Inc. v. W.C. Foy & Sons, Inc.*, 665 P.2d 1320, 1322 (Utah 1983) (citations omitted). Accordingly, we will "upset a jury verdict 'only upon a showing that the evidence so clearly preponderates in favor of the appellant that reasonable people would not differ on the outcome of the case.'" *Pratt v. Prodata, Inc.*, 885 P.2d 786, 788 (Utah 1994) (quoting *E.A. Strout*, 665 P.2d at 1322); *see also Cambelt Int'l*, 745 P.2d at 1242. Having considered the evidence in accordance with this standard, we must let the verdict stand.

At trial, the following colloquy took place between Billings' counsel and Billings' father:

Q: Have you observed Mr. Billings, Stanley Billings, in a state of depression?

A: Most definitely.

Q: And can you describe how you were able to determine the depression, or how you reached this conclusion?

A: Well, he becomes very, or has been since his return, very discouraged as to the fact that he hasn't been able to do what he possibly could have done....

....

Q: ... [D]o you have any understanding that the depressions that you have observed associated with Stan are related to the fact that he may have recovered more, or not?

A: Yes.... [H]e's constantly making the statement, quote, "Dad, I want to be a better man. I think I could have been a better man," words to that effect.

In addition, two doctors testified that Billings was capable of experiencing mental anguish and that Billings understood that his recovery from his brain injury was not as full and complete as it could have been. One of those doctors explained:

[E]very patient, including Mr. Billings, that has sustained an injury and has the

of a different outcome [absent the error] is sufficiently high as to undermine our confidence in the verdict." *Crookston*, 817 P.2d at 796.

ability to look back and see what they were like prior to the injury, and compare what they are like now, experiences distress. And when they can perceive that they have not recovered because of a lack of treatment, or inappropriate treatment, it only accentuates that distress.

Although this evidence does not necessarily compel the conclusion that Billings suffered mental anguish as a result of Union Bankers' breach of the implied covenant, it is sufficient to sustain the verdict under that theory of recovery. Accordingly, we affirm the verdict.

[15, 16] Finally, we address Billings' cross-appeal from the district court's award of attorney fees. Attorney fees may be recoverable as consequential damages flowing from an insurer's breach of either the express or the implied terms of an insurance contract. See *Canyon Country Store v. Bra-cey*, 781 P.2d 414, 420 (Utah 1989).<sup>4</sup> However, as consequential damages, attorney fees are recoverable only if they were "reasonably within the contemplation of, or reasonably foreseeable by, the parties at the time the contract was made." *Beck*, 701 P.2d at 801. In the instant case, the district court found that although it was foreseeable at the time the parties entered into the insurance contract that Billings would incur attorney fees if Union Bankers breached, the amount of fees Billings incurred under his contingency fee arrangement was not foreseeable. Accordingly, the district court awarded Billings what it determined to be a reasonable attorney fee of \$110,651 but refused to award the substantially higher contingency fee which Billings actually incurred.<sup>5</sup>

[17] Billings now argues that the district court's finding that Billings' contingency fee arrangement was not foreseeable was not supported by the evidence. We reverse a trial court's findings of fact only if they are

"against the clear weight of the evidence," thus making them 'clearly erroneous.'" *In re Estate of Bartell*, 776 P.2d 885, 886 (Utah 1989) (quoting *State v. Walker*, 743 P.2d 191, 193 (Utah 1987)). In this case, Union Bankers presented no evidence that would support the district court's finding, while Billings presented substantial evidence to the contrary. For example, Billings established by uncontradicted testimony that in actions against insurance companies to recover the benefits of an insurance policy, the usual and customary attorney fee arrangement in Utah is a contingency fee of one-third of any recovery for claims pursued through trial and a higher percentage of any recovery if the case is appealed. In addition, Billings presented testimony that "all insurance carriers would reasonably anticipate and foresee that if their insured has to hire an attorney to pursue a claim, the insured may pay at least  $\frac{1}{3}$  or more of the recovery in attorneys fees and would also have to reimburse all advanced costs and expenses." Because there was no evidence to the contrary before the district court, we conclude that Billings' contingency fee arrangement was foreseeable and therefore that the district court's finding that the fee amount under Billings' contingency fee arrangement was not foreseeable was clearly erroneous. We therefore vacate the district court's award of attorney fees and remand for recalculation of the fees in accordance with Billings' contingency fee arrangement.

In sum, we conclude that *Beck* established a fairly debatable defense to a claim for breach of the implied covenant of good faith and fair dealing, but we reject Union Bankers' argument that Billings' claim was fairly debatable as a matter of law. Therefore, we affirm the jury's finding that Union Bankers is liable for breaching the implied covenant of good faith and fair dealing. We also conclude that the district court erred in instructing the jury that it could award broad conse-

4. We express no opinion as to whether attorney fees are recoverable as consequential damages in other contexts. However, we note that our prior cases have allowed such recovery for breach of an implied-in-fact employment contract. *Heslop v. Bank of Utah*, 839 P.2d 828, 840-41 (Utah 1992), and for breach of a construction contract where the plaintiff incurred attorney fees in defending against liens which arose out of the

contractor's failure to pay its subcontractors. *Pacific Coast Title Ins. Co. v. Hartford Accident & Indem. Co.*, 325 P.2d 906, 908 (Utah 1958).

5. Billings agreed to pay his attorney one-third of any recovery for claims pursued through trial and forty percent of any recovery if the case was appealed.



quential damages for breach of the express terms of the insurance contract. We nonetheless affirm the verdict because the jury was properly instructed that it could award such damages for breach of the implied covenant and the evidence is sufficient to sustain the verdict under that alternative theory of recovery. Finally, we vacate the district court's award of attorney fees and remand for recalculation of the fees in accordance with Billings' contingency fee arrangement.

STEWART, A.C.J., and DURHAM, J., concur in ZIMMERMAN, C.J., opinion.

HOWE, Justice, concurring and dissenting:

I concur except that I would allow the recovery of attorney fees by plaintiff as consequential damages only for defendant's breach of the implied covenant of good faith and fair dealing. I would not allow fees based on any breach of the express terms of the contract.

The general rule observed in this jurisdiction is that attorney fees can be awarded to the prevailing party in litigation only where the award is predicated upon a statute or the express terms of a written instrument such as a promissory note or a contract. However, we have departed from that general rule in a few cases and upheld the recovery of fees by a successful insured in a first-party suit against his or her insurer. The fees have been awarded as an element of consequential damages for breach of the implied covenant of good faith and fair dealing inherent in every insurance policy. *Zions First Nat'l Bank v. National Am. Title Ins. Co.*, 749 P.2d 651, 657 (Utah 1988); *Beck v. Farmers Ins. Exch.*, 701 P.2d 795, 801-02 (Utah 1985); see also *Moore v. Energy Mut. Ins. Co.*, 814 P.2d 1141, 1147 (Utah Ct.App. 1991). Attorney fees were also awarded to an insured suing his insurer in *Canyon Country Store v. Bracey*, 781 P.2d 414, 420 (Utah 1989), although it is not clear whether the fees in that case were awarded for breach of the implied covenant or for breach of the express terms of the insurance contract.

The majority in the instant case recognizes:

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. Such an insurer ought to incur no greater damage exposure than any other person breaching the express terms of a contract.

Yet despite this statement, the majority sanctions the award of attorney fees as an element of consequential damages for *both* the breach of the implied covenant and the express provisions of the insurance contract. With that determination I cannot agree. It does violence to our general rule that in a breach of contract action, attorney fees cannot be awarded to the successful party unless the parties have so provided in their agreement. I would award fees only for breach of the implied covenant, consistent with the majority's holding that "the trial court erred in instructing the jury that it could award broad consequential damages for breach of either the implied covenant of good faith and fair dealing or the express terms of the insurance contract."

RUSSON, J., concurs in Justice HOWE's concurring and dissenting opinion.



Julia Lee ASKEW, Plaintiff  
and Respondent,

v.

Paul HARDMAN, Defendant  
and Petitioner.

No. 940613.

Supreme Court of Utah.

June 7, 1996.

Motor vehicle passenger who was injured as result of collision with horse brought

Tab D



Wayne BECK, Plaintiff and Appellant,

v.

FARMERS INSURANCE EXCHANGE,  
Defendant and Respondent.

No. 18926.

Supreme Court of Utah.

June 12, 1985.

Insured brought action against insurer for alleged bad-faith refusal to settle a claim for insured motorist benefits. The Third District Court, Salt Lake County, Philip P. Fishler, J., entered summary judgment for insurer, and insured appealed. The Supreme Court, Zimmerman, J., held that: (1) in a first-party relationship between an insurer and its insured, the duties and obligations of the parties are contractual rather than fiduciary in nature and, without more, a breach of those implied or express duties can give rise only to a cause of action in contract, not one in tort, and (2) question whether insurer breached its duty of good faith in rejecting insured's claim for uninsured motorist benefits without explanation and in failing to further investigate matter, such that insured was damaged when it was forced to accept settlement offered by insurer because of financial pressure caused by delay in resolving matter, was question of fact precluding summary judgment on contractual theory of failure to fulfill implied contractual duty to deal in good faith.

Reversed and remanded.

**1. Insurance ⇨602.1**

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 is a duty which upon violation may give rise to a claim for breach of contract.

**2. Insurance ⇨602.2(1)**

Refusal to bargain or settle under an insurance contract may, standing alone, be

sufficient to prove a breach under appropriate circumstances.

**3. Insurance ⇨602.1**

Practical end of providing a strong incentive for insurers to fulfill their contractual obligations to their insureds can be accomplished as well through a contract cause of action upon a failure to bargain in good faith without analytical straining necessitated by the tort approach and with far less potential for unforeseen consequences to the law of contracts.

**4. Insurance ⇨602.1**

A tort cause of action does not arise in a first-party insurance contract situation by reason of a failure to bargain in good faith because the relationship between the insurer and its insured is fundamentally different than in a third-party context.

**5. Insurance ⇨602.1**

In a first-party relationship between an insurer and its insured, the duties and obligations of the parties are contractual rather than fiduciary in nature and, without more, a breach of those implied or express duties can give rise only to a cause of action in contract, not one in tort.

**6. Insurance ⇨156(1)**

As parties to a contract, the insured and the insurer have parallel obligations to perform the contract in good faith, obligations that inhere in every contractual relationship.

**7. Insurance ⇨563**

The implied contractual obligation of good-faith performance contemplates, at the very least, that the insurer will diligently investigate these acts to enable it to determine whether a claim filed by its insured is valid, will fairly evaluate the claim, and will thereafter act promptly and reasonably in rejecting or settling the claim, and also requires the insurer to deal with laymen as laymen and not as experts in the subtleties of law and underwriting and to refrain from actions that will injure the insured's ability to obtain the benefits of the contract.

**8. Insurance ⇨602.2(1)**

Performance of the implied contractual obligation of good faith is the essence of what the insurer has bargained and paid for and, if breached, will render insurer liable for damages suffered in consequence thereof.

**9. Insurance ⇨602.10(1)**

Damages recoverable against an insurer for breach of its implied contractual obligation of good faith toward insured include both general damages, those flowing naturally from breach, and consequential damages, those reasonably within contemplation of, or reasonably foreseeable by, parties at time contract was made.

**10. Insurance ⇨602.10(1)**

In an action against an insurer for breach of a duty to bargain in good faith, given that insured frequently faces catastrophic consequences if funds are not available within a reasonable period of time to cover an insured loss, damages for a loss well in excess of policy limits, such as for a home or a business, may be foreseeable and provable.

**11. Damages ⇨56.10**

In unusual cases concerned with an insurer's breach of a duty to bargain in good faith, damages for mental anguish to insured might be provable, but foreseeability of any such damages will always hinge upon nature and language of contract and reasonable expectations of parties.

**12. Judgment ⇨181(23)**

Question whether insurer breached its duty of good faith in rejecting insured's claim for uninsured motorist benefits without explanation and in failing to further investigate matter, such that insured was damaged when it was forced to accept settlement offered by insurer because of financial pressure caused by delay in resolving matter, was question of fact precluding summary judgment on contractual theory of failure to fulfill implied contractual duty to deal in good faith.

Robert J. Debry, Salt Lake City, for plaintiff and appellant.

Don J. Hanson, Salt Lake City, for defendant and respondent.

**ZIMMERMAN, Justice:**

Plaintiff Wayne Beck appeals from a summary judgment dismissing his claim against Farmers Insurance Exchange, his automobile insurance carrier, alleging that Farmers had refused in bad faith to settle a claim for uninsured motorist benefits. We hold that on the record before us, Beck stated a claim for relief and a summary judgment was inappropriate. We reverse and remand for further proceedings consistent with this opinion.

Beck injured his knee in a hit-and-run accident on January 16, 1982, when his car was struck by a car owned by Ann Kirkland. Ms. Kirkland asserted that her car had been stolen and denied any knowledge of or responsibility for the accident. Beck filed a claim with Kirkland's insurer, but liability was denied on April 20, 1982.

At the time of the accident, Beck carried automobile insurance with Farmers. Under that policy, Beck was provided with both no-fault and uninsured motorist insurance benefits. On February 23, 1982, while his claim against Kirkland was pending, Beck filed a claim with Farmers for no-fault benefits. Sometime prior to May 26, 1982, Farmers paid Beck \$5,000 for medical expenses (the no-fault policy limit) and \$1,299.43 for lost wages.

On June 23, 1982, Beck's counsel filed a claim with Farmers for uninsured motorist benefits, demanding the policy limit, \$20,000, for general damages suffered as a result of the accident. His counsel alleges that the brochure documenting Beck's damages, submitted to Farmers with the June 23rd settlement offer, established that his claim was worth substantially more than \$20,000. Farmers' adjuster rejected the settlement offer without explanation on July 1, 1982.

Beck filed this lawsuit one month later, on August 2, 1982, alleging three causes of

action: first, that by refusing to pay his uninsured motorist claim, Farmers had breached its contract of insurance with him; second, that by acting in bad faith in refusing to investigate the claim, bargain with Beck, or settle the claim, Farmers had breached an implied covenant of good faith and fair dealing; and third, that Farmers had acted oppressively and maliciously toward Beck with the intention of, or in reckless disregard of the likelihood of, causing emotional distress. Under the first claim, Beck sought damages for breach of contract in the amount of the policy limits; under the second, he asked for compensatory damages in excess of the policy limits for additional injuries, including mental anguish; and under the third, he sought punitive damages of \$500,000.

Sometime in August of 1982, Beck's counsel contacted Farmers' counsel and offered to settle the whole matter for \$20,000. This offer was rejected. Farmers filed an answer on September 1, 1982, and at the same time, moved to strike the prayer for punitive damages on the ground that they were unavailable for a breach of contract. Farmers' motion was granted. On September 29th, the trial court bifurcated the case and agreed to try the claim for failure to pay uninsured motorist benefits independent of Beck's claim alleging breach of an implied covenant of good faith and fair dealing.

Immediately after the trial judge bifurcated the case, Beck's counsel expressly revoked the previously rejected offer to settle the whole matter for \$20,000. Instead, Beck offered to settle only the failure to pay the uninsured motorist benefits claim for \$20,000, reserving the implied covenant or "bad faith" claim for separate resolution.

On October 20, 1982, Farmers apparently counteroffered. Negotiations proceeded, and sometime in late November, the parties agreed to settle the uninsured motorist claim for \$15,000. On December 6, 1982, the parties stipulated to dismissal of that claim and specifically reserved the bad faith claim for later disposition.

In mid-December, Farmers moved to dismiss the reserved bad faith claim on two theories. First, Farmers asserted that under *Lyon v. Hartford Accident and Indemnity Co.*, 25 Utah 2d 311, 480 P.2d 739 (1971), it "had no duty to bargain with or settle plaintiff's uninsured motorist claim and, therefore, [could not] be held liable" for breach of contract or bad faith. Second, Farmers argued that even if it had some duty to bargain or to settle the claim, the facts set forth in the pleadings on file did not establish that it had breached the duty. No memoranda or factual affidavits supported this motion.

Farmers' motion was opposed by affidavits of Beck, his counsel, and a former insurance adjuster who worked for Beck's counsel as a paralegal. In his affidavit, Beck's counsel recited the dates and terms of the various settlement offers and the fact that they had been rejected without counteroffer. Beck's affidavit stated that he had accepted the \$15,000 offer only because of financial pressures caused by the substantial expenses he had incurred in the ten months since the accident. The paralegal's affidavit stated that he had been an insurance adjuster for 19 years and that he had reviewed the settlement documentation submitted to Farmers in June when the claim was first filed. He expressed the opinion that a reasonable and prudent insurance company would have valued the claim at between \$30,000 and \$40,000 and attempted to settle the matter within weeks after the initial offer. The paralegal charged that the "only reason for such a substantial delay in settling this claim would be to put Mr. Beck in a situation of financial need and stress so that he would accept the first settlement offer," a tactic he characterized as acting in bad faith. Farmers filed no rebuttal affidavits, and the trial court granted Farmers' motion without specifying the basis for its holding.

Beck asks this Court to overrule *Lyon* and permit an insured to sue for an insurer's bad faith refusal to bargain or settle. He points out that many states now allow a tort action for breach of an insurer's duty



to deal fairly and in good faith with its insured. Assuming that we abandon *Lyon*, Beck argues that the affidavits submitted in opposition to Farmers' motion for summary judgment were sufficient to create a genuine issue of material fact as to whether Farmers breached an implied covenant of good faith and fair dealing.

Farmers does not now contend, as it did below, that it had no duty to bargain or settle. Instead, it argues that under *Lyon*, an insurer cannot be held liable for bad faith simply because it refused to bargain or to settle a claim; rather, it argues, to sustain such a claim a plaintiff must produce evidence of bad faith wholly apart from the "mere failure" to bargain or settle.

Our ruling in *Lyon* left an insured without any effective remedy against an insurer that refuses to bargain or settle in good faith with the insured. An insured who has suffered a loss and is pressed financially is at a marked disadvantage when bargaining with an insurer over payment for 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. See *Lawton v. Great Southwest Fire Insurance Co.*, 118 N.H. 607, 392 A.2d 576, 579 (1978); Harvey & Wiseman, *First Party Bad Faith: Common Law Remedies and a Proposed Legislative Solution*, 72 Ky.L.J. 141, 146, 167-69 (1983-84) (hereinafter cited as "First Party Bad Faith"); Note, *The Availability of Excess Damages for Wrongful Refusal to Honor First Party*

*Insurance Claims—An Emerging Trend*, 45 Fordham L.Rev. 164, 164-67 (Oct. 1976) (hereinafter cited as "Availability of Excess Damages").

[1, 2] In light of these considerations, we now conclude that an insured should be provided with a remedy. However, we do not agree with plaintiff that a tort action is appropriate. Instead, we hold 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.<sup>1</sup> In addition, we do not adopt the limitation suggested by Farmers, but hold that the refusal to bargain or settle, standing alone, may, under appropriate circumstances, be sufficient to prove a breach.

We recognize that a majority of states permit an insured to institute a tort action against an insurer who fails to bargain in good faith in a "first-party" situation,<sup>2</sup> adopting the approach first announced by the California Supreme Court in *Gruenberg v. Aetna Insurance Co.*, 9 Cal.3d 566, 510 P.2d 1032, 108 Cal.Rptr. 480 (1973). See, e.g., *Bibeault v. Hanover Insurance Co.*, R.I., 417 A.2d 313 (1980); *Craft v. Economy Fire & Casualty Co.*, 572 F.2d 565 (7th Cir.1978) (applying Indiana law); *MFA Mutual Insurance Co. v. Flint*, Tenn., 574 S.W.2d 718 (1978). Apparently, these courts have taken this step as a matter of policy in order to provide what they perceive to be an adequate remedy for an insured wronged by an insurer's recalcitrance. These courts have reasoned that under contract law principles, an insurer who improperly refuses to settle a first-party claim may be liable only for damages measured by the maximum dollar amount

to pay claims submitted to it by the insured for losses suffered by the insured. The present case involves such a first-party situation. In contrast, a "third-party" situation is one where the insurer contracts to defend the insured against claims made by third parties against the insured and to pay any resulting liability, up to the specified dollar limit.

1. The Court in *Lyon* considered only the question of whether a claim of bad faith gave rise to a tort cause of action; however, to the extent that *Lyon* is philosophically inconsistent with our recognition today of a cause of action in contract, it is overruled.
2. We use the term "first-party" to refer to an insurance agreement where the insurer agrees

of the insurance provided by the policy, and such a damage measure provides little or no incentive to an insurer to promptly and faithfully fulfill its contractual obligations. Accordingly, these courts have adopted a tort approach in order to allow an insured to recover extensive consequential and punitive damages, which they consider to be unavailable in an action based solely on a breach of contract. See *Availability of Excess Damages*, *supra*, at 168-77; *First Party Bad Faith*, *supra*, at 158.

[3] We conclude that the tort approach adopted by these courts is without a sound theoretical foundation and has the potential for distorting well-established principles of contract law. Moreover, the practical end of providing a strong incentive for insurers to fulfill their contractual obligations can be accomplished as well through a contract cause of action, without the analytical straining necessitated by the tort approach and with far less potential for unforeseen consequences to the law of contracts.

The analytical weaknesses of the tort approach are easily seen. In *Gruenberg*, the California court held that an insurer has a duty to deal in good faith with its insured and that an insured can bring an action in tort, rather than contract, for breach of that duty because the duty is imposed by law and, being nonconsensual, does not arise out of the contract. Glossing over any distinctions between first- and third-party situations, the court concluded that the duty imposed upon the insurer when bargaining with its insured in a first-party situation is merely another aspect of the fiduciary duty owed in the third-party context. *Gruenberg v. Aetna Insurance Co.*, 9 Cal.3d at 573-74, 510 P.2d at 1037, 108 Cal.Rptr. at 485.

Although this Court, in *Ammerman v. Farmer's Insurance Exchange*, 19 Utah 2d 261, 430 P.2d 576 (1967), recognized a tort cause of action for breach of an insurer's obligation to bargain in a third-party context, we cannot agree with the *Gruenberg* court that the considerations which compel the recognition of a tort cause of action in a third-party context are present in the

first-party situation. In *Ammerman*, we stated that because a third-party insurance contract obligates the insurer to defend the insured, the insurer incurs a fiduciary duty to its insured to protect the insured's interests as zealously as it would its own; consequently, a tort cause of action is recognized to remedy a violation of that duty. 19 Utah 2d at 265-66, 430 P.2d at 578-79.

[4] However, in *Lyon v. Hartford Accident and Indemnity Co.*, we held that a tort cause of action did not arise in a first-party insurance contract situation because the relationship between the insurer and its insured is fundamentally different than in a third-party context:

In the [third-party] situation, the insurer must act in good faith and be as zealous in protecting the interests of the insured as it would be in regard to its own. In the [first-party] situation, the insured and the insurer are, in effect and practically speaking, adversaries.

25 Utah 2d at 319, 480 P.2d at 745 (citations omitted). See also *Lawton v. Great Southwest Fire Insurance Co.*, 392 A.2d at 580-81.

This distinction is of no small consequence. In a third-party situation, the insurer controls the disposition of claims against its insured, who relinquishes any right to negotiate on his own behalf. *Craft v. Economy Fire & Casualty Co.*, 572 F.2d at 569. An insurer's failure to act in good faith exposes its insured to a judgment and personal liability in excess of the policy limits. *Santilli v. State Farm Life Insurance Co.*, 278 Or. 53, 61-62, 562 P.2d 965, 969 (1977). In essence, the contract itself creates a fiduciary relationship because of the trust and reliance placed in the insurer by its insured. Cf. *Hal Taylor Associates v. UnionAmerica, Inc.*, Utah, 657 P.2d 743, 748-49 (1982). The insured is wholly dependent upon the insurer to see that, in dealing with claims by third parties, the insured's best interests are protected. In addition, when dealing with third parties, the insurer acts as an agent for the insured with respect to the disputed claim. Wholly apart from the contractual

obligations undertaken by the parties, the law imposes upon all agents a fiduciary obligation to their principals with respect to matters falling within the scope of their agency. *Id.* at 748; *see generally* 3 Am. Jur.2d Agency § 199 (1962).

In the first-party situation, on the other hand, the reasons for finding a fiduciary relationship and imposing a corresponding duty are absent. No relationship of trust and reliance is created by the contract; it simply obligates the insurer to pay claims submitted by the insured in accordance with the contract. *Santilli v. State Farm Life Insurance Co.*, 278 Or. at 61-62, 562 P.2d at 969. Furthermore, none of the indicia of agency are present. *See generally Duncan v. Andrew County Mutual Insurance Co.*, Mo.App., 665 S.W.2d 13, 18-20 (1984).

Clearly, then, it is difficult to find a theoretically sound basis for analogizing the duty owed in a third-party context to that owed in a first-party context. And wholly apart from any theoretical problems, tailoring the tort analysis to first-party insurance contract cases has proven difficult. The pragmatic reason for adopting the tort approach is that it exposes insurers to consequential and punitive damages awards in excess of the policy limits. However, the courts appear to have had difficulty in developing a sound rationale for limiting the tort approach to insurance contract cases. This may be because there is no sound theoretical difference between a first-party insurance contract and any other contract, at least no difference that justifies permitting punitive damages for the breach of one and not the other. In any event, the tort approach and the accompa-

nying punitive damages have moved rather quickly into areas far afield from insurance. *See, e.g., Seaman's Direct Buying Service, Inc. v. Standard Oil Co.*, 36 Cal.3d 752, 686 P.2d 1158, 1166-67, 206 Cal.Rptr. 354, 362-63 (1984); *Wallis v. Superior Court*, 160 Cal.App.3d 1109, 207 Cal.Rptr. 123, 127-29 (1984); *Gates v. Life of Montana Insurance Co.*, Mont., 668 P.2d 213, 214-16 (1983).

Furthermore, the courts adopting the tort approach have had some difficulty in determining what degree of bad faith is necessary to sustain a claim. *E.g., Anderson v. Continental Insurance Co.*, 85 Wis.2d 675, 692-94, 271 N.W.2d 368, 376-77 (1978). From a practical standpoint, the state of mind of the insurer is irrelevant; even an inadvertent breach of the covenant of good faith implied in an insurance contract can substantially harm the insured and warrants a remedy.

[5, 6] We therefore hold that in a first-party relationship between an insurer and its insured, the duties and obligations of the parties are contractual rather than fiduciary. Without more, a breach of those implied or express duties can give rise only to a cause of action in contract, not one in tort.<sup>3</sup> This position has not been widely adopted by other courts, although a "respectable body of authority" is developing. *See Duncan v. Andrew County Mutual Insurance Co.*, 665 S.W.2d at 18-19, and cases cited therein; *Lawton v. Great Southwest Fire Insurance Co.*, 118 N.H. 607, 392 A.2d 576 (1978); *Kewin v. Massachusetts Mutual Life Insurance Co.*, 409 Mich. 401, 295 N.W.2d 50 (1980); *Avail-*

3. We recognize that in some cases the acts constituting a breach of contract may also result in breaches of duty that are independent of the contract and may give rise to causes of action in tort. *Hal Taylor Assoc. v. UnionAmerica*, 657 P.2d at 750; *Lawton v. Great Southwest Fire Ins. Co.*, 392 A.2d at 580. For example, the law of this state recognizes a duty to refrain from intentionally causing severe emotional distress to others. *Samms v. Eccles*, 11 Utah 2d 289, 358 P.2d 344 (1961). Thus, intentional and outrageous conduct by an insurer against an insured, coupled with a failure to bargain, could

conceivably result in tort liability independent of (and concurrent with) liability for breach of contract. Additionally, the facts that give rise to a breach of the duty to bargain in good faith could also amount to fraudulent activity, rendering an insurer independently liable for damages flowing from the fraud. *See Wetherbee v. United Ins. Co.*, 265 Cal.App.2d 921, 71 Cal.Rptr. 764 (1968). Also, under various unfair practices acts, there may be statutory requirements that give rise to independent causes of action. *E.g., U.C.A.*, 1953, §§ 31-27-1 to -24.



ability of *Excess Damages*, *supra* p. 4, at 168-71. We further hold that as parties to a contract, the insured and the insurer have parallel obligations to perform the contract in good faith, obligations that inhere in every contractual relationship. *State Automobile & Casualty Underwriters v. Salisbury*, 27 Utah 2d 229, 232, 494 P.2d 529, 531 (1972); *Leigh Furniture & Carpet Co. v. Isom*, Utah, 657 P.2d 293, 306 (1982).<sup>4</sup>

[7, 8] Few cases define the implied contractual obligation to perform a first-party insurance contract in good faith. However, because the considerations are similar, we freely look to the tort cases that have described the incidents of the duty of good faith in the context of first-party insurance contracts. From those cases and from our own analysis of the obligations undertaken by the parties, we conclude that the implied obligation of good faith performance contemplates, at the very least, that the insurer will diligently investigate the facts to enable it to determine whether a claim is valid, will fairly evaluate the claim, and will thereafter act promptly and reasonably in rejecting or settling the claim. See *Anderson v. Continental Insurance Co.*, 85 Wis.2d at 692-93, 271 N.W.2d at 377; *Egan v. Mutual of Omaha Insurance Co.*, 24 Cal.3d 809, 818-19, 620 P.2d 141, 145-46, 169 Cal.Rptr. 691, 695-96 (1979). The duty of good faith also requires the insurer to "deal with laymen as laymen and not as experts in the subtleties of law and underwriting" and to refrain from actions that will injure the insured's ability to obtain the benefits of the contract. *MFA Mutual Insurance Co. v. Flint*, 574 S.W.2d at 720, quoting *Merchants Indemnity Corp. v. Eggleston*, 37 N.J. 114, 122, 179 A.2d 505, 509 (1962); accord *Bowler v. Fidelity & Casualty Co.*, 53 N.J. 313, 327, 250 A.2d 580, 587 (1969). These performances are the essence of what the insured has bargained and paid

for, and the insurer has the obligation to perform them. When an insurer has breached this duty, it is liable for damages suffered in consequence of that breach.

In adopting the contract approach, we are not ignoring the principal reason for the adoption of the tort approach—to provide damage exposure in excess of the policy limits and thus remove any incentive for breaching the duty of good faith. Despite what some courts have suggested, *e.g.*, *Santilli v. State Farm Insurance Co.*, 562 P.2d at 969, and what some commentators have asserted, *e.g.*, J. Appleman, *Insurance Law & Practice* § 8878.15 at 424-26 (1981), there is no reason to limit damages recoverable for breach of a duty to investigate, bargain, and settle claims in good faith to the amount specified in the insurance policy.<sup>5</sup> Nothing inherent in the contract law approach mandates this narrow definition of recoverable damages. 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. *Lawton v. Great Southwest Fire Insurance Co.*, 392 A.2d at 579.

[9] 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 foreseeable by, the parties at the time the contract was made. *Pacific Coast Title Insurance Co. v. Hartford Accident & Indemnity Co.*, 7 Utah 2d 377, 379, 325 P.2d 906, 907 (1958), citing *Hadley v. Barendale*, 9 Exch. 341, 156 Eng.Rep. 145 (1854). We have repeatedly recognized that consequential damages for breach of contract may reach beyond the bare contract terms. See, *e.g.*, *Pacific Coast Title Insurance Co. v. Hartford Accident & Indemnity*, 7 Utah 2d at 379, 325 P.2d at 908

4. The duty to perform the contract in good faith cannot, by definition, be waived by either party to the agreement.

5. In *Ammerman*, we suggested in dicta that in an action for breach of an insurance policy, the damages could not exceed the policy limits. 19 Utah 2d at 264, 430 P.2d at 578. We expressly disavow this dicta.

(attorney fees incurred for settling and defending claims were foreseeable result of contractor's default); *Bevan v. J.H. Construction Co.*, Utah, 669 P.2d 442, 444 (1983) (home purchasers entitled to damages for loss of favorable mortgage interest rate resulting from builder's breach of contract).

[10,11] In an action for breach of a duty to bargain in good faith, a broad range of recoverable damages is conceivable, particularly given the unique nature and purpose of an insurance contract. An insured frequently faces catastrophic consequences if funds are not available within a reasonable period of time to cover an insured loss; damages for losses well in excess of the policy limits, such as for a home or a business, may therefore be foreseeable and provable. See, e.g., *Reichert v. General Insurance Co.*, 59 Cal.Rptr. 724, 728, 428 P.2d 860, 864 (1967), *vacated on other grounds*, 68 Cal.2d 822, 442 P.2d 377, 69 Cal.Rptr. 321 (1968) (because bankruptcy was a foreseeable consequence of fire insurer's failure to pay, insurer was liable for consequential damages flowing from bankruptcy). Furthermore, it is axiomatic that insurance frequently is purchased not only to provide funds in case of loss, but to provide peace of mind for the insured or his beneficiaries. Therefore, although other courts adopting the contract approach have been reluctant to allow such an award, *Lawton v. Great Southwest Fire Insurance Co.*, 392 A.2d at 581-82, we find no difficulty with the proposition that, in unusual cases, damages for mental anguish might be provable.<sup>6</sup> See *Kewin v. Massachusetts Mutual Life Insurance Co.*, 409 Mich. at 440-55, 295 N.W.2d at 64-72 (Williams, J., dissenting); cf. *Lambert v. Sine*, 123 Utah 145, 150, 256 P.2d 241, 244 (1953). The foreseeability of any such damages will always hinge upon the nature and language of the contract and the reasonable expectations of the parties. J. Calamari &

6. Clearly, damages will not be available for the mere disappointment, frustration, or anxiety normally experienced in the process of filing an

J. Perillo, *Contracts* § 14-5 at 523-25 (2d ed. 1977).

With the foregoing principles in mind, we return to a consideration of the present case. The trial court granted summary judgment for the insurer in the face of affidavits of the insured, his counsel, and a paralegal who had been an adjuster for many years. In the absence of any responsive affidavits, we take the assertions of the affidavits as true and view all unexplained facts in a light most favorable to Beck. It appears that the insurer was served with Beck's claim on June 23, 1982. On July 1st, the claim was rejected without explanation and without any request for additional facts. The insured heard nothing more from the insurer until after August 2d, when this suit was filed. The affidavits state that the insured accepted the settlement offered by the insurer in late October because of the financial pressure caused by the delay in resolving the matter. The affidavits also offer the opinion of the expert adjuster turned paralegal that the delay was in bad faith.

From January until late June, Beck was apparently negotiating with the car owner's carrier and not with Farmers, for no claim was filed with Farmers until June 23rd. Therefore, none of the delay between January and June 23rd can be attributed to Farmers. The unexplained delay thereafter, however, together with a flat rejection of plaintiff's offer, provides a factual basis for this cause of action sufficient to withstand summary judgment. Farmers had an obligation to diligently investigate and evaluate Beck's claim. It rejected the claim in one week, and we must infer that the insurer did nothing to investigate or evaluate the claim during the following month.

[12] Under these circumstances and resolving all doubts in Beck's favor, we cannot say that a jury could not find that Farmers breached its duty of good faith in rejecting Beck's claim without explanation

insurance claim and negotiating a settlement with an insurer.



and in failing to further investigate the matter. Therefore, we remand the matter to the trial court for further proceedings.

Affirmed.

Stewart, J., concurred in result.

HALL, C.J., and STEWART, HOWE and DURHAM, JJ., concur.



Claron D. BAILEY, Plaintiff  
and Respondent,

v.

DESERET FEDERAL SAVINGS AND  
LOAN ASSOCIATION, Defendant  
and Appellant.

No. 18961.

Supreme Court of Utah.

June 19, 1985.

Assignee of second deed of trust filed action requesting that he be awarded excess sale proceeds over amount due holder of first deed of trust. The Third District Court, Salt Lake County, Homer F. Wilkinson, J., found for assignee, and holder of first deed of trust appealed. The Supreme Court, Durham, J., held that affidavit of attorney representing assignee of second deed of trust establishing that bankruptcy judge dismissed assignee's complaint seeking to stay trustee's sale because of secured claims on debtor's property and because bankruptcy court had no interest in funds, and that bankruptcy judge had earlier favorably responded to statement that assignee would prefer to go to state court, demonstrated that bankruptcy court did not make adjudication on merits, and thus, bankruptcy court's dismissal was not res judicata so as to bar state court action by assignee seeking to recover excess sale proceeds over amount due holder of first deed of trust.

**1. Appeal and Error**  $\S$ 204(4)

In action brought by assignee of second deed of trust seeking to be awarded excess sale proceeds over amount due holder of first deed of trust, holder of first deed of trust, by failing to interpose any objection at trial to use of affidavit of plaintiff's attorney, waived objection on basis of allegation that such affidavit was hearsay, and could not raise such issue for first time on appeal.

**2. Judgment**  $\S$ 654

Finding that court does not have jurisdiction is not the sort of adjudication that can serve as basis for res judicata on merits.

**3. Judgment**  $\S$ 829(3)

Affidavit of attorney representing assignee of second deed of trust establishing that bankruptcy judge dismissed assignee's complaint seeking to stay trustee's sale because of secured claims on debtor's property and because bankruptcy court had no interest in funds, and that bankruptcy judge had earlier favorably responded to statement that assignee would prefer to go to state court, demonstrated that bankruptcy court did not make adjudication on merits, and thus, bankruptcy court's dismissal was not res judicata so as to bar state court action by assignee seeking to recover excess sale proceeds over amount due holder of first deed of trust.

Edward M. Garrett, Joseph E. Hatch, Salt Lake City, for defendant and appellant.

J. Steven Newton, Salt Lake City, for plaintiff and respondent.

DURHAM, Justice:

The plaintiff, a mechanic's lien holder and assignee of a second position trust deed, filed a complaint with the federal bankruptcy court asking the court to stay a