

No. G053914

**IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA  
FOURTH APPELLATE DISTRICT  
DIVISION 3**

---

PACIFICARE LIFE AND HEALTH INSURANCE COMPANY,  
*Plaintiff and Respondent*

v.

DAVE JONES, IN HIS CAPACITY AS INSURANCE  
COMMISSIONER OF THE STATE OF CALIFORNIA,  
*Defendant and Appellant.*

---

On appeal from the Superior Court for the County of Orange  
Hon. Kim G. Dunning, Judge Presiding  
Superior Court Case No. 30-2014-00733375-CU-WM-CXC

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**RESPONDENT'S BRIEF**

---

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<b>CERTIFICATE OF INTERESTED ENTITIES OR PERSONS</b>	
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1. This form is being submitted on behalf of the following party (name): PacifiCare Life and Health Insurance Co.
2. a.  There are no interested entities or persons that must be listed in this certificate under rule 8.208.
- b.  Interested entities or persons required to be listed under rule 8.208 are as follows:

**Full name of interested entity or person**

**Nature of interest (Explain):**

- (1) UnitedHealth Group Incorporated
- (2) United HealthCare Services, Inc.
- (3)
- (4)
- (5)

- 100% owner of United HealthCare Services, Inc.
- 100% owner of PacifiCare Life and Health Ins. Co.

Continued on attachment 2.

The undersigned certifies that the above-listed persons or entities (corporations, partnerships, firms, or any other association, but not including government entities or their agencies) have either (1) an ownership interest of 10 percent or more in the party if it is an entity; or (2) a financial or other interest in the outcome of the proceeding that the justices should consider in determining whether to disqualify themselves, as defined in rule 8.208(e)(2).

Date: August 1, 2017

Daniel M. Kolkey  
(TYPE OR PRINT NAME)

  
(SIGNATURE OF APPELLANT OR ATTORNEY)

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## I. INTRODUCTION

The Insurance Commissioner's defense of the three invalidated regulations construing the Unfair Insurance Practices Act ("UIPA") (Ins. Code, § 790 et seq.) boils down to his contention that they "embody the Commissioner's considered policy choices" in pursuit of "consumer protection" and must be upheld in deference to his "technical knowledge and expertise." (AOB 27.)

But his regulatory interpretations of Insurance Code section 790.03(h)<sup>1</sup> conflict with, and were promulgated in defiance of, the California Supreme Court's interpretation of section 790.03(h); they conflict with the Department of Insurance's ("Department's") original interpretation of the statute; they were not made contemporaneously with the statute's enactment but 20 years later; and they do not draw on the Commissioner's "technical knowledge and expertise," but interpret commonly used statutory terms, like "general business practice" and "knowingly."

Accordingly, no deference is due to an interpretation that departs from the promulgating agency's original interpretation and our high court's construction. And the Commissioner's pursuit of "consumer protection" cannot absolve his departure from the statute's plain language because "[n]o text pursues its purpose at all costs." (Scalia and Garner, *Reading Law: The Interpretation of Legal Texts* (2012), p. 57.)

Significantly, by diluting the text of the relevant statutes, the Commissioner's regulations enabled him to impose an unprecedented \$173.6 million penalty against PacifiCare Life and Health Insurance Company ("PacifiCare"), when 98% of the alleged violations encompassed (1) two forms

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<sup>1</sup> Except where designated otherwise, all subsequent statutory references are to the Insurance Code. For convenience, section 790.03, subdivision (h) will be referred to as "section 790.03(h)."

that omitted a statutory notice while PacifiCare was awaiting the Department’s approval of the notices’ text, (2) the inadvertent failure to issue letters acknowledging receipt of insurance claims (which caused no harm), and (3) the failure to process less than 5% of claims within 30 working days of receipt – a failure rate that was within the standard that his predecessor established for PacifiCare. (1AA18(¶5), 1AA20(¶14), 1AA46, 1AA383.)

*No court has ever endorsed these regulations.* And the trial court correctly invalidated them for at least the following reasons:

**Regulation 2695.1(a)**<sup>2</sup>. Section 790.03(h) prohibits “[k]nowingly committing or performing with such frequency as to indicate a *general business practice* any of the following [16] unfair claims settlement *practices* ...” (Italics added.) But regulation 2695.1(a) interprets section 790.03(h) to mean that “an insurer violates Insurance Code section 790.03(h) by a *single act* knowingly committed” *or* by a general business practice. (1AA97, italics added.) This interpretation conflicts with leading California Supreme Court decisions, the most recent of which stated that section 790.03(h) “contemplates only administrative sanctions for practices amounting to a *pattern of misconduct*.” (*Zhang v. Superior Court* (2013) 57 Cal.4th 364, 379, fn. 8 (*Zhang*); italics added.) It also conflicts with his Department’s original interpretation of section 790.03(h), which advised the California Supreme Court in 1978 that “[s]ince its enactment, the Department has consistently construed this section to *require a general business practice* in order to establish a violation.” (PacifiCare’s Motion for Judicial Notice (“MJN”), exh. A, p. 30<sup>3</sup> [Amicus Curiae Brief of the Department and the Insurance

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<sup>2</sup> All regulatory references are to title 10 of the California Code of Regulations and shall be designated as “regulation” followed by the section number.

<sup>3</sup> All page references to PacifiCare’s MJN are to the exhibits attached to the motion itself. A separately paginated courtesy copy has also been provided.

Commissioner, p. 8]; italics added.) Nonetheless, 20 years after section 790.03(h) was enacted, and in defiance of contrary California Supreme Court authority, the Insurance Commissioner issued regulation 2695.1(a) interpreting section 790.03(h) to prohibit “a single act knowingly committed.” (1AA97; AOB 28.) This regulatory interpretation enabled the Commissioner to argue, for instance, that *each* untimely *payment* by PacifiCare was an unfair insurance *practice*. (1AA158.)

**Regulation 2695.2(l).** The Commissioner also diluted the definition of “knowingly” under section 790.03(h) to include “implied or constructive knowledge.” (Reg. 2695.2(l).) This interpretation *departs* from the common definition of “[k]nowingly”; *ignores* California Supreme Court precedent, which construed “knowingly” under section 790.03(h) to mean “deliberately”; fails to recognize that the Legislature has specified constructive knowledge in the same statute when it so intends; and is inconsistent with his predecessor Insurance Commissioner’s acknowledgment that “knowingly” was added to section 790.03(h) to avoid penalties for “innocent” violations. (PacifiCare’s MJN, pp. 27-28 [exh. A: Department’s Amicus Curiae Brief, pp. 5-6].) Under the Commissioner’s regulations, an *inadvertently* committed *single act* can become a *knowingly* committed unfair claims settlement *practice*.

**Regulation 2695.2(y).** Under section 790.035, the maximum penalty for each act comprising a violation of any of the subdivisions of section 790.03 – including section 790.03(h) – is increased from \$5,000 to \$10,000 if the act is “[w]illful.” But the Commissioner’s regulation defines “[w]illful” as merely the “willingness to commit the act,” without “any intent to violate law, or to injure another.” (Reg. 2695.2(y).) This diluted definition is inconsistent with section 790.035’s two-tiered penalty structure because it makes meaningless the distinction between “willful” and “non-willful” acts; gives “willful” a different

meaning under section 790.035 than that in its mirror-image, companion statute (§1858.07); and conflicts with the long-standing statutory definition of “willful” under the Insurance Code. Under this regulation, the Commissioner found that PacifiCare’s failure to insert a required statutory notice into an Explanation of Benefits form, *while “await[ing] ][the Department’s] staff ‘approval’”* (1AA152), was “willful.” (1AA149.)

This Court should affirm the superior court’s ruling.

## **II. FACTUAL AND PROCEDURAL BACKGROUND**

Although the validity of the three challenged regulations must be adjudicated as a matter of law, the Commissioner’s brief seeks to cast PacifiCare in a negative light, presumably to justify his interpretation of section 790.03(h).

Accordingly, PacifiCare responds briefly to the Commissioner’s “statement of the case” and procedural history. (AOB 19-23.) In that connection, PacifiCare notes that the Commissioner’s factual characterizations of PacifiCare’s conduct in his Decision (1AA83-303) frequently mischaracterize the evidence, lack substantial evidence, or omit key facts. PacifiCare is vigorously litigating the validity of these factual characterizations in the ongoing administrative mandamus action from which this appeal arises; thus, the Commissioner’s factual characterizations are as unreliable as they are irrelevant to the issues of statutory interpretation in this appeal.

### **A. The Market Conduct Examination.**

The Commissioner’s brief argues that a “large volume of complaints triggered an investigation” and “prompted the Department to undertake a targeted market conduct examination [‘MCE’]” of PacifiCare for the period between June 23, 2006, and May 31, 2007, pursuant to Insurance Code section 730. (AOB 20; 2AA892-895.)

But an email was uncovered from the lead staff attorney responsible for the underlying enforcement action against PacifiCare, which expressly *urged* the California Medical Association to bring more complaints during the examination in order to build a case against PacifiCare, because “the more [complaints] racked up, the better.” (AA21 (¶16).) *After* the litigation was commenced, the Department admittedly destroyed the documents on that attorney’s desktop computer, which violated the Department’s document retention obligations, depriving PacifiCare of uncovering the full extent of the Department’s efforts to solicit complaints. (§ 12921.1, subd. (a)(4); 1AA21(¶16), 1AA78(¶119).)

Significantly, the public MCE report, which resulted from the examination, cited PacifiCare for only 90 specific instances (later amended to 92) in which PacifiCare purportedly engaged in an unfair insurance act or practice in violation of the UIPA. (1AA24; 2AA892, 895.)

**B. The Department’s Enforcement Action.**

However, rather than the *90 unfair acts or practices* alleged in the MCE report, this enforcement action, brought by the Department in January 2008 and *expressly based on the MCE* (2AA841:1-6), alleged *130,000 acts* in violation of the UIPA. (1AA24.)

The Department thereafter increased the purported violations from 130,000 to over *850,000*. (1AA25.) But nearly 800,000 of the newly alleged violations were based on the mere omission of a notice in two form documents during the period that PacifiCare *was awaiting the Department’s approval of both notices’ language*. (1AA43, 46, 151-153.) Significantly, the Department had characterized the omission of such notices in a confidential MCE report as “violations of laws other than Section 790.03.” (1AA383:5-7; 2AA868, 873 [§10169, subd. (i) violation].)

**C. The Administrative Proceedings.**

An administrative law judge (“ALJ”) presided over a nearly four-year evidentiary hearing between December 2009 and June 2013. (1AA91.)

Relying on the Commissioner’s regulations and his many other interpretations of section 790.03(h), the ALJ issued a proposed decision in August 2013, recommending a penalty of \$11.5 million against PacifiCare. (1AA92.)

The Commissioner rejected the ALJ’s recommended decision (1AA92), and on June 9, 2014, issued his decision (the “Decision”) that increased the penalty to \$173.6 million – a *fifteen-fold* increase. (1AA302-303.)

His Decision relied, in part, on (1) his “single act” interpretation of section 790.03(h), (2) his definition of “knowingly committed” under section 790.03(h), and (3) his definition of “willful” under section 790.035, which interpretations are at issue in this appeal.

**D. PacifiCare’s Action Against the Commissioner.**

On July 10, 2014, PacifiCare filed a petition for writ of administrative mandamus, challenging the Commissioner’s Decision under Code of Civil Procedure section 1094.5 and Government Code section 11523, *and* a complaint for declaratory and injunctive relief challenging the three aforementioned regulations pursuant to Government Code section 11350. (1AA13, 78-80.)

On March 2, 2015, the trial court divided the action into phases. (RT55:5-25.) Phase One addressed, *inter alia*, the validity of the three regulations at issue pursuant to PacifiCare’s motion for judgment on the pleadings. (1AA362-363; 3AA1130-1132.)

On September 8, 2015, the trial court issued its order (the “September 8 Order”), invalidating the three regulations as incompatible with the text of the relevant statutes and legislative history. (3AA1194-1198.)

### **E. The Commissioner's Appeal.**

During an “extensive” off-the-record discussion at a June 15, 2016, status conference, the Commissioner expressed his desire to use a preliminary injunction order as a basis for an immediate appeal of the court’s September 8 Order invalidating his regulations. (RT297, 343:18-23.)

On July 15, 2016, PacifiCare filed its preliminary injunction motion, which included a declaration specifying the threat of continued enforcement of the invalidated regulations. (4AA1290-1305.)

In his response, the Commissioner “agree[d]” that the September 8 Order “warrants issuance of a preliminary injunction,” but did “not stipulate to the validity of the September 8 Order.” (4AA1307.)

On August 10, 2016, the court held a hearing (RT301-341), and two days later, issued a minute order, which stated that “[a]s the court reads the Commissioner’s July 28, 2016 Response to PacifiCare’s Motion, the Commissioner stipulates to entry of an injunction enjoining enforcement of the subject regulations[,]” which “would appear to resolve the issue of irreparable harm.” (Respondent’s Appendix, p. 5.)

At the next hearing on August 18, 2016, the Commissioner filed a response arguing that he “ha[d] *not* stipulated to an injunction, to the existence of irreparable harm or to the absence of harm to the public,” but he contended that “the irreparable harm issue ... is not relevant” and did not offer any evidence that such an injunction would result in any harm to the public. (4AA1328.)

The superior court described the Commissioner’s position at that hearing as follows: “[I]rreparable harm is not an issue ... the court can go ahead and issue an injunction .... And then that preserves [the Commissioner’s] right to appeal which is one of the reasons we were talking about issuing an injunction to begin with.”

(RT343:18-23.) The Commissioner confirmed the court’s understanding of his position. (RT343:24-26.)

The court thereafter issued its order enjoining the Commissioner from enforcing the invalidated regulations (4AA1334-1337). On August 19, 2016, the Commissioner filed his notice of appeal from that order. (4AA1345.)

Three weeks later, on September 6, 2016, the Commissioner filed a motion and an accompanying declaration, seeking confirmation that his appeal acted as an automatic stay of the preliminary injunction or to stay the injunction and to stay the entire trial court proceedings. (4AA1363-1395.) This motion was denied. (4AA1514.)<sup>4</sup>

On September 28, 2016, in response to the Commissioner’s petition for a writ of supersedeas, this Court suspended the preliminary injunction pending resolution of this appeal, noting that it involves “‘substantial’ issues of law,” while acknowledging the Court’s ruling “does not pass on the merits of [the] appeal.” It denied the Commissioner’s application to stay the superior court proceedings. (November 3, 2016 Order.)

### **III. STANDARD OF REVIEW**

This appeal concerns whether three of the Commissioner’s regulations are invalid because they conflict with the statutes that they purport to define.

The Commissioner argues that “[t]he regulations embody the Commissioner’s considered policy choices” to promote “the Legislature’s consumer protection objectives” and “thus are quasi-legislative in nature,” and that

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<sup>4</sup> This *post-appeal* motion and the accompanying declaration (4AA1363-1395) were not before the superior court when issuing the preliminary injunction; therefore, PacifiCare objects to their inclusion in the Commissioner’s appendix.

“this court’s inquiry could end with a determination that the rules are within the Commissioner’s broad delegated lawmaking authority.” (AOB 27.)

Alternatively, the Commissioner argues that “[e]ven assuming the regulations [are] mostly or wholly interpretative, ... they must be upheld” because he has ““technical knowledge and expertise”” and ““properly interpreted the statutory mandate.”” (AOB 27.)

In fact, the regulations are interpretative since they do not implement, but *solely* interpret, sections 790.03(h) and 790.035. Moreover, as shown herein, little, if any, deference is owed to the Commissioner’s interpretations.

**A. Regulations Are Either Quasi-Legislative or Interpretative.**

“It is a ‘black letter’ proposition that there are two categories of administrative rules and that the distinction between them derives from their different sources and ultimately from the constitutional doctrine of the separation of powers. One kind – quasi-legislative rules – represents an authentic form of substantive lawmaking: Within its jurisdiction, the agency has been delegated the Legislature’s lawmaking power. [Citations.] Because agencies granted such substantive rulemaking power are truly ‘making law,’ their quasi-legislative rules have the dignity of statutes. When a court assesses the validity of such rules, the scope of its review is narrow.” (*Yamaha Corp. of America v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 10 (*Yamaha*).)

“It is the other class of administrative rules, those *interpreting* a statute, that is at issue in this case. Unlike quasi-legislative rules, an agency’s interpretation does not implicate the exercise of a delegated lawmaking power; instead, *it represents the agency’s view of the statute’s legal meaning and effect, questions lying within the constitutional domain of the courts*. But because the agency will often be interpreting a statute within its administrative jurisdiction, it may possess

special familiarity with satellite legal and regulatory issues. It is this ‘expertise,’ expressed as an interpretation ... that is the source of the presumptive value of the agency’s views. ... Because an interpretation is an agency’s *legal opinion*, however ‘expert,’ rather than the exercise of a delegated legislative power to make law, it commands a commensurably lesser degree of judicial deference.” (*Yamaha, supra*, 19 Cal.4th at p. 11, second set of italics added.)

**B. The Regulations at Issue Are Interpretive.**

The regulations here are interpretative because they *define* particular words in sections 790.03(h) and 790.035 and *interpret* the introductory phrase in section 790.03(h).

In *Association of California Insurance Companies v. Jones* (2017) 2 Cal.5th 376 (*ACIC*), upon which the Commissioner relies (AOB 23-25), our Supreme Court considered the validity of regulations *implementing* section 790.03, *subdivision (b)* – which is not at issue here – which prohibits making or disseminating any “untrue, deceptive, or misleading” statements with respect to the business of insurance. The Court found that the regulations at issue there, which treated an incomplete replacement cost estimate for homeowners insurance as a misleading statement under subdivision (b), was within the Commissioner’s lawmaking authority. (*Id.* at p. 396.) Observing that “in certain circumstances, a regulation may have both quasi-legislative and interpretative characteristics – as when an administrative agency exercises a legislatively delegated power to interpret key statutory terms” (*id.* at p. 397, quotation marks omitted), the court declined to decide “whether the Regulation’s interpretation of a ‘misleading’ statement under section 790.03, subdivision (b) was best characterized as quasi-legislative or merely an interpretative rule devoid of any quasi-legislative authority.” (*Ibid.*) Instead, it found that “[e]ven if the Regulation were considered

purely interpretive, [it] would conclude the Commissioner has reasonably and properly interpreted the statutory mandate” because “the Regulation does no more than identify a particular class of offending statements within the general statutory prohibition on any untrue, deceptive, or misleading statements in connection with the business of insurance.” (*Id.* at pp. 397-398.)

Still, the challenged regulations in *ACIC* clearly assumed elements of lawmaking because they specified *how* an insurer must calculate and communicate cost estimates in order to avoid their being deemed “untrue, deceptive, or misleading” under section 790.03, subdivision (b). (*ACIC, supra*, 2 Cal.5th at pp. 383-384.) Thus, they *implemented* subdivision (b) in the context of replacement cost estimates for homeowners insurance.

Significantly, our high court compared the Commissioner’s authority under section 790.03, *subdivision (b)*, with *section 790.03(h)* at issue here, and stated, “When the Legislature is confident that it has identified a given problem and the best solution, it may enact its specific remedy into statutory law – as it did with unfair claims settlement practices in section 790.03, *subdivision (h)*. But the Legislature may also choose to grant an administrative agency broad authority to apply its expertise in determining whether and how to address a problem without identifying specific examples of the problem or articulating possible solutions.” (*ACIC, supra*, 2 Cal.5th at p. 399; italics added.) And the regulations at issue in *ACIC* addressed a particular problem (replacement cost estimates) and implemented a standardized solution to avoid a misleading statement under section 790.03, subdivision (b), thereby applying the Commissioner’s “expertise in determining ... how to address a problem.” (*Ibid.*)

In contrast, here, the Commissioner is solely interpreting words or phrases in sections 790.03(h) and 790.035, which is purely an interpretative function because it “represents the agency’s view of the statute’s legal meaning and effect.”

(*Yamaha, supra*, 19 Cal.4th at p. 11.) Indeed, in *ACIC*, our high court defined an “interpretative characteristic” “as when an administrative agency exercises a legislatively delegated power to interpret key statutory terms.” (*ACIC, supra*, 2 Cal.5th at p. 397, quotation marks omitted.) That is precisely what the regulations for sections 790.03(h) and 790.035 do.

Accordingly, both *Yamaha* and *ACIC* support PacifiCare’s position that the Commissioner’s interpretation of sections 790.03(h) and 790.035 is purely an interpretative function.

**C. Whether Quasi-Legislative or Interpretative, No Regulation Is Valid Unless Consistent and Not in Conflict with the Relevant Statute.**

Government Code section 11342.2 provides: “Whenever by the express or implied terms of any statute a state agency has authority to adopt regulations to implement, interpret, make specific or otherwise carry out the provisions of the statute, no regulation adopted is valid or effective unless consistent and not in conflict with the statute and reasonably necessary to effectuate the purpose of the statute.”

Thus, “ ‘the rulemaking authority of an agency is circumscribed by the substantive provisions of the law governing the agency .... [R]egulations that alter or amend the statute or enlarge or impair its scope are void.’ ” (*Carmel Valley Fire Protection Dist. v. State of California* (2001) 25 Cal.4th 287, 300.)

“Where regulations are void because of inconsistency or conflict with the governing statute, a court has a duty to strike them down.” (*California Sch. Bds. Assn. v. State Bd. of Educ.* (2010) 191 Cal.App.4th 530, 544; accord, *Assn. for Retarded Citizens of Cal. v. Dept. of Developmental Services* (1985) 38 Cal.3d 384, 391; *Morris v. Williams* (1967) 67 Cal.2d 737,748.)

When “an implementing regulation is challenged on the ground that it is ‘in conflict with the statute,’ ” the court “exercises independent judgment.” (*Western*

*States Petroleum Assn. v. Bd. of Equalization* (2013) 57 Cal.4th 401, 415.)

“[E]ven quasi-legislative rules are reviewed independently for consistency with controlling law. ... The court, not the agency, has ‘final responsibility for the interpretation of the law’ under which the regulation was issued.” (*Yamaha, supra*, 19 Cal.4th at p. 11, fn. 4; accord, *ACIC, supra*, 2 Cal.5th at p. 396; *Esberg v. Union Oil Co.* (2002) 28 Cal.4th 262, 269.)

The Commissioner suggests that a heightened burden of showing a “ ‘total and fatal conflict’ ” applies to PacifiCare’s “facial” challenge to his regulations. (AOB 25-26.) But with one exception noted below, the cases cited by the Commissioner to heighten PacifiCare’s burden (AOB 26) are not relevant because they involve challenges to *statutes* or *ordinances*, not regulations as inconsistent with statute. (See, e.g., *Today’s Fresh Start, Inc. v. Los Angeles Cty. Office of Educ.* (2013) 57 Cal.4th 197, 218 [facial constitutional challenge to Legislature’s procedures for revocation of charter school]; *Tobe v. City of Santa Ana* (1995) 9 Cal.4th 1069, 1083-1084 [facial challenge to the constitutional validity of an ordinance]; *Coyne v. City & Cty. of San Francisco* (2017) 9 Cal.App.5th 1215 [ordinance is preempted by Ellis Act].) Only *T.H. v. San Diego Unified School Dist.* (2004) 122 Cal.App.4th 1267, involved a challenge to regulations on the ground they “violate state law and are unconstitutional” (*id.* at p.1273), but that decision simply quoted the standard in *Tobe* for a facial challenge to the constitutionality of a *statute* (*id.* at p. 1281), and ultimately determined the regulations were not “inconsistent with state law” (*id.* at p. 1285).

**D. The Scope of Judicial Deference to an Agency’s Interpretation Is Fundamentally Situational.**

“Whether judicial deference to an agency’s interpretation is appropriate and, if so, its extent – the ‘weight’ it should be given – is ... fundamentally *situational*. A court assessing the value of an interpretation must consider a

complex of factors material to the substantial legal issue before it, the particular agency offering the interpretation, and the comparative weight the factors ought in reason to command.” (*Yamaha, supra*, 19 Cal.4th at p. 12.)

There are “two broad categories of factors relevant to a court’s assessment.” (*Yamaha, supra*, 19 Cal.4th at p. 12.) “In the first category are factors that ‘assume the agency has expertise and technical knowledge, especially where the legal text to be interpreted is technical, obscure, complex, open-ended, or entwined with issues of fact, policy, and discretion.’ ” (*Ibid.*)

The second category of factors are those “suggesting that the agency’s interpretation is likely to be correct,” which includes (1) the care taken, (2) “evidence that the agency ‘has consistently maintained the interpretation in question,’” and (3) “indications that the agency’s interpretation was contemporaneous with legislative enactment of the statute being interpreted.” (*Yamaha, supra*, 19 Cal.4th at p. 13.)

Although the Commissioner claims that his statutory interpretations are entitled to “great weight and respect” (AOB 24), his regulations do not satisfy *any* of the factors that support deference. As explained more fully in section IV.D.2, the regulatory interpretations of section 790.03(h) were *not* made contemporaneously with the enactment of section 790.03(h), but 20 years later; the Commissioner has *not* consistently maintained the interpretations of section 790.03(h); the regulations were promulgated in deliberate defiance of the Supreme Court’s interpretation; and the regulations do not draw upon the agency’s “technical knowledge and expertise,” but interpret commonly used statutory language, like “general business practice,” “knowingly,” and “willful.”

By contrast, in *ACIC, supra*, 2 Cal.5th at pages 383-384, the Commissioner drew upon his expertise that insurers were providing replacement-cost estimates for homeowners insurance far lower than the actual replacement cost and then

crafted regulations requiring insurers to abide by standardized criteria for calculating and communicating replacement costs.

**IV. The Trial Court Correctly Held that Regulation 2695.1(a)'s "Single-Act" Interpretation Conflicts with Section 790.03(h).**

Section 790.03(h) proscribes "[k]nowingly committing or performing with such frequency as to indicate a general business *practice* any of the following [16] unfair claims settlement *practices*." (§ 790.03(h), italics added.)

Regulation 2695.1(a) interprets section 790.03(h) as follows: "Section 790.03(h) ... enumerates sixteen claims settlement practices that, when *either* knowingly committed *on a single occasion* or performed with such frequency as to indicate a general business practice, are considered to be unfair claims settlement practices and are, thus, prohibited by this section of the California Insurance Code. The Insurance Commissioner has promulgated these regulations in order to accomplish the following objectives: [¶] (1) To delineate certain minimum standards for the settlement of claims which, *when violated knowingly on a single occasion* or performed with such frequency as to indicate a general business practice shall constitute an unfair claims settlement practice ...." (Reg. 2695.1, subd. (a), italics added.)

In his Decision against PacifiCare, the Commissioner reaffirmed his interpretation that "an insurer violates Insurance Code section 790.03, subdivision (h) by a single act knowingly committed or by actions performed with such frequency as to indicate a general business practice." (1AA97.)

**A. The Supreme Court and Lower Courts Have Repeatedly Rejected the Commissioner's "Single-Act" Interpretation of Section 790.03(h).**

As the trial court correctly ruled, this regulation's interpretation of section 790.03(h) is contrary to the California Supreme Court's construction of its statutory text and legislative history. (3AA1195-1196; 4AA1335-1336.)

The Commissioner responds that *Royal Globe Insurance Co. v. Superior Court* (1979) 23 Cal.3d 880 (*Royal Globe*) “held that a single act may violate section 790.03[.]” (AOB 14, 31.)

But regulation 2695.1, subdivision (a) was issued in 1992 *after Moradi-Shalal v. Fireman’s Fund Insurance Cos.* (1988) 46 Cal.3d 287 (*Moradi-Shalal*) overruled *Royal Globe*. And *Moradi-Shalal* endorsed Justice Richardson’s dissenting opinion in *Royal Globe*, which “criticized the [*Royal Globe*] majority for holding that a single act of misconduct could constitute a violation of section 790.03.” (*Moradi-Shalal, supra*, 46 Cal.3d at p. 295.)

Moreover, in 2013, in *Zhang, supra*, 57 Cal.4th at page 380, footnote 8, our Supreme Court confirmed, “We approved the reasoning of Justice Richardson’s *Royal Globe* dissent, holding that the UIPA contemplates only administrative sanctions for *practices* amounting to a *pattern of misconduct*.” (Italics added.)

Nonetheless, the Commissioner contends that “the *Moradi-Shalal* Court deferred to the Legislature and declined to revisit the interpretation of section 790.03(h).” (AOB 15, 31.) The Commissioner is wrong, as shown below:

In authorizing a private right of action in 1979, the majority in *Royal Globe* had interpreted section 790.03(h) “as conferring on the injured claimant a cause of action arising from a *single instance* of unfair conduct, so that a plaintiff did not have to prove that the insurer committed the acts prohibited by the statute as a general business practice.” (*Moradi-Shalal, supra*, 46 Cal.3d at p. 294.)

In his dissenting opinion in *Royal Globe* (subsequently adopted by the *Moradi-Shalal* majority), Justice Richardson explained why *Royal Globe*’s “single-act” reading was wrong. (*Royal Globe, supra*, 23 Cal.3d at p. 894 (conc. & dis. opn. of Richardson, J.)) He noted that under the plain language of section 790.03(h), conduct “does not become unfair or unlawful until those acts are repeated with such frequency as to constitute a ‘general business practice[.]’” and

he criticized the majority for attempting to rewrite the statutory text (in the same way that the Commissioner has done here):

Under this strained interpretation, the majority reads subdivision (h) as distinguishing between acts “knowingly committed” and acts “performed,” limiting to the latter class the qualifying phrase “with such frequency” etc. In essence, the majority’s reading simply deletes the “frequency” requirement of the act. This is strange parsing. First, it will be noted that no comma separates the words – “committed or performing,” suggesting that they are to be read together. Furthermore, the majority would split the two present participles “committing” and “performing,” applying the modifying “frequency” clause to the “performing” but not to the “committing” function. It seems obvious, however, that one could not *unknowingly* either “commit” or “perform” a prohibited act under the statute, thus strongly suggesting that the term “knowingly” applies to both “committing” or “performing” and that they are to be read together. Similarly, if they are to be read together for purposes of the adverb “knowingly,” in consistent fashion they should be read together for purposes of the “frequency” clause.

(*Ibid.*)

In *Moradi-Shalal*, our Supreme Court rejected the private cause of action endorsed in *Royal Globe* and ruled that Justice Richardson’s interpretation of section 790.03(h) was “irrefutable.” (*Moradi-Shalal, supra*, 46 Cal.3d at p. 304.) After observing that “[t]he California Unfair Practices Act was derived from the National Association of Insurance Commissioners’ Model Unfair Claims Practices Act, which has been adopted by 48 states” (*id.* at p. 297), the Court stated: “As previously indicated, the cases from other states *without exception* reject *Royal Globe*’s holding that an action under section 790.03 could be based upon a single wrongful act [citation]. Such unanimity of disagreement strongly suggests we erred in our contrary holding. Yet, for the reasons stated by the majority in *Royal Globe*, the plaintiffs in these cases ... seldom have the ability to prove any widespread pattern of wrongful settlement practices on the part of the insurer.

[Citation.] Although the *Royal Globe* majority believed this proof problem justified its conclusion that a single act will subject the insurer to liability for damages for unfair practices, it is more likely that the majority’s initial premise – that a direct action is permitted under section 790.03 – was incorrect, and that the provision was instead limited to providing *administrative* sanctions by the Insurance Commissioner, *once an investigation revealed such a pattern.*” (*Id.* at p. 303, third italics added.)

Our Supreme Court then concluded, “The points raised by the dissent in *Royal Globe*, as reflected in the cases from other states, the adverse scholarly comment, and the available legislative history, seem irrefutable. Neither section 790.03 nor section 790.09 was intended to create a private cause of action against an insurer that commits one of the various acts listed in section 790.03, subdivision (h). ... For all of the foregoing reasons, we have concluded that *Royal Globe*, *supra*, 23 Cal.3d 880, should be overruled. [¶] We caution, however, that our decision is not an invitation to the insurance industry to commit the unfair practices proscribed by the Insurance Code. We urge the Insurance Commissioner and the courts to continue to enforce the laws forbidding such practices to the full extent consistent with our opinion.” (*Moradi-Shalal*, *supra*, 46 Cal.3d at p. 304.)

Several points are clear from this ruling. First, *Royal Globe* had “justified its conclusion that a single act will subject the insurer to liability” in order to permit a plaintiff to bring a private cause of action since private parties “seldom have the ability to prove any widespread pattern of wrongful settlement practices[.]” (*Moradi-Shalal*, *supra*, 46 Cal.3d at p. 303.) Thus, the overruled private cause of action was inextricably intertwined with the single-act interpretation of section 790.03(h).

Second, having rejected a private cause of action under section 790.03(h), the *Moradi-Shalal* majority stated that “the provision [in section 790.03(h)] was

instead limited to providing *administrative* sanctions by the Insurance Commissioner, once an investigation *revealed such a pattern.*” (*Moradi-Shalal, supra*, 46 Cal.3d at p. 303, second italics added.) This language establishes that our high court rejected not only the private right of action, but also the single-act interpretation. This also refutes the Commissioner’s position in his opening brief that “*Moradi-Shalal* did not address whether the Commissioner had administrative enforcement authority to take action against the knowing commission of single acts of unfair claim settlement.” (AOB 31.)

Third, the Commissioner is incorrect when he argues that the Supreme Court’s admonition that its decision ““is not an invitation to the insurance industry to commit the unfair practices proscribed by the Insurance Code”” implies that it did not reject the single-act interpretation. (AOB 32.) To the contrary, the high court’s statement that its decision was not an invitation to commit “unfair *practices* proscribed by the Insurance Code” (italics added) conforms with its statutory interpretation that section 790.03(h) “was instead limited to providing *administrative* sanctions by the Insurance Commissioner, once an investigation *revealed such a pattern.*” (*Moradi-Shalal, supra*, 46 Cal.3d at p. 303, second italics added.)

Fourth, further proof that *Moradi-Shalal* rejected the single-act interpretation of section 790.03(h) is found in Justice Mosk’s dissenting opinion in *Moradi-Shalal*, which acknowledged that the majority had decided the “single-act” question: “But, assert the majority as did the defendants unsuccessfully in *Royal Globe*, a pattern of unfair business practices *must* be shown, not a single deceptive act.” (*Moradi-Shalal, supra*, 46 Cal.3d at p. 316 (dis. opn. of Mosk, J.), italics added.)

Finally, any doubts about the rejection of the single-act interpretation were eliminated in 2013, when our Supreme Court in *Zhang, supra*, 57 Cal.4th 364,

reconfirmed that “[w]e approved [in *Moradi-Shalal*] the reasoning of Justice Richardson’s *Royal Globe* dissent, holding that the UIPA contemplates only administrative sanctions for *practices amounting to a pattern of misconduct*.” (*Id.* at p. 380, fn. 8, italics added.)

After *Moradi-Shalal*, numerous courts have confirmed that section 790.03(h) “is framed in terms of many instances, *not just a single case*[.]” (*Neufeld v. Balboa Ins. Co.* (2000) 84 Cal.App.4th 759, 762, italics added; see *Lance Camper Mfg. Corp. v. Republican Indem. Co. of Am.* (1996) 44 Cal.App.4th 194, 200 [section 790.03(h) applies to an “insurer who *regularly* engages in unfair *practices*,” italics added]; *Carlton v. St. Paul Mercury Ins. Co.* (1994) 30 Cal.App.4th 1450, 1459, fn. 1 [“*Moradi-Shalal* held the Insurance Commissioner is authorized to impose administrative sanctions if investigation reveals a *pattern* of unfair settlement practices, as opposed to a single wrongful act”]; ; *Crenshaw v. MONY Life Ins. Co.* (S.D.Cal. May 3, 2004, No. 02cv2108-LAB (RBB)) 2004 WL 7094011, at \*20 [violation of section 790.03(h) requires evidence that the insurer’s conduct was “part of [a] general business pattern or practice that is unlawful, fraudulent, or unfair”].)

The Commissioner cites *National Cable & Telecommunications Association v. Brand X Internet Services* (2005) 545 U.S. 967, 982, for the proposition that under *Chevron* deference, a court’s *prior* interpretation of a statute trumps an agency interpretation *only* if the statute is unambiguous. (AOB 32.) This reliance is misplaced. First, Justice Richardson’s dissent in *Royal Globe* – which the *Moradi-Shalal* majority adopted – expressly found that section 790.03(h) was *not* ambiguous. (*Royal Globe, supra*, 23 Cal.3d at p. 894 (conc. & dis. opn. of Richardson, J.)) Second, *National Cable* addresses *federal* deference under the *Chevron* doctrine, which is inconsistent with the rules

governing deference in California under *Yamaha*.<sup>5</sup> In any event, the California Supreme Court’s interpretation of section 790.03(h) *subsequent* to the enactment of regulation 2695.1(a) binds the courts. (*Easter v. United States* (2008) 83 Fed.Cl. 236, 248 [*National Cable* does not apply to *subsequent* judicial interpretations of statutes].)

Accordingly, because regulation 2695.1(a) directly conflicts with the Supreme Court’s interpretation of section 790.03(h), the regulation is invalid on its face.

**B. The Commissioner’s “Single-Act” Reading of Section 790.03(h) Is Contrary to the Statute’s Text.**

The Commissioner’s “single-act” reading is also inconsistent with the statute’s plain language based on the canons of statutory construction.

When analyzing the meaning of a statute, courts “begin by examining the statutory language” and “give the language its usual and ordinary meaning and [i]f there is no ambiguity, [courts] presume the lawmakers meant what they said, and the plain meaning of the language governs.” (*People v. Gutierrez* (2014) 58 Cal.4th 1354, 1369, quotation marks omitted, second alteration added.)

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<sup>5</sup> Under *Chevron*, “[i]f a statute is ambiguous, and if the implementing agency’s construction is reasonable, *Chevron* requires a federal court to accept the agency’s construction of the statute, even if the agency’s reading differs from what the court believes is the best statutory interpretation.” (*National Cable, supra*, 545 U.S. at p. 980.) In contrast, under *Yamaha, supra*, 19 Cal.4th at pages 12-13, courts consider “a complex of factors” in determining the weight to give an agency interpretation. Likewise, under *Chevron*, “[a]gency inconsistency is not a basis for declining to analyze the agency’s interpretation” and agencies are obligated to consider the wisdom of their interpretations on a continuing basis (*National Cable, supra*, 545 U.S. at p. 981), whereas under *Yamaha*, courts consider whether the agency has consistently maintained its interpretation. (See section III, *ante*, p. 26.)

Here, section 790.03(h) prohibits “[k]nowingly committing or performing with such frequency as to indicate a general business practice any of the following [16] unfair claims settlement practices ....”

The text and punctuation of section 790.03(h) confirm that an unfair claims settlement practice must be both knowingly performed *and* constitute a general business practice.

First, as Justice Richardson observed, the term “knowingly” in section 790.03(h) modifies both “committing” and “performing” because “no comma separates the words – ‘committing or performing,’ suggesting that they are to be read together.” (*Royal Globe, supra*, 23 Cal.3d at p. 894 (conc. & dis. opn. of Richardson, J.).)

Indeed, other subdivisions of section 790.03 also have overlapping participles that are not separated by a comma and are clearly meant to be read together. (See, e.g., § 790.03, subd. (b) [“[m]aking or disseminating ... any statement ... which is untrue, deceptive, or misleading ...”]; § 790.03, subd. (f)(1) [“[m]aking or permitting any unfair discrimination between individuals of the same class”]; § 790.03, subd. (g) [“[m]aking or disseminating ... any statement that ... named insurers ... are members of the California Insurance Guarantee Association ....”].)

The Commissioner ignores the parallel structure found in many subdivisions of section 790.03 and argues that “[t]he word ‘or’ between the two phrases – ‘knowingly committing’ and ‘performing with such frequency ...’ – allows for the reading that they are alternatives,” whereas Justice Richardson’s interpretation “treats the words ‘committing’ and ‘performing’ as synonyms, rendering one surplusage.” (AOB 28-29.)

However, the different types of unfair practices enumerated under section 790.03(h) require that its opening sentence cover two different ways of

engaging in them, since some of the unfair practices are best described as being “committed” while others are “performed.” For instance, an insurer can *commit* misrepresentations under section 790.03(h)(1), but a misrepresentation is not “performed.” By contrast, other practices are “performed,” but not “committed,” like the practice of “[f]ailing to settle claims promptly” under section 790.03(h)(12). Consequently, interpreting section 790.03(h) according to its plain text does not result in “surplusage” – the Commissioner’s primary argument in support of his interpretation. (AOB 29.)

Second, in contrast with section 790.03(h), the Legislature *has inserted a comma* in other statutory schemes where the adverb adjacent to “committing” or “performing” is *not* intended to modify both participles. For instance, Health and Safety Code section 1367.03, subdivision (g)(3), authorizes administrative penalties “if the director determines that a health care service plan has knowingly committed, or has performed with a frequency that indicates a general business practice, either of the following ....” (See also Health & Saf. Code, § 1368.04, subd. (b) [similar]; Ins. Code § 10199.7, subd. (d) [similar].)

Third, other sections of the Insurance Code use *separate clauses* to distinguish between “knowing” actions and those committed with frequency. For instance, section 789.3, subdivision (e) provides, “Any insurer who violates this article *with a frequency* as to indicate a general business practice *or commits a knowing violation* of this article, is liable for an administrative penalty of no less than thirty thousand dollars (\$30,000) ....” (Italics added; accord, § 10123.31, subd. (c) [similar]; § 10140.5, subd. (c) [similar]; § 10192.165, subd. (b)(4) [similar]; § 10509.9, subd. (d) [similar]; § 10718.5, subd. (d) [similar].) Where “the Legislature uses materially different language in statutory provisions addressing the same subject or related subjects, the normal inference is that the

Legislature intended a difference in meaning.” (*People v. Trevino* (2001) 26 Cal.4th 237, 242.)

Fourth, there is nothing unusual about requiring that conduct be performed *both* “knowingly” and “with a frequency that indicates a general business practice” in order to impose penalties. For instance, Labor Code section 5814.6, subdivision (a) provides, “[a]ny employer or insurer that knowingly violates section 5814 with a frequency that indicates a general business practice is liable for administrative penalties ....”

Fifth, the Commissioner’s interpretation of section 790.03(h) to prohibit a knowingly committed *single act* conflicts with the fact that section 790.03(h) expressly prohibits “practices” – unlike other subdivisions of section 790.03. By definition, a “practice” cannot be committed or performed on a single occasion. Instead, a “practice” is “[a] habitual or customary action.” (Webster’s II New College Dict. (2001) p. 867.)

The Commissioner nonetheless argues that “[s]ection 790.03(h)’s phrase ‘unfair claims settlement practices’ does not support an argument against single-act liability” because “in numerous contexts ‘practice’ has been defined to include single acts.” (AOB 29.) But the two cases cited for this proposition do not support his argument.

In *Walnut Creek Manor v. Fair Employment & Housing Commission* (1991) 54 Cal.3d 245, 269, the relevant statute authorized \$1,000 in damages for any “unlawful practice.” Although the statute did not define “practice,” the California Supreme Court held that the term is “unambiguous” and “means a course of conduct, i.e., to do or perform often, customarily, or habitually; to make a practice of,” or “repeated or customary action; habitual performance; a succession of acts of similar kind; custom; usage.” (*Ibid.*) Thus, the Supreme

Court’s interpretation of “practice” in *Walnut Creek* is consistent with *Moradi-Shalal*, but contrary to the Commissioner’s.

The Commissioner also cites *People v. Ring* (1937) 26 Cal.App.2d Supp. 768, disapproved on other grounds by *Birbrower, Mantalbano, Condon & Frank v. Superior Court* (1998) 17 Cal.4th 119, 128. (AOB 29-30.) However, that decision merely held that “the giving of legal advice for a fee, would constitute the *practice of law* though done but once.” (*Ring, supra*, 26 Cal.App.2d Supp. at p. 773, italics added.) But the “practice of law” is a term of art. (*People ex rel. Lawyers’ Institute of San Diego v. Merchants’ Protective Corp.* (1922) 189 Cal. 531, 535.) *Ring* does not purport to define the generic term, “practice.”

The Commissioner also argues that section 790.03(h) “identifies, among the 16 categories, violations phrased in the singular,” such as “[a]ttempting to settle a claim by an insured for less than the amount to which a reasonable person would have believed he or she was entitled.” (AOB 30, quoting § 790.03(h)(7).) But section 790.03(h)’s introductory sentence explicitly prohibits “any of the following ... [16] practices.” The fact that some practices are described in terms of processing a single claim – for instance, an attempt “to settle a claim ... for less than the amount to which a reasonable person ... was entitled” (§ 790.03(h)(7)) – does not mean that it need not be performed as a practice to be prohibited.

Finally, to the extent section 790.03(h) is ambiguous – and it is not – the Court should reject the Commissioner’s broad single-act reading because “[w]here the [penalty] statute is susceptible of two reasonable constructions ... a defendant is ordinarily entitled to that construction most favorable to him.” (*Bowland v. Municipal Court* (1976) 18 Cal.3d 479, 488 [construing Business and Professions Code provision prohibiting the unlicensed practice of the healing arts]; *Tos v. Mayfair Packing Co.* (1984) 160 Cal.App.3d 67, 75.)

In sum, the canons of statutory construction compel the conclusion that the superior court correctly rejected the Commissioner’s single-act interpretation of section 790.03(h).

**C. The Legislative History Further Confirms that the Single-Act Interpretation Is Incorrect.**

The legislative history further confirms that the Commissioner’s single-act interpretation of section 790.03(h) is incorrect.

The original February 1972 bill (Assembly Bill no. 459), which ultimately enacted section 790.03(h), authorized the Insurance Commissioner to suspend an insurer’s certificate of authority for “committing or performing with such frequency as to indicate a general business practice” any of the enumerated unfair claims settlement practices. (See Assem. Bill No. 459 (1972 Reg. Sess.) as introduced Feb. 17, 1972, cited in PacifiCare’s MJN, exh. B, pp. 135-136 [1AA492-493].) In that version, both “committing or performing” indisputably referred to the “general business practice.” There was no “knowing” element at all.

A subsequent April 1972 amendment to the bill added the word, “knowingly,” to the beginning of the sentence, so that the new statute prohibited “*knowingly* committing or performing with such frequency as to indicate a general business practice” any of the enumerated unfair claims settlement practices. (Assem. Amend. to Assem. Bill No. 459 (1972 Reg. Sess.) April 17, 1972, cited in PacifiCare’s MJN, exh. C, p. 141 [1AA498], italics added.)

No comma was inserted after “knowingly committing,” and this element of scienter was likely added because, as the then-Insurance Commissioner represented to our Supreme Court after section 790.03(h)’s enactment, industry had asked that “some allowance ought to be made for innocent violations in this

area.” (PacifiCare’s MJN, exh. A, pp. 27-28 [Department’s Amicus Brief in *Royal Globe*, pp. 5-6].)

The Commissioner’s brief ignores this legislative history, which confirms that “knowingly” was added to modify the entire introductory sentence to section 790.03(h).

**D. The Commissioner’s Contrary Arguments Are Meritless.**

**1. The Commissioner cannot rely on *subsequent* statutory enactments to interpret section 790.03(h).**

To interpret section 790.03(h), the Commissioner relies on three *subsequent* statutory enactments that did not amend it.

First, the Commissioner argues that section 790.035, enacted in 1989 (after *Moradi-Shalal*), “clarifies that single acts may constitute a violation of the Unfair Insurance Practices Act” because section 790.035 “makes express reference to the words ‘any *act*’ (singular) six times.” (AOB 34-35, italics added.)

This is a red herring. Section 790.035 grants the Commissioner the power to impose penalties for *all subdivisions* of section 790.03, not just subdivision (h). Because section 790.03 prohibits both “acts” and “practices” – depending upon the subdivision – section 790.035 must refer to *both* acts and practices. For instance, subdivisions (a), (c), (d), and (e) prohibit single acts, like issuing a statement misrepresenting the terms of any policy (§ 790.03, subd. (a)), or filing any false statement of financial condition with a public official (*id*, subd. (d)). But section 790.03, subdivision (h) – the subdivision at issue here – addresses only unfair claims settlement “practices.” Accordingly, the reference to “any act” in section 790.035 does not affect the interpretation of section 790.03(h).

The Commissioner next misrepresents section 790.035’s legislative history, citing a background information sheet provided to the Assembly Committee on Finance and Insurance (Commissioner’s RJN, exh. K), which stated “ ‘[t]his bill

[enacting section 790.035] will make insurance companies liable for the initial act.’ ” (AOB 36.) But that committee’s subsequent report explained that the bill authorized the Commissioner to impose penalties for acts comprising prohibited practices *before* a cease-and-desist order was issued – the “initial acts” – whereas current law limited the Commissioner to imposing penalties for acts comprising practices that “continue[d] after a cease and desist order has been issued”:

Under current law, insurers cannot be fined for practices determined by the Commissioner to be unfair or deceptive unless the practices continue after a cease and desist order has been issued. This measure will allow the Commissioner to impose charges for the *initial acts* which prompt regulator action. The author expresses the belief that such authority will serve as a more effective and flexible regulatory tool than restricting penalties to violations of a cease and desist order only.

(Commissioner’s RJN, exh. J [Assem. Com. On Finance and Insurance Analysis], p. 123, italics added.)

Significantly, and contrary to the Commissioner’s position, the Senate Floor Analysis for the very bill enacting section 790.035 acknowledges *Moradi-Shalal’s* conclusion that *section 790.03(h)* prohibits a *pattern of practices*, not single acts:

Under Section 790.03, insurance companies are prohibited from engaging in such practices as [¶] *Committing a pattern* of certain undesirable, specified practices in settling claims. (These claims settlement *practices* are contained in Section 790.03(h) that was the subject of review in both the *Royal Globe* and the *Moradi-Shalal* decisions.)

(Commissioner’s RJN, exh. L [Sen. Rules Com., Office of Sen. Floor Analysis], p. 129; PacifiCare’s MJN, exh. D, p. 145 [1AA551], italics added.) The Commissioner’s brief ignores the Legislature’s acknowledgment of section 790.03(h)’s meaning.

The Commissioner also argues that the enactment of a different statute – section 12921.1 – is a “directive for the Commissioner to investigate an individual consumer complaint about insurance claims handling, and, if appropriate, bring an enforcement action based on that consumer complaint,” which is “in harmony with” the single-act interpretation of section 790.03(h). (AOB 36.)

But section 12921.1’s enactment in 1990 – 18 years after section 790.03(h)’s enactment – sheds no light on section 790.03(h)’s intent. First, a *subsequent* legislature may not interpret a *prior* legislature’s intent. (*Del Costello v. State of California* (1982) 135 Cal.App.3d 887, 893, fn. 8.) Second, section 12921.1 does not purport to interpret section 790.03(h). Third, the ability to *investigate* complaints under *section 12921.1* does not suggest that *section 790.03(h)* covers something other than “unfair claims settlement practices,” as the statutory language plainly provides.

Finally, the Legislature did not “ratify” the Commissioner’s single-act regulation by enacting section 790.034 in 2001, as contended by the Commissioner. (AOB 51.) Section 790.034 merely directs every insurer, upon receipt of a notice of claim, to provide the insured with a copy of “subdivisions (h) and (i) of Section 790.03 along with a written notice” that “Fair Claims Settlement Practices Regulations govern how insurance claims must be processed in this state” and are available on the Department of Insurance web site. (§ 790.034, subd. (b)(1).) Information regarding *how* insurance claims are “*processed* in this state” in no way endorses the Commissioner’s interpretation of the UIPA’s *penalty* provisions, including his single-act interpretation of section 790.03(h).

Critically, section 790.034 calls out only four regulations: “Sections 2695.5, 2695.7, 2695.8, and 2695.9.” (§ 790.034, subd. (b)(2).) *Notably absent from that list are the regulations at issue in this appeal: sections 2695.1 and 2695.2.* “The presumption that the Legislature is aware of an administrative

construction of a statute should be applied only on a showing that the construction ... had been made known to the Legislature.” (*Robinson v. Fair Employment & Housing Com.* (1992) 2 Cal.4th 226, 235, fn. 7.)

Nor does *Yeoman v. Dept. of Motor Vehicles* (1969) 273 Cal.App.2d 71, support the Commissioner’s contention that section 790.034 ratified his single-act interpretation. (AOB 51.) In that case, the Legislature expressly made the regulations applicable since the subsequent legislation declared it a misdemeanor to operate “ ‘a school bus in violation of *any regulation or order of the State Board of Education.*’ ” (*Id.* at p. 81, italics added.)

In any event, since the legislative history for section 790.035 shows that the Legislature was aware of *Moradi-Shalal*’s interpretation of section 790.03(h) (PacifiCare’s MJN, exh. D, p. 145 [1AA551]), it is far more significant that the Legislature has declined to amend section 790.03(h) in the nearly three decades since *Moradi-Shalal*: “When a statute has been construed by judicial decision, and that construction is not altered by subsequent legislation, it must be presumed that the Legislature is aware of the judicial construction and approves of it.” (*In re Estate of Heath* (2008) 166 Cal.App.4th 396, 402.) In contrast, “an erroneous administrative construction does not govern the interpretation of a statute, even though the statute is subsequently reenacted without change.” (*Yeoman, supra*, 273 Cal.App.2d at p. 80.)

**2. The Commissioner’s flawed regulatory interpretation cannot be saved by deference or by its “consumer protection” purpose.**

The Commissioner’s primary defenses of his counter-textual reading of section 790.03(h) is that the “court must give the Commissioner’s approach great weight” and his interpretation serves UIPA’s “consumer protection purpose.” (AOB 28, 30-31.)

The Commissioner is wrong for multiple reasons.

First, regarding the degree of deference owed the Commissioner's interpretation, as noted at pages 25-27, *ante*, any judicial deference depends on "a complex of factors," primarily whether " 'the agency has a comparative interpretive advantage over the courts' " and whether " 'the interpretation in question is probably correct,' " which considers such factors like whether the interpretation was made contemporaneously with the statute's enactment and whether the interpretation has been consistently applied. (*Yamaha, supra*, 19 Cal.4th at pp. 12-13.)

Here, all of the relevant factors counsel against deference to the Commissioner's interpretation: The Commissioner has no comparative advantage in interpreting section 790.03(h), particularly since our Supreme Court rendered a contrary interpretation both *before* and *after* he made his interpretation; the Commissioner's interpretation in 1992 was not contemporaneous with section 790.03(h)'s enactment in 1972; and his agency's interpretation has not been consistent.

Regarding this last point, the then Commissioner and his Department originally endorsed *PacifiCare's* interpretation of section 790.03(h): In *Royal Globe*, Justice Richardson observed that "[s]ince its enactment, the Department [of Insurance] has consistently construed that Section to require a general business practice in order to establish a violation." (*Royal Globe, supra*, 23 Cal.3d at p. 897 (conc. & dis. opn. of Richardson, J.)) Indeed, the Department's amicus brief in *Royal Globe* cited the Department's press release issued after section 790.03(h)'s enactment, which asserted: " 'The law [section 790.03(h)] is patterned upon a model bill developed by the National Association of Insurance Commissioners ... and specifies 13 unfair claims settlement practices which, *if engaged in as a general business practice by an insurer*, authorizes the Insurance Commissioner to issue orders against the insurance company.' "

(PacifiCare’s MJN, exh. A, pp. 30 & 122 [exh. L thereto].)

Second, “where there is no ambiguity in a statute and the administrative interpretation of it is clearly erroneous, even the fact that such administrative interpretation is a longstanding one does not give it legal sanction.” (*Rose v. City of Hayward* (1981) 126 Cal.App.3d 926, 941.) Here, there is nothing ambiguous about section 790.03(h)’s prohibition of “unfair claims settlement *practices*.”

Finally, the Commissioner’s “consumer protection” objective cannot save a regulation that directly conflicts with the statutory text. “[N]o legislation pursues its purposes at all costs” (*Rodriguez v. United States* (1987) 480 U.S. 522, 525-526), and “purpose ... cannot be used to contradict text or to supplement it.” (Scalia and Garner, *supra*, at p. 57.)

Nonetheless, the Commissioner’s “consumer protection” argument is overblown. Limiting liability under section 790.03(h) to unfair *practices* does not give insurers “one free bite” to harm policyholders (AOB 30) or leave a consumer without recourse. (AOB 37.) Instead, as our Supreme Court explained in *Moradi-Shalal*, insurers remain subject to civil (and sometimes punitive) damages “based on such traditional theories as fraud, infliction of emotional distress, and ... either breach of contract or breach of the implied covenant of good faith and fair dealing.” (*Moradi-Shalal, supra*, 46 Cal.3d at pp. 304-305.) Further, “a UCL claim may be based on a *single instance* of unfair business practice.” (*Zhang, supra*, 57 Cal.4th at p. 383, italics added.) And a policyholder can sue his or her insurer for a single, bad-faith act, in which instance, the jury is instructed to consider the same list of unfair practices contained in section 790.03(h). (See CACI No. 2337.)

Moreover, the Department of Insurance has extensive authority to investigate complaints, respond to them, and request “appropriate relief for the complainant.” (§12921.4; see § 12921.1, §12921.3.) It can and does cite insurers

for violations of both non-penal and penal statutes. (See 2AA873-875, 894-896.) The Commissioner also has the authority under *section 790.06* to go to court to enjoin as unfair “any act or practice ... not defined in Section 790.03” (§ 790.06, subd. (a)) and to seek penalties for violations of the resulting injunction (§ 790.07).

In sum, not only is the Commissioner’s interpretation of section 790.03(h) wrong, but he has sufficient authority to perform his duties without having to (i) usurp the Legislature’s right to rewrite section 790.03(h) or (ii) disregard the Supreme Court’s authority to interpret it.

**V. THE TRIAL COURT PROPERLY FOUND THAT  
REGULATION 2695.2(I)’S DEFINITION OF “KNOWINGLY” ALTERS  
THE SCOPE OF SECTION 790.03(h).**

Section 790.03(h) prohibits practices that are “knowingly” committed.

However, regulation 2695.2(*l*) interprets “knowingly” to mean “performed with actual, implied or constructive knowledge, including, but not limited to, that which is implied by operation of law.”

The Commissioner’s unlimited interpretation of “knowingly” enlarges, alters, and is inconsistent with section 790.03(h), as the superior court correctly found. (3AA1196:26-1197:7; 4AA1336.)

And no deference is due the Commissioner’s erroneous imputed-knowledge definition of “knowingly” because the definition “is neither technical nor complex” (*Cal. Veterinary Medical Assn. v. City of W. Hollywood* (2007) 152 Cal.App.4th 536, 556), was promulgated 20 years *after* the statute’s enactment, and is contrary to both the Supreme Court’s interpretation and the legislative history. (See *Yamaha, supra*, 19 Cal.4th at pp. 12-13.)

**A. “Knowingly” Means “Having Awareness” or “Deliberately.”**

“[I]n the absence of specifically defined meaning, a court looks to the plain meaning of a word as understood by the ordinary person, which would typically be a dictionary definition.” (*Hammond v. Agran* (1999) 76 Cal.App.4th 1181, 1189; (*Holland v. Assessment Appeals Bd. No. 1* (2014) 58 Cal.4th 482, 490.)

Black’s Law Dictionary defines “knowing” as “*Having or showing awareness or understanding; well-informed* <a knowing waiver of the right to counsel> 2. *Deliberate; conscious* <a knowing attempt to commit fraud>.” (Black’s Law Dictionary (10th ed. 2014), p. 1003; italics added.) And it defines “knowingly” as “knowledge that the social harm that the law was designed to prevent was practically certain to result; deliberately.” (*Ibid.*)

Consistent with this ordinary meaning, the California Supreme Court in *Royal Globe* stated in dictum that “knowingly committed” under section 790.03(h) means the litigant must “demonstrate that the insurer acted *deliberately*.” (*Royal Globe, supra*, 23 Cal.3d at p. 891, italics added.) While, as explained earlier, *Royal Globe* was overruled regarding its ruling that “section 790.03 ... was intended to create a private cause of action against an insurer that commits one of the various acts listed in section 790.03” (*Moradi-Shalal, supra*, 46 Cal.3d at p. 304), the Supreme Court’s interpretation of “knowingly” to mean “deliberately” has not been called into question.<sup>6</sup>

A requirement of deliberate action or awareness necessarily precludes constructive or implied knowledge, which does not require any subjective awareness. (E.g., *People v. Martinez* (1991) 230 Cal.App.3d 197, 205 [“knowingly” focuses on “the *subjective* awareness, or knowledge, of the

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<sup>6</sup> “Even if properly characterized as dictum, statements of the Supreme Court should be considered persuasive.” (*United Steelworkers of America* (1984) 162 Cal.App.3d 823, 835.)

defendant,” italics added]; *Arthur Andersen LLP v. U.S.* (2005) 544 U.S. 696, 705 [“ ‘[K]nowledge’ and ‘knowingly’ are normally associated with awareness, understanding, or consciousness”]; *Moyer v. Workmen’s Comp. Appeals Bd.* (1973) 10 Cal.3d 222, 231 [“deliberate” is “ ‘characterized by or as resulting from unhurried, careful, thorough, and cool calculation and consideration of effects and consequences’ ”].)

Even the Commissioner conceded that the “dictionary definition” of “knowingly” is “narrow[er]” than that in his regulation 2695.2, subdivision (l). (1AA98.)

**B. Where the Legislature Intended to Apply Constructive Knowledge, It Has Expressly So Provided.**

“When the Legislature uses materially different language in statutory provisions addressing the same subject or related subjects, the normal inference is that the Legislature intended a difference in meaning.” (*Trevino, supra*, 26 Cal.4th at p. 242.)

Here, the Legislature expressly referenced constructive knowledge in another subdivision of section 790.03 when it chose to include both actual *and* constructive knowledge. Specifically, section 790.03, subdivision (b) proscribes the dissemination of any statement about the business of insurance “which is untrue, deceptive, or misleading, and which is known, *or which by the exercise of reasonable care should be known*, to be untrue, deceptive, or misleading.” (Italics added.)

Likewise, section 791.19, subdivision (c) authorizes the suspension or revocation of a license “if the insurance institution or agent *knew* or reasonably *should have known* it was in violation of this article.” (Italics added.)

This suggests that the Legislature intended “knowingly” to denote its ordinary meaning in section 790.03(h) and did not intend to extend it to constructive (or implied) knowledge.

**C. A Constructive- or Implied-Knowledge Standard Conflicts with Section 790.03(h)’s Penal Nature.**

The Commissioner’s diluted definition of “knowingly” also conflicts with the penal nature of section 790.03(h).

By defining “knowingly” to include imputed or constructive knowledge, regulation 2695.2(l) effectively writes out any scienter element from the statute.

For example, the Commissioner imposed a \$2.9 million penalty because PacifiCare denied 3,862 claims pursuant to an insurance policy that had been *expressly approved by the Department*, but that contained an erroneous 12-month (rather than 6-month) exclusionary period for preexisting conditions. (1AA124-125, 131.) PacifiCare subsequently *self-reported* its concerns about the exclusionary period to the Department (1AA125, 130), and once PacifiCare confirmed that the provision was erroneous, it “took quick measures to remediate those 2006 claims.” (1AA130.) Nonetheless, the Commissioner found that this mutual, inadvertent mistake constituted a *knowing* misrepresentation of the policy terms under section 790.03(h)(1) because “PacifiCare is charged with knowing the applicable pre-existing condition exclusionary periods set forth in the Insurance Code.” (1AA127.)

As this example illustrates, the added element of “knowingly” becomes virtually surplusage under the Commissioner’s definition: Any of the unfair claims settlement practices under section 790.03(h) – from “[m]isrepresenting ... pertinent facts” (§ 790.03(h)(1)) to “[f]ailing to affirm or deny coverage ... within a reasonable time after proof of loss” (§ 790.03(h)(4)) – will necessarily be done with either constructive or implied knowledge.

This violates the canon of construction to give “effect” to every word and every provision whenever possible. (Scalia and Garner, *supra*, p. 174.) It also runs afoul of the canon that “[w]here the [penalty] statute is susceptible of two reasonable constructions ... a defendant is ordinarily entitled to that construction most favorable to him.” (*Bowland v. Municipal Court, supra*, 18 Cal.3d. at p. 488.)

Finally, the Commissioner’s removal of the scienter element from section 790.03(h) cannot be squared with its legislative history, which, as explained in section IV.C, shows that the Legislature added the “knowingly” element to the original bill to avoid liability for innocent actions. (*Ante*, pp. 38-39; PacifiCare’s MJN, exh. A, p. 28.)

**D. The Commissioner’s Arguments in Favor of Constructive and Implied Knowledge Are Meritless.**

**1. The Commissioner confuses concepts by relying on the agency principle of imputed knowledge.**

One of the Commissioner’s primary defenses of his definition of “knowingly” is that “a corporation can only act and acquire knowledge through its employees and agents” and therefore he must be allowed to impute knowledge from an insurer’s employees to the insurer to enforce the UIPA. (AOB 38.)

But this confuses two different concepts: (1) the requisite state of mind that triggers liability (here, “knowingly”); and (2) how knowledge is acquired by corporate defendants.

No one disagrees that an agent’s knowledge is imputed to his or her principal, or that a corporation can only obtain knowledge through its employees. But knowledge cannot be imputed from agent to principal when no agent has actual knowledge. (*San Diego Hospice v. County of San Diego* (1995) 31 Cal.App.4th 1048, 1055-1056.) The Commissioner’s “double imputation”

framework – whereby every agent is imputed with implied or constructive knowledge of every fact and legal requirement, and that imputed knowledge is then imputed to the company – creates absurd results: The insurer is held liable for a “knowingly” committed violation over which *no one* in the company had actual knowledge.

**2. The fact that constructive and imputed knowledge are “well-established” legal concepts is irrelevant.**

The Commissioner argues that implied and constructive knowledge are “well-established” in the law. (AOB 38.) That is true, but irrelevant in interpreting *this* statute.

Citing Civil Code section 18 (which defines “[N]otice; actual and constructive”) and Civil Code, section 19 (defining “[c]onstructive *notice*”), the Commissioner argues that “[k]nowledge generally encompasses both actual and constructive knowledge.” (AOB 40-41.)

Not so. Civil Code sections 18 and 19 merely define actual and constructive *notice*, which begs the question whether “knowingly” should be defined to include both actual and constructive notice.

The Commissioner argues that “Black’s Law Dictionary includes within its definition of ‘knowledge,’ not only a definition for ‘actual knowledge’ but also one for ‘constructive knowledge.’ ” (AOB 40.) This, too, is misleading. Black’s Law Dictionary *separately* defines “actual knowledge,” “constructive knowledge,” and “imputed knowledge.” (Black’s Law Dict., *supra*, at p. 1004.) But it defines “knowingly” to mean “knowledge that the social harm that the law was designed to prevent was practically certain to result; deliberately.” (*Id.* at p. 1003.)

The Commissioner also cites the Assembly Committee comment to Civil Code section 683.2, subdivision (b), which concerns joint tenancy and protects “the rights of a purchaser ... in good faith and without knowledge of the

[prior, contrary] written agreement.” (AOB 40, citing Leg. Com. Com., 6A West’s Ann. Civ. Code (2007 ed.) foll. § 683.2, p. 275.) That comment – recommended by the Law Revision Commission (18 Cal. Law Revision Com. Rep. (1986) p. 359) – defines “knowledge” “[f]or purposes of this subdivision” to include “both actual knowledge and constructive knowledge through recordation of the agreement.” But contrary to the Commissioner’s position, the Legislature’s publication of the Law Revision Commission’s definition of “knowledge” in the Assembly Journal (Assem. J. (1985-1986 Reg. Sess.) p. 1368), as reflected in the comment in the annotated code, evidences the Legislature’s recognition that a departure from the ordinary definition of “knowledge” warrants an express definition.<sup>7</sup>

Finally, the Commissioner argues that “[i]n many circumstances, courts have recognized that ‘the means of knowledge is equivalent to knowledge.’” (AOB 41.) But the Commissioner’s cited authorities address “knowledge” in entirely different contexts:

*DuBeck v. California Physicians’ Service* (2015) 234 Cal.App.4th 1254, 1267, addressed the diligence exercised in bringing a claim, observing that “ ‘a party who has the opportunity of knowing the facts constituting the fraud ... cannot be supine and inactive.’ ”

And in *San Francisco Unified School District ex rel. Contreras v. First Student, Inc.* (2014) 224 Cal.App.4th 627, the court had no occasion to interpret “knowingly” because the *Legislature* had already defined that term in the California False Claims Act to include actual knowledge, “ ‘deliberate ignorance

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<sup>7</sup> The Commissioner also cites a Department of Industrial Relations regulation defining “knowingly” (AOB 39-40), but a different agency’s promulgation of a regulatory definition for a different statute does not make it relevant or judicially correct.

of the truth or falsity of the information,’ ” or “ ‘reckless disregard of the truth or falsity of the information.’ ” (*Id.* at pp. 645-646, quoting Gov. Code, § 12650, subd. (b)(3).)

In short, the existence of the concepts of implied and constructive knowledge does not mean that the Legislature intended to depart from the ordinary meaning of “knowingly” in section 790.03(h). Indeed, had it wished to depart from the ordinary meaning of “knowingly,” the Legislature could easily have expressly done so, as it did with section 790.03, subdivision (b), section 791.19, subdivision (c), the California False Claims Act, and Civil Code section 683.2.

**3. The purported purpose of the UIPA does not allow the Commissioner to disregard the statute’s plain meaning.**

The Commissioner argues that “any interpretation that would limit knowledge to actual knowledge would improperly restrict the scope of regulatory authority and fail to serve the consumer protection purposes of the statute.” (AOB 38.)

Again, “consumer protection” does not authorize the Commissioner to dilute the definition so as to make it surplusage or to ignore the Supreme Court’s definition of “knowingly” as “deliberately.” “[N]o legislation pursues its purposes at all costs.” (*Rodriguez, supra*, 480 U.S. at pp. 525-526.)

In support of his position that actual knowledge “would not effectuate the Legislature’s purpose in enacting the Unfair Insurance Practices Act,” the Commissioner cites his predecessor Commissioner’s rebuttal to a comment during the rulemaking process for regulation 2695.2(*I*). (AOB 42, referencing Commissioner’s RJN, exh. I, p. 113.)<sup>8</sup> The comment claimed the Commissioner’s definition makes “[e]very violation ... knowingly committed”; and his response

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<sup>8</sup> The Commissioner mistakenly cites this as exhibit J, p. 43 in his opening brief, but it is clear that he meant exhibit I, p. 113 of his RJN.

laid bare that he had no analytic basis for his definition of “knowingly” since he responded: “The Commissioner has the authority to promulgate regulations that are consumer oriented” because “[t]he NAIC model regulations are the result of an industry dominated effort with a bias in favor of the insurer.” (Commissioner’s RJN, exh. I, p. 113.) In short, there was no effort to derive the correct definition of “knowingly,” but only to dilute it out of existence.

The Commissioner next asserts that his definition prevents companies from intentionally setting up silos to keep the right hand from knowing what the left hand is doing. (AOB 42.) But the Commissioner’s regulation is not limited to extending “knowingly” to include *deliberate ignorance*. Instead, it extends to “implied or constructive knowledge.” (Regulation 2695.2, subd. (l).)

Finally, the Commissioner claims that his diluted definition of “knowingly” is necessary “given the inherent difficulty of establishing a defendant’s state of mind.” (AOB 42.) But knowledge can be proven by circumstantial evidence. (See *People v. Cain* (1968) 261 Cal.App.2d 383, 386; CACI No. 202 [Direct and Indirect Evidence].) Indeed, the prisons are filled with felons whose state of mind was proven by circumstantial evidence, despite the higher burden of proof for criminal cases.

In sum, the Commissioner’s regulation is invalid because it is contrary to the common meaning of “knowingly,” ignores the Supreme Court’s definition of “knowingly” in section 790.03(h), ignores the legislative history by which “knowingly” was added to section 790.03(h) to avoid penalizing innocent errors, and effectively writes “knowingly” out of the statute.

## **VI. THE TRIAL COURT CORRECTLY INVALIDATED REGULATION 2695.2(y)’S DEFINITION OF “WILLFUL.”**

Section 790.035 provides a two-tiered penalty scheme for violations of any subdivision of section 790.03: “Any person who engages in any unfair method of

competition or any unfair or deceptive act or practice defined in Section 790.03 is liable to the state for a civil penalty to be fixed by the commissioner, not to exceed five thousand dollars (\$5,000) for each act, or, if the act or practice was willful, a civil penalty not to exceed ten thousand dollars (\$10,000) for each act. ...” (§ 790.035, subd. (a).)

The Commissioner’s regulation provides: “‘Willful’ or ‘Willfully’ when applied to the intent with which an act is done or omitted means simply a purpose or willingness to commit the act, or make the omission referred to in the California Insurance Code or this subchapter. It does not require an intent to violate law, or to injure another, or to acquire any advantage.” (Reg. 2695.2, subd. (y).)

The superior court correctly found that the Commissioner’s definition of “willful” is inconsistent with the two-tiered structure of section 790.035 and blurs the distinction between willful and non-willful. (3AA1197, 4AA1337.) The Commissioner’s definition also departs from the only statutory definitions of “willful” in the Insurance Code and gives “willful” a different meaning from that applied to a virtually identical companion statute enacted simultaneously with section 790.035.

**A. The Definition of “Willful” Conflicts with Section 790.035’s Two-Tiered Penalty Structure.**

The Legislature did not define “willful” for purposes of section 790.035. Accordingly, to determine the Legislature’s intended meaning, “[t]he words of the statute must be construed in context, keeping in mind the statutory purpose.” (*Dyna-Med, Inc. v. Fair Employment & Housing Com.* (1987) 43 Cal.3d 1379, 1387.)

In *Kwan v. Mercedes-Benz of North America* (1994) 23 Cal.App.4th 174, the Court of Appeal addressed a similar two-tiered civil penalty scheme in the Song-Beverly Consumer Warranty Act, which authorizes a civil penalty of up to

twice the actual damages if “the failure to comply was willful[.]” (Civ. Code, § 1794, subd. (c).) Justice Werdegar, writing for the Court of Appeal, ruled that defining “willful” as “simply a purpose or willingness to commit the act or to make the omission in question” – the same interpretation that the Commissioner adopted here – was inconsistent with the Song-Beverly Act’s two-tiered penalty scheme because it “would render meaningless or inoperative the Act’s distinction between willful and nonwillful violations.” (*Kwan, supra*, 23 Cal.App.3d at p. 184; see *id* at p. 185.)

The Commissioner argues that *Kwan* is distinguishable because it involved a definition of “willful” in a *jury* instruction whereas the Commissioner has enough “expertise in the California insurance market” to properly assess willfulness notwithstanding his definition. (AOB 45-46.) But *Kwan* did not turn on the identity of the fact finder. Rather, Justice Werdegar ruled that willfulness required a higher standard because of the two-tiered penalty scheme and because a lower standard was unfair *to the defendant*. (See *Kwan, supra*, 23 Cal.App.4th at pp. 184-185.)

The Commissioner also argues that, unlike the jury in *Kwan*, he considers various factors in regulation 2695.12 when imposing penalties (including the insurer’s “good faith”). (AOB 46.) But those regulation 2695.12 factors are applied in calculating the penalty *after* deciding willfulness, which increases the maximum penalty range under section 790.035 from \$5,000 to \$10,000 per act.

Here, for example, the Commissioner found that PacifiCare’s failure to timely pay 100% of claims within 30 working days was willful. (1AA165.) This allowed the Commissioner to set the “per act” penalty at \$5,500 – thereby exceeding the maximum \$5,000 “per act” penalty for non-willful violations – despite his application of the regulation 2695.12 factors and PacifiCare’s

satisfaction of the performance standard for timely payments required as a condition of PacifiCare's merger with UnitedHealth. (1AA159, 167.)

The Commissioner contends that he can preserve the integrity of the two-tiered penalty scheme because "if subdivision (h) is read in the disjunctive," a prohibited general business practice "may be a violation that is neither knowingly committed nor willful." (AOB 47.) But if a practice is performed with such frequency to be a general business practice, it is difficult to argue that those frequently performed acts were not done with a "willingness to commit" them (Reg. 2695.2(y)).

Alternatively, the Commissioner argues that "[k]nowing violations are not necessarily willful." (AOB 47.) But if "knowingly" is defined as it should, i.e., requiring awareness, a "knowingly" committed act would always be performed with a "willingness to commit" it. Alternatively, even if "knowingly" includes constructive or implied knowledge, as the Commissioner contends, performance of the act, regardless of the nature of the "knowledge," would still likely be with the "willingness to commit the act" (Reg. 2695.2, subd. (y)).

The Commissioner next argues that since the Legislature did not define "willful," he was entitled to model it on the definition in Penal Code section 7 (AOB 44) and argues that "knowingly is not synonymous with willful" under Penal Code section 7. (AOB 48.)

But the Commissioner's premise – that the Penal Code definitions are appropriately applied to Insurance Code section 790.035 – is wrong. First, Penal Code section 7 was intended to provide a *minimum* level of intent (which must be proven beyond a reasonable doubt) before finding a defendant guilty of a criminal violation. It was not designed for the purpose of *enhancing* a penalty, as in section 790.035. Second, "knowingly" as defined in Penal Code section 7 requires more knowledge than the Commissioner's diluted definition of

“knowingly” since “knowledge” under Penal Code section 7 requires “knowledge that the facts exist.” (Pen. Code, §7(5).) Thus, under the Penal Code, all “knowingly” committed acts are necessarily “willful” acts – the opposite of the UIPA’s scheme by which “willful” conduct is the aggravating circumstance that doubles the penalty range.

In sum, the Commissioner’s definition of “willful” ignores section 790.035’s two-tiered structure.

**B. The Commissioner’s Definition Fails to Harmonize Section 790.035 with Section 790.03 Because It Makes the *Enhanced Penalty* the *Customary Penalty*.**

In construing a statute, “statutes or statutory sections relating to the same subject must be harmonized ... to the extent possible.” (*Dyna-Med, Inc., supra*, 43 Cal.3d at p. 1387.)

Sections 790.03 and 790.035 are related because section 790.03 defines the unlawful acts or practices upon which the penalties in section 790.035 rest. But if the Commissioner’s definition of “willful” were correct, an insurer’s violation of any of section 790.03’s prohibited acts or practices would usually be “willful.”

For instance, section 790.03(h) – which is at issue here – prohibits “[k]nowingly committing or performing with such frequency as to indicate a general business practice any of the following [16] unfair claims settlement practices.” By definition, knowingly performing an act with such *frequency* to indicate a general business practice suggests a *willingness* to commit the acts that happen to be unlawful.

Other subdivisions of section 790.03 also constitute “willful” actions as defined by the Commissioner. Section 790.03, subdivision (a) prohibits “[m]aking, issuing, [or] circulating ... any ... statement misrepresenting the terms of any policy ....” Under the Commissioner’s definition, any misstatement –

intentional or not – would qualify as “willful” since virtually no statement is made without the “willingness” to make it. (Reg. 2695.2(y).) Similarly, section 790.03, subdivisions (b), (c), (d), (e), and (f) involve (in various contexts) making untrue assertions, “entering into ... agreement[s]” that restrain trade, filing a “false statement of financial condition,” “[m]aking any false entry,” or “permitting any unfair discrimination.” All of these acts would necessarily be “willful” under the Commissioner’s definition since the regulation defines “the intent with which an act is done” as “simply” a “willingness to commit the act.” (Reg. 2695.2, subd. (y).)

In sum, the regulation has so diluted the definition of “willful” that the *enhanced* penalty under section 790.035 becomes the *customary* penalty, thereby failing to harmonize sections 790.03 and 790.035.<sup>9</sup>

**C. The Legislative History of Section 790.035 Confirms that “Willful” Requires Specific Intent to Commit the Violation.**

The legislative history of section 790.035 confirms that “willful” cannot be defined as a mere willingness to commit the act, but is conduct performed with the specific intent to commit the violation.

Both Section 790.035 and section 1858.07 of the McBride-Grunsky Act were enacted simultaneously as companion bills (Sen. Bills Nos. 1363 and 1364) in 1989. (Sen. Rules Com., Off. of Sen. Floor Analysis, Sen. Bill No. 1363 (1989-

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<sup>9</sup> In his reply, the Commissioner may argue that he did not find all of PacifiCare’s actions to be willful in this action. First, his findings of a lack of willfulness in a minority of cases – while welcome – were arbitrary. For instance, he found that PacifiCare “misrepresented member coverage,” but did not find willfulness, even though PacifiCare willingly made the representations alleged to be false. (1AA279-280.) Second, not *all* violations need to qualify as “willful” for the Commissioner’s definition of “willful” to transform the *enhanced* penalty into the *customary* penalty for the vast majority of violations, thereby upsetting the statutory scheme.

1990 Reg. Sess.) as amended Sept. 11, 1989, p. 4 [“SB 1363 is a companion bill to SB 1364 which deals with the McBride-Grunsky rate violations”] cited in PacifiCare’s MJN, exh. F, p. 146 [1AA553]; accord, PacifiCare’s MJN, exhs. D-H [1AA583, 588; 2AA740, 762]; *id.*, exhs. I-J [simultaneous passage].)

Section 790.035, subdivision (a), and section 1858.07, subdivision (a) are virtually mirror images of each other and authorize “a civil penalty not to exceed five thousand dollars (\$5,000) for each act, or, if the act or practice was willful, a civil penalty not to exceed ten thousand dollars (\$10,000) for each act.”

Neither bill enacting section 790.035 or section 1858.07 expressly defined “willful.” However, *section 1850.5* of the McBride-Grunsky Act – enacted in 1947 – defined “willful” for purposes of that Act and thus applied to section 1858.07. It provides:

In this chapter “wilful” or “wilfully” in relation to an act or omission which constitutes a violation ... means with *actual knowledge or belief* that such act or omission constitutes such violation and with *specific intent to commit such violation*.

(§ 1850.5, italics added.)

Given that sections 1858.07, subdivision (a) and 790.035, subdivision (a) were companion statutes, contain virtually identical language, and did not contain a definition of “willful,” it would be illogical if the Legislature intended the virtually identically phrased statutes to have a different definition of willful. “When the Legislature uses the same language ... , we can infer that the same result is intended.” (*People v. McKay* (2002) 27 Cal.4th 601, 622.)

**D. All Statutory Definitions of “Willful” in the Insurance Code Are Identical and Require Specific Intent.**

All three statutory definitions of “willful” found in the Insurance Code are identical and require actual knowledge and a specific intent to violate the law.

(§§1850.5, 11750.1, subd. (d), 12340.9.) In each case, the definitions of “willful” apply to two-tiered penalty statutes in the Insurance Code. (§§1858.07, 1859.1, 11756, 12424.25.)

For instance, under the two-tiered penalty scheme for worker’s compensation in section 11756, subdivision (a) – pursuant to which “willful” failures to comply with a final order of the Commissioner are subject to a maximum \$5,000 penalty, whereas mere failures are subject to a \$50 fine – “willful” is defined as being done “with *actual knowledge or belief* that such act or omission constitutes such violation *and with specific intent* to commit such violation.” (§ 11750.1, subd. (d), italics added.)

“It is a venerable principle that when a word or phrase appearing in a statute ‘has a well-established *legal* meaning, it will be given that meaning in construing the statute ....’” (*Brown v. Superior Court* (2016) 63 Cal.4th 335, 351, citing *Harris v. Reynolds* (1859) 13 Cal. 514, 518; see also *United States v. Bishop* (1973) 412 U.S. 346, 360 [applying the same definition of “willful” to various tax crimes to “promote[] coherence” in the tax law].)

Here, since the only definition that the Legislature has given “willful” in the Insurance Code is to require a specific intent to violate the law, and that definition has been applied to statutes that increase the penalty for “willful” violations – including the concomitantly enacted section 1858.07 – the meaning of “willful” in section 790.035 should be given the same definition.

The Commissioner makes several arguments against the use of the Insurance Code’s definition of “willfully” for purposes of increasing the maximum penalty under section 790.03(h). First, he suggests that “those formulations [of willful] ... would work counter to the purposes of the Unfair Insurance Practices Act.” (AOB 45.) But demanding a higher standard for an *aggravated* penalty does not counter the purposes of section 790.03. Nowhere is there any indication

that the purpose of section 790.035 was to maximize the amount of penalties, regardless of the insurer's good faith or lack of intent to violate the law.

Second, the Commissioner contends that he was empowered to define "willful" as he chooses since the Legislature has not defined the term. (AOB 44.) But the omission of a definition for "willful" in section 790.035 does not mean that he can depart from its "well-established legal meaning" (*Brown v. Superior Court, supra*, 63 Cal.4th at p. 351) or in conflict with the statute's two-tiered structure.

Strikingly, section 790.035, subdivision (a), expressly grants the Commissioner "the discretion to establish what constitutes an act" for purposes of assessing the "per act" penalty. However, it does not grant him discretion to determine what constitutes "willful." This raises "a strong inference" that the Legislature did not intend to grant the Commissioner broad discretion to define "willful," particularly given its settled meaning in the Insurance Code. (*People v. Drake* (1977) 19 Cal.3d 749, 755, superseded by statute on other grounds.) " " "Where a statute, with reference to one subject contains a given provision, the omission of such provision from [the same] statute concerning a related subject ... is significant to show that a different intention existed." ' ' (*Ibid.*) In short, granting the Commissioner the discretion to establish what constitutes "an act," but not "willful," is meaningful.

Finally, the Commissioner argues that "where the Legislature has elected not to so limit the term ["willful"], it has often been understood to require merely deliberate action." (AOB 44.) His cited cases are inapposite. They interpret "willful" in *non-insurance* statutes, and none involves a two-tiered penalty scheme. (See, e.g., *Heritage Residential Care, Inc. v. Division of Labor Standards Enforcement* (2011) 192 Cal.App.4th 75, 84 [stating in dicta that "in some Labor Code contexts," willfulness simply denotes an employer's failure to perform a

required act]; *Patarak v. Williams* (2001) 91 Cal.App.4th 826, 829-830 [interpreting “willful” in Civil Code section 798.86, which is not a two-tiered penalty scheme]; *Apollo Estates, Inc. v. Department of Real Estate* (1985) 174 Cal.App.3d 625, 639 [defining “willfully” in Business and Professions Code section 10177 (not a two-tiered penalty scheme)]; *People v. Clem* (1974) 39 Cal.App.3d 539, 542 [defining “willfully” under the Corporate Securities Law, but this was not a two-tiered penalty scheme and the legislative history supported the court’s definition].)

Indeed, our Supreme Court disagrees with the Commissioner’s characterization of the common understanding of “willful.” It has observed that “the case law appears relatively uniform” in the civil context that “the mere intent to do an act which constitutes negligence is not enough to establish willful misconduct,” and instead “willful” “must relate to the misconduct and not merely to the fact that some act was intentionally done.” (*Calvillo-Silva v. Home Grocery* (1998) 19 Cal.4th 714, 729-730, disapproved on other grounds in *Aguilar v. Atlantic Richfield Co.* (2001) 25 Cal.4th 826.)

## VII. CONCLUSION

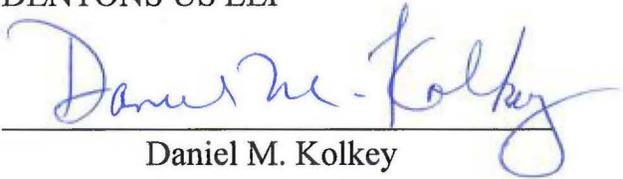
PacifiCare respectfully requests that the trial court's order invalidating Regulations 2695.1(a), 2695.2(l), and 2695.2(y) be affirmed.

DATED: August 1, 2017

Respectfully Submitted,

GIBSON, DUNN & CRUTCHER LLP

DENTONS US LLP



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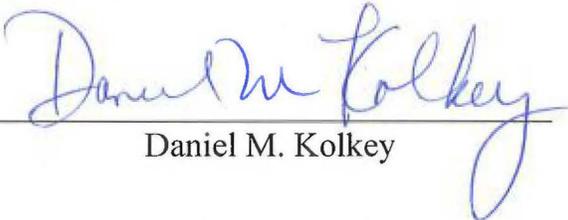
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## CERTIFICATE OF WORD COUNT

Pursuant to rule 8.204(c)(1) of the California Rules of Court, the undersigned hereby certifies that the foregoing Respondent's Brief contains 13,960 words, excluding the cover, the tables, the Certificate of Interested Entities or Persons, the signature block, and this certificate, according to the word count generated by the computer program used to produce the brief.

Dated: August 1, 2017

  
Daniel M. Kolkey

## PROOF OF SERVICE

I, Ariella Boeck, declare as follows:

I am employed in the County of San Francisco, State of California; I am over the age of eighteen years and am not a party to this action; my business address is 555 Mission Street, Suite 3000, San Francisco, California 94105, in said County and State. On August 1, 2017, I served the following documents:

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Cal. Rules of Court,  
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I certify under penalty of perjury that the foregoing is true and correct, that the foregoing document is printed on recycled paper, and that this Proof of Service was executed by me on August 1, 2017, at San Francisco, CA 94105.



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Ariella Boeck