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David H. Yamasaki

Chief Executive Officer/Clerk

Superior Court of CA, County of Santa Clara

Case #1-08-CV-129264 Filing #G-82963

By R. Walker, Deputy

SUPERIOR COURT OF CALIFORNIA

COUNTY OF SANTA CLARA

THE DOAN, an individual on behalf of himself
and a class of similarly situated persons,

Plaintiffs,

vs.

STATE FARM GENERAL INSURANCE
COMPANY, an Illinois corporation,

Defendants.

Case No.: 1-08-CV-129264

FINAL STATEMENT OF DECISION

Trial Date: November 9, 2015
Time: 9:00 am
Dept.: 1 (Complex Civil Lit)

Complaint Filed: 12/4/08
1st Amended Complaint Filed: 1/28/09
2nd Amended Complaint Filed: 5/8/09
3rd Amended Complaint Filed: 7/20/12
4th Amended Complaint Filed: 3/9/15

Judge: Hon. Peter H. Kirwan
Dept: 1 (Complex Civil Litigation)

The above-entitled matter was tried before the Honorable Peter H. Kirwan, sitting without a jury, commencing on November 9, 2015. The court trial proceeded over the course of eight court days between November 9, 2015 and December 3, 2015. Attorneys Robert Buccola, Steven Campora, Brooks Cutter and John R. Parker, Jr. represented Plaintiffs. Attorneys Raoul Kennedy, James Schaefer, and Michael O'Neill represented Defendant State Farm General Insurance Company.

Following the submission of evidence, the Court afforded the parties an opportunity to submit their respective Proposed Statements of Decision. Both parties presented closing

1 arguments on December 3, 2015, and the matter was then taken under submission by the Court.
2 Having considered all of the evidence, the credibility of the witnesses, and pre- and post-trial
3 briefs, the Court issued its Proposed Statement of Decision on March 2, 2016 in accordance
4 with and pursuant to Code of Civil Procedure section 632 and California Rules of Court, Rule
5 3.1590. Thereafter, Defendant State Farm General Insurance Company filed its Objections to
6 Proposed Statement of Decision on March 17, 2016 pursuant to California Rules of Court,
7 Rule 3.1590(g). In addition, Plaintiffs filed a Response to the Proposed Statement of Decision
8 on March 17, 2016 and Defendants immediately filed their Objection to Plaintiffs' Response.
9 To the extent that this Statement of Decision has not elaborated upon certain arguments and/or
10 objections raised by Defendant, they have been reviewed and considered prior to the issuance
11 of this Decision.

12 I. PROCEDURAL BACKGROUND

13 This litigation was originally filed on December 4, 2008. This Court sustained
14 Defendant State Farm's Demurrer to Plaintiff's Second Amended Complaint in June, 2009.
15 Plaintiffs then filed an appeal and on May 14, 2011, the Court of Appeal (6th District) reversed
16 this Court's Order sustaining the demurrer and dismissing Plaintiff's Complaint (See *Doan v.*
17 *State Farm General Insurance Co. (2011) 195 Cal.App.4th 1082*). The matter was then
18 remanded back to this Court and on March 18, 2013, this Court entered an Order certifying
19 Plaintiff's two proposed classes: (1) all California residents insured under a State Farm
20 homeowners or commercial insurance policy; and (2) all California residents insured under a
21 State Farm homeowners or commercial insurance policy who made a claim for actual cash
22 value in a person property claim and who accepted a first party settlement for less than the
23 applicable policy limits, or whose claims are still pending and who have not been offered the
24 policy limits, between December 31, 2004 and the time of this trial.

25 In reversing and remanding, the Court of Appeal found that the Plaintiff could seek
26 declaratory relief where a statutory construction question lies at the heart of the parties'
27 dispute. The Court of Appeal found that the Plaintiff could seek pre-appraisal declaratory
28 relief and that the trial court had discretion to stay the appraisal proceeding pending resolution

1 of the legal questions. Following remand, this Court issued an Order dated February 25, 2014
2 which outlined the issues to be tried in the declaratory relief portion of the case which was set
3 for trial on June 9, 2014. The Order reads, in pertinent part:

4
5 “Thus, the following factual and legal questions are to be adjudicated at the March 3 trial
6 for declaratory relief:

- 7
- 8 ■ Is Defendant’s mere use of the Depreciation Guide a violation of Insurance Code
9 section 2051? If not, is Defendant’s exclusive use of the Depreciation Guide a
10 violation of Insurance Code section 2051?
 - 11 ■ Is Defendant’s use of the Depreciation Guide kept “secret” or “concealed” from
12 claimants? If not, does Defendant “fully explain[] to the claimant in writing” the
13 basis for a depreciation adjustment as required by California Code of Regulations,
14 Title 10, Chapter 5, Section 2695.9 subdivision (f)?

15 The trial will necessarily involve interpreting the meaning of statutory phrases such as “a
16 fair and reasonable deduction for physical depreciation based upon its condition at the time of
17 the injury” as used in Cal. Ins. Code, § 2051, subd. (b)(2), and the “fully explained” requirement
18 of section 2695.9 subdivision (f). The trial will also involve making factual findings on whether
19 Defendant’s claim adjustment conduct violates the relevant statutes and regulations as set forth
20 in paragraph 69 of the TAC. However, the trial will not resolve Plaintiffs’ other causes of action
21 for violation of the Unfair Competition Law (Bus. & Prof. Code, § 17200), breach of contract,
22 and breach of the implied covenant of good faith and fair dealing, or Plaintiffs’ request for
23 injunctive relief. The resolution of Plaintiffs’ declaratory relief cause of action will be limited to
24 a declaratory judgment on the actual controversy as set forth in the TAC.”

25 Prior to the scheduled trial date of June 9, 2014, State Farm moved to stay the case until
26 completion of the Department of Insurance’s Market Conduct Examination of State Farm’s
27 depreciation practices. Ultimately, the case was stayed and the results of the Department of
28 Insurance’s Market Conduct Examination were received by this Court on February 18, 2015.
The stay was then lifted and the declaratory relief cause of action was tried before this Court
between November 9, 2015 and December 3, 2015.¹

¹ During the Phase 1 trial, there was some evidence presented that in May of 2014, State Farm began using a new program for personal property losses (XactContents) in place of it internally created PPIF. This Statement of Decision only addresses State Farm’s practices before it changed to XactContents.

1 **II. FINDINGS OF FACT**

2 Following the submission of evidence and argument by counsel, the Court makes the
3 following findings.

4 Both Plaintiffs Paul Endres and Jane Mariani were insured with State Farm at the time
5 they suffered fire losses at their residences. Mr. Endres suffered a fire loss at his home in
6 Berkeley on April 7, 2011. Ms. Mariani suffered a fire loss at her townhouse in Sacramento on
7 February 28, 2011. Both Plaintiffs submitted claims for damaged personal property resulting
8 from the respective fires. For personal property losses, Plaintiffs' policies provided that State
9 Farm would pay the cost to repair or replace less depreciation. (Trial Exhibit 42).

10 While adjusting a claim for personal property loss following a fire, State Farm would
11 require its insured to complete a Personal Property Inventory Form ("PPIF") itemizing the items
12 claimed as damaged or lost. The PPIF Form had separate columns for the insured to list the
13 quantity of the item, a description of the item, the brand name, the purchase source, the age, and
14 the replacement cost. This form did not contain a separate column for the description of an
15 item's condition at the time of loss. The PPIF is sent or given to the insured who then
16 completes it and returns it to the claims adjuster. During this claims process, State Farm
17 adjusters will often meet with the insured at the property or communicate by telephone or
18 correspondence to assist in the claims process. Once an insured submits the PPIF to State Farm,
19 the items are programmed onto a computer spreadsheet by the claims adjuster using the
20 information obtained by the insured on the PPIF. In addition, State Farm uses a Depreciation
21 Guide (the "Guide") during its claims adjustment process. The Guide is a set of guidelines that
22 provides assistance in the claims adjustment process as it provides useful work life estimates for
23 household items commonly owned by insureds. The Guide had been used by State Farm for
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1 many years and is an age-based useful life expectancy schedule that assumes average quality and
2 average use. Upon receipt of the PPIF from the insured, State Farm then generates a Content
3 Inventory Summary ("CIS") which includes the items on the PPIF and also states the amount of
4 depreciation for each item. For items that are specifically listed in the Guide, State Farm
5 adjusters are trained to start with the Guide's schedule for determining the amount of the
6 depreciation allocated to a particular item on the CIS Form. The preamble to the Guide reads as
7 follows:
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10 The most important factor in determining depreciation is good judgment. Depreciation
11 will vary with usage which, in turn, varies with each family. Determination of the value of an
12 article which is lost, damaged or destroyed requires consideration and reporting of all pertinent
13 factors, including the quality of the articles, model, brand, extent of wear and tear, and the
14 extent to which the article had been used prior to the incident which generated the claim. A
15 depreciation guide or schedule is to be used in conjunction with other indications of value
16 including visual inspection, whenever possible.

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18 Once the CIS is generated by the claims adjuster, it is sent to the insured for review. If
19 the insured is satisfied with the depreciation deduction and has no questions or concerns, State
20 Farm will tender a check to the insured for the Actual Cash Value ("ACV") of the claimed
21 property. If the insured has questions or concerns about the amount of depreciation or how the
22 claim was processed, the adjuster will normally obtain additional information from the insured
23 regarding the disputed item and, if appropriate, make adjustments to the ACV of a particular
24 item. The adjusters were permitted to deviate from the Guide but were instructed to document
25 any change or deviation from the Guide in the claims file. While State Farm does not provide a
26 copy of its Guide to its insureds, the adjusters are permitted to advise the insureds that the Guide
27 will be used in adjusting the claim if asked. While State Farm did not have a policy of hiding or
28 concealing the Guide, there was no evidence presented during the trial that State Farm ever
provided its insured with a copy of the Guide while adjusting a claim. According to one State

1 Farm employee (Stephanie Cheezum), some percentage of insureds between 30% and 60%
2 request their ACV check after receiving the CIS Form from State Farm without further
3 discussion about their claim.
4

5 State Farm's employees testified that ACV is the cost to replace an item less
6 depreciation. In adjusting a claim for personal property, State Farm would typically calculate
7 the ACV by determining the cost of replacing an item new less the depreciation. For items that
8 could not be easily replaced as new such as antiques, collectibles, art, etc., State Farm would
9 typically determine the Fair Market Value in determining its value. With respect to the Mariani
10 and Endres claims, there was evidence at trial that certain items of personal property were
11 depreciated significantly (50%-80%) without full consideration of their condition at the time of
12 loss. In calculating the ACV for many of these items, State Farm appeared to base their
13 depreciation solely on the age of the item, rather than the condition. This was also true with the
14 claim presented by former class representative, The Doan. Although State Farm relies on its
15 CIS Form to show the amount of depreciation taken for an item, there is no requirement that
16 adjusters provide the insureds with any further written explanation of the basis for the
17 depreciation taken.
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20 A Market Study Conduct Examination was performed by the Department of Insurance in
21 2014 regarding State Farm's practices. The Department's Market Study Examination found that
22 State Farm did not consider the actual condition of each item of property before depreciating it.
23 The Department examiners randomly selected 70 Homeowner Claims Files and 70 Commercial
24 Property claims files for examination and ultimately found 78 violations of the California
25 Insurance Code and Code of Regulations. In its report, the Department noted that State Farm's
26 claim files did not include evidence that condition was considered and used in the calculation of
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1 depreciation deducted from the identified claim files except in certain limited cases. In addition,
2 the report found that State Farm failed to fully explain the basis for adjustments for depreciation
3 to claimants in writing, which must reflect a measurable difference in market value attributable
4 to the condition and age of the property.
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6 There was also evidence at trial regarding the review of claims files of 340 class
7 members once their consent was obtained to review their files. Of the 340 files reviewed, there
8 were 158 complete claims files. Several word searches were performed and the word
9 “condition” in the context of a pre-loss condition appeared in only 30 of the 340 claims files,
10 representing 8.8% of all files.
11

12 **III. LEGAL ANALYSIS AND FINDINGS**

13 **A. Declaratory Relief**

14 Preliminarily, this Court finds that Declaratory Relief is an appropriate remedy
15 to attain judicial clarification of the parties’ rights and obligations under the applicable
16 law. (See *Kirkwood v. California State Automobile Assn.* (2011) 193 Cal.App.4th 49).
17 Plaintiffs’ Fourth Amended Complaint (FAC) includes a cause of action for
18 Declaratory Relief which alleges that a dispute has arisen between Plaintiffs and
19 Defendants regarding whether Defendant’s use of the Depreciation Guide violates
20 California Insurance Code Section 2051 and whether Defendant’s practices are in
21 violation of Title 10, Chapter 5, Section 2695.9(f) of the California Code of
22 Regulations. In fact, the California Court of Appeal (6th District) in this very case held
23 that this Court had discretion to stay appraisal pending adjudication of the cause of
24 action for Declaratory Relief in order to resolve matters not encompassed within the
25 scope of appraisal. (See *Doan v. State Farm General Insurance Company* (2011) 195
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1 *Cal.App.4th 1082*). “The trial court’s discretion to consider declaratory relief extends to
2 cases like this, where a statutory construction question lies at the heart of the parties’
3 dispute. [Citations.] And “judicial economy favors resort to declaratory relief in this
4 instance by heading off duplicative future actions challenging [the insurer’s] statutory
5 interpretation as reflected in its adjustment policy. “ (*Doan*, supra, 195 Cal. App.4th at
6 p. 1098).

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8 **B. California Insurance Code Section 2071**

9 California Insurance Code Section 2071 sets forth the language and
10 requirements for the standard form of fire insurance policy for this state. The language
11 in Section 2071 states that the insured will receive the “**actual cash value** of the
12 property at the time of loss, but not exceeding the amount which it would cost to repair
13 or replace the property with material of like kind and quality within a reasonable time
14 after the loss...” (Emphasis added).

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17 **C. California Insurance Code Section 2051**

18 California Insurance Code Section 2051 sets forth the measure of indemnity
19 under an open policy of fire insurance. Section 2051(b) reads, in pertinent part:
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- 21 (b) Under an open policy that requires payment of actual cash value, the
22 measure of the actual cash value recovery, in whole or partial settlement
23 of the claim, shall be determined as follows:
- 24 (1) In case of total loss to structure, the policy limit or the fair market
25 value of the structure, whichever is less.
- 26 (2) In case of a partial loss to the structure, or loss to its **contents**, the
27 amount it would **cost the insured to** repair, rebuild, or **replace** the
28 thing lost or injured less a fair and reasonable deduction for physical
 depreciation based upon its condition at the time of the injury or
 the policy limit, whichever is less. In case of a partial loss to the
 structure, a deduction for physical depreciation shall apply only to

1 components of a structure that are normally subject to repair and
2 replacement during the useful life of that structure. (Emphasis added).

3 As set forth above, the standard form fire policy which is set forth in Insurance
4 Code Section 2071 requires an insurer to pay “the actual cash value of the property at
5 the time of loss.” During the Phase 1 trial, the parties argued for different
6 interpretations of what “actual cash value” meant in the context of a claim for damage
7 or loss to personal property. Plaintiffs argued that Section 2015(b)(2) sets forth the
8 formula for determining actual cash value. Plaintiffs argued that since Section 2051
9 was amended in 2004, the term “actual cash value” is no longer synonymous with “fair
10 market value” when adjusting a loss of personal property. According to Plaintiffs,
11 actual cash value is the cost to replace an item with a new item of like kind and quality,
12 less reasonable depreciation based on the physical condition of the item at the time of
13 the injury. In contrast, Defendants argued that the intent of Section 2051 was to
14 compensate the insured for the fair market value of their lost property at the time of the
15 loss and therefore, actual cash value is synonymous with fair market value when
16 adjusting a loss of personal property.
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20 After a full and thorough consideration of the evidence and arguments presented
21 by the parties, the Court finds Plaintiffs’ interpretation of the meaning of actual cash
22 value to be more persuasive. California Insurance Code Section 2051, as amended in
23 2004, sets forth the precise formula to determine actual cash value. (See *Alexander v.*
24 *Farmers Ins. Co. (2013) 219 Cal.App.4th 1183*). Section 2051(b) only refers to “fair
25 market value” in subsection (1) with regard to a total loss to the structure. Subsection
26 (2) which relates to partial loss to a structure or loss to its **contents**, specifies a different
27 method for recovery for actual cash value and does not include the term “fair market
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1 value.” Had the legislature intended the measure of recovery for subsection (2) to
2 reflect fair market value, it would have included that term as it did in subsection (1).
3 To the contrary, the measure of recovery for actual cash value, per the express language
4 of subsection (2), is the amount it would cost the insured to repair, rebuild, or replace
5 the thing lost or injured less fair and reasonable deduction for physical depreciation
6 based on its condition at the time of the injury.
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8 State Farm’s policy language and claims handling practices provide further
9 support that actual cash value means the cost to repair or replace less depreciation. The
10 Section of State Farm’s policy entitled “**COVERAGE B-PERSONAL PROPERTY**”
11 reads as follows:
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14 1. B1—Limited Replacement Cost Less Settlement.

15 a. We will pay the cost to repair or replace property covered under Section 1-
16 COVERAGES, **COVERAGE B-PERSONAL PROPERTY**, except for property listed
in item b. below, subject to the following:

17 (1) until repair or replacement is completed, we will pay only the cost to repair or
18 replace less depreciation.

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20 b. We will pay market value at the time of loss for:

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22 (1) antiques, fine arts, paintings, statuary and similar articles which by their inherent
23 nature cannot be replaced with new articles;

24 (2) articles whose age or history contribute substantially to their value including, but
25 not limited to, memorabilia, souvenirs, and collector’s items; and

26 (3) property not useful for its intended purpose.

27 2. B2—Depreciated Loss Settlement.
28

1 a. We will pay the cost to repair or replace less depreciation at the time of loss for
2 property covered under Section 1-COVERGES, COVERAGE B—PERSONAL
3 PROPERTY, except for property listed in item b. below.

4 State Farm employees who testified at trial confirmed that when completing the
5 CIS Form, the cost of replacement for most household items would typically be the cost
6 to replace that item with a new item of like kind and quality. For items that were not
7 easily replaceable with new items (antiques, paintings, collector's items, etc.), State Farm
8 would pay the fair market value at the time of loss. This is also consistent with the
9 policy language referenced above.
10

11 One of the critical issues before this Court concerns whether State Farm was in
12 compliance with Section 2051 in determining the actual cash value when adjusting
13 personal property loss claims. More specifically, was State Farm's use of only the Guide
14 in determining actual cash value a violation of Section 2051? Although the preamble to
15 the Guide sets forth a variety of factors to be considered for depreciation purposes, it is
16 clear from the content of the Guide itself that depreciation is based upon average useful
17 years of a particular item and that depreciation is based upon the age and useful life of
18 the average item, not the actual condition of the item at the time of loss. This is not
19 consistent with the language of Section 2051 which clearly contemplates that physical
20 condition will be based upon the condition of the item at the time of loss. Accordingly,
21 the Court finds that State Farm's use of its Depreciation Guide, based on age and average
22 quality goods, to populate its CIS Form does not comply with Section 2051(b), because
23 the Guide fails to consider the condition of the insured's personal property at the time of
24 the injury.
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1 At trial, there was evidence that the Department of Insurance came to a similar
2 conclusion following their Market Conduct examination of State Farm's practices.
3 Specifically, the DOI found that "State Farm did not consider the actual condition of
4 each item of property before depreciating it. Failure to consider and document condition
5 of property in depreciating it violates California Insurance Code sections
6 2051(b)(2)(requiring depreciation to be based on "condition")..." (See correspondence
7 from DOI General Counsel Adam Cole dated Feb. 10, 2015 with attached Public Report
8 of the Targeted Market Conduct Examination of State Farm General Insurance
9 Company). While the Court's findings are consistent with those in the DOI Report, the
10 findings in this Statement of Decision are based exclusively on the evidence presented at
11 trial and independent of the findings of the DOI.
12
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14 **D. Section 2695.9(f) of the California Code of Regulations**

15 Another critical issue that was litigated during Phase 1 concerned whether State
16 Farm's practices met the requirements of Section 2695.9(f) of the California Code of
17 Regulations, Title 10. Section 2695.9(f) states, in pertinent part:
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19 (f) When the amount claimed is adjusted because of betterment,
20 depreciation, or salvage, all justification for the adjustment shall be contained in
21 the claim file. Any adjustments shall be discernable, measurable, itemized and
22 specified as to dollar amount, and shall accurately reflect the value of the
23 betterment, depreciation or salvage. Any adjustments for betterment or
24 depreciation shall reflect a measurable difference in market value attributable to
25 the condition and age of the property and apply only to property normally subject
26 to repair and replacement during the useful life of the property. The basis for any
27 adjustment shall be fully explained to the claimant in writing.

28 As discussed in *Kirkwood v. California State Automobile Assn. Inter-Ins. Bureau*
(193 Cal.App.4th 49, 54 (2011)), the legislature adopted specific regulations following the
amendment to Section 2051 in 2004 that mandated that the insurer itemize, justify and

1 fully explain all adjustments to the amount claimed, including for depreciation. Simply
2 put, Section 2695.9(f) requires that insurers not only document the basis/justification for
3 claims adjustments due to betterment, depreciation or salvage in the claim file, but it also
4 requires the insurer to fully explain to their insured the reason or reasons why they did so.
5 Applying this to the instant case, Section 2695.9(f) imposed, among other things, a duty
6 upon State Farm to advise their insureds in writing as to how the claimed property was
7 depreciated.
8

9
10 There is no limiting language that excludes the applicability of Section 2695.9(f)
11 from claims for damaged personal property/contents. Nor has State Farm cited to any
12 legal authority which supports this position. Accordingly, the Court finds that it does
13 apply to the facts and conduct at issue in the instant case. The real question, therefore, is
14 whether State Farm met the requirements of Section 2695.9(f) in advising their insureds
15 in writing as to how the claimed property was depreciated. At trial, State Farm argued
16 that the CIS Form provided the insured with a written explanation of the depreciation as
17 it contained information about the replacement cost, depreciation percentage,
18 depreciation amount applied, and actual cash value of each item. In addition, State Farm
19 produced evidence of a form letter sent to the claimant advising them that the loss had
20 been adjusted to actual cash value (replacement cost less depreciation) in accordance with
21 the terms of their policy. Notably, the letter also provided a definition of the term
22 Depreciation², however neither the letter nor the CIS Form describes, in writing, the basis
23 of the depreciation taken or whether the physical condition of the items was ever
24 considered during the adjustment of the claim. As noted above, the actual basis for
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² The letter includes the following definition of Depreciation. "Depreciation is a deduction from the replacement cost based on age, condition, quality, and use of the property at the time of the loss."

1 depreciation in a large percentage of cases was premised entirely upon the age and useful
2 life of the item as set forth in the Guide. State Farm's own witnesses testified that any
3 deviations from the Guide were to be documented in the claim file and the evidence
4 presented at trial was that the majority of claims followed the formula from the Guide
5 (age and useful life) without any explanation to the claimant about the use of the Guide,
6 its formula for depreciation, or that the actual physical condition was even considered.
7 While there was no evidence of any active scheme by State Farm to conceal its use of the
8 Guide, it is equally true that State Farm did not provide its insureds with a copy of the
9 Guide nor did they advise the insureds in writing that age and useful life of the property
10 was the basis for depreciation in the cases where the Guide was used exclusively.
11

12
13 While the Court acknowledges the evidence submitted by State Farm relating to
14 the training of its adjusters to have conversations with insureds about the condition of
15 their property at the time of loss, those conversations alone simply do not meet the
16 written requirements of 2695.9(f). Accordingly, the Court finds that State Farm's
17 submission of the CIS Form to the insured without any further written explanation as to
18 the actual basis for the adjustment fails to meet the requirements of Section 2695.9(f).
19 In so ruling, the Court recognizes the impracticality and burden of providing a full
20 written explanation for each and every item that is depreciated in a large fire loss case
21 where often there are hundreds (and possibly thousands) of items claimed. State Farm
22 is required, however, to provide some written explanation for the amounts deducted and
23 the reasons for doing so which takes into consideration the age and condition of the
24 item. Pursuant to Section 2695.9(f), State Farm is required to maintain all justifications
25 for these adjustments in the insured's claims file.
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