

**BAD FAITH INSURANCE LAW IN CALIFORNIA**

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## **SUMMARY AND INTRODUCTION**

Under California law, an insurance company which unreasonably denies coverage has committed the tort of bad faith and faces a possible judgment for the payment of compensatory damages, the payment of attorney's fees, and the payment of punitive damages.

There are three main issues: 1) did the insurance company breach the contract by denying or delaying the payment of benefits? 2) was the conduct of the insurance company unreasonable?; and 3) was the conduct so egregious (done with "malice, oppression or fraud") as to justify the award of punitive damages?

An insurance company which unreasonably denies coverage for a covered claim, or fails to pay for a covered claim, or delays payment of a covered claim, has not only committed a breach of contract, but has also committed the tort of bad faith. When an insurance company has acted in bad faith, the policyholder is entitled to recover not just what the insurance company owed in the first place had it paid the claim, but certain additional damages. Those additional damages include the attorney's fees paid by the policyholder in bringing the lawsuit to establish coverage; emotional distress suffered by the policyholder, and punitive damages.

The California Department of Insurance has enacted the Fair Claims Settlement Practices Regulations at 10 CCR 2695.1. These regulations implement California Insurance Code section 790.03 (h), which prohibit unfair or deceptive practices in the business of insurance.

The Regulations require insurance companies to investigate claims within certain time limits, to advise the policyholder of benefits and coverage under the policy, to promptly pay covered claims, and to explain why any claims are not covered.

Failure to follow these regulations is evidence of bad faith.

## **BREACH OF THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING**

There is an implied covenant of good faith and fair dealing in every contract, requiring that neither party do anything that will injure the right of the other party to receive the benefits of the agreement. *Foley v. Interactive Data Corp.*, 47 Cal. 3d 654, 684 (1988).

When an insurer unreasonably, or without proper cause, withholds a payment or denies a payment that is due under the policy, the insurer has not only breached the contract, but is subject to the tort of bad faith. *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566, 574-75 (1973); *Waters v. United Services Auto Ass'n*, 41 Cal. App. 4<sup>th</sup> 1063, 1070 (1996).

The ultimate test is whether the insurance company acted unreasonably. *Opsal v. United Services Auto Assoc.*, 2 Cal. App. 4<sup>th</sup> 1197, 1205 (1991); *Guebara v. Allstate Ins. Co.*, 237 F. 3d 987, 992 (9th Cir. 2001).

## **BREACH OF DUTIES**

An insurance company has a duty to 1) investigate the pertinent matters thoroughly, impartially, and promptly; 2) to communicate honestly and promptly with the policyholder as the claim is processed; 3) to make timely decisions about the claim; and 4) to explain clearly and forthrightly the bases on which the carrier premised its decision.

Unreasonable conduct can take many different forms. The most common examples are denial of coverage, withholding of benefits, delay in payment of benefits, improper investigation, misrepresenting coverage, refusal to settle claims against the insured, and failing to provide a defense to the insured. But the list is not exhaustive, offering too little to settle.

## **UNREASONABLE DENIAL OF COVERAGE**

Not every denial of coverage amounts to bad faith. The denial must be unreasonable. It is possible that the insurance company breached the contract by failing to pay a covered claim but did not act unreasonably in doing so. In that instance, there is no bad faith. *Tomaselli v. Transamerica Ins. Co.*, 25 Cal. App. 4<sup>th</sup> 1269, 1280-1281 (1994); *Opsal v. United Services Auto Ass'n*, 2 Cal. App. 4<sup>th</sup> 1197, 1205 (1991).

## **“GENUINE DISPUTE DOCTRINE”**

At one end of the spectrum, an insurance company acts in bad faith when it knows there is coverage but denies coverage anyway. *Richardson v. Employers Liability Assurance Co.*, 25 Cal. App. 3d 232, 245 (1972) (punitive damages awarded where insurance company knew that insured had a valid uninsured motorists claim, but nevertheless forced insured to undergo a lengthy arbitration process); *Delgado v. Heritage Life Ins. Co.*, 157 Cal. App. 3d 262, 277 (1994) (actual knowledge that denial of claim is wrongful demonstrates bad faith). At the other end of the spectrum, there may be only modest inferences of bad faith. *Shade Foods, Inc. v. Innovative Products Sales & Marketing, Inc.*, 78 Cal. App. 4<sup>th</sup> 847, 909 (2000).

Whether an insurance company acted unreasonably normally presents a question of fact for the jury. *Walbrook Ins Co. v. Liberty Mutual Ins. Co.*, 5 Cal. App. 4<sup>th</sup> 1445, 1454 (1992); *Filippo Industries, Inc. v. Sun Ins. Co.*, 74 Cal. App. 4<sup>th</sup> 1429, 1438 (1999); *Davy v. Public National Ins. Co.*, 181 Cal. App. 2d 387, 397 (1960). There are instances in which the court may decide, as a matter of law, that the conduct was either reasonable or unreasonable. *Wilson v. 21<sup>st</sup> Century Insurance Co.*, 42 Cal. 4<sup>th</sup> 713, 724 (2003) (insurance company is entitled to summary judgment based on a “genuine dispute” only where there is an absence of triable issues as to whether the insurance company acted reasonably in good faith). See *Chateau Chamberay Homeowners Ass'n v. Associated Intern. Ins. Co.*, 90 Cal. App. 4<sup>th</sup> 335 (2001) (under so-called “genuine dispute doctrine”, there is no bad faith if there was a “legitimate dispute” as to the insurance company’s liability); *Century Sur. Co. v. Polisso*, 139 Cal. App. 4<sup>th</sup> 922, 948-949 (2006) (explaining and limiting the doctrine); *Filippo, supra* at 1438

(doctrine not appropriate where there was no uncertainty in case law about words in policy at issue); *Amadeo v. Principal Mutual Life Ins. Co.*, 290 F.3d 1152 (9<sup>th</sup> Cir. 2002) (doctrine not appropriate where insurance company's interpretation of disability was arbitrary and pretextual).

### **UNREASONABLE DELAY IN PAYMENT OF CLAIM**

An insurance company commits bad faith when it fails to act reasonably in processing and handling a claim. *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566 (1973). One hallmark of bad faith is unreasonable delay in adjusting a claim. Insurance Code section 790(h); *Fleming v. Safeco Ins. Co.*, 160 Cal. App. 3d 31, 37 (1984); *Palmer v. Financial Indem. Co.*, 215 Cal. App. 2d 419, 429 (1963); *Austero v. National Cas. Co.*, 84 Cal. App. 3d 1, 29-30 (1978); *Bodenhamer v. Superior Court*, 192 Cal. App. 3d 1472, 1476 (insurance company deliberately delayed payment); *Richardson v. Employers' Liability Assurance Co.*, 25 Cal. App. 3d 232, 247 (1972) (nine month delay in paying benefits on a claim carrier knew to be valid constitutes bad faith as a matter of law).

### **DUTY TO INVESTIGATE**

An insurer cannot deny payments to its insured without conducting a thorough investigation. *Egan v. Mutual of Omaha Ins. Co.*, 24 Cal. 3d 809, 819 (1979) (“[I]t is essential that an insurer fully inquire into the possible bases that might support the insured's claim”).

An insurance company has a duty to look for coverage and cannot just look for ways to deny coverage. *Mariscal v. Old Republic Ins. Co.*, 42 Cal. App. 4<sup>th</sup> 1617 (1996)(company determined that insured died of illness but ignored other medical records indicating that insured's death was caused by auto accident); *Betts v. Allstate Ins. Co.*, 154 Cal. App. 3d 688, 702 (1984)(insurance company relied on insured's self-serving account of accident and ignored mass of other available evidence indicating insured's negligence; obstinate “no pay” attitude justified punitive damages); *Downey Savings & Loan Association v. Ohio Cas. Ins. Co.*, 189 Cal. App. 3d 1072 (1987); *Hughes v. Blue Cross of Northern California*, 215 Cal. App. 3d 832, 846 (1989) (insurer made no reasonable effort to obtain all medical records in reviewing medical necessity of hospitalization).

An insurer must affirmatively seek out witnesses who can provide information in support of the insured's claim. *Frommoethelydo v. Fire Ins. Exchange*, 42 Cal. 3d 208, 220 (1996); *Mariscal* at 1624; *McCormick v Sentinel Life Ins. Co.*, 153 Cal. App.3d 1030, 1047-1048 (1984).

The insurer cannot in good faith reject its own experts' advice. *Neal v. Farmers Insurance Exchange*, 21 Cal. 3d 910, 921-23 (1978).

*Delgado v. Heritage Life Ins Co.*, 157 Cal App. 3d 262, 278-279 (1994)(evidence that insurer ignored evidence in file which supported claim, while focusing on facts to deny

claim, supported award of \$3 million in punitive damages); *Sprague v. Equifax, Inc.*, 166 Cal. App. 3d 1012, 1025 (1985)(\$ 4 million in punitive damages upheld where claims adjuster testified that he was instructed by supervisor not to find ways to pay claims, but to find ways to deny claims); *Caddice v. Ins. Co. of North America*, 126 Cal. App. 3d 86 (1981) (de facto practice of minimizing payment of claims, as inferred through testimony of claims adjusters and policy manuals); *Tibbs v. Great American Ins. Co.*, 755 F. 2d 1370 (9th Cir. 1985) (bad faith failure to investigate where in-house counsel conducted little investigation and ignored employees who said insured probably entitled to a defense).

The duty to investigate includes the duty to consider legal issues. *Shade Foods, Inc. v. Innovative Product Sales & Marketing, Inc.*, 78 Cal. App. 4<sup>th</sup> 847, 908 (2000) (bad faith failure to evaluate choice-of-law issues).

*Betts v. Allstate Ins. Co.*, 109 Cal. App. 3d 688 (1984). Refusal to face up to adverse evidence of insured's liability for accident. Punitive damages upheld.

*Campbell v. Cal-Gard Security Services, Inc.*, 62 Cal. App. 4<sup>th</sup> 563, 571 (1998). "PAT took no investigation of Campbell's claim or her excuse for late reporting. The jury could reasonably infer from that evidence that PAT had an established practice of not investigating claims and denying payment of them and therefore acted in conscious disregard of the rights of its insured." Punitive damages upheld.

*Jordan v. Allstate Ins. Co.*, 148 Cal. App. 4<sup>th</sup> 1062 (2007). Although insurance company's interpretation of policy was reasonable, factual issues remained as to whether it conducted a reasonable investigation.

*Walker v. Farmers Insurance Co*, 153 Cal. App. 4<sup>th</sup> 965 (2007) (failure to investigate and other bad acts).

*Pulte Home Corp. v. American Safety Indemnity Co.*, 14 Cal. App. 5<sup>th</sup> 1086 (2017) (pattern and practice of refusing coverage under additional insured endorsements; misrepresenting coverage; punitive damages upheld).

### **DUTY TO DISCLOSE COVERAGE**

California Code of Regulations section 2695.4 requires an insurer to disclose all benefits, coverages or other provisions of the insurance policy that may apply to the claim presented. Failure to advise the policyholder of pertinent time limits resulted in waiver to enforce those time limits. *Spray, Gould & Bowers v. Associated International Ins. Co.*, 71 Cal. App. 4<sup>th</sup> 1260, 1272-73 (1999); *Sarchett v. Blue Shield of California*, 43 Cal. 3d 1, 15 (1987); See also, *Textron Financial Corp. v. National Union*, 118 Cal. App. 4<sup>th</sup> 1061 (2004)(punitive damages awarded for concealment of coverage); *Hangarter v. Paul Revere Life Ins. Co.*, 236 F. Supp. 2d 1069 (N.D.Cal. 2002), aff'd, 373 F. 3d 998 (9th Cir. 2004)(failure to advise insured of coverage

amongst many other bad faith acts); *Ramirez v. U.S.A.A.*, 234 Cal. App. 3d 391 (1991)( duty to disclose possible existence of underinsured motorist coverage).

*Baron v. Fire Insurance Exchange*, 154 Cal. App. 4<sup>th</sup> 1184 (2007).  
Misrepresentations and concealment of coverage for fire loss. Punitive damages upheld.

### **WRONGFUL REFUSAL TO DEFEND THIRD PARTY CLAIM**

*Pershing Park Villas v. United Pacific Ins. Co.*, 219 F. 3d 895 (9<sup>th</sup> Cir. 2000);  
*Campbell v. Superior Court*, 44 Cal. App. 4<sup>th</sup> 1308 (1996); *Shade Foods, supra*; *Century Surety Co v. Polisso*, 139 Cal. App. 4<sup>th</sup> 922 (2006); *Amato v. Mercury Cas. Co.*, 53 Cal. App. 4<sup>th</sup> 825 (1997); *Walker v. Farmers Insurance Exchange*, 153 Cal. App. 4<sup>th</sup> 965 (2007).

### **DUTY TO SETTLE**

The insurance company has a duty to make good faith efforts to negotiate towards a reasonable settlement. *Shade Foods, supra*, at 906-907. An insurance company is required to attempt to settle a claim against the insured when there is a reasonable likelihood of a judgment in excess of the insured's policy limits. *Garner v. American Mutual Liability Co.*, 31 Cal. App. 3d 843, 848 (1973); *Communale v. Traders General Ins. Co.*, 50 Cal. 2d 654, 659-660 (1958); *Crisci v. Security Ins. Co.*, 66 Cal. 2d 425, 429 (1967); *Murphy v. Allstate Ins. Co.*, 17 Cal. 3d 937, 941 (1976).

However, the duty may also be breached when there is an unreasonable denial of a settlement offer below the limits of the policy. *Shade Foods, supra*, at 905-907.

A written, formal offer to settle is not necessary to trigger the insurance company's obligation to settle. *Gibbs v. State Farm Mut. Ins. Co.*, 544 F.2d 423, 427 (9<sup>th</sup> Cir. 1976); *Du v. Allstate Ins. Co.*, 697 F.3d 753, 757 (9<sup>th</sup> Cir. 2012).

The duty to settle is implied at law, even if the policy does not contain such a provision. *Murphy, supra*.

When the insurer's own counsel advises the insurer to seek settlement rather than gamble on a verdict, the insurer acts in bad faith when it heedlessly gambles on a verdict and loses. *Kinder v. Western Pioneer Ins. Co.*, 231 Cal. App. 2d 894, 901 (1965).

Conditioning settlement upon demand that insured give up other coverage constitutes bad faith. *Shade Foods, Inc. Innovative Product Sales & Marketing, Inc.*, 78 Cal. App. 4<sup>th</sup> 847 (2000).

### **DAMAGES FOR BREACH OF DUTY TO SETTLE**

The insurance company which breaches the duty to settle is liable for the amount of the judgment or settlement. *Hamilton v. Maryland Cas. Co.*, 27 Cal. 4<sup>th</sup> 718, 725; *Samson v. Transamerica Ins. Co.*, 30 Cal. 3d 220 (1981); *Kransco v. American Empire Surplus Insurance Co.*, 54 Cal. App. 4<sup>th</sup> 1171, 1194; *Consolidated American Insurance Co. v. Mike Soper Marine Services*, 951 F.2d 190-191 (9<sup>th</sup> Cir. 1991); *National Steel Corp. v. Golden Eagle Ins. Co.*, 121 F.3d 496 (9<sup>th</sup> Cir. 1997); *Anderson v. Nationwide Mutual Insurance Co.* 339 F. Supp. 933, 942 (E.D. Cal. 2018); *Metropolitan Prop. & Cas. Ins. Co. v. Hedlund*, 2016 U.S. Dist. LEXIS 152878 (N.D. Cal.) (insurance company liable for stipulated judgment of \$5 million where it breached duty to settle).

### **UNREASONABLE (“LOW BALL”) SETTLEMENT OFFERS**

*Clayton United Servs. Auto Ass’n*, 54 Cal. App. 4<sup>th</sup> 1158 (1997) (insurance company offered \$10,000 on policy limits of \$300,000 to parents whose only child was killed in automobile accident); *White v. Western Title Ins. Co.*, 40 Cal. 3d 870 (1985) (low settlement offers made in course of bad faith litigation). Note California Fair Claims Settlement Practices Regulations on this subject.

### **UNREASONABLY DEMANDING THAT POLICYHOLDER CONTRIBUTE TO A SETTLEMENT**

*Coe v. State Farm Mutual Auto Ins. Co.*, 66 Cal. App. 3d 981 (1977); *Shade Foods, supra* (insurance company offered to pay only a fraction of the covered loss).

### **UNREASONABLY FILING LAWSUIT AGAINST INSURED**

*Hillenbrand, Inc v. Ins. Co. of North America*, 102 Cal. App. 4<sup>th</sup> 584 (2002).

### **UNREASONABLE INTERPRETATION OF COVERAGE**

Plainly unreasonable interpretation of coverage led to punitive damages in *Amadeo v. Principal Mutual Life Ins. Co.*, 290 F. 3d 1152, 1165 (9<sup>th</sup> Cir. 2001); *Hangarter v. Paul Revere Life Ins. Co.*, 236 F. Supp. 2d 1069 (N.D. Cal. 2002), *aff’d*, 373 F. 3d 998 (9<sup>th</sup> Cir. 2004) and *Walker v. Farmers Ins. Exchange*, 153 Cal. App. 4<sup>th</sup> 965 (2007); *Amerigraphics, Inc. v. Mercury Cas. Co.*, 182 Cal. App. 4<sup>th</sup> 1538, 1551-1552 (2010) (unreasonable interpretation of “business income” provision).

Unduly restrictive interpretation of disability on questionnaire. *Moore v. American United Life Ins. Co.*, 150 Cal. App. 3d 610, 621 (1984); *Delgado v. Heritage Life Ins. Co.*, 157 Cal. App. 3d 262, 277 (1984); *Miller v. National American Life Ins. Co.*, 54 Cal. App. 3d 331, 339 (1976).

## ABUSIVE TACTICS

An insurer may not attempt or threaten to rescind the policy where there are no valid grounds for rescission. *Fletcher v. Western Nat'l Life Ins. Co.*, 10 Cal. App. 3d 376, 392 (1970).

An insurer may not attempt to “retire the file without payment” if the insurer, in fact, has no defense to the claim and is simply trying to pressure the claimant into accepting the settlement offer. *Mustachio v. Ohio Farmers Ins. Co.*, 44 Cal. App. 3d 358 (1975).

Unsupported allegations that the insured is guilty of insurance fraud constitute evidence of bad faith. *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566, 575-76 (1973); *Mustachio, supra* at 362 (accusation of arson after basis for charge eliminated by investigator).

Hostile attitude of claims personnel may constitute evidence of bad faith. *Egan v. Mutual of Omaha Ins. Co.*, 24 Cal. 3d 809, 821 (1979) (claims personnel reduced an insured to tears in view of wife and daughter by asserting that insured was a fraud and did not want to return to work).

Adjuster's curt and sarcastic attitude, combined with threats to sue insured, will support a finding of bad faith. *Pistorius v. Prudential Ins. Co.*, 123 Cal. App. 3d 541, 547 (1981).

False promise to provide coverage. *Diamond Woodworks, Inc. v. Argonaut Ins. Co.*, 109 Cal. App. 4<sup>th</sup> 1020 (2003).

Low settlement offers made during course of bad faith litigation. *White v. Western Title Ins. Co.*, 40 Cal. 3d 870 (1985).

Trickery, fraud, backdating documents, concealing evidence, persisting in denial during course of litigation. *Textron Financial Corp v. National Union*, 118 Cal. App. 4<sup>th</sup> 1061 (2004).

Misleading policyholder about uninsured motorist coverage. *Delos v. Farmers Ins. Group*, 93 Cal. App. 3d 642 (1979).

Stalling, stonewalling, and engaging in scare tactics. *Century Surety Co. v. Polisso*, 139 Cal. App. 4<sup>th</sup> 922 (2006) (punitive damages upheld).

Forcing the policyholder to sue in order to obtain benefits. *Richardson v. Employers Liab. Assur. Corp.*, 25 Cal. 3d 232, 246 (1972). Punitive damages upheld where insurance company forced policyholder to litigate an uninsured motorists claim in which there was clear liability and no grounds to contest the claim. The insurance company stalled for



months, forcing Richardson to pursue his claim through arbitration and then through court proceedings to confirm the award.

*George F. Hillenbrand, Inc. v. Insurance Co. Of North America*, 104 Cal. App. 4<sup>th</sup> 784, 818 (2002). Insurance company engaged in protracted nonmeritorious litigation against insured when coverage should have been provided. Punitive damages upheld.

*Notrica v. State Compensation Insurance Fund*, 70 Cal. App. 4<sup>th</sup> 911, 949 (1999). Punitive damages upheld where senior management misled insureds about reserving practices of company

*Bertero v. National General Corp.*, 13 Cal. 3d 43, 65 (1974) (“defendants’ conduct consisted of filing fabricated claims in order to coerce Bertero to settle or abandon a legitimate claim. This flagrant abuse of the judicial process is precisely the type of tortious conduct that an award of exemplary damages is designed to deter”)

*Caddice v. Ins. Co. Of North America*, 126 Cal. App. 3d 86 (1981) (punitive damages upheld where claims representatives misled insured and concealed coverage)

*Walker v. Farmers Insurance Exchange*, 153 Cal. App. 4<sup>th</sup> 965 (2007) (breach of duty to defend, to investigate, to evaluate coverage appropriately; punitive damages upheld but reduced); *Shell Oil Co. v. National Union Ins. Co.*, 44 Cal. App. 4<sup>th</sup> 1633, 1646-1647 (insurance company paid entire policy limits to settle for one insured, leaving another insured without coverage.

### **DUTY OF GOOD FAITH CONTINUES DURING LITIGATION**

The duty of good faith continues even after the insured sues the insurer because the contract and relationship does not terminate with commencement of litigation. *White v. Western Title Insurance Co.*, 30 Cal. 3d 870, 885 (1985). A different rule would allow the insurance company to delay serious investigation until suit is filed and insulate post-litigation conduct from the duty of good faith.

“An insurer’s duty of good faith and fair dealing does not evaporate after litigation commenced.” *Jordan v. Allstate Insurance Co.*, 148 Cal. App. 4<sup>th</sup> 1062, 1076, n.7 (2007); *Fidelity National Financial, Inc. v. National Union*, 2014 U.S. Dist. LEXIS 140030 (S.D. Cal. 2014).

Distinguish between insurance company’s conduct, post litigation, in handling the claim from pleadings filed in court. *California Physicians Service v. Superior Court*, 9 Cal. App. 4<sup>th</sup> 1321 (1992) (allegedly false defensive pleading is protected by litigation privilege but may be used as evidence of prior bad faith).

## **VIOLATION OF FAIR CLAIMS SETTLEMENT PRACTICES REGULATIONS**

Evidence that insurance company violated these regulations is admissible to prove bad faith. *Jordan v. Allstate Ins. Co.*, 148 Cal. App. 4<sup>th</sup> 1062, 1076 (2007). Policyholder submitted declaration from expert in opposing summary judgment on bad faith.

### **STATUTE OF LIMITATIONS**

Four years for actions based on breach of contract and two years for actions based on tort. Breach of failure to settle may be pled in tort or contract. *Archdale v. American International Specialty Lines*, 154 Cal. App. 4<sup>th</sup> 449 (2007).

### **RECOVERY OF “BRANDT FEES” TO PROVE COVERAGE**

When the denial of coverage, or benefits, is unreasonable, the policyholder may recover fees and costs in proving coverage, but not fees incurred proving bad faith. *Brandt v. Superior Court*, 37 Cal. 3d 813 (1988). May be proved to a judge or jury. But a subtraction must be made for time spent pursuing bad faith. Keeping accurate time records is advisable. Problems arise when a case is handled on contingency basis and no time records are kept. See *Cassim v. Allstate Ins. Co.*, 33 Cal. 4<sup>th</sup> 780 (2004) for complicated calculations in this situation.

There is no specific allocation method for subtracting time spent in pursuing bad faith from time spent in pursuing coverage.

Attorneys' fees constitute an element of damages and must be placed in evidence before the trier of fact, before a verdict is rendered. The fees may be waived if not so presented. Otherwise, the parties must stipulate to let the judge award attorneys' fees after the jury verdict.

### **USE OF EXPERTS TO PROVE OR REFUTE BAD FAITH**

In virtually every bad faith case, both sides use experts. See, e.g., *Neal v. Farmers Insurance Exchange*, 21 Cal. 3d 910 924. In *Jordan v. Allstate Insurance Co*, 14 Cal. App. 4<sup>th</sup> 1062, 1076 (2007) the Court ruled that an expert's opinion that the insurance company violated the fair claims settlement practices regulations was properly admissible to show bad faith.