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**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA**

RICHARD HOWARD KELLY, an individual,

Plaintiff,

vs.
PROVIDENT LIFE AND ACCIDENT INSURANCE COMPANY, an insurance company; DOES 1-50,

Defendants.

CASE NO. 04cv807 WQH (BGS)
ORDER

HAYES, Judge:

The matter before the Court is Defendant Provident Life and Accident Insurance Company’s Motion for Summary Judgment. (Doc. # 106).

BACKGROUND

Plaintiff initiated this action relating to his own-occupation disability insurance policy with Defendant by filing his complaint on April 19, 2004. (Doc. # 1). Plaintiff alleged three claims: (1) rescission of an August 2001 settlement agreement ending prior litigation between the parties in this district; (2) breach of disability insurance contracts; and (3) breach of the implied covenant of good faith and fair dealing. *Id.* at ¶¶ 53-75. On August 13, 2004, this Court dismissed Plaintiff’s claims with prejudice, holding Plaintiff’s breach of contract and bad faith claims were barred by the statute of limitations and that Plaintiff’s rescission claim

1 failed to allege sufficient facts to establish undue influence pursuant to *Odorizzi v. Bloomfield*
2 *School Dist.*, 246 Cal. App. 2d 123, 130 (1966). (Doc. # 21 at 5-8). On October 16, 2007, the
3 United States Court of Appeals for the Ninth Circuit reversed this Court's decision in an
4 unpublished memorandum disposition, holding that the seven factors listed in *Odorizzi* were
5 not the only factors which could support a claim for rescission based on undue influence under
6 California law. (Doc. # 55 at 5). The Ninth Circuit also held that if Plaintiff could establish
7 that he is entitled to rescission, this Court should equitably toll the statute of limitations on
8 Plaintiff's breach of contract and bad faith claims. *Id.* at 7-8.

9 On remand, Defendant filed an answer (Doc. # 59) and the parties proceeded with
10 discovery. The Magistrate Judge bifurcated discovery into two phases. (Doc. # 93, 94). The
11 first phase was limited to discovery on the rescission claim. *See id.* Pursuant to the Magistrate
12 Judge's orders, if Plaintiff's rescission claim survives summary judgment, the parties will then
13 conduct the second phase discovery on Plaintiff's bad faith and breach of contract claim. *Id.*
14 On October 8, 2009, the Magistrate Judge ordered Defendant to produce its Rule 30(b)(6)
15 witness most knowledgeable about the underlying litigation for a second deposition because
16 the witness was unprepared to answer questions about the prior litigation and settlement at the
17 first deposition. (Doc. # 102). On November 4, 2009, Defendant objected to the order. (Doc.
18 # 103). On November 30, 2009, Defendant filed its pending Motion for Summary Judgment.
19 (Doc. # 106). On December 3, 2009, Plaintiff filed a Motion to Continue the Motion for
20 Summary Judgment pursuant to Federal Rule of Civil Procedure 56(f). (Doc. # 108). On
21 December 4, 2009, this Court ordered Plaintiff to respond to Defendant's objection to the
22 Magistrate Judge's order. (Doc. # 110). On February 2, 2010, the Court overruled
23 Defendant's objection and granted Plaintiff's Motion to Continue the Motion for Summary
24 Judgment. (Doc. # 122). The Court ordered Defendant to make its Rule 30(b)(6) witness
25 available for deposition before March 8, 2010 and set a briefing schedule for the Motion for
26 Summary Judgment. *Id.* at 9. On April 20, 2010, Plaintiff filed an Opposition to the Motion
27 for Summary Judgment. (Doc. # 143). Plaintiff also filed the Declaration of Plaintiff's
28 Counsel, Aaron Markowitz, which describes a dispute over bifurcated discovery and states that

1 Plaintiff seeks additional discovery concerning Defendant's adjusting practices because
2 Defendant reversed its earlier position that bad faith was irrelevant to rescission and argued
3 in support of its motion that it did not act in bad faith by terminating Plaintiff's benefits. (Doc.
4 # 143-5). On April 26, 2010, Defendant filed a Reply, objections to some of the evidence
5 Plaintiff submitted with his Opposition, and additional evidence in support of its motion.
6 (Doc. # 153). On April 30, 2010, Plaintiff filed a Supplemental Response to the motion,
7 objections to the evidence Defendant submitted with the Reply, and responses to Defendant's
8 objections. (Doc. # 155). On June 18, 2010, the Court held oral argument. *See* Doc. # 157.

9 **FACTS**

10 Defendant issued Plaintiff two own-occupation disability insurance policies in the early
11 1980s which provided a combined benefit of \$5,500 per month. (Undisputed Fact # 1, Doc.
12 # 143-7).¹ At the time he purchased the policies, Plaintiff sold insurance as a General Agent
13 for General American Life Insurance Company. Kelly Decl., Doc. # 143-4 at ¶ 7. Pursuant
14 to the disability policies, Plaintiff could claim total disability if he was unable "to perform the
15 substantial and material duties of his occupation" and was "under the care and attendance of
16 a Physician." Defendant's Ex. A, Doc. # 107-2 at 3; Defendant's Ex. B, Doc. # 107-2 at 18.
17 In May of 1986, Plaintiff began seeing psychologist Russell Gold, Ph.D., who diagnosed
18 Plaintiff with depression, dysthymic disorder, and schizoid personality disorder. (Undisputed
19 Fact # 10, Doc. # 143-7). Dr. Gold attributed Plaintiff's condition to stress from contentious
20 divorce proceedings. *Id.* Plaintiff filed a claim for complete disability in September of 1986.
21 (Kelly Decl., Doc. # 143-4 at ¶ 17). Defendant accepted the claim and began paying benefits.
22 *Id.* Plaintiff continued to see Dr. Gold for the thirteen-year period he received disability
23 benefits from Defendant. (Undisputed Fact # 10, Doc. # 143-7).

24 In addition to paying benefits of \$5,500 per month, in 1986 and 1987, Defendant paid
25 Plaintiff's business expenses, such as rent for his office, salaries of employees, utilities, and
26

27 ¹ The parties submitted separate statements of uncontroverted facts. The designation
28 "Undisputed Fact" means Plaintiff agreed in his separate statement that the fact is undisputed.
The citations for "Undisputed Facts" are to Plaintiff's separate statement, which is Doc. # 143-
7.

1 accounting services. Plaintiff's Ex. 101 at 737-42.

2 While Plaintiff was on disability benefits, various insurance companies terminated their
3 relationship with Plaintiff as an agent. In February of 1989, General American sent Plaintiff
4 two letters warning him that his production for 1988 was insufficient and that if he failed to
5 produce significantly higher commissions in 1989, his general agency would be terminated.
6 Plaintiff's Exs. 5-6 at 11-12.² General American again warned Plaintiff that he was in danger
7 of losing his general agency in April of 1990. Plaintiff's Ex. 14 at 30. In April of 1990, Aetna
8 sent Plaintiff a letter terminating Plaintiff's appointment as an agent because Plaintiff had
9 recently done "little or no business activity with the Aetna Life Insurance Company" In
10 November of 1992, General American "closed [Plaintiff's] General Agent contract . . .
11 effective November 30, 1992." Plaintiff's Ex. 25 at 184. After Plaintiff's general agency was
12 terminated, he could still write General American policies, but he had to go through the
13 General Agent for his local area. *Id.* In June of 1993, Jackson National Life informed Plaintiff
14 that it would "be unable to renew [Plaintiff's] contract due to inactivity for the past twelve
15 months." Plaintiff's Ex. 26 at 185. In October of 1994, Blue Shield of California terminated
16 Plaintiff's agency because Plaintiff failed to meet "minimum production requirements."
17 Plaintiff's Ex. 31 at 247.

18 Over the course of Plaintiff's disability claim, Defendant investigated Plaintiff's
19 medical condition and whether Plaintiff had returned to work on multiple occasions. In
20 February of 1990, Defendant stopped paying Plaintiff benefits for a six month period, stating
21 in a letter to Plaintiff's then attorney Harris Steinberg that Plaintiff failed to file his monthly
22 claim forms. Defendant's Ex. I, Doc. # 107-2 at 64. Defendant stated that it had "recently
23 learned information which, in our opinion, shows that not only is Mr. Kelly not totally disabled
24 but, in fact, doing quite well and working in his occupation as an insurance agent." *Id.* at 65.
25 Defendant stated it would resume payment of benefits "subject of course, to continued proof
26

27 ² Page citations for Plaintiff's Exhibits are to the consecutive pagination in the lower
28 right hand corner of the page, not to the CM/ECF pagination or the internal pagination of the
documents.

1 of disability.” *Id.* In response, Steinberg sent a letter which stated:

2 Mr. Kelly is not involved in any current work activities. As you know, Mr.
3 Kelly is the principal in an insurance agency and has kept the agency open for
4 purposes of collecting the renewal commissions which he is entitled to for work
5 done in previous years on behalf of several different insurance companies.
6 Additionally the office is being kept open as a result of lease obligations on
7 which Mr. Kelly has personal liability in addition to servicing the accounts of
8 his prior customers. . . .

6 Mr. Kelly has not returned to work. He did briefly attempt to resume some of
7 his duties in February of this year, but found himself frustrated, stressed, and
8 unable to resume his previous occupation and duties. . . . Mr. Kelly has, as a
9 courtesy to existing clients, serviced isolated insurance accounts which required
10 conversions of coverage from the term coverage to whole life coverage at the
11 insured’s request or in one or two instances [added] additional coverage [] to
12 existing policies

10 Mr. Kelly has advised me that Provident Life recently offered to pay him one-
11 year’s worth of disability benefits (60,000) to resolve his claim. Please be
12 advised that Mr. Kelly formally rejects this offer and wishes his benefits to
13 continue as promised under the policy on a “monthly” basis for the remainder
14 of his disability

13 Lastly, while you pursue your “investigation” of this claim, I must insist that all
14 monthly disability payments be made promptly and that all past monthly
15 disability payments be brought current forthwith.

15 Plaintiff’s Ex. 18 at 45. Enclosed with the letter, Steinberg sent over a hundred pages of
16 business records showing Plaintiff’s transactions during the disability period. *Id.* at 46-162.

17 In his declaration, Plaintiff states:

18 Early in my disability, when I was first contacted by an existing client to make
19 an adjustment to his insurance coverage, I contacted Provident at their local
20 office. I spoke to one of their representatives and explained the situation. I
21 explained that I was out on disability and was collecting benefits on an “own
22 occupation” disability policy. I asked if performing the limited work [of
23 modifying an existing client’s coverage, adding coverage, or switching to a new
24 insurance type] would disqualify me for continued benefits. I was told it was
25 not. . . . I have always been open and honest with Provident about the work I
26 was doing.

23 (Kelly Decl., Doc. # 143-4 at ¶¶ 21-22).

24 Defendant also contacted Dr. Gold, seeking additional information about Plaintiff’s
25 condition. Plaintiff’s Ex. 19. In the letter dated October 28, 1990, Defendant revealed it has
26 covertly videotaped Plaintiff’s activities “over a period of four (4) separate days between May
27 23, 1990 and June 28, 1990” and sought Dr. Gold’s explanation of “why [Plaintiff’s] activities
28 in the videotape make it appear that he leads a normal life and is not disabled.” *Id.* at 163-164.

1 The letter also requested a list of “objective symptoms” of Plaintiff’s psychological conditions.
2 *Id.* at 163. In a response dated February 6, 1991, Dr. Gold detailed the history of Plaintiff’s
3 case, described Plaintiff’s difficulties with interacting with other people, particularly face to
4 face, his social isolation, depression, excessive sleeping, abusive family background, and stress
5 from his divorce, and concluded that Plaintiff “cannot perform a significant number of the
6 usual and necessary responsibilities of an insurance agent.” *Id.* at 164-167. As to the
7 videotape, Dr. Gold stated he does not “believe anything in the videotape contradicts the
8 statements made herein.” *Id.* at 168. Dr. Gold notes Plaintiff “has always maintained the
9 capacity to perform errands and menial daily functions in order to live autonomously. Had he
10 ever not been able to function at this minimal level, he would have been hospitalized.” *Id.*

11 A report sent by the investigator to Defendant in June of 1990 shows that Plaintiff went
12 to his insurance office once during the four days of surveillance. Plaintiff’s Ex. 16 at 33-39.
13 It is not clear how long Plaintiff remained in his office, because ten minutes after Plaintiff
14 arrived at his office, Defendant instructed its private investigator “to terminate the
15 investigation at this time since it did appear Mr. Kelly was at work.” *Id.* at 37. Plaintiff was
16 also observed running errands and performing chores during the surveillance period. *Id.* at 39.

17 In August 1990, Defendant resumed payments after receiving the letter from Steinberg.
18 Kos³ Decl., Doc. 106-3 at ¶ 13. On December 11, 1990, Dr. Gold submitted a form to
19 Defendant which stated Plaintiff’s disability was “permanent and stationary.” (Undisputed
20 Fact # 16, Doc. # 143-7). On April 3, 1991, Defendant asked Plaintiff “to submit to an
21 Independent Medical Examination (“IME”) by Stephen Stahl, M.D., Ph.D., a psychiatrist who
22 was on the faculty of UCSD Medical School” and sought to send Plaintiff for psychological
23 testing. Kos Decl., Doc. # 106-3 at ¶ 15. Around the same time, Defendant offered to settle
24 the disability claim for \$200,000. *See* Plaintiff’s Ex. 21 at 172 (Letter from Defendant to
25 Steinberg dated April 22, 1991). Defendant rejected Plaintiff’s counteroffer of \$431,000. *Id.*
26 On June 7, 1991, Steinberg sent a letter to Defendant asserting further examination of Plaintiff

27
28 ³ John Kos is Defendant’s Director of Long Term Disability. *Id.* at ¶ 2.

1 would damage his psychological health and was unnecessary. Plaintiff's Ex. 22 at 174.
2 However, Plaintiff did submit to the psychological testing on August 14, 1991, and the results
3 were forwarded to Dr. Stahl on September 11, 1991. Kos Decl., Doc. # 106-3 at ¶ 16;
4 Defendant's Ex. K, Doc. # 107-2 at 76. Dr. Stahl also examined Plaintiff. Defendant's Ex.
5 K, Doc. # 107-2 at 76-77.

6 Dr. Stahl's report concluded Plaintiff was suffering from dysthymia, or low-grade
7 depression, as well as "mixed personality disorder with schizoid and passive aggressive
8 features" at the time of the examination and that Plaintiff had previously experienced a major
9 depressive episode brought on by his divorce which was then in remission. *Id.* Dr. Stahl
10 concluded Plaintiff was

11 temporarily totally disabled at the very least from November of 1990 until the
12 time of my final evaluation on September 25, 1991. Dating the exact onset of
13 his temporary total disability is difficult because of the impossibility of getting
14 reliable information from Mr. Kelly. In the absence of better information, I
15 would tend to rely on Dr. Gold's assessment and date the onset of total disability
16 to be 1986, when Mr. Kelly stopped working. Dating the recovery of total
disability with return to the baseline state of partial long standing disability is
clearer. Mr. Kelly was already recovering notably from his major depression at
the time of his first interview with me in May, 1991, but was still temporarily
totally disabled. By the time of his final interview, Mr. Kelly was no longer
totally disabled.

17 Mr. Kelly is currently able to perform the substantial and material duties of his
18 usual occupation. However, he has no interest in doing so. In fact, hearing this
19 opinion that he is able to work again will undoubtedly anger Mr. Kelly and
20 could precipitate various hostile acts towards various parties including himself.
21 Mr. Kelly has made vague references to shooting himself if he does not get his
22 own way, which is to continue totally disabled indefinitely. Such implicit
23 threats, however, do not change the objective assessment of temporary total
24 disability, which are from 1986 to September 1991.

21 *Id.* at 76-78.

22 Despite this finding, Defendant continued to pay benefits. Kos. Decl. Doc. # 106-3 at
23 ¶ 17. Kos states in his declaration that this was because Defendant learned that "Dr. Stahl had
24 once been investigated . . . for an alleged impropriety in connection with a professional
25 publication, Provident chose to forego any action based on Dr. Stahl's IME report. Again,
26 given the potential for questions regarding Dr. Stahl's credibility, Provident chose to give
27 Kelly the benefit of the doubt." *Id.*

28 In February of 1995, Provident informed Plaintiff that it had "recently completed a

1 comprehensive review of your claim and have determined that it will only be necessary for you
2 and your Attending Physician to complete an ‘Insured’s Supplementary Statement of Claim’
3 form 4 times per year.” Plaintiff’s Ex. 36 at 280. In 1997, however, “Provident . . . began
4 another investigation.” Kelly Decl., Doc. # 143-4 at ¶ 40. Kos states the investigation
5 revealed Kelly was still licensed to sell insurance and that he had income “for all but two years
6 during the period from 1986 to 1996.” Kos Decl., Doc. # 106-3 at ¶ 20-21. In May of 1997,
7 Defendant also had a second IME with Dr. Alan S. Bergsma, M.D., a psychiatrist and
8 additional psychological testing. *Id.* at 22; Defendant’s Ex. P, Doc. # 107-2 at 103.

9 In his report dated May 27, 1997, Dr. Bergsma concluded that Plaintiff was suffering
10 from Dysthymic disorder and a “mixed character disorder with schizoid features.”
11 Defendant’s Ex. P, Doc. # 107-2 at 118. Dr. Bergsma concluded that Plaintiff had previously
12 suffered from a major depressive episode from 1986 through 1991 which was in remission at
13 the time of the examination. *Id.* Dr. Bergsma states that the “diagnosis of personality disorder
14 refers to a chronic pattern of behaviors which interfere with his ability to function socially and
15 interpersonally [which] also affect his occupational behavior.” *Id.* Dr. Bergsma concluded
16 that Plaintiff’s

17 mood disorder does not intrude into his life any more than it did when he was
18 employed as an insurance salesman. Similarly, his personality disorder with all
19 of its difficulties is a baseline pattern of functioning which has been present
20 throughout his adult lifetime. There is no more reason to believe that it now
21 would preclude him from functioning in his occupation of insurance salesman
22 than it did in the past. . . .

23 Returning to work as an insurance person would be difficult for Mr. Kelly now,
24 just as it was in the past. He was always more task than people-oriented. His
25 disability benefits enable him to avoid interpersonal stresses to a large degree.

26 *Id.* at 118-120. The report does not state the standard Dr. Bergsma used for determining
27 whether Plaintiff was totally disabled. *Id.* Defendant continued to pay benefits after receiving
28 this report. *See* Defendant’s Ex. X, Doc. # 107-3 at 82.

29 In July of 1997, Defendant sent a field investigator, Lorenz E. Blochl, to Plaintiff’s
30 residence. *See* Defendant’s Ex. R, Doc. # 107-3 at 1; Kelly Decl., Doc. # 143-4 at ¶ 40.
31 Plaintiff refused to allow the investigator into his house and gave very short answers to

1 questions. *Id.* The investigator’s report commented on Blochl’s estimate of the price of
2 Plaintiff’s home (\$600,000-\$700,000), the landscaping, pool, and the make of a car in
3 Plaintiff’s garage (a Mercedes). Defendant’s Ex. R, Doc. # 107-3 at 2.⁴ The report also noted
4 that assets, including the house, cars, and Wobegone Enterprises, a company Plaintiff founded,
5 were held in Plaintiff’s wife Anna’s name, not his own name. *Id.* Blochl interviewed
6 Plaintiff’s ex-wife Wanda, who stated Plaintiff threatened to go on disability if she filed for
7 divorce, that Plaintiff abused her, that Plaintiff went to Europe with another woman while on
8 disability, and that Plaintiff faked his depression. Defendant’s Ex. T, Doc. # 107-3, 8-9.

9 Defendant also obtained business records from Plaintiff’s former employer, General
10 American Life Insurance Company, which had allowed him to continue writing policies after
11 terminating his general agency in 1992. Defendant’s Ex. U, Doc. # 107-3 at 10-11. The
12 records provided by General American showed total commissions by Plaintiff’s company,
13 Kelly Insurance Services, which changed its name to Wobegone Enterprises in 1997, ranging
14 from approximately \$88,000 to \$185,000 per year from 1991 through 1998. *Id.* at 159. Kos
15 states these records “confirmed for the first time that Kelly was working, and receiving income
16 from activities other than mere ‘renewals’ and ‘sporadic courtesy services’ during the entire
17 period of his claimed disability.” Kos Decl. Doc. # 106-3 at ¶ 31. The records do not state
18 how many transactions Kelly performed in these years or how these sales compare to other
19 agents. A letter from General American in 1994 informs Plaintiff that as of October, Plaintiff
20 had only met 2.8% of his yearly sales goals. Plaintiff’s Ex. 32 at 248; Kelly Decl., Doc. # 143-
21 4 at ¶ 38. Plaintiff states that over the course of the thirteen year period he received benefits,
22 he sold 54 policies to 19 clients, “all but two [of whom] were clients that I had prior to going
23 on disability.” Kelly Decl., Doc. # 143-4 at ¶ 48. Plaintiff states “more than three-quarters of
24 the first year commission income that I earned between 1991 and 1998 came from only one
25 client, which was a client I had before my disability.” *Id.* After Plaintiff’s general agency
26 with General American was terminated in 1992 because of poor sales performance, he was

27
28 ⁴ Citation is to the CM/ECF page number, not the internal pagination. (For the first 148
pages of exhibits, these numbers match.)

1 assigned to the general agent for his geographical area, Thomas Gore. Kelly Decl., Doc. #
2 143-4 at ¶ 37. All of Plaintiff's work after 1992 went through Gore's office. *Id.* Defendant
3 also sent an inquiry to Gore, who stated in response that although he had a business
4 relationship with Plaintiff for "7-8 years," he had "never met [Plaintiff] personally. We've
5 only spoken by phone." Plaintiff's Ex. 71 at 399. Gore stated Plaintiff was generating "3-5
6 policy sales [per year]. Virtually all are repeat sales to existing customers." *Id.* at 400. Gore
7 stated he spoke to Plaintiff "[p]erhaps 10-12 times per year." *Id.* Defendant received that
8 letter on February 4, 1999. *Id.*

9 In early 1999, Defendant also contacted other insurance companies which had
10 relationships with Plaintiff prior to his disability claim. CPIC Life Insurance Company
11 responded to Defendant's inquiries by stating Plaintiff and Wobegone Enterprises were on
12 "Inactive Status," and that Plaintiff had not submitted any new business or earned any
13 commissions since 1991. Plaintiff's Ex. 70 at 381-82. Safeco Life Insurance Company
14 informed Defendant that Plaintiff and Wobegone were on inactive status and that Plaintiff's
15 agency had been cancelled in April of 1993. *Id.* at 383. In response to a similar inquiry,
16 Executive Life Insurance informed Defendant that it had no record on file of Plaintiff and did
17 not do any business with him. *Id.* at 385. Guarantee Life Insurance also could not find any
18 record of Plaintiff as an agent and stated that although Wobegone was an agent, "we also have
19 no indication (on our records) that Wobegone Enterprises continues to be active with us." *Id.*
20 at 388-89. Massachusetts Casualty informed Defendant that Plaintiff had been on inactive
21 status since January of 1985 and that it had never done business with Wobegone. *Id.* at 390.
22 Chubb Sovereign Life Insurance stated it had terminated Plaintiff as an agent in 1995 and had
23 not done business with Wobegone. *Id.* at 391.

24 Defendant did not contact Plaintiff's wife to determine her involvement in Wobegone
25 Enterprises. In a declaration, Plaintiff's wife Anna Kelly states:

26 Shortly after we were married [in 1991], Richard gave me his company. . . .
27 Since 1991, Richard's association with [the company] has been very limited due
28 to Richard's disability. . . . Prior to me obtaining my insurance license [in 2001],
Richard maintained his license so that we could sell insurance to some of
Richard's old clients, and occasionally to an acquaintance of mine.

1 Decl. of Anna Kelly, Doc. # 143-1 at ¶¶ 2-5.

2 During the investigation, Blochl contacted the San Diego District Attorney's Office, the
3 United States' Attorney's Office, and the FBI to report insurance fraud. Plaintiff's Ex. 67 at
4 371; Plaintiff's Ex. 68 at 375; Plaintiff's Ex. 75 at 420. A deputy district attorney informed
5 Blochl that "Mr. Kelly should be asked if he in fact has sold policies after his date of disability
6 and whether or not he has an office. Very specific questions about sales, marketing, and
7 prospecting should be asked" and warned Blochl that "the questions on the Insured's
8 Supplementary Statement of Claim form were vague." Plaintiff's Ex. 68 at 375. Defendants
9 never asked Plaintiff these questions. The deputy district attorney also "suggested that the
10 Insured should be examined under oath by Provident attorneys regarding this claim. She
11 indicated that very specific questions about the insured[']s alleged disability and possible
12 insurance related activity should be explored." *Id.* at 376. Defendant never conducted such
13 an interview. In his deposition, Blochl testified that when he investigated Plaintiff and
14 contacted various law enforcement agencies, he was unaware that Plaintiff had ever informed
15 Defendant that he was continuing to provide some services to existing clients, that he was
16 unaware that Plaintiff's attorney had provided Plaintiff's business records to Defendant in
17 1990, and that he was unaware that Plaintiff had informed Defendant that Plaintiff had initiated
18 some new policies. Blochl Depo., Plaintiff's Ex. 121 at 994-996. Blochl testified in his
19 deposition that this information would have affected his determination of whether fraud had
20 been committed and that this information was the reason the FBI declined to pursue the case
21 after a preliminary investigation. *Id.* at 1000.⁵

22 On March 9, 1999, Defendant informed Plaintiff that it was sending him for another
23 IME. Plaintiff's Ex. 72 at 403. On April 16, 1999, Dr. Alan Abrams, M.D., J.D., examined
24 Plaintiff. Kos Decl., Doc. # 106-3 at ¶ 33. Dr. Abrams' report states he was asked to address
25 twelve questions provided to him by Defendant, and quotes the questions provided as follows:

26
27 ⁵ Although Plaintiff was never charged criminally in connection with the alleged
28 insurance fraud, he was convicted of tax evasion in 2004. (Undisputed Fact # 66, Doc. # 143-7).

1 “1. Do you believe the insured is making a choice not to return to work, or does
2 a psychiatric impairment prevent the insured from doing so? 2. What psychiatric
3 impairment exists that would prevent the insured from returning to work in
4 insurance sales? 3. Please identify occupation specific restrictions, limitations,
5 and/or skill deficits resulting from the identified psychiatric impairment [?]
6 4. Would these restrictions, limitations, and/or skill deficits manifest irrespective
7 of the particular setting of the insured’s occupation? If not, in what settings
8 could the insured perform his occupation? 5. Are there significant physical
9 complications to the insured’s condition? . . . 6. Are there restrictions,
10 limitations, and/or skill deficits resulting solely from the insured’s physical
11 condition that predominate those related to psychiatric impairment? 7. Do you
12 believe the insured is receiving care that is appropriate and adequate for the
13 condition causing the psychiatric condition? . . . 8. What is the prognosis under
14 [adequate] care, for the insured to return to work full-time? Part-time? . . . 11.
15 Are the clinical elements of the claim predominantly those of prevention and
16 risk of recurrence or of a present psychiatric impairment? . . .”

17 Defendant’s Ex. W, Doc. 107-3 at 17. Dr. Abrams concluded that Plaintiff has Narcissistic
18 Personality Disorder with “additional features of other personality disorders.” *Id.* Dr. Abrams
19 concluded that “[n]either Mr. Kelly’s limited capacity for empathy or deeper human
20 relationship, nor other aspects of his personality disorders, are work disabling.” *Id.* Dr.
21 Abrams did not state what standard he used to measure whether Plaintiff was disabled. Dr.
22 Abrams based his diagnosis in part on

23 other documents that strongly suggest that Mr. Kelly is both selling insurance
24 policies, and running an insurance agency, and has been doing that throughout
25 the period of disability, beginning in 1991. It appears he might have been
26 funneling income from Richard Kelly Insurance, Inc. [sic] through his present
27 wife, Anna, to avoid reporting this income to Family Court. If these documents
28 in fact demonstrate that Mr. Kelly is working, this would confirm the conclusion
of the two prior IME’s that Mr. Kelly has not been disabled since at least 1991.

Id. at 18. Dr. Abrams stated “I do not find evidence that Mr. Kelly was ever disabled by a
mental illness, during the entire period of claimed disability” and that “[n]on-clinical elements,
i.e. malingering, completely dominate the claim.” *Id.* at 78, 81.

On August 18, 1999, Defendant sent Plaintiff a letter notifying him that it was
terminating his benefits, although it would provide him with benefits through August 16, 1999,
which was the date it concluded Plaintiff was not disabled. Defendant’s Ex. X, Doc. # 107-3
at 82. The letter informed Plaintiff that he was required to pay his premiums in order to
continue coverage under his policies. *Id.* Plaintiff sent a series of letters to Defendant after
the termination and Dr. Gold also wrote to Defendant on Plaintiff’s behalf. Kelly Decl., Doc.
143-4 at ¶ 49. In April of 2000, Defendant stated it was reviewing Plaintiff’s submissions

1 and would get back to him. Plaintiff's Ex. 83 at 447. However, Defendant never responded.
2 Kelly Decl., Doc. # 143-4 at ¶ 49.

3 In November of 2000, Plaintiff was served with process in *Provident Life and Accident*
4 *Insurance Co. v. Kelly*, No. 00cv2169 H (JFS), the prior litigation before this Court. *Id.* at 50;
5 *see also* Compl., *Provident Life and Accident Insurance Co. v. Kelly*, No. 00cv2169 H (JFS)
6 (S.D.C.A. Oct. 25, 2000), Defendant's Ex. CC, Doc. # 107-4 at 16. Defendant Provident, as
7 a plaintiff in that suit, alleged claims for fraud, conspiracy to defraud, breach of the covenant
8 of good faith and fair dealing, rescission, and restitution against Kelly. *Id.* Defendant
9 Provident also sued Kelly Insurance Services, Inc. and Wobegone Enterprises, Inc., alleging
10 a cause of action for conspiracy to defraud. *Id.*

11 Plaintiff attempted to retain his former attorney, Steinberg, to represent him and the
12 companies, however, Steinberg told Plaintiff that he did not handle defense cases and advised
13 Plaintiff to hire another attorney. Kelly Decl., Doc. # 143-4 at ¶ 51. Plaintiff attempted to hire
14 an attorney, but could not afford the fees and could not find an attorney who would take his
15 case on a contingency basis because he was a defendant. *Id.* Plaintiff contacted Defendant,
16 seeking a settlement, because Defendant had previously offered Plaintiff \$330,000 to surrender
17 the policies. *Id.* at 52. Defendant's attorney, Gregory Scarlett, told Plaintiff that he would put
18 the lawsuit on hold while he looked into a settlement. *Id.*

19 On April 11, 2001, Plaintiff learned that a clerk's default had been entered against him
20 and the companies and that Defendant was moving for default judgment. *Id.* at 52. Plaintiff,
21 proceeding *pro se*, wrote a letter to Judge Huff explaining that he had not responded to the
22 lawsuit because of his conversation with Defendant's attorney. *Id.* at 53; Defendant's Ex.DD,
23 Doc. # 107-4 at 90. Plaintiff stated he believed the litigation was on hold. *Id.* In the letter,
24 Plaintiff also stated that he did not own either of the corporate defendants, rather his wife Anna
25 did. Defendant's Ex. DD, Doc. # 107-4 at 91. At this time, Plaintiff was still under
26 investigation by the FBI, which he found "tremendously upsetting" Kelly Decl., Doc. #
27 143-4 at ¶ 54. Plaintiff did not understand how he could be accused of fraud because
28 "Provident never asked for any additional information" about his "limited work" after

1 Steinberg sent Defendant his work records in 1990. *Id.* at ¶ 55. Plaintiff states “I did not
2 understand how I could lie about something I was never asked about.” *Id.*

3 Because Plaintiff was not an attorney, he could not file an answer or oppose default
4 judgment on behalf of the corporate defendants, and Defendant obtained a default judgment.
5 *Id.* at ¶ 56. Although Plaintiff’s wife, not Plaintiff, was the registered agent for service of
6 process, she was never served. Decl. of Anna Kelly, Doc. 143-1 at ¶ 5. Plaintiff’s wife states
7 in a declaration that the default judgment

8 put a tremendous financial strain on Richard and I. With Richard unable to work,
9 I needed to make money to support us both. I counted on the income from my
10 insurance sales, including the residual commissions flowing through Wobegone,
in order to make ends meet. When Provident entered default against my
company, it took away this source of income entirely.

11 *Id.* at ¶ 8. After the default judgment, Plaintiff began drinking heavily. Kelly Decl., Doc.
12 # 143-4 at ¶ 58. Plaintiff’s wife states that his condition worsened after Defendant cut off
13 Plaintiff’s disability benefits and during the lawsuit and that at one point, she discovered he
14 had been researching suicide. Anna Kelly Decl., Doc. # 143-1 at ¶ 7. On July 2, 2001 and July
15 5, 2001, Plaintiff and Defendant’s attorney attended an early neutral evaluation conference
16 before the magistrate judge. (Undisputed Fact # 55, Doc. # 143-7). Plaintiff settled his case
17 with Defendant, giving up his claim for disability benefits in exchange for Defendant agreeing
18 to dismiss the lawsuit and “giving up its judgment against Anna’s company.” Kelly Decl., Doc.
19 # 143-4 at ¶¶ 60-62. The settlement agreement was signed by both parties on November 21,
20 2001. (Undisputed Fact # 61, Doc. # 143-7). Plaintiff states he signed the settlement
21 agreement “because I did not have the mental or emotional capacity to engage in the
22 conflictual situation that Provident had created. I did not sign the agreement because it was
23 what I wanted to do, but because I could not resist Provident’s pressure.” Kelly Decl., Doc.
24 # 143-4 at ¶ 62.

25 Plaintiff submitted the declaration of Dr. Lynn Ponton, M.D., a Professor of Clinical
26 Psychiatry at the University of California, San Francisco, who reviewed Plaintiff’s medical
27 records and the records of the three IMEs with Defendant’s selected doctors. Ponton Decl.,
28 Doc. # 143-3 at ¶¶ 1, 7. Based on her review of the records, Dr. Ponton offers her opinion that

1 Plaintiff suffers from Avoidant Personality Disorder with schizoid features. *Id.* at ¶ 9. Dr.
2 Ponton states “Avoidant Personality Disorder is often characterized by shifts in the level of
3 avoidant behavior depending on the level of conflict associated with certain interpersonal
4 relationships. *Id.* at ¶ 12. Dr. Ponton states that Plaintiff’s condition creates “undue
5 susceptibility to [] pressure,” such as the pressure that Defendant’s investigations, the prior
6 lawsuit, and the investigations of alleged insurance fraud by various law enforcement agencies
7 would create. *Id.* at ¶ 48. Under this pressure, given Plaintiff’s diagnosis, “[h]is depression
8 and social avoidance would have been at an all-time high” at the time of the settlement. *Id.* at
9 ¶ 56.

10 Dr. Ponton also criticizes the three IME evaluations performed at Defendant’s request.
11 *Id.* at ¶¶ 63-65. Dr. Ponton opines that the September 27, 1991 report by Dr. Stahl is deficient
12 in that it finds

13 that Richard is no longer disabled after September 25, 1991, but provides no
14 analysis of the substantial and material duties of Richard’s occupation as an
15 insurance broker/general agent for General American – which includes extensive
marketing and solicitation of new business – or why Dr. Stahl believes that
Richard can engage in those activities on a reasonably continuous basis.

16 *Id.* at ¶ 63.

17 As to Dr. Bergsma’s 1997 conclusions, Dr. Ponton opines

18 I believe the more accurate diagnosis is Avoidant Personality Disorder with
19 schizoid features. . . . [G]iven this more accurate diagnosis, I am critical of Dr.
20 Bergsma’s opinion that Richard is not totally disabled from performing the
21 substantial and material duties of his former occupation as an insurance agent
22 because he is at his affective baseline. Due to the stress created by interpersonal
difficulties, and the effect the stress has on Richard’s dysthymic disorder –
leading to episodes of major depression – Richard’s emotional state varies based
on stress and conflict

23 and would worsen if Plaintiff returned to work. *Id.* at ¶ 64.

24 Dr. Ponton criticizes Dr. Abrams’s 1999 conclusions as well, noting Dr. Abrams used
25 an outdated test which had been performed on Plaintiff in 1986 rather than more recent
26 psychological testing performed in 1991. *Id.* at 65. Dr. Ponton notes that Dr. Abrams
27 requested this testing from Defendant, but Defendant never provided it. *Id.* Dr. Ponton opines
28 that Dr. Abrams’s conclusion that Plaintiff was malingering was linked to his opinion that

1 Plaintiff has Narcissistic Personality Disorder, which in turn was based on flawed methodology
2 and limited information. *Id.* Dr. Ponton notes that “Dr. Abrams seems to have completely
3 ignored the valid results of the 1997 Millon Clinical Multiaxial Inventory-III (MCMI-III)” in
4 which “Richard scored on the very low end for narcissistic personality pattern” *Id.* Dr.
5 Ponton opines this score “negates the diagnosis that Richard is suffering from narcissistic
6 personality disorder causing him to malingering.” *Id.* Dr. Ponton notes the same test supports her
7 conclusion that Plaintiff has Avoidant Personality Disorder based on other subscores. *Id.*
8 Further, Dr. Ponton opines that Dr. Abrams’s diagnosis “is centered on the presumption that
9 Richard is deceitful” and that Plaintiff had lied to Defendant about his work activities. *Id.* Dr.
10 Ponton continues

11 [t]he letter from Harris Steinberg [which informs Defendant about Plaintiff’s
12 work activities] is conspicuously missing from the list of documents that
13 Provident provided to Dr. Abrams. . . . Moreover, Dr. Abrams specifically asks
Provident for additional information, including “Records from the General
American Life Insurance Company covering 1986 to 1991”

14 which Defendant failed to provide. *Id.*

15 LEGAL STANDARD

16 Summary judgment is appropriate under Rule 56 of the Federal Rules of Civil
17 Procedure where the moving party demonstrates the absence of a genuine issue of material fact
18 and entitlement to judgment as a matter of law. Fed. R. Civ. P. 56(c); *see also Celotex Corp.*
19 *v. Catrett*, 477 U.S. 317, 322 (1986). A fact is material when, under the governing substantive
20 law, it could affect the outcome of the case. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242,
21 248 (1986). A dispute over a material fact is genuine if “the evidence is such that a reasonable
22 jury could return a verdict for the nonmoving party.” *Id.*

23 “When the party moving for summary judgment would bear the burden of proof at trial,
24 it must come forward with evidence which would entitle it to a directed verdict if the evidence
25 went uncontroverted at trial. In such a case, the moving party has the initial burden of
26 establishing the absence of a genuine issue of fact on each issue material to its case.” *Miller*
27 *v. Glenn Miller Prods., Inc.*, 454 F.3d 975, 987 (9th Cir. 2006) (quotation omitted). “Once the
28 moving party comes forward with sufficient evidence, the burden then moves to the opposing

1 party, who must present significant probative evidence tending to support its claim or defense.”
2 *C.A.R. Transp. Brokerage Co., Inc. v. Darden Rests., Inc.*, 213 F.3d 474, 480 (9th Cir. 2000)
3 (citation omitted).

4 “In ruling on a motion for summary judgment, the nonmoving party’s evidence is to be
5 believed, and all justifiable inferences are to be drawn in that party’s favor.” *Hunt v.*
6 *Cromartie*, 526 U.S. 541, 552 (1999) (quotation omitted); *see also DiRuzza v. County of*
7 *Tehama*, 206 F.3d 1304, 1314 (9th Cir. 2000) (“For purposes of summary judgment . . . , we
8 must presume the facts to be those most favorable to the non-moving party.”); *Leslie v. Grupo*
9 *ICA*, 198 F.3d 1152, 1159 (9th Cir. 1999) (The nonmoving party’s declaration or sworn
10 testimony “is to be accepted as true [The non-movant’s] evidence should not be weighed
11 against the evidence of the [movant].”). At the summary judgment stage, “[c]redibility
12 determinations, the weighing of the evidence, and the drawing of legitimate inferences from
13 the facts are jury functions, not those of a judge.” *Anderson*, 477 U.S. at 255; *see also*
14 *Dominguez-Curry v. Nevada Transp. Dep’t*, 424 F.3d 1027, 1035-36 (9th Cir. 2005) (“The
15 district court ... improperly dismissed Dominguez’s allegations as consisting of nothing more
16 than ‘self-serving statements in her own deposition and affidavit.’ Such observations go to
17 whether Dominguez is credible, a determination that is exclusively within the province of the
18 factfinder at trial, not the district court on summary judgment”). “But the non-moving
19 party must come forward with more than the mere existence of a scintilla of evidence. Thus,
20 ‘where the record taken as a whole could not lead a rational trier of fact to find for the
21 nonmoving party, there is no genuine issue for trial.’” *Miller*, 454 F.3d at 988 (quoting
22 *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986)). “Simply
23 because the facts are undisputed does not make summary judgment appropriate. Instead,
24 where divergent ultimate inferences may reasonably be drawn from the undisputed facts,
25 summary judgment is improper.” *Id.* (citation omitted).

26 ANALYSIS

27 I. Rescission of the Settlement Agreement

28 Defendant contends that the settlement agreement and general release is binding and

1 cannot be rescinded because there was no fraud, duress, or undue influence. (Doc. # 106-1 at
2 21-22). Defendant contends Plaintiff cannot establish undue influence because there is no
3 fiduciary relationship between an insurance company and an insured. *Id.* at 22. Defendant
4 contends that Kelly cannot establish undue influence because “there is no evidence that
5 Provident’s counsel engaged in any specific coercive behavior during the settlement
6 negotiations.” *Id.* at 23. Defendant contends that the settlement agreements “spanned several
7 months,” allowing Plaintiff to review the documents thoroughly, think over the decision, and
8 to consult with an attorney if he so chose. *Id.* Defendant contends that Kelly initially raised
9 the issue of settling the case in a letter sent to Judge Huff on May 10, 2001. *Id.* at 24.
10 Defendant contends that there is no evidence of duress based on mental incompetence because
11 Plaintiff is not incompetent. *Id.* at 25. Defendant contends there is no evidence of economic
12 duress because Plaintiff “continued generating hundreds of thousands of dollars in insurance
13 commissions.” *Id.* Defendant contends any bad faith in terminating Plaintiff’s benefits and
14 suing him cannot be the basis for rescission, “[o]therwise, it would never be possible to achieve
15 finality in the settlement of a case where bad faith is alleged.” *Id.* at 26.

16 Plaintiff contends that there is a genuine issue of material fact as to whether Plaintiff’s
17 agreement to settle the prior litigation was obtained by undue influence or duress. (Doc. # 143
18 at 14-16). Plaintiff contends that a bad faith threat to breach a contract or withhold a payment
19 can be the basis for rescinding a contract due to economic duress. *Id.* at 15. Plaintiff contends
20 that Defendant’s decision to terminate benefits and sue Plaintiff and Plaintiff’s wife’s business
21 was made in bad faith. *Id.* at 16. Plaintiff contends there was no legal basis for naming
22 Plaintiff’s wife’s company as a defendant in the original lawsuit. *Id.* Plaintiff contends that
23 terminating his benefits and initiating the lawsuit in bad faith constitutes taking unfair
24 advantage of Plaintiff’s mental illness. *Id.* Plaintiff contends that he was unduly susceptible
25 to pressure from Defendant to settle because of his mental illness and because he was
26 dependent on his disability benefits. *Id.* at 19-23. Plaintiff contends Defendant’s bad-faith
27 refusal to pay his benefits, coupled with his undue susceptibility, resulted in undue influence.
28 *Id.* Plaintiff contends that a reasonable jury could find that the settlement agreement should

1 therefore be rescinded. *Id.* at 24. Plaintiff contends that there is a genuine issue of material
2 fact as to whether a confidential relationship existed between Plaintiff and Defendant as a
3 result of Defendant's access to private information about Plaintiff, Plaintiff's reliance on the
4 policy payments, and Plaintiff's weakness of mind. *Id.* Plaintiff contends that Defendant took
5 advantage of their confidential relationship by suing Plaintiff, knowing that Plaintiff was
6 unable to defend himself against the suit due to his mental health problems. *Id.* at 25. Plaintiff
7 contends a jury could find that the agreement should be rescinded on this basis. *Id.*

8 In its Reply, Defendant contends the Court should not credit Plaintiff's sworn statement
9 that Defendant was aware that Plaintiff continued to do limited insurance sales because
10 "[g]iven [Plaintiff's] conviction of a felony involving honesty, his credibility is in issue."
11 (Doc. # 153 at 2). Defendant contends that Plaintiff "does not explain whether his reduced
12 sales activity was simply a choice he made to reduce his work level in order to receive
13 non-taxable disability benefits while continuing to receive substantial income in the form of
14 hidden insurance commissions." *Id.* at 3. Defendant contends Plaintiff falsely reported his
15 income during his divorce proceedings. *Id.* Defendant contends Plaintiff relies on evidence
16 of wrongdoing by Defendant in other cases related to other insureds with no evidence that
17 Defendant used the same practices in Plaintiff's case. *Id.* Defendant contends that Plaintiff's
18 statement that he was distraught and contemplated suicide after receiving the letter denying
19 further benefits in August of 1999 "is at odds with [his] admission that he took trips to Europe
20 in January 2000 and again in September 2000." *Id.* at 5. Defendant contends there is no
21 evidence that it sued Plaintiff to force him to give up his policies. *Id.* Defendant contends
22 Plaintiff "does not explain whether" he transferred his interest in his business to his wife in
23 order "to conceal income generated by Wobegone from his former wife Wanda, from
24 Provident, and from the IRS." *Id.* at 6.

25 Pursuant to California Civil Code § 1575,

26 Undue influence consists:

- 27 1. In the use, by one in whom a confidence is reposed by another, or who holds
28 a real or apparent authority over him, of such confidence or authority for the
purpose of obtaining an unfair advantage over him;
2. In taking an unfair advantage of another's weakness of mind; or,
3. In taking a grossly oppressive and unfair advantage of another's necessities

1 or distress.

2 A seminal California appellate case defined undue influence as follows:

3 [u]ndue influence . . . is a shorthand legal phrase used to describe
4 persuasion which tends to be coercive in nature, persuasion which
5 overcomes the will without convincing the judgment. The hallmarks of
6 such persuasion is high pressure, a pressure which works on mental,
moral, or emotional weakness to such an extent that it approaches the
boundaries of coercion. In this sense, undue influence has been called
overpersuasion.”

7 *Odorizzi*, 246 Cal. App. 2d at 130. If the party seeking to rescind a contract is a “person of
8 subnormal capacities,” even subjecting them to “ordinary force” may constitute undue
9 influence. *Id.* at 132.

10 *Odorizzi* lists seven factors which “generally accompany” overpersuasion:

11 (1) discussion of the transaction at an unusual or inappropriate time, (2)
12 consummation of the transaction in an unusual place, (3) insistent demand that
13 the business be finished at once, (4) extreme emphasis on untoward
14 consequences of delay, (5) the use of multiple persuaders by the dominant side
15 against a single servient party, (6) absence of third-party advisers to the servient
16 party, (7) statements that there is no time to consult financial advisers or
17 attorneys. If a number of these elements are simultaneously present, the
18 persuasion may be characterized as excessive.

19 *Id.* at 133. Although *Odorizzi* states these factors are generally present, the Ninth Circuit’s
20 previous ruling in this case states “[t]he *Odorizzi* list was not described as exhaustive. Some
21 contracts might be formed through undue influence even if most or all of the *Odorizzi* factors
22 are absent.” (Doc. # 55 at 5). In *Keithley v. Civil Service Bd. of the City of Oakland*, 11 Cal.
23 App. 3d 443, 451 (1970), a California Court of Appeals made the same point: “[i]ndeed, there
24 are no fixed definitions or inflexible formulas. Rather, we are concerned with whether from
25 the entire context it appears that one’s will was overborne and he was induced to do or forbear
26 to do an act which he would not do, or would do, if left to act freely.” The same opinion notes
27 “direct evidence of undue influence is rarely obtainable and, thus the court is normally
28 relegated to determination by inference from the totality of facts and circumstances.” *Id.*

At least one California appellate decision addresses mental illness as a form of
“weakness of the mind.” See *Smalley v. Baker*, 262 Cal. App. 2d 824, 834 (1968). In *Smalley*,
the court held that a manic depressive man was competent to enter a contract, but that his
mental illness was a “weakness of the mind” pursuant to California Civil Code § 1575 (2)

1 because his “judgment was affected.” *Id.* at 836. The court explained that “the lesser
2 weakness of the mind [which does not render a party incompetent] referred to in section 1575
3 need not be long lasting or wholly incapacitating, but may consist of such factors as a lack of
4 vigor due to age, physical condition, emotional anguish, or a combination of such factors.” *Id.*
5 at 835. However, Smalley ultimately lost because there was “no claim or showing that Baker
6 knew or was aware of Smalley’s mental illness, or that he took advantage of such illness so as
7 to bring Civil Code section 1575 into play.” *Id.* at 836.

8 Plaintiff’s statements, Plaintiff’s wife’s statements, the records of a long period of
9 psychological counseling, the opinion of psychologist Russell Gold, Ph.D., the opinion of
10 psychiatrist Dr. Lynn Ponton, M.D.⁶, and the fact that Defendant paid Plaintiff disability
11 benefits for thirteen years could lead a reasonable jury to conclude that Plaintiff was suffering
12 from mental illness which amounts to “weakness of the mind” under California law. Although
13 Defendant disputes Plaintiff’s diagnosis, viewed in the light most favorable to Plaintiff, this
14 evidence could lead a reasonable jury to conclude that Defendant knew that Plaintiff was
15 unusually susceptible to pressure.

16 The Court must next examine whether there is evidence that could lead a reasonable
17 jury to determine that Defendant took unfair advantage of Plaintiff’s weakened state of mind.
18 Although Defendant contends the Court should only consider the settlement negotiations, the
19 Court finds that the appropriate inquiry is broader. The ultimate question is “whether from
20 the *entire context* it appears that [Plaitiff’s] will was overborne.” *See Keithley*, 11 Cal. App.3d
21 at 451 (emphasis added). In this case, the “entire context” of the settlement agreement
22 includes Defendant’s investigation of Plaintiff’s claim, Defendant’s termination of Plaintiff’s
23 benefits, Defendant reporting that Plaintiff had committed insurance fraud to various law
24 enforcement agencies, and Defendant suing Plaintiff. The Court must determine whether there

25
26 ⁶ Defendant contends Dr. Ponton is not qualified as an expert and lacks sufficient
27 foundation for her opinions. The Court finds that Dr. Ponton’s education and experience
28 is a sufficient basis for her opinions about Plaintiff’s condition and about the validity of
Defendant’s IME examinations. However, the Court finds that Dr. Ponton’s opinions about
Defendant’s motivation for terminating Plaintiff’s benefits and for suing Plaintiff are
inadmissible as outside the scope of her expertise.

1 is sufficient evidence in the record, viewed in the light most favorable to Plaintiff, that a jury
2 could find that Defendant acted in bad faith in its investigation and subsequent termination of
3 Plaintiff's benefits and by suing Plaintiff in order to take advantage of Plaintiff's weakened
4 state of mind. This determination requires an examination of California law on own
5 occupation disability insurance policies and bad faith termination.

6 Under California law, own occupation insurance policies define total disability not as
7 "an absolute state of helplessness but means such disability as renders the insured unable to
8 perform the substantial and material acts necessary to the prosecution of a business or
9 occupation in the usual or customary way." *Hangarter v. Provident Life and Accident Ins. Co.*,
10 373 F.3d 998, 1006 (9th Cir. 2004) (quoting *Erreca v. Western States Life Ins. Co.*, 19 Cal. 3d
11 388 (1942)). Regardless of the definition of "total disability" in an own occupation insurance
12 policy, "California law *requires* courts to deviate from the explicit policy definition of 'total
13 disability' in the occupational policy context." *Hangarter*, 373 F.3d at 1006.

14 Under California law, "[t]he fact that the insured may do some work or transact some
15 business duties during the time for which he claims indemnity for total disability or even the
16 fact that he may be physically able to do so is not conclusive evidence that his disability is not
17 total, if reasonable care and prudence require that he desist." *Id.* at 1007 (citation omitted).
18 If an insured can perform the duties of his occupation intermittently, but cannot do so in a
19 "continuous, normal" way, the insured is totally disabled under California law. *Id.* at 1008.
20 An insured's income is irrelevant to the disability determination. *Id.* "[T]he magnitude of [the
21 insured's] enterprise and his income therefrom . . . have *no proper place* in the determination
22 of whether [the insured] is totally disabled [because such insurance] *does not insure against*
23 *loss of income.*" *Id.* at 1009 (citation omitted).

24 In determining whether an insurer acted in bad faith by denying coverage, the fact-
25 finder must determine whether the denial was reasonable. *Id.* at 1010 (citing *Amadeo v.*
26 *Principal Mut. Life Ins. Co.*, 290 F.3d 1152, 1161 (9th Cir. 2002)). If there was a genuine
27 dispute as to whether the insurer was required to make payments, a court may find as a matter
28 of law that the insurer did not act in bad faith. *Hangarter*, 373 F.3d at 1010. However, if the

1 insurer's investigation of a claim was biased, even if experts stated the insured was not totally
2 disabled, a fact finder may conclude that any dispute over coverage was not genuine and that
3 the insurer acted in bad faith. *Id.* (citing *Guebara v. Allstate Ins. Co.*, 237 F.3d 987, 996 (9th
4 Cir. 2001)).

5 An insurer's bias may be shown through the following factors:

- 6 (1) The insurer may have misrepresented the nature of the investigatory
7 proceedings;
- 8 (2) The insurer's employees lied in depositions or to the insured;
- 9 (3) The insurer dishonestly selected its experts;
- 10 (4) The insurer's experts were unreasonable; or
- 11 (5) The insurer failed to conduct a thorough investigation.

12 *Hangarter*, 373 F.3d at 1010. Under California law, evidence of failure to conduct a thorough,
13 fair, and unbiased investigation must be submitted to the finder of fact to determine whether
14 the evidence establishes the insurer acted in bad faith. *Id.*

15 Lorenz Blochl, Defendant's field investigator, testified that he was unaware that
16 Plaintiff had ever disclosed working in any capacity, and that knowing about Plaintiff's
17 previous disclosures would have affected his determination that Plaintiff had committed fraud.
18 *See* Bloch Depo., Plaintiff's Ex. 121 at 994-96, 1000. Blochl further testified that the prior
19 disclosures were the reason the FBI declined to pursue the case. *Id.* A reasonable jury could
20 conclude that Defendant presented a skewed or incomplete version of the facts to law
21 enforcement agencies through Blochl, who was unaware of Plaintiff's previous disclosures
22 about his work activities, in order to put pressure on Plaintiff to drop his insurance claim. *See*
23 Bloch Depo., Plaintiff's Ex. 121 at 994-996.

24 Despite the suggestion of the deputy district attorney that Defendant should ask more
25 specific questions in order to establish whether Plaintiff was committing fraud, Defendant
26 failed to ask Plaintiff directly about his work activities after 1991. *See* Kelly Decl., Doc. #
27 143-4 at ¶ 55; Plaintiff's Ex. 68 at 375. Viewing this evidence in the light most favorable to
28 Plaintiff and drawing all reasonable inferences in Plaintiff's favor, the Court concludes that a
jury could find that this was an intentional omission to make it appear that Plaintiff was
withholding information he was never asked to disclose. Further, Defendant's failure to ask
these questions itself may show bias under California law. *See Hangarter*, 373 F.3d at 1010.

1 A reasonable jury could conclude that failure to ask direct questions about Plaintiff's work
2 activities prior to terminating benefits shows that Defendant "failed to conduct a thorough
3 investigation." *See id.*

4 In conducting the first IME evaluation in 1991, Dr. Stahl failed to apply the correct
5 standard in determining whether Plaintiff was disabled. *See* Defendant's Ex. K, Doc. # 107-2
6 at 76-78. Dr. Stahl determined that Plaintiff was "able to perform the substantial and material
7 duties of his usual occupation," rather than determining whether Plaintiff was "unable to
8 perform the substantial and material acts necessary to the prosecution of a business or
9 occupation *in the usual or customary way,*" as is required pursuant to *Hangarter*, 373 F.3d at
10 1006. A reasonable jury could find that Defendant's expert's application of the wrong standard
11 in evaluating Plaintiff's disability shows bias in Defendant's investigation. Further, despite Dr.
12 Stahl's opinion that Plaintiff was not disabled, Defendant informed Plaintiff that it had
13 "completed a comprehensive review of" the claim and would continue to pay benefits.
14 Plaintiff's Ex. 36 at 280. A reasonable jury could conclude based on this fact that Defendant
15 knew that the evaluation was flawed and would not hold up as a justification for terminating
16 benefits.

17 In conducting the second IME evaluation, Dr. Bergsma does not state the standard he
18 used for determining that Plaintiff was not disabled. *See* Defendant's Ex. X, Doc. # 107-3 at
19 82. A reasonable jury could find that failure to state the standard by which he determined that
20 Plaintiff was not disabled shows that Dr. Bergsma's evaluation was not sufficiently thorough
21 and that Defendant cannot rely on it to establish a genuine dispute as to whether Plaintiff was
22 disabled.

23 As for the third IME evaluation, there are facts in the record which could lead a jury to
24 conclude that Defendant failed to provide Dr. Abrams with all of its records of prior testing on
25 Plaintiff, despite the doctor's request for the records, and failed to inform the doctor that
26 Plaintiff had previously disclosed engaging in limited work activities. *See* Defendant's Ex. W,
27 Doc. # 107-3 at 71. A reasonable jury could find that these omissions were intentional and
28 resulted in a biased conclusion that Plaintiff was not disabled. Additionally, according to Dr.

1 Ponton, Dr. Abrams disregarded test results from the 1997 IME which show a very low score
2 for “narcissistic personality pattern,” which rules out Dr. Abrams’ diagnosis of Narcissistic
3 Personality Disorder. *See* Ponton Decl., # 143-3 at ¶ 65. Based on this fact, a reasonable jury
4 could find that Dr. Abrams’ diagnosis was unreasonable. Dr. Abrams does not state what
5 standard he used to determine whether Plaintiff was disabled. Dr. Abrams appears to have
6 assumed that *any* work activity by Plaintiff would indicate that he is not disabled under the
7 terms of his policy, which is incorrect under California law. *See* Defendant’s Ex. W, Doc. #
8 107-3 at 71, 77. Dr. Abrams also focuses on the amount of income Plaintiff may have received
9 while on disability, rather than whether Plaintiff could work full-time as an insurance salesman
10 “in the usual or customary way.” *See id.* at 76-77. If Defendant failed to inform its expert of
11 the correct standard or the expert failed to apply the correct standard, a reasonable jury could
12 find that Defendant failed to conduct a thorough investigation before terminating benefits.

13 Defendant also appears to have directly relied on evidence of Plaintiff’s income in
14 determining that he was not totally disabled, rather than on evidence of the extent of his work
15 activity, which is improper as a matter of California law. *See Hartanger*, 373 F.3d at 1009.
16 When Defendant terminated Plaintiff’s benefits, contacted law enforcement agencies, and sued
17 Plaintiff, it was in possession of evidence that Plaintiff’s activities were limited to “generating
18 3-5 policy sales [per year]” which were “virtually all [] repeat sales to existing customers.”
19 *See* Plaintiff’s Ex. 71 at 399 (letter from Thomas Gore, General Agent of General American,
20 received by Defendant Feb. 4, 1999). A reasonable jury could conclude that Defendant applied
21 the wrong standard for determining whether Plaintiff was disabled, which could amount to bad
22 faith under California law.

23 There is evidence in the record which, viewed in the light most favorable to Plaintiff,
24 could lead a jury to conclude that, despite knowing that Plaintiff was mentally ill, Defendant
25 terminated Plaintiff’s coverage in bad faith after conducting a biased investigation, contacted
26 law enforcement agencies to instigate an investigation of Plaintiff for the purposes of
27 harassment and sued Plaintiff for the return of all benefits without a valid basis for doing so
28 in order to take unfair advantage of Plaintiff’s weakness of mind. Although Defendant points

1 out that none of the *Odorizzi* factors are present, this is not dispositive, as the Ninth Circuit
2 previously ruled. The *Odorizzi* list of factors is not exclusive, and under California law, all of
3 the circumstances surrounding contract negotiations should be examined to determine whether
4 a party to a contract engaged in “overpersuasion.” *Keithley*, 11 Cal. App. 3d at 451. If a jury
5 determined that Defendant took these actions in bad faith in order to pressure Plaintiff to
6 surrender his benefits via a settlement agreement, it could find that Defendant “took unfair
7 advantage of [Plaintiff’s] weakness of mind,” allowing rescission of the settlement agreement
8 for undue influence. Defendant’s motion for summary judgment on Plaintiff’s rescission
9 claim is denied.

10 **II. Federal Rule of Civil Procedure 60**

11 Defendant contends that Plaintiff’s claims are barred by Federal Rule of Civil Procedure
12 60(b) because more than one year has passed since the dismissal of Plaintiff’s previous suit.
13 (Doc. # 106-1 at 27). Defendant contends that Plaintiff cannot establish that a grave
14 miscarriage of justice would occur if he is not permitted to pursue this litigation despite the
15 delay. *Id.*

16 Plaintiff contends Rule 60(b) would not prevent rescission of the settlement agreement
17 because he is entitled to rescission as a matter of substantive state law which cannot and has
18 not been modified by the Federal Rules of Civil Procedure. (Doc. # 143 at 26). Plaintiff
19 contends that modifying the applicable state substantive law would go beyond the authority
20 conferred in the Rules Enabling Act. *Id.* at 27. Plaintiff contends that rescission would require
21 placing Plaintiff back into the position he was in before he entered the contract, which requires
22 both tolling the statute of limitations and permitting this lawsuit to proceed. *Id.* at 28. Finally,
23 Plaintiff contends that even if the Court finds that Rule 60(b)—rather than state law on
24 remedies—controls, Rule 60(b) allows Plaintiff to “be relieved of the judgment in the
25 underlying litigation” due to fraud on the court and a grave miscarriage of justice. *Id.* at 28-29.

26 Pursuant to Federal Rule of Civil Procedure 60(b), a “court may relieve a party . . . from
27 a final judgment . . . for the following reasons:

- 28 (1) mistake, inadvertence, surprise, or excusable neglect;
- (2) newly discovered evidence that, with reasonable diligence, could not have

1 been discovered in time to move for a new trial under Rule 59(b);
2 (3) fraud (whether previously called intrinsic or extrinsic), misrepresentation, or
3 misconduct by an opposing party;
4 (4) the judgment is void;
5 (5) the judgment has been satisfied, released, or discharged; it is based on an
6 earlier judgment that has been reversed or vacated; or applying it prospectively
7 is no longer equitable; or
8 (6) any other reason that justifies relief.

9 A motion brought under Rule 60(b)(1), (2), or (3) must be brought within one year of the
10 judgment, whereas under the other provisions, the motion “must be made within a reasonable
11 time” Fed. R. Civ. P. 60(c). Relief may only be obtained pursuant to the other provisions
12 if a motion is brought “within a reasonable time” *Id.* Relief under Rule 60(b)(6) is only
13 available if none of the other categories apply and may only be granted in extraordinary
14 circumstances. *See Liljeberg v. Health Services Acquisition Corp.*, 486 U.S. 847 (1988);
15 *Gonzales v. Crosby*, 545 U.S. 524, 535 (2005).

16 Pursuant to Rule 60(d), the other provisions of Rule 60 “do not limit a court’s power
17 to [] entertain an independent action to relieve a party from judgment” In an independent
18 action, a court may only generally reverse if allowing the judgment to stand would be a “grave
19 miscarriage of justice.” *United States v. Beggerly*, 524 U.S. 38, 46 (1998). If a jury finds that
20 Defendant terminated Plaintiff’s disability benefits, sued him, and reported him to law
21 enforcement agencies in bad faith, allowing the prior judgment to bar this suit would be a grave
22 miscarriage of justice.

23 Additionally, if “there is a substantive right as a matter of state law to have a judgment
24 reopened,” the substantive state law would prevail over the federal procedural standard for
25 Rule 60(d). *See* Charles Alan Wright, Arthur R. Miller and Mary Kay Kane, 11 Federal
26 Practice and Procedure § 2853 (2d ed. 1995). Interpreting an earlier version of Rule 60, the
27 Third Circuit held that the identically worded “independent action” clause then located in Rule
28 60(b) allowed state-law claims for fraud outside the one-year time limit imposed by Rule
 60(b)(3). *See Averbach v. Rival Mfg. Co.*, 809 F.2d 1016, (3d Cir. 1987); *see also* Wright,
 Miller, and Kane, 11 Federal Practice and Procedure § 2868. Where vindicating a substantive
 state law right requires reversing the judgment, a federal court may do so in an independent
 action. *See Averbach*, 809 F.2d 1016. In the memorandum disposition reversing this Court’s

1 order dismissing Plaintiff's claims, the Ninth Circuit held:

2 The statutory remedy of rescission is designed to restore the parties to where
3 they were before entering the contract. Section 1692 of the California Civil Code
4 provides that "[w]hen a contract has been rescinded in whole or in part . . . [t]he
5 aggrieved party shall be awarded complete relief, including restitution of
6 benefits, if any, conferred by him as a result of the transaction" When one
7 party is unable to restore the other party to its pre-contract position, § 1692
8 allows a court to "adjust equities a) that implicitly need adjustment, and b) that
9 the parties have not already expressly adjusted by their contract." *Hedging*
10 *Concepts Inc. v. First Alliance Mortgage Co.*, 41 Cal. App. 4th 1410, 1422, (Cal.
11 App. 1996). Courts are empowered to adjust equities where necessary to "grant
12 such relief as will achieve substantial justice under the circumstances of the case
13 presented to it." *Snelson v. Ondulando Highlands Corp.*, 5 Cal. App. 3d 243,
14 258 (Cal. App. 1970). Indeed, courts should go as far as possible in restoring
15 rescinding parties to their prior state of being. *See, e.g., Runyan v. Pacific Air*
16 *Industries*, 2 Cal.3d 304, 316 (1970); *Gardiner Solder Co. v. Supalloy Corp.*,
17 232 Cal. App. 3d 1537, 1543-45, (Cal. App. 1991); *Bank of America v.*
18 *Greenbach*, 98 Cal. App. 2d 220, 237-240 (Cal. App. 1950).

19 The most obvious way to restore Kelly to his prior state of being would be to act
20 as if the settlement had never happened and to let him pursue his bad-faith and
21 breach-of-contract claims.

22 (Doc. # 55 at 4-6).⁷ This Court concludes that if Plaintiff succeeds in convincing a jury that
23 he is entitled to rescission, as a matter of state substantive law, awarding "complete relief"
24 would require allowing Plaintiff to pursue his bad faith and breach of contract claims. *See* Cal.
25 Civ. Code § 1692; *Averback*, 809 F.2d 1016.

26 **III. Objections**

27 In his Opposition, Plaintiff raised 29 objections to evidence Defendant filed in support
28 of the motion. (Doc. # 143-6). Plaintiff also objected on due process grounds to additional
evidence submitted by Defendant with Defendant's reply. (Doc. # 155). In addition to the
objection to Dr. Ponton's declaration, Defendant objected to Anna Kelly's declaration, Dr.
Gold's declaration, Plaintiff's counsel's declaration, and Plaintiff's declaration. (Docs. # 153-
1, 153-2, 153-3, 153-4, 153-5, 153-6). All objections to evidentiary materials cited in this
Order are overruled. All objections to evidentiary materials not cited in this Order are denied
as moot.


⁷ The Court notes that the Ninth Circuit expressly declined to rule on the Rule 60 issue.
However, in delineating the extent of the remedy required under state law, including tolling
the statute of limitations, the Ninth Circuit's ruling is helpful in applying the principle explored
in *Averback* that the Federal Rules of Civil Procedure do not override state-law substantive
rights.

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CONCLUSION

IT IS HEREBY ORDERED that Defendant's Motion for Summary Judgment (Doc. # 106) is **DENIED**. The parties shall contact the Magistrate Judge to schedule a status conference to set a schedule to complete discovery.

DATED: August 12, 2010


WILLIAM Q. HAYES
United States District Judge