

Evidence of a defendant's financial condition in the punitive damages phase of trial

Although it may be rare to find yourself in the punitive damages phase of a trial, there are some things you must know to maximize your recovery. First and foremost, evidence of a defendant's financial condition is a prerequisite to support an award for punitive damages. The plaintiff has the burden to present evidence of a defendant's financial condition to the jury. (Evid. Code § 500; See also *Adams v. Murakami* (1991) 54 Cal.3d 105, 119 [284 Cal.Rptr. 318].) This article addresses the various ways a plaintiff's attorney can obtain that evidence, and the procedural rules relating to the presentation of it.

Civil Code section 3294, subdivision (a), paves the way for punitive damages. That section states, "[i]n an action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice, the plaintiff, in addition to the actual damages, may recover damages for the sake of example and by way of punishing the defendant." Attorneys tend to focus discovery on issues that support a finding of "oppression, fraud, or malice." This focus is paramount, as evidence of a defendant's financial condition is irrelevant without a finding of "oppression, fraud, or malice." However, there are methods to conduct discovery, both formally and informally, of a defendant's financial condition. An effective pretrial discovery plan of a defendant's financial condition will not only give you a jump start on the discovery of key evidence that is too often ignored before trial, it could also result in a favorable settlement.

Discovery of a defendant's financial condition by court order

The general rule is that pretrial discovery of a defendant's financial condition, although relevant in a punitive damage claim, is prohibited. (*Doak v. Superior Court of Los Angeles County* (1968) 257 Cal.App.2d 825, 832-834 [65 Cal.Rptr. 193].) Courts have upheld this general rule based upon public policy and the right of privacy arguments. This has not always been the case. For a review of the development of this rule, and corresponding legislative history, see *Rawnsley v. Superior Court* (1986) 183 Cal.App.3d 86 [227 Cal.Rptr. 806]. The general rule in no way diminishes the importance of this evidence. A defendant's net worth bears on the sting necessary to effectuate the punishment purposes of a punitive damages award. This remains the law post *State Farm Mut. Auto Ins. v. Campbell* (2003) 538 U.S. 408.

Notwithstanding the general rule, plaintiffs can still conduct discovery of a defendant's financial condition by way of court order. Civil Code section 3295, subdivision (c), states, "No pretrial discovery by the plaintiff shall be permitted with respect to the evidence referred to in paragraphs (1) and (2) of subdivision (a) unless the court enters an order permitting such discovery pursuant to this subdivision." Civil Code section 3295, subdivision (a), paragraphs (1) and (2), refer to profits gained by wrongful conduct and the defendant's financial condition. This assumes that the plaintiff has properly pleaded a claim for punitive damages. A defendant's financial condition is not at issue absent a properly punitive damages claim, save several exceptions, and the plaintiff has no right to conduct discovery relating to it. (*Brown v. Superior Court* (1990) 224 Cal.App.3d 989, 994 [274 Cal.Rptr. 442].)

The procedure to obtain a court order allowing pretrial discovery of a defendant's wealth is relatively simple. Procedurally, the order must be obtained by way of noticed motion. Civil Code section 3295, subdivision (c), gives further guidance, and states in relevant part, "Upon motion by the plaintiff

supported by appropriate affidavits and after a hearing, if the court deems a hearing to be necessary, the court may at any time enter an order permitting the discovery otherwise prohibited by this subdivision if the court finds, on the basis of the supporting and opposing affidavits presented, that the plaintiff has established that there is a *substantial probability that the plaintiff will prevail on the claim* pursuant to Section 3294." Essentially, the plaintiff must file a noticed containing declarations that support a finding of "oppression, fraud, or malice." Whether a hearing is required is left to the discretion of the court.

Although the procedural process may be simple, the plaintiff's burden is not. What amounts to "substantial probability" is not crystal clear, and depends on the facts of your case, and your judge. *Jabro v. Superior Court* (2002) 95 Cal.App.4th 754 [115 Cal.Rptr.2d 843] provides some further guidance, stating that a "court must (1) weigh the evidence presented by both sides, and (2) make a finding that it is *very likely the plaintiff will prevail on his claim for punitive damages.*" (*Id.* at 755.)

With terminology like "substantial probability" and "very likely," it is obvious the burden for a court order allowing discovery into a defendant's wealth is high. A showing that it is *probable* there is "oppression, fraud, or malice" is insufficient. To prevail on a claim for punitive damages at trial, the plaintiff must prove "oppression, fraud, or malice" by "clear and convincing evidence." Some judges require that burden of proof to entitle you to discovery of a defendant's financial condition. The plaintiff must go above and beyond what would be required to defeat summary adjudication. In practice, court's are reluctant to allow this discovery. Even so, with the right facts, moving for a court order pursuant to Civil Code section 3295, subdivision (c), can put enormous pressure upon the defendant to settle.

It should be noted that Civil Code section 3295, subdivision (c), applies to arbitrations as well. Plaintiffs must obtain a court order to conduct discovery with respect to a defendant's wealth in arbitration. (Code of Civ. Proc. § 1141.19.5.)

If the court finds there is a substantial probability that the plaintiff will prevail on the punitive damages claim and allows pretrial discovery of a defendant's financial condition, it is not a per se finding of "oppression, fraud, or malice." Civil Code section 3295, subdivision (c), states that such an order, "shall not be considered to be a determination on the merits of the claim or any defense thereto and shall not be given in evidence or referred to at the trial." The plaintiff must still convince the trier of fact.

If the court allows the discovery of a defendant's financial condition, be cautious about sharing the information. The defendant is presumptively entitled to a protective order that the disclosure of the financial documents is limited solely to the discovering party, its counsel, counsel's representative, and solely for the purposes of the pending lawsuit. (*Richards v. Superior Court* (1978) 86 Cal.App.3d 265 [150 Cal.Rptr. 77].)

Civil Code section 3295 confers limited discovery rights of a defendant's financial condition when punitive damages are alleged. This is not a plaintiff's only means of discovering a defendant's financial condition. Although this article focuses on the discovery of a defendant's financial condition when punitive damages are alleged, such information is discoverable when it is germane to a material issue in the case. Whether punitive damages are alleged or not is irrelevant. If the proof of an allegation is dependent upon the defendant's profits or wealth then it is discoverable. Conversion is the classic example. For further insight on these issues, and other circumstances in which a defendant's financial condition is discoverable absent a punitive damages claim, see *Rawnsley v. Superior Court, supra*.

Similarly, evidence of a defendant's financial condition is admissible in the liability phase of trial if the evidence is relevant to liability or other issues not relating to the amount of punitive damages. (*Notrica v. State Comp. Ins. Fund* (1999) 70 Cal.App.4th 911, 939 [83 Cal.Rptr.2d 89].) In the foregoing circumstances, there would be no need to seek a court order pursuant to Civil Code section 3295, but expect to file some motions to compel.

Obtaining the identity of key documents and witnesses in pretrial discovery

There may be tactical reasons to not seek a court order pursuant to Civil Code section 3295. It may be futile given the facts of the case, and the reluctance of judges to grant the motion. If your motion fails you can expect the defendant at the close of plaintiff's case to ask for a nonsuit/directed verdict on the issue of punitive damages. The defendant will argue that the plaintiff has not produced any new evidence that would allow a jury to find "oppression, fraud or malice" than what was raised in plaintiff's motion. The court denied that motion for discovery of defendant's financial condition, because it had not met the requisite burden of proof then, and it has not met it at trial.

Choosing to make the motion should be determined on a case by case basis. No matter the decision, plaintiffs may still be able to discover the identity of key witnesses, and financial records relating to the defendant's financial condition, without the need for court order. Civil Code section 3295, subdivision (c), states, "the defendant may be required to identify documents in the defendant's possession which are relevant and admissible for that purpose and the witnesses employed by or related to the defendant who would be most competent to testify to those facts." This allows plaintiffs to request the identity of documents and witnesses relating to profits or the financial condition of the defendant.

Being thrust into the punitive damages phase of trial is stressful. Time is short, and you are about to enter the world of accounting. Knowing the identity of documents and the witnesses most competent to testify as to the defendant's profits and financial condition long before trial streamlines the process. Request that defendant identify documents relating to its financial condition, and the witnesses who are most qualified to testify as to those documents.

Informal discovery of a defendant's financial condition

Google is an excellent starting point for informal discovery of a Defendant. Defendants, and plaintiffs, are all over the internet doing foolish things. They pose in front of expensive cars on *Facebook*. They rent out their condos in Mammoth on *Craigslist*. They blog. They even blog about your lawsuit. If you do not continuously monitor your defendants on the internet, start. If you do not continuously monitor your client on the internet, it is imperative you start. The internet is an absolute goldmine for impeachment evidence on a defendant's financial condition.

Financial information for public companies is easily accessible. The Securities and Exchange Commission maintains a website where electronic versions of financial reports can be downloaded (www.sec.gov/edgar.shtml). SEC filings and corporate balance sheets can also be obtained through

Yahoo Finance (<http://finance.yahoo.com>), and Google Finance (<http://finance.google.com/> finance and <http://google.brand.edgar-online.com>).

Virtually all businesses maintain a website. Perhaps chief of the many reasons for a business to maintain a website is to get more business. As a result, businesses project themselves as being rich on the internet. This provides fantastic evidence to impeach the CFO/accountant who will invariably testify about the poor financial condition of the business.

Insurance Code section 900 requires insurance companies to file with the state insurance commissioner "statements exhibiting its condition and affairs" every year. These statements include the overall viability and assets of the company. This information is key in insurance bad faith cases. The files can be found at the California Department of Insurance website (www.insurance.ca.gov). Filings are updated on March 1st every year.

Plaintiff's can also purchase asset checks of individuals and businesses. These asset checks range in degree of detail and price. Repeated asset checks may be useful to demonstrate to the jury that the defendant is playing fast and loose with his claim of limited assets. It may also be useful to establish that the defendant has fraudulently conveyed assets in an attempt to frustrate your efforts to collect a judgment. Asset checks can be instrumental in understanding the settlement value of a case. One attorney, and CAALA member, recently discovered several large income properties owned by a seemingly poor Defendant overseas that were not disclosed in deposition. Needless to say, the value of that case increased significantly. Consult the CAALA list of vendors for companies that provide asset checks.

Evidence of a Defendant's Financial Condition at Trial

Typically, a defendant will seek a bifurcation of profits and financial condition evidence from the liability phase of trial. Civil Code section 3295, subdivision (d), states, the court "shall, on application of any defendant, preclude the admission of evidence of that defendant's profits or financial condition until after the trier of fact returns a verdict for plaintiff awarding actual damages and finds that a defendant is guilty of malice, oppression, or fraud in accordance with Section 3294. Evidence of profit and financial condition shall be admissible only as to the defendant or defendants found to be liable to the plaintiff and to be guilty of malice, oppression, or fraud. Evidence of profit and financial condition shall be presented to the same trier of fact that found for the plaintiff and found one or more defendants guilty of malice, oppression, or fraud." In practice this is essentially a motion in limine precluding evidence of defendant's financial condition until a finding of actual injury, and "malice, oppression, or fraud."

In the first phase of a bifurcated trial the jury will consider liability, causation, actual injury, and whether there is clear and convincing evidence that would support a punitive damages award. The jury cannot consider evidence relating to the amount of the punitive damages award. However, if the defendant chooses to not to bifurcate, the plaintiff can go ahead and present evidence in support of the amount of a punitive damages award.

If the defendant has minimal assets, but has insurance, the plaintiff should request a bifurcation. If the jury hears evidence of limited financial worth during the compensatory damage phase of the case, the jury may be reluctant to award substantial compensatory damages.

Civil Code section 3295, subdivision (c), does not bar a plaintiff from subpoenaing relevant profits and financial condition evidence for trial. (Civ. Code § 3295 subd. (c).) The only caveat is the plaintiff cannot look at the documents until the condition of Civil Code section 3295, subdivision (d), are met: that a jury returns a verdict for actual damages; and a finding of "oppression, fraud or malice." If the jury finds for the plaintiff on these issues, the plaintiff may examine the relevant financial information and introduce the evidence during the bifurcated portion of the trial.

It is important to understand plaintiffs have the burden of producing meaningful evidence of a defendant's financial condition to support an award for punitive damages. (Evid. Code § 500; see also *Adams v. Murakami*, *supra*.) Plaintiffs cannot rely on the defendant to set forth their financial condition at trial. The plaintiff must subpoena the necessary witnesses and documents for trial. Plaintiff must also depose identified witnesses and persons most qualified to testify on the overall financial condition of the defendant after the jury finds "oppression, fraud or malice." If an accurate and complete picture of the defendant's financial is not presented to the jury by the plaintiff, a punitive damages award is vulnerable to reversal on appeal. (See *Baxter v. Peterson* (2007) 150 Cal.App.4th 673 [58 Cal.Rptr.3d 686]; and *Lara v. Cadag* (1993) 13 Cal.App.4th 1061 [16 Cal.Rptr.2d 811].) Do not rely solely net worth, gross income, or gross assets. There are a number of other items that reflect on a defendant's overall financial condition.

This burden puts the plaintiff in a relatively precarious position. The plaintiff has the obligation to show the defendant's cards, but the defendant still controls the deck. If a defendant "hides the ball" by refusing to produce financial information, the defendant is presumed to have waived its right to challenge a punitive damages award based upon lack of wealth evidence. (*Mike Davidov Co. v. Issod* (2000) 78 Cal.App.4th 597, 608-610 [92 Cal.Rptr.2d 897].) In the situation where the defendant is "hiding the ball," request the court give CACI Jury Instruction No. 203 which states, "You may consider the ability of each party to provide evidence. If a party provided weaker evidence when it could have provided stronger evidence, you *may* distrust the weaker evidence." You may request the court instruct that the defendant's evidence *should* be viewed with distrust. This instruction is based upon Evidence Code section 412.

What kinds of evidence you want

Two words of caution with discovery of defendant's wealth: be broad. Make sure discovery is designed to obtain the defendant's complete financial condition. Do not shy away from discoverable items that would show the defendant is not wealthy. Plaintiffs have the burden of producing meaningful evidence of a Defendant's financial condition to support an award for punitive damages. If it's good for your case or bad, it must be shown to the jury if you want your award upheld. Again, go beyond net worth, gross income, and gross assets. In addition to broad categories, such as "All documents relating to defendant's assets...", be sure to also request credit information, liabilities, tax returns with all schedules (portions of tax returns may be privileged), W-2s, 1099s, luxury items, accounts receivable, audits and reviews, general ledgers, trial balances, balance sheet reports, income statement records, rent reports, payable reports, cash disbursement reports, cash receipts reports, cash flow reports, real property statements, personal property statements, credit reports, and loan/credit applications.

Loan/credit applications are terrific source of information. When a person wants to borrow money, he or she is more likely to exaggerate their financial worth in order to secure a loan. If you examine the defendant during the punitive damages phase of trial, the defendant will be hard pressed to tell the jury that he really does not have the asset he listed on the loan application. Is he going to admit he lied to get the loan? If he makes such an admission remind the jury during argument that the defendant has admitted that he is willing to lie to achieve what he wants.

Conclusion

Although it may be rare, even lucky, to be in the punitive damages phase of trial, that does not mean that you should not be prepared for it.

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