SUPERIOR COURT OF THE STATE OF CALIFORNIA

FOR THE COUNTY OF LOS ANGELES

HOLLY WEDDING, et al.,

Plaintiffs,

v.

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, et al.,

Defendants.

Lead Case No. BC517444
JCCP Case No. 4936

[DRAFT] PROPOSED STATEMENT OF DECISION Re BIFURCATED COURT TRIAL

Trial Date: June 10, 2019

This is the Court's [Draft] Proposed Statement of Decision submitted in Phase 1 pertaining to contract interpretation and Phase 2 pertaining to California Public Employees' Retirement System's ("CalPERS") statute of limitations affirmative defense in the above entitled matter subject to a party's objection under California Rule of Court 3.1590(g).

I. EXECUTIVE SUMMARY

CalPERS, like virtually all other insurance carriers which entered the Long-Term Care insurance market a generation ago, has learned a bitter lesson: **Actuaries do not always make correct predictions about the true cost of insuring a new class of risks.** Here, the result is that the original premium schedule has been inadequate to fund current and anticipated claims, and multiple premium increases have been implemented as a result.[1] This insurance product was intended to be self-sufficient financially and not to require any subsidy by the State of California or by the various public employers who participate in CalPERS or CalSTRS (whose members were given access to this CalPERS offering). CalPERS stated that by managing its own risk pool and not using available insurance products it could undercut the prices charged for similar coverage since the plan would be run as a non-profit and draw on CalPERS' vast experience and competence. While CalPERS did have the State Department of Insurance review the original contract and certain sales materials, CalPERS is not regulated by that agency and this Long Term Care Plan does not qualify for assistance from the California Life and Health Insurance

[1] CalPERS is hardly the only long-term care insurer that has been forced to raise premiums. The program for federal employees, which Congress has contracted out to private entities to insure and administer, has seen premium increases commensurate with industry-wide experience. (U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-11-630, LONG-TERM CARE INSURANCE: CARRIER INTEREST IN THE FEDERAL PROGRAM, CHANGES TO ITS ACTUARIAL ASSUMPTIONS, AND OPM OVERSIGHT 2 (2011) (available at https://www.gao.gov/products/GAO-11-630).) Inflation protection benefits have been particularly problematic due to actuarial oversights. (*See id.* at 2, 29-31.) Premium increases have been a feature of private plans, not just those directed at government employees. (*See* Lawrence A. Frolik, *Private Long-Term Care Insurance: Not the Solution to the High Cost of Long-Term Care for the Elderly*, 23 Elder L.J. 371, 383 & nn. 88-89 (2016) (discussing increases by private long-term care insurers).)

Guarantee Association or the California Insurance Guarantee Association.

The problem giving rise to this suit and this bifurcated trial is that the standard form "Evidence of Coverage" ("EOC") document given to all insureds (aka "enrollees") involved in this suit as named Plaintiffs or class members made certain statements which Plaintiffs construe to be a promise that premiums for "Inflation Protection" coverage would not be increased because, in Plaintiffs' view, CalPERS had represented to potential insureds that these premiums (which were typically 200 percent or more higher than monthly premiums for more basic coverage without ongoing inflation increases to available daily reimbursement amounts included per contract terms) were "locked in" when an insured's guaranteed-renewable policy was issued, presumably because the premiums had been correctly priced from the beginning.

In the pithy language of CalPERS's lawyers in this case, Plaintiffs' interpretation of the "Inflation Protection" language of the EOC makes it a "suicide pact" since insolvency is the inevitable consequence of the sale of an insurance product for an inadequate premium if the right to adjust the premium is given up. The Court finds Plaintiffs' contract interpretation to be the more realistic linguistic interpretation of how the "your premium will not increase" language when read by an objectively reasonable insured, even though the Court also realizes that this interpretation necessarily sows the seeds of an almost inevitable insolvency disaster if, as here, the original pricing of the Inflation-Protection benefit was materially wrong. The Court cannot agree with CalPERS' argument that an objectively reasonable insured would expect the language in question to receive a tortured judicial interpretation simply to avoid the obviously bad consequence of plan insolvency.

The parties have a separate contract interpretation dispute which this Court is resolving in CalPERS's favor as to whether or not it was allowed to raise premium rate increases at all if they were not applied uniformly as to all insureds subject to a given form of CalPERS Long-Term

Care contract, i.e., LTC1 or LTC2.[2] Subsequently, CalPERS started to sell under form LTC3, then it stopped selling the product to new enrollees for a time and then it reopened sales under the LTC4 form of EOC. The Court agrees with CalPERS that it could impose selective rate increases on current insureds (subject however to such limits as the EOC imposed on price increases for Inflation-Protection coverage as discussed above in brief) as long as the increases were consistent, from a pricing point of view, with a given risk pool, e.g., those who bought "Lifetime" benefits claiming rights as compared to persons who bought a more basic (and cheaper) product with a capped duration of possible claim payments, e.g., three years.

As the undisputed record in this case shows based on this trial, CalPERS has imposed some across-the-board premium increases and many selective rate increases as it tried to steer this self-funded plan to long-term solvency over the years. Many of these increases were imposed on the recommendation of CalPERS's consulting actuaries selectively on enrollees who had bought Inflation-Protection coverage or Lifetime benefit coverage, or both. Seventy-five (75) percent of the risk pool under LTC1 and LTC2 fell into this group.

The earlier rate increases generated some legislative concern but no litigation. However, in late 2012, on the recommendation of CalPERS's actuaries, the Board of Administration approved a re-pricing of monthly premiums which implemented an 85 percent increase in premiums for the subset of insureds who had Inflation-Protection, Lifetime benefits, or both, phased in two price increases to take effect in 2015 and 2016. The 85 percent increase was in lieu of a previously announced plan to subject a subset of insureds to annual 5 percent rate increases ad infinitum. Those rate increases were publicly announced in early 2013, and this suit was filed in August 2013.

[2] CalPERS changed the fine print of the contract in 2003 for new enrollees. The first form is called LTC1 by the parties, and the revised form is called LTC2. To the Court's understanding the legal issues discussed in this Draft Statement of Decision are controlled by identical language in the two forms.

Plaintiffs contend that the re-pricing was intended to create "shock lapse," a process by which insureds react to a drastic price change by dropping the coverage entirely or, as possible here under the EOC's terms, by converting to a less generous benefit package so that they can hold on to their current monthly premium and avoid the large price increase. The 2013 price increase caused: (a) a number of class members to drop their CalPERS Long-Term Care entirely, (b) a substantial number to convert away from Inflation Protection and/or Lifetime benefits to more basic coverage, and (c) a substantial number to pay the increased premiums to retain their coverage. The three class representatives chose Options (b) or (c).

A class of over 100,000 enrollees was certified by Judge Jane Johnson on January 28, 2016 on the contract claim and breach-of-fiduciary duty claim as against CalPERS and on a negligence claim against Co-Defendants Towers Watson & Co. and its affiliates, the actuaries when the CalPERS plan was first launched. Towers Watson & Co. settled with the class for $9,750,000, and final approval of this settlement was given by Judge Ann I. Jones (to whom the case had been reassigned upon Judge Johnson's retirement) on January 26, 2018. CalPERS's later motion to decertify the class was denied by Judge Jones on May 15, 2018. On April 4, 2019 this case was transferred to Judge William F. Highberger for trial.

Judge Jones had granted CalPERS's motion for summary adjudication in part on June 15, 2017, dismissing the fiduciary duty claim based on sovereign immunity. She ruled there was a triable issue of fact on the two class claims for alleged breach of contract. As noted above, this Court has, in the context of this trial on contract interpretation and not in the context of a motion for summary adjudication, agreed with CalPERS on one of the two contract issues, but also agreed with Plaintiffs on the "Inflation-Protection" premium issue.

It is notable that Sandra Smoley, then Secretary of the California Health and Welfare Agency and the State's "Honorary Chairwoman" for the marketing of this new product to state

employees, shared the view that this is what the EOC meant after being briefed by then CalPERS staff as to how to pitch the product to state workers. It is also notable that this Court (although not these Plaintiffs) believes that CalPERS could have implemented any number of general rate increases which did not single out the Inflation-Protection insureds, but that is not what has happened to date, particularly in regard to the challenged 2013 rate increase. "Could have" or "should have" is not the same as "what I actually did."

Plaintiffs have different theories for what recompense is due each of the affected subsets of the class, and Plaintiffs developed their theories and proof (primarily through forensic experts) at a time when they hoped to win on both contract theories. This bifurcated trial on contract interpretation issues has not given this Court an opportunity to pass on the correctness of some or all of Plaintiffs' theories of compensable damage. Plaintiffs' counsel has frankly recognized that their damages proof needs to be reworked in view of their loss on one of the two contract theories. There is no class representative who has claims typical of those who chose to lapse.

The Court is issuing this [Draft] Proposed Statement of Decision at this time because the parties are urged to contemplate the settlement option, which will necessarily involve the State's Executive branch, particularly the Department of Finance, and the Legislature. Since the enrollees in the certified class are all state and local employees, including teachers in the CalSTRS system (or close family members), there are many additional concerned stakeholders, including the labor organizations representing state and local employees and the state retiree associations.

Many of the outcomes which Plaintiffs and their counsel desire, e.g., reinstatement of lapsed policies, are only possible via a voluntary compromise since the only outcome of this case if it is litigated to closure is a money judgment against CalPERS and/or injunction regarding its future course of conduct in handling price increases for Long-Term Care coverage. The Court is

also hopeful that the parties herein via negotiation may be able to place the plan on a stable financial footing going forward and without need for a continuing annual state subsidy from the General Fund, if they can agree to a model for future price adjustments which is deemed a permissible interpretation of the relevant EOCs—as a matter of compromise only and not as a waiver of their current litigation position. If such a practical interpretation of the EOC's premium adjustment language was agreed by the parties, made part of the class notice of proposed settlement, and eventually given judicial approval as part of a Motion For Final Approval of class settlement, then CalPERS could proceed with the newly obtained peace of mind that future price increases consistent with the settlement's terms were subject to a "safe harbor."

Mindful that named Plaintiffs and their counsel have spent thousands of hours litigating this case for the last 70 months and approximately $2 million[3] in hard-dollar costs for forensic experts and on other litigation expenses, this case can only settle if CalPERS and the State find a way to make peace with the class and its counsel. While the Long-Term Care plan was indisputably authorized by the Legislature in 1995 on the theory that it would be self-sustaining and not a drag on the General Fund or public employers, there is a very serious risk that a money judgment for a rather large amount of money will be issued in due course in this case, given that this Court agrees with Plaintiffs that the "your premium will not increase as a result of . . ." language in the EOC (specific to Inflation-Protection coverage) creates a triable issue of fact as to whether or not the 2013 85 percent rate increase selectively imposed on Inflation-Protection insureds (and on Lifetime benefit insureds) was a breach of this promise. The plan currently has some substantial reserves (needed in the actuaries' view to pay foreseeable future claims) which could pay a money judgment in the near term, but doing so would then set the plan up for

[3] Approximately $1.5 million of this has been reimbursed by the Towers Watson settlement.

insolvency some time in the near future.

The plan by its inherent nature is intended to provide the peace of mind of guaranteed-renewable coverage for the lifetime of each insured so there are persons in the certified class with a foreseeable life expectancy of decades, not months or years. If such a person qualifies due to physical decrepitude for coverage at some future date before they die, they have a right to receive benefits (assuming they have continued to pay premiums). These obligations accrue monthly and extend out decades from today. An inability of this CalPERS plan to pay just claims will create an obvious default by an arm of the State in the fulfillment of its contract obligations. This, in turn, could seriously impair the credit rating of the State. If the case is not settled in the near term, a very large money judgment against CalPERS appears to be the most likely outcome. For this reason, the best path forward, in this experienced jurist's view, is for the parties to try to strike a deal which requires a one-time appropriation by the Legislature to resolve the pending suit while also providing a judicially-approved road map (as part of judicial approval of a class action settlement with due notice to the many class members of its terms) so that the plan is self-sustaining thereafter.

II. PROCEDURAL BACKGROUND

Although this case was originally filed on August 6, 2013, the parties stipulated to extend the five-year rule deadline to July 29, 2019, under C.C.P. § 583.310. The parties further filed a stipulation on or about June 3, 2019, in which it was agreed that when the parties, through their counsel, appeared before the Court on June 10, 2019, for the Bench Trial, regardless of whether a witness is sworn in at the Bench Trial, Plaintiffs' entire action, including claims to be tried before the Court and claims to be tried to a jury, and including all individual and Class claims, shall be deemed to have been brought to trial for the purpose of the five-year dismissal statutes

(Code Civ. Proc., §§ 583.310-583.360), as of June 10, 2019. The Court approved the stipulation and signed an Order to that effect.

Summary adjudication was granted on June 15, 2017 on the claims for breach of fiduciary duty (based primarily on sovereign immunity) and rescission (based on both sovereign immunity and that the purported claim was a remedy only, not a cause of action), but denied on the claims for breach of contract, breach of the implied covenant of good faith and fair dealing, and the related claim for declaratory relief.

Judge Jane Johnson, to whom the case was originally assigned from its inception, certified a plaintiff class (the "Class") on January 28, 2016, as to some but not all the claims pled. Notice was given to the certified Class in the summer of 2016 and the deadline to file a request for exclusion expired on October 14, 2016. The certified Class representatives are Holly Wedding, Eileen Lodyga, and Richard Lodyga. A total of 169 members opted out of the Class. A list of all of the individuals who timely requested exclusion is attached to the Judgment on Class Action Settlement between Plaintiffs and Towers Watson Defendants, filed January 31, 2018. In 2018, CalPERS moved to decertify the Class, which motion was denied on May 15, 2018 by Judge Ann I. Jones. CalPERS sought review from the Court of Appeal of the order denying its motion for decertification. CalPERS's writ to the Court of Appeal was denied on December 12, 2018. The only claim remaining certified for class treatment is the breach of contract claim.

The case was reassigned to Judge William F. Highberger on April 4, 2019, with a trial date of June 10, 2019.

Defendant CalPERS brought a motion to bifurcate (or more appropriately, "trifurcate") the trial as follows: (1) a court trial, without a jury, pertaining to contract interpretation as a matter of law ("Phase 1"); (2) a jury trial on CalPERS's affirmative defense of the statute of

limitations ("Phase 2"); and (3) if Defendant does not prevail as a matter of law in Phase 1, or on its statute of limitations defense in Phase 2, then a jury trial on the merits to determine if CalPERS breached the Evidence of Coverage and the amount of damages ("Phase 3"). On May 24, 2019, this Court granted CalPERS's motion, and trifurcated the trial into three phases, with the court trial on the first phase relating to contract interpretation beginning on the previously scheduled date of June 10, 2019.

On May 24, 2019 the Court also granted CalPERS's motion for leave to file a declaratory relief cross-complaint. After overruling Plaintiffs' due process objections to the cross-complaint, Plaintiffs filed their answer to the cross-complaint on June 5, 2019. The Court determined that Phase 1 of the trial also involves resolution of the sole legal issue framed by the cross-complaint.

The trial began on June 10, 2019 before Judge William F. Highberger, sitting without a jury. The court trial proceeded over the course of two court days from June 10, 2019 through June 11, 2019. Representing the Plaintiffs and the Class were Michael J. Bidart and Steven Schuetze from Shernoff Bidart Echeverria LLP, Gretchen Nelson and Gabriel Barenfeld from Nelson & Fraenkel LLP, Gregory Bentley and Clare Lucich from Bentley & More LLP, and Stuart Talley from Kershaw Cook & Talley PC. Representing Defendant CalPERS were Daralyn Durie, Ragesh Tangri, Michael Proctor, Allyson Bennett, Aaron Benmark, and Adam Brausa from Durie Tangri LLP, and Adam Thurston from Drinker Biddle & Reath LLP.

Following the submission of evidence, the Court directed Plaintiffs to prepare and file a [Proposed] Statement of Decision by June 19, 2019 and Defendant to respond to Plaintiffs' submission by June 25, 2019. Having considered all of the evidence and the credibility of the witnesses, the Court issues the following Statement of Decision in accordance with and pursuant to C.C.P.§ 632 and California Rule of Court 3.1590.

III. FACTUAL OVERVIEW

CalPERS, acting on permissive legislative authority granted by California Government Code §§ 21660–21661, started in 1995 to offer its public employee participants the elective right to buy Long-Term Care Insurance coverage for themselves and for family members, including parents and siblings, pursuant to the terms of an Evidence of Coverage document ("EOC"), which along with the application constitutes the terms of the written insurance contract for analytical purposes.

Under the legislative authorization, this product was to be financially self-supporting with no subsidies from the taxpayers or the public employers, although Government Code § 21664(f) provides that "[i]t is the intent of the Legislature to provide, in the future, appropriate resources to properly administer the long-term care program." Thus, premium rates charged and investment earnings are intended to cover actual expenses over the long haul. Similar to Long-Term Care Insurance products then being offered in the private marketplace, the monthly premium was highly dependent on the enrollee's age, aka "issue age," when coverage starts, with lower rates for younger enrollees reflecting the statistical likelihood that most such enrollees would have to remain covered by the plan (and paying premiums but not collecting benefits) for many years before their decrepitude in later years would possibly qualify them for benefits.

Further, a rather broad menu of alternative and cumulative types of benefits were offered with notably different monthly premiums reflective of the view at plan inception of the likely risks incurred by the plan. There were distinctions:

1. As between (a) the cheaper PERS Nursing Home/Assisted Living Facility Plan and (b) the more inclusive and more expensive PERS Comprehensive Plan, which included both institutional care and reimbursement for in-home assistance.[4]

[4] There was a third Plan, the PERS Partnership (Medical "Spend Down" Protection) which is not at issue here.

2. As between subsets under either the Nursing Home or Comprehensive Plan, a choice between (a) more expensive "Lifetime" benefits with no maximum payment cap and (b) cheaper alternative with a lifetime payment cap of $131,400 per enrollee.

3. As between (a) a premium pegged to daily benefits which were fixed in dollar terms with an option to increase the daily maximum of such benefits from time to time in the future in return for paying a higher premium at such later time ("Benefit Increase Option") and (b) an alternative (higher) premium at inception which would provide "Inflation Protection" whereby the daily benefit would escalate 5 percent a year, compounded, to anticipate the likely increase in the cost of obtaining such services in future years.

There were prior premium increases in the program.[5] The first general premium increase was implemented in 2003[6] where all members (including the Partnership Plans) received a premium increase ranging from 6 percent to 30 percent. The premium increases varied by the plan and benefits selected and the issue-age, with members in the plan who had a lower issue-age (typically between 34-55) with plans that had greater benefits (such as comprehensive with lifetime and inflation protection) receiving higher increases, while older members ages 75 and older (even those who also purchased the plans with the greatest benefits) were subjected to lower premium increases.

---

[5] CalPERS raised an affirmative defense based on the statute of limitations based on the earlier premium increases. This Court will separately address the statute of limitations defense in this Statement of Decision.

[6] LTC1 is the policy issued and sold from 1995 through 2002. LTC2 is the policy issued and sold from 2003 through 2004. The LTC3 policy, which is not at issue in this action, was issued and sold from 2005 through 2007. From 2008 to 2013, CalPERS did not issue or sell any long-term care policies. Starting in December 2013, CalPERS issued and sold the LTC4 policy. The first increase in 2003 was imposed on those existing members in LTC1, and presumably was incorporated into the rates for LTC2.

In 2007, there was a second premium increase as to all LTC1 and LTC2 policyholders (including the Partnership Plans).[7] As with the 2003 increase, the rate increases were differential in impact and ranged from 5 percent to 47.1 percent with those members who purchased lifetime and inflation protection receiving higher increases.

In 2010, there was a third premium increase. This increase applied to all LTC1 and LTC2 policies. Policies without inflation protection or lifetime benefits received a 15 percent increase, and those with either, or both, lifetime benefits or the inflation protection benefit received a 22 percent increase.

Starting in 2011, there was an annual premium rate increase of 5 percent that was applied to only those enrollees who purchased an LTC1 policy with both lifetime benefits and inflation protection.

These rate increases did not result in litigation. In October 2012, CalPERS approved an 85 percent rate increase, that was to be spread over two years (to take effect in 2015 and 2016), which would impact some, but not all, of the "coverages" offered. The 85 percent increase applied to any enrollee in LTC1 and LTC2 with either the Comprehensive or Nursing Home Plan who had signed up for either Inflation Protection or Lifetime benefits (or both). Conversely, an enrollee who had signed up for the least generous and least expensive plan for a capped benefit (e.g., $131,400) and no Inflation Protection would have no rate change.

IV. PHASE 1: COURT TRIAL ON CONTRACT INTERPRETATION

A. Issues to be Tried at Court Trial

There are three related questions of contract interpretation to be decided as questions of

[7] Although the LTC3 policy had been sold for a period of approximately two years at the time of the 2007 increase, those who purchased the LTC3 policy were not subjected to the 2007 increase.

law by the Court.

1. Do the terms of the provision in the EOC that has been called the "Guaranteed Renewal clause" allow for benefit-specific premium rate increases or must CalPERS implement any premium rate increase uniformly as to all enrollees in either LTC1 or LTC2?

2. Do the terms of the provision in the EOC that has been called the "Inflation Protection clause" allow for the imposition of premium rate increases insofar as such rate increases are needed to cover the cost of providing the annually compounded benefits provided by the Inflation Protection clause?

3. Do the terms of the Guaranteed Renewal clause in the EOC trump the terms of the Inflation Protection clause or vice versa?

B. The Contract and Extrinsic Evidence

The relevant text of the EOCs issued to policyholders in LTC1 and LTC2 pertaining to the Guaranteed Renewable clause and the Inflation Protection clause has never been modified at any time as to the over a hundred thousand individuals who purchased the LTC1 or LTC2 policies, whether they bought Comprehensive Coverage or Nursing Home Coverage. For these purposes, subject only to slight format variation, it is the same language.

In addition to the EOC, the integrated insurance contract includes the application and the Schedule of Benefits. As stated in the integration clause of the EOC, the application is part of the contract, and the Court has been provided a copy of Ms. Wedding's application form. The language of the form application is the same as to everybody in the certified Class for the entire period when enrollments were being accepted for LTC1 and LTC2. And then, necessarily, although it is more implied by the EOC than expressed, one must also take into account an

enrollee's schedule of benefits to know what the respective rights and responsibilities are pertaining to Class members.

The Court considered and evaluated extrinsic evidence offered by the parties during the trial. Such evidence included the Long-Term Care Letters issued by CalPERS, a Rate Sheet, Employer Manuals issued by CalPERS, Annual Letters to Policyholders from 1997-2011 from CalPERS regarding their Inflation Protection benefits, certain Board Meeting Minutes, and Letters to Policyholders pertaining to earlier premium increases, as well as marketing videos that were prepared and issued by CalPERS from 1995 to 2004. The Court also viewed videotape excerpts of the depositions of Ann Boynton, Eileen Tell, and Sandra Smoley.[8] In reviewing the extrinsic evidence, the Court gave the most weight to the Long-Term Care Letters, the Rate Sheets, and Sandra Smoley's testimony.

The Long-Term Care Letters were worthy of serious consideration. The application, which is a part of the integrated agreement, refers to the fact that "[t]he benefits and coverage options of the PERS plans are described in detail in the Long-Term Care letter."

A Rate Sheet was also admitted into evidence. (Exh. 109-002/003; see also Exh. 115-025 to 115-026.) The Rate Sheet was explained in the offered testimony of Ann Boynton, the designated Person Most Knowledgeable of CalPERS, and Eileen Tell, the designated Person Most Knowledgeable of the Long Term Care Group, which is a vendor that was retained by CalPERS to administer the long term care plan. Both Ms. Boynton and Ms. Tell testified that the Rate Sheet would have been included in the application kit. On the Rate Sheet, there is no language pertaining to CalPERS reserving the right to increase premiums. This was also confirmed by both Ms. Boynton and Ms. Tell in their testimony.

[8] The testimony of Richard Lodyga offered by CalPERS is excluded and not considered on the grounds such testimony is not relevant and further is simply the subjective understanding of a single policyholder.

In addition to the testimony of Ms. Boynton and Ms. Tell, the Court also heard the testimony of Sandra Smoley. From 1993 to 1999, Ms. Smoley was Secretary of the California Health and Welfare Agency, appointed by Governor Pete Wilson. Ms. Smoley supervised 42,000 people in a high position in the California state government and was designated as the honorary chairwoman of marketing of the Long-Term Care Program for CalPERS. She necessarily dealt with responsible officials of CalPERS and was put out in front of the State employees at the inception to try to generate enthusiasm in the program to increase sales of the policies.

This Court excluded the following evidence offered by Plaintiffs as not relevant: the EOC of LTC4 (Exh. 96), the Sample Memorandum described by Sandra Smoley (Exh. 123),[9] a compilation of documents from the enrollment period in 1997 (Exh. 152), and a 2011 Question and Answer guide for a Call Center (Exh. 1165). As to evidence offered by CalPERS, the Court excluded policies issued by other insurers,[10] including a MedAmerica Policy (Exh. 2308), and all evidence related to the 2013 85 percent rate increase, including the long-term care annual valuation reports. (Exhs. 2191, 2192, 2194, 2196, 2197.)

C. Applicable Law Governing Insurance Contract Interpretation

In deciding these questions, judicial construction of insurance contracts in California proceeds under a three-step process. (Croskey, et al., CALIFORNIA PRACTICE GUIDE—INSURANCE LITIGATION (Rutter 2019) ¶ 4:5 ("INSURANCE LITIGATION"), citing, *inter alia, AIU Insurance Co. v. Superior Court* (*FMC Corp.*) (1990) 51 Ca1.3d 807, 821-22.) The INSURANCE

[9] The Court has also excluded the memorandum based on CalPERS's authenticity objection.

[10] The exhibits were identified on CalPERS's Exhibit List as exhibits 2258, 2259, 2260, 2261, 2302, 2303, 2304, 2305, 2306, 2307, 2308, 2309, 2310, 2311, 2312, 2313, 2314, 2315, 2316, 2317, 2318, and 2319.

LITIGATION treatise describes this "basic framework" as having three steps:

- Rule No. 1—"Plain Meaning" Rule: First, an insurance policy is given its "plain Meaning": i.e., the terms must be read in their "ordinary and popular sense" in the context of the policy as a whole and the circumstances of the case. (*See* INSURANCE LITIGATION ¶ 4:6 ff; *Powerine Oil Co. v. Superior Court* (2005) 37 Cal.4th 377, 390.)
- Rule No. 2—"Objectively Reasonable Expectations of Insured" Rule: If the terms have no "plain meaning" and thus are ambiguous or uncertain, they must be interpreted in the sense the insurance company reasonably believed the insured understood them when the policy was issued; i.e., in accordance with the insured's "objectively reasonable expectations." (See INSURANCE LITIGATION ¶ 4:305 ff; *Bank of the West v. Superior Court* (1992) 2 Cal.4th 1254, 1264-65.)
- Rule No. 3—"Contra-Insurer" Rule: If the previous rule fails to resolve the ambiguity or uncertainty, it is to be resolved against the insurer as the drafter of the policy. (*See* INSURANCE LITIGATION ¶¶ 4:5; 4:405 ff; *Powerine Oil Co.*, 37 Cal.4th at 391.)

Within the three-step framework, there are additional rules that apply to insurance contract interpretation. First, if the policy provision is subject to more than one reasonable interpretation, it is ambiguous. To prevail, the insurer must establish its interpretation of the policy is the only reasonable one." (*Palp, Inc. v. Williamsburg National Insurance Co.* (2001) 200 Cal.App.4th 282, 290.) The Court is not "required, in deciding the case at bar, to select one 'correct' interpretation from a variety of suggested readings . . . even assuming the insurer's suggestions are reasonable interpretations which would bar recovery by the claimants, we must nonetheless affirm the trial courts' finding of coverage so long as there is any other reasonable interpretation which recovery would be permitted in the instant cases." (*MacKinnon v. Truck*

Insurance Exchange (2003) 31 Cal.4th 635, 655 (quoting *State Farm Mutual Auto Insurance Co. v. Jacober* (1973) 10 Cal.3d 193, 202-03).)

Second, *specific* provisions to a specific subject will govern with respect to that subject, even if there is a *general* provision that is broad enough to include the same subject. (*Kashmiri v. Regents of University of California* (2007) 156 Cal.App.4th 809, 834; *Kavruck v. Blue Cross of California* (2003) 108 Cal.App.4th 773, 781.)

Courts should also avoid construing insurance policies in a way that either ignores a clearly made distinction between terms or renders a term nugatory. (*See, e.g., Mirpad, LLC v. California Insurance Guarantee Ass'n* (2005) 132 Cal.App.4th 1058, 1070-72; *Foster–Gardner, Inc. v. National Union Fire Insurance Co.* (1998) 18 Cal.4th 857.)

Finally, "[t]he policy should be read as a layman would read it and not as it might be analyzed by an attorney or insurance expert." (*Crane v. State Farm Fire & Casualty Co.* (1971) 5 Cal.3d 112, 114.)

Extrinsic evidence can be used to show that the policy is subject to an interpretation at variance from its apparent plain meaning, if the latent ambiguity illuminated by such extrinsic evidence does not do violence to the written language of the contract. As the California Supreme Court stated in *Gribaldo, Jacobs, Jones & Assocs. v. Agrippina Versicherunges A.G.* (1970) 3 Cal.3d 434, 443, "[t]he test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible." (*Id.* (citations omitted).) Extrinsic evidence may be admissible to explain (but not vary) contract language, notwithstanding an integration clause in the policy. "Ordinarily, even in an integrated contract, extrinsic evidence can be admitted to explain the meaning of the contractual language, although it cannot be used to contradict it or

offer an inconsistent meaning. The language, in such a case, must be 'reasonably susceptible' to the proposed meaning." (*Hot Rods, LLC v. Northrop Grumman Systems Corp.* (2015) 242 Cal.App.4th 1166, 1175-76.)

Extrinsic evidence is generally admissible to establish the objective reasonable expectations of policyholders. "If the terms of a promise are in any respect ambiguous or uncertain, it must be interpreted in the sense in which the promisor believed, at the time of making it, that the promisee understood it." (*Bank of West v. Superior Court* (1992) 2 Cal.4th 1254, 1264-65.) "This rule, as applied to a promise of coverage in an insurance policy, protects not the subjective beliefs of the insurer but, rather, the objectively reasonable expectations of the insured." (*Id.*)

Extrinsic evidence that can be relevant to this inquiry has been held to include, *inter alia*, the original premium rates charged (*Golden Eagle Insurance Co. v. Insurance Co. of West* (2002) 99 Cal.App.4th 837, 849); and the manner in which the insurance policy was advertised or marketed. (*Kavruck*, 108 Cal.App.4th at 782.)

D. Issue 1: The Guaranteed Renewable Clause

The first provision which this Court must interpret is the scope of the Guaranteed Renewable clause in permitting premium increases. The Guaranteed Renewable clause states:

> **Your Coverage Is Guaranteed Renewable**
> **We** cannot cancel or refuse to renew **Your** coverage until benefits have been exhausted as long as **You** pay premiums on time. **Your** premiums will never increase due solely to a change in **Your** age or health. CalPERS can, however, change **Your** premiums, but only if **We** change the premium schedule on an issue-age basis for all similar coverage issued in **Your** state on the same form as this coverage. **We** must give **You** as least 60 days written notice before **We** change **Your** premiums. The premium for any increases in ***coverage*** which You voluntarily elect will be based on Your age at the time You elect the increase.

(Exh. 16-002 (underlined emphasis added as to the sentence at issue for interpretation;

bold emphasis in the original).)

On summary judgment, Judge Jones agreed with Plaintiffs' interpretation that "benefits" are not synonymous with "coverages." While there are many defined terms in the EOC, the words "coverage" and "benefits" are not amongst this universe of defined terms. In her ruling of June 15, 2017 on CalPERS's motion for summary judgment or summary adjudication, at footnote 11, Judge Jones stated that: "The distinction by Plaintiffs between 'coverage' and 'benefits' is a reasonable interpretation." Plaintiffs in their brief as well as during the Phase 1 Trial argued that the term "insurance policy" or "plan" is the term which best could be substituted for the term "coverage" in many parts of the EOC.

On May 24, 2019, this Court advised the parties that it would *sua sponte* reconsider Judge Jones' interpretation of the Guaranteed Renewable clause. This became the first issue to be determined by the Court in Phase 1 of the trial.

This Court considered the interpretation advanced by CalPERS that for purposes of interpreting the Guaranteed Renewable clause, the terms "coverage" and "benefits" were synonyms for analytical purposes, particularly since there was a 3:1 to 4:1 spread in the monthly cost of the least generous "benefit" package (aka "coverage") versus the most generous package. A reasonable interpretation is that the Guaranteed Renewable clause permitted selective pricing increases according to the nature of the specific risk(s) insured, whether the risk is termed a "coverage" or a "benefit." Judge Jones' reading of the key sentence negates any meaning to the phrase "same form as this coverage." The undefined word "coverage" is used twice in that sentence, suggesting that its first use refers to a potential subset of the universe of enrollees encompassed within the subsequent reference to "issued in your state on the same form as this coverage."

This Court recognizes in the first step of the three-step analysis, since two judges reading

the language reached different conclusions, that the interpretation of the provision cannot be resolved under the Plain Meaning Rule. Rather, this Court determines that CalPERS' interpretation prevails under Rule No. 2 — "Objectively Reasonable Expectations of Insured" Rule.

The language used shows that these were not identical risks pools subject only to enrollee-age risk variances. To force all enrollees to pay for the actuarial costs associated with a subset of the total risks would be unfair to the other enrollees not themselves the source of the cost increases. And, the Court finds that the objectively reasonable expectation of a policyholder would be to permit CalPERS to increase premiums based on such risk pools, unless expressly stated otherwise elsewhere within the policy.

E. Issue 2: The Inflation Protection Clause

The Inflation Protection clause is included in the section of the EOC titled "Benefit: Inflation Protection." (Exh. 16-017.) The Inflation Protection clause states, without any limitation or qualification limiting its scope:

> **Your Premium Will Not Increase[:]**
> **Your** premium will not increase as a result of these annual benefit increases.
>
> (Emphasis in original.)

Judge Jones in her summary judgment ruling stated that "the unambiguous terms of the EOC do not permit rate increases that are the 'result of' increasing benefits owed to policyholders who purchased inflation protection." (Order on Summary Judgment, June 15, 2017, at p. 12.)

This Court stated in its May 24, 2019 Order, and it repeated the statement at multiple hearings, that it was not inclined to reconsider Judge Jones's ruling as to the Inflation Protection

clause. CalPERS made a promise to anybody who saw fit to buy inflation protection that those rates would not increase as a direct result of the annual increases in potential daily/monthly benefit maximums provided by this benefit. Under the "Plain Meaning Rule," and reading the words as a layman would read the clause, CalPERS made an express promise in the EOC that premiums would not increase "as a result" of this intrinsic aspect of the inflation protection benefits. While there is some wiggle room for CalPERS to increase premiums paid by this group if it was for some other reason, the selective price increases imposed here on only Inflation-Protection insureds and Lifetime insureds (but not on all insureds) creates a triable issue of fact as to what, in fact, were CalPERS' reason(s) for imposing the premium increase. Only after a jury speaks will we know if the reasons were entirely acceptable, entirely unacceptable or a blend of the bad with the good.

In order to evaluate whether the Inflation Protection clause was susceptible to another reasonable interpretation, the Long-Term Care Letters are specifically referenced on the application. According to the testimony of Ms. Boynton and Ms. Tell, the Long-Term Care Letters were part of the Application Kit for enrollees. Ms. Tell testified that the Long-Term Care Letters were the "educational piece of the Application Kit." The Long-Term Care Letters graphically demonstrated a flat line to illustrate that premiums will not increase if the Inflation Protection was purchased; this Exhibit is so important that it is attached hereto as Exhibit A. (Exh. 115-006; Exh. 23-006; Exh. 187-015; Exh. 240-20; Exh. 34- 058.) In the Long-Term Care Letters, CalPERS consistently reiterated that premium rates would not increase if an enrollee purchased Inflation Protection. (Exh. 115-004; Exh. 5-003; Exh. 23-004 ("automatic inflation protection with rates that do not go up as your benefits increase"); Exh. 187-014 ("With this option, your premium is designed to remain level and won't increase even though your coverage amounts increase each year"); Exh. 240-018; Exh. 34-056 ("With this option, your premium is

designed to remain constant and will not increase even though your coverage amounts increase each year"); Exhs. 115-005 to 115-006 ("The plans with 'built-in' annual benefit increases will cost more on a monthly basis initially, but you lock in a rate now that is designed to remain level over the life of the plan and that won't rise simply with age); Exh. 115-017; Exh. 5-006; Exh. 23-017 ("Built-in automatic 5% annual increases with level premiums); Exh. 187-011 ("automatic 5% compound inflation built in at a level cost").) This extrinsic evidence is all consistent with the plain meaning of the Inflation Protection clause that premiums will not increase as a result of the inflation protection benefits.

Additionally, the Rate Sheets (Exhs. 109-002 to 109-003; 115-025 to 115-026) were included in the Application Kits according to Ms. Boynton and Ms. Tell. Although the Rate Sheet differentiates between the cost of purchasing and not purchasing Inflation Protection, there is no language on the Rate Sheet where CalPERS stated that it was reserving the right to increase premiums.

The Court also gives considerable weight to the testimony of Ms. Smoley, who was the Secretary of the California Health and Welfare Agency from 1993–1999, appointed by Governor Pete Wilson. Her testimony functions as a declaration against interest by CalPERS of what an objectively reasonable interpretation of the EOC would be based on her high government position and presumed sophistication and responsibilities specific to the marketing of the program to potential enrollees. Ms. Smoley came away with the impression that persisted for 20 years that rates would not increase, and testified it was "very definitely" her understanding that "the plans with built in annual benefit increases will cost more on a monthly basis initially but you lock in a rate now that is designed to remain level over the life of the plan that won't rise simply with age."

The extrinsic evidence outlined above all supports and is consistent with an interpretation

under the plain meaning of the Inflation Protection clause that the EOC does not permit rate increases that are as a result of increasing benefits owed to policyholders who purchased inflation protection. Whether a given rate increase does or does not violate this contract limitation in whole or in part is a fact question to be decided by a jury.

F. Issue 3: Specific Controls Over General

The last issue is whether the language of the Inflation Protection clause trumps the Guaranteed Renewable clause. Based on the Court's interpretation, the Inflation Protection clause carves an express exception to the general reserved rights stated in the Guaranteed Renewable clause. In other words, CalPERS is prohibited from increasing premiums as a result of inflation protection benefits, even if it has a general right to increase premiums based on different subsets and risk pools.

The Court agrees that the specific provision stated in the Inflation Protection clause controls over the general provision of the Guaranteed Renewable clause. Civil Code § 3534 states, "[p]articular expressions qualify those that are general." As stated in *Kashmiri v. Regents of University of California* (2007) 156 Cal.App.4th 809, 834, "under well-established principles of contract interpretation, when a general and a particular provision are inconsistent, the particular and specific provision is paramount to the general provision." In other words, "[i]n construing insurance contracts it is also settled that 'a specific provision relating to a particular subject will govern in respect to that subject, as against a general provision even though the latter, standing alone, would be broad enough to include the subject to which the more specific provision relates.'" (*Jane D. v. Ordinary Mutual* (1995) 32 Cal.App.4th 643, 651 (quoting *Southern California Edison Co. v. Harbor Insurance Co.* (1978) 83 Cal.App.3d 747, 759).)

G. Interpreting the Inflation Protection Clause, Causation, and Damages

The Court has determined that the terms of the Evidence of Coverage ("EOC") do not permit rate increases that are as a result of increasing benefits owed to policyholders who purchased inflation protection. The EOC provides no definition of the phrase "as a result of" as it is used in the Inflation Protection clause. The use of the term "as a result of" means that the inherent annual escalation of the daily maximum allowance for the Inflation Protection benefit could not, in and of itself, be "a factor" in increasing premiums, even in the presence of other factors. CalPERS asserts that the 2013 premium increase was primarily, if not exclusively, driven by a reduction in the actuarial assumptions for the rate of return on the plan's reserves, and this actuarial assumption is certainly not unique to escalating daily maximum inherent in the provision of Inflation-Protection benefits. Then again, faced with a revenue-shortfall problem that reached across all risk pools, CalPERS on the recommendations of its actuaries selectively imposed the needed rate increase on insureds with either Inflation-Protection or Lifetime benefits. At a minimum (and as previously found by Judge Ann Jones in denying summary adjudication) this raises a triable issue of material fact as to whether or not the disputed 2013 increase was imposed on this group of insureds on account of the cost of providing Inflation-Protection benefits.

The law is clear that "substantial factor" causation provides the proper standard. The EOC says that premiums would not increase "as a result of" the Inflation Protection Benefit. This phrase is synonymous with "because of." In *State of California v. Allstate Insurance Co.* (2009) 45 Cal.4th 1008, 1035, the Court explained that substantial-factor causation applied to insurance policies that promise indemnity for liabilities incurred by the insured "because of" property damage.

As stated in *Bruckman v. Parliament Escrow* (1987) 190 Cal.App.3d 1051: "The [trial]

court looked to section 999 of 5 Corbin on Contracts (1964) which cites *Krauss v. Greenbarg* (3d Cir. 1943) 137 F.2d 569, 572 as applying the substantial factor test to a breach of contract. Two other cases, *Nelson v. Lake Canal Co. of Colo.* (1981) 644 P.2d 55, 59 and *Reiman Assoc., Inc. v. R/A Advertising, Inc.* (1981) 102 Wis. 2d 305 [306 N.W.2d 292, 301] also apply Corbin's adoption of this test. [¶] We find the authorities cited persuasive." (*Bruckman,* 190 Cal.App.3d at 1063.)

Therefore, a premium-rate increase will be considered to be "as a result of" the Inflation Protection benefits if the inherent annual escalation of the daily/monthly maximum benefit amounts provided by the Inflation Protection Benefit was the cause, in whole or in part, of the disputed rate increase. The jury will be tasked to determine whether a breach occurred, and whether that breach caused damages, based on the above-described principles. The drafting of a Special Jury Instruction will occur later in the course of trial and/or trial preparation.

As to CalPERS's declaratory-relief Cross-Complaint, consistent with this Court's interpretation of the EOC, this Court finds that CalPERS cannot increase premiums specifically "as a result" of the increasing liabilities from the Inflation Protection Benefit's annual increase in the daily/monthly maximum allowable benefit, but the Court also finds that CalPERS can implement across-the-board increases which include Inflation Protection insureds as long as the reason for the increase is some matter of general applicability to all insureds; e.g., lower-than-anticipated lapse rates of all insureds, longer than expected longevity of all insureds, longer duration on claim by all categories of insureds, and/or a further change in the discount rate. To that extent the Court grants the requested declaratory relief sought by CalPERS in its cross-complaint.

///

///

V. PHASE 2: STATUTE OF LIMITATIONS

This Court issued the following tentative on June 8, 2019, and CalPERS submitted on the tentative. This tentative (which is set forth in full below) now becomes the order of the Court and part of this Statement of Decision:

Defendant CalPERS's Answer to the Corrected First Amended Complaint, filed on June 26, 2014 (and made applicable to the later-filed Second Amended Complaint per Stipulation and Order filed on March 4, 2019) includes the Statute of Limitations as the First Separate and Additional Defense. Plaintiffs and the certified class are proceeding to trial on a breach of contract claim only. As stated in the Answer, "Plaintiffs' second cause of action for breach of contract is barred by the four year statute of limitations set forth in California Code of Civil Procedure § 337 because Plaintiffs experienced rate increases in 2003, 2007, 2010, 2011, 2012 and 2013 . . . ." Defendant is now invoking both the four-year statute in C.C.P. § 337 and a one-year limitations set forth in Government Code § 911.2 even though no such affirmative defense is set forth in the operative pleading.

At the urging of Defendant and over Plaintiffs' objection, this Court severed this affirmative defense and set it for jury trial to follow the resolution of the Phase 1 Court Trial on contract interpretation issues. Exhibit Lists and Witness Lists for the Phase 2 jury trial have been filed, and the Court on June 11 will consider the Defendant's proposed Exhibits and Witnesses in conjunction with the Declaration of Michael Proctor and Exhibits 1-24 thereto, filed on June 7, 2019, in anticipation of the June 11 hearing to be its offer of proof on the statute-of-limitations affirmative defense. Counsel can supplement those items with an oral (or written) offer of proof on June 11 at the hearing if they want.

Under the authority of *Cottle v. Superior Court* (1992) 3 Cal.App.4th 1367, 1381 and *Lockheed Corp. v. Continental Insurance Co.* (2005) 134 Cal.App.4th 187, 211-12 (disapproved

on other grounds in *State of California v. Allstate Insurance Co.* (2009) 45 Cal. 4th 1008, 1036), a trial court managing a case deemed complex (as here) has inherent authority to conduct a hearing in advance of trial to determine if the parties have made a *prima facie* showing on each issue on which they have a burden of proof at trial. Defendant has the burden of proof of an affirmative defense, for which reason Defendant has been authorized to go first if this bifurcated defense is to be presented to a jury.

As correctly noted by Plaintiffs in their briefing in support of the "continuing accrual" theory of when the limitations period on Plaintiffs' and the certified Plaintiff Class's claims accrued and as explained more fully below, it is now obvious that any alleged prior breaches by CalPERS in raising Long-Term Care Plan premiums for LTC1 and LTC2 enrollees (or a subset of all such enrollees) in 2012 or in earlier years are irrelevant to the timeliness of the pending complaint (filed in August 2013) for disputed rate increases first demanded to be paid (in terms of due date of payment) in 2015. It is not legally possible for this Complaint to be untimely such that a statute of limitations defense could work. For this reason, there is no relevant admissible evidence which can be offered in support of this affirmative defense, and it would be a pure waste of citizen time to put twelve jurors in the box to hear an Opening Statement such that a Motion for Nonsuit under C.C.P. § 581c(a) could then be made. *See Atkinson v. Elk Corp.* (2003) 109 Cal.App.4th 739, 748-49, 757 (affirming dismissal of shingle purchaser's Song-Beverly Consumer Warranty Act claim on the Court's own motion prior to opening statement despite "irregular" procedure employed since plaintiff "would not have withstood a motion for nonsuit after opening statement as to the Song-Beverly causes of action.").

When contracts call for multiple payments, e.g., a lease or insurance contract, California case law is well settled that each such payment obligation gives rise to a separate cause of action with its own limitations period. One consequence is that stale, prior breach events fall outside the

realm of recoverable damages since the earlier breaches each triggered a series of separate limitations periods. See generally, B. Witkin, CALIFORNIA PROCEDURE (5th ed.), "Actions" § 520:

> (4) *Severable Contract.* When a contract is severable, the duty to perform each part arises independently and the statute begins to run on the severable obligations from the time the performance of each is due. (*See Lee v. De Forest* (1937) 22 C.A.2d 351, 360, . . . [deficiency in monthly rental was recoverable under terms of lease after lessor's lease to new tenant]; *Trigg v. Arnott* (1937) 22 C.A.2d 455, 459, . . . [installment note]; *Tillson v. Peters* (1940) 41 C.A.2d 671, 674, . . . [rent due under lease]; *Carrasco v. Greco Canning Co.* (1943) 58 C.A.2d 673, 675, . . . [monthly salary increase]; *Conway v. Bughouse* (1980) 105 C.A.3d 194, 200, . . . [buy-sell agreement with monthly payments for life]; *White v. Moriarty* (1993) 15 C.A.4th 1290, 1299, . . . [promissory note]; 51 AmJur.2d (2011 ed.), Limitation of Actions § 145.

In addition to the many authorities cited by Witkin's authoritative treatise, there are many newer cases to the same effect. (*See, e.g., Tsemetzin v. Coast Federal Savings & Loan Ass'n* (1997) 57 Cal.App.4th 1334, 1344 ("It is settled in California that periodic monthly rental payments called for by a lease agreement create severable contractual obligations where the duty to make each rental payment arises independently and the statue begins to run on such severable obligations from the time performance of *each* is due.").) In the context of an Unfair Competition Law claim arising from a contractual relationship, our Supreme Court approved and applied the continuing accrual theory in *Aryeh v. Canon Business Solutions, Inc.* (2013) 55 Cal.4th 1185, 1200-01:

> By its nature, the duty Canon owed—the duty not to impose unfair charges in monthly bills—was a continuing one, susceptible to recurring breaches. Accordingly, each alleged breach must be treated as triggering a new statute of limitations. (*Hogar Dulce Hogar v. Community Development Commission*, *supra*, 110 Cal.App.4th at p. 1295 ["When an obligation or liability arises on a recurring basis, a cause of action accrues each time a wrongful act occurs, triggering a new limitations period."]; see *Armstrong Petroleum Corp. v. Tri-Valley Oil & Gas Co.*, *supra*, 116 Cal.App.4th at pp. 1388–1391 [treating each disputed monthly bill as triggering a new statute of limitations]; *Tsemetzin v. Coast Federal Savings & Loan Assn.*, *supra*, 57 Cal.App.4th at p. 1344 [same].) Aryeh cannot recover alleged excess charges preceding the four-year limitations

> period, but is not foreclosed from seeking recovery for charges to the extent they fall within that period. Because the complaint alleges excess charges within the four years preceding suit, it is not completely barred by the statute of limitations.

Here the disputed breach is not non-payment by the customer or promisor. Rather, it is the alleged breach by Defendant CalPERS of the contractual promises allegedly made in the EOC regarding when and if premium increases could be imposed on enrollees. At a minimum, each rate increase was a severable contract event for accrual purposes whether or not one slices the claims so finely that each monthly payment demand is itself a severable alleged contract violation. Since the disputed 85 percent rate increase was first demanded (in terms of due date) in 2015—AFTER this suit had been filed in August 2013—the only thing that could be said about the timeliness of this suit is that it was arguably premature, which is not, however, a valid statute of limitations defense.

None of Defendant's arguments can overcome the brute force of the well-settled authority. For example, *Jozovich v. Central California Berry Growers Ass'n* (1960) 183 Cal.App.2d 216, cited by CalPERS at pg. 11 and also cited by K. Banke and J. Segal, CALIFORNIA PRACTICE GUIDE: CIVIL PROCEDURE BEFORE TRIAL, STATUTES OF LIMITATIONS ¶ 3:61 (a text cited in turn by CalPERS) is a good example of a contract which was NOT divisible even though installment payments (i.e., progress payments) were involved. There the plaintiff machinery manufacturer promised to build a "revolutionary" strawberry freezing machine in 1954 for defendant for $21,454.09 with plaintiff retaining patent rights. Defendant was to pay in two payments, and the legal question was whether the payment obligations were severable. In holding that they were not since they both related to the delivery of a machine which would work as promised (regrettably not what happened), the Court there correctly held that the payment obligations were interrelated and NOT divisible. That is entirely different from the question of whether one premium increase in violation of a contract thereafter privileges the same party to

commit future premium increase breaches, particularly when the challenged increase is exponentially larger than the earlier breaches. That this is a breach of contract claim against a government Defendant, as compared to a private party, does not change the analysis (even assuming the state can put Plaintiffs to the test of making their own showing of timely compliance with Government Code § 911.2).

The portion cited by CalPERS from *Coe v. Farmers New World Life Insurance Co.* (1989) 209 Cal.App.3d 600, 606 at pg. 11 of its brief for the proposition that "Insurance contracts, on the other hand, have generally been held to be indivisible" is factually inapposite. The question there was whether a spouse/beneficiary could claim on a life insurance policy which was expressly canceled by the insured when a renewal premium was otherwise with the former insured thereafter dying during what otherwise would have been a 30-day coverage-extension grace period following non-payment. In holding that the express cancellation had legal effect such that the grace period was inapplicable, the court was not analyzing anything remotely similar to the question of sequential breaches, and the following complete quote from *Coe* shows the case has no persuasive effect since the context is entirely different:

> The sections in American Jurisprudence Second on cancellation of insurance policies similarly do not mention new consideration. The requirement is that "cancellation . . . be by the consent of the parties, express or implied from the circumstances . . . ." (43 Am.Jur.2d, Insurance, § 415, p. 483.) "Whether cancellation by mutual agreement has been effected depends on the intention of the parties as evidenced by their acts, conduct, and words, taken in connection with the attendant circumstances. There must be a meeting of minds, or mutual assent, to constitute a valid cancellation, and each party must act with knowledge of the material facts." (*Id.* at § 416, p. 484.)
>
> Why is it that consideration is not required to support the new agreement reflected by cancellation? Perhaps it derives from unique qualities inherent in the insurance contract. Williston confirms that consideration is necessary in the inception of the insurance contract (7 Williston, Contracts (3d ed. 1963) § 907, pp. 308-309), but then elaborates on the special terms of the contract as follows: "*What is the nature of the insured's obligation to pay premiums under a policy of life insurance? Can he be sued in debt for failure to pay his premiums as they fall due? All courts agree that he cannot; he has nowhere in his application or policy*

> *promised to pay premiums. What then is the nature of the insurance company's promise?* Although there is respectable authority to the contrary, the great weight of authority holds that a contract of insurance is a single, indivisible agreement of the company **for the agreed period of time, subject to defeasance or 'lapse' by the occurrence of the condition subsequent—the insured's refusal or failure to pay a premium when due."** (*Id.* at § 907, p. 311.)
>
> The insurance contract, then, is a continuing obligation by the insurance company to pay benefits, subject to the unilateral power of termination by the insured. The insured is free to terminate by failing to make premium payments. He is also free to terminate or "cancel" by any means provided in the policy or by local statute or common law. Cases considering the insured's unilateral and unfettered power of termination emphasize this right.

(209 Cal.App.3d at 606-07 (emphasis added).)

The 118-year old precedent in *McMaster v. New York Life Insurance Co.* (1901) 183 U.S. 25, cited by CalPERS at pg. 11, is another grace-period death case and equally inapposite to the present issue. There the insured paid a one-year premium up front on a policy with a one-month grace period (subject to an interest charge on the unpaid premium) if there was a failure to timely pay a renewal premium. The actual squabble which the court had to resolve involved the issuance date of the policy since some notes indicated that the insured and/or the local agent wanted it back-dated to December 12, but the company in fact issued the policy at headquarters on December 18. The carrier had denied the claim, claiming that December 12 of year two was the premium due date, not December 18. The insured in fact died on January 18, i.e., the very last day of the one-month grace period if the issuance date controlled (as stated expressly in the written policy) since he had not, in fact, paid the renewal premium (but he had also not expressly canceled the policy). The Supreme Court ruled for beneficiary and against the carrier. The full sentence shows that this case stands for nothing more than the proposition that the life insurance contract would remain in effect "subject to forfeiture by failure to perform." To be clear, the complete sentence reads:

> The contracts were not assurances for a single year, with the privilege of renewal from year to year on payment of stipulated premiums, but were entire

> contracts for life, **subject to forfeiture by failure to perform the condition subsequent of payment as provided**; or to conversion in 1913 at the election of the assured.

(183 U.S. at 35 (emphasis added).)

The last citation for the legally erroneous assertion that "Insurance contracts, on the other hand, have generally been held to be indivisible" is merely to an unpublished decision of a United States District Court in North Carolina and does not merit any further comment.

On June 10, 2019, Defendant CalPERS advised the Court that it was submitting on the Tentative. The Court hereby adopts its tentative ruling and strikes Defendant's First Affirmative Defense based on the statute of limitations and finds for Plaintiffs and against Defendant as a matter of law as to Defendant's First Affirmative Defense.

VI. CONCLUSION

The Court rules for Plaintiffs on the interpretation of the "Inflation-Protection" clauses in the EOC and for CalPERS on the premium-adjustments permitted by the "Guaranteed Renewable" clauses (subject, however, to the override of the Inflation-Protection promise where the two terms appear to conflict). The Court agrees with CalPERS on the Cross-Claim for Declaratory Relief that CalPERS can subject insureds with Inflation-Protection benefits to future rate increases (and retroactive rate increases which are less than the disputed 85 percent increase actually imposed) insofar as CalPERS can persuade the fact-finder (now or in future litigation) that such rate increases are driven by cost factors other than the inherent escalation of daily/monthly limits on Inflation-Protection benefits over time as long as those increases are spread over the entire risk pool and not selectively imposed to a greater-than-average degree on the Inflation-Protection insureds.

Objections to this Proposed Statement of Decision[11] must be served and filed within fifteen (15) calendar days plus two (2) court days for e-service from this date.[12]

A Trial-Readiness Conference is set for August 21, 2019 at 10:00 a.m. with Joint Report due August 19, 2019. Final Status Conference set for October 3, 2019 at 10:00 a.m. Jury Trial (10 days) set for October 30, 2019 at 10:00 a.m. If the parties are making any progress with their settlement negotiations, the Court will be cooperative in continuing the trial date.

Dated: July __, 2019

Hon. William F. Highberger
Judge of the Superior Court

[11] The Court intends to receive further briefing from counsel on this Draft before an "Official" Proposed Statement Of Decision is filed. The timeline set forth here will run from the issuance and filing of the "Official" Proposed Statement Of Decision.

[12] See n. 11 above regarding how time calculation will run. It does NOT run from July 1, 2019.

you lock in a rate now that is designed to remain level over the life of the plan and that won't rise simply with age. In the long run, automatic inflation protection is both more predictable and probably more cost effective. You get guaranteed annual increases of 5 percent in both the benefits and coverage of your plan. And, the 5 percent annual increases in coverage continue even if you begin to receive long-term care—when you need the protection the most.

Periodic Upgrades

Your second option is to "upgrade" your coverage on a regular basis to keep benefits up with the rising cost of care. Under this option, PERS will offer you an opportunity every three years to purchase additional coverage at an additional premium. As long as you regularly take advantage of each opportunity offered to upgrade your coverage, and you are not already receiving benefits under the plan, you will not have to undergo any medical exams to be eligible to increase your coverage.

The cost of each upgrade will be based on your age at the time you elect to increase your coverage. Because rates for older individuals are significantly higher and you will be older when each upgrade is offered, each upgrade you accept will result in higher additional premium payments. The advantage of the periodic upgrade option is that your monthly cost for your plan will be much lower initially than if you had chosen to build in inflation protection. However, in the long run you could end up paying quite a bit more to protect your benefits against inflation because of the additional premium payments required to purchase each upgrade.

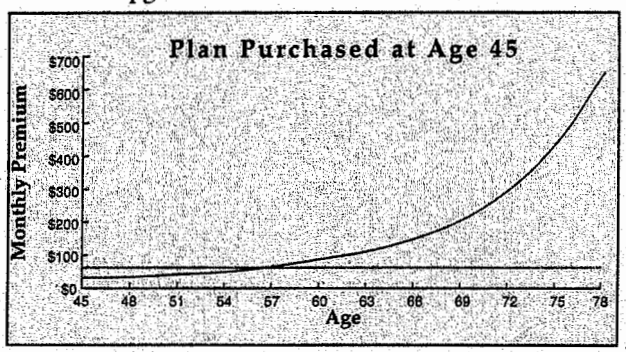
This option also provides less complete protection against spiraling costs in the long run because you will not be eligible to increase your coverage once you begin to receive benefits. Therefore, the periodic upgrade option is designed for people who are prepared to pay out-of-pocket to supplement the plan benefits if they need care for a long period of time, since coverage cannot be increased once benefits begin. So, this option is only suitable for people who expect to have increasing income or assets or reduced financial obligations in the future. Please refer to page 15 for a summary of the inflation protection options.

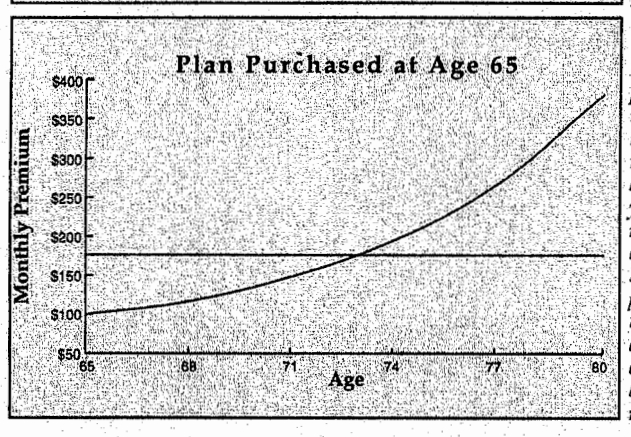
John Jones, Senior Transportation Planner, California Department of Transportation, PERS member.

"I've been amazed to see how the rates have increased in just three years. My mom was paying $82 a day three years ago and the rates are now up to $100 a day—15 percent is a phenomenal increase as far as I'm concerned. If you need care 15 years from now and the prices have doubled, you'll end up taking money out of your own pockets."

The graphs below illustrate how monthly premiums for plans purchased at age 45 or 65 will differ over time for the periodic upgrade option (black line) vs. the automatic inflation protection option (blue line). The monthly premiums for the periodic upgrades rise over time (as each offer is accepted) while premiums for plans with automatic compound inflation protection are designed to remain level.

Periodic Upgrade vs. Automatic Inflation Protection





The charts are for illustration only. Premiums for periodic upgrades depend upon the amount of additional coverage offered, the rates in effect at the time of the upgrade offer, and the number of upgrade offers accepted. The monthly premiums shown are for the PERS Comprehensive Lifetime coverage plan. These premiums assume periodic upgrades in coverage will be offered and accepted every three years, the coverage increases will be equivalent to 5 percent compounded annually, the premium increases will be based on current rates, and benefits do not begin until age 80.