# Murchison & Cumming

# TRENDS

**Third Quarter, 2004**

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## CASUALTY & COVERAGE

### COURT OF APPEALS HOLDS THAT UNDER EMINENT DOMAIN ACTION THE COST OF REPAIR REDUCED FROM THE MARKET VALUE OF PROPERTY IS NOT "DAMAGES" UNDER INSURANCE POLICY

**FACTS:** Plaintiff owned real property which the City of Long Beach sought to acquire by the power of eminent domain. The city offered Plaintiff just compensation for the property, which reflected the cost to remediate environmental problems with the property. Plaintiff disputed the city's assessment of fair market value and the cost to remediate. Parties eventually settled on the amount paid to Plaintiff. During this time, Plaintiff tendered defense of the eminent domain action to three insurance carriers which declined to defend the action. Plaintiff argued the remediation costs were "damages" and the action was a "suit" or "claim" for "damages" under her policy.

**PROCEDURAL HISTORY:** Plaintiff appeals from summary judgment entered for Defendants. Judgment affirmed.

**ISSUE:** Where there is neither a "suit" nor a "claim" for "damages" under a liability policy, such as in an eminent domain action to determine environmental remediation costs, is there any duty to defend?

**HOLDING:** No.

**ANALYSIS:** First, the Court restated the precedent case that an insurer owes a broad duty to defend its insured against claims that create a potential for indemnity, or damages, within the coverage of a policy. [See Montrose Chemical Corp. v. Superior Court, 6 Cal.4th 287 (1993)]. However, the court noted that such duty may exist at the beginning of a suit where coverage may be in doubt and ultimately may not develop. But where there is a question whether facts establish a duty to defend, such doubts are to be resolved in favor of coverage and in the insured's favor. [See Montrose, supra.].

Plaintiff argued that the eminent domain action was a claim for damages because the city was reducing the market value of her property by the costs of remediation. The court disagreed with Plaintiff's application of the term "damages." The court reasoned that since Plaintiff was not obligated to compensate the city in money [but was actually the opposite] as a result of any *loss or detriment* suffered by the city, which would have been considered a form of "damages", and since there was nothing in her policies that would give an insured an expectation of coverage for "simple diminution" of market value of property, the court found that Plaintiff suffered no damages under the policy. Therefore, liability policies that do not insure against a diminution in market value due to environmental conditions of property do not constitute "damages" under the policy and as such, there is no duty to defend.

*Block v. Golden Eagle Ins. Corp.,* 121 Cal.App.4th 186 (2004).

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## CALIFORNIA SUPREME COURT CLARIFIES AND LIMITS APPLICATION OF BRANDT FEES IN BAD FAITH ACTION

**FACTS:** The plaintiffs successfully sued Allstate for bad faith in the handling of their insurance claim. The jury awarded plaintiffs $3,594,600 in compensatory damages, $5,000,000 in punitive damages and $1,193,533 in Brandt fees. Allstate contended that the trial court erred by calculating the Brandt fees as a percentage of the overall compensatory damage award, rather than as a percentage of only that portion of the award that represented lost benefits on the insurance policy

**PROCEDURAL HISTORY:** Allstate appealed the judgment as it pertained to the awarding of Brandt fees.

**ISSUE:** Where the successful plaintiff in an insurance bad faith action has a contingency fee arrangement with its attorney, how are Brandt fees determined?

**HOLDING:** The trial court must allocate the amount to be awarded as Brandt fees by apportioning the number of hours spent on the case as a whole vis-à-vis the contract cause of action.

**ANALYSIS:** Although each party to a suit must pay his own attorney fees, an exception was noted in the Brandt case with respect to insurance bad faith cases. There, if an insurer fails to act in good faith when discharging its responsibilities under an insurance contract, the insurer may be liable to pay the attorneys fees incurred to vindicate the insured's legal rights under the insurance policy. These must be distinguished from attorneys fees for the bringing and prosecution of the bad faith action itself, which remain subject to the general rule that each party is responsible for their own attorneys fees. Thus, the fees recoverable cannot exceed the amount attributable to the attorneys efforts to obtain the rejected payment due on the insurance contract. In this particular case, the plaintiffs had a 40% contingency fee agreement with their attorney. Nothing in the agreement differentiated between recovery on the tort vs. contract causes of action. Thus, Allstate argued that the Brandt fees awarded should have been 40% of the amount due under the contract of insurance ($40,856.40) or a total of $16,342.56. Plaintiffs argued that all of the fees awarded were proper because all of the causes of action were inextricably bound in the litigation. The Court rejected both proffered methods of calculation. With respect to Allstate's argument, the Court noted that nothing in Brandt limits the amount of fees awarded as damages to a percentage of the contract benefits. The amount "attributable to the attorneys efforts" to recover contract benefits could certainly exceed the amount of those benefits. However, that does not mean that the lower courts were correct in awarding over $1 million in Brandt fees. It would be inconsistent with fees. It would be inconsistent with Brandt to permit plaintiffs to recover, in a mixed contract/tort case, the majority of their attorneys fees attributable to the entire compensatory damages award. The proper method of allocation in a mixed action requires the trial court to determine the percentage of the legal fees paid to the attorney that reflects the work attributable to obtaining the contract recovery. No portion of legal fees attributable to punitive damages may be recoverable. The Brandt fees can never exceed the legal fees for the combined tort and contract recovery. To determine the percentage of legal fees attributable to the contract recovery, the trial court should determine the total number of hours an attorney spent on the case and then determine how many hours were spent working exclusively on the contract recovery.

*Cassim v. Allstate Insurance Co.* 33 Cal.4th 780 (2004)

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# COURT OF APPEALS HOLDS THAT CIGA MAY NOT REDUCE PAYMENTS TO AN INSURED BY AMOUNTS PAYABLE UNDER SSDI AND CALIFORNIA'S UNEMPLOYMENT COMPENSATION INSURANCE BENEFITS

**FACTS:** Plaintiff, Jocelyn Cole, was insured by, and made a claim against, National Auto and Casualty Ins. Co., which was a member of the California Insurance Guarantee Association (CIGA) for an automobile personal injury. However, during the claim National became insolvent and CIGA took over the defense of the covered claim pursuant to Ins. Code section 1063. Plaintiff had also been collecting federal SSDI benefits and state UCI benefits during this time. CIGA maintained it could offset its payout to Plaintiff against her SSDI and UCI benefits. CIGA also claimed that Plaintiff was required to exhaust her SSDI and UCI benefits before she could recover under CIGA.

**PROCEDURAL HISTORY:** The trial court held for defendant. Plaintiff appeals. Judgment reversed.

**ISSUE:** May federal disability and state unemployment benefits be credited or offset against payment of a motorist's claim by the CIGA?

**HOLDING:** No.

**ANALYSIS:** The court first analyzed the statute to find that CIGA only pays "covered claims". And under the statute dealing with offsetting covered claims, section 1063 provides that a person's right of recovery for covered claims under governmental insurance must first exhaust her right under the program. However, the statute expressly does not include any obligation arising disability insurance which is not a covered claim. The court read the statute narrowly to find that it does not include offsetting claims for any governmental program available, but only for specific claims. Therefore, CIGA cannot cover or credit all forms of insurance but only those where the loss falls within the definition of "covered claim".

The court reasoned that nothing in the policy provides for unemployment compensation arising out of a disability and that SSDI and UCI do not give compensation for bodily injury if one is able to work. Thus, the motorist claim by Plaintiff was not covered by "any other insurance" under the statute and therefore, the court held that because both SSDI and UCI are disability insurance, they may not be credited against Plaintiff's recovery.

*Cole v. California Insurance Guarantee Association*, ---Cal.App.4th--- (2004)

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## COURT OF APPEAL HOLDS THAT INSURER WAS NOT ESTOPPED FROM INVOKING STATUTE OF LIMITATIONS ON A NEW CLAIM AFTER IT HAD SETTLED THE ORIGINAL CLAIM

**FACTS:** The plaintiff made an earthquake claim under her property insurance policy with Allstate. The claim was limited to damage to the roof and chimney of plaintiff's home. Allstate paid the claim in February, 1990. In November of 1992, plaintiff asked Allstate to re-open the claim. The trial court held that the one year statute of limitations for an action seeking recovery on an insurance claim expired in February 1991.
**PROCEDURAL HISTORY:** Plaintiff appealed the trial court's ruling which barred her claim on the grounds of the statute of limitations.

**ISSUE:** Was the insured's claim barred by the one year statute of limitations, despite the failure of the insurer to advise of the statute?

**HOLDING:** Yes

**ANALYSIS:** The California Supreme Court has held that the one year limitations period begins running at the "inception of the loss" but is equitably tolled from the time that the insured gives notice of the damage to his insurer until coverage is denied. This is to avoid penalizing the insured for the time consumed by the insurer investigating the claim, while preserving the central idea that an insured will only have 12 months to institute suit. Plaintiff here argued that because Allstate did not deny her claim, nor send her an unequivocal statement that the claim was closed, the statute was tolled even after she had received payment on the claim. The court rejected this argument, holding that nothing justifies a judicial extension of the equitable tolling rule to create a right to reopen claims that have been paid. If an insured is unsatisfied with a settlement, the tolling of the limitations period during the claims investigation process provides the insured with ample opportunity to press a further claim. If an insured has a bona fide claim that was not discovered before the expiration of the limitations period, the right to bring suit is preserved by the delayed discovery rule. The court of appeal also held that the trial court correctly ruled that Allstate was not estopped to deny coverage because it had failed to inform her of the statute of limitations. Plaintiff had no earthquake claim pending with Allstate for over a year after the original claim was paid. Allstate could hardly have been expected to advise her of the statute of limitations.

*Marselis v. Allstate Ins. Co.* 121 Cal.App.4th 122 (2004)

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# COURT OF APPEAL FINDS DUTY TO DEFEND INSURED IN SUIT ALLEGING SALE OF SUBSTANDARD PARTS

**FACTS:** The insureds were manufacturers of parts used in municipal water systems. In the underlying suit, various municipalities alleged injury to their water systems and lead contamination of water resulting from substandard parts sold by the insured. The suits alleged that the plaintiffs would have to replace nearly 300,000 of the insured's parts to protect the water supply and the health/welfare of the water customers. In addition, plaintiffs sought damages for the cost of replacing the parts, plus other monetary damages. The insured tendered the suits to its CGL carrier, under a policy in which the carrier promised to pay sums that the insured became legally obligated to pay as damages because of covered "bodily injury" or "property damage". "Property damage" was defined as "physical injury to tangible property" or "loss of use of tangible property". The policy also contained various exclusions pertaining to damage to the insured's own product. Zurich refused to defend the insured, asserting that the damages claimed were strictly economic and not due to "bodily injury" or "property damage", and that the product exclusions applied. The insured sued for bad faith and breach of contract. The insured filed a motion for summary adjudication as to the duty to defend.

**PROCEDURAL HISTORY:** The trial court granted the motion for summary adjudication. The court found that the underlying action sought damages for physical injury to municipal water and to parts not supplied by the insured, including costs for investigation, correction, abatement, monitoring and public education regarding lead contamination. Zurich appealed.

**ISSUE:** Did the trial court correctly hold that the underlying action stated a covered claim of "property damage", potentially covered under the Zurich policy?

**HOLDING:** Yes

**ANALYSIS:** Zurich argued that the underlying action sought merely prophylactic remedies. However, the court noted that the complaint itself alleged that water customers have been damaged because of the exposure to lead, and implicitly that the parts are leaching lead into the municipal water supplies. As such, the alleged damages were not merely prophylactic because they address harm which is already occurring, not just harm that might occur. By alleging that their water supply is contaminated with lead, the plaintiffs have claimed covered property damage. Preventing releases that have not yet occurred or caused harm is different from stopping releases that already are occurring and causing harm. The former is prophylactic; the latter is remedial and results in costs that constitute covered damages. Zurich also argued that there was no covered "property damage" since the plaintiffs did not claim physical injury to other parts of the munipal water system. The court rejected that argument, relying on the principle announced in Armstrong World Industries and other cases, namely, that the incorporation of a hazardous product into a larger system may constitute "property damage". Moreover, the plaintiffs alleged structural problems due to the use of substandard parts. Lastly, the court rejected application of the policy's exclusions for damage to the insured's own product and the impaired property exclusion – the complaints alleged physical injury to their water systems through the incorporation of the insured's parts.

*Watt Industries v. Zurich* --- Cal.App. 4th ---, WL 2053276 (2004)

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## GENERAL TORTS

### COURT OF APPEAL HOLDS THAT INDEMNITY CLAIM REQUIRES PREDICATE TORT

**FACTS:** Plaintiff and a school district entered into a contract whereby the plaintiff agreed to prepare architectural drawings for and supervise construction of a high school. The District also entered into contracts with general contractors. The District sued the architect for breach of contract and professional negligence, alleging that after construction was completed, the general contractor submitted a claim for more than $11 million, citing delays and disruptions from the architect's defective design. The District settled that action. The architect filed a cross-complaint against the general contractors, alleging in a negligent claim that they breached their standard of care in the construction of the structures. It further alleged that these deficiencies caused the delays and disruptions which led to the underlying dispute between the District and the general contractor. The architect also sought implied equitable indemnity, apportionment of fault/contribution and declaratory relief. The defendants each filed a demurrer to the complaint, arguing that the negligence claim failed to state a cause of action because they (the general contractors) owed no duty to the architect in connection with plaintiff's obligations to the District. They further argued that the equitable causes of action were based on the invalid negligence claim and cannot stand alone. Finally, they argued that the economic loss doctrine applied.

**PROCEDURAL HISTORY:** At the demurrer hearing, plaintiff agreed with the court's tentative ruling that the negligence cause of action failed because of the economic loss doctrine. The court granted the demurrers on the ground that the equitable claims failed because they were purely derivative of the invalid negligence cause of action. Plaintiff appealed.

**ISSUE:** Can a party seek equitable indemnity without pleading an underlying tort?

**HOLDING:** No

**ANALYSIS:** The doctrine of equitable indemnity only applies among defendants who are jointly and severally liable to the plaintiff. It can apply to acts that are concurrent or successive, joint or several, as long as they create a detriment caused by several actors. However, there must be some basis for tort liability against the proposed indemnitor, generally based on a duty owed to the underlying plaintiff. Thus, in this case, plaintiff had to show that the defendants owed a duty to the district. The plaintiff's own complaint was fatal. It alleged that the defendants breached their duties to the District by failing to comply with the terms of their contracts, an allegation which the court said was not a cognizable claim on which to base equitable indemnity. A person may not recover in tort for the breach of duties that merely restate contractual obligations. The only allegations of defendants' misconduct were based on their alleged breach of contract, which was an improper attempt to recast a breach of contract cause of action as a tort claim.

*BFGC Architects Planners, Inc. v. Forcum* 119 Cal.App.4th 848 (2004)

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# COURT OF APPEALS HOLDS THAT PRIOR OWNER OF PROPERTY IS NOT LIABLE FOR INJURIES CAUSED BY A DEFECTIVE CONDITION AFTER RELINQUISHING OWNERSHIP AND CONTROL OF PROPERTY

**FACTS:** Plaintiff was injured in 2000 while working as a contractor on real property that Defendant owned eight years prior to Plaintiff's injury in 1992. Defendant motioned for summary judgment based on fact that other entities had owned the property since 1992 and Defendant did not "own, lease, rent, maintain, manage, supervise, and operate" the property where the incident occurred in 2000. Plaintiff claimed Defendant created the defect causing his injury. Defendant claimed even if it had created the defect, as a predecessor owner or real property, it is not liable to third parties injured by a defective condition on the property after it is sold.

**PROCEDURAL HISTORY:** Plaintiff appeals from summary judgment for Defendant. Judgment is affirmed.

**ISSUE:** Is a prior owner of real property liable for injuries caused by a defective condition on the property long after the owner has relinquished ownership and control of it, even if the prior owner negligently created the condition?

**HOLDING:** No.

**ANALYSIS:** The court began its analysis with the question, whether former owners, who may have been negligent in their former ownership of real property, should be subject to liability for injuries sustained on the property long after they have relinquished ownership and control of it? The court answered no, subject to certain conditions. [See Preston v. Goldman, 42 Cal.3d 108 (1986), Lorenzen-Hughes v. MacElhenny, Levy & Co. 24 Cal.App.4th 1684 (1994)].

Plaintiffs argued that the personal injury was due to a latent defect in a pipe that burst, and was not controlled by Preston. But the court did not distinguish between a patent defect, which is one that is discovered by inspection as would be made while exercising ordinary care and prudence, or a latent defect, which is one that is hidden and would not be discovered by reasonable inspection. The court focused on the exception to the general rule to injuries on the land where an owner is under a duty to disclose hidden defects which he knows or should know would present a risk of harm to persons on the premises, and which the owner anticipates will not be discovered. Here, no facts showed Defendants knew or should have known of such hidden defects long after selling their property and as such, the general rule of non-liability applies.

*Lewis v. Chevron USA Inc.,* 119 Cal.App.4th 690 (2004)

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# COURT OF APPEALS HOLDS THAT PROPERTY OWNERS OWE DUTY OF CARE REGARDING OPEN AND OBVIOUS DANGERS AND MAY BE SUED FOR PREMISES LIABILITY FOR RESULTING INJURY TO VISITORS

**FACTS:** Plaintiff was walking to defendant's premises and crossed the sidewalk adjacent to defendant's driveway where water was present on the ground. Plaintiff slipped and fell between the two areas. In Plaintiff's deposition, Plaintiff stated she had seen the water on the ground before she stepped on it. Defendant maintained 1) that it had no duty to maintain the sidewalk unless it created the dangerous condition, which it claimed it did not do, and 2) that it had not duty to warn plaintiff of the water because it was an open and obvious condition.

**PROCEDURAL HISTORY:** The trial court granted defendant's motion for summary judgment on ground of 1) and 2) above. Plaintiff appeals. Judgment reversed.

**ISSUE:** Since a landowner is not under a duty to *warn* of an obvious danger, if the danger is *foreseeable*, is he under a duty to *remedy* the danger?

**HOLDING:** Yes.

**ANALYSIS:** The court reasoned that, ordinarily, the obviousness of a condition excuses the potential duty of a landowner to warn of the condition. However, modern and controlling law on the subject is that if the danger is foreseeable that it may cause injury, even though it may be obvious to one encountering it, there may still be a duty to remedy the danger, and a breach of that duty can form the basis of liability. [See Osborn v. Mission Ready Mix, 224 Cal.App.3d 104 (1990), Beauchamp v. Los Gatos Golf Course, 273 Cal. App.2d 20 (1969)].

The court found that even though the slippery condition on the driveway may have excused defendant from warning of it, it was still predictable and foreseeable that despite the "constructive warning", the wet cement would still attract pedestrian use. Therefore, defendant was under a duty to remedy that condition.

*Martinez v. Chippewa Enterprises, Inc.,* 121 Cal.App.4th 1179 (2004)

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# COURT OF APPEALS HOLDS THAT BUILDING OWNERS CAN RECOVER IN NEGLIGENCE FOR FAULTY DESIGN AND ENGINEERING OF CONTRACT-ORS THAT CAUSES DAMAGE ONLY TO REPAIRED PART OF BUILDING

**FACTS:** This is a construction defect case where building owner plaintiff's apartment building was damaged and partially collapsed in the 1994 Northridge earthquake. Plaintiff hired contractors to repair and reconstruct their earthquake damaged building and alleged that such repair, design, engineering, and construction of their building was itself defective thus, causing damage to the property.

**PROCEDURAL HISTORY:** Trial court granted defendant's demurrers to Plaintiff's complaint for the cause of action for negligence. Plaintiff appealed. Judgment reversed.

**ISSUE:** Can property owners recover for the negligence of building contractors whose faulty design and engineering caused damage only to the repaired part of the building?

**HOLDING:** Yes.

**ANALYSIS:** The court relied upon Aas v. Superior Court, 24 Cal.4th 627 (2000) in its holding. There, the court held that where construction defects have not actually caused any property damage, a homeowner cannot recover damages in negligence from a contractor or subcontractor. But here, defendants asked that damage must be to property "other than" the property they defectively repaired, based upon the theory that damage caused by defective products is recoverable, but damage to the product itself is not. Thus, defendants wanted protection for their own repairs and for the repairs to be considered a product. However, the court disagreed and stated that this is not a defective product case but rather a construction defect case which arises from negligent engineering and design services. Thus, product liability cases that require damage to "other" property, and do not allow recovery for damage to the defective product itself, do not apply here. Here, where defects ripen into property damage, property owners can recover for damages where such defective design and engineering results in physical damage to the repaired structure.

*Naum Shekhter v. Seneca Structrual Design,INC.*, 121 Cal.App.4th 1055 (2004)

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## PROFESSIONAL LIABILITY

### COURT OF APPEAL HOLDS THAT COUNSEL WHO INADVERTENTLY RETAINED AN EXPERT WITNESS WHO HAD BEEN HIRED AS A CONSULTANT BY THE OPPOSING PARTY SHOULD NOT HAVE BEEN DISQUALIFIED

**FACTS:** The plaintiff was a client of an attorney in a personal injury case. The attorney hired an expert witness in the area of windshields. Unbeknownst to the attorney, that same expert had been retained as a consultant a year earlier by the defendant's counsel in the same case. He provided the defendant's counsel with his thoughts on the case. When plaintiff's counsel contacted that same expert about serving as an expert witness, the expert did not disclose his prior hiring by the defense counsel – he later indicated that he had forgotten about it. The expert shared little information with plaintiff's counsel. After plaintiff's counsel disclosed the expert through discovery, defendant's counsel moved to disqualify plaintiff's counsel on the grounds that counsel had wrongfully communicated with the expert witness.

**PROCEDURAL HISTORY:** The trial court granted the motion to disqualify plaintiff's counsel. Plaintiff appealed.

**ISSUE:** Must an attorney for a party be disqualified from a case when it accidentally designates an expert previously retained by the opposing party?

**HOLDING:** No – automatic disqualification is not necessary.

**ANALYSIS:** Disqualification of opposing counsel is authorized when it would protect an opposing party from the unfair use of confidential information against that party. A motion to disqualify must be balanced with the right of a client to choose counsel of its choice. In the present action, plaintiff's counsel had no notice of the expert's dual status until defense counsel raised the issue. When the dual role was revealed, plaintiff's counsel ceased all contact with the expert. No confidential information originating with the defendants or their attorneys was transmitted by the expert to plaintiff's counsel. The court pointed out that there was not "the slightest hint" that the expert had disclosed a secret attorney-client privilege. As such, disqualification of counsel was not proper. Counsel was innocent of wrongdoing when it hired the expert and acted ethically after the issue was discovered.

*Collins v. State of California* 121 Cal.App.4th 1112 (2004)