

Key Decisions

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An Indemnity Agreement In A Construction Contract Gave Rise To A Duty To Defend

Crawford v. Weather Shield Manufacturing, Inc.

(*Cal. Sup. Ct.*), filed July 21, 2008, published July 22, 2008

Key Facts

J.M. Peters Co. (JMP) was the developer, builder, and general contractor of a large residential project. Weather Shield Manufacturing Co., Inc. (Weather Shield), contracted with JMP to manufacture and supply wood-framed windows for the project. In the contract, Weather Shield promised (1) "to indemnify and save [JMP] harmless against all claims for damages . . . loss, . . . and/or theft . . . growing out of the execution of [Weather Shield's] work," and (2) "at [its] own expense to defend any suit or action brought against [JMP] founded upon the claim of such damage[,] . . . loss or theft."

Owners of homes in the project brought construction defect actions, naming JMP, Weather Shield, and others. JMP cross-complained against the subcontractors on the job. It sought defense and indemnity.

JMP, and all the subcontractors except Weather Shield and the framing contractor, settled before trial. The cross-complaints against the settling subcontractors also settled.

The window leak and framing issues went to trial against Weather Shield and the framing

contractor. The Framing contractor was found liable. Weather Shield was found not liable.

JMP's cross-complaint against Weather Shield was tried separately. JMP sought both (1) express indemnity for amounts paid to the homeowners in settlement, and (2) under the duty-to-defend provisions of Weather Shield's subcontract, attorney fees and expenses incurred by JMP in defending itself against the homeowners' suit.

The trial court ruled that since the jury found Weather Shield was not liable, the subcontract did not require it to indemnify JMP for amounts paid to the homeowners. However, the court concluded, the subcontract still made Weather Shield responsible for JMP's legal defense against the homeowners' claims, insofar as those claims concerned the windows supplied by Weather Shield.

Since 70% of the money JMP paid in settling the homeowners' claims was for window problems, the trial court awarded it 70% of its total attorneys' fees. The trial court also awarded JMP its attorney's fees on the cross-complaint.

The Court of Appeal affirmed.

Holding & Reasoning

The California Supreme Court granted review, but limited that review to a single issue: Did a contract under which a subcontractor agreed "to defend any suit or action" against a developer "founded upon" any claim "growing out of the execution of the work" require the subcontractor to provide a defense to a suit against the developer even if the subcontractor was not negligent?

It held that in the context of a construction defect action, the provisions of a pre-2006 res-

idential construction subcontract that obligated a subcontractor to indemnify the developer-builder, also obligated the subcontractor to defend the developer-builder. The Court reached this holding even though (1) the parties interpreted the subcontract as giving the builder no right of indemnity unless the subcontractor was actually negligent, and (2) a jury ultimately found that the subcontractor was not negligent.

Subject to public policy and established rules of contract interpretation, the parties to a contract have great freedom to allocate responsibility for indemnity and the cost of defense as they see fit. They can agree that the promisor's indemnity and/or defense obligations will apply only if the promisor was negligent, or, conversely, even if the promisor was not negligent.

In general, an indemnity agreement is construed under the same rules as govern the interpretation of other contracts. However, indemnity agreements in the form of insurance policies are interpreted differently from other contracts. For example, ambiguities in a policy of insurance are construed against the insurer, who generally drafted the policy, and who has received premiums to provide the agreed protection.

In the context of an insurance contract, the insurer/indemnitor is usually in the superior bargaining position and forces the insured/indemnitee to accept its terms and language. Thus, courts tend to interpret insurance contracts in favor of coverage.

In the context of other contracts, the *indemnitee* often has the superior bargaining position and uses this to shift responsibility for its own legal fault to another. Courts tend to interpret

noninsurance contracts against “coverage.” Moreover, statutory law imposes some absolute limits on the enforceability of noninsurance indemnity agreements in the construction industry.

Civil Code section 2778 sets forth general rules for the interpretation of indemnity contracts, “unless a contrary intention appears.” The statute provides that a promise of *indemnity* against claims, demands, or liability “embraces the *costs of defense* against such claims, demands, or liability” insofar as such costs are incurred reasonably and in good faith. The statute also specifies that the indemnitor “is bound, on request of the [indemnitee], to *defend* actions or proceedings brought against the [indemnitee] in respect to the matters embraced by the indemnity,” though the indemnitee may choose to conduct the defense. And, the statute declares that if the indemnitor declines the indemnitee’s tender of defense, “a recovery against the [indemnitee] suffered by him in good faith, is conclusive in his favor against the [indemnitor].” However, if the indemnitor was not provided reasonable notice of the action, or was not allowed to control the indemnitee’s defense, recovery by the third party against the indemnitee is only presumptive evidence against the indemnitor.

Turning to the specific contract, the Court held the provisions “expressly, and unambiguously, obligated Weather Shield to defend, from the outset, any suit against JMP insofar as that suit was ‘founded upon’ claims alleging damage or loss arising from Weather Shield’s negligent role in the . . . project.” Thus, “Weather Shield thus had a contractual obligation to defend such a suit even if it was later determined, as a result of this very litigation, that Weather Shield was not negligent.”

According to the Court:

A contractual promise to “defend” another against specified claims clearly connotes an obligation of active responsibility, from the outset, for the promisee’s defense against such claims. The duty promised is to render, or fund, the service of providing a defense on the promisee’s behalf — a duty that necessarily arises as soon as such claims are made against the promisee, and may continue until they have been resolved. This is the common understanding of the word “defend” as it is used in legal parlance.

This interpretation is supported by the fact that Section 2778, which applies in the absence of a contract to the contrary, does not impose a duty to defend from the outset.

The Court noted:

Parties to an indemnity contract can easily disclaim any responsibility of the indemnitor for the indemnitee’s defense, or the costs thereof. Short of that, they can specify that the indemnitor’s sole defense obligation will be to reimburse the indemnitee for costs incurred by the latter in defending a particular claim. However, the instant subcontract did neither. On the contrary, it specified that Weather Shield would be required, “at [its] own expense,” to “defend” JMP against suits “founded upon” claims arising from Weather Shield’s performance of its subcontract. This language indicated a more immediate obligation, one that would necessarily arise before the litigation to be defended could determine whether Weather Shield owed indemnity to JMP.

Weather Shield cited authorities that did not persuade the court. Several authorities had addressed indemnity duties, not defense obligations, and the court believed another was wrongly decided.

The Court then addressed Weather Shield's public policy arguments. The primary one was that "Large builders and developers use their superior bargaining power, and self-drafted contract terms, unfairly to shift the financial consequences of their own legal liability to faultless subcontractors, who are not compensated for the risk and agree only because they need the work." The vice, argued Weather Shield and amicus curiae, is that as a result, developers don't feel the need to exercise proper care in overseeing a project. Further, the subcontractors may not be able to fund the developers' defense while defending themselves, often against both the plaintiff and the developer.

Although the Court acknowledged the arguments, it found that the particular contract was so explicit and clear that it could not simply rewrite the contract. And, it noted that Weather Shield was not a small, naive subcontractor who did not know what it was signing and was powerless to negotiate the terms.

Analysis

This decision could minimize the distinction between subcontractor insurers who issue additional insured endorsements in favor of owners, developers, or general contractors, on the one hand, and subcontractor carriers who do not issue additional insured endorsements, on the other. Conceivably, subcontractors will have a "duty to defend" the developer or general contractor in more situations, and conceivably, the subcontractors' insurer could end up

contributing to the developer or general contractor's defense whether or not an additional insured endorsement has been issued in favor of the developer or general contractor.

It is important to note that this decision does not answer a long list of questions that are sure to arise in its wake. Issues that may arise include:

(1) Will subcontractors be treated worse than liability insurers with respect to issues that are typically controlled through detailed policy language or even special statutes such as Civil Code section 2860? Issues such as responsibility for "pre-tender" fees, selection of defense counsel and control of defense, input into settlement negotiations, hourly rates of defense counsel, and related issues may arise.

(2) Will subcontractor liability insurers end up paying to defend developers and general contractors even when no additional insured endorsement exists? In other words, will a subcontractor's contractual defense obligation be interpreted as involving "liability because of property damage" that would be "covered" under the subcontractor's liability insurance policy? Particularly since the subcontractor is required to defend even in situations where the subcontractor has not acted negligently or caused any property damage, one could argue that the subcontractor's agreement to fund the developer or general contractor's defense merely involves economic loss.

(3) Even assuming that the subcontractor's liability insurer ultimately becomes responsible for the subcontractor's agreement to provide a defense, when does that responsibility mature? It would seem that the subcontractor's liability insurer would, at most, pay for the

subcontractor's share of the developer or general contractor's defense at the conclusion of the lawsuit, as part of the insurer's duty to indemnify. Of course, subcontractors and developers and general contractors will want to argue that the carrier should be obligated to pay the subcontractor's share of the defense obligation on an ongoing basis.

(4) What are the consequences of subcontractors' breach of the contractual agreement to defend?

These questions and many others may surface as courts and litigants grapple with the impact of the Crawford decision in construction defect litigation and in other types of situations involving indemnity agreements.

This opinion appears in the July 22, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 11114.

Employers Merely Need to Provide — Not Ensure — Meal And Rest Periods

Brinker Restaurant Corp. v. Superior Court (Cal. Ct. of App., 2d Dist.), filed July 22, 2008, published July 23, 2008

Key Facts

Brinker operates many California restaurants, such as Chili's and Macaroni Grill. California's Division of Labor Standards Enforcement (the DLSE) investigated Brinker from 1999 to 2001. In 2002, the DLSE sued Brinker. Brinker settled the suit, paying \$10,000,000 in connection with charges involving alleged failures to provide unpaid meal periods and periodic rest breaks. Meanwhile, the purported class action lawsuit was filed on behalf of Brinker employees. The

purported class action alleged that Brinker had failed to provide meal periods for non-exempt employees who worked shifts that exceeded five hours, failed to provide a second meal period when the workday exceeded ten hours, improperly required "early lunching," required off-the-clock work and unlawfully altered employee time records.

The trial court granted plaintiffs' motion for class certification. The plaintiffs' motion emphasized the availability of computer records and statistical evidence and what were described as Brinker's "corporate policies."

Among Brinker's many arguments against certification was the argument that it only had to provide meal and rest periods, and did not have to actually ensure that employees actually took breaks or stopped working in order to eat lunch. Brinker also argued that any claim involving off-the-clock work would be subject to individualized proof, making the class action procedure inappropriate. The trial court granted the motion for class certification, reasoning that "common questions regarding the meal and rest period breaks are sufficiently pervasive to permit adjudication in this one class action."

Brinker filed a writ petition.

Holding & Reasoning

The appellate court issued the writ and ordered the trial court to reverse its decision. The decision includes several important holdings on substantive issues of California employment law. First, the court rejected the DLSE's interpretation of how often rest breaks were required. According to the court, "it is only when an employee is scheduled for a shift that is more than three and one-half hours, but

less than four hours, that he or she is entitled to a rest break before the four hour mark.”

Next, the appellate court rejected the plaintiffs’ argument that Brinker policies that allowed “early lunching” meal periods taken early in the employee’s shift, rather than during busier time periods during the middle of an employee’s shift, was unlawful. The appellate court directly held that there was no law that prohibited employees from taking meal periods early in their shifts.

Next, the appellate court held that Brinker satisfied its legal obligations by providing employees with the opportunity to take unpaid meal breaks. The law did not require Brinker to force employees to take meal breaks. According to the court:

“Public policy does not support the notion that meal breaks must be ensured. If this were the case, employers would be forced to police their employees and force them to take meal breaks. With thousands of employees working multiple shifts, this would be an impossible task. If they were unable to do so, employers would have to pay an extra hour of pay anytime an employee voluntarily chose not to take a meal period, or to take a shortened one.”

Analysis

This decision is important, both from the standpoint of substantive employment law, and from the standpoint of class action procedure. Substantively, the court recognized the business realities that confront restaurants whose employees would want to be actively working during busy time periods so that they can earn

maximum tips. By articulating a rule that required employers to provide employees an opportunity to take meal breaks and rest periods, but did not require employers to force employees to take breaks or eat lunch, the court also recognized the reality that employers cannot efficiently police a large number of employees under the normal circumstances that confront many businesses on a day-to-day basis.

From the standpoint of class action procedure, the court emphasized that trial judges must consider the merits of claims plaintiffs make against defendants in class action contexts when ruling on class certification issues. If class certification is divorced from the elements of the plaintiffs’ claim, the trial judge is not in a position to meaningfully assess whether issues can effectively be tried on a class-wide basis. Here, the availability of computer records or statistical evidence was not enough to overcome the fact that substantively speaking, the reason a particular employee did not take a break or meal period would ultimately involve an individualized assessment of that particular employee’s circumstances on that particular occasion. As a result individualized issues predominated, and the class action procedure was not an efficient means of resolving these issues.

This opinion appears in the July 23, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 11267.

Underinsured Motorist Status Is Determined Based On A Comparison Of The Policy Limits, Not On What A Victim Actually Receives

Explorer Insurance Company v. Gonzalez (Cal. Ct. of App., 3d Dist.), filed July 16, 2008, published July 17, 2008

Key Facts

Dwayne Gonzalez was injured in an automobile collision caused by Benjamin Fernandez.

Fernandez was insured under a Fireman's Fund Insurance Company policy that covered liability "arising out of the use of his automobile with combined single limits in the amount of \$100,000.00 for all bodily injury and property damage caused by any single accident." Gonzalez was insured by an Explorer Insurance Company policy that included uninsured and underinsured motorist benefits of \$100,000 for all damages from bodily injury sustained by any one person in any single accident.

Fireman's Fund paid Gonzalez \$21,584.11 for property damage and \$78,415.89 for bodily injuries arising from the collision, exhausting the limits of its policy.

Gonzalez then made a claim under the underinsured motorist coverage of his policy for \$21,584.11. That represented the difference between the \$78,415.89 he received from Fireman's Fund for bodily injuries and the \$100,000 limit of his underinsured motorist coverage.

Explorer denied the claim, concluding it did not qualify as an underinsured motorist claim because Fernandez's \$100,000 combined single limit for liability coverage policy afforded

bodily injury limits of up to \$100,000 and was, therefore, not less than the underinsured motor vehicle bodily injury liability limits of the Explorer policy.

In the ensuing litigation, the trial court held that because the Fireman's Fund policy had limits of \$100,000, which could be applied to Gonzalez' bodily injuries, Fernandez was not underinsured. Therefore, Explorer had no duty to make any payment under its policy.

Holding & Reasoning

The Court of Appeal affirmed. It held:

As did the trial court, we conclude the underinsured coverage of the injured person's policy was not triggered in this circumstance. This is so because the tortfeasor's policy covered damages for bodily injury up to \$100,000 if there is no property damage—such as if the tortfeasor hit a pedestrian rather than another car as occurred in this case. Thus, it cannot be said that the tortfeasor's policy was for an amount less than the \$100,000 bodily injury coverage of the underinsured motorist provision in the injured person's policy. In other words, the comparison in coverage is based on the potential for recovery, not what is actually recovered in a particular case.

Analysis

California courts continue to use a comparison of policy limits approach to determine whether at-fault drivers should be considered "underinsured" for purposes of underinsured motorist coverage. This approach typically means that if the at-fault driver's limits and the injured

insured's limits are equal (or if the at-fault driver's limits are higher), there is no underinsured motorist claim, even if the insured actually recovers less than the limits. Because the determination is made by comparing policy limits, the particular facts and circumstances of the accident become largely irrelevant to the analysis.

California courts have used this approach since at least the early 1990's, when *State Farm Mutual Auto Ins. Co. v. Messinger*, 232 Cal.App.3d 508 (1991) was decided. Under this approach, if the available liability insurance limits equal or exceed the uninsured motorist limits, there is no underinsured motorist claim to be made. By focusing on a comparison of policy limits, the actual facts and circumstances of the particular accident become largely irrelevant. In accidents that involve multiple injury victims or so-called "single limit" policies, there is usually some possibility that the insured will not receive an amount of money that equals his or her uninsured motorist limit. Nevertheless, there is no underinsured motorist claim to be made unless the tortfeasor's liability limits are less than the insured's uninsured motorist limit.

This opinion appears in the July 17, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 10896.

An Insurer Had A Duty To Defend An Insured Who Intentionally Threw The Claimant Into A Swimming Pool But Did Not Intend To Throw Him On The Concrete Step

State Farm Fire & Casualty Company v. Superior Court
(Cal. Ct. of App., 2d Dist.), filed June 26, 2008, published June 30, 2008

Key Facts

Jeffrey Lint and Joshua Wright were at a party. During the evening, the two began to argue. After an exchange of words, Wright went outside. Lint followed Wright, grabbed him, picked him up, and threw him into the shallow end of the swimming pool. Wright landed on the pool's concrete step, which was not covered by water. Wright sustained a fractured right clavicle and was hospitalized for approximately four days.

Lint apologized to Wright. Wright reported that, after the incident, Lint told him that Lint had not meant to hurt him. Wright characterized the incident as "horse-playing around." In a recorded statement Lint said, "if I wanted to hurt this guy . . . I would have just hit him, but I didn't want to hurt him."

Lint's parents had a State Farm homeowners' insurance policy. Lint was an insured under this policy. The policy covered "damages because of bodily injury . . . caused by an occurrence . . ." The policy defined "occurrence" as "an accident, including exposure to conditions, which results in: a. bodily injury; or b. property damage . . ." The policy excluded from coverage, "[B]odily injury . . . (1) which is either expected or

intended by the insured; or (2) which is the result of willful and malicious acts of the insured[.]”

Lint tendered the claim to State Farm. State Farm refused to defend or indemnify him. It relied on the requirement that there be an “occurrence” or “accident,” asserting that there was no accident because Lint intended to throw Wright into the pool.

In the ensuing coverage litigation, the trial court found that State Farm had a duty to defend. State Farm sought review by way of a petition for a writ of mandate.

Holding & Reasoning

The Court of Appeal rejected State Farm’s request for relief. It concluded that there had been an “occurrence.” It reasoned that Lint had intended to get Wright wet, not to hurt him and that Lint had merely miscalculated how far he had to throw Wright.

Although State Farm cited numerous cases holding that where the conduct is deliberate or volitional, the incident is not an “accident” for the purposes of insurance law, the court noted that “the term ‘accident’ has also been used to refer to the unintended or unexpected *consequence* of the act.” It explained:

The following paradigms are illustrative: During a pick-up baseball game, a batter hits the ball with the intention of sending it into deep right field for a homerun. But, because of the batter’s stance and the angle of contact with the ball, the batter sends the baseball in a trajectory that breaks a window in foul territory. The batter deliberately

hit the ball and intended that it move far and fast. It cannot be said that this batter intended to cause the property damage, i.e., to hit a foul ball and break the window. This was an accident because one aspect in the causal series of events -- too much force at an inadvertent angle leading to the broken window -- was unintended by the batter, and as such was fortitious. In the second example, an intentionally speeding driver negligently hits another car. The speeding was an intentional act; but, “the act directly responsible intended by the driver and resulting in injury would be deemed an accident.” (*Merced Mutual Ins. Co. v. Mendez*, supra, 213 Cal.App.3d at p. 50.) In these examples, the conduct resulting in harm was intended but the ultimate result was not because the actor mistakenly miscalculated the physics involved. (See *Lyons v. Fire Ins. Exchange* (2008) 161 Cal.App.4th 880, 888.)

The circumstances here, based on the complaint and the undisputed facts discovered by State Farm, parallel the baseball batter, the egging in *National American Ins. Co.*, the speeding driver in posited by *Merced Mutual Ins. Co.*, and the drilling company in *Meyer*. Although he deliberately picked Wright up and threw him at the pool, Lint did not intend or expect the consequences, namely, that Wright would land on a step. Lint miscalculated one aspect in the causal series of events leading to

Wright's injury, namely, the force necessary to throw Wright far enough out into the pool so that he would land in the water.

The court distinguished cases that involved sexual harassment or sexual assault. It described other cases as being ones in which "the insured intended all of the acts in the causal chain, including the injury."

Analysis

Case law concerning the accident requirement has become increasingly difficult to reconcile. In cases involving issues as diverse as trespass, alleged sexual assault, deliberately inflicted injuries allegedly undertaken in self-defense, and alleged horseplay, courts have grappled with difficult distinctions that make a one-size-fits-all rule extremely difficult to articulate in a way that reasonably governs the virtually infinite variety of factual circumstances that can arise.

The California Supreme Court is currently evaluating the accident requirement in the context of alleged self-defense. Perhaps the Supreme Court's opinion will add clarity to a concept that has been increasingly problematic.

This opinion appears in the June 30, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 9798.

A Plaintiff Seeking To Establish A Duty Of Care Must Remember To Articulate Specific Preventive Measures That Are Not Unduly Burdensome

Garcia v. Paramount Citrus Association, Inc. (Cal. Ct. of App., 5th Dist.), filed July 21, 2008, published July 22, 2008

Key Facts

Salud Andrade was a crew supervisor for a farm labor contractor. Andrade had a crew picking oranges on the Burdick Ranch, which was adjacent to Paramount Citrus Association's Abercrombie Ranch. Andrade had delivered a forklift to his crew and was going to another crew's worksite. Andrade cut through the Abercrombie Ranch on one of its private roads.

Access to the road was usually blocked by cables. However the cables were lowered on days Paramount Citrus Association's workers needed access to the property. The cables had been lowered for such access on the day in question.

As Andrade went from Abercrombie Road onto the public roadway, he rammed a van in which Garcia and other farm workers were being transported to a worksite. Garcia was severely injured.

Garcia sued Paramount Citrus Association and others. He asserted Paramount Citrus Association owed a duty to him and others to place a warning on its private road alerting drivers to the approaching intersection with the public road. He alleged Paramount Citrus Association breached that duty, causing his injuries.

After trial, a jury awarded Garcia substantial damages as against Paramount Citrus Association.

Holding & Reasoning

The Court of Appeal reversed. It held that Paramount Citrus Association did not owe Garcia a duty to place warning signs on its property and thus could not be liable.

The court addressed the question of duty, saying:

In determining whether a duty should be imposed in a particular case, a court must consider the following factors in the circumstances of the case: the foreseeability of harm to the injured party, the degree of certainty that party has suffered injury, the closeness of the connection between the condition of the property and the injury, the moral blame attached to the landowner's conduct, the policy of preventing future harm, the extent of the burden the duty would impose compared to the benefit to the community from imposing the burden, and the practical availability of insurance for the risk involved (that is, cost, prevalence and availability of such insurance).

It then turned to the analysis that a court should use:

“First, the court must determine the specific measures the plaintiff asserts the defendant should have taken to prevent the harm. This frames the issue for the court's determination by defining

the scope of the duty under consideration. Second, the court must analyze how financially and socially burden some these proposed measures would be to a landlord, which measures could range from minimally burdensome to significantly burdensome under the facts of the case. Third, the court must identify the nature of the third party conduct that the plaintiff claims could have been prevented had the landlord taken the proposed measures, and assess how foreseeable (on a continuum from a mere possibility to a reasonable probability) it was that this conduct would occur. Once the burden and foreseeability have been independently assessed, they can be compared in determining the scope of the duty the court imposes on a given defendant. The more certain the likelihood of the harm, the higher the burden a court will impose on a landlord to prevent it; the less foreseeable the harm, the lower the burden a court will place on a landlord.”

The court then used this framework. It reasoned:

Respondent does not assert specific preventative measures that should be taken by a rural landowner. From his various statements on the subject, we think a fair summary of his assertions would be this: Where traffic on a public road is not visible before a driver on a private road reaches the right-of-way of the public road, the owner of the private road is required to post a stop sign or a warning to notify drivers on the private road that there is a road crossing ahead.

Having interpreted and summarized Garcia's assertions, the court looked at the burden Garcia sought to impose. Despite Garcia's protestations to the contrary, the court held:

The duty would require every owner of such property to inspect every road on the property to determine whether the view of an intersection is obscured from some vantage point an undefined distance from the public road, and then to post a warning sign on the private road.

The court concluded this burden was excessive given the foreseeability of harm, and it declined to impose a duty. Since there was no duty, there could be no liability.

Analysis

This case is noteworthy in that a great deal of Garcia's problems stemmed from the fact that he did not articulate the specific preventive measures he felt Paramount Citrus Association should have taken. This led the court to frame those measures for him and to do so in a way quite different from what he might have wanted. Unfortunately for Garcia, the court framed the measures in such a way that it then found the burden excessive.

A plaintiff seeking to establish a duty of care may increase the likelihood of success by articulating specific preventive measures that are not unduly burdensome.

This opinion appears in the July 22, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 11146.

An Insurer Was Estopped To Rely On A Policy Provision Requiring The Insured To Enter Into A Contract To Rebuild Fire Damaged Premises Within 180 Days

City of Hollister v. Montgomery Insurance Company
(Cal. Ct. of App., 6th Dist.), filed July 29, 2008, published July 31, 2008

Key Facts

An old municipal building at the Hollister airport caught fire. The building was insured against fire by an insurance policy issued by Montgomery Insurance Company ("MIC"). The policy included a "Functional Building Valuation" endorsement. The endorsement obligated MIC to pay the cost to repair or replace the building, but only if, within 180 days after the loss, City "contract[ed] for repair or replacement of the loss or damage to restore the building . . . for the same occupancy and use . . ." If the City failed to satisfy this condition, it could only recover the building's "market value."

MIC refused to confirm that it would honor the City's claim for payment under the "Functional Building Valuation" endorsement. Instead, MIC raised spurious grounds for its refusal to confirm coverage, delayed in communicating basic determinations affecting coverage, refused to disclose its best estimate of the functional replacement value, permitted the City to labor under misapprehensions concerning its rights under the policy, and ignored communications from the City seeking clarification of these and other matters. Among other things, MIC asserted that its investigation had disclosed that even before the fire, the City was contemplating demolishing the building and that this might preclude payment on the claim. As the time to enter into a contract to replace

the building neared expiration, the City brought a declaratory relief action against MIC. It sought a declaration that in light of MIC conduct in handling the claim and failing to confirm coverage, MIC was estopped to assert the requirement that the City enter into a contract to replace the building within 180 days. The trial court found for City, and MIC appealed.

Holding & Reasoning

The Court of Appeal affirmed.

The court explained the doctrine of estoppel in great detail. Among other things, it explained the doctrine as follows:

Broadly speaking, “estoppel” refers less to a doctrine than to a conceptual pattern, first articulated in the courts of equity, which has come to pervade our law. When it is successfully invoked, the court in effect closes its ears to a point-a fact, argument, claim, or defense-on the ground that to permit its assertion would be intolerably unfair. It is commonly said that the party to be estopped, having conducted himself in manner X, will “not be heard” to assert Y.

The court also distinguished the doctrine of estoppel from that of waiver:

Estoppel effects a forfeiture, i.e., the loss of an otherwise viable right. It is akin to the doctrine of waiver, often invoked in the same breath, and sometimes confused with it. The essence of waiver, however, is the voluntary relinquishment of a known right, which may be effective as a matter of law without

any demonstration that the other party was caused by the waiver to expose himself to any harm.

The court held that while the elements often recited for the application of the doctrine of estoppel may appear to require a fraud by the party to be estopped, fraud is not actually necessary.

Turning to the insurance context, the court stated:

In the insurance context especially, estoppel may arise from a variety of circumstances in which the insurer's conduct threatens to unfairly impose a forfeiture of benefits upon the insured. Indeed, California courts have long held that “equitable relief” may be broadly available in a proper case to relieve an insured of a forfeiture under a contractual condition of coverage.

It noted that this is particularly apropos in the context of contractual limitation of actions provisions that would otherwise expire while the insurer is still investigating the claim or where the insurer conceals the identity of the wrongdoer or fails to comply with regulatory obligations relative to giving the insured notice of relevant time limitations. The court noted that under Cal. Code Regs., tit. 10, § 2695.4, subd. (a):

“When additional benefits might reasonably be payable under an insured's policy upon receipt of additional proofs of claim, the insurer shall immediately communicate this fact to the insured and cooperate with and assist the insured in determining the extent of the insurer's additional liability.”

In addition to the foregoing, the court observed that the implied covenant of good faith and fair dealing, which exists in every insurance policy, precludes the insurer from doing anything to deprive the insured of the expected benefits of the policy.

Turning to the facts, the court reasoned that, throughout the time City was supposed to be arranging a contract to replace the building, MIC threatened to deny reimbursement for such a project, while refusing to take any definite position on coverage until after City had bound itself by contract to pay for a replacement building. Among other things, MIC repeatedly asserted that the City had a pre-existing intention to demolish the building and MIC suggested that such an intention would bar a claim for functional replacement coverage. The City could not have been sure that had it obligated itself to rebuild, MIC would have paid the replacement costs, this despite, according to the court, the fact that “no legal basis for this position has ever been offered.”

Given such facts, the court reasoned that the trial court could properly have found an estoppel.

Analysis

This decision logically flows from decisions estopping insurers from asserting other policy limitations, such as the 1-year limitation of actions provision. It should serve as a warning to insurers whose policies include replacement cost coverage and require either that there be a contract for the replacement or actual replacement within a stated time, that they cannot delay in reaching at least a basic coverage determination.

MIC seems to have fixated on the City's sup-

posed intention to demolish the building before the fire. That did not sit well the court, particularly in light of the fact that there was no law which would have supported a refusal to pay for the loss even if the City had intended to demolish it. Similarly, in the case of *Wilson v. 21st Century Ins. Co.*, 42 Cal.4th 713 (2007), the Supreme Court commented on how the insurer, in assessing the value of a personal injury claim, fixated on the fact the insured's medical bills were relatively low and found there was a basis for finding the insurer acted in bad faith in failing to offer a reasonable settlement. Insurers who overemphasize one aspect of a claim can quickly find themselves fighting a uphill battle when they fail to persuade the court on the issue.

This opinion appears in the July 31, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 11873.

An Arbitration Provision In An Employment Agreement Was Unenforceable As Being Unconscionable

Ontiveros v. DHL Express (USA), Inc.
(Cal. Ct. of App., 6th Dist.), filed June 30, 2008, published July 2, 2008

Key Facts

Gina Ontiveros sued her former employer, DHL Express. She asserted various claims related to sex discrimination, harassment, and retaliation arising from her employment with DHL.

DHL moved to compel the dispute to be resolved by arbitration. It relied on a “Mutual Agreement to Arbitrate Claims” that Ontiveros signed when she became a permanent DHL

employee.

The agreement to arbitrate covered all claims between the parties, whether or not arising out of Ontiveros' employment or its termination. The agreement provided that "[t]he Arbitrator, and not any federal, state, or local court or agency, shall have exclusive authority to resolve any dispute relating to the interpretation, applicability, enforceability or formation of this Agreement, including but not limited to any claim that all or part of this Agreement is void or voidable." The agreement stated that arbitration would be held under the auspices of either the American Arbitration Association (AAA) or Judicial Arbitration and Mediation Services, Inc. (JAMS), "with the designation of the sponsoring organization to be made by the party who did not initiate the claim."

The agreement further stated that each party would have the right to take the deposition of one individual and any expert witness designated by another party. Additional discovery was at the arbitrator's discretion, "upon a showing of substantial need." The agreement also stated that the parties would share the costs of the arbitrator and that each party would pay its own costs and attorney fees, except that if a party prevailed on a statutory claim that affords the prevailing party attorney fees, the arbitrator may award reasonable fees to the prevailing party.

At the conclusion of the agreement was a sentence in all capital letters stating, "I understand that by signing this agreement I am giving up my right to a jury trial," with a line underneath where Ontiveros wrote her initials. Just above her signature was another sentence in all capital letters stating, "I further acknowledge that I have been given the opportunity to discuss this agreement with my private legal counsel and

have availed myself of that opportunity to the extent I wish to do so."

Ontiveros opposed the motion, declaring that she received the arbitration agreement as part of a packet of hiring paperwork, which her manager said to fill out; sign; and return in order to start her new job and get paid. She further stated:

At no time did [my manager] explain or describe the contents of the documents in that hiring packet. The hiring packet contained documents like an Immigration Form I-9, documents pertaining to health care coverage, documents relating to my base compensation, documents welcoming me to the company and other documents the content of which I do not recall. The hiring packet came in a binder file. At no time did anyone inform me that I was signing an Agreement to Arbitrate Claims or explain what that was or how it affected my substantive rights. At no time did anyone inform me that I was required to give up any rights I might have to a jury trial in order to work for Airborne. When I was hired, I was informed that I needed to sign the paperwork in order to get paid and start my new job, and I was not afforded an opportunity [to] negotiate further the terms of my employment. I was already working long hours at that point in time and did not have any real opportunity to review the documents I was told to sign. I was not told that I should review the documents with a lawyer or discuss my rights with a lawyer. The first time I can recall knowing about the Agreement to Arbitrate Claims was when DHL raised this issue in this law-

suit. I had not been given a copy of the agreement prior to filing this lawsuit.

The trial court denied DHL's motion to compel.

Holding & Reasoning

The Court of Appeal affirmed.

The court relied on *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal.4th 83 (2000), where the California Supreme Court articulated the five minimum requirements for lawful arbitration of nonwaivable statutory civil rights in the workplace pursuant to a mandatory employment arbitration agreement: "Such an arbitration agreement is lawful if it (1) provides for neutral arbitrators, (2) provides for more than minimal discovery, (3) requires a written award, (4) provides for all of the types of relief that would otherwise be available in court, and (5) does not require employees to pay either unreasonable costs or any arbitrators' fees or expenses as a condition of access to the arbitration forum."

The court held that the particular agreement was part of a contract of adhesion because Ontiveros had no ability to negotiate its terms. She had to agree to DHL's terms if she was to work for it.

The court also held that because the agreement was adhesive, it was unconscionable and therefore unenforceable. Among other things, provisions giving the arbitrator the right to determine the validity of the agreement was unconscionable in light of the fact that arbitrators have an inherent incentive to find arbitration agreements valid. Next, the requirement that the employee pay half of the cost of arbitration was unconscionable in light of the fact she would not have had to pay such

costs in connection with a lawsuit brought in a court. Further, the limitation on discovery was unconscionable in light of the fact that an employee generally needs to conduct extensive discovery to prove discrimination.

Because of these unconscionable provisions in a "take-it-or-leave-it" contract, the court held that the agreement was unenforceable.

Analysis

Employers who want to maximize the likelihood that employment disputes will be resolved via arbitration should consult with an employment attorney who can provide guidance with respect to the procedural and substantive elements of arbitration agreements that are likely to be upheld by California courts.

This opinion appears in the July 2, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 10045.

Other Cases Of Interest

A Defendant Moving For Summary Judgment Can Use Factually Devoid Interrogatory Answers Only Against An Opponent Who Gave Those Answers

Great American Insurance Companies v. Gordon Trucking, Inc. (Cal. Ct. of App., 5th Dist.), filed July 29, 2008, published July 31, 2008

Great American brought a subrogation action against Gordon Trucking. It alleged that as a result of Gordon's negligent maintenance of its truck, the truck caught fire and damaged a truck owned by Great American's

insured.

Gordon moved for summary judgment. It asserted it was entitled to a judgment as a matter of law because Great American could not prove negligence. Gordon's motion relied in part on answers to interrogatories which Gordon had previously served on Great American's insured. Those answers reflected that the insured had no information showing negligence by Gordon.

The trial court granted the motion. Great American appealed.

The Court of Appeal reversed.

The court explained that under *Aguilar v. Atlantic Richfield Co.* 25 Cal.4th 826 (2001):

A defendant moving for summary judgment may demonstrate a cause of action has no merit by either (1) showing that one or more elements of the cause of action cannot be established, or (2) establishing an affirmative defense to the cause of action. (Code Civ. Proc., § 437c, subd. (o), (p)(2).) To show that one or more elements of the cause of action cannot be established, the defendant may either “present evidence that conclusively negates an element of the plaintiff's cause of action” or “present evidence that the plaintiff does not possess, and cannot reasonably obtain,” the evidence needed to establish the cause of action, such “as through admissions by the plaintiff following extensive discovery to the effect that he has discovered nothing.”

And, it explained that a party may rely on an opponent's factually devoid interrogatory

answers to establish that opponent's inability to establish an essential element of its case. However, it ruled that such factually devoid interrogatory answers can only be used against the particular responding party. Since it was Great American's insured and not Great American itself that gave the factually devoid answers, they could not be used against Great American.

Since the interrogatory answers could not be used against Great American, Gordon had not established Great American's inability to prove its case. The trial court erred in granting a summary judgment in favor of Gordon.

This opinion appears in the July 31, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 11859.

A Juror's Reaction To A Statement Made During Closing Argument Did Not Amount To Prejudicial Misconduct

Bandana Trading Co., Inc. v. Quality Infusion Care, Inc.
(Cal. Ct. of App., 2d Dist.), filed July 21, 2008, published July 22, 2008

Bandana Trading Company sued Quality Infusion Care. The case went to trial. During closing arguments, counsel for Bandana Trading told the jury it could reject the entire testimony of a witness if it determined that the witness had been willfully false in a material aspect of his or her testimony. One of the jurors clapped her hands in response to this statement.

Quality Infusion Care asked that the particular juror be replaced. The trial court questioned the particular juror about the incident. It also

questioned the other jurors. The juror who clapped stated that she was pleased by counsel's statement that if a witness had willfully lied, she could disregard everything that witness had said. The other jurors recalled the clapping incident, but not the circumstances surrounding it.

The trial court concluded that the clapping incident was not prejudicial and did not show prejudice by the particular juror. It therefore refused to replace her.

After the jury returned a verdict in favor of Bandana Trading, Quality Infusion Care appealed.

The Court of Appeal affirmed. It held that there was no evidence of prejudice.

The court noted that the statement by counsel, to which the juror clapped, was an accurate statement of the law. And, it pointed out that it is not misconduct for a juror to agree with an accurate statement of the law.

The court also noted that while jurors are admonished not to express an opinion until the case is submitted for deliberation, jurors are only human and that the formation of tentative opinions "is a natural response consistent with processing information." Thus, while it was wrong for the juror to have clapped, it did not, under the circumstances, amount to prejudicial misconduct.

This opinion appears in the July 22, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 11135.

Evidence Of Mediation Conduct Was Not Admissible To Establish A Settlement When The Defendant Sought To Back Out Of A Settlement Made At The Mediation

Simmons v. Ghaderi
(Cal. Sup. Ct.), filed July 21, 2008, published July 22, 2008

The parties to a medical malpractice case attended a mediation. Defendant Lida Ghaderi, M.D. provided her medical malpractice insurer, Cooperative American Physicians/Mutual Protection Trust ("CAP-MPT") with her written consent to settle the case for the amount of \$125,000. The plaintiffs unconditionally accepted a \$125,000 settlement offer. While the mediator was reducing the settlement agreement to writing, the CAP-MPT claims specialist told Dr. Ghaderi a settlement had been reached. Dr. Ghaderi promptly revoked her consent to settle, and left the mediation.

Plaintiffs ultimately amended their medical malpractice complaint to include a cause of action for breach of the oral settlement contract. After a bifurcated trial on that cause of action, the trial court entered judgment in favor of plaintiffs in the amount of \$125,000. Dr. Ghaderi appealed, arguing that the Evidence Code provisions governing mediation confidentiality prevented plaintiffs from introducing any evidence of the oral settlement agreement.

The court of appeal concluded that Dr. Ghaderi was estopped from relying on mediation confidentiality and therefore affirmed.

The California Supreme Court reversed. It held that the statutory scheme for mediations limited the instances in which conduct undertaken in connection with the mediation could

be used and that the scheme did not include establishing a settlement under the circumstances.

The Court recognized that the statutory scheme could give a wrongdoer, such as a litigant who wanted to back out of a settlement, an unfair advantage, but nonetheless held that the courts were not empowered to create exceptions.

This opinion appears in the July 22, 2008 edition of the Los Angeles Daily Journal, Daily Appellate Report, at p. 11107.

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