Appellate Reports

Two rulings on insurance bad faith and the genuine dispute doctrine; also collateral estoppel in employment class actions

By Jeffrey I. Ehrlich

Insurance bad faith; genuine-dispute doctrine

***Fadeeff v. State Farm Gen. Ins. Co.* (2020)** __ Cal.App.5th __ (First Dist., Div. 2)

The Fadeeffs' home was damaged in a wildfire. State Farm's initial inspection of the home described it as "well maintained with no apparent deferred maintenance" and that "[a]ll damage is related to smoke and soot." State Farm found smoke and soot on the interior walls, ceilings and carpeting, and on all exterior elevations including on the very large deck and handrail. State Farm paid $50,000 to address the damage. The Fadeeffs then hired a public adjuster and submitted supplemental claims totaling about $75,000. State Farm retained an independent adjuster for that claim, who was not licensed in California and was not licensed in any building trade. He inspected the Fadeeffs' property in March 2016 and stated he could not find smoke damage.

State Farm hired two licensed environmental contractors to inspect the home and its HVAC system. They found that no additional cleaning was necessary to address smoke or fire damage. State Farm then denied the entire supplemental claim, which went beyond the issues addressed by these experts.

The Fadeeffs sued State Farm for bad faith. The trial court granted State Farm's motion for summary judgment. Reversed.

State Farm failed to show that all aspects of its denial of the claim were based on the recommendation of the experts it retained, as opposed to the unlicensed adjuster. For example, despite the initial finding of no deferred maintenance, State Farm denied the claim for damage to the exterior paint caused by the power washing to remove soot and smoke, claiming that it was "wear and tear" and not related to the fire. This was the conclusion of the adjuster, not the experts. The same conclusion applied to the denial of coverage for the wallpaper and carpet.

There were also triable issues of fact about whether State Farm could have reasonably relied on its experts in denying the supplemental claims. State Farm's second adjuster failed to follow the company's operational guide for the hiring of third-party experts and, as a result, failed to provide the experts with clear and concise instructions about the specific questions they were to address. The court agreed that from the circumstances presented, a jury could find that the experts were hired to "rubber stamp" State Farm's conclusion to deny the claim for supplemental benefits. "In these circumstances, we cannot conclude that it is undisputed or indisputable that the denial of supplemental claims was reasonable based on a genuine dispute created by the retention of experts." Hence, the genuine-dispute doctrine did not support summary judgment.

Insurance bad faith; genuine-dispute doctrine; novel legal issues; reversal of summary judgment based on argument not raised in trial court; initial burden on summary judgment; breach-of-contract versus bad-faith claims

Mosley v. Pacific Specialty Insurance Company (2020) __ Cal.App.5th __ (Fourth Dist., Div. 2)

The Mosleys rented out a home they own in Cambria, which they insured with Pacific Specialty Insurance Company (PSIC). Without the Mosleys' knowledge, the tenant started growing marijuana in the home. To support his marijuana-growing operation, he re-routed the home's electrical system to steal power from a main utility line. This caused a fuse to blow, which started a fire that damaged the house. PSIC denied coverage, citing a provision in the policy that excluded any loss associated with "[t]he growing of plants" or the "manufacture, production, operation or processing of ... plant materials."

The Mosleys sued PSIC for denying coverage. The trial court granted summary judgment in PSIC's favor, finding that PSIC properly denied coverage because the Mosleys had control over their tenant's conduct. Reversed in part; affirmed in part. While the exclusion in the policy for losses "resulting from" the growing of plants applied to preclude coverage, the court agreed that the policy was void because it failed to provide the minimum level of coverage mandated by Insurance Code section 2070. That provision generally requires fire policies in California to be on the standard form set forth in Insurance Code section 2071, but permits insurers to deviate from the form "provided, that coverage with respect to the peril of fire, when viewed in its entirety, is substantially equivalent to or more favorable to the insured than that contained in such standard form fire insurance policy." (Ins. Code, § 2070.) Section 2071 provides, in relevant part, that an insurer "shall not be liable for loss occurring ... while the hazard is increased by any means within the control or knowledge of the insured." The trial court found that the Policy was valid and enforceable because it provided "substantially equivalent" coverage to section 2070's standard form because, like the standard form, the Policy limits coverage

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for hazards increased by means within the insured's control or knowledge. The trial court thus found that PSIC was not liable for the loss caused by the fire because Lopez's marijuana growing operation, as well as the electrical alterations he made to the property, increased a hazard "'within the control or knowledge'" of the Mosleys.

PSIC implicitly conceded that the Mosleys had no knowledge of the tenant's marijuana growing operation but argued that they had control over it because they "had control over what occurred in their home." No California decisions address what constitutes a "hazard ... increased by any means within the control ... of the insured" under section 2071. The court therefore looked to decisions of sister-state courts construing their states' version of section 2071.

Those decisions stand for the proposition that an insured increases a hazard "within its control" *only if* the insured is aware of the hazard or reasonably could have discovered it through exercising ordinary care or diligence. PSIC failed to cite, nor could the court locate, any authority that suggests a landlord-insured is strictly liable for a hazard created by the insured's tenant even if the insured is unaware of the hazard.

It is undisputed the Mosleys did not know about the tenant's marijuana growing operation or his altering the property's electrical system. There is likewise no evidence as to whether the Mosleys could have discovered the marijuana growing operation "by exercising ordinary care or diligence." On this record, the issue of whether the tenant's conduct was "within the control" of the Mosleys is a fact issue for the jury to decide because the record is silent as to what, if anything, the Mosleys reasonably could have done to prevent or discover Lopez's marijuana growing operation.

To the extent PSIC's interpretation of the Policy renders the Mosleys strictly liable for Lopez's conduct, the Policy is void under section 2071. By holding the Mosleys responsible for the damage Lopez caused, irrespective of the Mosleys' knowledge of his conduct or their responsibility for it, the Policy subjects the Mosleys to increased liability – and less favorable coverage that is not "substantially equivalent" to coverage provided under section 2071.

At oral argument, PSIC argued that the Moselys had forfeited any argument that their tenant's conduct was not within their knowledge or control because they did not address it in the trial court and their opening brief on appeal only addressed it in passing. But since the trial court's order granting summary judgment turned on its conclusion that the tenant's conduct was within the Mosleys' control, the court was required to address that issue.

The fact that the Mosleys did not oppose PSIC's argument that the tenant's conduct was within their control or knowledge did not mean the trial court properly granted summary judgment on that basis. A party is entitled to summary judgment only if it meets its initial burden of showing there are no triable issues of fact and the moving party is entitled to judgment as a matter of law. That is true even if the opposing party fails to file any opposition to the motion. "For the reasons explained above, we conclude PSIC failed to meet its initial burden because an issue of fact remains as to whether [the tenant's] conduct was within their 'control or knowledge.'" PSIC's motion for summary judgment therefore should have been denied – regardless of what the Mosleys did or did not argue in their opposition – because the burden never shifted to them.

Although this finding required reversal of the summary judgment on the breach-of-contract claim, the court affirmed the dismissal of the bad-faith claim. It concluded that even if its interpretation of the policy was wrong, PSIC acted reasonably in denying the Mosleys' claim. Because there was no clear, controlling California law that establishes whether PSIC properly denied coverage – an issue that turns on whether the tenant's conduct was within the Mosleys' control, which remains to be determined. Under the unique circumstances presented and the lack of guiding California precedent, the court concluded that PSIC reasonably construed its policy to deny coverage.

Class actions; collateral estoppel

Williams v. U.S. Bancorp Investments, Inc. (2020) __ Cal.App.5th __ (First Dist., Div. 4.)

In 2005, employees of U.S. Bancorp filed a putative class action against it seeking restitution of overtime wages and wage deductions, waiting time penalties, and meal and rest breaks (the *Burakoff* action.) The superior court certified the *Burakoff* action as a class action in 2008. Plaintiff Williams joined US Bancorp as a financial consultant in 2007 and became a member of the *Burakoff* putative class. In 2010, he filed his own putative class action against US Bancorp alleging similar causes of action. The trial court stayed Williams' case until the *Burakoff* action concluded because the two cases were founded on the same primary rights and the same causes of action.

In 2011, the trial court in *Burakoff* decertified one subclass of which Williams was a member (subclass A) based on a lack of commonality, but allowed the case to proceed as to a second subclass (subclass B), of which Williams was also a member. The parties settled the *Burakoff* action the following year. Williams participated in the settlement and received compensation as a member of subclass B. Wiliams did not, however, release his wage and hour claims at issue in subclass A, nor did any of the other absent members of alleged subclass A.

U.S. Bancorp then demanded in the present action that Williams drop his class claims and arbitrate his individual claims. When Williams did not agree to arbitrate his individual claims, U.S. Bancorp brought a motion to compel arbitration and to dismiss the first amended complaint. It argued the *Burakoff* decertification order collaterally estopped Williams

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from relitigating the appropriateness of class certification because he was a member of the *Burakoff* class, and because the two cases raised substantially the same claims and identical class certification issues. Williams agreed to the dismissal of his claim for unpaid business expenses only.

The trial court initially denied U.S. Bancorp's motion to compel arbitration and dismiss the remaining class claim, concluding that *Burakoff*'s subclass A and the putative class in this case were not identical. They were comprised of different class members during different time periods, so collateral estoppel did not apply, the trial court ruled. This order was affirmed on appeal.

On remand, U.S. Bancorp renewed its motion to compel arbitration of Williams's individual claims after conducting discovery relevant to class certification. The trial court granted the motion on October 25, 2018, concluding that a class decertification order may have collateral estoppel effect, and that the decertification order in *Burakoff* barred Williams's claims because facts developed in discovery showed brokers' job duties and time spent performing those duties were materially the same during both class periods. On November 21, 2018, the trial court dismissed Williams's class claims with prejudice, and then added that it was making no "order regarding the class claims of absent putative class members." Reversed.

The question before the court is whether claim-preclusion principles operate to preclude an unnamed class member in a first action from relitigating the question of class certification in a second action, if the trial court in the original case certified but then decertified a class.

In answering that question, the court first determined that the absent class members in *Burakoff* were "parties" for the purposes of assessing that case's preclusive effects. In general, a "party" to litigation is one by or against whom a lawsuit is brought, or one who becomes a party by intervention, substitution, or third-party practice. Williams filled no such role in *Burakoff*. Here, Williams is a person whom, in the final analysis, the named plaintiffs in *Burakoff* were denied leave to represent.

Next, the court found that the trial court's order decertifying subclass A in *Burakoff* based on a lack of commonality meant that *Burakoff*'s named plaintiffs and their attorneys may *not* have adequately represented Williams's interests. Preclusion requires a "properly certified class" precisely "because only in those circumstances can the court in the later proceeding conclude that prior class members' interests were adequately represented in the prior proceeding." Where, as here, the trial court in the prior proceeding determined that individual issues predominated over common ones, there could be no community of interest. And where there is no community of interest, a later court can only speculate as to the extent to which the interests of the named plaintiffs and the absent class members conflicted or aligned.

Because *Burakoff*'s subclass A was, in the end, "a rejected class," no judicial finding that the named plaintiffs adequately represented the absent members of that subclass survived to become final. For that reason, the decisions of the *Burakoff* court can have no preclusive effect on the absent members of that subclass.

Ultimately, the court held that, "under California law, an order decertifying a class has no preclusive effect on absent class members. The trial court's order dismissing Williams's class claims with prejudice and compelling Williams's individual claims to arbitration must be reversed."

Public entity liability; dangerous condition

City not liable for failure to erect barrier to keep pedestrians from going around guardrail to railroad tracks: *Hedayatzadeh v. City of Del Mar* (2020) 44 Cal.App.5th 555 [257 Cal.Rptr.3d 718] (Fourth District, Div. 1.)

Hedayatzadeh's 19-year-old son was struck by a train on an oceanfront bluff in Del Mar on property owned by North County Transit District (NCTD). Hedayatzadeh filed a wrongful-death lawsuit against the City of Del Mar, based on the City's failure to erect barriers to prevent pedestrians from accessing NCTD's train tracks. The trial court granted summary judgment in favor of the City. Affirmed.

A dangerous condition exists when public property "'is physically damaged, deteriorated, or defective in such a way as to foreseeably endanger those using the property itself,' or possesses physical characteristics in its design, location, features or relationship to its surroundings that endanger users."

It is undisputed that the railroad right-of-way, which consists of the train tracks and an area approximately 50 feet to both the west and east of the tracks is owned and controlled by NCTD, not by the City. Although the exact boundaries are not clear from the record, the City's property terminates somewhere near the guardrail that is at end of 13th Street. Hedayatzadeh takes the position that the City's property poses a dangerous condition because (1) it is *adjacent* to NCTD's right-of-way containing the train tracks; (2) the train tracks pose a danger to trespassers; and (3) the City has not taken any action, such as constructing a fence at the location of the guardrail at the end of 13th Street, to prevent pedestrians from walking around the guardrail and trespassing on NCTD's train tracks.

Here, the City is not liable as a matter of law for merely failing to erect a barrier at the site of the guardrail to prevent pedestrians from choosing to enter a hazardous area on NCTD's adjacent right-of-way.

Negligence, duty, mortgage-loan modifications

Lenders who offer loan modifications owe a duty of reasonable care in processing application: *Weimer v. Nationstar Mortgage, LLC* (2020) 47 Cal.App.5th 341, 346 [260 Cal.Rptr.3d 712, 714], pet. for review filed (May 6, 2020) (Third District)

Plaintiff Robert Weimer, Jr. purchased real property in Carnelian Bay in 1993.

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He refinanced the mortgage in 2006 with a loan from defendant Bank of America, N.A. (BANA). After defaulting, plaintiff entered into a loan modification process with BANA. Subsequently, loan servicing was transferred, successively, to defendants Specialized Loan Servicing, LLC (SLS) and Nationstar Mortgage, LLC (Nationstar). According to plaintiff, BANA, SLS, and Nationstar successively each engaged in deliberate and negligent misconduct in the loan modification process. In 2014, BANA transferred beneficial interest in the loan to defendant U.S. Bank, N. A. (U.S. Bank), as trustee for the Certificateholders of Banc of America Funding Corporation Mortgage Pass Through Certificates Series 2007-7. Eventually, Nationstar, acting as U.S. Bank's agent, recorded a notice of trustee's sale and had an agent enter onto the property and change the locks.

Weimer sued BANA, U.S. Bank, and Nationstar asserting causes of action sounding in intentional and negligent misrepresentation, negligence, trespass to land, seeking declaratory relief, and asserting violations of the unfair competition law. The trial court sustained their demurrers, finding that the claim against BANA was time barred and that his claims against the other defendants were not viable. The Court of Appeal affirmed as to BANA, but reversed as to the other defendants, finding that Weimer sufficiently stated causes of action sounding in intentional and negligent misrepresentation and violations of the unfair competition law against them.

[A]s a general rule, a financial institution owes no duty of care to a borrower when the institution's involvement in the loan transaction does not exceed the scope of its conventional role as a mere lender of money. Additionally, California law generally does not impose a duty of care to avoid causing purely economic losses in negligence cases. But the California Supreme Court has recognized an exception when the plaintiff and defendant have a "special relationship." In this context, "special relationship" means "that the plaintiff was an intended beneficiary of a particular transaction but was harmed by the defendant's negligence in carrying it out."

Determination of the existence of such a duty is based on an application of the factors set forth in n *Biakanja v. Irving* (1958) 49 Cal.2d 647, 650. The *Biakanja* factors are: (1) the extent to which the transaction was intended to affect the plaintiff, (2) the foreseeability of harm to the plaintiff, (3) the degree of certainty that the plaintiff suffered injury, (4) the closeness of the connection between the defendant's conduct and the injury suffered, (5) the moral blame attached to the defendant's conduct, and (6) the policy of preventing future harm.

Based on the application of those factors, the court concluded that the trial court erred in concluding that the defendants other than BANA owed Weimer a duty of care.

Attorneys; ethics

Fee-split agreement; mandatory disclosures re: malpractice insurance; referral fees; quantum meruit: *Hance v. Super Store Industries* (2020) 44 Cal.App.5th 676 [257 Cal.Rptr.3d 761] (Fifth District).

Attorneys who represented plaintiff class in class action moved for award of attorney fees and division of award among attorneys, which referring attorney and co-counsel disputed. The Superior Court made fee award and divided fees in accordance with written fee division agreement. Co-counsel appealed. Reversed.

As an issue of apparent first impression, attorney-fee division agreement was unenforceable based on ethical violation of failure to disclose lack of professional liability insurance, but any quantum meruit recovery was not limited to hours reflected in referring attorney's time records, but could include reasonable value of referral.

Settlement

Settlement credit; res judicata; privity between co-defendants: *Shuler v. Capital Agricultural Property Services, Inc.* (2020) __ Cal.App.5th __ (Second Dist., Div. 6.)

The Shulers' horse farm was inundated by a landslide caused by the negligence of its adjoining uphill landowners. The Shulers sued the landowners and their management company for trespass, nuisance, and negligence. Their action in state court was originally dismissed for failure to join an indispensable party, the National Resource Conservation Service (NCRS), a federal agency whose employees worked on the erosion-control permit issued to the uphill landowners. The Shulers refiled in federal court, including the NCRS as a defendant. While the case was pending in federal court, the Shulers accepted a $50,000 settlement from the federal government under FRCP 68, a rule corresponding to Code of Civil Procedure section 998 in California. The settlement was reflected in a consent judgment releasing the federal government and its agents and employees from liability in exchange for the $50,000 payment. The federal court approved a motion for good-faith settlement under Code of Civil Procedure section 877.6 and then dismissed the case because there were no remaining federal claims. The Shulers refiled in state court and won a verdict against the defendants of $1.7 million in economic damages. Each defendant was found to be 10% at fault, and the two NCRS employees who worked on the permits were each held 34% at fault.

When the trial court entered judgment, it ordered that the defendant would be jointly and severally liable to appellants only for their 30 percent share of the negligence: $526,950, less an offset of $66,666.67 for amounts paid by settling tortfeasors. Accordingly, the defendants' joint and several liability for economic damages was reduced from $1,756,499.99 to $460,283.33. (In short, the trial court discounted the defendants' liability by the 2% comparative fault allocated to the Shulers, plus the 68% fault allocated to the federal employees.) Reversed.

In the settlement with the United States, appellants did not waive their right to seek full compensation for their loss from other tortfeasors under the California rule of joint and several liability. They waived their right to seek further compensation from the United States and its

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employees. Therefore, the incorporation of the settlement into a judgment does not shield respondents from joint and several liability. "'Although a stipulated judgment is no less conclusive than a judgment entered after trial and contest [citations][,] it is axiomatic that its res judicata effect extends only to those issues embraced within the consent judgment....'"

Each of the defendants was held to be independently liable for its own negligence. Hence, they could not claim that they were held "vicariously liable" for the negligent conduct of the federal employees, whose liability had been released in the settlement. Under the doctrine of joint and several liability, which applies to economic damages in California, each of the defendants was jointly and severally liable to the Shulers for the entire amount of the judgment.

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