Supreme Court No. S161008

IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

VILLAGE NORTHRIDGE HOMEOWNERS ASSOCIATION
Plaintiff and Appellant,

vs.

STATE FARM FIRE & CASUALTY COMPANY, et al.
Defendant and Respondent.

REVIEW AFTER A DECISION BY THE COURT OF APPEAL
SECOND DISTRICT, DIVISION EIGHT, 2ND CIV. NO. B188718
LOS ANGELES COUNTY SUPERIOR COURT NO. BC265328

ANSWER TO PETITION FOR REVIEW

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MISCELLANEOUS

1. INTRODUCTION

State Farm's Petition for Review invites this Court to engage in a slippery slope analysis regarding the potential impact of the published Court of Appeal decision. According to State Farm's version of events, the Court of Appeals completely disregarded 80 years of settled California law on the topic of settlement agreements and that in doing so forever destroyed one's ability to settle a dispute in exchange for a waiver of California *Civil Code* section 1542. This is simply not true. Not only did the Court of Appeal explain exactly how this case was factually distinguishable from *Garcia* and *Taylor*[1], the Court of Appeal went so far as to quell State Farm's fears by spelling out the very limited factual scenario to which this holding can be applied as controlling authority. Furthermore, State Farm's musings about fairness and equity are nothing short of contemptible given its constant misrepresentations regarding the policy limits for over ten years.[2] In this published opinion, the Court of Appeals applied an existing rule of law to a set of facts significantly different from those stated in prior published

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[1] *Garcia v. California Truck Co.* (1920) 183 Cal. 767; *Taylor v. Hopper* (1929) 207 Cal. 102.

[2] For the most recent misrepresentation, see the hearsay explanation of earthquake policy limits in Footnote 5 of State Farm's Petition for Review with no supporting citation to the record – because no such support exists.

opinions. Review is not necessary to secure uniformity of decisional law nor would it be sound in that it would permit State Farm to use this Court to further its agenda of making misrepresentation of policy limits an easily accomplished objective by an insurance company so long as a release is involved. Village Northridge respectfully submits that the Court of Appeal's decision was properly decided and need not be reviewed.

2. THE COURT OF APPEAL'S DECISION DID NOT ERADICATE *GARCIA/TAYLOR*

State Farm claims that the Court of Appeal dramatically changed the rules of engagement for settlement of all non-personal injury cases and committed plain error by creating an "exception" to the *Garcia/Taylor* line of authority. What State Farm fails to mention is that this exception has been part of the rule from day one. "As *Garcia* pointed out, a well-recognized rule – not applicable in *Garcia* – provides that 'one who attempts to rescind a transaction on the ground of fraud is not required to restore that which in any event he would be entitled to retain either by virtue of the contract sought to be set aside, or of the original liability.'" *Persson v. Smart Inventions* (2005) 125 Cal.App.4th 1141, 1155, quoting *Garcia v. California Truck Co.* (1920) 183 Cal. 767, 771. The point was clarified further in *Sime v. Malouf*, in which the Court found that since the plaintiff

had the right, independently of the release itself, to retain the sums he received, restoration of the consideration was not required. *Sime v. Malouf* (1949) 95 Cal.App.2d 82, 111-112. As the *Sime* Court observed in 1949, "The law does not require, as the price of attack upon a fraudulently induced release, sacrifice of independent rights, or the doing of idle acts. . . . Rescission and restoration are required only under equitable principles and to prevent the taking of unfair advantage. Restoration is not required unless the ends of justice require it." *Id.*

As the Court of Appeal stated, "***because of the underlying insurance obligation***, the circumstance [in this case] is not unlike both (1) cases in which a settlement agreement and the mutual releases in it are considered separable, thus permitting the plaintiff to affirm the settlement and sue for fraud despite the release [*Persson, supra*, 125 CalApp.4th at 1154], or (2) cases, as described in *Garcia*, applying the 'well-recognized' rule that one who rescinds a contract for fraud 'is not required to restore that which in any event he would be entitled to retain.' [*Garcia, supra*, 183 Cal. at 771]." (Typed Opn. at p. 7, emphasis added.) The distinction which makes *Garcia* and *Taylor* inapplicable to this case is the presence of an underlying contractual obligation. This same distinguishing factor was present in *Persson v. Smart Inventions*, (2005) 125 Cal.App.4th 1141, a

case in which the same *Garcia* based argument which is being made here today was rejected by the Court of Appeals. *See Persson, supra,* 125 Cal.App.4th at 1152-1156. Notably, this case was not cited anywhere in State Farm's Petition for Review. Review by the Supreme Court was denied. *Persson v. Smart Inventions* (2005) 2005 Cal. LEXIS 4328. Much to State Farm's dismay, the Court of Appeals is not obligated to blindly adhere to holdings articulated 90 years ago in fairly distinguishable Supreme Court cases. As the Court of Appeals explained, given the presence of an underlying contractual obligation and State Farm's statutory obligation not to misrepresent the terms of the policy (California *Insurance Code* section 790.03), this case is fairly distinguishable from *Garcia* and *Taylor* Thus, there is no *stare decisis* issue to be addressed.

3. *CIVIL CODE* SECTION 1542 HAS NOT BEEN RENDERED USELESS

State Farm's fears regarding the finality of settlement agreements as a result of this case are irrational and unfounded. This concern was specifically addressed and dismissed by the Court of Appeals:

> "State Farm both misstates its premise and exaggerates the consequences. Correctly stated, the effect of our holding in this case is that a plaintiff could settle a disputed insurance

claim, keep the money paid, and then sue for fraud (rather than on the released claim) if it was fraudulently induced to settle the claim by a misrepresentation of policy limits. The consequences of applying this principle are not dire. Indeed, to avoid them, the insurer need only avoid misrepresenting policy limits when it settles claims." (Typed Opinion at p. 10)

Furthermore, contrary to State Farm's assertions in its Petition, this was *not* the first published California case to permit a party to affirm a settlement agreement, keep the settlement money, and sue for damages based on fraud. *See Persson, supra,* 125 Cal.App.4th at 1152-1156.

4. EQUITIES OF THE CASE: STATE FARM CONTINUES TO MAKE MISREPRESENTATIONS ABOUT POLICY LIMITS

State Farm is of the opinion that this case is the poster child for requiring a defrauded party to return consideration prior to filing suit and is obviously upset by the Court of Appeal's assessment that public policy considerations suggest that the risk of overpayment by an insurer who is alleged to have misrepresented policy limits in obtaining a settlement is more acceptable than the risk that an insured will be deprived by fraud of the full insurance protection for which it paid. (Typed Opn. at p. 11, footnote 4) Village Northridge respectfully disagrees with this assessment.

As the Court of Appeal noted, absent an action for fraud, plaintiffs in the insurance settlement context would be left with no practical remedy because in many cases, plaintiffs have spent much, if not all, of the settlement sum on necessities – the damages which formed the subject matter of the claim – before discovering the fraud. (Typed Opn. at p. 13)

For anyone who might not appreciate that equity is not in State Farm's corner, let us not forget the history surrounding the elusive policy declarations. State Farm never produced a Declarations page evidencing their version of the policy limits, not in discovery, not in the law and motion hearings conducted at the trial court level, and not after the Court of Appeal characterized its failure to document its version of the policy limits as "the elephant in the room" in the first decision. [APP 0549, footnote 8] Rather than produce a counter-version of the plaintiff's Policy Declarations which State Farm contends are wrong, State Farm submitted inadmissible parole evidence in the form of a hearsay Declaration in attempt to convince the trial court that its version of the terms of the contract are correct ($4.9 million - vs. - $11.9 million). In a continuing effort to pull the wool over everyone's eyes and in total disregard of the facts and prior appellate opinion, State Farm is now attempting to "document" its version of the policy limits with attorney argument:

"The amount of the Section I limit does not dictate the limits for earthquake coverage. The earthquake limit was frequently shown on another section of the declarations page, the portion not provided by Village Northridge, or as part of an endorsement. . . . " (Petition at p. 12, footnote 5)

Predictably, no citation follows. If this really is the case, why is State Farm withholding this crucial evidence? That State Farm has the temerity to present this unverified and unsupported attorney rhetoric to this Supreme Court as "evidence" is appalling and is a befitting illustration of why this case was decided correctly. This is exactly the type of fraudulent conduct by insurers which would be permitted to continue unchecked if policyholders were left without the option to affirm and sue.

5. THE RULE AGAINST SPECULATIVE DAMAGES DOES NOT BAR THIS LAWSUIT

State Farm insists that this case is barred by the rule against speculative damages yet cannot seem to find a proper case to support its position. As the Court of Appeal stated, *Cedars-Sinai v. Superior Court,* (1998) 18 Cal.4th 1, was a case wherein the court refused to create a separate tort cause of action for intentional spoilation of evidence, observing it would be impossible for the jury to assess the role the missing

evidence would have played in the determination of the underlying action. (Published Opn. at p. 14, footnote 6) The other two cases cited in support of its position, *Viner v. Sweet*, (2003) 30 Cal.4th 1232, and *Wiley v. County of San Diego*, (1998) 19 Cal.4th 532, are legal malpractice cases involving an entirely different causation standard.[3] Once again, State Farm suggests that if the legal malpractice standard were used in this case, Village Northridge would be forced to show what the agreement between the parties would have been had the representations regarding limits not been made. So stipulated. What State Farm fails to mention is that the causation standard used in legal malpractice cases is not the same as that used in this fraud case. Furthermore, causation is a question of fact to be determined at summary judgment or trial, not at demurrer. As such, these cases are inapposite.

Furthermore, it is not as though the damages in this case are inherently speculative; they will be based on the amount of policy benefits

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[3] In fact, *Wiley v. County of San Diego, supra*, is a case involving a criminal defendant's legal malpractice case against his public defender and the county, wherein the Court held that the plaintiff was required to prove actual innocence by a preponderance of the evidence as an element of his malpractice claim. The eloquent quotation from *Wiley* appearing at page 9 of State Farm's Petition ["The mental gymnastics required to reach an intelligent verdict would be difficult to comprehend much less execute"] is referring to the difficulty of reaching a verdict which would follow if the plaintiff/former criminal defendant were not required to prove his actual innocence. *Id.* at 544.

available under the subject insurance contract for the loss in question. The amount of damages, based on the amount which the parties would have settled had Village Northridge known the actual policy limits, will be determined the same way damages are determined by most any other case – via competing expert witnesses and with whatever empirical or statistical evidence is marshalled and presented.

6. CONCLUSION

After the Court of Appeal published its unanimous decision, State Farm has twice petitioned the Court of Appeal for rehearing and was appropriately denied both times. It is evident that State Farm is not comfortable with the Court of Appeal's decision. Any other insurer who fraudulently misrepresents its policy limits would be similarly uncomfortable. This does not render the decision erroneous. The Court of Appeals applied an existing rule of law to a set of facts fairly distinguishable from those stated in prior published opinions. Thus, review is not necessary to secure uniformity of decisional law. Furthermore, review would be unsound in that it would permit State Farm and potentially other insurers to use this Court and the lower courts to further an agenda of tolerating misrepresentation of policy limits by precluding any remedy for the crime in instances where a release is involved. The public policy

favoring settlement would only be hindered by a contrary result. Village Northridge respectfully submits that the Court of Appeal's decision was properly decided that State Farm's Petition for Review should be summarily denied.

March 10, 2008

Respectfully Submitted:
ENGSTROM, LIPSCOMB & LACK

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BRIEF FORMAT CERTIFICATION PURSUANT TO CALIFORNIA *RULES OF COURT*, RULE 8.204(c)

Pursuant to California *Rules of Court*, Rule 8.204(c), I certify that Appellants' Answer to Petition for Review is proportionately spaced, has a typeface of 13 points and contains 2,103 words, including footnotes.

March 10, 2008

Respectfully Submitted:
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PROOF OF SERVICE

STATE OF CALIFORNIA)
)
COUNTY OF LOS ANGELES)

I am employed in the County of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is 10100 Santa Monica Boulevard, 16th Floor, Los Angeles, California 90067-4107. On March 10, 2008, I served the foregoing document described as **ANSWER TO PETITION FOR REVIEW** placing a true copy thereof enclosed in a sealed envelope addressed as follows:

** SEE ATTACHED MAILING LIST **

__X__ (BY MAIL) I deposited such envelope in the mail at Los Angeles, California. The envelope was mailed with postage thereon fully prepaid. I am "readily familiar" with the firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. Postal Service on that same date in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than one day after date of deposit for mailing in affidavit.

__X__ STATE: I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed on March 10, 2008 at Los Angeles, California.

Yvonne R. Thompson

YVONNE R. THOMPSON

SERVICE LIST

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2nd Civil No. B188718

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