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UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF CALIFORNIA

CAROLINA CASUALTY INSURANCE)
COMPANY, a California)
Professional Corporation)

Plaintiff,)
v.)

JONES HELSLEY, PC, a)
California Professional)
Corporation; TIMOTHY JONES)
ESQ., a California)
Resident; JACK HINDMARSH,)
ESQ., a California)
Resident, JACK HINDMARSH,)
PLC, a California)
Professional Law)
Corporation; and DOES 1-45,)
inclusive,)

Defendants.)

1:10-cv-00916-LEW

**ORDER Re: Plaintiff
Carolina Casualty
Insurance Company's
Motion to Set Aside Stay
Based on Material
Developments in the
Underlying Action
Demonstrating No
Potential for Coverage
[85]**

Before the Court is Plaintiff Carolina Casualty Insurance Company's ("Plaintiff") Motion to Set Aside Stay Based on Material Developments in the Underlying Action Demonstrating No Potential for Coverage [85]. The Motion was originally set for hearing before

1 Magistrate Judge Michael J. Seng in the Eastern
2 District of California on December 13, 2011. Before
3 the hearing, Magistrate Judge Seng recused himself from
4 this Action, and the hearing was vacated [99]. On
5 January 9, 2012, however, the Ninth Circuit reassigned
6 all further proceedings in this Action to this Court
7 [100], and the Matter was taken under submission on
8 February 8, 2012. Having reviewed all the papers and
9 arguments submitted pertaining to this Motion, **THE**
10 **COURT NOW FINDS AND RULES AS FOLLOWS:**

11 The Court hereby **DENIES** Plaintiff's Motion to Set
12 Aside Stay.

13 I. BACKGROUND

14 This Action stems from a legal malpractice action,
15 entitled James A. Bratton and Bratton Investments, LLC
16 v. Timothy Jones, et al. ("Bratton Action" or "the
17 Underlying Action"), filed in the Fresno County
18 Superior Court by a third-party against Defendants from
19 the instant Action, which include: Jones Helsley PC,
20 Timothy Jones, Esq., Jack Hindmarsh, Esq. and Jack
21 Hindmarsh PLC ("Defendants"). In the instant Eastern
22 District of California Action, Plaintiff Carolina
23 Casualty Insurance Company ("Plaintiff"), a legal
24 malpractice insurer for Defendants, seeks a judicial
25 declaration that it had no duty to defend or indemnify
26 Defendants in the Underlying Action.

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1 **A. The Instant Eastern District Action**

2 Plaintiff is an insurance company that provides
3 legal malpractice insurance for attorneys. Defendants
4 are two attorneys and their respective law firms that
5 purchased insurance coverage from Plaintiff. In the
6 instant Action, Plaintiff has sought declaratory relief
7 that it has no duty to defend or indemnify Defendants
8 from liability in the Underlying Action. Plaintiff
9 asserts that two exclusions, Exclusions E and F, from
10 Plaintiff's Lawyers Professional Insurance Policy No.
11 9904986 (the "CCIC Policy" or the "Policy") bar
12 insurance coverage in the Underlying Action.

13 On October 21, 2010, Defendants filed a Motion for
14 a Stay of All Proceedings Pending Resolution of
15 Underlying Action [29]. On January 13, 2011,
16 Magistrate Judge Michael J. Seng issued Findings and
17 Recommendations recommending that Defendants' Motion to
18 Stay be Granted [66]. However, Magistrate Judge Seng
19 recommended that Plaintiff be given the right to seek
20 relief from the stay "if and when it in good faith
21 believes and represents that circumstances have changed
22 so that the reasons for stay no longer exist, provided
23 no such motion for relief from the stay be initiated
24 for at least six months." On February 25, 2011,
25 Eastern District Judge O'Neill adopted Magistrate Judge
26 Seng's Recommendations after de novo review. On
27 November 4, 2011, Plaintiff filed the present Motion to
28 Set Aside Stay Based on Material Developments in the

1 Underlying Action Demonstrating No Potential for
2 Coverage [85].

3 On January 9, 2012, this case was reassigned to
4 this Court for all further proceedings, including
5 adjudication of the Present Motion [100].

6 **B. The Underlying Action**

7 In the Underlying Action, filed in the Fresno
8 Superior County Court, third-parties James Bratton and
9 his company, Bratton Investments LLC ("the Bratton
10 plaintiffs") were allegedly involved in the development
11 of certain real properties in Selma, Merced, and
12 Kingsburg, California. In 2005, the Bratton plaintiffs
13 engaged Defendant Timothy Jones, Esq. ("Defendant
14 Jones") and his predecessor law firm to Defendant Jones
15 Helsley PC ("Defendant J&H") to provide legal services
16 in connection with the formation of various LLCs
17 corresponding to each real estate development venture.
18 The Bratton plaintiffs allege that Defendant Jack
19 Hindmarsh, Esq. ("Defendant Hindmarsh"), an independent
20 contract attorney that Defendant J&H retains for
21 transactional work, also assisted with the formation of
22 the LLCs. Defendant Hindmarsh PLC is the professional
23 law corporation for Defendant Hindmarsh's law firm.

24 The Bratton plaintiffs allege that Defendant Jones,
25 among others, performed all legal services necessary to
26 form and create various LLCs, including Selma Crossings
27 LLC ("Selma LLC") and Merced Gateway LLC ("Merced
28 LLC"). When these LLCs were organized, Defendant Jones

1 allegedly received a membership/ownership interest in
2 both LLCs. Subsequently, in 2008, Defendant Jones
3 allegedly transferred his interest in these two LLCs to
4 Central Pacific Ventures LLC ("CPV"), an LLC in which
5 Defendant Jones allegedly holds a fifty percent
6 membership interest. The Bratton plaintiffs further
7 allege that in late 2008, the Bratton plaintiffs
8 transferred their ownership interest in both Selma LLC
9 and Merced LLC to a third party. The Bratton
10 plaintiffs allege that this was a proximate result of
11 their reliance on Defendants Jones and Hindmarsh. The
12 Bratton Plaintiffs state that the sale of their shares
13 in these entities was for a purchase price sum far
14 below the fair market value.

15 **II. ANALYSIS**

16 **A. Judicial Notice and Evidentiary Objections**

17 As a preliminary matter, both parties have filed
18 requests for this Court to take judicial notice of
19 certain documents relevant to its papers. Defendant
20 has also made evidentiary objections to the Declaration
21 of Chad B. Wootton, Plaintiff's attorney.

22 1. Requests for Judicial Notice

23 Plaintiff asks the Court to take Judicial Notice of
24 the Second Amended Complaint filed in the Underlying
25 Action. Defendants have asked the Court to take
26 Judicial Notice of a November 30, 2011 order by the
27 trial judge in the Underlying Action adopting a
28 "tentative order Re: Motion to Disqualify, Set Aside,

1 to Strike, and to Unseal." Pursuant to Federal Rule of
2 Evidence 201, the Court has discretion to take judicial
3 notice of a court record in another court, such as
4 those that are directly relevant to the matter at
5 issue. United States ex rel. Robinson Rancheria
6 Citizens Council v. Borneo, Inc., 971 F.2d 244, 248
7 (9th Cir. 1992)("we may take notice of proceedings in
8 other courts, both within and without the federal
9 judicial system, if those proceedings have a direct
10 relation to matters at issue."). Here, the Court finds
11 that the two records from the Underlying Action are
12 directly relevant to this Motion. As such the Court
13 **GRANTS** both requests for judicial notice.

14 2. Evidentiary Objections

15 Defendants have made evidentiary objections to a
16 statement and two Exhibits attached to the Declaration
17 of Chad B. Wootton.

18 First, Defendants object to Exhibit G, which is the
19 entire "Declaration of Howard A. Sagaser in Support of
20 Opposition of Defendants' Motion to Compel." The Court
21 **SUSTAINS** Defendants' hearsay objection as Plaintiff has
22 offered Exhibit G for the truth of the matter asserted,
23 which is to prove Defendant Jones's relationship with
24 Selma LLC.

25 Second, Defendants object to portions of Exhibit H,
26 which are excerpts from a deposition transcript of
27 Howard Sagaser, a former partner to the law firm of

1 Defendant J&H. The Court **OVERRULES** Defendants'
2 objections. More specifically, the Court finds that
3 Howard Sagaser's testimony has foundation and is not
4 hearsay.

5 Third, Defendants object to paragraph 9 of Chad B.
6 Wootton declaration. The **OVERRULES** Defendants'
7 objections as **MOOT** given that this testimony is not
8 necessary for the Court's analysis.

9 **III. DISCUSSION**

10 As a preliminary matter, before the Court analyzes
11 the merits of the present Motion, the Court reviews
12 whether a stay was appropriate in the first place.
13 When a declaratory relief action regarding the duty to
14 defend depends on insurance coverage issues, it may be
15 that the resolution of those issues may severely
16 prejudice the insured in the underlying litigation.
17 Great Am. Ins. Co. v. Superior Court, 178 Cal. App. 4th
18 221, 235 (2009); Montrose Chemical Corp. of Calif. v.
19 Superior Court, 6 Cal. 4th 287, 302 (1994) ("Montrose
20 I").

21 This prejudice arises due to the potential
22 consequences that can result due to collateral
23 estoppel. If the declaratory relief action is tried
24 before the underlying litigation is concluded, the
25 insured may be collaterally estopped from relitigating
26 any adverse factual findings in the underlying
27 litigation. Montrose Chemical Corp. of Calif. v

1 Superior Court, 25 Cal. App. 4th 902, 910 (Ct. App.
2 1994) ("Montrose II"). On the other hand, any
3 favorable findings for the insured could not be used by
4 the insured against the opposing party in the
5 underlying litigation. Id. Accordingly, to prevent
6 this unfair result for an insured, a stay in a
7 declaratory relief action is mandatory if the factual
8 issues to be resolved in the declaratory relief action
9 overlap with the issues to be resolved in the
10 underlying action. Great Am. Ins., 178 Cal. App. 4th
11 at 235.

12 As such, in determining whether the stay was
13 appropriate, the Court must first determine whether
14 there are overlapping factual issues between the
15 instant declaratory relief Action and the Underlying
16 Action. This can be done by first identifying the
17 factual issues in the instant Action and then comparing
18 them to the factual issues in the Underlying Action.

19 In the instant Action, Plaintiff primarily argues
20 that Exclusions E and F in the "Lawyers's Professional
21 Insurance Policy" signed with Defendants excuse
22 Plaintiff from covering Defendants in the Underlying
23 Action. Thus, the factual issues to be resolved in
24 this instant Action involve issues of fact pertaining
25 to the applicability of Exclusion E and F.

26 More specifically, Exclusion E provides, in
27 pertinent part, that Plaintiff does not have to provide
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1 coverage for Defendants for any action:

2 based upon, arising out of, directly or indirectly
3 resulting from or in consequence of, or in any way
4 involving any Insured's activities as an officer,
5 director, partner, trustee, or employee of a
6 business enterprise.

7 As applied to the facts of the Underlying Action, the
8 factual issue to be resolved in determining whether
9 Exclusion E applies is whether: (1) Defendant Jones is
10 an officer, director, partner, trustee, or employee of
11 any of the relevant business entities, such as CPV,
12 Selma LLC, or Merced LLC and (2) the claim stemmed from
13 activities that Defendant Jones did in those roles.

14 As for Exclusion F, the Contract provides that
15 Plaintiff will be excluded from coverage
16 responsibilities for any action:

17 by or in connection with any business enterprise .
18 . . in which the Insured owns more than a 10
19 percent interest, or in which any insured is an
20 owner, partner, or employee, or which is directly
21 or indirectly controlled, operated, or managed by
22 any Insured, other than solely in a fiduciary
23 capacity, but only if the act or omission in
24 dispute is in the rendering of services ordinarily
25 performed as a lawyer, and then only to the extent
26 of such services.

1 In this case, for Exclusion F to apply, the underlying
2 factual issues involve whether: (1) Defendant Jones
3 owned more than a 10 percent interest in any of the
4 aforementioned companies, (2) Defendant Jones is an
5 owner, partner, or employee of those companies, (3)
6 Defendant Jones acted in a fiduciary capacity, and (4)
7 Defendant Jones acted in a capacity as a lawyer.

8 Here, the Court finds that the factual issues that
9 are involved with determining the applicability of
10 Exclusion E and F significantly overlap with issues
11 raised in the Underlying Action. In the Underlying
12 Action, the complaint has gone through two amendments
13 since the time of the original stay. In the original
14 complaint examined by Magistrate Judge Seng and Judge
15 O'Neill, the Bratton plaintiffs alleged that some of
16 the Defendants were officers, directors, and/or
17 trustees of various LLCs. Moreover, the Bratton
18 plaintiffs alleged that some of the Defendants breached
19 their fiduciary duties and used their positions in the
20 LLCs to defraud the Bratton plaintiffs. As such,
21 liability for Defendants in the Underlying Action
22 involved a factual determination of (1) whether
23 Defendants were actually officers, directors, and/or
24 trustees of the relevant LLCs and (2) if they breached
25 any fiduciary duty owed to the Bratton plaintiffs in
26 their roles with the LLCs. Similarly, in the instant
27 Action, the factual issues that are yet to be resolved

1 include (1) whether Defendant Jones's business or
2 ownership role in the relevant LLCs and (2) whether the
3 claims arose out of Defendant Jones' role in those
4 companies. Thus, both the Underlying Action and the
5 instant Action involve a yet to be made factual
6 determination of Defendant Jones's role, if any, with
7 the relevant LLCs.

8 Accordingly, because of the significant factual
9 overlap between both actions, the Court finds that
10 allowing the instant Action to proceed before
11 resolution of the pertinent factual issues in the
12 Underlying Action would result in extreme prejudice to
13 Defendants. Due to principles of collateral estoppel,
14 a determination of the factual issues in the Underlying
15 Action would leave Defendants in a no-win position.

16 As such, the Court finds that Magistrate Judge Seng
17 and Judge O'Neill were correct in instituting a stay
18 pending either a resolution in the Underlying Action or
19 "until circumstances have changed such that the
20 elements of Exclusions E [and F] are no longer in
21 dispute in the Underlying Action or no longer can be
22 legitimately disputed."

23 As to the merits of this Motion, although a year
24 has passed since the original stay order, the Court
25 finds that the stay should not be lifted at this time.
26 The Court finds that the same concerns that mandated
27 the stay in the first place have yet to be resolved.

1 The most current iteration of the complaint in the
2 Underlying Action, a Second Amended Complaint ("Bratton
3 SAC"), alleges, in pertinent part (1) that officers of
4 CPV breached their fiduciary duty to Defendants and (2)
5 that Defendant Jones manages/controls CPV. Bratton SAC
6 ¶ 29. Moreover, the Bratton SAC continues to allege
7 that Defendant Jones is a manager of Selma LLC, Merced
8 LLC, and Kingsburg LLC and that Defendant Jones owed
9 fiduciary duties to the Bratton plaintiffs who were co-
10 owners of those same three companies. Bratton SAC ¶
11 25. Accordingly, the Underlying Action still involves
12 a factual determination of whether Defendant Jones was
13 a manager of the relevant LLCs. As before, a
14 determination in the instant Action of the factual
15 issues pertinent for Exclusions E and F could
16 potentially prejudice Defendants. Thus, this Court
17 finds that a stay should remain until resolution of the
18 Underlying Action or until there is at least a
19 significant change in the Underlying Action.

20 Plaintiff argues, however, that significant
21 developments have occurred in the Underlying Action,
22 which have resolved the overlapping factual issues.
23 The Court, however, finds Plaintiff's argument without
24 merit. As support, Plaintiff relies on a "Report and
25 Recommendation of Discovery Referee," (hereafter "Entry
26 of Discovery Order") that allegedly make findings
27 regarding Defendant Jones's management role in various

1 LLCs. The Court, however, finds that the Entry of
2 Discovery Order was not a finding of fact by the trial
3 court in the Underlying Action. At issue in the Entry
4 of Discovery Order was whether certain discovery could
5 be compelled. The discovery referee was not tasked
6 with making a factual determination as to the
7 ownership, control, or management of the entities. As
8 such, the Court finds that the Entry of Discovery Order
9 did not resolve any of the factual issues, which
10 warranted the stay in the instant Action.

11 On the contrary, the Court finds that the
12 overlapping factual issues are still at dispute in the
13 Underlying Action. On November 4, 2011, more than two
14 months after the Entry of the Discovery Order, the
15 trial court in the Underlying Action issued a ruling
16 stating that “[i]f [Defendant] Jones did something else
17 as an agent or controlling manager of one or more of
18 the [LLCs], that is not clearly alleged.” In other
19 words, when Plaintiff filed the present Motion,
20 Defendant Jones’s role in the relevant LLCs still had
21 not been sufficiently alleged, much less conclusively
22 determined. Though the Bratton plaintiffs have since
23 filed the Bratton SAC to address the issues in the
24 November 4, 2011 ruling, in the instant Action,
25 Plaintiff still has not proffered any ruling as of the
26 date of this Order that has conclusively resolved
27 whether Defendant Jones was a manager with any of the

1 relevant LLCs.

2 Plaintiff argues that the Court should find that
3 Defendant Jones's management and control of the
4 relevant LLCs can no longer be legitimately disputed.
5 As support, Plaintiff points to various corporate
6 documents and declarations from Defendant Jones himself
7 that allegedly indicate Defendant Jones's role as a
8 manager. The Court finds that the majority of these
9 items were already considered by Magistrate Judge Seng
10 in January and in February, when Judge O'Neill adopted
11 the Stay Order. The present Motion seems to rehash
12 many of the arguments made in support of Plaintiff's
13 Opposition to the original Motion to Stay, Objections
14 to Findings and Recommendations of Magistrate Judge
15 Seng, and in a Sur-Reply. In all the filings,
16 Plaintiff repeated that a stay was improper because
17 various corporate documents and declarations show that
18 Defendant Jones managed the relevant LLCs. Both
19 Magistrate Judge Seng and Judge O'Neill did not find
20 these arguments convincing, and this Court does not
21 find these arguments persuasive here.

22 IV. CONCLUSION

23 For the foregoing reasons, the Court hereby **DENIES**
24 Plaintiff's Motion to Set Aside Stay Based on Material
25 Developments in the Underlying Action Demonstrating No
26 Potential for Coverage. Furthermore, the Court hereby
27 orders that:

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- 1 1. The stay shall remain in place until the
- 2 Underlying Action is resolved;
- 3 2. Plaintiff may seek relief from the stay if and
- 4 when it in good faith believes and represents
- 5 that circumstances have changed so that the
- 6 reason for stay no longer exists;
- 7 3. Such motion for relief from stay, however,
- 8 cannot be initiated by Plaintiff within six
- 9 months of the date of this Court's Order.
- 10 4. The Parties shall continue to follow Judge
- 11 O'Neill's Order to file a joint report
- 12 outlining the status of the Underlying Action
- 13 every sixty days. If the Underlying Action is
- 14 resolved at any time, the Parties shall
- 15 promptly notify the Court.

16
17 **IT IS SO ORDERED.**

18 DATED: March 14, 2012

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20 RONALD S.W. LEW

21 **HONORABLE RONALD S.W. LEW**
22 Senior, U.S. District Court Judge
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