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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

LIBERTY MUTUAL INSURANCE)
CO., a Massachusetts Corp.,)
Plaintiff(s),)
v.)
UPA CALIFORNIA, a California)
general partnership, et al.,)
Defendant(s).)

No. C08-0611 BZ

**ORDER GRANTING IN PART AND
DENYING IN PART PLAINTIFF'S
MOTION TO DISMISS FIRST
AMENDED COUNTERCLAIM**

Plaintiff and counter-defendant Liberty Mutual Insurance Company ("Liberty") has moved to dismiss defendants UPA Group, L.C.'s, Amako Resort Construction (U.S.), Inc.'s, and Amir Etemadi's ("defendants") first amended counterclaim ("counterclaim") for failure to state a claim upon which relief can be granted.¹ Defendants' counterclaim alleges common law breach of contract; breach of the implied covenant of good faith and fair dealing; negligence and negligent performance of a contract; misrepresentation; and declaratory

¹ All parties have consented to my jurisdiction, for all proceedings including entry of final judgment, pursuant to 28 U.S.C. § 636(c).

1 relief. By Order dated November 18, 2008, I granted Liberty's
2 first motion to dismiss defendant's original counterclaim, and
3 specified the particular areas of the counterclaim that were
4 deficient. (See Doc. No. 47.) For the following reasons,
5 Liberty's motion is **DENIED IN PART AND GRANTED IN PART.**

6 *Breach of Contract and Breach of the Implied Covenant*

7 Defendants' counterclaim for breach of contract and
8 breach of the implied covenant of good faith and fair dealing²
9 alleges that Liberty breached paragraph Thirteen of the
10 Indemnity Agreement which states, in part, that "[Liberty]
11 shall have the right, at its option and sole discretion, to
12 adjust, settle or compromise any claim, demand suit or
13 judgment upon any Bond." (Pl.'s First Amend. Compl. Exh. 1.
14 ¶ 13.) The counterclaim alleges, among other things, that
15 Liberty first represented to defendants that the claims
16 against them were without merit, that it would deny all of
17 the City Walk Project owner's claims against the bond and
18 that the City Walk Project owner would be obligated to pay
19 defendants. The counterclaim further alleges that Liberty
20 ceased communicating with defendants and prohibited them from
21 attending meditations at which Liberty "grossly overpaid" the
22 City Walk Project claimants and that in so doing, "Liberty
23 breached the [Indemnity Agreement] by its failure to settle
24 the claims . . . with the required skill, reasonable

25
26 ² I see no difference between defendants first and
27 second claims for relief. Both claims allege that Liberty
28 breached an implied term of the Indemnity Agreement by grossly
overpaying claims and by failing to use care, skill, reasonable
experience, and faithfulness in settling the claims.

1 expedience and faithfulness required of it under California
2 law." (Def.'s First Amend. Counterclaim ¶¶ 21-27, 34.)³ The
3 counterclaim further alleges that defendants were not
4 informed that Liberty had paid twenty-five million dollars to
5 settle the City Walk Project claim until the initial case
6 management conference in this action. (Id. at ¶ 29.)

7 Accepting as true all material allegations, as well as
8 all reasonable inferences to be drawn from them, so as to
9 construe the pleading in the light most favorable to the
10 non-moving party, I find that defendants have sufficiently
11 pled a claim for breach of the implied covenant of good faith
12 and fair dealing in the Indemnity Agreement. "Every contract
13 imposes upon each party a duty of good faith and fair dealing
14 in its performance and its enforcement." Carma Developers,
15 Inc. v. Marathon Dev. California, Inc., 2 Cal.4th 342, 371
16 (1992). While the Indemnity Agreement gives Liberty broad
17 discretion to settle all outstanding claims against
18 defendants, it does not relieve it of the implied obligation
19 to exercise its discretion in good faith. "The covenant of
20

21 ³ When ruling on a motion to dismiss, if the Court
22 "considers evidence outside the pleadings, it must normally
23 convert the 12(b)(6) motion into a Rule 56 motion for summary
24 judgment, and it must give the nonmoving party an opportunity
25 to respond." U.S. v. Ritchie, 342 F.3d 903, 907 (9th Cir.
26 2003); Fed. R. Civ. P. 12(b). However, "documents whose
27 contents are alleged in a complaint and whose authenticity no
28 party questions, but which are not physically attached to the
pleading, may be considered in ruling on a Rule 12(b)(6) motion
to dismiss." Branch v. Tunnell, 14 F.3d 449, 454 (9th Cir.
1994) (overruled on other grounds in Marder v. Lopez, 450 F.3d
445 (9th Cir. Cal. 2006)). Here, neither party questions the
authenticity of the Indemnity Agreement. Accordingly, I may
consider the terms of the Indemnity Agreement in ruling on
defendants' motion to dismiss.

1 good faith finds particular application in situations where
2 one party is invested with a discretionary power affecting
3 the rights of another. Such power must be exercised in good
4 faith." Id. at 372.

5 This is consistent with the general rule that a surety
6 is not entitled to indemnification for any payments made
7 fraudulently or without good faith. See Arntz Contracting
8 Co. v. St. Paul Fire & Marine Ins. Co., 47 Cal.App.4th 464
9 (1996) ("A surety is not entitled to indemnification for
10 amounts paid in settlement of claims upon its bonds if the
11 settlement is not made in good faith.").⁴ Defendants have
12 sufficiently alleged that Liberty did not exercise its
13 discretion to settle the City Walk Project claim in good
14 faith; therefore, Liberty's motion to dismiss defendants'
15 first and second claims for relief is **DENIED**.

16 *Negligence and Negligent Performance of Contract*

17 Defendants also seek to recover tort damages for
18 Liberty's alleged breach of the implied covenant of good
19 faith and fair dealing. Liberty argues that defendants'
20 claims for negligence and negligent performance of contract
21 must be dismissed because defendants' only negligence
22 allegations are based on Liberty's alleged breach of the
23 Indemnity Agreement, which is a breach of contract, not a
24 tort. In California, "conduct amounting to a breach of
25 contract becomes tortious only when it also violates a duty

26
27 ⁴ Liberty's reliance on Travelers Casualty & Surety Co.
28 of Amer. v. Amoroso, 2004 WL 1918890 (N.D. Cal.) is misplaced
since Amoroso, does not discuss or cite to Arntz, the state
court ruling most on point.

1 independent of the contract arising from principles of tort
2 law." Erlich v. Menezes, 21 Cal.4th 543, 551 (1999) (citing
3 Applied Equip. Corp. v. Litton Saudi Arabia Ltd., 7 Cal.4th
4 503, 515 (1994)).⁵ Defendants do not allege that Liberty owed
5 them a duty independent of the Indemnity Agreement, and the
6 California Supreme Court has declined to extend tort
7 liability to the breach of a construction performance bond.
8 Cates Construction, Inc. v. Talbot Partners, 21 Cal.4th 28,
9 44-45 (1999).⁶ Here, because defendants allege only a surety
10 relationship with Liberty to support their negligence claim,
11 Liberty's motion to dismiss defendants' third claim for
12 relief is **GRANTED**.

13 *Negligent Misrepresentation*

14 Liberty next argues that defendants' counterclaim for
15 misrepresentations should be dismissed for failure to meet
16 the particularity requirements of Rule 9(b).⁷ Without
17 deciding whether Rule 9(b)'s heightened pleading standards
18 apply to claims for negligent misrepresentation, I find that

20 ⁵ Defendants' reliance on Eads v. Marks, 39 Cal.2d 807,
21 811 (1952) is misplaced. Eads has been refuted by later
22 California case law that establishes the independent duty
23 requirement.

23 ⁶ Defendants mistakenly rely on North American Chemical
24 Co. v. Superior Court, 59 Cal.App.4th 764 (1997), for the
25 proposition that negligent performance of a contract may be a
26 breach of contract or a tort, and a party may assert both
27 claims until the appropriate time for an election of remedies.
28 While that statement may be true in certain contexts, Menezes
and Cates Construction, decided after North American Chemical,
make clear that this is not one of them.

27 ⁷ Rule 9(b) requires that "in all averments of fraud or
28 mistake, the circumstances constituting fraud or mistake shall
be stated with particularity." Fed. R. Civ. Proc. 9(b).

1 defendants have adequately pled a claim for negligent
2 misrepresentation. "Rule 9(b) particularity requirements
3 must be read in harmony with Federal Rule of Civil Procedure
4 8's requirement of a 'short and plain' statement of the
5 claim" so that a pleading is sufficient under Rule 9(b) if
6 "it identifies the circumstances constituting the
7 misrepresentation so that the defendant can prepare an
8 adequate answer from the allegations." Berger v. Seyfarth
9 Shaw, LLP, Case No. 07-05279, 2008 WL 4067436 at *1 (N.D.
10 Cal. Aug. 28, 2008) (quoting Neubronner v. Milken, 6 F.3d 666,
11 671 (9th Cir. 1993)). Here, defendants have sufficiently
12 alleged facts regarding the nature of Liberty's
13 misrepresentations such that Liberty can prepare an adequate
14 answer. (See Amend. Counterclaim ¶¶ 12-14, 21-29.)
15 Accordingly, Liberty's motion to dismiss defendants' fourth
16 claim for relief is **DENIED**.⁸

17 *Declaratory Relief*

18 An action for declaratory judgment is procedural in
19 nature and purpose. A federal court exercising diversity
20 jurisdiction follows federal procedural rules and, thus,
21 federal law determines the rules to apply to a request for
22 declaratory judgment relief in a given case. Golden Eagle
23 Ins. Co. v. Travelers Cos., 103 F.3d 750, 753 (9th Cir.
24 1996), *overruled on other grounds by Gov't Employees. Ins.*

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26 ⁸ To the extent that defendants are claiming that
27 Etemadi was induced to enter into the Indemnity Agreement in
28 his individual capacity by the misrepresentation that Liberty
would also induce Anderson to do the same, I do not read
paragraphs ten and sixteen of the Indemnity Agreement as
barring that claim as a matter of law.

1 Co. v. Dizol, 133 F.3d 1220 (9th Cir. 1998); see also Federal
2 Kemper Ins. Co. v. Rauscher, 807 F.2d 345, 352 (3d Cir.
3 1986). "The Declaratory Judgment Act confers on federal
4 courts unique and substantial discretion in deciding whether
5 to declare the rights of litigants." Wilton v. Seven Falls
6 Co., 515 U.S. 277, 286-87(1995); Greater Los Angeles Council
7 on Deafness, Inc. v. Zolin, 812 F.2d 1103, 1112 (9th Cir.
8 1987) (citing Doe v. Gallinot, 657 F.2d 1017, 1024 (9th Cir.
9 1981)). Pursuant to section 2201, any court "may declare the
10 rights and other legal relations of any interested party
11 seeking such declaration, whether or not further relief is or
12 could be sought." 28 U.S.C. § 2201 (a).

13 The Declaratory Judgment Act ("DJA") permits a federal
14 court to "declare the rights and other legal relations" of
15 parties to "a case of actual controversy." 28 U.S.C. § 2201;
16 see Wickland Oil Terminals v. Asarco, Inc., 792 F.2d 887, 893
17 (9th Cir. 1986). "A declaratory judgment is inappropriate
18 solely to adjudicate past conduct." Delaware State
19 University Student Housing Foundation v. Ambling Management
20 Co., 556 F.Supp.2d 367, 374-4 n.52 (D. Del. 2008); see also
21 Alpine Group, Inc. v. Johnson, Case No. 01-5532, 2002 WL
22 10495, at *4 (S.D.N.Y. Jan. 3, 2002). Because defendants are
23 not entitled to declaratory relief with respect to past
24 wrongs, Liberty's motion to dismiss defendants' claim for
25 declaratory relief regarding the City Walk Project is
26 **GRANTED**; however, to the extent that defendants also seek
27 declaratory relief with respect to the Curry Village Project,
28 Liberty's motion is **DENIED**.

1 Liberty shall file an answer by March 2, 2009.

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3 Dated: February 13, 2009



4 Bernard Zimmerman
5 United States Magistrate Judge
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8 G:\BZALL\BZCASES\LIBERTY MUTUAL V. UPA CALIFORNIA\ORDER ON MOTION TO DISMISS
9 AMENDED COUNTERCLAIM.FINAL ORDER.wpd

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