

1
2 UNITED STATES DISTRICT COURT
3 FOR THE NORTHERN DISTRICT OF CALIFORNIA
4 OAKLAND DIVISION
5

6 THE BURLINGTON INSURANCE
7 COMPANY, et al.,

8 Plaintiffs,

9 vs.

10 DEVDHARA, et al.,

11 Defendants.

Case No: C 09-00421 SBA

**ORDER REGARDING PLAINTIFFS'
MOTION FOR SUMMARY
JUDGMENT AND/OR PARTIAL
SUMMARY JUDGMENT**

[Docket 49]

12 The parties are presently before the Court on Plaintiffs' Motion for Summary Judgment
13 and/or Partial Summary Judgment. (Docket 49.) Having read and considered the papers filed
14 in connection with this matter, and having considered counsel's arguments at the July 14, 2010
15 hearing, and being fully informed, the Court hereby GRANTS IN PART and DENIES IN
16 PART the motion for the reasons set forth below.

17 **I. BACKGROUND**

18 **A. THE INSURANCE POLICIES**

19 Plaintiff The Burlington Insurance Company ("TBIC") issued two commercial general
20 liability insurance policies to Defendants: 1) policy number 157V000851, issued to Defendants
21 Devdhara and Thakor dba Auburn Hotel, covering the policy period 2/28/05 through 2/28/06;
22 and 2) policy number 150B005234, issued to Defendants Devdhara and Thakor, and Auburn
23 Hotel, covering the policy period of 3/2/07 through 3/2/08 ("TBIC Policies"). (Creighan Decl.,
24 ¶ 2, Exs. 1, 2.)

25 Plaintiff First Financial Insurance Company ("FFIC") also issued two commercial
26 general liability insurance policies to Defendants: policy number 157F000308, issued to
27 Defendants Devdhara dba Auburn Hotel, covering the policy period 2/28/03 through 2/28/04;
28 and 2) policy number 157F000681, issued to Defendants Devdhara and Thakor dba Auburn

1 Hotel, covering the policy period of 2/28/04 through 2/28/05 (“FFIC Policies”). (Id., ¶ 3, Exs.
2 3, 4.)

3 The TBIC and FFIC Policies (collectively, “the Policies”) provided Defendants with
4 liability coverage under the following pertinent provisions:

5 **SECTION I – COVERAGES**

6 **COVERAGE A. BODILY INJURY AND PROPERTY DAMAGE LIABILITY**

7 **1. Insuring Agreement**

8 a. We will pay those sums that the insured becomes legally obligated to pay
9 as damages because of “bodily injury” or “property damage” to which this insurance
10 applies. We will have the right and duty to defend the insured against any “suit”
11 seeking those damages. However, we will have no duty to defend the insured against
12 any “suit” seeking damages for “bodily injury” or “property damage” to which this
insurance does not apply. We may, at our discretion, investigate any “occurrence” or
settle any claim or “suit” that may result. But: ...

13 b. This insurance applies to “bodily injury” or “property damage” only if:

14 (1) The “bodily injury” or “property damage” is caused by an
15 “occurrence” that takes place in the “coverage territory”;

16 **2. Exclusions**

17 This insurance does not apply to:

18 **a. Expected or Intended Injury**

19 “Bodily injury” or “property damage” expected or intended from the
20 standpoint of the insured. This exclusion does not apply to “bodily injury”
21 resulting from the use of reasonable force to protect persons or property.

22 **COVERAGE B. PERSONAL AND ADVERTISING INJURY LIABILITY**

23 **1. Insuring Agreement**

24 a. We will pay those sums that the insured becomes legally obligated to pay
25 as damages because of “personal injury” or “advertising injury” to which this insurance
26 applies. We will have the right and duty to defend the insured against any “suit”
27 seeking damages. However, we will have no duty to defend the insured against any
28 “suit” seeking damages for “personal and advertising injury” to which this insurance
does not apply. We may, at our discretion, investigate any offense and settle any claim
or “suit” that may result. ...

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2. Exclusions

This insurance does not apply to:

- a. Knowing Violation of Rights of Another - “Personal and advertising injury” caused by or at the direction of the insured with the knowledge that the act would violate the rights of another and would inflict “personal and advertising injury.”
...

EXCLUSIONS - PUNITIVE DAMAGES

This insurance does not apply to any claim of or indemnification for punitive or exemplary damages. If a “suit” seeking both compensatory and punitive or exemplary damages has been brought against you for a claim covered by this policy, we will provide defense for such action. We will not have any obligation to pay for any costs, interest or damages attributable to punitive or exemplary damages.

SECTION V - DEFINITIONS

3. “Bodily injury” means bodily injury, sickness or disease sustained by a person, including death resulting from any of these at any time. ...

13. “Occurrence” means an accident, including continuous or repeated exposure to substantially the same general harmful conditions. ...

14. “Personal and advertising injury” means injury, including consequential “bodily injury,” arising out of one or more of the following offenses: ...

- c. The wrongful eviction from, wrongful entry into, or invasion of the right of private occupancy of a room, dwelling or premises that a person occupies, committed by or on behalf of its owner, landlord or lessor. ...

17. “Property damage” means:

- a. Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or
- b. Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the “occurrence” that caused it.

(Id., Exs. 1-4) (emphasis added).

1 **B. THE UNDERLYING ACTION**

2 Defendants owned, leased, and managed a residential hotel called “Auburn Hotel” in
3 San Francisco, California. In August 2007, several tenants of the Auburn Hotel filed a class
4 action lawsuit against Defendants, entitled Wilson, et al. v. Nikita Holding, LLC, et al., San
5 Francisco Superior Court Case No. CGC-07-466543 (“Underlying Action”). (Pls.’ RJN, Ex.
6 13.)

7 In that case, the underlying plaintiffs (“Tenants”) alleged in their Amended Complaint
8 that Defendants failed to maintain the Auburn Hotel in a habitable manner, and brought the
9 following causes of action: (1) Breach of Implied Warranty of Habitability; (2) Habitability
10 Tort; (3) Nuisance; (4) Breach of Implied Covenant of Quiet Enjoyment; (5) Violation of Civil
11 Code § 1942.4; (6) Negligence; (7) Negligent Violation of Statutory Duty; (8) Injunctive
12 Relief, Civil Code §§ 333, 3422; California Code of Civil Procedure §§ 526, 527; and Civil
13 Code § 1942-4; (9) For Order Restraining Unlawful Business Practices; and (10) Unfair
14 Business Practices - Disgorgement. (Id., Ex. 14.) The Tenants did not specifically allege a
15 cause of action for wrongful eviction. (Id.)

16 **C. DEFENDANTS’ TENDER AND THE PARTIES’ EFFORTS TO SETTLE THE**
17 **UNDERLYING ACTION**

18 In February 2008, Defendants tendered the defense of the Underlying Action to TBIC,
19 FFIC, and their third liability carrier, United National Insurance Company (“United”). On June
20 25, 2008, the Area Claims Manager for both TBIC and FFIC wrote Defendants’ personal
21 coverage counsel, Michael Heath, accepting the tender and agreeing to provide a full defense.
22 (Creighan Decl., ¶ 5, Ex. 5.) In that letter, Plaintiffs advised Defendants of their position that
23 the Underlying Action included no allegations of “bodily injury” or “property damage,” or of
24 damages caused by an “occurrence,” as defined in the Policies. (Id., Ex. 5 at 7.) Plaintiffs also
25 reserved their rights to seek reimbursement from Defendants for some or all of the amount paid
26 by Plaintiffs as defense costs, and some or all of the amount paid by Plaintiffs as settlement of
27 the Underlying Action. (Id. at 13.) (“FFIC/TBIC reserves its right to seek recovery of the legal
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1 fees and expenses it paid in defense of this matter and to seek reimbursement of any payments
2 made in settlement or judgment related to non-covered claims.”).

3 Defendants accepted the defense provided by Plaintiffs, and permitted appointed panel
4 counsel, Randy Wertz, to represent them in the Underlying Action. (Creighan Decl., ¶¶ 6-7.)
5 FFIC, TBIC, and United shared equally in the payment of Defendants’ defense costs, with each
6 carrier paying one-third. (Id., ¶ 6.)

7 During the course of the Underlying Action, Plaintiffs and United engaged in settlement
8 discussions with the Tenants. (Id., ¶ 8; Demo Decl., ¶ 2, Exs. 6-8.) On November 25, 2008,
9 Plaintiffs’ coverage counsel, David B.A. Demo, wrote to Mr. Heath and to Defendants
10 concerning the Tenants’ expected settlement demand of \$800,000. (Demo Decl., ¶ 3, Exs. 6,
11 7.) Mr. Demo advised Defendants that Plaintiffs would agree to fund all but \$100,000 of that
12 amount, which would be paid by United. (Id.) Mr. Demo reiterated Plaintiffs’ reservation of
13 rights, stated Plaintiffs’ belief that the settlement demand was reasonable, and requested that
14 Defendants consent to the settlement. (Id.)

15 The Tenants ultimately submitted a demand of \$802,500 against Defendants.
16 Defendants liability insurers agreed to fund that sum as follows: TBIC would pay \$400,000,
17 FFIC would pay \$300,000, and United would pay \$102,500. (Creighan Decl., ¶ 9.) Mr. Demo
18 wrote Defendants and their personal coverage attorney, Mr. Heath, on December 10, 2008,
19 again setting forth Plaintiffs’ reimbursement rights and offering Defendants the choice of
20 taking over their own defense if they did not consent to the settlement. (Demo Decl., ¶ 4, Ex.
21 8.)

22 Mr. Wertz, appointed panel counsel, reported to Plaintiffs that he believed the
23 settlement was reasonable in light of Defendants’ potential exposure. (Creighan Decl., ¶ 10;
24 Demo Decl., ¶ 6.) Defendants disagreed with Mr. Wertz’ assessment of their potential liability.
25 (Demo Decl., ¶ 5, Ex. 9.) Plaintiffs allege that Defendants, through their counsel Mr. Heath,
26 did agree to follow Mr. Wertz’s recommendation as to whether it was reasonable to settle
27 Tenants’ claims for \$800,000. (Id., ¶ 7.) Defendants dispute this allegation.

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1 In December 2008 or January 2009, Plaintiffs learned that Defendants had replaced
2 their personal coverage counsel, Mr. Heath, with new coverage counsel - Alexander J. Berline.
3 (Id., ¶ 9.) In January 2009, Mr. Berline sent Mr. Demo an email objecting to the \$802,500
4 settlement as “unreasonable.” (Id.) Mr. Demo responded to Mr. Berline on January 16, 2009,
5 stating that Plaintiffs “hereby again offer your clients the option of promptly assuming their
6 own defense in this matter,” and “[s]hould your clients elect to assume their own defense, my
7 clients will not move forward with any further efforts to settle the case for \$802,500 as
8 proposed, my clients will withdraw from their participation in funding the continued defense of
9 your clients, and my clients will be relieved of any further obligations to either defend or
10 indemnify your clients in this matter.” (Id., Ex. 11.)

11 On January 21, 2009, Mr. Berline responded by stating that Mr. Wertz’s opinion
12 regarding the reasonableness of the settlement should be disregarded, as Defendants should
13 have been assigned independent Cumis counsel pursuant to California Civil Code § 2860. (Id.,
14 Ex. 12.) In addition, Mr. Berline objected to Plaintiffs’ assertion that, should Defendants reject
15 the settlement offer and assume their own defense, Plaintiffs would be relieved of any further
16 obligation to indemnify Defendants. (Id.) Lastly, Mr. Berline stated:

17 The insureds, having objected to the settlement as being
18 unreasonable and too high, stand ready to take over their own
19 defense - but only if (1) TBIC and FFIC expressly drop their
20 erroneous reservation that the insureds’ objection to the settlement
21 somehow “relieves” the insurers of their obligation to “indemnify”
(i.e. voids the policy), and (2) offer some reasonable compensation
to insureds who will now have to hire independent counsel to
review and/or re-do the work conflicted panel defense performed.

22 (Id.)

23 **D. SETTLEMENT OF THE UNDERLYING ACTION**

24 The Underlying Action was certified as a class and ultimately settled for over \$1
25 million, despite Defendants’ objections. On March 25, 2009, following a motion for
26 preliminary approval of the class action settlement, the court in the Underlying Action
27 approved the settlement. (Id., Ex. 15.) In June 2009, the Tenants filed a motion for final
28 approval of the class action settlement, which was granted on July 10, 2009 without objection

1 from any party. (Id., Ex. 17.) The underlying court “specifically [found] that the settlement is
2 fair, reasonable, and adequate.” (Id.)

3 Pursuant to the underlying court’s order, the settlement was divided as follows: (1)
4 \$470,599.26 to be paid to class members, with members receiving approximately \$5 per day of
5 residence at the Auburn Hotel during the class period; (2) \$135,000 to the nine class
6 representatives; (3) \$333,333.33 to Tenants’ counsel for attorney’s fees; (4) \$26,067.41 to
7 Tenants’ counsel for past costs; and (5) \$35,000 to Tenants’ counsel for the cost of
8 administering the settlement. (Id.) TBIC contributed \$400,000 and FFIC contributed \$300,000
9 to the total settlement fund. (Creighan Decl., ¶ 11.) The remainder was paid by the co-
10 defendant in the Underlying Action, Nikita Holdings, LLC. (Pls.’ RJN, Exs. 15-17.)

11 Of that total settlement amount, Plaintiffs allege in their motion – without reference to
12 any supporting evidence or declaration – that Plaintiffs’ combined share of the \$605,599.26
13 paid to the class members and representatives (i.e., \$470,599.26 plus \$135,000) was
14 “\$423,919.482.” (Pls.’ Motion at 14.) Plaintiffs further indicate that they collectively paid
15 \$79,655.16 in defense of the Underlying Action. (Creighan Decl., ¶ 12.)

16 **E. THE INSTANT ACTION**

17 Plaintiffs filed this action on January 29, 2009. In their First Amended Complaint, filed
18 on March 25, 2009, Plaintiffs bring claims for Equitable Indemnity (First Cause of Action),
19 Reimbursement of Defense Costs (Second Cause of Action), Reimbursement of
20 Indemnity/Settlement Costs (Third Cause of Action), and Declaratory Relief (Fourth Cause of
21 Action). In short, Plaintiffs seek reimbursement of defense costs and indemnity/settlement
22 payments incurred on Defendants’ behalf in the Underlying Action, as well as declaratory
23 relief regarding those issues. Plaintiffs now move for summary judgment or partial summary
24 judgment on their claims.¹

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26 _____
27 ¹ As indicated, Plaintiffs’ First Cause of Action is for Equitable Indemnity. By that
28 claim, Plaintiffs seek indemnification “for any and all amounts that have been ... paid by
[Plaintiffs] for the defense and/or settlement of the Underlying Action,” under the theory that
Plaintiffs were not “in any way primarily liable for [Defendants’] defense expenses.” (First
Am. Compl. at 5.)

1 **II. LEGAL STANDARDS**

2 **A. SUMMARY JUDGMENT STANDARD**

3 Rule 56(c) of the Federal Rules of Civil Procedure authorizes summary judgment if
4 there is no genuine issue as to any material fact and the moving party is entitled to judgment as
5 a matter of law. See Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 247-48 (1986). The
6 moving party bears the initial burden of demonstrating the basis for the motion and identifying
7 the portions of the pleadings, depositions, answers to interrogatories, affidavits, and admissions
8 on file that establish the absence of a triable issue of material fact. Celotex Corp. v. Catrett,
9 477 U.S. 317, 323 (1986). If the moving party meets this initial burden, the burden then shifts
10 to the non-moving party to present specific facts showing that there is a genuine issue for trial.
11 Fed.R.Civ.P. 56(e); Celotex, 477 U.S. at 324; Matsushita Elec. Indus. Co. v. Zenith Radio
12 Corp., 475 U.S. 574, 586-87 (1986).

13 “On a motion for summary judgment, ‘facts must be viewed in the light most favorable
14 to the nonmoving party only if there is a ‘genuine’ dispute as to those facts.’” Ricci v.
15 DeStefano, -- U.S. --, 129 S.Ct. 2658, 2677 (2009) (quoting Scott v. Harris, 550 U.S. 372, 380
16 (2007)). An issue of fact is “material” if, under the substantive law of the case, resolution of
17 the factual dispute might affect the outcome of the claim. See Anderson, 477 U.S. at 248.
18 Factual disputes are genuine if they “properly can be resolved in favor of either party.” Id. at
19 250. Accordingly, a genuine issue for trial exists if the non-movant presents evidence from
20 which a reasonable jury, viewing the evidence in the light most favorable to that party, could
21 resolve the material issue in his or her favor. Id. “If the evidence is merely colorable, or is not
22 significantly probative, summary judgment may be granted.” Id. at 249-50 (internal citations
23 omitted). Only admissible evidence may be considered in ruling on a motion for motion for
24 summary judgment. Fed.R.Civ.P. 56(e); Orr v. Bank of Am., 285 F.3d 764, 773 (9th Cir.
25 2002).

26 **B. AN INSURER’S DUTY TO DEFEND**

27 An insurer must defend its insured against claims that create a potential for indemnity
28 under the policy. Scottsdale Ins. Co. v. MV Transp., 36 Cal.4th 643, 654 (2005) (citing

1 Montrose Chemical Corp. v. Superior Court, 6 Cal.4th 287 (1993)). The duty to defend is
2 broader than the duty to indemnify. Id. Determination of the duty to defend depends, first, on
3 a comparison between the allegations of the complaint and the terms of the policy. Id. But the
4 duty also exists where extrinsic facts known to the insurer suggest that the claim may be
5 covered. Id. “Moreover, that the precise causes of action pled by the third-party complaint
6 may fall outside policy coverage does not excuse the duty to defend where, under the facts
7 alleged reasonably inferable, or otherwise known, the complaint could fairly be amended to
8 state a covered liability.” Id. (citing Gray v. Zurich Ins. Co., 65 Cal.2d 263, 275-276 (1966)).

9 The duty to defend arises upon tender of a potentially covered claim and lasts until the
10 underlying lawsuit is concluded, or until it has been shown that there is no potential for
11 coverage. Id. at 655. “When the duty, having arisen, is extinguished by a showing that no
12 claim can in fact be covered, ‘it is extinguished only prospectively and not retroactively.’” Id.
13 (quoting Buss v. Superior Court, 16 Cal.4th 35, 46 (1997)). By contrast, “in an action wherein
14 none of the claims is even potentially covered because it does not even possibly embrace any
15 triggering harm of the specified sort within the policy period caused by an included occurrence,
16 the insurer does not have a duty to defend.” Id.

17 **C. AN INSURER’S RIGHT TO REIMBURSEMENT FOR DEFENSE COSTS INCURRED IN**
18 **DEFENDING CLAIMS WITH NO POTENTIAL FOR COVERAGE**

19 In a “mixed” action against an insured, in which some of the claims are at least
20 potentially covered under the policy and the others are not, the insurer has a duty to defend the
21 action in its entirety. Buss, 16 Cal.4th at 47-48. However, an insurer has an implied-in-law
22 right to seek reimbursement from the insured for defense costs incurred solely in defense of
23 claims for which there was no potential for coverage under the policy, if the insurer defends
24 under a “reservation of rights.” Id. at 52.

25 “Through reservation, the insurer gives the insured notice of how it will, or at least may,
26 proceed and thereby provides it an opportunity to take any steps that it may deem reasonable or
27 necessary in response – including whether to accept defense at the insurer’s hands and under
28 the insurer’s control ... or, instead, to defend itself as it chooses.” Id. at 61, n. 27. A

1 reservation of rights to recover defense costs is effective even when an insured objects to the
2 reservation but accepts the defense. Blue Ridge Ins. Co. v. Jacobsen, 25 Cal.4th 489, 498
3 (2001). The insurer carries the burden of proof to show, by a preponderance of the evidence,
4 that it is entitled to reimbursement of defense costs. Buss, 16 Cal.4th at 53.

5 **D. AN INSURER’S RIGHT TO REIMBURSEMENT OF SETTLEMENT PAYMENTS**
6 **MADE FOR NON-COVERED CLAIMS**

7 Insurers have a quasi-contractual right to seek reimbursement for settlement payments
8 made for claims not covered by the policy. Blue Ridge, 25 Cal.4th at 503. Specifically, an
9 insurer may settle a third party action within policy limits, even over the insured’s objection,
10 and then obtain reimbursement of its reasonable settlement payments from the insured upon a
11 later determination that the underlying claims were not covered. Scottsdale Ins. Co. v. MV
12 Transp., 36 Cal.4th 643, 660 n.5 (2005).²

13 In order to perfect its right to reimbursement, an insurer must provide the insured with:
14 (1) a timely and express reservation of rights; (2) an express notification of the insurer’s intent
15 to accept a proposed settlement offer; and (3) an express offer that the insured may assume its
16 own defense when the insurer and insured disagree whether to accept the proposed settlement.
17 Blue Ridge, 25 Cal.4th at 502. If these requirements are met, the insurer has an implied-in-law
18 right to reimbursement for reasonable settlement payments on non-covered claims, even over
19 the insured’s objection. Id. at 503.

20 **III. DISCUSSION**

21 **A. PLAINTIFFS’ CLAIM FOR REIMBURSEMENT OF ALL DEFENSE COSTS**

22 By their motion, Plaintiffs seek an order that they are entitled to reimbursement of all
23 defense costs incurred on Defendants’ behalf because, accordingly to Plaintiffs, none of the
24 Tenants’ claims was potentially covered under the Policies.

25 _____
26 ² The Scottsdale court provided the following rationale for allowing reimbursement of
27 settlement payments for non-covered claims: “because an insurer risks unlimited exposure to
28 bad faith liability if it declines a reasonable offer within policy limits on grounds that there is
no coverage ... an insured’s refusal to authorize the settlement unless the insurer agreed to
forgo reimbursement would place the insurer in a Catch-22 and force it to indemnify uncovered
claims, contrary to its contractual obligations.” Id.

1 The evidence confirms that Plaintiffs properly reserved their rights to seek
2 reimbursement of defense costs under Buss. Specifically, Plaintiffs conditioned their proffer of
3 defense on the reservation of their rights to seek reimbursement of costs advanced to defend
4 claims that were not potentially covered. (See Creighan Decl., ¶ 5, Ex. 5 at 13.) However, as
5 to Plaintiffs’ claim for recovery of all defense costs, under Buss, Plaintiffs are only allowed to
6 reimbursement for defense costs incurred solely in defense of claims for which there was no
7 potential for coverage.

8 Here, Plaintiffs have failed to show the lack of potential coverage for the “Habitability
9 Tort” claim (Second Cause of Action) in the Underlying Action.³ In fact, Plaintiffs conceded
10 in their June 25, 2008 reservation of rights letter that there was a potential for coverage under
11 the Tenant’s Habitability Tort claim: “the only potential indemnity that might be owed to you
12 under the policies in this litigation is in connection with the damages claimed for ‘Habitability’
13 (i.e., Plaintiffs (sic) inability to have full access to those rented premises).” (Creighan Decl.,
14 Ex. 5 at 11.) Plaintiffs admit in their motion that they provided a defense because there was a
15 possibility that the Tenants could amend their complaint to allege a cause of action for
16 wrongful eviction. (Pls.’ Mtn. at 10.) (As discussed below, the Tenants’ “Habitability Tort”
17 claim, as plead, did not state a claim for wrongful eviction. In addition, the Tenants never
18 amended their complaint to include such a claim.) Plaintiffs’ understanding of their duty to
19 defend was consistent with Scottsdale, which holds “that the precise causes of action pled by
20 the third-party complaint may fall outside policy coverage does not excuse the duty to defend
21 where, under the facts alleged, reasonably inferable, or otherwise known, the complaint could
22 fairly be amended to state a covered liability.” Scottsdale, 36 Cal.4th at 654.

23 Accordingly, the Court finds that Plaintiffs are entitled to recover defense costs paid in
24 defense of all claims except for the Habitability Tort claim, to the extent that such costs can be
25 allocated. However, Plaintiffs have failed to offer any proof as to what portion of defense costs
26 were spent on the remaining claims, which precludes summary judgment on allocation issues.

28 ³Other than the Habitability Tort claim, Defendants do not assert that any of the
Tenants’ other causes of action was potentially covered.

1 Therefore, as indicated below, this matter is referred to the Chief Magistrate Judge for a
2 determination of the amount of defense costs, if any, that can be allocated to the defense of all
3 claims other than the Habitability Tort claim.

4 **B. PLAINTIFFS' CLAIM FOR REIMBURSEMENT OF ALL ATTORNEY'S FEES AND**
5 **COSTS PAID TO THE TENANTS AS PART OF THE SETTLEMENT**

6 Apart from the defense costs Plaintiffs incurred on behalf of Defendants, Plaintiffs have
7 also moved for recovery of all attorneys' fees and costs Plaintiffs paid to the Tenants as part of
8 the settlement in the Underlying Action.

9 The Tenants in the Underlying Action sought attorney's fees and costs under California
10 Civil Code Section 1942.4 (collection of rent where defective conditions exist) (Fifth Cause of
11 Action) and pursuant to the private attorney general provision of California Code of Civil
12 Procedure Section 1021.5. (Pls.' RJN, Ex. 14 at 15.) Section 1942.4(b)(2) provides that a
13 "prevailing party shall be entitled to recovery of reasonable attorney's fees and costs of the suit
14 in an amount fixed by the court." Cal. Civ. Code § 1942.4(b)(2). Likewise, Section 1021.5
15 allows a court to "award attorneys' fees to a successful party against one or more opposing
16 parties in any action which has resulted in the enforcement of an important right affecting the
17 public interest" Cal. Code Civ. P. § 1021.5.

18 In the Underlying Action, the court's order finally approving the settlement awarded the
19 Tenants a total of \$394,400.74 in attorney's fees and costs. The court specifically found the
20 attorney's fees award (\$333,333.33), which constituted one-third of the total settlement, to be
21 "reasonable." (Pls.' RJN, Ex. 17 at 4.) However, the court did not indicate the statutory
22 authority or cause of action under which fees and costs were being awarded. Plaintiffs
23 represent that they paid \$276,080.52 of the attorney's fees and costs award, for which they now
24 seek complete reimbursement.

25 Plaintiffs argue that complete reimbursement is appropriate because, pursuant to the
26 Policies, the attorney's fees and costs awarded to the Tenants are only covered by the policy if
27 those fees and costs stem from potentially covered causes of action. See also State Farm
28 General Ins. Co. v. Mintarsih, 175 Cal.App.4th 274, 284-285 (2009) (insurer had no obligation

1 to pay attorney's fees and costs awarded against the insured arising solely from claims that
2 were not potentially covered). Again, Plaintiffs argue that no claims were potentially covered,
3 which, as indicated above, is incorrect as to the Habitability Tort claim. Moreover, as with
4 their claim for reimbursement of defense costs, Plaintiffs have failed to show what portion of
5 the attorney's fees and costs, if any, stem from claims that had no potential for coverage (i.e.,
6 all claims except for the Habitability Tort claim).

7 Accordingly, the Court finds that Plaintiffs are entitled to recover attorney's fees and
8 costs, if any, that stem from claims other than the Habitability Tort claim, to the extent such
9 attorney's fees and costs can be allocated.

10 **C. PLAINTIFFS' CLAIM FOR REIMBURSEMENT OF THE REMAINDER OF THE**
11 **SETTLEMENT AMOUNT (I.E., THE AMOUNT EXCLUDING THE TENANTS'**
12 **ATTORNEY'S FEES AND COSTS)**

13 As to the remainder of the settlement amount, Plaintiffs seek an order that they are
14 entitled, under Blue Ridge, to reimbursement of the entirety of that amount because none of the
15 Tenants' claims was actually covered under the Policies. Furthermore, Plaintiffs contend that
16 they satisfied the notification requirements set forth in Blue Ridge by: providing Defendants
17 with timely notice that they were providing a defense under a reservation of rights; by notifying
18 Defendants, in writing, that they intended to accept the Tenants' settlement offer; and by
19 offering Defendants the option of rejecting the settlement offer and assuming their own
20 defense. (Demo Decl., ¶ 3, Exs. 6-8, 11.)

21 In their opposition, Defendants argue that Plaintiffs are not entitled to reimbursement
22 for any settlement amounts because: (1) Plaintiffs did not make a valid offer to Defendants to
23 assume their own defense because Plaintiffs stated that, should Defendants assume their own
24 defense, Plaintiffs would be relieved of any further obligations to either defend or indemnify
25 Defendants; (2) Defendants accepted the offer to assume their own defense; and (3) the
26 settlement amount was unreasonable.

27 The parties' respective arguments are addressed in turn below.
28

1 **1. None of the Tenants’ Claims Was Actually Covered by the Policies**

2 The interpretation of the meaning of an insurance policy and the scope of coverage are
3 questions of law. Barnett v. Fireman’s Fund Ins. Co., 90 Cal.App.4th 500, 508 (2001).

4 Whether a third party action asserts a potentially covered claim under the policy requires a
5 court to interpret the language of the insuring agreement and is a question of law. Id. Where
6 the provisions of the policy are clear, the language must be read accordingly. Buss, 16 Cal.4th
7 at 45.

8 Here, the parties do not assert that the policy language is ambiguous. The Policies
9 plainly provide liability coverage under: Coverage A, for those sums that Defendants become
10 legally obligated to pay as damages because of “bodily injury” or “property damage” caused by
11 an “occurrence,” which is defined as an “accident”; and Coverage B, for those sums that
12 Defendants become legally obligated to pay as damages because of “personal and advertising
13 injury” arising out of a list of offenses that includes “wrongful eviction.” When comparing the
14 allegations of the underlying complaint with the terms of the Policies, it becomes clear that
15 none of the Tenant’s claims was actually covered under the Policies.

16 **a) The Tenants’ First Through Fifth Causes of Action**

17 By their First through Fifth causes of action, the Tenants allege that Defendants
18 willfully failed and/or refused to correct various defective conditions at the Auburn Hotel,
19 thereby causing the Tenants to suffer damages in overpaid rent, to lose full use of the premises,
20 and to suffer annoyance and discomfort.⁴ (Pls.’ RJN, Ex. 14 at 5-11.)

21 These claims do not fall under Coverage A because they do not allege either “bodily
22 injury” or “property damage,” as those terms are defined in the Policies. Moreover, those
23 claims do not arise from an “occurrence,” which is defined as an “accident.” An “accident” is
24 an unintentional, unexpected, chance occurrence. Modern Devel. Co. v. Navigators Ins. Co.,
25 111 Cal.App.4th 932, 940, n. 4 (2003). The Tenants alleged that Defendants purposefully

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27 4 These claims are: (1) Breach of Implied Warranty of Habitability; (2) Habitability
28 Tort; (3) Nuisance; (4) Breach of Implied Covenant of Quiet Enjoyment; and (5) Violation of
Civil Code § 1942.4.

1 failed to repair and maintain the Auburn Hotel in a habitable condition, and knowingly
2 continued to collect rent. Those actions are not “accidents” covered by the Policies.

3 With respect to Coverage B (personal and advertising injury liability), Defendants argue
4 that the Tenants’ Habitability Tort claim is one for “constructive eviction.”⁵ According to
5 Defendants, a claim for constructive eviction falls under the Policies’ definitions of “personal
6 and advertising injury,” which include “[t]he wrongful eviction from, wrongful entry into, or
7 invasion of the right of private occupancy of a room, dwelling or premises that a person
8 occupies, committed by or on behalf of its owner, landlord or lessor.”

9 By their Habitability Tort claim, the Tenants allege that due to Defendants’ failure to
10 repair and maintain the property, the Tenants “lost and continue to lose full use of the
11 premises.” (Pls.’ RJN, Ex. 14 at 7-8.) However, other than alleging that some, but not all, of
12 the named plaintiff Tenants no longer reside at the Auburn Hotel, the Tenants did not allege
13 that any named plaintiff was dispossessed of or vacated the property due to Defendants’
14 actions. “In order that there be a constructive eviction it is essential that the tenant should
15 vacate the property. There is no constructive eviction if the tenant continues in possession of
16 the premises however much he may be disturbed in the beneficial enjoyment.” Cunningham,
17 98 Cal.App.4th at 1152. Therefore, Defendants’ characterization of this claim as one for
18 constructive eviction fails.

19 Accordingly, the Tenants’ First through Fifth causes of action are not covered by the
20 Policies.

21 ***b) The Tenants’ Sixth and Seventh Causes of Action***

22 The Tenants’ Sixth and Seventh Causes of Action for Negligence and Negligent
23 Violation of Statutory Duty, which are also not covered, rely almost entirely on the previously
24 stated allegations in the complaint. As to Coverage A, no “bodily injury,” “property damage,”
25 or covered “occurrence” was alleged by the Tenants by these claims. As to Coverage B,
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27
28 ⁵ A wrongful eviction claim can encompass a wrongful “constructive eviction.”
Cunningham v. Universal Underwriters, 98 Cal.App.4th 1141, 1152 (2002).

1 “negligence” is not an offense listed in the definition of “personal and advertising injury.” Of
2 note, Defendants have not argued that these causes of action are covered under the Policies.

3 *c) The Tenants’ Eighth Through Tenth Causes of Action*

4 The Tenants’ Eighth, Ninth, and Tenth Causes of Action seek only equitable relief, i.e.,
5 a temporary restraining order, preliminary injunction, and permanent injunction (Eight and
6 Ninth Causes of Action), and disgorgement of unlawfully collected rent (Tenth Cause of
7 Action).

8 A cause of action that seeks these types of equitable relief does not seek “damages” that
9 can be covered by a liability policy. See e.g., Nationwide Ins. Co. v. King, 673 F.Supp. 384,
10 387 (S.D. Cal. 1987) (summary judgment granted in favor of insurer because underlying action
11 sought only equitable relief and the policy limited coverage to damages); Bank of the West v.
12 Superior Court, 2 Cal.4th 1254, 1266 (1992) (provisions of a comprehensive liability policy
13 that covered “damages” did not extend to claims for disgorgement or restitution). In this case,
14 because the Policies only provide coverage for suits seeking “damages,” the Eighth through
15 Tenth Causes of Action cannot give rise to coverage. Again, Defendants have offered no
16 argument to the contrary.

17 In sum, the undisputed facts show that none of the Tenant’s claims in the Underlying
18 Action was covered under the Policies.

19 **2. Plaintiffs Provided a Valid Blue Ridge Offer to Defendants to**
20 **Assume Their Own Defense**

21 Defendants assert that Plaintiffs’ offer to Defendants to assume their own defense was
22 invalid because it added an “unreasonable additional penalty” that Plaintiffs “will be relieved
23 of any further obligations to ... indemnify [Defendants] in this matter.” (See Demo Decl., Ex.
24 11 at 3.) This offer was invalid under Blue Ridge, Defendant argue, because if an insured
25 accepts the offer to take over its own defense, then the insurer is only relieved from any further
26 obligation to defend, and indemnity coverage remains unaffected.

27 It should be noted that Blue Ridge is silent as to any impact that an insured’s
28 assumption of its own defense may have on indemnity coverage. Moreover, neither party has

1 cited any authority that expressly states that, by assuming its own defense costs, an insured
2 waives (or does not waive) all indemnity coverage. Both parties only cite allegedly
3 “analogous” case law and certain policy considerations in support of their respective positions.

4 Specifically, Defendants rely exclusively on Valentino v. Elliott Sav-On Gas, Inc., 201
5 Cal.App.3d 692 (1988). However, Valentino is inapposite. There, the defendant in a personal
6 injury action had made a settlement offer pursuant to California Code of Civil Procedure § 998,
7 which the plaintiff rejected. Id. at 698. The plaintiff subsequently received a jury award of
8 less than the amount of the defendant’s offer. Id. The appellate court found that the trial court
9 had erred in awarding defendant its costs pursuant to Section 998 because the settlement offer
10 also would have required the plaintiff to release the defendant, its attorneys, and its insurance
11 carrier from all other claims, including insurance bad faith. Id. at 698-699.⁶ Even though the
12 facts of that case are distinguishable, Defendants argue that this situation is “analogous”
13 because it is unreasonable to expect Defendants to give up all indemnity benefits. However,
14 Valentino fails to inform the instant analysis because that case did not involve any contractual
15 obligations of the parties.

16 In response, Plaintiffs assert that they were not threatening to “void” the indemnity
17 provisions, but rather were acting consistent with the principle that, when an insured tenders
18 and accepts a defense under a liability insurance contract, it does so pursuant to the terms and
19 conditions of that contract. Should the insured later assume its own defense, that would
20 constitute a withdrawal of tender and cause the insured to withdraw from benefits under both
21 the defense and indemnity provisions of the policy. Plaintiffs also discuss case law and certain
22 policy provisions that promote an insurer’s right to manage the defense. See e.g., Safeco Ins.
23 Co. v. Superior Court (McKinney), 71 Cal. App.4th 782, 787 (1999) (“When the insurer
24 provides a defense to its insured, the insured has no right to interfere with the insurer’s control
25 of the defense.”). However, like Defendants, Plaintiffs have failed to cite any authority directly

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27 ⁶ Under Section 998(c)(1), “if an offer made by a defendant is not accepted and the
28 plaintiff fails to obtain a more favorable judgment or award, the plaintiff shall not recover his
or her postoffer costs and shall pay the defendant’s costs from the time of the offer.” Cal. Code
Civ. P. § 998.

1 supporting their position that an insured's assumption of its own defense results in a waiver of
2 indemnity coverage.

3 Given the parties' failure to provide meaningful authority to support their respective
4 positions, the Court turns to the policy considerations underlying the Blue Ridge decision for
5 guidance. In Blue Ridge, the court held that an insurer has an implied-in-law right of
6 reimbursement for settlement costs paid for non-covered claims in order "to avoid the insureds'
7 unjust enrichment." Blue Ridge, 25 Cal.4th at 503. As noted by the Blue Ridge court, "[e]ven
8 if the policy's language were unclear, the hypothetical insured could not have an objectively
9 reasonable expectation that it was entitled to what would in fact be a windfall." Id. In other
10 words, the court found that an insurer should be allowed to recoup payments it was not
11 contractually obligated to pay. Id. Furthermore, the court held that an insurer can unilaterally
12 reserve its right to later assert non-coverage of any settled claim, even over the insured's
13 objection: "[a]n insured's mere objection to a reservation of rights would create coverage
14 contrary to the parties' agreement in the insurance policy and violate basic notions of fairness."
15 Id. at 502. In allowing for an insurer to proceed under a unilateral reservation of rights, the
16 Blue Ridge court noted that an insurer is "obligated to accept a reasonable settlement offer as
17 part of its duty of good faith and fair dealing or risk excess exposure." Id. at 504.

18 However, an insurer's right to seek reimbursement for settlement costs for non-covered
19 claims is not unbounded. Blue Ridge requires, inter alia, that the insurer make an "an express
20 offer to the insureds that they may assume their own defense when the insurer and the insured
21 disagree whether to accept the proposed settlement." Id. at 502. Here, in Plaintiffs' first letter
22 to Defendants explaining the settlement offer (dated December 10, 2008), Plaintiffs stated that
23 should Defendants "ultimately disagree over the terms and conditions under which the case
24 against them should be settled, they are expressly offered the option of assuming their own
25 continued defense in this matter, with FFIC not paying any further costs of that defense."
26 (Demo Decl., Ex. 8.) Notably, in that letter, Plaintiffs did not assert that Defendants would
27 waive indemnification coverage if they assumed their own defense. Therefore, by virtue of the
28 December 10, 2008 letter, Defendants were placed on notice, in accordance with Blue Ridge,

1 that Plaintiffs planned to settle the Underlying Action. Defendants were also informed of their
2 right to assume their own defense if they disagreed with the terms of the settlement. As such,
3 Plaintiffs satisfied the Blue Ridge prerequisites for seeking reimbursement of settlement
4 payments made for non-covered claims.

5 It was only in a subsequent January 16, 2009 letter, sent after Defendants' newly-
6 retained coverage counsel objected to the settlement as unreasonable, that Plaintiffs stated that
7 they would be "relieved of any further obligations to either defend or indemnify your clients in
8 this matter" should Defendants assume their own defense. (Id., Ex. 11.) However, at that
9 point, Plaintiffs had already discharged their obligations under Blue Ridge. In addition, if this
10 Court were to find that the January 16, 2009 letter effectively "negated" Plaintiffs' prior Blue
11 Ridge notice, such a finding would lead to the unjust enrichment of Defendants, by allowing
12 them to benefit from a level of coverage for which they did not pay premiums.

13 Accordingly, the submitted evidence shows that Plaintiffs sufficiently reserved their
14 rights for reimbursement of settlement payments made for non-covered claims.

15 3. The Evidence Shows that Defendants Did Not Assume Their Own 16 Defense

17 Defendants further argue that the settlement was improper because they did, in fact,
18 assume their own defense. This argument is unsupported by the submitted evidence. In their
19 correspondence, Defendants informed Plaintiffs that they "stand ready to take over their own
20 defense - but only if : (1) TBIC and FFIC expressly drop their erroneous reservation that the
21 insureds' objection to the settlement somehow 'relieves' the insurers of their obligation to
22 'indemnify' (i.e. voids the policy), and (2) offer some reasonable compensation to insureds
23 who will now have to hire independent counsel to review and/or re-do the work conflicted
24 panel defense performed." (Demo Decl., Ex. 12) (emphasis added). Because Defendants
25 imposed conditions that had to be met (and were, in fact, not met) before they would take over
26 their defense, Defendants never did agree to "assume their own defense" within the meaning of
27 Blue Ridge. Moreover, Defendants have not produced any evidence showing that they
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1 attempted to substitute Mr. Berline or some other counsel in Mr. Wertz' stead, to cause Mr.
2 Wertz' withdrawal, or to take some other affirmative action in their own defense.

3 In support of their position, Defendants argue simply that these provisos are not actually
4 "conditions" because they were legally entitled to receive indemnity payments and the
5 appointment of independent Cumis counsel. However, the fact remains that Defendants did not
6 actually assume their own defense so as to preclude Plaintiffs' recovery of settlement
7 amounts.⁷

8 **4. Defendants Have Failed To Show that the Settlement Amount Was**
9 **Unreasonable**

10 Lastly, Defendants attempt to create a factual issue regarding the reasonableness of the
11 settlement amount paid by Plaintiffs in the Underlying Action. In doing so, Defendants submit
12 a declaration from their former lawyer, Mr. Heath, disputing Plaintiffs' assertion that he agreed
13 to the reasonableness of the settlement amount. (Heath Decl., ¶¶ 5-7, Ex. 9.) This only
14 reiterates Defendants already-stated position, expressed to Plaintiffs by Mr. Berline, that the
15 settlement was unreasonable. (See Demo Decl., ¶ 9.) Defendants' position does not
16 demonstrate that the settlement was objectively unreasonable. Indeed, in the Underlying
17 Action, the state court found that the settlement was reasonable, fair, and accurate. As such,
18 Defendants have failed to show that there is a genuine issue of material fact as to the
19 reasonableness of the settlement amount.

20 In view of the above, this Court finds that Plaintiffs are entitled to reimbursement of all
21 settlement payments (other than those paid as attorney's fees and costs, which are subject to the
22 analysis in Section III.B above) made in the Underlying Action. But again, Plaintiffs have not
23 provided an allocation of such settlement payments.

24 **D. PLAINTIFFS' CLAIM FOR PREJUDGMENT INTEREST**

25 Plaintiffs argue that they are entitled to an award of prejudgment interest against
26 Defendants. However, prejudgment interest is only appropriate where damages are certain or

27 ⁷ Other than Mr. Berline's assertion to Plaintiffs that Defendants should have been
28 assigned independent Cumis counsel, Defendants have failed to submit any evidence showing
that they actually requested Cumis counsel under California Civil Code § 2860.

1 capable of calculation on a particular day. Cal. Civ. Code § 3287(a). Here, the amount of
2 damages is not certain because Plaintiffs have yet to prove the amount of defense costs and
3 settlement payments that they are entitled to recover. Accordingly, this request is denied,
4 without prejudice.

5 **IV. CONCLUSION**

6 For the foregoing reasons,

7 IT IS HEREBY ORDERED THAT:

8 1. Plaintiffs' Motion for Summary Judgment on their claim for Reimbursement of
9 Defense Costs is GRANTED IN PART. To the extent they can be allocated, Plaintiffs are
10 entitled to recover defense costs, if any, incurred in the Underlying Action in defense of all
11 claims other than the Habitability Tort claim.

12 2. Plaintiffs' Motion for Summary Judgment for Reimbursement of
13 Indemnity/Settlement Costs paid as attorney's fees and costs to the Tenants in the Underlying
14 Action is GRANTED IN PART. To the extent they can be allocated, Plaintiffs are entitled to
15 recover attorney's fees and costs, if any, that stem from all claims other than the Habitability
16 Tort claim.

17 3. Plaintiffs' Motion for Summary Judgment on their claim for Reimbursement of
18 Indemnity/Settlement Costs – other than those paid as attorney's fees and costs – is
19 GRANTED. Plaintiffs are entitled to recover all indemnity/settlement costs (other than those
20 paid as attorney's fees and costs) incurred in the Underlying Action.

21 4. This matter is REFERRED to the Chief Magistrate Judge or her designee for
22 further proceedings regarding the allocation of the above-indicated amounts, and a report and
23 recommendation regarding the same.

24 5. Before appearing before the Magistrate Judge, the parties are directed to meet
25 and confer in an effort to reach a stipulation as to the above-indicated amounts.


26 6. Plaintiffs' request for prejudgment interest is DENIED without prejudice.
27 Plaintiffs may reassert this request before the Magistrate Judge, at which point the Magistrate
28 Judge shall provide a report and recommendation on the issue of prejudgment interest.

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7. This Order terminates Docket No. 49.

IT IS SO ORDERED.

Dated: September 23, 2010


SAUNDRA BROWN ARMSTRONG
United States District Judge