S161008

IN THE

Supreme Court

OF THE STATE OF CALIFORNIA

VILLAGE NORTHRIDGE HOMEOWNERS ASSOCIATION,

Plaintiff and Appellant,

vs.

STATE FARM FIRE & CASUALTY COMPANY,

Defendant and Respondent.

ANSWER TO AMICUS CURIAE BRIEF OF PERSONAL INSURANCE FEDERATION OF CALIFORNIA AND NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

REVIEW AFTER A DECISION BY THE COURT OF APPEAL
SECOND APPELLATE DISTRICT, DIVISION EIGHT
[2d Civil No. B188718] [L.A.S.C. No. BC265328]

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The Personal Insurance Federation of California ("PIFC") and National Association of Mutual Insurance Companies ("NAMIC") (collectively "Amici") have filed an amici brief which, upon cursory review, is alluring. Upon a more thoughtful examination, one can see that this brief fails to take into account the complexity of the situation presented by this case. Stated differently, it ignores the facts. This is reminiscent of Justice Boland's holding in the first appeal wherein he noted that State Farm ignores "the elephant in the room". *[APP0549 at n. 8]*

Amici oversimplify the situation at hand, painting Village Northridge as a plaintiff attempting to play the lottery by electing an "unfair" remedy with nothing but benefits for Village Northridge and nothing but burdens for State Farm. As far as Amici are concerned, if Village Northridge felt it had been defrauded and wanted to pursue this matter in a court of law, it had the option of rescinding the settlement agreement and refunding the consideration previously paid. Though it would undoubtedly be ideal from State Farm's perspective to be refunded this money, this is simply not an option for Village Northridge. As Village Northridge stated in its Answer Brief on the Merits, this remedy is simply not practicable and leaves Village Northridge with no viable remedy. As the provider of earthquake insurance, State Farm's payments to Village Northridge were intended for one thing and one thing only

– to cover the cost of earthquake repairs. As should be expected, all of the money State Farm paid Village Northridge was allocated to just that. This money was not a windfall and Village Northridge was in no position to hold onto the money in cash in the event it ever needed to be paid back. This money was spent exactly as it should have been – on much needed earthquake repairs. To expect a nonprofit homeowners association to reimburse insurance proceeds spent on repairs after discovering that they were defrauded re: policy limits is absurd. Not being able to spend this money on earthquake repairs defeats the purpose of it having been paid in the first place. Furthermore, it is not as though Building and Safety would have permitted people to continue living in such structurally compromised buildings. These were exigent circumstances in which Village Northridge had no choice but to use all the resources at its disposal to repair earthquake damage. Even State Farm's own policy requires that the property be repaired and maintained.

Amici frame Village Northridge's position as "a settlement is not a settlement if it is between an insurer and an insured". This misconstrues Village Northridge's position and illustrates just how Amici fail to appreciate the facts of this case which render the result reached in the Court of Appeal's decision just. Village Northridge and State Farm entered into an agreement wherein State Farm agreed to pay Village Northridge $1.5 million in exchange

for Village Northridge foregoing (a) the right to pursue policy benefits owed and (b) the right to sue State Farm relative to the claim at issue. Village Northridge, a State Farm insured, sustained significant damage as a result of the Northridge Earthquake in January 1994. Village Northridge's claim for policy benefits, initiated promptly after the earthquake which caused the damage, was reopened several years later when additional damage was noted. At this time, State Farm inspected the property and indicated it would pay $1.5 million if Village Northridge would forego seeking any further policy benefits. Little did Village Northridge know that the amount of available policy benefits was much higher than State Farm had represented them to be – $11.9 million instead of $4.9 million. At the time, desperate to fix the significant earthquake damage it had sustained, Village Northridge thought it was getting the best deal available, accepted State Farm's proposal and used the money it received from State Farm to fund much needed earthquake repairs. It was not until well after this fact that Village Northridge discovered it had been lied to regarding the amount of its policy limits. The amount of potential benefits available was clearly *material*. $4.9 million and $11.9 million present different stratospheres and materially altered what Village Northridge was walking away from.

Amici argue that *Garcia v. California Truck Company,* (1920) 183 Cal. 767, and *Taylor v. Hopper*, (1929) 207 Cal.102, both of which held that the

plaintiff could not affirm a settlement agreement and sue for damages, should control in this case and, leaving Village Northridge with no practicable remedy. They claim that if Village Northridge prevails in this case that it would open a Pandora's Box which would forever disturb the finality of settlements. Village Northridge agrees that settlements are important and suggests that a rule permitting fraudulent inducement of settlements, particularly in a first party insurance case, would defeat the very object that Amici purport to protect. Misrepresenting policy limits does nothing to further the public policy of encouraging settlements.

Amici's assessment of this case is based on this Court's holding in *Garcia v. California Truck Company* (1920) 183 Cal. 767. In *Garcia*, this Court held that a party seeking to avoid a settlement agreement on grounds of fraud must rescind the agreement and return the consideration paid "where the claim is for unliquidated damages or when the settlement is made to adjust a matter in dispute, or where there is a controversy as to the amount owing." *Id.* at 772. This Court further held in *Garcia* that there is a well-recognized exception to this rule – not applicable to the facts of the *Garcia* case – which 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 to be set aside, or of the original liability". *Id.*

at 771; quoting *Kley v. Healy* (1891) 127 N.Y. 555, 561, italics omitted. This latter rule is applied to situations where there is no dispute over the settling party's entitlement to the consideration. *See, e.g., Persson v. Smart Inventions* (2005) 125 Cal.App.4th 1141, 1154-1156.

According to Amici, this case is exactly like *Garcia* in that there was a "controversy as to the amount owing". Village Northridge maintains its position that this case is more like *Persson* in that Village Northridge gave up more than just the right to sue when it signed the Release. Upon a closer look, as recognized by the Court of Appeal, one can see that the instant case does not squarely fit *either* principle. The Court of Appeal addressed this "incongruity":

> "Because of the underlying insurance obligation, the circumstance 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 sue for fraud despite the release (*Persson* 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* at 771). While neither principle fits perfectly, either is more appropriately applied to a

> case in which an insurer has misrepresented policy limits to obtain a settlement than is a principle that requires the return of the insurance settlement monies as the price of a challenge to the insurer's fraud." [Typed Opn. at p. 7]

When Village Northridge signed the Release, the consideration it received from State Farm was not only in exchange for an agreement not to sue but also in exchange for the agreement not to pursue very certain and available policy benefits. Although the "amount owing is in dispute" (as was the case in *Garcia*), Village Northridge gave up much more than the right to sue in exchange for the consideration paid by State Farm (as was the case in *Persson*). The unique facts of this case coupled with the statutory duty to disclose policy benefits at the outset of the claim [Cal. *Code of Regs* §2695.4(a)] and the quasi-fiduciary relationship between the parties [*Love v. Fire Ins. Exchange* (1990) Cal.App.3d 1136, 1147] are the reasons why the *Garcia/Taylor* rule of mandatory restoration of consideration should not have been automatically applied in this case.

Amici claim that it would be "unfair" to permit Village Northridge to prevail in this case because such a result provides no risk to Village Northridge. With all due respect to this assessment, it is hardly without risk to spend the significant amount of time, energy and money required to litigate

a case – this case is in its sixth year of existence and the Village Northridge property remains in a state of significant disrepair. And remember, it was *State Farm* who made the material misrepresentation. Amici and State Farm ignore this fact in assigning "no risk" status to the tremendously burdensome claim Village Northridge is presenting here. State Farm is the proximate cause of this scenario, not Village Northridge.

Village Northridge respectfully submits that it would be "unfair" to allow State Farm to prevail in this case given the blatant fraud being perpetrated against not only Village Northridge but now this very Court. If this Court finds that upholding Court of Appeal's opinion would create dangerous precedent, Village Northridge submits that depublication would be the most appropriate method of limiting the impact of this decision. The Court of Appeal's decision reversing the trial court's order sustaining the demurrer as to the cause of action for fraud was the just result in this case and should be affirmed accordingly.

DATED: September 15, 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 this Answer Brief is proportionately spaced, has a typeface of 13 points and contains 1,590 words, including footnotes.

DATED: September 15, 2008 ENGSTROM, LIPSCOMB & LACK

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PROOF OF SERVICE BY MAIL

In Re: ANSWER TO AMICUS CURIAE BRIEF OF PERSONAL INS. FED. OF CA AND NATIONAL ASSOC. OF MUTUAL INS. COMPANIES; No. S161008
Caption: Village Northridge Homeowners Assoc. v. State Farm Fire & Casualty Co.
Filed: IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

STATE OF CALIFORNIA)
) ss:
COUNTY OF LOS ANGELES)

I am a citizen of the United States and a resident of or employed in the City and County of Los Angeles; I am over the age of eighteen years and not a party to the within action; my business address is: 900 Wilshire Blvd., Suite 1530, Los Angeles, California 90017. On this date, I served the persons interested in said action by placing one copy of the above-entitled document in sealed envelopes with first-class postage fully prepaid in the United States post office mailbox at Los Angeles, California, addressed as follows:

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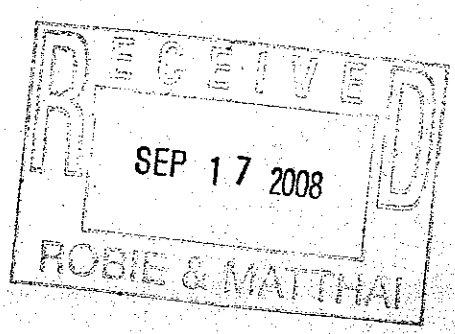
I certify (or declare) under penalty of perjury that the foregoing is true and correct. Executed on September 16, 2008, at Los Angeles, California.

E. Gonzales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