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IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

FARMERS INSURANCE COMPANY, INC., et al.,

Petitioners and Defendants,

v.

FRANCES MARC ALEXANDER, et al.,

Respondents and Plaintiffs.

After a Decision by the Court of Appeal
Second Appellate District, Division Eight
Case No. B239840

PETITION FOR REVIEW

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Service on Attorney General and Los Angeles County District Attorney Pursuant to California Business & Professions Code Section 17209

ISSUE PRESENTED

May the statutorily required appraisal remedy for property loss disputes under fire insurance policies be evaded – and resort to suit in the first instance be had – by simply alleging that the other side's valuation methodology does not comply with the law?

The statutorily mandated terms of each and every standard fire insurance policy in California requires that if the parties disagree about the value of a property loss, "then, on the written request of either," the insured and the carrier must engage in an appraisal process – an arbitration as to the property loss value. Consistent with public policy favoring arbitration, Insurance Code section 2071 directs that no suit may be pursued "unless all the requirements" of the policy "have been complied with." At issue is how and when such a mandatory appraisal prerequisite to suit is to be enforced.

The law on this issue is uncertain and conflicting. *Community Assisting Recovery, Inc. v. AEGIS Security Ins. Co.,* 92 Cal. App. 4th 886 (2001), the Dissent in this case, and a uniform line of federal decisions hold that regardless of how an insurer computes the value of a loss, pursuing the appraisal remedy is a prerequisite to any lawsuit. Directly to the contrary, *Kirkwood v. California State Auto. Assn.,* 193 Cal. App. 4th 49 (2011), *Doan v. State Farm General Ins. Co.,* 195 Cal. App. 4th 1082 (2011), and the Majority Opinion in this case hold that the appraisal remedy may be skipped simply by claiming that the insurer's methodology does not comply with the law.

INTRODUCTION

The Standard Fire Policy has been in existence for well over 100 years. *See Mitchell v. United National Ins. Co.,* 127 Cal. App. 4th 457, 470 n.4 (2005). In California, the Standard Fire policy is codified in Section 2071 of the Insurance Code. Section 2071 dictates the provisions that must be included in ***every*** fire insurance policy issued in California. One of those provisions is that in the event of a dispute as to the value of a loss, either party is entitled to an "appraisal," a loss valuation arbitration. If requested by either party, appraisal is a mandatory, initial remedy.

For years, one thing insureds, insurers and practitioners could bank on was that if there was a dispute as to how an insurer valued a property loss, appraisal was required. In 2011, two Court of Appeal decisions threw this area of the law into conflict.

The Line of Authorities Requiring Appraisal

In *Community Assisting,* the plaintiff non-profit corporation sued 194 insurers alleging that they were adjusting property loss claims in violation of California law. Despite the claims that the insurers' valuation methodologies violated California law, the court found that compliance with the appraisal provision was required:

> ". . . Insurance Code section 2071 requires appraisal for resolution of contested claims. . . . Thus, ***notwithstanding how the insurer approaches valuation of the damaged property during the adjustment of the claim,*** the Legislature has provided the remedy to

> which the parties must resort for determination of the amount of the loss." *Community Assisting, supra* at 893 (emphasis added).

An unbroken line of federal decisions, applying California law, have followed *Community Assisting* and ordered appraisal.[1] Frequently, these decisions involved claims by the plaintiff that a "legal issue" – whether the insurer was correctly applying the law – allowed them to avoid or at least to delay appraisal. Uniformly, the federal courts rejected such claims. *Enger DC, supra* at 11-13; *Garner, supra* at *17-23; *Goldberg, supra* at *9.

The Conflicting Line of Authorities Disregarding Appraisal When an Insured Claims That the Insurer's Methodology Is Improper

This consistent law has been thrown into disarray by *Kirkwood* and *Doan*, which have now been joined by the Majority Opinion in this case. These decisions claim that *Community Assisting* has effectively been overruled by a 2004 amendment to section 2051 of the Insurance Code, an amendment that had nothing to do with whether appraisal is required.

As a result, California law is now unsettled. *Kirkwood, Doan* and the Majority Opinion declare that appraisal is not the mandatory remedy

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[1] *Enger v. Allstate Ins. Co.*, 407 Fed. Appx. 191, 193 (9th Cir. 2010); *Enger v. Allstate Ins. Co.*, 682 F. Supp. 2d 1094, 1098-99 (E.D. Cal. 2009) ("*Enger DC"*); *Pavlina v. SAFECO Ins. Co.*, 2012 U.S. Dist. LEXIS 159991, *13 (N.D. Cal. 2012); *Pivonka v. Allstate Ins. Co.*, 2011 U.S. Dist. LEXIS 142770, *7-15 (E.D. Cal. 2011); *Garner v. State Farm Mutual Auto. Ins. Co.*, 2008 U.S. Dist. LEXIS 120263, *22-23 (N.D. Cal. 2008); *Goldberg v. State Farm Fire & Cas. Co.*, 2002 U.S. Dist. LEXIS 7131, *7-9 (C.D. Cal. 2002).

when valuation questions are involved, while the federal cases, all of which are applications of California law, *Community Assisting*, and the Dissent declare just the opposite.[2]

The effect of *Kirkwood*, *Doan* and the Majority Opinion here is to make the statutorily required appraisal process illusory. Property value disputes are always going to be about methodology, assumptions or baseline values. One party or the other will always be able to allege that the other's approach does not comport with some legal standard and therefore the dispute should be determined by lawsuit, not appraisal/arbitration.

The Disagreement on a Court's Discretion to Deny Appraisal

As the Dissent stresses, *Kirkwood* and *Doan* rejected appraisal as the initial remedy without considering the limitation on a court's discretion to deny arbitration. *Slip Opinion* ("*SO*") (Dissent), pp. 2-3, 7.[3] But appraisal is a form of arbitration, *e.g.*, *Lambert v. Carneghi*, 158 Cal. App. 4th 1120, 1130 (2008); *Michael v. Aetna Life & Casualty Ins. Co.*, 88 Cal. App. 4th 925, 934 (2001), a remedy favored by the strong public policy of California as a speedy and relatively inexpensive means of dispute resolution, *e.g.*, *Ericksen, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak Street*, 35 Cal. 3d 312, 322 (1983); *Acquire II, Ltd. v. Colton Real Estate Group*,

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[2] In this regard, it is important to note that both *Pavlina* and *Pivonka* (cited in the prior footnote) were decided after *Kirkwood* and *Doan*, and these decisions each considered and declined to follow *Kirkwood* and *Doan*. Review was not sought in *Doan*; and review was denied in both *Community Assisting* and *Kirkwood*.

[3] A copy of the *Slip Opinion* is attached as Exhibit A.

213 Cal. App. 4th 959, 967 (2013). Given that context, until the decisions in *Kirkwood*, *Doan* and the Majority Opinion, trial courts have been limited to denying a request for appraisal only if the issue not subject to appraisal is likely to render appraisal unnecessary. Code of Civil Procedure, § 1281.2(c). But no such finding was made in this case, in *Kirkwood* or in *Doan*, which apparently have done away with the statutory limitation.

This Unsettled Law Has Produced Eight Conflicting Decisions in the Last Five Years

The importance of this issue is illustrated by its recurrent nature. Since 2008, the question of whether appraisal is required prior to civil litigation has produced eight decisions and one ringing Dissent. *Kirkwood, Doan,* and the Majority Opinion in this case have found that appraisal could be deferred in favor of civil litigation. *Garner, Enger DC, Enger, Pivonka, Pavlina,* and the Dissent all found that appraisal was the initial, mandatory remedy in loss valuation cases.

In summary, review should be granted in this case to secure uniformity of decision and to resolve an important question of law.

STATEMENT OF THE CASE

Plaintiffs' Insurance Claims

The original plaintiff in this action, Francis Marc Alexander ("Alexander"), a Fire Insurance Exchange policyholder, suffered a partial fire loss to his home and personal property. *Appellants' Appendix* (*AA*), Tab 1, p. 000005. Thomas and Ana Downie ("Downies") were added as plaintiffs in the First Amended Complaint. *AA*, Tab 11, p. 000316. As Fire

Insurance Exchange policyholders, they too suffered a partial fire loss to their home and personal property in San Francisco, California.[4] *AA*, Tab 11, p. 000318. Plaintiffs submitted "property claims to Farmers,[5] identifying the damaged property and the estimated cash value of each item." Plaintiffs "disputed Farmers' adjustment of their claims," resulting in the present putative class action litigation. *SO* (Majority), p. 2.

The Trial Court Denies Appraisal

Plaintiffs allege that Farmers' adjustment of their claims, and those of the putative class members, violated Insurance Code section 2051 in estimating the actual cash value of their losses. *AA*, Tab 1, p. 000006; Tab 11, p. 000318. First, with respect to their personal property, plaintiffs allege that Farmers improperly based depreciation of lost or damaged items on age alone. Second, with respect to structural components, plaintiffs allege that Farmers depreciated components not normally repaired or replaced during the useful life of the structure, which should not have been subject to depreciation. *AA*, Tab 17, p. 000787.

Farmers demurred[6] to the First Amended Complaint (*AA*, Tab 12, p. 000469), filed a motion to strike (*AA*, Tab 13, p. 000492), and filed a

[4] The claims of Alexander and the Downies include both a claim for loss of personal property and a claim for loss to a structure. As amended, section 2051 requires that in the case of a partial loss to a structure, depreciation may only be taken for "components of a structure that are normally subject to repair and replacement during the useful life of that structure." Insurance Code, § 2051(b)(2). Neither *Kirkwood* nor *Doan* appear to have involved structural claims.

[5] In this Petition, unless otherwise noted, Petitioners are collectively referred to as "Farmers."

[6] Farmers' demurrer did not dispute the requirement to consider an item's "condition." Rather, it sought a ruling that "age" was also a factor to be

motion to compel appraisal. *AA,* Tab 14, p. 000516. At the hearing on the demurrer and motions to strike and compel appraisal, Farmers agreed that section 2051 "requires you to consider a condition in making a determination of physical [depreciation]," and thus that there was no legal dispute but rather "an agreement between the plaintiff and the defendant that [section 2051] requires consideration of condition. . . ." Reporter's Transcript, Jan. 26, 2012, pp. B-2:24-27, B-3:14-20.

The trial court overruled the demurrer and denied the motions to strike and to compel appraisal. *AA,* Tab 28, p. 111003. The court denied the motion to compel appraisal "without prejudice to potential renewal of the motion at a subsequent phase of the litigation." *AA,* Tab 30, p. 001025. Farmers timely appealed from the denial of its motion to compel appraisal. *AA,* Tab 32, pp. 001053-54.

The Court of Appeal's 2-1 Published Decision and Dissent

On September 23, 2013, the Court of Appeal filed its Opinion.

The Majority Opinion

The Court of Appeal's Majority reads section 2051(b)(2)'s definition of actual cash value, and Code of Regulations section 2695.9(f) implementing section 2051(b)(2), as requiring consideration of "the condition and age of the property," as presenting a legal issue that could only be determined by the courts. *SO* (Majority), pp. 2-3.

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considered pursuant to section 2051(b)(2). *AA,* Tab 12, p. 000476.

Following the lead of *Doan*[7], the Majority found that appraisal is a limited form of arbitration and that appraisers have no "'power to interpret insurance contracts or the governing statutes.'" *SO* (Majority), p. 4.

The Majority recognized the fractured state of the law between "a line of decisions which hold that the remedy for an insured" when there is a valuation dispute "is appraisal," specifically referring to *Community Assisting* and *Pivonka*, on the one hand, and "state court decisions which hold that the trial court has discretion to defer appraisal," specifically *Kirkwood* and *Doan*, on the other. It concluded that "the more reasoned approach lies with *Kirkwood* and *Doan* . . . ." *SO* (Majority) p. 8.

The Majority distinguished *Community Assisting* on two bases. First, in agreement with *Kirkwood* and *Doan*, the Majority Opinion found that the 2004 amendment to section 2051 effectively overruled *Community Assisting*. *SO* (Majority), p. 14. Prior to the amendment, in the Majority Opinion's view, "'there was no statutory direction dictating how the insurer was to measure actual cash value" and therefore *Community Assisting*, decided in 2001, did not consider the statutory direction found in section 2051. *SO* (Majority), p. 10. The Majority did not explain how a statutory definition of value affected the separate appraisal requirement.

Second, the Majority distinguished *Community Assisting* by asserting that there the plaintiff "failed to assert an unlawful business claim because it failed to allege the defendant's conduct was unlawful."[8] It read

[7] *Doan, supra* at 1094.

[8] As we discuss below, the plaintiff in *Community Assisting* in fact did

Community Assisting as not considering declaratory relief, but merely finding the merits of the plaintiffs' claim to be lacking. In the Majority's view, *Community Assisting* did not need to "invoke Code of Civil Procedure section 1281.2 to determine whether other issues not subject to appraisal need to be determined prior to appraisal." *SO* (Majority), p. 14.

Following *Kirkwood*, the Majority then opined that based on "judicial economy," the trial court had discretion to defer appraisal because appraisal might "be averted" if plaintiffs receive both a favorable declaration and "an order that Farmers readjust" all claims. *SO* (Majority), pp. 15-16.

Finally, the Majority distinguished *Pivonka*, which had required appraisal where the insurer had recognized that it was required to "consider the age and condition of an item during its evaluation," meaning that there was no "statutory or regulatory 'controversy' between the parties," to be resolved outside of appraisal. *Pivonka*, *supra* at *7-11. The Majority found that Farmers had "waived" reliance on *Pivonka*, holding that "Farmers' attorney's statements during" the motion hearing was somehow not a timely concession on the legal point. *SO* (Majority), p. 17. Likewise, it held that the insurer's letter stating that depreciation was applied "'based on average quality, ***condition***, age and useful life,'" of the property, was insufficient to concede the ***legal*** standard because there was no "offer[] to recalculate depreciation." *SO* (Majority), p. 18 (emphasis added).

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allege that the actions of 194 insurers were "***in violation of controlling California law."*** *Community Assisting*, *supra* at 890 (emphasis by the court).

The Dissent

Justice Grimes in dissent disagreed with the Majority Opinion in two regards. First, the Dissent observed that any dispute over acceptable methodology to be addressed in civil litigation would not make the ensuing appraisal unnecessary – the standard for disregarding the appraisal/arbitration requirement – and the trial court could not have "reasonably" made such a finding. Second, the Dissent explained that "even if the *Kirkwood* and *Doan* cases are correct that appraisal may be deferred for a declaratory judgment on statutory interpretation issues, there are none in this case; the issues are factual ones about whether Farmers does what section 2051 requires it to do." *SO* (Dissent), p. 1.

The Dissent explained that "section 2071 is clear" that no suit may be filed until "'all the requirements'" of section 2071 had been complied with, and appraisal is one such requirement. Appraisal is a form of arbitration and "the arbitration statutes compel the same result." Specifically, section 1281.2(c) of the Code of Civil Procedure permits deferral of arbitration "'only if the court first determines that resolving the nonarbitrable claims in court may make arbitration'" unnecessary. *SO* (Dissent), pp. 2-3. But, as the Dissent noted, "the trial court made no such determination," nor could it "reasonably be made in this case." *SO* (Dissent), pp. 1, 3.

The Dissent directly disagreed with *Kirkwood* and *Doan.* Although *Kirkwood* found that declaratory relief "'would inform the appraisal'" and would serve "'judicial economy,'" the Dissent concluded that *Kirkwood*

considered the wrong "consideration;" the "only consideration is the one stated in the statute: if the court finds resolution of the other issues may make the appraisal unnecessary." *SO* (Dissent), p. 5.

Doan, the Dissent noted, "unlike *Kirkwood*, referred to and quoted the pertinent arbitration statute . . . ." *SO* (Dissent), p. 6. However, having done that, *Doan* did not "acknowledge or address the express limitation on the court's discretion," and in fact relied upon cases involving a "third party" where a trial court's discretion is more expansive than the necessity of a finding that litigation may make the arbitration unnecessary. Accordingly, the Dissent rejected *Kirkwood* and *Doan* and concluded that, without more, the trial court's denial of appraisal had to be reversed. *SO* (Dissent), pp. 6-7. But the Dissent continued to explain other reasons for reversal.

The Dissent further noted that a judicial declaration is neither needed nor beneficial, as there "is no reason to believe the appraisers will misconceive the law." "Appraisers do not need a judicial opinion on the legality of Farmers' practices, or on the meaning of 'physical depreciation,' or on precisely which structural components are normally repaired or replaced during the structure's useful life." *SO* (Dissent), pp. 8-11.

Moreover, the Dissent added that "even if I agreed with *Kirkwood*," its rationale is inapplicable in this case since Farmers acknowledges that an item's "condition" must be considered. Given that acknowledgement, "in fact there is no need to construe the meaning of the statute." *SO* (Dissent), pp. 3-4. Thus, the Dissent concluded there "is no real statutory

interpretation issue in this case." Farmers had conceded that "condition" must be considered in determining actual cash value and that only structural components normally subject to repair or replacement can be depreciated. *SO* (Dissent), p. 8.

The Dissent concluded that *Community Assisting, Enger* and *Pivonka* were "California and federal precedents supporting the view" that without regard to section 1281.2(c), "appraisal may not be delayed." *SO*, (Dissent), p. 11-13.

The Petition For Rehearing

On October 7, 2013, Farmers filed a Petition for Rehearing. Farmers sought rehearing on three issues. First, the Majority Opinion's statement that "no appraisal would be necessary" if plaintiffs could obtain "an order that Farmers readjust claims," was based on an issue first raised in oral argument[9] but which was never briefed. Second, Farmers sought to correct the Majority Opinion's statement[10] that Farmers had waived reliance on the argument that the parties were in agreement as to the meaning of section 2051. Third, in footnote 7, the Majority Opinion stated that "Farmers acknowledges that the claims regarding its valuation methodology are not subject to appraisal." In fact, Farmers' position is that any challenge to valuation methodology is initially subject to appraisal.

On October 9, 2013, the Petition for Rehearing was denied.

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[9] *SO* (Majority), p. 16.

[10] *SO* (Majority), p. 17.

WHY REVIEW SHOULD BE GRANTED

A. The Central Role of the Statutorily Required Appraisal Process

California courts "have enforced appraisal clauses in fire policies for" over "100 years." *Appalachian Ins. Co v. Rivcom Corp.*, 130 Cal. App. 3d 818, 824 (1982). The appraisal clause is part of what is known as the Standard Fire Policy, which has been in existence since 1873. *Mitchell, supra,* 127 Cal. App. 457 4th at 470 n.4. California made appraisal a statutory remedy at least as early as 1909. *Hyland v. Millers National Ins. Co.*, 91 F.2d 735, 737 (9th Cir. 1937). Sections 2070 and 2071 of the Insurance Code contain California's version of the Standard Fire Policy.

Every property policy issued in California must conform to sections 2070 and 2071 and thus must contain a provision which makes appraisal mandatory, upon the request of either the insured or insurer when there is a valuation dispute over a property loss. The appraisal provision was created to be a "substitute for the complicated and time-consuming processes of the common law . . . ." *Hyland, supra* at 735. This fact – that appraisal was created to help not hinder insureds – underscores the rationale for requiring appraisal as the mandatory, initial remedy.

The appraisal remedy performs an important function. It means the valuation disputes about property losses do not burden parties with undue litigation expenses nor clog the courts. Rather, such disputes are to be resolved expeditiously by experts through a fair process involving well-

recognized principles. Of course, an appraisal may yield the valuation result that the insured seeks. If so, a lawsuit as to the proper valuation is wholly unnecessary. If an insured believes that a carrier has acted improperly and unfairly in the claims valuation process, the insured may still sue for bad faith once the appraisal process has been completed.

B. The Law Becomes Confused

Community Assisting declared without reservation that appraisal was a mandatory remedy "notwithstanding how the insurer approaches valuation of the damaged property during the adjustment of the claim . . . ." *Community Assisting, supra* at 893.

Prior to 2011, *Community Assisting* was applied with approval in *Goldberg v. State Farm Fire & Cas. Co., supra,* 2002 U.S. Dist. LEXIS at 7131 *7-9; *Garner v. State Farm Mutual Auto. Ins. Co., supra,* 2008 U.S. Dist. LEXIS at 120263, *22-23; *Enger DC, supra,* 682 F. Supp. 2d at 1098-99; *Enger v. Allstate Ins. Co., supra,* 407 Fed. Appx. at 193. In short, California law was settled that, in the event of a dispute over the valuation of a property claim, if appraisal was requested, then it was mandatory regardless of how the insurer had adjusted the claim.

That changed in 2011. *Kirkwood* and *Doan* rejected *Community Assisting,* deferring appraisal in favor of civil litigation. The result is confusion as to when appraisal is required. The danger posed by *Kirkwood* and *Doan* is not that appraisal can sometimes be deferred in favor of litigation – section 1281.2(c) has so provided for many years. The danger, as the Dissent so well explains, is that any factual dispute over valuation

can be restated as a legal dispute by simply pleading that the insurer's method of valuation is inconsistent with the requirements of section 2051 and such restatement nullifies the requirement of appraisal. This danger threatens to abrogate the appraisal remedy.

Underscoring the fact that California law is unsettled is the 2-1 decision in this case. The Majority Opinion, falling in line with *Kirkwood* and *Doan*, absolutely rejects *Community Assisting's* position that regardless of the insurer's method of valuation, appraisal is required. In direct contradiction, the Dissent cuts through plaintiffs' pleadings, declaring that the issues in this case "are factual ones," not statutory interpretation issues. *SO* (Dissent), p. 1. Judged by any standard, California law regarding appraisal is unsettled.

C. <u>This Issue Affects Every California Homeowners' Policy</u>

According to the U.S. Census, in 2011 there were over 13.7 million homeowners in California. The vast majority of those homeowners unquestionably have fire insurance. It is required to obtain a home loan. And, section 2071 dictates that each of those policies ***must*** contain an appraisal provision; if a policy does not contain such a provision, it is implied. California is unfortunately subject to frequent fires and fire storms. Thus, necessarily, whether appraisal is a mandatory remedy for disputes over property losses is an issue that impacts millions of California insureds and the entire California homeowner's insurance market. One way or the other, whether appraisal is a mandatory remedy is an issue that should be settled.

D. As the Dissent Demonstrates, the Rule of *Kirkwood, Doan,* and the Majority Opinion Will Abrogate the Appraisal Remedy and Is Unsupportable

(1) *Kirkwood, Doan* and the Majority Opinion Effectively Negate The Appraisal Process

The Majority Opinion exemplifies what *Kirkwood* and *Doan* have wrought – the death-knell to the statutorily mandated appraisal process. A party can always claim that the other party isn't applying the correct legally mandated valuation standard or is not doing so properly. According to the Majority Opinion, that is so even where the carrier expressly ***agrees*** as to what the legal standard for valuation should be. Given the breadth of the rule that the Majority Opinion has formulated, it is hard to conceive of a case that a party could not frame in terms that would take it out of the appraisal process.

Little consideration is given in *Kirkwood* or the Majority Opinion to the public policy supporting appraisal. To the extent it is considered at all, *Kirkwood* sought to dismiss appraisal as some inferior form of arbitration[11] – "a special form of limited arbitration." *Kirkwood, supra* at 58. Continuing this view, the court noted that appraisers "have no power to interpret the insurance contract or the governing statutes." *Id.*[12] In this,

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[11] "Just because the role of appraisers may be more limited than that of arbitrators . . . does not make an appraisal any less of an arbitration." *Lambert v. Carneghi,* 158 Cal. App. 4th1120, 1131 (2008).

[12] It is an overstatement to say appraisers cannot interpret the statutes under which they are empowered to act. Certainly, they cannot ascribe meaning to terms not supported by California law, but to perform their jobs they must review sections 2071 and 2051 and act in accordance with the dictates of those sections.

Kirkwood wholly misses the point. Section 2071 intentionally limits an appraiser's power to ensure that appraisal is speedy and relatively inexpensive. Rather than being a reason to prefer civil litigation over appraisal, the limited nature of appraisal further justifies its role as the mandatory remedy in valuation disputes.[13]

Strong public policy favors appraisal. Appraisal is, of course, a form of arbitration. *Mahnke v. Superior Court*, 180 Cal. App. 4th 565, 573 (2009): *Devonwood Condominium Owners Assn v. Farmers Ins. Exchange*, 162 Cal. App. 4th 1498, 1505 (2008); *Michael v. Aetna Life & Cas. Ins. Co*., 88 Cal. App. 4th 925, 934 (2001). As a form arbitration, appraisal is favored by California public policy as a "speedy and relatively inexpensive means of dispute resolution." *Ericksen, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak Street*, 35 Cal. 3d 312, 322 (1983); *Lewis v. Fletcher Jones Motor Cars, Inc*., 205 Cal. App. 4th 436, 443 (2012). *Kirkwood, Doan* and the Majority Opinion here have converted what was intended to be a speedy and inexpensive form of dispute resolution into a cumbersome, time-consuming and expensive one, the expense of which must be borne not only by a particular claimant, but by all insureds who ultimately pay for the process through premiums.

This Court has disapproved "'procedural gamesmanship' aimed at undermining the advantages of arbitration." *Ericksen, Arbuthnot, supra* at

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[13] The Majority Opinion states that "Farmers acknowledges that the claims regarding its valuation methodology are not subject to appraisal." To the contrary, Farmers' unwavering position is that any dispute over its valuation methodology is subject to appraisal. Farmers sought rehearing to correct this misstatement in the Majority Opinion.

323. That disapproval is particularly relevant here. As this case demonstrates, the fact is that any competent attorney can frame a factual valuation question as a disputed legal question and, if allowed, render appraisal meaningless. And, such really specific, factual disputes about the value of particular property can almost always be ginned up into a broader argument about "methodology" or "approach" and framed as a class action. If allowed, the result would be to substitute for the informal appraisal proceedings one of civil litigation's most expensive and time consuming products – the class action.

(2) The Majority, *Kirkwood*, and *Doan* Were Wrong In Not Following *Community Assisting* And Its Progeny

The common denominator of *Kirkwood*, *Doan* and the Majority is their disagreement with *Community Assisting*, a disagreement framed as *Community Assisting* having somehow been superseded by statute. However, an examination of the analysis of those opinions demonstrates their uniform error.

The Majority Opinion, *Kirkwood* and *Doan* all claim that the amendment of section 2051 (defining "actual cash value") after the issuance of *Community Assisting* somehow disapproved it. But they focus on the wrong statute. The mandatory requirement of appraisal found in section 2071 is ***unchanged from its enactment***[14] and certainly from 2001

[14] In 2001, the appraisal section was amended. However, the amendment merely prohibited "depositions, interrogatories request for admission, or other forms of formal civil discovery," unless the parties agree otherwise. *Mahnke v. Superior Court*, 180 Cal. App. 4th 565, 573 (2009). The amendment did not, in any way, change the requirement that appraisal is

when *Community Assisting* was decided. The key to *Community Assisting* is not how actual cash value is defined by statute, but rather the mandatory appraisal process under section 2071. The 2004 amendments to section 2051 were not intended to and did not alter the mandatory appraisal requirement of section 2071. "The Legislature is deemed to be aware of judicial decisions already in existence and to have enacted or amended a statute in light thereof. [Citation omitted.] When a statute has been construed by judicial decision, and that construction is not altered by subsequent legislation, it must be presumed that the Legislature is aware of the judicial construction and approves it.'" *Blankenship v. Allstate Ins. Co.,* 186 Cal. App. 4th 87, 96 (2010). The 2004 amendment to section 2051 without addressing the appraisal process, section 2071, or *Community Assisting*, thus, has to be construed as the Legislature's ***approval*** of *Community Assisting.*

This conclusion is reinforced by the mistaken belief by *Kirkwood, Doan* and the Majority Opinion that the amended section 2051 was some wholly new, extra-appraisal scheme because, when *Community Assisting* was decided, "there was no statutory direction dictating how the insurer was to measure the actual cash value of recovery under an open policy." *Kirkwood, supra* at 60; *Doan, supra* at 1097; *SO* (Majority), p. 10. But that's just not the case.

Since 1935, well before *Community Assisting*, section 2051 had governed how the value of recovery under an open policy had to be

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the mandatory remedy for a valuation dispute.

measured, and specifically included consideration of condition at the time of loss as part of that valuation process. Former section 2051 provided:

> "Under an open policy, the measure of indemnity in fire insurance is the expense to the insured of replacing the thing lost or injured ***in its condition at the time of the injury***, such expense being computed as of the time of the commencement of the fire." (Emphasis added).[15]

This earlier statutory definition did not make valuation disputes any less subject to appraisal under *Community Assisting*. The amendment to section 2051 added a specific measurement for actual cash value recovery. But that was not a rewriting of the whole statutory scheme. It was, at most, a tweak or refinement.

The battle between plaintiffs and Farmers here is generally over "condition" as used in the valuation process. That is, plaintiffs assert that "Farmers calculated depreciation based primary on the ***age*** of the each item . . . without regard to the ***condition*** of the property . . . ." *AA*, Tab 11, p. 000318 (emphasis added). The requirement that "condition" of the property be considered did not spring into being in 2004. Since 1935, it has been a statutory directive for valuation and was part of California law in 2001 when *Community Assisting* was decided. The 2004 amendment to section 2051 did not change the basic statutory framework in existence when *Community Assisting* was decided. The Legislature's tweak of

[15] Former section 2051 is quoted in *Breshears v. Indiana Lumbersmans Mut. Ins. Co*, 256 Cal. App. 2d 245, 247 (1967).

section 2051 did nothing to change *Community Assisting*'s broader holding regarding appraisal.

The Majority, *Kirkwood* and *Doan* also all attempted to distinguish *Community Assisting* procedurally. The Majority asserted "that the plaintiff . . . failed to allege the defendant's conduct was unlawful." *SO* (Majority), p. 14. In fact, the plaintiff in *Community Assisting* alleged that "defendants have adjusted and continue to adjust, or have concluded such claims on the basis of 'replacement cost less depreciation' ***in violation of controlling California law***." *Community Assisting*, *supra* at 890 (emphasis by the court). While the Majority noted that *Community Assisting* rejected the plaintiff's claim on the merits, they failed to note that this rejection was only ***after*** it first decided that appraisal was mandatory "notwithstanding how the insurer approaches valuation . . . ." *Community Assisting*, *supra* at 893; *see id*. at 894 [deciding merits issue].

Kirkwood, *Doan* and the Majority also observe that no claim for declaratory relief was involved in *Community Assisting*. *Kirkwood*, *supra* at 60; *Doan*, *supra* at 1094-97; *SO* (Majority), p. 16. But, so what? Whether pled as a claim for declaratory relief, unfair business practices, injunction, breach of contract, breach of the implied covenant of good faith and fair dealing, elder abuse or any other theory that a creative pleader could imagine, if the valuation of property losses is involved, appraisal is the remedial process.

Accordingly, the Majority, *Kirkwood* and *Doan* incorrectly conclude that the amendment to section 2051 effectively disapproved of *Community*

Assisting. As *Enger, Enger DC, Goldberg, Garner, Pivonka* and *Pavlina*[16] and the Dissent all declare, *Community Assisting* is still good law and appraisal remains the mandatory remedy when there is a dispute as to the valuation of losses under an insurance policy.

(3) The Dissent Has The Better Of The Debate Over Judicial Economy

The Dissent also disagreed with the Majority, *Kirkwood* and *Doan* on two other bases: whether delaying appraisal would likely render it unnecessary and whether declaratory relief is either needed or beneficial.

Code of Civil Procedure section 1281.2(c) permits delay of arbitration "only if the court first determines that resolving nonarbitrable claims in court may make the arbitration of the arbitrable claims unnecessary." *Acquire II, Ltd v. Colton Real Estate Group,* 213 Cal. App. 4th 959, 977 (2013); *RN Solution, Inc. v. Catholic Healthcare West,* 165 Cal. App. 4th 1511, 1521 (2008).

Kirkwood evaded this requirement by imposing a "judicial economy" exception. There, the trial court, in denying the motion to compel appraisal, noted that "'I don't see how the plaintiff gets out of an appraisal later.'" *Kirkwood, supra* at 57. *Kirkwood* agreed but nonetheless upheld denying appraisal, because declaratory relief ''would inform the

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[16] *Enger, supra,* 407 Fed. Appx. at 193; *Enger DC, supra,* 682 F. Supp. 2d at 1098-99; *Pavlina, supra,* 2012 U.S. Dist. LEXIS 159991, at *13; *Pivonka, supra,* 2011 U.S. Dist. LEXIS 142770, at *7-15; *Garner, supra,* 2008 U.S. Dist. LEXIS 120263, at *22-23; *Goldberg, supra,* 2002 U.S. Dist. LEXIS 7131, at *7-9.

appraisal'" and serve "'judicial economy.'" *Kirkwood, supra* at 63. In doing so, as the Dissent here notes, "*Kirkwood* used an erroneous standard," as "[p]olicy considerations such as judicial economy . . . or the 'strong policy favoring declaratory relief'. . . have no place in a trial court's exercise of its discretion to delay appraisal: the only consideration is the one stated in the statute: if the court finds resolution of other issues may make the appraisal unnecessary." *SO* (Dissent), pp. 5-6. Indeed, it would be hard to imagine a circumstance where a judicial declaration on the same facts would not "inform" an appraisal or arbitration. If that is the standard then courts have carte blanche to skip the appraisal/arbitration process.

Doan sought to at least give lip service to the section 1281.2(c). But *Doan* relied on a portion of that subsection inapplicable to appraisals, specifically, the rules applicable when a "third party" is involved in litigation otherwise subject to arbitration. *Doan, supra* at 1100-01; *see SO* (Dissent), p. 7. In the "third party" situation, subsection (c) permits a trial court to delay arbitration if there is a "possibility of conflicting rulings on a common issue of law or fact." But this portion of subsection (c) only applies when a third party is involved. *Rowe v. Exline,* 153 Cal. App. 4th 1276, 1290 (2007); *Laswell v. AG Seal Beach, LLC,* 189 Cal. App. 4th 1399, 1408 (2010) ("Because no defendant in this case is a third party to the arbitration agreement, the discretion afforded by Code of Civil Procedure section 1281.2, subdivision (c), does not come into play and thus the trial court erred as a matter of law in denying defendants' petition to compel arbitration."); *RN Solution, Inc., supra,* 165 Cal. App. 4th 1511, 1521 n.15 (contrasting discretion afforded court when a "third party" is involved with "the much ***narrower discretion*** provided under the ***third*** paragraph of

subdivision (c)" when only parties subject to an arbitration agreement are involved) (emphasis added).

Recognizing *Doan's* error, the Dissent here stressed, "[n]one of the cases *Doan* cites on the trial court's discretion involves the court's discretion to delay arbitration between two parties who have agreed to arbitrate; they involve the court's discretion . . . where litigation with a third party is at issue. [Citation omitted.] That provision of the arbitration statute is irrelevant to this case." *SO* (Dissent), p. 7.

The Majority Opinion followed the *Kirkwood* and *Doan* reasoning that section 1281.2(c) could be ignored if a judicial declaration might somehow inform a later appraisal or afford a class-wide recalculation of benefits. *SO* (Majority), p. 16. But as the Dissent details, such a supposed benefit is nonexistent:

> ". . . there is no reason to believe that the appraisers will misconceive the law. In short, the declaratory relief plaintiffs seek – in substance, a declaration that Farmers does not use the condition of the item to determine physical depreciation in violation of section 2051, subdivision (b)(2) – will do nothing at all to affect or 'inform' the appraisal process, and there is thus no purpose to be served by declaratory relief in advance of the appraisal." *SO* (Dissent), p. 8.

Underscoring this point, it is unnecessary for "a declaration to precede the appraisal Farmers has requested . . . . Expert appraisers already

know what 'physical depreciation' and 'condition' mean, and they do not need the court to explain them." *SO* (Dissent), p. 9.

Indeed, rather than to "inform" an appraisal, it is clear that the object and effect of the declaratory relief claim in this case – and in the cases that inevitably will follow this model – is not to "inform" appraisal, but to ***replace*** appraisal. For example, plaintiffs argue that only "a jury" can decide whether an item is of the type normally subject to repair or replacement during the useful life of the structure (see section 2051 [setting this as the partial-loss standard]).[17] But it is "particularly striking that a trial court" – or in plaintiffs' view, a jury – "should be asked to declare that specific categories of structural components" are or are not subject to repair or replacement. "Who better than an expert appraiser would know the useful life of a structure, and who better than an expert appraiser would know which of the components of a structure are 'normally subject to repair and replacement' during that structure's useful life?" *SO* (Dissent), pp. 9-10.

Unlike *Kirkwood* and *Doan*, in this case Farmers has acknowledged that section 2051(2)(b) requires consideration of "condition" in valuing personal property losses. Thus, here, it is clear that all that is to be determined is application of an acknowledged legal standard to the facts. See *Pivonka*, *supra*, 2011 U.S. Dist. LEXIS 142770, at *8, * 13 (given absence of "a dispute about the standard that governs appropriate

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[17] *Respondents' Brief,* pp. 19-20.

depreciation," there is no "need to clarify the parties' legal relations before appraisal is ordered").[18]

The bottom line is that judicial economy – that is, assuring speedy and inexpensive resolution of property value disputes in the insurance context – is best served by honoring the statutory directives mandating appraisal and forbidding undue evasion of arbitral processes.

CONCLUSION

The Majority Opinion here on the heels of *Kirkwood* and *Doan* will effectively destroy the statutorily mandated appraisal process. It opens the doors to cumbersome and expensive litigation over virtually every insured property loss dispute. And, it does so by directly contradicting *Community Assisting* and the numerous cases following that decision.

Review is necessary to resolve the conflict in the law. Review is necessary to provide certainty to courts, millions of insureds, insurers and the California homeowner's market as a whole.

Accordingly, Farmers urges this Court to grant review.

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[18] The Majority Opinion claimed that Farmers had "waived" its concession of the applicable governing section 2051(b)(2) legal standard. *SO* (Majority), p. 17. But the statute says what it says. Farmers agreed that (as the statute has required since 1935) "condition" had to be considered. *AA*, Tab 11, p. 000434 (emphasis added). As the Dissent notes, Farmers is "bound by" that acknowledgement. *SO* (Dissent), p. 4. More to the point, the statutory wording is not at issue. All that is disputed is how it applies to specific facts.

Dated: October 31, 2013 BARGER & WOLEN LLP

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CERTIFICATE OF WORD COUNT

Pursuant to California Rules of Court, Rule 8.204(c)(1), Petitioners and Defendants' Petition for Review has a typeface of 13 points and contains 6,738 words, based on the word count of the computer program used to prepare the Brief.

October 31, 2013 _____

Kent Keller

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