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UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF CALIFORNIA

STEADFAST INSURANCE COMPANY, a Delaware corporation; and AMERICAN GUARANTEE AND LIABILITY INSURANCE COMPANY, a New York corporation,

Plaintiffs,

vs.

JAMES DOBBAS, an individual; PAMELA DOBBAS, an individual; DONALD DOBBAS, an individual; PETER MANCINI and LISA MANCINI, husband and wife; PETER MANCINI as Special Administrator of the ESTATE OF CLAUDETTE MANCINI, deceased; LISA MANCINI as the Guardian Ad Litem for NASYA MANCINI, a minor; FALLON TURNER, an individual; MERRICK TURNER, an individual,

Defendants.

AND RELATED COUNTER-CLAIMS.

Case No. 2:05-CV-00632-FCD-JFM

PLAINTIFFS/COUNTER-DEFENDANTS STEADFAST INSURANCE COMPANY AND AMERICAN GUARANTEE AND LIABILITY INSURANCE COMPANY'S MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF SECOND MOTION FOR SUMMARY JUDGMENT OR, IN THE ALTERNATIVE, SUMMARY ADJUDICATION

Hearing Date: December 14, 2007
Time: 10:00 a.m.
Courtroom: 2
Judge: Hon. Frank C. Damrell, Jr.

Date of Filing: March 30, 2005
Trial Date: May 6, 2008

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I. INTRODUCTION

Plaintiffs/Counter-Defendants Steadfast Insurance Company ("Steadfast") and American Guarantee and Liability Insurance Company ("American Guarantee") commenced this action against James Dobbas ("Dobbas" or the "Insured"), Pamela Dobbas, Donald Dobbas, Peter Mancini and Lisa Mancini (the "Mancinis"), and Fallon Turner and Merrick Turner (the "Turners"), seeking declaratory relief to determine whether Steadfast and American Guarantee are obligated to pay $4 million of the $5 million arbitration award the Mancinis and the Turners obtained against Dobbas.

The Mancinis and the Turners have counterclaimed against Steadfast and American Guarantee under the "direct action" provision of the California Insurance Code, Ins. Code. § 11580, seeking to collect under the arbitration award.

On October 31, 2005, Steadfast and American Guarantee moved for summary judgment or, in the alternative, summary adjudication, arguing no coverage existed under Steadfast Commercial General Liability Policy No. SCO 3680716-01 (the "Steadfast Policy") and American Guarantee Commercial Umbrella Liability Policy No. AUC 3778756-01 (the "American Guarantee Policy") based on Dobbas's failure to give notice until after a $5 million award had been entered in a binding, non-appealable arbitration.

On January 11, 2006, the Court denied Steadfast and American Guarantee's motion, concluding Steadfast and American Guarantee had not met their burden of proving actual prejudice.

Steadfast and American Guarantee now move for summary judgment or, in the alternative, summary adjudication, on their Fourth Claim for Relief (For Declaratory Relief That the Insureds Did Not Comply With the Notice Requirements of the Policies), on their Fifth Claim for Relief (For Declaratory Relief That the Insureds Failed to Comply With The Terms and Conditions of the Policies), on their Sixth Claim for Relief (For Equitable Relief From Judgment on the Basis of Collusion), and against the Mancinis and the Turners on their counterclaims on the basis that the undisputed evidence shows: (1) there is no "judgment" for purposes of recovery

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under California Insurance Code § 11580 because the arbitration award was not entered after an "actual trial"; and (2) Steadfast and American Guarantee were actually prejudiced by late notice.

II. FACTS

On May 27, 2002, Dobbas was pasturing seven to eight Angus bulls on property owned by Milton Holstrom ("Holstrom") in Sierra County, California. (*See* Separate Statement of Undisputed Facts ("SUF") ¶ 1). One of the bulls escaped from the pasture and eventually entered an adjoining roadway, where it was struck by the Turner automobile. (*Id.* ¶ 2). The Turner vehicle then collided with the Mancini automobile. (*Id.* ¶ 3). The collisions killed two individuals and injured four of the vehicles' occupants. (*Id.* ¶ 4).

The Mancinis and the Turners sued Dobbas, Holstrom, and certain other defendants in separate actions. (SUF ¶¶ 5-7). The Mancinis and the Turners then consolidated their cases in the United States District Court for the District of Nevada. (*Id.* ¶ 8). Dobbas and Holstrom tendered defense of the Claim to CalFarm Insurance ("CalFarm") (which later became Allied Insurance Company), which had insured Dobbas's livestock-husbandry activities under a $1 million Farm Liability Policy and a $3 million Umbrella Policy. (*Id.* ¶¶ 9-13). Dobbas, however, subsequently learned the CalFarm $3 million Umbrella Policy had been cancelled by his insurance broker. (*Id.* ¶ 14).

The Mancinis and the Turners accepted a $1 million settlement offer from CalFarm under the $1 million primary Farm Liability Policy. (SUF ¶¶ 15-17). They then agreed to participate in binding, unappealable arbitration to apportion an additional recovery against Dobbas and to give "legal effect" to their claim so they could take an assignment of Dobbas's action against his insurance broker, Fred Vitas ("Vitas") and Vitas Insurance Agency ("VIA"), for improper cancellation of Dobbas's CalFarm $3 million Umbrella Policy. (*Id.* ¶¶ 17-18). In exchange, the Mancinis and the Turners agreed not to execute ("Covenant Never to Execute") against Dobbas's personal assets. (*Id.* ¶¶ 19, 21-22).

The arbitration was held on February 25, 2004. (SUF ¶¶ 20, 23). Dobbas presented only two witnesses, including himself for one-half hour, and no expert testimony. (*Id.* ¶ 27-28).

In March 2004, the arbitrator issued a $5 million award against Dobbas–$3 million in favor of the Turners and $2 million in favor of the Mancinis. (SUF ¶ 48). By Order dated April 26, 2004, the United States District Court for the District of Nevada confirmed the arbitrator's award and entered a judgment of $5 million against Dobbas. (*Id.* ¶ 49). By agreement of the parties, the judgment confirming the arbitration award was not appealable. (*Id.* ¶ 50).

By letter dated May 7, 2004 (the "May 7, 2004 Letter"), counsel for Dobbas for the first time advised counsel for the Mancinis and the Turners that two additional insurance policies issued by Steadfast and American Guarantee had been located, of which Dobbas had previously been unaware ("the Claim"). Counsel also admitted Steadfast and American Guarantee had not been given notice.[1] (SUF ¶ 51). Steadfast had issued a the Steadfast Policy to Jim Dobbas, Inc. ("JDI"), a railroad salvage business, with a policy period of August 1, 2001 to August 1, 2002, and with coverage of up to $1 million for each occurrence and $2 million in the aggregate. (*Id.* ¶¶ 52-53). The Steadfast Policy identified Dobbas as an additional Named Insured. (*Id.* ¶ 54). American Guarantee had issued the American Guarantee Policy to JDI with a policy period of August 1, 2001 to August 1, 2002, and with coverage of up to $7 million. (*Id.* ¶¶ 55-56). The American Guarantee Policy identified Dobbas as an additional Named Insured. (*Id.* ¶ 57).

Steadfast and American Guarantee first learned of the Claim through service of process of a cross-complaint filed by CalFarm in a related action. (SUF ¶¶ 58-61). By letter dated May 14, 2004, Steadfast acknowledged receipt of the Claim and reserved all rights. (*Id.* ¶ 62).

The Steadfast and American Guarantee Policies require prompt notice of an occurrence or offense which may result in covered damages. (SUF ¶ 63-64). Both Policies also state there is no right of action against the insurer if the insured does not comply with all conditions of the Policy, and unless the insured's liability was determined after an "actual trial." (*Id.* ¶¶ 65-66).

On March 30, 2005, Steadfast and American Guarantee filed the instant action, seeking declaratory and equitable relief. (SUF ¶ 67).

[1] The May 7, 2004 Letter said, in part, "Steadfast and Zurich may raise issues related to their lack of notice of the underlying case prior to this time." (SUF ¶ 51).

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III. STANDARD FOR SUMMARY JUDGMENT

The Court may grant a motion for summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file together with the affidavits, if any, show there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." FED. R. CIV. P. 56(c). Judgment for the moving party must be entered "if, under the governing law, there can be but one reasonable conclusion as to the verdict." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 250 (1986).

The party seeking summary judgment bears the initial responsibility of identifying those portions of "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, which it believes demonstrates the absence of a genuine issue of material fact." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986).

Once the moving party has met its initial burden, Federal Rule of Civil Procedure 56(e) requires the nonmoving party having the ultimate burden of proof to go beyond the pleadings and identify facts which show a genuine issue for trial. *See id.* at 531. The nonmoving party must present evidence, and may not rely upon the mere allegations or denials of its pleadings. *See id.* Conclusory arguments unsupported by factual statements or evidence do not meet this burden. *See In re Lewis*, 97 F.3d 1182, 1187 (9th Cir. 1996). A dispute is "genuine" only if the evidence is such that a reasonable jury could return a verdict for the nonmoving party. *Anderson*, 477 U.S. at 248.

Even in cases in which summary judgment is unavailable with respect to all alleged claims, summary judgment may be granted in part as to the claims for which no genuine issues of material fact exist. *See* FED. R. CIV. P. 56(a), (b), (d). Rule 56 expressly authorizes a motion for summary judgment as to "all or any part" of the alleged claims, and provides for the entry of partial summary judgment as to particular claims for which no genuine issue of material fact exists. *Id.* The standards and procedures are the same for partial summary judgment as they are for a summary judgment disposing of all claims. *See Wang Labs., Inc. v. Mitsubishi Elec. Am., Inc.*, 860 F. Supp. 1448, 1450 (C.D. Cal. 1993).

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IV. ARGUMENT

The undisputed evidence shows: (1) there is no "judgment" for purposes of recovery under California Insurance Code § 11580 because the arbitration award was not entered after an "actual trial"; and (2) Steadfast and American Guarantee were actually prejudiced by late notice.

A. There is no "judgment" for purposes of recovery under California Insurance Code § 11580 or the Steadfast Policy and the American Guarantee Policy because the arbitration award was not entered after an "actual trial."

The Mancinis and the Turners filed counterclaims against Steadfast and American Guarantee under section 11580 of the California Insurance Code. Section 11580 grants an injured third party a statutory right to bring a direct action against the tortfeasor's liability insurer as long as there is a "judgment" against the insured. Ins. Code § 11580(b)(2) ("whenever judgment is secured against the insured . . . , then an action may be brought against the insurer on the policy and subject to its terms and limitations, by such judgment creditor to recover on the judgment").

Because no action can be brought against an insurer until a judgment is first secured, the clauses in policies embodying that rule are called "no action" clauses. *See Safeco Ins. Co. v. Superior Court*, 71 Cal. App. 4th 782, 786-87 (1999) (holding section 11580's requirement of a judgment against the insured is reflected in the standard "no action" provision of a liability insurance policy, which bars any action against the insurer until the insured's liability to the claimant has been determined by either a final judgment or an agreement signed by the insurer). The Steadfast and American Guarantee Policies both contain "no action" provisions. The Steadfast Policy states, in pertinent part: "A person or organization may sue us to recover on . . . a final judgment against an insured obtained after an actual trial." (SUF ¶ 65). Likewise, the American Guarantee Policy states, in pertinent part: "There will be no right of action against us under this insurance unless . . . the amount . . . has been determined . . . by actual trial and final judgment." (*Id.* ¶ 66).

"[A] trial does not have to be adversarial to be considered an 'actual trial' under the 'no action' clause, or to be considered binding against the insurer in a section 11580 proceeding." *Nat'l Union Fire Ins. Co. v. Lynette C.*, 27 Cal. App. 4th 1434, 1449 (1994). Rather, "courts focus on *whether the facts have been adjudicated independently in a process that does not create*

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the potential for abuse, fraud or collusion." *Id.* (emphasis added). Thus, "the term 'actual trial' in the standard 'no action' clause has two components: (1) an independent adjudication of facts based on an evidentiary showing; and (2) a process that does not create the potential for abuse, fraud or collusion." *Id.* The arbitration award at issue in this case fails to satisfy both of these components. Therefore, the Court should grant summary judgment to Steadfast and American Guarantee on their Fifth Claim for Relief (For Declaratory Relief That the Insureds Failed to Comply With The Terms and Conditions of the Policies) and against the Mancinis and the Turners on their counterclaims.

1. There was no independent adjudication of facts based on an evidentiary showing.

"To be enforceable against an insurer, a judgment need not be based on a contested or adversarial trial, but may rest upon a default hearing held following a settlement or an uncontested trial where the insured settled with the claimant and thereafter presented no defense." *Garamendi v. Golden Eagle Ins. Co.*, 116 Cal. App. 4th 694, 711 (2004) (internal quotation and citations omitted). "These circumstances *necessarily involve significant independent adjudicatory action by the court, thus mitigating the risk of a fraudulent or collusive settlement between an insured and the claimant.*" *Id.* (quotation omitted) (emphasis added). The term "actual trial" "presupposes a *contest* of issues leading up to final determination by court or jury, in contrast to a resolving of the same issues by agreement of the parties; i.e., *without a contest.*" *Rose v. Royal Ins. Co. of Am.*, 2 Cal. App. 4th 709, 716 (1991) (internal quotation omitted).

California courts have held there is no independent adjudication of facts based on an evidentiary showing where the insurer did not receive timely notice of the underlying proceedings and the underlying proceedings went uncontested. In *Lipson v. Jordache Enterprises, Inc.*, 9 Cal. App. 4th 151, 153-54 (1992), plaintiff George Lipson ("Lipson"), a commissioned sales representative, sued his employer, Jordache Enterprises, Inc. ("Jordache") for breach of contract. Jordache tendered defense of the claim to its general liability insurer, Royal Insurance Company of America ("Royal"). *Id.* at 154. Royal denied coverage and refused to defend. *Id.*

Pursuant to a stipulation between Lipson and Jordache, Lipson filed an amended complaint, adding potentially covered claims for negligence and defamation two days before trial. *Id.* Also two days before trial, Jordache's counsel attempted to notify Royal of the amended claims. *Id.* at 155. When Royal received the amended complaint, it agreed to defend. *Id.* However, "[u]nbeknownst to Royal, the trial had already taken place and judgment entered." *Id.* Following a 25-minute bench trial in which Lipson was the only witness, the court entered a $100,000 judgment against Jordache. *Id.* at 154-55.

The *Lipson* court reversed, characterizing the underlying proceedings as "an alleged trial on the merits." *Id.* at 161. The court noted:

> clearly something seems amiss in the circumstances surrounding the "trial": the last-minute stipulation to amend the complaint with new causes of action arguably covered by the policy and the extremely perfunctory trial itself with virtually no opposition from defendant. It appears that the *trial was substituted for a stipulated judgment, in order to provide unchallengeable findings of negligence and defamation, with the aim of creating some form of policy coverage.*

Id. at 158 (emphasis added).

While the facts in *Lipson* are similar to those in the instant case, Steadfast and American Guarantee, in fact, received no prior notice of the underlying proceedings. Instead, Steadfast and American Guarantee first learned of the Claim through service of process of a cross-complaint filed by CalFarm in a later, and related, action. (SUF ¶¶ 58-61).

Just as the underlying judgment in *Lipson* resulted from an "extremely perfunctory trial . . . with virtually no opposition from defendant," *Lipson*, 9 Cal. App. 4th at 158, the Mancinis and the Turners' claims went almost completely unchallenged at the arbitration. During the one-day arbitration hearing, the Mancinis and the Turners presented six live witnesses, one witness by deposition testimony, 27 exhibits, and the expert testimony of Dr. Michael J. Pontrelli. (SUF ¶¶ 23, 25-26). Dobbas, on the other hand, presented only two witnesses (including himself) and, perhaps most significantly, no expert witness testimony to rebut Dr. Pontrelli's expert opinions, although an expert witness was available to Dobbas. (*Id.* ¶¶ 27, 31).

Dobbas does not consider himself an expert about cattle ranching standards of care, and he did not hold himself out as a ranching expert at the arbitration hearing. (SUF ¶ 29).

Understandably, Dobbas's testimony was insufficient to rebut Dr. Pontrelli's expert opinions. Michael E. Neal, Dobbas's personal counsel, believed it was very important for Dobbas to have a competent ranching expert on his defense team, given the liability issue. (*Id.* ¶¶ 32-34). Mr. Neal did not find it advisable for Dobbas to act as his own expert witness, because his testimony would be characterized as biased and based on his own economic benefit or detriment. (*Id.* ¶ 35).

But, not surprisingly, the CalFarm-financed defense failed to present any expert testimony to contest Dr. Pontrelli's opinions, despite the availability of an expert witness. That fact is compelling evidence that the Mancinis and the Turners' claims proceeded virtually unchallenged at the arbitration. (SUF ¶¶ 31, 41). While Dobbas had recommended Todd York, a person knowledgeable about ranching in Sierra Valley, be used as an expert witness to testify on his behalf regarding the ranching issues (*Id.* ¶ 36), no expert was offered. Mr. Neal also recommended to Dobbas's defense counsel that Mr. York testify as an expert witness at the arbitration hearing. (*Id.* ¶ 37). Mr. Neal and Dobbas worked together the week before the arbitration hearing to confirm Mr. York's availability to testify as an expert on behalf of Dobbas. (*Id.* ¶ 38). Mr. York's name was even listed as an expert witness on the arbitration brief. (*Id.* ¶ 39). Mr. Neal expected Mr. York would be used as an expert witness at the arbitration hearing, based in part on the arbitration brief listing Mr. York as an expert witness. (*Id.* ¶ 40). Nonetheless, Dobbas's defense counsel did not call Mr. York, or anyone else, to rebut Dr. Pontrelli's expert testimony. (*Id.* ¶ 41). Mr. York's testimony would have been the only liability defense testimony because no one else was qualified to testify as an expert. (*Id.* ¶ 43).

It is plainly evident that the arbitration was essentially a one-sided evidentiary showing. For example, no one had told the arbitrator there was a large amount of hay in the back of Lot 8, which was inconsistent with Dr. Pontrelli's testimony that the bulls had nothing upon which to graze. (SUF ¶ 45). Mr. Neal further believes defense counsel did not have a good grasp on the factual basis of the litigation. (*Id.* ¶ 46). Based upon his substantial trial and arbitration experience, Mr. Neal does not think a full liability defense was presented to the arbitrator. (*Id.* ¶ 47). Even Dobbas himself was disappointed in the poor presentation at the arbitration hearing. (*Id.* ¶ 30). Dobbas did not believe his defense counsel asked him good questions. (*Id.* ¶ 30). In

light of this deficient, one-sided evidentiary showing, the arbitrator could not possibly make an independent adjudication of the facts.[2] Like *Lipson*, therefore, something "was clearly amiss" in the circumstances surrounding the arbitration, and the Mancinis and the Turners should not be permitted now to recover against Steadfast and American Guarantee on the underlying judgment.

In an analogous case, *Fuller-Austin Insulation Co. v. Highlands Insurance Co.*, 135 Cal. App. 4th 958, 966 (2006), plaintiff Fuller-Austin Insulation Company ("Fuller-Austin") was in the business of installing and removing building materials containing asbestos. Faced with thousands of personal injury lawsuits arising from asbestos exposure, Fuller-Austin filed for bankruptcy protection. *Id.* at 967. A "prepackaged" bankruptcy plan called for the establishment of a trust to meet the company's asbestos-related obligations. *Id.* at 968. The plan called for the bankruptcy court to decide the total amount of liability the trust would cover for present and future claimants. *Id.* Several insurance companies that had issued excess insurance policies to Fuller-Austin failed to convince the bankruptcy court that they had standing to challenge the plan. *Id.* at 971. Fuller-Austin then sued the excess insurers in an effort to force them to provide indemnification to fund the trust. *Id.* at 968.

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[2] In order to appreciate fully the reasons why Dobbas's defense counsel did not vigorously contest liability, one must understand the purpose of the arbitration. The arbitration was *not* to obtain a judgment against Dobbas so that damages could be collected from him or his primary insurer. Indeed, Dobbas had already received the Covenant Never to Execute, and CalFarm had already paid or agreed to pay its $1 million policy limits on the only policy that Dobbas believed existed. (SUF ¶¶ 19-22). Rather, the true purpose of the arbitration was to create a damage claim against Dobbas's insurance broker for the cancellation of the $3 million Umbrella Policy, which the Mancinis and the Turners could take under an assignment for the wrongful and negligent acts of the broker. (*Id.* ¶¶ 16-17). Dobbas had already sued his broker in the Vitas Action alleging negligent cancellation of the CalFarm Umbrella Policy. (*Id.* ¶ 58). In his May 29, 2003 status letter to Dobbas's primary insurer, Dobbas's defense attorney Kelly Watson stated, "there was an umbrella policy of three million dollars to protect Mr. Dobbas. . . . When canceling this coverage, Vitas Insurance unknowingly cancelled the umbrella. . . . During the course of the mediation it was agreed that plaintiffs' counsel would attempt to collect on the claim against Vitas Insurance for the three million dollars in coverage. . . . It is anticipated that plaintiffs' counsel will use this nine months to perfect a right as against Vitas Insurance for the additional three million dollars in coverage through the E&O carrier for Vitas Insurance." (*Id.* ¶ 17). Similarly, on January 14, 2004, Dobbas's defense attorney reported to his primary insurer, "As you will recall, the parties agreed at the mediation held last May that the intent is for Mr. Dobbas to assign to the plaintiffs his claim against his insurance broker, Fred Vitas, and Vitas Insurance Agency, regarding the unintended cancellation of Mr. Dobbas' umbrella coverage." (*Id.* ¶ 17). Finally, Dobbas's defense attorney wrote to the Mancinis and the Turners counsel on January 19, 2004, approximately one month before the arbitration: "From our perspective, we want to make sure that the written terms of the binding arbitration agreement make clear that *we do not intend the arbitration to be binding on the issue of Mr. Dobbas' liability and we do not intend to present or argue that issue at the arbitration.* (emphasis added). (*Id.* ¶ 17).

The excess insurers appealed, arguing confirmation of the bankruptcy plan did not trigger their indemnity obligations because there was no actual trial on Fuller-Austin's liability or a settlement to which they consented. *Id.* The *Fuller-Austin* court agreed:

> The confirmation hearing was not a contested evidentiary hearing. Indeed, the bankruptcy court expressly limited the scope of the hearing to Fuller-Austin's one-hour presentation of evidence in support of disclosure and the proposed Plan, without any cross-examination. Moreover, the "evidence" offered during the hearing did not address Fuller-Austin's liability; rather, the testimony focused on the Plan's fairness to the claimants. Further, the Plan was the result of negotiation–not fact-finding.... Additionally, the key purpose of the bankruptcy court's findings were to ascertain the Plan's good faith and reasonableness as to the asbestos claimants. The bankruptcy court intentionally did not address the Plan's fairness to [the excess insurers], as it found that they were "not 'directly and pecuniarily affected'" by the Plan.

Id. at 980 (internal citation omitted).

The *Fuller-Austin* court further reasoned that because the excess insurers "did not participate in prehearing negotiations and were precluded from participating in the confirmation hearing," the bankruptcy court confirmation proceedings "were not an 'actual trial' within the meaning of the insurance policies." *Id.* at 981. The *Fuller-Austin* court thus reversed imposition of liability as to the excess insurers and remanded the case for retrial. *Id.*

The rationale of *Fuller-Austin* applies here. Because Steadfast and American Guarantee never received an opportunity to participate in the arbitration hearing, the arbitration hearing was not a genuinely contested evidentiary hearing, and the arbitration hearing does not qualify as an "actual trial." Indeed, the arbitration was conveniently arranged to create the appearance of a judgment so the Mancinis and Turners could then pursue an action against Vitas, pursuant to an assignment of Dobbas's rights for the broker's wrongful cancellation of Dobbas's $3 million Umbrella Policy. (SUF ¶ 17). Dobbas had already been given a Covenant Never to Execute and CalFarm had paid or agreed to pay its $1 million primary policy limits. Dobbas was not at risk and there was no reason for the arbitration, other than to create a predicate judgment for the so-called "claim" against Vitas and VIA that the Mancinis and the Turners could assert under the assignment of Dobbas's rights. Accordingly, there was no "actual trial," and the arbitration award does not constitute a "judgment" to permit recovery under California Insurance Code §

11580. Therefore, summary judgment must be entered in Steadfast and American Guarantee's favor on their Fifth Claim for Relief (For Declaratory Relief That the Insureds Failed to Comply With The Terms and Conditions of the Policies) and against the Mancinis and the Turners on their counterclaims.

2. The underlying process created the potential for abuse, fraud, or collusion.

The arbitration award presents the same potential for abuse, fraud, and collusion as those judgments California courts have deemed unenforceable under California Insurance Code § 11580.[3] California courts are reluctant to bind insurers by stipulated judgments accompanied by covenants not to execute and to which the insurers did not participate or consent. For example, in *Wright v. Fireman's Fund Insurance Cos.*, 11 Cal. App. 4th 998, 1019 (1992), the court observed the potential for "abuse and collusion" where the insured and a third party tort claimant enter into a stipulated judgment not based upon a contested trial proceeding. The insurer in *Wright* had provided its insured with independent counsel under a reservation of rights. *Id.* at 1003-04. While the insurer was providing a defense, the insured's personal counsel negotiated a settlement without the insurer's participation or consent. *Id.* at 1019. In the stipulated judgment, the injured party received $1 million and an assignment of the insured's causes of action in exchange for a covenant not to execute. *Id.* at 1003, 1024.

The insurer in *Wright* argued it could not be bound by the stipulated judgment in which it did not participate and to which it did not consent. *Id.* at 1013. Because the judgment was based on the injured party's covenant not to execute against the insured, that arrangement eliminated any interest the insured otherwise might have had in actually defending in good faith. *Id.* The insurer further asserted the entire purpose of the settlement "arrangement" was to convert the injured party's personal injury suit into a direct action against the insurer "for money damages of $1 million without the benefit of an iota of evidence." *Id.*

The *Wright* court acknowledged other courts have held "[a] judgment on the merits . . . is not always required and insurers have been bound by default and stipulated judgments under

[3] In light of the collusive nature of the arbitration, Steadfast and American Guarantee also move for summary judgment on their Sixth Claim for Relief (For Equitable Relief From Judgment on the Basis of Collusion).

certain circumstances." *Id.* at 1016-17 (citations omitted). The *Wright* court distinguished its case, where the insurer did not breach its duty to its insured, from these cases: "All of the cases in which a judgment not on the merits has been found binding on the insurer were based upon the principle an insurer who has an opportunity to defend and wrongfully fails to do so is liable on the judgment against the insured." *Wright*, 11 Cal. App. 4th at 1019. The *Wright* court emphasized the potential for abuse and collusion under the circumstances: "We are frankly disturbed by the potential for abuse apparent in a situation where an insurer, in the absence of a breach of its duty to its insured, could be bound by a consent judgment of this nature." *Id.* The court added, "*With no personal exposure* the insured has no incentive to contest liability or damages. To the contrary, the insured's best interests are served by agreeing to damages in any amount as long as the agreement requires the insured will not be personally responsible for those damages." *Id.* at 1023 (emphasis added). The *Wright* court concluded, "where an insurer provide[s] a defense to its insured in the underlying litigation, and the insured, without the participation or consent of the insurer, stipulate[s] to a judgment without evidentiary support and with no potential for personal loss, such judgment is insufficient to impose liability on the insurer in a later action against the insurer." *Id.* at 1024 (footnote omitted). In other words, the *Wright* court held a stipulated judgment against an insured with a covenant not to execute, *and no personal exposure*, which was entered without the insurer's consent or participation, was insufficient to bind the insurer under section 11580. *Id.*

Likewise, in *Safeco Insurance Co. v. Superior Court*, 71 Cal. App. 4th 782, 785-86 (1999), without the consent of the insurer, the insureds agreed to a stipulated judgment in the amount of $645,000, with $145,000 to be paid by a settling insurer and the remainder by the insureds. *Id.* at 786. The plaintiffs, however, agreed not to execute on the $500,000 remainder against the insureds, in exchange for the insureds' assignment of their rights against the nonsettling insurer. *Id.* Thereafter, the plaintiffs filed a direct action against the nonsettling insurer seeking to recover the liability limits of the policy pursuant to the stipulated judgment. *Id.*

The *Safeco Insurance* court held that since the insureds settled the matter without the nonsettling insurer's consent, the stipulated judgment between the insureds and the wrongful

death plaintiffs was unenforceable against the nonsettling insurer for purposes of recovery under California Insurance Code § 11580. *Id.* at 786-87. In so holding, the court noted the potential for abuse "where an insurer, in the absence of a breach of its duty to its insured, could be bound by a consent judgment of this nature." *Id.* at 787 (quoting *Wright*, 11 Cal. App. 4th at 1019). The court further noted, "[e]ven a stipulated judgment negotiated with the help of the insured's independent *Cumis* counsel is not binding on the insurer without its consent." *Id.* (citation and footnote omitted).

In this case, the underlying judgment analogously presents the same potential for (if not actual) fraud and collusion as those stipulated judgments deemed unenforceable in *Wright* and *Safeco Insurance*.[4] The arbitration award was tantamount to a stipulated judgment because the Mancinis and the Turners' evidence was virtually uncontested. Because Dobbas received the Covenant Never to Execute, and the Mancinis and the Turners had accepted CalFarm's settlement offer of the $1 million limits of the Farm Liability Policy, Dobbas and CalFarm had neither *any risk* nor *any incentive* to actually attempt to minimize the damages.

These circumstances raise the fundamental question: "What, then, was the purpose, except to allocate damages between the plaintiffs and to set up their later claim against Dobbas' insurance broker Vitas and VIA?"

At the time of the arbitration, Dobbas and the plaintiffs were not aware of the Steadfast or American Guarantee Policies. (SUF ¶ 51). They were aware, however, that the plaintiffs could never collect any additional damages from Dobbas, nor from his primary insurer, beyond the $1 million primary policy limit CalFarm had already committed. Accordingly, Dobbas's defense counsel, perhaps earnestly believing it was in Dobbas's interest to go along with the scheme in order to protect him from liability in excess of the CalFarm primary limit, proceeded with the arbitration in order to give the appearance of a legitimate proceeding that could justify and support the Mancinis and the Turners' later claim against Vitas and VIA.

[4] California law requires only showing the *potential* for abuse, fraud, or collusion; there is no requirement that *actual* fraud, abuse, or collusion be shown. *See Nat'l Union*, 27 Cal. App. 4th at 1449 (holding one attribute of an "actual trial" is "a process that does not create the *potential* for abuse, fraud or collusion" (emphasis added)).

Merely because an arbitration occurred, however, makes it no less a sham.[5] As Dobbas's own defense counsel *admitted* in the October 27, 2003 letter to Dobbas's primary carrier, "Our efforts have been *geared* toward perfecting the claim as against Vitas Insurance and assigning that claim to the plaintiffs. This, together with the insurance money, is hoped to fully and finally resolve all issues in this case." (SUF ¶ 17) (emphasis added). Not surprisingly under the circumstances, no mention was made of actually defending Dobbas.

Accordingly, the arbitration was conducted virtually without any semblance of an independent adjudication. Under all of these circumstances, the arbitration award certainly should not now be enforceable against Steadfast and American Guarantee under California Insurance Code § 11580. *See Pruyn v. Agric. Ins. Co.*, 36 Cal. App. 4th 500, 516-17 (1995) (holding a stipulated judgment may be enforced against an insurer under section 11580 only where the court entered judgment with "significant independent adjudicatory action").

It is a critical fact that the arbitration award was coupled with a covenant not to execute personally against Dobbas. The potential for fraud and collusion is blatant. *See Nat'l Union*, 27 Cal. App. 4th at 1449 (holding the concern for abuse, fraud, or collusion "is heightened when the injured party provides the insured with a covenant not to execute"). Here, because the judgment could never be collected from Dobbas, the underlying judgment is nothing more than a sham. The sham effect of the proceeding is not revealed as much by what happened, but by what *should* have happened, but didn't. *See Pruyn*, 36 Cal. App. 4th at 518 (holding a stipulated judgment coupled with a covenant not to execute "brings with it a high potential for fraud or collusion. With no personal exposure the insured has no incentive to contest liability or damages. To the contrary, the insureds' best interests are served by agreeing to damages in any amount as long as the agreement requires the insured will not be personally responsible for those damages." (internal quotation omitted)). Likewise, as a one-sided sham, the underlying judgment in this case cannot be enforced against Steadfast and American Guarantee under section 11580.

[5] The fact that Dobbas appeared at the arbitration does not mean it was a truly contested proceeding. In fact, Dobbas was dissatisfied with his defense counsel and evidently unaware of the effect of the Covenant Never to Execute that was negotiated by others hired by CalFarm, his insurer, to "protect" Dobbas. (SUF ¶¶ 24, 30).

Furthermore, the underlying judgment should not be enforceable under section 11580 because Steadfast and American Guarantee did not breach any duty to Dobbas. California courts recognize "[a] judgment on the merits . . . is not always required and insurers have been bound by default and stipulated judgments under certain circumstances." *Wright*, 11 Cal. App. 4th at 1016-17 (citing *Zander*, 259 Cal. App. 2d at 799, 804-806; *Clemmer*, 22 Cal. 3d at 884-86; *Samson*, 30 Cal. 3d at 228, 236-42). However, "[a]ll of the cases in which a judgment not on the merits has been found binding on the insurer were based upon the principle an insurer who has an opportunity to defend and wrongfully fails to do so is liable on the judgment against the insured." *Wright*, 11 Cal. App. 4th at 1019. The present case is not one where the insurers, Steadfast and American Guarantee, had notice and refused to defend, or had the opportunity to set aside the post-verdict judgment but declined. Instead, an unappealable arbitration award was entered and the award was reduced to judgment, without any notice to the insurers. Steadfast and American Guarantee did not breach any duty to Dobbas, and the underlying judgment should not be enforced against Steadfast and American Guarantee under section 11580.

Because the undisputed evidence and reasonable inferences establish the unabashedly flawed procedure through which the Mancinis and the Turners obtained their judgment not only had the potential for abuse, fraud, or collusion, but in fact, *was* the product of a collusive scheme to set up the predicate judgment for a subsequent claim *against Vitas and VIA*, the judgment cannot be collected from Steadfast and American Guarantee.[6] Accordingly, summary judgment should be entered in favor of Steadfast and American Guarantee on their Fifth Claim for Relief (For Declaratory Relief That the Insureds Failed to Comply With The Terms and Conditions of the Policies), on their Sixth Claim for Relief (For Equitable Relief From Judgment on the Basis of Collusion), and against the Mancinis and the Turners on their counterclaims.

[6] The fact that the collusive scheme was not originally directed against Steadfast and American Guarantee does not mean it, nevertheless, was not collusive. In fact, the true purpose of the arbitration again was revealed by the May 7, 2004 Letter regarding the "discovery" of the Steadfast and American Guarantee policies in which Dobbas's counsel said, "[T]his may allow you to be fully compensated on the judgment rather than having to litigate the Vitas case to conclusion." (SUF ¶ 51).

B. Steadfast and American Guarantee were actually prejudiced by late notice.

Because Steadfast and American Guarantee were actually prejudiced by the insured's failure to give timely notice, summary judgment should be entered in favor of Steadfast and American Guarantee on their Fourth Claim for Relief (For Declaratory Relief That the Insureds Did Not Comply With the Notice Requirements of the Policies).

"The 'general rule' is that an insurer is not bound by a judgment unless it had notice of the pendency of the action." *Samson*, 30 Cal. 3d at 238. Notice provisions in insurance policies are designed to help the insurer investigate, defend, and settle third-party claims. *Am. Int'l Specialty Lines Ins. Co. v. Cont'l Cas. Ins. Co.*, 142 Cal. App. 4th 1342, 1366 (2006). "If an insured breaches a notice provision, resulting in substantial prejudice to the defense, the insurer is relieved of liability." *Id.* Thus, late notice of a claim will excuse the insurer's obligations if the insurer has been prejudiced by the late notice. *See Nw. Title Sec. Co. v. Flack*, 6 Cal. App. 3d 134, 141 (1970).

"In order to demonstrate actual, substantial prejudice from lack of timely notice, an insurer must show it lost something that would have changed the handling of the underlying claim." *Shell Oil Co. v. Winterthur Swiss Ins. Co.*, 12 Cal. App. 4th 715, 763 (1993). "To establish actual prejudice, the insurer must show a substantial likelihood that, with timely notice, and notwithstanding a denial of coverage or reservation of rights, it would have settled the claim for less or taken steps that would have reduced or eliminated the insured's liability." *Id.* Thus, in order to show prejudice under the notice-prejudice rule, Steadfast and American Guarantee need only show a "substantial likelihood" they could have settled or reduced the judgment. *Am. Int'l Surplus Lines Ins. Co. v. City of San Diego*, 2005 WL 658930 at *2 (9th Cir. 2005); *Sequoia Ins. Co. v. Royal Ins. Co. of Am.*, 971 F.2d 1385, 1394 (9th Cir. 1992).

Under the notice-prejudice rule, "prejudice is not shown simply by displaying end results; the probability that such results could or would have been avoided absent the claimed default or error must also be explored." *Clemmer*, 22 Cal. 3d at 865, n.12. Indeed, Steadfast and American Guarantee recognize the Court's ruling on their first motion for summary judgment was based on the conclusion that they failed to offer evidence of actual prejudice. Steadfast and American

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Guarantee request the Court take a fresh look at the evidence submitted in connection with this Motion.

Although the issue of prejudice is ordinarily may be one of fact, it may be established as a matter of law by the facts proved. *Nw. Title Sec.*, 6 Cal. App. 3d at 141. Because the facts in this case are undisputed, resolution of the prejudice issue is appropriate for summary judgment. *See Earle v. State Farm Fire & Cas. Co.*, 935 F. Supp. 1076, 1082 (N.D. Cal. 1996) (finding actual prejudice existed as a matter of law based on undisputed facts contained in declaration).

Here, Steadfast and American Guarantee have presented evidence proving they suffered actual prejudice because there is a "substantial likelihood" that if Steadfast and American Guarantee had received timely notice, they would have: (1) refused to agree to binding arbitration, which would have resulted in a more favorable outcome; (2) convinced the arbitrator to reach a different decision; (3) reduced the amount of the award; or (4) settled for a lesser amount. Therefore, the Court should grant summary judgment in favor of Steadfast and American Guarantee on their Fourth Claim for Relief (For Declaratory Relief That the Insureds Did Not Comply With the Notice Requirements of the Policies).

1. Steadfast and American Guarantee would have obtained a more favorable outcome if they had an opportunity to try the Claim to a jury.

The undisputed evidence demonstrates that had Steadfast and American Guarantee received timely notice of the Claim, they would not have agreed to binding arbitration. (SUF ¶ 69). According to attorney Donald Walter, if the case had been properly presented to a jury, it would have been a "defensible case," and the Mancinis and Turners would not have won. (*Id.* ¶ 70). The one-sided presentation at the arbitration is no indicator of what would have occurred had the case been fairly and truly contested.

Mr. Walter's testimony provides evidence of a substantial likelihood that Steadfast and American Guarantee would have obtained a more favorable outcome if the case had been actually tried. Accordingly, Steadfast and American Guarantee have demonstrated actual prejudice due to late notice. *See Earle*, 935 F. Supp. at 1082 (finding prejudice as a matter of law where insurer "present[ed] evidence that the [insured's] exposure, as well as its own, could have been

substantially reduced with an earlier tender because" the jury may have found in favor of the insurer based on policy exclusions). Thus, summary judgment should be granted to Steadfast and American Guarantee on their Fourth Claim for Relief (For Declaratory Relief That the Insureds Did Not Comply With the Notice Requirements of the Policies).

2. The arbitrator would have reached a different decision.

As the Court explained in its earlier Memorandum and Order, in order to succeed on summary judgment, Steadfast and American Guarantee must present evidence establishing that if they had presented expert testimony at the arbitration rebutting the opinions of Dr. Pontrelli, there is a "substantial likelihood" the arbitrator would have reached a different decision. Steadfast and American Guarantee have satisfied this burden.

Had Steadfast and American Guarantee received timely notice, the following chart demonstrates how Dobbas would have presented expert testimony that would have rebutted Dr. Pontrelli's shallow opinions. (SUF ¶ 71).

Issue	Dr. Pontrelli's Opinions	Steadfast and American Guarantee's Expert Witnesses
Bulls were undernourished	Dr. Pontrelli: the bulls were hungry and stressed. (SUF ¶ 72).	Professor Hall: the pasture was not severely overgrazed nor were the bulls undernourished. (SUF ¶ 73). Professor Hall: Dr. Pontrelli "never evaluated the body condition score of the animals . . . and without that, he really did not get a true indication of really the feed conditions or the general well-being of the animals." (*Id.* ¶ 74).
Hungry bulls are more likely to fight	Dr. Pontrelli: because the bulls were hungry and stressed, they became crowded and angry, and the bigger bulls would push and kick the smaller bulls. (SUF ¶ 72).	Professor Hall: "[a]nimals that are starving to death will not fight." (SUF ¶ 75). Professor Hall: the bulls became frisky at dusk, and another bull pushed the bull through the fence while they were playing. (SUF ¶ 76).
Pasture was overgrazed	Dr. Pontrelli: that Lot 8 was dry, eaten down, and severely overgrazed, and that the grass was virtually gone. (SUF ¶ 72).	Professor Hall: the pasture was not overgrazed. (SUF ¶ 73).
Dobbas was	Dr. Pontrelli: Dobbas failed	Professor Hall: "Mr. Dobbas adhered to the

negligent	to provide reasonable care and neglected the bulls (SUF ¶ 72).	standard of care," and "this was an accident." (SUF ¶ 77). Mr. Walter: Dobbas was not negligent. (*Id.* ¶ 78).

Moreover, according to Mr. Walter, if Steadfast and American Guarantee had presented expert witnesses, such as Mr. York or Professor Hall, the Mancinis and the Turners would not have won. (SUF ¶ 79). Accordingly, Steadfast and American Guarantee have demonstrated actual prejudice. *See Earle*, 935 F. Supp. at 1082 (finding actual prejudice as a matter of law where insurer "present[ed] evidence that the [insured's] exposure, as well as its own, could have been substantially reduced with an earlier tender"). As a result, summary judgment should be granted on Steadfast and American Guarantee's Fourth Claim for Relief (For Declaratory Relief That the Insureds Did Not Comply With the Notice Requirements of the Policies).

3. The arbitration award would have been lower.

Had Steadfast and American Guarantee been given timely notice of the Claim, they would have requested Dobbas seek allocation of fault and/or a cross-claim against the property owner, Holstrom. (SUF ¶ 80). Any allocation of fault to Holstrom for negligent maintenance of the fence and pasture areas necessarily would have reduced Dobbas's liability. *See* CAL. CIV. CODE § 1431.2(a) ("In any action for personal injury, property damage, or wrongful death, based on principles of comparative fault, the liability of each defendant for non-economic damages shall be several only and shall not be joint.").

According to Professor Hall, because Holstrom owned the property where the bull was pastured, "if overgrazing was the cause of the bull escaping the fenced-in pasture, according to plaintiff's witness, Dr. Pontrelli, then some of the liability should be transferred to Holstrom for not being an active steward of his land." (SUF ¶ 81).

Mr. Walter also opined that fault should have been allocated to Holstrom: "To the extent Dobbas had any potential exposure, it was shared on at least an equal basis with Mr. Holstrom, the owner of the property from which the bull escaped." (SUF ¶ 82). Mr. Walter explained that because Holstrom knew Dobbas intended to have cattle on the property, and because the fencing was inadequate, Holstrom should have done something about the fencing. (*Id.*).

This expert testimony establishes a substantial likelihood that if Steadfast and American Guarantee received timely notice, they never would have agreed to the dismissal of Hostrom and they would have sought allocation of fault to Holstrom. Dobbas's share of the fault, then, necessarily would have been lesser. But *any allocation of fault at all* to Holstrom would have reduced the damages allocable to Dobbas. Accordingly, Steadfast and American Guarantee have proven a substantial likelihood they would have taken steps that would have reduced Dobbas's liability and summary judgment must be entered in their favor on their Fourth Claim for Relief (For Declaratory Relief That the Insureds Did Not Comply With the Notice Requirements of the Policies).

4. Steadfast and American Guarantee would have settled for less.

Had Steadfast and American Guarantee received timely notice of the Claim, they would have sought a negotiated settlement for much less than $5 million. (SUF ¶¶ 83-84). An insurer is substantially prejudiced by late notice where the insurer can show the untimely delay deprived it of at least the "*opportunity* to settle." *Select Ins. Co. v. Superior Court*, 226 Cal. App. 3d 631, 638 (1990).

The lack of notice deprived Steadfast and American Guarantee of the opportunity to settle the Claim for less than the amount of the judgment. Therefore, summary judgment must be entered in favor of Steadfast and American Guarantee on their Fourth Claim for Relief (For Declaratory Relief That the Insureds Did Not Comply With the Notice Requirements of the Policies).

For the foregoing reasons, Steadfast and American Guarantee respectfully request the Court enter summary judgment, or in the alternative, summary adjudication, in their favor.

Dated: November 15, 2007

KUTAK ROCK LLP

By: /s/ Paul F. Donsbach
Attorneys for
Plaintiffs/Counter-Defendants
STEADFAST INSURANCE COMPANY
and AMERICAN GUARANTEE AND
LIABILITY INSURANCE COMPANY

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PROOF OF SERVICE

I, Kathy Powell, declare:

I am a citizen of the United States and employed in Orange County, California. I am over the age of eighteen years and not a party to the within-entitled action. My business address is Suite 1100, 18201 Von Karman Avenue, Irvine, California 92612-1077. On November 15, 2007, I served a copy of the within document(s):

PLAINTIFFS/COUNTER-DEFENDANTS STEADFAST INSURANCE COMPANY AND AMERICAN GUARANTEE AND LIABILITY INSURANCE COMPANY'S MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF SECOND MOTION FOR SUMMARY JUDGMENT OR, IN THE ALTERNATIVE, SUMMARY ADJUDICATION

☐ by transmitting via facsimile the document(s) listed above to the fax number(s) set forth below on this date before 5:00 p.m.

☐ by placing the document(s) listed above in a sealed envelope with postage thereon fully prepaid, in the United States mail at Irvine, California addressed as set forth below.

☒ by Notice of Electronic Filing. Counsel who have consented to electronic service have been automatically served by the Notice of Electronic Filing, which is automatically generated by CM/ECF at the time said document was filed, and which constitutes service pursuant to FRCP 5(b)(2)(D).

☐ by placing the document(s) listed above in a sealed Federal Express envelope and affixing a pre-paid air bill, and causing the envelope to be delivered to a Federal Express agent for delivery.

☐ by personally delivering the document(s) listed above to the person(s) at the address(es) set forth below.

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I am readily familiar with the firm's practice of collecting and processing correspondence for mailing. Under that practice it would be deposited with the U.S. Postal Service on that same day with postage thereon fully prepaid in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if postal cancellation date or postage meter date is more than one day after date of deposit for mailing in affidavit.

I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Executed on November 15, 2007, at Irvine, California.

/s/ Kathy Powell (with permission)

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