

Gray v. Am. Safety Indem. Co.

Court of Appeal of California, Second Appellate District, Division Four

December 3, 2018, Opinion Filed

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Reporter

2018 Cal. App. Unpub. LEXIS 8160 *

DEBRA GRAY et al., Plaintiffs and Appellants, v. AMERICAN SAFETY INDEMNITY COMPANY, Defendant and Respondent.

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Prior History: [*1] APPEAL from a Judgment of the Superior Court of Los Angeles County, No. BC653477, William F. Highberger, Judge.

Disposition: Affirmed.

Counsel: Kabateck Brown Kellner, Richard L. Kellner and Brian S. Kabateck for Plaintiffs and Appellants.

Chamberlin & Keaster, Robert W. Keaster and David M. Berke for Defendant and Respondent.

Judges: MICON, J.; MANELLA, P. J., COLLINS, J. concurred.

Opinion by: MICON, J.

Opinion

Plaintiffs Debra Gray and numerous other former tenants of an apartment building successfully sued the owner for multiple serious habitability violations. They did so as part of a settlement with the owner, which included an assignment of the building owner's claim for bad faith and breach of contract against the owner's insurer—American Safety Indemnity Co. (ASIC)—after ASIC refused to defend and cover those claims. The trial court sustained without leave to amend ASIC's demurrer to the complaint on the ground that the building owner's assignment of claims to plaintiffs included a release so broad that it encompassed the plaintiffs' bad faith claims. We affirm the judgment for ASIC on an alternative ground—the building owner's failure to comply with a condition precedent to coverage under the ASIC policy.

*Judge of the Los Angeles Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

FACTUAL BACKGROUND AND [*2] PROCEDURAL HISTORY

Debra Gray and the other plaintiffs were tenants at an apartment building (Royal Park Motel & Residence) located at 1906 West Third Street in Los Angeles. During the period July 1, 2012 to December 26, 2013, New Hampshire Apartment, Inc. (New Hampshire) owned, maintained, and leased the property.

On February 14, 2013, plaintiffs asserted claims for habitability against New Hampshire, including breach of the warranty of habitability, breach of the covenant of quiet enjoyment, negligence, and related claims based on the conditions of the property. Plaintiffs alleged that the premises were infested by vermin and cockroaches, lacked security, had broken windows and doors that were off their hinges, lacked adequate water supply, heat, proper sewage disposal, and the smoke detectors were either missing or inoperable, and was generally unsanitary and in poor repair. (Habitability Action.)

New Hampshire was insured by ASIC. ASIC refused to defend New Hampshire.

A settlement agreement (Agreement) entered into between plaintiffs and New Hampshire on April 30, 2014, provided for the release of New Hampshire from plaintiffs' claims and assignment of New Hampshire's claims against [*3] its insurer to plaintiffs, based upon certain terms and conditions.¹ The Agreement provided:

"1. Release and Discharge

In consideration of the terms set forth in Section 2, Plaintiffs hereby completely release and forever discharge Defendant from any and all past, present or future claims, demands, obligations, actions, causes of action, wrongful death claims, rights, damages, costs, losses of service. . . .

"2. Terms

"In consideration for the release set forth above, Defendant agrees to the following terms:

"a) The Parties to the Agreement will enter into a stipulation to submit to a trial by reference pursuant to California Code of Civil Procedure 638 and according to the provisions of California Rule of Court 3.902 and all related subparts. The general reference trial will be presided over [by] a retired judge to be mutually agreed upon and the issues to be decided will be all issues remaining in the litigation between Plaintiffs and Defendants. . . .

"d) The Parties hereby understand and agree that they are waiving their right to trial by jury and submit to the decision, judgment and ruling of the mutually selected private judge.

"e) In consideration for a covenant not to execute or collect any judgment or award granted to Plaintiffs ("Assignee") in this matter [*4] against Defendant ("Assignor"), Assignor hereby transfers and assigns to Assignee all of Assignor's rights, titles, and interests in and to any cause of action against Assignor's insurer, including, but not limited to persons and/or entities who are responsible for breach of contract,

¹Under *Pruyn v. Agricultural Ins. Co.* (1995) 36 Cal.App.4th 500, 515. where the insurer refuses to defend a third party claim, the insured assigns its claim against the insurer to the third party pursuant to a covenant not to execute on any judgment the third party obtains against the insured.

failure to defend and indemnify, failure to fulfill its obligation for the allegations set forth in the Complaint. . . ."

The parties agreed to a trial by reference before a retired judge, who was appointed by the trial court in April 2015. On August 30, 2016, the judge ruled in favor of plaintiffs and issued a judgment for \$1.3 million. A corrected judgment was entered September 12, 2017. The judgment specified numerous deficiencies in the property, including "lack of smoke detectors, or smoke detectors that were inoperable."

On March 17, 2017, plaintiffs filed their complaint in this action against ASIC, and the operative second amended complaint filed October 6, 2017 alleged claims for breach of contract, breach of the implied covenant of good faith and fair dealing, and declaratory relief. Plaintiffs asserted that ASIC had refused to defend New Hampshire in the Habitability Action, and refused to provide [*5] coverage.

ASIC demurred to the second amended complaint on four grounds, asserting that (1) New Hampshire had failed to satisfy a condition precedent to coverage, namely it did not have working smoke detectors at the premises; (2) New Hampshire's conduct in maintaining the premises in such condition did not constitute an "occurrence" within the meaning of the policy; (3) plaintiffs failed to join New Hampshire, an indispensable party; and (4) plaintiffs' complete release of New Hampshire rendered its assignment of its claims a nullity.

On the first argument, ASIC argued that plaintiffs failed to satisfy a condition precedent, precluding coverage. ASIC relied on the insurance policy's language regarding the "Protective Safeguard Promissory Warranty." The language of this warranty provided that "the insured shall maintain in complete working order all equipment and services pertaining to the operation of the described protective safeguard. . . . [¶] Smoke Detectors in all units/living spaces. [¶] Breach of any warranty(s) shall render coverage provided by this policy null and void." ASIC argued that the pleadings (including the first amended complaint in the habitability action and judicially [*6] noticed matters) disclosed that the property had no working smoke detectors. ASIC argued the complaint and first amended complaint in the habitability action alleged a "lack of smoke detectors, or smoke detectors that are inoperable." ASIC requested judicial notice of tenants' complaints regarding the property and citations from the Los Angeles Department of Housing, which stated that the property lacked operating smoke detectors.

Plaintiffs objected to the judicially noticed materials as hearsay. Plaintiffs asserted factual questions existed regarding whether the smoke detectors had been repaired and how many were not working, and claimed the question of whether New Hampshire was in "substantial compliance" with the requirement precluded demurrer. Further, plaintiffs asserted compliance with the smoke detector requirement should be equitably excused because the missing or unrepaired smoke detectors constituted a technical forfeiture. Finally, plaintiffs asserted that defendant waived the condition because it issued a second policy in June 2013 to New Hampshire, after receiving the complaint in the habitability action alleging that the smoke detectors were missing or not operational. [*7]

Defendant replied that substantial compliance was not a defense to a condition precedent; compliance could not be equitably excused; and defendant did not waive the warranty condition because its denial of coverage was inconsistent with waiver.

At the hearing, although the court stated it recognized the intent of the parties was clear that plaintiffs did not intend to release New Hampshire without being in a position to collect on New Hampshire's claim, the trial court stated it would sustain the demurrer on the fourth argument on the basis that the broad language

of the release precluded plaintiffs from pursuing the action. Based upon the release, the court ruled that the assignment to plaintiffs was rendered ineffective by plaintiffs' release of all claims against New Hampshire more than three years before judgment of the habitability complaint was entered.

DISCUSSION

Plaintiffs assert that their position in the two actions regarding the condition precedent (the smoke detectors) is not inconsistent, and in any event, factual issues regarding substantial compliance, waiver, and equitable excuse preclude demurrer. We disagree.

I. STANDARD OF REVIEW.

We independently review the ruling on [*8] a demurrer and determine de novo whether the complaint alleges facts sufficient to state a cause of action. (*McCall v. PacifiCare of Cal., Inc.* (2001) 25 Cal.4th 412, 415.) We assume the truth of the properly pleaded factual allegations, facts that reasonably can be inferred from those expressly pleaded, and matters of which judicial notice has been taken. (*Schifando v. City of Los Angeles* (2003) 31 Cal.4th 1074, 1081.) We construe the pleading in a reasonable manner and read the allegations in context. (*Ibid.*) We review the trial court's ruling for legal error, not its reasoning. If the judgment is correct on any ground stated in the demurrer, we affirm. (*Fonteno v. Wells Fargo Bank* (2014) 228 Cal.App.4th 1358, 1365.)

II. NEW HAMPSHIRE'S FAILURE TO SATISFY THE CONDITION PRECEDENT PRECLUDES COVERAGE UNDER THE POLICY.

A. The Protective Safeguard Promissory Warranty is a Condition Precedent to Coverage Under the Policy.

A condition precedent refers to an act, condition, or event that must occur before the insurance contract becomes effective or binding on the parties. (*North American Capacity Ins. Co. v. Claremont Liability Ins. Co.* (2009) 177 Cal.App.4th 272, 289.) Conditions precedent in insurance policies neither confer nor exclude coverage for a particular risk, but impose certain duties on the insured in order to obtain the coverage provided by the policy. (*Id.* at p. 291.) The existence of a condition precedent depends on the intent of the parties as set forth in the [*9] insurance contract. (*Realmuto v. Gagnard* (2003) 110 Cal.App.4th 193, 199.)

Here, New Hampshire's policy specified that "[i]n consideration of the premium charged, it is understood and agreed by the insured that it is a condition precedent to the acceptance of this insurance and payment of any claim under the policy that the insured warrants that at all times during the currency of the policy, (1) the premises described herein is protected by the protect safeguard described in the SCHEDULE, and (2) the insured shall maintain in complete working order all equipment and services pertaining to the operation of the described protective safeguard. . . . [¶] Smoke Detectors in all units/living spaces. **BREACH OF ANY WARRANTY(S) SHALL RENDER COVERAGE PROVIDED BY THIS POLICY NULL AND VOID.**" New Hampshire failed to satisfy this condition, and as a result ASIC's

obligation to provide coverage under the policy never accrued. (See *American Way Cellular, Inc. v. Travelers Property Casualty* (2013) 216 Cal.App.4th 1040, 1055 [insured failed to maintain sprinkler system as required by the terms of the endorsement].)

B. Plaintiffs Are Estopped From Asserting the Smoke Detector Condition Was Met.

ASIC argues that plaintiffs are estopped from taking inconsistent positions in the habitability action (the smoke detectors were broken) and this action [*10] (New Hampshire was in substantial compliance because it undertook to fix some of them). Plaintiffs argue that estoppel does not apply because there are fact questions concerning the duration and scope of noncompliance and thus their positions in the two proceedings are not inconsistent.

The doctrine of judicial estoppel is designed to protect the integrity of the judicial process. The doctrine prevents a party from asserting a position in a legal proceeding that is contrary to a position previously taken in the same or some earlier proceeding. (*Jackson v. County of Los Angeles* (1997) 60 Cal.App.4th 171, 181-182.) Judicial estoppel is appropriate where a party has taken inconsistent positions in separate proceedings. (*Ibid.*)

Here, we need only look to the judgment in the habitability action to conclude plaintiffs are estopped from asserting the smoke detectors were in substantial compliance with the warranty condition.² The judgment in the habitability action made a finding that "[p]laintiffs allege that during the time they resided at the Property, they became aware of defective and dangerous conditions at the Property, including: . . . [¶] Lack of smoke detectors, or smoke detectors that are inoperable." The judgment further found, "[p]laintiffs allege [*11] that because of the defects such as those listed above [including missing or inoperable smoke detectors], the premises of the Property were rendered uninhabitable and unfit for human occupation." Finally, the trial court found that the plaintiffs were entitled to recover on their causes of action because they experienced the "problems, defects and issues . . . as set forth in the [court's] Factual Summary." As noted, this factual summary included the allegations concerning the lack of smoke detectors. Plaintiffs cannot now change their position in this proceeding and assert that the smoke detectors were installed and functioning, or at the very least that their condition was in substantial compliance with the condition precedent of the policy.

Similarly, under principles of collateral estoppel, plaintiffs cannot now assert that the condition precedent was satisfied. Issue preclusion prohibits the relitigation of issues argued and decided in a prior case, even where the second suit raises different causes of action. Issue preclusion will apply (1) after final adjudication (2) of an identical issue (3) actually litigated and necessarily decided in the first suit (4) asserted against one [*12] who was a party in the first suit or in privity with that party. (*DKN Holdings, LLC v. Faerber* (2015) 61 Cal.4th 813, 824-825.) Here, the judgment in the habitability action found nonfunctional or missing smoke detectors, the same issue plaintiffs assert here as the basis for the bad faith complaint. Plaintiffs are bound by that finding.

C. For a Condition Precedent in a Warranty to Void Coverage, No Nexus to the Loss is Necessary.

²The record does not indicate that the trial court actually took judicial notice of the documents both parties submitted in connection with ASIC's demurrer.

Plaintiffs further argue the warranty condition does not preclude coverage because any noncompliance with the warranty lacked a nexus with the condition insured against. We disagree.

Generally, an insured must be in strict compliance with a condition precedent to the right of recovery under a policy. (*Hogins v. Supreme Council of the Champions of Red Cross* (1888) 76 Cal. 109, 112.) As explained in *Wells Fargo & Co. v. Pacific Ins. Co.* (1872) 44 Cal. 397, 412, "the very meaning of a warranty is, to preclude all question whether it has been *substantially* complied with; it must be literally" complied with. Some courts have suggested, however, that there must be a connection between the warranty and the loss claimed. (*De Campos v. State Compensation Ins. Fund* (1954) 122 Cal.App.2d 519, 530 ["compliance with the terms of this warranty [was] a condition precedent to a right of recovery insofar as this particular risk [was] concerned".])

Lack of a nexus to the loss does not vitiate a warranty as a precondition to coverage. "California [*13] courts have held the breach of even an immaterial warranty will void a policy 'where the policy expressly declares that it shall avoid it.' [Citation]." (*Certain Underwriters at Lloyd's v. Montford* (9th Cir. 1995) 52 F.3d 219, 223.) In *Certain Underwriters*, the insured obtained a policy on a vessel that contained a "cruising warranty" that specifically excluded Colombian and Nicaraguan waters, and that a breach of the warranty would render the policy "null and void." (*Id.* at p. 221.) The insured sought reimbursement after the vessel disappeared from its berth in Costa Rica. The captain admitted that the vessel had recently cruised in waters near Colombia one month before it disappeared. (*Ibid.*) The insured argued that the breach of the cruising warranty was immaterial because the actual loss occurred in Costa Rica, which was not excluded from coverage. (*Id.* at p. 223.) *Certain Underwriters* rejected this argument, finding that the policy's warranty language covered even immaterial breaches. (*Ibid.*; *Pacific Fisheries Corp. v. HIH Cas. & General Ins. Co.* (9th Cir. 2001) 239 F.3d 1000, 1003 [causation between breach of warranty and any loss claimed is not required].) We therefore conclude that no nexus was required.

D. ASIC Did Not Waive The Condition.

Plaintiffs assert that ASIC waived the enforcement of the warranty because it received a copy of the pleadings in this matter—highlighting [*14] the smoke detector problem—but ASIC did not raise the issue.

This contention is contrary to established law. As explained in *Advanced Network, Inc. v. Peerless Ins. Co.* (2010) 190 Cal.App.4th 1054, the rule is well established that the doctrines of implied waiver and estoppel, based upon the conduct or action of the insurer, do not bring within the coverage of a policy risks not covered by its terms, or risks expressly excluded therefrom. (*Id.* at p. 1066.) As a result, ASIC's asserted conduct in failing to respond to the factual allegations of the habitability complaint by deeming them failures of the condition precedent cannot operate as a waiver here to revive plaintiffs' claims.

E. No Equitable Excusal of Condition.

Finally, plaintiffs argue that because enforcement of the warranty will result in a forfeiture in this instance, they should be equitably excused from compliance with a condition (smoke detectors) that has no relationship to the loss (habitability). (See, e.g., *Bollinger v. National Fire Ins. Co.* (1944) 25 Cal.2d

399, 405; *Root v. American Equity Specialty Ins. Co.* (2005) 130 Cal.App.4th 926, 942 (*Root*.) We disagree.

In *Root, supra*, 130 Cal.App.4th 926, the court relied upon the general contract rule that strict compliance with a condition precedent will be excused where adherence to the condition would work a forfeiture. (*Id.* at p. 939 ["California's common law of contracts has traditionally allowed for the equitable excusal or [*15] remediation of nonoccurrence of conditions precedent in contracts when such nonoccurrence works a forfeiture"]; see also Civ. Code, § 3275 [relief from forfeiture].)

In *Root*, the court considered whether noncompliance with the policy's reporting requirement of a claims-made policy could be equitably excused where enforcement would cause a forfeiture. (*Root, supra*, 130 Cal.App.4th at p. 942.) The insured, an attorney, received ambiguous notice of the claim three days before the policy expiration period, and did not report the claim until two days after the policy expired. (*Id.* at p. 930.)

Root found grounds to excuse the condition because the policy was ambiguous as to whether the claims reporting requirement was a condition or part of the insuring clause. (*Root, supra*, 130 Cal.App.4th at p. 943.) However, *Root* concluded that the provision was a condition precedent and equitable excusal did "no violence to the claims made and reported nature of the policy." Given that the insurer did not give the insured an opportunity to purchase an extended reporting endorsement and the insured had insufficient opportunity to investigate the claim and had not delayed reporting it, the facts supported equitable excusal of the condition. (*Id.* at pp. 947; see also *Bollinger v. National Fire Ins. Co., supra*, 25 Cal.2d at p. 405 ["when claims are honestly made, [*16] care should be taken to prevent technical forfeitures such as would ensue from an unreasonable enforcement of a rule of procedure unrelated to the merits"].)

Here, there are no such grounds for equitable excusal. There is no evidence that New Hampshire's compliance with the condition was rendered nearly impossible to perform, as in *Root*, or that New Hampshire made any effort to honestly comply with the condition before obtaining the insurance. Thus, the failure to have operational equipment does not work a forfeiture but merely prevents the insurer's obligation under the policy from accruing.

DISPOSITION

The judgment is affirmed. Respondent shall recover its costs on appeal.

MICON, J.:

We concur:

MANELLA, P. J. COLLINS, J.

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