

Letter from  
the President

I am nearing the end of my term as ABTL President and member of its Board of Governors. My involvement in ABTL has been one of the most rewarding experiences of my professional career. I am very proud of this organization that has as its mission the continuing education of the bar and facilitating bench/bar relationships.



Bruce A. Friedman

In the past few years, our Board has successfully initiated ABTL chapters in San Francisco and San Diego, making the ABTL a statewide organization of 2,500 members. This year, ABTL took another step forward in advancing our relationship with the Superior Court by co-hosting ABTL's first Judicial College. The program was a great success, with 50 judges and 200 lawyers in attendance. The panels and program materials were outstanding and accomplished the purpose of educating the

judges on issues in unfair competition, antitrust, trade secrets, corporate and partnership dissolution, bankruptcy, and employment related claims of discrimination and harassment. I am pleased that the Board is committed to making the Judicial College a regular ABTL event.

I want to acknowledge and thank Eric Waxman, the program chair for the Judicial College, and Judge Diane Wayne for their planning and execution of this fine program. Special thanks also

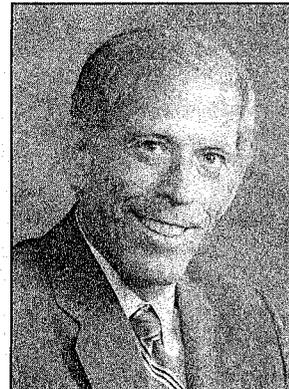
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When Civil and Criminal Trials Collide: A Civil  
Defendant's Rights under the 5th Amendment

When your client is the target of a civil lawsuit that involves allegations of illegal conduct, an important consideration is whether the civil proceedings can be stayed until conclusion of the criminal investigation. Only two California cases have addressed this issue, *People v. Coleman*, 13 Cal.3d 867 (1975), and *Pacers, Inc. v. Superior Court*, 162 Cal.App.3d 686 (1984). Neither case provides a definitive answer to this question under California law. However, federal courts and other jurisdictions have generally held that defendants are not entitled to such a stay by virtue of a constitutional mandate. Instead, whether to impose a stay rests in the sound discretion of the civil trial court.



Larry R. Feldman

This issue is significant when a defendant's conduct forms the basis for a civil claim as well as criminal prosecution. When the plaintiff commences the civil action before all potential criminal violations have been resolved, the defendant may contend that his Fifth Amendment privilege against self-incrimination and the requirements of due process mandate that the civil proceedings be stayed. The defendant may believe that it is in his best interest to assert his Fifth Amendment privilege against self-incrimination in the criminal action, but also to testify in the civil action. The defendant may argue that it is unfair to allow the prosecutor to use the fruits of discovery from the civil action to build a criminal case.

The two California cases considering this issue reached apparently inconsistent conclusions. In *People v. Coleman*, the defendant, a probationer, had his probation revoked on the same grounds that formed the basis for independent criminal charges. The defendant contended that revocation of his probation in advance of trial on the criminal charges denied him procedural due process by forcing him to forego his opportunity to testify on his own behalf at the probation revocation hearing in order to avoid incriminating himself at the pending criminal trial.

Without addressing the defendant's constitutional claim, the California Supreme Court held, as a judicial rule of evidence, that, upon timely objection, the testimony of a probationer at a

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probation revocation hearing held prior to the disposition of criminal charges arising out of the alleged violation of the conditions of his probation would be inadmissible against the probationer during subsequent proceedings on the related criminal charges. (13 Cal.3d at 889.) In reaching this decision, the California Supreme Court discussed the law applicable to the question presented in this article and stated that a defendant does not have a constitutional right to a stay of civil proceedings until resolution of a related criminal matter:

Whatever their response to requests for accommodation of the conflicting constitutional rights of a defendant in concurrent civil and criminal proceedings, courts have consistently refrained from recognizing any constitutional need for such accommodation. Rather, the alleviation of tension between constitutional rights has been treated as within the

province of a court's discretion in seeking to assure the sound administration of justice.... Justice is meted out in both civil and criminal litigation. The overall interest of the courts that justice be done may very well require that the compensation and remedy due a civil plaintiff should not be delayed (and possibly denied). The court, in its sound discretion, must assess and balance the nature and substantiality of the injustices claimed on either side.



Robert M. Turner

(13 Cal.3d at 885 [emphasis in original].)

In *Pacers*, Federal Drug Enforcement Administration (DEA) agents were involved in a brawl at the Pacers Bar. The agents brought a civil suit against Pacers' employees. The U.S. Attorney sought criminal indictments but the grand jury refused to issue indictments. Despite this refusal, the U.S. Attorney maintained an "open file" in hopes that further evidence would be developed in the civil case. At their depositions, the *Pacers* defendants asserted their privilege against self-incrimination. The trial court granted plaintiff's request for an order prohibiting defendants from testifying at trial as a consequence of their failure to answer deposition questions.

The court in *Pacers* directed the superior court to set aside its order prohibiting the petitioners from testifying at trial and directed the court to stay the petitioners' depositions until the statute of limitations for the criminal charges had expired. The court explained its holding as follows:

Where, as here, a defendant's silence is constitutionally guaranteed, the court should weigh the parties' competing interests with a view toward accommodating the interests of both parties, if possible. An order staying discovery until expiration of the criminal statute of limitations would allow real parties to prepare their lawsuit while alleviating petitioners' difficult choice between defending either the civil or criminal case. (See *United States v. Kordel* (1970) 397 U.S. 1, 9.)

This remedy is in accord with federal practice where it has been consistently held that[,] when both civil

and criminal proceedings arise out of the same or related transactions, an objecting party is generally entitled to a stay of discovery in the civil action until disposition of the criminal matter. (See, e.g., *Campbell v. Eastland* (5th Cir. 1962) 307 F.2d 478, cert. denied, 371 U.S. 955; *Perry v. McGuire* (S.D.N.Y. 1964) 36 F.R.D. 272; *Paul Harrigan & Sons, Inc. v. Enterprises Animal Oil Co., Inc.* (E.D. Pa. 1953) 14 F.R.D. 333; *National Discount Corp. v. Holzbaugh* (E.D. Mich. 1952) 13 F.R.D. 236.) The rationale of the federal cases is based on Fifth Amendment principles as well as the inherent unfairness of compelling disclosure of a criminal defendant's evidence and defenses before trial. Under these circumstances, the prosecution should not be able to obtain, through the medium of the civil proceedings, information to which it was not entitled under the criminal discovery rules. (See *People v. Collie* (1981) 30 Cal.3d 43.) Here, although petitioners are not criminal defendants, they are nevertheless threatened with criminal prosecution. To allow the prosecutors to monitor the civil proceedings hoping to obtain incriminating testimony from petitioners through civil discovery would not only undermine the Fifth Amendment privilege but would also violate concepts of fundamental fairness.

(162 Cal.App.3d at 690.)

The *Pacers* court accurately stated that the trial court should "weigh the parties' competing interests," but inaccurately described the federal practice, since the federal cases do not consistently hold that an objecting party is entitled to a stay of discovery in a civil action until disposition of a criminal matter. The federal cases and cases from other states generally hold that all relevant facts must be weighed in determining whether to grant a stay.

In *Federal Sav. & Loan Ins. Corp. v. Molinaro*, 889 F.2d 899 (9th Cir. 1989), the FSLIC filed a civil action against Molinaro, the director of a federally insured savings and loan who was also being investigated by the Federal Bureau of Investigation. "Molinaro was afraid that the criminal investigators would take advantage of any inculpatory evidence generated during the course of civil proceedings, and on August 18, he filed a motion to stay all civil proceedings or alternatively to stay all civil discovery indefinitely. His motion was denied on September 14." (889 F.2d at 901.)

The Ninth Circuit held that the district court properly denied the defendant's motion to stay:

Molinaro claims that the district court erred in refusing to stay this civil action pending the outcome of any criminal proceedings. We review a district court's ruling on a party's request to stay proceedings for an abuse of discretion. [Citation omitted.]

While a district court may stay civil proceedings pending the outcome of parallel criminal proceedings, such action is not required by the Constitution... [Citations omitted.]

A court must decide whether to stay civil proceedings in the face of parallel criminal proceedings in light of the particular circumstances and competing interests involved in the case. *Dresser Indus.*, 628 F.2d at 1375. Obviously, a court should consider the extent to which the defendant's fifth amendment rights are implicated. *Id.* at 1375-76. Other factors a court should consider will vary according to the case itself, but generally will include: (1) the interest of the plaintiffs in proceeding expeditiously with this litigation or any particular aspect of it, and the potential

prejudice to plaintiffs of a delay; (2) the burden which any particular aspect of the proceedings may impose on defendants; (3) the convenience of the court in the management of its cases, and the efficient use of judicial resources; (4) the interests of persons not parties to the civil litigation; and (5) the interest of the public in the pending civil and criminal litigation.

(889 F.2d at 902-903.)

In *Rosenberg v. Board of Education*, 710 P.2d 1095 (Colo. 1986), the Supreme Court of Colorado, at an *en banc* hearing, ruled that a tenured teacher who was alleged to have had sexual contact with a student was not entitled to have his dismissal proceedings, in which he lost his teaching position, stayed pending the outcome of criminal charges.

In *Hoover v. Knight*, 678 F.2d 578 (5th Cir. 1982), a police officer was terminated for alleged illicit sexual involvement with a 15-year-old female and alleged use of a narcotic drug with two juveniles. The termination of the police officer's employment was appealed. The Court of Appeals held that failure to postpone the administrative hearing pending resolution of related charges was proper.

In *In re Melissa M.*, 506 A.2d 324 (N.H. 1986), a father permanently lost custody of his daughter at a custody hearing. The father was charged with sexually abusing the daughter. The trial court refused to continue the custody hearing until the criminal prosecutions had been concluded. On appeal, the New Hampshire Supreme Court held that the trial court's refusal to continue the custody hearing was appropriate.

In *Shaw v. Riverdell Hospital*, 376 A.2d 228 (N.J. 1977), the Superior Court of New Jersey, Law Division, held that a defendant doctor was not entitled to stay a civil action for wrongful death even though the defendant doctor had been indicted for murder of plaintiffs' decedent.

In *Securities & Exchange Com'n v. Dresser Indus.*, 628 F.2d 1368 (D.C. Cir. 1980), the Court of Appeals refused to quash a subpoena duces tecum issued by the SEC in a civil proceeding when there was a pending criminal investigation arising out of the same transactions.

In *United States v. White*, 589 F.2d 1283 (5th Cir. 1979), the defendants were sued by their employer in a civil action for the theft of funds belonging to the employer. These thefts resulted in indictments. The Fifth Circuit held that the trial court in the civil case had acted properly in denying a motion by the defendants to stay the civil case while there were pending criminal charges.

In *In re Mid-Atlantic Toyota Antitrust Litigation*, 92 F.R.D. 358 (D. Md. 1981), the defendant in a civil antitrust lawsuit moved for a protective order to stay discovery pending completion of criminal antitrust proceedings. The court held that a stay would be inappropriate.

Although there is no clear California decision that determines the circumstances under which a civil action can be stayed when there is a pending criminal investigation or proceeding, analysis of the relevant federal authorities and cases from other jurisdictions supports the conclusion that there is no constitutional mandate for such a stay and the decision ultimately rests in the sound discretion of the trial court based on all relevant facts.

—Larry R. Feldman and Robert M. Turner

### Securities Fraud

In a landmark decision, *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 94 Daily Journal D.A.R. 5160 (April 19, 1994), the United States Supreme Court held that a private plaintiff may not maintain an action for aiding and abetting under Section 10(b) of the Securities Exchange Act of 1934, holding that the language "directly or indirectly" in Section 10(b) did not cover aiding and abetting. However, the court noted that its holding did not mean that secondary actors would be free from liability under the securities laws. Lawyers, accountants and banks could still be held liable as primary violators assuming they met all the requirements for primary liability under Rule 10b-5.

### Law Firm Disqualification

A law firm may be disqualified based on its employment of an expert accounting firm that was interviewed by opposing counsel. *Shadow Traffic Network v. Superior Court*, 94 Daily Journal DAR 5966 (May 2, 1994). The Court of Appeal upheld a trial court order disqualifying Latham & Watkins from representing Shadow Traffic Network in litigation brought by a rival in the traffic reporting business, Metro Traffic Control. Counsel for Metro Traffic Control had interviewed the accounting firm of Deloitte & Touche for about one hour on July 19, 1993, but decided not to hire the firm due to cost considerations. A few weeks later, on August 9, 1993, Latham & Watkins decided to hire the firm and served a supplemental witness list. The court held that disqualification was warranted, rejecting Shadow's contention that no privilege attached to information shared with a prospective expert who is never retained. The court so held although no formal confidentiality agreement had been executed and the employees of Deloitte & Touche submitted declarations stating that they did not recall receiving any confidential information from Metro Traffic Control.



Denise M. Parga

### Class Actions

On April 21, 1994, the Ninth Circuit conducted an *en banc* rehearing in *In re Glenfed Securities Litigation*, 11 F.3d 843 (9th Cir. 1993). Presumably, the Court will issue a decision that will reduce current confusion stemming from the apparently conflicting rulings in *Glenfed* and *In re Wells Fargo Securities Litigation*, 12 F.3d 922 (9th Cir. 1993). *GlenFed* affirmed the dismissal of a complaint, while *Wells Fargo* reversed a dismissal order in a case involving remarkably similar facts.

### Conspiracy to Induce Breach of Contract

A contracting party can no longer be held liable for conspiracy to induce breach of contract. In *Applied Equipment Corporation v. Litton Saudi Arabia Limited*, 94 Daily Journal D.A.R. 4265 (March 31, 1994), the California Supreme Court reversed a long line of appellate decisions and held that a contracting party is not liable in tort for conspiracy to interfere

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## The New Federal Rules: A Confusing Mosaic of Local-Local Rules

**I**n theory, federal practice was to be profoundly altered as of December 31, 1993, when amendments to the Federal Rules of Civil Procedure became effective due to Congressional inaction. In practice, however, action by local courts has forestalled implementation of the more controversial provisions in many federal courts in California, as illustrated in the chart on page 5.

Federal courts have the option of refusing to accept certain amendments to the Federal Rules — that is, Rules 5(c), 16(b), 26(a)(1), 26(a)(2)(c), 26(a)(3), 26(a)(4), 26(b)(2), 26(d), 29, 30(d)(2), 32(c) and 54(d)(2)(D). Local courts have elected to opt-out of many of these provisions, at least on an interim basis, in favor of local rules with varying provisions. Thus, what used to be a relatively straightforward set of Federal Rules, is now a hodge podge of different practices and procedures. The chart on page 5 attempts to sort out some of the confusion by listing the provisions that have been accepted and rejected by the local federal district courts.



Carrie Battilega

The rules of the district courts must be consulted to determine the local provisions that are in effect. In addition, many judges adhere to their own personal "local-local" rules. These rules will become apparent when an individual judge issues an order advising counsel of requirements governing, for example, early meetings of counsel and joint reports.

### The New Provisions

Provisions not presently in effect in most California District Courts include Rule 26(a)(1) and (a)(4), which would require litigants to make extensive disclosures at the outset of the litigation without inquiry, providing the location of documents and the identity of witnesses, and subjects of their information "relevant to disputed facts alleged with particularity in the pleadings". The Northern District has adopted these Amended Federal Rules in theory, but they are superseded by the similar provisions of General Orders 34 and 39 to the extent of any conflict with respect to most civil cases.

**L**itigators in the Central and Southern Districts are free to conduct discovery from the moment when litigation is filed, without the constraints of new Rule 26(f), requiring parties to meet "as soon as practicable" or Rule 26(d), prohibiting discovery until this meeting has taken place.

### The Central District

The Central District deferred accepting most of the amended rules under General Order 339 and General Order 339A.

Those orders provide for the Rules Committee of the Central District to study the Amended Federal Rules and make recommendations.

The Court thus opted out of implementing Rule 5(c), 16(b), 26(a)(1), 26(a)(2)(c), 26(a)(3), 26(a)(4), 26(b)(2), 26(d), 29, 30(d)(2), 32(c) and 54(d)(2)(D). The other Amended Federal Rules are effective and they supersede the Local Rules to the extent that there is any conflict.

Thus, early meeting requirements continue to be governed by Local Rule 6, except to the extent that particular judges may have their own rules governing such meetings and early meeting reports. Under Local Rule 6, counsel will continue to be required to meet within 20 days after service of an answer by each defendant.

### Northern District

The Northern District has generally adopted the spirit of the Amended Federal Rules, but has imposed its own variations on those provisions through its General Orders Nos. 34 and 39. General Order 39 states that, except as specifically provided in General Orders 34 and 39, the Amended Federal Rules will govern all civil cases filed on or after December 1, 1993, and, to the extent practicable, cases pending on that date.

General Order 34 supersedes the Amended Federal Rules to the extent of any conflict with respect to cases governed by General Order 34. (General Order 39(III)(A).)

**N**otwithstanding Rule 26(a)(4), disclosures made pursuant to the Federal Rules or General Order 34 shall not be filed with the Court. (General Order 39(III)(B).)

Rule 26(a)(3) is supplanted by Local Rules 235-7, 235-8, and 235-9, except to the extent those provisions are modified or extended by standing or case-specific orders entered by a judge. Additionally, Appendix A to General Order 39 lists specific cases that are not affected by Amended Federal Rules 16(b), 26(a)(1) and 26(a)(2), 26(d), or 26(f). These include bankruptcy appeals, and Freedom of Information Act proceedings. Bankruptcy cases are not affected by that portion of Rule 16(b) that fixes a deadline for entry of a scheduling order; Rule 26(a)(1)-(4); Rule 26(d)'s presumptive stay of discovery until completion of the meet and confer required by Rule 26(f), Rule 26(f), Rule 30(a)(2)(C); Rule 31(a)(2)(C); or those portions of Rules 32(a), 33(a), 34(b), and 36(a) that incorporate the requirements of Rule 26(d).

General Order 34 provides detailed requirements governing discovery that are largely consistent with those required under Amended Rule 26. It applies to most civil litigation, with exceptions listed in Appendix B, including multidistrict litigation, class actions, transferred cases, cases filed by pro se plaintiffs, cases remanded from appellate court, and reinstated and reopened cases.

**U**nder General Order 34, except by stipulation of the parties, no formal discovery can take place until after the parties have completed disclosures and meetings required under Sections VII and VIII of General Order 34. (General Order 34, §VI.) Under Section VII, required initial disclosures include the name, title, and address of each person known to have information about factual matters relevant to the case; unprivileged documents that tend to support the disclosing party's likely position; insurance agreements; and damages computations. These disclosure requirements supersede those of Amended Federal Rule 26(a)(1-4).

General Order 34 also supersedes the pre-trial disclosure requirements of 26(a)(3). Additionally, it changes the timing

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## CHART OF FEDERAL RULES

	<u>Northern District</u>	<u>Eastern District</u>	<u>Central District</u>	<u>Southern District</u>
Governing document (states the status of Amendments to the Federal Rules)	Gen. Orders 34 and 39.	Amended local rules.	Gen. Order 339 and 339A.	Gen. Order 394-E and 394-F.
FRCP 4: (Summons)	In effect but modifies 4(d)(2)(F) and 4(m).	In effect	In effect.	In effect.
FRCP 5: (Service and Filing of Pleadings)	In effect.	In effect.	Deferred Implementation of 5(c) until after consideration of Rules Committee ("Deferred").	In effect.
FRCP 11: (Signing of Pleadings ... Sanctions)	In effect.	In effect.	In effect.	In effect.
FRCP 12: (Defenses and Objections)	In effect.	In effect.	In effect.	In effect.
FRCP 16: (Pretrial Conferences)	In effect, but 16(b) does not apply to Gen. Order 39 Appendix A cases: 1) Bankruptcy appeals and w/drawals; 2) Freedom of Info Act; 3) in forma pauperis; 4) habeas corpus; 5) defaulted student loans; 5) recovery of overpayment, enforcement of judgment; 6) recovery of overpayment of veteran's benefits; and 7) Social Security review.  16(b) provision regarding deadline for entry of scheduling order in-applicable to bankruptcy cases.	Declined to adopt.	Deferred 16(b).	In effect (except reference to 26(f) meeting).
FRCP 26(a)(1-4) (Required Disclosures)	Requirements of 26(a)(1) & (a)(2) do not apply to Gen. Order 39 Appendix A cases.  Gen. Order 34 supersedes conflicting disclosure requirements.  Disclosures not filed with court.  Rule 26(a)(3) supplanted by Local Rules 235-7, 235-8, and 235-9 and judicial orders.  Rules 26(a)(1)-(4) inapplicable to bankruptcy cases.	Declined to adopt.	Deferred 26(a)(1)-(4) except 26(a)(2)(A) & 26(a)(2)(B) (which require disclosure of expert witnesses and reports).  (District already operates under mandatory disclosure provisions.)	Deferred implementation until after court's evaluation of Report from local advisory panel ("Deferred").
FRCP 26(b)(2) (allows court to alter discovery limits by local rule, so check local rules for limits)	In effect.	In effect.	Deferred.	In effect.

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CHART OF FEDERAL RULES (Continued)

	<u>Northern District</u>	<u>Eastern District</u>	<u>Central District</u>	<u>Southern District</u>
FRCP 26(d) (Discovery Timing)	In effect, but does not apply to Gen. Order 39 Appendix A cases and the presumptive stay of discovery does not apply to bankruptcy cases.	Opted out.	Deferred.	Deferred.
FRCP 26(f) (Meeting of Parties)	In effect, but does not apply to Gen. Order 39 Appendix A cases or bankruptcy cases.	Opted out.	In effect, except reference to 26(a) mandatory disclosures.	Deferred.
FRCP 29	In effect.	In effect.	Deferred.	In effect.
FRCP 30	In effect. Rule 30(a)(2)(C) does not apply to bankruptcy cases.	In effect, but opted out of 30(a)(2)(A) requirement via 26(b)(2).	In effect, but deferred 30(d)(2) (time limit for depositions).	In effect, but deferred 30(a)(2)(A).
FRCP 31	In effect. Rule 31(a)(2)(C) does not apply to bankruptcy cases.	In effect, but opted out of 31(a)(2)(A) requirement via 26(b)(2).	In effect.	In effect but deferred 31(a)(2)(A).
FRCP 32	In effect.	In effect.	In effect but deferred 32(c).	In effect.
FRCP 33: (Interrogatories)	In effect.	Opted out of 33(a) Requirement via 26(b)(2).	In effect, except 33(a) reference to 26(d) timing.	In effect, except 33(a) reference to 26(d) timing.
FRCP 34: (Requests for Documents & Things)	In effect.	In effect, except 34(b)'s reference to 26(d) timing.	In effect, except 34(b)'s reference to 26(d) timing.	In effect except 34(b)'s reference to 26(d) timing.
FRCP 37: (Discovery Sanctions)	In effect.	In effect.	In effect.	In effect.
FRCP 54: (Judgment; Costs)	In effect.	In effect.	Deferred 54(d)(2)(D).	In effect.
FRCP 58: (Entry of Judgment)	In effect.	In effect.	In effect.	In effect.
Application of Amendments to Removed Cases	<ul style="list-style-type: none"> <li>Filing of Removal Notice triggers deadlines in Gen. Order 34.</li> <li>Removing defendant must serve copy of Gen. Order 34 w/ Notice of Removal.</li> </ul>	No mention.	No mention.	No mention.
Application to Transferred Cases	Within 30 days after filing of transferred case, plaintiffs will be notified of status conference at which Judge will decide whether Gen. Order 34 applies.	No mention.	No mention.	No mention.

## Defending Against Tort-Based Lender Liability Claims

**A**sksed why he robbed banks, Willie Sutton replied, "because that is where the money is." Mr. Sutton's statement reflects the attitude of many borrowers trying to recoup losses on financed projects gone bad.

Beginning in the mid 1980's, borrowers began to prevail on new theories of recovery against their lenders. These included claims arising out of a purported "special relationship" between lenders and borrowers and the implied covenant of good faith and fair dealing. According to two prominent lender liability plaintiffs' attorneys, these claims have since "fallen by the wayside in favor of more traditional claims such as breach of contract and fraud." A. Barry Capello, Frances E. Komoroske, *Lender Liability*, p. 11-3 (2d ed. 1993). Notwithstanding this pronouncement, borrowers are still asserting these claims in actions against lenders. Here is a brief discussion of how to dispose of them.

### Claims Based Upon "Quasi-Fiduciary" Relationships

The Court of Appeal first acknowledged a "special" or "quasi-fiduciary" relationship between banks and their checking account customers in *Commercial Cotton Co. v. United California Bank*, 163 Cal. App. 3d 511, 516 (1985). This opened the door to tort claims brought by borrowers against lenders in loan disputes based upon a purported "quasi-fiduciary" relationship between lenders and borrowers. The "quasi-fiduciary" allegations most often appeared in claims of breach of fiduciary duty, constructive fraud and tortious breach of the implied covenant of good faith and fair dealing. Soon after the holding in *Commercial Cotton*, the Court of Appeal affirmed the existence of a "quasi-fiduciary" relationship between commercial lenders and borrowers in *Barrett v. Bank of America*, 183 Cal. App. 3d 1362, 1369 (1986).

The "quasi-fiduciary" relationship theory was severely criticized and appears to have been short-lived. It was rejected for the depositor-bank relationship in *Copesky v. Superior Court*, 229 Cal. App. 3d 678, 694 (1991). It was also rejected in the lender/borrower context. See, e.g., *Kim v. Sumitomo Bank*, 17 Cal. App. 4th 974, 979 (1993); *Careau & Co. v. Security Pacific Business Credit, Inc.*, 222 Cal. App. 3d 1371, 1400 (1990); and *Price v. Wells Fargo Bank*, 213 Cal. App. 3d 465, 478 (1989). No reported California decision subsequent to *Price* has found facts sufficient to support the imposition of "quasi-fiduciary" or regular fiduciary obligations in a commercial lender/borrower relationship. (The Court of Appeal did affirm a trial court's finding of a fiduciary relationship between a lender and a borrower in *Security Pacific National Bank v. Williams*, 213 Cal. App. 3d 927 (1989), but the court's opinion was decertified and ordered not published by the California Supreme Court's order of December 21, 1989.)

**I**n the absence of case law establishing a unique standard for finding a fiduciary relationship, quasi or otherwise, between a lender and a borrower, a borrower must look to the general law of fiduciary relationships to assert such a claim. Pursuant to the California Supreme Court's decision in *Committee on Children's Television, Inc. v. General Foods Corp.*, 35

Cal. 3d 197, 221 (1983), a party claiming a fiduciary relationship must allege and prove (a) that the person to be charged with a fiduciary obligation either knowingly undertook to act on behalf and for the benefit of another, or (b) entered into a relationship which imposes that undertaking as a matter of law.

Since fiduciary obligations are not imposed in lender/borrower relationships as a matter of law, borrowers must allege and prove that the lender knowingly assumed the obligations of a fiduciary. The assumption of such obligations, however, "precludes the idea of profit or advantage resulting from the dealings of the parties and the person in whom the confidence is reposed." *Rickel v. Schwinn Bicycle Co.*, 144 Cal. App. 3d 648, 654 (1983). This is a difficult hurdle for borrowers to overcome in proving a fiduciary relationship.

**G**enerally, a lender's expectation of profit to be derived from a loan is inconsistent with any claims that the lender assumed fiduciary obligations. As the court in *Nymark v. Hart Fed. Savings & Loan Ass'n*, 231 Cal. App. 3d 1089, 1093 n. 1 (1991), so aptly put it, a lender's right to pursue its own economic interests "is inconsistent with the obligations of a fiduciary which require that the fiduciary knowingly agreed to subordinate its interests to act on behalf of and for the benefit of another."

### Claims Based Upon The Implied Covenant of Good Faith and Fair Dealing

Claims arising out of the implied covenant of good faith and fair dealing come in two varieties — tortious breaches and contractual breaches.

The tortious breach claims (and the punitive damages claims that accompanied them) were based upon the "quasi-fiduciary" relationship discussed in *Commercial Cotton* and *Barrett*. Following the Supreme Court's holding in *Foley v. Interactive Data Corp.*, 47 Cal. 3d 654 (1988) (which rejected tort recovery for breach of the implied covenant in claims brought by employees against employers), the courts have routinely rejected claims for tortious breaches of the implied covenant in lending situations. See, e.g., *Kim*, 17 Cal. App. 4th at 979; *Careau*, 222 Cal. App. 3d at 1400; *Price*, 213 Cal. App. 3d at 478; and *Mitsui Manufacturers Bank v. Superior Court*, 212 Cal. App. 3d 726, 732 (1989).

Claims of contractual breaches of the implied covenant, however, still continue to surface. Many times these claims are based upon nothing more than breaches of expressed terms of the loan agreements or acts that are consistent with the lender's rights under those agreements. Both types of claims are improper.

**I**n the first instance, where the alleged acts constitute a breach of the express terms of the loan agreement, the court should disregard the claim as superfluous. *Careau*, 222 Cal. App. 3d at 1395. In the second instance, the claim is frivolous because the implied covenant does not require a lender to act inconsistently with its statutory or contractual obligations and rights. See, *AARTS Productions, Inc. v. Crocker National Bank*, 179 Cal. App. 3d 1061, 1069 (1986). Nor does the implied



John A. Sturgeon

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## Lender Liability Claims

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covenant impose a duty of moderation on the part of the lender in enforcing its rights. *Price*, 213 Cal. App. 3d at 479.

### Analyzing the Lender Liability Case

When commencing representation of a lender against claims involving these lender liability issues, the first thing that counsel should do is carefully review all of the loan documents. Those documents may contain several provisions that can effectively defuse the appeal of the borrower's claims.

For example, jury waivers in the loan agreements are enforceable. *Trizec Properties, Inc. v. Superior Court*, 229 Cal. App. 3d 1616 (1991). These waivers, along with arbitration clauses, may prevent a jury from trying the borrower's contract issues after being unduly prejudiced by evidence on collateral tort claims.

The loan documents may also reveal that the acts constituting the purported breach of the implied covenant alleged by the borrower may well have been expressly authorized by the loan documents and therefore not actionable. This is especially true where the claim arises out of the lender's refusal to extend further credit or actions it took upon default.

Next, counsel should take steps to eliminate these claims early in the action so that evidence of intent and any collateral wrongdoing arguably relevant to the tort claims does not get to the trier of fact. If the claims to be tried go beyond breach of contract, it opens the door to all types of evidence to be heard by the trier of fact, much of which can be unduly prejudicial and confusing.

The first line of attack should be to dispose of the claims by demurrer, motion to dismiss or summary judgment. For example, a lender can demur to breach of fiduciary duty, constructive fraud and tortious breach of the implied covenant claims on the ground that the facts alleged do not give rise to a fiduciary or "quasi-fiduciary" relationship. The existence of a fiduciary relationship is a question of law to be decided by the judge. *Kirschner Bros. Oil, Inc. v. Natomas Co.*, 185 Cal. App. 3d 784, 790 (1986). The parol evidence rule can also be used at this stage to bar the borrower from prosecuting breach of the implied covenant claims that are contrary to the terms of the loan documentation.

The lender may also force resolution of these issues through the discovery process. In one recent case, a trial court denied a defendant bank's motion for judgment on the pleadings on procedural grounds, but nonetheless denied the plaintiff's motion to compel discovery on the claims for which the bank sought judgment on the pleadings. This issue may arise in a lender liability case when the borrower seeks to compel the discovery of the lender's internal procedural guidelines. The lender may want to resist such discovery on the grounds that the guidelines are immaterial and will not lead to the discovery of admissible evidence because they do not give rise to any duties, contractual, fiduciary or otherwise, owed to the borrower, but are instead implemented to protect the interests of the lender's shareholders and/or insurers.

Finally, counsel can exclude evidence of breach of fiduciary duty or breach of the implied covenant by way of motions in limine. Courts wary of dismissing claims early on in the action may be willing to exclude evidence necessary to prove these claims when faced with an imminent, extended trial.

—John A. Sturgeon

## Cases of Note

Continued from page 3

with or induce the breach of its own contract, even when one of the co-conspirators is a third party. The Supreme Court held that a conspiracy claim is not an independent tort and can only support tort recovery against a party who already owes the duty. Because a party to a contract owes no tort duty to refrain from interfering with its performance, it cannot be bootstrapped into tort liability through the claim of conspiracy.

### Bad Faith Denial of Contract

In *Stoll v. Shuff*, 93 Daily Journal D.A.R. 1226 (Jan. 28, 1994), the Fourth Appellate District held that liability for bad faith denial of the existence of a contract is not limited to denials made directly to the contracting party and can be supported by evidence of denials made to third parties. The court rejected the proposition that the denial of the existence of the contract must be expressly stated before the commencement of the litigation and directly by the defendant to the plaintiff. In dicta, it noted that the denial may also be proven by internal memoranda or notes that were never shown to anyone until disclosed in pretrial discovery.

### Contractual Attorneys' Fees and Costs

The Third Appellate District has held that a contractual attorneys' fee provision providing for recovery of reasonable attorneys' fees and costs does not cover experts' fees. In *Ripley v. Pappadopoulos*, 94 Daily Journal D.A.R. 4414 (April 1, 1994), the Court of Appeal held that a contractual provision that "the prevailing party shall be entitled to reasonable attorney's fees and costs" does not cover expert witness fees. It stated in dicta that, if an appropriate contract provision did cover expert witness fees, those fees would have to be specially pleaded and proven at trial rather than included in a memorandum of costs. The court also held that expenses of copying documents, Federal Express and postage charges, and telecopy/fax charges are expressly disallowed as costs and therefore were not recoverable under the contractual attorneys' fee provision.

A contractual attorneys' fee provision does not cover the costs of self-representation by a non-attorney. *Wyzard v. Goller*, 94 Daily Journal D.A.R. 4005 (March 25, 1994).

### Civil Procedure

In *Beisel v. Aid Assoc. for Lutherans*, 94 Daily Journal D.A.R. 2381 (Feb. 9, 1994), the Central District held that 28 U.S.C. §1446(b) must be strictly construed as barring removal of an action from state court more than one year after its commencement. In a case of first impression for courts in the Ninth Circuit, the court so held, despite the fact that defendants first removed the case to federal court in a timely manner. After initial removal, plaintiffs added a non-diverse individual defendant and the case was remanded. In August, 1993, more than one year after the action was filed, the state court granted summary judgment in favor of the non-diverse defendant. Plaintiffs then voluntarily dismissed the action against the non-diverse defendant and defendant again filed removal of the action.

The court disagreed with other jurisdictions which permit a second removal more than one year after commencement of

(Continued next page)

the action on the theory that strict construction of 28 U.S.C. §1446(b) would encourage plaintiffs to add diversity-destroying defendants for the purpose of proceeding in state court. The Central District held that 28 U.S.C. §1446(b) must be strictly construed and therefore any removal one year after commencement of the action is barred.

#### Class Action Attorney Fees

In *Class Plaintiffs v. Jaffe & Schlesinger P.A.*, 94 Daily Journal DAR 3749 (9th Cir. March 23, 1994), the court held that attorneys were not entitled to share in attorney fees awarded in a class action lawsuit although they may have benefited the class through parallel state court litigation. The case arose from the \$2.25 billion bond default involving the Washington Public Power Supply System. Attorneys who brought a parallel derivative action agreed with class action plaintiffs that they would seek an award of attorneys fees from the settlement fund created for the class action plaintiffs. The court concluded that no authority mandates an award of fees to attorneys who did not formally represent class action plaintiffs, even if they inci-

dentally benefitted the class through derivative litigation brought in state court.

#### Attorney-Client Privilege

The U.S. District Court for the Northern District of California ruled that the attorney-client privilege was waived with respect to documents shown to an accountant for non-legal purposes. *Samuels v. Mitchell*, 94 Daily Journal D.A.R. 5300 (N.D. Cal. April 12, 1994). The court held that the litigant thus waived the privilege as to documents shown to a non-testifying accountant, Ernst & Young, where the purpose was to keep Ernst & Young up to date on an arbitration proceeding, and not to obtain Ernst & Young's assistance in rendering legal advice. At the same time, the Court ruled that the documents were protected from disclosure pursuant to the work product doctrine because they were given to Ernst & Young in confidence. The court held that the work product privilege is not automatically waived by any disclosure to third persons, but only if the disclosure substantially increases the opportunity for potential adversaries to obtain the information.

#### Conflicting 'Other Insurance' Clauses

The Second Appellate District ruled that an excess "other insurance" clause would not be enforced where a second insurer's policy provided for pro rata contribution among multiple insurers. *CSE Ins. Group v. Northbrook Property & Cas. Co.*, 94 Daily Journal DAR 4851 (April 11, 1994). CSE Insurance and Northbrook each provided umbrella coverage applicable to the same risk. Northbrook's policy provided that it was excess over other insurance and not contributory. The CSE policy provided that it would contribute pro rata with other insurance at the same level. The court provided an exhaustive recitation of conflicting authorities on the subject and then concluded that the excess clause would not be enforced for several reasons, including a public policy that appeared to favor apportioning a loss among those who have contracted to insure it.



Vivian R. Bloomberg

#### Assignment of Rents

In *MDFC Loan Corp. v. Greenbrier Plaza Partners*, 21 Cal. App. 4th 1045, 26 Cal. Rptr. 2d 596, 94 Daily Journal DAR 505 (Jan. 13, 1994), the Court of Appeal held that the transfer of rental proceeds to a beneficiary under an absolute assignment of rents following a nonjudicial foreclosure sale did not constitute a deficiency judgment under Code of Civil Procedure §580d because the assignment of rents merely constituted additional primary security.

#### Lis Pendens

In *Hunting World, Inc. v. Superior Court*, 94 Daily Journal D.A.R. 1301 (Jan. 31, 1994), the First Appellate District concluded that an action to set aside a fraudulent conveyance, which was filed as an adjunct to an independent action for trademark infringement, was a "real property claim" within the meaning of the lis pendens statutes.

—Denise M. Parga and Vivian R. Bloomberg

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## Recent Cases in Environmental Insurance Coverage Litigation: A Survey

[Environmental insurance coverage cases] raise the question of who will pay for the cleanup of millions of tons of toxic waste produced in the United States since World War II. This problem has sparked a legal war that has raged in both federal and state courts from Maine to California.

*ACL Technologies, Inc. v. Northbrook Prop. & Cas. Co.*,  
17 Cal.App.4th 1773, 1777 (1993).

With these words, Justice Sills aptly described the legal battleground that has raged since enactment in 1980 of the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), 41 U.S.C. §9601, *et seq.* CERCLA authorizes the Environmental Protection Agency (EPA) to require polluters to clean up toxic chemicals which have been disposed of at a wide variety of sites, in many cases over decades of time. The response of most targeted polluters has been to sue their liability insurance carriers under their CGL policies issued by different insurers over periods of many years — even decades.



John A. Dito

Many of the environmental insurance coverage lawsuits have been filed in California, presumably because there is a perception of a policyholder-friendly judicial climate in this state (some insurers would say that “friendly” is a greatly exaggerated understatement).

In this environmental litigation, a number of controversial issues have preoccupied the courts across the country, and as cases in California have wended their way through the appellate system, some of those issues have been decided under California law. This article will report on recent significant cases in this developing area: *Montrose Chemical Corp. v. Superior Court*, 6 Cal.4th 287 (1993); *Titan Corp. v. Aetna Cas. & Sur. Co.*, 22 Cal.App.4th 457 (1994); *ACL Technologies, Inc. v. Northbrook Property & Casualty Ins. Co.*, 17 Cal.App.4th 1773 (1993); and *Iolab v. Seaboard Surety Co.*, 15 F.3d 1500 (9th Cir. 1994).

### Montrose Chemical

The policyholder, Montrose Chemical, had manufactured DDT at its Torrance, California site for many years. The United States and the State of California sued Montrose under CERCLA, alleging that the operation of the manufacturing facility had caused environmental contamination. Montrose requested that its liability insurers defend the action, and, on their refusal, filed an action, seeking a declaration that the insurers were obligated to defend. Montrose moved for summary adjudication on the issue of the duty to defend, which was denied by the trial court. The Court of Appeal reversed.

On review, the Supreme Court affirmed the Court of Appeal, and held that the insurers had a duty to defend, relying on the established principle that the duty to defend is broader than the duty to indemnify.

Significantly, the Court also resolved a split among the Districts of the Court of Appeal with respect to matters that can be considered in determining whether there is a duty to defend.

Some courts had held that an insurer could not rely on extrinsic evidence — that is, evidence beyond the four corners of the complaint in the underlying litigation against the insured. The court ruled to the contrary, finding that an insurer can rely on such extrinsic evidence to defeat the duty.

In finding a duty to defend, the court reiterated its holding in *Gray v. Zurich*, 65 Cal.2d 263, 299 (1966), that the insured is entitled to a defense if the underlying complaint alleges the insured's liability for damages “potentially” covered under the policy. The Court rejected the argument proffered by one insurer that the standard should be “reasonable potential for coverage”. The Court held that, in a declaratory relief action concerning the duty to defend, the insured need only “prove the existence of a potential for coverage” while the insurer must “establish the absence of any such potential.” (*Id.* at 300.)

Finally, the Court held that an action for declaratory relief regarding insurance coverage should be stayed if it turns on facts which, if proved by the insurer, could prejudice the insured in the underlying action. The court cited the example of a third party seeking damages because of the insured's negligent conduct. In such a case, the insurer might seek to avoid providing a defense by arguing that the insured engaged in intentional conduct that would not be covered under the subject policy. The insurer's proof could prejudice the insured in the underlying litigation. To avoid such prejudice, the Court held that the declaratory relief action could be stayed.

### Titan

The Titan Corporation had operated a plant that produced waste materials in New Jersey from 1906 until 1985. New Jersey law required Titan to clean up the site. Aetna denied coverage. The Court of Appeal held that there was no coverage on the basis of two principal issues: (a) the “owned property” exclusion, and (b) the personal injury endorsement.

### Owned Property Exclusion

The policy provided that, “This insurance does not apply . . . to property damage to (1) property owned or occupied by or rented to the insured; (2) property used by the insured. . . .” The Court held that this exclusion precluded coverage for costs to remove solid wastes which injured only the insured's property and not third-party property. The court also held that prophylactic measures taken to prevent future contamination are not covered, whereas steps taken to abate continuing harm from extant sources of contamination are covered.

The Court distinguished cases which have held that the “owned property” exclusion does not apply, on the ground that such cases “invariably” involved cleanup of existing contamination of damages to third parties, “and the cleanup costs were incurred to ameliorate actual injury and to prevent the contaminants from continuing to injure or threaten third parties.” (22 Cal. App.4th at 472.) (Original emphasis.)

### Personal Injury Exclusion

Although the Aetna policy contained an “absolute” pollution exclusion, the policyholder contended that coverage should nevertheless apply under a separate “personal injury” endorsement providing liability coverage for such torts as “wrongful entry or eviction or other invasion of the right of private occupancy.” This argument has proved persuasive to some courts, even though it seems far-fetched. The *Titan* court did not fall prey to any meretricious allure of the argument.

The Court held that the personal injury endorsement did not “negate” the absolute pollution exclusion, and that, to hold otherwise would violate “basic principles of contract interpreta-

(Continued on next page)

to Presiding Judge Robert Mallano for agreeing to have the court co-host the event.

I would also like to thank Kim Wardlaw for her efforts in planning the flawless ABTL annual seminar last fall at La Quinta and David Stern who, as dinner chair, has continued the ABTL tradition of outstanding dinner programs in 1993 and 1994. Thanks also to Vivian Bloomberg, editor of the *ABTL Report*, for her fine work in producing an excellent and widely read legal journal distributed to our members and the entire Los Angeles bench. I would be remiss in not also thanking the members of the entire ABTL Board of Governors both for their work and support.

The ABTL is the finest group of lawyers and friends I will ever be associated with. Thank you all for allowing me to serve as your President.

### AB 3738

Before concluding, I want to call to your attention a bill before the California Legislature which I believe is an overreaction to the unwarranted criticism of Justice Lucas' travel, and threatens ABTL's programs and mission. AB 3738 prohibits a state judge from receiving more than \$250 in "gifts" from any one source.

No one would argue with this concept; it goes to the very heart of judicial integrity. It is the exception to the rule which needs reconsideration. The legislation excepts travel reimbursement only in connection with a "speech." Reimbursement is limited to the day preceding and following the speech.

This raises a number of problems for our organization. First does "speech" include serving on a panel in a qualified MCLE program?

Second, we invite state and federal judges to participate as panelists in our annual seminars which take place over a weekend. The ABTL reimburses the judges for their travel expenses. The judges not only make presentations on panels, but also spend time during the weekend discussing legal issues with lawyers attending the program. This communication between bench and bar is an important aspect of the ABTL mission. Passage of AB 3738 as drafted would interfere with an important function of our association.

Jerome Falk, President of ABTL Northern California, suggests that the bill be amended to permit reimbursement for attendance at or participation in any program for which MCLE credit is given to participants as well as professional functions hosted by state or local bar associations, provided the host organization does not confine or focus the representation of its members to a particular side or point of view. These are important changes if the bill is to be enacted at all.

Personally, I do not believe the bill is necessary. The bench has a code of ethics to which they adhere. I do not believe that legislation is necessary and suggest that the legislators focus on regulating the sources of their own campaign contributions before engaging in this effort to interfere with the educational activities of judges whose integrity and impartiality is rarely questionable.

—Bruce A. Friedman

requirement of the 26(f) meet and confer provision, requiring that an early meeting be conducted no later than 100 days after the complaint is filed. (General Order 34, §VIII.)

### Eastern District

Pursuant to Rule 253, the Eastern District specifically declined to adopt the mandatory disclosure provisions described in Rule 26, and the limitations on depositions and interrogatories described in Rules 30 and 31. Thus, it will be governed by its local rules and the non-discovery related Amended Federal Rules (see Chart).

### Southern District

Pursuant to General Order 394-E, as extended by General Order 394-F, the Southern District deferred implementation of most of the discovery related amendments. The Civil Justice Reform Act Committee for the Southern District is studying the potential effects of the new rules. After reviewing the Committee's report, the court will decide the form in which the amendments will be implemented in the Southern District.

Thus, the days of a single embodiment of the substantive Federal Rules appear to be over. The opt-out provisions have created a situation in which counsel must carefully and frequently review the local rules in the different districts to keep abreast of the multiple Federal Rules.

—Carrie Battleg

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