

STATE WATER RESOURCES CONTROL BOARD

P. O. BOX 100 • SACRAMENTO 95801
322-0188



In Reply, Refer
to: 230/MM

JUN 11 1980

Mr. Robert J. Monogan
California Manufacturers Association
923 12th Street
P. O. Box 1138
Sacramento, CA 95805

Dear Mr. Monogan:

This is in response to your letter of June 4, 1980, notifying Assemblyman McCarthy of CMA opposition to Section 3 of AB 2700 which would amend the Water Code.

It appears that you have three main concerns:

1. The extension of Regional Water Quality Control Board cleanup and abatement authority to "threatened" discharges;
2. The extent of retroactive liability imposed on a person who has discharged in the past; and
3. The proposed addition of Section 13362 of the Water Code, which declares damages obtained by the State from wrongful discharges, to be civil in nature and therefore subject to a three-year statute of limitations.

With respect to your first concern, existing Section 13304 of the Water Code is written in the present tense. The Regional Boards have the authority to issue an order directing a person to clean up and abate or take other necessary remedial action only in the following two circumstances:

1. If waste is discharged in violation of any waste discharge requirement or other order issued by a Regional Board; or
2. If, in the absence of waste discharge requirements, a person causes or permits any waste to be discharged or deposited where it is or probably will be discharged into the waters of the State, and creates or threatens to create a condition of pollution or nuisance.

(800) 666-1917

LEGISLATIVE INTENT SERVICE



LEGISLATIVE INTENT SERVICE

LEGISLATIVE INTENT SERVICE

SP 10

By enclosed Amendments 1 and 2, we have deleted the language extending Regional Board authority to require that remedial measures be taken for threatened violations of waste discharge requirements.

We have retained the language in the bill pertaining to a threatened discharge or deposit of waste by one who is not under waste discharge requirements for the simple reason that this amendment is needed. The need can best be demonstrated by example. During the dry summer months, the owner of an inoperative mine does not "discharge or deposit" mine waste in a manner which creates or threatens to create a condition of pollution or nuisance in an adjacent stream. However, when the rainy season arrives, acid wastes at the mine will combine with runoff and in fact reach the stream and cause pollution. Under existing law, the Regional Boards could not issue an order directing the mine owner to take necessary remedial action to prevent this from occurring. This is false economy since avoidance of pollution is less worthy to both the discharger and the environment than the cleanup of a problem after the fact.

Contrary to the assertion in your letter, in no event could a remedial action order issued by a Regional Board specify changes in design or operation procedures. Section 13360 of the Water Code expressly prohibits the Boards from telling a discharger the manner in which he must comply with any order issued. The Boards can only identify the problem and direct the person to take steps to abate or avoid it altogether. The ultimate measures taken are left up to the discharger.

With regard to the need for clarifying Regional Board cleanup and abatement authority over past discharges, as discussed above, Section 13304 is written in the present tense. Since it is impossible for our Boards to know of every discharge as it is taking place, we want to make it crystal clear that a person who has discharged, either in violation of waste discharge requirements or so as to create a condition of pollution or nuisance, can be held responsible.

Your concern over the language "has threatened", is resolved by proposed Amendments 3 and 4 which delete these words.

Liability for past discharges has been limited by Amendment 6 which provides that Section 13304 does not impose any new liability for acts occurring before the effective date of the Porter-Cologne Water Quality Control Act.

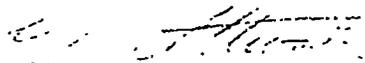
Finally, you request that proposed Section 4 of the bill be revised. This Section was drafted in response to an adverse and erroneous ruling in the Federal District Court. The Court ruled that suit under Section 13350 of the Water Code for civil damages for wrongful discharges is subject to a one-year penal statute of limitations. State case law clearly holds that civil damages under the Water Code are in fact subject to a three-year statute of limitations.

Mr. Robert J. Monogan

-3-

Although this particular ruling pertained to Section 13350 damages, it is not the only section of the Water Code which provides for civil recovery. Section 13350 applies only to illegal discharges to groundwaters. Civil damages for wrongful discharges to surface waters are requested under a different section; Section 13385. Consequently, to avoid a similar ruling in the future on either section, we are codifying state case law by declaring as civil damages recovery under "this division".

Sincerely,


William R. Attwater
Chief Counsel

cc: All Members of the Senate Committee
on Health and Welfare



OP 12

AMENDMENTS TO AB 2700

Amendment 1

On page 5, line 1, of the printed bill, as amended in the Assembly on May 19, 1980, after "discharged", insert: or

Amendment 2

On page 5, line 2, of the printed bill, strike out ", or threatens to discharge"

Amendment 3

On page 5, line 6, of the printed bill, strike out "or has"

Amendment 4

On page 5, line 7, of the printed bill, strike out "threatened"

Amendment 5

On page 6, line 4, of the printed bill, strike out "If" and insert: Without regard to whether a cleanup and abatement order has been issued, if

Amendment 6

On page 6, after line 20, of the printed bill, insert:

(e) This section does not impose any new liability for acts occurring before the effective date of this division.

SEC.4. Section 13362 is added to the Water Code to read:
13362. Civil damages recovered pursuant to this division are liquidated damages which operate to more fully compensate the people of the state of California for unquantifiable harm to the waters of the state.

SEC.5. The addition of Section 13362 to the Water Code by this act does not constitute a change in, but is declaratory of, the preexisting law.



CP-13

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
 (Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)



Court of Appeal, First District, Division 4, California.

CITY OF MODESTO REDEVELOPMENT
 AGENCY et al., Petitioners,

v.

The SUPERIOR COURT of San Francisco County,
 Respondent,
 The Dow Chemical Company et al., Real Parties in
 Interest.

No. A104367.

May 28, 2004.

As Modified on Denial of Rehearing June 28, 2004.
 Review Denied Sept. 15, 2004.^{FN*}

FN* Chin, J., did not participate therein.

Background: City and city redevelopment agency brought actions against dry cleaning solvent and equipment manufacturers and distributors, seeking damages based on claim that defendants were responsible for dry cleaners' discharge of environmentally damaging chlorinated solvents into public sewer systems. The Superior Court, City and County of San Francisco, Nos. 999345, 999643, Richard A. Kramer, J., granted defendants' motions for summary adjudication of causes of action for cost recovery under Polanco Redevelopment Act and negligence per se. City and agency petitioned for writ of mandate.

Holdings: The Court of Appeal, Rivera, J., held that:

- (1) those defendants which took affirmative steps directed toward discharge of solvent wastes could be subject to liability under Polanco Redevelopment Act, but those defendants which merely placed solvents in stream of commerce without warning of dangers of improper commerce could not be subject to such liability, and
- (2) same standards of liability governed cause of action for negligence per se.

Writ issued with directions.

West Headnotes

[1] **Environmental Law 149E** ↪ 445(1)

149E Environmental Law

149EIX Hazardous Waste or Materials

149Ek436 Response and Cleanup; Liability

149Ek445 Persons Responsible

149Ek445(1) k. In general. Most Cited

Cases

Those dry cleaning solvent and equipment manufacturers and distributors which took affirmative steps directed toward dry cleaners' discharge of solvent wastes into public sewer system or onto ground, such as instructing dry cleaners to set up equipment to facilitate such discharge, could be subject to liability for cleanup costs of environmental contamination under Polanco Redevelopment Act, but those manufacturers and distributors which merely placed solvents in stream of commerce without warning of dangers of improper commerce could not be subject to such liability. West's Ann.Cal.Health & Safety Code § 33459.4 (a); West's Ann.Cal.Water Code § 13304(a). See 4 *Witkin, Summary of Cal. Law (9th ed. 1987) Real Property, § 77A*; 8 *Miller & Starr, Cal. Real Estate (3d ed. 2001) § 23:57*.

[2] **Environmental Law 149E** ↪ 214

149E Environmental Law

149EV Water Pollution

149Ek214 k. Civil liability; cleanup costs.

Most Cited Cases

The Porter-Cologne Water Quality Act appears to be harmonious with the common law of nuisance. West's Ann.Cal.Water Code § 13000 et seq.

[3] **Nuisance 279** ↪ 9

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
 (Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

Therefor

279k9 k. Persons creating or causing nuisance. Most Cited Cases

Liability for nuisance does not hinge on whether the defendant owns, possesses or controls the property, nor on whether he is in a position to abate the nuisance; the critical question is whether the defendant created or assisted in the creation of the nuisance.

[4] Nuisance 279 ↪41

279 Nuisance

279I Private Nuisances

279I(D) Actions for Damages

279k41 k. Nature and form of remedy.

Most Cited Cases

The law of nuisance is not intended to serve as a surrogate for ordinary products liability.

[5] Nuisance 279 ↪9

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability

Therefor

279k9 k. Persons creating or causing nuisance. Most Cited Cases

Those who create or assist in creating a system that results in the unauthorized disposal of hazardous wastes, or who provide instructions on the disposal of those wastes, can be liable under the law of nuisance.

[6] Environmental Law 149E ↪214

149E Environmental Law

149EV Water Pollution

149Ek214 k. Civil liability; cleanup costs.

Most Cited Cases

Those dry cleaning solvent and equipment manufacturers and distributors which took affirmative steps directed toward dry cleaners' discharge of solvent wastes into public sewer system or onto ground, such as instructing dry cleaners to set up equipment to facilitate such discharge, could be

subject to liability for negligence per se based on a provision of the Porter-Cologne Water Quality Act which imposed liability for discharge of hazardous substance into state waters, but those manufacturers and distributors which merely placed solvents in stream of commerce without warning of dangers of improper commerce could not be subject to such liability. West's Ann.Cal.Water Code § 13350(b)(1).

****866 *31** Duane C. Miller, Sacramento, Michael D. Axline, A. Curtis Sawyer, Jr., Tracey L. O'Reilly, Tamarin E. Austin, Evan Eickmeyer, Sacramento, Daniel Boone, Miller, Axline & Sawyer, for Appellant.

No appearance, for Respondent.

Gary J. Smith, Alexia L. Beer, San Francisco, Mark A. Turco, Robert Brager, Beveridge & Diamond, P.C., for Real Party in Interest, PPG Industries, Inc.

Gennaro A. Filice, Oakland, Stephen J. Valen, Filice Brown Eassa & McLeod, LLP, for Real Party in Interest, The Dow Chemical Company.

Patrick L. Finley, Adam Friedenber, Walnut Creek, Glynn & Finley, LLP, for Real Party in Interest, E.I. du Pont De Nemours and Company.

Stephen C. Lewis, R. Morgan Gilhuly, Barg Coffin Lewis & Trapp, LLP, for Real Party in Interest, Occidental Chemical Corporation.

****867 *32** Christine K. Noma, Wendel, Rose, Black & Dean, Gene A. Weisberg, Melanie D. Long, Marina del Rey, Berger Kahn, for Real Party in Interest, Echco Sales and Equipment Co., Inc.

Edward R. Hugo, Roland E. Thé, Brydon Hugo & Parker LLP, William W. Burns, Los Gatos, Law Offices of William W. Burns, for Real Party in Interest, Goss-Jewett Company of Northern California.

Roger M. Mansukhani, Kristin N. Reyna, San Diego, Gordon & Rees, LLP, for Real Party in Interest, American Laundry Machinery Inc., Cooper

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

Industries.

A. Raymond Hamrick III, David L. Evans, Universal City, Kenneth A. Hearn, Encino, Hamrick & Evans, LLP, for Real Party in Interest, M.B.L., Inc.

James Colopy, San Francisco, Farella Braun & Martel LLP, for Real Party in Interest, Vulcan Materials Company.

Benjamin P. Klatsky, Peterson, Wilka, Weyand & Martin, for Real Party in Interest, Boewe Passat.

Alexander M. Weyand, Peterson Weyand & Martin LLP, for Real Party in Interest, Bowe Permac, Inc., Vic Manufacturing Company.

Richard S. Baron, Foley Baron & Metzger, PLLC, Peter Labrador, Leach McGreevy & Labrador, LLP, for Real Party in Interest, Hoyt Corporation.

RIVERA, J.

This case comes to us on a petition for extraordinary relief after the trial court granted summary adjudication to defendants, manufacturers and suppliers of dry cleaning solvents and equipment. We are called on to decide whether the Polanco Redevelopment Act (Health & Saf.Code, § 33459 et seq.) (the Polanco Act) allows a local agency to recover the costs of cleaning up hazardous substances from parties that did not directly discharge wastes, control the site of the discharge, or have authority to prevent the discharge of those substances. We grant the petition and direct the trial court to reconsider the motions for summary adjudication in light of the views expressed herein.

I. BACKGROUND

The City of Modesto Redevelopment Agency brought an action against numerous defendants, alleging causes of action for strict liability, negligence, *33 negligence per se, continuing trespass, private and public nuisance, private and public nuisance per se, response costs and declaratory relief under the Carpenter–Presley–Tanner Hazardous Substance Account Act (Health & Saf.Code, §

25300 et seq.), ultrahazardous activity, and cost recovery under the Polanco Act (case No. 999345). The City of Modesto, along with the City of Modesto Sewer District No. 1, brought another action against a nearly identical group of defendants seeking damages for solvent contamination under many of the same legal theories; this action did not include a Polanco Act cause of action (case No. 999643).^{FN1} The defendants included chlorinated solvent manufacturers, distributors of solvents and dry cleaning equipment, chlorinated solvent equipment manufacturers, and dry cleaning retailers. Before us on this petition are the trial court's rulings on the Polanco Act and negligence per se causes of action.

FN1. For the sake of convenience, we will refer to the plaintiffs in the two actions collectively as the City.

The complaints alleged that two cleaning solvents, perchloroethylene (PERC or PCE) and trichloroethylene, cause risks to health and the environment, that dry **868 cleaners customarily dumped solvent wastewater into the public sewer systems, and that dry cleaners experienced a habitual problem of chlorinated solvents leaking into the environment. According to the complaints, the defendants who manufactured and supplied solvents and equipment instructed dry cleaners that chlorinated solvents could be discharged into sewers, and/or failed to issue recalls or warnings regarding the equipment and solvents.

The manufacturer and distributor defendants filed motions for summary adjudication of the Polanco Act and negligence per se causes of action.^{FN2} The court granted summary adjudication on the Polanco Act cause of action to all but two of the moving defendants, concluding, among other things, that they neither discharged waste nor “ ‘cause[d] or permit[ted] any waste to be discharged....’ ” (Wat.Code, § 13304, subd. (a).) On the negligence per se causes of action, the trial court granted summary adjudication to all but one of the moving defendants, concluding they did not

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

dispose of PCE-containing products or wastes and did not exercise authority or control over the disposal *34 of such products or wastes by any Modesto dry cleaner. Pursuant to Code of Civil Procedure section 166.1, the trial court expressed its belief that the motions involved a controlling question of law as to which there were substantial grounds for difference of opinion, and that appellate resolution of the issue of law might materially advance the conclusion of the litigation.

FN2. The motions regarding the Polanco Act were brought by a group of defendants known as the Solvent Manufacturers (The Dow Chemical Company, PPG Industries, Inc., Occidental Chemical Corporation, and E.I. du Pont de Nemours and Company); the Equipment Defendants (American Laundry Machinery, Inc., Bowe Permac, Inc., Cooper Industries, as successor in interest to McGraw Edison Company, Hoyt Corporation, and Vic Manufacturing Company, joined by R.R. Street & Company); Vulcan Materials Company (a solvent manufacturer); and the Distributor Defendants (Echco Sales & Equipment Co., Inc., joined by M.B.L., Inc., and Goss-Jewett Company of Northern California). These motions were heard on August 8, 2003. The motions regarding the negligence per se causes of action were brought by the Solvent Manufacturers, the Equipment Defendants (with the exception of R.R. Street & Company), and Vulcan Materials Company. These motions were heard on August 15, 2003.

The City petitioned this court for a writ of mandate. On December 1, 2003, we issued an alternative writ of mandate, commanding the superior court to set aside its orders granting the motions for summary adjudication on the Polanco Act and negligence per se causes of action and enter a new order denying those motions, or show cause why it should not be compelled to do so. The superior

court declined to set aside the orders “in order to receive additional guidance from the Court of Appeal on the relevant issues,” and ordered the real parties in interest to show cause why the trial court should not be compelled to set aside the orders granting summary adjudication.^{FN3}

FN3. We will refer to the defendants who prevailed on the motions for summary adjudication as the prevailing defendants or simply as defendants.

II. DISCUSSION

A. The Polanco Act

The Polanco Act, enacted in 1990, authorizes redevelopment agencies to remediate contaminated properties within a project area. (*Redevelopment Agency of San Diego v. San Diego Gas & Electric Co.* (2003) 111 Cal.App.4th 912, 918, 4 Cal.Rptr.3d 317.) It provides in part that “if a redevelopment agency undertakes action to remedy or remove, or to require others to remedy or remove, ... a release of **869 hazardous substance, any responsible party or parties shall be liable to the redevelopment agency for the costs incurred in the action.” (Health & Saf.Code, § 33459.4, subd. (a); see also *Redevelopment Agency v. Salvation Army* (2002) 103 Cal.App.4th 755, 770, 127 Cal.Rptr.2d 30 (*Salvation Army*).)

The Polanco Act defines a “[r]esponsible party” as “any person described in subdivision (a) of Section 25323.5 of [the Health and Safety] Code or subdivision (a) of Section 13304 of the Water Code.” (Health & Saf.Code, § 33459, subd. (h).) Health and Safety Code section 25323.5 defines responsible parties as those described as covered persons in the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) (42 U.S.C. § 9607(a)).^{FN4} The City does not contend that the *35 prevailing defendants would be responsible under CERCLA. Instead, the issue here is whether the prevailing defendants are responsible parties under subdivision (a) of Water Code section 13304.^{FN5}

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

FN4. Title 42 United States Code section 9607(a) describes a covered person as “(1) the owner and operator of a vessel or a facility, [¶] (2) any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of, [¶] (3) any person who by contract, agreement, or otherwise arranged for disposal or treatment, or arranged with a transporter for transport for disposal or treatment, of hazardous substances owned or possessed by such person, by any other party or entity, at any facility or incineration vessel owned or operated by another party or entity and containing such hazardous substances, and [¶] (4) any person who accepts or accepted any hazardous substances for transport to disposal or treatment facilities, incineration vessels or sites selected by such person, from which there is a release, or a threatened release which causes the incurrence of response costs, of a hazardous substance....”

FN5. We are mindful there is language in *Salvation Army* indicating that “responsible party” under the Polanco Act is limited to those enumerated as responsible parties under CERCLA. In *Salvation Army* the court cited Health and Safety Code section 33459.4, subdivision (c), which provides in part: “The scope and standard of liability for cost recovery pursuant to this section shall be the scope and standard of liability under [CERCLA]....” Relying on this language, the court stated: “We construe that reference in the Polanco Act to CERCLA's scope of liability as simply incorporating CERCLA's definitions of who is liable for remedial costs.” (*Salvation Army*, *supra*, 103 Cal.App.4th at pp. 765–766, 127 Cal.Rptr.2d 30.) But this statement was not made in the context of a dispute over who was a responsible party;

rather, it was made in the context of the court *rejecting* the defendant's contention that the Polanco Act had adopted certain federal procedural requirements: “[W]e construe the Polanco Act's reference to CERCLA's standard of liability as merely incorporating the liability standards applied by courts in CERCLA cases.... In doing so, we reject Army's contention that the Polanco Act adopted various procedural requirements of the national contingency plan as an element of a cause of action for recovery of costs under the Polanco Act.” (*Id.* at p. 766, 127 Cal.Rptr.2d 30.) In fact, the question of whether responsible parties under the Polanco Act were limited to those responsible under CERCLA did not arise at all in *Salvation Army*; the parties disputed only whether the defendant landowner remained a responsible party after the plaintiff redevelopment agency had taken over the property and removed certain contaminated waste. (*Id.* at pp. 770–771, 127 Cal.Rptr.2d 30.) As has been noted, the Polanco Act on its face *does not* limit responsible parties to those enumerated in CERCLA. We therefore conclude that the cited language in *Salvation Army* is dictum (with which we disagree). We further note that neither the trial court nor defendants rely upon it to restrict the definition of “responsible party” under the Polanco Act.

The Porter–Cologne Water Quality Control Act (Wat.Code, § 13000 et seq.) (Porter–Cologne Act) provides in pertinent part: “Any person ... who has caused or permitted, causes or permits, or threatens to cause or permit any waste to be discharged or deposited where it is, or probably will be, discharged into the waters of **870 the state and creates, or threatens to create, a condition of pollution or nuisance, shall upon order of the regional board, clean up the waste or abate the effects of the waste, or, in the case of threatened pollution or nuisance, take

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

other necessary remedial action, including, but not limited to, overseeing cleanup and abatement efforts....” (Wat.Code, § 13304, subd. (a).) The question before us is whether the trial court was correct in ruling that, as a matter of law, the prevailing defendants did not cause wastes to be discharged or deposited.

The trial court concluded the prevailing Solvent Manufacturers and Equipment Defendants were not responsible parties under *36 Water Code section 13304 because the evidence showed they neither disposed of PCE-containing products or wastes nor exercised authority or control over the disposal of such products or wastes by any Modesto dry cleaner, and that the prevailing Distributor Defendants neither disposed of PCE waste in Modesto nor instructed, directed, or recommended that any Modesto-area dry cleaner dispose of chlorinated solvents on the ground or in the sewer. In explaining its ruling at the hearing on the motion, the trial court stated that in order for a party to “cause” a discharge for purposes of Water Code section 13304, “[Y]ou have to have some sort of physical control or the ability to stop it from happening.”

The City argues the trial court erred in concluding that only those who directly participated in or exercised authority or control over on-site activities or disposal activities could be considered responsible parties under Water Code section 13304. According to the City, we should apply the traditional tort “substantial factor” test in determining who has caused a discharge for purposes of Water Code section 13304. The prevailing defendants, not surprisingly, defend the trial court’s conclusion that a party must have the ability to control the discharge of waste to be liable under the Polanco Act.

“Well-established rules of statutory construction require us to ascertain the intent of the enacting legislative body so that we may adopt the construction that best effectuates the purpose of the law. [Citation.] We first examine the words themselves because the statutory language is generally the most reliable indicator of legislative intent. [Citation.]

The words of the statute should be given their ordinary and usual meaning and should be construed in their statutory context. [Citations.] These canons generally preclude judicial construction that renders part of the statute ‘meaningless or inoperative.’ [Citation.] In addition, words should be given the same meaning throughout a code unless the Legislature has indicated otherwise. [Citations.]” (*Hasan v. Mercy American River Hospital* (2003) 31 Cal.4th 709, 715–716, 3 Cal.Rptr.3d 623, 74 P.3d 726.) Where the words of a statute do not have a “plain meaning,” statutory construction is necessary. (*Jacobs, Malcolm & Burt v. Voss* (1995) 33 Cal.App.4th 1399, 1404, 39 Cal.Rptr.2d 774.) In interpreting a statute, “[c]ourts generally give great weight and respect to an administrative agency’s interpretation of a statute governing its powers and responsibilities.” (*Ibid.*) Courts may also look to the legislative history in discerning the intent of the Legislature. (See *Moradi-Shalal v. Fireman’s Fund Ins. Companies* (1988) 46 Cal.3d 287, 300–301, 250 Cal.Rptr. 116, 758 P.2d 58.)

[1] Thus, we first ask, does the plain language of Water Code section 13304, subdivision (a) tell us who is a responsible party? The statute imposes liability on anyone who causes or permits a discharge or deposit of wastes; *37 however, it does not indicate whether “cause” refers to a **871 party who was directly involved with a discharge, to anyone whose actions were a substantial factor in causing the discharge, or even, as city argued below, to anyone who places a hazardous substance into the chain of commerce.

In considering this issue, we are guided by *Leslie Salt Co. v. San Francisco Bay Conservation etc. Com.* (1984) 153 Cal.App.3d 605, 200 Cal.Rptr. 575 (*Leslie Salt*). There, Division Two of the First Appellate District considered whether a landowner on whose land fill had been placed, without the landowner’s knowledge, could be required to remove the fill and be subjected to penalties under the McAteer–Petris Act (Gov.Code, § 66600 et seq.), as one who “has undertaken, or is

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

threatening to undertake” unauthorized fill activity (Gov.Code, § 66638, subd. (a)). The court stated: “It needs to be emphasized at this point that the McAteer–Petris Act is the sort of environmental legislation that represents the exercise by government of the traditional power to regulate public nuisances. (*CEED v. California Coastal Zone Conservation Com.* (1974) 43 Cal.App.3d 306, 318 [118 Cal.Rptr. 315]....) Such legislation ‘constitutes but “a sensitizing of and refinement of nuisance law.”’ (*Id.*, at p. 319 [118 Cal.Rptr. 315].) Where, as here, such legislation does not expressly purport to depart from or alter the common law, it will be construed in light of common law principles bearing upon the same subject. [Citations.]” (*Leslie Salt*, at pp. 618–619, 200 Cal.Rptr. 575.)^{FN6} Noting that under the common law, a landowner’s liability for a public nuisance could result from the failure to act as well as from affirmative conduct, the court concluded that a landowner could be liable under the McAteer–Petris Act even if it was not actively involved in the condition that caused harm, and even if it did not know of or intend to cause such harm. (*Leslie Salt*, at pp. 619, 622, 200 Cal.Rptr. 575.) This liability could include both responsibility to obey a cease and desist order, and civil fines on a per-day basis for violating the order. (*Id.* at p. 618, 200 Cal.Rptr. 575.)

FN6. The court in *CEED* stated: “Contemporary environmental legislation represents an exercise by government of this traditional power to regulate activities in the nature of nuisances....” (*CEED v. California Coastal Zone Conservation Com.*, *supra*, 43 Cal.App.3d at p. 318, 118 Cal.Rptr. 315.)

[2] The Porter–Cologne Act similarly appears to be harmonious with the common law of nuisance. Water Code section 13304, subdivision (a) authorizes cleanup or abatement orders against a person who “has caused or permitted, causes or permits, or threatens to cause or permit any waste to be discharged or deposited where it is, or probably

will be, discharged into the waters of the state and creates, or threatens to create, a condition of pollution or nuisance” (Italics added.) The Porter–Cologne Act defines “ ‘[n]uisance’ ” to mean “anything which meets all of the following requirements: [¶] (1) Is injurious to health, or is indecent or offensive to the senses, or an obstruction of the free use of property, so as to interfere with the comfortable *38 enjoyment of life or property. [¶] (2) Affects at the same time an entire community or neighborhood, or any considerable number of persons, although the extent of the annoyance or damage inflicted upon individuals may be unequal. [¶] (3) Occurs during, or as a result of, the treatment or disposal of wastes.” (Wat.Code, § 13050, subd.(m).) The first two paragraphs of this definition track relevant portions of the language of Civil Code sections 3479 and 3480, which define nuisance and public nuisance. The third paragraph establishes that the Porter–Cologne Act regulates only nuisances **872 that are connected with the treatment or disposal of wastes. Thus, it appears that the Legislature not only did not intend to depart from the law of nuisance, but also explicitly relied on it in the Porter–Cologne Act.

[3] Having concluded that the statute must be construed “in light of the common law principles bearing upon the same subject” (*Leslie Salt*, *supra*, 153 Cal.App.3d at p. 619, 200 Cal.Rptr. 575)—here the subject of public nuisance—we turn next to identify those principles. It has long been the law in California that “ ‘[n]ot only is the party who maintains the nuisance liable but also the party or parties who create or assist in its creation are responsible for the ensuing damages.’ ” (*Mangini v. Aerojet–General Corp.* (1991) 230 Cal.App.3d 1125, 1137, 281 Cal.Rptr. 827.) Thus, courts have upheld as against a demurrer a nuisance claim founded upon allegations that defendants disposed of hazardous substances on property during their lease, but at the time of the action did not have a possessory interest in the property (*id.* at pp. 1132–1133, 1137, 281 Cal.Rptr. 827); and on allegations that defendant soils engineer prepared a plan for slope

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

repair on a neighboring property which, when constructed, caused water, mud, and debris to flow onto the plaintiff's property (*Shurpin v. Elmhirst* (1983) 148 Cal.App.3d 94, 100–101, 195 Cal.Rptr. 737). Similarly, a nonsuit on plaintiff's cause of action for nuisance was reversed where the evidence showed defendant contractor dumped fill on a street, interfering with drainage and causing the plaintiff's property to be flooded. (*Portman v. Clementina Co.* (1957) 147 Cal.App.2d 651, 654, 659–660, 305 P.2d 963.) And the Supreme Court has held that a defendant who obstructs a private road can be liable for nuisance, irrespective of whether he claims any interest in the land over which the plaintiff claimed a right of way. (*Hardin v. Sin Claire* (1896) 115 Cal. 460, 462–463, 47 P. 363.) In sum, liability for nuisance does not hinge on whether the defendant owns, possesses or controls the property, nor on whether he is in a position to abate the nuisance; the critical question is whether the defendant created or assisted in the creation of the nuisance. (*Newhall Land & Farming Co. v. Superior Court* (1993) 19 Cal.App.4th 334, 343, 23 Cal.Rptr.2d 377.)

*39 While liability for nuisance is broad,^{FN7} however, it is not unlimited. *City of San Diego* established one important limitation. There, the city brought an action on various theories, including nuisance, against defendants who manufactured, distributed or supplied asbestos-containing building materials, alleging asbestos had contaminated city buildings and seeking recovery for, among other things, money the city spent to identify and abate the asbestos danger. (*City of San Diego, supra*, 30 Cal.App.4th at pp. 578–579, 35 Cal.Rptr.2d 876.) The Court of Appeal concluded the city could not maintain an action based on nuisance, stating, “City cites no California decision ... that allows recovery for a defective product under a nuisance cause of action. Indeed, under City's theory, nuisance ‘would become a monster that would devour in one gulp the entire law of tort...’ (*Tioga Public School Dist. v. U.S. Gypsum* (8th Cir.1993) 984 F.2d 915, 921.)” (*Id.* at p. 586, 35 Cal.Rptr.2d 876.) The court

also noted that other jurisdictions**873 considering the issue had not allowed plaintiffs to recover on a nuisance theory for defective asbestos-containing building materials. (*Ibid.*, citing *Tioga Public School Dist. v. U.S. Gypsum, supra*, 984 F.2d at pp. 920–921, *Detroit Bd. of Educ. v. Celotex Corp.* (Mich.App.1992) 196 Mich.App. 694, 493 N.W.2d 513, 520–522, *Town of Hooksett School Dist. v. W.R. Grace Co.* (D.N.H.1984) 617 F.Supp. 126, 133, *Johnson County, Tenn. v. U.S. Gypsum Co.* (E.D.Tenn.1984) 580 F.Supp. 284, 294 [stating that allowing such a nuisance action “ ‘would convert almost every products liability action into a nuisance claim’ ”].) The court concluded this was “a products liability action in the guise of a nuisance action” (*City of San Diego, supra*, 30 Cal.App.4th at pp. 586–587, 35 Cal.Rptr.2d 876), and affirmed summary judgment in favor of the defendants (*id.* at p. 590, 35 Cal.Rptr.2d 876).

FN7. As stated in *City of San Diego v. U.S. Gypsum Co.* (1994) 30 Cal.App.4th 575, 585, 35 Cal.Rptr.2d 876 (*City of San Diego*), “Nuisance has been described as an ‘impenetrable jungle.’ (Prosser & Keeton, *Law of Torts* (5th ed.1984) § 86, p. 616.) ‘[Nuisance] has meant all things to all people, and has been applied indiscriminately to everything from an alarming advertisement to a cockroach baked in a pie. There is general agreement that it is incapable of any exact or comprehensive definition.’ (*Ibid.*, fns. omitted.)”

[4] We agree with *City of San Diego* that the law of nuisance is not intended to serve as a surrogate for ordinary products liability.^{FN8} In light of that conclusion, the question we face here is whether the Polanco Act claims *40 fall within the realm of nuisance or of products liability; stated another way, has city presented evidence that the defendants assisted in the creation of a nuisance, or only that they produced or supplied defective products?

FN8. We are aware that some courts have concluded an action for nuisance may be

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

maintained against manufacturers, distributors, and dealers of guns on the theory that they created, participated in, or facilitated the flow of guns into a market that targeted illegal gun purchasers. (See, e.g., *Ileto v. Glock Inc.* (9th Cir.2003) 349 F.3d 1191, 1209–1215; *Cincinnati v. Beretta U.S.A. Corp.* (Ohio 2002) 95 Ohio St.3d 416, 768 N.E.2d 1136, 1142–1144; *Gary ex rel. King v. Smith & Wesson, Corp.* (Ind.2003) 801 N.E.2d 1222, 1231–1234, and cases cited therein.) Our research reveals no California state cases holding such defendants liable for causing a nuisance. In any event, the theory in those cases was not that the products were defective or that the defendants failed to warn of their dangers. (See *Ileto v. Glock Inc.*, *supra*, 349 F.3d at p. 1213, fn. 29 [distinguishing *City of San Diego* on ground that action against gun defendants was not “ ‘a products liability action in the guise of a nuisance action’ ”].)

We look first to *Selma Pressure Treating Co. v. Osmose Wood Preserving Co.* (1990) 221 Cal.App.3d 1601, 271 Cal.Rptr. 596 (*Selma*), which applied the law of nuisance to a similar case. There, the State of California and the Regional Water Quality Control Board (collectively, the State) sued the defendants, operators of a wood treatment facility, alleging they improperly disposed of hazardous waste and seeking, among other things, damages flowing from a nuisance. (*Id.* at pp. 1606, 1608, 271 Cal.Rptr. 596.) The defendants cross-complained, seeking equitable indemnity from several cross-defendants. One was a company that designed the wood treatment technique, installed cross-complainants' equipment, provided training and made recommendations on operating policies that resulted in wood-treating chemicals being deposited into soil overlying an aquifer. Other cross-defendants included chemical suppliers that provided “assistance and advice” and knew or should have known of the potential health threats

posed by improper use or disposal of the chemicals, but failed to warn of those risks. (*Id.* at pp. 1607, 1609, 271 Cal.Rptr. 596.)

The Court of Appeal concluded the cross-complainants had pled, or could plead, facts showing the cross-defendants might be liable for the nuisance—specifically, that the installer of the equipment recommended creation of an unlined dirt pond for disposing of the waste products; that it knew or should have known that such disposal could threaten the safety of the water supply; that the cross-complainants**874 did not know of the danger; and that the installer failed to warn of that danger. The court reasoned that this kind of direct involvement in the design and installation of the disposal system, coupled with the installer's knowledge and the user's lack of knowledge of the dangers, could support a finding that the designer/installer created or assisted in the creation of a nuisance. (*Selma, supra*, 221 Cal.App.3d at p. 1620, 271 Cal.Rptr. 596.)

The involvement of the chemical companies was less direct, but the court concluded they, too, could be held liable. The cross-complaint alleged: as direct purchasers of the chemicals, the owners (cross-complainants) were foreseeable users; disposal of the chemical residue was a foreseeable use of the product; the chemical companies knew or should have known of the dangers of improper disposal of the chemicals; the owners did not know of those dangers; the companies failed to warn of the dangers; and that failure to warn was a substantial factor in causing the damage. (*Selma, supra*, 221 Cal.App.3d at pp. 1621–1624, 271 Cal.Rptr. 596.)

[5] We agree with the first stated conclusion in *Selma*—that those who create or assist in creating a system that causes hazardous wastes to be disposed *41 of improperly, or who instruct users to dispose of wastes improperly, can be liable under the law of nuisance. Here, for example, the City claims that, with knowledge of the hazards involved, some of the defendants instructed the dry cleaners to set up their equipment to discharge solvent-containing

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

wastewater into the drains and sewers, and that others gave dry cleaners instructions to dispose of spilled PERC on or in the ground. We conclude that these kinds of affirmative acts or instructions could support a finding that those defendants assisted in creating a nuisance, and therefore would defeat a summary adjudication motion on the Polanco Act cause of action.

Defendants argue the circle of liability should be drawn more tightly, pointing out that the only parties the State Water Resources Control Board (State Board) has held liable for penalties or cleanup costs were those that controlled either the discharge activity or the premises where the discharge occurred. (See, e.g., *In re Exxon Company, U.S.A.* (Order No. WQ 85-7, Aug. 22, 1985) 1985 WL 20026 at pp. *1, 6-7 (Cal.St.Wat.Res.Bd.) [oil company and gasoline distributor not properly named where there was no reasonable evidence they owned gasoline tanks that leaked]; *In re Spitzer* (Order No. WQ 89-8, May 16, 1989) 1989 WL 97148 at pp. *3-4 (Cal.St.Wat.Res.Bd.) [landowners who know of discharge on their property and have sufficient control of the property to correct it are subject to a cleanup order]; *In re Stuart* (Order No. WQ 86-15, Sept. 18, 1986) 1986 WL 25522 at pp. *3-5 (Cal.St.Wat.Res.Bd.) [lessee of property did not cause discharge under Water Code section 13304, but he permitted it because he had legal power to stop the contamination].) While *In re Exxon* does suggest that a party who merely supplies a hazardous substance is not responsible under Water Code section 13304, the authorities defendants rely on are of limited value in assessing the responsibility of a party that instructs users to dispose of hazardous wastes in an unsafe manner or a party that creates a system that would result in improper disposal of hazardous wastes. Furthermore, the State Board has concluded that even a relatively minor contribution to a discharge may support a finding of responsibility. For instance, in *In re County of San Diego* (Order No. WQ 96-2, Feb. 22, 1996) 1996 WL 101751 at p. *5 (Cal.St.Wat.Res.Bd.), the State Board ruled that the

Regional Water Quality Control Board had properly treated a city as a discharger,**875 solely because the city had an easement over and authority to control a street that overlay part of a landfill, and subsidence of landfill material beneath the roadway was contributing to runoff coming from the street to the landfill surface, which in turn was adversely affecting water quality beneath the site.

Thus, we disagree with defendants' contention that only those who are physically engaged in a discharge or have the ability to control waste disposal activities are liable under section 13304. In harmony with *Selma*, we *42 think a reasonable fact finder might conclude that defendants who manufactured equipment designed to discharge waste in a manner that will create a nuisance, or who specifically instructed a user to dispose of wastes in such a manner, could be found to have caused or permitted a discharge.

With respect to *Selma's* second stated conclusion—the potential liability of defendants who fail to warn of the dangers of improper disposal of hazardous materials but give no guidance or instructions pertaining to that disposal—we face a more difficult question. In this case the involvement of certain defendants was limited to manufacturing or selling solvents to dry cleaners, with knowledge of the hazards of those substances, without alerting the dry cleaners to proper methods of disposal. The City's theory that these suppliers should be held liable is similar to that proffered by the plaintiff in *City of San Diego*: “City claims the manufacturer of an allegedly defective product can be liable in nuisance ... because ‘[t]he stream of commerce can carry pollutants every bit as effectively as a stream of water.’ ” (*City of San Diego, supra*, 30 Cal.App.4th at pp. 584-585, 35 Cal.Rptr.2d 876.) As did the court in *City of San Diego*, we reject this contention.

Here, any failure to warn was not an activity directly connected with the disposal of solvents. In our view, such behavior is analogous to the manufacture, distribution, and supplying of asbestos-

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

containing materials in *City of San Diego*; it does not fall within the context of nuisance, but is better analyzed through the law of negligence or products liability, which have well-developed precedents to determine liability for failure to warn. (See, e.g., *Carlin v. Superior Court* (1996) 13 Cal.4th 1104, 1110, 56 Cal.Rptr.2d 162, 920 P.2d 1347; *Anderson v. Owens-Corning Fiberglas Corp.* (1991) 53 Cal.3d 987, 995–1003, 281 Cal.Rptr. 528, 810 P.2d 549; *Artiglio v. General Electric Co.* (1998) 61 Cal.App.4th 830, 835, 71 Cal.Rptr.2d 817.)^{FN9}

FN9. The *Selma* court's reasoning in holding the supplier-defendants potentially liable is not entirely clear. As noted, in *Selma* the state sued the defendants who discharged hazardous waste alleging a cause of action for nuisance. The defendants cross-complained against their codefendants—among them, their chemical suppliers—for equitable indemnity. (*Selma, supra*, 221 Cal.App.3d at pp. 1606–1607, 271 Cal.Rptr. 596.) Recognizing that an equitable indemnity claim requires the cross-defendants to have potential joint and several liability to the *plaintiff*, the Court of Appeal posed the question “whether the pleadings adequately plead ... facts which suggest ... the chemical suppliers created or assisted in the creation of the nuisance here.” (*Id.* at p. 1620, 271 Cal.Rptr. 596.) However, in answering the question, and holding cross-complainants could state a claim against the chemical suppliers, the court relied solely upon a classic negligence/failure to warn theory. (*Id.* at pp. 1621–1624, 271 Cal.Rptr. 596.) We therefore read *Selma* to mean that a defendant sued in nuisance and subjected to liability for nuisance damages, may cross-complain against codefendants or third parties under other appropriate theories, such as products liability or failure to warn. If *Selma* is interpreted as holding that one who merely supplies a product

and fails to warn of the hazards of improper disposal can be liable under the law of nuisance, we would disagree with it.

*43 Thus, construing Water Code section 13304, subdivision (a) “in light of the common law principles bearing upon [nuisance]” **876(*Leslie Salt, supra*, 153 Cal.App.3d at p. 619, 200 Cal.Rptr. 575), we conclude that those who took affirmative steps directed toward the improper discharge of solvent wastes—for instance, by manufacturing a system designed to dispose of wastes improperly or by instructing users of its products to dispose of wastes improperly—may be liable under that statute, but those who merely placed solvents in the stream of commerce without warning adequately of the dangers of improper disposal are not liable under that section of the Porter-Cologne Act.

We have reviewed the legislative history of the relevant portions of the Polanco Act and the Porter-Cologne Act, and see nothing inconsistent with this result. Indeed, the legislative history of the “causes or permits” language in a different provision within the Porter-Cologne Act, Water Code section 13350, supports our conclusion that the Legislature did not intend the act to impose liability on those with no ownership or control over the property or the discharge, and whose involvement in a discharge was remote and passive. The phrase “causes or permits” was added to the statute in 1971, in an amendment providing civil penalties for those who, among other things, caused or permitted waste or oil to be discharged into the waters of the state. (Stats.1971, ch. 668, § 1, p. 1322; see Stats.1969, ch. 482, § 18, p. 1070.) The Department of Finance enrolled bill report stated, “Effects of this bill would be (1) waste dischargers would be more careful in their operations and (2) some funds would be provided for cleanup of anonymous oil spills.” (Cal. Dept. of Finance, Enrolled Bill Rep. on Sen. Bill No. 225 (1971 Reg. Sess.) Aug. 12, 1971.)

Water Code section 13350 was again amended in 1980, to authorize imposition of civil liabilities

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

on “[a]ny person who, without regard to intent or negligence, causes or permits” a discharge of hazardous substances into the waters of the state. (Stats.1980, ch. 877, § 3, p. 2754.) The statute also provided there would be no liability if the discharge were caused by events beyond the discharger’s control, including any “circumstance or event which causes the discharge despite the exercise of every reasonable precaution to prevent or mitigate the discharge.” (*Id.* at p. 2755.) An enrolled bill report on this revision stated: “This bill would provide a higher standard of liability for anyone who discharges a reportable quantity of a hazardous substance in or on the State’s waters where it creates a condition of pollution or nuisance.... [¶] ... [¶] The imposition of this higher standard of care will provide a greater incentive for hazardous waste handlers to avoid spills.” (Cal. Environmental Quality Agency, Enrolled Bill Rep. on Assem. Bill No. 2823 (1979–1980 Reg. Sess.) Sept. 5, 1980, pp. 1–2.) Thus, it appears section 13350 was intended to encourage hazardous waste handlers to be careful in their operations and to avoid spills. Persons who had no active involvement in activities leading to a discharge do not appear to fall into this category.

*44 Two other provisions within the Porter–Cologne Act are also instructive. Water Code section 13271, subdivision (a)(1) requires any person who “without regard to intent or negligence, causes or permits” any hazardous substance to be discharged on the waters of the state, to notify the Office of Emergency Services as soon as possible after that person has knowledge of the discharge. Failure to do so is a misdemeanor, punishable by a fine or imprisonment for not more than one year. (*Id.*, subd. (c).) Water Code section 13272, subdivisions (a) and (c) make it a misdemeanor for one who causes or permits a discharge of oil or petroleum products into the waters of the state to fail to notify the Office of Emergency Services as soon as possible after having knowledge of the discharge. A Department of Fish and Game report stated that section 13271 would “require[] a spiller of a hazardous substance, with certain exceptions, to imme-

diately notify the Office of Emergency Services of **877 such a spill....” (Cal. Dept. of Fish & Game, Rep. on Assem. Bill No. 2823 (1979–1980 Reg. Sess.) May 2, 1980.) A bill analysis prepared by the Department of Conservation indicated that section 13272 would “require any person in charge of a vessel or facility to report a spill as soon as possible,” and that “the penalty provisions set forth in AB 2281 should provide adequate incentive for a spiller to promptly report such an incident.” (Cal. Dept. of Conservation, Analysis of Assem. Bill No. 2281 (1981–1982 Reg. Sess.) Nov. 10, 1981, p. 1.) Thus, we see no indication the Legislature intended the words “causes or permits” within the Porter–Cologne Act to encompass those whose involvement with a spill was remote and passive.

In light of the ongoing nature of this case, and the trial court’s familiarity with the parties and the evidence, we will leave it to the trial court to apply the standards articulated in this decision to the facts in the first instance. The trial court is directed to reconsider the motions for summary adjudication of the Polanco Act cause of action in accordance with the views expressed herein.^{FN10}

FN10. In reaching our conclusion, we do not limit any other remedies available to either the City or to any party who is held liable for the cleanup. In fact, this case includes causes of action for negligence and strict liability, which remain to be tried. Nothing in this ruling is intended to affect those causes of action.

B. Negligence Per Se

[6] The City also challenges the trial court’s action in granting summary adjudication of the negligence per se causes of action. These causes of action allege violations of seven statutes: Water Code sections 13050, subdivision (m), 13350, and 13387; Health and Safety Code sections 5411, 5411.5, and 117555; and Fish and Game Code section 5650. In its briefing before this court, however, the City analyzes only Water Code section 13350. We will *45 not consider the other alleged statutory violations.

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452
(Cite as: 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865)

(See *Badie v. Bank of America* (1998) 67 Cal.App.4th 779, 784–785, 79 Cal.Rptr.2d 273 [point not supported by reasoned argument and citations to authority is treated as waived].)

Water Code section 13350, subdivision (b)(1), a part of the Porter–Cologne Act, makes liable any person who “causes or permits any hazardous substance to be discharged in or on any of the waters of the state....” The City argues that the substantial factor test for causation should be used to determine whether defendants caused a hazardous substance to be discharged in violation of this statute. Our views regarding the meaning of the words “causes or permits” in the Porter–Cologne Act are fully explained above, and we need not repeat them here. The trial court is directed to reconsider the motions for summary adjudication of the negligence per se causes of action based on Water Code section 13350 in light of the views expressed herein.

III. DISPOSITION

Let a writ of mandate issue directing the superior court to vacate and set aside its orders of October 17, 2003, granting the prevailing defendants' motions for summary adjudication on the Polanco Act and negligence per se causes of action, and further directing the superior court to reconsider the motions for summary adjudication in accordance with the views expressed herein. The City of Modesto Redevelopment Agency, the City of Modesto, and the City of Modesto Sewer District No. 1 shall recover their costs on appeal.

We concur: KAY, P.J., and REARDON, J.

Cal.App. 1 Dist., 2004.

City of Modesto Redevelopment Agency v. Superior Court

119 Cal.App.4th 28, 13 Cal.Rptr.3d 865, 04 Cal. Daily Op. Serv. 4692, 2004 Daily Journal D.A.R. 6452

END OF DOCUMENT

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

C

ARNOLD CLEJAN et al., Plaintiffs and Appellants,
v.
SAMUEL REISMAN, Defendant and Appellant

Civ. No. 33406.

Court of Appeal, Second District, Division 3, California.
March 11, 1970.

SUMMARY

Plaintiffs financed the purchase of a ranch located in Nevada and Utah with funds advanced by California investors and transferred to the investors a document purportedly transferring to each undescribed interests in the ranch on the basis of 1 percent of the property for each \$5,000 invested. A Nevada corporation was formed with plaintiff and his wife as directors and plaintiff as president. A 90 percent interest in the ranch was then transferred to the corporation subject to its assumption of plaintiff's obligations. The remaining 10 percent interest was then sold to two defendants with the money to be used to pay off other investors. Defendants contracted, without knowing the corporation had been formed, to convey their 10 percent interest to the corporation when formed in exchange for stock. Friction developed between plaintiff and the investors and one of the defendants loaned the corporation money to repay the investors in return for a transfer of a portion of the stock of plaintiff and his wife (also a plaintiff) to defendant and his attorney, another defendant and the appellant in the suit later brought. Plaintiffs were then ousted as directors and officers and defendants took control of the corporation. The attorney and another of the defendants agreed in California to purchase plaintiffs' remaining shares. Following default in payment, plaintiffs sued for the payments due and recovered judgment. (Superior Court of Los Angeles County, Allen T. Lynch, Judge.)

On appeal, the judgment was affirmed in all respects except as to an award of attorney's fees, which represented an allowance of about \$6 per hour. This matter was remanded to the trial court for a determination of the reasonable value of the services rendered. Defendant attorney contended on appeal that plaintiffs organized the corporation as a speculative scheme to acquire land for resale to the public. Defendant claimed that passive California investors financed the venture and received in return securities within the meaning of the Corporate Securities Law, and that, as a result of the sale of the securities in California without a permit, the stock thereafter issued, including the shares sold to defendants, was void. Defendant further contended that the agreement to purchase plaintiffs' remaining stock was voidable at the option of defendants and that defendant was entitled to recover the sum previously paid to plaintiffs. The Court of Appeal held that the transactions whereby California investors advanced cash in return for escrow agreements purportedly transferring undescribed interests in the ranch constituted sales of securities and the interests were void as having been made without a permit. However, it was also held that the illegal transaction did not invalidate the subsequently issued stock since the transfers to the California investors were never consummated. Further, it was held that when plaintiffs sold their stock to defendants they were not the *alter ego* of the corporation and that the stock was sold as their own property for which no permit was required. (Opinion by Schweitzer, J., with Cobey, Acting P. J., and Allport, J., concurring.)

HEADNOTES

Classified to California Digest of Official Reports
(1) Appeal § 1244(2)--Questions of Law and Facts--Presumptions and Inferences.

Even where the probative facts are undisputed, the inferences to be drawn therefrom are still within the trial court's exclusive province; and where any substantial evidence supports them, the appellate

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

court is bound by the trial court's determination.

(2) Corporations § 167(1)--Corporate Securities Act--Security.

In the statutory definition of a security stating that a security "includes all of the following," the use of the word "includes" suggests that the items mentioned were intended to be illustrative and that the law was intended to embrace unnamed items similar to those listed.

(3) Corporations § 165.1--Corporate Securities Act--Purpose.

The regulatory purpose of the Corporate Securities Act is not to be vitiated by inventive substitutes for conventional means of raising risk capital.

(4) Corporations § 179--Corporate Securities Act--Effect of Want of Permit--Evidence.

Transactions whereby California investors advanced cash to plaintiffs in return for escrow agreements purportedly transferring undescribed interests in ranch property in Nevada and Utah on the basis of 1 percent of the property for each \$5,000 invested constituted sales of securities within the meaning of the Corporate Securities Law, and the interests sold were void as having been made without a permit.

(5) Corporations § 175(5)--Corporate Securities Act--Effect of Want of Permit--Stock in Foreign Corporations.

Prior illegal transactions will not invalidate subsequently issued stock, and where plaintiffs owned a ranch located in Nevada and Utah, subject to encumbrances and the claims of California investors, and transferred the ranch to a Nevada corporation, the invalid transactions with the California investors involving a sale of securities without a permit had no effect on the validity of the stock, since the transfers to the California investors were never consummated.

[Statutory requirements respecting issuance of stock as applicable to foreign corporations, note, 8 A.L.R.2d 1185.]

(6a, 6b) Corporations § 168--Corporate Securities

Act--Sales.

The trial court properly found that defendants' agreement to purchase plaintiffs' stock in a Nevada corporation covered the sale of securities exempt from the requirement of a permit, that the transaction was not illegal, and that the parties were not *in pari delicto* where, at the date of the agreement, 13 months after issuance of the stock and one year after defendants became the majority stockholders and took over management of the corporation, plaintiffs could not be deemed the *alter ego* of the corporation and sold their stock as their own property for their own account without any scheme or intent to violate the Corporate Securities Law.

(7) Pleading § 265--Issues.

When the facts of a case present an issue of illegality of a contract, it must be considered by the court, whether pleaded or not; the court may raise the issue on its own motion.

(8) Corporations § 6(2)--Disregard of Corporate Entity--Prevention of Fraud and Injustice.

Though the doctrine of ignoring a corporate entity that is the *alter ego* of individuals does not depend on the presence of actual fraud, the doctrine is designed to prevent what would be fraud or injustice if accomplished; accordingly, bad faith in one form or another is an underlying consideration and will be found in some form or another in cases in which the trial court was justified in disregarding the corporate entity.

[See Cal.Jur.2d, Corporations, § 8; Am.Jur.2d, Corporations, § 14 et seq.]

(9) Corporations § 6(1)--Disregard of Corporate Entity--When Power Will Be Exercised.

Conditions under which a corporate entity may be disregarded vary according to the circumstances in each case.

(10) Accord and Satisfaction § 2--Requisites.

For an accord and satisfaction to be effected, there must be a bona fide dispute as to the amount due.

(11) Evidence § 186--Admissions--Judicial Admis-

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

sions.

A party is bound by an agreed statement of facts and evidence contrary thereto is inadmissible.

(12a, 12b) Attorneys at Law §
108--Compensation--Amount.

An award of \$3,000 in attorney's fees was wholly inadequate and an abuse of discretion, requiring a remand for redetermination of the reasonable value of services rendered, where counsel informed the court that 468 hours were spent by members of his office in preparing the case for trial and that, in addition, two firm members were present in court during the eight days of trial, thus allowing only \$6 per hour.

(13) Attorneys at Law §
112--Compensation--Remedies.

Testimony or other direct evidence of the reasonable value of an attorney's services need not be introduced, the knowledge and experience of the trial judge being sufficient.

(14) Attorneys at Law §
131(6)--Compensation--Appeal--Finding of Value of Services.

Where the parties' contracts provide for attorneys' fees to the successful litigant, such provision covers fees on appeal and may be determined by either the appellate court or the trial court at the time it determines costs.

COUNSEL

Schwartz & Alschuler, Benjamin F. Schwartz, Herbert A. Karzer and Irving L. Halpern for Plaintiffs and Appellants.

Ball, Hunt, Hart & Brown, Ball, Hunt, Hart, Brown & Baerwitz, Joseph A. Ball, Joseph D. Mullender, Jr., and Frederic G. Marks for Defendant and Appellant. *228

SCHWEITZER, J.

Action by plaintiffs on a contract for the sale by plaintiffs to defendants of 350 shares of the cap-

ital stock of Gamble Ranch Investments, Inc.

Plaintiffs Arnold Clejan and Katherine Clejan, husband and wife, are the respondents and cross-appellants herein. Defendants Joe Benaron and J. J. Byrnes entered into a settlement with plaintiffs before trial and are no longer parties to this action. The remaining defendant, Samuel Reisman, is the appellant and cross-respondent herein.

Because of defendant Reisman's contentions that various transactions were in violation of the Corporate Securities Law and that the stock sold by the contract was therefore void, a detailed chronology of the facts behind the contract is necessary. In May 1959 plaintiff Arnold Clejan agreed to buy for \$2,500,000 the Gamble Ranch, some 236,000 acres located in Nevada and Utah, with annexed grazing rights of approximately 370,000 acres. It was his intention to subdivide and sell parcels of the land. Terms of sale were a cash down payment of \$70,000, the assumption of an indebtedness on the property of approximately \$230,000, the execution of a promissory note to the seller in the sum of \$1,973,000 and the payment of a portion of the real estate brokers' commissions. Two California residents, Omansky and Klein, advanced Clejan \$50,000, and another California resident, Rosenberg, advanced him \$20,000 to make the \$70,000 down payment. Clejan, Omansky and Klein agreed that Clejan was to own one-half of the venture and was to manage the subdividing and sale of the property; Omansky and Klein were each to own one-quarter interests.

It developed thereafter that Clejan needed additional capital to obtain a deed to the land and to establish a real estate office from which he could sell the land as it was subdivided. During June and July 1959 he solicited and obtained a total of \$85,000 from nine California residents, including an additional \$5,000 from Rosenberg, in return for which he delivered to each a document denoted as an escrow agreement which purportedly transferred to each undescribed interests in the Gamble Ranch on the basis of 1 percent of the property for each

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

\$5,000 invested. At trial Clejan and five of the nine investors testified that their original agreement was for the purchase and sale of land, that nothing was said about stock, and that the reason for their investment was an expectation of profit upon resale of the land by Clejan. Only one investor testified that the agreement involved the sale of stock.

Sometime in July 1959 Clejan entered into an agreement with Omansky *229 and Klein to purchase their interest in the venture for the amount of their initial \$50,000 investment. He gave them a down payment of \$15,000.

On August 13, 1959 Clejan formed a Nevada corporation, known as Gamble Ranch Investment, Inc., with himself, his wife and Rosenberg as directors. Clejan was elected president at the August 31, 1959 organizational meeting and by resolution was given full authority to act for the corporation on all corporate affairs without prior approval of the board of directors. At the meeting Clejan announced his intent to convey a 90 percent interest in the property to the corporation in return for 900 shares of corporate stock and the assumption by the corporation of Clejan's obligations. At the same meeting Clejan announced that he intended to sell a 5 percent undivided interest in the land to defendant Benaron and a 5 percent interest to defendant Byrnes for a total price of \$50,000, and that he was retaining 10 percent of the property for this possible sale. It was Clejan's intention to use \$35,000 of the \$50,00 to be received from Benaron and Byrnes to pay Omansky and Klein the balance due them.

On September 9, 1959 Clejan entered into a contract with Benaron and Byrnes under which they paid him \$50,000 for the 10 percent interest in the property and further agreed that if a corporation were formed, they would convey their 10 percent interest to the corporation in return for the issuance to each of 50 shares of stock in the corporation. It should be noted that the corporation had been organized prior to the date of this agreement, but that Clejan apparently did not so advise Benaron and Byrnes. Defendant Reisman served as Benaron's at-

torney in connection with this transaction. From the \$50,000 received from Benaron and Byrnes, Clejan paid Omansky and Klein the \$35,000 balance due them.

In November 1959, 900 shares of stock were issued and delivered in Nevada to plaintiffs for their 90 percent interest in the ranch. In December 1959 certificates for 50 shares each to Benaron and Byrnes were delivered to Reisman in Nevada for Benaron and Byrnes in exchange for their 10 percent interest in the property.

Friction developed between plaintiffs and the nine investors. To settle their disagreement, Clejan offered the nine investors a gift of 170 shares of stock from his 900-share holding, two shares for each \$1,000 invested. Each, except Rosenberg, demanded a return of his money in lieu of stock. Since this factor as well as others presented a financial crisis, Clejan entered into an agreement with Benaron whereby Benaron loaned the corporation on December 7, 1959 approximately \$100,000 in return for the transfer to him by the Clejans of 365 of their 900 shares. Each of the nine California investors, except Rosenberg, was thereupon repaid the amount of his investment. Fifty shares from the 170 shares set aside for these investors were *230 transferred to Rosenberg, whose investment totalled \$25,000, and at a later date 100 shares were transferred to Benaron and 20 shares were transferred to his attorney, Reisman, defendant-appellant herein. These stock transactions reduced plaintiffs' holdings to 365 shares.

At a directors' meeting held in Nevada on December 6, 1959 plaintiffs were ousted as directors and officers of the corporation. Defendants Byrnes and Benaron were elected directors, defendant Reisman, their attorney, was elected president, and thereafter defendants were in control of the corporation.

In April 1960 plaintiffs conveyed 15 of their remaining 365 shares to their attorney, leaving them with a total of 350 shares.

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

On December 23, 1960, Reisman and Byrnes entered into an agreement in California with plaintiffs whereby Reisman and Byrnes agreed to purchase the 350 remaining shares held by plaintiffs for the sum of \$250,000 to be paid in stated instalments over a period of years.

After several defaults in payments under this contract, on February 1, 1963, the parties entered into an agreement in California providing that as of January 31, 1963, there was due plaintiffs under the December 23, 1960 agreement \$149,845.50; that defendants have no defense thereto and that plaintiffs are entitled to payment thereof; that defendants would pay Clejan \$35,000 forthwith and the balance of \$114,845.50 together with 6 percent interest per annum on January 15, 1964; that as of January 15, 1964, the total principal and interest due the Clejans would be \$121,454; that the Clejans would accept land from Gamble Ranch Investments, Inc. in lieu of cash on January 15, 1964, at the agreed price of \$12 per acre, a total of 10,121 acres, in full payment of the obligation; and that in the event suit be brought on the agreement, the successful party would be entitled to reasonable attorneys' fees. Benaron had not been a party to the December 23, 1960 agreement. By the February 1, 1963, agreement he agreed to be bound by the December 23, 1960, contract "to the same extent as though he were a principal thereof and had executed the agreement of December 23, 1960, as such principal."

It should be noted that as of February 1, 1963, title to the real property was in the corporation, that the defendants were officers, directors and majority stockholders thereof, and that by providing in the February 1, 1963, agreement that they would convey 10,121 acres of the corporate real estate to plaintiffs on January 15, 1964 in full payment of their personal obligation to plaintiffs, they were considering the corporation as their *alter ego*. *231

The present action is the result of an alleged default by defendants under the December 23, 1960, and February 1, 1963, agreements.

Defendant Reisman contends that plaintiffs organized the corporation as a speculative scheme to acquire land for resale to the public; that the venture was financed by soliciting the nine California investors for money; that these persons were "passive investors" and received in return "securities" within the meaning of the Corporate Securities Law; that the "securities" were sold in California without a permit of the Corporation Commissioner pursuant to a scheme to evade the Corporate Securities Law; that as a result all of the stock thereafter issued, including the 350 shares sold defendants under the December 23, 1960, agreement, was void; that as a result, the agreement was voidable at the option of defendants; and that defendant Reisman is entitled to recover the sum of \$36,859.83 previously paid by him to plaintiffs in part performance of the contract because issuance and sale of the stock without a permit breached an implied warranty that the stock had been validly issued to plaintiffs. Defendant Reisman prayed that plaintiffs take nothing by their complaint and that he have judgment on his cross-complaint for the \$36,859.83.

Plaintiffs deny these contentions and argue that even if the interests sold the nine California investors were "securities" within the meaning of the Corporate Securities Law, the stock issued thereafter to plaintiffs in Nevada by the Nevada corporation was valid under Nevada law and was not subject to the Corporate Securities Law; that even if it came under the Corporate Securities Law, the sale of the stock was specifically exempted from the Law as a sale of "personally owned" stock, not made for the issuer of a security or as a part of a promotional scheme created for the purpose of evading the Corporate Securities Law; that even if the stock were void for lack of a permit, because defendant Reisman was aware at all times of the circumstances surrounding the issuance of the stock, he should be estopped from denying its validity, and if not, he should be denied any recovery on his cross-complaint on the ground that he was *in pari delicto*.

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

Trial was by the court sitting without a jury. The court found for plaintiffs on the complaint and against defendant Reisman on the cross-complaint and rendered judgment for plaintiffs in the sum of \$40,759.27, the unpaid balance due under the February 1, 1963, agreement, together with interest thereon, and awarded plaintiffs' attorneys' fees in the sum of \$3,000. Defendant Reisman appeals from the entire judgment; plaintiffs appeal from that portion of the judgment awarding them \$3,000 attorneys' fees, asserting that the award was inadequate.

In reaching its decision, the trial court concluded that Gamble Ranch Investments, Inc. was a bona fide Nevada corporation; that the sale and *232 issuance of 900 shares of its stock to plaintiffs was a valid bona fide transaction, supported by a valuable consideration, occurred entirely within the State of Nevada and was therefore not subject to the California Corporate Securities Law; that plaintiffs did not sell the stock for the direct or indirect benefit of the corporation or any underwriter, or for the direct or indirect promotion of any scheme or enterprise with the intent of violating or evading the Corporate Securities Law; that the conveyance of the stock by plaintiffs was exempt from the Corporate Securities Law; that the contracts with the nine investors were unenforceable because of the failure to describe the specific acres each was to acquire; that since the contracts were unenforceable, each had only a right to the return of his money; that plaintiffs' intent to transfer 170 shares of their 900 shares to the nine investors did not invalidate the issuance of the remaining 730 shares to plaintiffs and the subsequent transfer of their remaining shares to Reisman, Benaron and Byrnes; that Reisman, Benaron and Byrnes purchased valid shares and no permit of the Corporation Commissioner was required for their transfer; that Reisman took an active part in formulating the plans and procedures for the issuance of the stock to plaintiffs and is therefore estopped from questioning the validity of that stock; that the plaintiffs were not joint venturers or partners with the nine investors; that the nine investors

had no claim or legal right at any time to any of plaintiffs' stock; that plaintiffs had the sole legal title to the stock at the time of issuance, and had legal title to the Gamble Ranch property at the time the corporation was organized, subject to encumbrances and the rights of the nine investors; that the December 23, 1960, agreement and the February 1, 1963, extension agreement were valid and enforceable, and without a defense.

Defendant Reisman points out that the facts are for the most part undisputed and calls our attention to the recent statement of our Supreme Court in *Morrison v. State Board of Education*, 1 Cal.3d 214, 238 [82 Cal.Rptr. 175, 461 P.2d 175]: "In any event, 'the ultimate conclusion to be drawn from undisputed facts is a question of law for an appellate court [citations].'" (1) We do not question this statement but note a more complete statement of the applicable rule in *Tobola v. Wholey*, 75 Cal.App.2d 351, 355 [170 P.2d 952]: "Appellant's view of the situation fails to take into account the rule that even where the probative facts are undisputed, the question as to the inferences to be drawn therefrom is still within the exclusive province of the trial court, and if there is any substantial evidence to support them this court is bound by the determination of the trial court. In other words, it is just as much the function of the trial court to resolve a conflict between opposing inferences as it is to resolve a conflict between contradictory statements of fact." *233

Validity of Transactions With Nine California Investors

Since the Corporate Securities Law relates primarily to the sale of securities and the licensing of persons selling securities, its scope depends to a great extent upon the meaning of the term "security." Section 25008, Corporations Code ^{FN1} provided in pertinent part:

FN1 Repealed 1968 and now incorporated in Corporations Code section 25019.

"Security' includes all of the following:

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

“(a) Any stock ... ; any certificate of interest or participation; any certificate of interest in a profit-sharing agreement; any certificate of interest in an oil, gas, or mining title or lease; any transferable share, investment contract, or beneficial interest in title to property, profits or earnings.”

(2) The use of the word “includes” in the statutory definition suggests that the items mentioned were intended to be illustrative and that the law was intended to embrace unnamed items similar to those listed. Thus the courts in examining an instrument of indebtedness have sought to determine whether the instrument seemed to perform the function stocks or bonds would have performed if the venture had been organized in a conventional manner. (3) The regulatory purpose of the law is not to be “vitiating by inventive substitutes for conventional means of raising risk capital.” (*Silver Hills Country Club v. Sobieski*, 55 Cal.2d 811, 816 [13 Cal.Rptr. 186, 361 P.2d 906, 87 A.L.R.2d 1135].) On page 814, the court added that courts must “look through form to substance.”

In *Silver Hills Country Club, supra*, promoters were in possession of a small ranch under a contract to purchase it for \$75,000 and had made only a \$400 down payment thereon. They proposed to raise \$165,000 through the sale of “memberships” and to construct facilities for the use of the members. Memberships were to be transferable only to persons approved by the club's board of directors, were to be subject to payment of dues, and were to convey no rights in the income or assets of the club. In upholding the Commissioner of Corporations' conclusion that the membership interests were a “security” and that the sales thereof without a permit were prohibited by the Corporate Securities Law, the court noted that since the sale of the memberships was not underwritten, there was no assurance that funds sufficient to construct the promised facilities, or even to pay the balance of the purchase price on the ranch, would be raised; that the \$400 down payment of the promoters was an insignificant sum compared to the undertaking; that if the

venture failed, nearly all the money lost would be that supplied by the public; that the promoters were “soliciting the risk capital with which to develop a business for profit” (55 Cal.2d at p. 815); that the memberships appeared to be performing the function ordinarily performed by shares of *234 stock; and that the objective of the law “is to afford those who risk their capital at least a fair chance of realizing their objectives in legitimate ventures whether or not they expect a return on their capital in one form or another.” (55 Cal.2d at p. 815.)

The court in *Silver Hills Country Club, supra* (55 Cal.2d at p. 814) noted that “security” has been defined “broadly to protect the public against spurious schemes, however ingeniously devised, to attract risk capital,” and stated on page 815: “as a general rule, the sale of “securities” that is condemned by the courts involves an attempt by an issuer to raise funds for a business venture or enterprise; an indiscriminate offering to the public at large where the persons solicited are selected at random; a passive position on the part of the investor; and the conduct of the enterprise by the issuer with other people's money.” (Dahlquist, *Regulation and Civil Liability Under the California Securities Act ...* 33 Cal. L. Rev. 343, 360.)”

Illustrations of similar transactions held to be “securities” within the meaning of the Corporate Securities Law are found in *Hollywood State Bank v. Wilde*, 70 Cal.App.2d 103, 107 [160 P.2d 846] (sale of fur-bearing animals and the entrusting of those animals to the seller for care and disposition of the fur); *Oil Lease Service, Inc. v. Stephenson*, 162 Cal.App.2d 100, 107-108 [327 P.2d 628] (the selling of “services” in procuring oil leases); *Securities & Exchange Com. v. W. J. Howey Co.*, 328 U.S. 293, 298 [90 L.Ed. 1244, 1249, 66 S.Ct. 1100, 163 A.L.R. 1043] (the sale of orange groves coupled with a contract to have the vendor service the land); *People v. Sidwell*, 27 Cal.2d 121 [162 P.2d 913] (beneficial interest in oil lease and drilling operations); *Mary Pickford Co. v. Bayly Bros., Inc.*, 12 Cal.2d 501 [86 P.2d 102] (beneficial

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

interest in trust formed to develop land); and *Menke v. Rand Min. Co.*, 81 Cal.App.2d 169 [183 P.2d 755] (agreement to pay share of profits from mining venture).

In the instant case the trial court made no finding as to whether the contracts with the nine investors involved sales of “securities” within the meaning of the Corporate Securities Law. It did find that each was a sale of an “interest in land,” and specifically found that the contracts were unenforceable because of the failure to describe the acreage involved. (*Craig v. Zelian*, 137 Cal. 105 [69 P. 853].)

(4) The facts surrounding these several transactions come squarely within the holding of the Supreme Court in *Silver Hills Country Club*, *supra*, 55 Cal.2d 811. They were sales of profit sharing interests in a business venture. The agreements attempted to perform the function stock would have performed if the venture had been organized in a conventional manner. The agreements were the result of the solicitation of risk capital to develop a business for profit. Plaintiffs, the promoters, contributed no capital, yet they *235 retained full control over the management and destiny of the promotion and intended to receive, and ultimately did receive a majority of stock in the corporation. Each contributor was a passive investor at most. Each received a “security” within the meaning of the Corporate Securities Law.

“Sale” is broadly defined by the Corporate Securities Law to include “every disposition ... of a security for value” and includes: “An offer to sell; an attempt to sell; a solicitation of a sale; an option of sale; a contract of sale; a taking of a subscription; an exchange; ...” (Corp. Code, § 25009. ^{FN2}) The uncontroverted facts support the conclusion that each transaction constituted a “sale” within the meaning of the Law.

FN2 Repealed 1968 and now incorporated in Corporations Code, section 25017.

The law defines the word “company” as including individuals (Corp. Code, § 25003 ^{FN3}), and provided that no “company” shall sell, offer for sale or negotiate for sale of a security of its own issue until it has obtained a permit from the Corporation Commissioner (Corp. Code, § 25500 ^{FN4}), and that every security of its own issue sold by any “company” without such permit is void. (Corp. Code, § 26100 ^{FN5}; but see: *Eberhard v. Pacific Southwest Loan & Mortg. Corp.*, 215 Cal. 226 [9 P.2d 302], holding that a security sold without a permit is voidable at the “behest of the purchaser.”) Plaintiffs, acting as individuals in the promotion before incorporation, were therefore subject to the law.

FN3 Repealed 1968.

FN4 Repealed 1968 and now incorporated in Corporations Code, section 25110.

FN5 Repealed 1968.

We conclude that plaintiffs' transactions with the nine investors in California constituted sales of securities within the meaning of the Corporate Securities Law, and that the interests sold were void as having been made without a permit.

Effect on Stock Subsequently Issued and Sold

Defendant argues that since the 900 shares were “promotional stock” acquired by plaintiffs as an indirect result of the purchase of the property by money raised through the foregoing illegal sales of “securities” in California without a permit, the stock, including the shares sold Reisman was void (Corp. Code, § 26100), or at least voidable at the instance of the purchasers. (*Eberhard v. Pacific Southwest Loan & Mortg. Corp.*, *supra*, 215 Cal. 226.) Defendant's argument is supported by an impassioned reference to the fact that Clejan acquired this stock without investment of any of his own money. We do not agree with this contention.

(5) (1) *Prior Illegal Transactions Will Not Invalidate Subsequently *236 Issued Stock.* Defendant

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

relies on *Wells v. Comstock*, 46 Cal.2d 528, 531 [297 P.2d 961] (stock sold contrary to permit held void and contract for sales price unenforceable), *Duntley v. Kagarise*, 10 Cal.App.2d 394, 397 [52 P.2d 560] (escrowed stock sold contrary to permit was void and seller's recovery of purchase price denied), *Boss v. Silent Drama Syndicate*, 82 Cal.App. 109, 113 [255 P. 225] (subsequent receipt of permit will not validate prior sale of stock void for lack of permit), *Reed v. Norman*, 41 Cal.2d 17 [256 P.2d 930] (stock sold contrary to permit held void), *Perego v. Seymour*, 196 Cal.App.2d 773 [16 Cal.Rptr. 831] (broker's commission denied for sale of stock sold contrary to permit), and *Stonehocker v. Cassano*, 154 Cal.App.2d 732 [316 P.2d 717] (stock sold contrary to permit held void). These cases are not in point. Each involved a particular transaction. None held that all subsequent independent transactions are invalidated by the illegal prior transaction.

It has been held that obligors on subsequent transactions cannot take advantage of a prior illegal transaction. Thus in *N. C. Roberts Co. v. Topaz Transformer Products, Inc.*, 239 Cal.App.2d 801 [49 Cal.Rptr. 209], the court said at page 816: "The void sale or issuance of certain shares made in violation of the terms of the permit under which they were issued does not invalidate the sale of other shares of the same issue made in compliance with the requirements of the permit [citation], even when the shares issued in violation of the permit were issued as a part of the same transaction and represented by the same certificate as the shares sold in compliance with the permit [citation]."

A similar holding is found in *Kent v. Kent*, 6 Cal.App.2d 488, 492-493 [44 P.2d 445]: "The Corporate Securities Act as it existed at the time of the stock issue here involved provided that every security issued without a permit of the corporation commissioner authorizing the same should be void. We do not believe that this language can be construed to mean that the issue of a part of the shares of a corporation without a permit should render the en-

tire stock issue void, ... The section is clearly limited to the single effect of declaring void those shares not issued in accordance with the required permit." (See also *Austin v. Hallmark Oil Co.*, 21 Cal.2d 718, 727 [134 P.2d 777]; *Wortley v. Wood-Callahan Oil Co., Ltd.*, 17 Cal.2d 762, 767 [112 P.2d 226].)

In the instant case as of August 31, 1959, plaintiffs owned the entire ranch, subject to encumbrances and the claims of the nine California investors. Pursuant to resolution of the corporate board of directors at the August 31, 1959 organizational meeting held in Nevada, the Nevada corporation issued and delivered to plaintiffs in Nevada in November 1959, 900 shares of stock in consideration for the transfer by plaintiffs to the corporation *237 of a 90 per cent interest in the ranch. No question has been raised as to noncompliance with Nevada law as to this transaction and we find no basis for holding that the stock issued and delivered to the plaintiffs in Nevada by the Nevada corporation was not valid under Nevada law. Even if Clejan intended to transfer a portion of the stock to the nine California investors, either as a gift or as consideration for their loans, and even if transfers to the nine investors would have been violative of the Corporate Securities Law, since the transfers were never consummated, the transactions with the nine investors had no effect on the validity of the stock.

(6a) (2) *The Stock Sold Defendant Was an Exempt Transaction*. Section 25152 of the Corporations Code ^{FN6} provided that "... the Corporate Securities Law does not apply to the sale of securities when (a) made by or on behalf of a vendor not the issuer or underwriter thereof who, being a bona fide owner of the securities, disposes of his own property for his own account, and (b) the sale is not made, directly or indirectly, for the benefit of the issuer or an underwriter of the security, or for the direct or indirect promotion of any scheme or enterprise with the intent of violating or evading any provision of the Corporate Securities Law."

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

FN6 Repealed 1968 and now incorporated in Corporations Code section 25104, subdivision (a).

In support of his contention that the sales agreement made in California on December 23, 1960, was not exempted under section 25152, Corporations Code, defendant Reisman argues that the corporation was the *alter ego* of plaintiffs at the time the stock was issued, that an *alter ego* who issues to himself stock in a corporation solely owned and controlled by himself does not come within the exemptions of section 25152, Corporations Code (*Conrad v. Superior Court*, 209 Cal.App.2d 143 [25 Cal.Rptr. 670]); that plaintiffs were in effect the issuers and underwriters of the stock; that the issuance and subsequent sale of the stock by plaintiffs required a permit (*Maner v. Mydland*, 250 Cal.App.2d 526 [58 Cal.Rptr. 740]; Corp. Code, § 25500^{FN7}; Corp. Code, § 25003; Corp. Code, § 26104^{FN8}); and that the sale of the stock under the December 23, 1960, agreement was therefore illegal (*Pyle v. Shipman*, 251 Cal.App.2d 913, 916-917 [60 Cal.Rptr. 46]) and void (*Tevis v. Blanchard*, 122 Cal.App.2d 731, 738 [266 P.2d 85]; Corp. Code, § 26100).

FN7 Now Corporations Code section 25110.

FN8 Now Corporations Code section 25540.

Plaintiffs deny these contentions, arguing (1) that since the sale was made some 13 months after the stock had been issued and approximately 12 months after plaintiffs were ousted as officers and directors of the corporation and had become minority stockholders and defendants had become *238 the majority stockholders, officers and directors of the corporation, it cannot be held to have been for the direct or indirect benefit of the issuer or underwriter; (2) that they sold by the December 23, 1960, agreement "personally owned" stock; and (3) that it was not a part of a scheme to evade the Corporate Securities Law. Plaintiffs further urge this court to

disregard the *alter ego* theory because it was neither pleaded nor set forth as an issue in the pre-trial order.

(7) If the facts of a case present an issue of illegality of a contract, it must be considered by the court, whether pleaded or not; the court may raise the issue on its own motion. (*Pyle v. Shipman*, *supra*, 251 Cal.App.2d 913, 917; *Tevis v. Blanchard*, *supra*, 122 Cal.App.2d 731, 733.) We therefore consider the contention that plaintiffs were the *alter ego* of the corporation and therefore do not qualify for exemption under section 25152 of the Corporations Code.

Reisman relies on *Conrad v. Superior Court*, *supra*, 209 Cal.App.2d 143. In *Conrad* a promoter was charged with several felony counts under the Corporate Securities Law, and sought a writ of prohibition to restrain the superior court from further proceedings. The evidence was summarized on page 148: "[T]he evidence creates a clear picture of a promoter of a speculative mining venture soliciting and obtaining money from four individuals upon representations and, in fact, an agreement, that they were to receive his personal shares in the corporation, represented to be then issued and in escrow, with a further agreement that the money thus obtained would be used for the benefit of the corporation; all of this done when, in fact, the corporate shares had not been issued and when the application before the California Corporation Commissioner for their issuance had been removed from the 'pending file' and was later abandoned." In denying the writ of prohibition, the court held that the facts presented were legally sufficient to hold the promoter for trial, that under the *alter ego* theory, it could be found that he was not only the corporation, but also both the issuer and underwriter of the shares.

Plaintiffs rely on *Associated Vendors, Inc. v. Oakland Meat Co.*, 210 Cal.App.2d 825, 837-838 [26 Cal.Rptr. 806]: ""Before a corporation's acts and obligations can be legally recognized as those of a particular person, and vice versa, it must be

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

made to appear that the corporation is not only influenced and governed by that person, but that there is such a unity of interest and ownership that the individuality, or separateness, of such person and corporation has ceased, and that the facts are such that an adherence to the fiction of the separate existence of the corporation would, under the particular circumstances, sanction a fraud or promote injustice. "" [Citations.] *239

"The gist of the cases which have considered the doctrine is that *both* of these requirements must be found to exist before the corporate existence will be disregarded; that such determination is primarily one for the trial court and is not a question of law; and that the conclusion of the trier of fact will not be disturbed if it be supported by substantial evidence. [Citations.] (8) It should also be noted that, while the doctrine does not depend on the presence of actual fraud, it is designed to prevent what would be fraud or injustice, if accomplished. Accordingly, bad faith in one form or another is an underlying consideration and will be found in some form or another in those cases wherein the trial court was justified in disregarding the corporate entity. [Citations.]" (9) Conditions under which a corporate entity may be disregarded vary according to the circumstances in each case. (*Automotriz etc. De California v. Resnick*, 47 Cal.2d 792, 796 [306 P.2d 1, 63 A.L.R.2d 1042].)

It appears that in the instant case the first requirement of the *alter ego* doctrine was present as of the date of issuance of the stock, namely, that there was such a unity of interest and ownership that the separate personalities of the corporation and the individual did not exist. We look to the second requirement, that if the acts are treated as those of the corporation alone, an inequitable result will follow. Although numerous factors have been held to be a sufficient basis for meeting this requirement (see *Associated Vendors, Inc. v. Oakland Meat Co.*, *supra*, 210 Cal.App.2d 825, 838-840), the only one relevant under the facts of this case is inadequate capitalization. However, with respect to

the cases that pertain to the effect of inadequate capitalization, we find a common factual situation, an attempt to escape liability by the incorporators or shareholders. The element of fraud is present. (See: *Minton v. Cavaney*, 56 Cal.2d 576, 579-580 [15 Cal.Rptr. 641, 364 P.2d 473]; *Automotriz etc. De California v. Resnick*, *supra*, 47 Cal.2d 792, 796-798; *Shea v. Leonis*, 14 Cal.2d 666 [96 P.2d 332]; *Carlesimo v. Schwebel*, 87 Cal.App.2d 482 [197 P.2d 167]; *Ballantine, Corporations* (rev. ed. 1946) § 129, pp. 302-303.)

Reisman has cited no authority, and we have found none, wherein the corporate entity has been disregarded under facts similar to the instant case where there was no allegation or evidence of fraud, or where, during a lapse of a considerable period of time, the incorporator is no longer the majority stockholder and is no longer a part of the management of the corporation. *Conrad v. Superior Court*, *supra*, 209 Cal.App.2d 143, relied on by Reisman is inapplicable under these circumstances.

(6b) We conclude that in the instant case there was substantial evidence to support the trial court's findings that due to the passage of time, the change in stock ownership, and the change in management, plaintiffs cannot *240 be deemed to be the *alter ego* of the corporation or the issuers or underwriters of the stock within the meaning of section 25152 of the Corporations Code as of the date of the sales agreement. December 23, 1960, approximately 13 months after the stock was issued and one year after defendants had become the majority stockholders and had taken over the management of the corporation; that as of December 23, 1960, the plaintiffs were the bona fide owners of 350 shares of stock; that they sold their own property for their own account; that the sale was not made directly or indirectly, for the benefit of the issuer or an underwriter of the security, or for the direct or indirect promotion of any scheme or enterprise with the intent of violating or evading any provisions of the Corporate Securities Law. The trial court properly found that the December 23, 1960, agreement covered the

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

sale of exempt securities, was not an illegal transaction, and that the parties were not *in pari delicto*.

In view of our conclusion we need not discuss plaintiffs' contention and the trial court's finding that defendant Reisman is estopped from denying the validity of the stock.

Exclusion of Evidence of Accord and Satisfaction

Defendant contends that evidence was erroneously excluded which tended to show that a check in the sum of \$8,125 and the signed agreement of February 1, 1963, were delivered to Albert H. Allen, plaintiffs' attorney, upon the following conditions: (1) that Clejan would obtain a grant deed to 10,121 acres of Gamble Ranch land from Benaron, or a contract from Benaron agreeing to convey such land to Clejan free and clear; (2) that Allen would hold the Reisman check and signed agreement until receipt of the above from Benaron and would then and only then deliver the check and signed agreement to Clejan; (3) that Clejan's receipt of the deed or contract to convey land from Benaron would discharge any further liability of Reisman to Clejan; and (4) that Allen also agreed the check and signed agreement would be returned to Reisman if Benaron did not deliver either a deed to the land or a contract to convey the land. Reisman contends that since these conditions were not satisfied, he was exonerated upon the theory of accord and satisfaction.

The evidence was offered for the sole purpose of showing that Reisman never completed the execution of the agreement by delivery. (Witkin, Cal. Evidence (2d ed. 1966) §§ 741-742.)

Without discussing the evidentiary ruling, we dispose of the point on other grounds. (10) First, for an accord and satisfaction to be effected, there must be a bona fide dispute as to the amount due. (*Kelly v. David D. Bohannon Organization*, 119 Cal.App.2d 787, 795 [260 P.2d 646].) *241 Here there was none. (11) Second, the proffered evidence is in direct conflict with the agreed statement of facts as to the events and agreement of February 1,

1963. Defendant is bound by that statement and evidence contrary thereto is inadmissible.

Attorneys' Fees

(12a) Plaintiffs' appeal presents only one issue, the contention that the award of \$3,000 for attorneys' fees was inadequate and constituted an abuse of discretion. No evidence was received on the issue. Counsel for plaintiffs informed the court that 468 hours were spent by members of his office in preparation of the case for trial. In addition, two members of his firm were present in court during the eight days of trial. Counsel argues that based on a total of 500 hours, the award allows only \$6 per hour.

Berry v. Chaplin, 74 Cal.App.2d 669, 679 [169 P.2d 442], summarizes the major factors to be considered in determining the reasonableness of attorneys' fees: "the nature of the litigation, its difficulty, the amount involved, the skill required and the skill employed in handling the litigation, the attention given, the success of the attorney's efforts, his learning, his age, and his experience in the particular type of work demanded [citation]; the intricacies and importance of the litigation, the labor and the necessity for skilled legal training and ability in trying the cause, and the time consumed."

(13) Testimony or other direct evidence of the reasonable value of the services need not be introduced, the knowledge and experience of the trial judge being sufficient. (*Frank v. Frank*, 213 Cal.App.2d 135, 137 [28 Cal.Rptr. 687].)

(12b) Considering the various factors mentioned in *Berry, supra*, we hold that the award of \$3,000 was wholly inadequate and an abuse of discretion, and that the case must be remanded for the purpose of redetermining the reasonable value of the services rendered.

(14) The contracts provide for attorneys' fees to the successful litigant. This provision covers fees on appeal and may be determined by this court or the trial court when it determines costs. (Code Civ.

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856
(Cite as: 5 Cal.App.3d 224)

Proc., § 1034; *Rabinowitch v. California Western Gas Co.*, 257 Cal.App.2d 150, 160 [65 Cal.Rptr. 1].) The latter procedure is preferred in this case.

The judgment is affirmed in all respects except as to the award of attorneys' fees; as to the latter, it is reversed and the matter is remanded to the trial court for the purpose of redetermining the reasonable value of the services rendered in the preparation and trial of the case, for the purpose *242 of fixing an award of attorneys' fees on appeal, and for the additional purpose of modifying the judgment accordingly. Plaintiffs are awarded their costs on appeal.

Cobey, Acting P. J., and Allport, J., concurred.

A petition for a rehearing was denied March 31, 1970, and the petition of defendant and appellant for a hearing by the Supreme Court was denied May 6, 1970. Mosk, J., was of the opinion that the petition should be granted. *243

Cal.App.2.Dist.

Clejan v. Reisman

5 Cal.App.3d 224, 84 Cal.Rptr. 897, Blue Sky L. Rep. P 70,856

END OF DOCUMENT

33 Cal.App.4th 245, 39 Cal.Rptr.2d 292, 60 Cal. Comp. Cases 192
 (Cite as: 33 Cal.App.4th 245)

H
 MEL DONEY et al., Plaintiffs and Appellants,
 v.
 TRW, INC., Defendant and Respondent.

No. H011835.

Court of Appeal, Sixth District, California.
 Mar 21, 1995.

[Opinion certified for partial publication. ^{FN*}]

FN* Pursuant to California Rules of Court, rules 976(b) and 976.1, this opinion is certified for publication with the exception of part C.

SUMMARY

Heirs of employees who died during a third party's murderous rampage at a corporate employer's building brought a wrongful death action against the employer and the employer's parent corporation. The action against the parent corporation was premised on an alter ego theory. Summary judgment was entered in favor of the employer based on the exclusive remedy provisions of the Workers' Compensation Act (Lab. Code, § 3602). The parent corporation thereafter obtained summary judgment in its favor. (Superior Court of Santa Clara County, No. 676206, Richard C. Turrone, Judge.)

The Court of Appeal affirmed. It held that an action cannot proceed against a parent corporation on an alter ego theory for its subsidiary corporation's conduct when the subsidiary corporation is shielded from such an action by the exclusive remedy provisions of the Workers' Compensation Act. The alter ego doctrine is an equitable theory of vicarious liability, which was not applicable to this situation. First, applying the theory of vicarious liability under these circumstances would produce the anomalous result that the liability of a nonnegligent entity would be greater than that of the negligent entity. Second, permitting employees of subsidi-

diary corporations to recover from the corporate owner under an alter ego theory of vicarious liability would give those employees an unwarranted windfall by exempting a single class of employees (those who work for corporations) from the statutorily mandated limits of workers' compensation. Finally, because of the unavailability of equitable indemnity (Lab. Code, § 3864), application of the alter ego doctrine to permit the owner of the subsidiary corporation to be held liable in tort would place an onerous burden on someone who is fault-free. (Opinion by Mihara, J., with Cottle, P. J., and Wunderlich, J., concurring.)

HEADNOTES

Classified to California Digest of Official Reports (1a, 1b, 1c) Workers' Compensation § 7--Exclusivity of Remedy-- Liability of Employer's Parent Corporation--Alter Ego Theory.

In a wrongful death action arising from a third party's murderous rampage at a corporate employer's building, brought by heirs of the deceased employees against the employer's parent corporation, the trial court properly granted defendant summary judgment. An action against the employer was precluded by the exclusive remedy provisions of workers' compensation (Lab. Code, § 3602), since the subsidiary had fulfilled its statutory obligation to secure workers' compensation insurance, and plaintiffs premised their action against defendant on an alter ego theory. The alter ego doctrine is an equitable theory of vicarious liability, which was not applicable to this situation. First, applying the theory of vicarious liability under these circumstances would produce the anomalous result that a nonnegligent entity's liability would be greater than that of the negligent entity. Second, permitting employees of subsidiary corporations to recover from the corporate owner under an alter ego theory of vicarious liability would give those employees an unwarranted windfall by exempting a single class of employees (those who work for corporations) from the statutorily mandated limits of workers' com-

33 Cal.App.4th 245, 39 Cal.Rptr.2d 292, 60 Cal. Comp. Cases 192
(Cite as: 33 Cal.App.4th 245)

pensation. Finally, because of the unavailability of equitable indemnity (Lab. Code, § 3864), application of the alter ego doctrine to permit the owner of the subsidiary corporation to be held liable in tort would place an onerous burden on someone who is fault-free.

[See 2 **Witkin**, Summary of Cal. Law (9th ed. 1987) Workers' Compensation, § 25 et seq.]

(2a, 2b) Corporations § 3--Power of Court to Disregard Corporate Entity--Alter Ego Doctrine.

The alter ego doctrine arises when a plaintiff comes into court claiming that an opposing party is using the corporate form unjustly and in derogation of the plaintiff's interests. The essence of the alter ego doctrine is that justice be done. The critical question is whether in the particular case presented, and for the purposes of such case, justice and equity can best be accomplished, and fraud and unfairness defeated, by a disregard of the distinct entity of the corporate form. The alter ego doctrine is strictly limited by the demands of equity; it applies only in narrowly defined circumstances and only when the ends of justice so require. The alter ego doctrine will only be applied to avoid an inequitable result. Alter ego is essentially a theory of vicarious liability under which the owners of a corporation may be held liable for harm for which the corporation is responsible where, because of the corporation's utilization of the corporate form, the party harmed will not be adequately compensated for its damages.

(3) Corporations § 3--Power of Court to Disregard Corporate Entity--Alter Ego Doctrine--Parent and Subsidiary Corporation.

A parent corporation may be deemed the alter ego of its subsidiary corporation, and thus liable for the subsidiary's wrongdoing, only if there is such unity of interest and ownership that the separate personalities of the subsidiary and the parent no longer exist, and it appears that, if the acts are treated as those of the subsidiary alone, an inequitable result will follow. The corporate wall will be breached. Yet the wall remains: the parent is liable through the acts of the subsidiary, but as a separate entity.

(4) Independent Contractors § 5--Liability of Employer--Peculiar Risk Doctrine.

The peculiar risk doctrine is a theory of vicarious liability that is applied to avoid inequity. In its original form the doctrine made a landowner liable to innocent bystanders or neighboring property owners who were injured by the negligent acts of an independent contractor hired by the landowner to perform dangerous work on his or her land. In turn, the landowner could sue the contractor for equitable indemnity. The peculiar risk doctrine was created to ensure that innocent third parties injured by the negligence of an independent contractor hired by a landowner to do inherently dangerous work on the land would not have to depend on the contractor's solvency in order to receive compensation for the injuries.

COUNSEL

Liccardo, Rossi, Sturges & McNeil, Gregory D. Hull and Laura Liccardo for Plaintiffs and Appellants.

Berliner & Cohen, William J. Goines, Nancy J. Johnson and Thomas P. Murphy for Defendant and Respondent.

MIHARA, J.

In February 1988, Richard Wade Farley killed numerous employees of ESL during a murderous rampage in ESL offices in a building *248 owned by ESL. Plaintiffs are the heirs of some of the ESL employees killed by Farley. Plaintiffs brought a wrongful death action against defendant TRW, Inc., and its wholly owned subsidiary ESL for negligence and premises liability. Summary judgment was entered in favor of ESL based on the exclusive remedy provisions of the Workers' Compensation Act (Lab. Code, § 3602). Defendant TRW thereafter obtained a summary judgment in its favor. Plaintiffs appeal contending that there were triable issues of material fact which precluded summary judgment in TRW's favor. The critical issue on appeal is whether an action can proceed against a par-

33 Cal.App.4th 245, 39 Cal.Rptr.2d 292, 60 Cal. Comp. Cases 192
(Cite as: 33 Cal.App.4th 245)

ent corporation on an alter ego theory for its subsidiary corporation's conduct when the subsidiary corporation is shielded from such an action by the exclusive remedy provisions of the Workers' Compensation Act. Plaintiffs also claim that summary judgment was precluded because there were disputed factual questions underlying their claim that TRW was directly liable to them because it voluntarily undertook to protect ESL's employees and negligently failed to do so. We affirm the judgment.

Analysis

A. Standard of Review

Appellate review of a summary judgment is de novo. (*Stratton v. First Nat. Life Ins. Co.* (1989) 210 Cal.App.3d 1071 [258 Cal.Rptr. 721]; *Barisich v. Lewis* (1990) 226 Cal.App.3d 12, 15 [275 Cal.Rptr. 331].) "First, we identify the issues framed by the pleadings since it is these allegations to which the motion must respond by establishing a complete defense or otherwise showing there is no factual basis for relief on any theory reasonably contemplated by the opponent's pleading.... [¶] Secondly, we determine whether the moving party's showing has established facts which negate the opponent's claim and justify a judgment in movant's favor.... [¶] [If] a summary judgment motion prima facie justifies a judgment, the third and final step is to determine whether the opposition demonstrates the existence of a triable, material factual issue." (*AARTS Productions, Inc. v. Crocker National Bank* (1986) 179 Cal.App.3d 1061, 1064, 1065 [225 Cal.Rptr. 203].)

B. Alter Ego Theory Not Viable

(1a) Plaintiffs' primary theory of liability was that TRW was liable to them because TRW was the alter ego of ESL, plaintiffs' decedents' allegedly negligent employer. This theory is not legally viable. (2a) "The essence of the alter ego doctrine is that justice be done." (*Mesler v. Bragg Management Co.* (1985) 39 Cal.3d 290, 301 [216 Cal.Rptr. 443, 702 P.2d 601].) *249 "The alter ego doctrine arises when a plaintiff comes into court claiming that an opposing party is using the corporate form

unjustly and in derogation of the plaintiff's interests." (*Id.* at p. 300.) The critical question is "whether in the particular case presented and for the purposes of such case justice and equity can best be accomplished and fraud and unfairness defeated by a disregard of the distinct entity of the corporate form." (*Id.* at p. 301.) (3) A parent corporation may be deemed the 'alter ego' of its subsidiary corporation only if there is "such unity of interest and ownership that the separate personalities of the [subsidiary] and the [parent] no longer exist" and it appears that "if the acts are treated as those of the [subsidiary] alone, an inequitable result will follow." (*Id.* at p. 300, citation omitted.) "[T]he corporate wall [will] be breached. Yet the wall remains: the parent is liable through the acts of the subsidiary, but as a separate entity." (*Id.* at p. 301.) (2b) The alter ego doctrine is strictly limited by the demands of equity; it applies "only in narrowly defined circumstances and only when the ends of justice so require." (*Id.* at p. 301.) The alter ego doctrine will only be applied to avoid an inequitable result. Alter ego is essentially a theory of vicarious liability under which the owners of a corporation may be held liable for harm for which the corporation is responsible where, because of the corporation's utilization of the corporate form, the party harmed will not be adequately compensated for its damages. (*Mesler* at pp. 300, 302-304.)

(1b) In this case, ESL is the corporation which utilized the corporate form and was allegedly responsible for the harm suffered, and TRW is the owner of ESL. However, the equitable principles underlying the doctrine of alter ego preclude holding TRW liable for the harm for which ESL was responsible. All California employers are required to "secure the payment" of workers' compensation benefits. (Lab. Code, § 3700.) Ordinarily, the employer meets this obligation by obtaining a workers' compensation insurance policy. (Lab. Code, § 3700, subd. (a).) If the employer satisfies this obligation and its employee suffers harm in the course of the employment, workers' compensation benefits are the exclusive remedy available to that employee,

33 Cal.App.4th 245, 39 Cal.Rptr.2d 292, 60 Cal. Comp. Cases 192
(Cite as: 33 Cal.App.4th 245)

the employee is not permitted to bring a legal action against the employer for damages arising from this harm, and the employer is also shielded from an action for equitable indemnity. (Lab. Code, §§ 3600, 3706, 3864.) ESL satisfied its obligation to “secure the payment” of workers’ compensation benefits to its employees. Consequently, no legal action could be brought against ESL for harm suffered by its employees in the course of their employment. It is undisputed that the harm for which plaintiffs seek compensation in this action was suffered by ESL’s employees in the course of their employment.

The question presented here is whether the owner of a corporation can be held vicariously liable under the equitable doctrine of alter ego for damages *250 suffered by the employees of the corporation in the course of their employment where the corporation has satisfied its obligation to these employees by securing the payment of workers’ compensation benefits. We conclude that the owner cannot be held vicariously liable under the equitable doctrine of alter ego in this situation for many of the same reasons that the hirer of an independent contractor cannot be held vicariously liable to the independent contractor’s employees under the equitable doctrine of peculiar risk. (*Privette v. Superior Court* (1993) 5 Cal.4th 689 [21 Cal.Rptr.2d 72, 854 P.2d 721].) The California Supreme Court held in *Privette v. Superior Court, supra*, 5 Cal.4th 689 that, where an independent contractor has satisfied its obligation to secure the payment of workers’ compensation benefits, its employee cannot hold the person who had hired the independent contractor vicariously liable under the equitable doctrine of peculiar risk for harm suffered by the employee in the course of employment. The reasons offered by the California Supreme Court for its refusal to permit liability under the doctrine of peculiar risk in *Privette* mirror our reasons for refusing to permit liability under the doctrine of alter ego here.

(4) Peculiar risk, like alter ego, is a theory of vicarious liability which is applied to avoid in-

equity. (*Privette v. Superior Court, supra*, 5 Cal.4th at pp. 694-695.) “[I]n its original form the doctrine of peculiar risk made a landowner liable to innocent bystanders or neighboring property owners who were injured by the negligent acts of an independent contractor hired by the landowner to perform dangerous work on his or her land. In turn, the landowner could sue the contractor for equitable indemnity.” (*Id.* at p. 696.) The peculiar risk doctrine was created “to ensure that innocent third parties injured by the negligence of an independent contractor hired by a landowner to do inherently dangerous work on the land would not have to depend on the contractor’s solvency in order to receive compensation for the injuries.” (*Id.* at p. 694.) Eventually, in 1962, the California Supreme Court expanded the peculiar risk doctrine to permit an independent contractor’s employee to recover tort damages from the person who hired the independent contractor. (*Id.* at p. 696.)

In *Privette*, the California Supreme Court overruled its 1962 expansion of the peculiar risk doctrine. The court ruled that since the employee of an independent contractor could not recover in tort from the independent contractor, because the independent contractor was his employer and his recovery was therefore limited by the Workers’ Compensation Act’s exclusive remedy provisions, the employee could not be permitted to obtain tort damages from the hirer of the independent contractor based on the equitable doctrine of peculiar risk. First, the court explained that permitting application of a theory of vicarious liability under these circumstances “produces *251 the anomalous result that a nonnegligent person’s liability for an injury is greater than that of the person whose negligence actually caused the injury” (*Privette v. Superior Court, supra*, 5 Cal.4th at p. 698.) Second, permitting employees of independent contractors to recover under this theory of vicarious liability “would give those employees an unwarranted windfall.” (*Id.* at p. 700.) “[T]o permit such recovery would give these employees something that is denied to other workers: the right to recover tort damages for

33 Cal.App.4th 245, 39 Cal.Rptr.2d 292, 60 Cal. Comp. Cases 192
(Cite as: 33 Cal.App.4th 245)

industrial injuries caused by their employer's failure to provide a safe working environment. This, in effect, would exempt a single class of employees, those who work for independent contractors, from the statutorily mandated limits of workers' compensation." (*Id.* at p. 700.) Third, because equitable indemnity cannot be obtained from the negligent employer, application of the peculiar risk doctrine to permit the hirer to be held liable in tort "places an onerous burden on someone who is 'fault-free.'" (*Id.* at p. 701.)

These three reasons convinced the California Supreme Court that employees should not be permitted to recover tort damages under the equitable doctrine of peculiar risk where workers' compensation benefits are available to them. "[T]he workers' compensation system of recovery regardless of fault achieves the identical purposes that underlie recovery under the doctrine of peculiar risk: It ensures compensation for injury by providing swift and sure compensation to employees for any workplace injury; it spreads the risk created by the performance of dangerous work to those who contract for and thus benefit from such work, by including the cost of workers' compensation insurance in the price for the contracted work; and it encourages industrial safety." (*Privette v. Superior Court, supra*, 5 Cal.4th at p. 701.) Accordingly, the doctrine of peculiar risk is unavailable where "the injuries resulting from an independent contractor's performance of inherently dangerous work are to an employee of the contractor, and thus subject to workers' compensation coverage" (*Id.* at p. 702.)

(1c) Similar reasoning applies here. In this case, plaintiffs brought a tort action against the owner (TRW) of the corporation (ESL) which had employed their decedents. Plaintiffs were barred from bringing a tort action against ESL because ESL was covered by the Workers' Compensation Act's exclusive remedy provisions. Instead, plaintiffs sought to hold TRW vicariously liable through the equitable doctrine of alter ego. Like the peculiar risk doctrine addressed in *Privette*, the al-

ter ego doctrine is an equitable theory of vicarious liability. Each of the justifications offered by the California Supreme Court in *Privette* for refusing to permit imposition of vicarious liability is equally applicable here. First, as in *Privette*, permitting the application of a theory of vicarious liability under these circumstances would produce "the anomalous result that a nonnegligent person's [TRW's] liability for an injury is greater than that of the person [ESL] whose negligence *252 actually caused the injury" (*Privette v. Superior Court, supra*, 5 Cal.4th at p. 698.) Second, also as in *Privette*, permitting employees of subsidiary corporations to recover from the corporate owner under an alter ego theory of vicarious liability "would give those employees an unwarranted windfall" by "exempt[ing] a single class of employees, those who work for [corporations], from the statutorily mandated limits of workers' compensation." (*Id.* at p. 700.) Finally, because of the unavailability of equitable indemnity (Lab. Code, § 3864), application of the alter ego doctrine to permit the owner of the subsidiary corporation to be held liable in tort "places an onerous burden on someone who is 'fault-free.'" (5 Cal.4th at p. 701.)

The owner of a corporation incurs the expense of workers' compensation insurance as a corporate expense which reduces any profits reaped by the owner from the corporation in return for ensuring "swift and sure compensation to employees for any workplace injury" and encouraging industrial safety. Consequently, there is no justification for holding the owner of the corporation liable in tort for workplace injuries to employees of the corporation. Because this scenario is equitable, an employee of the corporation cannot utilize the doctrine of alter ego to hold the owner of the corporation liable in tort for a workplace injury where the corporation has ensured the payment of workers' compensation benefits.

C. TRW Did Not Independently Breach a Duty to Decedents to Provide Them With Reasonable Security^{FN*}

33 Cal.App.4th 245, 39 Cal.Rptr.2d 292, 60 Cal. Comp. Cases 192
(Cite as: 33 Cal.App.4th 245)

FN* See footnote, *ante*, page 245.

.....
Conclusion

The judgment is affirmed.

Cottle, P. J., and Wunderlich, J., concurred.

Appellants' petition for review by the Supreme
Court was denied July 20, 1995. *253

Cal.App.6.Dist.

Doney v. TRW, Inc.

33 Cal.App.4th 245, 39 Cal.Rptr.2d 292, 60 Cal.
Comp. Cases 192

END OF DOCUMENT



ECLECTIC PROPERTIES EAST, LLC, a California Limited Liability Company, et al., Plaintiffs, v. THE MARCUS & MILLICHAP COMPANY, a California corporation, et al., Defendants.

No. C-09-0511 RMW

UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF CALIFORNIA, SAN JOSE DIVISION

2010 U.S. Dist. LEXIS 7381

**January 29, 2010, Decided
January 29, 2010, Filed**

SUBSEQUENT HISTORY: Claim dismissed by, Dismissed without prejudice by *Eclectic Props. East, LLC v. Marcus & Millichap Co.*, 2011 U.S. Dist. LEXIS 41251 (N.D. Cal., Apr. 12, 2011)

COUNSEL: [*1] For Eclectic Properties East, LLC, a California Limited Liability Company, Risola Family LP II, a Florida Limited Partnership, CECA 3000, LP, a Nevada Limited Partnership, Cheatham Properties, LLC, a California Limited Liability Company, successor in the interest of John and Mary Cheatham, VAS Enterprises I LLC, a California Limited Liability Company, Amnon Danus, Rivka Danus, Fred Engelberg, Linda Farrell, Joseph W. Amirkhas, Joseph W. Amirkhas, as Trustee under the Amirkhas Trust, dated January 14, 2000, Justus L. Ahrend, Susan W. Ahrend, Trustees of the Justus and Susan Ahrend Trust, dated December 6, 1990, Kevork Belikian, Sylvia S. Belikian, Trustees under The Kevork Belikian and Sylvia S. Belikian Living Trust, dated July 10, 2000, Mani Etemad, Susan Khoshnood, Trustee of the Mani Etemad and Susan Khoshnood 2001 Revocable Trust, Eugenia Gagnon, Trustee of the Genie Debs Revocable Trust, dated October 10, 1995, Thomas H. Linden, Sylvia E. Linden, Trustees of The Thomas H. Linden and Sylvia E. Linden Family Trust, dated September 19, 2000, Johannes Moderbacher, Eileen Starr Moderbacher, as Trustees of The Moderbacher Family Trust, Established by Declaration of Trust, dated

February [*2] 1, 2006, Richard W. Siebert, Debra M. Siebert, Trustees of The Siebert Family Trust U/DT, dated January 13, 2003, Allen Ernest Hom, Trustee for The Allen Ernest Hom Trust, dated August 19, 1992, Linda J. Call, Trustee for The Linda Jeanne Call Family Trust, dated September 12, 2002, Plaintiffs: Bonny E. Sweeney, LEAD ATTORNEY, Phong L. Tran, Coughlin Stoia Geller Rudman & Robbins LLP, San Diego, CA; Bailie L Heikkinen, James L. Davidson, Mary B. Clark, Stuart Andrew Davidson, PRO HAC VICE, Coughlin Stoia Geller Rudman & Robbins LLP, Boca Raton, FL; Cullin Avram O'Brien, Coughlin Stoia Geller Rudman & Robbins LLP, Boca Raton, FL; David J. George, PRO HAC VICE, Boca Raton, FL; John Granville Crabtree, Key Biscayne, FL.

For The Marcus & Millichap Company, a California corporation, Sovereign Investment Company, a California corporation, Sovereign Scranton LLC, a Delaware Limited Liability Company, Sovereign CC, LLC, a Delaware Limited Liability Company, Sovereign JF, LLC, a California Limited Liability Company, Defendants: Daniel E. Jackson, Kecker & Van Nest, San Francisco, CA; Daniel Edward Purcell, John Watkins Kecker, Kecker & Van Nest LLP, San Francisco, CA.

For Marcus & Millichap Real [*3] Estate Investment Services Inc., a California corporation, Marcus & Millichap Real Estate Investment Brokerage Company, a

California corporation, Defendants: David Charles Scheper, LEAD ATTORNEY, Overland Borenstein Scheper & Kim LLP, Los Angeles, CA; Daniel E. Jackson, Kecker & Van Nest, San Francisco, CA; Katherine Blanca Farkas, Scheper Kim & Overland LLP, Los Angeles, CA.

For Paul A. Morabito, individually and as the alter-ego of Eureka Petroleum Inc., a New York corporation, Tibarom Inc., a Delaware corporation, Tibarom NY LLC, a Nevada Limited Liability Company, Tibarom PA LLC, a Nevada Limited Liability Company, Scranton Lube, LLC a Delaware, Defendant: Eric Joseph Schindler, LEAD ATTORNEY, Robert John McKennon, McKENNON SCHINDLER LLP, Laguna Beach, CA; Brendan H. Little, Dennis C. Vacco, Kevin J. Cross, PRO HAC VICE, Lippes Mathias Wexler Friedman LLP, Buffalo, NY.

For Tibarom NY LLC, a Nevada Limited Liability Company, Tibarom PA LLC, a Nevada Limited Liability Company, Defendants: Timothy Alan Horton, LEAD ATTORNEY, McKenna Long & Aldridge LLP, San Diego, CA.

For Baruk Management, Inc., a California corporation, Defendant: Eric Joseph Schindler, LEAD ATTORNEY, Robert John McKennon, [*4] McKENNON SCHINDLER LLP, Laguna Beach, CA.

For PGP Valuation, Inc., a Oregon corporation, Defendant: Michael Lloyd Smith, LEAD ATTORNEY, Manning & Marder, Kass, Ellrod, Ramirez LLP, San Francisco, CA.

For Glen D. Kunofsky, Daizy Gomez, Defendants: Eugene Ashley, LEAD ATTORNEY, Hopkins & Carley, San Jose, CA.

For Marcus Muirhead, Sean Perkin, Donald Emas, Andrew Leshner, Stewart Weston, Brice Head, Bret King, Defendants: David Charles Scheper, LEAD ATTORNEY, Overland Borenstein Scheper & Kim LLP, Los Angeles, CA; Katherine Blanca Farkas, Scheper Kim & Overland LLP, Los Angeles, CA.

For Glen D. Kunofsky, Daizy Gomez, Defendants: Eugene Ashley, Hopkins & Carley, San Jose, Ca.

JUDGES: RONALD M. WHYTE, United States District Judge.

OPINION BY: RONALD M. WHYTE

OPINION

ORDER

On January 22, 2010, the court heard seven motions in this case: (1) a motion to dismiss by defendants The Marcus & Millichap Company, Sovereign Investment Company, Sovereign Scranton, LLC, Sovereign CC, LLC, and Sovereign JF LLC (collectively, the "Sovereign Defendants"), which was joined by defendants Marcus & Millichap Real Estate Investment Services Inc., Marcus & Millichap Real Estate Investment Brokerage Company, Marcus Muirhead, Sean Perkin, Donald [*5] Emas, Andrew Leshner, Stewart Weston, Brice Head, and Bret King (collectively, the "Broker Defendants"); (2) a motion to dismiss by the Broker Defendants, which was joined by defendants Glen Kunofsky and Daisy Gomez; (3) a motion to dismiss by real estate appraiser defendant PGP Valuation, Inc.; (4) a motion to dismiss, sever or transfer by defendants Paul Morabito and Baruk Management, Inc., which was joined by defendants Tibarom NY, LLC, and Tibarom PA, LLC; (5) a motion by plaintiffs to compel the deposition of defendant Morabito on jurisdictional issues; (6) defendant Morabito's motion for a protective order to preclude the taking of his deposition; and (7) a motion to strike plaintiffs' jury demand by the Sovereign Defendants. All motions are opposed. Having considered the papers submitted by the parties and the arguments of counsel at the hearing, and for good cause appearing for the reasons set forth below and stated at the hearing, the motions to dismiss are granted with leave to amend, the motion to compel defendant Morabito's deposition is denied, the motion for a protective order is granted, and the motion to strike plaintiffs' jury demand is denied without prejudice.¹

¹ Additionally, [*6] the Sovereign defendants' request for judicial notice (Docket 62) is denied without prejudice; the Morabito defendants' motion to strike plaintiffs' opposition (Docket 144) is denied.

This is a complex real estate investment fraud case where the complexity arises largely because of the number of plaintiffs, defendants, and transactions with little obvious connection to each other. Twenty-six plaintiffs filed suit against thirty-one defendants relating to twenty-two commercial real estate 1031 exchanges

into commercial properties with long-term triple net leases. Fourteen of the properties involved Jiffy Lube franchises, eight of the properties involved Church's Chicken franchises. None of the properties are located in California. Instead, the properties are located in New York, Florida, Pennsylvania and Georgia. The complaint breaks out seventeen groups of transactions, each involving a separate individual or couple who purchased the property (and sometimes two or three properties), and generally separate groups of defendants. The defendants include real estate investment firms (including parent corporations with no direct involvement in the complained of transactions), subsidiaries, [*7] individual employees, real estate brokers and agents, an appraiser, tenants and the tenants' corporate owners. The complaint is long -- 174 pages, 624 paragraphs -- and seeks to assert seven causes of action:

1. RICO (*18 U.S.C. § 1962(c)-(d)*);
2. Negligent Misrepresentation;
3. Fraudulent Concealment under *California Civil Code § 1710*;
4. Unjust enrichment and imposition of a constructive trust;
5. Money had and received;
6. Violation of *California Business and Professions Code Section 17500*; and,
7. Violation of *California Business and Professions Code Section 17200*.

The court's subject matter jurisdiction is based solely on the RICO claim.

The overarching theory is that each plaintiff was defrauded into investing in a commercial property which was subject to a long-term triple net lease. The "scheme," as described by plaintiffs, took place in three stages: first, defendant Morabito or Waelti (or one of their respective companies) sold a commercial property to an entity (generally, one of the Sovereign defendants) at an inflated price and immediately entered into a leaseback transaction, with the lease payments set significantly higher than fair rental value. These long-term, high rent, triple [*8] net, leases made each property appear to be worth significantly more than its true market value.

Second, the Sovereign entity then marketed the properties for sale (through the Broker defendants) to real estate investors, such as plaintiffs, using allegedly sham appraisals to support the artificially high values. Third, after a plaintiff's purchase, the underlying tenant walked away from the lease, causing the value of the property to plummet.² Through this scheme, each plaintiff was allegedly defrauded into paying significantly more than the property was actually worth, based on misrepresentations regarding the underlying leases and tenants.

2 The alleged scheme did not always follow this pattern, however. In the case of plaintiffs Gagnon and Call, each purchased directly from either a Morabito-related entity or a Waelti-related entity. Additionally, in five of the transactions, the first "inflated" sale is alleged to have been for the same price that was paid by the Morabito or Waelti-related entity when acquiring the property. See the transactions involving Cheatham (Complaint at 122), Danus (Complaint, p. 127); Engelberg (Complaint at 142); and Armenta (Complaint at 149) and the [*9] third purchase by Hom (Complaint at 115). In a sixth transaction, the inflated price is only \$ 600 higher than the original price. See Amirkas purchase (Complaint at 104). Moreover, the length of time in which the allegedly inflated lease was in place before the tenant walked away varied tremendously, ranging from six months to four years.

But, while the complaint repeatedly alleges that each purported "scam" was executed "with mathematical precision," the facts that are pleaded show significant differences between the transactions, including the amount of the purported price inflation, the amount of time between the inflated sales price and the ultimate sale to a plaintiff during which the tenant is alleged to have paid artificially high rent under the "sham" lease (as long as 19 months), the amount of time after that passed after a plaintiff acquired the property and the abandonment of the lease by the tenant (generally measured in years). A plain reading of the seventeen narratives alleged in the complaint does not give rise to a plausible inference of a single fraudulent scheme executed with precision.

Each of the motions to dismiss challenges the adequacy of the RICO allegations. [*10] The court agrees that the complaint does not adequately plead the

RICO claim with adequate particularity. The fundamental difficulty with the complaint is that it fails to allege facts sufficient to put each defendant on notice of what it is that he, she or it is alleged to have done that gives rise to the claims asserted against him, her, or it. While long and colorful, the complaint nevertheless fails to adequately plead *facts* sufficient to inform each defendant of the specific allegations against it under each asserted cause of action, and many of the allegations simply lump all of the defendants together in a group. The complaint does not adequately allege the misrepresentations and omissions that form the foundation of the fraud and knowledge of falsity by the defendants who are alleged to have made them. The complaint similarly does not allege facts which plausibly suggest each defendant's knowledge of the alleged fraudulent scheme. For example, the complaint is silent with regard to the individual broker's knowledge that the offered sales price was artificially inflated, that the underlying lease which purportedly supported the sale price was a sham, or that the tenant intended [*11] to walk away from the underlying lease after a plaintiff purchased the property.

RICO makes it unlawful for any person employed by or associated with any enterprise to conduct or participate, directly or indirectly, in the conduct of the enterprise's affairs through a pattern of racketeering activity. 18 U.S.C. § 1962(c). "To state a claim under § 1962(c), a plaintiff must allege '(1) conduct (2) of an enterprise (3) through a pattern (4) of racketeering activity.'" *Odom v. Microsoft Corp.*, 486 F.3d 541, 547 (9th Cir. 2006) (quoting *Sedima S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 496, 105 S. Ct. 3275, 87 L. Ed. 2d 346 (1985)). These requirements must be established as to each individual defendant. *Craig Outdoor Advertising Inc. v. Viacom Outdoor, Inc.*, 528 F.3d 1001, 1027 (8th Cir. 2008). Plaintiffs have not done so.

First, plaintiffs simply have failed to plead RICO with the requisite degree of particularity. Section X of the Complaint, PP 534-572, sets forth only conclusory boilerplate RICO allegations, with little factual specificity to establish the RICO enterprise, or each defendant's conduct in relation to the enterprise, the pattern of racketeering activity, and the predicate acts of mail fraud and wire fraud. For [*12] example, with regard to the "pattern of racketeering activity," Paragraph 550 alleges:

Defendants conducted the affairs of the

M&M Enterprise by a "pattern of racketeering activity," as defined by 18 U.S.C. § 1961(5), by committing or aiding and abetting in the commission of at least two acts of racketeering activity, *i.e.*, indictable violations of 18 U.S.C. §§ 1341 and 1343 as described above, within the past 10 years. In fact, Defendants have committed or aided and abetted in the commission of hundreds of acts of racketeering activity. Each racketeering act was related, had a similar purpose, involved the same or similar participants and method of commission, had similar results and impacted similar victims, including the Plaintiffs.

Similarly, with regard to the predicate acts, Paragraph 553 alleges:

For the purpose of executing and/or attempting to execute the above-described fraudulent scheme, Defendants, in violation of 18 U.S.C. § 1341 (mail fraud), placed in post offices and/or in authorized repositories, matter and things to be sent or delivered by the U.S. Postal Service, caused matters and things to be delivered by commercial interstate carriers, and received matter and things [*13] from the U.S. Postal Service and/or commercial interstate carriers, including, but not limited to, marketing and sale materials, financial information, correspondence, contract, sales and lending documents, escrow and title documents, and other materials relating to the properties sold to Plaintiffs.

These allegations are not pleaded with sufficient factual particularity. *Lancaster Community Hospital v. Antelope Valley Hospital Dist.*, 940 F.2d 397, 405 (9th Cir. 1991).

The complaint does not adequately allege facts showing that each defendant conducted the enterprise through a pattern of racketeering activity, in particular lacking facts for the individual broker defendants who are alleged to have been involved in only one transaction, or a couple of transactions within a relatively short amount of time. *Craig Outdoor Advertising Inc. v. Viacom Outdoor, Inc.*, 528 F.3d 1001, 1027 (8th Cir. 2008). The

complaint also does not adequately allege facts that each defendant who plaintiffs seek to hold liable under RICO acted with a common purpose. *Odom v. Microsoft Corp.*, 486 F.3d 541, 549 (9th Cir. 2005). The "common purpose" allegations, for example, allege only that:

537. Defendants have engaged [*14] in a common course of conduct and conspiracy with the common purpose of defrauding Plaintiffs into purchasing the Properties at artificially inflated prices. To achieve their common purpose, Defendants have associated-in-fact as an ongoing "enterprise" within the meaning of 18 U.S.C. § 1961(4).

567. The objects of the conspiracy were, and are: (a) to sell the Properties and other real property at artificially inflated prices; (b) to maximize sales for Defendants; and (c) to defraud Plaintiffs and other members of the public.

No facts are alleged to show a common purpose. Similarly, the complaint does not allege facts demonstrating that each defendant conducted or participated in the conduct of the enterprise's affairs, *i.e.* participated in the operation or management of the enterprise itself. *Reves v. Ernst & Young*, 507 U.S. 170, 183, 113 S. Ct. 1163, 122 L. Ed. 2d 525 (1993); *Walter v. Drayson*, 538 F.3d 1244, 1247-48 (9th Cir. 2008). Additionally, the complaint does not adequately allege that each defendant proximately caused plaintiff's damages. *Oki Semiconductor v. Wells Fargo Bank*, 298 F.3d 768, 774. The allegations are insufficient.

There are other pleading deficiencies as well. Plaintiffs seek to impose liability [*15] on several defendants through an alter ego theory, but the alter ego allegations are insufficient. No facts -- as opposed to conclusory assertions -- have been pleaded to support the alter ego theory. For example, Paragraph 53 alleges:

At all times alleged herein, M&M owned, managed, maintained, and controlled the activities of its agents M&M Investment and Sovereign Investment, as well as those entities' subsidiaries and affiliates. Therefore, the activities, acts, and omissions of M&M

Investment and Sovereign Investment were and are, in reality, the activities, acts, and omissions of M&M. Accordingly, M&M is fully responsible and liable for the wrongdoing of its agents as alleged in this complaint.

Similarly, paragraph 69 alleges:

At all relevant times, Waelti controlled and dominated the affairs of QSR, QSR One, and QSR II, directed the business and financial activities of those entities, used assets of the corporate entities for his personal use, and caused assets of those entities to be transferred to him personally without adequate consideration as well as to other business entities which he controlled. At all relevant times, each of those entities were a mere shell, instrumentality [*16] and conduit through which Waelti carried on his business, including his participation as a co-conspirator in Defendants; scheme.

Additionally, various entities are also alleged to be "at all relevant times, controlled by, and the alter-ego of, Morabito" and the QSR entities are alleged to have been "at all relevant times, controlled by, and the alter-ego of, Waelti." PP 55-63 (Morabito), PP 66-68 (Waelti). Conclusory allegations of "alter ego" status are not sufficient. *Neilson v. Union Bank of Cal.*, 290 F. Supp. 2d 1101, 1116 (C.D. Cal. 2003). If plaintiffs seek to hold any defendant liable under an alter ego theory, plaintiffs must allege facts from which a plausible inference could be drawn that a defendant is the alter ego of another.

The same pleading defect -- lack of factual specificity -- also undermines each of the other asserted claims, all of which rely on the same underlying allegedly fraudulent conduct. *Rule 9(b)* requires more.

Accordingly, the motions to dismiss for failure to plead the asserted claims with the required level of specificity are granted, with leave to amend.

Turning to defendant Morabito's motion to dismiss for lack of personal jurisdiction, the motion is [*17] denied without prejudice. As became clear at the hearing, if plaintiffs are successful in pleading a claim under RICO, there will be personal jurisdiction over Morabito

pursuant to the nationwide reach of *Section 1965(b)*. On the other hand, if plaintiffs are not successful in pleading a claim under RICO, then there is no basis for the court to exercise subject matter jurisdiction, and the question of personal jurisdiction over Morabito does not arise. Because the court has dismissed the RICO claim, albeit with leave to amend, there is no present need to address the issue of personal jurisdiction over defendant Morabito. For the same reason, there is also no reason to require Morabito to appear for a deposition to be conducted on personal jurisdiction issues. Thus, Morabito's motion for a protective order is granted and plaintiffs' motion to compel the deposition is denied.

The Sovereign defendants' motion to strike plaintiffs' jury demand is denied without prejudice, as are the alternative motions to sever or transfer venue. For the reasons stated at the hearing, and as a matter of case management, the court prefers to take up the issues regarding jury waiver, venue, severance, and [*18] the

like only after the factual basis for plaintiffs' claims and defendants' liability is pleaded with the requisite degree of specificity.

Accordingly, for the foregoing reasons, the motions to dismiss the complaint are granted in part. Plaintiffs shall have twenty days' leave in which to file and serve an amended complaint. Plaintiffs' motion to compel the deposition of defendant Morabito is denied; defendant Morabito's motion for a protective order is granted for the reasons stated herein. The Sovereign defendants' motion to strike the jury demand is denied without prejudice.

DATED: 1/29/10

/s/ Ronald M. Whyte

RONALD M. WHYTE

United States District Judge

▷
HOLLYWOOD CLEANING & PRESSING CO. (a
Corporation), Appellant,
v.
HOLLYWOOD LAUNDRY SERVICE, INCOR-
PORATED (a Corporation), Respondent.

Supreme Court of California.
L. A. No. 12102.
December 28, 1932.

[1] AP-
PEAL—JUDGMENT-ROLL—PRESUMPTIONS.

When an appeal is taken on the judgment-roll alone nothing can be assumed or considered that does not appear upon the face of the judgment-roll, and all intendments and presumptions must be made in support of the judgment.

[2] CONTRACTS—ACTION FOR
BREACH—CORPORATIONS—CORPORATE
ENTITY—PARTIES.

In this action for damages for breach of a written contract, wherein defendant laundry corporation agreed to solicit dry cleaning, dyeing and pressing business and to turn the same over to plaintiff, the burden of proof was on plaintiff, and in the absence of any finding to the contrary it must be conclusively assumed, on appeal on the judgment-roll alone, that, contrary to plaintiff's contention, a second corporation, which owned all the stock of defendant corporation, acquired certain business in good faith and without any intent of assisting defendant in evading liability under the contract.

[3] ID.—CORPORATIONS—DISREGARDING
CORPORATE EXISTENCE.

Bad faith in one form or another must be shown before the court may disregard the fiction of separate corporate existence; and the mere fact that one or two individuals or corporations own all of the stock of a corporation is not of itself sufficient to cause the court to disregard the corporate entity of such corporation and to treat it as the *alter ego* of

the individual or corporation that owns its stock, but, in addition, it must be shown that there is such a unity of interest and ownership that the individuality of such corporation and the owner or owners of its stock has ceased, and it must further appear that the observance of the fiction of separate existence would, under the circumstances, sanction a fraud or promote injustice.

APPEAL from a judgment of the Superior Court of Los Angeles County. Edward T. Bishop, Judge. Affirmed.

The facts are stated in the opinion of the court.

*125 Meserve, Mumper, Hughes & Robertson and Baldwin Robertson for Appellant.

Walter H. Hewicker and O'Melveny, Tuller & Myers for Respondent.

THE COURT.

Plaintiff appeals from that portion of a judgment adverse to it, rendered in an action brought by plaintiff for damages for breach of a written contract by defendant. The appeal is taken on the judgment-roll alone so that none of the evidence produced before the trial court is before us. Defendant has separately appealed from those portions of the judgment adverse to it. (See *Hollywood Cleaning & Pressing Co. v. Hollywood Laundry Service, Inc.* (L. A. No. 12345), post, p. 131 [17 Pac. (2d) 712].)

*126 The facts giving rise to the controversy between the parties are as follows:

On April 18, 1924, plaintiff and defendant entered into a written contract by the terms of which defendant agreed that for a period of ten years it would solicit, together with its general laundry business, dry cleaning, dyeing and pressing business, and would turn over to plaintiff exclusively all the dry cleaning, dyeing and pressing business it thus acquired. Defendant agreed that all dur-

ing the term of the contract it would advertise for and solicit such business in order to secure the maximum thereof. The contract provided that the drivers of defendant should pick up the cleaning, dyeing and pressing work from its customers and should deliver the same to plaintiff's plant, and should redeliver the goods to the customers after plaintiff had completed it. Plaintiff agreed to furnish special accommodations at its plant for handling the business secured by defendant. Defendant was to collect for the work, and to retain 37 1/2 per cent thereof for itself and to remit the balance to plaintiff. There was an express provision to the effect that defendant "agrees to include in this agreement any other laundry plant that it may acquire during the continuation of this agreement, provided that any other agreement does not exist covering its dry-cleaning, dyeing and pressing business with the other laundry plant".

For a short time after the agreement was entered into both parties lived up to its terms and conditions. The court found that about January, 1925, defendant "without cause or justification breached said agreement and sent only a part of its dry-cleaning, dyeing and pressing business to the plant of plaintiff, and thereafter from on or about the 21st day of March, 1925, without cause or justification defendant failed and refused, in all respects and in every respect, to comply with the terms of said written agreement". Plaintiff elected to treat the breach by defendant as terminating the contract, and brought this action. The trial court awarded damages to plaintiff, in the amount that it found plaintiff would have made as profit had the contract been fully performed. The correctness of that award is not involved on this appeal. Defendant has perfected a separate appeal from that award. (*Post*, p. 131.) The present appeal is concerned with the following facts: The *127 trial court found that at the time the written contract was entered into all of the capital stock of defendant Hollywood Laundry Service, Incorporated, was owned either by Frank L. Meline, an individual, or Frank L. Meline, Inc., a corporation; that all of the capital stock of Frank L.

Meline, Inc., was then owned and is still owned by Frank L. Meline; that on various dates during the period included within the contract, Frank L. Meline, Inc., acquired all the capital stock and assets of four laundry companies; that defendant Hollywood Laundry Service, Incorporated, did not cause these laundries acquired by Frank L. Meline, Inc., to turn their dry-cleaning, dyeing and pressing business over to plaintiff; that if defendant had required these newly acquired laundries to turn their dry-cleaning, dyeing and pressing business over to plaintiff during the term of this contract, plaintiff would have made a profit of approximately \$10,000 from such business. However, the trial court refused to include this amount as damages for the reason that it found that "it is not true that it was intended or contemplated by the parties hereto, or that said written agreement provided, that any other laundry plants acquired by either Frank L. Meline or Frank L. Meline, Inc., during the terms of said agreement should be included in the terms of said agreement of April 18, 1924". The trial court also found that "it is further true that defendant has not acquired any laundries since the execution of said agreement".

Plaintiff has appealed solely from this portion of the judgment refusing to award damages for the failure of defendant Hollywood Laundry Service, Incorporated, to turn over to plaintiff the dry-cleaning, dyeing and pressing business of the four laundries acquired by Frank L. Meline, Inc. It is the contention of the plaintiff that under the above circumstances a situation is presented where this court should hold, as a matter of law, that the separate corporate existence of Frank L. Meline, Inc., should be disregarded and that the laundries acquired by it must be deemed to have been acquired by defendant corporation within the meaning of the contract. Plaintiff asks that this be done, even though it failed to plead or prove, so far as the findings disclose, that title was taken to the newly acquired laundries by Frank L. Meline, Inc., instead of in the name of Hollywood Laundry Service, Incorporated, with the intent *128 or for the purpose of evading

liability under the contract. For all that appears on the record before us the corporation Frank L. Meline, Inc., acquired these laundries in good faith without any intent of assisting defendant to evade liability under the contract. No facts are pleaded or found which would indicate that to recognize the separate corporate entities of the two corporations would, under the circumstances, sanction a fraud or promote injustice. It must be remembered that this appeal is taken on the judgment-roll alone. None of the evidence introduced before the trial court is before us.

(1) It is, of course, elementary that when an appeal is taken on the judgment-roll nothing can be assumed or considered that does not appear upon the face of the judgment-roll. All intendments and presumptions must be made in support of the judgment.

(2) In the absence of any finding to the contrary we must conclusively assume that Frank L. Meline, Inc., acquired these laundries in good faith and without any intent of assisting defendant in evading liability under the contract. The burden of proof to show the contrary was on the plaintiff and in the absence of a record, we must necessarily assume that plaintiff failed to sustain the burden imposed upon it. Keeping these well-settled rules in mind, we can come to no other conclusion but that the judgment appealed from should be affirmed. The trial court expressly found that it was not intended or contemplated by the parties to the contract that any laundries acquired by Frank L. Meline or Frank L. Meline, Inc., should be included within the contract. Under ordinary circumstances we would have to assume that the above finding was amply supported by the evidence. However, we find in the record a stipulation between counsel representing the respective parties to the effect that "no evidence whatever was offered or received during the trial of this action touching the intention or contemplation of the parties to the contract of April 18, 1924, as to whether any other laundry plants acquired by either Frank L. Meline or Frank L.

Meline, Inc., during the term of said agreement should be included within the provisions thereof". Assuming that this stipulation may be considered as properly before us (but see *Spreckels v. Ord*, 72 Cal. 86 [13 Pac. 158]; *Spinetti v. Brignardello*, 53 Cal. 281; *People v. Hawes*, 41 Cal. 632; 2 Cal. Jur., p. 519, sec. 258), a question we do not find *129 it necessary to now decide, we fail to see how the fact that that finding is unsupported by the evidence can assist the plaintiff. The finding that defendant did not acquire any new laundries stands unimpaired. All that the record shows, even if this last-mentioned finding were to be disregarded, is that the plaintiff corporation entered into a contract with defendant, Hollywood Laundry Service, Incorporated; that all of the stock of defendant was owned either by Frank L. Meline or Frank L. Meline, Inc.; that Frank L. Meline owned all the stock of Frank L. Meline, Inc. What other stock was owned by Frank L. Meline, Inc., if any, does not appear. The contract purports to be between plaintiff and defendant alone. It does not purport to bind any other person or corporation, whatsoever. No facts are alleged or found which would indicate that to recognize the separate corporate entities of the two corporations would sanction a fraud or promote an injustice. In other words, plaintiff's contention narrows down to the contention that the separate corporate entities of the two corporations should be disregarded solely because all of the stock of defendant corporation is owned by another corporation, Frank L. Meline, Inc., or by Frank L. Meline, and that the last-named party owns all the stock of Frank L. Meline, Inc. This has never been the rule in this state.

(3) Whatever may be the rule in other jurisdictions, the rule is well settled in this state that the mere fact one or two individuals or corporations own all of the stock of another corporation is not of itself sufficient to cause the courts to disregard the corporate entity of the last corporation and to treat it as the *alter ego* of the individual or corporation that owns its stock. In addition it must be shown that there is such a unity of interest and ownership

that the individuality of such corporation and the owner or owners of its stock has ceased; and it must further appear that the observance of the fiction of separate existence would, under the circumstances, sanction a fraud or promote injustice. Bad faith in one form or another must be shown before the court may disregard the fiction of separate corporate existence.

In the leading case of *Erkenbrecher v. Grant*, 187 Cal. 7, 11 [200 Pac. 641], the rule is stated as follows:

“The finding of the trial court that the company acquired the notes because the then holder of them was pressing *130 plaintiff in his capacity as indorser for payment does not negative the separate entity of the company. In the absence of any dishonest motive or intention to accomplish a wrong, and, as we have said, none was proven, we fail to discover any objection whatever to plaintiff directing the company to purchase the notes. If it be assumed that he caused their purchase for the reason that it was not then convenient for him to meet his obligations as indorser, there would still be wanting the elements to which we have referred, and the presence of which we hold is essential to justify treating plaintiff and the company as identical—as a unit. In order to cast aside the legal fiction of distinct corporate existence as distinguished from those who own its capital stock, it is not enough that it is so organized and controlled and its affairs so managed as to make it ‘merely an instrumentality, conduit, or adjunct’ of its stockholders, but it must further appear that they are the ‘business conduits and *alter ego* of one another’, and that to recognize their separate entities would aid the consummation of a wrong. Divested of the essentials which we have enumerated, the mere circumstance that all of the capital stock of a corporation is owned or controlled by one or more persons, does not, and should not, destroy its separate existence; were it otherwise, few private corporations could preserve their distinct identity, which would mean the complete destruction of the primary object of

their organization.”

In *Wood Estate Co. v. Chanslor*, 209 Cal. 241, 245 [286 Pac. 1001], it is stated: “The law is well settled that, in order to cast aside the legal fiction of a distinct corporate existence, it must appear that the corporation is the business conduit and *alter ego* of its stockholders, and that to recognize it as a separate entity would aid in the consummation of a wrong. In other words, not only must it appear that one man or two men own the stock and control the policies, but it must also be shown that there is such a unity of interest and ownership that the individuality of such corporation and such person or persons has ceased; and it must further appear from the facts that the observance of the fiction of separate existence would, under the circumstances, sanction a fraud or promote injustice.” (See, also, *D. N. & E. Walter & Co. v. Zuckerman*, 214 Cal. 418 [6 Pac. (2d) 251, 79 A. L. R. 329]; *131 *Minifie v. Rowley*, 187 Cal. 481 [202 Pac. 673]; *Llewellyn Iron Works v. Abbott Kinney Co.*, 172 Cal. 210 [155 Pac. 986]; *Wenban Estates, Inc., v. Hewlett*, 193 Cal. 675 [227 Pac. 723]; *Ellet v. Los Altos Country Club Properties*, 88 Cal. App. 740 [264 Pac. 270].)

Under the principles enunciated in the above cases, and for the reasons already advanced it is obvious that on the record before us it is impossible for this court to disregard the separate existence of Frank L. Meline, Inc., and to treat it and the Hollywood Laundry Service, Incorporated, as the *alter ego* of Frank L. Meline.

For the foregoing reasons that portion of the judgment appealed from by plaintiff is hereby affirmed.

Rehearing denied.

Cal. 1932.
Hollywood Cleaning & Pressing Co. v. Hollywood Laundry Service
217 Cal. 124, 17 P.2d 709

END OF DOCUMENT

1993 WL 522521 (Cal.St.Wat.Res.Bd.)

State Water Resources Control Board
State of California
Division of Water Rights

*1 IN THE MATTER OF THE PETITION OF
LINDSAY OLIVE GROWERS

ORDER NO. WQ 93-17

November 18, 1993

For Review of Cleanup and Abatement Order No. 92-708 of the California Regional Water Quality Control Board, Central Valley Region. Our File No. A-823.

BY THE BOARD:

Lindsay Olive Growers seeks review of Cleanup and Abatement Order No. 92-708 (Order or CAO) issued by the Executive Officer of the California Regional Water Quality Control Board, Central Valley Region (Regional Water Board). The Order requires the City of Lindsay and the Petitioner to clean up and abate the effects of the discharge of wastewater to olive brine disposal ponds operated on behalf of Petitioner by the City. Petitioner has requested that it be removed from the CAO or that the CAO be rescinded. Petitioner argues that it was improperly named as a party to the Order and that the process by which the Order was issued violated legal requirements.

For the reasons hereafter stated, we find no defects with the Order or the process by which the Order was issued. We therefore affirm the Cleanup and Abatement Order issued by the Regional Water Board.

I. BACKGROUND

The City of Lindsay is in central Tulare County, about 15 miles east of Tulare, and about 15 miles southeast of Visalia. Petitioner's olive processing plant has been in the City since 1916. During operations, olive processing wastewater was generated which contained high amounts of dissolved solids.

Wastewater from the plant is classified as "designated waste" in accordance with Title 23, Cal.Code of Regs. Section 2510 et seq. (Chapter 15). Designated waste is defined as "non-hazardous waste which consists of or contains pollutants which, under ambient environmental conditions at the waste management unit, could be released at concentrations in excess of applicable water quality objectives, or which could cause degradation of waters of the State". 23 Cal.Code of Regs. § 2522(a)(1). Wastewater sampling indicates that electrical conductivity (EC) has ranged from 1,020 to 61,000 umhos/cm and chloride concentration has ranged from 80 milligrams per liter (mg/l) to 20,700 mg/l. "Typical" EC of the wastewater has been above 4,000 umhos/cm and chloride has been above 1,000 mg/l. Background EC in the ground water is approximately 1,000 umhos/cm, and chloride concentration is approximately 70 mg/l. The recommended drinking water standard for EC is 900 umhos/cm and for chloride is 250 mg/l, and the maximum allowable drinking water standard for EC is 1600 umhos/cm and

chloride concentration is 500 mg/l. 22 Cal.Code of Regs. § 64473.

Beginning in 1916, wastewater from Petitioner's plant has been discharged to the City sewer. That wastewater was in turn discharged from the Lindsay Sewage Treatment Plant to unlined ponds and fields. In 1962, the Department of Water Resources (DWR) determined that due to its salinity, the wastewater discharged by the Lindsay sewage treatment plant was unsatisfactory for most crops. DWR determined that approximately half the flow and most of the salt load to the City's sewage system was contributed by the Petitioner's plant. It also determined that ground water had been degraded by saline wastewater migration from the plant.

*2 As a result of the DWR study, the Regional Water Board imposed waste discharge requirements (WDRs) on the City (Resolution No. 63-183) for the sewage effluent, which still contained the olive brine wastewater component. The WDRs set effluent limits for TDS, chloride, and sodium ratio. In order to comply with the WDRs, the City constructed four new ponds with compacted soil for the brine discharge. Wastewater from Petitioner was discharged to the sewer during low flow periods (i.e., early morning), and when it reached the sewage treatment plant, it was diverted to the brine ponds. The discharge was diverted to the new ponds when the EC exceeded a certain level. During higher flow hours, domestic wastewater was discharged to unlined ponds and fields as it was before construction of the brine ponds.

The plan was ineffective at preventing saline wastewater from being discharged with the domestic wastewater. In 1966, a series of inspections by DWR found chloride concentrations in the domestic wastewater ponds as high as 3,300 mg/l, well in excess of the 450 mg/l effluent limit for chloride. As a result, the Regional Water Board adopted Cease and Desist Order (C & D) No. 67-84 on the City.

In response to the C & D, the City built the present ponds exclusively to handle the brine wastewater from Petitioner's processing plant. The ponds were built between 1967 and 1974, and were lined with a single 10 mil PVC liner. At least one of the ponds (Pond F) was built by Petitioner at its own expense. In 1969, the City completed a dedicated outfall line from Petitioner's processing plant to the new ponds. One of the ponds (Pond D) was reconstructed in 1985 with a 30 mil "hypalon" liner.

The ponds and outfall were financed by local bonds, and state and federal loans and grants. The City in turn assessed Petitioner for repayment of the local bonds and the state loans. As a result of this work, the Regional Water Board rescinded the C & D in 1971 (Order No. 71-331).

In the early and mid 1980s, DWR determined that the disposal of Petitioner's brine wastewater at this site was continuing to impair ground water quality. Monitoring wells at the site exhibited salinities well in excess of background and drinking water standards. Ground water EC was measured as high as 14,000 umhos/cm and chloride concentration was measured as high as 5,705 mg/l. Numerous domestic and agricultural wells in the vicinity were polluted, with chloride concentrations as high as 5,686 mg/l and EC as high as 14,900 umhos/cm. Ground water is the only drinking water source in the area. Odors had also become a perennial problem. Numerous complaints regarding odors generated by the ponds have been received each year from 1981 to 1992. The ground water pollution and odors were violations of the City's WDRs, which prohibited the creation of pollution or nuisance conditions.

In 1984, the State Water Resources Control Board (State Water Board) revised Chapter 15 (then called "subchapter 15") standards for waste discharges to land. 23 Cal.Code of Regs. § 2510, et seq. The single-lined brine disposal ponds did not meet the minimum construction standards contained in Chapter 15 for containing designated waste (Class II surface impoundments). Therefore, in 1987, the Regional Water Board adopted

WDRs (Order No. 87-054) requiring the City to close or retrofit the ponds in accordance with Chapter 15.

*3 In 1991 the Regional Water Board determined that the City had not complied with the 1987 WDRs. The Board adopted C & D Order No. 91-151 requiring the City to cease generation of nuisance odors, close or retrofit the brine ponds in accordance with Chapter 15, develop a corrective action program for ground water remediation, and evaluate alternatives for a water supply to affected private well owners. The C & D remains in effect.

In 1992, the Executive Officer issued CAO No. 92-708 to the City and to the Petitioner. The Cleanup and Abatement Order required both parties to cease generation of nuisance odors, close or retrofit the ponds in accordance with Chapter 15, develop a corrective action program for ground water remediation, and provide an alternative water supply to affected private well owners. It is this latest order which is the subject of this review.

II. CONTENTIONS AND FINDINGS

1. Contention: Petitioner contends that it is not a responsible party for contamination from the City of Lindsay's ponds because it discharges lawfully to a permitted municipal system. Such discharges, it argues, are exempted from regulation under the Water Code.^[FN1]

Finding: The California Water Code does not insulate Petitioner from responsibility for the discharges to the City's sewage system. There is no express exemption, and the terms of Water Code Section 13304 are broad enough to include responsibility on behalf of Petitioner.

Water Code Section 13304 authorizes the Regional Water Board to issue a CAO to any person who "discharges waste ... in violation of any waste discharge requirements" or any person who "causes or permits ... any waste to be discharged or deposited where it is, or probably will be, discharged into the waters of the state and creates, or threatens to create, a condition of pollution or nuisance."

Petitioner argues that no WDRs were issued naming Petitioner, therefore it was never in violation of WDRs. That contention is true, but not relevant. Petitioner further argues that it never "caused or permitted" pollution of ground water at the Facility. Petitioner contends the City owned and operated the Facility, and Petitioner had no control over its operation, therefore Petitioner cannot be held liable for problems at the Facility. With this contention, under the facts of this case, we disagree.

Petitioner argues that once it disposed of the waste in the City's sewer system, it "had no control over the treatment and handling of the waste." Petition at 8. The facts in the record belie this contention. The relationship between Petitioner and the City has been such that in effect Petitioner shared control of the operation of the Facility. According to the 1968 contract between the City and Petitioner, the "size, dimension, design, and capacity of the industrial waste line" had to be mutually agreed upon by the City and Petitioner (then Consolidated Olive Growers). The Facilities described by the agreement were for the exclusive use of Petitioner, although the agreement allowed other users. Generally, all direct costs were to be paid by users of the system, i.e., Petitioner. Petitioner had to approve any additional industrial users of the system and the user fee charged those users. The maximum term of the bonds to be issued by the City to finance the ponds and the waste line was set at 25 years, and "[a]ny shorter term [was] at the sole discretion of" Petitioner. Petitioner was the sole user of a system that includes 190 acres of ponds and a dedicated outfall line between the plant and the ponds. All costs for the system, including construction, operation, and maintenance expenses and repayment of construction bonds have been borne by Petitioner until it ceased operations in September 1992. Petitioner in fact built one of the ponds (Pond F) at its own expense. Petitioner controlled operation of the facility, repaying the debt incurred by the

City on its behalf, exercising prior approval over design, terms of the debt, and connection of additional users. The pollution has been caused by the high chloride concentration and EC from Petitioner's wastewater.

*4 In short, the record demonstrates that: the Facility was constructed for the sole purpose of receiving Petitioner's wastewater; the Facility was financed by the City on behalf of Petitioner; all construction and operating expenses have been paid by Petitioner until it ceased operations; and the ground water pollution is due to waste from Petitioner. Based on such facts, it was appropriate to include Petitioner within the broad coverage of Water Code Section 13304.

Petitioner also contends that its discharge to a community sewer system is insulated from liability under the Water Code and the Federal Clean Water Act. A discharger of wastewater to a community sewer system is not required to file a report of waste discharge with the Regional Water Board. Water Code § 13260(a)(1). However, the fact that Petitioner does not have to file a report of waste discharge does not insulate Petitioner from being subject to other sections of the Water Code.

The Federal Clean Water Act does not apply in this case because no NPDES permit or other action under federal law is at issue in this case.

Petitioner was properly named as a party to the CAO for cleaning up and abating the effects of the discharge to the ponds because it had caused or permitted wastewater with high chloride concentrations and EC to be discharged or deposited in unlined and inadequately lined ponds, where it was discharged into the ground waters of the State and created a condition of pollution and nuisance.

2. Contention: Petitioner argues that it cannot be responsible for cleanup and abatement of the ponds, because Water Code Section 13304(f) states that cleanup and abatement orders cannot impose any new liability for acts occurring before January 1, 1981.

Finding: This contention is incorrect for two reasons. First, the record clearly reflects that new contamination and nuisance conditions have occurred since 1981. In addition, discharges which caused nuisance conditions prior to 1981 did not comply with the existing law at that time.

The ponds were constructed in 1969, and contamination was documented before 1981. Petitioner argues that the Facility was in compliance until 1985 when Chapter 15 was adopted, and that any pollution reaching ground water at the site is most likely due to waste deposited prior to 1981. Petitioner contends that since actions under Section 13304 do not impose any new liability for acts occurring before January 1, 1981 if the acts were not in violation of laws and regulations at the time they occurred, a CAO cannot be applied to Petitioner in this case.

The record does not support Petitioner's contention that all pollution of ground water has resulted from waste discharged prior to 1981. Much of the ground water pollution at the Facility is due to leakage of brine waste from the ponds after 1981 (and 1985). Many of the ponds have contained wastewater continuously since 1981. Ground water quality in a monitoring well adjacent to these ponds (MW-20) has continued to decline since the well was installed, while ground water quality in a well adjacent to ponds dry since 1985 (MW-06) has improved. This evidence indicates that the ponds are still leaking and polluting ground water. In addition, the ponds have created nuisance odor conditions every year since 1981.

*5 Second, though Water Code Section 13304(f) limits strict liability for acts before January 1, 1981, it does not limit liability for acts that were in violation of existing laws or regulations at that time. The leakage and pollu-

tion which resulted from Petitioner's discharge before 1981 was a violation of the law in existence at the time. Since 1872, California law has prohibited the creation of a public nuisance. In 1925, water pollution was held by the courts to be a public nuisance. And since 1949, California law has expressly prohibited any discharge of waste in a manner which results in pollution, contamination, or nuisance. Additionally, the Porter-Cologne Water Quality Act of 1969 defined nuisance and authorized Regional Water Boards to order cleanup. The definition included anything that: (1) is injurious to health, or is indecent or offensive to the senses, or an obstruction to the free use of property, so as to interfere with the comfortable enjoyment of life or property; (2) affects at the same time an entire community or neighborhood, or any considerable number of persons, although the extent of the annoyance or damage inflicted upon individuals may be unequal; and (3) occurs during or as a result of the treatment of wastes.

It is clear from the facts that the Petitioner wastewater disposal meets the definition of a nuisance under the 1969 law: Petitioner's wastewater was piped to the brine ponds; the wastewater was "treated" by aeration and evaporation; the "treated" wastewater polluted the ground water, producing high chloride concentrations and EC and creating odors which were offensive to the senses; and domestic and agricultural wells in the community were adversely impacted.

Evidence in the record indicates that the ponds were leaking and polluting ground water before, during, and after 1981. Odors from the facility have created documented nuisance conditions every year since 1981. Nuisance conditions, leakage, and pollution which occurred before 1981 was a violation of statutes in existence at the time, and was actionable under law at the time. Thus, Petitioner's contention that Water Code Section 13304(f) insulates it from responsibility is without merit.

3. Contention: Petitioner argues that it cannot be named as a responsible party in the CAO because the Tulare County Superior Court has already ruled on the question of Petitioner's liability.

Finding: The Superior Court's ruling is not dispositive here, because (1) the court case did not involve the Regional or State Water Board as a party, and (2) the burden of proof in the private litigation is different from the showing that the Regional Water Board needs to include a party in a CAO. In private litigation initiated by landowners with polluted wells, the Superior Court held that the City, not the petitioner, was responsible for the pollution. Petitioner seeks to assert the legal doctrine of res judicata against the Regional Water Board. That doctrine allows a ruling in one case to be used in a different case either against the same parties or against different parties under very limited circumstances. The fact that the Board was not a party to the earlier litigation, and the different burdens of proof involved preclude the use of the doctrine in this case. That ruling is binding only on the parties involved, and does not preclude the Regional Water Board from proceeding with the cleanup and abatement order against Petitioner.

*6 4. Contention: Petitioner contends that the CAO was improperly issued by the Regional Water Board staff—not the Executive Officer—an action which is an impermissible delegation of authority.

Finding: The CAO was properly issued by the Executive Officer of the Regional Water Board. This contention is really two separate arguments. First, petitioner claims that the signature on the CAO was not the Executive Officer's but was instead signed by the Principal Engineer for the Fresno office. Petitioner was correct in asserting that the Principal Engineer cannot issue a CAO, but that did not happen here. The CAO was signed by the Principal Engineer on behalf of the Executive Officer. It was the Executive Officer's signature line, and the order went out under the Executive Officer's name. The Principal Engineer is authorized to sign documents in

the Executive Officer's absence. There is nothing improper in this case.

Petitioner also argues that the CAO was, in effect, an amendment of the cease and desist order that had been issued against the City, and as such, could be issued only after a hearing by the Regional Water Board. Thus, Petitioner contends that no staff, not even the Executive Officer, could issue the Order.

Cleanup and Abatement Order No. 92-708 did not modify either the C & D or the WDRs regulating the facility, and did not affect either of their requirements or applicability. The Order was a CAO issued pursuant to Water Code Section 13304. All actions required by the CAO are designed to clean up or abate the effects of the discharge of wastewater from Petitioner's plant, and fall within the authority of a CAO as established by statute. The Water Code allows delegation of the issuance of a CAO to the Executive Officer. The Regional Water Board has in fact delegated duties and powers to the Executive Officer, which include issuance of a CAO, in Resolution No. 70-118. In the absence of the Executive Officer, the Assistant Executive Officer, or in his/her absence, the Principal Engineer may sign for the Executive Officer. The Principal Engineer of the Fresno office signed the CAO upon authorization of the Executive Officer.

Finally, it must be noted that the Regional Water Board held a hearing on October 23, 1992 to consider amendments of the time schedules contained in the CAO. At the close of the hearing, the Regional Water Board noted to maintain the timetable, thus ratifying it.

5. Contention: Petitioner claims that the lack of a hearing before issuance of the CAO violated its constitutional right to due process.

Finding: There is no constitutional defect either with the CAO process or with the process afforded to Petitioner. Petitioner argues that the issuance of the CAO was an action that required a public hearing, under the California and U.S. Constitutions. However, no hearing was held, and there was no provision for an automatic hearing to review the administrative action. Therefore, Petitioner argues that its due process rights were violated.

*7 Following issuance of the CAO, Petitioner requested a hearing before the Regional Water Board to reconsider the dates and time schedules in the CAO. Board staff responded by scheduling a hearing at the next regular Board meeting (October 23, 1992). This hearing was held as mentioned above. Petitioner did not attend. Additionally, Water Code Section 13320 provides that any party may petition the State Water Board for review of a Regional Water Board action or failure to act. Petitioner has exercised this option, and is receiving its second opportunity for review. There is no constitutional violation here.

6. Contention: Petitioner contends that the CAO was issued in violation of California Environmental Quality Act (CEQA).

Finding: The CAO cites 14 Cal.Code of Regs. Section 15321(a) to reference the categorical exemption from compliance with CEQA. Petitioner suggests two other exemptions that might also apply: 14 Cal.Code of Regs. Sections 15307 and 15308. Petitioner then argues why these sections would not be appropriate. These sections may or may not have applied in this case; however, the Regional Water Board relied on the cited section.

Petitioner argues that in any case an exemption only applies when "it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment." Petitioner argues that the CAO may have significant impacts on the environment (e.g., through closure of the ponds), and therefore the exemptions should not have applied.

The issuance of an enforcement order is categorically exempt from CEQA in accordance with 14 Cal.Code of Regs. Section 15321 and Public Resources Code Sections 21083 and 21087. While some of the alternatives which petitioner may choose to comply with the CAO may have "a significant effect on the environment," these alternatives are by no means the only ones available to the petitioner. Independent CEQA review will occur at the time that Petitioner chooses a remedy and seeks the appropriate permits and approvals. If the chosen alternatives will indeed have a significant adverse affect on the environment, then a categorical exemption would be inappropriate. At this time, however, the Regional Water Board is simply instructing Petitioner to clean up and abate the effects of the discharge, without specifying manner of compliance. At this stage it is unlikely that cleanup and abatement itself will have an adverse impact on the environment. The Regional Water Board action was properly exempt from CEQA according to Section 15321(a).

7. Contention: Petitioner was not named in Cease and Desist Order 91-151 issued in 1991, nor in any of the prior orders issued by the Regional Water Board governing discharges to the Lindsay Ponds and, thus, is not responsible for any violations of any conditions in such orders or for failure to act thereon.

Finding: Cease and Desist Order No. 91-151 was issued in accordance with Water Code Section 13301 against the City for failure to comply with WDRs Order No. 87-054. A C & D can only be issued for violations of WDRs. Since Petitioner was not issued WDRs, it was not subsequently named on the C & D.

*8 Petitioner is correct in its assertion that it is not responsible for violations of the C & D Order No. 91-151 or the WDRs on which the C & D was based. However, the Board's issuance of a C & D against the City for pollution from the brine ponds does not preclude the Board from issuing a CAO to Petitioner if the criteria established in Water Code Section 13304 are met. The findings in CAO No. 92-708 meet the criteria of Water Code Section 13304.

The CAO does not hold Petitioner liable for violations of WDRs. Instead, Petitioner is named as a party to the CAO because it caused or permitted ... olive brine waste to be discharged into waters of the State and created conditions of pollution and nuisance. As discussed above, Petitioner's plant was the sole source of all wastes discharged to the ponds, and the pollution at the Facility is due the Petitioner wastewater.

IV. ORDER

IT IS HEREBY ORDERED that the Cleanup and Abatement Order is affirmed.

FN1. All contentions not discussed in this order are denied for failure to raise substantial issues appropriate for review. Title 23, California Code of Regulations, Section 2052(a)(1). *People v. Barry* (1987) 194 Cal.App.3d 158, 139 Cal.Rptr. 349.

1993 WL 522521 (Cal.St.Wat.Res.Bd.)

END OF DOCUMENT

1996 WL 101751 (Cal.St.Wat.Res.Bd.)

State Water Resources Control Board
State of California
Division of Water Rights

*1 IN THE MATTER OF THE PETITIONS OF COUNTY OF SAN DIEGO, CITY OF NATIONAL CITY,
AND CITY OF NATIONAL CITY COMMUNITY DEVELOPMENT COMMISSION

Order No. WQ 96-2

Our File Nos.

A-898, A-973, A-980, A-980(a), and A-980(b)

February 22, 1996

For Review of Waste Discharge Requirements Order No. 88-57, Addenda Nos. 2 and 4, and Cleanup and Abatement Order No. 95-66 of the California Regional Water Quality Control Board, San Diego Region

BY THE BOARD:

This order addresses five petitions filed by three separate entities concerning waste discharge requirements (WDRs) and a cleanup and abatement order (CAO) issued by the California Regional Water Quality Control Board, San Diego Region (SDRWQCB). The matters have been consolidated for consideration by the State Water Resources Control Board (SWRCB) because they are closely related factually and legally.^[FN1]

These matters involve a complex procedural history involving several parties and several SDRWQCB orders. Despite this procedural complexity, the essential question is whether each of the petitioners, having had some level of involvement with a landfill known as the Duck Pond Landfill, is appropriately named in a WDR order or a CAO regarding water quality problems at the landfill. The three petitioners are San Diego County (County), the City of National City (City), and the City of National City Community Development Commission (CDC or Commission). Boulevard Investors owns land overlying the landfill, but has not challenged inclusion in the orders.

I. BACKGROUND

The County operated the Duck Pond Landfill, a small, 2 1/2-acre site, under a lease between 1960 and 1963 as a disposal site for nonhazardous municipal waste pursuant to SDRWQCB WDR Order No. 60-R26. The County was the landfill's only operator. The landfill ceased accepting waste in 1963. Thereafter, the SDRWQCB rescinded Order No. 60-R26 by its issuance of Order No. 73-12. The property apparently sat vacant in a post-closure state for some two decades following its closure.

Around 1984 the CDC became involved in a plan to purchase the property in order to develop the National City Mile of Cars. Under the plan, the Commission would purchase the property from the County and later transfer the property to a private investor who would actually develop the property. The Commission proceeded to buy the property, and later sold it to Boulevard Investors (the present owner of much of the property) who sub-

sequently built a car dealership on part of the property.

In 1987 the SDRWQCB adopted WDR Order No. 87-55, which named the City of National City^[FN2] as operator of the Duck Pond Landfill, assigning to the City the responsibility to properly maintain the site in an adequate post-closure condition as required by Title 23, Division 3, Chapter 15 (Post-Closure Regulations). Generally, the SDRWQCB order requires ongoing surface and subsurface monitoring and surface maintenance. Upon conveyance of the property to Boulevard Investors, Addendum No. 1 to Order No. 87-55, dated April 24, 1988, was adopted by the SDRWQCB, replacing National City with Boulevard Investors as the entity solely responsible for post-closure maintenance. According to the SDRWQCB and the CDC, Boulevard Investors was expected to assume responsibility for known problems with the landfill, including subsidence resulting in ponding of stormwater, leaking sewer lines beneath the surface, and other potential water quality concerns.

*2 Several years later, according to the SDRWQCB, monitoring reports disclosed evidence of impacts upon the water quality beneath the site, apparently caused by the landfill. The record in this matter contains documentation of communications between the SDRWQCB and the parties regarding the apparent leakage from the landfill, and efforts of the SDRWQCB staff to compel responsive action.^[FN3] Given this evidence of water quality problems, in January 1994, the SDRWQCB notified the parties of its intent to again modify the WDRs by including the names of all the parties having previous involvement with the property as responsible under the post-closure WDRs.

A hearing was held on February 10, 1994, and Addendum No. 2 to Order No. 87-55 was adopted by the SDRWQCB. Finding No. 5 of that Addendum indicates that the City, the CDC and Boulevard Investors are named in the WDRs because of their status as prior or current landowners. Finding No. 6 makes clear that the County is named as the only operator of the landfill. The County of San Diego filed a petition contesting the addendum (Petition No. A-898).^[FN4]

On May 3, 1995, the SWRCB held a workshop to consider a draft order which would have removed the County as a responsible party under the WDRs. During the workshop, the SDRWQCB notified the SWRCB and the parties that it was planning to issue a cleanup and abatement order naming the County as a discharger. On May 5, 1995, the SDRWQCB's Executive Officer issued Cleanup and Abatement Order No. 95-66 naming all four parties in this matter as dischargers: the County, the City, the CDC, and Boulevard Investors, Inc. The SDRWQCB itself, following a hearing held on June 8, 1995, affirmed the cleanup and abatement order.

Also following the SWRCB's workshop, the SDRWQCB took two additional actions regarding WDR Order No. 87-55, which resulted in no net effect on the parties' status under the order. On May 12, 1995, it adopted Addendum No. 3, which removed the CDC as a responsible party under the WDRs, and on May 16, 1995, it adopted Addendum No. 4, which put the CDC back in as a responsible party under the WDRs.^[FN5] Shortly thereafter, the County, the CDC, and the City each filed petitions challenging their respective inclusion in the WDRs and the CAO.^[FN6]

Boulevard Investors filed an opposition to the County's petition.

II. CONTENTIONS AND FINDINGS

In summary, the three local government agencies argue that the SDRWQCB acted improperly by naming them, respectively, as dischargers under the WDRs and the CAO. All three argue that they should not be named in either order. This order first examines contentions regarding the petitioners' responsibilities under the WDRs,

then turns to the CAO issues.

1. Contention: The County contends that it should not be named a “discharger” in the post-closure WDRs for the Duck Pond Landfill since its activities at the landfill ceased over twenty years ago. The CDC contends that, as a prior owner having terminated its involvement with the landfill several years ago and never having operated the landfill, it is not properly named in the WDRs. The City asserts that it should not be named in the WDRs because its involvement with the landfill has been even more limited than that of the other petitioners.

*3 Finding: The record indicates that, in issuing its orders, the SDRWQCB has attempted to address actual, current clean-up needs. In addition, since the site happens to be a landfill, the SDRWQCB has sought to impose upon the parties the responsibility of assuming duties required by Title 23, California Code of Regulations, Chapter 15. The SDRWQCB's response to the petitions (memorandum dated October 10, 1995) states, in part, at page 3:

“The purpose of naming the four responsible parties (Boulevard Investors, the County, the CDC, and the City) as dischargers in Order No. 87-55 is to ensure compliance with ongoing post-closure maintenance and monitoring requirements and prevent further degradation of the site.”

The approach taken by the SDRWQCB, to broadly name all parties in both the WDRs and the CAO, unnecessarily blurs a purposeful distinction between WDRs and CAOs.

Water Code Section 13260 provides, in part, that the following persons must apply for, and obtain WDRs:

“(1) Any person discharging waste, or proposing to discharge waste, within any region that could affect the quality of the waters of the state, other than into a community sewer system.

“(2) Any person who is a citizen, domiciliary, or political agency or entity of this state discharging waste, or proposing to discharge waste, outside the boundaries of the state in a manner that could affect the quality of the waters of the state within any region.

“(3) Any person operating, or proposing to construct, an injection well.”

Water Code Section 13263 provides in part:

“(a) The regional board, after any necessary hearing, shall prescribe requirements as to the nature of any proposed discharge, existing discharge, or material change therein, except discharges into a community sewer system, with relation to the conditions existing from time to time in the disposal area or receiving waters upon, or into which the discharge is made or proposed.”

The language of Water Code Sections 13260 and 13263 suggests that WDRs are applicable to proposed or current controlled discharges, as opposed to past discharges.

On the other hand, Water Code Section 13304 provides:

“Any person who has discharged or discharges waste into the waters of this state in violation of any waste discharge requirement or other order or prohibition issued by a regional board or the state board, or who has caused or permitted, causes or permits, or threatens to cause or permit any waste to be discharged or deposited where it is, or probably will be, discharged into the waters of the state and creates, or threatens to create, a condition of pollution or nuisance, shall upon order of the regional board, clean up the waste or abate the effects of the waste”

Water Code Section 13304 is broader in its coverage than Sections 13260 and 13263. It applies to discharges that are past discharges, and clearly applies to uncontrolled, intentional, or negligent releases. In previous or-

ders, the SWRCB has made known its intention to maintain a distinction between WDRs and CAOs. In one case, the SWRCB reversed a Regional Water Quality Control Board decision to use WDRs to require investigation and cleanup of sites where extensive investigation and cleanup activities are involved. In County of Santa Clara, et al., Order No. WQ 86-8 (Footnote No. 11), the SWRCB indicated that the proper action to effectuate cleanup in most cases is adoption of a CAO rather than WDRs.) Again, in Vallico Park, Ltd., Order No. WQ 86-18 (Footnote No. 1), and in Prudential Insurance Company of America, Order No. WQ 87-6 (Footnote No. 2), the SWRCB made it clear that a CAO issued in accordance with Water Code Section 13304 is the appropriate means to require clean-up actions, not WDRs.

*4 The Duck Pond Landfill matter clearly involves a clean-up situation. The clean-up issues appear paramount to the closure and post-closure maintenance requirements of Chapter 15. In such a situation, the most appropriate regulatory approach is to issue one order, a CAO, to deal with both issues.^[FN7]

Having concluded that a CAO is the most appropriate action to comprehensively deal with the water quality issues at the Duck Pond Landfill, the WDRs should be rescinded. Applicable provisions from the WDRs should be added to the CAO to address the closure and post-closure maintenance issues. Because the WDRs are being rescinded, this Board need not resolve petitioners' questions as to whether they can legally be named in the WDRs.

We now turn to the issues involving who is appropriately named in the CAO. Each party's responsibility will be taken up in turn.

2. Contention: The County contends that it should not be named as a discharger in the CAO because it has not discharged into the ground water at the site, nor is it currently discharging. Furthermore, according to the County, any pollution at the site was caused by subsequent owners' and operators' lack of proper maintenance. Finally, the County argues that Water Code Section 13304(f) prevents the SDRWQCB from imposing liability upon the County for pre-1981 conduct.

Finding: The SWRCB disagrees. The County was the sole operator of the landfill during its active life. There is no dispute in the record that its placement of waste during 1960-1963 (perhaps combined with faulty surface maintenance) caused the current conditions at the site, which include volatile organic compounds detected at elevated levels, particularly in Monitoring Wells 6 and 7. It is clear that under Water Code Section 13304, any person whose action is the direct cause of a waste discharge is properly included in a CAO. Lake Madrone Water District v. Department of Water Resources Control Board (1989) 209 Cal.App.3d 163, 246 Cal.Rptr. 894. The fact that there were other exacerbating factors, such as faulty surface maintenance, does not absolve the County of its liability.

Finally, the County's argument that Water Code Section 13304(f) provides a shield to liability, is unmeritorious. That section provides that acts occurring prior to 1981, if lawful then, do not become unlawful by virtue of Water Code Section 13304. The County's placement of waste in a landfill, as the County suggests, is not the conduct with which the CAO is concerned. It is the release of pollutants associated with that waste into the ground water that is the subject of the CAO, and that release is a violation of law. Since 1872, California law has prohibited the creation or continuation of a public nuisance. See Civ. Code § 3490. Water pollution can constitute a public nuisance. See People v. Truckee Lumber Co., 116 Cal. 397, 48 P. 374 (1897). A successor property owner who fails to abate a continuing nuisance created by a prior owner is liable in the same manner as the prior owner. See City of Turlock v. Bristow, 103 Cal.App. 750, 284 P. 962 (1930). Additionally, since 1949, Califor-

nia law has prohibited the discharge of waste in any manner which will result in a pollution, contamination, or nuisance. Health and Saf. Code § 5411. See also Gov. Code § 12608 and Fish and G. Code § 5650.

*5 For these reasons, it was appropriate for the SDRWQCB's CAO to include the County, the landfill's only operator, as a discharger.

3. Contention: The City contends that it should not be named as a discharger in the CAO because, at most, it has been an easement holder for public right of way (30th Street) adjacent to the landfill.

Finding: The SWRCB disagrees. The SDRWQCB's CAO indicates (at Finding No. 7) that the City is named because of its easement of and authority to control and maintain 30th Street, which overlies part of the landfill. Furthermore, according to the SDRWQCB, improper maintenance of the roadway, sewage, and stormwater collection systems operated by the City have contributed to the pollution problems at the landfill. The City counters that it is not responsible for the sewer line beneath the landfill and that the maintenance of the street and the stormwater collection system has not contributed to pollution at the landfill. Also, control over the easement alone should not serve as the basis for naming the City.

Thirtieth Street overlies part of the landfill. During the SDRWQCB's hearing on this matter, information was presented to the SDRWQCB showing that subsidence of landfill material beneath the roadway was contributing to runoff coming from the street to the uncapped landfill surface. While the City's contribution to the effects of landfill discharges to the ground water in this regard may be relatively minor, it is apparent that the City's participation in the remediation effort will be necessary. In the absence of any other entity otherwise responsible for the roadway, the City's control of the roadway by easement is properly relied upon by the SDRWQCB to name the City in the CAO.^[FN8]

4. Contention: The CDC contends that it should not be named as a discharger because it was only an owner of the property for a "relatively short period of time", and that it neither discharged pollutants on the property nor exacerbated the existing problems. It further argues that the fact that it filed the Report of Waste Discharge, in application for WDRs in 1986, does not make it responsible. The CDC argues that it ended its obligations when it sold the property to Boulevard Investors on the condition that the latter assume full responsibility to address all regulatory requirements. It relies on the SWRCB's decision in Wenwest, Inc., (Order No. WQ 92-13) for the proposition that, as a short-term owner, it assumed no clean-up responsibility.

Finding: The SWRCB disagrees. First, the Wenwest case is inapplicable to this matter because factors on which that decision turned are not present in this matter. In the Wenwest case, short-term ownership meant four months. Here, the CDC held title to the property for the two-year period between 1986 and 1988. More significantly, several other responsible parties were available to address the environmental concerns. Here, relatively few are available. Additionally, the CDC filed a report of waste discharge in 1986, which led to the issuance (albeit to the City) of WDR Order No. 87-55 under which the CDC was to undertake some action to address the post-closure needs. This indicates an intent to assume such responsibility, and supports a conclusion that it is more than a mere short-term owner who intended to quickly sell to another.

*6 The CDC's argument that its sale of the property to Boulevard Investors on the condition that the latter assume environmental responsibilities relieves it of responsibility, is without merit. While the CDC may be able to pursue this argument against Boulevard Investors in a court of law, the argument does not make it inappropriate for the SDRWQCB to name all parties for which there is a reasonable basis.^[FN9]

III. CONCLUSIONS

1. Order No. 87-55 and its addenda should be rescinded and incorporated into CAO No. 95-66.
2. CAO No. 95-66 appropriately includes the County as a discharger.
3. CAO No. 95-66 appropriately includes the City as a discharger.
4. CAO No. 95-66 appropriately includes the CDC as a discharger.

IV. ORDER

IT IS HEREBY ORDERED that the SDRWQCB's Order No. 87-55 and its addenda are rescinded.

IT IS FURTHER ORDERED that all of the terms and provisions of Order No. 87-55 and its addenda are incorporated into CAO No. 95-66.

AYE:

John P. Caffrey

Marc Del Piero

James M. Stubchaer

John W. Brown

NO:

None

ABSENT:

None

ABSTAIN:

Mary Jane Forster

FN1. *The SWRCB's regulations permit consolidation of legally or factually related cases. 23 Calif. Code Regs. § 2054. Although the time for formal disposition of the County's first petition (A-898) has elapsed, we have elected to review the SDRWQCB's action on our own motion. Water Code § 13320.*

FN2. *The order names the City of National City, despite the fact that it was the CDC that purchased, owned, and later sold the property. This action fails to recognize the fact that the City and the CDC are apparently legally separate, individually viable entities. Evidently, the City failed to take action to correct the SDRWQCB's action in naming it--instead of the CDC--as the discharger responsible for WDR Order No. 88-57. While there is some confusion in the SDRWQCB record (prior to issuance of Addendum No. 4) regarding the City's and the CDC's status, it is not an issue in these consolidated petitions.*

FN3. *The record contains numerous items of correspondence in this connection. For example, the SDRWQCB sent a letter to the CDC on April 3, 1991; another was sent to Boulevard Investors on April 26, 1991, transmitting an Administrative Civil Liability Complaint; and Mr. Herbert Fox, of Boulevard Investors, wrote the SDRWQCB concerning his efforts to comply on May 7, 1991.*

FN4. *Neither the City nor the CDC filed a petition regarding Addendum No. 2.*

FN5. *Addendum No. 3 was the result of the SDRWQCB's apparent belief at that time that the CDC was not legally separate from the City and, therefore, was superfluous. Addendum No. 4 reflects the SDRWQCB's corrected interpretation that the CDC is a legally separate entity and, therefore, must be included in the WDR as a responsible party.*

FN6. *The County filed a second petition challenging its inclusion in the CAO (Petition No. A-980(b)); the City petitioned its inclusion in the CAO and the WDRs (Petition No. A-980(a)); the CDC filed a petition challenging its inclusion in the WDR (Petition No. A-973) and in the CAO (Petition No. A-980). The CDC and the City requested that the SDRWQCB's orders be stayed to the extent that they are included in such orders. By letter dated September 11, 1995, the Office of the Chief Counsel notified the CDC and the City that their requests for stay were incomplete, and extended an opportunity to submit further documentation. No response having been received, those stay requests are deemed abandoned and, if not, then denied for failure to submit the necessary documentation.*

FN7. *This approach is consistent with Chapter 15 requirements. Chapter 15 requires the issuance of a cease and desist order to provide for early closure of waste management units in order to prevent violation of WDRs at active sites. 23 Calif. Code Regs. § 2593. Such orders are to include closure and post-closure plans. Where the site is no longer active, issuance of a CAO to deal with both clean-up issues and closure and post-closure maintenance activities is appropriate.*

FN8. *It is not within the authority of the SWRCB or the SDRWQCB to apportion responsibility for the remediation activities. However, principles of equity would dictate that the City should not have to bear a substantial portion of the cost of the overall remediation effort at the landfill as a consequence of its easement authority.*

FN9. *The fact that CDC is a public agency does not alter its responsibility.*

1996 WL 101751 (Cal.St.Wat.Res.Bd.)

END OF DOCUMENT



In the Matter of the Petitions of ARTHUR SPITZER, HARVEY JACK MULLER AND
BETTINA BRENDEL SPIC & SPAN, INC. AND S & S ENTERPRISES, INC.
ARATEX SERVICES, INC. For Review of Cleanup and Abatement Orders Nos. 88-10
and 88-69 of the California Regional Water Quality Control Board, Santa Ana Region.
Our File Nos. A-537, A-537(a) and A-537(b)

Order No. WQ 89-8

State of California
State Water Resources Control Board

1989 Cal. ENV LEXIS 11

May 16, 1989

BEFORE: [*1] W. Don Maughan, Edwin H. Finster, Eliseo M. Samaniego, Darlene E. Ruiz

OPINIONBY: BY THE BOARD

OPINION:

On March 11, 1988, the Regional Water Quality Control Board, Santa Ana Region (Regional Board) adopted Cleanup and Abatement Order 88-10. The Order provides for the cleanup of soil and groundwater contaminated by perchloroethylene (PCE) at a site where dry cleaning businesses had operated for many years. PCE is commonly used as a dry cleaning solvent. The property is located at 14072 Magnolia Avenue in the City of Westminster (the Property). The dischargers named in the order include New Fashion Cleaners, Inc., which operated a dry cleaning business on the Property (New Fashion) and Spic & Span, Inc. and S & S Enterprises, Inc. (collectively referred to as Spic & Span). Spic & Span leased a building on the Property and its subsidiary, S & S Enterprises, Inc., operated a dry cleaning business there. Spic and Span and S & S have petitioned the State Board for review of Order No. 88-10. Also named as dischargers were Arthur Spitzer, Harvey Jack Muller and Bettina Brendel, who are the owners of the Property (referred to collectively, along with all their predecessors in [*2] interest, as the Owners). They have also petitioned the State Board for review of Order No. 88-10. Sol E. Tunks and Ed Tsuruta (formerly T & F, Inc.) are lessees of the Property under a ground lease and they subleased the property to the dry cleaners. They were also named as dischargers but are not petitioners.

After Order 88-10 was issued, the Regional Board learned that New Fashion had been acquired by Aratex, Services Inc. (Aratex). On July 8, 1988, the Regional Board adopted Cleanup and Abatement Order 88-69 to include Aratex. Aratex has petitioned the State Board for review of both Orders No. 88-10 and 88-69 (Cleanup and Abatement Orders 88-10 and 88-69 are referred to collectively as the Orders).

Because Order 88-69 was adopted after Spic & Span and Owners had filed petitions and because Orders No. 88-69 merely amends Order No. 88-10, their petitions will be reviewed as applicable to both Orders.

I. BACKGROUND

On July 6, 1987 a construction contractor discovered a manhole cover which was part of an old subsurface disposal system on the Property. The contractor was working for Shopwest Partners, Ltd. (the successor in interest of Los Angeles Land Company, collectively [*3] referred to as L.A. Land) which was developing the Property as a shopping center. Further investigations would disclose that the soils around the disposal system were contaminated with PCE and that there was a pollution plume extending approximately 250 feet from the disposal system. On March 11, 1988, the Regional Water Quality Control Board, Santa Ana Region issued Cleanup and Abatement Order 88-10, requiring numerous parties to provide for the cleanup of the PCE. The dispute under review here encompasses the responsibilities of the many individuals and business entities that have owned or occupied the Property, and their successors in interest.

The history of ownership and possession of this Property is complex and that history is an important element of this case.

In 1959, the Owners leased the Property to Ed Tunks and Martha E. Tunks for a period of 75 years. n1 The Tunks' then assigned their ground lease to T & F, Inc. (T & F) n2

n1 The owners in 1959, were Arthur Spitzer and his wife, Bettina Brendel. During the term of the ground lease, Arthur Spitzer's ownership interest in the Property was assigned to the Ann Violet Spitzer Lucas Trust. The trustees of the Trust are Arthur Spitzer and Jack Harvey Muller. Mr. Spitzer and Mr. Muller are named in the Cleanup and Abatement Order as trustees of the Trust. Bettina Brendel's ownership was continuous through the date of the Cleanup and Abatement Order. They are referred to in this order collectively as the Owners.

[*4]

n2 T & F, Inc. dissolved in 1987 and assigned the ground lease to Sol E. Tunks and Ed Tsuruta, who are named as dischargers in the Cleanup and Abatement Order.

In 1960, T & F built a market building on the Property, which was vacant land at the time. A few years later, T & F built another building which was used for a variety store until 1966. In 1966, T & F subleased the variety store to New Fashion which installed dry cleaning equipment in the building and began operation. At that time the building was not connected to a sewer but used a subsurface disposal system. A sewer connection was completed in 1969 but the subsurface disposal system remained in place.

In 1970, New Fashion moved out and Spic & Span moved in under a sublease with T & F. Spic & Span operated a dry cleaning business in the variety store building until May, 1987.

In 1986, the Owners and T & F completed negotiations with L.A. Land, a company which wanted to develop a shopping center on the Property. As a result of these discussions Owners and T & F negotiated a new ground lease of the Property so that T & F could sublease [*5] the entire Property to L.A. Land.

In December, 1986, T & F agreed to sublease the entire Property to L.A. Land until May 30, 2034. Under the sublease, T & F, assigned to L.A. Land all of its rights and responsibilities under the ground lease between Owners and T & F. T & F, Inc. also assigned to L.A. Land, its sublease with Spic & Span. Subject to the terms of the sublease and the ground lease, L.A. Land will have exclusive possession and control of the Property for the next forty-five years.

L.A. Land also negotiated a lease termination agreement with Spic & Span. Among other things, the termination agreement provided that Spic & Span

"shall remove all toxic or hazardous waste (sic) containers from the Premises, and they have no knowledge of other toxic or hazardous waste on the Premises."

The termination agreement also provided that the Spic & Span sublease would terminate May 22, 1987, one day after the effective date of the sublease between L.A. Land and T & F.

On July 6, 1987, a contractor who was grading the Property for L.A. Land encountered a manhole cover which was part of the old subsurface disposal system. The manhole cover had been buried under one or two feet [*6] of soil and was part of what appeared to be a septic tank or seepage pit.

Liquid sludge was observed after the cover was removed. The Garden Grove Sanitary District instructed the contractor to pump out the sludge. The following day approximately 30 gallons of sludge were pumped out by a waste hauler.

The grading contractor then proceeded to further excavate the area and remove the underground structure which was part of the subsurface disposal system. In the process, the structure's cover was broken and the pieces were removed to another part of the Property. As excavation of the area immediately below the seepage pit progressed, severe PCE fumes began to emanate from the area. After complaints from neighbors, local fire department and health department officials ordered that the pit and the contaminated soils be temporarily covered with clean soils to eliminate the fumes until the soils could be fully excavated and hauled away.

L.A. Land immediately retained contractors to excavate the site and remove contaminated soils. Approximately 338 cubic yards of soil was removed. Soils were removed to the level at which ground water was encountered.

In August, 1987, L.A. Land's [*7] consultant installed monitoring wells in order to perform a preliminary assessment of the extent of the groundwater pollution at the site. Samples showed PCE in the groundwater as high as 72,000 parts per billion. Data indicated that a pollution plume extended at least 250 feet from the excavation site. A diagram showing the locations of the wells is attached and incorporated in this order as Exhibit A.

The consultant also designed and installed an interim groundwater cleanup system. Some elements of the system, a recovery well and infiltration gallery, were installed in December, 1987. The treatment system was not installed and so the cleanup system is not operational.

The Regional Board issued Cleanup and Abatement Order No. 88-10 on March, 11 1988. It required New Fashion, Spic & Span, and T & F to delineate the pollution plume and to cleanup of the pollution by certain dates. The Order also provided that the Owners would be responsible for these activities only if the other named dischargers did not timely complete these tasks. The Regional Board decided not to include L.A. Land in the Order. A few months later the Regional Board learned that New Fashion had changed [*8] its name to Fashion-Tex and that all of its stock had been purchased by Aratex. They adopted Order 88-69 amending Order 88-10 to substitute Aratex for New Fashion.

Since the Orders were adopted, planning for cleanup has proceeded. However, to date the partially installed system has not been completed nor is any other cleanup system operated on the Property.

II. CONTENTIONS AND FINDINGS

1. Contention: The Owners contend that they should not be included in the order because they have no involvement or control over the use of the Property.

Finding: A long line of State Board orders have upheld Regional Board orders holding landowners responsible for cleanup of pollution on their property regardless of their involvement in the activities that initially caused the pollution. Most recently, this Board held that a landowner had ultimate responsibility for a cleanup even though he acquired the property after a previous owner had discharged pesticides to the land. (Schmidl, (1989) Order No. WQ 89-1)

A Regional Board may order any person to cleanup a discharge if that person has permitted or permits a discharge

which causes water pollution (Water Code Section 13304). [*9] A discharge is

"the flowing or issuing out, of harmful material from the site of the particular operation into the water of the State. The operation which produced the harmful material need not, however be currently conducted." (27 Ops Atty Gen. 182, 183 (1956); Zoecon, (1986) Order No. WQ 86-2)

A landowner is ultimately responsible for the condition of his property, even if he is not involved in day-to-day operations. If he knows of a discharge on his property and has sufficient control of the property to correct it, he should be subject to a cleanup order under Water Code Section 13304 (Logsdon, (1984) Order No. 84-6; Vallco Park, Ltd., (1986) Order No. WQ 86-18; cf. Leslie Salt Company v. San Francisco Bay Conservation & Development Commission (1984) 153 Cal.App.3d 605, 200 Cal.Rptr. 575).

The Owners in this case claim that they did not know anything about activities on the Property. Although, they knew that a dry cleaning business was located there, they did not know what the dry cleaners were doing with the PCE. However, they now know that there is PCE contamination in the soil and ground water at the Property. The discharge of the PCE did not cease when [*10] the dry cleaning businesses stopped. The discharge continues as long as the PCE remains in the soil and ground water. Therefore, the Owners do know about the discharge of pollutants on their property. (Zoecon, supra; Schmidl, supra).

The Owners also have sufficient control of the Property to permit them to conduct a cleanup in the event that T & F and the other parties named in the cleanup and abatement order fail to do so. n3 The original lease with T & F required the lessee to,

"perform all work necessary to maintain the premises in good order and condition and to comply with all laws, ordinances, orders, rules, regulations and requirements of federal, state and municipal governments, and appropriate departments, commissions, boards and officers thereof." (Petition of Owners, Points and Authorities, Page 2)

A new lease was negotiated in 1986 and the original lease was terminated. According to Owner's petition;

"The new lease also requires the tenant, at no cost or expense to the landlord, to keep and maintain the premises in good order and condition, and the tenant has agreed to comply with all laws, ordinances, rules orders and regulations from time to time applicable, [*11] including those relating to health, safety, noise, environmental protection, waste disposal, and air and water quality." (Ibid.)

The Owners have the right to regain possession of the Property if the lessee does not perform its obligations.

n3 Cleanup and Abatement Orders 88-10 and 88-69 do not require Owners to undertake cleanup unless the other named parties fail to comply with the time schedule in the orders.

These lease terms are very similar to the lease terms analyzed in two previous State Board orders, Logsdon, supra and Vallco Park, Ltd, supra, which addressed the issue of landlord control over leased property. In Vallco Park, Ltd. and in the case at hand, the landlord was not required to cleanup the pollution unless the lessee or other responsible parties failed to do so. In both Logsdon and Vallco Park, Ltd., it was determined that the landlord had control of the property sufficient to permit the landlord to comply with the Regional Board order. (See also Southern California Edison [*12] Co. (1986) Order No. WQ 86-11; U.S. Forest Service (1987) Order No. WQ 87-5; Prudential Insurance Company of America, (1987) Order No. WQ 87-6). We reach the same conclusion here.

2. Contention: All of the petitioners contend that L.A. Land should have been included in the Orders as a discharger. This contention is based on three separate theories which are discussed below under the sub-headings of Contentions A, B and C.

Contention A: Spic & Span and Aratex contend that when L.A. Land excavated the subsurface disposal system it shattered a septic tank spilling PCE on the Property.

Findings: The evidence does not support this contention.

The evidence indicates that the subsurface disposal structure was a seepage pit or cess pool and not a septic tank. The only eyewitness report, that of L.A. Land's contractor, describes it as a seepage pit or cess pool with a concrete cover. No government representative who observed the pieces of the concrete structure after it was removed describes it as a tank. The only contradictory evidence is a declaration of Spic & Span's manager who did not see the structure but who states that L.A. Land's representative [*13] described it as a tank. This declaration does not outweigh the other evidence to the contrary.

Regardless of the nature of the structure, other evidence on the record indicates that L.A. Land's excavation did not cause the PCE pollution on the Property.

Liquid sludge was observed in the seepage pit area and the Garden Grove Sanitary District instructed L.A. Land to pump the sludge out. Although, Spic & Span claims that only half of the sludge was pumped, they have no evidence to prove this claim. There is no reason why L.A. Land would report its findings to the Sanitary District and then not follow the District's instructions. Because the liquid sludge was pumped before the structure was removed, the likelihood of a spill was minimized.

Moreover, the evidence demonstrates that PCE had been present in the soils for many years. Monitoring wells at the site indicate a pollution plume of approximately 250 feet emanating from the area of the seepage pit. L.A. Land's consultants indicate an average flow rate of 2.1 feet/year. Based on lithology from boreholes, which indicate a heterogeneous section consisting of interfingering lenses of sand, silt, and clay, and the consultant's [*14] estimate of the ground water gradient, this is a reasonable figure. Assuming a worst case situation, with a steeper gradient and a hydraulic conductivity characteristic of a sand medium, the flow rate could be as high as 480 feet/year (although a flow rate this high is unlikely due to the heterogeneity and poorly sorted nature of the soils). Given this range of flow rates, a 250 foot plume could not have occurred unless the PCE was been present before the excavation started. Additionally, PCE had been detected in a nearby drinking water well in 1986, indicating that the soils and water were polluted before excavation began.

The excavation may have caused a minor increase in discharge by disturbing the soils. However, any disturbance was offset by the removal of approximately 338 cubic yards of contaminated soils.

Contention B: Spic & Span and Aratex contend that L.A. Land contaminated a previously protected deep-water aquifer by negligently drilling through a protective clay layer protecting the aquifer, providing a vertical conduit through which PCE contaminated water may have descended.

Findings: There is no evidence on the record that the deeper aquifer was polluted [*15] after the drilling was done. In fact, samples taken from a deep aquifer drinking water well collected after L.A. Land came on the scene did not contain PCE, even though samples taken in 1986 did contain PCE.

There is not substantial evidence demonstrating that the drilling pierced the protective clay layer. L.A. Land's consultant stated that the well was drilled to 55 feet. Regional characteristics indicate that the protective clay layer begins at 40 to 50 feet but may begin as deep as 60 feet. The clay layer is approximately 10 feet thick. Gamma logs provided by L.A. Land's consultant show that the clay layer was not pierced. Although gamma logs are not reliable without additional evidence, there is no evidence to the contrary.

The Orders require dischargers to define the vertical extent of the PCE contamination, including possible contamination of the deeper aquifer. If evidence is produced which shows deeper aquifer contamination or that the well drilling did pierce the protective clay layer, this issue should be reconsidered by the Regional Board.

Contention C: All petitioners assert that L.A. Land should be included as a discharger under the Orders because L.A. Land [*16] has exclusive possession and control of the Property and the Cleanup system which it installed.

Findings: It is undisputed that L.A. Land had no connection with the Property at the time that the dry cleaning businesses were operated. It is also clear, based on previous orders of this board, that if L.A. Land had purchased fee title to the Property it would have been named as a discharger in the Orders. (Zoecon, supra; Schmidl, supra). However, even though L.A. Land is not the fee owner, it did acquire exclusive possession and control of the Property for a term exceeding forty-five years. Additionally, L.A. Land took possession of the land knowing that hazardous chemicals had been used there and was aware of the possibility of pollution. n4

n4 This is evidenced by the termination agreement with Spic & Span which required Spic & Span to remove all hazardous waste from the site.

The question is whether L.A. Land is a person who is permitting the discharge of pollutants, within the meaning of Water Code Section [*17] 13304, even though it does not have fee title to the Property. The answer is yes. During the forty-five year term of its lease, L.A. Land has the same ability to control the continuing discharge on the Property as it would have if it had fee title. Therefore, it is permitting the discharge of pollutants and should be named as a discharger under the Orders.

Previous orders of this Board, Attorney General's opinions and common law principles regarding duties to abate hazardous conditions on real property support this conclusion. They indicate that responsibility rests with one who has possession and control of the property and that it is not limited to those who hold fee ownership.

As noted above, the Attorney General has concluded that discharge continues as long as pollutants are being emitted at the site. He has further concluded that the "dischargers are the persons who now have legal control of the property from which such drainage arises." (26 Ops. Atty. Gen. 88, 90 (1955); 27 Ops. Atty. Gen. 182 (1956)). The Attorney General has also noted that in the case of a discharge from a mine if the fee ownership of the mine is separate from the mineral rights ownership, both [*18] the holder of the mineral rights as well as the fee owner are "dischargers." (Ibid.)

We applied similar reasoning in *Stuart Petroleum*, (1986) Order No. 86-15, when we held a lessee was liable for cleanup of pollution caused by its sublessee. We held that to "permit" a discharge included failing to take action when "the ability to obviate the condition" existed. In that case it was found that lessee knew about the sublessee's activities at the time the initial release occurred. Nonetheless, the same reasoning applies here when the one who controls the property knows of an ongoing discharge and has the ability to obviate it.

This interpretation is supported by common law principles regarding responsibility for hazardous conditions on property. In ruling on this issue in the past, this Board has relied on the principles stated in *Rowland v. Christian* (1968) 69 C.2d 108, 70 Cal.Rptr. 97, 443 P.2d 651. In *Rowland*, the California Supreme Court held that a possessor or occupier of land is liable for injuries when he fails to exercise reasonable care in the management of his property. The defendant in that case was a tenant of the property and not the fee owner. [*19] She was held liable for injuries caused by a broken faucet. There was no finding that she had caused the defect in the faucet. The court emphasized the tenant's failure to correct problem after she discovered it, not her culpability in causing it. The Court's holding was based on what it characterized as "the basic policy of the state" in Civil Code Section 1714 which provides in pertinent part,

"Every one is responsible, not only for the result of his willful acts, but also for an injury occasioned to another by his want of ordinary care or skill in the management of his property or person"

Commentators have also enunciated the principle that the possession not ownership is a key factor in liability.

"The liability is imposed on an owner or possessor. 'The important thing in the law of torts is the possession, and not whether it is or is not rightful as between the possessor and some third person.' (6 Witkin Summary of California Law, (9th edition 1988) Section 892, p. 261 quoting Restatement of Torts 2d, Section 32BE, Comment a)

Following the reasoning in Rowland, a person who possesses property is responsible for the maintenance of hazardous conditions [*20] on the property such as water pollution. Legal ownership is not a significant factor. Therefore, one who possesses and controls property should be considered a person who is permitting the continued discharge of water pollution on the property and is subject to a Cleanup and Abatement Order under Water Code Section 13304 during the term of that possession and control.

Although, L.A. Land should be named as a discharger in the Orders, it should have the same status as the Owners. It should be required to take responsibility for the cleanup only if the other dischargers fail to perform. This would be the equitable conclusion because, L.A. Land had no connection with the activities which initially caused the pollution, the parties directly responsible for the PCE release have been identified and are making some progress toward cleanup, and while L.A. Land has possession and control of the Property for a very long time, it shares that control with the Owners, who have the reversionary rights to the Property.

3. Contention: Aratex, which purchased all the stock of New Fashion in 1984, contends that it should not be named as a discharger in the Orders because it is not legally [*21] responsible for the actions of New Fashion which occurred between 1966 and 1969.

Findings: New Fashion operated a dry cleaning business on the Property from 1966 through 1969 during the time that the drainage system was connected to a subsurface disposal system. Studies indicate that PCE pollution has existed on the Property for many years. It is reasonable to conclude that New Fashion disposed of at least some of the PCE found on the Property.

In 1982, New Fashion changed its name to Fashion-Tex Services, Inc. (Fashion-Tex). In 1984 the two shareholders of Fashion-Tex, Grant Wada and Shoji Yoshihara (collectively Wada and Yoshihara) sold all of their stock to Aratex. The purchase agreement required the officers of Fashion-Tex to resign and according to the records of the Secretary of State, the president of Aratex became the president of Fashion-Tex.

The question here is whether Aratex is legally responsible for the actions of Fashion-Tex which occurred fourteen years before Aratex purchased its stock.

Generally a parent corporation is not liable for the actions of its subsidiary. Like any other stockholder it is protected from liability by the corporate veil (McLaughlin [*22] v. L. Bloom Sons Co. (1962) 206 Cal.App.2d 848, 24 Cal.Rptr. 311). However, that corporate veil may be pierced if it is determined that the parent is really the alter ego of the subsidiary (6 Witkin Summary of California Law (8th Edition 1974) Corporations Section 11, p. 4323).

The conditions under which a corporate entity may be disregarded are founded in equity and vary depending on the special circumstances of the case (Goldsmith v. Tub-O-Wash (1959) 199 Cal.App.2d 132, 18 Cal.Rptr. 446, 451). Generally, the corporate entity will be disregarded when it is "so organized and controlled and its affairs are so conducted, as to make it merely an instrumentality, agency, conduit, or adjunct of another corporation." (McLaughlin v. L. Bloom Sons Co., supra 24 Cal.Rptr. at 313)

Aratex asserts that an inequity would result if it were held liable for actions taken by Fashion-Tex fourteen years before Aratex purchased it. However, it should be emphasized that the equities to be considered here do not concern Aratex's involvement in the release of the pollution on the Property. It is undisputed that they had no direct involvement there. The equities to be considered here, [*23] concern Aratex's status as the owner of Fashion-Tex and whether Aratex's control of Fashion-Tex was in accordance with accepted principles of corporate law. (See generally 2 Marsh's California Corporation Law (1988) Section 15-16).

Directing our analysis to corporate law, we conclude that it would be inequitable if Aratex were not held liable. The California Supreme Court has stated the principle that if one corporation acquires all the assets of another corporation without paying substantial consideration for the assets, the purchasing corporation is liable for the pre-purchase activities of the selling corporation. (*Ray v. Alad*, (1977) 19 Cal.3d 22, 136 Cal.Rptr. 574; *Malone v. Red Top Cab*, (1936) 16 Cal.App.2d 268, 60 P.2d 543; see *Schoenberg v. Benner*, (1967) 251 Cal.App.2d 154, 59 Cal.Rptr. 359). That principle applies here. Aratex acquired control of the assets of Fashion-Tex while ostensibly buying only the stock of Fashion-Tex. It then permitted Fashion-Tex to go out of business, leaving no corporate assets or ongoing business to pursue for the obligations of Fashion-Tex.

Aratex purchased Fashion-Tex from Wada and Yoshihara. Wada and Yoshihara received the [*24] proceeds of the sale and set up a new, wholly unrelated corporation, coincidentally called New Fashion Cleaners. The corporation, Fashion-Tex, received no payment in that transaction. Only the former stockholders were paid.

The effect of the stock purchase was that Aratex acquired the assets of Fashion-Tex without paying cash to Fashion-Tex. Aratex's attorney testified at the Regional Board hearing that Fashion-Tex's assets "were not sold to the parent corporation; they were held by Aratex" (Regional Board hearing transcript, July 8 1988 at 22:13-14). Another Aratex attorney in correspondence to the State Board, repeatedly refers to the 1984 stock purchase as a purchase of Fashion-Tex assets (letter dated February 12, 1989, from Bonnie Ezkanazi, Aratex's attorney, to Jennifer Soloway, Staff Counsel, State Board). It is also reasonable to conclude that Aratex is using Fashion-Tex's assets because Fashion-Tex is not using them. Aratex's attorney has testified that Fashion-Tex does not carry on any business (Regional Board Transcript, July 8 1988, 18:8-13).

If Aratex had, in good faith, purchased the assets from Fashion-Tex, cash payment should have been made to the corporation [*25] not the shareholders. Here, Aratex may have paid substantial consideration to Wada and Yoshihara for their stock, but they paid nothing to Fashion-Tex for its assets. In accordance with the principle articulated in *Ray v. Alad*, supra, it would be inequitable to afford Aratex the protection of the corporate veil of Fashion-Tex.

Aratex asserts that if it is named in the Orders it should be only "secondarily" liable. That would not be appropriate. Fashion-Tex, under its former name, New Fashion, released PCE to the soils at the Property, polluting the waters of the State. There is no doubt that Fashion-Tex should be responsible for the cleanup to the same degree as Spic & Span and T & F. For the reasons stated above, Aratex has stepped into Fashion-Tex's shoes and is responsible for Fashion-Tex's liabilities. Therefore, there is no justification for imposing different liability against Aratex than would be imposed against Fashion-Tex.

III. CONCLUSIONS

1. Arthur Spitzer, Harvey Jack Muller and Bettina Brendel are fee owners of the Property and are persons who are permitting the discharge of pollutants on the Property and the Regional Board acted appropriately [*26] when it included them as dischargers in the Orders.
2. The evidence on the record demonstrates that L.A. Land did not cause a spill of PCE at the site when it excavated the subsurface disposal system.
3. There is not sufficient evidence on the record to support Spic & Span's contention that L.A. Land contaminated the deeper aquifer when drilling a monitoring well.
4. L.A. Land, which has exclusive possession and control of the Property until 2034, is a person who is permitting the discharge of pollution within the meaning of Water Code Section 13304 and the Regional Board acted improperly when it failed to include L.A. Land as a discharger in the Orders. L.A. Land should be responsible for the tasks required by the Orders, only if Spic & Span, Aratex and T & F fail to timely carry out the requirements of the Orders.
5. As a matter of law, Aratex is liable for the acts of Fashion-Tex Services, Inc. and the Regional Board acted

appropriately when it included Aratex Services, Inc. in the orders. Because Aratex is responsible for the actions of Fashion-Tex, Aratex should be responsible for the tasks required by the Orders on the same basis as Spic & Span and T & F.

IV. ORDER [*27]

1. The portion of the petition of Arthur Spitzer, Harvey Jack Muller and Bettina Brendel which requests that the Orders be amended to remove their names, is dismissed.

2. The portion of the petition of Aratex Services, Inc. which requests that the Orders be amended to remove its name, is dismissed.

3. The petition of Spic & Span, Inc. and S & S Enterprises, Inc., and the portion of the petition of Arthur Spitzer, Harvey Jack Muller and Bettina Brendel, and the portion of the petition of Aratex Services, Inc. which request that Los Angeles Land Company, Inc. and Shopwest Partners, Ltd. be included as dischargers in the Orders are granted and order No. 88-10 of the Regional Water Quality Control Board, Santa Ana Region is amended as follows:

(1) Amend the title by adding Los Angeles Land Company, Inc. and Shopwest Partners, Ltd. to the list of dischargers.

(2) Amend the introductory clause of item B. of the order to read:

"Spitzer, Los Angeles Land Company, Inc. and Shopwest Partners, Ltd. shall:"

The rest of item B. shall remain the same except as it may be amended by subsequent Regional Board order.

(3) Amend the introductory clause of item C. of the order to read:

"Spitzer, [*28] Los Angeles Land Company, Inc., Shopwest Partners, Ltd., Sol E. Tunks and Ed Tsuruta, Aratex Services, Inc., Spic and Span, Inc., and S & S Enterprises, Inc., shall:"

The rest of item C. shall remain the same except as it may be amended by subsequent Regional Board order.
[SEE ILLUSTRATION IN SOURCE]

Legal Topics:

For related research and practice materials, see the following legal topics:

Real Property LawEnvironmental RegulationLiabilities & RisksContractual RelationshipsReal Property LawWater RightsGroundwaterTortsPremises Liability & PropertyLessees & LessorsLiabilities of LessorsNegligenceDuty to RepairGeneral Overview



In the Matter of the Petition of ZOECON CORPORATION For Review of Order No.
85-67 of the California Regional Water Quality Control Board, San Francisco Bay
Region. Our File No. A-397

Order No. WQ 86-2

State of California
State Water Resources Control Board

1986 Cal. ENV LEXIS 4

February 20, 1986

BEFORE: [*1] Raymond V. Stone, Darlene E. Ruiz, E. H. Finster, Eliseo M. Samaniego, Danny Walsh

OPINIONBY: BY THE BOARD

OPINION:

On May 15, 1985, the California Regional Water Quality Control Board, San Francisco Bay Region (Regional Board) adopted waste discharge requirements (Order No. 85-67) for a five-acre industrial site in East Palo Alto. Both Zoecon Corporation, the current owner of the property, and Rhone-Poulenc, Inc., a former owner of the site, were named as dischargers in the requirements. On June 14, 1985, the State Board received a petition from Zoecon Corporation (petitioner) asserting that Zoecon was improperly named as a discharger in the order.

I. BACKGROUND

Before discussing the issue raised on appeal, it is helpful to briefly review the history of the site.

Prior to 1926, the property in question was occupied by Reed Zinc Company whose activities are unknown. From 1926 to 1964 the site was occupied by Chipman Chemical Company for the production and formulation of pesticides and herbicides including sodium arsenite compounds. In 1964, Rhodia Inc. acquired Chipman and its operations. In 1971 the Chipman operation was shut down and the following year the property was sold to Zoecon Corporation. [*2] Rhodia subsequently changed its name to Rhone-Poulenc, Inc. in 1978. Zoecon has occupied the site from 1972 to the present for the purpose of formulating and manufacturing insect control chemicals.

Sodium arsenite was formulated by Chipman and Rhodia in an underground tank located along a railroad spur. Some of the wastes from this process were disposed of in a shallow sludge pond located on the northeast portion of the property. Contaminated surface runoff from the site has discharged and still poses a potential to discharge onto adjoining land including a non-tidal marsh.

Zoecon Corporation contends that the chemicals used in their manufacturing and formulating operations are unrelated to the contaminants found on the site. Chipman Chemical Company and Rhodia, Inc. are known to have produced arsenical pesticides at that site and the Regional Board found that they are the probable source of the

contaminants found in the soil and ground water both onsite and on adjacent properties. Zoecon Corporation has legal title to the site where the contaminants are concentrated however and the Regional Board therefore concluded that the petitioner has certain legal responsibility for [*3] any investigation or remedial action.

In fact, initial site investigations were conducted in 1981 by Zoecon. They revealed heavy metal contamination of the soil and ground water (including arsenic, lead, cadmium, selenium and mercury) in excess of background levels. The Regional Board adopted a cleanup and abatement order and several subsequent revisions to it, requiring both Rhone-Poulenc, Inc. and Zoecon Corp. to determine the lateral and vertical extent of heavy metals and organic compounds in the soil and ground water both on and off-site. The cleanup and abatement order also required the dischargers to submit and implement remedial measures to mitigate the contamination.

The two companies did not recommend similar mitigation alternatives since they have differing opinions about the appropriate level of cleanup. Therefore, the waste discharge requirements do not require the implementation of a specific mitigation plan but, instead, establish a required level of clean up.

II. CONTENTIONS AND FINDINGS

1. Contention: Petitioner contends that it cannot be classified as a "discharger" under applicable sections of the Water Code because Zoecon never discharged, deposited or [*4] in any way contributed to the contamination of the property.

Finding: Waste discharge requirements were adopted by the Regional Board pursuant to Water Code § 13263(a) which states, in pertinent part, that "the regional board, after any necessary hearing, shall prescribe requirements as to the nature of any proposed discharge, existing discharge or material change therein . . ." Petitioner argues that there is no factual or legal basis for the contention that there is an ongoing "discharge" of waste at the site such that waste discharge requirements may be issued.

Factually, petitioner argues that the soil and ground water contamination is in a relatively steady state due to the low mobility characteristic of arsenic in soils. Petitioner also points out that one consultant has estimated that at current flow rates it will take 1,000 years for the contaminated ground water to discharge to San Francisco Bay which is about 2,000 feet west of the site. n1 Even if this calculation is accurate, such movement of contamination, albeit slow, is still a discharge to waters of the state that must be regulated. In addition, ground water quality in the shallow zone has been degraded and existing [*5] and potential beneficial uses of currently uncontaminated ground water in the vicinity of the site within the shallow and deep aquifers could be adversely affected if the spread of contamination remains uncontrolled. Therefore, we must conclude that there is an actual movement of waste from soils to ground water and from contaminated to uncontaminated ground water at the site which is sufficient to constitute a "discharge" by the petitioner for purposes of Water Code § 13263(a).

n1 Evaluation of Corrective Measure Plans for the 1990 Bay Road Site, East Palo Alto, California by Woodward-Clyde Consultants, November 27, 1984, p. 24-25.

We note also that although the petitioner argues that the contamination is in a relatively steady state, the petitioner's suggested remedial action plan actually calls for the excavation of all on-site soils having arsenic concentrations in excess of 500 ppm and the installation of a ground water extraction and treatment system to remove contaminants from the shallow ground water aquifer. [*6] This remedial plan, which is more stringent in its recommendations than the one proposed by Rhone-Poulenc, supports our contention that a discharge is continuing to occur which must be abated.

Petitioner cites U.S. v. Occidental Petroleum Corp., Civ. No. S-79-989 MLS (E.D. Cal. 1980) in support of its argument that the term "discharge" as used in the Porter-Cologne Act is the act of depositing a contaminant and not the continuous leaching of the contaminant into ground water. We note, first of all, that this case has no value as precedent.

It is an unpublished decision and could not be cited or relied on in a court of law. (Cal. Rules of Court, Rule 977.) In addition, it is a federal, as opposed to California, court decision. Furthermore, the situation reviewed in that case is not analogous to the issue before us today. In the Occidental Petroleum case, the court was construing Water Code § 13350 which concerns the imposition of penalties rather than the initial issuance of waste discharge requirements. Finally, unlike the situation in the Occidental Petroleum case, here the waste discharge requirements were imposed on Zoecon not because it has "deposited" chemicals on to land [*7] where they will eventually "discharge" into state waters, but because it owns contaminated land which is directly discharging chemicals into water. For all of these reasons, we decline to follow the reasoning of this case.

Petitioner also relies on the California Superior Court opinion in *People ex rel. Younger v. Superior Court* 16 Cal.3d 34, 127 Cal.Rptr. 122 (1976). We do not find this decision, however, to be inconsistent with the Regional Board's determination that property owner is a discharger for purposes of issuing waste discharge requirements when wastes continue to be discharged from a site into waters of the state. In *Younger* the Court was concerned with the proper interpretation of Water Code § 13350(a)(3), which imposes a \$ 6,000 per day penalty for each day in which a deposit of oil occurs. The Court held that this section imposes liability for each day in which oil is deposited in the waters of the state, not for each day during which oil remains in the water. In reaching this conclusion, the Court placed great reliance upon the fact that Harbors and Navigation Code § 151 n2 provides an adequate remedy for the cost of oil spill cleanup. The Court surmised, therefore, [*8] that the purpose of § 13350(a)(3) was not to address the concerns of the State regarding the problems engendered by the size of an oil spill, the length of time the spill persists, or the costs of cleanup, but rather to provide an effective deterrent to those individuals who continuously cause oil spills. (*Id.*, 16 Cal.3d at 44.)

n2 Under this section, any person who intentionally or negligently causes or permits any oil to be deposited in waters of the state is liable for a maximum civil penalty of \$ 6,000 and for all actual damages, in addition to the reasonable costs actually incurred in abating or cleaning up the oil deposit.

Water Code § 13263(a) speaks to the issue of prescribing requirements for a "proposed discharge, existing discharge, or material change therein." Civil penalties are not at issue in the case before us today. An enforcement action is not being taken and there is no provision analogous to the Harbors and Navigation Code section relied on for the reasoning in the *Younger* case. The *Younger* case [*9] dealt simply with the issue of imposing liability for each day in which oil remains in waters of the state and as such is clearly distinguishable from the issue before us now. Finally, the *Younger* case interprets the word "deposit" as used in Water Code § 13350(a)(3). The petitioner seems to imply that this term is synonymous with the word "discharge" as used in Water Code § 13263(a) which we are considering today. Yet Water Code § 13350(a)(2) speaks to causing or permitting waste to be "deposited" where it is "discharged" into the waters of the state. Clearly, the words must mean different things or the Legislature would not have used both terms in § 13350(a)(2).

We note that the petitioner cites an Attorney General's opinion defining "discharge" which arose from problems at abandoned mines in the State (26 Ops.Atty.Gen. 88, Opinion No. 55-116, (1955)). Petitioner argues that the decision is not on point because the conditions factually are quite different than in this instant case. The reasoning of the Opinion nonetheless is consistent with our conclusions herein. We note also that the opinion states:

"In the case of harmful drainage from inoperative or abandoned mines, [*10] the dischargers are the persons who now have legal control of the property from which such drainage arises. If the fee of the land where the mine is located is owned separately from the mineral rights, both the owner of the mineral rights in whose tunnels and shafts or dumps the water has picked up the material which has tainted it, and the owner of the fee from whose land the tainted water is permitted to pour out, are discharges within the contemplation of the Dickey Act. By failing to take action which is within their legal power to halt the defilement of the drainage or to render it harmless by treatment before it departs their property, both are responsible for the deleterious discharge. It is immaterial that the mining operations may have

terminated before either purchased his present interest because the discharge for which they are accountable is the existing and continuing drainage from their holdings, not the now discontinued mining." (Id. at p. 90-91.)

This is consistent with the conclusion in 27 Ops.Atty.Gen. 182 Opinion No. 55-236 (1956) regarding issuance of waste discharge requirements for inactive, abandoned or completed operations. The opinion concluded:

"The [*11] person upon whom the waste discharge requirements should be imposed to correct any condition of pollution or nuisance which may result from discharges of the materials discussed above are those persons who in each case are responsible for the current discharge. In general, they would be the persons who presently have legal control over the property from which the harmful material arises, and thus have the legal power either to halt the escape of the material into the waters of the State or to render the material harmless by treatment before it leaves their property. Under this analysis, the fact that the persons who conducted the operations which originally produced or exposed the harmful material have left the scene does not free for accountability those permitting the existing and continuing discharge of the material into the waters of the State." (Id. p. 185.)

Although both of these opinions interpret the Dickey Water Pollution Act which has been superseded by the Porter-Cologne Act, the relevant wording and intent of the statutes remains the same. In fact, in 63 Ops.Atty.Gen. 51, 56 (1980), it states:

"The legislative history of the Porter-Cologne Act clearly indicates that [*12] the previous Attorney General opinions on dirt run-off, mine tailing run-off and the responsibility of the present owner were intended to be incorporated in the definition of 'waste' under the Porter-Cologne Act." n3

n3 Section 36 of the bill that enacted the Porter-Cologne Act (Stats. 1969, Ch. 482) provided:

"This act is intended to implement the legislative recommendations of the final report of the State Water Resources Control Board submitted to the 1969 Regular Session of the Legislature entitled 'Recommended Changes in Water Quality Control', prepared by the Study Project-Water Quality Control Program."

The cited report contained the following comment, at page 24 of Appendix A to the report, about the definition of waste in Water Code Section 13050(d):

"It is intended that the proposed definition of waste will be interpreted to include all the materials, etc, which the Attorney General has interpreted to be included in the definitions of 'sewage', 'industrial waste', and 'other waste' [under the Dickey Act]."

Even without this indication of legislative intent to adopt specific opinions of the Attorney General as part of legislation, under general rules of statutory construction, it is presumed that an interpretation of a statute in an opinion of the Attorney General has come to the attention of the Legislature, and if that interpretation were contrary to the intent of the Legislature, the Legislature would have adopted corrective language in amendments on the subject. (*California Correctional Officers' Assn. v. Board of Administration* (1978) 76 Cal.App.3d 786, 794.)

[*13]

2. Contention: The petitioner also argues that it is inequitable to impose requirements on Zoecon when the actual discharger is known and capable of performing the clean up.

Finding: We hasten to point out that neither the waste discharge requirements nor this order speak to the issue of apportioning responsibility between Zoecon and Rhone-Poulenc for the clean up of the site. There are other forums that provide a more appropriate setting for the resolution of that matter. In fact, we understand that Zoecon has initiated

legal action in San Mateo Superior Court to get Rhone-Poulenc to compensate Zoecon for the damages and to declare Rhone-Poulenc responsible for the Contamination. n4 In addition, liability will be apportioned among all potentially responsible parties as part of the Department of Health Services' development of a remedial action plan. (Health & Safety Code § 25356.3)

n4 Reporter's Transcript, California Regional Water Quality Control Board, San Francisco Bay Region, Proceedings Regarding Rhone-Poulenc and Zoecon Corporation - Waste Discharge Requirements, May 15, 1985, Page 29: Zoecon Corp. v. Rhone-Poulenc, Inc., Cal. Superior Court, County of San Mateo, No. 260687.

[*14]

Issues regarding indemnity, the application of the doctrine of caveat emptor n5 or possible misrepresentation at the time of the sale of the property can not, and should not, be resolved by this Board. However, we do want to point out that we disagree with the Petitioner's contention that as a policy matter requiring a present landowner to share responsibility for discharges of waste that began under a prior owner will undercut efforts to promote prompt disclosure and clean up of contaminated sites. The petitioner argues that this will encourage discharges to conceal their actions in order to shift responsibility on to innocent purchasers of contaminated property. On the contrary, we believe that our determination that present property owners are also responsible for waste discharges will encourage potential buyers to more thoroughly examine the conditions of property which they may acquire. Zoecon states that it purchased the property in 1972 and conducted an environmental audit of it in 1980. If the audit had taken place prior to the purchase of the property, it is most probable that this matter would not be before us today.

n5 Under the general rule of caveat emptor (let the buyer beware) in the absence of an express agreement, the vendor of land is not liable to his vendee for the condition of the land existing at the time of transfer.

[*15]

In addition, the petitioner characterizes itself as the "mere landowner" in the situation. Yet it is this very role that puts Zoecon in the position of being well suited to carrying out the needed onsite cleanup. The petitioner has exclusive control over access to the property. As such, it must share in responsibility for the clean up.

Petitioner's final argument concerns the alleged inequity in imposing waste discharge requirements on the basis of site ownership when the actual discharger is known and can perform the clean up. Zoecon cites State Dept. of Environmental Protection v. Exxon, 376 A.2d 1339 (NJ Superior Court, Chancery Division 1977). We do not speak here to the Court's application of New Jersey statutes since we question the comparability to the California statutory scheme. We do note however that the New Jersey court's conclusion regarding application of the common law nuisance doctrine would probably not be applied by a California court. This is because California Civil Code § 3483 provides that every successive owner of property who neglects to abate a continuing nuisance upon, or in the use of, such property, created by a former owner, is liable therefore [*16] in the same manner as the one who first created it. n6

n6 Common law governs in California only to the extent that it has not been modified by statute. [Victory Oil Co. v. Hancock Oil Co. 125 Cal.App.2d 222, 229, 270 P.2d 604 (1954)]

We find that our decision today is in many ways analogous to our long standing policy of naming a landlord in waste discharge requirements if necessary and appropriate to the circumstances before the Regional Board. This is consistent with the recent trend in California cases that is contrary to the traditional rule of landlord's non-liability subject to certain exceptions. In Rowland v. Christian (1968) 69 C.2d. 108, 70 Cal.Rptr. 97, 443 P.2d 651, California repudiated the traditional classification of duties governing the liability of an owner or possessor of land and substituted

the basic approach of foreseeability of injury to others. See, e.g. 3 Witkin, Summary of California Law (8th Ed. 1980 Supp.) Section 453A, *Uccello v. Lauderslayer* (1975) 44 Cal.App.3d 504, 118 Cal.Rptr. [*17] 741.

The court in *Uccello* held that an enlightened public policy requires that a landlord owes a duty of care to correct a dangerous condition created by a tenant, where the landlord has actual knowledge of the condition and an opportunity and the ability to obviate it. "To permit a landlord in such a situation to sit idly by in the face of the known danger to others must be deemed to be socially and legally unacceptable." (44 Cal.App.3d at 513.)

For all of the above reasons, we conclude that the petitioner is a discharger of waste who was appropriately named in the Regional Board's waste discharge requirements.

3. Contentions: Petitioner argues that it has been unconstitutionally denied due process and equal protection of the law in that it is the only property owner named as a discharger despite the fact that adjacent properties are also contaminated.

Finding: Unrefuted testimony before the Regional Board indicates that the vast majority of the contaminated area is now owned by Zoecon. A small portion of the contaminants have migrated off the site onto adjacent properties. Given the magnitude of the contamination found on the five-acre site which is the subject of the waste [*18] discharge requirements relative to the amount of contaminants of adjacent property, we find that it was appropriate for the regional Board to exercise its discretion pursuant to Water Code § 13269 and not issue waste discharge requirements for adjacent property at this time. We note that such a waiver of requirements may be terminated at any time. If additional fact finding should reveal more extensive off-site contamination, the Regional Board should, of course, reconsider its decision to waive requirements for adjacent properties.

III. CONCLUSIONS

After review of the record and consideration of the contentions of the petitioner, and for the reasons discussed above, we conclude:

Zoecon Corporation was properly named as a discharge in Order No. 85-67 (Waste Discharge Requirements for Rhone-Poulenc, Inc. and Zoecon Corporation, East Palo Alto, San Mateo County) by the California Regional Water Quality Control Board, San Francisco Bay Region.

IV. ORDER

IT IS HEREBY ORDERED THAT the petition is denied.

Legal Topics:

For related research and practice materials, see the following legal topics:

Environmental Law Hazardous Wastes & Toxic Substances Cleanup Real Property Law Torts General

Overview Torts Premises Liability & Property Lessees & Lessors Liabilities of Lessors Negligence General Overview



Supreme Court of the United States
 IMMIGRATION AND NATURALIZATION SER-
 VICE, Petitioner,
 v.
 Enrico ST. CYR.

No. 00-767.
 Argued April 24, 2001.
 Decided June 25, 2001.

Permanent resident alien filed petition for habeas corpus, seeking review of decision of Board of Immigration Appeals (BIA) that he was removable by reason of having pleaded guilty to aggravated felony and was ineligible to apply for discretionary relief from deportation. The United States District Court for the District of Connecticut, Alan H. Nevas, J., 64 F.Supp.2d 47, determined that it had jurisdiction and that repeal of discretionary relief from deportation did not apply retroactively to alien. Immigration and Naturalization Service (INS) appealed. The Court of Appeals, 229 F.3d 406, affirmed. Certiorari was granted. The Supreme Court, Justice Stevens, held that: (1) Antiterrorism and Effective Death Penalty Act (AEDPA) and Illegal Immigration Reform and Immigrant Responsibility Act (IIRIRA) did not deprive court of jurisdiction to review alien's habeas petition, and (2) provisions of AEDPA and IIRIRA repealing discretionary relief from deportation did not apply retroactively to alien, who pled guilty to sale of controlled substance prior to statutes' enactment.

Affirmed.

Justice Scalia filed dissenting opinion in which Chief Justice Rehnquist and Justice Thomas joined, and Justice O'Connor joined in part.

Justice O'Connor filed dissenting opinion.

West Headnotes

[1] Habeas Corpus 197 ↪205

197 Habeas Corpus
 197I In General
 197I(A) In General
 197I(A)1 Nature of Remedy in General
 197k205 k. Constitutional and statutory provisions. Most Cited Cases
 Implications from statutory text or legislative history are not sufficient to repeal habeas jurisdiction; instead, Congress must articulate specific and unambiguous statutory directives to effect a repeal. 28 U.S.C.A. § 2241.

[2] Constitutional Law 92 ↪999

92 Constitutional Law
 92VI Enforcement of Constitutional Provisions
 92VI(C) Determination of Constitutional Questions
 92VI(C)3 Presumptions and Construction as to Constitutionality
 92k998 Intent of and Considerations Influencing Legislature
 92k999 k. In general. Most Cited Cases
 (Formerly 92k48(3))
 When a particular interpretation of a statute invokes the outer limits of Congress' power, court expects a clear indication that Congress intended that result.

[3] Constitutional Law 92 ↪994

92 Constitutional Law
 92VI Enforcement of Constitutional Provisions
 92VI(C) Determination of Constitutional Questions
 92VI(C)3 Presumptions and Construction as to Constitutionality
 92k994 k. Avoidance of constitutional questions. Most Cited Cases
 (Formerly 92k48(1))
 If an otherwise acceptable construction of a

(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

statute would raise serious constitutional problems, and where an alternative interpretation of the statute is fairly possible, court is obligated to construe the statute to avoid such problems.

[4] Constitutional Law 92 ↻990

92 Constitutional Law

92VI Enforcement of Constitutional Provisions

92VI(C) Determination of Constitutional Questions

92VI(C)3 Presumptions and Construction as to Constitutionality

92k990 k. In general. Most Cited Cases

(Formerly 92k48(1))

Every reasonable construction of a statute must be resorted to in order to save the statute from unconstitutionality.

[5] Constitutional Law 92 ↻999

92 Constitutional Law

92VI Enforcement of Constitutional Provisions

92VI(C) Determination of Constitutional Questions

92VI(C)3 Presumptions and Construction as to Constitutionality

92k998 Intent of and Considerations Influencing Legislature

92k999 k. In general. Most Cited Cases

(Formerly 92k1007, 92k48(4.1))

Courts, when interpreting a statute, will not lightly assume that Congress intended to infringe constitutionally protected liberties or usurp power constitutionally forbidden it.

[6] Habeas Corpus 197 ↻912

197 Habeas Corpus

197V Suspension of Writ

197k912 k. Constitutional and statutory provisions. Most Cited Cases

Suspension Clause of Federal Constitution requires some judicial intervention in alien deporta-

tion cases. U.S.C.A. Const. Art. 1, § 9, cl. 2.

[7] Habeas Corpus 197 ↻912

197 Habeas Corpus

197V Suspension of Writ

197k912 k. Constitutional and statutory provisions. Most Cited Cases

At the absolute minimum, the Suspension Clause protects the writ of habeas corpus as it existed in 1789. U.S.C.A. Const. Art. 1, § 9, cl. 2.

[8] Habeas Corpus 197 ↻521

197 Habeas Corpus

197II Grounds for Relief; Illegality of Restraint

197II(C) Relief Affecting Particular Persons or Proceedings

197k521 k. Aliens. Most Cited Cases

Section of Antiterrorism and Effective Death Penalty Act (AEDPA) entitled "Elimination of Custody Review by Habeas Corpus," which repealed statute providing habeas relief for aliens in custody pursuant to a deportation order, did not deprive federal district court of jurisdiction to review alien's habeas corpus petition challenging decision of Board of Immigration Appeals (BIA) that he was ineligible to apply for discretionary relief from deportation. 28 U.S.C.A. § 2241; Immigration and Nationality Act, § 106(a)(10), as amended, 8 U.S.C.(1994 Ed.) § 1105a(a)(10).

[9] Habeas Corpus 197 ↻521

197 Habeas Corpus

197II Grounds for Relief; Illegality of Restraint

197II(C) Relief Affecting Particular Persons or Proceedings

197k521 k. Aliens. Most Cited Cases

Provisions of Illegal Immigration Reform and Immigrant Responsibility Act (IIRIRA) limiting judicial review of a final order of removal did not deprive federal district court of jurisdiction to review alien's habeas corpus petition challenging decision of Board of Immigration Appeals (BIA) that he was ineligible to apply for discretionary relief from de-

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

portation. Immigration and Nationality Act, § 242(a)(1), (a)(2)(C), (b)(9), 8 U.S.C.A. § 1252(a)(1), (a)(2)(C), (b)(9); 28 U.S.C.A. § 2241.

[10] Aliens, Immigration, and Citizenship 24
↪216

24 Aliens, Immigration, and Citizenship
24V Denial of Admission and Removal
24V(A) In General
24k212 Constitutional and Statutory Provisions
24k216 k. Retroactive operation. Most Cited Cases
(Formerly 24k40)

Provisions of Antiterrorism and Effective Death Penalty Act (AEDPA) and Illegal Immigration Reform and Immigrant Responsibility Act (IIRIRA) precluding alien who was removable because of conviction for aggravated felony from applying for discretionary relief from deportation did not apply retroactively to alien who pled guilty to sale of controlled substance prior to statutes' enactment. Immigration and Nationality Act, § 212(c), as amended, 8 U.S.C.(1994 Ed.) § 1182(c); § 242(a)(2)(C), as amended, 8 U.S.C.(1994 Ed.Supp. V) § 1252(a)(2)(C).

[11] Statutes 361 ↪278.7

361 Statutes
361VI Construction and Operation
361VI(D) Retroactivity
361k278.7 k. Express retroactive provisions. Most Cited Cases
(Formerly 361k263)

Congressional enactments will not be construed to have retroactive effect unless their language requires this result.

[12] Statutes 361 ↪278.3

361 Statutes
361VI Construction and Operation
361VI(D) Retroactivity
361k278.3 k. Power to enact and validity.

Most Cited Cases
(Formerly 92k186)

Congress has the power to enact laws with retrospective effect.

[13] Statutes 361 ↪278.7

361 Statutes
361VI Construction and Operation
361VI(D) Retroactivity
361k278.7 k. Express retroactive provisions. Most Cited Cases
(Formerly 92k188)

A statute may not be applied retroactively absent a clear indication from Congress that it intended such a result.

[14] Statutes 361 ↪278.7

361 Statutes
361VI Construction and Operation
361VI(D) Retroactivity
361k278.7 k. Express retroactive provisions. Most Cited Cases
(Formerly 92k188)

The first step in determining whether a statute has an impermissible retroactive effect is to ascertain whether Congress has directed with the requisite clarity that the law be applied retrospectively.

[15] Statutes 361 ↪278.2

361 Statutes
361VI Construction and Operation
361VI(D) Retroactivity
361k278.2 k. Nature and scope. Most Cited Cases
(Formerly 361k263)

The inquiry into whether a statute operates retroactively demands a commonsense, functional judgment about whether the new provision attaches new legal consequences to events completed before its enactment.

[16] Statutes 361 ↪278.9

361 Statutes

361VI Construction and Operation

361VI(D) Retroactivity

361k278.9 k. Statutes affecting vested rights. Most Cited Cases
(Formerly 361k265)

Statutes 361 ↪ 278.10

361 Statutes

361VI Construction and Operation

361VI(D) Retroactivity

361k278.10 k. Statutes imposing liabilities, penalties, duties, obligations, or disabilities. Most Cited Cases

(Formerly 361k265, 361k266)

A statute has retroactive effect when it takes away or impairs vested rights acquired under existing laws, or creates a new obligation, imposes a new duty, or attaches a new disability, in respect to transactions or considerations already past.

[17] Statutes 361 ↪ 278.1

361 Statutes

361VI Construction and Operation

361VI(D) Retroactivity

361k278.1 k. In general. Most Cited Cases

(Formerly 361k263)

The judgment whether a particular statute acts retroactively should be informed and guided by familiar considerations of fair notice, reasonable reliance, and settled expectations.

****2273 Syllabus** ^{FN*}

FN* The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States v. Detroit Timber & Lumber Co.*, 200 U.S. 321, 337, 26 S.Ct. 282, 50 L.Ed. 499.

***289** Before the effective dates of the Antiterrorism and Effective Death Penalty Act of 1996 (AEDPA) and the Illegal Immigration Reform and Immigrant Responsibility Act of 1996 (IIRIRA), §

212(c) of the Immigration and Nationality Act of 1952 was interpreted to give the Attorney General broad discretion to waive deportation of resident aliens. As relevant here, the large class of aliens depending on § 212(c) relief was reduced in 1996 by § 401 of AEDPA, which identified a broad set of offenses for which convictions would preclude such relief; and by IIRIRA, which repealed § 212(c) and replaced it with a new section excluding from the class anyone “convicted of an aggravated felony,” 8 U.S.C. § 1229b(a)(3). Respondent St. Cyr, a lawful permanent United States resident, pleaded guilty to a criminal charge that made him deportable. He would have been eligible for a waiver of deportation under the immigration law in effect when he was convicted, but his removal proceedings were commenced after AEDPA’s and IIRIRA’s effective dates. The Attorney General claims that those Acts withdrew his authority to grant St. Cyr a waiver. The Federal District Court accepted St. Cyr’s habeas corpus application and agreed that the new restrictions do not apply to removal proceedings brought against an alien who pleaded guilty to a deportable crime before their enactment. The Second Circuit affirmed.

Held:

1. Courts have jurisdiction under 28 U.S.C. § 2241 to decide the legal issue raised by St. Cyr’s habeas petition. Pp. 2278-2287.

(a) To prevail on its claim that AEDPA and IIRIRA stripped federal courts of jurisdiction to decide a pure question of law, as in this case, petitioner Immigration and Naturalization Service (INS) must overcome both the strong presumption in favor of judicial review of administrative action and the longstanding rule requiring a clear and unambiguous statement of congressional intent to repeal habeas jurisdiction. Here, that plain statement rule draws additional reinforcement from other canons of statutory construction: First, when a statutory interpretation invokes the outer limits of Congress’ power, there must be a clear indication that Congress intended that result; and ***290** second, if an

otherwise acceptable construction would raise serious constitutional problems and an alternative interpretation is fairly possible, the statute must be construed to avoid such problems. Pp. 2278-2279.

(b) Construing the amendments at issue to preclude court review of a pure question of law would give rise to substantial constitutional questions. The Constitution's Suspension Clause, which protects the privilege of the habeas corpus writ, unquestionably requires some judicial intervention in deportation cases. *Heikkila v. Barber*, 345 U.S. 229, 235, 73 S.Ct. 603, 97 L.Ed. 972. Even assuming that the Clause protects only the writ as it existed in 1789, substantial evidence supports St. Cyr's claim that pure questions of law could have been answered in 1789 by a common-law judge with power to issue the writ. Thus, a serious Suspension Clause issue would arise if the 1996 statutes have withdrawn that power from federal judges and provided no adequate substitute. The need to resolve such a serious and difficult constitutional question and the desirability of avoiding that necessity reinforce the reasons for requiring a clear and unambiguous statement of constitutional intent. Pp. 2279-2282.

(c) To conclude that the writ is no longer available in this context would also represent a marked departure from historical immigration law practice. The writ has always been available to review the **2274 legality of Executive detention, see, e.g., *Felker v. Turpin*, 518 U.S. 651, 663, 116 S.Ct. 2333, 135 L.Ed.2d 827, and, until the 1952 Act, a habeas action was the sole means of challenging a deportation order's legality, see, e.g., *Heikkila*, 345 U.S., at 235, 73 S.Ct. 603. Habeas courts have answered questions of law in alien suits challenging Executive interpretations of immigration law and questions of law that arose in the discretionary relief context. Pp. 2282-2283.

(d) Neither AEDPA § 401(e) nor three IIRIRA provisions, 8 U.S.C. §§ 1252(a)(1), (a)(2)(C), and (b)(9), express a clear and unambiguous statement of Congress' intent to bar 28 U.S.C. § 2241 petitions. None of these sections even mentions § 2241.

Section 401(e)'s repeal of a subsection of the 1961 Act, which provided, *inter alia*, habeas relief for an alien in custody pursuant to a deportation order, is not sufficient to eliminate what the repealed section did not grant—namely, habeas jurisdiction pursuant to § 2241. See *Ex parte Yerger*, 8 Wall. 85, 105-106, 19 L.Ed. 332. The three IIRIRA provisions do not speak with sufficient clarity to bar habeas jurisdiction. They focus on “judicial review” or “jurisdiction to review.” In the immigration context, however, “judicial review” and “habeas corpus” have historically distinct meanings, with habeas courts playing a far narrower role. Pp. 2283-2287.

2. Section 212(c) relief remains available for aliens, like St. Cyr, whose convictions were obtained through plea agreements and who, notwithstanding those convictions, would have been eligible for § 212(c) relief at the time of their plea under the law then in effect. Pp. 2287-2293.

*291 a) A statute's language must require that it be applied retroactively. *Bowen v. Georgetown Univ. Hospital*, 488 U.S. 204, 208, 109 S.Ct. 468, 102 L.Ed.2d 493. The first step in the impermissible-retroactive-effect determination is to ascertain whether Congress has directed with the requisite clarity that the law be applied retrospectively. *Martin v. Hadix*, 527 U.S. 343, 352, 119 S.Ct. 1998, 144 L.Ed.2d 347. Such clarity is not shown by the comprehensiveness of IIRIRA's revision of federal immigration law, see *Landgraf v. USI Film Products*, 511 U.S. 244, 260-261, 114 S.Ct. 1483, 128 L.Ed.2d 229, by the promulgation of IIRIRA's effective date, see *id.*, at 257, 114 S.Ct. 1483, or by IIRIRA § 309(c)(1)'s “saving provision.” Pp. 2287-2290.

(b) The second step is to determine whether IIRIRA attaches new legal consequences to events completed before its enactment, a judgment informed and guided by considerations of fair notice, reasonable reliance, and settled expectations. *Landgraf*, 511 U.S., at 270, 114 S.Ct. 1483. IIRIRA's elimination of § 212(c) relief for people who

entered into plea agreements expecting that they would be eligible for such relief clearly attaches a new disability to past transactions or considerations. Plea agreements involve a *quid pro quo* between a criminal defendant and the government, and there is little doubt that alien defendants considering whether to enter into such agreements are acutely aware of their convictions' immigration consequences. The potential for unfairness to people like St. Cyr is significant and manifest. Now that prosecutors have received the benefit of plea agreements, facilitated by the aliens' belief in their continued eligibility for § 212(c) relief, it would be contrary to considerations of fair notice, reasonable reliance, and settled expectations to hold that IIRIRA deprives them of any possibility of such relief. The INS' argument that application of deportation law can never have retroactive effect because deportation proceedings are inherently prospective is not particularly helpful in undertaking *Landgraf's* analysis, and the fact that deportation is not punishment for past crimes does not mean that the Court cannot consider an alien's reasonable reliance on the continued availability of discretionary relief from deportation **2275 when deciding the retroactive effect of eliminating such relief. That § 212(c) relief is discretionary does not affect the propriety of this Court's conclusion, for there is a clear difference between facing possible deportation and facing certain deportation. Pp. 2290-2293.

229 F.3d 406, affirmed.

STEVENS, J., delivered the opinion of the Court, in which KENNEDY, SOUTER, GINSBURG, and BREYER, JJ., joined. O'CONNOR, J., filed a dissenting opinion, *post*, p. 2293. SCALIA, J., filed a dissenting opinion, in *292 which REHNQUIST, C.J., and THOMAS, J., joined, and in which O'CONNOR, J., joined as to Parts I and III, *post*, p. 2293.

Edwin S. Kneedler, Washington, DC, for petitioner.

Lucas Guttentag, for respondent.

For U.S. Supreme Court briefs, see:2001 WL

210189 (Pet.Brief)2001 WL 324615
(Resp.Brief)2001 WL 394838 (Reply.Brief)

Justice STEVENS delivered the opinion of the Court.

Both the Antiterrorism and Effective Death Penalty Act of 1996 (AEDPA), enacted on April 24, 1996, 110 Stat. 1214, and the Illegal Immigration Reform and Immigrant Responsibility Act of 1996 (IIRIRA), enacted on September 30, 1996, 110 Stat. 3009-546, contain comprehensive amendments to the Immigration and Nationality Act (INA), 66 Stat. 163, as amended, 8 U.S.C. § 1101 *et seq.* This case raises two important questions about the impact of those amendments. The first question is a procedural one, concerning the effect of those amendments on the availability of habeas corpus jurisdiction under 28 U.S.C. § 2241. The second question is a substantive one, concerning the impact of the amendments on conduct that occurred before *293 their enactment and on the availability of discretionary relief from deportation.

Respondent, Enrico St. Cyr, is a citizen of Haiti who was admitted to the United States as a lawful permanent resident in 1986. Ten years later, on March 8, 1996, he pleaded guilty in a state court to a charge of selling a controlled substance in violation of Connecticut law. That conviction made him deportable. Under pre-AEDPA law applicable at the time of his conviction, St. Cyr would have been eligible for a waiver of deportation at the discretion of the Attorney General. However, removal proceedings against him were not commenced until April 10, 1997, after both AEDPA and IIRIRA became effective, and, as the Attorney General interprets those statutes, he no longer has discretion to grant such a waiver.

In his habeas corpus petition, respondent has alleged that the restrictions on discretionary relief from deportation contained in the 1996 statutes do not apply to removal proceedings brought against an alien who pleaded guilty to a deportable crime before their enactment. The District Court accepted jurisdiction of his application and agreed with his

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

submission. In accord with the decisions of four other Circuits, the Court of Appeals for the Second Circuit affirmed.^{FN1} 229 F.3d 406 (2000). The importance of both questions warranted our grant of certiorari. 531 U.S. 1107, 121 S.Ct. 848, 148 L.Ed.2d 733 (2001).

FN1. See *Mahadeo v. Reno*, 226 F.3d 3 (C.A.1 2000); *Liang v. INS*, 206 F.3d 308 (C.A.3 2000); *Tasios v. Reno*, 204 F.3d 544 (C.A.4 2000); *Flores-Miramontes v. INS*, 212 F.3d 1133 (C.A.9 2000). But see *Max-George v. Reno*, 205 F.3d 194 (C.A.5 2000); *Morales-Ramirez v. Reno*, 209 F.3d 977 (C.A.7 2000); *Richardson v. Reno*, 180 F.3d 1311 (C.A.11 1999).

I

The character of the pre-AEDPA and pre-IIRIRA law that gave the Attorney General discretion to waive deportation in certain cases is relevant to our appraisal of **2276 both the substantive and the procedural questions raised by *294 the petition of the Immigration and Naturalization Service (INS). We shall therefore preface our discussion of those questions with an overview of the sources, history, and scope of that law.

Subject to certain exceptions, § 3 of the Immigration Act of 1917 excluded from admission to the United States several classes of aliens, including, for example, those who had committed crimes “involving moral turpitude.” 39 Stat. 875. The seventh exception provided “[t]hat aliens returning after a temporary absence to an unrelinquished United States domicile of seven consecutive years may be admitted in the discretion of the Secretary of Labor, and under such conditions as he may prescribe.” *Id.*, at 878.^{FN2} Although that provision applied literally only to exclusion proceedings, and although the deportation provisions of the statute did not contain a similar provision, the INS relied on § 3 to grant relief in deportation proceedings involving aliens who had departed and returned to this country after the ground for deportation arose. See, e.g., *Matter of L*, 1 I. & N. Dec. 1, 2, 1940 WL

7544 (1940).^{FN3}

FN2. The INS was subsequently transferred to the Department of Justice. See *Matter of L*, 1 I. & N. Dec. 1, n. 1 (1940). As a result, the powers previously delegated to the Secretary of Labor were transferred to the Attorney General. See *id.*, at 2

FN3. The exercise of discretion was deemed a *nunc pro tunc* correction of the record of reentry. In approving of this construction, the Attorney General concluded that strictly limiting the seventh exception to exclusion proceedings would be “capricious and whimsical.” *Id.*, at 5.

Section 212 of the Immigration and Nationality Act of 1952, which replaced and roughly paralleled § 3 of the 1917 Act, excluded from the United States several classes of aliens, including those convicted of offenses involving moral turpitude or the illicit traffic in narcotics. See 66 Stat. 182-187. As with the prior law, this section was subject to a proviso granting the Attorney General broad discretion to *295 admit excludable aliens. See *id.*, at 187. That proviso, codified at 8 U.S.C. § 1182(c), stated:

“Aliens lawfully admitted for permanent residence who temporarily proceeded abroad voluntarily and not under an order of deportation, and who are returning to a lawful unrelinquished domicile of seven consecutive years, may be admitted in the discretion of the Attorney General”

Like § 3 of the 1917 Act, § 212(c) was literally applicable only to exclusion proceedings, but it too has been interpreted by the Board of Immigration Appeals (BIA) to authorize any permanent resident alien with “a lawful unrelinquished domicile of seven consecutive years” to apply for a discretionary waiver from deportation. See *Matter of Silva*, 16 I. & N. Dec. 26, 30, 1976 WL 32326 (1976) (adopting position of *Francis v. INS*, 532 F.2d 268 (C.A.2

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

1976)). If relief is granted, the deportation proceeding is terminated and the alien remains a permanent resident.

The extension of § 212(c) relief to the deportation context has had great practical importance, because deportable offenses have historically been defined broadly. For example, under the INA, aliens are deportable upon conviction for two crimes of “moral turpitude” (or for one such crime if it occurred within five years of entry into the country and resulted in a jail term of at least one year). See 8 U.S.C. §§ 1227(a)(2)(A)(i)-(ii) (1994 ed., Supp. V). In 1988, Congress further specified that an alien is deportable upon conviction for any “aggravated felony,” Anti-Drug Abuse Act of 1988, 102 Stat. 4469-4470, § 1227(a)(2)(A)(iii), which was defined to include numerous offenses without regard to how long ago they were committed.^{FN4} **2277 Thus, the class of aliens *296 whose continued residence in this country has depended on their eligibility for § 212(c) relief is extremely large, and not surprisingly, a substantial percentage of their applications for § 212(c) relief have been granted.^{FN5} Consequently, in the period between 1989 and 1995 alone, § 212(c) relief was granted to over 10,000 aliens.^{FN6}

FN4. See 8 U.S.C. § 1101(a)(43) (1994 ed. and Supp. V). While the term has always been defined expansively, it was broadened substantially by IIRIRA. For example, as amended by that statute, the term includes all convictions for theft or burglary for which a term of imprisonment of at least one year is imposed (as opposed to five years pre-IIRIRA), compare § 1101(a)(43)(G) (1994 ed., Supp. V) with § 1101(a)(43)(G) (1994 ed.), and all convictions involving fraud or deceit in which the loss to the victim exceeds \$10,000 (as opposed to \$200,000 pre-IIRIRA), compare § 1101(a)(43)(M)(i) (1994 ed., Supp. V) with § 1101(a)(43)(M)(i) (1994 ed.). In addition, the term includes any “crime of vi-

olence” resulting in a prison sentence of at least one year (as opposed to five years pre-IIRIRA), compare § 1101(a)(43)(F) (1994 ed., Supp. V) with § 1101(a)(43)(F) (1994 ed.), and that phrase is itself broadly defined. See 18 U.S.C. § 16 (“[A]n offense that has as an element the use, attempted use, or threatened use of physical force against the person or property of another,” or “any other offense that is a felony and that, by its nature, involves a substantial risk that physical force against the person or property of another may be used in the course of committing the offense”).

FN5. See, e.g., Rannik, The Anti-Terrorism and Effective Death Penalty Act of 1996: A Death Sentence for the 212(c) Waiver, 28 U. Miami Inter-Am. L.Rev. 123, 150, n. 80 (1996) (providing statistics indicating that 51.5% of the applications for which a final decision was reached between 1989 and 1995 were granted); see also *Mattis v. Reno*, 212 F.3d 31, 33 (C.A.1 2000) (“[I]n the years immediately preceding the statute's passage, over half the applications were granted”); *Tasios*, 204 F.3d, at 551 (same).

In developing these changes, the BIA developed criteria, comparable to common-law rules, for deciding when deportation is appropriate. Those criteria, which have been set forth in several BIA opinions, see, e.g., *Matter of Marin*, 16 I. & N. Dec. 581, 1978 WL 36472 (1978), include the seriousness of the offense, evidence of either rehabilitation or recidivism, the duration of the alien's residence, the impact of deportation on the family, the number of citizens in the family, and the character of any service in the Armed Forces.

FN6. See Rannik, 28 U. Miami Inter-Am.L.Rev., at 150, n. 80. However, based

on these statistics, one cannot form a reliable estimate of the number of individuals who will be affected by today's decision. Since the 1996 statutes expanded the definition of "aggravated felony" substantially and retroactively—the number of individuals now subject to deportation absent § 212(c) relief is significantly higher than these figures would suggest. In addition, the nature of the changes (bringing under the definition more minor crimes which may have been committed many years ago) suggests that an increased percentage of applicants will meet the stated criteria for § 212(c) relief.

*297 Three statutes enacted in recent years have reduced the size of the class of aliens eligible for such discretionary relief. In 1990, Congress amended § 212(c) to preclude from discretionary relief anyone convicted of an aggravated felony who had served a term of imprisonment of at least five years. § 511, 104 Stat. 5052 (amending 8 U.S.C. § 1182(c)). In 1996, in § 440(d) of AEDPA, Congress identified a broad set of offenses for which convictions would preclude such relief. See 110 Stat. 1277 (amending 8 U.S.C. § 1182(c)).^{FN7} And finally, that same year, Congress passed IIRIRA. That statute, *inter alia*, repealed § 212(c), see § 304(b), 110 Stat. 3009-597, and replaced it with a new section that gives the Attorney General the authority to cancel removal for a narrow class of inadmissible or deportable aliens, see *id.*, at 3009-594 (creating 8 U.S.C. § 1229b (1994 ed., Supp. V)). So narrowed, that class does not include anyone previously "convicted of any aggravated felony." § 1229b(a)(3) (1994 ed., Supp. V).

FN7. The new provision barred review for individuals ordered deported because of a conviction for an aggravated felony, for a drug conviction, for certain weapons or national security violations, and for multiple convictions involving crimes of moral turpitude. See 110 Stat. 1277.

In the Attorney General's opinion, these amendments have entirely withdrawn his **2278 § 212(c) authority to waive deportation for aliens previously convicted of aggravated felonies. Moreover, as a result of other amendments adopted in AEDPA and IIRIRA, the Attorney General also maintains that there is no judicial forum available to decide whether these statutes did, in fact, deprive him of the power to grant such relief. As we shall explain below, we disagree on both points. In our view, a federal court does have jurisdiction to decide the merits of the legal question, and *298 the District Court and the Court of Appeals decided that question correctly in this case.

II

The first question we must consider is whether the District Court retains jurisdiction under the general habeas corpus statute, 28 U.S.C. § 2241, to entertain St. Cyr's challenge. His application for a writ raises a pure question of law. He does not dispute any of the facts that establish his deportability or the conclusion that he is deportable. Nor does he contend that he would have any right to have an unfavorable exercise of the Attorney General's discretion reviewed in a judicial forum. Rather, he contests the Attorney General's conclusion that, as a matter of statutory interpretation, he is not eligible for discretionary relief.

The District Court held, and the Court of Appeals agreed, that it had jurisdiction to answer that question in a habeas corpus proceeding.^{FN8} The INS argues, however, that four sections of the 1996 statutes—specifically, § 401(e) of AEDPA and three sections of IIRIRA (8 U.S.C. §§ 1252(a)(1), 1252(a)(2)(C), and 1252(b)(9) (1994 ed., Supp. V))—stripped the courts of jurisdiction to decide the question of law presented by respondent's habeas corpus application.

FN8. See n. 1, *supra*; n. 33, *infra*.

[1] For the INS to prevail it must overcome both the strong presumption in favor of judicial review of administrative action^{FN9} and the long-

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

standing rule requiring a clear statement of congressional intent to repeal habeas jurisdiction. See *Ex parte Yerger*, 8 Wall. 85, 102, 19 L.Ed. 332 (1869) (“We are not at liberty to except from [habeas corpus jurisdiction] any cases not plainly excepted by law”); *Felker v. Turpin*, 518 U.S. 651, 660-661, 116 S.Ct. 2333, 135 L.Ed.2d 827 (1996) (noting that “[n]o provision of Title I *299 mentions our authority to entertain original habeas petitions,” and the statute “makes no mention of our authority to hear habeas petitions filed as original matters in this Court”).^{FN10} Implications from statutory text or legislative history are not sufficient to repeal habeas jurisdiction; instead, Congress must articulate specific and unambiguous **2279 statutory directives to effect a repeal. *Ex parte Yerger*, 8 Wall., at 105 (“Repeals by implication are not favored. They are seldom admitted except on the ground of repugnancy; and never, we think, when the former act can stand together with the new act”).^{FN11}

FN9. See, e.g., *Bowen v. Michigan Academy of Family Physicians*, 476 U.S. 667, 670, 106 S.Ct. 2133, 90 L.Ed.2d 623 (1986); see also *McNary v. Haitian Refugee Center, Inc.*, 498 U.S. 479, 498, 111 S.Ct. 888, 112 L.Ed.2d 1005 (1991); *Webster v. Doe*, 486 U.S. 592, 603, 108 S.Ct. 2047, 100 L.Ed.2d 632 (1988); *Johnson v. Robison*, 415 U.S. 361, 373-374, 94 S.Ct. 1160, 39 L.Ed.2d 389 (1974).

FN10. “In traditionally sensitive areas, ... the requirement of [a] clear statement assures that the legislature has in fact faced, and intended to bring into issue, the critical matters involved in the judicial decision.” *Gregory v. Ashcroft*, 501 U.S. 452, 461, 111 S.Ct. 2395, 115 L.Ed.2d 410 (1991) (internal quotation marks and citations omitted); see *United States v. Nordic Village, Inc.*, 503 U.S. 30, 33, 112 S.Ct. 1011, 117 L.Ed.2d 181 (1992) (“Waivers of the [Federal] Government's sovereign im-

munity, to be effective, must be ‘unequivocally expressed’ ”); *Atascadero State Hospital v. Scanlon*, 473 U.S. 234, 242, 105 S.Ct. 3142, 87 L.Ed.2d 171 (1985) (“Congress may abrogate the States' constitutionally secured immunity from suit in federal court only by making its intention unmistakably clear in the language of the statute”); see also Eskridge & Frickey, *Quasi-Constitutional Law: Clear Statement Rules as Constitutional Law-making*, 45 Vand. L.Rev. 593, 597 (1992) (“[T]he Court ... has tended to create the strongest clear statement rules to confine Congress's power in areas in which Congress has the constitutional power to do virtually anything”).

FN11. Cf. *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1018, 104 S.Ct. 2862, 81 L.Ed.2d 815 (1984) (“[W]here two statutes are capable of co-existence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective” (internal quotation marks omitted)).

[2][3][4][5] In this case, the plain statement rule draws additional reinforcement from other canons of statutory construction. First, as a general matter, when a particular interpretation of a statute invokes the outer limits of Congress' power, we expect a clear indication that Congress intended that result. See *Edward J. DeBartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council*, 485 U.S. 568, 575, 108 S.Ct. 1392, 99 L.Ed.2d 645 (1988). Second, if an otherwise acceptable construction of a statute *300 would raise serious constitutional problems, and where an alternative interpretation of the statute is “fairly possible,” see *Crowell v. Benson*, 285 U.S. 22, 62, 52 S.Ct. 285, 76 L.Ed. 598 (1932), we are obligated to construe the statute to avoid such problems. See *Ashwander v. TVA*, 297 U.S. 288, 341, 345-348, 56 S.Ct. 466, 80 L.Ed. 688 (1936) (Brandeis, J., concurring);

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

United States ex rel. Attorney General v. Delaware & Hudson Co., 213 U.S. 366, 408, 29 S.Ct. 527, 53 L.Ed. 836 (1909).^{FN12}

FN12. “As was stated in *Hooper v. California*, 155 U.S. 648, 657, 15 S.Ct. 207, 39 L.Ed. 297 (1895), “[t]he elementary rule is that every reasonable construction must be resorted to, in order to save a statute from unconstitutionality.’ This approach ... also recognizes that Congress, like this Court, is bound by and swears an oath to uphold the Constitution. The courts will therefore not lightly assume that Congress intended to infringe constitutionally protected liberties or usurp power constitutionally forbidden it.” *Edward J. DeBartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council*, 485 U.S. 568, 575, 108 S.Ct. 1392, 99 L.Ed.2d 645 (1988) (citing *Grenada County Supervisors v. Brown*, 112 U.S. 261, 269, 5 S.Ct. 125, 28 L.Ed. 704 (1884)); see also *NLRB v. Catholic Bishop of Chicago*, 440 U.S. 490, 499-501, 504, 99 S.Ct. 1313, 59 L.Ed.2d 533 (1979); *Murray v. Schooner Charming Betsy*, 6 Cranch 64, 118, 2 L.Ed. 208 (1804); *Machinists v. Street*, 367 U.S. 740, 749-750, 81 S.Ct. 1784, 6 L.Ed.2d 1141 (1961); *Crowell v. Benson*, 285 U.S. 22, 62, 52 S.Ct. 285, 76 L.Ed. 598 (1932); *Lucas v. Alexander*, 279 U.S. 573, 577, 49 S.Ct. 426, 73 L.Ed. 851 (1929); *Panama R. Co. v. Johnson*, 264 U.S. 375, 390, 44 S.Ct. 391, 68 L.Ed. 748 (1924); *Delaware & Hudson Co.*, 213 U.S., at 407-408, 29 S.Ct. 527; *Parsons v. Bedford*, 3 Pet. 433, 448-449, 7 L.Ed. 732 (1830) (Story, J.).

[6] A construction of the amendments at issue that would entirely preclude review of a pure question of law by any court would give rise to substantial constitutional questions. Article I, § 9, cl. 2, of the Constitution provides: “The Privilege of the Writ of Habeas Corpus shall not be suspended, un-

less when in Cases of Rebellion or Invasion the public Safety may require it.” Because of that Clause, some “judicial intervention in deportation cases” is unquestionably “required by the Constitution.” *Heikkila v. Barber*, 345 U.S. 229, 235, 73 S.Ct. 603, 97 L.Ed. 972 (1953).

[7] Unlike the provisions of AEDPA that we construed in *Felker v. Turpin*, 518 U.S. 651, 116 S.Ct. 2333, 135 L.Ed.2d 827 (1996), this case involves an alien subject to a federal removal order rather than a person confined pursuant to a state-court conviction. Accordingly, regardless of whether the protection of the Suspension *301 Clause encompasses all cases covered by the 1867 Amendment extending the protection of the writ to state prisoners, cf. *id.*, at 663-664, 116 S.Ct. 2333, or by subsequent legal developments, see *LaGuerre v. Reno*, 164 F.3d 1035 (C.A.7 1998), at the absolute minimum, the Suspension Clause protects the writ “as it existed in 1789.”^{FN13} **2280 *Felker*, 518 U.S., at 663-664, 116 S.Ct. 2333.

FN13. The fact that this Court would be required to answer the difficult question of what the Suspension Clause protects is in and of itself a reason to avoid answering the constitutional questions that would be raised by concluding that review was barred entirely. Cf. Neuman, Habeas Corpus, Executive Detention, and the Removal of Aliens, 98 Colum. L.Rev. 961, 980 (1998) (noting that “reconstructing habeas corpus law ... [for purposes of a Suspension Clause analysis] would be a difficult enterprise, given fragmentary documentation, state-by-state disuniformity, and uncertainty about how state practices should be transferred to new national institutions”).

At its historical core, the writ of habeas corpus has served as a means of reviewing the legality of Executive detention, and it is in that context that its protections have been strongest.^{FN14} See, e.g., *Swain v. Pressley*, 430 U.S. 372, 380, n. 13, 97

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

S.Ct. 1224, 51 L.Ed.2d 411 (1977); *id.*, at 385-386, 97 S.Ct. 1224 (Burger, C. J., concurring) (noting that “the traditional Great Writ was largely a remedy against executive detention”); *Brown v. Allen*, 344 U.S. 443, 533, 73 S.Ct. 397, 97 L.Ed. 469 (1953) (Jackson, J., concurring in result) (“The historic purpose of the writ has been to relieve detention by executive authorities without judicial trial”). In England prior to 1789, in the Colonies,^{FN15} and in this Nation during the formative years of our Government, the writ of habeas corpus was available to nonenemy aliens as well as to citizens.*302

^{FN16} It enabled them to challenge Executive and private detention in civil cases as well as criminal.

^{FN17} Moreover, the issuance of the writ was not limited to challenges to the jurisdiction of the custodian, but encompassed detentions based on errors of law, including the erroneous application or interpretation of statutes.^{FN18} It was used to command

the discharge of seamen who had a statutory exemption from impressment into the British Navy,^{FN19} to emancipate slaves,^{FN20} and to obtain the freedom of apprentices^{FN21} and asylum inmates.^{FN22}

Most important, for our purposes, those early cases contain no suggestion that habeas relief in cases involving*303 Executive detention was only available for constitutional error.^{FN23}

FN14. At common law, “[w]hile habeas review of a court judgment was limited to the issue of the sentencing court’s jurisdictional competency, an attack on an executive order could raise all issues relating to the legality of the detention.” Note, Developments in the Law-Federal Habeas Corpus, 83 Harv. L.Rev. 1038, 1238 (1970).

FN15. See W. Duker, A Constitutional History of Habeas Corpus 115 (1980) (noting that “the common-law writ of habeas corpus was in operation in all thirteen of the British colonies that rebelled in 1776”).

FN16. See *Somerset v. Stewart*, 20 How. St. Tr. 1, 79-82 (K.B.1772); *Case of the*

Hottentot Venus, 13 East 195, 104 Eng. Rep. 344 (K.B.1810); *King v. Schiever*, 2 Burr. 765, 97 Eng. Rep. 551 (K.B.1759); *United States v. Villato*, 2 U.S. 370, 2 Dall. 370, 1 L.Ed. 419, 28 F.Cas. 377 (No. 16,622) (C.C.Pa.1797); *Commonwealth v. Holloway*, 1 Serg. & Rawle 392, 1815 WL 1249 (Pa.1815); *Ex parte D’Olivera*, 7 F.Cas. 853 (No. 3,967) (C.C.Mass.1813); see also Brief for Legal Historians as *Amici Curiae* 10-11; Neuman, Habeas Corpus, Executive Detention, and the Removal of Aliens, 98 Colum.L.Rev., at 990-1004.

FN17. See *King v. Nathan*, 2 Strange 880, 93 Eng. Rep. 914 (K.B.1724); *Ex parte Boggin*, 13 East 549, 104 Eng. Rep. 484 (K.B.1811); *Hollingshead’s Case*, 1 Salkeld 351, 91 Eng. Rep. 307 (K.B.1702); *Dr. Groenvelt’s Case*, 1 Ld.Raym. 213, 91 Eng. Rep. 1038 (K.B.1702); *Bushell’s Case*, Vaughn 135, 124 Eng. Rep. 1006 (C.P. 1670); *Ex parte Randolph*, 20 F. Cas. 242 (No. 11,558) (C.C.D.Va. 1833) (Marshall, C. J., on circuit); *Ex parte D’Olivera*, 7 F. Cas. 853 (No. 3,967) (C.C.D.Mass. 1813); *Respublica v. Keppeler*, 2 Dall. 197, 1 L.Ed. 347 (Pa.1793).

FN18. See, e.g., *Hollingshead’s Case*, 1 Salkeld 351, 91 Eng. Rep. 307 (K.B.1702); *King v. Nathan*, 2 Strange 880, 93 Eng. Rep. 914 (K.B.1724); *United States v. Bainbridge*, 24 F.Cas. 946 (No. 14,497) (C.C.Mass.1816); *Ex parte Randolph*, 20 F. Cas. 242 (No. 11,558) (C.C.Va.1833) (Marshall, C. J., on circuit); see also Brief for Legal Historians as *Amici Curiae* 3-10 (collecting cases).

FN19. See, e.g., the case of *King v. White* (1746) quoted in the addendum to *Somerset v. Stewart*, 20 How. St. Tr., at 1376.

FN20. *Id.*, at 79-82.

FN21. *King v. Delaval*, 3 Burr. 1434, 97 Eng. Rep. 913 (K.B.1763).

FN22. *King v. Turlington*, 2 Burr. 1115, 97 Eng. Rep. 741 (K.B.1761).

FN23. See, e.g., *Ex parte Boggin*, 13 East 549, n. (b), 104 Eng. Rep. 484, n. (a)² (K.B.1811) (referring to *Chalacombe's Case*, in which the court required a response from the Admiralty in a case involving the impressment of a master of a coal vessel, despite the argument that exemptions for "seafaring persons of this description" were given only as a matter of "grace and favour," not "of right"); *Hollingshead's Case*, 1 Salkeld 351, 91 Eng. Rep. 307 (K.B.1702) (granting relief on the grounds that the language of the warrant of commitment-authorizing detention until "*otherwise discharged by due course of law*"—exceeded the authority granted under the statute to commit "till [the bankrupt] submit himself to be examined by the commissioners"); see also Brief for Legal Historians as *Amici Curiae* 8-10, 18-28.

The dissent, however, relies on *Chalacombe's Case* as its sole support for the proposition that courts treated Executive discretion as "lying entirely beyond the judicial ken." See *post*, at 2302 (opinion of SCALIA, J.). Although Lord Ellenborough expressed "some hesitation" as to whether the case should "stand over for the consideration of the Admiralty," he concluded that, given the public importance of the question, the response should be called for. 13 East, at 549, n. (b), 104 Eng. Rep., at 484, n.(a)². The case ultimately became moot when the Admiralty discharged Chalacombe, but it is significant that,

despite some initial hesitation, the court decided to proceed.

****2281** Notwithstanding the historical use of habeas corpus to remedy unlawful Executive action, the INS argues that this case falls outside the traditional scope of the writ at common law. It acknowledges that the writ protected an individual who was held without legal authority, but argues that the writ would not issue where "an official had statutory authorization to detain the individual ... but ... the official was not properly exercising his discretionary power to determine whether the individual should be released." Brief for Respondent in *Calcano-Martinez v. INS*, O.T.2000, No. 00-1011, p. 33. In this case, the INS points out, there is no dispute that the INS had authority in law to hold St. Cyr, as he is eligible for removal. St. Cyr counters that there is historical evidence of the writ issuing to redress the ***304** improper exercise of official discretion. See n. 23, *supra*; Hafetz, *The Untold Story of Noncriminal Habeas Corpus and the 1996 Immigration Acts*, 107 Yale L.J. 2509 (1998).

St. Cyr's constitutional position also finds some support in our prior immigration cases. In *Heikkila v. Barber*, the Court observed that the then-existing statutory immigration scheme "had the effect of precluding judicial intervention in deportation cases *except insofar as it was required by the Constitution*," 345 U.S., at 234-235, 73 S.Ct. 603 (emphasis added)—and that scheme, as discussed below, did allow for review on habeas of questions of law concerning an alien's eligibility for discretionary relief. Therefore, while the INS' historical arguments are not insubstantial, the ambiguities in the scope of the exercise of the writ at common law identified by St. Cyr, and the suggestions in this Court's prior decisions as to the extent to which habeas review could be limited consistent with the Constitution, convince us that the Suspension Clause questions that would be presented by the INS' reading of the immigration statutes before us are difficult and significant.^{FN24}

FN24. The dissent reads into Chief Justice

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

Marshall's opinion in *Ex parte Bollman*, 4 Cranch 75, 2 L.Ed. 554 (1807), support for a proposition that the Chief Justice did not endorse, either explicitly or implicitly. See *post*, at 2300-2301 (opinion of SCALIA, J.). He did note that "the first congress of the United States" acted under "the immediate influence" of the injunction provided by the Suspension Clause when it gave "life and activity" to "this great constitutional privilege" in the Judiciary Act of 1789, and that the writ could not be suspended until after the statute was enacted. 4 Cranch, at 95. That statement, however, surely does not imply that Marshall believed the Framers had drafted a Clause that would proscribe a temporary abrogation of the writ, while permitting its permanent suspension. Indeed, Marshall's comment expresses the far more sensible view that the Clause was intended to preclude any possibility that "the privilege itself would be lost" by either the inaction or the action of Congress. See, *e.g.*, *ibid.* (noting that the Founders "must have felt, with peculiar force, the obligation" imposed by the Suspension Clause).

****2282** In sum, even assuming that the Suspension Clause protects only the writ as it existed in 1789, there is substantial ***305** evidence to support the proposition that pure questions of law like the one raised by the respondent in this case could have been answered in 1789 by a common-law judge with power to issue the writ of habeas corpus. It necessarily follows that a serious Suspension Clause issue would be presented if we were to accept the INS' submission that the 1996 statutes have withdrawn that power from federal judges and provided no adequate substitute for its exercise. See Hart, *The Power of Congress to Limit the Jurisdiction of Federal Courts: An Exercise in Dialectic*, 66 Harv. L.Rev. 1362, 1395-1397 (1953). The necessity of resolving such a serious and difficult constitutional issue-and the desirability of avoiding that necessity-

simply reinforce the reasons for requiring a clear and unambiguous statement of congressional intent.

Moreover, to conclude that the writ is no longer available in this context would represent a departure from historical practice in immigration law. The writ of habeas corpus has always been available to review the legality of Executive detention. See *Felker*, 518 U.S., at 663, 116 S.Ct. 2333; *Swain v. Pressley*, 430 U.S., at 380, n. 13, 97 S.Ct. 1224; *id.*, at 385-386, 97 S.Ct. 1224 (Burger, C. J., concurring); *Brown v. Allen*, 344 U.S., at 533, 73 S.Ct. 397 (Jackson, J., concurring in result). Federal courts have been authorized to issue writs of habeas corpus since the enactment of the Judiciary Act of 1789, and § 2241 of the Judicial Code provides that federal judges may grant the writ of habeas corpus on the application of a prisoner held "in custody in violation of the Constitution or laws or treaties of the United States."^{FN25} 28 U.S.C. § 2241. Before and after the enactment in 1875 of the first statute regulating immigration, 18 Stat. 477, that jurisdiction was regularly invoked on behalf of noncitizens, particularly in the immigration context. See, *e.g.*, ***306***In re Kaine*, 14 How. 103, 14 L.Ed. 345 (1853); *United States v. Jung Ah Lung*, 124 U.S. 621, 626-632, 8 S.Ct. 663, 31 L.Ed. 591 (1888).

FN25. In fact, § 2241 descends directly from § 14 of the Judiciary Act of 1789 and the 1867 Act. See Act of Sept. 24, 1789, ch. 20, § 14, 1 Stat. 82; Act of Feb. 5, 1867, ch. 28, 14 Stat. 385. Its text remained undisturbed by either AEDPA or IIRIRA.

Until the enactment of the 1952 Immigration and Nationality Act, the sole means by which an alien could test the legality of his or her deportation order was by bringing a habeas corpus action in district court.^{FN26} See, *e.g.*, *United States v. Jung Ah Lung*, 124 U.S. 621, 8 S.Ct. 663, 31 L.Ed. 591 (1888); *Heikkila*, 345 U.S., at 235, 73 S.Ct. 603; *Chin Yow v. United States*, 208 U.S. 8, 28 S.Ct. 201, 52 L.Ed. 369 (1908); *Ng Fung Ho v. White*, 259 U.S. 276, 284, 42 S.Ct. 492, 66 L.Ed. 938

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

(1922). In such cases, other than the question whether there was some evidence to support the order,^{FN27} the courts generally did not review factual determinations made by the Executive. See *Ekiu v. United States*, 142 U.S. 651, 659, 12 S.Ct. 336, 35 L.Ed. 1146 (1892). However, they did review the Executive's legal determinations. See *Gegiow v. Uhl*, 239 U.S. 3, 9, 36 S.Ct. 2, 60 L.Ed. 114 (1915) ("The statute by enumerating the conditions upon which the allowance to land may be denied, prohibits the denial in other cases. And when the record shows that a commissioner of immigration is exceeding his power, the **2283 alien may demand his release upon *habeas corpus*"); see also Neuman, *Jurisdiction and the Rule of Law after the 1996 Immigration Act*, 113 Harv. L.Rev.1963, 1965-1969 (2000).^{FN28} In case after case, courts answered questions of law in habeas*307 corpus proceedings brought by aliens challenging Executive interpretations of the immigration laws.^{FN29}

FN26. After 1952, judicial review of deportation orders could also be obtained by declaratory judgment actions brought in federal district court. *Shaughnessy v. Pedreiro*, 349 U.S. 48, 75 S.Ct. 591, 99 L.Ed. 868 (1955). However, in 1961, Congress acted to consolidate review in the courts of appeals. See *Foti v. INS*, 375 U.S. 217, 84 S.Ct. 306, 11 L.Ed.2d 281 (1963).

FN27. See, e.g., *United States ex rel. Vajtauer v. Commissioner of Immigration*, 273 U.S. 103, 106, 47 S.Ct. 302, 71 L.Ed. 560 (1927) (holding that deportation "on charges unsupported by any evidence is a denial of due process which may be corrected on *habeas corpus*").

FN28. "And when the record shows that a commissioner of immigration is exceeding his power, the alien may demand his release upon *habeas corpus*. The conclusiveness of the decisions of immigration officers under § 25 is conclusiveness upon matters of fact. This was implied in

Nishimura Ekiu v. United States, 142 U.S. 651, 12 S.Ct. 336, 35 L.Ed. 1146, relied on by the Government." *Gegiow v. Uhl*, 239 U.S. 3, 9, 36 S.Ct. 2, 60 L.Ed. 114 (1915).

FN29. See, e.g., *Delgadillo v. Carmichael*, 332 U.S. 388, 391, 68 S.Ct. 10, 92 L.Ed. 17 (1947) (rejecting on habeas the Government's interpretation of the statutory term "entry"); *Bridges v. Wixon*, 326 U.S. 135, 149, 65 S.Ct. 1443, 89 L.Ed. 2103 (1945) (rejecting on habeas the Government's interpretation of the term "affiliation" with the Communist Party); *Kessler v. Strecker*, 307 U.S. 22, 35, 59 S.Ct. 694, 83 L.Ed. 1082 (1939) (holding that "as the Secretary erred in the construction of the statute, the writ must be granted"). Cf. *Mahler v. Eby*, 264 U.S. 32, 46, 44 S.Ct. 283, 68 L.Ed. 549 (1924) (reviewing on habeas the question whether the absence of an explicit factual finding that the aliens were "undesirable" invalidated the warrant of deportation).

Habeas courts also regularly answered questions of law that arose in the context of discretionary relief. See, e.g., *United States ex rel. Accardi v. Shaughnessy*, 347 U.S. 260, 74 S.Ct. 499, 98 L.Ed. 681 (1954); *United States ex rel. Hintopoulos v. Shaughnessy*, 353 U.S. 72, 77, 77 S.Ct. 618, 1 L.Ed.2d 652 (1957).^{FN30} Traditionally, courts recognized a distinction between eligibility for discretionary relief, on the one hand, and the favorable exercise of discretion, on the other hand. See Neuman, 113 Harv. L.Rev., at 1991 (noting the "strong tradition in habeas corpus law ... that subjects the legally erroneous failure to exercise discretion, unlike a substantively unwise exercise of discretion, to inquiry on the writ"). Eligibility that was "governed by specific*308 statutory standards" provided "a right to a ruling on an applicant's eligibility," even though the actual granting of relief was "not a matter of right under any circumstances, but rather is in all cases a matter of grace." *Jay v.*

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

Boyd, 351 U.S. 345, 353-354, 76 S.Ct. 919, 100 L.Ed. 1242 (1956). Thus, even though the actual suspension of deportation authorized by § 19(c) of the Immigration Act of 1917 was a matter of grace, in *United States ex rel. Accardi v. Shaughnessy*, 347 U.S. 260, 74 S.Ct. 499, 98 L.Ed. 681 (1954), we held that a deportable alien had a right to challenge the Executive's failure to exercise the discretion authorized by the law. The exercise of the District Court's habeas corpus jurisdiction to answer a pure question of law in this case is entirely consistent with the exercise of such jurisdiction in *Accardi*. See also *United States ex rel. Hintopoulos v. Shaughnessy*, 353 U.S., at 77, 77 S.Ct. 618.

FN30. Indeed, under the pre-1952 regime which provided only what *Heikkila* termed the constitutional minimum of review, on habeas lower federal courts routinely reviewed decisions under the Seventh Proviso, the statutory predecessor to § 212(c), to ensure the lawful exercise of discretion. See, e.g., *United States ex rel. Devenuto v. Curran*, 299 F. 206 (C.A.2 1924); *Hee Fuk Yuen v. White*, 273 F. 10 (C.A.9 1921); *United States ex rel. Patti v. Curran*, 22 F.2d 314 (S.D.N.Y.1926); *Gabriel v. Johnson*, 29 F.2d 347 (C.A.1 1928). During the same period, habeas was also used to review legal questions that arose in the context of the Government's exercise of other forms of discretionary relief under the 1917 Act. See, e.g., *United States ex rel. Adel v. Shaughnessy*, 183 F.2d 371 (C.A.2 1950); *United States ex rel. Kaloudis v. Shaughnessy*, 180 F.2d 489 (C.A.2 1950); *Mastrapasqua v. Shaughnessy*, 180 F.2d 999 (C.A.2 1950); *United States ex rel. De Sousa v. Day*, 22 F.2d 472 (C.A.2 1927); *Gonzalez-Martinez v. Landon*, 203 F.2d 196 (C.A.9 1953); *United States ex rel. Berman v. Curran*, 13 F.2d 96 (C.A.3 1926).

Thus, under the pre-1996 statutory scheme-and

consistent with its common-law antecedents-it is clear that St. Cyr **2284 could have brought his challenge to the BIA's legal determination in a habeas corpus petition under 28 U.S.C. § 2241. The INS argues, however, that AEDPA and IIRIRA contain four provisions that express a clear and unambiguous statement of Congress' intent to bar petitions brought under § 2241, despite the fact that none of them mention that section. The first of those provisions is AEDPA's § 401(e).

[8] While the title of § 401(e)-"ELIMINATION OF CUSTODY REVIEW BY HABEAS CORPUS"-would seem to support the INS' submission, the actual text of that provision does not.^{FN31} As we have previously noted, a title alone is not controlling. *309 *Pennsylvania Dept. of Corrections v. Yeskey*, 524 U.S. 206, 212, 118 S.Ct. 1952, 141 L.Ed.2d 215 (1998) (" '[T]he title of a statute ... cannot limit the plain meaning of the text. For interpretive purposes, [it is] of use only when [it] shed[s] light on some ambiguous word or phrase' " (quoting *Trainmen v. Baltimore & Ohio R. Co.*, 331 U.S. 519, 528-529, 67 S.Ct. 1387, 91 L.Ed. 1646 (1947))). The actual text of § 401(e), unlike its title, merely repeals a subsection of the 1961 statute amending the judicial review provisions of the 1952 Immigration and Nationality Act. See n. 31, *supra*. Neither the title nor the text makes any mention of 28 U.S.C. § 2241.

FN31. The section reads as follows:

"(e) ELIMINATION OF CUSTODY REVIEW BY HABEAS CORPUS.-Section 106(a) of the Immigration and Nationality Act (8 U.S.C. 1105a(a)) is amended-

"(1) in paragraph (8), by adding 'and' at the end;

"(2) in paragraph (9), by striking; 'and' at the end and inserting a period; and

"(3) by striking paragraph (10)." 110

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

Stat. 1268.

Under the 1952 Act, district courts had broad authority to grant declaratory and injunctive relief in immigration cases, including orders adjudicating deportability and those denying suspensions of deportability. See *Foti v. INS*, 375 U.S. 217, 225-226, 84 S.Ct. 306, 11 L.Ed.2d 281 (1963). The 1961 Act withdrew that jurisdiction from the district courts and provided that the procedures set forth in the Hobbs Act would be the “sole and exclusive procedure” for judicial review of final orders of deportation, subject to a series of exceptions. See 75 Stat. 651. The last of those exceptions stated that “any alien held in custody pursuant to an order of deportation may obtain review thereof by habeas corpus proceedings.” See *id.*, at 652, codified at 8 U.S.C. § 1105a(10) (repealed Sept. 30, 1996).

The INS argues that the inclusion of that exception in the 1961 Act indicates that Congress must have believed that it would otherwise have withdrawn the pre-existing habeas corpus jurisdiction in deportation cases, and that, as a result, the repeal of that exception in AEDPA in 1996 implicitly achieved that result. It seems to us, however, that the 1961 exception is best explained as merely confirming the limited scope of the new review procedures. In fact, the 1961 House Report provides that this section “in no way disturbs the Habeas Corpus Act.”^{FN32} H.R.Rep. No. 1086, 87th Cong., 1st *310 Sess., 29 (1961). Moreover, a number of the courts that considered the interplay between the general habeas provision and INA § 106(a)(10) after the 1961 Act and before the enactment of AEDPA did not read the 1961 Act’s specific habeas provision as supplanting jurisdiction under § 2241. **2285 *Orozco v. INS*, 911 F.2d 539, 541 (C.A.11 1990); *United States ex rel. Marcello v. INS*, 634 F.2d 964, 967 (C.A.5 1981); *Sotelo Mondragon v. Ilchert*, 653 F.2d 1254, 1255 (C.A.9 1980).

FN32. Moreover, the focus of the 1961 amendments appears to have been the elimination of Administrative Procedure

Act (APA) suits that were brought in the district court and that sought declaratory relief. See, e.g., H.R. No. 2478, 85th Cong., 2d Sess., 9 (1958) (“[H]abeas corpus is a far more expeditious judicial remedy than that of declaratory judgment”); 104 Cong. Rec. 17173 (1958) (statement of Rep. Walter) (stating that courts would be “relieved of a great burden” once declaratory actions were eliminated and noting that habeas corpus was an “expeditious” means of review).

In any case, whether § 106(a)(10) served as an independent grant of habeas jurisdiction or simply as an acknowledgment of continued jurisdiction pursuant to § 2241, its repeal cannot be sufficient to eliminate what it did not originally grant—namely, habeas jurisdiction pursuant to 28 U.S.C. § 2241.^{FN33} See *Ex parte Yerger*, 8 Wall., at 105-106 (concluding that the repeal of “an additional grant of jurisdiction” does not “operate as a repeal of jurisdiction theretofore allowed”); *Ex parte McCardle*, 7 Wall. 506, 515, 19 L.Ed. 264 (1869) (concluding that the repeal of portions of the 1867 statute conferring appellate jurisdiction on the Supreme Court in habeas proceedings did “not affect the jurisdiction which was previously exercised”).

FN33. As the INS acknowledges, the overwhelming majority of Courts of Appeals concluded that district courts retained habeas jurisdiction under § 2241 after AEDPA. See *Goncalves v. Reno*, 144 F.3d 110 (C.A.1 1998); *Henderson v. INS*, 157 F.3d 106 (C.A.2 1998); *Sandoval v. Reno*, 166 F.3d 225 (C.A.3 1999); *Bowrin v. INS*, 194 F.3d 483 (C.A.4 1999); *Requena-Rodriguez v. Pasquarell*, 190 F.3d 299 (C.A.5 1999); *Pak v. Reno*, 196 F.3d 666 (C.A.6 1999); *Shah v. Reno*, 184 F.3d 719 (C.A.8 1999); *Magana-Pizano v. INS*, 200 F.3d 603 (C.A.9 1999); *Jurado-Gutierrez v. Greene*, 190 F.3d 1135 (C.A.10 1999); *Mayers v. INS*, 175 F.3d 1289 (C.A.11

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

1999). But see *LaGuerre v. Reno*, 164 F.3d 1035 (C.A.7 1998).

[9] The INS also relies on three provisions of IIRIRA, now codified at 8 U.S.C. §§ 1252(a)(1), 1252(a)(2)(C), and *311 1252(b)(9) (1994 ed., Supp. V). As amended by § 306 of IIRIRA, 8 U.S.C. § 1252(a)(1) (1994 ed., Supp. V) now provides that, with certain exceptions, including those set out in subsection (b) of the same statutory provision, “[j]udicial review of a final order of removal ... is governed only by” the Hobbs Act’s procedures for review of agency orders in the courts of appeals. Similarly, § 1252(b)(9), which addresses the “[c]onsolidation of questions for judicial review,” provides that “[j]udicial review of all questions of law and fact, including interpretation and application of constitutional and statutory provisions, arising from any action taken or proceeding brought to remove an alien from the United States under this subchapter shall be available only in judicial review of a final order under this section.”^{FN34} Finally, § 1252(a)(2)(C), which concerns “[m]atters not subject to judicial review,” states: “Notwithstanding any other provision of law, no court shall have jurisdiction to review any final order of removal against an alien who is removable by reason of having committed” certain enumerated criminal offenses.

FN34. Title 8 U.S.C. § 1252(g) (1994 ed., Supp. V), entitled “Exclusive jurisdiction,” is not relevant to our analysis of the jurisdictional issue. In *Reno v. American-Arab Anti-Discrimination Comm.*, 525 U.S. 471, 119 S.Ct. 936, 142 L.Ed.2d 940 (1999) (*AADC*), we explained that that provision applied only to three types of discretionary decisions by the Attorney General—specifically, to commence proceedings, to adjudicate cases, or to execute removal orders—none of which are at issue here.

The term “judicial review” or “jurisdiction to review” is the focus of each of these three provisions. In the immigration context, “judicial review”

and “habeas corpus” have historically distinct meanings. See *Heikkila v. Barber*, 345 U.S. 229, 73 S.Ct. 603, 97 L.Ed. 972 (1953). In *Heikkila*, the Court concluded that the finality provisions at issue “preclud[ed] judicial review” to the maximum extent possible under the Constitution, and thus concluded that the APA was inapplicable. *Id.*, at 235, 73 S.Ct. 603. Nevertheless, the Court reaffirmed the right to habeas *312 corpus. *Ibid.* Noting that the limited role played by the courts in habeas corpus proceedings was far narrower than the judicial review authorized by the APA, the Court concluded that “it is the scope of inquiry on habeas corpus that differentiates” habeas review from “judicial review.” *Id.*, at 236, 73 S.Ct. 603; see also, e.g., **2286 *Terlinden v. Ames*, 184 U.S. 270, 278, 22 S.Ct. 484, 46 L.Ed. 534 (1902) (noting that under the extradition statute then in effect there was “no right of review to be exercised by any court or judicial officer,” but that limited review on habeas was nevertheless available); *Ekiu*, 142 U.S., at 663, 12 S.Ct. 336 (observing that while a decision to exclude an alien was subject to inquiry on habeas, it could not be “impeached or reviewed”). Both §§ 1252(a)(1) and (a)(2)(C) speak of “judicial review”—that is, full, nonhabeas review. Neither explicitly mentions habeas,^{FN35} or 28 U.S.C. § 2241.^{FN36} Accordingly, neither provision*313 speaks with sufficient clarity to bar jurisdiction pursuant to the general habeas statute.

FN35. Contrary to the dissent, see *post*, at 2295 (opinion of SCALIA, J.), we do not think, given the longstanding distinction between “judicial review” and “habeas,” that § 1252(e)(2)’s mention of habeas in the subsection governing “[j]udicial review of orders under section 1225(b)(1)” is sufficient to establish that Congress intended to abrogate the historical distinction between two terms of art in the immigration context when enacting IIRIRA.

“[W]here Congress borrows terms of art in which are accumulated the legal tradi-

tion and meaning of centuries of practice, it presumably knows and adopts the cluster of ideas that were attached to each borrowed word in the body of learning from which it was taken and the meaning its use will convey to the judicial mind unless otherwise instructed. In such case, absence of contrary direction may be taken as satisfaction with widely accepted definitions, not as a departure from them.” *Morrisette v. United States*, 342 U.S. 246, 263, 72 S.Ct. 240, 96 L.Ed. 288 (1952).

At most, § 1252(e)(2) introduces additional statutory ambiguity, but ambiguity does not help the INS in this case. As we noted above, only the clearest statement of congressional intent will support the INS' position. See *supra*, at 2282.

FN36. It is worth noting that in enacting the provisions of AEDPA and IIRIRA that restricted or altered judicial review, Congress did refer specifically to several different sources of jurisdiction. See, e.g., § 381, 110 Stat. 3009-650 (adding to grant of jurisdiction under 8 U.S.C. § 1329 (1994 ed., Supp. V) a provision barring jurisdiction under that provision for suits against the United States or its officers or agents). Section 401(e), which eliminated supplemental habeas jurisdiction under the INA, expressly strikes paragraph 10 of § 106(a) of the INA, *not* 28 U.S.C. § 2241. Similarly, § 306 of IIRIRA, which enacted the new INA § 242, specifically precludes reliance on the provisions of the APA providing for the taking of additional evidence, and imposes specific limits on the availability of declaratory relief. See, e.g., 8 U.S.C. § 1535(e)(2) (1994 ed., Supp. V) (explicitly barring aliens detained under “alien terrorist removal” procedures from seeking “judicial review, including applic-

ation for a writ of habeas corpus, except for a claim by the alien that continued detention violates the alien's rights under the Constitution”). At no point, however, does IIRIRA make express reference to § 2241. Given the historic use of § 2241 jurisdiction as a means of reviewing deportation and exclusion orders, Congress' failure to refer specifically to § 2241 is particularly significant. Cf. *Chisom v. Roemer*, 501 U.S. 380, 396, n. 23, 111 S.Ct. 2354, 115 L.Ed.2d 348 (1991).

The INS also makes a separate argument based on 8 U.S.C. § 1252(b)(9) (1994 ed., Supp. V). We have previously described § 1252(b)(9) as a “zipper clause.” *AADC*, 525 U.S. 471, 483, 119 S.Ct. 936, 142 L.Ed.2d 940 (1999). Its purpose is to consolidate “judicial review” of immigration proceedings into one action in the court of appeals, but it applies only “[w]ith respect to review of an order of removal under subsection (a)(1).” 8 U.S.C. § 1252(b) (1994 ed., Supp. V).^{FN37} Accordingly, this provision, by its own terms, does not bar habeas jurisdiction over removal orders *not* subject to judicial review under § 1252(a)(1)-including orders against aliens who are removable by reason of having committed one or more criminal offenses. Subsection (b)(9) simply provides for the consolidation of issues to be brought in petitions for “[j]udicial review,”^{**2287} which, as we note above, is a term historically distinct^{*314} from habeas. See *Mahadeo v. Reno*, 226 F.3d 3, 12 (C.A.1 2000); *Flores-Miramontes v. INS*, 212 F.3d 1133, 1140 (C.A.9 2000). It follows that § 1252(b)(9) does not clearly apply to actions brought pursuant to the general habeas statute, and thus cannot repeal that statute either in part or in whole.

FN37. As we noted in *AADC*, courts construed the 1961 amendments as channeling review of final orders to the courts of appeals, but still permitting district courts to exercise their traditional jurisdiction over claims that were viewed as being outside

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
 (Cite as: 533 U.S. 289, 121 S.Ct. 2271)

of a “final order.” 525 U.S., at 485, 119 S.Ct. 936. Read in light of this history, § 1252(b)(9) ensures that review of those types of claims will now be consolidated in a petition for review and considered by the courts of appeals.

If it were clear that the question of law could be answered in another judicial forum, it might be permissible to accept the INS' reading of § 1252. But the absence of such a forum, coupled with the lack of a clear, unambiguous, and express statement of congressional intent to preclude judicial consideration on habeas of such an important question of law, strongly counsels against adopting a construction that would raise serious constitutional questions.^{FN38} Cf. *Felker*, 518 U.S., at 660-661, 116 S.Ct. 2333. Accordingly, we conclude that habeas jurisdiction under § 2241 was not repealed by AE-DPA and IIRIRA.

FN38. The dissent argues that our decision will afford more rights to criminal aliens than to noncriminal aliens. However, as we have noted, the scope of review on habeas is considerably more limited than on APA-style review. Moreover, this case raises only a pure question of law as to respondent's statutory eligibility for discretionary relief, not, as the dissent suggests, an objection to the manner in which discretion was exercised. As to the question of timing and congruent means of review, we note that Congress could, without raising any constitutional questions, provide an adequate substitute through the courts of appeals. See, e.g., *Swain v. Pressley*, 430 U.S. 372, 381, 97 S.Ct. 1224, 51 L.Ed.2d 411 (1977) (“[T]he substitution of a collateral remedy which is neither inadequate nor ineffective to test the legality of a person's detention” does not violate the Suspension Clause).

III

[10] The absence of a clearly expressed state-

ment of congressional intent also pervades our review of the merits of St. Cyr's claim. Two important legal consequences ensued from respondent's entry of a guilty plea in March 1996: (1) He became subject to deportation, and (2) he became eligible for a discretionary waiver of that deportation under the prevailing^{*315} interpretation of § 212(c). When IIRIRA went into effect in April 1997, the first consequence was unchanged except for the fact that the term “removal” was substituted for “deportation.” The issue that remains to be resolved is whether IIRIRA § 304(b) changed the second consequence by eliminating respondent's eligibility for a waiver.

The INS submits that the statute resolves the issue because it unambiguously communicates Congress' intent to apply the provisions of IIRIRA's Title III-A to all removals initiated after the effective date of the statute, and, in any event, its provisions only operate prospectively and not retrospectively. The Court of Appeals, relying primarily on the analysis in our opinion in *Landgraf v. USI Film Products*, 511 U.S. 244, 114 S.Ct. 1483, 128 L.Ed.2d 229 (1994), held, contrary to the INS' arguments, that Congress' intentions concerning the application of the “Cancellation of Removal” procedure are ambiguous and that the statute imposes an impermissible retroactive effect on aliens who, in reliance on the possibility of § 212(c) relief, pleaded guilty to aggravated felonies. See 229 F.3d, at 416, 420. We agree.

[11] Retroactive statutes raise special concerns. See *Landgraf*, 511 U.S., at 266, 114 S.Ct. 1483. “The Legislature's unmatched powers allow it to sweep away settled expectations suddenly and without individualized consideration. Its responsiveness to political pressures poses a risk that it may be tempted to use retroactive legislation as a means of retribution against unpopular groups or individuals.”^{FN39} ****2288** *Ibid.* Accordingly, “congressional enactments ... will not be construed to have retroactive effect unless their language requires this ^{*316} result.” *Bowen v. Georgetown Univ. Hospital*, 488 U.S. 204, 208, 109 S.Ct. 468,

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

102 L.Ed.2d 493 (1988).

FN39. The INS appears skeptical of the notion that immigrants might be considered an “unpopular group.” See Brief for Petitioner 15, n. 8. But see Legomsky, Fear and Loathing in Congress and the Courts: Immigration and Judicial Review, 78 Texas L.Rev. 1615, 1626 (2000) (observing that, because noncitizens cannot vote, they are particularly vulnerable to adverse legislation).

“[This] presumption against retroactive legislation is deeply rooted in our jurisprudence, and embodies a legal doctrine centuries older than our Republic. Elementary considerations of fairness dictate that individuals should have an opportunity to know what the law is and to conform their conduct accordingly; settled expectations should not be lightly disrupted. For that reason, the ‘principle that the legal effect of conduct should ordinarily be assessed under the law that existed when the conduct took place has timeless and universal human appeal.’ *Kaiser*, 494 U.S., at 855, 110 S.Ct. 1570 (SCALIA, J., concurring). In a free, dynamic society, creativity in both commercial and artistic endeavors is fostered by a rule of law that gives people confidence about the legal consequences of their actions.” *Landgraf*, 511 U.S., at 265-266, 114 S.Ct. 1483 (footnote omitted).

[12][13][14] Despite the dangers inherent in retroactive legislation, it is beyond dispute that, within constitutional limits, Congress has the power to enact laws with retrospective effect. See *id.*, at 268, 109 S.Ct. 468. A statute may not be applied retroactively, however, absent a clear indication from Congress that it intended such a result. “Requiring clear intent assures that Congress itself has affirmatively considered the potential unfairness of retroactive application and determined that it is an acceptable price to pay for the countervailing benefits.” *Id.*, at 272-273, 109 S.Ct. 468. Accordingly, the first step in determining whether a

statute has an impermissible retroactive effect is to ascertain whether Congress has directed with the requisite clarity that the law be applied retrospectively. *Martin v. Hadix*, 527 U.S. 343, 352, 119 S.Ct. 1998, 144 L.Ed.2d 347 (1999).

The standard for finding such unambiguous direction is a demanding one. “[C]ases where this Court has found truly ‘retroactive’ effect adequately authorized by statute have *317 involved statutory language that was so clear that it could sustain only one interpretation.” *Lindh v. Murphy*, 521 U.S. 320, 328, n. 4, 117 S.Ct. 2059, 138 L.Ed.2d 481 (1997). The INS makes several arguments in favor of its position that IIRIRA achieves this high level of clarity.

First, the INS points to the comprehensive nature of IIRIRA's revision of federal immigration law. “Congress's comprehensive establishment of a new immigration framework,” the INS argues, “shows its intent that, after a transition period, the provisions of the old law should no longer be applied at all.” Brief for Petitioner 33-34. We rejected a similar argument, however, in *Landgraf*, a case that, like this one, involved Congress' comprehensive revision of an important federal statute. 511 U.S., at 260-261, 114 S.Ct. 1483. By itself, the comprehensiveness of a congressional enactment says nothing about Congress' intentions with respect to the retroactivity of the enactment's individual provisions.^{FN40}

FN40. The INS' argument that refusing to apply § 304(b) retroactively creates an unrecognizable hybrid of old and new is, for the same reason, unconvincing.

The INS also points to the effective date for Title III-A as providing a clear statement of congressional intent to apply IIRIRA's repeal of § 212(c) retroactively. See IIRIRA § 309(a), 110 Stat. 3009-625. But the mere promulgation of an effective date for a statute does not provide sufficient assurance that Congress specifically considered the potential unfairness that retroactive application

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

would produce. For that reason, a “statement that a statute will become effective on a certain date does not even arguably suggest that it has any application to conduct that occurred at **2289 an earlier date.” *Landgraf*, 511 U.S., at 257, 114 S.Ct. 1483.

The INS further argues that any ambiguity in Congress' intent is wiped away by the “saving provision” in IIRIRA § 309(c)(1), 110 Stat. 3009-625. Brief for Petitioner 34-36. That provision states that, for aliens whose exclusion or deportation proceedings began prior to the Title III-A effective *318 date, “the amendments made by [Title III-A] shall not apply, and ... the proceedings (including judicial review thereof) shall continue to be conducted without regard to such amendments.” FN41 This rule, however, does not communicate with unmistakable clarity Congress' intention to apply its repeal of § 212(c) retroactively. Nothing in either § 309(c)(1) or the statute's legislative history even discusses the effect of the statute on proceedings based on pre-IIRIRA convictions that are commenced *after* its effective date. FN42 Section 309(c)(1) is best read as merely setting out the *procedural* rules to be applied to removal proceedings pending on the effective date of the statute. Because “[c]hanges in procedural rules may often be applied in suits arising before their enactment without raising concerns about retroactivity,” *Landgraf*, 511 U.S., at 275, 114 S.Ct. 1483, it was necessary for Congress to identify which set of procedures would apply in those circumstances. As the Conference Report expressly explained, “[§ 309(c)] provides for the transition to new *procedures* in the case of an alien already in exclusion or deportation proceedings on the effective date.” H.R. Conf. Rep. No. 104-828, p. 222 (1996) (emphasis added).

FN41. “(c) TRANSITION FOR ALIENS IN PROCEEDINGS.-

“(1) GENERAL RULE THAT NEW RULES DO NOT APPLY.-Subject to the succeeding provisions of this subsection, in the case of an alien who is in exclusion or deportation proceedings as of

the title III-A effective date-

“(A) the amendments made by this subtitle shall not apply, and

“(B) the proceedings (including judicial review thereof) shall continue to be conducted without regard to such amendments.” § 309, 110 Stat. 3009-625.

FN42. The INS' reliance, see Reply Brief for Petitioner 12, on *INS v. Aguirre-Aguirre*, 526 U.S. 415, 420, 119 S.Ct. 1439, 143 L.Ed.2d 590 (1999), is beside the point because that decision simply observed that the new rules would not apply to a proceeding filed *before* IIRIRA's effective date.

Another reason for declining to accept the INS' invitation to read § 309(c)(1) as dictating the temporal reach of IIRIRA § 304(b) is provided by Congress' willingness, in other sections of IIRIRA, to indicate unambiguously its intention *319 to apply specific provisions retroactively. IIRIRA's amendment of the definition of “aggravated felony,” for example, clearly states that it applies with respect to “conviction[s] ... entered before, on, or after” the statute's enactment date. § 321(b). FN43 As the Court of Appeals noted, **2290 the fact that Congress*320 made some provisions of IIRIRA expressly applicable to prior convictions, but did not do so in regard to § 304(b), is an indication “that Congress did not definitively decide the issue of § 304's retroactive application to pre-enactment convictions.” See 229 F.3d, at 415. The “saving provision” is therefore no more significant than the specification of an effective date.

FN43. See also IIRIRA § 321(c) (“The amendments made by this section shall apply to actions taken on or after the date of the enactment of this Act, regardless of when the conviction occurred ...”); § 322(c) (“The amendments made by subsection (a) shall apply to convictions and sen-

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

tences entered before, on, or after the date of the enactment of this Act”); § 342(b) (the amendment adding incitement of terrorist activity as a ground for exclusion “shall apply to incitement regardless of when it occurs”); § 344(c) (the amendment adding false claims of U.S. citizenship as ground for removal “shall apply to representations made on or after the date” of enactment); § 347(c) (amendments rendering alien excludable or deportable any alien who votes unlawfully “shall apply to voting occurring before, on, or after the date” of enactment); § 348(b) (amendment providing for automatic denial of discretionary waiver from exclusion “shall be effective on the date of the enactment ... and shall apply in the case of any alien who is in exclusion or deportation proceedings as of such date unless a final administrative order in such proceedings has been entered as of such date”); § 350(b) (amendment adding domestic violence and stalking as grounds for deportation “shall apply to convictions, or violations of court orders, occurring after the date” of enactment); § 351(c) (discussing deportation for smuggling and providing that amendments “shall apply to applications for waivers filed before, on, or after the date” of enactment); § 352(b) (amendments adding renunciation of citizenship to avoid taxation as a ground for exclusion “shall apply to individuals who renounce United States citizenship on and after the date” of enactment); § 380(c) (amendment imposing civil penalties on aliens for failure to depart “shall apply to actions occurring on or after” effective date); § 384(d)(2) (amendments adding penalties for disclosure of information shall apply to “offenses occurring on or after the date” of enactment); § 531(b) (public charge considerations as a ground for exclusion “shall apply to applications submitted on or after such

date”); § 604(c) (new asylum provision “shall apply to applications for asylum filed on or after the first day of the first month beginning more than 180 days after the date” of enactment). The INS argues that the Title III-B amendments containing such express temporal provisions are unrelated to the subject matter of § 304(b). Brief for Petitioner 37-38. But it is clear that provisions such as IIRIRA § 321(b), which addresses IIRIRA's redefinition of “aggravated felony,” deal with subjects quite closely related to § 304(b)'s elimination of § 212(c) relief for aliens convicted of aggravated felonies.

The presumption against retroactive application of ambiguous statutory provisions, buttressed by “the longstanding principle of construing any lingering ambiguities in deportation statutes in favor of the alien,” *INS v. Cardoza-Fonseca*, 480 U.S. 421, 449, 107 S.Ct. 1207, 94 L.Ed.2d 434 (1987), forecloses the conclusion that, in enacting § 304(b), “Congress itself has affirmatively considered the potential unfairness of retroactive application and determined that it is an acceptable price to pay for the countervailing benefits.”^{FN44} *Landgraf*, 511 U.S., at 272-273, 114 S.Ct. 1483. We therefore proceed to the second step of *Landgraf's* retroactivity analysis in order to determine whether depriving removable aliens of consideration for § 212(c) relief produces an impermissible retroactive effect for aliens who, like respondent, were convicted pursuant to a plea agreement at a time when their plea would not have rendered them ineligible for § 212(c) relief.^{FN45}

FN44. The legislative history is significant because, despite its comprehensive character, it contains no evidence that Congress specifically considered the question of the applicability of IIRIRA § 304(b) to pre-IIRIRA convictions. Cf. *Harrison v. PPG Industries, Inc.*, 446 U.S. 578, 602, 100 S.Ct. 1889, 64 L.Ed.2d 525 (1980)

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473

(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

(REHNQUIST, J., dissenting) (“ ‘In a case where the construction of legislative language such as this makes so sweeping and so relatively unorthodox a change as that made here, I think judges as well as detectives may take into consideration the fact that a watchdog did not bark in the night’ ”), cited in *Chisom v. Roemer*, 501 U.S., at 396, n. 23, 111 S.Ct. 2354 (citing A. Doyle, *Silver Blaze*, in *The Complete Sherlock Holmes* 335 (1927)).

FN45. The INS argues that we should extend deference under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984), to the BIA's interpretation of IIRIRA as applying to all deportation proceedings initiated after IIRIRA's effective date. We only defer, however, to agency interpretations of statutes that, applying the normal “tools of statutory construction,” are ambiguous. *Id.*, at 843, n. 9, 104 S.Ct. 2778; *INS v. Cardoza-Fonseca*, 480 U.S., at 447-448, 107 S.Ct. 1207. Because a statute that is ambiguous with respect to retroactive application is construed under our precedent to be unambiguously prospective, *Landgraf*, 511 U.S., at 264, 114 S.Ct. 1483, there is, for *Chevron* purposes, no ambiguity in such a statute for an agency to resolve.

[15][16][17] *321 “The inquiry into whether a statute operates retroactively demands a common-sense, functional judgment about ‘whether the new provision attaches new legal consequences to events completed before its enactment.’ ” *Martin*, 527 U.S., at 357-358, 119 S.Ct. 1998 (quoting *Landgraf*, 511 U.S., at 270, 114 S.Ct. 1483). A statute has retroactive effect when it “ ‘takes away or impairs vested rights acquired under existing laws, or creates a new obligation, imposes a new duty, or attaches a new disability, in respect to transactions or **2291 considerations already past...’ ” FN46

Id., at 269, 114 S.Ct. 1522 (quoting *Society for Propagation of the Gospel v. Wheeler*, 22 F.Cas. 756, 767, No. 13,156 (C.C.D.N.H. 1814) (Story, J.)). As we have repeatedly counseled, the judgment whether a particular statute acts retroactively “ ‘should be informed and guided by ‘familiar considerations of fair notice, reasonable reliance, and settled expectations.’ ” *Martin*, 527 U.S., at 358, 119 S.Ct. 1998 (quoting *Landgraf*, 511 U.S., at 270, 114 S.Ct. 1483).

FN46. As we noted in *Hughes Aircraft Co. v. United States ex rel. Schumer*, 520 U.S. 939, 117 S.Ct. 1871, 138 L.Ed.2d 135 (1997), this language by Justice Story “ ‘does not purport to define the outer limit of impermissible retroactivity.’ ” *Id.*, at 947, 117 S.Ct. 1871. Instead, it simply describes several “ ‘sufficient,’ ” as opposed to “ ‘necessary,’ ” conditions for finding retroactivity. *Ibid.*

IIRIRA's elimination of any possibility of § 212(c) relief for people who entered into plea agreements with the expectation that they would be eligible for such relief clearly “ ‘attaches a new disability, in respect to transactions or considerations already past.’ ” *Id.*, at 269, 114 S.Ct. 1483. Plea agreements involve a *quid pro quo* between a criminal defendant and the government. See *322 *Newton v. Rumery*, 480 U.S. 386, 393, n. 3, 107 S.Ct. 1187, 94 L.Ed.2d 405 (1987). In exchange for some perceived benefit, defendants waive several of their constitutional rights (including the right to a trial) and grant the government numerous “ ‘tangible benefits, such as promptly imposed punishment without the expenditure of prosecutorial resources.’ ” FN47 *Ibid.* There can be little doubt that, as a general matter, alien defendants considering whether to enter into a plea agreement are acutely aware of the immigration consequences of their convictions. FN48 See *Magana-Pizano v. INS*, 200 F.3d 603, 612 (C.A.9 1999) (“That an alien charged with a crime ... would factor the immigration consequences of conviction in deciding whether to

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
 (Cite as: 533 U.S. 289, 121 S.Ct. 2271)

plead or proceed to trial is well-documented”); see also 3 Bender, Criminal Defense Techniques §§ 60A.01, 60A.02[2] (1999) (“ ‘Preserving the client’s right to remain in the United States may be more important to the client than any potential jail sentence’ ” (quoted in Brief for National Association of Criminal Defense Lawyers*323 et al. as *Amici Curiae* 13)). Given the frequency with which § 212(c) relief was granted in the years leading up to AEDPA and IIRIRA,^{FN49} preserving the possibility of such relief would have been one of the principal benefits sought by defendants deciding whether to accept a plea offer or instead to proceed to trial.^{FN50}

FN47. “If every criminal charge were subjected to a full-scale trial, the States and the Federal Government would need to multiply by many times the number of judges and court facilities.” *Santobello v. New York*, 404 U.S. 257, 260, 92 S.Ct. 495, 30 L.Ed.2d 427 (1971).

FN48. Many States, including Connecticut, the State in which respondent pleaded guilty, require that trial judges advise defendants that immigration consequences may result from accepting a plea agreement. See Cal.Penal Code Ann. § 1016.5 (West 1985); Conn. Gen.Stat. § 54-1j (2001); D.C.Code Ann. § 16-713 (1981-1997); Fla. Rule Crim. Proc. 3.172(c)(8) (1999); Ga.Code Ann. § 17-7-93 (1997); Haw.Rev.Stat. § 802E-2 (1993); Md. Rule 4-242 (2001); Mass. Gen. Laws § 278:29D (1996 Supp.); Minn. Rule Crim. Proc. 15.01 (2000); Mont.Code Ann. § 46-12-210 (1997); N.M. Rule Crim. Proc. 9-406 (2001); N.Y.Crim. Proc. Law § 220.50(7) (McKinney 2001 Cum.Supp. Pamphlet); N.C. Gen.Stat. § 15A-1022 (1999); Ohio Rev.Code Ann. § 2943.031 (1997); Ore.Rev.Stat. § 135.385 (1997); R.I. Gen. Laws § 12-12-22 (2000); Tex.Code Crim. Proc. Ann., Art. 26.13

(a)(4) (Vernon 1989 and Supp.2001); Wash. Rev.Code § 10.40.200 (1990); Wis. Stat. § 971.08 (1993-1994). And the American Bar Association’s Standards for Criminal Justice provide that, if a defendant will face deportation as a result of a conviction, defense counsel “should fully advise the defendant of these consequences.” 3 ABA Standards for Criminal Justice 14-3.2 Comment, 75 (2d ed.1982).

FN49. See n. 5, *supra*.

FN50. Even if the defendant were not initially aware of § 212(c), competent defense counsel, following the advice of numerous practice guides, would have advised him concerning the provision’s importance. See Brief for National Association of Criminal Defense Lawyers et al. as *Amici Curiae* 6-8.

**2292 The case of Charles Jideonwo, a petitioner in a parallel litigation in the Seventh Circuit, is instructive. Charged in 1994 with violating federal narcotics law, Jideonwo entered into extensive plea negotiations with the Government, the sole purpose of which was to ensure that “ ‘he got less than five years to avoid what would have been a statutory bar on 212(c) relief.’ ” *Jideonwo v. INS*, 224 F.3d 692, 699 (C.A.7 2000) (quoting the Immigration Judge’s findings of fact). The potential for unfairness in the retroactive application of IIRIRA § 304(b) to people like Jideonwo and St. Cyr is significant and manifest. Relying upon settled practice, the advice of counsel, and perhaps even assurances in open court that the entry of the plea would not foreclose § 212(c) relief, a great number of defendants in Jideonwo’s and St. Cyr’s position agreed to plead guilty.^{FN51} Now that prosecutors have received the benefit of these plea agreements, agreements that were likely facilitated by the aliens’ belief in their continued eligibility for § 212(c) relief, it would surely be contrary to “familiar considerations of fair notice, reasonable reliance, and settled expectations,” *324 *Landgraf*, 511 U.S., at 270, 114

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
 (Cite as: 533 U.S. 289, 121 S.Ct. 2271)

S.Ct. 1483, to hold that IIRIRA's subsequent restrictions deprive them of any possibility of such relief.^{FN52}

FN51. Ninety percent of criminal convictions today are obtained by guilty plea. See U.S. Dept. of Justice, Office of Justice Programs, Bureau of Justice Statistics, Section 5: Judicial Processing of Defendants, in United States Sentencing Commission, 1999 Sourcebook of Criminal Justice Statistics (2000) Tables 5.30, 5.51.

FN52. The significance of that reliance is obvious to those who have participated in the exercise of the discretion that was previously available to delegates of the Attorney General under § 212(c). See *In re Soriano*, 16 BIA Immig. Rptr. B1-227, B1-238 to B1-239 (1996) (Rosenberg, Board Member, concurring and dissenting) (“I find compelling policy and practical reasons to go beyond such a limited interpretation as the one the majority proposes in this case. All of these people, and no doubt many others, had settled expectations to which they conformed their conduct”).

The INS argues that deportation proceedings (and the Attorney General's discretionary power to grant relief from deportation) are “inherently prospective” and that, as a result, application of the law of deportation can never have a retroactive effect. Such categorical arguments are not particularly helpful in undertaking *Landgraf's* common-sense, functional retroactivity analysis. See *Martin*, 527 U.S., at 359, 119 S.Ct. 1998. Moreover, although we have characterized deportation as “look[ing] prospectively to the respondent's right to remain in this country in the future,” *INS v. Lopez-Mendoza*, 468 U.S. 1032, 1038, 104 S.Ct. 3479, 82 L.Ed.2d 778 (1984), we have done so in order to reject the argument that deportation is punishment for past behavior and that deportation proceedings are therefore subject to the “various protections that apply in the context of a criminal trial.” *Ibid.* As our

cases make clear, the presumption against retroactivity applies far beyond the confines of the criminal law. See *Landgraf*, 511 U.S., at 272, 114 S.Ct. 1483. And our mere statement that deportation is not punishment for past crimes does not mean that we cannot consider an alien's reasonable reliance on the continued availability of discretionary relief from deportation when deciding whether the elimination of such relief has a retroactive effect.^{FN53}

FN53. We are equally unconvinced by the INS' comparison of the elimination of § 212(c) relief for people like St. Cyr with the Clayton Act's elimination of federal courts' power to enjoin peaceful labor actions. In *American Steel Foundries v. Tri-City Central Trades Council*, 257 U.S. 184, 42 S.Ct. 72, 66 L.Ed. 189 (1921), and *Duplex Printing Press Co. v. Deering*, 254 U.S. 443, 464, 41 S.Ct. 172, 65 L.Ed. 349 (1921), we applied the Clayton Act's limitations on injunctive relief to cases pending at the time of the statute's passage. But unlike the elimination of § 212(c) relief in this case, which depends upon an alien's decision to plead guilty to an “aggravated felony,” the deprivation of the District Court's power to grant injunctive relief at issue in *Duplex Printing* did not in any way result from or depend on the past action of the party seeking the injunction. Thus, it could not plausibly have been argued that the Clayton Act attached a “‘new disability, in respect to transactions or considerations already past.’” *Landgraf*, 511 U.S., at 269, 114 S.Ct. 1483.

****2293 *325** Finally, the fact that § 212(c) relief is discretionary does not affect the propriety of our conclusion. There is a clear difference, for the purposes of retroactivity analysis, between facing possible deportation and facing certain deportation. Cf. *Hughes Aircraft Co. v. United States ex rel. Schumer*, 520 U.S. 939, 949, 117 S.Ct. 1871, 138 L.Ed.2d 135 (1997) (an increased likelihood of fa-

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
 (Cite as: 533 U.S. 289, 121 S.Ct. 2271)

cing a *qui tam* action constitutes an impermissible retroactive effect for the defendant); *Lindsey v. Washington*, 301 U.S. 397, 401, 57 S.Ct. 797, 81 L.Ed. 1182 (1937) (“Removal of the possibility of a sentence of less than fifteen years ... operates to [defendants'] detriment” (emphasis added)). Prior to AEDPA and IIRIRA, aliens like St. Cyr had a significant likelihood of receiving § 212(c) relief.^{FN54} Because respondent, and other aliens like him, almost certainly relied upon that likelihood in deciding whether to forgo their right to a trial, the elimination of any possibility of § 212(c) relief by IIRIRA has an obvious and severe retroactive effect.^{FN55}

FN54. See n. 5, *supra*.

FN55. The INS cites several cases affirming Congress' power to retroactively unsettle such expectations in the immigration context. See Brief for Petitioner 40-41, and n. 21. But our recognition that Congress has the power to act retrospectively in the immigration context sheds no light on the question at issue at this stage of the *Landgraf* analysis: whether a particular statute in fact has such a retroactive effect. Moreover, our decision today is fully consistent with a recognition of Congress' power to act retrospectively. We simply assert, as we have consistently done in the past, that in legislating retroactively, Congress must make its intention plain.

Similarly, the fact that Congress has the power to alter the rights of resident aliens to remain in the United States is not determinative of the question whether a particular statute has a retroactive effect. See *Chew Heong v. United States*, 112 U.S. 536, 5 S.Ct. 255, 28 L.Ed. 770 (1884). Applying a statute barring Chinese nationals from reentering the country without a certificate prepared when they left to people who exited the country before the statute went into ef-

fect would have retroactively unsettled their reliance on the state of the law when they departed. See *id.*, at 559, 5 S.Ct. 255. So too, applying IIRIRA § 304(b) to aliens who pleaded guilty or *nolo contendere* to crimes on the understanding that, in so doing, they would retain the ability to seek discretionary § 212(c) relief would retroactively unsettle their reliance on the state of the law at the time of their plea agreement.

*326 We find nothing in IIRIRA unmistakably indicating that Congress considered the question whether to apply its repeal of § 212(c) retroactively to such aliens. We therefore hold that § 212(c) relief remains available for aliens, like respondent, whose convictions were obtained through plea agreements and who, notwithstanding those convictions, would have been eligible for § 212(c) relief at the time of their plea under the law then in effect.

The judgment is affirmed.

It is so ordered.

Justice O'CONNOR, dissenting.

I join Parts I and III of Justice SCALIA's dissenting opinion in this case. I do not join Part II because I believe that, assuming, *arguendo*, that the Suspension Clause guarantees some minimum extent of habeas review, the right asserted by the alien in this case falls outside the scope of that review for the reasons explained by Justice SCALIA in Part II-B of his dissenting opinion. The question whether the Suspension Clause assures habeas jurisdiction in this particular case properly is resolved on this ground alone, and there is no need to say more.

Justice SCALIA, with whom THE CHIEF JUSTICE and Justice THOMAS join, and with whom Justice O'CONNOR joins as to Parts I and III, dissenting.

The Court today finds ambiguity in the utterly clear language of a statute that forbids the district court (and all *327 other courts) to entertain the

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

claims of aliens **2294 such as respondent St. Cyr, who have been found deportable by reason of their criminal acts. It fabricates a superclear statement, “magic words” requirement for the congressional expression of such an intent, unjustified in law and unparalleled in any other area of our jurisprudence. And as the fruit of its labors, it brings forth a version of the statute that affords *criminal* aliens *more* opportunities for delay-inducing judicial review than are afforded to noncriminal aliens, or even than were afforded to criminal aliens prior to this legislation concededly designed to *expedite* their removal. Because it is clear that the law deprives us of jurisdiction to entertain this suit, I respectfully dissent.

I

In categorical terms that admit of no exception, the Illegal Immigration Reform and Immigrant Responsibility Act of 1996 (IIRIRA), 110 Stat. 3009-546, unambiguously repeals the application of 28 U.S.C. § 2241 (the general habeas corpus provision), and of all other provisions for judicial review, to deportation challenges brought by certain kinds of criminal aliens. This would have been readily apparent to the reader, had the Court at the outset of its opinion set forth the relevant provisions of IIRIRA and of its statutory predecessor, the Antiterrorism and Effective Death Penalty Act of 1996 (AEDPA), 110 Stat. 1214. I will begin by supplying that deficiency, and explaining IIRIRA's jurisdictional scheme. It begins with what we have called a channeling or “ ‘zipper’ clause,” *Reno v. American-Arab Anti-Discrimination Comm.*, 525 U.S. 471, 483, 119 S.Ct. 936, 142 L.Ed.2d 940 (1999)-namely, 8 U.S.C. § 1252(b)(9) (1994 ed., Supp. V). This provision, entitled “Consolidation of questions for judicial review,” provides as follows:

“Judicial review of *all* questions of law and fact, including interpretation and application of constitutional and statutory provisions, arising from *any action taken* *328 *or proceeding brought to remove an alien* from the United States under this subchapter shall be available *only* in judicial re-

view of a final order under this section.” (Emphases added.)

In other words, *if* any review is available of any “questio[n] of law ... arising from any action taken or proceeding brought to remove an alien from the United States under this subchapter,” it is available “only in judicial review of a final order under this section [§ 1252].” What kind of review does that section provide? That is set forth in § 1252(a)(1), which states:

“Judicial review of a final order of removal (other than an order of removal without a hearing pursuant to [the expedited-removal provisions for undocumented aliens arriving at the border found in] section 1225(b)(1) of this title) is governed only by chapter 158 of title 28 [the Hobbs Act], except as provided in subsection (b) of this section [which modifies some of the Hobbs Act provisions] and except that the court may not order the taking of additional evidence under section 2347(c) of [Title 28].”

In other words, *if* judicial review is available, it consists *only* of the modified Hobbs Act review specified in § 1252(a)(1).

In some cases (including, as it happens, the one before us), there can be no review at all, because IIRIRA categorically and unequivocally rules out judicial review of challenges to deportation brought by certain kinds of criminal aliens. Section 1252(a)(2)(C) provides:

“Notwithstanding *any* other provision of law, *no court* shall have jurisdiction to review *any* final order of removal against an alien who is removable by reason of having committed [one or more enumerated] criminal offense[s] [including drug-trafficking offenses of the sort of which respondent had been convicted].” (Emphases added.)

*329 Finally, the pre-IIRIRA antecedent to the foregoing provisions-AEDPA § 401(e)-and the statutory background **2295 against which that was enacted, confirm that § 2241 habeas review, in the

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

district court or elsewhere, has been unequivocally repealed. In 1961, Congress amended the Immigration and Nationality Act of 1952 (INA), 66 Stat. 163, by directing that the procedure for Hobbs Act review in the courts of appeals “shall apply to, and shall be the *sole and exclusive procedure for*, the judicial review of all final orders of deportation” under the INA. 8 U.S.C. § 1105a(a) (repealed Sept. 30, 1996) (emphasis added). Like 8 U.S.C. § 1252(a)(2)(C) (1994 ed., Supp. V), this provision squarely prohibited § 2241 district-court habeas review. At the same time that it enacted this provision, however, the 1961 Congress enacted a specific exception: “any alien held in custody pursuant to an order of deportation may obtain judicial review thereof by habeas corpus proceedings,” 8 U.S.C. § 1105a(a)(10) (1994 ed.). (This would of course have been surplusage had § 2241 habeas review not been covered by the “sole and exclusive procedure” provision.) Section 401(e) of AEDPA repealed this narrow exception, and there is no doubt what the repeal was thought to accomplish: the provision was entitled “ELIMINATION OF CUSTODY REVIEW BY HABEAS CORPUS.” 110 Stat. 1268. It gave universal preclusive effect to the “sole and exclusive procedure” language of § 1105a(a). And it is this regime that IIRIRA has carried forward.

The Court's efforts to derive ambiguity from this utmost clarity are unconvincing. First, the Court argues that §§ 1252(a)(2)(C) and 1252(b)(9) are not as clear as one might think—that, even though they are sufficient to repeal the jurisdiction of the courts of appeals, see *Calcano-Martinez v. INS*, ante, 533 U.S. 348, 351-352, 121 S.Ct. 2268, 150 L.Ed.2d 392,^{FN1} they do not cover habeas jurisdiction in the district court, since, “[i]n the immigration context, ‘judicial review’ and ‘habeas corpus’ have historically distinct*330 meanings,” ante, at 2285, 2286, n. 35. Of course § 1252(a)(2)(C) does not even *use* the term “judicial review” (it says “jurisdiction to review”)—but let us make believe it does. The Court's contention that in *this* statute it does not include habeas corpus is decisively refuted by the language of § 1252(e)(2),

enacted along with §§ 1252(a)(2)(C) and 1252(b)(9): “*Judicial review* of any determination made under section 1225(b)(1) of this title [governing review of expedited removal orders against undocumented aliens arriving at the border] is available in *habeas corpus* proceedings” (Emphases added.) It is hard to imagine how Congress could have made it any clearer that, when it used the term “judicial review” in IIRIRA, it included judicial review through habeas corpus. Research into the “historical” usage of the term “judicial review” is thus quite beside the point.

FN1. In the course of this opinion I shall refer to some of the Court's analysis in this companion case; the two opinions are intertwined.

But the Court is demonstrably wrong about that as well. Before IIRIRA was enacted, from 1961 to 1996, the governing immigration statutes unquestionably treated “judicial review” as encompassing review by habeas corpus. As discussed earlier, 8 U.S.C. § 1105a (1994 ed.) made Hobbs Act review “the sole and exclusive procedure for, the *judicial review* of all final orders of deportation” (emphasis added), but created (in subsection (a)(10)) a limited exception for habeas corpus review. Section 1105a was entitled “*Judicial review* of orders of deportation and exclusion” (emphasis added), and the exception for habeas corpus stated that “any alien held in custody pursuant to an order of deportation may obtain *judicial review* thereof by *habeas corpus* proceedings,” § 1105a(a)(10) (emphases added). Apart from this prior statutory usage, many of our own immigration cases belie the Court's suggestion that the term “judicial review,” when used in the immigration **2296 context, does not include review by habeas corpus. See, e.g., *United States v. Mendoza-Lopez*, 481 U.S. 828, 836-837, 107 S.Ct. 2148, 95 L.Ed.2d 772 (1987) (“[A]ny alien held in custody pursuant to an order of deportation may obtain*331 *judicial review* of that order in a *habeas corpus* proceeding” (emphases added)); *Shaughnessy v. Pedreiro*, 349 U.S. 48, 52, 75 S.Ct.

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

591, 99 L.Ed. 868 (1955) (“Our holding is that there is a right of *judicial review* of deportation orders *other than by habeas corpus ...*” (emphases added)); see also *id.*, at 49, 75 S.Ct. 591.

The *only* support the Court offers in support of the asserted “longstanding distinction between ‘judicial review’ and ‘habeas,’ ” *ante*, at 2286, n. 35, is language from a single opinion of this Court, *Heikkila v. Barber*, 345 U.S. 229, 73 S.Ct. 603, 97 L.Ed. 972 (1953).^{FN2} There, we “differentiate [d]” “habeas corpus” from “judicial review *as that term is used in the Administrative Procedure Act.*” *Id.*, at 236, 73 S.Ct. 603 (emphasis added). But that simply asserts that habeas corpus review is different from ordinary APA review, which no one doubts. It does *not* assert that habeas corpus review is not judicial review *at all*. Nowhere does *Heikkila* make such an implausible contention.^{FN3}

FN2. The recent Circuit authorities cited by the Court, which postdate IIRIRA, see *Mahadeo v. Reno*, 226 F.3d 3, 12 (C.A.1 2000); and *Flores-Miramontes v. INS*, 212 F.3d 1133, 1140 (C.A.9 2000), cited *ante*, at 2287, hardly demonstrate any historical usage upon which IIRIRA was based. Anyway, these cases rely for their analysis upon a third Court of Appeals decision—*Sandoval v. Reno*, 166 F.3d 225, 235 (C.A.3 1999)—which simply relies on the passage from *Heikkila* under discussion.

FN3. The older, pre-1961 judicial interpretations relied upon by the Court, see *ante*, at 2285-2286, are similarly unavailing. *Ekiu v. United States*, 142 U.S. 651, 12 S.Ct. 336, 35 L.Ed. 1146 (1892), never purported to distinguish “judicial review” from habeas, and the Court’s attempt to extract such a distinction from the opinion is unpersuasive. *Ekiu* did state that the statute “prevent[ed] the question of an alien immigrant’s right to land, when once decided adversely by an inspector, acting within the jurisdiction conferred upon him, from

being *impeached or reviewed*,” *id.*, at 663, 12 S.Ct. 336 (emphasis added; italicized words quoted *ante*, at 2286); but the clear implication was that the question whether the inspector was “acting within the jurisdiction conferred upon him” *was* reviewable. The distinction pertained, in short, to the *scope* of judicial review on habeas—not to whether judicial review was available. *Terlinden v. Ames*, 184 U.S. 270, 278, 22 S.Ct. 484, 46 L.Ed. 534 (1902), likewise drew no distinction between “judicial review” and habeas; it simply stated that the extradition statute “gives no right of review to be exercised by any court or judicial officer, and what cannot be done directly [under the extradition statute] cannot be done indirectly through the writ of *habeas corpus*.” Far from saying that habeas is *not* a form of judicial review, it says that habeas *is* an *indirect* means of review.

*332 The Court next contends that the zipper clause, § 1252(b)(9), “by its own terms, does not bar” § 2241 district-court habeas review of removal orders, *ante*, at 2286, because the opening sentence of subsection (b) states that “[w]ith respect to review of an order of removal *under subsection (a)(1) of this section*, the following requirements apply ...” (Emphasis added.) But in the broad sense, § 1252(b)(9) *does* “apply” “to review of an order of removal under subsection (a)(1),” because it mandates that “review of all questions of law and fact ... arising from any action taken or proceeding brought to remove an alien from the United States under this subchapter” must take place *in connection with* such review. This is “application” enough—and to insist that subsection (b)(9) be given effect only *within* the review of removal orders that takes place under subsection (a)(1), is to render it meaningless. Moreover, other of the numbered subparagraphs of subsection (b) make clear that the introductory sentence does not at all operate as a limitation upon what follows. Subsection (b)(7) specifies the pro-

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

cedure by which “a defendant in a criminal proceeding” charged with failing to depart after being ordered to do so may contest “the validity of [a removal] order” **2297 before trial; and subsection (b)(8) prescribes some of the prerogatives and responsibilities of the Attorney General and the alien after entry of a final removal order. These provisions have no effect if they must apply (even in the broad sense that subsection (b)(9) can be said to apply) “to review of an order of removal under subsection (a)(1).”

Unquestionably, unambiguously, and unmistakably, IIRIRA expressly supersedes § 2241’s general provision for habeas jurisdiction. The Court asserts that *Felker v. Turpin*, 518 U.S. 651, 116 S.Ct. 2333, 135 L.Ed.2d 827 (1996), and *333*Ex parte Yerger*, 8 Wall. 85, 19 L.Ed. 332 1869), reflect a “longstanding rule requiring a clear statement of congressional intent to repeal habeas jurisdiction,” *ante*, at 2278. They do no such thing. Those cases simply applied the general principle—not unique to habeas—that “[r]epeals by implication are not favored.” *Felker, supra*, at 660, 116 S.Ct. 2333; *Yerger, supra*, at 105. *Felker* held that a statute which by its terms prohibited only further review by this Court (or by an en banc court of appeals) of a court-of-appeals panel’s “ ‘grant or denial of ... authorization ... to file a second or successive [habeas] application,’ ” 518 U.S., at 657, 116 S.Ct. 2333 (quoting 28 U.S.C. § 2244(b)(3)(E) (1994 ed., Supp. II)), should not be read to imply the repeal of this Court’s separate and distinct “authority [under 28 U.S.C. § 2241 and 28 U.S.C. § 2254 (1994 ed. and Supp. V)] to hear habeas petitions filed as original matters in this Court,” 518 U.S., at 661, 116 S.Ct. 2333. *Yerger* held that an 1868 Act that by its terms “repeal[ed] only so much of the act of 1867 as authorized appeals, or the exercise of appellate jurisdiction by this court,” should be read to “reach no [further than] the act of 1867,” and did not repeal by implication the appellate jurisdiction conferred by the Judiciary Act of 1789 and other pre-1867 enactments. 8 Wall., at 105. In the present case, unlike in *Felker* and *Yerger*, none of the stat-

utory provisions relied upon—§ 1252(a)(2)(C), § 1252(b)(9), or 8 U.S.C. § 1105a(a) (1994 ed.)—requires us to imply from one statutory provision the repeal of another. All *by their terms* prohibit the judicial review at issue in this case.

The Court insists, however, that since “[n]either [§ 1252(a)(1) nor § 1252(a)(2)(C)] explicitly mentions habeas, or 28 U.S.C. § 2241,” “neither provision speaks with sufficient clarity to bar jurisdiction pursuant to the general habeas statute.” *Ante*, at 2286. Even in those areas of our jurisprudence where we *have* adopted a “clear statement” rule (notably, the sovereign immunity cases to which the Court adverts, *ante*, at 2278, n. 10), clear statement has never meant the kind of magic words demanded by the Court *334 today—explicit reference to habeas or to § 2241—rather than reference to “judicial review” in a statute that explicitly calls habeas corpus a form of judicial review. In *Gregory v. Ashcroft*, 501 U.S. 452, 467, 111 S.Ct. 2395, 115 L.Ed.2d 410 (1991), we said:

“This [the Court’s clear-statement requirement] does not mean that the [Age Discrimination in Employment] Act must mention [state] judges explicitly, though it does not. Cf. *Dellmuth v. Muth*, 491 U.S. 223, 233 [109 S.Ct. 2397, 105 L.Ed.2d 181] (1989) (SCALIA, J., concurring). Rather, it must be plain to anyone reading the Act that it covers judges.”

In *Gregory*, as in *United States v. Nordic Village, Inc.*, 503 U.S. 30, 34-35, 112 S.Ct. 1011, 117 L.Ed.2d 181 (1992), and *Atascadero State Hospital v. Scanlon*, 473 U.S. 234, 241, 246, 105 S.Ct. 3142, 87 L.Ed.2d 171 (1985), we held that the clear-statement requirement was not met, not because there was no explicit reference to the Eleventh Amendment, but because the statutory intent to eliminate state sovereign immunity was *not clear*. For the reasons discussed above, the intent to eliminate habeas jurisdiction in the present case is entirely clear, and that is all that is required.

**2298 It has happened before—too frequently,

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

alas—that courts have distorted plain statutory text in order to produce a “more sensible” result. The unique accomplishment of today’s opinion is that the result it produces is as far removed from what is sensible as its statutory construction is from the language of the text. One would have to study our statute books for a long time to come up with a more unlikely disposition. By authorizing § 2241 habeas review in the district court but foreclosing review in the court of appeals, see *Calcano-Martinez*, ante, 533 U.S. 348, 351-352, 121 S.Ct. 2268, the Court’s interpretation routes all legal challenges to removal orders brought by criminal aliens to the district court, to be adjudicated under that court’s § 2241 habeas authority, which specifies no time limits. After review by that court, criminal aliens will presumably have an appeal as of right to the court of appeals, and can then petition this Court for a writ of certiorari.*335 In contrast, noncriminal aliens seeking to challenge their removal orders—for example, those charged with having been inadmissible at the time of entry, with having failed to maintain their nonimmigrant status, with having procured a visa through a marriage that was not bona fide, or with having become, within five years after the date of entry, a public charge, see 8 U.S.C. §§ 1227(a)(1)(A), (a)(1)(C), (a)(1)(G), (a)(5) (1994 ed., Supp. V)—will still presumably be required to proceed directly to the court of appeals by way of petition for review, under the restrictive modified Hobbs Act review provisions set forth in § 1252(a)(1), including the 30-day filing deadline, see § 1252(b)(1). In fact, prior to the enactment of IIRIRA, criminal aliens also had to follow this procedure for immediate modified Hobbs Act review in the court of appeals. See 8 U.S.C. § 1105a(a) (1994 ed.). The Court has therefore succeeded in perverting a statutory scheme designed to expedite the removal of criminal aliens into one that now affords them more opportunities for (and layers of) judicial review (and hence more opportunities for delay) than are afforded non-criminal aliens—and more than were afforded criminal aliens prior to the enactment of IIRIRA.^{FN4} This outcome speaks for itself; no Congress ever imagined it.

FN4. The Court disputes this conclusion by observing that “the scope of review on habeas is considerably more limited than on APA-style review,” ante, at 2287, n. 38 (a statement, by the way, that confirms our contention that habeas is, along with the Administrative Procedure Act (APA), one form of judicial review). It is more limited, to be sure—but not “considerably more limited” in any respect that would disprove the fact that criminal aliens are much better off than others. In all the many cases that (like the present one) involve “question[s] of law,” *ibid.*, the Court’s statutory misconstruction gives criminal aliens a preferred position.

To excuse the violence it does to the statutory text, the Court invokes the doctrine of constitutional doubt, which it asserts is raised by the Suspension Clause, U.S. Const., Art. I, § 9, cl. 2. This uses one distortion to justify another, transmogrifying a doctrine designed to maintain “a just respect*336 for the legislature,” *Ex parte Randolph*, 20 F.Cas. 242, 254 (No. 11,558) (C.C.D.Va. 1833) (Marshall, C.J., on circuit), into a means of thwarting the clearly expressed intent of the legislature. The doctrine of constitutional doubt is meant to effectuate, not to subvert, congressional intent, by giving *ambiguous* provisions a meaning that will avoid constitutional peril, and that will conform with Congress’s presumed intent not to enact measures of dubious validity. The condition precedent for application of the doctrine is that the statute can *reasonably be construed* to avoid the constitutional difficulty. See, e.g., *Miller v. French*, 530 U.S. 327, 341, 120 S.Ct. 2246, 147 L.Ed.2d 326 (2000) (“We cannot press statutory construction “to the point of disingenuous evasion” even to avoid a constitutional question’ ” (quoting *United States v. Locke*, 471 U.S. 84, 96, 105 S.Ct. 1785, 85 L.Ed.2d 64 (1985), in turn quoting *George Moore Ice Cream Co. v. Rose*, 289 U.S. 373, 379, 53 S.Ct. 620, 77 L.Ed. 1265 (1933))); **2299 *Salinas v. United States*, 522 U.S. 52, 60, 118 S.Ct. 469, 139

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

L.Ed.2d 352 (1997) (quoting *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 57, n. 9, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996)). It is a device for interpreting what the statute says—not for *ignoring* what the statute says in order to avoid the trouble of determining whether what it says is unconstitutional. For the reasons I have set forth above, it is crystal clear that the statute before us here bars criminal aliens from obtaining judicial review, including § 2241 district-court review, of their removal orders. It is therefore also crystal clear that the doctrine of constitutional doubt has no application.

In the remainder of this opinion I address the question the Court *should* have addressed: Whether these provisions of IIRIRA are unconstitutional.

II A

The Suspension Clause of the Constitution, Art. I, § 9, cl. 2, provides as follows:

*337 “The Privilege of the Writ of Habeas Corpus shall not be suspended, unless when in Cases of Rebellion or Invasion the public Safety may require it.”

A straightforward reading of this text discloses that it does not guarantee any content to (or even the existence of) the writ of habeas corpus, but merely provides that the writ shall not (except in case of rebellion or invasion) be suspended. See R. Fallon, D. Meltzer, & D. Shapiro, *Hart & Wechsler's The Federal Courts and the Federal System* 1369 (4th ed. 1996) (“[T]he text [of the Suspension Clause] does not confer a right to habeas relief, but merely sets forth when the ‘Privilege of the Writ’ may be suspended”). Indeed, that was precisely the objection expressed by four of the state ratifying conventions—that the Constitution failed affirmatively to guarantee a right to habeas corpus. See Collings, *Habeas Corpus for Convicts—Constitutional Right or Legislative Grace?*, 40 Calif. L.Rev. 335, 340, and nn. 39-41 (1952) (citing 1 J. Elliott, *Debates on the Federal Constitution* 328 (2d ed. 1836) (New York); 3 *id.*, at 658 (Virginia);

4 *id.*, at 243 (North Carolina); 1 *id.*, at 334 (Rhode Island)).

To “suspend” the writ was not to fail to enact it, much less to refuse to accord it particular content. Noah Webster, in his *American Dictionary of the English Language*, defined it—with patriotic allusion to the constitutional text—as “[t]o cause to cease for a time from operation or effect; as, to *suspend* the habeas corpus act.” Vol. 2, p. 86 (1828 ed.). See also N. Bailey, *An Universal Etymological English Dictionary* (1789) (“To Suspend [in *Law*] signifies a temporal stop of a man's right”); 2 S. Johnson, *A Dictionary of the English Language* 1958 (1773) (“to make to stop for a time”). This was a distinct abuse of majority power, and one that had manifested itself often in the Framers' experience: temporarily but entirely eliminating the “Privilege of the Writ” for a certain geographic area or areas, or for a certain class *338 or classes of individuals. Suspension Acts had been adopted (and many more proposed) both in this country and in England during the late 18th century, see B. Mian, *American Habeas Corpus: Law, History, and Politics* 109-127 (1984)—including a 7-month suspension by the Massachusetts Assembly during Shay's Rebellion in 1787, *id.*, at 117. Typical of the genre was the prescription by the Statute of 1794, 34 Geo. 3, c. 54, § 2, that “[an Act for preventing wrongful imprisonment, and against undue delays in trials], insofar as the same may be construed to relate to the cases of Treason and suspicion of Treason, be suspended [for one year]” Mian, *supra*, at 110. See also 16 *Annals of Cong.* 44, 402-425 (1852) (recording the debate on a bill, reported to the House of Representatives from the Senate on January 26, 1807, and ultimately rejected, to “suspend[d], for and during the term of three months,” “the privilege of the writ of *habeas corpus*” for “any person or persons, charged on oath with treason, misprision of treason,” and **2300 other specified offenses arising out of the Aaron Burr conspiracy).

In the present case, of course, Congress has not

temporarily withheld operation of the writ, but has permanently altered its content. That is, to be sure, an act subject to majoritarian abuse, as is Congress's framing (or its determination not to frame) a habeas statute in the first place. But that is not the majoritarian abuse against which the Suspension Clause was directed. It is no more irrational to guard against the common and well known "suspension" abuse, without guaranteeing any particular habeas right that enjoys immunity from suspension, than it is, in the Equal Protection Clause, to guard against unequal application of the laws, without guaranteeing any particular law which enjoys *that* protection. And it is no more acceptable for this Court to write a habeas law, in order that the Suspension Clause might have some effect, than it would be for this Court to write other laws, in order that the Equal Protection Clause might have some effect.

*339 The Court cites many cases which it says establish that it is a "serious and difficult constitutional issue," *ante*, at 2282, whether the Suspension Clause prohibits the elimination of habeas jurisdiction effected by IIRIRA. Every one of those cases, however, pertains not to the meaning of the Suspension Clause, but to the content of the habeas corpus provision of the United States Code, which is quite a different matter. The closest the Court can come is a statement in one of those cases to the effect that the Immigration Act of 1917 "had the effect of precluding judicial intervention in deportation cases except insofar as it was required by the Constitution," *Heikkila*, 345 U.S., at 234-235, 73 S.Ct. 603. That statement (1) was pure dictum, since the Court went on to hold that the judicial review of petitioner's deportation order was unavailable; (2) does not specify to *what* extent judicial review *was* "required by the Constitution," which could (as far as the Court's holding was concerned) be zero; and, most important of all, (3) does not refer to the Suspension Clause, so could well have had in mind the due process limitations upon the procedures for determining deportability that our later cases establish, see Part III, *infra*.

There is, however, another Supreme Court dictum that is unquestionably in point—an unusually authoritative one at that, since it was written by Chief Justice Marshall in 1807. It supports precisely the interpretation of the Suspension Clause I have set forth above. In *Ex parte Bollman*, 4 Cranch 75, one of the cases arising out of the Burr conspiracy, the issue presented was whether the Supreme Court had the power to issue a writ of habeas corpus for the release of two prisoners held for trial under warrant of the Circuit Court of the District of Columbia. Counsel for the detainees asserted not only statutory authority for issuance of the writ, but inherent power. See *id.*, at 77-93. The Court would have nothing to do with that, whether under Article III or any other provision. While acknowledging an inherent power of the courts "over their own officers, or *340 to protect themselves, and their members, from being disturbed in the exercise of their functions," Marshall says that "the power of taking cognizance of any question between individuals, or between the government and individuals,"

"must be given by written law.

"The inquiry, therefore, on this motion will be, whether by any statute compatible with the constitution of the United States, the power to award a writ of *habeas corpus*, in such a case as that of Erick Bollman and Samuel Swartwout, has been given to this court." *Id.*, at 94.

In the ensuing discussion of the Judiciary Act of 1789, the opinion specifically addresses the Suspension Clause—not invoking it as a source of habeas jurisdiction, but to the contrary pointing out that without *legislated* habeas jurisdiction the Suspension Clause would have no effect.

**2301 "It may be worthy of remark, that this act was passed by the first congress of the United States, sitting under a constitution which had declared 'that the privilege of the writ of *habeas corpus* should not be suspended, unless when, in cases of rebellion or invasion, the public safety might require it.'

“Acting under the immediate influence of this injunction, they must have felt, with peculiar force, the obligation of providing efficient means by which this great constitutional privilege should receive life and activity; for if the means be not in existence, the privilege itself would be lost, although no law for its suspension should be enacted. Under the impression of this obligation, they give to all the courts the power of awarding writs of *habeas corpus*.” *Id.*, at 95.^{FN5}

FN5. The Court claims that I “rea[d] into Chief Justice Marshall’s opinion in *Ex parte Bollman* ... support for a proposition that the Chief Justice did not endorse, either explicitly or implicitly,” *ante*, at 2281, n. 24. Its support for this claim is a highly selective quotation from the opinion, see *ibid*. There is nothing “implici[t]” whatsoever about Chief Justice Marshall’s categorical statement that “the power to award the writ [of *habeas corpus*] by any of the courts of the United States, must be given by written law,” 4 Cranch, at 94. See also *ibid.*, quoted *supra*, at 2300 (“[T]he power of taking cognizance of any question between individuals, or between the government and individuals ... must be given by written law”). If, as the Court concedes, “the writ could not be suspended,” *ante*, at 2281, n. 24, within the meaning of the Suspension Clause until Congress affirmatively provided for *habeas* by statute, then surely Congress may subsequently alter what it had initially provided for, lest the Clause become a one-way ratchet, see *infra* this page. The Court’s position that a permanent repeal of *habeas* jurisdiction is unthinkable (and hence a violation of the Suspension Clause) is simply incompatible with its (and Marshall’s) belief that a failure to confer *habeas* jurisdiction is *not* unthinkable.

*341 There is no more reason for us to believe, than there was for the Marshall Court to believe, that the Suspension Clause means anything other than what it says.

B

Even if one were to assume that the Suspension Clause, despite its text and the Marshall Court’s understanding, guarantees some constitutional minimum of *habeas* relief, that minimum would assuredly not embrace the rarified right asserted here: the right to judicial compulsion of the exercise of Executive *discretion* (which may be exercised favorably or unfavorably) regarding a prisoner’s release. If one reads the Suspension Clause as a guarantee of *habeas* relief, the obvious question presented is: *What* *habeas* relief? There are only two alternatives, the first of which is too absurd to be seriously entertained. It could be contended that Congress “suspends” the writ whenever it eliminates *any* prior ground for the writ that it adopted. Thus, if Congress should ever (in the view of this Court) have authorized immediate *habeas corpus*-without the need to exhaust administrative remedies-for a person arrested as an illegal alien, Congress would *never* be able (in the light of sad experience) to revise that disposition. The Suspension*342 Clause, in other words, would be a one-way ratchet that enshrines in the Constitution every grant of *habeas* jurisdiction. This is, as I say, too absurd to be contemplated, and I shall contemplate it no further.

The other alternative is that the Suspension Clause guarantees the common-law right of *habeas corpus*, as it was understood when the Constitution was ratified. There is no doubt whatever that this did not include the right to obtain discretionary release. The Court notes with apparent credulity respondent’s contention “that there is historical evidence of the writ issuing to redress the improper exercise of official discretion,” *ante*, at 2281. The only Framing-era or earlier cases it alludes to in support of that contention, see *ante*, at 2281, n. 23, referred to *ante*, at 2281, establish no such thing. In *Ex parte Boggin*, 13 East 549, 104 Eng. Rep. 484

(K.B.1811),**2302 the court did not even bother calling for a response from the custodian, where the applicant failed to show that he was statutorily exempt from impressment under any statute then in force. In *Chalacombe's Case*, reported in a footnote in *Ex parte Boggin*, the court did “let the writ go”—i.e., called for a response from the Admiralty to Chalacombe's petition—even though counsel for the Admiralty had argued that the Admiralty's general policy of not impressing “seafaring persons of [Chalacombe's] description” was “a matter of grace and favour, [and not] of right.” But the court never decided that it had authority to grant the relief requested (since the Admiralty promptly discharged Chalacombe of its own accord); in fact, it expressed doubt whether it had that authority. See 13 East, at 550, n. (6), 104 Eng. Rep., at 484, n. (a)² (Lord Ellenborough, C.J.) (“[C]onsidering it merely as a question of discretion, is it not more fit that this should stand over for the consideration of the Admiralty, to whom the matter ought to be disclosed?”). And in *Hollingshead's Case*, 1 Salkeld 351, 91 Eng. Rep. 307 (K.B.1702), the “warrant of commitment” issued by the “commissioners of bankrupt” was “held naught,” since it authorized *343 the bankrupt's continued detention by the commissioners until “otherwise discharged by due course of law,” whereas the statute authorized commitment only “till [the bankrupt] submit himself to be examined by the commissioners.” (Emphasis deleted.) There is nothing pertaining to executive discretion here.

All the other framing-era or earlier cases cited in the Court's opinion—indeed, all the later Supreme Court cases until *United States ex rel. Accardi v. Shaughnessy*, 347 U.S. 260, 74 S.Ct. 499, 98 L.Ed. 681, in 1954—provide habeas relief from executive detention only when the custodian had no legal authority to detain. See 3 J. Story, Commentaries on the Constitution of the United States § 1333, p. 206 (1833) (the writ lies to ascertain whether a “sufficient ground of detention appears”). The fact is that, far from forming a traditional basis for issuance of the writ of habeas corpus, the whole

“concept of ‘discretion’ was not well developed at common law,” Hafetz, *The Untold Story of Non-criminal Habeas Corpus and the 1996 Immigration Acts*, 107 Yale L.J. 2509, 2534 (1998), quoted in Brief for Respondent in *Calcano-Martinez v. INS*, O.T.2000, No. 00-1011, p. 37. An exhaustive search of cases antedating the Suspension Clause discloses few instances in which courts even discussed the concept of executive discretion; and on the rare occasions when they did, they simply confirmed what seems obvious from the paucity of such discussions—namely, that courts understood executive discretion as lying entirely beyond the judicial ken. See, e.g., *Chalacombe's Case*, *supra* this page. That is precisely what one would expect, since even the executive's evaluation of the facts—a duty that was a good deal more than discretionary—was not subject to review on habeas. Both in this country, until passage of the Habeas Corpus Act of 1867, and in England, the longstanding rule had been that the truth of the custodian's return could not be controverted. See, e.g., *Opinion on the Writ of Habeas Corpus*, Wilm 77, 107, 97 Eng. Rep. 29, 43 (H.L.1758); Note, *Developments in *344 the Law-Federal Habeas Corpus*, 83 Harv. L.Rev. 1038, 1113-1114, and nn. 9-11 (1970) (quoting Act of Feb. 5, 1867, ch. 28, § 1, 14 Stat. 385); Oaks, *Legal History in the High Court-Habeas Corpus*, 64 Mich. L.Rev. 451, 453 (1966). And, of course, going beyond inquiry into the legal authority of the executive to detain would have been utterly incompatible with the well-established limitation upon habeas relief for a convicted prisoner: “[O]nce a person had been convicted by a superior court of general jurisdiction, a court disposing of a habeas corpus petition could not go behind the conviction for any purpose other than to verify the formal jurisdiction of the committing court.” *Id.*, at 468, quoted in **2303 *Swain v. Pressley*, 430 U.S. 372, 384-385, 97 S.Ct. 1224, 51 L.Ed.2d 411 (1977) (Burger, C. J., concurring in part and concurring in judgment).

In sum, there is no authority whatever for the proposition that, at the time the Suspension Clause was ratified—or, for that matter, even for a century

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

and a half thereafter-habeas corpus relief was available to compel the Executive's allegedly wrongful refusal to exercise discretion. The striking proof of that proposition is that when, in 1954, the Warren Court held that the Attorney General's alleged refusal to exercise his discretion under the Immigration Act of 1917 could be reviewed on habeas, see *United States ex rel. Accardi v. Shaughnessy*, *supra*, it did so without citation of any supporting authority, and over the dissent of Justice Jackson, joined by three other Justices, who wrote:

"Of course, it may be thought that it would be better government if even executive acts of grace were subject to judicial review. But the process of the Court seems adapted only to the determination of legal rights, and here the decision is thrusting upon the courts the task of reviewing a discretionary and purely executive function. Habeas corpus, like the currency, can be debased by over-issue quite as certainly as by too niggardly use. We would ... leave the responsibility for suspension or *345 execution of this deportation squarely on the Attorney General, where Congress has put it." *Id.*, at 271, 74 S.Ct. 499.

III

Given the insubstantiality of the due process and Article III arguments against barring judicial review of respondent's claim (the Court does not even bother to mention them, and the Court of Appeals barely acknowledges them), I will address them only briefly.

The Due Process Clause does not "[r]equir[e] [j]udicial [d]etermination [o]f" respondent's claim, Brief for Petitioners in *Calcano-Martinez v. INS*, O.T.2000, No. 00-1011, p. 34. Respondent has no legal entitlement to suspension of deportation, no matter how appealing his case. "[T]he Attorney General's suspension of deportation [is] 'an act of grace' which is accorded pursuant to her 'unfettered discretion,' *Jay v. Boyd*, 351 U.S. 345, 354, 76 S.Ct. 919, 100 L.Ed. 1242 (1956) ..., and [can be likened, as Judge Learned Hand observed,] to 'a judge's power to suspend the execution of a

sentence, or the President's to pardon a convict," 351 U.S., at 354, n. 16, 76 S.Ct. 919" *INS v. Yueh-Shaio Yang*, 519 U.S. 26, 30, 117 S.Ct. 350, 136 L.Ed.2d 288 (1996). The furthest our cases have gone in imposing due process requirements upon analogous exercises of Executive discretion is the following. (1) We have required "minimal procedural safeguards" for death-penalty clemency proceedings, to prevent them from becoming so capricious as to involve "a state official flipp[ing] a coin to determine whether to grant clemency," *Ohio Adult Parole Authority v. Woodard*, 523 U.S. 272, 289, 118 S.Ct. 1244, 140 L.Ed.2d 387 (1998) (O'CONNOR, J., concurring in part and concurring in judgment). Even assuming that this holding is not part of our "death-is-different" jurisprudence, *Shafer v. South Carolina*, 532 U.S. 36, 55, 121 S.Ct. 1263, 149 L.Ed.2d 178 (2001) (SCALIA, J., dissenting) (citation omitted), respondent here is not complaining about the absence of procedural safeguards; he disagrees with the Attorney General's judgment on a point of law. (2) We have recognized the existence of a due process liberty interest when *346 a State's statutory parole procedures prescribe that a prisoner "shall" be paroled if certain conditions are satisfied, see *Board of Pardons v. Allen*, 482 U.S. 369, 370-371, 381, 107 S.Ct. 2415, 96 L.Ed.2d 303 (1987); *Greenholtz v. Inmates of Neb. Penal and Correctional Complex*, 442 U.S. 1, 12, 99 S.Ct. 2100, 60 L.Ed.2d 668 (1979). There is no such statutory entitlement to suspension of deportation, no matter what the facts. Moreover, in neither *Woodard*, nor *Allen*, nor *Greenholtz* did we intimate that the Due Process Clause conferred jurisdiction of its **2304 own force, without benefit of statutory authorization. All three cases were brought under 42 U.S.C. § 1983.

Article III, § 1's investment of the "judicial Power of the United States" in the federal courts does not prevent Congress from committing the adjudication of respondent's legal claim wholly to "non-Article III federal adjudicative bodies," Brief for Petitioners in *Calcano-Martinez v. INS*, O.T.2000, No. 00-1011, at 38. The notion that Art-

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473
(Cite as: 533 U.S. 289, 121 S.Ct. 2271)

Article III requires every Executive determination, on a question of law or of fact, to be subject to judicial review has no support in our jurisprudence. Were it correct, the doctrine of sovereign immunity would not exist, and the APA's general permission of suits challenging administrative action, see 5 U.S.C. § 702, would have been superfluous. Of its own force, Article III does no more than commit to the courts matters that are "the stuff of the traditional actions at common law tried by the courts at Westminster in 1789," *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 90, 102 S.Ct. 2858, 73 L.Ed.2d 598 (1982) (REHNQUIST, J., concurring in judgment)-which (as I have discussed earlier) did not include supervision of discretionary Executive action.

* * *

The Court has created a version of IIRIRA that is not only unrecognizable to its framers (or to anyone who can read) but gives the statutory scheme precisely the *opposite* of its intended effect, affording criminal aliens *more* opportunities*347 for delay-inducing judicial review than others have, or even than criminal aliens had prior to the enactment of this legislation. Because § 2241's exclusion of judicial review is unmistakably clear, and unquestionably constitutional, both this Court and the courts below were without power to entertain respondent's claims. I would set aside the judgment of the court below and remand with instructions to have the District Court dismiss for want of jurisdiction. I respectfully dissent from the judgment of the Court.

U.S.,2001.

I.N.S. v. St. Cyr

533 U.S. 289, 121 S.Ct. 2271, 150 L.Ed.2d 347, 69 USLW 4510, 01 Cal. Daily Op. Serv. 5235, 2001 Daily Journal D.A.R. 6475, 14 Fla. L. Weekly Fed. S 401, 2001 DJCAR 3473

END OF DOCUMENT

116 Cal.App.3d 111, 172 Cal.Rptr. 74
 (Cite as: 116 Cal.App.3d 111)



INSTITUTE OF VETERINARY PATHOLOGY,
 INC., Plaintiff and Appellant,
 v.
 CALIFORNIA HEALTH LABORATORIES, INC.,
 et al., Defendants and Appellants.

Civ. No. 18578.

Court of Appeal, Fourth District, Division 1, Cali-
 fornia.

Feb 23, 1981.

SUMMARY

In an action for damages for intentional interference with prospective business advantage by a corporation, headed by a veterinary pathologist and organized to engage in diagnostic testing of nonhuman samples, against a parent corporation and two subsidiaries, a jury awarded compensatory damages against all defendants and punitive damages against the subsidiaries. The trial court had directed a verdict for the parent on the issue of punitive damages and later granted its motion for judgment notwithstanding the verdict. The court also granted the subsidiaries' motion for new trial unless plaintiff accepted a reduced amount of compensatory damages in satisfaction of all verdicts. By agreement, plaintiff corporation had been engaged with the subsidiaries in a cooperative effort to conduct veterinary pathology. Defendants, having decided to continue veterinary pathology activities without plaintiff corporation and its pathologist, surreptitiously secured forms similar to those used by plaintiff and compiled and reviewed plaintiff's billing data and customer list to determine their worth. Defendants then terminated the relationship with plaintiff without advance notice and concurrently instituted a "sales blitz" primarily focused on plaintiff's accounts. The admitted purpose of defendants' actions was to gain a competitive advantage over plaintiff in defendants' effort to attract as many of plaintiff's existing accounts as possible. (Superior Court of San Diego County, No. 339628,

Joseph A. Kilgarif, Judge.)

The Court of Appeal affirmed the judgment in favor of the parent corporation and the order granting a new trial in favor of the subsidiaries. The court held the parent's relationship with the subsidiaries did not warrant submitting the issue of its liability for compensatory or punitive damages to the jury. It also held the trial court did not abuse its discretion in ordering the new trial on the ground the compensatory and punitive damage awards were excessive. The court further held, however, the trial court erred in ruling plaintiff was not entitled to punitive damages as a matter of law since defendant subsidiaries had no justification or privilege entitling them to surreptitiously engage in a course of conduct designed to deprive plaintiff of its business. (Opinion by Wiener, J., with Brown (Gerald), P. J., concurring. Staniforth, J., concurred in the result.)

HEADNOTES

Classified to California Digest of Official Reports
 (1) Trial § 123--Direction of Verdict--Review--Consideration of Evidence.

An order granting a motion for directed verdict for the defendant in a civil action may be affirmed only when the reviewing court is satisfied that after taking the plaintiff's evidence in the light most favorable to it, including indulging in every legitimate inference, the evidence would not support a jury verdict in its favor.

(2a, 2b, 2c) Corporations § 46--Actions by and Against Corporations-- Liability of Parent for Acts of Subsidiary.

In an action against a parent corporation and two wholly owned subsidiaries for compensatory and punitive damages for tortious destruction of plaintiff corporation's business, the trial court properly granted the parent corporation's motion for a directed verdict as to punitive damages and its motion for judgment notwithstanding the verdict as to compensatory damages, where the evidence only

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

established intercorporate connections between the parent and the subsidiaries and there was no direct evidence of manipulative control by the parent of its subsidiaries which would require imposition of liability on an alter ego theory, and where, though a managerial employee of one of the subsidiaries who was allegedly responsible for the actions complained of by plaintiff reported to the chairman of the board of directors and chief executive officer of that subsidiary who was also on the parent's board of directors, there was no evidence the employee was an agent and employee of the parent. His superior's position as a director of the parent, without more, was not sufficient evidence to support a finding of agency between the parent and the employee; it did not establish the assumption of a supervisory role by the parent over the subsidiary.

[Liability of corporation for torts of subsidiary, note, 7 A.L.R.3d 1343. See also Cal.Jur.3d, Corporations § 179; Am.Jur.2d, Corporations, § 717.]

(3) Corporations § 46--Actions by and Against Corporations--Liability of Parent for Acts of Subsidiary.

A parent corporation is not liable for the torts of its subsidiaries simply because of stock ownership. Liability may be imposed only where the parent controls the subsidiary to such a degree as to render the subsidiary the mere instrumentality of the parent.

(4) Corporations § 46--Actions by and Against Corporations--Liability of Parent for Acts of Subsidiary--Application of Doctrine of After Ego.

Whether the doctrine of alter ego applies so as to make a parent corporation liable for the torts of its subsidiaries is a question of fact which necessarily varies according to the circumstances of each case. The trier of fact must consider whether such a unity of interest in ownership exists so as to dissolve the separate corporate personalities of the parent and the subsidiary, relegating the subsidiary to the status of merely an instrumentality, agency, conduit or adjunct of the parent, and whether an inequitable result will occur if the conduct is treated as that of the subsidiary alone.

(5) Damages § 25--Exemplary or Punitive Damages--Persons Liable--Liability of Principal for Acts of Agent.

Punitive damages may be imposed against a principal for the acts of an agent where the principal authorized the doing and the manner of the act and the agent was employed in a managerial capacity and was acting in the scope of employment or the principal approves the act.

(6) New Trial § 6--Discretion of Court.

Granting or denying a motion for a new trial rests in the trial court's sole discretion which will not be disturbed on appeal unless a manifest and unmistakable abuse of that discretion clearly appears. Thus, Code Civ. Proc., § 657, provides such an order based on the ground of insufficiency of the evidence should be reversed "only if there is no substantial basis in the record" for any of the reasons specified in the order.

(7a, 7b, 7c) New Trial § 46--Grounds for New Trial--Excessive or Inadequate Damages--Application of Rule.

In an action by a corporation against other corporations for damages for intentional interference with prospective business advantage, the trial court's order granting defendants a new trial, insofar as it was based on excessiveness of the jury's award of compensatory and punitive damages, was proper. Its order for new trial unless plaintiff should accept a reduced amount of compensatory damages was legally and factually supported by its meticulous specifications, reasons and reference to the factual record. Though the court erred in finding there was no evidence to support a punitive damage award against one of defendant corporations and rejecting wealth as a factor in determining the size of a punitive damage award, it did not abuse its discretion in finding there was no rational relationship between the award of punitive damages and the extent of the wrong.

(8a, 8b, 8c) Interference § 7--Interference With Business Relationships--Actions and Remedies--Punitive Damages.

116 Cal.App.3d 111, 172 Cal.Rptr. 74
 (Cite as: 116 Cal.App.3d 111)

In an action for damages for intentional interference with prospective business advantage by a corporation, headed by a veterinary pathologist and organized to engage in diagnostic testing of nonhuman samples, against two corporations which had, by agreement, been engaging with plaintiff in a cooperative effort to conduct veterinary pathology, the trial court erred in finding, as one of the bases for an order granting defendants a new trial, that plaintiff, as a matter of law, was not entitled to punitive damages, where defendants, having decided to continue veterinary pathology activities without plaintiff corporation and its pathologist, surreptitiously secured forms similar to those used by plaintiff and compiled and reviewed plaintiff's billing data and customer list to determine their worth, where defendants then terminated the relationship with plaintiff without advance notice and concurrently instituted a "sales blitz" primarily focused on plaintiff's major accounts, where the express and admitted purpose of defendants' actions was to gain a competitive advantage over plaintiff in defendants' effort to attract as many of plaintiff's existing accounts as possible, where defendants knew the sudden termination of plaintiff, without notice, and the simultaneous denial of further lab facilities or services to plaintiff would result in plaintiff's inability to continue its veterinary pathology business unless it could immediately arrange for equivalent lab services, and where plaintiff's efforts to use stop-gap measures to mitigate its losses were unsuccessful.

(9) Damages § 27--Exemplary or Punitive Damages--Review.

In reviewing a trial court's grant of a new trial in a civil case on the ground of excessive punitive damages, deference must be given to the trial court for it is in a far better position than an appellate court to determine whether a damage award was influenced by passion or prejudice. It has the prerogative to independently determine the reprehensibility of a defendant's conduct in a particular case and may consider the amount of compensatory damages in assessing the degree of reprehensibility.

(10) Interference § 6--Interference With Business Relationships-- Prospective Business Advantage.

The tort of intentional interference with prospective business advantage is premised on the ideal everyone has the right to establish and conduct a lawful business and is entitled to the protection of organized society, through its courts, whenever that right is unlawfully invaded. It imposes liability for improper methods of diverting or taking business from another which are not within the privilege of fair competition. Consequently, in order to be actionable, the interference with prospective economic advantage or an advantageous business relationship must be unjustified and/or without privilege. The unjustifiability or wrongfulness of the act may consist of the methods used and/or the purpose or motive of the actor. It will lie where the right to pursue a lawful business is intentionally interfered with either by unlawful means or by means otherwise lawful when there is a lack of sufficient justification.

(11) Interference § 6--Interference With Business Relationships-- Prospective Business Advantage--Elements.

The elements of the tort of intentional interference with prospective business advantage include the existence of a prospective business relationship advantageous to the plaintiff, the defendant's knowledge of the existence of the relationship, the defendant's intentional conduct designed to disrupt the relationship, actual causation, and damages to the plaintiff proximately caused by the defendant's conduct.

COUNSEL

Wylie A. Aitken, John Bradshaw and John C. Adams III for Plaintiff and Appellant.

Freshman, Mulvaney, Marantz, Comsky, Forst, Kahan & Deutsch, Wesley B. Hills and Linda G. Landres for Defendants and Appellants.

WIENER, J.

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

This case involves the economic life and corporate death of the Institute of Veterinary Pathology, Inc. (IVP). IVP, believing its untimely demise was due to the actions of defendants USV Pharmaceutical Corporation (USV), National Health Laboratories Incorporated (NHL), and Revlon, Inc., sued for compensatory and punitive damages for the tortious destruction of its business. A jury agreed, awarding IVP \$88,000 in compensatory damages against all defendants plus \$221,000 and \$442,000 in punitive damages against NHL and USV respectively. Revlon escaped assessment for punitive damages because the court directed a verdict in its favor on that issue. In posttrial proceedings, the court also granted Revlon's motion for judgment notwithstanding the verdict (NOV) and granted the motions by NHL and USV for new trial unless IVP accepted \$26,250 in satisfaction of all verdicts. Plaintiff appeals the directed verdict, judgment NOV, and the new trial order.^{FN1} We conclude each of the court's orders has adequate legal and factual support. Accordingly, we affirm.

FN1 Counsel for the parties will note we omit certain procedural and factual details in our opinion. We admit to simplifying the procedural morass of whether the court granted Revlon's nonsuit motion as to punitive damages or directed a verdict on that issue. For our purposes, the label given is immaterial because our scope of review is the same. *Estate of Lounsberry* (1957) 149 Cal.App.2d 857, 858 [309 P.2d 554]; *Elmore v. American Motors Corp.* (1969) 70 Cal.2d 578, 583 [75 Cal.Rptr. 652, 451 P.2d 84].) We also do not dwell on such matters as the myriad of corporate names used by California Health Laboratories (CHL), defendant's cross-appeal, or the fact that NHL as cross-complainant obtained a verdict of \$4,523.80 against IVP.

Factual Background

IVP is the surrogate for Dr. Charles Sodikoff, a veterinary pathologist, a rare professional, uniquely

qualified to perform and analyze clinical diagnostic testing on animals. In September 1969, Dr. Sodikoff *117 went into business with Dr. Russell Irwin of the San Diego Institute of Pathology (SDIP) to establish and manage a veterinary division for that laboratory. It was Sodikoff's job to introduce into the San Diego veterinary community the relatively new concept of veterinary pathology. He prepared educational materials to solicit customers, presented lecture series on clinical pathology, personally contacted local veterinarians, developed "panel testing" procedures specifically designed for nonhuman samples, established a list of "normal values" for the various animals commonly treated by veterinarians in the San Diego area, and developed special forms for requesting and reporting of veterinary pathology tests for SDIP customers. Through his efforts, SDIP acquired about 50 to 60 veterinary clients generating gross monthly sales of between \$5,000 and \$6,000.

The parties parted in July 1970 because this pioneering venture was not sufficiently profitable for SDIP. Sodikoff was permitted to withdraw, taking with him the veterinary pathology business he developed with SDIP, the good will created, and the IVP trade name which he incorporated.

Sodikoff made contact with a Norbert Mootz, the director and part owner of Automated Biochemistry (ABC), an established laboratory which did some veterinary testing. In September 1970, they orally agreed ABC would perform laboratory testing services for one-half of IVP's gross billing for each test IVP interpreted for veterinarians. ABC would pick up samples, deliver the results, and provide office space and clinical apparatus. IVP was to handle its own billing and collections and interpret test results for its veterinary clients. Dr. Sodikoff was to continue to solicit new business. In effect, they were to engage in a cooperative effort to conduct veterinary pathology.

California Health Laboratories (CHL), wholly owned by Revlon, acquired ABC in April 1971. By August 1972, CHL was one of a number of labs

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

comprising the health services division of USV, a wholly owned subsidiary of Revlon. NHL is the successor-in-interest to CHL. (In this opinion NHL and CHL are used interchangeably.)

Richard Whalley, a trained forensic pathologist, replaced Mootz as director of the CHL laboratory in early 1972. Robert Draper was his immediate superior. In 1971, Draper was the western division vice president of the health services division of USV. He became general manager of that division in March 1972. He reported to John H. Williford, who in 1972 was chairman of the board of directors and chief executive officer of USV. Mr. Williford was also on Revlon's board.

In the spring of 1972, Dr. Sodikoff became interested in selling IVP. He met with Draper and offered the business to CHL for \$100,000 plus \$2,000 monthly if he were to remain as a consultant. He gave Draper a profit and loss statement to serve as the basis for CHL's independent economic evaluation. After preparing a cost projection, CHL's controller, Hal Lawrence, concluded the purchase of IVP would result in a monthly net loss to CHL. There was no further discussion relating to the purchase.

Sometime after Lawrence prepared his cost projection, about mid-July 1972, CHL decided to terminate its relationship with IVP. Several factors contributed to this decision, including a deteriorating relationship with Dr. Sodikoff. Draper told Whalley to handle the termination.

CHL, unlike SDIP, did not wish to eliminate its veterinary pathology activities because absent Sodikoff, it felt the business could be lucrative. Accordingly, in order to establish its competitive position, CHL ordered veterinary forms comparable to those previously used by IVP modified to reflect the change in business ownership. CHL also compiled and reviewed IVP's billing data and customer list to determine their worth. All this was done without telling Dr. Sodikoff. The forms were hidden at CHL where Sodikoff would not see them. On

August 1, 1972, Sodikoff was inadvertently told by a CHL employee his relationship was about to end. He telephoned Whalley, who verified the information-termination was effective immediately. He received more formal notice a few days later in CHL's certified letter dated August 1. The activities of CHL to assure its place in the market from mid-July to August 1, 1972, are deferred to our discussion of punitive damages. Suffice it to say, CHL successfully gained a place in the market. In doing so, IVP was effectively squeezed out. It died in December 1972.

Revlon's Liability

The Directed Verdict on Punitive Damages

(1)The granting of a motion for directed verdict is tested against a rigorous standard. We may affirm only when we are satisfied that after taking plaintiff's evidence in the light most favorable to it, including indulging in every legitimate inference, the evidence would not support a jury verdict in its favor. (*Elmore v. American Motors Corp.*, supra, 70 Cal.2d 578, 583; *Ewing v. Cloverleaf Bowl* (1978) 20 Cal.3d 389, 395 [143 Cal.Rptr. 13, 572 P.2d 1155].) (2a)In applying this standard, we hold Revlon's relationship with NHL and USV, based on either "alter ego" or agency principles, did not warrant the issue of its liability for punitive damages to reach the jury.

Alter Ego

(3)A parent corporation is not liable for the torts of its subsidiaries simply because of stock ownership. (*Northern Natural Gas Co. v. Superior Court* (1976) 64 Cal.App.3d 983, 991 [134 Cal.Rptr. 850].) Liability may be imposed only where the parent controls the subsidiary to such a degree as to render the latter the mere instrumentality of the former. (6 Witkin, Summary of Cal. Law (8th ed. 1974) Corporations, § 11, p. 4323; 7 A.L.R.3d 1343.) "With increasing frequency, courts have demonstrated a readiness to disregard the corporate entity when a wholly owned subsidiary is merely a conduit for, or is financially dependent on, a parent corporation. In the interests of justice and

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

to prevent fraud, the courts will ignore the existence of a corporate entity used to cut off either causes of action against or defenses by another corporate entity.” (1A Ballantine & Sterling, Cal. Corporation Laws (4th ed. 1980) § 296.02, pp. 14-32.1-14-33.)

(4) Whether alter ego applies is a question of fact which necessarily varies according to the circumstances of each case. *Associated Vendors, Inc. v. Oakland Meat Co.* (1962) 210 Cal.App.2d 825, 836-837 [26 Cal.Rptr. 806]; *McLoughlin v. L. Bloom Sons Co., Inc.* (1962) 206 Cal.App.2d 848, 851-852 [24 Cal.Rptr. 311].) The trier of fact must consider whether (1) such a unity of interest in ownership exists so as to dissolve the separate corporate personalities of the parent and the subsidiary, relegating the latter to the status of merely an instrumentality, agency, conduit or adjunct of the former, and (2) an inequitable result will occur if the conduct is treated as that of the subsidiary alone. (*Automotriz etc. De California v. Resnick* (1957) 47 Cal.2d 792, 796 [306 P.2d 1, 63 A.L.R.2d 1042]; *Walker v. Signal Companies, Inc.* (1978) 84 Cal.App.3d 982, 1001 [149 Cal.Rptr. 119].)

Here, IVP points to the following facts relating to Revlon's management, control and domination over USV and NHL which would have supported a jury verdict in its favor: (1) Revlon owned 100 percent of *120 the stock of both USV and NHL; (2) interlocking directors and officers of Revlon, USV and NHL (the record, however, only establishes the directors and officers of NHL as of 1973); (3) the minute and stock books of both USV and NHL were kept by Revlon's secretary at its New York corporate headquarters; (4) consolidated financial statements including income from divisions and subsidiaries were contained in Revlon's annual reports; (5) Draper's testimony relating to the corporate structure of Revlon relative to USV and NHL; and (6) Lawrence's testimony regarding his transfers from a Revlon-owned company to USV, then to CHL as its controller.

(2b) This evidence, however, only establishes intercorporate connections between Revlon, USV, and NHL. It fails to set forth any direct evidence of Revlon's manipulative control of its subsidiaries which would require imposition of liability. There is nothing to support a finding that the validly formed and existing corporate subsidiaries were only instrumentalities or conduits for Revlon.

Interlocking directorates, although of concern because of the potential for improper conduct of the parent over a subsidiary is not, in and of itself, sufficient without direct evidence of specific manipulative conduct to warrant the piercing of the corporate veil. Further, in light of the equitable nature of the doctrine in controversy, IVP has failed to satisfy the necessary requirement of establishing an inequitable result if the conduct were to be treated as that of the subsidiaries alone.

Agency

IVP alternatively urges “there is ample evidence ... that Mr. Draper was acting in [a] managerial capacity, exercising ... broad discretion over the acts of NHL within the extensive authority emanating directly from Revlon's board of directors through his immediate superior, Mr. Williford.” In other words, “[t]he jury ... could have found that [he] was acting as an agent, in a managerial capacity for Revlon in exactly the same sense as he was for USV.”

(5) Punitive damages may be imposed against a principal for the acts of an agent where the principal authorized the doing and the manner of the act, the agent was employed in a managerial capacity and was acting in the scope of employment or the principal approves the act. (*Egan v. Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d 809, 822 [169 Cal.Rptr. 691, 620 P.2d 141].) (2c) There is no evidence *121 Draper was an agent and employee of Revlon. The record only establishes he was a managerial employee of USV. Although Williford was the chief executive officer and chairman of the board of directors of USV, his position on Revlon's board of directors alone, without more, is not suffi-

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

cient evidence to support a finding of agency between Revlon and Draper, as it does not establish the assumption of a supervisory role by Revlon over USV. (See generally, *Walker v. Signal Companies, Inc.*, *supra.*, 84 Cal.App.3d at pp. 1001-1002.)

Compensatory Damages-The Judgment NOV

Guided by the foregoing discussion, we also conclude the court properly granted the judgment notwithstanding the verdict in favor of Revlon in regard to compensatory damages. Applying essentially the same rigorous standard used to test the directed verdict on punitive damages, but in a different procedural context, we agree there was insufficient evidence to support a verdict in plaintiff's favor for compensatory damages. (*Clemmer v. Hartford Insurance Co.* (1978) 22 Cal.3d 865, 877-878 [151 Cal.Rptr. 285, 587 P.2d 1098]; *Hauter v. Zogarts* (1975) 14 Cal.3d 104, 110-111 [120 Cal.Rptr. 681, 534 P.2d 377, 74 A.L.R.3d 1282].) Granted, there is a difference between punitive and compensatory damages because of the necessary finding of malice with regard to the former. Nevertheless, even where compensatory damages are at issue, there must be some other basis other than stock ownership to establish liability for the tortious acts of a subsidiary. (*Northern Natural Gas Co. v. Superior Court*, *supra.*, 64 Cal.App.3d at p. 991.) Because IVP has failed under both alter ego and agency principles to establish Revlon's corporate responsibility for the conduct of its subsidiaries during the period in question, the court correctly determined Revlon has no liability.

The New Trial Order

General Principles and Considerations

IVP attacks the new trial order claiming the court's specification of reasons is inadequate to comply with the requirements of Code of Civil Procedure section 657 as construed in *Mercer v. Perez* (1968) 68 Cal.2d 104 [65 Cal.Rptr. 315, 436 P.2d 315] and *Scala v. Jerry Witt & Sons, Inc.* (1970) 3 Cal.3d 359 [90 Cal.Rptr. 592, 475 P.2d 864], and even if adequate, it is not supported by substantial

evidence. *122

(6)A trial court has considerable power in ruling on a motion for a new trial. Granting or denying the motion rests in its sole discretion which will not be disturbed on appeal unless a manifest and unmistakable abuse of that discretion clearly appears. (*Jiminez v. Sears, Roebuck & Co.* (1971) 4 Cal.3d 379, 387 [93 Cal.Rptr. 796, 482 P.2d 681, 52 A.L.R.3d 92].) Code of Civil Procedure section 657 provides such an order based upon the ground of insufficiency of the evidence should be reversed "only if there is no substantial basis in the record" for any of the reasons specified in the order. Underlying policy reasons for this trial court prerogative include not only the notion that trial judges are in a better position to judge the credibility of witnesses and must necessarily do so in determining whether a new trial is essential to achieve justice, but also there can be no harm when parties are afforded the full opportunity to relitigate their controversy. Implicit in this latter premise is that a second trial is the same as the first save only for the time lag. We disagree with this premise, for the burden on our courts, the difficulties in gaining access for trial, the immense cost of litigation, and the social and psychological expense to the parties, now appear to far outweigh the simple maxim that a full retrial is the solution in every case where a new trial order is tied to a number of reasons and only one of those reasons has validity. An all or nothing rule makes little sense.

We recently expressed our frustration with the present legislative scheme in *Delos v. Farmers Insurance Group* (1979) 93 Cal.App.3d 642, 667-668 [155 Cal.Rptr. 843]. There, after describing the court's reduction of damages as inordinate because of what we held was its erroneous view of the law, we lamented it was indeed unfortunate that a more judicially efficient approach was not possible by merely sending the case back for reconsideration of punitive damages in light of our opinion. For reasons which will become apparent, we would like to do the same here to allow the very experienced and

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

capable trial judge who presided over this case to consider modification of his post trial rulings in accordance with our comments, including, if necessary, limiting the issues on retrial.^{FN2} *123

FN2 The trial court was not requested, nor did it order, a limited new trial restricted to one or more issues. (See *Leipert v. Honold* (1952) 39 Cal.2d 462, 467 [247 P.2d 324, 29 A.L.R.2d 1185].) “The power of an appellate court in reviewing an order granting a new trial must be distinguished from its power on an appeal from a judgment. Where an appeal is from the whole judgment, a reviewing court may, upon reversal of the judgment, order retrial of a particular issue if ‘those trial court determinations which were affected with error may be fairly and conveniently severed from those which were not.’ [Citations.]” (*Richard v. Scott* (1978) 79 Cal.App.3d 57, 69, fn. 4 [144 Cal.Rptr. 672].)

The court's reasons granting defendants' motion for new trial were contained in a 14-page document. In effect, the court relied on two alternative grounds. First, IVP was not entitled to punitive damages because the evidence was insufficient to establish any tortious conduct by NHL, its wrongful termination of IVP without reasonable notice constituting no more than a breach of contract. (7a) Second, damages, both compensatory and punitive, were excessive. We conclude the second reason is legally and factually sound. Accordingly, we must affirm. (8a)As we will point out, however, there was ample evidence to support the jury's finding of tortious conduct warranting a punitive damage award. Unfortunately, we may not merely remand to the trial court for reconsideration of its determination IVP was not entitled to punitive damages. Our discussion represents only guidance for the trial court upon retrial. We hope, however, our comments will motivate the trial bar and other interested persons to take up the cudgels for a legislative solution which can protect the conflicting interests

involved while permitting a less costly judicial process.

Excessive Compensatory Damages

(7b)The court found \$88,000 in compensatory damages to be excessive and reduced them to \$26,250. Its specifications, reasons and reference to the factual record are meticulous. The court reviewed the three witnesses' respective conclusions of IVP's value of \$100,000 (Sodikoff), \$104,170 (Richard Mills for IVP), \$9,000-\$15,000 (Arthur Bradshatzer for defendants). The court also carefully evaluated Mills' arguments and found his conclusion to be arithmetically unpersuasive and incomplete. The court compared this analysis with that of Bradshatzer which it found to be intellectually and mathematically sound. The court further opined that even the reduced value had some blue sky because there was no willing or knowledgeable buyer interested in purchasing IVP. We hold the court acted within its discretion in reducing the amount of compensatory damages and in granting the motion for new trial unless IVP accepted the reduced sum.

Excessive Punitive Damages

The court also granted the new trial on the ground the punitive damages were excessive and against the law. It found there was no evidence to warrant an award of damages against USV and the punitive damages award against CHL was grossly excessive. We respectfully *124 disagree with the court's reasoning for as we shall explain, there is a substantial evidentiary basis and legal justification for an award of punitive damages. Nevertheless, and even though the court also erred in rejecting wealth as a factor in determining the size of a punitive damage award, it did correctly describe the need for there to be some relationship between the amount of compensatory, \$26,250, and punitive damages in assessing the propriety of the punitive damage award. (*Neal v. Farmers Ins. Exchange* (1978) 21 Cal.3d 910, 928 [148 Cal.Rptr. 389, 582 P.2d 980].) This reason alone requires us to affirm the new trial order. (9) Deference must be given to

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

the trial court for “it is in a far better position than an appellate court to determine whether a damage award was influenced by ‘passion or prejudice.’ [Citation.]” (*Schroeder v. Auto Driveway Co.* (1974) 11 Cal.3d 908, 919 [114 Cal.Rptr. 622, 523 P.2d 662].) It has “the prerogative to independently determine the reprehensibility of defendants’ conduct in a particular case and may consider the amount of compensatory damages in assessing the degree of reprehensibility.” (*Delos v. Farmers Insurance Group, supra.*, 93 Cal.App.3d 642, 666.) (7c) Thus, here, although some of the court’s reasons for granting the new trial are, in our view, erroneous, the correct reasons stated are sufficient to support the new trial order.^{FN3}

FN3 The reasons we hold erroneous include the court’s conclusion defendants’ conduct was not tortious, its apparent concern with the windfall aspect of punitive damages, and the immateriality of wealth as a factor in determining the amount of punitive damages. In addition, we respectfully disagree with the court’s finding there was insufficient evidence to warrant punitive damages against USV. The trial judge explained such liability would have been based upon the actions of USV’s vice-president Draper; that he never ratified Whalley’s actions, and that he merely instructed CHL to sever relations with IVP, delegating the full responsibility as to manner, method and time of severance to Whalley.

Punitive damages can properly be awarded against a principal for an act of an agent not only if the former authorizes or ratifies the latter’s act but also if “... the agent was employed in a managerial capacity and was acting in the scope of employment” (*Egan v. Mutual of Omaha Ins. Co.*, *supra.*, 24 Cal.3d at p. 822; Rest. 2d Torts, § 909.) Draper’s managerial position with USV as vice president and general man-

ager of its health services division, taken with evidence of the manner in which Whalley, Lawrence and Cleveland conducted themselves in reference to the entire matter, supports a finding of a ratification by USV. The parties continued to work for NHL and they were never criticized or disciplined for their conduct by Draper, who said he was satisfied with the method in which the termination was handled. (1 Witkin, Summary of Cal. Law (8th ed. 1973.) Agency and Employment, § 154, p. 754.)

The court recognized the basic “purpose of punitive damages is to punish, not to make plaintiff wealthy.” While complimenting IVP’s counsel for his talented advocacy, it expressed concern that counsel’s *125 continued reference to the well publicized \$118 million punitive damage award against Ford Motor Company caused the jury to emotionally respond in calculating punitive damages. Although we believe there was sufficient evidence to support a punitive damage award, we cannot substitute our instincts at this level for the sound judgment of the trial judge in assessing the degree of reprehensibility involved. The trial court, in a much better position to determine the degree of reprehensibility, found there was no rational relationship between the amount of punitive damages and the extent of the wrong and, accordingly, ordered a new trial. In light of the respective roles between the trial and appellate courts, we defer to this exercise of trial court discretion.

Defendants’ Tortious Conduct-Interference With a Prospective Business Advantage

(8b) The court’s specification of reasons in its new trial order included its determination that plaintiff, as a matter of law, was not entitled to punitive damages. It said, “This action falls squarely within the parameters of C. C. 3294, the obligation arising out of contract and the termination, for the various reasons given herein, was not tortious and may not be so stretched so as to give rise to any en-

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

titlement for punitive damages.” IVP reacts to this characterization of its lawsuit by claiming the entire matter reeks of NHL’s conscious and premeditated plan to take advantage of IVP’s known vulnerabilities enabling it to solicit and pirate as many of IVP’s clients as possible.

(10)The tort of intentional interference with prospective business advantage has been described as a relatively unsettled and developing legal phenomenon, the principles of which are still very vague. (*Buckaloo v. Johnson* (1975) 14 Cal.3d 815, 822 [122 Cal.Rptr. 745, 537 P.2d 865]; *Lowell v. Mother’s Cake & Cookie Co.* (1978) 79 Cal.App.3d 13, 17 [144 Cal.Rptr. 664].) It is premised upon the ideal “[e]veryone has the right to establish and conduct a lawful business and is entitled to the protection of organized society, through its courts, whenever that right is unlawfully invaded.” (*Buxbom v. Smith* (1944) 23 Cal.2d 535, 546 [145 Cal.Rptr. 305].) It “imposes liability for improper methods of diverting or taking business from another ... [, which]’ are not within the privilege of fair competition.” (*Baldwin v. Marina City Properties, Inc.* (1978) 79 Cal.App.3d 393, 406 [145 Cal.Rptr. 406].) Consequently, “in order to be actionable the interference with prospective economic advantage or advantageous business *126 relationship must be *unjustified and/or without privilege* The unjustifiability or wrongfulness of the act may consist of the *methods* used *and/or* the *purpose* or motive of the actor [It] will lie where the right to pursue a lawful business is intentionally interfered with either by unlawful means or by means otherwise lawful when there is a lack of sufficient justification [citations].” (*Lowell v. Mother’s Cake & Cookie Co.*, *supra.*, 79 Cal.App.3d at pp. 17-18.) (11)The elements of the tort in our context include (1) the existence of a prospective business relationship advantageous to plaintiff, (2) defendants’ knowledge of the existence of the relationship, (3) defendants’ intentional conduct designed to disrupt the relationship, (4) actual causation, and (5) damages to plaintiff proximately caused by defendants’ conduct. (*Buckaloo v. Johnson*, *supra.*, 14 Cal.3d

at p. 827; *Baldwin v. Marina City Properties, Inc.*, *supra.*, 79 Cal.App.3d at p. 407; see generally, *Top Serv. Body Shop, Inc. v. Allstate Ins. Co.* (1978) 283 Ore. 201 [582 P.2d 1365, 1368-1371]; 4 Witkin, Summary of Cal. Law (8th ed. 1974) Torts, §§ 389-397, pp. 2640-2652.) Simply stated, the marketplace should not be immune from ethics.

(8c)Our review of the record as qualified by the court’s comments at the new trial motion, supports IVP’s contention defendants’ acted tortiously. Draper’s decision to terminate CHL’s contractual relationship with IVP was made between mid-July and the 28th of that month. CHL, wanting to stay in the veterinary business, prepared the necessary veterinary reports and request forms without disclosure to Sodikoff. After preparing the forms and customer lists, Whalley and Lawrence prepared to launch a sales program to assure CHL’s place in the market. Concurrently with Sodikoff’s termination, they held a sales meeting to instruct CHL’s sales personnel, including Dennis Cleveland, the sales manager for CHL, on the method of conducting its concentrated sales campaign directed at soliciting veterinary accounts in San Diego. Whalley gave specific instructions on how to make the contacts with potential clients. Although the sales staff was told to say nothing derogatory about Sodikoff, they were instructed to explain there had been a voluntary disassociation between the parties. They were also told to explain, that because of the elimination of certain services, the veterinarians would receive a price reduction of 10 percent and supplies used to collect specimens would be provided free of charge. If a doctor wished to continue with IVP, CHL could no longer collect or process the work due to the termination of the parties’ relationship. This “sales blitz” of veterinary accounts occurred over a one-week period in which attention was primarily focused on the major accounts CHL identified *127 from IVP billing records. The better accounts were singled out for special emphasis and called upon personally by Whalley, Lawrence or Cleveland. CHL’s express and admitted purpose in these pretermination secret preparations and the im-

116 Cal.App.3d 111, 172 Cal.Rptr. 74
(Cite as: 116 Cal.App.3d 111)

mediate termination without notice to IVP followed immediately by the coordinated one-week "blitz" was to gain a "competitive advantage" over IVP in CHL's effort to "attract" as many of IVP's existing accounts as possible. All this was done at a time when CHL knew the sudden termination of IVP, without notice, and simultaneous denial of any further lab facilities or services to IVP would result in its inability to continue its veterinary pathology business unless it could immediately arrange for equivalent lab services, a task virtually impossible in the position it found itself. Sodikoff's efforts to use stop-gap measures to mitigate his losses were unsuccessful. He ultimately discontinued his business in December 1972.

We think this conduct describes more than a breach of contract. CHL had no justification or privilege to surreptitiously engage in a course of conduct designed to deprive IVP of its business. Granted the trial court apparently did not believe CHL intended to pirate IVP's business, since IVP, as the "shell" of Dr. Sodikoff, rendered a unique personal service of interpretive veterinary analysis which CHL wished to discontinue. We have no quarrel with the court's finding CHL had the right to return to the veterinary testing it had done before the joint venture without the expensive and unprofitable services of Sodikoff. We are concerned not with CHL's right to return to simple veterinary testing, but with its manner of transition. Even bound by the trial court's findings of the joint ownership of the customer lists and forms and that canvassing of the veterinary community was authorized only after the termination of the parties' relationship, one cannot rationalize defendants' conduct as being within the realm of fair competition. This is especially true in light of the parties' contractual relationship and the fiduciary implications of the trial court's finding the parties' relationship constituted a joint venture. Accordingly, putting aside the issue of damages, IVP was the victim of the tort in controversy based upon defendants' conduct viewed as a whole and highlighted by the immediate termination of its relationship with IVP without reasonable

notice with the apparent intent to render IVP unable to either effectively service its existing customers or to successfully resist CHL's preplanned and aggressive solicitation of IVP's customers, ultimately resulting in its functional demise. If the evidence at retrial is similar to that presented here, a reasonable award of punitive damages against NHL and USV may properly be imposed. *128

Disposition

The judgment in favor of Revlon is affirmed. The order granting a new trial in favor of NHL and USV is affirmed. Each party is to bear its own costs on appeal.

Brown (Gerald), P. J., concurred. Staniforth, J., concurred in the result.

A petition for a rehearing was denied March 23, 1981, and appellant's petition for a hearing by the Supreme Court was denied May 13, 1981. *129

Cal.App.4.Dist.
Institute of Veterinary Pathology, Inc. v. California Health Laboratories, Inc.
116 Cal.App.3d 111, 172 Cal.Rptr. 74

END OF DOCUMENT



**GRADY JACKSON and KELLEY ALEXANDER, Plaintiffs, v. BALANCED
HEALTH PRODUCTS, INC., et al., Defendants.**

No. C 08-05584 CW

**UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF
CALIFORNIA**

2009 U.S. Dist. LEXIS 48848

June 10, 2009, Decided

June 10, 2009, Filed

COUNSEL: [*1] For Grady Jackson, Plaintiff: Andrew A. August, Eric J. Farber, John Laurence Fitzgerald, LEAD ATTORNEYS, Pinnacle Law Group, LLP, San Francisco, CA; Adam Paul Brezine, Esq., Holme Roberts & Owen, San Francisco, CA.

For Kelley Alexander, Plaintiff: Eric J. Farber, LEAD ATTORNEY, Andrew A. August, Kevin Francis Rooney, Pinnacle Law Group LLP, San Francisco, CA.

For Balanced Health Products, Inc., a Delaware Corporation, Nikki Haskell, Defendants: David Laurence Gernsbacher, LEAD ATTORNEY, Attorney at Law, Beverly Hills, CA; Adam Paul Brezine, Esq., Holme Roberts & Owen, San Francisco, CA; Roger Rex Myers, Holme Roberts & Owen LLP, San Francisco, CA.

For General Nutrition Corporation, a Pennsylvania Corporation, Defendant: Leslie Mark Werlin, Sidney K. Kanazawa, LEAD ATTORNEYS, McGuireWoods LLP, Los Angeles, CA; Adam Paul Brezine, Esq., Holme Roberts & Owen, San Francisco, CA; Gordon W. Schmidt, Kevin Batik, PRO HAC VICE, McGuireWoods LLP, Pittsburgh, PA; Roger Rex Myers, Holme Roberts & Owen LLP, San Francisco, CA.

For General Nutrition Centers, Inc., a Pennsylvania Corporation, Defendant: Leslie Mark Werlin, Sidney K. Kanazawa, LEAD ATTORNEYS, McGuireWoods LLP, Los Angeles, CA; Adam Paul [*2] Brezine, Esq., Holme

Roberts & Owen, San Francisco, CA; Gordon W. Schmidt, Kevin Batik, PRO HAC VICE, McGuireWoods LLP, Pittsburgh, PA.

For Vitamin Shoppe Industries, Inc., a New York Corporation, Defendant: Roger Rex Myers, LEAD ATTORNEY, Katherine Anne Keating, Holme Roberts & Owen LLP, San Francisco, CA; Adam Paul Brezine, Esq., Holme Roberts & Owen, San Francisco, CA.

JUDGES: CLAUDIA WILKEN, United States District Judge.

OPINION BY: CLAUDIA WILKEN

OPINION

ORDER GRANTING IN PART DEFENDANTS' MOTIONS TO DISMISS

Plaintiffs Grady Jackson and Kelley Alexander bring a consumer class action under the Class Action Fairness Act of 2005. Dietary supplement retailer Defendants Vitamin Shoppe Industries, Inc. (VS) and General Nutrition Corporation (GNC) move to dismiss Plaintiffs' complaint. Defendants Balanced Health Products (BHP) and Nikki Haskell join in that motion. Nikki Haskell filed a separate motion to dismiss. Plaintiffs oppose the motions. The matter was heard on June 4, 2009. Having considered oral argument and all of the papers filed by

the parties, the Court grants in part Defendants' motions.

BACKGROUND ¹

¹ All facts are taken from Plaintiffs' FAC and are assumed to be true for purposes of this motion.

This case [³] centers around StarCaps, a dietary supplement manufactured by Defendant BHP and its principal, Defendant Nikki Haskell. Approximately twenty-five years ago, Nikki Haskell developed StarCaps and promoted it as an "all natural" over the counter diet pill that contained garlic and papaya extract as its main active ingredients." First Amended Complaint (FAC) P 26. Attached to each bottle is a pamphlet, which contains the following representation:

This all natural dietary supplement detoxes your system by metabolizing protein and eliminating bloat. It's safe, fast and effective, and it contains no ephedra. Lose between 10 and 125 pounds and keep it off! StarCaps are available at GNC, Great Earth and the Vitamin Shoppe.

Id. at P 34.

In the November/December 2007 issue of The Journal of Analytical Toxicology, an article entitled, "Detection of Bumetanide in an Over-the-Counter Supplement," reported that StarCaps contain a powerful diuretic called Bumetanide. ² The report described a study performed by the Center for Human Toxicology at the University of Utah. The Center purchased bottles of StarCaps and tested the pills through a high performance liquid chromatography, which revealed that all [⁴] pills contained equal amounts of Bumetanide at near therapeutic doses. The article also implied that the uniformity of Bumetanide in StarCaps indicated that inclusion of the drug in the pill was intentional.

² Bumetanide is available to consumers by prescription only.

Bumetanide is considered a banned substance by the National Football League (NFL). Although it is prescribed for the treatment of edema associated with congestive heart failure and hepatic and renal disease, Bumetanide can also mask steroid use. Plaintiff Grady Jackson is a professional football player and is subject to the drug testing regime of the NFL. ³ Jackson began

taking StarCaps in March, 2008 to help him lose weight in preparation for the upcoming football season. Later in the summer, Jackson tested positive for the drug and was suspended for four games. Jackson is currently appealing that suspension. After reports of Jackson's positive drug test became public, BHP issued a statement on StarCaps.com that it had temporarily suspended shipment of StarCaps to its retailers. However, the retailers continued to sell StarCaps until BHP issued a voluntary recall of the product.

³ The other named Plaintiff, Kelley Alexander, [⁵] is not a professional football player. Alexander is a California resident who purchased StarCaps for over four years because it was represented to be an all natural dietary supplement.

Defendants GNC and Vitamin Shoppe sell StarCaps. GNC is the world's largest retailer of the nutritional supplement products, operating over 4800 locations around the world. GNC claims to have quality control centers that monitor products received from vendors to ensure quality standards. The Vitamin Shoppe owns and operates more than 400 retail locations around the country. It claims to protect its customers by having quality control operating procedures to review vendors of third party products for their track records on quality, efficacy and safety.

Plaintiffs assert seven claims under California law, each based on selling and marketing the prescription drug Bumetanide in StarCaps: (1) unfair competition under *Business & Professions Code § 17200*, (2) false advertising under *Business & Professions Code § 17500*, (3) unjust enrichment, (4) breach of express and implied warranty, (5) strict product liability, (6) violation of the Sherman Law and (7) negligence.

LEGAL STANDARD

I. Motion to Dismiss for Failure [⁶] to State a Claim

A complaint must contain a "short and plain statement of the claim showing that the pleader is entitled to relief." *Fed. R. Civ. P. 8(a)*. Dismissal under *Rule 12(b)(6)* is appropriate if the complaint does not give the defendant fair notice of a legally cognizable claim and the grounds on which it rests. *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 555, 127 S. Ct. 1955, 167 L. Ed. 2d 929 (2007). In considering whether the complaint is

sufficient to state a claim, the court will take all material allegations as true and construe them in the light most favorable to the plaintiff. *NL Indus., Inc. v. Kaplan*, 792 F.2d 896, 898 (9th Cir. 1986).

When granting a motion to dismiss, the court is generally required to grant the plaintiff leave to amend, even if no request to amend the pleading was made, unless amendment would be futile. *Cook, Perkiss & Liehe, Inc. v. N. Cal. Collection Serv. Inc.*, 911 F.2d 242, 246-47 (9th Cir. 1990). In determining whether amendment would be futile, the court examines whether the complaint could be amended to cure the defect requiring dismissal "without contradicting any of the allegations of [the] original complaint." *Reddy v. Litton Indus., Inc.*, 912 F.2d 291, 296 (9th Cir. 1990). [*7] Leave to amend should be liberally granted, but an amended complaint cannot allege facts inconsistent with the challenged pleading. *Id.* at 296-97.

DISCUSSION

I. Pre-emption by the Federal Food, Drug and Cosmetic Act

Though this case is about a dietary supplement,⁴ the Court begins its discussion by noting the important recent United States Supreme Court decision on pre-emption, prescription drugs and the Food, Drug and Cosmetic Act in *Wyeth v. Levine*, 129 S. Ct. 1187, 173 L. Ed. 2d 51 (2009). The Court held that a failure-to-warn state law claim for lack of an adequate warning on a prescription label, even though the label had been approved by the Food and Drug Administration (FDA), was not pre-empted by the FDCA. The Court noted that Congress did not provide a federal remedy for consumers harmed by unsafe or ineffective drugs when it passed the FDCA in 1938 because "widely available state rights of action provided appropriate relief for injured consumers." *Id.* at 1199. The Court continued, "If Congress thought state-law posed an obstacle to its objectives, it surely would have enacted an express pre-emption provision at some point during the FDCA's 70-year history. But despite its 1976 enactment of an [*8] express pre-emption provision for medical devices . . . Congress has not enacted such a provision for prescription drugs." *Id.* at 1200.

4 The term "dietary supplement" is defined as "a product (other than tobacco) intended to supplement the diet that bears or contains one or

more of the following dietary ingredients: (A) a vitamin; (B) a mineral; (C) an herb or other botanical; (D) an amino acid; (E) a dietary substance for use by man to supplement the diet by increasing the total dietary intake; or (F) a concentrate, metabolite, constituent, extract, or combination of any ingredient described in clause (A), (B), (C), (D), or (E)." 21 U.S.C. § 321 (ff).

Thus, there is no express pre-emption of cases involving false advertising of dietary supplements in federal law under the FDCA. No federal statute or regulation states that the field of allegedly false advertising of dietary supplements is exclusively the province of federal law. However, the FDCA, which grants the FDA authority to oversee the safety of drugs, provides that "all such proceedings for the enforcement, or to restrain violations, of [the FDCA] shall be by and in the name of the United States." 21 U.S.C. § 337(a). "Courts [*9] have generally interpreted this provision to mean that no private right of action exists to redress alleged violations of the FDCA." *Summit Tech., Inc. v. High-Line Med. Instruments Co., Inc.*, 922 F. Supp. 299, 305 (C.D. Cal. 1996) (internal citations omitted). Instead, "the right to enforce the provisions of the FDCA lies exclusively within the federal government's domain, by way of either the FDA or the Department of Justice." *Id.*

Defendants assert that Plaintiffs' suit is an attempt to bring a private cause of action for violations of the FDCA and, as such, is precluded. Defendants cite many sections of the FDCA and argue that Plaintiffs' complaint is essentially an assertion that those sections are being violated. For instance, Defendants argue that the premise of Plaintiffs' complaint is that Defendants sold a misbranded product as a dietary supplement while knowing it contained a drug that could be sold by prescription only, and sold it without the disclosure required by the FDCA. 21 U.S.C. §§ 301-397. Dispensing a prescription drug without a proper prescription is "deemed to be an act which results in the drug being misbranded," 21 U.S.C. § 353(b)(1)(B), and selling misbranded [*10] drugs is a violation of the FDCA. *Id.* § 331. It is also a violation to sell a prescription drug without the proper FDA-approved label. 21 U.S.C. § 352; 21 C.F.R. § 201.50-201.57.⁵

5 It is important to note that, in contrast to the FDCA's regulation of prescription drugs, the DSHEA exempts dietary supplements from FDA

premarket approval. 21 U.S.C. § 343(r)(6) (exempting claims as to how a nutrient affects the structure or function of the body from FDA pre-market approval process).

Defendants rely on *Fraker v. KFC Corp.*, 2007 U.S. Dist. LEXIS 32041 (S.D. Cal. 2007). In *Fraker*, a plaintiff brought a putative class action against fast food chain KFC, alleging that KFC's advertising was misleading because its food was high in trans-fat content. Fraker directly brought FDCA claims against the defendant and the court concluded, "To the extent plaintiff contends that alleged violations of the FDCA and Sherman Law give rise to viable state law claims, such claims are impliedly preempted by the FDCA." *Id.* at *11. *Fraker* is distinguishable because, in the present case, Plaintiffs have not brought claims directly under the FDCA.

Defendants also rely on *In re Epogen & Aranesp Off-Label Mkt'g & Sales Practice Litig.*, 590 F. Supp. 2d 1282 (C.D. Cal. 2008). [*11] There, the plaintiffs brought RICO and state law claims for violations of §§ 17200 and 17500 for the defendants' alleged promotion of a prescription drug for "off-label use," which is prohibited under 21 C.F.R. § 202.1(e)(6). The court concluded that the plaintiffs' "allegations of off-label promotion are, in essence, misbranding claims that should be reviewed by the FDA." *Id.* at 1289. However, the court noted,

The existence of the FDCA does not completely preclude injured parties from asserting claims of fraud or false advertising. Other legislation, state and federal remains in effect to protect consumers from false and deceptive prescription drug advertising. The FDCA is not focused on the truth or falsity of advertising claims, but is instead directed to protect the public by ensuring that drugs sold in the marketplace are safe, effective and not misbranded, a task vested in the FDA to implement and enforce.

Id. at 1290 (internal citations omitted). The court concluded that "to the extent that Plaintiffs have alleged that Defendants made statements that were fraudulent (i.e., literally false, misleading, or omitted material facts), their claims are actionable. It is of no matter [*12] that the deceptive statements may have been made in order to

promote off-label uses of EPO." *Id.* at 1291. (internal citation omitted).

In the present case, Plaintiffs' claims are based on false and misleading advertising and mislabeling under the Sherman Law. Plaintiffs allege that the inclusion of Bumetanide in StarCaps renders Defendants' advertising of the product as "all natural" false and misleading. Simply alleging that StarCaps contains a prescription drug, Bumetanide, does not invoke federal pre-emption. Thus, Defendants' actions give rise to valid state law claims.

II. Uniform Single Publication Act

Defendants argue that the Uniform Single Publication Act (USPA), also known as the single publication rule, precludes Plaintiffs from asserting their second (false advertising), fourth (breach of warranty) and sixth (Sherman Law) causes of action. Defendants also argue that Plaintiffs' third (unjust enrichment), fifth (strict product liability) and seventh (negligence) causes of action should be dismissed to the extent that they rely on the same alleged mis-statement as the first cause of action.

The Uniform Single Publication Act provides:

No person shall have more than one cause of [*13] action for damages for libel or slander or invasion of privacy or any other tort founded upon any single publication or exhibition or utterance, such as one issue of a newspaper or book or magazine or any one presentation to an audience or any one broadcast over radio or television or any one exhibition of a motion picture. Recovery in any action shall include all damages for any such tort suffered by the plaintiff in all jurisdictions.

Cal. Civ. Code § 3425.3.

The law was originally directed at mass communications, such as newspapers, books, magazines, radio and television broadcasts, and speeches to an audience. When the offending language is read or heard by a large audience, the rule limits a plaintiff to a single cause of action for each mass communication.

The parties dispute whether advertisements and

product labels constitute a "publication or exhibition or utterance." The only California court to discuss this issue directly concluded that the use of the same image on various advertisements may constitute a single publication, exhibition or utterance. *Christoff v. Nestle USA*, 152 Cal. App. 4th 1439, 1461-62, 62 Cal. Rptr. 3d 122 (2007). However, the California Supreme Court granted review of that decision [*14] in October, 2007, and the case has not been decided yet. Therefore, the appellate decision may no longer be cited as precedent. Nevertheless, StarCap advertisements and labels, like publications, exhibitions and utterances, are communicative acts and, as such, the Court concludes that they are included in the statute. Further, the phrase "such as" in the statute indicates that the enumerated list of media is not exclusive but exemplary. Thus, the single publication rule is not limited to newspapers, books, magazines, radio, television and movies, and it has even been applied to the internet. *Traditional Cat Assn., Inc. v. Gilbreath*, 118 Cal. App. 4th 392, 394, 13 Cal. Rptr. 3d 353 (2004).

The parties also dispute whether Plaintiffs can maintain more than one cause of action for Defendants' alleged misstatements. "In cases where essentially one harm has been alleged, the courts have interpreted the single-publication rule to mean that a plaintiff may have only one cause of action for one publication rather than multiple causes of action for torts such as defamation, invasion of privacy, personal injury, civil rights violations, or fraud and deceit." *M.G. v. Time Warner*, 89 Cal. App. 4th 623, 629, 107 Cal. Rptr. 2d 504 (2001). In [*15] *M.G.*, a magazine and cable television station used a photograph of a Little League team to illustrate stories about adult coaches who sexually molest youths playing sports. The plaintiffs' first four causes of action were all for invasion of privacy on various theories of liability: misappropriation of identity, public disclosure of private facts, intrusion, and false light. Though these were plead as separate causes of action, the court concluded that it was proper to treat them as one cause of action "expressing four different theories." *Id.* at 630.

Here, it is not necessary to treat Plaintiffs' separate claims as one cause of action expressing different tort theories. The second (false advertising), third (unjust enrichment) and fourth (breach of warranty) causes of action are not traditional torts as contemplated by the phrase "or any other tort" in § 3425.3. Defendants do not cite any binding authority for the proposition that those

causes of action are subject to the statute. Therefore, the Court will not dismiss these causes of action under the single publication rule. The Court need not address whether Plaintiffs' fifth (strict product liability), sixth (Sherman Law) and seventh [*16] (negligence) causes of action should be dismissed under the single publication rule because those causes of action are dismissed on other grounds described below.

III. Economic Loss Rule

The economic loss rule provides that

recovery under the doctrine of strict liability is limited to physical harm to person or property. Damages available under strict products liability do not include economic loss, which includes damages for inadequate value, costs of repair and replacement of the defective product or consequent loss of profits -- without any claim of personal injury or damages to other property.

Jimenez v. Superior Court, 29 Cal. 4th 473, 482, 127 Cal. Rptr. 2d 614, 58 P.3d 450 (2002) (internal citations and quotations omitted). Similarly, economic losses are generally not allowed for negligence claims without any claim of personal injury or damages to other property. *Seely v. White Motor Co.*, 63 Cal. 2d 9, 18, 45 Cal. Rptr. 17, 403 P.2d 145 (1965).

Plaintiffs argue that Defendants' breach of contract violated a social policy such that purely economic losses should be allowed. Plaintiffs rely on *Robinson v. Dana Corp.*, 34 Cal. 4th 979, 22 Cal. Rptr. 3d 352, 102 P.3d 268 (2004). In that case, the California Supreme Court decided "whether the economic loss rule . . . applies to claims for [*17] intentional misrepresentation or fraud in the performance of a contract." *Id.* at 984. The court held that the "economic loss rule does not bar Robinson's fraud and intentional misrepresentation claims because they were independent of [the] breach of contract." *Id.* at 991. The court noted that "a party to a contract cannot rationally calculate the possibility that the other party will deliberately misrepresent terms critical to that contract." *Id.* at 993. Notably, the court focused on the plaintiff's intentional tort claims and did not state that its decision applied to negligence or strict liability claims. Therefore, *Robinson* is inapposite and the economic loss rule

precludes Plaintiffs' claims for strict liability and negligence. Thus, the fifth and seventh causes of action are dismissed.

IV. Private Right of Action Under the Sherman Law

Plaintiffs' sixth cause of action is brought directly under

the Sherman Law. The Court dismisses this cause of action because "no private right of action exists to enforce" the Sherman Law. *Summit*, 922 F. Supp. at 317. Plaintiffs may assert their Sherman Law violation under *Business & Professions Code § 17200*.

V. Alter Ego

Plaintiffs assert claims against [*18] Defendant Nikki Haskell, the sole owner of BHP. Before the alter ego doctrine may be invoked, two elements must be alleged: "First, there must be such a unity of interest and ownership between the corporation and its equitable owner that the separate personalities of the corporation and the shareholder do not in reality exist. Second, there must be an inequitable result if the acts in question are treated as those of the corporation alone." *Sonora Diamond Corp. v. Superior Court*, 83 Cal. App. 4th 523, 526, 99 Cal. Rptr. 2d 824 (2000). Here, Plaintiffs tersely allege that Haskell is "the alter ego of BHP." FAC P 9. This allegation fails to state a claim for alter ego liability. "Conclusory allegations of 'alter ego' status are

insufficient to state a claim. Rather, a plaintiff must allege specifically both of the elements of alter ego liability, as well as facts supporting each." *Neilson v. Union Bank of Cal., N.A.*, 290 F. Supp. 2d 1101, 1116 (C.D. Cal. 2003). Therefore, the Court dismisses Plaintiffs' FAC against Defendant Haskell, with leave to amend.

CONCLUSION

For the foregoing reasons, the Court dismisses with leave to amend all causes of action as they pertain to Defendant Haskell. As to the remaining [*19] Defendants, the Court dismisses without leave to amend Plaintiffs' fifth, sixth and seventh causes of action. If Plaintiffs wish to file an amended complaint as allowed by this order, they must do so within twenty days from the date of this order. Defendants BHP, VS and GNC must answer the complaint with respect to the first through fourth causes of action within thirty days from the date of this order.

IT IS SO ORDERED.

Dated: 6/10/09

/s/ Claudia Wilken

CLAUDIA WILKEN

United States District Judge

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
 (Cite as: 235 Cal.App.3d 1220)

▷ LAS PALMAS ASSOCIATES et al., Plaintiffs,
 Cross-defendants and Appellants,
 v.
 LAS PALMAS CENTER ASSOCIATES et al., De-
 fendants, Cross-complainants and Respondents.

No. B051688.

Court of Appeal, Second District, Division 2, Cali-
 fornia.
 Nov 5, 1991.

SUMMARY

On a cross-complaint by the buyers of a shopping center against the sellers, alleging fraud in their promise to guarantee certain leases without any intention to honor the guaranties, the jury rendered verdicts awarding the buyers \$232,393 for breach of contract, \$1.27 million for fraud, and \$10 million in punitive damages. In a separate trial, the trial court, sitting without a jury, denied the sellers declaratory relief. (Superior Court of Los Angeles County, No. C575906, Arthur Baldonado, Judge.)

The Court of Appeal modified the judgment to reduce the award of fraud damages and punitive damages, and remanded for a determination of attorney fees. The court held that the evidence was sufficient to support a fraud verdict based on the sellers' guaranty of two tenant leases without an intent to honor them. The sellers had maintained that one guaranty had terminated because the buyers unreasonably withheld their approval of new tenants, but then changed their position and asserted the guaranty had ended because the tenant remained current with its rent for three consecutive months, despite the guaranteeing corporation's having served the tenant with notices to quit for nonpayment of rent during the months in question. During that time, the sellers also began to dismantle the guaranteeing corporation, asserted the buyers' eviction of one tenant had terminated the lease guaranty, despite the sellers having encouraged the buy-

ers to evict, and engaged in other conduct seeking to nullify the guaranties. The court also held that although punitive damages may not ordinarily be given for breach of contract, whether the breach is intentional, willful or in bad faith, such damages may be awarded where a defendant fraudulently induces the plaintiff to enter into a contract. The court further held that the punitive damage award of \$10 million was not supported by substantial evidence in the light of the reduction on appeal of the compensatory damage award from \$1.27 million to \$232,393. Under these circumstances, a \$10 million award would be grossly disproportionate both in comparison to the buyers' compensatory losses and the gravity of the sellers' conduct. The ends of justice and judicial economy required the punitive damage award to be limited to \$2 million, which generally preserved the jury's initial ratio between compensatory and punitive damages. (Opinion by Nott, J., with Gates, Acting P. J., and Fukuto, J., concurring.)

HEADNOTES

Classified to California Digest of Official Reports
 (1a, 1b) Real Estate Sales § 29--Fraud--Actions and
 Proceedings-- Evidence--Sufficiency--Shopping
 Center--Lease Guaranties.

In an action by the buyers of a shopping center against the sellers, the evidence was sufficient to support a fraud verdict based on the sellers' guaranty of two tenant leases without an intent to honor them. The sellers had maintained that one guaranty had terminated because the buyers unreasonably withheld their approval of new tenants, but then changed their position and asserted the guaranty had ended because the tenant remained current with its rent for three consecutive months, despite the guaranteeing corporation's having served the tenant with notices to quit for nonpayment of rent during the months in question. During that time, the sellers also began to dismantle the guaranteeing corporation; asserted the buyers' eviction of one tenant had terminated the lease guaranty, despite the sellers

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

having encouraged the buyers to evict; and engaged in other conduct seeking to nullify the guaranties.

(2a, 2b) Fraud and Deceit § 7--Actual Fraud--False Representations-- Promises.

Civ. Code, § 1710, subd. 4, defines fraud as the making of a promise done without any intention of performing the obligation. A promise to do something necessarily implies the intention to perform, and, where such an intention is absent, there is an implied misrepresentation of fact, which is actionable fraud. The subsequent conduct of a defendant, such as his failure to immediately carry out his pledge, has some evidentiary value to show that the defendant made the promise without the intent to keep the obligation. However, something more than nonperformance is required to prove the intent not to perform the promise.

(3) Damages § 22.2--Exemplary or Punitive Damages--Availability--Fraudulent Inducement of Contract.

Although punitive damages may not ordinarily be given for breach of contract, whether the breach is intentional, willful or in bad faith, such damages may be awarded where a defendant fraudulently induces the plaintiff to enter into a contract. The words "oppression, fraud, or malice" in Civ. Code, § 3294, being in the disjunctive, fraud alone is an adequate basis for awarding punitive damages.

(4) Real Estate Sales § 31--Fraud--Actions and Proceedings--Appeal--Scope of Review.

On appeal of a judgment finding the sellers of a shopping center guilty of fraud, the appellate court's power of review commenced and ceased with the location of any substantial evidence, contradicted or uncontradicted, that would support the determination. The reviewing court cannot limit its review of the record to the evidence cited by the respondent, but must consider the entire record in determining whether the judgment is supported by sufficient evidence. Evidence is substantial if it is reasonable in nature, credible, and of solid value. Moreover, the testimony of a single witness is sufficient to satisfy the test of the substantial evidence

rule.

(5a, 5b) Damages § 22.4--Exemplary or Punitive Damages--Relation to Defendant's Wealth--Evidence--Exclusion Prior to Determination of Liability-- Waiver.

In an action by the buyers of a shopping center against the sellers for fraud, the trial court did not abuse its discretion in denying the sellers' motion to exclude evidence of their wealth from the jury until it found them liable for fraud, where the sellers withheld the motion until the buyers were to begin the presentation of their case, with an out-of-town witness standing by to testify. Moreover, the sellers waited until after the buyers had already told the jury twice in opening argument that the sellers' parent corporation was a billion dollar company, cross-examined a witness on the subject of that company's wealth, and made a motion to compel production of the sellers' financial records. Although Civ. Code, § 3295, subd. (d), provides the court "shall" on application of a defendant preclude the admission of evidence of a defendant's wealth until after a requisite verdict, the mandatory effect of the statute may be lost by a defendant who fails to act promptly to preserve its protection. Significantly, the trial court could have found that to grant the motion in the midst of trial would have been prejudicial to the buyers.

(6) Damages § 30--Evidence--Admissibility--Defendant's Wealth--Statutory Prohibition--Waiver.

Civ. Code, § 3295, subd. (d), providing the court shall on application of any defendant preclude the admission of a defendant's wealth until the requisite liability verdict has been returned, is a codification of the presumption that evidence of a defendant's wealth can induce fact finders to abandon their objectivity and return a verdict based on passion and prejudice. It is not true that the only deadline imposed by the statute is that the motion be made before the trier of fact delivers a verdict finding a defendant liable for acts worthy of assessing punitive damages. It is manifest that a party may be

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

estopped from claiming a statutory right if untimely asserted. A request under Civ. Code, § 3295, subd. (d), is essentially a motion in limine, and ordinarily should be made before trial.

[See 3 **Witkin**, Cal. Evidence (3d ed. 1986) § 2011.]

(7a, 7b) Trial § 29--Argument and Conduct of Counsel--Scope of Arguments--Defendant's Wealth--Fraud and Punitive Damages Action.

In an action by the buyers of a shopping center against the sellers for fraud, in which punitive damages were sought and defendants failed to timely move to exclude evidence of their wealth (Civ. Code, § 3295, subd. (d)), the references to the sellers' wealth in closing argument did not impermissibly sway the jury to render verdicts against the sellers. The purpose behind the exemplary damages statute (Civ. Code, § 3294) is to punish and deter a defendant for wrongful conduct, and evidence of the sellers' wealth was relevant not only to guide the jury in its assessment of the proper amount of punitive damages to award, but also as proof that the sellers intended to oppress the buyers into submission. Moreover, substantial evidence supported the jury's determination that an award of punitive damages was proper because the buyers met their burden of proving fraud by clear and convincing evidence. Viewed under these principles, it could not be said the buyers' counsel strayed beyond the bounds of his right to fairly comment on the state of the evidence.

(8) Damages § 30--Evidence--Admissibility--Defendant's Wealth.

Where liability and punitive damages are tried in a single proceeding, evidence of a defendant's wealth is admissible. While in an ordinary action for damages, information regarding the adversary's financial status is inadmissible, this is not so in an action for punitive damages. In such a case evidence of a defendant's financial condition is admissible for the purpose of determining the amount that it is proper to award. The relevancy of such evidence lies in the fact that punitive damages are not awarded for the purpose of rewarding the plaintiff,

but to punish the defendant. Obviously, the trier of fact cannot measure the "punishment" without knowledge of defendant's ability to respond to a given award.

(9a, 9b) Trial § 29--Argument and Conduct of Counsel--Scope of Arguments--Accusation of Misrepresentation and Concealment.

In an action by the buyers of a shopping center against the sellers, alleging fraud in their promise to guarantee certain leases without any intention to honor the guaranties, there was no misconduct in the suggestion by the buyers' counsel that the sellers made misrepresentations and attempted to conceal evidence, where the remarks were supported by the evidence. Although the buyers' counsel personalized the argument he did not exceed his right to comment on the state of the evidence, as the facts and the way they were portrayed to the jury represented highly relevant circumstantial evidence of whether the sellers ever intended to honor the lease guaranties. The buyers' counsel also had the right under the facts to comment on why the sellers suddenly attempted to suppress the testimony of one of their scheduled witnesses.

[See **Cal.Jur.3d**, Trial, § 40 et seq.; 7 **Witkin**, Cal. Procedure (3d ed. 1985) Trial, § 206 et seq.]

(10) Trial § 21--Argument and Conduct of Counsel--Personal Attacks.

Personal attacks by an attorney on opposing parties and their attorneys, whether outright or by insinuation, constitute misconduct. Such behavior only serves to inflame the passion and prejudice of the jury, distracting them from fulfilling their solemn oath to render a verdict based solely on the evidence submitted at trial. Lack of civility between counsel also breeds public disrespect for the judicial process.

(11) Trial § 28--Argument and Conduct of Counsel--Closing Arguments-- Evidence.

While trial counsel is entitled to argue his or her interpretation of the evidence to the jury, counsel has no right to cite facts unsupported by the evidence.

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

(12) Trial § 30--Argument and Conduct of Counsel--Objection, Cure, and Waiver.

A party is foreclosed from complaining on appeal of misconduct during arguments to the jury where counsel allowed the alleged improprieties to accumulate without objection, and simply made a motion for a mistrial at the conclusion of the argument. The ultimate determination of the issue of attorney misconduct rests on the appellate court's view of the overall record, taking into account such factors as the nature and seriousness of the remarks and misconduct, the general atmosphere, including the judge's control, of the trial, the likelihood of prejudicing the jury, and the efficacy of objection or admonition under all the circumstances. Another factor is the strength of the offending attorney's case. Accordingly, in an action by the buyers of a shopping center against the sellers, alleging fraud in their promise to guarantee certain leases without any intention to honor the guaranties, in which there was substantial evidence of the sellers' fraud, argument by the buyers' counsel intimating the sellers could influence judges in the county through political contributions made by the sellers' attorneys, a suggestion the buyers might donate the punitive damages to charity, and the insinuation that the sellers' attorneys were "whores" who would lie in court for their clients, constituted misconduct. However, the offending remarks had an innocuous effect on the jury's overall conclusion that the sellers had committed a tortious act in view of the substantial evidence of the sellers' fraud and the trial court's admonition to the jury to disregard the statements.

(13a, 13b) Corporations § 4--Disregard of Corporate Entity--When Power Will or Will Not Be Exercised.

In an action by the buyers of a shopping center against the sellers, alleging fraud in their promise to guarantee certain leases without any intention to honor the guaranties, the evidence supported the trial court's finding that one defendant, a wholly owned subsidiary, was the alter ego of defendant parent corporation, where substantial evidence sup-

ported the conclusion that the two entities formed a single enterprise for the purpose of committing a continuing fraud against the buyers. Certain guaranties of the subsidiary's debt by the parent indicated that the subsidiary's survivability as a developer was intertwined with its dependence on the parent, the corporations had two common directors, and when the subsidiary's board of directors fired the corporation's executives and staff, the parent used its employees, including its corporate counsel, to continue to manage what remained of the business. The parent actively participated in the sale of the shopping center from the beginning to the end, negating the argument that the parent was named a defendant only to increase the funds available for a punitive damage award.

(14) Corporations § 3--Disregard of Corporate Entity--General Principles.

It is the general rule that the conditions under which a corporate entity may be disregarded vary according to the circumstances of each case. Whether the corporate veil should be ignored is primarily a question of fact that should not be disturbed when supported by substantial evidence. Because society recognizes the benefits of allowing persons and organizations to limit their business risks through incorporation, sound public policy dictates that imposition of alter ego liability be approached with caution. Nevertheless, it is unjust to permit those who control companies to treat them as single or unitary enterprises and then assert their corporate separateness in order to commit frauds and other misdeeds with impunity. Although alter ego liability is generally reserved for the parent-subsidiary relationship, under the single-enterprise rule, liability can be found between sister companies.

(15) Damages § 17--Excessive and Inadequate Damages--Excessive Awards.

Although the law commits the responsibility for determining the amount of damages suffered by a plaintiff to the jury, its decision cannot be allowed to stand where the award as a matter of law

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

is excessive, or is so grossly disproportionate as to raise a presumption that the panel based its result on passion or prejudice.

(16) Real Estate Sales § 30--Fraud--Actions and Proceedings--Trial and Damages.

To recover damages for fraud, a plaintiff must have sustained damages proximately caused by the misrepresentation, and a damage award for an injury not related to the misrepresentation will be reversed. For fraud arising out of the purchase, sale, or exchange of property, Civ. Code, § 3343, provides for "out-of-pocket" damages. Accordingly, in an action by the buyers of a shopping center against the sellers, alleging fraud in their promise to guarantee certain leases without any intention to honor the guaranties, the difference in the shopping center's appraised value and what the buyers paid for it was not the proper measure of damages, where the sellers did not misrepresent the value of the shopping center, but acted fraudulently in guaranteeing two tenant leases without any intent to honor the obligations. With those rents included in the appraisal, any diminution in the property's value had to arise separate and apart from the fraudulent acts of the sellers, and the appraisal therefore only demonstrated the buyers overpaid for the shopping center by misjudging its worth. The damages resulting from the sellers' fraud were therefore limited to the diminished value of the lease guaranties.

(17a, 17b) Damages § 27--Exemplary or Punitive Damages--Review--Relation to Compensatory Damages.

In an action by the buyers of a shopping center against the sellers, alleging fraud in their promise to guarantee certain leases without any intention to honor the guaranties, a punitive damage award of \$10 million was not supported by substantial evidence in light of the reduction on appeal of the compensatory damage award from \$1.27 million to \$232,393. Under these circumstances, a \$10 million award would be grossly disproportionate both in comparison to the buyers' compensatory losses and the gravity of the sellers' conduct. The ends of

justice and judicial economy required the punitive damage award to be limited to \$2 million, which generally preserved the jury's initial ratio between compensatory and punitive damages.

(18) Damages § 22--Exemplary or Punitive Damages--Purpose.

The public policy behind punitive damages is to prevent future misdeeds by punishing the wrongdoer and making an example out of him or her for others to follow. The most important question on appeal is whether the amount of the punitive damages will have a deterrent effect without being excessive.

(19a, 19b) Damages § 26--Exemplary or Punitive Damages--Province and Discretion of Court and Jury.

In an action by the buyers of a shopping center against the sellers, alleging fraud in their promise to guarantee certain leases without any intention to honor the guaranties, the jury was not given inadequate guidelines to award punitive damages. It was instructed that an award of punitive damages was discretionary, and could only be made if they found the sellers guilty of oppression, fraud, or malice. It was also informed that punitive damages are awarded for the sake of example and by way of punishment. The jury was further instructed to consider the reprehensibility of defendants' conduct, the amount of punitive damages that would have a deterrent effect in light of defendants' financial condition, and that they must bear a reasonable relation to the injury suffered by the buyers (BAJI No. 14.71). Also, the "passion and prejudice" standard of post-trial and appellate review affords the sellers an additional safeguard to ensure that the award did not exceed an amount that would accomplish the goal of punishment and deterrence.

(20) New Trial § 107--Procedure--Appeal--Determination and Disposition.

On a motion for a new trial, the trial court sits in its role as an independent trier of fact and may disbelieve witnesses, reweigh evidence and draw

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
 (Cite as: 235 Cal.App.3d 1220)

reasonable inferences that are contrary to those drawn by the jury. Although the trial court's denial of a motion for new trial as to punitive damages should be given deference, an appellate court has the responsibility to intervene when the verdict is so palpably excessive as to raise the presumption of passion and prejudice. Appellate courts must scrutinize punitive damage verdicts because they constitute a windfall, create the anomaly of excessive compensation, and are therefore not favored in the law.

(21) Costs § 26--Attorney Fees--Contract Provisions--Fees Allowed-- Declaratory Relief Action.

In a declaratory relief action by the sellers of a shopping center against the buyers for a judicial determination that they had no liability to the buyers due to the occurrence of events contemplated by lease guaranties, in which action the buyers cross-complained against the sellers for fraud, the prevailing buyers were entitled to recover attorney fees incurred in the defense of the declaratory relief action even though they were barred from collecting contractual attorney fees in the fraud action. The declaratory relief action was "an action on the contract" within the meaning of Civ. Code, § 1717, subd. (a).

COUNSEL

Kaye, Scholer, Fierman, Hays & Handler, Pierce O'Donnell, Roger Furman, Hoon Chun, Irell & Manella, Steven L. Sloca, William M. Hensley and Patricia A. Hubbard for Plaintiffs, Cross-defendants and Appellants.

Terry M. Giles, Alton G. Burkhalter and Sean A. Davitt for Defendants, Cross-complainants and Respondents.

NOTT, J.

This lengthy and acrimonious litigation involves the sale of the Rancho Las Palmas Shopping Center, a 165,472-square-foot commercial complex located in Rancho Mirage, California. Appellants

Las Palmas Associates et al., built and sold the property to respondents Las Palmas Center Associates et al. When a dispute arose concerning their duty to guaranty the rents of two tenants, appellants commenced an action for declaratory relief. Respondents in turn filed a cross-complaint for, among other things, fraud and breach of contract. A jury rendered verdicts awarding respondents \$232,393 for breach of contract, \$1.27 million for fraud, and \$10 million in punitive damages. In a separate trial, the court, sitting without a jury, denied appellants declaratory relief. The court then awarded respondents \$352,918 in contractual attorney's fees and entered judgment in the sum of \$11,622,918. Appellants now appeal.

Because the undisputed evidence establishes that respondents' fraud damages are identical to their losses under the breach of contract theory, we hold that the fraud award must be reduced to \$232,393. Additionally, we find it necessary to lower the punitive damage award to \$2 million. Lastly, inasmuch as respondents have elected to take under the tort claim, the award for *1229 contractual attorney's fees allocated to prosecute that action must be reversed. However, because respondents were the prevailing parties in appellants' declaratory relief lawsuit, which was an "action on the contract," respondents are entitled to recover their attorney's fees incurred in defense of that litigation.

Contentions

Appellants seek a reversal of the judgment on the basis that (1) the trial court erroneously denied their motion to bifurcate the punitive damage trial from respondents' underlying action for fraud, in violation of Civil Code section 3295, subdivision (d); (2) there are no grounds to hold Hahn Devcorp as the alter ego of its sister corporation, Ernest Hahn, Inc.; (3) the fraud verdict is unsupported by substantial evidence and is invalid as a matter of law; (4) respondents' trial counsel committed prejudicial misconduct; (5) the \$1.27 million fraud award, among other things, improperly compensates buy-

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

ers for a claim that they previously relinquished; and, (6) the punitive damage verdict is unsupported by the evidence, excessive, unconstitutional, and the product of the jury's passion and prejudice. Appellants do not, however, complain that the breach of contract award is defective.

Introduction

In 1978, Las Palmas Associates (Associates), a limited partnership, agreed to build and then sell the Rancho Las Palmas Shopping Center (shopping center) to Villa Pacific Building Company (Villa Pacific), a corporation. Villa Pacific's sole shareholder and board chairman was Ronald Waranch, a real estate developer. Under the terms of the purchase agreement, Villa Pacific acquired an 84 percent interest in the yet to be constructed shopping center. The remaining 16 percent share belonged to Stanley Gribble, president of Hahn Devcorp (Devcorp), a builder of community and neighborhood shopping centers. Gribble received his interest in the shopping center as part of his executive compensation package from Devcorp. Besides being Associates' general partner, Devcorp was also at the time a wholly owned corporate subsidiary of Ernest W. Hahn, Inc. (Hahn Inc.), a nationwide developer of regional shopping centers. Together, Gribble and Villa Pacific formed a general partnership known as Las Palmas Center Associates (Las Palmas), which would eventually hold title to the property.

For the sake of clarity, we will refer to Associates, Devcorp and Hahn Inc. collectively as "sellers." Similarly, we will identify Villa Pacific, Waranch, and Las Palmas jointly as "buyers."
*1230

Facts

Viewing the evidence, as we must, in the light most favorable to the prevailing party (*Mozzetti v. City of Brisbane* (1977) 67 Cal.App.3d 565, 570 [136 Cal.Rptr. 751]; *Little v. Stuyvesant Life Ins. Co.* (1977) 67 Cal.App.3d 451, 462 [136 Cal.Rptr. 653]), the record reveals that the initial price for the shopping center was \$10,727,499. That amount, though, was subject to being either increased or de-

creased, depending on the project's completion date and the rental income generated from the leases of commercial tenants. Buyers paid up-front \$2 million in cash to sellers. To protect that investment, Hahn Inc. in 1978 issued two guaranties to assure buyers the cash payment would be refunded if the deal collapsed.

In conjunction with the sale, buyers leased back the property to sellers. The parties also entered into various other amended purchase agreements, the effect of which was to require sellers to secure construction and permanent financing, build the complex, and sublease the property to tenants meeting certain financial and operating specifications. As consideration for the lease, sellers promised to pay buyers a portion of the gross rentals beginning in March 1980. The parties, moreover, had title to the property placed into an escrow account scheduled to close upon the completion of the shopping center and the subleasing of the stores to tenants. At the end of escrow, the parties planned for buyers to assume the permanent financing and pay sellers another cash payment. They also agreed that after the transaction closed, sellers would manage the facility for a period of three years.

One component of the purchase price was the capitalization of the shopping center's rental income.^{FN1}

FN1 Capitalization is a method of establishing a present day price for an asset that produces future income, such as rental property. It has been defined as "The amount equal to the value of the sum of money that would earn a periodic interest return equal to the rent if invested at the current market rate of interest." (Dolan, *Basic Economics* (2d ed. 1980) ch. 32, *Rent, Interest, and Profits*, p. 554.)

To establish the final purchase price, Waranch testified at trial that the parties selected a 7 percent capitalization rate. They then divided that percentage into the net operating income of the shopping

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

center as of the date of closing. The parties defined net operating income as the actual rental income less operating expenses and debt service. The result of that operation was then multiplied by 84 percent, which represented buyers' interest in the property.
*1231

In 1980, a dispute arose between the parties concerning the amount of rental income sellers had collected. Buyers contended they were entitled to approximately \$1.6 million in rents. In contrast, sellers asserted there was no rental income because operating expenses exceeded rents by \$400,000. As a compromise, buyers relinquished their claim for the rents in exchange for sellers taking \$2,187,683 of the purchase price in the form of buyers' promissory note. The note had a rate of 7 percent interest and was secured by a deed of trust to the shopping center.

Sometime in either 1980 or 1981, Hahn Inc. merged with Trizec Centers, Inc., a subsidiary of Trizec Corporation Ltd. At trial, the court admitted into evidence the proxy statement of that transaction. According to the document, Ernest Hahn, the board chairman and chief executive officer of Hahn Inc., agreed to sell his 1.6 million shares of the company to Trizec Centers. The proxy statement further revealed that on May 19, 1980, Ernest Hahn executed an employment agreement to serve as chief executive officer for Hahn Inc. and Trizec Centers. Under the employment agreement, the board of directors of Hahn Inc. and Devcorp would consist of two persons appointed by Ernest Hahn and five directors named by Trizec Centers. It was also anticipated that Ernest Hahn would appoint himself and Robert W. Lees, the former president of Hahn Inc., to both boards.

Furthermore, the proxy statement revealed that in 1980 Devcorp had 25 shopping centers either under development or in operation. The document stated Devcorp owed over \$30 million in outstanding loans, had secured \$43.2 million in loan commitments, and that Hahn Inc. had fully guaranteed the financing.

On March 20, 1981, Hahn Inc. transferred all 10,000 of its shares of Devcorp to Trizec Centers. Three days later, Trizec Centers conveyed 659 shares of Devcorp to Goldlist Acquisition Corp. and the remaining 9,341 shares of Devcorp to Trizec Equities, Inc.

By early 1982, the shopping center had two problem tenants. Franchise Stores Realty Corp. (Franchise) held a 10-year lease that it assigned to one Robert Young. He, however, eventually abandoned the store, leaving the leasehold to revert back to Franchise with \$6,000 owed in back rent. At the same time, Phanny's Phudge Parlors (Phanny's Phudge), which had signed a 15-year lease, was out of business and attempting to sublet its store.

As the closing date approached, buyers objected to including Phanny's Phudge and Franchise into the capitalized purchase price. To persuade buyers to consummate the transaction, sellers had Devcorp guaranty the *1232 stores' two leases. Pursuant to the guaranties, Devcorp essentially pledged to pay all sums due under the leases until Phanny's Phudge and Franchise paid their rents for consecutive periods ranging from three to six months. The guaranties also obligated buyers not to unreasonably withhold their permission to assignments of the leases.^{FN2}

FN2 Specifically, the lease guaranties provided:

(1) "Seller unconditionally guarant[ees] to Buyer the full and uninterrupted payment by Phanny's Phudge Parlors ('Phanny's Phudge') of all amounts payable pursuant to its lease dated November 13, 1979, as amended July 1, 1981 (the 'Phanny's Phudge Lease'), of space within the Shopping Center (i) until such time as Phanny's Phudge shall not be delinquent in the payment of such amounts, or in the performance of their obligations under the Phanny's Phudge Lease to operate their business, for a period of any three (3) suc-

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

cessive months from and after the date of this Sixth Amendment, or (ii) until the written approval by Buyer of any further assignment, subletting or termination of the Phanny's Phudge Lease, which approval shall not be unreasonably withheld, whichever first occurs, and Seller shall thereupon be automatically released from its obligations under this Paragraph 4."

(2) "Seller unconditionally guarant[ees] to Buyer the full and uninterrupted payment by Franchise Stores Realty Corp. ('Franchise Stores') of all amounts payable pursuant to its lease ('Franchise Stores Lease') of space in the Shopping Center (i) until Franchise Stores shall not be delinquent in the payment of such amounts for a period of any six (6) successive months from and after the date of this Sixth Amendment, or (ii) until Franchise Stores takes back possession and operates the premises covered by the Franchise Stores Lease for a period of any three (3) successive months, or (iii) until written approval by Buyer of any further assignment, subletting or termination of the Franchise Stores Lease, which approval shall not be unreasonably withheld, whichever first occurs, and Seller shall thereupon be automatically released from its obligations under this Paragraph 5."

With the rents capitalized, the total face value of the cash and financing paid by buyers was \$15,046,800. Of that amount, \$639,898 represented the capitalized rents from the Franchise and Phanny's Phudge leases.

Following the execution of the guaranties, Franchise sought to assign its lease to Riverco. Buyers rejected the assignment until sellers orally agreed that Riverco was covered by the Devcorp guaranty. After Riverco assumed the lease, it never once kept its rent payments current for the number of consecutive months required by the lease guar-

anty. Then, in December 1983, Riverco declared bankruptcy.

Meanwhile, Phanny's Phudge also had closed its doors and was attempting to locate a subtenant. In May 1982, buyers asked Devcorp to honor its commitment under the Phanny's Phudge guaranty. Devcorp refused the request, contending it had no obligation to pay the rent because buyers had unreasonably denied an assignment of the property to another tenant. Subsequently, in a July 1982 correspondence, Devcorp's corporate counsel, Vaughn Hapeman, disavowed the guaranty, claiming Phanny's Phudge had kept its rent current for the requisite three consecutive months ending that *1233 June. Buyers would later present evidence at trial that Hapeman made the assertion, despite the fact: (1) sellers' own management company served three-day notices to Phanny's Phudge demanding payment of the rents for May and June 1982; and, (2) that Stanley Gribble, Devcorp's president, wrote margin notes to Hapeman on an internal copy of the letter stating he thought Phanny's Phudge rent was past due for the period in question.

By June 1983, Devcorp's board of directors was liquidating the company's assets and discharging its executives and employees. Eventually, Devcorp became a shell company with Hahn, Inc.'s staff transacting its remaining business.

Also that year, at the suggestion of Devcorp's attorney, buyers evicted Phanny's Phudge from the property and obtained a \$34,814 unlawful detainer judgment. On November 8, 1983, buyers assigned the judgment to sellers because, as discussed in more detail below, buyers had been offsetting from their loan payments the rents left unpaid by Phanny's Phudge and Franchise.

In the summer of 1984, buyers notified sellers that they had located a tenant who desired to open a Greek restaurant in the Phanny's Phudge store. On July 23, 1984, Randy Brant, the director of leasing operations for Hahn, Inc., wrote to buyers' property manager, stating: "Please proceed to finalize the

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

[deal for the Greek restaurant]. As the proposed rent will not reach our guarant[ie]d rent until the third year Ernest W. Hahn, Inc. will agree to pick up the difference. ... In addition Ernest W. Hahn, Inc. will agree to guarant[ee] this lease and pay the commission amount of \$7,235.00 to Weiman Property Management. ..." Relying on the offer, buyers entered into the lease with the new tenant.

On September 27, 1984, Jana Green, corporate counsel for Hahn Inc., wrote buyers' management company using Devcorp's stationery. The letter rescinded the Hahn Inc. guaranty and replaced it with one issued by Devcorp. The letter stated: "This letter supersedes that certain letter, dated July 24, 1984, from Mr. Randy Brant, Director of Leasing, rendering it void and of no force and effect. [¶] The purpose of this letter is to provide a new guarant[y] on the same terms and conditions of the 'Phanny[']s Phudge' lease guarant[y] which said terms and conditions are as set forth below. ..." Green signed the letter as corporate counsel for Devcorp.

A week later, Devcorp again changed its position and had Green write buyers that it was no longer responsible for any of the guaranties. First, she asserted buyers' eviction action had terminated the Phanny's Phudge guaranty. *1234 Her letter also announced that sellers were giving buyers a \$34,814 credit against the promissory note, apparently in recognition of the tender of the unlawful detainer judgment. Secondly, the attorney insisted the lease assignments to Young, and then later to Riverco, had relieved sellers from their obligations under the Franchise guaranty.

As previously discussed, buyers were offsetting the uncollected rents from their loan payments. They started to take the deductions in August 1982 and continued the practice without objection from sellers until May 1984. At that time, sellers asked buyers to stop the deductions and instead bill them for the uncollected rents. Buyers complied with the request, but never received any remittances from sellers. Eventually, buyers reinstated the offsets.

As events developed, it would not be until March 1986 before buyers located a tenant for the Franchise store who paid a sufficient number of consecutive rents to terminate that lease guaranty. Similarly, a tenant who paid the requisite number of consecutive rents for the Phanny's Phudge store was not found until October 1986.

Sellers commenced the present action in Riverside County. Their complaint sought a declaration that the lease guaranties had terminated and that buyers had defaulted on the promissory note by taking the offsets. After buyers succeeded in having venue for the lawsuit transferred to Los Angeles County, sellers initiated a nonjudicial foreclosure to collect the arrearages caused by the offsets. To cure the default, Buyers paid sellers \$322,288, which included the offsets, plus interest. Buyers then filed a cross-complaint seeking, among other things, damages for breach of the lease guaranties. They also sought punitive damages for fraud, tortious breach of contract, and intentional infliction of emotional distress. In their fraud action, buyers alleged that sellers had misrepresented their intent to honor the guaranties in order to induce buyers into consummating the sale.

At the conclusion of extensive pretrial proceedings, the court dismissed all the tort claims except for the fraud action. The court also decided to impanel a jury to hear both lawsuits and to return advisory verdicts on the equitable issues. The court further ruled on sellers' *in limine* motion to exclude buyers from introducing evidence on various matters. However, despite the fact that buyers were seeking punitive damages for fraud, sellers neglected to request a protective order to preclude buyers from introducing evidence of sellers' financial condition.

In opening statements to the jury, both sides announced that buyers were seeking punitive damages. In addition, buyers on two separate occasions *1235 during their opening statement informed the jury, without a challenge by sellers, that Hahn Inc. was a "billion-dollar company."

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

Sellers prosecuted their lawsuit first and called as a witness Vaughn Hapeman, general counsel for Devcorp. Under cross-examination by buyers, Hapeman acknowledged that Hahn Inc. was a billion dollar company.^{FN3}

FN3 At oral argument before us, sellers' counsel represented that his clients had objected to the questions directed at their wealth. Actually, the record reflects that sellers objected to buyers' inquiry concerning the merger with Trizec Centers, Inc.

To determine the shopping center's market value, sellers called as their expert witness Thomas Marshall, a member of the Appraisal Institute. He testified that in February 1982, he conducted an income, cost, and sales comparison analysis of the property. Having assumed a 6 percent vacancy rate, Marshall opined that under the income approach the shopping center's market value in 1982 was \$16.4 million, or \$13,776,000 for buyers' 84 percent interest. He further stated its present worth was \$22.9 million.

On cross-examination, buyers questioned Marshall concerning his written appraisal report that claimed buyers actually had underpaid for the shopping center. Marshall arrived at that conclusion by reducing the face value of buyers' promissory note (\$2,187,683) to \$600,000. Because of favorable terms, Marshall opined that the note needed to be discounted by approximately \$1.5 million to determine its present day value in 1982. Using the discounted value of the note, Marshall calculated that the consideration given by buyers was only \$13,546,800. By subtracting that amount from the \$13,776,000 appraised value of buyers' share of the shopping center, Marshall was able to demonstrate that buyers made an immediate \$229,200 profit from the transaction. Marshall admitted, however, that in arriving at his opinion he did not include the fact that buyers had relinquished their claim for \$1.6 million in back rents as consideration for the right to finance the final purchase price payment.

Sellers concluded their case on the sixth day of trial. The following morning, buyers brought a motion to have sellers make available their financial records. Buyers argued that the motion should be granted because through cross-examination of sellers' witnesses they had presented a prima facie case for punitive damages. Buyers further informed the court that their first witness was Vernon Schwartz, the former senior vice-president and chief financial officer of Hahn Inc., who had traveled from San Francisco to be in court.

Sellers opposed the discovery motion, contending buyers had failed to meet their statutory burden to establish by clear and convincing evidence *1236 that sellers were guilty of acts justifying exemplary damages. During argument on this point, the trial court inquired: "I take it you did not ask for bifurcation [of the issue of the sellers' wealth under Civil Code section 3295, subdivision (d)]?"^{FN4} Sellers answered in the negative because they believed there was insufficient evidence of fraud to warrant disclosure of their wealth.

FN4 All further statutory references are to the Civil Code unless otherwise indicated. As explained later in our opinion, section 3295, subdivision (d) grants a defendant the option of requesting the trial court to exclude from the trier of fact evidence of the defendant's wealth until a verdict is rendered for plaintiff awarding actual damages and a finding has been made that defendant was guilty of malice, oppression, or fraud.

The trial court ordered sellers to provide the financial records. Sellers then made an oral motion to exclude evidence of their finances from the jury under subdivision (d) of section 3295. The trial court denied the request.

Thereafter, during buyers' direct examination of Schwartz, the witness estimated that Hahn Inc. owned more than 40 shopping centers and had assets in excess of a billion dollars.

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

The remainder of the trial lasted for nearly three weeks. During their case-in-chief, buyers attempted to prove the economic downturn of the early 1980's, along with unanticipated construction costs and higher interest rates, caused sellers to overestimate their profit margin. Under buyers' scenario, sellers needed the rents from Franchise and Phanny's Phudge to be capitalized into the final purchase price to keep the deal profitable. Buyers also sought to prove that after the issuance of the guaranties, sellers drained Devcorp of its assets and manpower for the purpose of leaving the company a mere shell corporation.

Before submitting the case to the jury, the parties stipulated the net value of Hahn Inc. was \$497 million. They also agreed Devcorp had a total worth of \$4.1 million.^{FN5}

FN5 Apparently, half of Devcorp's net worth came from buyers' promissory note.

In closing summation to the jury, buyers argued that sellers owed them \$232,292 for breach of the guaranty agreements. The amount represented uncollected rents, management fees, taxes, penalties, interest, and other miscellaneous costs due under the Franchise and Phanny's Phudge leases. Turning to the tort action, they asked the jury to find that sellers had fraudulently promised to guaranty the leases as an inducement for them to complete the deal. In addressing the issue of fraud damages, buyers' counsel first told the panel: "I could ask you for a million, two-seventy *1237^{FN[6]} We're not going to do that because I think that is a-I think ridiculous, even though it works to our advantage at this point. I think it's a ridiculous theory. I don't think it's justified and I don't think it's right." He then urged the jury to find that the proper measure of the fraud damages was the capitalized cost of the two leases: \$639,878 (\$374,702 for Phanny's Phudge and \$265,176 for Franchise).

FN[6] Buyers arrived at that figure by subtracting the appraised value of their share of the shopping center (\$13,776,000) from

the face value of the consideration they paid (\$15,046,800).

On the other hand, sellers asserted in their closing argument that buyers had not suffered any fraud damages because the shopping center in 1982 was worth more than what buyers had paid. Then referring to the property's current value, sellers' attorney stated: "Of course, we also know that when we talk about market value, you heard the testimony of the appraiser, the market value conservatively appraised is \$22.9 million. Far more than what [buyers] paid."

Seizing on sellers' closing argument, buyers' attorney on rebuttal told the jury: "I'm going to change my mind from yesterday. [Sellers' attorney] stands up here and he says that the real measure of damages on the shopping center is that [buyers get what they] paid for, and he says ... today that the center was worth [\$]22,900,000. You heard the appraiser. The appraiser said it was worth sixteen million four and 84 percent of it was that number. And that is what [buyers] paid, and that is what [they] overpaid. That theory is the dumbest theory in the world to base damages on. And the real theory, the second one that's easily had, and that is the one I told you about on the [\$]639,000. You know, if he wants to be dumb enough to stand up and continue to argue that is the way to do it, then bury him with it, okay? On that verdict form when you put down how much is the guilt of fraud, don't put the [\$]639,000, follow his instruction and put [\$]1,270,000 down there. That is what he wants you to do."

After deliberating for only one day, the panel unanimously agreed sellers had breached the two guaranties. The jury set damages at \$232,393. By a vote of 10 to 2, the jury also found (1) sellers had fraudulently misrepresented their intent to honor the guaranties, causing buyers to overpay \$1.27 million for the shopping center; and (2) in making the guaranties, sellers acted with oppression, fraud, or malice. Voting 9 to 3, the panel assessed sellers \$10 million in punitive damages. Finally, the jury

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

also unanimously found that Devcorp was the alter ego of Hahn Inc. and that Hahn Inc. should be held liable for the obligations of Devcorp. *1238

The court thereafter dismissed the jury and allowed the parties to address the merits of sellers' declaratory relief action. The parties also argued whether Hahn Inc. should be held accountable for Devcorp's conduct. Following argument, the trial court determined that sellers had breached the guaranties. It further held there was a sufficient unity of interest and ownership between the two corporations to find Devcorp to be the alter ego of Hahn Inc.

Sellers made various posttrial motions. In their request for a new trial, they contended, inter alia, that an award of \$1.27 million in fraud damages was unsupported by the evidence and that the punitive damage verdict was excessive. The trial court took the motions under submission, remarking "... I have never seen a simple commercial real estate sale transaction screwed up so badly by so many members of the bar over a long period of time as I have in this situation. [¶] It is absolutely unbelievable what has happened to these parties over this period of time." Two days later, the trial court summarily denied the motions.

Discussion

I. *Whether the Fraud Verdict Should Be Affirmed*

(1a) Sellers assert the evidence is insufficient to support a finding that at the time they initially entered into the lease guaranties they harbored an intent to defraud buyers. We conclude otherwise.

We are aware of the danger of grafting tort liability on what ordinarily should be a breach of contract action. While society has a strong interest in the security of transactions, parties dealing at arm's length are permitted to reach a reasoned decision to breach an agreement, knowing their risk is limited to the reimbursement of the other side's compensatory losses. However, no public policy is served by permitting a party who never intended to fulfill his obligations to fraudulently induce another

to enter into an agreement. (2a) In recognition of this principle, section 1710, subdivision (4) defines fraud as the making of a promise done without any intention of performing the obligation. " 'A promise to do something necessarily implies the *intention to perform*, and, where such an intention is absent, there is an implied misrepresentation of fact, which is actionable fraud. [Citations.]' [Citations.]" (*Joanaco Projects, Inc. v. Nixon & Tierney Constr. Co.* (1967) 248 Cal.App.2d 821, 831 [57 Cal.Rptr. 48], italics in original.)

Recognizing the adverse effect fraud has on commercial transactions, the law permits a defrauded party to seek punishment of the wrongdoer through *1239 the imposition of punitive damages. (3) "Although punitive damages may not ordinarily be given for breach of contract, whether the breach be intentional, willful or in bad faith [citations], such damages may be awarded where a defendant fraudulently induces the plaintiff to enter into a contract. [Citations.] The words 'oppression, fraud, or malice' in Civil Code section 3294 being in the disjunctive, fraud alone is an adequate basis for awarding punitive damages. [Citations.]" (*Glendale Fed. Sav. & Loan Assn. v. Marina View Heights Dev. Co.* (1977) 66 Cal.App.3d 101, 135 [135 Cal.Rptr. 802], fn. omitted.)

(2b) In proving fraud, however, rarely does a plaintiff have direct evidence of a defendant's fraudulent intent. Therefore, the subsequent conduct of a defendant, such as his failure to immediately carry out his pledge has some evidentiary value to show that a defendant made the promise without the intent to keep the obligation. But, " 'something more than nonperformance is required to prove the defendant's intent not to perform his promise.' [Citations.]" (*Tenzer v. Superscope, Inc.* (1985) 39 Cal.3d 18, 30 [216 Cal.Rptr. 130, 702 P.2d 212].)

(4) As in all substantial evidence challenges, the appellate court's power of review commences and ceases with the location of any substantial evidence, contradicted or uncontradicted, which will

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

support the determination. (*Gray v. Don Miller & Associates, Inc.* (1984) 35 Cal.3d 498, 503 [198 Cal.Rptr. 551, 674 P.2d 253, 44 A.L.R.4th 763]; *Bowers v. Bernards* (1984) 150 Cal.App.3d 870, 873-874 [197 Cal.Rptr. 925].) The appellate court cannot limit its review of the record to the evidence cited by the respondent; it must consider the entire record in determining whether the judgment is supported by sufficient evidence. (*Bowers v. Bernards, supra*, at p. 873.) Evidence is substantial if it is "reasonable in nature, credible, and of solid value." (*Estate of Teed* (1952) 112 Cal.App.2d 638, 644 [247 P.2d 54].) Moreover, the testimony of a single witness is sufficient to satisfy the test of the substantial evidence rule. (*Kearl v. Board of Medical Quality Assurance* (1986) 189 Cal.App.3d 1040, 1052 [236 Cal.Rptr. 526].)

(1b) Applying this framework of principles to the present case, the record contains credible evidence from which a trier of fact could conclude sellers committed fraud and then systematically attempted to avoid honoring the guaranties. In May 1982, sellers contended that the Phanny's Phudge guaranty had terminated because buyers unreasonably withheld their approval of new tenants. In July 1982, sellers changed their position and asserted the Phanny's Phudge guaranty had ended because the tenant remained current with its rent for three consecutive months. Sellers made the assertion even though (1) Devcorp's president disputed the claim in an *1240 internal memo; and (2) Devcorp's own property manager had served Phanny's Phudge with three-day notices to quit for nonpayment of rent during the months in question.

Moreover, in June 1983, sellers began to dismantle Devcorp by selling off its assets and firing its employees. After sellers encouraged buyers to evict Phanny's Phudge from the store, they later asserted the eviction had terminated the lease guaranty. In May 1984, sellers asked buyers to bill them for the unpaid rents. When buyers complied with the request, sellers ignored the billings. Following the promise by Hahn Inc. to guarantee the rent of a

replacement tenant for Phanny's Phudge, Devcorp quickly rescinded the offer and in its place issued its own guaranty. Finally, a week later, Devcorp informed buyers that it considered all the guaranties to be null and void. Based on this record, substantial evidence exists from which a jury could infer that sellers made the guaranties without an intent to perform them.

Sellers also urge that as a matter of law they cannot be held liable for fraud because they partly performed the guaranties. (See *Kaylor v. Crown Zellerbach, Inc.* (9th Cir. 1981) 643 F.2d 1362, 1368.) As evidence of their part performance, sellers point to the \$34,818 credit they gave buyers against the promissory note in October 1984. The contention is unavailing. First, it took sellers almost two and a half years to give the credit. Second, it is arguable whether sellers actually gave up anything for the credit because they made it after receiving from buyers the unlawful detainer judgment against Phanny's Phudge. Third, and most importantly, at the same time sellers credited the promissory note, they reiterated their position that the guaranties were no longer valid.

II. Whether It Was Prejudicial Error to Allow the Jury Knowledge of Sellers' Wealth

(5a) Sellers argue the trial court committed prejudicial error when it failed to heed the mandatory language of section 3295 and grant them a protective order excluding evidence of their wealth from the jury until the panel found them liable for fraud. Buyers counter that sellers waived the mandatory command of the statute by not raising the motion in a timely fashion. As the facts of this case clearly illustrate, a statute written in mandatory language must nonetheless come within the trial court's discretion when a party delays seeking its rights to the detriment of the opposition.

(6) Subdivision (d) of section 3295 provides that "[t]he court shall, on application of any defendant, preclude the admission of evidence of that *1241 defendant's profits or financial condition until after the trier of fact returns a verdict for

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

plaintiff awarding actual damages and finds that a defendant is guilty of malice, oppression, or fraud in accordance with Section 3294. Evidence of profit and financial condition shall be admissible only as to the defendant or defendants found to be liable to the plaintiff and to be guilty of malice, oppression, or fraud. Evidence of profit and financial condition shall be presented to the same trier of fact that found for the plaintiff and found one or more defendants guilty of malice, oppression, or fraud.” (Italics added.)

On its face, section 3295, subdivision (d) is a codification of the presumption that evidence of a defendant's wealth can induce fact finders to abandon their objectivity and return a verdict based on passion and prejudice. (See *Adams v. Murakami* (1991) 54 Cal.3d 105, 121 [284 Cal.Rptr. 318, 813 P.2d 1348].)

Sellers urge the only deadline imposed by section 3295, subdivision (d) is that the motion be made before the trier of fact delivers a verdict finding a defendant liable for acts worthy of assessing punitive damages. We refuse to subscribe to such a rule. In our view, it is manifest that a party may be estopped from claiming a statutory right if untimely asserted. It is a maxim of jurisprudence that “[t]he law helps the vigilant, before those who sleep on their rights.” (§ 3527.)

A request under section 3295, subdivision (d) is essentially a motion *in limine*, and ordinarily should be made before trial. (See 3 Witkin, Cal. Evidence (3d ed. 1986) § 2011(a), p. 1969; 2 Cal. Trial Objections (Cont.Ed.Bar 2d ed. 1984) § 1.2, p. 4; Cal. Judges Benchbook, Civil Trials (CJER 1981) § 3.12, pp. 72-73.)

(5b) In the matter at hand, sellers have no excuse for their delay in seeking the bar of the statute. From the inception of buyers' lawsuit, sellers had notice punitive damages were being sought. Yet, they inexplicably waited to bring the motion until after buyers had already (1) told the jury twice in opening argument Hahn Inc. was a billion dollar

company; (2) cross-examined a witness on the subject of Hahn Inc.'s wealth; and (3) made a motion to compel production of the sellers' financial records.

More egregious, though, is the fact sellers withheld the motion until buyers were to begin the presentation of their case. Apparently in response to sellers' unwillingness to voluntarily produce their records, buyers had Vernon Schwartz, a Hahn Inc. executive, standing by to testify as their initial witness. Because he was from out of town, buyers possessed a legitimate *1242 reason to have Schwartz testify at the earliest possible moment. It was only at this late date—after months of pretrial proceedings and five days of testimony—that sellers insisted the court was under a mandatory duty to exclude evidence of their finances.

This litigation, we think, aptly demonstrates that the mandatory effect of section 3295, subdivision (d), like many other rights, may be lost by a defendant who fails to act promptly to preserve its protection. Our decision, of course, does not mean a defendant who chooses to delay the exercising of his statutory right before trial is totally precluded thereafter from objecting to evidence of his financial status. Even before the enactment of subdivision (d), the trial court had discretion to exclude such evidence as being unduly prejudicial. (*Hilliard v. A. H. Robins Co.* (1983) 148 Cal.App.3d 374, 392-393 [196 Cal.Rptr. 117]; Code Civ. Proc., § 598.)

Turning to the record at hand, we cannot say it was an abuse of discretion for the trial court to deny sellers' motion. The jury learned in opening argument, and also during cross-examination of one of sellers' own witnesses, that Hahn Inc. was a company of substantial worth. From these events alone, the trial court reasonably could have concluded it would be impossible to “unring the bell.” More significantly, however, the court also could have found that to grant the motion in the midst of trial would have been prejudicial to buyers. As noted, buyers had an out-of-town witness waiting to discuss sellers' finances when sellers made their motion. In

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301.
(Cite as: 235 Cal.App.3d 1220)

conclusion, sellers cannot complain on appeal they were denied the benefit of section 3295, subdivision (d) when it was within their power to make a timely motion.

(7a) Sellers also contend that even if it was not reversible error for the court to have denied their belated request for a protective order, we must still grant them a new trial because buyers impermissibly used evidence of their wealth in closing argument to inflame the passion and prejudice of the jury. We disagree.

Both the pauper and the millionaire are entitled to be treated fairly before the trier of fact. (*Seimon v. Southern Pac. Transportation Co.* (1977) 67 Cal.App.3d 600, 606 [136 Cal.Rptr. 787]; *Love v. Wolf* (1964) 226 Cal.App.2d 378, 388 [38 Cal.Rptr. 183]) This follows from the rule that evidence of a party's wealth is generally irrelevant to the issue of liability. "Justice is to be accorded to rich and poor alike, and a deliberate attempt by counsel to appeal to social or economic prejudices of the jury, including the wealth or poverty of the litigants, is misconduct where the asserted wealth or poverty is not relevant to the issues of the case." (*1243 *Hoffman v. Brandt* (1966) 65 Cal.2d 549, 552-553 [55 Cal.Rptr. 417, 421 P.2d 425].) (8) However, where liability and punitive damages are tried in a single proceeding, evidence of wealth is admissible. "[W]hile in the ordinary action for damages information regarding the adversary's financial status is *inadmissible*, this is not so in an action for punitive damages. In such a case evidence of defendant's financial condition is admissible at the trial for the purpose of determining the amount that it is proper to award [citations]. The relevancy of such evidence lies in the fact that punitive damages are not awarded for the purpose of rewarding the plaintiff but to punish the defendant. Obviously, the trier of fact cannot measure the 'punishment' without knowledge of defendant's ability to respond to a given award." (*Coy v. Superior Court* (1962) 58 Cal.2d 210, 222-223 [23 Cal.Rptr. 393, 373 P.2d 457, 9 A.L.R.3d 678], italics in original.)

(7b) In urging the jury to punish sellers, buyers' counsel stated: "Think about just how big this company is. When you talk about them beating up on people that are smaller than they are. ... There is probably nothing, in my opinion, that is more sickening in our society than a company that will take as much money as they've got and use it to pound away on you legally. ... There's one thing we can do about it. We can take away some of their money so they don't have that money at least anymore to grind people into the dirt. ... You've got to send a message loud enough to them that they won't treat people this way ... That they wouldn't use their money to buy lawyers to try to legally nail your knees to the floor."

Because sellers failed to timely assert their right to a protective order under subdivision (d) of section 3295, buyers had an opportunity to try the fraud and punitive damage issues in a unified proceeding. In light of that fact, we think nothing said by buyers in argument was inappropriate. The purpose behind section 3294, the exemplary damages statute, is to punish and deter the defendant for his wrongful conduct. (*Neal v. Farmers Ins. Exchange* (1978) 21 Cal.3d 910, 928, fn. 13 [148 Cal.Rptr. 389, 582 P.2d 980]; *Downey Savings & Loan Assn. v. Ohio Casualty Ins. Co.* (1987) 189 Cal.App.3d 1072, 1098 [234 Cal.Rptr. 835]; *Emerson v. J. F. Shea Co.* (1978) 76 Cal.App.3d 579, 594 [143 Cal.Rptr. 170].) To achieve that goal, the jury's attention must be focused on a number of considerations: "One factor is the particular nature of the defendant's acts in light of the whole record; clearly, different acts may be of varying degrees of reprehensibility, and the more reprehensible the act, the greater the appropriate punishment, assuming all other factors are equal. [Citations.] Another relevant yardstick is the amount of compensatory damages awarded; in general, even an act of considerable reprehensibility will not be seen to justify a proportionally high amount of *1244 punitive damages if the actual harm suffered thereby is small. [Citation.] Also to be considered is the wealth of the particular defendant; obviously, the function of

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

deterrence [citation], will not be served if the wealth of the defendant allows him to absorb the award with little or no discomfort. [Citations.]” (*Neal v. Farmers Ins. Exchange, supra*, 21 Cal.3d 910, 928.) Viewed under these principles, it cannot be said buyers' counsel strayed beyond the bounds of his right to fairly comment on the state of the evidence.

Moreover, evidence of sellers' wealth was relevant not only to guide the jury in its assessment of the proper amount of punitive damages to award, but also as proof that sellers intended to oppress buyers into submission.

At this juncture, we think it important to further note that substantial evidence supports the jury's determination that an award of punitive damages was proper because buyers met their burden of proving fraud by clear and convincing evidence. (See *Patrick v. Maryland Casualty Co.* (1990) 217 Cal.App.3d 1566, 1576 [267 Cal.Rptr. 24]; § 3294, subd. (a).) Sellers would have us believe they were guilty of nothing more than bad judgment and overzealousness. The jury, however, viewed the evidence differently, drawing the conclusion that sellers fraudulently promised to honor the guaranties. We are bound by that decision, because as our detailed recitation of the facts demonstrates, the jury's characterization of the evidence is supported by the record. Thus, we are convinced that the references to sellers' wealth in closing argument did not impermissibly sway the jury to render verdicts against the sellers.

III. *Whether Buyers' Trial Counsel Committed Prejudicial Misconduct*

Sellers complain they were denied a fair trial because in closing argument buyers' counsel committed purported acts of misconduct, to wit, he (1) suggested buyers sought a change of venue because sellers' attorneys used political contributions to exert influence over the judiciary in Riverside County; (2) intimated sellers paid their attorneys to lie for them in court and to conceal evidence; (3) misrepresented the amount of money buyers ultimately

spent for the shopping center; (4) appealed to the jury to be sympathetic to Waranch; and, (5) implied that Waranch might donate an award of punitive damages to charity. Sellers also assert buyers' attorney poisoned the proceedings by abusing witnesses, making improper objections, and repeatedly propounding argumentative questions. We do not agree.

(9a) First, we find no misconduct in buyers' suggestion that sellers made misrepresentations and attempted to conceal evidence. These remarks are *1245 supported by the record. As described above, Vaughn Hapeman, Devcorp's corporate counsel, wrote a letter to buyers in July 1982 contending the Phanny's Phudge lease guaranty had terminated because the tenant had paid its rent for three consecutive months. Hapeman made the claim despite the fact that Devcorp's president, Stanley Gribble, had made notations on an internal copy of the correspondence stating: “Vaughn. Before you make these statements be sure Phanny's was current for 3 months on all rents. My opinion is they were not current on all accounts for 3 months and have not been. Suggest you change your position.”

At trial, sellers called Hapeman as a witness and had him testify concerning the letter. They then offered into evidence a copy of the correspondence without Gribble's comments. In closing argument, buyers' counsel directed the jury's attention to an unedited copy of the letter which contained the incriminating margin notes. Buyers' attorney told the panel: “Reasonable men might disagree as to whether facts demonstrate A or B, but reasonableness has nothing to do with lying and distorting and cheating and trying to suppress evidence.”

In another instance before the jury, buyers' attorney charged the opposition of suppressing evidence by not calling Sue Cook, an earlier announced witness. Cook was Devcorp's manager of the shopping center. In his testimony, Hapeman stated Cook had confirmed to him that Phanny's Phudge was not delinquent with its rent for three straight months. On cross-examination, buyers confronted Hapeman

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

with Cook's denial that she had ever spoken to him. Subsequently, buyers had Cook testify that one of sellers' attorneys during the trial had telephoned her and stated it was unnecessary for her to appear in court.

Directing the jury's attention to this episode, buyers' attorney stated: "So you would not have ever heard from Miss Sue Cook at that point except for the fact we got hold of her and we brought her back in here. And now I know [sellers' attorney is] sighing and going crazy. I don't blame him. I was pretty embarrassed for him at the time, too."

Buyers' counsel also accused sellers' attorney of not being forthright on two other minor matters concerning his involvement in drafting a pleading and propounding certain interrogatories. He argued to the jury: "But when you're caught lying or you're caught cheating or you're caught stealing, it's real hard to look cool. That's when you start to stutter and stammer, and you look unorganized and you can't put it together, and you just end up looking stupid. ... ¶ It's simply because it's hard to look good when you have to uphold the lies of your client. ¶ And then you can add insult to injury by *1246 continuing to outright tell lies to you, for example, over the last three weeks. ¶ It's probably fairly clear to you that I've been pretty angry in this case."

(10) Personal attacks on opposing parties and their attorneys, whether outright or by insinuation, constitute misconduct. (*Stone v. Foster* (1980) 106 Cal.App.3d 334, 335 [164 Cal.Rptr. 901].) Such behavior only serves to inflame the passion and prejudice of the jury, distracting them from fulfilling their solemn oath to render a verdict based solely on the evidence admitted at trial. (*Neumann v. Bishop* (1976) 59 Cal.App.3d 451, 484- 485 [130 Cal.Rptr. 786].) Lack of civility between counsel, moreover, only breeds public disrespect for the judicial process. (9b) Although we regret that buyers' attorney personalized his argument in such a fashion, we are left unconvinced that, on the whole, he exceeded his right to comment on the state of the

evidence. Here, the facts surrounding the making of Vaughn Hapeman's letter, and the way those events were portrayed to the jury, represented highly relevant circumstantial evidence of whether sellers ever intended to honor the lease guaranties. Buyers also had the right under the facts to comment on why sellers suddenly attempted to suppress the testimony of one of their scheduled witnesses. (*Freitas v. Peerless Stages, Inc.* (1952) 108 Cal.App.2d 749, 761 [239 P.2d 671, 33 A.L.R.2d 778]; Evid. Code, § 413.)

We next turn to whether buyers' attorney misrepresented the price his clients paid for the shopping center. (11) While trial counsel is entitled to argue his interpretation of the evidence to the jury, he has no right to cite facts unsupported by the evidence. (*Malkasian v. Irwin* (1964) 61 Cal.2d 738, 747 [40 Cal.Rptr. 78, 394 P.2d 822].) This is what sellers claim buyers' counsel did in order to convince the jury that sellers fraudulently made the lease guaranties. As described earlier, buyers argued that sellers underestimated the cost of constructing the shopping center. Sellers committed fraud, according to buyers, because the project only would turn a profit if the rents from Franchise and Phanny's Phudge were capitalized into the final purchase price.

Sellers essentially claim that buyers' attorney had no factual basis for making the argument because he knew that they realized a \$3 million profit from "selling" Stanley Gribble a 16 percent interest in the shopping center. The contention is not supported by the evidence. Gribble never testified that he paid money for his ownership interest. Rather, the record reveals that he had "earned" his share of the shopping center as part of what he characterized as the "sweat equity" included in his executive compensation package *1247 from Devcorp. In other words, Gribble received his interest in the shopping center for services rendered to Devcorp.

Having not parted with cash, the exact sum Gribble "contributed" to the profitability of the transaction is questionable, to say the least. Consid-

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

ering this fact, we think buyers' attorney could fairly argue that sellers committed fraud to insure their profits through the capitalization of the Phanny's Phudge and Franchise leases.

(12) We next turn to sellers' remaining contentions regarding attorney misconduct. First, we find that buyers' counsel blatantly did commit misconduct when he intimated sellers could influence judges in Riverside County through political contributions made by sellers' attorneys. He also improperly appealed to the jury's sympathy when he suggested buyers might donate the punitive damages to charity. (Cf. *Lewis v. Union Pacific R. Co.* (1954) 127 Cal.App.2d 280, 283 [273 P.2d 706].) Even so, any prejudice from these statements were cured when the trial court admonished the jury to disregard the statements. (*Mendoza v. Gomes* (1956) 143 Cal.App.2d 172, 179 [299 P.2d 707].)

We also think buyers' counsel was guilty of misconduct to a lesser degree when he insinuated that sellers' attorneys were "whores" who would lie in court for their clients. This remark, along with a number of other purported acts of misconduct, was left unchallenged by sellers and, thus, must be deemed waived.

"A party is foreclosed from complaining on appeal of misconduct during arguments to the jury where his counsel sat silently back during the arguments, allowed the alleged improprieties to accumulate without objection, and simply made a motion for a mistrial at the conclusion of the argument. [Citation.]" (*Brokopp v. Ford Motor Co.* (1977) 71 Cal.App.3d 841, 860 [139 Cal.Rptr. 888, 93 A.L.R.3d 537]; see also *Horn v. Atchison, T. & S. F. Ry. Co.* (1964) 61 Cal.2d 602, 610 [39 Cal.Rptr. 721, 394 P.2d 561].)

Citing *Simmons v. Southern Pac. Transportation Co.* (1976) 62 Cal.App.3d 341 [133 Cal.Rptr. 42], sellers contend that multiple objections need not be raised when an adversary engages in flagrant and repeated episodes of misconduct. It is also important to note that *Simmons* states: "The ultimate

determination of [the issue of attorney misconduct] rests upon [the appellate] court's 'view of the overall record, taking into account such factors, inter alia, as the nature and seriousness of the remarks and misconduct, the general atmosphere, including the judge's control, of the trial, the likelihood of prejudicing the jury, and the efficacy of objection or admonition under all *1248 the circumstances.' [Citation.]" (*Id.* at p. 351.) To this list we prominently would add the strength of the offending attorney's case. Here, there was substantial evidence of sellers' fraud. Thus, even if buyers' counsel was guilty of a pervasive pattern of misconduct, we think it had an innocuous effect on the jury's overall conclusion that sellers had committed a tortious act.

IV. *Whether the Record Supports the Finding That Devcorp Was the Alter Ego of Hahn Inc.*

(13a) Hahn Inc. complains buyers cannot pierce its corporate veil because the undisputed evidence established that it had no interest in the corporation at the time the 1982 lease guaranties were created. We find the contention meritless.

(14) "The law as to whether courts will pierce the corporate veil is easy to state but difficult to apply." (*Talbot v. Fresno-Pacific Corp.* (1960) 181 Cal.App.2d 425, 432 [5 Cal.Rptr. 361].) Because it is founded on equitable principles, application of the alter ego "is not made to depend upon prior decisions involving factual situations which appear to be similar. ... 'It is the general rule that the conditions under which a corporate entity may be disregarded vary according to the circumstances of each case.' " (*McLoughlin v. L. Bloom Sons Co., Inc.* (1962) 203 Cal.App.2d 848, 853 [24 Cal.Rptr. 311]; see *Stark v. Coker* (1942) 20 Cal.2d 839, 846 [129 P.2d 390]; *Jack Farenbaugh & Son v. Belmont Construction, Inc.* (1987) 194 Cal.App.3d 1023, 1033 [240 Cal.Rptr. 78].) Whether the evidence has established that the corporate veil should be ignored is primarily a question of fact which should not be disturbed when supported by substantial evidence. (*Jack Farenbaugh & Son v. Belmont Construction, Inc.*, *supra*, 194 Cal.App.3d at p.

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

1032.)

Hahn Inc. relies on *Riddle v. Leuschner* (1959) 51 Cal.2d 574 [335 P.2d 107]. There, the California Supreme Court reversed a judgment, based on an alter ego theory, against a manager of businesses owned by two corporations. The court stated: "It is undisputed that he held none of the stock, and there is no evidence that he had any interest as an owner in the business operated by either of the two corporations or that he had a right to share in any profits they might make. Instead, he received a monthly salary. Under all the circumstances, he is to be regarded as having been a managing employee of the two companies, and his control over their affairs must be treated as that which would be exercised by a managing agent rather than that of a shareholder or owner. It follows that there was not such unity of 'interest and ownership' between [the manager] and the corporations that the separate *1249 personalities of the corporations and the individual no longer existed, within the meaning of the rule. ..." (*Id.* at p. 580.)

Riddle stands for the proposition that it would be unfair to impose personal liability on an individual for corporate conduct unless he had an ownership interest in the company. At the same time, under the facts of this case, it would be as equally unfair to permit Hahn Inc. to escape liability for the unperformed guaranties simply because it earlier had transferred ownership of Devcorp to, among others, a sister corporation within the Trizec family of companies.

"Usually, a disregard of the corporate entity is sought in order to fasten liability upon individual stockholders. ... 'It has been stated that the two requirements for application of this doctrine are (1) that there be such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist and (2) that, if the acts are treated as those of the corporation alone, an inequitable result will follow.' [¶] However, only a difference in wording is used in stating the same concept where the entity sought to

be held liable is another corporation instead of an individual. 'A very numerous and growing class of cases wherein the corporate entity is disregarded is that wherein it is so organized and controlled, and its affairs are so conducted, as to make it merely an *instrumentality, agency, conduit, or adjunct of another corporation.*' [Citations.]" (*McLoughlin v. L. Bloom Sons Co., Inc.*, *supra*, 206 Cal.App.2d 848, 851- 852, italics added.)

Because society recognizes the benefits of allowing persons and organizations to limit their business risks through incorporation, sound public policy dictates that imposition of alter ego liability be approached with caution. (*Cascade Energy and Metals Corp. v. Banks* (1990) 896 F.2d 1557, 1576.) Nevertheless, it would be unjust to permit those who control companies to treat them as a single or unitary enterprise and then assert their corporate separateness in order to commit frauds and other misdeeds with impunity. Here, buyers essentially tried the case based on a single-enterprise theory of liability. In closing argument to the jury, buyers argued the evidence established that the line of command ran from Trizec at the top, with Hahn Inc. in the middle, and Devcorp at the bottom.

Generally, alter ego liability is reserved for the parent-subsidiary relationship. However, under the single-enterprise rule, liability can be found between sister companies. The theory has been described as follows: " 'In effect what happens is that the court, for sufficient reason, has determined that though there are two or more personalities, there is but one enterprise; *1250 and that this enterprise has been so handled that it should respond, as a whole, for the debts of certain component elements of it. The court thus has constructed for purposes of imposing liability an entity unknown to any secretary of state comprising assets and liabilities of two or more legal personalities; endowed that entity with the assets of both, and charged it with the liabilities of one or both.' (2 Marsh's Cal. Corp. Law (3d ed. 1990) § 16.23, p. 1416, quoting a law review article by Professor Berle found at 47 Colum.

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

L. Rev. (1947) 343, 350.)

In *Pan Pacific Sash & Door Co. v. Greendale Park, Inc.* (1958) 166 Cal.App.2d 652 [333 P.2d 802], defendants formed Greendale Park, Inc., and the Ralmor Corporation to build homes on undeveloped lots. Defendants transferred the real property to Greendale Park and later had that corporation contract with Ralmor for the construction. Plaintiff sold sash doors, frames and jambs to Ralmor. When Ralmor did not pay for the goods, plaintiff sued each corporation asserting they were both one and the same. The trial court entered judgment against both corporations under the alter ego theory.

The Court of Appeal in *Pan Pacific* affirmed the judgment, stating: "Upon the basis of the ... evidence the trial court was warranted in concluding, as it did, that each corporation was but an instrumentality or conduit of the other in the prosecution of a single venture namely, the construction and sale of houses upon the tract in question. ... There was such unity of interest and ownership that the separateness of the two corporations had in effect ceased and an adherence to the fiction of a separate existence of the two corporations would, under the circumstances here present, promote injustice and make it inequitable for Greendale to escape liability for an obligation incurred as much for its benefit as for Ralmor." (166 Cal.App.2d at pp. 658-659.)

(13b) We find there is substantial evidence to support the conclusion that Hahn Inc. and Devcorp formed a single enterprise for the purpose of committing a continuing fraud against buyers. First, the evidence that Hahn Inc. had guaranteed \$43.2 million in loans and loan commitments to Devcorp strongly suggests Devcorp was undercapitalized for a company in the business of developing shopping centers. Likewise, in 1978 Hahn Inc. issued two guaranties to buyers to protect the \$2 million cash downpayment they made to Devcorp. Moreover, besides the loan guaranties, Hahn Inc. temporarily guaranteed the Phanny's Phudge lease, despite the

fact that Hahn Inc. no longer had a stock ownership interest in Devcorp. These guaranties indicate that Devcorp's survivability as a developer was intertwined with its dependence on Hahn Inc. *1251

Furthermore, Ernest Hahn and Robert Lees sat as directors on the boards of Hahn Inc. and Devcorp. When Devcorp's board of directors fired the corporation's executives and staff, Hahn Inc. used its employees, including its corporate counsel, to continue to manage what remained of the business. In short, the trial court reasonably could have concluded that Hahn Inc. and Devcorp were combined into a single enterprise to defraud buyers.

Sellers next assert that even assuming there was a unity of interest between Hahn Inc. and Devcorp, the record lacks substantial evidence to support a finding that justice required the trial court to pierce the corporate veil. They premise their argument on the fact the parties stipulated at trial that Devcorp was worth \$4.1 million, an amount sufficient to satisfy the \$1.27 million award of compensatory damages and a suitable punitive damage award. They contend buyers dragged Hahn Inc., with its sizeable assets, into the lawsuit only to increase the funds available for a punitive damage award. We are unpersuaded by the claim.

Sellers cite *Walker v. Signal Companies, Inc.* (1978) 84 Cal.App.3d 982 [149 Cal.Rptr. 119] in support of their argument. There, plaintiffs obtained a judgment awarding fraud and punitive damages against two affiliated corporations. The trial court, however, had entered a judgment of nonsuit in favor of the corporate parent. In affirming the judgment, the appellate court stated: "We conclude that more is required than solely a parent-subsidiary corporate relationship to create liability of a parent for the actions of its subsidiary. [¶] ... The sole basis for holding [the parent] liable would be to enable the plaintiffs to obtain an increased award of punitive damages because of the substantial net worth of the parent. There is no factual justification to do so." (*Id.* at p. 1001.) The present case is obviously distinguishable from *Walker*. Hahn Inc. act-

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

ively participated in the sale of the shopping center from the very beginning to the very end. Hence, there is a sufficient factual basis for allowing buyers to pierce the corporate veil of Devcorp.

Finally, as explained in the next section, we have reduced substantially the jury's award of compensatory and punitive damages. Still, we think it appropriate to maintain Hahn Inc.'s liability for the judgment. Even though at trial the parties stipulated that Devcorp was worth \$4.1 million, it is unclear from the record how much of that amount is composed of buyers' promissory note, which buyers presumably have been paying down throughout this litigation. Moreover, buyers suggest in their respondent's brief that by the time this appeal becomes final, sellers could totally deplete Devcorp of all its assets. *1252

For all the above reasons, we will uphold the trial court's determination that Devcorp is the alter ego of Hahn Inc.

V. Whether the \$1.27 Million Fraud Award Is Excessive as a Matter of Law

We agree with sellers that the \$1.27 million fraud award is excessive, but not on the grounds urged by them. Before oral argument we requested counsel to address whether the injurious effect of the fraud was limited to the value of the lease guaranties or rather infected the total worth of the shopping center. (See Gov. Code, § 68081.) Because we now conclude that the record is devoid of any substantial evidence indicating that sellers' tortious conduct resulted in buyers incurring \$1.2 million in damages, that award must be reversed.

(15) Although the law commits the responsibility for determining the amount of damages suffered by a plaintiff to the jury, its decision cannot be allowed to stand where the award as a matter of law is excessive, or is so grossly disproportionate as to raise a presumption that the panel based its result on passion or prejudice. (*Cunningham v. Simpson* (1969) 1 Cal.3d 301, 308-309 [81 Cal.Rptr. 855, 461 P.2d 39]; *Fagerquist v. Western Sun Aviation,*

Inc. (1987) 191 Cal.App.3d 709, 727 [236 Cal.Rptr. 633].)

(16) To recover damages for fraud, a plaintiff must have sustained damages proximately caused by the misrepresentation. (*State Farm Mut. Auto. Ins. Co. v. Allstate Ins. Co.* (1970) 9 Cal.App.3d 508, 528 [88 Cal.Rptr. 246]; §§ 3333, 3343, subd. (a)(4)(iii).) A damage award for fraud will be reversed where the injury is not related to the misrepresentation. (*Gray v. Don Miller & Associates, Inc., supra*, 35 Cal.3d 498, 504.)

For fraud arising out of the purchase, sale, or exchange of property, section 3343 provides that a plaintiff is entitled to his "out-of-pocket" damages. The formula for determining "out-of-pocket" losses under the statute is the difference between the actual value of what the defrauded person parted with and the actual value of what he received in return. The statute also allows a plaintiff under certain conditions to recover his lost profits as a form of consequential damages. (§ 3343, subd. (a)(4).)

When considered against these standards, the shopping center's appraised value in 1982 simply cannot constitute substantial evidence to support a causal connection between sellers' fraud and \$1.27 million in damages. First, buyers' counsel admitted in closing argument before the jury that he never seriously considered \$1.27 million to be the extent of his clients' damages. *1253 Second, sellers did not misrepresent the value of the shopping center. Their wrongful conduct was to guaranty the leases without any intent to honor the obligations. Lastly, Thomas Marshall (sellers' appraiser) testified that his valuation of the property took into account the rental income based on an industry average of a 94 percent occupancy rate. As such, the appraisal encompassed the rents from the Phanny's Phudge and Franchise leases. With those rents included in the appraisal, any diminution in the property's value had to arise separate and apart from the fraudulent acts of sellers. Hence, the appraisal at best only demonstrated that buyers overpaid for the shopping center because they misjudged its worth.

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

As an alternative basis for damages, buyers' counsel at oral argument proposed that we reduce the fraud award to \$639,878, the amount his clients paid for capitalizing the Phanny's Phudge and Franchise leases. Again, we have come across no evidence in the record for finding a sufficient relationship between sellers' fraud and a \$639,878 loss incurred by buyers. Sellers did not misrepresent or hide from buyers the financial conditions of Phanny's Phudge and Franchise. By their own admissions, buyers knew at the time of closing that these two tenants were commercially unsound. It seems self-evident that when a purchaser of rental property capitalizes a stream of future income he or she assumes the risk of insolvencies, economic turn downs, and depressed property values. A prudent buyer would thus take these risks into consideration and negotiate for a capitalization rate sufficient to protect his investment.

We realize, of course, that the guaranties, acting as a form of insurance, would influence a buyer in his choice of a capitalization rate. Common sense dictates the greater the protection offered by the guaranty, the more a buyer will pay for the stream of income. In this regard, sellers' wrongful conduct had some measurable effect on the value placed on the Phanny's Phudge and Franchise leases. We would bestow, however, an extraordinary windfall on buyers if we allowed them to recover damages for that portion of the capitalized rents left untainted by the fraud. Here, it is difficult to perceive how the fraud was a substantial factor in causing \$639,878 in damages. The capitalization rate in the instant case was set at 7 percent in 1978 and remained the same at closing, even though buyers had knowledge of the financial difficulties facing Phanny's Phudge and Franchise. One would think that if buyers had desired to shift more of the risk of these long-term leases to sellers, buyers would have negotiated guaranties lasting beyond the payment of three or six consecutive months of rents. This buyers did not do, perhaps because of sellers' superior bargaining power. On the other hand, *1254 buyers may have settled for such minimal

protection because they believed suitable replacement tenants could be secured with little effort.

In any event, it plainly appears that in regard to the capitalization of the rents, the lease guaranties were not the driving force behind the deal. Analyzed in this light, the causal relationship between the fraud and a devaluation of the capitalized rents is too tenuous to support an award of \$639,878.

In our view, the damages resulting from sellers' fraud must be limited to the diminished value of the lease guaranties. This is where the strongest line of causation exists. It is also where the most reliable evidence of buyers' damages can be found. While it would be approaching mere speculation to place a market value on the guaranties under these facts, a true gauge of their worth can be established under the lost profit provision of section 3343. Subdivision (a)(4) of the statute permits a victim of fraud to recover "an amount which will compensate him for any loss of profits or other gains which were reasonably anticipated and would have been earned by him from the use or sale of the property had it possessed the characteristics fraudulently attributed to it by the party committing the fraud" The subdivision further commands, however, that lost profits can only be sought if the defrauded party acquired the property for profit, reasonably relied on the fraud, and that his damages were proximately caused by the wrongful conduct. All of these conditions are met in the case at bar.

A defrauded party need not prove an "out-of-pocket" loss before seeking consequential damages. (*Stout v. Turney* (1978) 22 Cal.3d 718, 729-730 [150 Cal.Rptr. 637, 586 P.2d 1228].) His damages, though, must be measured from the date the promise is breached, not when the promise was made. (*Glendale Fed. Sav. & Loan Assn. v. Marina View Heights Dev. Co.*, *supra*, 66 Cal.App.3d 101, 145-146; see also *Pao Ch'en Lee v. Gregoriou* (1958) 50 Cal.2d 502, 505 [326 P.2d 135].) Here, we are presented with multiple breaches transpiring each time sellers refused to pay the rents owed under the guaranties. In its award for breach of con-

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
 (Cite as: 235 Cal.App.3d 1220)

tract, the jury found that the breaches occurred each month until the guaranties terminated in 1986. Since that award (\$232,393) effectively compensated buyers for their lost profits, it is also the appropriate measure of buyers' damages under the fraud theory. Finally, because the breach of contract award has been left unchallenged by sellers, its utilization also allows us to modify the fraud award without the need of a new trial.

VI. *Whether the Punitive Damage Award Must Also Be Reduced*

Sellers insist the punitive damage award cannot be upheld because there is no reasonable relationship between the award's size and (1) the reprehensibility *1255 of their conduct; (2) the injuries suffered by buyers; and, (3) their net worth. (See *Neal v. Farmers Ins. Exchange, supra*, 21 Cal.3d 910, 928.) (17a) In light of our holding that the jury's \$1.27 million fraud award was not supported by substantial evidence, we agree that the \$10 million award for punitive damage must be reduced.

(18) The public policy behind punitive damages is to prevent future misdeeds by punishing the wrongdoer and making an example out of him for others not to follow. (*Adams v. Murakami, supra*, 54 Cal.3d 105, 110.) While on appeal all three factors set forth in *Neal* must be satisfied, the "most important question is whether the amount of the punitive damages award will have deterrent effect-without being excessive." (*Id.* at p. 111.)

(17b) Here, a \$10 million award would be grossly disproportionate both in comparison to buyers' compensatory losses and the gravity of sellers' misconduct. The case at bar is not an instance of a heartless conglomerate oppressively depriving a widow and her small children of the family homestead. Buyers were sophisticated real estate developers with the financial resources to weather the type of sharp business practices found in the present litigation.

This is not to say that sellers' wrongdoing should go unpunished. We conclude, however, that

the ends of justice and judicial economy require us to limit the punitive damage award to \$2 million. First, a \$2 million award generally preserves the jury's 7.9 to 1 ratio between compensatory and punitive damages. Based on the evidence presented, such a ratio is well within reason, and with the reduced compensatory damages, results in a punishment that is commensurate with sellers' culpability.

Second, we believe a \$2 million award still sends a forceful message to sellers that they cannot fraudulently induce parties to enter into agreements without penalty. Besides punishing sellers, the award also acts as a deterrent against future misconduct. Although sellers have a combined net worth of nearly a half billion dollars, they will no doubt think twice before fraudulently entering into another contract.

Lastly, the trial below was an arduous and exhaustive affair, spanning more than one month. Buyers left no stone unturned in proving the reprehensibility of sellers' fraud. There is little likelihood that at a retrial buyers could produce additional evidence establishing sellers were guilty of any greater wrongdoing than shown by the record which now exists. In other words, the litigation below has set the "outer limits" of sellers' punishment. While the amount of punitive damages to be awarded is within the discretion *1256 of the jury, any amount higher than \$2 million would certainly be the result of passion and prejudice. When required by justice, a reviewing court should modify a punitive damage award to ensure that the public policies behind its making are served. (*Allard v. Church of Scientology* (1976) 58 Cal.App.3d 439, 453 [129 Cal.Rptr. 797]; *Gerard v. Ross* (1988) 204 Cal.App.3d 968, 980 [251 Cal.Rptr. 604].)

As their last complaint, sellers contend California's system for imposing punitive damages violates both their state and federal constitutional rights to due process. Specifically, they urge that California law is unconstitutional because defendants cannot predict the size of a possible award and juries are given inadequate guidelines for assessing penalties.

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

Today, the constitutionality of punitive damages, both on the state and federal levels, is a major topic of discussion. The California Supreme Court has recently held that the plaintiff must prove a defendant's wealth before punitive damages can be imposed. (*Adams v. Murakami, supra*, 54 Cal.3d 105, 123.) Additionally, the United States Supreme Court within this year has determined that the common law approach to awarding punitive damages is not per se unconstitutional. (*Pacific Mut. Life Ins. Co. v. Haslip* (1991) 499 U.S. ___ [113 L.Ed.2d 1, 111 S.Ct. 1032].) Under the common law method, "[T]he amount of the punitive damages is initially determined by a jury instructed to consider the gravity of the wrong and the need to deter similar wrongful conduct. The jury's determination is then reviewed by trial and appellate courts to ensure that it is reasonable." (499 at p. ___ [113 L.Ed.2d at p. 18, 111 S.Ct. at p. 1042].)^{FN7}

FN7 Section 3294 is California's codification of the common law on punitive damages. (*Bertero v. National General Corp.* (1974) 13 Cal.3d 43, 66, fn. 13 [118 Cal.Rptr. 184, 529 P.2d 608, 65 A.L.R.3d 878].)

The high court in *Haslip* held that Alabama's system of awarding and reviewing punitive damage verdicts provided Pacific Mutual with due process of law. The trial court there had instructed the jury on the purpose of punitive damages, that the making of an award was discretionary, and that the panel " 'must take into consideration the character and the degree of the wrong as shown by the evidence and necessity of preventing similar wrong.' [Citation.]" (499 at p. ___ [113 L.Ed.2d at p. 20, 111 S.Ct. at p. 1044].)

Secondly, the *Haslip* court noted that on a postverdict challenge to a punitive damage award, trial courts in Alabama are required to reflect on the record their reasons for either approving or disturbing the verdict. Moreover, the factors which the trial courts in Alabama can consider are the culpability *1257 of the defendant, the need to deter, and

the impact on the parties, including third persons. (499 U.S. at p. ___ [113 L.Ed.2d at p. 20, 111 S.Ct. at p. 1044].)

Lastly, the court in *Haslip* pointed out that Alabama's Supreme Court measured punitive damage verdicts against a number of criteria "to ensure that the award does 'not exceed an amount that will accomplish society's goals of punishment and deterrence.' [Citations.]" (499 U.S. at p. ___ [113 L.Ed.2d at p. 22, 111 S.Ct. at p. 1045].)

In contrast, the California Supreme Court in *Adams* recognized that the basis for review of punitive damage verdicts in our state (setting them aside when the awards are deemed to be the result of passion or prejudice) may not pass constitutional scrutiny because it resembles other state schemes criticized in *Haslip*. (*Adams v. Murakami* at p. 118, fn. 9.) The *Adams* Court, however, refused to consider the issue, noting that it and the United States Supreme Court had remanded a number of decisions back to the California Court of Appeal for further consideration in light of *Haslip*. (*Ibid.*)

(19a) Addressing sellers' contentions, we first disagree with the notion that California juries are given inadequate guidelines to award punitive damages. In the instant case, the jury was instructed that an award of punitive damages was discretionary, and could only be made if they found sellers guilty of oppression, fraud, or malice. Additionally, the court informed the panel that punitive damages are awarded "for the sake of example and by way of punishment."

The trial court also directed the jury that "[i]n arriving at any award of punitive damages, you are to consider the following: [¶] 1. The reprehensibility of the conduct of [sellers]; [¶] 2. The amount of punitive damages which will have a deterrent effect on the [sellers] in light of [sellers'] financial condition; and [¶] 3. That the punitive damages must bear a reasonable relation to the injury, harm, or damage actually suffered by [buyers]." (See generally BAJI No. 14.71 (7th ed. 1989 rev. mod.) We

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

think these instructions offer the same degree of protection against arbitrary jury decisions as found constitutionally acceptable in *Haslip*.

Secondly, the “passion and prejudice” standard of posttrial and appellate review required by California law does afford sellers an additional safeguard to ensure that the jury’s award has not exceeded “an amount that will accomplish society’s goals of punishment and deterrence.” (*Pacific Mut. Life Ins. Co. v. Haslip*, *supra*, 499 U.S. ___ [113 L.Ed.2d 1, 22, 111 S.Ct. 1032, 1045].) *1258

(20) On a motion for new trial, the trial court sits in its role as an independent trier of fact and may “[d]isbelieve witnesses, reweigh evidence and draw reasonable inferences that are contrary to those drawn by the jury.” [Citation.]” (*Sanchez v. Hasencamp* (1980) 107 Cal.App.3d 935, 944 [166 Cal.Rptr. 118]; *Neal v. Farmers Ins. Exchange*, *supra*, 21 Cal.3d 910, 933; *Grimshaw v. Ford Motor Co.* (1981) 119 Cal.App.3d 757, 823 [174 Cal.Rptr. 348].) ^{FN8}

FN8 Unlike in Alabama, California law does not mandate that the trial court state on the record why it refused to interfere with the award. However, the trial court must specify in the record its reasons for disturbing the verdict. (*Neal v. Farmers Ins. Exchange*, *supra*, 21 Cal.3d 910, 931; § 657.) Requiring a statement of reasons in the latter situation, serves the purpose of “‘encourag[ing] careful deliberation by the trial court before ruling on the new trial motion and [making] a sufficiently precise record to permit meaningful appellate review’ [citation].” (*Neal*, *supra*, 21 Cal.3d at p. 931.) While an explanation of the trial court’s decision to uphold the verdict would give an added degree of protection, we think, on the whole, California law affords defendants enough safeguards to satisfy the requirements of due process.

Although the trial court’s denial of a motion for

new trial should be given deference, an appellate court has the responsibility to intervene when the verdict is so palpably excessive to raise the presumption of passion and prejudice. (*Dumas v. Stocker* (1989) 213 Cal.App.3d 1262, 1266 [262 Cal.Rptr. 311]. Appellate courts must scrutinize punitive damage verdicts because they “constitute a windfall, create the anomaly of excessive compensation, and are therefore not favored in the law. [Citation.]” (*Ibid.*, fn. omitted.)

(19b) Moreover, application of the “passion and prejudice” standard does not occur in a vacuum, but is measured against the identical criteria utilized by the jury: reprehensibility of defendant’s misdeeds, the ratio between the compensatory and punitive damages, and the relationship between the punitive damages and defendant’s net worth. (*Neal v. Farmers Ins. Exchange*, *supra*, 21 Cal.3d 910, 928; *Adams v. Murakami*, *supra*, 54 Cal.3d 105, 110-111; *Burnett v. National Enquirer, Inc.* (1983) 144 Cal.App.3d 991, 1010-1011 [193 Cal.Rptr. 206, 49 A.L.R.4th 1125].) This quantum of critical evaluation thus makes certain that punitive damage verdicts will be limited to that amount of money necessary to accomplish the public policy of punishment and deterrence. In sum, the “passion and prejudice” test affords in posttrial proceedings and on appeal the same general degree of scrutiny as found in the Alabama review process. ^{FN9} (See *1259 *Liberty Transport, Inc. v. Harry W. Gorst. Co.* (1991) 229 Cal.App.3d 417, 441 [280 Cal.Rptr. 159].) It is only when the award exceeds the amount needed to accomplish the goal of punishment and deterrence that an appellate court can conclude the jury acted on its passion and prejudice.

FN9 The court in *Haslip* also observed that under Alabama law a reviewing tribunal can evaluate a punitive damage award in light of the duration of the defendant’s conduct; defendant’s awareness and concealment of its acts; the existence and frequency of similar past conduct; and the de-

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

sirability of disgorging defendant of its illicit gain. Additionally, the courts in Alabama can consider as mitigating circumstances the imposition of criminal sanctions and the existence of other civil awards against the defendant for the same conduct. (*Pacific Mut. Life Ins. Co. v. Haslip*, *supra*, 499 U.S. at p. ___ [113 L.Ed.2d at p. 22, 111 S.Ct. at p. 1045].) We think the basic structure of the *Neal* test affords a defendant the opportunity to raise these and other relevant factors to attack the jury's punitive damage verdict.

In the instant case, we have painstakingly detailed sellers' fraudulent conduct, taken notice of their net worth, and considered the amount of compensatory damages they caused buyers. From that, we have determined the punitive damage award must be reduced to \$2 million to keep it in line with the actual compensatory losses suffered by buyers. In making its decision, the jury concluded that only a multimillion dollar damage award would be sufficient to punish and deter buyers. We agree. However, as we have already stated, in view of the fact that the actual amount of buyers' compensatory damages is \$232,393, a punitive damage award exceeding \$2 million would be excessive.

Finally, sellers insist that California's punitive damage law offends due process because a defendant is given no fair notice of the possible size of a punitive damage verdict. The argument is meritless. Seldom does an intentional tortfeasor know the extent of his liability at the time of his wrongful act. If what sellers are contending is that there should be a fixed ceiling on punitive damage liability regardless of whether that amount would punish and deter, then the proper audience for that idea is the California Legislature.

VII. *The Award of Contractual Attorney's Fee Must Be Reversed*

A party is barred from collecting contractual attorney's fees in an action for fraud. (*Schlocker v. Schlucker* (1976) 62 Cal.App.3d 921 [133

Cal.Rptr. 485]; see also *Stout v. Turney*, *supra*, 22 Cal.3d 718, 730.) In their respondent's brief, buyers in effect have stated they desire to take under their fraud action. The award of contractual attorney's fees allocated to prosecute that claim, therefore, must be reversed. (21) However, sellers' declaratory relief lawsuit, which alleged that they had no liability to buyers due to the occurrence of certain events contemplated by the guaranties, clearly was "an action on the contract" within the meaning of subdivision (a) of section 1717.^{FN10} Hence, buyers as the prevailing party in that litigation are *1260 entitled to recover their reasonable attorney's fees incurred in the defense of that action.

FN10 That section commands, in relevant part: "In any action on a contract, where the contract specifically provides that attorney's fees and costs, which are incurred to enforce that contract, shall be awarded either to one of the parties or to the prevailing party, then the party who is determined to be the party prevailing on the contract, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's fees in addition to other costs. ..."

VIII. *Sellers' Other Contentions*

Sellers have raised numerous other issues that we have reviewed and find unnecessary to discuss.

Disposition

The judgment is modified to reflect our decision to reduce respondents' award of fraud damages to \$232,393 and the award of punitive damages to \$2 million and is otherwise affirmed. The matter is remanded to the trial court for its determination and award of attorney's fees incurred by respondents in defense of appellants' declaratory relief action. Each side is to bear its own costs of appeal.

Gates, Acting P. J., and Fukuto, J., concurred.

Respondents' petition for review by the Supreme Court was denied February 11, 1992. *1261

235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301
(Cite as: 235 Cal.App.3d 1220)

Cal.App.2.Dist.
Las Palmas Associates v. Las Palmas Center Asso-
ciates
235 Cal.App.3d 1220, 1 Cal.Rptr.2d 301

END OF DOCUMENT

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

H

Court of Appeal, Third District, California.
Donna LEEK et al., Plaintiffs and Appellants,

v.

Jay COOPER, Defendant and Respondent.
Larry Leonardo, Plaintiff and Appellant,

v.

Jay Cooper, Defendant and Respondent.

Nos. C061510, C063152.

April 15, 2011.

Background: Employees of a corporate-owned car dealership brought actions against corporation and its sole shareholder, alleging causes of action for age discrimination under the California Fair Employment and Housing Act (FEHA) and violation of the California Family Rights Act. The Superior Court, Placer County, Nos. SCV21570 and SCV21571, Larry D. Gaddis, J., and Margaret E. Wells, Court Commissioner, granted shareholder's motions for summary judgment and for attorney's fees and costs. Employees appealed.

Holdings: The Court of Appeal, Blease, J., held that:

- (1) shareholder was not employees' "employer";
- (2) employees did not adequately plead alter ego theory of liability;
- (3) employees failed to show an inequitable result if corporation and shareholder were not treated as one in the same, as required for leave to amend;
- (4) were not completely groundless, frivolous, unreasonable or without foundation, as required for award of attorney fees to shareholder; and
- (5) shareholder was not entitled to appellate fees and costs.

Reversed in part; otherwise affirmed.

West Headnotes

[1] Civil Rights 78 ↪1113

78 Civil Rights

78II Employment Practices

78k1108 Employers and Employees Affected

78k1113 k. Individuals as "employers".

Most Cited Cases

Labor and Employment 231H ↪347

231H Labor and Employment

231HVI Time Off; Leave

231Hk343 Employers Affected

231Hk347 k. Individuals as "employers".

Most Cited Cases

Corporate employer's sole shareholder was not employees' "employer" for purposes of employees' California Fair Employment and Housing Act (FEHA) and Family Rights Act claims, even if he exercised a right of control over them. West's Ann.Cal.Gov.Code §§ 12940, 12945.1.

[2] Civil Rights 78 ↪1736

78 Civil Rights

78V State and Local Remedies

78k1734 Persons Protected, Persons Liable, and Parties

78k1736 k. Employment practices. Most Cited Cases

Individuals may be held liable under California Fair Employment and Housing Act (FEHA) for harassment. West's Ann.Cal.Gov.Code § 12900.

[3] Civil Rights 78 ↪1736

78 Civil Rights

78V State and Local Remedies

78k1734 Persons Protected, Persons Liable, and Parties

78k1736 k. Employment practices. Most Cited Cases

Only an employer may be liable for discrimination under the California Fair Employment and Housing Act (FEHA). West's Ann.Cal.Gov.Code § 12940.

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

[4] Civil Rights 78 ↪1113

78 Civil Rights

78II Employment Practices

78k1108 Employers and Employees Affected

78k1113 k. Individuals as "employers".

Most Cited Cases

Corporations and Business Organizations 101

↪1064

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1057 Particular Occasions for Determining Corporate Entity

101k1064 k. Labor and employment liabilities and violations. Most Cited Cases

A determination that a person is the alter ego of a corporate employer does not make the alter ego an employer under the California Fair Employment and Housing Act (FEHA); rather it makes the alter ego liable for the obligations of the corporation. West's Ann.Cal.Gov.Code § 12940.

[5] Corporations and Business Organizations

101 ↪1039

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1039 k. Alter ego in general. Most Cited Cases

Where a third party seeks to hold the sole shareholder liable for the wrongdoing of the corporation, an alter ego theory is the appropriate way to determine whether the shareholder is liable.

[6] Corporations and Business Organizations

101 ↪1011

101 Corporations and Business Organizations

101I Nature and Theory of Incorporation

101k1010 Corporation as Distinct Entity

101k1011 k. In general. Most Cited Cases
Ordinarily, a corporation is regarded as a legal

entity, separate and distinct from its stockholders, officers and directors, with separate and distinct liabilities and obligations.

[7] Corporations and Business Organizations

101 ↪1037

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1037 k. Justice and equity in general.

Most Cited Cases

The corporate form will be disregarded only in narrowly defined circumstances and only when the ends of justice so require.

[8] Corporations and Business Organizations

101 ↪1037

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1037 k. Justice and equity in general.

Most Cited Cases

Corporations and Business Organizations 101

↪1039

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1039 k. Alter ego in general. Most Cited Cases

Before a corporation's obligations can be recognized as those of a particular person, the requisite unity of interest and inequitable result must be shown.

[9] Corporations and Business Organizations

101 ↪1085(2)

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

101k1079 Actions to Pierce Corporate Veil
101k1085 Pleading
101k1085(2) k. Justice and equity in general. Most Cited Cases

Corporations and Business Organizations 101
↪1085(4)

101 Corporations and Business Organizations
101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil
101k1085 Pleading
101k1085(4) k. Alter ego, instrumentality, or agency in general. Most Cited Cases

Employees did not adequately plead alter ego theory of liability against corporate employer's sole shareholder, and thus shareholder was not required to show that claim could not be established in order to be entitled to summary judgment on discrimination claims under the California Fair Employment and Housing Act (FEHA) and Family Rights Act claims on grounds that shareholder was not employees' "employer" as required for liability; employees' allegations in their pleadings, including that they were employed by corporation and shareholder, that shareholder was the sole owner of the corporation and made all of its business decisions, and that employees were employer's and shareholder's employees, neither specifically alleged alter ego liability, nor alleged facts showing a unity of interest and inequitable result from treatment of the corporation as the sole actor, and complaint contained no allegations that shareholder should be held liable for the corporation's wrongdoing. West's Ann.Cal.Gov.Code §§ 12940, 12945.1.

See *Cal. Jur. 3d, Corporations*, § 22 et seq.; 9 *Witkin, Summary of Cal. Law (10th ed. 2005) Corporations*, § 9 et seq.; *Friedman, Cal. Practice Guide: Corporations (The Rutter Group 2010)* ¶ 2:51 (CACORPS Ch. 2-B); *Flahavan et al., Cal. Practice Guide: Personal Injury (The Rutter Group 2010)* ¶ 2:2018 (CAPI Ch. 2(II)-J); *Cal. Civil Practice (Thomson Reuters 2011) Business Litigation*, §§ 5:9, 5:10.

[10] Judgment 228 ↪183

228 Judgment
228V On Motion or Summary Proceeding
228k182 Motion or Other Application
228k183 k. In general. Most Cited Cases
The function of the pleadings in a motion for summary judgment is to delimit the scope of the issues.

[11] Judgment 228 ↪181(2)

228 Judgment
228V On Motion or Summary Proceeding
228k181 Grounds for Summary Judgment
228k181(2) k. Absence of issue of fact.
Most Cited Cases

Judgment 228 ↪183

228 Judgment
228V On Motion or Summary Proceeding
228k182 Motion or Other Application
228k183 k. In general. Most Cited Cases
The pleadings are the outer measure of materiality in a summary judgment proceeding.

[12] Judgment 228 ↪181(11)

228 Judgment
228V On Motion or Summary Proceeding
228k181 Grounds for Summary Judgment
228k181(5) Matters Affecting Right to Judgment
228k181(11) k. Sufficiency of pleading. Most Cited Cases

The summary judgment procedure presupposes that the pleadings are adequate to put in issue a cause of action or defense thereto.

[13] Judgment 228 ↪181(11)

228 Judgment
228V On Motion or Summary Proceeding
228k181 Grounds for Summary Judgment
228k181(5) Matters Affecting Right to Judgment

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

228k181(11) k. Sufficiency of pleading. Most Cited Cases

Judgment 228 ⚡183

228 Judgment

228V On Motion or Summary Proceeding

228k182 Motion or Other Application

228k183 k. In general. Most Cited Cases

A pleading may be defective in failing to allege an element of a cause of action or in failing to intelligibly identify a defense thereto; in such a case, the party moving for summary judgment need not address a missing element or respond to assertions which are unintelligible or make out no recognizable legal claim.

[14] Pleading 302 ⚡8(1)

302 Pleading

302I Form and Allegations in General

302k8 Matters of Fact or Conclusions

302k8(1) k. In general. Most Cited Cases

Pleading 302 ⚡48

302 Pleading

302II Declaration, Complaint, Petition, or Statement

302k48 k. Statement of cause of action in general. Most Cited Cases

Pleading 302 ⚡72

302 Pleading

302II Declaration, Complaint, Petition, or Statement

302k72 k. Prayer for relief. Most Cited Cases

Although California courts take a liberal view of inartfully drawn complaints, it remains essential that a complaint set forth the actionable facts relied upon with sufficient precision to inform the defendant of what plaintiff is complaining, and what remedies are being sought.

[15] Pleading 302 ⚡48

302 Pleading

302II Declaration, Complaint, Petition, or Statement

302k48 k. Statement of cause of action in general. Most Cited Cases

Fairness dictates that a complaint give the defendant sufficient notice of the cause of action stated to be able to prepare the case.

[16] Corporations and Business Organizations 101 ⚡1085(4)

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil

101k1085 Pleading

101k1085(4) k. Alter ego, instrumentality, or agency in general. Most Cited Cases

To recover on an alter ego theory, a plaintiff need not use the words "alter ego" in the pleadings, but must allege sufficient facts to show a unity of interest and ownership, and an unjust result if the corporation is treated as the sole actor.

[17] Corporations and Business Organizations 101 ⚡1085(9)

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil

101k1085 Pleading

101k1085(9) k. Number and relation of shareholders. Most Cited Cases

An allegation in the pleadings that a person owns all of the corporate stock and makes all of the management decisions is insufficient to cause the court to disregard the corporate entity.

[18] Corporations and Business Organizations 101 ⚡1039

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

101k1035 Reasons and Justifications

101k1039 k. Alter ego in general. Most

Cited Cases

The essence of the alter ego doctrine is not that the individual shareholder becomes the corporation, but that the individual shareholder is liable for the actions of the corporation; for all other purposes, the separate corporate existence remains.

[19] Corporations and Business Organizations
101 ↪1085(2)

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil

101k1085 Pleading

101k1085(2) k. Justice and equity in general. Most Cited Cases

Employees failed to show an inequitable result if corporate employer and its sole shareholder were not treated as one in the same, as required for leave during summary judgment hearing to amend California Fair Employment and Housing Act (FEHA) and Family Rights Act complaints to add alter ego allegations; there was no evidence regarding the corporation's financial situation, or the amount or nature of corporate assets, or whether the corporation was adequately capitalized, there was no evidence the corporation was a mere sham or shell, nor was there evidence shareholder had diverted assets from the corporation to avoid paying creditors, but rather employees merely contended that shareholder might raid the corporate coffers based upon the fact that he raised rent substantially in the past. West's Ann.Cal.Gov.Code §§ 12940, 12945.1.

[20] Judgment 228 ↪185(5)

228 Judgment

228V On Motion or Summary Proceeding

228k182 Motion or Other Application

228k185 Evidence in General

228k185(5) k. Weight and sufficiency.

Most Cited Cases

Judgment 228 ↪185.2(4)

228 Judgment

228V On Motion or Summary Proceeding

228k182 Motion or Other Application

228k185.2 Use of Affidavits

228k185.2(4) k. Showing to be made on opposing affidavit. Most Cited Cases

Where the parties have had sufficient opportunity adequately to develop their factual cases through discovery and the defendant has made a sufficient showing that the plaintiff's action has no merit, in order to avert summary judgment the plaintiff must produce substantial responsive evidence sufficient to establish the existence of a triable issue of material fact on the issues raised by the plaintiff's causes of action.

[21] Corporations and Business Organizations
101 ↪1038

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1038 k. Fraud or illegal acts in general. Most Cited Cases

Several factors are to be considered in applying the alter ego doctrine; among them are commingling of funds and other assets, failure to segregate funds of the separate entities, and the unauthorized diversion of corporate funds or assets to other than corporate uses, the treatment by an individual of the assets of the corporation as his own, the failure to obtain authority to issue stock or to subscribe to or issue the same, the holding out by an individual that he is personally liable for the debts of the corporation, the failure to maintain minutes or adequate corporate records, sole ownership of all of the stock in a corporation by one individual or the members of a family, the failure to adequately capitalize a corporation, the total absence of corporate assets, and undercapitalization, the use of a corporation as a mere shell, instrumentality or conduit for a single venture or the business of an individual or another corporation, the concealment and misrepresentation

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

of the identity of the responsible ownership, management and financial interest, or concealment of personal business activities, the disregard of legal formalities and the failure to maintain arm's length relationships among related entities, the use of the corporate entity to procure labor, services or merchandise for another person or entity, the diversion of assets from a corporation by or to a stockholder or other person or entity, to the detriment of creditors, or the manipulation of assets and liabilities between entities so as to concentrate the assets in one and the liabilities in another, the contracting with another with intent to avoid performance by use of a corporate entity as a shield against personal liability, or the use of a corporation as a subterfuge of illegal transactions, and the formation and use of a corporation to transfer to it the existing liability of another person or entity.

[22] Corporations and Business Organizations
101 ↪1043

101 Corporations and Business Organizations
101III Disregarding Corporate Entity; Piercing Corporate Veil

101k1042 Factors Considered

101k1043 k. In general. Most Cited Cases

No single factor is determinative when considering alter ego liability, and the result depends on the circumstances of each particular case.

[23] Corporations and Business Organizations
101 ↪1088

101 Corporations and Business Organizations
101III Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil

101k1088 k. Questions of law or fact.
Most Cited Cases

Whether a party is liable under an alter ego theory is a question of fact.

[24] Corporations and Business Organizations
101 ↪1031

101 Corporations and Business Organizations
101III Disregarding Corporate Entity; Piercing Corporate Veil

101k1031 k. Nature of remedy. Most Cited Cases

A claim based upon an alter ego theory is not itself a claim for substantive relief; it is a procedural device by which courts will disregard the corporate entity in order to hold the alter ego individual liable on the obligations of the corporation.

[25] Judgment 228 ↪310

228 Judgment

228VIII Amendment, Correction, and Review in Same Court

228k310 k. Parties. Most Cited Cases

Under some circumstances a judgment against a corporation may be amended to add a nonparty alter ego as a judgment debtor; this is an equitable procedure based on the theory that the court is not amending the judgment to add a new defendant but is merely inserting the correct name of the real defendant. West's Ann.Cal.C.C.P. § 187.

[26] Corporations and Business Organizations
101 ↪1080

101 Corporations and Business Organizations
101III Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil

101k1080 k. In general. Most Cited Cases

It is possible for a party to bring a wholly separate action against the individual to enforce a prior judgment against the corporation on an alter ego theory.

[27] Civil Rights 78 ↪1773

78 Civil Rights

78V State and Local Remedies

78k1771 Costs and Fees

78k1773 k. Employment practices. Most Cited Cases

Employees' California Fair Employment and

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

Housing Act (FEHA) claims against corporate employer's sole shareholder were not completely groundless, frivolous, unreasonable or without foundation, as required for award of attorney fees to shareholder; argument that shareholder was employees' actual employer based on amount of control, while incorrect, was a legitimate argument, and there was evidence relevant to some aspects of an alter ego theory of liability. West's Ann.Cal.Gov.Code § 12965(b).

[28] Civil Rights 78 ↪1773

78 Civil Rights

78V State and Local Remedies

78k1771 Costs and Fees

78k1773 k. Employment practices. Most Cited Cases

A prevailing defendant in an employment discrimination action under the California Fair Employment and Housing Act (FEHA) cannot recover attorney fees unless the action was unreasonable, frivolous, meritless or vexatious. West's Ann.Cal.Gov.Code § 12965(b).

[29] Civil Rights 78 ↪1773

78 Civil Rights

78V State and Local Remedies

78k1771 Costs and Fees

78k1773 k. Employment practices. Most Cited Cases

A prevailing plaintiff in an employment discrimination action under the California Fair Employment and Housing Act (FEHA) should ordinarily recover attorney's fees, absent special circumstances rendering such an award unjust. West's Ann.Cal.Gov.Code § 12965(h).

[30] Civil Rights 78 ↪1773

78 Civil Rights

78V State and Local Remedies

78k1771 Costs and Fees

78k1773 k. Employment practices. Most Cited Cases

A meritless case warranting an award of attorney's fees to a successful employer in a discrimination action under the California Fair Employment and Housing Act (FEHA) is one that is groundless or without a legal or factual basis. West's Ann.Cal.Gov.Code § 12965(h).

[31] Civil Rights 78 ↪1772

78 Civil Rights

78V State and Local Remedies

78k1771 Costs and Fees

78k1772 k. In general. Most Cited Cases

The trial court is required to make written findings when awarding attorney fees to defendants under the California Fair Employment and Housing Act (FEHA). West's Ann.Cal.Gov.Code § 12965(h).

[32] Appeal and Error 30 ↪1178(1)

30 Appeal and Error

30XVII Determination and Disposition of Cause 30XVII(D) Reversal

30k1178 Ordering New Trial, and Directing Further Proceedings in Lower Court

30k1178(1) k. In general. Most Cited Cases

If no findings are made, the Court of Appeal must reverse and remand an award of attorney's fees to a defendant in a discrimination action brought under the California Fair Employment and Housing Act (FEHA) absent a determination that no findings supporting the order reasonably could be made. West's Ann.Cal.Gov.Code § 12965(h).

[33] Costs 102 ↪260(5)

102 Costs

102X On Appeal or Error

102k259 Damages and Penalties for Frivolous Appeal and Delay

102k260 Right and Grounds

102k260(5) k. Nature and form of judgment, action, or proceedings for review. Most Cited Cases

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

Employees' appeal of grant of summary judgment to corporate employer's sole shareholder on California Fair Employment and Housing Act (FEHA) claims was not frivolous as required for award of appellate attorney's fees and costs to shareholder; there was no evidence that appeal was taken solely to harass or delay, appeal was obviously not totally and completely without merit, as award of trial attorney's fees to shareholder was reversed on appeal, and, even as to that portion of the judgment affirmed, the appeal was not one that any reasonable attorney would agree was totally and completely devoid of merit. West's Ann.Cal.C.C.P. § 907.

**60 Kevin W. Harris, Sacramento, Martin F. Jennings, Jr., for Plaintiffs and Appellants.

Costa Law Firm, Daniel P. Costa, Gold River, Doreen R. Altman; Wright and Britton, John A. Britton, Roseville, for Defendant and Respondent.

BLEASE, J.

*405 This is a pleading case masquerading as a summary judgment case. Employees of a corporate-owned car dealership sued the corporation and its sole shareholder, alleging causes of action for age discrimination and violation of the California Family Rights Act. The trial court granted the shareholder's motions for summary judgment on the ground that only the corporation as the employer could be held liable for discrimination, and an alter ego theory was not pleaded in the complaint. The court further granted the shareholder's motion for attorney fees and costs pursuant to Government Code section 12965, subdivision (b).

Plaintiffs' claims regarding the merits of the summary judgment motion are twofold. They do not deny that only an employer may be liable to an *406 employee for discrimination under the California Fair Employment and Housing Act (FEHA) or for violation of the Family Rights Act. They claim that Cooper was an employer under the statutes, the proper test for determining who is an em-

ployer being the degree to which that person controls the employee. They also claim that Cooper is liable for the wrongdoing of the corporate employer under an alter ego theory.

The alter ego theory was tendered in a motion to amend their pleading to assert it as a ground of Cooper's liability. The plaintiffs did not make an offer of proof in support of the motion. Rather, they offered**61 the facts tendered in opposition to the motion for summary judgment as grounds justifying an amendment. The trial court denied the request on the ground the facts, if true, did not establish Cooper's liability as an alter ego of the corporation.

We shall conclude that Cooper's control over the employees is not the proper test to determine whether he was the actual employer. The essence of the alter ego doctrine is not that the individual shareholder becomes the corporation, but that the individual shareholder is liable for the actions of the corporation. (*Mesler v. Bragg Management Co.* (1985) 39 Cal.3d 290, 300, 216 Cal.Rptr. 443, 702 P.2d 601.) The proper method for determining whether the sole shareholder of a corporate employer is liable for the wrongdoing employer/corporation, is by the application of an alter ego theory. We agree with the trial court that plaintiffs did not adequately plead an alter ego theory of recovery in their complaint. This being the case, defendant Cooper was under no duty to negate an alter ego claim.

Plaintiffs attempted to raise the issue of alter ego in their opposition to the summary judgment motion. Because the facts they claimed to be undisputed were insufficient to state a claim of alter ego, it is not reasonably possible that they could amend their complaints to allege the theory, and the trial court did not abuse its discretion in denying leave to amend.

We shall reverse the portion of the judgment awarding attorney fees to Cooper because we do not find the action unreasonable, frivolous, meritless or vexatious. Likewise, we deny Cooper's mo-

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

tions for sanctions on appeal because we do not find the appeal frivolous.

FACTUAL AND PROCEDURAL BACKGROUND

We deal with two separate actions, which we have consolidated for purposes of oral argument and for this opinion. In the first action, plaintiffs Donna Leek, John Borden, and Cindy Buschmann alleged that they were *407 employed by Auburn Honda, a California corporation, and Cooper. ^{FN1} In the second action Leonardo also alleged that he was employed by Auburn Honda and Cooper. All plaintiffs alleged that Cooper is the sole owner of Auburn Honda, owning all of its stock and making all of its business decisions.

FN1. The actual name of the corporation is Auburn Associates, Inc. Auburn Honda is a dba. The parties nevertheless refer to the corporation as Auburn Honda, as do we.

At the time of their terminations, Leek was 49, Buschmann was 51, Borden was 66, and Leonardo was 56. All allege that they were replaced by substantially younger employees, and that Cooper told Leonardo he planned to get rid of older employees in order to reduce payroll expenses. Both actions alleged age discrimination pursuant to FEHA. (Gov.Code, § 12900 et seq.)

Leonardo's complaint additionally contained a cause of action for violation of the California Family Rights Act. (Gov.Code, § 12945.1 et seq.) The factual basis for this claim was that just prior to his termination Leonardo informed Cooper he needed to take leave to care for his terminally ill mother, that Cooper became enraged at the request, and that he informed Leonardo he had a business to run, which did not include taking care of old sick people.

Cooper filed an answer to each complaint that consisted of a general denial and numerous affirmative defenses, including the defense that he had no employer-employee relationship with the plaintiffs.

**62 Cooper then filed a motion for summary judgment in both actions. The basis for the motions for summary judgment was that Government Code section 12940, barring discrimination against employees, limits liability for discrimination to the employer, not to management personnel. With respect to the Leonardo complaint, Cooper argued the Family Rights Act and FEHA contain the same definition of an employer. Thus, he asserted the same argument with respect to his claim based on the Family Rights Act.

The plaintiffs responded to the summary judgment motion, arguing that Cooper was the alter ego of Auburn Honda on the apparent theory that Cooper was their employer. They pointed to evidence that Cooper was the president of Auburn Honda, and that there were no directors of the corporation, that Cooper "individually" fired the plaintiffs, that Cooper "individually" makes all policy, procedure, and management decisions for Auburn Honda, that Cooper "individually" owns the land on which the dealership is located, and that he raises the rent as he sees fit.

The trial court granted summary judgment as to both complaints. It ruled that pursuant to *408 *Reno v. Baird* (1998) 18 Cal.4th 640, 76 Cal.Rptr.2d 499, 957 P.2d 1333 (*Reno*), an individual manager or supervisor could not be held liable for discrimination under the FEHA. It further ruled that plaintiffs had not alleged alter ego liability in their complaint, thus the evidence proffered to that effect was unavailing. The court denied plaintiffs' request to amend the complaint to allege alter ego liability, finding that the evidence proffered was insufficient to establish alter ego liability.

The trial court granted Cooper's motions for attorney fees pursuant to Government Code section 12965, subdivision (b), providing that the court may, in its discretion, award reasonable attorney fees and costs to the prevailing party. Cooper was awarded a total of \$49,747.00 in attorney fees.

DISCUSSION

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

I

Employer Liability

[1][2] In *Reno, supra*, the California Supreme Court held that only the employer, not individual supervisory employees, may be held personally liable under FEHA for discriminatory hiring, firing, and personnel practices. (18 Cal.4th at p. 645, 76 Cal.Rptr.2d 499, 957 P.2d 1333.) By contrast, individuals may be held liable under FEHA for harassment. (*Ibid.*) In so holding, the Supreme Court agreed with an earlier Court of Appeal decision, *Janken v. GM Hughes Electronics* (1996) 46 Cal.App.4th 55, 53 Cal.Rptr.2d 741 (*Janken*), which reasoned that discrimination claims arise “out of the performance of necessary personnel management duties.” (*Id.* at p. 63, 53 Cal.Rptr.2d 741.) By contrast, harassment is not conduct necessary to personnel management, but is instead “conduct outside the scope of necessary job performance, conduct presumably engaged in for personal gratification, because of meanness or bigotry, or for other personal motives.” (*Ibid.*)

[3] It is thus settled that only an employer may be liable for discrimination under FEHA, and Leonardo does not argue that anyone other than an employer may be liable for violation of the Family Rights Act.

Notwithstanding plaintiffs' agreement with the conclusion that liability under the statutes in question extends only to employers, they argue that the policy reasons cited in *Reno* and *Janken, supra*, are inapplicable here. Leonardo argues a distinction **63 must be made because Cooper is the sole shareholder of the corporate employer and makes all of its management decisions. Specifically, he claims that this situation does not result in any conflict of interest between an individual supervisory employee and the employer that would have a chilling effect on management decisions.

*409 *Janken* and *Reno, supra*, expressed the opinion that imposing personal liability on individual supervisory employees would impair the exercise of supervisory judgment, creating conflicts

of interest and chilling effective management. (*Janken, supra*, 46 Cal.App.4th at p. 72, 53 Cal.Rptr.2d 741; *Reno, supra*, 18 Cal.4th at pp. 651–652, 76 Cal.Rptr.2d 499, 957 P.2d 1333.) They reasoned that holding supervisory employees liable: “would coerce the supervisory employee not to make the optimum lawful decision for the employer. Instead, the supervisory employee would be pressed to make whatever decision was least likely to lead to a claim of discrimination against the supervisory employee personally, or likely to lead only to that discrimination claim which could most easily be defended. The employee would thus be placed in the position of choosing between loyalty to the employer's lawful interests at severe risk to his or her own interests and family, versus abandoning the employer's lawful interests and protecting his or her own personal interests.” (*Janken, supra*, 46 Cal.App.4th at p. 74, 53 Cal.Rptr.2d 741, quoted in *Reno, supra*, 18 Cal.4th at p. 653, 76 Cal.Rptr.2d 499, 957 P.2d 1333.)

We agree that these policy reasons are not applicable in this case. Nevertheless, the Supreme Court has made clear that liability for discrimination extends only to the employer, and not to individual employees. Plaintiffs make no argument that liability rests with anyone but the employer. Instead, they argue that Cooper was in fact the employer because of the control he exercised over them. They point to tests other courts have employed to determine whether a person is an employee or independent contractor, whether a shareholder in a professional corporation is an employee for purposes of the Americans with Disabilities Act, or whether two corporations should be considered a single employer for Title VII purposes, and argue that those methods are appropriate for determining when a sole shareholder of an employer corporation may be considered an employer.

[4][5] We disagree. A determination that a person is the alter ego of a corporation does not make the alter ego an employer. Rather it makes the alter ego liable for the obligations of the corporation. In

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

this instance, where a third party seeks to hold the sole shareholder liable for the wrongdoing of the corporation, an alter ego theory is the appropriate way to determine whether the shareholder is liable. As demonstrated below, the cases cited by plaintiffs for determining who is an employer for other purposes are distinguishable.

Citing *Vernon v. State* (2004) 116 Cal.App.4th 114, 124, 10 Cal.Rptr.3d 121, plaintiffs argue that Cooper is an employer under the “totality of the circumstances” test. The goal of the “totality of the circumstances” test is to determine whether a worker is an employee or an independent contractor. (See *410 *Lambertsen v. Utah Dept. of Corrections* (10th Cir.1996) 79 F.3d 1024, 1028 fn. 1, cited in *Vernon v. State, supra*.) Many of the factors to be considered simply make no sense in the context of this case.

Thus, determining whether plaintiffs are paid a salary or other employment benefits, where the work is performed, the skill required of the work, the extent to which the work is done under the direction of a **64 supervisor, whether the work is part of the defendant's regular business operations, the duration of the relationship of the parties, and the duration of the plaintiffs' employment, does not provide any meaningful assistance in resolving whether Cooper as an individual was plaintiffs' employer. (See *Vernon v. State, supra*, 116 Cal.App.4th at p. 125, 10 Cal.Rptr.3d 121.)

Likewise, the test used by the United States Supreme Court to determine whether a shareholder in a professional corporation was an employee for purposes of the Americans with Disabilities Act is not helpful in resolving the question of a sole shareholder's liability as an employer. That test, taken from the Equal Employment Opportunities Commission guidelines, considers the following factors:

“ ‘Whether the organization can hire or fire the individual [shareholder] or set the rules and regulations of the individual's work

‘Whether and, if so, to what extent the organization supervises the individual's work

‘Whether the individual [shareholder] reports to someone higher in the organization

‘Whether and, if so, to what extent the individual [shareholder] is able to influence the organization

‘Whether the parties intended that the individual [shareholder] be an employee, as expressed in written agreements or contracts

‘Whether the individual [shareholder] shares in the profits, losses, and liabilities of the organization.’ EEOC Compliance Manual § 605:0009.”

(*Clackamas Gastroenterology Associates, P.C. v. Wells* (2003) 538 U.S. 440, 449–450, 123 S.Ct. 1673, 1680, 155 L.Ed.2d 615, 626, fn. omitted.)

Whether the corporation can hire or fire a shareholder is logically related to the question of whether the shareholder is an employee, but not to the question whether the corporation and the shareholder can both be considered employers. Again, this is a determination best made by the alter ego doctrine.

*411 Leonardo also asserts the “integrated enterprise test” is relevant. This is a test federal courts have developed to determine whether two corporations should be considered a single employer for Title VII purposes. (*Laird v. Capital Cities/ABC, Inc.* (1998) 68 Cal.App.4th 727, 737, 80 Cal.Rptr.2d 454.) It looks at the two corporations to determine whether there is an interrelation of operations, common management, centralized control of labor relations, and common ownership or financial control. (*Ibid.*) Again, these factors have little relevance when the issue is whether a sole shareholder should be held liable for the corporation's wrongdoing.

[6][7][8] “Ordinarily, a corporation is regarded as a legal entity, separate and distinct from its stockholders, officers and directors, with separate

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

and distinct liabilities and obligations. [Citations.]” (*Sonora Diamond Corp. v. Superior Court* (2000) 83 Cal.App.4th 523, 538, 99 Cal.Rptr.2d 824 (*Sonora Diamond*)). “[T]he corporate form will be disregarded only in narrowly defined circumstances and only when the ends of justice so require.” (*Mesler v. Bragg Management Co.*, *supra*, 39 Cal.3d at p. 301, 216 Cal.Rptr. 443, 702 P.2d 601.) Before a corporation's obligations can be recognized as those of a particular person, the requisite unity of interest and inequitable result must be shown. (*Arnold v. Browne* (1972) 27 Cal.App.3d 386, 394, 103 Cal.Rptr. 775, overruled on other grounds in *Reynolds Metals Co. v. Alperson* (1979) 25 Cal.3d 124, 129, 158 Cal.Rptr. 1, 599 P.2d 83.) These factors**65 comprise the elements that must be present for liability as an alter ego.

The various tests asserted by plaintiffs are useful for determining who may be considered an employer or employee in other contexts, but for determining whether Cooper may be held to answer for the wrongdoing of the corporation is the alter ego doctrine.

II

Burdens of the Parties on Summary Judgment

A defendant moving for summary judgment bears the burden of persuasion that one or more elements of the cause of action at issue cannot be established, or that there is a complete defense to the cause of action. (*Aguilar v. Atlantic Richfield Co.* (2001) 25 Cal.4th 826, 850, 107 Cal.Rptr.2d 841, 24 P.3d 493.) The moving party bears the initial burden of making a prima facie showing of the nonexistence of a triable issue of material fact, and only if the moving party carries the initial burden does the burden shift to the opposing party to produce a prima facie showing of the existence of a triable issue of material fact. (*Ibid.*)

[9] We must determine whether defendant's showing was sufficient to entitle him to a summary judgment. Defendant's showing on summary judgment *412 was that plaintiffs could not prevail on their claims against him because only an employer

may be liable for discrimination or violation of the Family Rights Act. Since Auburn Honda, the corporation, was the employer, there could be no liability attributed to defendant Cooper.

Plaintiffs' response was that Cooper was liable under an alter ego theory, or because he was the actual employer by virtue of his control over the employees of Auburn Honda. They argue the defendant's showing was insufficient because there were triable issues of fact as to his liability as an alter ego. Thus, before we can determine whether defendant's showing was sufficient, we must determine whether the complaint adequately alleged that Cooper was liable to plaintiffs on an alter ego theory. Only if the allegations were adequate to apprise Cooper that he was being held accountable as an alter ego, was it necessary for him to produce evidence that he could not be held liable under such theory.

[10][11][12][13] “ ‘The function of the pleadings in a motion for summary judgment is to delimit the scope of the issues....’ [Citations.]” (*FPI Development, Inc. v. Nakashima* (1991) 231 Cal.App.3d 367, 381, 282 Cal.Rptr. 508, quoting *Orange County Air Pollution Control Dist. v. Superior Court* (1972) 27 Cal.App.3d 109, 113, 103 Cal.Rptr. 410.) The pleadings are the “outer measure of materiality in a summary judgment proceeding.” (*Ibid.*) The summary judgment procedure “presupposes that the pleadings are adequate to put in issue a cause of action or defense thereto. [Citation.] However a pleading may be defective in failing to allege an element of a cause of action or in failing to intelligibly identify a defense thereto. In such a case, the moving party need not address a missing element or, obviously, respond to assertions which are unintelligible or make out no recognizable legal claim. The summary judgment proceeding is thereby necessarily transmuted into a test of the pleadings and the summary judgment motion into a motion for judgment on the pleadings. In these circumstances it has been said that a defendant's ‘motion for summary judgment necessarily in-

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

cludes a test of the sufficiency of the complaint and as such is in legal effect a motion for judgment on the pleadings.’ [Citation.]” (*Id.* at p. 382, 282 Cal.Rptr. 508.)

****66** In this case, the plaintiffs do not contend that anyone other than an employer is liable for employment discrimination under FEHA or for violation of the Family Rights Act. In fact, plaintiffs pleaded that Cooper was their employer.^{FN2} Defendant’s summary judgment motion adduced facts showing that plaintiffs were employed by Auburn Honda, rather than Cooper. The question ***413** is whether the complaint contained sufficient factual allegations to inform the defendant that plaintiffs were seeking relief on the basis of Cooper’s liability as an alter ego. We conclude it did not.

FN2. In the previous section, we explained that plaintiffs’ theory that Cooper was their employer is wrong. Plaintiffs’ alter ego theory seeks to show not that Cooper was the employer, but that as the alter ego of the employer, he should be liable for its wrongdoing.

[14][15] Although California courts take a liberal view of inartfully drawn complaints, “[i]t remains essential ... that a complaint set forth the actionable facts relied upon with sufficient precision to inform the defendant of what plaintiff is complaining, and what remedies are being sought.” (*Signal Hill Aviation Co. v. Stroppe* (1979) 96 Cal.App.3d 627, 636, 158 Cal.Rptr. 178.) Fairness dictates that a complaint give the defendant sufficient notice of the cause of action stated to be able to prepare the case. (*Bradley v. Hartford Acc. & Indem. Co.* (1973) 30 Cal.App.3d 818, 825, 106 Cal.Rptr. 718, overruled on another point in *Silberg v. Anderson* (1990) 50 Cal.3d 205, 212–213, 266 Cal.Rptr. 638, 786 P.2d 365.)

Auer v. Frank (1964) 227 Cal.App.2d 396, 403, 38 Cal.Rptr. 684 (*Auer*), noted a split of authority whether the alter ego doctrine must be pleaded in the complaint. Some cases say that it must be, while

others state that if a defendant is charged with liability, the denial of liability is sufficient to place the alter ego doctrine at issue. (*Ibid.*) *Auer, supra*, sided with those cases holding that the alter ego theory need not be pleaded in the complaint. (*Ibid.*)

Having reviewed those cases holding that the alter ego doctrine need not be pleaded in the complaint, we conclude they were presented in a different posture than the case before us, and are not compelling authority in this case. In *Auer, supra*, 227 Cal.App.2d 396, 38 Cal.Rptr. 684, the complaint lacked alter ego allegations yet the case went to trial, and plaintiff’s counsel informed the court during the opening statement that plaintiffs intended to rely on an alter ego theory, that they had not been aware of such a theory when the complaint was filed, but had been made aware of the issue after taking depositions. (*Id.* at pp. 401–402, 38 Cal.Rptr. 684.) The trial court allowed introduction of the alter ego evidence.

Likewise in *Pan Pacific Sash & Door Co. v. Greendale Park, Inc.* (1958) 166 Cal.App.2d 652, 654–655, 333 P.2d 802, cited in *Auer*, no alter ego allegations appeared in the complaint, but the case went to trial and alter ego evidence was admitted over objection. The court held that the charge of liability and denial was sufficient to authorize the reception of evidence on the alter ego theory, or that the reception of such evidence was not reversible error. (*Id.* at p. 655, 333 P.2d 802.) The court noted that the defendants were apprised in advance of trial that plaintiff intended to rely on the doctrine, that both defendants (in that case both were corporations) were parties to the action and represented by the same counsel. (*Id.* at p. 656, 333 P.2d 802.) The court concluded that “[u]nder these circumstances conceding that the plaintiff’s complaint was ***414** deficient in the particular above referred to, it ****67** may not be said that defendants were misled to their prejudice by any variance between the pleading and the proof.” (*Id.* at p. 657, 333 P.2d 802.)

Also in *Gordon v. Aztec Brewing Co.* (1949) 33 Cal.2d 514, 516, 203 P.2d 522, cited by *Auer*,

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

supra, the appeal was after judgment upon a jury verdict. Although the complaint did not allege alter ego, alter ego evidence was admitted and an alter ego instruction was given. (*Id.* at p. 521, 203 P.2d 522.) In response to the argument that no alter ego relationship was pleaded, therefore it was not before the trial court, the Court of Appeal reasoned that “even if the pleadings were to be considered deficient in this respect, it is clear that the defendant has not been misled to its prejudice by any variance between pleadings and proof.... From the beginning of the proceedings it was prepared to maintain, and did maintain throughout the trial, that the liabilities of the partnership could not be fastened upon the corporation.” (*Id.* at p. 523, 203 P.2d 522.)

Finally, in *Marr v. Postal Union Life Ins. Co.* (1940) 40 Cal.App.2d 673, 678, 105 P.2d 649, cited by *Auer, supra*, the case was tried to a jury, and alter ego evidence was presented. The court held that appellant had not been surprised or misled by presentation of the alter ego theory at trial. “Not having actually misled appellant to its prejudice in presenting its defense, the variance, if any, between the allegations of the complaint and the proof cannot be considered as a material variance.” (*Id.* at p. 681, 105 P.2d 649.)

However, when the court is asked to take some action upon an alter ego theory at the pleadings stage, more is required than was pleaded here. For example, in *Norins Realty Co. v. Consolidated Abstract & Title Guaranty Co.* (1947) 80 Cal.App.2d 879, 182 P.2d 593, the action against the corporation was filed in Los Angeles County, where the individual defendants resided. (*Id.* at pp. 879–880, 182 P.2d 593.) Defendants' motion for change of venue to San Bernardino County, where the corporation's principal place of business was located, was granted. The Court of Appeal affirmed, concluding that the action was not triable in Los Angeles County because although the individuals were named defendants, no facts were alleged from which alter ego liability could be inferred. (*Id.* at p. 883, 182 P.2d 593.) “The allegation that a corpora-

tion is the *alter ego* of the individual stockholders is insufficient to justify the court in disregarding the corporate entity in the absence of allegations of facts from which it appears that justice cannot otherwise be accomplished.” (*Ibid.*)

In *Sheard v. Superior Court* (1974) 40 Cal.App.3d 207, 114 Cal.Rptr. 743, the issue was whether service on the individual, out-of-state stockholder defendants should be quashed because the complaint did not allege sufficient facts to support jurisdiction over them. The court found that neither the complaint nor the declaration in opposition to the motion to quash contained *415 sufficient allegations to support the two requirements (unity of interest and inequitable result) to the application of the alter ego theory. (*Id.* at pp. 211–212, 114 Cal.Rptr. 743.)

Here, even though the case arises on motion for summary judgment, it is in fact a pleading case because the pleadings delimit the scope of the issues in a motion for summary judgment, and the question on appeal from this judgment is whether the alter ego theory was sufficiently pleaded to put it at issue for purposes of the summary judgment motion. (See *FPI Development, Inc. v. Nakashima, supra*, 231 Cal.App.3d at p. 381, 282 Cal.Rptr. 508.)

**68 [16][17] A complaint must set forth the facts with sufficient precision to put the defendant on notice about what the plaintiff is complaining and what remedies are being sought. (*Signal Hill Aviation Co., Inc. v. Stroppe, supra*, 96 Cal.App.3d at p. 636, 158 Cal.Rptr. 178.) To recover on an alter ego theory, a plaintiff need not use the words “alter ego,” but must allege sufficient facts to show a unity of interest and ownership, and an unjust result if the corporation is treated as the sole actor. (*Vasey v. California Dance Co.* (1977) 70 Cal.App.3d 742, 749, 139 Cal.Rptr. 72.) An allegation that a person owns all of the corporate stock and makes all of the management decisions is insufficient to cause the court to disregard the corporate entity. (*Meadows v. Emett & Chandler* (1950) 99 Cal.App.2d 496, 499,

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

222 P.2d 145.)

Here, the pertinent allegations of the complaints were: (1) that the plaintiffs were employed by Auburn Honda and Jay Cooper; (2) that Auburn Honda is a corporation; (3) that “Defendant Cooper is the sole owner of AUBURN HONDA, owning all of its stock and making all of its business decisions personally[;]” and (4) that all defendants were “the agents, servants and employees of their co-defendants, and in doing the things hereinafter alleged were acting within the scope and authority as such agents, servants and employees and with the permission and consent of their co-defendants. All of said acts of each of the Defendants were authorized by or ratified by their co-defendants.”

[18] These allegations neither specifically alleged alter ego liability, nor alleged facts showing a unity of interest and inequitable result from treatment of the corporation as the sole actor. Furthermore, although plaintiffs alleged Cooper was the employer, the complaint contains no allegations that he should be held liable for the corporation's wrongdoing. The essence of the alter ego doctrine is not that the individual shareholder becomes the corporation, but that the individual shareholder is liable for the actions of the corporation. (*Mesler v. Bragg Management Co.*, *supra*, 39 Cal.3d at p. 300, 216 Cal.Rptr. 443, 702 P.2d 601.) For all other purposes, the separate corporate existence remains. (*Id.* at p. 301, 216 Cal.Rptr. 443, 702 P.2d 601.)

*416 Because the alter ego theory was not adequately pleaded, Cooper had no burden to show that plaintiffs' alter ego claim could not be established. “Where a complaint does not state a cognizable claim, ... a defendant has no obligation to present evidence to negate a legally inadequate claim.” (*Hansra v. Superior Court* (1992) 7 Cal.App.4th 630, 638–639, 9 Cal.Rptr.2d 216.) Cooper therefore had no obligation to adduce evidence to negate an alter ego theory in his motion for summary judgment, and the trial court properly granted the motion.

III

Motion to Amend Complaint

[19] Plaintiffs requested leave to amend their complaints to add alter ego allegations at the hearing on the summary judgment motions. They did not make an offer of proof in support of the request. Rather, they offered the facts tendered in opposition to the motion for summary judgment as grounds justifying an amendment. The trial court denied the motion of Leek, Borden and Buschmann to amend on the ground that even if the facts adduced in plaintiffs' opposition to the summary judgment motion were true, they would not establish alter ego liability. The Leonardo court did not rule on the motion to amend. Plaintiffs argue the trial court should have allowed amendment of the complaints.

**69 “ [A] defendant's motion for summary judgment “necessarily includes a test of the sufficiency of the complaint....” Motions for summary judgment in such situations [where the complaint does not state a cognizable claim] have otherwise been allowed as being in legal effect motions for judgment on the pleadings. [Citations.] ” (*Hansra v. Superior Court*, *supra*, 7 Cal.App.4th at p. 639, 9 Cal.Rptr.2d 216.) Thus, in determining whether the trial court erred in denying the motions to amend the complaint, we treat the matter as if it arose on a motion for judgment on the pleadings.

The standard of review for a motion for judgment on the pleadings is the same as that for a demurrer. (*Ellerbee v. County of Los Angeles* (2010) 187 Cal.App.4th 1206, 1213, 114 Cal.Rptr.3d 756.) When the trial court has sustained a demurrer without leave to amend, we must decide whether there is a reasonable possibility that the defect can be cured by amendment. (*Blank v. Kirwan* (1985) 39 Cal.3d 311, 318, 216 Cal.Rptr. 718, 703 P.2d 58.) If it can be, the trial court has abused its discretion and we reverse. It is the plaintiff's burden to prove the reasonable possibility of curing the defect by amendment. (*Ibid.*)

[20] In this case we may look to the papers plaintiffs adduced in opposition to the summary

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

judgment motion to determine whether there is a “reasonable *417 possibility” they will be able to amend to state a claim against Cooper on an alter ego theory. “[W]here the parties have had sufficient opportunity adequately to develop their factual cases through discovery and the defendant has made a sufficient showing that the plaintiff’s action has no merit, in order to avert summary judgment the plaintiff must produce *substantial* responsive evidence sufficient to establish the existence of a triable issue of material fact on the issues raised by the plaintiff’s causes of action.” (*Eisenberg v. Alameda Newspapers, Inc.* (1999) 74 Cal.App.4th 1359, 1376, 88 Cal.Rptr.2d 802.) Plaintiffs made no offer of proof. As noted, they sought to rely on the facts tendered in opposition to the motion for summary judgment. We may assume that plaintiffs understood their burden in this regard and that they proffered all the facts made available to them through discovery to show the existence of an alter ego claim.

To succeed on their alter ego claim, plaintiffs must be able to show: (1) such a unity of interest and ownership between the corporation and its equitable owner that no separation actually exists, and (2) an inequitable result if the acts in question are treated as those of the corporation alone. (*Sonora Diamond, supra*, 83 Cal.App.4th at p. 538, 99 Cal.Rptr.2d 824.)

[21] Several factors are to be considered in applying the doctrine, among them are: “[c]ommingling of funds and other assets, failure to segregate funds of the separate entities, and the unauthorized diversion of corporate funds or assets to other than corporate uses; ... the treatment by an individual of the assets of the corporation as his own; ... the failure to obtain authority to issue stock or to subscribe to or issue the same; ... the holding out by an individual that he is personally liable for the debts of the corporation; ... the failure to maintain minutes or adequate corporate records ...; sole ownership of all of the stock in a corporation by one individual or the members of a family; ... the failure

to adequately capitalize a corporation; the total absence of corporate assets, and undercapitalization; ... the use of a corporation as a mere shell, instrumentality or conduit for a single venture or the business of an individual or another corporation; ... the concealment and misrepresentation of the identity **70 of the responsible ownership, management and financial interest, or concealment of personal business activities; ... the disregard of legal formalities and the failure to maintain arm’s length relationships among related entities; ... the use of the corporate entity to procure labor, services or merchandise for another person or entity; ... the diversion of assets from a corporation by or to a stockholder or other person or entity, to the detriment of creditors, or the manipulation of assets and liabilities between entities so as to concentrate the assets in one and the liabilities in another; ... the contracting with another with intent to avoid performance by use of a corporate entity as a shield against personal liability, or the use of a corporation as a subterfuge of illegal transactions; ... and *418 the formation and use of a corporation to transfer to it the existing liability of another person or entity.’ ... [¶] This long list of factors is not exhaustive. The enumerated factors may be considered ‘[a]mong’ others ‘under the particular circumstances of each case.’ ” (*Morrison Knudsen Corp. v. Hancock, Rothert & Bunshoft, LLP* (1999) 69 Cal.App.4th 223, 249–250, 81 Cal.Rptr.2d 425, quoting *Associated Vendors, Inc. v. Oakland Meat Co.* (1962) 210 Cal.App.2d 825, 838–840, 26 Cal.Rptr. 806.)

[22][23] Plaintiffs have proffered evidence to support only two of the above factors, that Cooper was the sole owner of all of the stock in the corporation, and that corporate formalities were disregarded.^{FN3} Nevertheless, no single factor is determinative and the result depends on the circumstances of each particular case. (*Zoran Corp. v. Chen* (2010) 185 Cal.App.4th 799, 812, 110 Cal.Rptr.3d 597; *Baize v. Eastridge Companies* (2006) 142 Cal.App.4th 293, 302, 47 Cal.Rptr.3d 763.) Whether a party is liable under an alter ego theory is a

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

question of fact. (*Zoran, supra*, at p. 811, 110 Cal.Rptr.3d 597.)

FN3. Deanna Keck, the corporate secretary, did not recall participating in any corporate meetings.

While plaintiffs arguably adduced sufficient facts to show a unity of interest and ownership, in order to recover under a theory of alter ego liability they also would have to show an inequitable result if Cooper and the corporation are not treated as one in the same. Difficulty in enforcing a judgment does not alone satisfy this element. (*Sonora Diamond, supra*, 83 Cal.App.4th at p. 539, 99 Cal.Rptr.2d 824.) There also must be some conduct amounting to bad faith that makes it inequitable for Cooper to hide behind the corporate form. (*Ibid.*)

Plaintiffs have proffered no evidence to support this element. All they offer on appeal is their argument that Cooper might raid the corporate coffers, based upon the fact that he raised the dealership's rent substantially between 2004 and 2006. There is no evidence regarding the corporation's financial situation, or the amount or nature of corporate assets, or whether the corporation is adequately capitalized. There is no evidence the corporation was a mere sham or shell. There is no evidence Cooper has diverted assets from the corporation to avoid paying creditors. In short, there is nothing to indicate that plaintiffs, if successful against the corporation, will not be able to collect on any judgment against the corporation. Absent such evidence, plaintiffs cannot show that the result will be inequitable, and have not stated the second element of an alter ego claim. The trial court acted within its discretion when it denied the motion to amend.

**71 [24] A claim based upon an alter ego theory is not itself a claim for substantive relief. *419(*Hennessey's Tavern, Inc. v. American Air Filter Co.* (1988) 204 Cal.App.3d 1351, 1359, 251 Cal.Rptr. 859.) It is a procedural device by which courts will disregard the corporate entity in order to hold the alter ego individual liable on the obligations of the

corporation. (*Ibid.*) Because it is not a substantive claim that has been decided, we do not necessarily rule out the possibility that plaintiffs could still recover from Cooper individually if they obtain a judgment that the corporation is unable to satisfy.

[25][26] Under some circumstances a judgment against a corporation may be amended to add a nonparty alter ego as a judgment debtor. (*Hall, Goodhue, Haisley & Barker, Inc. v. Marconi Conf. Center Bd.* (1996) 41 Cal.App.4th 1551, 1555, 49 Cal.Rptr.2d 286; Code Civ. Proc., § 187.) "This is an equitable procedure based on the theory that the court is not amending the judgment to add a new defendant but is merely inserting the correct name of the real defendant." (*NEC Electronics, Inc. v. Hurt* (1989) 208 Cal.App.3d 772, 778, 256 Cal.Rptr. 441.) It is also possible for a party to bring a wholly separate action against the individual to enforce a prior judgment against the corporation on an alter ego theory. (*Brenelli Amedeo, S.P.A. v. Bakara Furniture, Inc.* (1994) 29 Cal.App.4th 1828, 1840, 35 Cal.Rptr.2d 348.)

IV

Attorney Fees

[27] The trial court awarded attorney fees to defendant in both actions. Government Code section 12965, subdivision (b) authorizes an award of reasonable attorney fees and costs to the prevailing party in an action brought under FEHA. The section states in pertinent part: "In actions brought under this section, the court, in its discretion, may award to the prevailing party reasonable attorney fees and costs, including expert witness fees, except where the action is filed by a public agency or a public official, acting in an official capacity."

[28][29] Despite this statutory authorization allowing attorney fees to either party that prevails, California courts have interpreted the statute in accordance with the principles developed by federal courts in employment discrimination claims, to the effect that a prevailing defendant in an employment discrimination action cannot recover attorney fees unless the action was unreasonable, frivolous, mer-

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

itless or vexatious. (*Cummings v. Benco Building Services* (1992) 11 Cal.App.4th 1383, 1386–1387, 15 Cal.Rptr.2d 53 (*Cummings*); *Mangano v. Verity, Inc.* (2008) 167 Cal.App.4th 944, 951, 84 Cal.Rptr.3d 526; *Rosenman v. Christensen, Miller, Fink, Jacobs, Glaser, Weil & Shapiro* (2001) 91 Cal.App.4th 859, 865–866, 110 Cal.Rptr.2d 903 (*Rosenman*)).) This standard is in contrast to that applied to a prevailing *420 plaintiff, who should ordinarily recover absent special circumstances rendering such an award unjust. (*Cummings, supra*, 11 Cal.App.4th at p. 1387, 15 Cal.Rptr.2d 53.)

The policy behind this disparate treatment with respect to the recovery of attorney fees is to “make it easier for a plaintiff of limited means to bring a meritorious suit[.]” while serving “to deter the bringing of lawsuits without foundation,” “to discourage frivolous suits,” and “to diminish the likelihood of unjustified suits being brought.” (*Christiansburg Garment Co. v. EEOC* (1978) 434 U.S. 412, 420, 98 S.Ct. 694, 699–700, 54 L.Ed.2d 648, 656 (*Christiansburg*)).

[30] As explained by the Supreme Court, “In applying these criteria, it is **72 important that a district court resist the understandable temptation to engage in *post hoc* reasoning by concluding that, because a plaintiff did not ultimately prevail, his action must have been unreasonable or without foundation. This kind of hindsight logic could discourage all but the most airtight claims, for seldom can a prospective plaintiff be sure of ultimate success.” (*Christiansburg, supra*, 434 U.S. at pp. 421–422, 98 S.Ct. at p. 700, 54 L.Ed.2d at p. 657.) A meritless case in this context is one that is groundless or without a legal or factual basis. (*Id.* at pp. 420–421, 98 S.Ct. at pp. 699–700, 54 L.Ed.2d at p. 656.)

[31][32] The trial court is required to make written findings when awarding attorney fees to defendants. (*Rosenman, supra*, 91 Cal.App.4th at p. 868, 110 Cal.Rptr.2d 903 [imposing a “nonwaivable requirement” that trial courts make written findings in every case awarding attorney

fees in favor of defendants in FEHA actions].) Such a requirement ensures that fees are awarded only in the rare cases envisioned by *Christiansburg*. (*Ibid.*) If no findings are made, we must reverse and remand absent a determination that no findings supporting the order reasonably could be made. (*Ibid.*)

In the Leonardo case, the trial court's tentative ruling, which apparently became the final ruling, made the finding that Leonardo's complaint against Cooper “was frivolous, unreasonable, and groundless given the rulings in *Reno v. Baird* (1998) 18 Cal.4th 640 [76 Cal.Rptr.2d 499, 957 P.2d 1333] and *Janken v. GM Hughes* (1996) 46 Cal.4th 55 [53 Cal.Rptr.2d 741]. Plaintiff's attorney is an admittedly experienced employment attorney who was aware of these cases at the time the complaint was filed.” No written findings were made in the other case.

The findings in the Leonardo case relate to the fact that Cooper was not the employer. Leonardo argued below, as all plaintiffs do here, that Cooper was the actual employer based upon the amount of control he exercised over the employees. While we disagree that control of the employees is the proper test, the argument was a legitimate one. Furthermore, the problem with plaintiffs' alter ego theory on summary judgment was not that there was no *421 legal or factual basis to hold Cooper individually liable. There was, in fact, evidence relevant to some aspects of an alter ego theory, including the fact that Cooper owned all of the corporate stock, was the president of the corporation, and made all of the management decisions. However, there was no evidence of bad faith, or even inequitable result—even assuming alter ego liability was adequately pled.

Also because of such evidence, plaintiffs' argument that their motion to amend should have been granted is not completely groundless. The fact that plaintiffs did not develop sufficient evidence to show that an inequitable result would follow absent the application of the alter ego doctrine does not mean that the action had absolutely no basis in fact.

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

(Cite as: 194 Cal.App.4th 399, 125 Cal.Rptr.3d 56)

This case is dissimilar to others that have awarded attorney fees where, for example, the employee lied about having been subjected to discrimination (*Saret-Cook v. Gilbert, Kelly, Crowley & Jennett* (1999) 74 Cal.App.4th 1211, 88 Cal.Rptr.2d 732), or where the employee had signed a release of all claims, including a FEHA discrimination claim, in exchange for the payment of money (*Linsley v. Twentieth Century Fox Film Corp.* (1999) 75 Cal.App.4th 762, 89 Cal.Rptr.2d 429), or where there was absolutely no evidence to support the employee's claims of discrimination. (*Villanueva v. City of Colton* (2008) 160 Cal.App.4th 1188, 1200, 73 Cal.Rptr.3d 343.)

**73 We therefore conclude that the actions were not completely groundless, frivolous, unreasonable or without foundation. We shall reverse the award of attorney fees against the employees.

IV

Motion for Sanctions on Appeal

[33] Cooper has also filed a motion for sanctions for filing a frivolous appeal in each case. He claims attorney fees and costs in the amount of \$12,045.48 for the Leek, Borden, and Buschmann appeal. He claims attorney fees and costs in the amount of \$9,614.85 for the Leonardo appeal.

Code of Civil Procedure section 907 provides that we may award sanctions if it appears the appeal was frivolous or taken solely for delay. The Supreme Court has defined a frivolous appeal as one that "is prosecuted for an improper motive—to harass the respondent or delay the effect of an adverse judgment—or when it indisputably has no merit—when any reasonable attorney would agree that the appeal is totally and completely without merit." (*In re Marriage of Flaherty* (1982) 31 Cal.3d 637, 650, 183 Cal.Rptr. 508, 646 P.2d 179.) The court stressed that an appeal is not frivolous simply *422 because it is without merit. (*Ibid.*) Sanctions are intended to prevent "indefensible conduct [,]" but not to deter the "vigorous assertion of clients' rights." (*Id.* at p. 648, 183 Cal.Rptr. 508, 646 P.2d 179.)

There is no evidence that this appeal was taken solely to harass or delay. Since we are reversing that portion of the judgment that awarded attorney fees, the appeal is obviously not totally and completely without merit. Furthermore, even as to that portion of the judgment we affirm, the appeal is not one that any reasonable attorney would agree is totally and completely devoid of merit. We therefore deny Cooper's motions for sanctions on appeal.

DISPOSITION

The portions of the judgments awarding attorney fees to Cooper are reversed. In all other respects the summary judgments are affirmed. Respondent's motions for sanctions on appeal are denied. The parties shall bear their own costs on appeal.

We concur: RAYE, P.J., and HULL, J.

Cal.App. 3 Dist., 2011.

Leek v. Cooper

194 Cal.App.4th 399, 125 Cal.Rptr.3d 56, 112 Fair Empl.Prac.Cas. (BNA) 33, 11 Cal. Daily Op. Serv. 4571, 2011 Daily Journal D.A.R. 5433

END OF DOCUMENT

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

▽

Supreme Court of the United States
 Aaron LINDH, Petitioner,
 v.
 James P. MURPHY, Warden.

No. 96-6298.
 Argued April 14, 1997.
 Decided June 23, 1997.

After his sentences were reinstated by state Supreme Court, 161 Wis.2d 324, 468 N.W.2d 168, inmate sought federal habeas relief. The United States District Court for the Eastern District of Wisconsin, Rudolph T. Randa, J., denied relief, and inmate appealed. The Court of Appeals, Easterbrook, Circuit Judge, 96 F.3d 856, affirmed, and inmate petitioned for certiorari. The Supreme Court, Justice Souter, held that amendments to habeas corpus statute by Antiterrorism and Effective Death Penalty Act (AEDPA) did not apply to inmate's pending noncapital case.

Reversed and remanded.

Chief Justice Rehnquist filed dissenting opinion, in which Justice Scalia, Justice Kennedy, and Justice Thomas joined.

West Headnotes

[1] Statutes 361 ↪278.1

361 Statutes
 361VI Construction and Operation
 361VI(D) Retroactivity
 361k278.1 k. In General. Most Cited Cases
 (Formerly 361k263)

Judicial default rule governing retroactivity for purposes of determining ultimate temporal reach of new statute, which on its face could apply to litigation of events that occurred before it was enacted, did not apply to exclusion of all other standards of

statutory interpretation; although default rule would deny application when retroactive effect would otherwise result, other construction rules may apply to remove even possibility of retroactivity.

[2] Statutes 361 ↪278.1

361 Statutes
 361VI Construction and Operation
 361VI(D) Retroactivity
 361k278.1 k. In General. Most Cited Cases
 (Formerly 361k263)

Normal rules of statutory construction apply in determining whether statute's terms would produce retroactive effect, and in determining statute's temporal reach generally.

[3] Statutes 361 ↪278.17

361 Statutes
 361VI Construction and Operation
 361VI(D) Retroactivity
 361k278.17 k. Amendatory Acts. Most Cited Cases
 (Formerly 92k190)

Statutes 361 ↪234.5

361 Statutes
 361VI Construction and Operation
 361VI(A) General Rules of Construction
 361k234.5 k. Prospective Operation. Most Cited Cases

If application of statutory term in amendment would be retroactive as to party, term will not be applied, even if, in absence of retroactive effect, term might be applicable; if it would be prospective, particular degree of prospectivity intended will be identified in normal course to determine whether term does apply to party.

[4] Habeas Corpus 197 ↪205

197 Habeas Corpus

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

197I In General

197I(A) In General

197I(A)1 Nature of Remedy in General

197k205 k. Constitutional and Statutory Provisions. Most Cited Cases

Amendments to habeas corpus statute by Anti-terrorism and Effective Death Penalty Act (AEDPA) did not apply to pending noncapital cases; AEDPA created entirely new chapter for habeas proceedings in capital cases, with special rules favorable to states that meet certain conditions, that expressly applied to pending cases, so that, by negative implication, amendments were meant to apply only to those noncapital cases filed after enactment. 28 U.S.C.A. § 2254(b).

[5] Statutes 361 ↪278.17

361 Statutes

361VI Construction and Operation

361VI(D) Retroactivity

361k278.17 k. Amendatory Acts. Most Cited Cases
 (Formerly 361k270)

If statutory amendment were merely procedural in strict sense, natural expectation would be that it would apply to pending cases.

[6] Statutes 361 ↪185

361 Statutes

361VI Construction and Operation

361VI(A) General Rules of Construction

361k180 Intention of Legislature

361k185 k. Implications and Inferences. Most Cited Cases

Negative implications raised by disparate provisions are strongest when portions of statute treated differently had already been joined together and were being considered simultaneously when language raising implication was inserted.

****2060 Syllabus** FN*

FN* The syllabus constitutes no part of the opinion of the Court but has been prepared

by the Reporter of Decisions for the convenience of the reader. See *United States v. Detroit Timber & Lumber Co.*, 200 U.S. 321, 337, 26 S.Ct. 282, 287, 50 L.Ed. 499.

Wisconsin tried petitioner Lindh on noncapital murder and attempted murder charges. In response to his insanity defense, the State called a psychiatrist who had examined Lindh but who had come under criminal investigation for sexual exploitation of patients before the trial began. Lindh's attempt to question the doctor about that investigation in hopes of showing the doctor's interest in currying favor with the State was barred by the trial court, and Lindh was convicted. He was denied relief on his direct appeal, in which he claimed a violation of the Confrontation Clause. He raised that claim again in a federal habeas corpus application, which was denied, and he promptly appealed. Shortly after oral argument before the Seventh Circuit, the Anti-terrorism and Effective Death Penalty Act of 1996 (Act) amended the federal habeas statute. Following an en banc rehearing to consider the Act's impact, the court held that the amendments to chapter 153 of Title 28, which governs all habeas proceedings, generally apply to cases pending on the date of enactment; that applying the new version of 28 U.S.C. § 2254(d)-which governs standards affecting entitlement to relief-to pending cases would not have a retroactive effect barring its application under *Landgraf v. USI Film Products*, 511 U.S. 244, 114 S.Ct. 1483, 128 L.Ed.2d 229, because it would not attach new legal consequences to events preceding enactment; and that the statute applied to Lindh's case.

Held: Since the new provisions of chapter 153 generally apply only to cases filed after the Act became effective, they do not apply to pending noncapital cases such as Lindh's. Pp. 2062-2068.

(a) Wisconsin errs in arguing that whenever a new statute on its face could apply to the litigation of events preceding enactment, there are only two alternative sources of rules to determine its ultimate temporal reach: either Congress's express command

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

or application of the *Landgraf* default rule governing retroactivity. Normal rules of construction apply in determining a statute's temporal reach generally and whether a statute's terms would produce a retroactive effect. Although *Landgraf*'s rule would deny application when a retroactive effect would otherwise result, other construction rules may apply to remove even the possibility of retroactivity (as by rendering the statutory provision *321 wholly inapplicable to a particular case), as Lindh argues the recognition of a negative implication would do here. Pp. 2062-2063.

(b) The statute reveals Congress's general intent to apply the chapter 153 amendments only to cases filed after its enactment. The Act revised chapter 153 for all habeas proceedings. Then § 107 of the Act created an entirely new chapter 154 for habeas proceedings in capital cases, with special rules favorable to those States that meet certain conditions. Section 107(c) expressly applies chapter 154 to pending cases. The negative implication is that the chapter 153 amendments were meant to apply only to cases filed after enactment. If Congress was reasonably concerned to ensure that chapter 154 applied to pending cases, only a different **2061 intent explains the fact that it did not enact a similar provision for chapter 153. Had the chapters evolved separately and been joined together at the last minute, after chapter 154 had acquired its mandate, there might have been a possibility that Congress intended the same rule for each chapter, but was careless in the rough-and-tumble. But those are not the circumstances here: § 107(c) was added after the chapters were introduced as a single bill. Section 107(c)'s insertion thus illustrates the familiar rule that negative implications raised by disparate provisions are strongest when the portions of a statute treated differently had already been joined together and were being considered simultaneously when the language raising the implication was inserted. See *Field v. Mans*, 516 U.S. 59, 116 S.Ct. 437, 133 L.Ed.2d 351. Respondent's one competing explanation-that § 107(c) was intended to fix an ambiguity over when a State would qualify for

chapter 154's favorable rules-is too remote to displace the straightforward inference that chapter 153 was not meant to apply to pending cases. Finally, while new § 2264(b)-which was enacted within chapter 154 and provides that new §§ 2254(d) and (e) in chapter 153 would apply to pending chapter 154 cases-does not speak to the present issue with flawless clarity, it tends to confirm the interpretation of § 107(c) adopted here. It shows that Congress assumed that in the absence of § 2264(b), new §§ 2254(d) and (e) would not apply to pending cases. Pp. 2063-2068.

96 F.3d 856 (C.A.7), reversed and remanded.

SOUTER, J., delivered the opinion of the Court, in which STEVENS, O'CONNOR, GINSBURG, O'CONNOR, GINSBURG, and BREYER, JJ., joined. REHNQUIST, C.J., FILED A DISSENTING OPINION, IN WHICH SCALIA, KENNEDY, KENNEDY AND THOMAS, JJ., JOINED, *POST*, P. 2068.

James S. Liebman, New York City, for petitioner.

*322 Sally L. Wellman, Madison, WI, for respondent.

For U.S. Supreme Court briefs, see:1997 WL 82672 (Pet.Brief)1997 WL 126151 (Resp.Brief)1997 WL 163976 (Reply.Brief)

Justice SOUTER delivered the opinion of the Court.

The Antiterrorism and Effective Death Penalty Act of 1996, 110 Stat. 1214, signed into law on April 24, 1996, enacted the present 28 U.S.C. § 2254(d) (1994 ed., Supp.II). The issue in this case is whether that new section of the statute dealing with petitions for habeas corpus governs *323 applications in noncapital cases that were already pending when the Act was passed. We hold that it does not.

I

Wisconsin tried Aaron Lindh on multiple charges of murder and attempted murder. In re-

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
 (Cite as: 521 U.S. 320, 117 S.Ct. 2059)

response to his insanity defense, the State called a psychiatrist who had spoken with Lindh immediately after the killings but had later, and before Lindh's trial, come under criminal investigation by the State for sexual exploitation of some of his patients. Although, at trial, Lindh tried to ask the psychiatrist about that investigation, hoping to suggest the witness's interest in currying favor with the State, the trial court barred the questioning. Lindh was convicted.

On direct appeal, Lindh claimed a violation of the Confrontation Clause of the National Constitution, but despite the denial of relief, Lindh sought neither review in this Court nor state collateral review. Instead, on July 9, 1992, he filed a habeas corpus application in the United States District Court, in which he again argued his Confrontation Clause claim. When relief was denied in October 1995, Lindh promptly appealed to the Seventh Circuit. Shortly after oral argument there, however, the federal habeas statute was amended, and the Seventh Circuit ordered Lindh's case be reheard en banc to see whether the new statute applied to Lindh and, if so, how his case should be treated.

The Court of Appeals held that the Act's amendments to chapter 153 of Title 28 generally did apply to cases pending on the date of enactment. 96 F.3d 856, 863 (1996). Since the court did not read the statute as ****2062** itself answering the questions whether or how the newly amended version of § 2254(d) would apply to pending applications like Lindh's, *id.*, at 861-863, it turned to this Court's recent decision in *Landgraf v. USI Film Products*, 511 U.S. 244, 114 S.Ct. 1483, 128 L.Ed.2d 229 (1994). *Landgraf* held that, where a statute did not clearly mandate an application with retroactive effect, a court had to determine ***324** whether applying it as its terms ostensibly indicated would have genuinely retroactive effect; if so, the judicial presumption against retroactivity would bar its application. The Seventh Circuit concluded that applying the new § 2254(d) to cases already pending would not have genuinely retroactive ef-

fect because it would not attach "new legal consequences" to events preceding enactment, and the court held the statute applicable to Lindh's case. 96 F.3d, at 863-867 (citing *Landgraf, supra*, at 270, 114 S.Ct., at 1499-1500). On the authority of the new statute, the court then denied relief on the merits. 96 F.3d, at 868-877.

The Seventh Circuit's decision that the new version of § 2254(d) applies to pending, chapter 153 cases conflicts with the holdings of *Edens v. Hannigan*, 87 F.3d 1109, 1112, n. 1 (C.A.10 1996), *Boria v. Keane*, 90 F.3d 36, 37-38 (C.A.2 1996) (*per curiam*), and *Jeffries v. Wood*, 114 F.3d 1484 (C.A.9 1997). In accord with the Seventh Circuit is the § 2253(c) case of *Hunter v. United States*, 101 F.3d 1565, 1568-1573 (C.A.11 1996) (en banc) (relying on *Lindh* to hold certain amendments to chapter 153 applicable to pending cases). We granted certiorari limited to the question whether the new § 2254(d) applies to Lindh's case, 519 U.S. 1074, 117 S.Ct. 726, 136 L.Ed.2d 643 (1996), and we now reverse.

II

[1] Before getting to the statute itself, we have to address Wisconsin's argument that whenever a new statute on its face could apply to the litigation of events that occurred before it was enacted, there are only two alternative sources of rules to determine its ultimate temporal reach: either an "express command" from Congress or application of our *Landgraf* default rule. In *Landgraf*, we said:

"When a case implicates a federal statute enacted after the events in suit, the court's first task is to determine whether Congress has expressly prescribed the statute's proper reach. If Congress has done so, of course, there is no need to resort to judicial default ***325** rules. When, however, the statute contains no such express command, the court must determine whether the new statute would have retroactive effect.... If the statute would operate retroactively, our traditional presumption teaches that it does not govern absent clear congressional intent favoring such a result."

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

Landgraf, supra, at 280, 114 S.Ct., at 1505.

Wisconsin insists that this language means that, in the absence of an express command regarding temporal reach, this Court must determine that temporal reach for itself by applying its judicial default rule governing retroactivity, to the exclusion of all other standards of statutory interpretation. Brief for Respondent 9-14; see also *Hunter v. United States, supra*, at 1569 (suggesting that *Landgraf* may have announced a general clear-statement rule regarding the temporal reach of statutes).

Wisconsin's reading, however, ignores context. The language quoted disposed of the question whether the practice of applying the law as it stands at the time of decision represented a retreat from the occasionally conflicting position that retroactivity in the application of new statutes is disfavored. The answer given was no, and the presumption against retroactivity was reaffirmed in the traditional rule requiring retroactive application to be supported by a clear statement. *Landgraf* thus referred to "express command [s]," "unambiguous directive[s]," and the like where it sought to reaffirm that clear-statement rule, but only there. See *Landgraf v. USI Film Products*, 511 U.S., at 263, 114 S.Ct., at 1495-1496 ("unambiguous directive" is necessary to authorize "retroactive application"); *id.*, at 264, 114 S.Ct., at 1496 (statutes "will not be construed to have retroactive effect unless their language requires this result" (internal quotation marks and citation omitted)); *id.*, at 272-273, 114 S.Ct., at 1501 ("Requiring clear intent assures that Congress itself has affirmatively considered the potential unfairness of retroactive**2063 application"); *id.*, at 286, 114 S.Ct., at 1508 (finding "no clear evidence of congressional intent" to rebut the "presumption *326 against statutory retroactivity"); *id.*, at 286, 114 S.Ct., at 1508 (SCALIA, J., concurring in judgment) (agreeing that "a legislative enactment affecting substantive rights does not apply retroactively absent *clear statement* to the contrary").

[2][3] In determining whether a statute's terms would produce a retroactive effect, however, and in

determining a statute's temporal reach generally, our normal rules of construction apply. Although *Landgraf*'s default rule would deny application when a retroactive effect would otherwise result, other construction rules may apply to remove even the possibility of retroactivity (as by rendering the statutory provision wholly inapplicable to a particular case), as Lindh argues the recognition of a negative implication would do here. In sum, if the application of a term would be retroactive as to Lindh, the term will not be applied, even if, in the absence of retroactive effect, we might find the term applicable; if it would be prospective, the particular degree of prospectivity intended in the Act will be identified in the normal course in order to determine whether the term does apply to Lindh.

III

[4] The statute reveals Congress's intent to apply the amendments to chapter 153 only to such cases as were filed after the statute's enactment (except where chapter 154 otherwise makes select provisions of chapter 153 applicable to pending cases). Title I of the Act stands more or less independent of the Act's other titles^{FN1} in providing for the revision of federal habeas practice and does two main things. First, in §§ 101-106, it amends § 2244 and §§ 2253-2255 of chapter 153 of Title 28 of the United States Code, governing all habeas corpus proceedings in the federal courts.^{FN2} 110 Stat. 1217-1221.*327 Then, for habeas proceedings against a State in capital cases, § 107 creates an entirely new chapter 154 with special rules favorable to the state party, but applicable only if the State meets certain conditions, including provision for appointment of postconviction counsel in state proceedings.^{FN3} 110 Stat. 1221-1226. In § 107(c), the Act provides that "Chapter 154 ... shall apply to cases pending on or after the date of enactment of this Act." 110 Stat. 1226.

FN1. The other titles address such issues as restitution to victims of crime (Title II), various aspects of international terrorism (Titles II, III, IV, VII, VIII), restrictions on

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

various kinds of weapons and explosives (Titles V and VI), and miscellaneous items (Title IX). See 110 Stat. 1214-1217.

FN2. Section 103 also amends Rule 22 of the Federal Rules of Appellate Procedure. 110 Stat. 1218.

FN3. Section 108 further adds a “technical amendment” regarding expert and investigative fees for the defense under 21 U.S.C. § 848(q). 110 Stat. 1226.

[5] We read this provision of § 107(c), expressly applying chapter 154 to all cases pending at enactment, as indicating implicitly that the amendments to chapter 153 were assumed and meant to apply to the general run of habeas cases only when those cases had been filed after the date of the Act. The significance of this provision for application to pending cases becomes apparent when one realizes that when chapter 154 is applicable, it will have substantive as well as purely procedural effects. If chapter 154 were merely procedural in a strict sense (say, setting deadlines for filing and disposition, see 28 U.S.C. §§ 2263, 2266 (1994 ed., Supp.II); 110 Stat. 1223, 1224-1226), the natural expectation would be that it would apply to pending cases. *Landgraf, supra*, at 275, 114 S.Ct., at 1502 (noting that procedural changes “may often be applied in suits arising before their enactment without raising concerns about retroactivity”). But chapter 154 does more, for in its revisions of prior law to change standards of proof and persuasion in a way favorable to a State, the statute goes beyond “mere” procedure to affect substantive entitlement to relief. See 28 U.S.C. § 2264(b) (1994 ed., Supp.II), 110 Stat. 1223 (incorporating revised legal standard of new § 2254(d)). *Landgraf* did not speak to the rules for determining the temporal reach of such a statute (having no need to do so). While the statute might not have a true retroactive effect, neither was it clearly “procedural” so **2064 as to fall within the *328 Court's express (albeit qualified) approval of applying such statutes to pending cases. Since *Landgraf* was the Court's latest word on the subject

when the Act was passed, Congress could have taken the opinion's cautious statement about procedural statutes and its silence about the kind of provision exemplified by the new § 2254(d) as counseling the wisdom of being explicit if it wanted such a provision to be applied to cases already pending. While the terms of § 107(c) may not amount to the clear statement required for a mandate to apply a statute in the disfavored retroactive way,^{FN4} they do serve to make it clear as a general matter that *329 chapter 154 applies to pending cases when its terms fit those cases at the particular procedural points they have reached. (As to that, of course, there may well be difficult issues, and it may be that application of *Landgraf*'s default rule will be necessary to settle some of them.)

FN4. In *United States v. Nordic Village, Inc.*, 503 U.S. 30, 34-37, 112 S.Ct. 1011, 1014-1016, 117 L.Ed.2d 181 (1992), this Court held that the existence of “plausible” alternative interpretations of statutory language meant that that language could not qualify as an “unambiguous” expression of a waiver of sovereign immunity. And cases where this Court has found truly “retroactive” effect adequately authorized by a statute have involved statutory language that was so clear that it could sustain only one interpretation. See *Graham v. Goodcell*, 282 U.S. 409, 416-420, 51 S.Ct. 186, 189-190, 75 L.Ed. 415 (1931) (holding that a statutory provision “was manifestly intended to operate retroactively according to its terms” where the tax statute spelled out meticulously the circumstances that defined the claims to which it applied and where the alternative interpretation was absurd); *Automobile Club of Mich. v. Commissioner*, 353 U.S. 180, 184, 77 S.Ct. 707, 709-710, 1 L.Ed.2d 746 (1957) (finding a clear statement authorizing the Commissioner of Internal Revenue to correct tax rulings and regulations “retroactively” where the statutory

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

authorization for the Commissioner's action spoke explicitly in terms of "retroactivity"); *United States v. Zacks*, 375 U.S. 59, 65-67, 84 S.Ct. 178, 181-183, 11 L.Ed.2d 128 (1963) (declining to give retroactive effect to a new substantive tax provision by reopening claims otherwise barred by statute of limitations and observing that Congress had provided for just this sort of retroactivity for other substantive provisions by explicitly creating new grace periods in which otherwise barred claims could be brought under the new substantive law). Cf. *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 55-57, 116 S.Ct. 1114, 1123-1124, 134 L.Ed.2d 252 (1996) (finding a clear statement of congressional abrogation of Eleventh Amendment immunity where the federal statute went beyond granting federal jurisdiction to hear a claim and explicitly contemplated "the State" as defendant in federal court in numerous provisions of the Act).

Landgraf suggested that the following language from an unenacted precursor of the statute at issue in that case might possibly have qualified as a clear statement for retroactive effect: "[This Act] shall apply to *all* proceedings pending on or commenced after the date of enactment of this Act." 511 U.S., at 260, 114 S.Ct., at 1494 (emphasis added; internal quotation marks omitted). But, even if that language did qualify, its use of the sort of absolute language absent from § 107(c) distinguishes it. Cf. *United States v. Williams*, 514 U.S. 527, 531-532, 115 S.Ct. 1611, 1615-1616, 131 L.Ed.2d 608 (1995) (finding a waiver of sovereign immunity "unequivocally expressed" in language granting jurisdiction to the courts over "[a]ny civil action against the United States for the recovery of any internal-revenue tax alleged to have been

erroneously or illegally assessed or *collected*") (emphasis in *Williams*; internal quotation marks omitted); *id.*, at 541, 115 S.Ct., at 1620 (SCALIA, J., concurring) ("The [clear-statement] rule does not ... require explicit waivers to be given a meaning that is implausible ...").

The next point that is significant for our purposes is that everything we have just observed about chapter 154 is true of changes made to chapter 153. As we have already noted, amended § 2254(d) (in chapter 153 but applicable to chapter 154 cases) governs standards affecting entitlement to relief. If, then, Congress was reasonably concerned to ensure that chapter 154 be applied to pending cases, it should have been just as concerned about chapter 153, unless it had the different intent that the latter chapter not be applied to the general run of pending cases.

Nothing, indeed, but a different intent explains the different treatment. This might not be so if, for example, the two chapters had evolved separately in the congressional process, only to be passed together at the last minute, after chapter 154 had already acquired the mandate to apply it to pending cases. Under those circumstances, there might have been a real possibility that Congress would have intended the same rule of application for each chapter, but in the rough-and-tumble no one had thought of being careful about chapter 153, whereas someone**2065 else happened to think of inserting a *330 provision in chapter 154. But those are not the circumstances here. Although chapters 153 and 154 may have begun life independently and in different Houses of Congress,^{FN5} it was only after they had been joined together and introduced as a single bill in the Senate (S.735) that what is now § 107(c) was added.^{FN6} Both chapters, therefore, had to have been in mind when § 107(c) was added. Nor was there anything in chapter 154 prior to the addition that made the intent to apply it to pending cases less likely than a similar intent to apply chapter 153. If anything, the contrary is true, as the

discussion of § 2264(b) will indicate.

FN5. See 96 F.3d 856, 861 (C.A.7 1996). Lindh concedes this much. Brief for Petitioner 23, n. 15.

FN6. Amendment 1199, offered by Senator Dole on May 25, 1995, added what was then § 607(c) and now is § 107(c). See 141 Cong. Rec. 14600, 14614 (1995). A comparison of S. 735 as it stood on May 1, 1995, and S. 735 as it passed the Senate on June 7, after the substitution of Amendment 1199, reveals that the part of the bill dealing with habeas corpus reform was substantially the same before and after the amendment in all ways relevant to our interpretation of § 107(c).

[6] The insertion of § 107(c) with its different treatments of the two chapters thus illustrates the familiar rule that negative implications raised by disparate provisions are strongest when the portions of a statute treated differently had already been joined together and were being considered simultaneously when the language raising the implication was inserted. See *Field v. Mans*, 516 U.S. 59, 75, 116 S.Ct. 437, 446, 133 L.Ed.2d 351 (1995) (“The more apparently deliberate the contrast, the stronger the inference, as applied, for example, to contrasting statutory sections originally enacted simultaneously in relevant respects ...”). When § 107(c) was added, that is, a thoughtful Member of the Congress was most likely to have intended just what the later reader sees by inference.

The strength of the implication is not diminished by the one competing explanation suggested, see Brief for Respondent 11-12, which goes as follows. Chapter 154 provides for expedited filing and adjudication of habeas *331 applications in capital cases when a State has met certain conditions. In general terms, applications will be expedited (for a State's benefit) when a State has made adequate provision for counsel to represent indigent habeas applicants at the State's expense. Thus, § 2261(b)

provides that “[t]his chapter is applicable if a State establishes ... a mechanism for the appointment, compensation, and payment of reasonable litigation expenses of competent counsel in State post-conviction proceedings brought by indigent prisoners....” 110 Stat. 1221-1222. There is an ambiguity in the provision just quoted, the argument runs, for it applies chapter 154 to capital cases only where “a State establishes ... a mechanism,” leaving a question whether the chapter would apply if a State had already established such a mechanism before chapter 154 was passed. The idea is that the present tense of the word “establishes” might be read to rule out a State that already had “established” a mechanism, suggesting that when § 107(c) was added to provide that the chapter would apply to “cases pending” it was meant to eliminate the ambiguity by showing that all pending cases would be treated alike.

This explanation of the significance of § 107(c) is not, however, very plausible. First, one has to strain to find the ambiguity on which the alternative explanation is supposed to rest. Why would a Congress intent on expediting capital habeas cases have wanted to disfavor a State that already had done its part to promote sound resolution of prisoners' petitions in just the way Congress sought to encourage? It would make no sense to leave such States on the slower track, and it seems unlikely that federal courts would so have interpreted § 2261(b). Second, anyone who had seen such ambiguity lurking could have dispatched it in a far simpler and straightforward fashion than enacting § 107(c); all the drafter would have needed to do was to insert three words into § 2261(b), to make it refer to a State that “establishes or has established ... a mechanism.” It simply is not plausible *332 that anyone so sensitive as to find the unlikely ambiguity would be so delphic as to choose § 107(c) to **2066 fix it. Indeed, § 107(c) would (on the ambiguity hypothesis) be at least as uncertain as the language it was supposed to clarify, since “cases pending” could be read to refer to cases pending in States that set up their mechanisms only after the effective date of the

Act. The hypothesis of fixing ambiguity, then, is too remote to displace the straightforward inference that chapter 153 was not meant to apply to pending cases.

Finally, we should speak to the significance of the new § 2264(b), which Lindh cites as confirming his reading of § 107(c) of the Act. While § 2264(b) does not speak to the present issue with flawless clarity, we agree with Lindh that it tends to confirm the interpretation of § 107(c) that we adopt. Section 2264(b) is a part of the new chapter 154 and provides that “[f]ollowing review subject to subsections (a), (d), and (e) of § 2254, the court shall rule on the claims [subject to expedited consideration] before it.” 110 Stat. 1223. As we have said before, § 2254 is part of chapter 153 applying to habeas cases generally, including cases under chapter 154. Its subsection (a) existed before the Act, simply providing for a habeas remedy for those held in violation of federal law. Although § 2254 previously had subsections lettered (d) and (e) (dealing with a presumption of correctness to be accorded state-court factual findings and the production of state-court records when evidentiary sufficiency is challenged, respectively) the Act eliminated the old (d) and relettered the old (e) as (f); in place of the old (d), it inserted a new (d) followed by a new (e), the two of them dealing with, among other things, the adequacy of state factual determinations as bearing on a right to federal relief, and the presumption of correctness to be given such state determinations. 110 Stat. 1219. It is to these new provisions (d) and (e), then, that § 2264(b) refers when it provides that chapter 154 determinations shall be made subject to them.

*333 Leaving aside the reference to § 2254(a) for a moment, why would Congress have provided specifically in § 2264(b) that chapter 154 determinations shall be made subject to §§ 2254(d) and (e), given the fact that the latter are part of chapter 153 and thus independently apply to habeas generally? One argument is that the answer lies in § 2264(a), which (in expedited capital cases) specially

provides an exhaustion requirement (subject to three exceptions), restricting federal habeas claims to those “raised and decided on the merits in the State courts ...” 110 Stat. 1223. See 96 F.3d, at 862-863. The argument assumes (and we will assume for the sake of the argument) that in expedited capital cases, this provision of § 2264(a) supersedes the requirements for exhaustion of State remedies imposed as a general matter by §§ 2254(b) and (c).^{FN7} The argument then **2067 goes *334 on, that § 2264(b) is explicit in applying §§ 2254(d) and (e) to such capital cases in order to avoid any suggestion that when Congress enacted § 2264(a) to supersede §§ 2254(b) and (c) on exhaustion, Congress also meant to displace the neighboring provisions of §§ 2254(d) and (e) dealing with such things as the status of State factual determinations. But we find this unlikely. First, we find it hard to imagine why anyone would read a superseding exhaustion rule to address the applicability not just of the other exhaustion requirement but of provisions on the effect of state factual determinations. Anyone who did read the special provision for exhaustion in capital cases to supersede not only the general exhaustion provisions but evidentiary status and presumption provisions as well would have had to assume that Congress could reasonably have meant to leave the law on expedited capital cases (which is more favorable to the States that fulfill its conditions) without any presumption of the correctness of relevant state factual determinations. This would not, we think, be a reasonable reading and thus not a reading that Congress would have feared and addressed through § 2264(b). We therefore have to find a different function for the express requirement of § 2264(b) that chapter 154 determinations be made in accordance with §§ 2254(d) and (e).

FN7. There are reasons why the position that § 2264(a) replaces rather than complements §§ 2254(b) and (c) is open to doubt: Lindh argues with some force that to read § 2264(a) as replacing the exhaustion requirement of §§ 2254(b) and (c) would mean that in important classes of cases

(those in the categories of three § 2264(a) exceptions), the State would not be able to insist on exhaustion in the state courts. In cases raising claims of newly discovered evidence, for example, the consequence could be that the State could not prevent the prisoner from going directly to federal court and evading § 2254(e)'s presumption of correctness of state- court factual findings as well as § 2254(d)'s new, highly deferential standard for evaluating state-court rulings. It is true that a State might be perfectly content with the prisoner's choice to go straight to federal court in some cases, but the State has been free to waive exhaustion to get that result. The State has not explained why Congress would have wanted to deprive the States of the § 2254 exhaustion tools in chapter 154 cases, and we are hard-pressed to come up with a reason, especially considering the Act's apparent general purpose to enhance the States' capacities to control their own adjudications. It would appear that the State's reading of § 2264(a) would also eliminate from chapter 154 cases the provisions of § 2254 that define the exhaustion requirement explicitly as requiring a claim to be raised by any and every available procedure in the State, 28 U.S.C. § 2254(c), that newly authorize federal courts to deny unexhausted claims on the merits, § 2254(b)(2), and that newly require a State's waiver of exhaustion to be shown to be express, § 2254(b)(3). No explanation for why Congress would have wanted to deny the States these advantages is apparent or offered by the parties, which suggests that no such effects were intended at all but that § 2264(a) was meant as a supplement to rather than a replacement for §§ 2254(b) and (c).

Nevertheless, as stated in the text, we assume for the sake of argument that the

State's understanding of § 2264(a) as replacing rather than complementing the chapter 153 exhaustion requirements for chapter 154 is the correct one. Forceful arguments can be made on each side, and we do not need to resolve the conflict here.

Continuing on the State's assumption that § 2264(a) replaces rather than complements § 2254's exhaustion provisions, we can see that the function of providing that §§ 2254(d) and (e) be applicable in chapter 154 cases is, in fact, *335 supportive of the negative implication apparent in § 107(c). There would have been no need to provide expressly that subsections (d) and (e) would apply with the same temporal reach as the entirely new provisions of chapter 154 if all the new provisions in both chapters 153 and 154 were potentially applicable to cases pending when the Act took effect, as well as to those filed later. If the special provision for applying §§ 2254(d) and (e) in cases under chapter 154 has any utility, then, it must be because subsections (d) and (e) might not apply to all chapter 154 cases; since chapter 154 and the new sections of chapter 153 unquestionably apply alike to cases filed after the Act took effect, the cases to which subsections (d) and (e) from chapter 153 would not apply without express provision must be those cases already pending when the Act took effect. The utility of § 2264(b), therefore, is in providing that when a pending case is also an expedited capital case subject to chapter 154, the new provisions of §§ 2254(d) and (e) will apply to that case. The provision thus confirms that Congress assumed that in the absence of such a provision, §§ 2254(d) and (e) (as new parts of chapter 153) would not apply to pending federal habeas cases.

This analysis is itself consistent, in turn, with Congress's failure in § 2264(b) to make any express provision for applying §§ 2254(f), (g), (h), or (i). Subsections (f) and (g) deal with producing state-court evidentiary records and their admissibility as evidence. Congress would obviously have wanted

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

these provisions to apply in chapter 154 pending cases, but because they were old provisions, which had already attached to “pending” capital habeas cases (only their letter designations had been amended), Congress had no need to make any special provision for their application to pending capital habeas cases that might immediately or later turn out to be covered by chapter 154. Subsections (h) and (i), however, are new; if Congress wanted them to apply to chapter 154 cases from the start it would on our hypotheses have had to make the same special provision that § 2264(b) *336 made for subsections (d) and (e). But there are reasons why Congress need not have made any special provisions for subsections (h) and (i) to apply to the “pending” chapter 154 cases. Subsections (h) and (i) deal, respectively, with the appointment of counsel for the indigent in the federal proceeding, and the irrelevance to habeas relief of the adequacy of counsel's performance in previous postconviction proceedings. See 110 Stat. 1219-1220. There was no need to make subsection (h) immediately available to pending cases, capital or **2068 not, because 21 U.S.C. § 848(q)(4)(B) already authorized appointment of counsel in such cases. And there was no reason to make subsection (i) immediately available for a State's benefit in expedited capital cases, for chapter 154 already dealt with the matter in § 2261(e), see 110 Stat. 1222. There is, therefore, a good fit of the § 2264(b) references with the inference that amendments to chapter 153 were meant to apply only to subsequently filed cases; where there was a good reason to apply a new chapter 153 provision in the litigation of a chapter 154 case pending when the Act took effect, § 2264(b) made it applicable, and when there was no such reason it did no such thing.

There is only one loose end. Section 2254(a) was an old provision, without peculiar relevance to chapter 154 cases, but applicable to them without any need for a special provision; as an old provision it was just like the lettered subsections (f) and (g). Why did § 2264(b) make an express provision for applying it to chapter 154 cases? No answer

leaps out at us. All we can say is that in a world of silk purses and pigs' ears, the Act is not a silk purse of the art of statutory drafting.

The upshot is that our analysis accords more coherence to §§ 107(c) and 2264(b) than any rival we have examined. That is enough. We hold that the negative implication of § 107(c) is that the new provisions of chapter 153 generally apply only to cases filed after the Act became effective. Because Lindh's case is not one of these, we reverse the *337 judgment of the Court of Appeals and remand the case for further proceedings consistent with this opinion.

It is so ordered.

Chief Justice REHNQUIST, with whom Justice SCALIA, Justice KENNEDY, and Justice THOMAS join, dissenting.

The Court in this case conducts a truncated inquiry into a question of congressional intent, and, I believe, reaches the wrong result. The Court begins, uncontroversially enough, by observing that application of the Antiterrorism and Effective Death Penalty Act of 1996 (AEDPA) to pending cases depends upon congressional intent, and that our inquiry into that intent should rely upon the “normal rules” of statutory construction. *Ante*, at 2063. The Court then proceeds, however, to disregard all of our retroactivity case law—which it rather oddly disparages as manifestations of “*Landgraf's* default rule,” *ibid.*—in favor of a permissible, but by no means controlling, negative inference that it draws from the statutory text. I would instead interpret the AEDPA in light of the whole of our longstanding retroactivity jurisprudence, and accordingly find that the amended 28 U.S.C. § 2254(d) (1994 ed. Supp.II) applies to pending cases.

The first question we must ask is whether Congress has expressly resolved whether the provision in question applies to pending cases. *Landgraf v. USI Film Products*, 511 U.S. 244, 280, 114 S.Ct. 1483, 1505, 128 L.Ed.2d 229 (1994). Here, the answer is plainly no. The AEDPA does not clearly

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

state, one way or the other, whether chapter 153 applies to pending cases. Given congressional silence, we must still interpret that statute, and that interpretation is in turn guided by the retroactivity principles we have developed over the years. The Court relies on one canon of statutory interpretation, *expressio unius est exclusio alterius*, to the exclusion of all others.

The Court's opinion rests almost entirely on the negative inference that can be drawn from the fact that Congress expressly made chapter 154, pertaining to capital cases, applicable*338 to pending cases, but did not make the same express provision in regards to chapter 153. That inference, however, is by no means necessary, nor is it even clearly the best inference possible. Certainly, Congress might have intended that omission to signal its intent that chapter 153 not apply to pending cases. But there are other, equally plausible, alternatives.

First, because chapter 154's applicability is conditioned upon antecedent events—namely, a State's establishing qualifying capital habeas representation procedures—Congress could have perceived a greater likelihood that, absent express provision otherwise, courts would fail to apply that chapter's provisions to pending capital cases. **2069 Second, because of the characteristically extended pendency of collateral attacks on capital convictions,^{FN1} and because of Congress' concern with the perceived acquiescence in capital defendants' dilatory tactics by some federal courts (as evidenced by chapter 154's strict time limits for adjudication of capital cases and, indeed, by the very title of the statute, the “Antiterrorism and *Effective Death Penalty Act of 1996*”), Congress could very well have desired to speak with exacting clarity as to the applicability of the AEDPA to pending capital cases. Or third, Congress, while intending the AEDPA definitely to apply to pending capital cases, could have been uncertain or in disagreement as to which of the many portions of chapter 153 should or should not apply to pending cases. Congress could simply have assumed that the courts

would sort out such questions, using our ordinary retroactivity presumptions.

FN1. See, e.g., Pet. for Habeas Corpus in *In re Mata*, O.T. 1995, No. 96-5679, p. 7 (describing how it took nine years and three months for a Federal District Court to deny, and the Ninth Circuit to affirm, petitioner's first federal capital habeas petition).

None of these competing inferences is clearly superior to the others. The Court rejects the first, *ante*, at 2065-2066, as an “implausible” solution to an “unlikely” ambiguity. But *339 the solution is not nearly as implausible as the Court's contention that, in order to show that it wished chapter 153 *not* to apply to pending cases, Congress chose to make chapter 154 *expressly applicable* to such cases. If Congress wanted to make chapter 153 inapplicable to pending cases, the simplest way to do so would be to say so. But, if Congress was instead concerned that courts would interpret chapter 154, because of its contingent nature, as not applying to pending cases, the most direct way to solve that concern would be the solution it adopted: expressly stating that chapter 154 did indeed apply to pending cases.

The Court finds additional support for its inference in the new 28 U.S.C. § 2264(b) (1994 ed., Supp.II), which it believes “tends to confirm,” *ante*, at 2066, its analysis. Section 2264 is part of chapter 154 and forbids (subject to narrow exceptions) federal district courts to consider claims raised by state capital defendants unless those claims were first raised and decided on the merits in state court. Section 2264(b) provides, “[f]ollowing review subject to subsections (a), (d), and (e) of section 2254 [contained within chapter 153], the court shall rule on the claims properly before it.” This section, I believe, is irrelevant to the question before us.

The Court's somewhat tortured interpretation of this section, as a backhanded way of making §§ 2254(a), (d), and (e) (but not the rest of chapter 153

) apply to pending cases, is not convincing. For one thing, § 2264(b) is not phrased at all as a timing provision; rather than containing temporal language applying select sections to pending cases, § 2264(b) speaks in present tense, about how review should be conducted under chapter 154. Even more tellingly, as the Court implicitly concedes when it blandly describes this provision as a “loose end,” *ante*, at 2068, the AEDPA did not alter § 2254(a), and so there is no need for an express provision making it applicable to pending cases.

Chapter 154 establishes special procedures for capital prisoners. Section 2264(b), by its terms, makes clear that *340 §§ 2254(a), (d), and (e) apply to chapter 154 proceedings. That clarification makes sense in light of § 2264(a), which replaces the exhaustion requirement of §§ 2254(b) and (c) with a requirement that federal courts consider (subject to narrow exceptions) only those claims “raised and decided on the merits in the State courts.” Without that clarification, doubt might exist as to whether the rest of § 2254 still applied in capital proceedings.

Petitioner protests that to read § 2264(a) as supplanting §§ 2254(b) and (c) would produce “outlandish” results, Brief for Petitioner 26, a conclusion that the Court finds plausible, *ante*, at 2066–2067, and n. 7 (although it ultimately assumes otherwise). The result would have to be “outlandish,” indeed, before a court should refuse to apply the language chosen by Congress, but no such result would obtain here. Petitioner and the Court both fail to appreciate the different litigating **2070 incentives facing capital and noncapital defendants. Noncapital defendants, serving criminal sentences in prison, file habeas petitions seeking to be released, presumably as soon as possible. They have no incentive to delay. In such circumstances, §§ 2254(b) and (c) quite reasonably require that their habeas claims be filed first in state courts, so that the state judicial apparatus may have the first opportunity to address those claims. In contrast, capital defendants, facing impending execution,

seek to avoid being executed. Their incentive, therefore, is to utilize every means possible to delay the carrying out of their sentence. It is, therefore, not at all “outlandish” for Congress to have concluded that in such circumstances §§ 2254(b) and (c) exhaustion would needlessly prolong capital proceedings and that § 2264(a)'s requirement that a claim have been raised and decided on the merits in state court was a sufficient protection of States' interests in exhaustion.^{FN2}

FN2. This conclusion would also be consistent with the conclusions of the Powell Committee, which was convened to address the problems in capital habeas cases and upon whose recommendations chapter 154 was substantially based. See Judicial Conference of the United States, Ad Hoc Committee on Federal Habeas Corpus in Capital Cases, Committee Report and Proposal (Aug. 23, 1989). The Committee's Comment to Proposed § 2259 (which tracks the AEDPA's § 2264) explained as follows: “As far as new or ‘unexhausted’ claims are concerned, [this section] represents a change in the exhaustion doctrine as articulated in *Rose v. Lundy*, 455 U.S. 509, 102 S.Ct. 1198, 71 L.Ed.2d 379 (1982). [This section] bars such claims from consideration unless one of the ... exceptions is applicable. The prisoner cannot return to state court to exhaust even if he would like to do so. On the other hand, if [an exception] is applicable, the district court is directed to conduct an evidentiary hearing and to rule on the new claim without first exhausting state remedies as *Rose v. Lundy* now requires. Because of the existence of state procedural default rules, *exhaustion is futile in the great majority of cases*. It serves the state interest of comity in theory, but in practice it results in delay and undermines the state interest in the finality of its criminal convictions. *The Committee believes that the States would prefer to see*

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

post-conviction litigation go forward in capital cases, even if that entails a minor subordination of their interest in comity as it is expressed in the exhaustion doctrine.” *Id.*, at 22-23 (emphasis added).

*341 At this point the Court's analysis stops. Based on the weak inference from Congress' designation of chapter 154 as applying to pending cases and a strained reading of § 2264, the Court concludes that Congress impliedly intended for chapter 153 not to apply to pending cases. I would go on, and apply our ordinary retroactivity principles, as Congress no doubt assumed that we would.

First, we have generally applied new procedural rules to pending cases. *Landgraf*, 511 U.S., at 275, 114 S.Ct., at 1502; see also *Beazell v. Ohio*, 269 U.S. 167, 170-171, 46 S.Ct. 68, 68-69, 70 L.Ed. 216 (1925); *Ex parte Collett*, 337 U.S. 55, 71, 69 S.Ct. 944, 952, 93 L.Ed. 1207 (1949); *Dobbert v. Florida*, 432 U.S. 282, 293-294, 97 S.Ct. 2290, 2298-2299, 53 L.Ed.2d 344 (1977); *Collins v. Youngblood*, 497 U.S. 37, 45, 110 S.Ct. 2715, 2720-2721, 111 L.Ed.2d 30 (1990). This is because “rules of procedure regulate secondary rather than primary conduct.” *Landgraf*, *supra*, at 275, 114 S.Ct., at 1502. Here, the primary conduct occurred when Lindh murdered two people in the sheriff's office of the City-County Building in Madison, Wisconsin. Obviously, the AEDPA in no way purports to regulate that past conduct. Lindh's state-court proceedings constituted secondary conduct. Under our retroactivity *342 precedents, were his state proceedings in federal court, we would have then applied existing procedural law, even though Lindh's primary conduct occurred some time earlier. The federal habeas proceeding at issue here is, in a sense, tertiary conduct. It is not the actual criminal conduct prohibited by law, nor is it the proceeding to determine whether the defendant in fact committed such conduct. Rather, it is a collateral proceeding that, in effect, attacks the judgment of the prior state proceeding. Section 2254(d), the precise section at issue here, simply alters the standard

under which that prior judgment is evaluated, and is in that sense entirely procedural. Cf. *Horning v. District of Columbia*, 254 U.S. 135, 139, 41 S.Ct. 53, 54, 65 L.Ed. 185 (1920) (applying newly enacted harmless-error statute, which changed the standard under which prior judgments were evaluated, to pending case).

**2071 Second, we have usually applied changes in law to prospective forms of relief. *Landgraf*, *supra*, at 273, 114 S.Ct., at 1501; see also *Duplex Printing Press Co. v. Deering*, 254 U.S. 443, 464, 41 S.Ct. 172, 175-176, 65 L.Ed. 349 (1921); *American Steel Foundries v. Tri-City Central Trades Council*, 257 U.S. 184, 201, 42 S.Ct. 72, 75-76, 66 L.Ed. 189 (1921); *Hall v. Beals*, 396 U.S. 45, 48, 90 S.Ct. 200, 201-202, 24 L.Ed.2d 214 (1969) (*per curiam*); *Kaiser Aluminum & Chemical Corp. v. Bonjorno*, 494 U.S. 827, 852, 110 S.Ct. 1570, 1584-1585, 108 L.Ed.2d 842 (1990) (SCALIA, J., concurring). Unlike damages actions, which are “quintessentially backward looking,” *Landgraf*, *supra*, at 282, 114 S.Ct., at 1506, the writ of habeas corpus is prospective in nature. Habeas does not compensate for past wrongful incarceration, nor does it punish the State for imposing it. See *Lane v. Williams*, 455 U.S. 624, 631, 102 S.Ct. 1322, 1326-1327, 71 L.Ed.2d 508 (1982). Instead, habeas is a challenge to unlawful custody, and when the writ issues it prevents further illegal custody. See *Preiser v. Rodriguez*, 411 U.S. 475, 489, 494, 93 S.Ct. 1827, 1836, 1838-1839, 36 L.Ed.2d 439 (1973).

Finally, we have regularly applied statutes ousting jurisdiction to pending litigation.^{FN3} *Landgraf*, *supra*, at 274, 114 S.Ct., at 1501-1502; see *343 also *Bruner v. United States*, 343 U.S. 112, 116-117, and n. 8, 72 S.Ct. 581, 584 and n. 8, 96 L.Ed. 786 (1952) (“Congress has not altered the nature or validity of petitioner's rights or the Government's liability but has simply reduced the number of tribunals authorized to hear and determine such rights and liabilities”); *Hallowell v. Commons*, 239 U.S. 506, 508, 36 S.Ct. 202, 203, 60 L.Ed. 409

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

(1916); *Sherman v. Grinnell*, 123 U.S. 679, 680, 8 S.Ct. 260, 261, 31 L.Ed. 278 (1887); *Assessors v. Osbornes*, 9 Wall. 567, 575, 19 L.Ed. 748 (1869); *Ex parte McCardle*, 7 Wall. 506, 514, 19 L.Ed. 264 (1868); *Insurance Co. v. Ritchie*, 5 Wall. 541, 544-545, 18 L.Ed. 540 (1866). This is because such statutes “ ‘speak to the power of the court rather than to the rights or obligations of the parties.’ ” *Landgraf, supra*, at 274, 114 S.Ct., at 1502 (quoting *Republic Nat. Bank of Miami v. United States*, 506 U.S. 80, 100, 113 S.Ct. 554, 565, 121 L.Ed.2d 474 (1992) (THOMAS, J., concurring)); see also 511 U.S., at 269, 114 S.Ct., at 1499, (SCALIA, J., concurring in judgment) (“Our jurisdiction cases are explained, I think, by the fact that the purpose of provisions conferring or eliminating jurisdiction is to permit or forbid the exercise of judicial power-so that the relevant event for retroactivity purposes is the moment at which that power is sought to be exercised”). This is the principle most relevant to the case at hand.

FN3. Although in *Hughes Aircraft Co. v. United States ex rel. Schumer*, 520 U.S. 939, 117 S.Ct. 1871, 138 L.Ed.2d 135 (1997), we recently rejected a presumption favoring retroactivity for jurisdiction-creating statutes, see *id.*, at 950-951, 117 S.Ct. at 1878, nothing in *Hughes* disparaged our longstanding practice of applying jurisdiction-ousting statutes to pending cases.

There is a good argument that § 2254(d) is itself jurisdictional. See *Brown v. Allen*, 344 U.S. 443, 460, 73 S.Ct. 397, 408-409, 97 L.Ed. 469 (1953) (“Jurisdiction over applications for federal habeas corpus is controlled by statute”); *Sumner v. Mata*, 449 U.S. 539, 548, n. 2, 101 S.Ct. 764, 770 n. 2, 66 L.Ed.2d 722 (1981) (“The present codification of the federal habeas statute is the successor to ‘the first congressional grant of jurisdiction to the federal courts,’ and the 1966 amendments embodied in § 2254(d) [now codified, as amended by the AEDPA, at § 2254(e)] were intended by Congress

as limitations on the exercise of that jurisdiction” (quoting *Preiser v. Rodriguez, supra*, at 485, 93 S.Ct., at 1833-1834); cf. *Arkansas v. Farm Credit Servs. of Central Ark.*, 520 U.S. 821, 826, 117 S.Ct. 1776, 1778, 138 L.Ed.2d 34 (1997) (explaining that the Tax Injunction Act-which has operative language similar to *344 § 2254(d) (“The district courts shall not enjoin ... ”)-is “first and foremost a vehicle to limit drastically federal district court jurisdiction to interfere with so important a local concern as the collection of taxes” (internal quotation marks omitted)). But even if it is not jurisdictional, it shares the most salient characteristic of jurisdictional statutes: its commands are addressed to courts rather than to individuals. Section 2254(d) does not address criminal defendants, or even state prosecutors; it prescribes or proscribes no private conduct. **2072 Instead, it is addressed directly to federal courts, providing, “[a]n application for a writ of habeas corpus on behalf of a person in custody pursuant to the judgment of a State court *shall not be granted ... unless*” (Emphasis added.)

Whether the approach is framed in terms of “retroactive effect,” as the *Landgraf* majority put it, 511 U.S., at 280, 114 S.Ct., at 1505, or in terms of “the relevant activity that the rule regulates,” as Justice SCALIA's concurrence put it, see *id.*, at 291, 114 S.Ct., at 1524 (opinion concurring in judgment), our longstanding practice of applying procedural, prospective, and jurisdiction-ousting statutes to pending cases must play an important part in the decision. These principles all favor application of § 2254(d) to pending cases.

It is a procedural statute, regulating prospective relief, and addressed directly to federal courts and removing their power to give such relief in specified circumstances. Our cases therefore strongly suggest that, absent congressional direction otherwise, we should apply § 2254(d) to pending cases. This is not because of any peculiar characteristic intrinsic to the writ of habeas corpus, but rather because modifications to federal courts' authority to issue the writ are necessarily of that stripe-

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70
(Cite as: 521 U.S. 320, 117 S.Ct. 2059)

procedural, prospective, and addressed to courts. It is therefore not surprising that the parties have not pointed us to a single case where we have found a modification in the scope of habeas corpus relief inapplicable to pending cases. To the contrary, respondent and *345 amici have pointed instead to the uniform body of our cases applying such changes to all pending cases. This has been true both of statutory changes in the scope of the writ, see, e.g., *Gusik v. Schilder*, 340 U.S. 128, 131-133, and n. 4, 71 S.Ct. 149, 151-153, and n. 4, 95 L.Ed. 146 (1950) (applying 1948 habeas amendments to pending claims); *Smith v. Yeager*, 393 U.S. 122, 124-125, 89 S.Ct. 277, 278-279, 21 L.Ed.2d 246 (1968) (*per curiam*) (applying 1966 habeas amendments to pending claims); *Carafas v. LaVallee*, 391 U.S. 234, 239, 88 S.Ct. 1556, 1560, 20 L.Ed.2d 554 (1968) (same); *Felker v. Turpin*, 518 U.S. 651, 116 S.Ct. 2333, 135 L.Ed.2d 827 (1996) (applying different section of the AEDPA to pending case), and of judicial changes, see, e.g., *Stone v. Powell*, 428 U.S. 465, 495, n. 38, 96 S.Ct. 3037, 3052-3053, n. 38, 49 L.Ed.2d 1067 (1976) (rejecting petitioner's contention that change in law should apply prospectively); *Sumner v. Mata*, *supra*, at 539, 549-551, 101 S.Ct., at 765, 770-771 (applying presumption of correctness of state-court findings of fact to pending case); *Wainwright v. Sykes*, 433 U.S. 72, 97 S.Ct. 2497, 53 L.Ed.2d 594 (1977) (applying the cause and prejudice doctrine to pending case); *Brecht v. Abrahamson*, 507 U.S. 619, 638-639, 113 S.Ct. 1710, 1722-1723, 123 L.Ed.2d 353 (1993) (applying actual prejudice standard to pending case).

END OF DOCUMENT

Because the Court's inquiry is incomplete, I believe it has reached the wrong result in this case. I would affirm the judgment of the Court of Appeals.

U.S., 1997.

Lindh v. Murphy

521 U.S. 320, 117 S.Ct. 2059, 138 L.Ed.2d 481, 65 USLW 4557, 97 Cal. Daily Op. Serv. 4801, 97 Daily Journal D.A.R. 7862, 97 CJ C.A.R. 976, 11 Fla. L. Weekly Fed. S 70

▷

WESLEY G. MESLER, Plaintiff and Appellant,
v.
BRAGG MANAGEMENT COMPANY, Defendant
and Respondent

L.A. No. 31996.

Supreme Court of California
Aug 1, 1985.

SUMMARY

The trial court granted summary judgment against an employee whose arm was amputated by the engine fan of a dozer, upon a motion brought by a management company that was the corporate parent of a company that had owned the dozer before the employer. Following discovery that revealed both the employer and such former owner of the dozer to be wholly owned subsidiaries of the management company, the employee substituted the management company for a fictitious defendant. The management company moved for summary judgment on the ground that it had no connection whatever with the dozer, the work place, or the employee. The trial court stated that the employee appeared to rely on an alter ego theory to hold the management company liable, and that, although much discovery had been conducted on the issue, an alter ego theory had not been pleaded. Despite the employee's request to amend the pleadings, the court granted the management company's motion. During the pendency of the appeal from the summary judgment, the injured employee settled with the subsidiary company that had owned the dozer before the employer. (Superior Court of Los Angeles County, No. SWC53127, John A. Shidler, Judge.)

The Supreme Court reversed the summary judgment. The trial court erred in denying the employee's request to amend the pleadings to allege an alter ego theory as to the management company's liability. The trial court apparently based its ruling

on its reluctance to postpone the employee's trial date, but it was the employee who desired to amend regardless of any resulting postponement. Additionally, the management company could hardly have been surprised by the employee's reliance on the alter ego theory. Moreover, the employee was prejudiced by this ruling, since his entire theory opposing summary judgment revolved around the relationship between the management company and the two subsidiaries. The court further held that a plaintiff may pursue a tort action against a parent corporation on the theory that it is the alter ego of its subsidiary, the alleged tortfeasor, despite entering into a settlement and release with the subsidiary. This is due to the applicability of Code Civ. Proc., § 877, which abrogated the common law rule that settlement with one alleged tortfeasor bars action against any others claimed liable for the same injury. Thus, the subsequent release of the subsidiary did not preclude the employee's suit against its claimed alter ego and parent corporation, the management company. (Opinion by Mosk, J., with Bird, C. J., Kaus, Broussard and Reynoso, JJ., concurring. Separate dissenting opinion by Lucas, J., with Grodin, J., concurring.)

HEADNOTES

Classified to California Digest of Official Reports
(1) Pleading § 67--Amendment by Leave of Court--Appellate Review.

When a request, pursuant to Code Civ. Proc., § 473, to amend a pleading has been denied, an appellate court is confronted by two conflicting policies. On the one hand, the trial court's discretion should not be disturbed unless it has been clearly abused; on the other, there is a strong policy in favor of liberal allowance of amendments. This conflict is often resolved in favor of the privilege of amending, and reversals are common where the appellant makes a reasonable showing of prejudice from the ruling.

(2) Summary Judgment § 10--Affidavits--Reliance on Pleadings.

Since the object of the summary judgment proceeding is to discover proof, the adverse party must file an affidavit in opposition to the motion. He cannot rely on a verified pleading alone. Thus, in a tort action, the trial court did not abuse its discretion by granting summary judgment for defendant on plaintiff's agency issue. Although agency was alleged in the pleadings, it was not argued in the summary judgment proceeding or supported by affidavits.

(3) Corporations § 46--Actions by and Against Corporations--Pleading-- Summary Judgment--Alter Ego Liability.

In a tort action, in which a management company was substituted for a fictitious defendant after discovery by plaintiff revealed two other defendants were wholly owned subsidiaries of the management company, the trial court erred in denying plaintiff's request to amend the pleadings to allege an alter ego theory as to the management company's liability for plaintiff's injuries, and in thereby granting the management company's motion for summary judgment. The trial court apparently based its ruling on its reluctance to postpone plaintiff's trial date, yet it was plaintiff who desired to amend regardless of any resulting postponement. Additionally, the management company could hardly have been surprised by plaintiff's reliance on the alter ego theory. Finally, plaintiff was clearly prejudiced by this ruling, since his entire theory opposing summary judgment revolved around the relationship between the management company and the two subsidiaries.

(4a, 4b) Compromise, Settlement, and Release § 9--Construction, Operation, and Effect--Settlement With Corporate Subsidiary--Alter Ego Liability of Parent Corporation.

A plaintiff may pursue a tort action against a parent corporation on the theory that it is the alter ego of its subsidiary, the alleged tortfeasor, despite the plaintiff's having entered into a settlement and release with the subsidiary. This is due to the applicability of Code Civ. Proc., § 877, which abrog-

ated the common law rule that settlement with one alleged tortfeasor bars action against any others claimed liable for the same injury. Thus, in a products liability and negligence action by an employee whose arm was amputated by the engine fan of a dozer, the trial court abused its discretion in refusing to allow the employee to amend his pleadings so as to proceed on an alter ego basis, against a management company that was the corporate parent of a company that had owned the dozer before the employer, even though the employee subsequently entered into a settlement with such former owner of the dozer, a wholly owned subsidiary of the management company. The release of the subsidiary, the company that had owned the dozer, during the pendency of the appeal, did not preclude suit against its claimed alter ego, the management company.

(5a, 5b) Corporations § 3--Power of Court to Disregard Corporate Entity--Alter Ego Doctrine.

The alter ego doctrine arises when a plaintiff comes into court claiming that an opposing party is using the corporate form unjustly and in derogation of the plaintiff's interest. In certain circumstances the court will disregard the corporate entity and will hold the individual shareholders liable for the actions of the corporation. However, when a court disregards the corporate entity, it does not dissolve the corporation.

(6) Corporations § 4--Power of Court to Disregard Corporate Entity--When Power Will or Will Not Be Exercised--General Requirements.

There is no litmus test to determine when the corporate veil will be pierced; rather, the result will depend on the circumstances of each particular case. There are, nevertheless, two general requirements: that there be such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist; and that, if the acts are treated as those of the corporation alone, an inequitable result will follow. Only a difference in wording is used in stating the same concept where the entity sought to be held liable is

another corporation instead of an individual.

(7) Corporations § 3--Power of Court to Disregard Corporate Entity--Alter Ego Doctrine--Equitable Result.

The essence of the alter ego doctrine, in which it is claimed that an opposing party is using the corporate form unjustly, is that justice be done. What the formula comes down to, once shorn of verbiage about control, instrumentality, agency and corporate entity, is that liability is imposed to reach an equitable result. Thus, the corporate form will be disregarded only in narrowly defined circumstances and only when the ends of justice so require.

(8) Compromise, Settlement, and Release § 9--Compromise and Settlement-- Construction, Operation, and Effect--Joint Tortfeasors.

The language in Code Civ. Proc., § 877, which abrogated the common law rule that settlement with one alleged tortfeasor bars action against any others claimed liable for the same injury, in using the broad term "tortfeasors claimed to be liable for the same tort" rather the narrower term "joint tortfeasors," was meant to eliminate the distinction between joint tortfeasors and concurrent or successive tortfeasors, and to permit broad application of the statute.

(9) Agency § 31--Rights, Duties and Liabilities--Liability of Principal for Torts of Agent--Following Settlement With Agent--Liability of Parent Corporation for Torts of Subsidiary Corporation.

A principal alleged to be vicariously liable in tort for the acts of its agent is subject to suit following settlement with the agent. The principal is held vicariously liable, not because it was necessarily at fault, but because justice requires that the enterprise be responsible for the risks of conducting its business. Similarly, the parent corporation is liable for the acts of its subsidiary under the alter ego doctrine because justice requires that the corporate wall be breached. Although the subsidiary may not be an agent in any true sense, the justification for a parent's or affiliate's liability is analogous to the justi-

fication of the liability of a principal for the acts of a general agent. An involuntary creditor who has had foisted upon him a subsidiary unable to respond in damages has a greater equity.

(10) Compromise, Settlement, and Release § 9--Construction, Operation, and Effect--Principal-agent Liability.

The provisions of Code Civ. Proc., § 877, which abrogated the common law rule that settlement with one alleged tortfeasor bars action against any others claimed liable for the same injury, applies to principal-agent liability. Thus, under § 877, the liability of a principal for the tortious acts of his agent, even though wholly vicarious, survives the release of the agent.

[Release of, or covenant not to sue, one primarily liable for tort, but expressly reserving rights against one secondarily liable, as bar to recovery against latter, note, 24 **A.L.R.4th** 547. See also, **Cal.Jur.3d**, Compromise, Settlement, and Release, § 95 et seq.; **Am.Jur.2d**, Release, § 37 et seq.]

(11) Statutes § 21--Construction--Legislative Intent--Existing Judicial Decisions.

The Legislature is presumed to be aware of existing judicial decisions.

(12) Compromise, Settlement, and Release § 4--Construction, Operation, and Effect--Joint Tortfeasors.

Three interests are at work in Code Civ. Proc., § 877, which abrogated the common law rule that settlement with one alleged tortfeasor bars action against any other claimed liable for the same injury. First is maximization of recovery of the injured party for the amount of his injury to the extent fault of others has contributed to it. Second is encouragement of settlement of the injured party's claim. Third is the equitable apportionment of liability among the tortfeasors.

COUNSEL

Wylie A. Aitken and John C. Adams III for Plaintiff and Appellant.

Pray, Price, Williams & Russell and Jay H. Picking for Defendant and Respondent.

MOSK, J.

We consider whether a plaintiff may pursue a tort action against a parent corporation on the theory that it is the alter ego of its subsidiary, the alleged tortfeasor, after entering into a settlement and release agreement with the subsidiary. At issue is the applicability of Code of Civil Procedure section 877,^{FN1} which abrogates the common law rule that settlement *295 with one alleged tortfeasor bars action against any others claimed liable for the same injury. We conclude that the statute does apply, and thus release of an alleged tortfeasor under these circumstances does not preclude suit against its claimed alter ego.

FN1 All statutory references are to the Code of Civil Procedure.

The relevant facts, as alleged by plaintiff, are as follows. One night in the summer of 1979, plaintiff was operating a Caterpillar D-9 Dozer atop a 30-foot coke pile. Because he had some difficulty raising the front blade of the dozer, he exited the cab to inspect the vehicle but left the engine running. While moving along the tread of the dozer he stumbled in the darkness. As he slipped, his right arm was thrust into the dozer's engine fan, and approximately one-third of the arm was amputated.

Plaintiff filed a claim for personal injuries against Crescent Cranes, Inc. dba Crescent Coke Handlers, Inc. (hereafter Crescent Coke), plaintiff's employer at the time of the accident;^{FN2} Mobil Oil Corporation, on whose premises the accident occurred; Great Lakes Carbon Corporation, owner of the coke pile; M.P. McCaffrey's, Inc., a corporation that had sold the used dozer to Crescent Coke; Caterpillar Tractor Company, manufacturer of the dozer; Bragg Crane Services, Inc. (hereafter Bragg Crane), a company that had owned the dozer before Crescent Coke; and Does. Plaintiff alleged strict products liability and negligence in design, manu-

facture, marketing, distribution, installation, inspection, purchase, maintenance, and handling of the dozer by Crescent Coke, McCaffrey, Caterpillar, Bragg Crane, and Does. Plaintiff further claimed that Mobil, Great Lakes Carbon, Crescent Coke, Bragg Crane and Does were negligent in the maintenance of the workplace. The complaint included a paragraph reciting that "each of the defendants was the agent and employee of each of the remaining defendants and was at all times herein mentioned acting within the scope of said agency and employment."

FN2 Plaintiff's suit against Crescent Coke was dismissed because of a pending workers' compensation proceeding.

Defendants filed various cross-complaints and motions for summary judgment. Relevant to the present action was a motion for summary judgment by Bragg Crane. It claimed to have no connection with the workplace or with plaintiff, and alleged it had had no contact with the dozer since it sold the machine to Crescent Coke in 1976. Plaintiff opposed the motion by asserting inter alia that Crescent Coke and Bragg Crane were alter egos, and thus Bragg Crane could be held responsible for Crescent Coke's negligence. The motion for summary judgment was denied.

Over two years after plaintiff filed his complaint, following discovery that revealed both Crescent Coke and Bragg Crane to be wholly owned subsidiaries *296 of another entity, Bragg Management Company (hereafter sometimes called defendant), plaintiff substituted the latter as Doe I. Bragg Management moved for summary judgment on the ground that it had no connection whatever with the dozer, the workplace, or plaintiff. The trial court stated that plaintiff appeared to rely on an alter ego theory to hold Bragg Management liable, and that although much discovery had been conducted on the issue an alter ego theory had not been pleaded. Despite plaintiff's request to amend the pleadings, the court granted defendant's motion. Plaintiff appeals from the judgment entered on this ruling.

Plaintiff contends there were triable issues of fact as to both alter ego and agency theories, that it is not necessary to specifically plead alter ego, and that the determination whether an alter ego relationship exists is for the trier of fact. Defendant responds that there were no triable issues of fact. Further, it argues that the point is moot because during the pendency of the appeal, plaintiff settled with Bragg Crane. Defendant claims that by dismissing with prejudice his suit against Bragg Crane plaintiff removed the basis of his action against Bragg Crane's alter ego. Plaintiff replies that section 877 governs this situation, and thus settlement with one defendant does not release the other.

I.

We first address the question whether summary judgment was proper in light of the posture of the case at the time the court ruled - that is, before plaintiff's settlement with Bragg Crane. The judge's reason for granting the motion is apparent from the transcript of the hearing. He stated he would probably grant plaintiff's request to amend the pleadings to include an alter ego allegation, and deny the summary judgment motion. Counsel for the defense then reminded him that the trial date was only six weeks away. The judge, remarking that to permit the new allegation would "destroy the plaintiff's time of trial" then declared he would not allow plaintiff to amend. Plaintiff's counsel urged that plaintiff would rather include Bragg Management and have trial postponed than retain the trial date as set, and that trial would be postponed in any event because an important party would be missing. These pleas fell on deaf ears, however, and the summary judgment motion was granted.

Section 473 provides that "in furtherance of justice" a court may allow a party to amend its pleadings. (1) When a request to amend has been denied, an appellate court is confronted by two conflicting policies. On the one hand, the trial court's discretion should not be disturbed unless it has been clearly abused; on the other, there is a strong policy in favor of liberal allowance of amendments. This

conflict "is often resolved in favor of the *297 privilege of amending, and reversals are common where the appellant makes a reasonable showing of prejudice from the ruling." (3 Witkin, Cal. Procedure (2d ed. 1971) Pleading, § 1042, pp. 2620-2621.) (2) (See fn. 3.) Unfair surprise to the opposing party is also to be considered. (*Id.*, § 1048, p. 2623.)^{FN3}

FN3 Plaintiff argues that the court should not have granted summary judgment because issues of fact remained as to his agency theory. However, although agency was alleged in the pleadings, it was not argued below or supported by affidavits. "Since the object of the [summary judgment] proceeding is to discover *proof*, the adverse party must file an affidavit in opposition to the motion; he cannot rely on a verified pleading alone." (4 Witkin, Cal. Procedure (2d ed. 1971), italics in original), Proceedings Without Trial, § 188, p. 2837; *Hayward, etc. School Dist. v. Madrid* (1965) 234 Cal.App.2d 100, 120 [44 Cal.Rptr. 268].) Thus the court did not abuse its discretion by granting summary judgment on the agency issue.

(3) In the case at bar the court should have permitted plaintiff to plead the alter ego issue. It apparently based its ruling on its reluctance to "destroy the plaintiff's time of trial," yet it was plaintiff who desired to amend regardless of any resulting postponement. Additionally, defendant could hardly have been surprised by plaintiff's reliance on the alter ego theory. As the court stated, there had been much discovery on the issue before defendant's and Bragg Crane's motions for summary judgment. Agency, a related concept, had been alleged in plaintiff's original complaint, to which defendant had been substituted as a Doe. And plaintiff had argued the alter ego theory in its opposition to defendant's motion. Finally, plaintiff was clearly prejudiced by this ruling, since his entire theory opposing summary judgment revolved around the relationship between defendant, Bragg

Crane and Crescent Coke.

II.

We turn to the key question whether plaintiff's settlement with Bragg Crane operated to release its alter ego, Bragg Management. For this purpose we examine the history and policies underlying section 877.

At common law if a plaintiff sued two or more tortfeasors and settled with one, the others were released. The rationale for this rule was that the plaintiff had suffered only one injury, for which there could be only one satisfaction. As each tortfeasor was jointly and severally liable for the entire injury, a settlement with any of them fully compensated the plaintiff. To permit the plaintiff to proceed against the others would sanction double recovery. (*Lamoreux v. San Diego etc. Ry. Co.* (1957) 48 Cal.2d 617, 624 [311 P.2d 1]; *Chetwood v. California National Bank* (1896) 113 Cal. 414, 426 [45 P. 704]; Thaxter, *Joint Tortfeasors: Legislative Changes in the *298 Rules Regarding Releases and Contribution* (1958) 9 Hastings L.J. 180, 182.)

The rule was thus based on the misconception, as Dean Prosser suggested, that a "satisfaction" is the equivalent of a "release." (Prosser, *Joint Torts and Several Liability* (1937) 25 Cal.L.Rev. 413, 423.) However, while "[a] satisfaction is an acceptance of full compensation for the injury; a release is a surrender of the cause of action, which may be gratuitous, or given for inadequate consideration." (*Ibid.*) Even if it could be said that any sum the plaintiff received in settlement was a compensation for the joint wrong(*Lamoreux, supra*, 48 Cal.2d at p. 624), the rule produced unfair results. For example, a plaintiff who settled with a defendant of modest resources for an amount below the value of his damages did not have his claim fully satisfied; nevertheless, under the common law rule he could not seek further compensation from other defendants.

In order to avoid this harsh rule, the covenant

not to sue was developed. These covenants were not releases, but rather promises not to prosecute a lawsuit against the covenantee. Since the "language is of covenant and indemnity, not of release" (*Kincheloe v. Retail Credit Co., Inc.* (1935) 4 Cal.2d 21, 23 [46 P.2d 971]), it would not preclude suit against other tortfeasors. (*Ibid.*) The problem then became whether an instrument should be interpreted as a release or a covenant not to sue. As this court recognized, "the distinction between a release and a covenant not to sue is entirely artificial. As between the parties to the agreement, the final result is the same in both cases, namely, that there is no further recovery from the defendant who makes the settlement, and the difference in the effect as to third parties is based mainly, if not entirely, on the fact that in one case, there is an immediate release, whereas in the other there is an agreement not to prosecute a suit." (*Pellett v. Sonotone Corp.* (1945) 26 Cal.2d 705, 711 [160 P.2d 783, 160 A.L.R. 863].)

In 1957 the Legislature responded to the problem by adopting section 877: "Where a release, dismissal with or without prejudice, or a covenant not to sue or not to enforce judgment is given in good faith before verdict or judgment to one or more of a number of tortfeasors claimed to be liable for the same tort - [¶] (a) It shall not discharge any other such tortfeasor from liability unless its terms so provide, but it shall reduce the claims against the others in the amount stipulated by the release, the dismissal or the covenant, or in the amount of the consideration paid for it whichever is the greater; and [¶] (b) It shall discharge the tortfeasor to whom it is given from all liability for any contribution to any other tortfeasor."

Section 877 is but one part of a package of legislation entitled "Releases From and Contribution Among Joint Tortfeasors." Included therein is a *299 section providing for contribution among joint judgment debtors (§ 875), a provision for the determination of each judgment debtor's pro rata share (§ 876), section 877 which abrogates the

common law release rule, a section added in 1977 to deal with sliding scale agreements (§ 877.5), a section enacted after *American Motorcycle Assn. v. Superior Court* (1978) 20 Cal.3d 578 [146 Cal.Rptr. 182, 578 P.2d 899], establishing procedures for determining whether a settlement is in good faith (§ 877.6), and a provision detailing the procedure a judgment debtor may follow to obtain contribution from another tortfeasor (§ 878).

(4a) It is clear that if section 877 applies to the case before us, it would allow plaintiff to pursue his action against defendant Bragg Management despite his settlement with Bragg Crane. Defendant argues, however, that section 877 does not apply to alter ego situations. It maintains that an alter ego claim rests on the theory that two distinct entities are really one, and thus settlement with one must ipso facto encompass the other. Section 877, defendant asserts, applies only to joint tortfeasors, not to a parent corporation held liable for the torts of its subsidiary on an alter ego rationale.

Defendant cites as controlling a federal district court case, *Fuls v. Shastina Properties, Inc.* (N.D.Cal. 1978) 448 F.Supp. 983. That case arose from the defendants' alleged fraud in selling certain property to the plaintiffs. The plaintiffs sued Shastina Properties, its sales agents, and its alleged alter ego, Beverly Enterprises. Subsequently, the plaintiffs entered a settlement and release agreement with the sales agents, which the court found to include by its express language Shastina Properties. (*Id.*, at p. 989.) The court dispensed with the plaintiffs' claim against Beverly Enterprises in one brief paragraph: "Beverly is alleged to have been the alter ego of Shastina Properties. Under California law, a corporation is treated as being the alter ego of another corporation only if there is 'such a unity of interest and ownership that the individuality of such corporation and the owner or owners of its stock has ceased.' [Citation.] Where the alter ego doctrine applies, therefore, the two corporations are treated as one for purposes of determining liability. It follows that where the one corporation is released

from liability, so too is the other. Thus, it is unnecessary to consider whether Beverly was in fact the alter ego of Shastina Properties in this case. If it were, it would also be released by the Agreement." (*Ibid.*; see also *M/V American Queen v. San Diego Marine Const.* (9th Cir. 1983) 708 F.2d 1483, 1490 (citing and relying on *Fuls*.)

These cases do not settle the matter. To begin with, of course, decisions of the federal courts interpreting California law are persuasive but not binding. Second, the cursory reasoning of *Fuls* would not be controlling in any event, for it contains no discussion whatever of section 877 or the cases *300 interpreting it. Further, the decision is based on a misinterpretation of the alter ego doctrine in California.

(5a) The alter ego doctrine arises when a plaintiff comes into court claiming that an opposing party is using the corporate form unjustly and in derogation of the plaintiff's interests. (6 Witkin, Summary of Cal. Law (8th ed. 1974) Corporations, § 5, p. 4318.) In certain circumstances the court will disregard the corporate entity and will hold the individual shareholders liable for the actions of the corporation: "As the separate personality of the corporation is a statutory privilege, it must be used for legitimate business purposes and must not be perverted. When it is abused it will be disregarded and the corporation looked at as a collection or association of individuals, so that the corporation will be liable for acts of the stockholders or the stockholders liable for acts done in the name of the corporation." (Comment, *Corporations: Disregarding Corporate Entity: One Man Company* (1925) 13 Cal.L.Rev. 235, 237.)

(6) There is no litmus test to determine when the corporate veil will be pierced; rather the result will depend on the circumstances of each particular case. There are, nevertheless, two general requirements: "(1) that there be such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist and (2) that, if the acts are treated as those of the corpora-

tion alone, an inequitable result will follow.” (*Automotriz etc. de California v. Resnick* (1957) 47 Cal.2d 792, 796 [306 P.2d 1, 63 A.L.R.2d 1042].) And “only a difference in wording is used in stating the same concept where the entity sought to be held liable is another corporation instead of an individual.” (*McLoughlin v. L. Bloom Sons Co., Inc.* (1962) 206 Cal.App.2d 848, 851 [24 Cal.Rptr. 311].)

(5b) However - and this is where the court in *Fuls* went astray - when a court disregards the corporate entity, it does not dissolve the corporation. “It is often said that the court will disregard the 'fiction' of the corporate entity, or will 'pierce the corporate veil.' Some writers have criticized this statement, contending that the corporate entity is not a fiction, and that the doctrine merely limits the exercise of the corporate privilege to prevent its abuse.” (6 Witkin, *op. cit. supra*, § 5, at p. 4317; see, e.g., Comment, *supra*, 13 Cal.L.Rev. at p. 237.)

In *Kohn v. Kohn* (1950) 95 Cal.App.2d 708 [214 P.2d 71], a marriage dissolution case, the question was whether the husband's corporation was the alter ego of the husband so that its income should have been included in the determination of his liability. The court explained the alter ego doctrine: “The issue is not so much whether, for all purposes, the corporation is the 'alter ego' of its stockholders or officers, nor whether the very purpose *301 of the organization of the corporation was to defraud the individual who is now in court complaining, as it is an issue of whether in the particular case presented and for the purposes of such case justice and equity can best be accomplished and fraud and unfairness defeated by a disregard of the distinct entity of the corporate form.” (*Id.* at p. 718.) “In the instant case there may well have been various business reasons sufficient to justify and support the formation or continuation of the corporation on the part of defendant. For such purposes the [corporation] still stands.” (*Id.*, at p. 719.) However, to the extent the purpose of the corporation was to fraudulently deprive the wife of a fair property settlement, the corporate entity would be

disregarded: “The law of this state is that the separate corporate entity will not be honored where to do so would be to defeat the rights and equities of third persons.” (*Id.*, at p. 720; see also *McLoughlin v. L. Bloom Sons Co., Inc.*, *supra*, 206 Cal.App.2d 848, 854 [bypassing the corporate entity to reach an alter ego corporation for the sole purpose of avoiding an injustice, otherwise the corporations remain separate].)

(7) The essence of the alter ego doctrine is that justice be done. “What the formula comes down to, once shorn of verbiage about control, instrumentality, agency, and corporate entity, is that liability is imposed to reach an equitable result.” (Latty, *Subsidiaries and Affiliated Corporations* (1936) p. 191.) Thus the corporate form will be disregarded only in narrowly defined circumstances and only when the ends of justice so require.

To apply the alter ego theory as the federal district court did in *Fuls* misinterprets the doctrine and ignores the policies behind it. It is not that a corporation will be held liable for the acts of another corporation because there is really only one corporation. Rather, it is that under certain circumstances a hole will be drilled in the wall of limited liability erected by the corporate form; for all purposes other than that for which the hole was drilled, the wall still stands. When it is claimed that a parent corporation should be liable because it is the alter ego of its subsidiary, equity commands that the corporate wall be breached. Yet the wall remains: the parent is liable through the acts of the subsidiary, but as a separate entity. A judgment obtained against a corporation and its alter ego is enforceable against both separately. Thus, when the plaintiff settles with only the subsidiary, the parent's liability continues. To hold otherwise would be to defeat the policy of promoting justice that lies behind the alter ego doctrine.

Nevertheless the alter ego corporation would be dismissed together with the subsidiary under the common law release rule, unless section 877 applies. Defendant maintains that this section is ap-

plicable only to joint tortfeasors and cannot control when alter ego is alleged as the basis for the non-settlor's liability. The point is untenable. In 1982 the Legislature amended *302 the contribution statute, changing its title to "Contribution Among Joint Judgment Debtors" and dividing it into two chapters. The first chapter, consisting of sections 875 to 880, retains the old denomination, "Releases From and Contribution Among Joint Tortfeasors." The sections remain unchanged. The second chapter, consisting of sections 881 to 883, is entitled "Contribution Among Other Judgment Debtors." It has been argued that section 877 covers only joint tortfeasors, while the fate of parties other than joint tortfeasors must be determined by chapter 2. (*Mayhugh v. County of Orange* (1983) 141 Cal.App.3d 763, 774 [190 Cal.Rptr. 537] (dis. opn. of McDaniel, J.).)

The short answer to this argument is that chapter 2 deals only with judgment debtors and their rights to obtain contribution from other tortfeasors, and thus is not applicable to cases involving prejudgment settlements.^{FN4} (8) More to the point, the language of section 877 is significant - its drafters did not use the narrow term "joint tortfeasors," they used the broad term "tortfeasors claimed to be liable for the same tort." This language was meant to eliminate the distinction between joint tortfeasors and concurrent or successive tortfeasors (4 Witkin, Summary of Cal. Law (8th ed. 1974) Torts, § 39, p. 2338), and to permit broad application of the statute. (*City of Sacramento v. Gemsch Investment Co.* (1981) 115 Cal.App.3d 869, 877 [171 Cal.Rptr. 764]; *Ritter v. Technicolor Corp.* (1972) 27 Cal.App.3d 152, 154 [103 Cal.Rptr. 686].) Further, another section in chapter 1 expressly extends beyond application to joint tortfeasors: section 876, subdivision (b), applies to "one or more persons ... liable solely for the tort of one of them or of another, as in the case of the liability of a master for the tort of his servant."

FN4 While the settlement in this case occurred after the court granted summary

judgment, an appeal was pending. Also, the named defendants were not "judgment debtors," as judgment had been rendered in their favor.

(9) Analogous to the issue before us is the question whether a principal alleged to be vicariously liable in tort for the acts of its agent is subject to suit following settlement with the agent. The principal is held vicariously liable not because it was necessarily at fault, but because justice requires that the enterprise be responsible for the risks of conducting its business. (*Hinman v. Westinghouse Elec. Co.* (1970) 2 Cal.3d 956, 959-960 [88 Cal.Rptr. 188, 471 P.2d 988]; *Rodgers v. Kemper Const. Co.* (1975) 50 Cal.App.3d 608, 618 [124 Cal.Rptr. 143].) Similarly, the parent corporation is liable for the acts of its subsidiary under the alter ego doctrine because justice requires that the corporate wall be breached. "Although the subsidiary may not be an agent in any true sense, the justification for a parent's or affiliate's liability is analogous to the justification of the liability *303 of a principal for acts of a general agent. The principal himself may have done nothing to mislead the third party, but may still be bound by a contract made by the agent within the general scope of his authority Although a parent or affiliate corporation has done nothing affirmative to prejudice the third party, it may similarly be just to hold it liable, but only if the creditor can show the kind of hardship which seems to be assumed as a matter of law in the general-agency situation. ... An involuntary creditor who has had foisted upon him a subsidiary unable to respond in damages has a greater equity." (Note, *Liability of a Corporation for Acts of a Subsidiary or Affiliate* (1958) 71 Harv.L.Rev. 1122, 1130.)

(10) The rule is clear in California that section 877 applies to principal-agent liability. In *Ritter v. Technicolor Corp.*, *supra*, 27 Cal.App.3d 152, the plaintiff sued the defendant film distribution corporation, another corporation, and two agents of the latter. The plaintiff and all but the defendant entered a settlement and release, and the latter then

sought a dismissal with prejudice. Proclaiming that the wording of the statute was broad enough to apply to situations involving parties that could not be considered "true" joint tortfeasors, the court found "inescapable the conclusion that under section 877, the liability of a principal for the tortious acts of his agent, even though wholly vicarious, survives the release of the agent." (*Id.* at p. 154.) In *Mayhugh v. County of Orange*, *supra*, 141 Cal.App.3d 763, 766, the Court of Appeal reaffirmed *Ritter*. It emphasized that the Legislature, while enacting section 877.6 in 1980, did not modify or overturn *Ritter*. (*Ibid.*) (11) Since the Legislature is presumed to be aware of existing judicial decisions (*Estate of McDill* (1975) 14 Cal.3d 831, 839 [122 Cal.Rptr. 754, 537 P.2d 874]), we can presume that it acquiesced in the application of section 877 to parties alleged to be vicariously liable.^{FN5}

FN5 Most states with legislation similar to section 877 hold that release of an agent does not preclude suit against the principal. (See, e.g., *Harris v. Aluminum Co. of America* (W.D.Va. 1982) 550 F.Supp. 1024, 1030; *Alaska Airlines, Inc. v. Sweat* (Alaska 1977) 568 P.2d 916, 929-930; *Holve v. Draper* (1973) 95 Idaho 193, 196-197 [505 P.2d 1265]; *Smith v. Raparot* (1967) 101 R.I. 565, 567-568 [225 A.2d 666].) However, there is opposing authority. (See, e.g., *Craven v. Lawson* (Tenn. 1976) 534 S.W.2d 653, 656; see also Annot., Release of, or Covenant not to Sue, One Primarily Liable for Tort, but Expressly Reserving Rights Against One Secondarily Liable, as Bar to Recovery Against Latter (1983) 24 A.L.R.4th 547.)

It has been argued that because liability of the principal is wholly dependent on liability of the agent, dismissal of the agent removes the basis of the principal's responsibility. (*Mayhugh v. County of Orange*, *supra*, 141 Cal.App.3d 763, 770 (dis. opn. by McDaniel, J.)) However, it does not follow that because *judgment* in favor of the agent exoner-

ates the principal (*Will v. Southern Pacific Co.* (1941) 18 Cal.2d 468, 472-473 [116 P.2d 44]), release of the agent has the same effect. A judgment in favor of the *304 agent means that under our system of law the plaintiff should not recover under the circumstances presented. A settlement has no such implication; it means simply that the parties have agreed to resolve their problems outside the courtroom. Thus liability of the principal - or parent corporation in the alter ego situation - has not been disproved. (See *Sampay v. Morton Salt Co.* (La. 1981) 395 So.2d 326, 328 [24 A.L.R.4th 541] ["Although the employer and employee are not joint tortfeasors, they are nonetheless each obligated for the same thing - total reparation of the damages to the victim. The derivative nature of the employer's liability is of no concern to the victim, and he can compel either the employer or the employee to compensate him for the whole of his damages".]) The liability of the principal (or parent) is not affected by the route the agent (or subsidiary) chooses to take in disposing of the action.

(12) An examination of the various policies underlying the contribution legislation further supports the rule that release of the subsidiary does not release its alter ego. In *Sears, Roebuck & Co. v. International Harvester Co.* (1978) 82 Cal.App.3d 492, 496 [147 Cal.Rptr. 262], the court recognized three interests at work in section 877: "First ... is maximization of recovery to the injured party for the amount of his injury to the extent fault of others has contributed to it. ... Second is encouragement of settlement of the injured party's claim. ... Third is the equitable apportionment of liability among the tortfeasors."

The statute must be interpreted to allow the plaintiff full recovery to the extent that others are responsible for his injuries. (See *Thornton v. Luce* (1962) 209 Cal.App.2d 542, 552 [26 Cal.Rptr. 393].) This policy would be violated if a corporation alleged to be liable as the alter ego of its subsidiary were to be dismissed because the subsidiary has settled with the plaintiff, especially if the

plaintiff has accepted a modest settlement because the subsidiary is undercapitalized. The court held, in *Mayhugh v. County of Orange*, *supra*, 141 Cal.App.3d 763, 766: “[Sections 877 and 877.6] were designed to clarify the liability of tortfeasors and to benefit the negligently injured plaintiff. The Legislature could not have intended that a settlement with one defendant which partially compensates the plaintiff for injuries sustained would effectively block the road to complete recovery. Release of the employer after settlement with the employee would accomplish such a road block and frustrate the purposes of the statute.”^{FN6} *305

FN6 See also *American Motorcycle Assn. v. Superior Court*, *supra*, 20 Cal.3d 578, upholding the joint and several liability rule in the face of the adoption of the doctrine of comparative negligence, and proclaiming that “from a realistic standpoint, we think that AMA's suggested abandonment of the joint and several liability rule would work a serious and unwarranted deleterious effect on the practical ability of negligently injured persons to receive adequate compensation for their injuries. One of the principal by-products of the joint and several liability rule is that it frequently permits an injured person to obtain full recovery for his injuries even when one or more of the responsible parties do not have the financial resources to cover their liability.” (*Id.* at p. 590.)

A second goal of the contribution statute is the early and final settlement of claims. A potential problem could arise in vicarious liability situations because the contribution statutes preserve the right of full indemnity. Section 875, subdivision (f), would seem to permit a secondarily liable defendant that has had judgment entered against it to seek indemnification from the primary tortfeasor. This threat of indemnification could keep a primarily liable defendant from settling. This court has not yet addressed the question whether an employer-judg-

ment debtor has a right to obtain indemnification from an employee who has settled with the plaintiff. However, to the extent such a right exists, “In light of the clear legislative expression, ... we must assume that this contingency was foreseen, and that this result was felt desirable.” (*Ritter v. Technicolor Corp.*, *supra*, 27 Cal.App.3d 152, 155.) Moreover, in the alter ego arena, where the corporations involved have comparable control, it is unlikely that the parent will sue the subsidiary for indemnity unless to do so would be in the best interests of both corporations. Finally, it should be noted that in many cases the parent and subsidiary will be represented by the same counsel, as is the situation in the case at bar, or by separate counsel working in close collaboration. Thus the easiest method for avoiding indemnity problems is to include both corporations in the settlement.

The third policy to be vindicated by the contribution legislation is equity among the defendants. Section 877, subdivision (a), provides that the plaintiff's recovery will be reduced by the amount of consideration paid by the settling defendant, not by the proportion of that defendant's liability. If the subsidiary is allowed to settle for a modest share of the plaintiff's liability and this settlement covers the parent as well, the remaining defendants will have a proportionately greater sum to pay. The low settlement, not made in bad faith because, for example, the subsidiary is undercapitalized, may indeed be unfair if the more affluent parent corporation is included in its terms. Since the remaining defendants cannot attack a settlement unless it was made in bad faith, the rule would be inequitable to the non-settlers.

It should be added that allowing the plaintiff to proceed against the nonsettling parent would reflect the parties' intent. When, as here alleged, the terms of settlement and release expressly include only the subsidiary and no other party, the parent should not magically benefit from the agreement. If it could do so, results unfair to plaintiffs might follow: not realizing that the parent would also be part of the

agreement, the plaintiff would base his settlement on the financial capabilities of the only other party to the agreement, the subsidiary. The amount the plaintiff would receive would likely *306 be disproportionately low if the settlement discharged the parent as well as the subsidiary. And as for the protection of the corporations, the solution is simple: both parties could and should participate in the negotiations. In this way, with every party's identity fully disclosed, an agreement fair to all can be reached.

(4b) We hold that when a plaintiff in a tort action sues one party as the alter ego of another, the plaintiff is not barred from proceeding against the former after settlement with its alter ego. In the case at bar the trial court abused its discretion in refusing to allow plaintiff to amend his pleadings for this purpose.

The summary judgment is reversed.

Bird, C. J., Kaus, J., Broussard, J., and Reynoso, J., concurred.

LUCAS, J.

I respectfully dissent. The settlement reached between Wesley Mesler and Bragg Crane Services, Inc. (Bragg Crane) resulting in Mesler's dismissal with prejudice of his action against Bragg Crane must preclude Mesler from continuing against Bragg Management Company (Bragg Management) on an alter ego theory. Using a confusing meld of incompatible and inapplicable principles, the majority concludes that the corporate veil may be pierced, and one entity deemed the "alter ego" of another for purposes of liability, while simultaneously concluding that the same veil remains intact when considering the effects of a settlement.

This inconsistency appears to be engendered in part by my colleagues' extensive reliance on cases involving principal-agent relationships and vicarious liability. However, plaintiff's action here rested on neither theory. Mesler asserted instead that the two corporate Bragg entities were so overlapping

and identical that in the context of this action the corporate veil must be ignored and the two treated as one entity.

Incorporation is specifically utilized to limit liability. When abused, the corporate structure may be ignored, but "The standards for the application of alter ego principles are high, and the imposition of liability notwithstanding the corporate shield is to be exercised reluctantly and cautiously." (1 Fletcher, *Cyclopedia Corporations* (perm. ed. 1983) § 41.10 at p. 397, fn. omitted [hereinafter *Fletcher*].) As an exception to the usual insulation from liability which incorporation provides to its shareholders, care is required before "alter ego" is found applicable.

The majority indulges in frequent analogies to and reliance upon cases involving agency relationships. "The traditional concept of agency refers *307 to a *special legal relationship between separate legal persons* as a result of which the acts of one are attributed to the other with attendant legal consequences." (Blumberg, *The Law of Corporate Groups* (1983) § 1.02.2, at p. 21, fn. omitted, italics added [hereinafter *Blumberg*].) This special relationship and its concomitant rights and liabilities may be statutorily prescribed: "An agent represents his principal for all purposes within the scope of his actual or ostensible authority, and all the rights and liabilities which would accrue to the agent from transactions within such limit, if they had been entered into on his own account, accrue to the principal." (Civ. Code, § 2330.) The principal's vicarious liability for the acts of his agent extends only to the limits of the agency and to acts "committed by such agent in and as part of the transaction of" the business of the agency, but not to any other acts unless authorized or ratified by the principal. (*Id.*, §§ 2338, 2339.)

When liability is imposed based on agency relationships, the *separate* legal identity of two or more defendants is acknowledged, but liability nonetheless is imputed under specified conditions. Normally, under general legal principles, a corporation

is *not* the agent of its shareholders, nor is a corporate subsidiary automatically considered an agent of a parent corporation. (*Blumberg, supra*, § 1.02.2 at pp. 21-22.) When, rather than an agency relationship, alter ego is asserted, the goal is to ignore the identity of the corporation and to withhold the separate recognition to which, *prima facie*, it would otherwise be entitled. The corporate veil is pierced to establish that two facially separate legal entities are in fact one and should be treated as such. In other words, “[u]nder the [alter ego] doctrine, the court merely disregards the corporate entity and holds the individual responsible for his acts knowingly and intentionally done in the name of the corporation. [¶] A corporation may be the alter ego of another corporation and where this occurs the distinct corporate entity will be disregarded and the two corporations will be treated as one.” (*Fletcher, supra*, § 41.10 at pp. 397-398, fns. omitted.)

With this background in mind, I turn to the majority's opinion here. Undoubtedly, a finding that one corporation is alter ego of another for the purpose of a particular action does not mean that the corporate veil will be breached as to all suits or creditors for all purposes. However, the majority utilizes this rule in a unique way: it permits reliance on a finding of alter ego for one part of analyzing a transaction, but adheres to corporate separateness for consideration of the exact *same* transaction. The contradictory pull thus created permeates my colleagues' opinion.

For example, the majority first observes that a finding of alter ego does *not* mean “It is not that a corporation will be held liable for the acts of *308 another corporation because there is really only one corporation.” (*Ante*, p. 301.) This disclaimer however is directly contrary to the generally accepted characterization of the effect of such a finding: “When a case calls for an exception to the entity view, courts usually construct a common identity for the parent and subsidiary corporations, *thereby treating them as one*.” (*Blumberg, supra*, § 1.02.1 at p. 9; see also 1A *Ballantine & Sterling, Cal. Cor-*

poration Laws (4th ed. 1984) § 295, at p. 14-32 [hereinafter *Ballantine*] [courts applying alter ego theory “treat the body of shareholders and the corporation as procedurally synonymous rather than as separate juristic entities”].) In fact, it is because in essence there is functionally but one entity that alter ego is appropriate in a given situation.

The majority opinion then pictures a hole drilled in the “wall of limited liability erected by the corporate form” and concludes that “When it is claimed that a parent corporation should be liable because it is the alter ego of its subsidiary, equity commands that the corporate wall be breached. Yet the wall remains: the parent is liable through the acts of the subsidiary, but as a separate entity.” (*Ante*, p. 301, italics added.) This confuses the separate legal identity of corporation and shareholder and the difference between agency and alter ego relationships. The opinion continues: “A judgment obtained against a corporation and its alter ego is enforceable against both separately. Thus, when the plaintiff settles with only the subsidiary, the parent's liability continues.” (*Ibid.*) There is an unwarranted leap of logic to the conclusion that the parent remains liable which apparently arises out of an assumption of continuing individual legal identity even when liability is based solely on a claim of alter ego identification. Part of the problem may also arise out of my colleagues' reliance on the parent-subsidiary relationship; however, not every alter ego situation arises from corporate connections and the rule established here will affect individual shareholders as well.

Bragg Management's status as the *parent* of Bragg Crane is insignificant once alter ego principles apply. The parent-subsidiary relationship *per se* is irrelevant except to the extent it bears on the original determination of whether alter ego is appropriate. If, as Mesler asserts, the two corporations are alter egos, they should be treated as one single entity. Once this is understood, it becomes difficult to understand how the majority can hold that the settlement here does not bar further action against

Bragg Management. If an action is settled with John Doe, the plaintiff cannot proceed against him as J. Doe for further and separate damages. Nonetheless, that is precisely the effect of the majority's reasoning here.

The United States District Court in *Fuls v. Shastina Properties, Inc.* (N.D.Cal. 1978) 448 F.Supp. 983, clearly understood that an alter ego *309 finding must be consistently applied. As it explained, "Where the alter ego doctrine applies, ... the two corporations are treated as one for purposes of determining liability. It follows that where the one corporation is released from liability, so too is the other." (P. 989.) This state of affairs arises, of course, because under the alter ego theory urged by Mesler, Bragg Management can only be liable if Bragg Crane is liable but only because the two entities are viewed as indivisible. (See *M/V American Queen v. San Diego Marine Const.* (9th Cir. 1983) 708 F.2d 1483, 1490.)

If Mesler had first sued Bragg Crane, settled and judgment had thereupon been entered in Bragg Crane's favor, Mesler would have been estopped from proceeding further against Bragg Management except to the extent that it might have sought to collect from it any unsatisfied portion of the judgment. Plaintiffs often move postjudgment to amend a judgment in their favor to add a previously unnamed person or entity as a defendant on the ground that it or he is the alter ego of an originally denominated defendant. (See *Alexander v. Abbey of the Chimes* (1980) 104 Cal.App.3d 39, 44-46 [163 Cal.Rptr. 377]; Code Civ. Proc., § 187.) However, such amendment is not permitted in the absence of a showing of due diligence on the part of the plaintiff, and of participation in the defense of the underlying action by the claimed alter ego. (*Minton v. Cavaney* (1961) 56 Cal.2d 576, 581 [15 Cal.Rptr. 641, 364 P.2d 473]; *Alexander, supra*, at pp. 47-48; *Ballantine, supra* § 299.04 at pp. 14.45-14.46 [factors considered in permitting amendment of judgment to include new defendant].) Such restrictions are necessary to protect the

newly named entity's constitutional rights. (See *Motores de Mexicali v. Superior Court* (1958) 51 Cal.2d 172, 176 [331 P.2d 1].)

The postjudgment use of alter ego doctrine can serve only to obtain collection based on already established liability. Moreover, its availability serves to counter the majority's claims about unsuspecting plaintiffs improvidently settling with an apparently "undercapitalized" corporation. A plaintiff may settle for full value and seek to collect not only from that corporation but also from any alter ego. Plaintiffs must, as noted, exercise due diligence but this encourages careful and timely investigation of claims and possible defendants. A plaintiff may also expressly reserve the right to seek further recovery from an alter ego when the question of the relationship between defendants remains unsettled. (See, e.g., *Meyer v. Stern* (D.Colo. 1984) 599 F.Supp. 295, 298.) A plaintiff thus may settle and obtain speedy recovery without foreclosing his options as to other potential sources of recovery.

Plaintiff here did not expressly reserve any rights in his settlement. Instead, Mesler's claim against Bragg Management was based on the assertion *310 that it was in fact the alter ego (not the parent or shareholder or superior or principal) of Bragg Crane, and the corporate walls dividing the two entities therefore were illusory. Mesler obviously knew long before his settlement with Bragg Crane of the existence and purported synonymy of Bragg Management, and in fact his motion to amend to add Bragg Management as an alter ego was the original subject of this appeal. It was only during the pendency of the appeal that Mesler settled with Bragg Crane, who, he had been alleging, was the *same* entity as Bragg Management. It is in this context that Mesler's invocation of Code of Civil Procedure section 877 must be rejected.

Section 877 provides in relevant part that where a release, dismissal or covenant not to sue is given to one defendant, "It shall not discharge any *other* tortfeasor from liability unless its terms so provide" (Italics added.) It does not apply here

because, under the theory of liability urged by Mesler, Bragg Management is not *another* tortfeasor but rather it is merely the alias of the tortfeasor with whom Mesler has already reached agreement. The analysis of section 877 by the majority is simply irrelevant.

The basic harm in the majority opinion is the potential erosion it may cause in the concept of limited liability created by use of the corporate form. Incorporation creates defined legal obligations and relationships between corporation and shareholder (corporate or individual). These relationships are distinct from those created in an agency or vicarious liability situation. The majority unfortunately blurs the line.

In summary, my colleagues may well have put the lie to Shakespeare's maxim:

“What's in a name: That which we call a rose

By any other name would smell as sweet.”

(Romeo and Juliet, Act II, sc. 2.)

I would dismiss the appeal as moot.

Grodin, J., concurred. *311

Cal.

Mesler v. Bragg Management Co.

39 Cal.3d 290, 702 P.2d 601, 216 Cal.Rptr. 443

END OF DOCUMENT



Supreme Court of California
BETTY JEAN MYERS, Plaintiff and Appellant,
v.
PHILIP MORRIS COMPANIES, INC., et al., De-
fendants and Respondents.

No. S095213.
Aug. 5, 2002.

SUMMARY

A smoker filed a products liability action against tobacco manufacturers after she was diagnosed with lung cancer allegedly caused by exposure to tobacco. After the case was removed to federal court, the United States District Court for the Eastern District of California granted defendants' motion to dismiss, on the ground that Civ. Code, § 1714.45, barred plaintiff's actions for any injuries incurred prior to January 1998. The first version of § 1714.45 (the immunity statute) granted tobacco companies complete immunity in certain product liability lawsuits effective Jan. 1, 1988. The second version (the repeal statute) rescinded that immunity 10 years later effective Jan. 1, 1998. Plaintiff appealed, and the United States Court of Appeals for the Ninth Circuit, No. 99-17383, certified a question to the California Supreme Court, asking whether the repeal statute governs a claim that accrued after Jan. 1, 1998, but which is based on conduct that occurred prior to Jan. 1, 1998.

The Supreme Court held that the immunity statute applied to statutorily described conduct that occurred during the 10-year immunity period, which began Jan. 1, 1988 and ended Dec. 31, 1997. No products liability cause of action could be based on that conduct, regardless of when plaintiff may have sustained or discovered injuries as a result of that conduct. That statutory immunity was rescinded, however, when the Legislature enacted the repeal statute, which as of Jan. 1, 1998, restored the general tort principles that had previously governed

the tort liability of tobacco companies. Thus, as to conduct falling before and after the 10-year immunity period, the tobacco companies were not shielded from the lawsuit. Application of the repeal statute to defendants for conduct during the immunity period would have been a retroactive application, subjecting them to liability for past conduct that was lawful during the immunity period. Such retroactive application was impermissible since the repeal statute had no express retroactive language, and extrinsic sources provided no clear indication of legislative intent to apply the statute retroactively. (Opinion by Kennard, J., with George, C. J., Baxter, Werdegar, Chin, and Brown, JJ., concurring. Dissenting opinion by Moreno, J. (see p. 848).)

HEADNOTES

Classified to California Digest of Official Reports (1a, 1b, 1c, 1d) Products Liability § 40--Strict Liability in Tort--Defenses--Statutory Immunity--Tobacco Products--Repeal of Immunity-- Liability of Tobacco Manufacturers for Conduct Falling Outside Immunity Period.

A products liability action by a smoker against tobacco manufacturers, arising from lung cancer caused by exposure to tobacco, was barred by the first version of Civ. Code, § 1714.45, granting complete immunity to tobacco companies in certain products liability actions, as to statutorily described conduct that occurred in the 10-year period in which the statute was in effect (Jan. 1, 1988, through Dec. 31, 1997). No products liability cause of action could be based on conduct that occurred during that period regardless of when plaintiff may have sustained or discovered injuries as a result of the conduct. The statutory immunity was rescinded, however, when the Legislature enacted a second version of Civ. Code, § 1714.45 (the repeal statute), which, as of Jan. 1, 1998, restored general tort principles that had previously governed the tort liability of tobacco companies. Thus, as to conduct falling before and after the 10-year immunity period, the

(Cite as: 28 Cal.4th 828)

tobacco companies were not shielded from the lawsuit. Application of the repeal statute to defendants for conduct during the immunity period would have been a retroactive application, subjecting them to liability for past conduct that was lawful during the immunity period. Such retroactive application was impermissible since the repeal statute had no express retroactive language, and extrinsic sources provided no clear indication of legislative intent to apply the statute retroactively. Constitutional considerations also reinforced construction of the repeal statute as prospective only.

[See 6 Witkin, Summary of Cal. Law (9th ed. 1988) Torts, § 1312; West's Key Number Digest, Products Liability ¶ 2.]

(2) Statutes § 5--Operation and Effect--Retroactive Law--What Constitutes.

A retroactive or retrospective law is one that affects rights, obligations, acts, transactions, and conditions that are performed or exist prior to the adoption of the statute. Every statute that takes away or impairs vested rights acquired under existing laws or creates a new obligation, imposes a new duty, or attaches a new disability, with respect to transactions or considerations already past, must be deemed retrospective. A statute that operates to increase a party's liability for past conduct is retroactive.

(3) Statutes § 5--Operation and Effect--Presumption of Prospective Application--Requirements for Retroactive Application.

Generally, statutes operate prospectively only. A retroactive application of a statute requires either express language or clear and unavoidable implication from the California Legislature. A retrospective operation will not be given to a statute that interferes with antecedent rights unless that is the unequivocal and inflexible import of the terms and the manifest intention of the Legislature. The presumption that legislation operates prospectively rather than retroactively is rooted in constitutional principles, and the antiretroactivity principle finds expression in several provisions of the Constitution, including the ex post facto clause, the takings

clause, and the due process clause. California courts apply the same general prospectivity principle as the United States Supreme Court. Under this formulation, a statute's retroactivity is, in the first instance, a policy determination for the Legislature and one to which the courts defer absent some constitutional objection to retroactivity. But a statute that is ambiguous with respect to retroactive application is construed to be unambiguously prospective.

(4) Statutes § 42--Construction--Aids--Comments by Bill's Author.

Courts decline to discern legislative intent from comments by a bill's author because they reflect only the views of a single legislator instead of those of the Legislature as a whole.

COUNSEL

Bourdette & Partners, Philip C. Bourdette and André P. Gaston for Plaintiff and Appellant.

Wartnick, Chaber, Harowitz & Tigerman, Harry F. Wartnick, Madelyn J. Chaber; Law Offices of Daniel U. Smith, Daniel U. Smith and Ted W. Pelletier for Patricia Henley, Leslie Whiteley and Leonard Whiteley as Amici Curiae on behalf of Plaintiff and Appellant.

Bill Lockyer, Attorney General, Richard M. Frank, Chief Assistant Attorney General, Dennis Eckhart, Assistant Attorney General, and Peter M. Williams, Deputy Attorney General, as Amici Curiae on behalf of Plaintiff and Appellant. *831

Howard, Rice, Nemerovski, Canady, Falk & Rabkin and H. Joseph Escher III for Defendant and Respondent R.J. Reynolds Tobacco Company.

Munger, Tolles & Olson, Michael R. Doyen, Fred A. Rowley, Jr., Daniel P. Collins and Ronald L. Olsen for Defendant and Respondent Philip Morris Incorporated.

Sedgwick, Detert, Moran & Arnold and Frederick D. Baker for Defendant and Respondent Brown &

Williamson Tobacco Corporation.

William L. Gausewitz for The Alliance of American Insurers, The American Insurance Association, The National Association of Independent Insurers, The National Association of Mutual Insurance Companies and The Reinsurance Association of America as Amici Curiae on behalf of Defendants and Respondents.

Fred Main for California Chamber of Commerce as Amicus Curiae on behalf of Defendants and Respondents.

KENNARD, J.

In 1995, the California Legislature found that “[t]obacco-related disease places a tremendous financial burden upon the persons with the disease, their families, the health care delivery system, and society as a whole,” and that “California spends five billion six hundred million dollars (\$5,600,000,000) a year in direct and indirect costs on smoking-related illnesses.” (Health & Saf. Code, § 104350, subd. (a)(7).) To obtain compensation for the physical and mental suffering and staggering expenses inflicted by tobacco-related illness, users of tobacco products and their families have sought relief in our courts through product liability lawsuits against manufacturers and sellers of tobacco products. In dealing with those lawsuits, courts have not been free to apply ordinary principles of tort law because, as we shall explain, the Legislature has enacted statutes that directly control the extent to which our courts may award damages against tobacco companies in product liability actions.

The statutes at issue are two successive versions of section 1714.45 of California's Civil Code.

^{FN1} The first version, which we here sometimes refer to as the Immunity Statute, granted tobacco companies complete immunity in *832 certain product liability lawsuits as of January 1, 1988.

^{FN2} (Added by Stats. 1987, ch. 1498, § 3, p. 5778.)

The second version, which we here sometimes refer

to as the Repeal Statute, rescinded that immunity 10 years later on January 1, 1998. (Stats. 1997, ch. 570, § 1.) The United States Court of Appeals for the Ninth Circuit has certified to us a question asking whether the Repeal Statute governs “a claim that accrued after January 1, 1998, but which is based on conduct that occurred prior to January 1, 1998.” (*Myers v. Philip Morris Companies, Inc.* (9th Cir. 2001) 239 F.3d 1029, 1030 (*Myers*).)

FN1 Further undesignated statutory references are to the Civil Code.

FN2 As this court has done in prior cases discussing this legislation, we use the term “immunity” rather loosely, without restricting it to its narrowest technical meaning, that is, “a complete defense ... [that] does not negate the tort.” (Black's Law Dict. (1996 pocket ed.) p. 298; see also *Delaney v. Superior Court* (1990) 50 Cal.3d 785, 797, fn. 6 [268 Cal.Rptr. 753, 789 P.2d 934] [discussing the “immunity-privilege distinction”].)

Our answer is this: The Immunity Statute applies to certain statutorily described conduct of tobacco companies that occurred *during* the 10-year immunity period, which began on January 1, 1988, and ended on December 31, 1997. With respect to such conduct, therefore, the statutory immunity applies, and no product liability cause of action may be based on that conduct, regardless of when the users of the tobacco products may have sustained or discovered injuries as a result of that conduct. That statutory immunity was rescinded, however, when the California Legislature enacted the Repeal Statute, which as of January 1, 1998, restored the general principles of tort law that had, until the 1988 enactment of the Immunity Statute, governed tort liability against tobacco companies. Therefore, with respect to conduct falling *outside* the 10-year immunity period, the tobacco companies are not shielded from product liability lawsuits.

I. Facts

(Cite as: 28 Cal.4th 828)

The Court of Appeals for the Ninth Circuit described the background of this case as follows: “Betty Jean Myers began smoking cigarettes in 1956 and continued to smoke heavily until 1997. Throughout this period, and until August of 1998, she also worked and lived in environments in which those around her smoked cigarettes. On April 8, 1998, Myers was diagnosed with lung cancer allegedly caused by her exposure to tobacco. On March 4, 1999, Myers filed a complaint in Tulare County Superior Court against Philip Morris and other defendant tobacco manufacturers (collectively, the ‘Tobacco Manufacturers’) alleging several claims, including strict liability, negligence, breach of implied warranties, fraud, and negligent misrepresentation.” (*Myers, supra*, 239 F.3d at p. 1030.)

The Ninth Circuit's description continues: “After removing this case to the United States District Court for the Eastern District of California, the *833 Tobacco Manufacturers moved, on April 13, 1999, to dismiss Myers's complaint for failure to state a claim. On May 25, 1999, the district court granted the motion to dismiss, with leave to amend, on the ground that Cal. Civ. Code § 1714.45 barred Myers's actions for any injuries incurred prior to January 1998. On June 30, 1999, Myers amended her complaint to allege that she was exposed to secondhand cigarette smoke between January 1, 1998 and April 8, 1998. On July 19, 1999, the Tobacco Manufacturers again moved to dismiss Myers's complaint for failure to state a claim. On October 6, 1999, the district court again dismissed Myers's complaint for failure to state [a] claim, this time without leave to amend, on the grounds that she had conceded that her lung cancer was not caused by her exposure to secondhand smoke after January 1, 1998, and, again, that pre-1998 exposures were not actionable. Myers filed a timely notice of appeal to the Ninth Circuit.” (*Myers, supra*, 239 F.3d at p. 1031.)

II. Background

We start with a review of the Immunity Statute

and two California cases that have construed that statute, *American Tobacco Co. v. Superior Court* (1989) 208 Cal.App.3d 480 [255 Cal.Rptr. 280], a decision of the state Court of Appeal, and *Richards v. Owens-Illinois, Inc.* (1997) 14 Cal.4th 985 [60 Cal.Rptr.2d 103, 928 P.2d 1181], a decision of this court.

A. The Immunity Statute

Enacted as part of the Willie L. Brown, Jr.-Bill Lockyer Civil Liability Reform Act of 1987, former section 1714.45 (the Immunity Statute) provided in full:

“(a) In a product liability action, a manufacturer or seller shall *not* be liable if:

“(1) The product is inherently unsafe and the product is known to be unsafe by the ordinary consumer who consumes the product with the ordinary knowledge common to the community; and

“(2) The product is a common consumer product intended for personal consumption, such as sugar, castor oil, alcohol, *tobacco*, and butter, as identified in comment *i* to Section 402A of the Restatement (Second) of Torts.

“(b) For purposes of this section, the term ‘product liability action’ means any action for injury or death caused by a product, except that the term does *834 not include an action based on a manufacturing defect or breach of an express warranty.

“(c) This section is intended to be declarative of and does not alter or amend existing California law, including *Cronin v. J.B.E. Olson Corp.*, (1972) 8 Cal. 3d 121 [104 Cal. Rptr. 433, 501 P.2d 1153], and shall apply to all product liability actions pending on, or commenced after, January 1, 1988.” (Stats. 1987, ch. 1498, § 3, pp. 5778-5779, italics added.)

We now discuss the two California decisions that have interpreted the Immunity Statute.

1. *American Tobacco Co. v. Superior Court*

The state Court of Appeal's 1989 decision in *American Tobacco Co. v. Superior Court*, *supra*, 208 Cal.App.3d 480 (*American Tobacco*), which was authored by Presiding Justice J. Anthony Kline, was the first to construe the Immunity Statute. In that case, the court described the Immunity Statute as the result of a " 'peace pact' " or "compromise between parties seeking and opposing comprehensive changes in California tort law who had been locked in a long political struggle that had reached [a] stalemate." (*American Tobacco, supra*, at pp. 486-487.) Those involved included major special interest groups such as insurers, physicians, manufacturers, and the plaintiff's lawyers. (*Id.* at p. 486.)^{FN3} The Court of Appeal in *American Tobacco* characterized the Immunity Statute as so "poorly drafted" that "on its face [, it was] amenable to two diametrically opposed interpretations, each of which conflict[ed] in some way with the words" used by the Legislature. (*American Tobacco, supra*, at p. 485.) But legislative history, the court noted, indicated that the Immunity Statute's intent was to ensure that " 'high-cholesterol foods, alcohol, and cigarettes that are *inherently unsafe and known to be unsafe by ordinary consumers*, [were] not to be subject to product liability lawsuits.' " (*American Tobacco, supra*, at p. 487, italics added.) In light of that legislative intent, the Court of Appeal in *American Tobacco* concluded that the statutory immunity was very broad, providing "nearly complete" immunity for manufacturers and sellers of tobacco and the other enumerated products. (*Ibid.*) *835

FN3 The compromise agreement reportedly is known as "the 'napkin deal' since it was hammered out by political adversaries"—(one side "wanting comprehensive changes in California tort law, the other wanting to maintain the status quo")—on a white cloth napkin in a Sacramento restaurant. (Moy, *Tobacco Companies, Immune No More-California's Removal of the Legal Barriers Preventing Plaintiffs From Recovering for Tobacco-related Illness*

(1998) 29 McGeorge L.Rev. 761, 770.)

2. *Richards v. Owens-Illinois, Inc.*

In 1997, some eight years after the Court of Appeal's decision in *American Tobacco, supra*, 208 Cal.App.3d 480, we construed the Immunity Statute in *Richards v. Owens-Illinois, Inc., supra*, 14 Cal.4th 985 (*Richards*). Because *Richards* is central to answering the question the Ninth Circuit has certified to us, we discuss it in some detail.

The plaintiff in *Richards, supra*, 14 Cal.4th 985, was a former shipyard worker who sued several asbestos manufacturers, claiming that his exposure to asbestos fibers at various shipyard jobs had caused him to develop asbestosis, a severe respiratory injury. At trial, one asbestos manufacturer, defendant Owens-Illinois, Inc., presented evidence that the plaintiff had contributed to the development of his respiratory injury by smoking for more than 40 years. (*Id.* at p. 990.) The issue before this court was whether the trial court should have allowed Owens-Illinois to present its so-called tobacco company defense, which would have required the jury, in determining fault with respect to noneconomic damages (to compensate the plaintiff for pain and suffering), to apportion to tobacco companies some percentage of fault, thereby reducing the percentage of the noneconomic damages award attributable to Owens-Illinois. (*Id.* at p. 991.)

To decide this question, we considered the interplay between the Immunity Statute and section 1431 et seq., enacted by the California electorate in an initiative known as Proposition 51. Proposition 51 provided in part that "in a tort action governed by principles of comparative fault, a defendant shall not be jointly liable for the plaintiff's 'noneconomic damages,' but shall only be severally liable for such damages 'in direct proportion to that defendant's percentage of fault.' " (*Richards, supra*, 14 Cal.4th at p. 988, quoting § 1431.2, subd. (a).) The specific question we addressed in *Richards* was this: "To the extent [the Immunity Statute] protects tobacco companies from direct 'liab[ility]' for harm caused by smoking, does it also preclude the alloca-

tion of proportionate 'fault' to absent tobacco companies in a smoker's suit for asbestos-related lung injury, in order to reduce the 'non-economic' damages payable by the asbestos defendant under Proposition 51?" (*Richards, supra*, 14 Cal.4th at p. 988.)

We explained: "Though the [Immunity Statute] states only an exemption from direct 'liab[ility]' where specified conditions are met, the *express premise* which justifies this immunity is of a *broad-er nature*. This premise is that suppliers of certain products which are 'inherently unsafe,' but which the public wishes to have available despite awareness of their dangers, *should not be responsible in tort* for resulting harm to those who voluntarily *836 consumed the products despite such knowledge. With respect to injuries meeting the statute's requirements, that principle precludes the assignment of legal 'fault' to such suppliers *in all contexts*, including suits from which they are absent by law." (*Richards, supra*, 14 Cal.4th at p. 1002, italics added, original italics omitted.)

We pointed out that the Immunity Statute drew "its express inspiration from product liability principles" set forth in comment *i* to section 402A of the Restatement Second of Torts (Restatement), and these principles provided the premise for the statute. (*Richards, supra*, 14 Cal.4th at p. 999.)

We observed: "Section 402A of the Restatement proposes generally that when a manufacturer or distributor sells a product 'in a defective condition *unreasonably dangerous* to the user or consumer' ([Rest.] p. 347, italics added), and the product reaches that person, as expected and intended, without substantial change in its condition, the seller is 'subject to liability' for physical harm 'thereby caused to the ultimate user or consumer.' [¶] However, comment *i* asserts an important qualification of the general rule [It] makes clear that ... '[t]he rule [of liability] applies *only* where the defective condition of the product makes it *unreasonably dangerous* to the user or consumer.' (Restatement, p. 352, italics added.) As comment *i*

then explains, '[m]any products cannot possibly be made entirely safe for all consumption,' but if a product is pure and unadulterated, its *inherent or unavoidable danger*, commonly known to the community which consumes it anyway, does not expose the seller to liability for resulting harm to a voluntary user." (*Richards, supra*, 14 Cal.4th at p. 999.)

Richards added: "The clear premise of comment *i* is that no 'liability' arises [for the manufacture or distribution of a product that in its pure and unadulterated form poses for its voluntary users an inherent and unavoidable danger] because *there is no sound basis for liability*. In other words, comment *i* posits, a manufacturer or seller *breaches no legal duty* to voluntary consumers by merely supplying, in unadulterated form, a common commodity which cannot be made safer, but which the public desires to buy and ingest despite general understanding of its inherent dangers." (*Richards, supra*, 14 Cal.4th at p. 1000.)

Because it would have been "anomalous" for a supplier of tobacco products, "though immunized ... from direct liability for providing an 'inherently unsafe' product to a knowing and voluntary consumer ... [to] nonetheless be assigned 'fault' for doing so in an action between that same consumer and a third party defendant," we held in *Richards* "that to the extent [the Immunity Statute] afford[ed] tobacco suppliers immunity from *837 'liab [ility]' in direct actions against them, on grounds that *the immunized conduct breache[d] no duty and constitute[d] no tort*, the statute also preclude[d] indirect assignment of comparative 'fault' ... to such entities for purposes of Proposition 51." (*Richards, supra*, 14 Cal.4th at pp. 1000-1001, italics added.)

In short, our unanimous decision in *Richards, supra*, 14 Cal.4th 985, made clear that between January 1, 1988, and December 31, 1997, when the Immunity Statute was in effect, supplying pure and unadulterated tobacco products to knowing and voluntary consumers of those products was not subject to tort liability because it *breached no legal duty and thus constituted no tort*.

B. *The Repeal Statute*

Ten years after enactment of the Immunity Statute and some eight months after our decision in *Richards, supra*, 14 Cal.4th 985, the California Legislature enacted the Repeal Statute, which amended former section 1714.45 to rescind the statutory immunity for tobacco companies as of January 1, 1998.^{FN4} When enacted, the Repeal Statute provided, and with one minor change still provides:

FN4 Earlier in the same legislative session, the California Legislature passed, as urgency legislation effective June 12, 1997, Assembly Bill No. 1603 (1997-1998 Reg. Sess.) (hereafter the Public Entity Amendment). That bill amended the Immunity Statute to allow for "an action brought by a public entity to recover the value of benefits provided to individuals injured by a tobacco-related illness caused by the tortious conduct of a tobacco company." (Former § 1714.45, subd. (d), as amended by Stats. 1997, ch. 25, § 2.) A third bill, regarding secondhand smoke (Sen. Bill No. 340 (1997-1998 Reg. Sess.)), was passed by the Legislature but vetoed by the Governor.

"(a) In a product liability action, a manufacturer or seller shall not be liable if both of the following apply:

"(1) The product is inherently unsafe and the product is known to be unsafe by the ordinary consumer who consumes the product with the ordinary knowledge common to the community.

"(2) The product is a common consumer product intended for personal consumption, such as sugar, castor oil, alcohol, and butter, as identified in comment *i* to Section 402A of the Restatement (Second) of Torts.

"(b) *This section does not exempt the manufacture or sale of tobacco products by tobacco manufacturers and their successors in interest from*

product liability actions, but does exempt the sale or distribution of tobacco *838 products by any other person, including, but not limited to, retailers or distributors.

"(c) For purposes of this section, the term 'product liability action' means any action for injury or death caused by a product, except that the term does not include an action based on a manufacturing defect or breach of an express warranty.

"(d) This section is intended to be declarative of and does not alter or amend existing California law, including *Cronin v. J.B.E. Olson Corp.*, (1972), 8 Cal. 3d 121, and shall apply to all product liability actions pending on, or commenced after, January 1, 1988.

"(e) This section does not apply to, and never applied to, an action brought by a public entity to recover the value of benefits provided to individuals injured by a tobacco-related illness caused by the tortious conduct of a tobacco company or its successor in interest, including, but not limited to, an action brought pursuant to Section 14124.71 of the Welfare and Institutions Code. In such an action brought by a public entity, the fact that the injured individual's claim against the defendant may be barred by a prior version of this section shall not be a defense. This subdivision does not constitute a change in, but is declaratory of, existing law relating to tobacco products.

"(f) *It is the intention of the Legislature in enacting the amendments to subdivisions (a) and (b) of this section adopted at the 1997-98 Regular Session to declare that there exists no statutory bar to tobacco-related personal injury, wrongful death, or other tort claims against tobacco manufacturers and their successors in interest by California smokers or others who have suffered or incurred injuries, damages, or costs arising from the promotion, marketing, sale, or consumption of tobacco products.* It is also the intention of the Legislature to clarify that such claims which were or are brought shall be determined on their merits, without

the imposition of any claim of statutory bar or categorical defense.

“(g) This section shall not be construed to grant immunity to a tobacco industry research organization.” (§ 1714.45, as amended by Stats. 1997, ch. 570, § 1, italics added.)^{FN5}

FN5 In 1998, the Legislature made non-substantive changes to the final sentence in subdivision (f) of the Repeal Statute. It now reads: “It is also the intention of the Legislature to clarify that those claims that were or are brought shall be determined on their merits, without the imposition of any claim of statutory bar or categorical defense.” (§ 1714.45, subd. (f), as amended by Stats. 1998, ch. 485, § 38, underscoring indicates changes.)

Through subdivisions (b) and (f), the Repeal Statute expressly rescinded the statutory immunity from product liability lawsuits for tobacco companies *839 that the Legislature had allowed 10 years earlier. Although the Repeal Statute retained the Immunity Statute's reference to comment *i* to section 402A of the Restatement, negating liability to voluntary users of certain common but inherently unsafe consumer products, the Repeal Statute in subdivision (a) omitted tobacco products from specified “inherently unsafe” products.

III. Discussion

(1a) We now turn to the question that the Ninth Circuit has asked us to decide: “Do the amendments to Cal. Civ. Code § 1714.45 that became effective on January 1, 1998, apply to a claim that accrued after January 1, 1998, but which is based on conduct that occurred prior to January 1, 1998?” To answer this question we must determine how the Repeal Statute affects product liability suits against tobacco companies based on their activities as manufacturers and sellers of tobacco products before, during, and after the statutory immunity period.

In certifying the question, the Ninth Circuit

noted plaintiff's contention that applying the Repeal Statute in her case would be a *prospective* rather than a *retroactive* application of that law because she was diagnosed with cancer on April 8, 1998, three months after January 1, 1998, the date on which the Repeal Statute took effect. We address that issue below.

A. Whether Applying the Repeal Statute to Defendant Tobacco Companies' Conduct During the Immunity Period Would Be a Prospective or a Retroactive Application of That Statute

(2) As we said more than 50 years ago, a retroactive or retrospective law “is one which affects rights, obligations, acts, transactions and conditions which are performed or exist prior to the adoption of the statute.” (*Aetna Cas. & Surety Co. v. Ind. Acc. Com.* (1947) 30 Cal.2d 388, 391 [182 P.2d 159]; accord, *Evangelatos v. Superior Court* (1988) 44 Cal.3d 1188, 1206 [246 Cal.Rptr. 629, 753 P.2d 585] (*Evangelatos*.) Similarly, the United States Supreme Court has stated: “[E]very statute, which takes away or impairs vested rights acquired under existing laws, or creates a new obligation, imposes a new duty, or attaches a new disability, in respect to transactions or considerations already past, must be deemed retrospective.” (*Landgraf v. USI Film Products* (1994) 511 U.S. 244, 269 [114 S.Ct. 1483, 1499, 128 L.Ed.2d 229].) Phrased another way, a statute that operates to “increase a party's liability for past conduct” is retroactive. (*Id.* at p. 280 [114 S.Ct. at p. 1505]; *Evangelatos, supra*, 44 Cal.3d at p. 1206.) *840

(1b) As we explained earlier, while the Immunity Statute was in effect—from January 1, 1988, through December 31, 1997—no tortious liability attached to a tobacco company's production and distribution of pure and unadulterated tobacco products to smokers. (Former § 1714.45, as added by Stats. 1987, ch. 1498, § 3, p. 5778; *Richards, supra*, 14 Cal.4th at p. 1001.) But on January 1, 1998, the California Legislature, through its enactment of the Repeal Statute, terminated that statutory immunity. (§ 1714.45.) Here, plaintiff started

(Cite as: 28 Cal.4th 828)

smoking in 1956 and, some 41 years later, quit smoking in 1997. But during 10 of those 41 years, from January 1, 1988, to December 31, 1997, because of the Immunity Statute, the manufacture and sale of covered products were not tortious. Accordingly, to have the Repeal Statute govern product liability suits against tobacco companies for supplying tobacco products to smokers during the immunity period would indeed be a retroactive application of that statute because it could subject those companies to "liability for past conduct" (*Landgraf v. USI Film Products*, *supra*, 511 U.S. at p. 280 [114 S.Ct. at p. 1505]; see also *Evangelatos*, *supra*, 44 Cal.3d at p. 1206) that was lawful during the immunity period (*Richards*, *supra*, 14 Cal.4th at p. 1001). Such retroactive application is impermissible unless there is an express intent of the Legislature to do so. We explore that issue below.

B. Whether the California Legislature Expressed an Intent That the Repeal Statute Govern Tobacco Companies' Liability During the Immunity Period

(3) Generally, statutes operate prospectively only. In the words of section 3 of California's Civil Code: "No part of [this code] is retroactive, unless expressly so declared." (Italics added.) The Ninth Circuit, in certifying the question to us, cited our decision in *Evangelatos*, *supra*, 44 Cal.3d at page 1208, when noting defendant tobacco companies' contention that "a retroactive application [of a statute] requires either 'express language or clear and unavoidable implication' from the California Legislature." (*Myers*, *supra*, 239 F.3d at p. 1032.) On that point, defendants are right. We explained in *Evangelatos*: "'[T]he first rule of [statutory] construction is that legislation must be considered as addressed to the future, not to the past.... The rule has been expressed in varying degrees of strength but always of one import, that a retrospective operation will not be given to a statute which interferes with antecedent rights ... unless such be 'the unequivocal and inflexible import of the terms, and the manifest intention of the legislature.' " (*Evangelatos*, *supra*, 44 Cal.3d at p. 1207, quoting *United States v. Security Industrial Bank* (1982) 459 U.S.

70, 78-79 [103 S.Ct. 407, 412-413, 74 L.Ed.2d 235], italics omitted.) In the words of the United States Supreme Court, "the 'principle that the legal effect of conduct *841 should ordinarily be assessed under the law that existed when the conduct took place has timeless and universal appeal.' " (*Landgraf v. USI Film Products*, *supra*, 511 U.S. at p. 265 [114 S.Ct. at p. 1497]; accord, *Hughes Aircraft Co. v. United States ex rel. Schumer* (1997) 520 U.S. 939, 946 [117 S.Ct. 1871, 1876, 138 L.Ed.2d 135].)

As the United States Supreme Court has consistently stressed, the presumption that legislation operates prospectively rather than retroactively is rooted in constitutional principles: "In a free, dynamic society, creativity in both commercial and artistic endeavors is fostered by a rule of law that gives people confidence about the legal consequences of their actions. [¶] It is therefore not surprising that the antiretroactivity principle finds expression in several provisions of our Constitution. The *Ex Post Facto* Clause flatly prohibits retroactive application of penal legislation.... The Fifth Amendment's Takings Clause[, and] [t]he Due Process Clause also protect[] the interests in fair notice and repose that may be compromised by retroactive legislation; a justification sufficient to validate a statute's *prospective* application under the [Due Process] Clause 'may not suffice' to warrant its *retroactive* application." (*Landgraf v. USI Film Products*, *supra*, 511 U.S. at pp. 265-266 [114 S.Ct. at p. 1497], italics added; accord, *INS v. St. Cyr* (2001) 533 U.S. 289, 316 [121 S.Ct. 2271, 2288, 150 L.Ed.2d 347].)

Just as federal courts apply the time-honored legal presumption that statutes operate prospectively "unless Congress has clearly manifested its intent to the contrary" (*Hughes Aircraft Co. v. United States ex rel. Schumer*, *supra*, 520 U.S. at p. 946 [117 S.Ct. at p. 1876]), so too California courts comply with the legal principle that unless there is an "express retroactivity provision, a statute will not be applied retroactively unless it is *very clear*

from extrinsic sources that the Legislature ... must have intended a retroactive application" (*Evan-gelatos*, *supra*, 44 Cal.3d at p. 1209, italics added). California courts apply the same "general prospective principle" as the United States Supreme Court. (*Id.* at p. 1208.) Under this formulation, a statute's retroactivity is, in the first instance, a policy determination for the Legislature and one to which courts defer absent "some constitutional objection" to retroactivity. (*Western Security Bank v. Superior Court* (1997) 15 Cal.4th 232, 244 [62 Cal.Rptr.2d 243, 933 P.2d 507].) But "a statute that is ambiguous with respect to retroactive application is construed ... to be unambiguously prospective." (*INS v. St. Cyr*, *supra*, 533 U.S. at pp. 320-321, fn. 45 [121 S.Ct. at p. 2290]; *Lindh v. Murphy* (1997) 521 U.S. 320, 328, fn. 4 [117 S.Ct. 2059, 2064, 138 L.Ed.2d 481] [" 'retroactive' effect adequately authorized by a statute" only when statutory language was "so clear that it could sustain only one interpretation"].) *842

1. *Repeal Statute has no express retroactivity language*

(1c) In contending that the Repeal Statute is not retroactive, defendant tobacco companies contrast it with other California statutes that our Legislature has expressly made retroactive. (See § 1646.5 ["This section applies to contracts ... entered into before, on, or after its effective date; it shall be fully *retroactive* ..."] (italics added)]; Gov. Code, § 9355.8 ["This section shall have *retroactive application* ..."] (italics added).)

In addition, defendants point to language in the Repeal Statute's subdivision (e) as a clear indication that the Legislature did not intend the Repeal Statute to be retroactive. (§ 1714.45, subd. (e).) That provision incorporates the substance of an earlier amendment to the Immunity Statute, the Public Entity Amendment (see fn. 4, *ante*), which was intended to allow public entities to sue tobacco companies notwithstanding the statutory immunity. When first enacted, the Public Entity Amendment added to the Immunity Statute a provision, subdivision

(d), which stated that in an "action brought by a public entity, the fact that the injured individual's claim against the defendant may be barred by *this section* shall not be a defense." (Former § 1714.45, subd. (d), as added by Stats. 1997, ch. 25, § 2, italics added.) But when that provision became subdivision (e) of the Repeal Statute, the Legislature rephrased it to state that a public entity's suit against a tobacco company would not be precluded by "the fact that the injured individual's claim against the defendant may be barred by a *prior version of this section*." (§ 1714.45, subd. (e), as added by Stats. 1997, ch. 570, § 1, italics added.) The italicized language suggests that even after the January 1, 1998, effective date of the Repeal Statute, "a prior version" of that statute, namely the Immunity Statute, may continue to bar claims against tobacco companies brought by individual smokers.

Plaintiff insists that certain phrases in the Repeal Statute are express legislative declarations of retroactivity notwithstanding the absence of the term "retroactive" in that provision. When enacted, subdivision (f) of the Repeal Statute provided: "It is the intention of the Legislature in enacting the amendments to subdivisions (a) and (b) of this section adopted at the 1997-98 Regular Session to declare that *there exists no statutory bar* to tobacco-related personal injury, wrongful death, or other tort claims against tobacco manufacturers and their successors in interest by California smokers or others *who have suffered or incurred injuries*, damages, or costs arising from the promotion, marketing, sale, or consumption of tobacco products. It is also the intention of the Legislature to clarify that such claims which *were or are brought* shall be determined on their merits, without the imposition of any claim of statutory bar or categorical defense." (§ 1714.45, subd. (f), as added by Stats. 1997, ch. 570, § 1, italics added.) *843

Focusing on the italicized phrases in isolation, plaintiff asserts, as does the dissent, that they are express declarations of the California Legislature's intent to retroactively apply the statute repealing

the tobacco companies' immunity from products liability lawsuits brought by smokers. We are not persuaded. Neither the italicized phrases nor section 1714.45, subdivision (f) as a whole states anything more than that the Repeal Statute rescinded any former statutory immunity for tobacco companies. But even were we to accept that proposed reading of subdivision (f), the Repeal Statute is, at best, ambiguous on the question of retroactivity because of the Legislature's reference in subdivision (e) (allowing public entities to sue tobacco companies) to "a prior version" of the statute as possibly precluding suits against tobacco companies by individual smokers. This ambiguity requires us to construe the Repeal Statute as "unambiguously prospective." (*INS v. St. Cyr, supra*, 533 U.S. at pp. 320-321, fn. 45 [121 S.Ct. at p. 2290].)

Furthermore, the time-honored presumption against retroactive application of a statute, as reflected in section 3 of the California Civil Code as well as in decisions by this court and the United States Supreme Court, would be meaningless if the vague phrases relied on by plaintiff and the dissent were considered sufficient to satisfy the test of a "clear[] manifest[ation]" (*Hughes Aircraft Co. v. United States ex rel. Schumer, supra*, 520 U.S. at p. 946 [117 S.Ct. at p. 1876]) or an "'unequivocal and inflexible' " assertion (*Evangelatos, supra*, 44 Cal.3d at p. 1207, italics omitted) of the Repeal Statute's retroactivity. After a painstaking review of the entire Repeal Statute, we find it to be devoid of any express legislative intent of retroactivity. Although we agree with the dissent that "no talismanic word or phrase is required to establish retroactivity" (dis. opn. of Moreno, J., *post*, at p. 849), we do not agree there is language in the Repeal Statute of the unequivocal and inflexible statement of retroactivity that *Evangelatos* requires.

Interestingly, the Attorney General, in his role as amicus curiae for plaintiff, does not join plaintiff in urging this court to construe the Repeal Statute as retroactive. Instead, in an effort to avoid "the constitutional concerns inherent in retroactive

laws," the Attorney General argues that the Immunity Statute did nothing more than codify the common law defense of assumption of risk, a statutory defense that the Legislature, by its enactment of the Repeal Statute effective January 1, 1998, eliminated for all trials after that date.

The Attorney General's argument disregards the logical basis of this court's 1997 decision in *Richards, supra*, 14 Cal.4th 985, 1001, which construed the Immunity Statute not as codifying an existing affirmative defense for trial but as declaring legally permissible and not wrongful certain *844 conduct of tobacco companies. Applying *Richards* here, we reject the Attorney General's interpretation of the Immunity Statute.

2. *Extrinsic sources provide no clear indication of legislative intent to apply the Repeal Statute retroactively*

In contending that the Repeal Statute's legislative history is a "very clear" indicator that the California Legislature intended the statute to apply retroactively, plaintiff points to a brief comment in a report of the Senate Judiciary Committee prepared for the April 8, 1997, hearing on the bill to enact the Repeal Statute. The comment appears under the heading "Prospective repeal only" and states: "Some concern has been expressed that [Senate Bill No.] 67 would apply only to causes of action arising on or after January 1, 1998, assuming it is enacted this year. In the absence of specific language in the legislation specifying retroactive application, a measure will operate prospectively only...." (Sen. Com. on Judiciary, Rep. on Sen. Bill No. 67 (1997-1998 Reg. Sess.) Apr. 8, 1997, p. 3.) Plaintiff observes that just eight days later, an amendment added to the bill language stating that "there exists no statutory bar to ... tobacco-related personal injury, wrongful death, or other tort claims by California smokers or others who have suffered or incurred injuries," and indicating "that such claims which were or are brought" should be determined on their merits. (Sen. Bill No. 67 (1997-1998 Reg. Sess.) as amended Apr. 16, 1997,

italics added; now § 1714.45, subd. (f).) Plaintiff characterizes this amendment as the Legislature's "direct response" to the expressed "concern" about retroactivity, and thus as comprising a "very clear" indication that the Repeal Statute was to apply retroactively. We are not persuaded.

As we observed earlier, a statute may be applied retroactively only if it contains express language of retroactivity *or* if other sources provide a clear and unavoidable implication that the Legislature intended retroactive application. (*Evangelatos, supra*, 44 Cal.3d at p. 1208.) Addressing in this section the latter ground, we conclude that plaintiff has not shown a clear and unavoidable implication of legislative intent to apply the Repeal Statute retroactively. The committee report that plaintiff cites merely states the general rule that legislation operates prospectively unless there is clear language of retroactivity; nothing in that report indicates that the Legislature desired retroactive application of the Repeal Statute. The April 16, 1997, bill amendment adding language to subdivision (f) of the Repeal Statute does not cure this omission, because the added language does not itself supply an unavoidable implication that the Legislature intended to subject tobacco companies to potential tort liability for conduct occurring during the 10-year period when the Immunity Statute declared that very conduct to be lawful. *845 Its addition to the Repeal Statute eight days after some unspecified person voiced concern about retroactivity suggests that subdivision (f) may have been "the product of a legislative compromise" (*Fremont Comp. Ins. Co. v. Superior Court* (1996) 44 Cal.App.4th 867, 874 [52 Cal.Rptr.2d 211]), a way for legislators with differing views on retroactivity to vote for the Repeal Statute. "Avoiding resolution of disputed points is one of the classic means by which legislators are able to achieve agreement on legislative text." (*Id.* at pp. 873-874; accord, *J.A. Jones Construction Co. v. Superior Court* (1994) 27 Cal.App.4th 1568, 1577 [33 Cal.Rptr.2d 206].)

Plaintiff also points to comments by the Repeal

Statute's author that "tobacco companies may have deliberately manipulated the level of nicotine" in tobacco products and "waged an aggressive campaign of disinformation about the health consequences of tobacco use." (Sen. Com. on Judiciary, Rep. on Sen. Bill No. 67 (1997-1998 Reg. Sess.) Apr. 8, 1997, p. 2.) According to plaintiff, these comments reflect the Legislature's intent to remedy "past fraud" by tobacco companies by making the Repeal Statute retroactive. Not so.

Those comments were simply reasons given "in support of repeal" of the statutory immunity for tobacco companies (Sen. Com. on Judiciary, Rep. on Sen. Bill No. 67 (1997-1998 Reg. Sess.) Apr. 8, 1997, p. 2); they did not at all address retroactivity of the Repeal Statute. (4) Moreover, we have repeatedly declined to discern legislative intent from comments by a bill's author because they reflect only the views of a single legislator instead of those of the Legislature as a whole. (*Quintano v. Mercury Casualty Co.* (1995) 11 Cal.4th 1049, 1062 [48 Cal.Rptr.2d 1, 906 P.2d 1057]; *Grupe Development Co. v. Superior Court* (1993) 4 Cal.4th 911, 922 [16 Cal.Rptr.2d 226, 844 P.2d 545].)^{FN6}

FN6 The dissent broadly asserts that these comments by the bill's author and similar remarks in a letter supporting passage of the Repeal Statute "suggest" that the 1987 enactment of the statutory immunity was "secured in part by deceptive representations by the tobacco companies about the lethal nature of their product." (Dis. opn. of Moreno, J., *post*, at p. 853 & fn. 2.) Neither these comments nor anything else in the record before us shows that the 1987 legislation was indeed a product of deception by tobacco companies. As an appellate court, we may not consider assertions of fact that are not supported by the record. (See *People v. Szeto* (1981) 29 Cal.3d 20, 35 [171 Cal.Rptr. 652, 623 P.2d 213].)

3. *Constitutional considerations reinforce our reading of the Repeal Statute as not having retroactive*

application

(1d) Earlier we discussed the constitutional underpinnings of the presumption against a statute's retroactive application. That presumption has particular force in this case, in which retroactive application of the California Legislature's repeal of tobacco companies' statutory immunity from *846 product liability lawsuits could expose them to huge monetary damages for conduct that occurred during the statutory immunity period when that conduct carried no tort liability.

Instructive on this point is the United States Supreme Court's recent decision in *Eastern Enterprises v. Apfel* (1998) 524 U.S. 498 [118 S.Ct. 2131, 141 L.Ed.2d 451] (*Apfel*), in which the high court invalidated a federal law that retroactively imposed on coal mining companies substantial financial obligations for the health care of their retired workers. In a plurality opinion, four of the nine justices concluded the law was an unconstitutional taking under the Fifth Amendment to the federal Constitution. (*Apfel, supra*, at p. 538 [118 S.Ct. at pp. 2153-2154] (plur. opn. of O'Connor, J.)) In his concurring opinion, Justice Kennedy concluded that the act violated the Fifth Amendment's due process clause by retroactively creating liability for past conduct. (*Apfel, supra*, at p. 549 [118 S.Ct. at p. 2159] (conc. opn. of Kennedy, J.)) He observed: "If retroactive laws change the legal consequences of transactions long closed, the change can destroy the reasonable certainty and security which are the very objects of property ownership. As a consequence, due process protection for property must be understood to incorporate our settled tradition against retroactive laws of great severity. Groups targeted by retroactive laws, were they to be denied all protection, would have a justified fear that a government once formed to protect expectations now can destroy them. Both stability of investment and confidence in the constitutional system, then, are secured by due process restrictions against severe retroactive legislation." (*Id.* at pp. 548-549 [118 S.Ct. at p. 2158] (conc. opn. of Kennedy, J.))

In an earlier decision, *Landgraf v. USI Film Products, supra*, 511 U.S. 244, the high court questioned the constitutionality of legislation that retroactively would result in the imposition of punitive damages for particularly egregious conduct, suggesting it might violate the constitutional prohibition against ex post facto laws. (U.S. Const., art. I, § 9, cl. 3 [restricting federal government]; see also *id.*, art. I, § 10, cl. 1 [restricting state governments]; Cal. Const., art. I, § 9.) In the words of the high court: "The very labels given 'punitive' or 'exemplary' damages, as well as the rationales that support them, demonstrate that they share key characteristics of criminal sanctions. Retroactive imposition of punitive damages would raise a serious constitutional question." (*Landgraf v. USI Film Products, supra*, at p. 281 [114 S.Ct. at p. 1505].)

An established rule of statutory construction requires us to construe statutes to avoid "constitutional infirmities." (*847 *United States v. Delaware & Hudson Co.* (1909) 213 U.S. 366, 407-408 [29 S.Ct. 527, 535-536, 53 L.Ed. 836]; *United States v. Security Industrial Bank, supra*, 459 U.S. 70, 78 [103 S.Ct. 407, 412]; see also *Curran v. Mount Diablo Council of the Boy Scouts* (1998) 17 Cal.4th 670, 727-728 [72 Cal.Rptr.2d 410, 952 P.2d 218] (conc. opn. of Kennard, J.)) That rule reinforces our construction of the Repeal Statute as prospective only.

C. Whether the Immunity Statute Precludes Recovery for Defendants' Conduct Before the Immunity Period

Plaintiff began smoking cigarettes in 1956 and continued to do so until 1997, a period of 41 years. For 10 years of this period—from January 1, 1988, through December 31, 1997—the Immunity Statute was in effect to shield tobacco companies from liability for personal injuries that their tobacco products caused to voluntary consumers. Because, as explained above, the Repeal Statute is not retroactive, plaintiff has no product liability claim against defendant tobacco companies for their conduct in manufacturing and distributing cigarettes

during the statutory immunity period.

Regarding the portion of plaintiff's claim attributable to her use of cigarettes that defendant tobacco companies manufactured or distributed *before* the period of statutory immunity afforded those companies, defendants contend that the Immunity Statute shields them from liability. In support, they point out that the statute was expressly retroactive, covering during its effective period "all product liability actions pending on, or commenced after, January 1, 1988" (former § 1714.45, subd. (c), added by Stats. 1987, ch. 1498, § 3, p. 5779), whereas (as we hold here) the Repeal Statute was not retroactive and thus could not remove any of the protection conferred by the Immunity Statute. We reject defendants' contention.

Although the Repeal Statute has no retroactive effect, it nonetheless removed the protection that the Immunity Statute gave to tobacco companies for their conduct occurring *before* the Immunity Statute's effective date. This is so because a retroactive effect is one that "impair[s] rights a party possessed *when he acted*." (*Landgraf v. USI Film Products*, *supra*, 511 U.S. at p. 280 [114 S.Ct. at p. 1505], italics added.) The Repeal Statute did not impair any rights that tobacco companies possessed *before* the immunity period. On the contrary, by abrogating the Immunity Statute, the Repeal Statute restored the law governing product liability for the manufacture or sale of tobacco products to what it had been before the January 1, 1988, effective date of the Immunity Statute.

Before January 1, 1988, general tort principles defined the extent of any tort liability that tobacco companies might have for manufacturing or distributing their tobacco products for sale to voluntary consumers. When, 10 *848 years later, the California Legislature repealed the statutory immunity for tobacco manufacturers in product liability actions, it reinstated those general tort rules. This repeal did not "change the legal consequences" (*Apfel, supra*, 524 U.S. at p. 548 [118 S.Ct. at p. 2158]) of defendants' conduct in manufacturing or distributing

tobacco products before the effective date of the immunity. Nor could defendants reasonably have relied upon the Immunity Statute before its enactment. (See *In re Marriage of Buol* (1985) 39 Cal.3d 751, 761 [218 Cal.Rptr. 31, 705 P.2d 354].) Accordingly, repeal of the Immunity Statute eliminated any retroactive effect it may have had, so that the tort liability, if any, that defendants could incur for their conduct before the effective date of the Immunity Statute is determined by applying general tort principles.

IV. Conclusion

The Repeal Statute rescinding the tobacco companies' statutory immunity in certain product liability lawsuits contains no express retroactivity provision. Nor has the Legislature given any clear indication that it wanted the Repeal Statute to apply retroactively. Thus, the Immunity Statute continues to shield defendant tobacco companies in product liability actions but only for conduct they engaged in *during* the 10-year period when the Immunity Statute was in effect. The liability of tobacco companies based on their conduct *outside* the 10-year period of immunity is governed by general tort principles. We stress, however, that we are not here asked to decide, and do not decide, what liability, if any, defendants may have under those general tort principles.

George, C. J., Baxter, J., Werdegar, J., Chin, J., and Brown, J., concurred.

MORENO, J.

I respectfully dissent.

I agree with the majority that "to have the Repeal Statute govern product liability suits against tobacco companies ... would indeed be a retroactive application of that statute" (Maj. opn., *ante*, at p. 840.) Unlike the majority, however, I believe both the statutory language and the legislative history of Civil Code section 1714.45 ^{FNI} evince a clear legislative intent to apply the statute retroactively. I further conclude that such retroactive application would not raise serious questions of constitutional-

28 Cal.4th 828, 50 P.3d 751, 123 Cal.Rptr.2d 40, Prod.Liab.Rep. (CCH) P 16,451, 02 Cal. Daily Op. Serv. 7019, 2002 Daily Journal D.A.R. 8796
(Cite as: 28 Cal.4th 828)

ity. (Maj. opn., *ante*, at p. 845.)

FN1 All statutory references are to the Civil Code unless otherwise indicated.

Statutes are presumed to operate prospectively. (*Evangelatos v. Superior Court* (1988) 44 Cal.3d 1188, 1208 [246 Cal.Rptr. 629, 753 P.2d 585] *849 (*Evangelatos*); § 3.) “Of course, when the Legislature clearly intends a statute to operate retrospectively, we are obliged to carry out that intent unless due process considerations prevent us. [Citation.]” (*Western Security Bank v. Superior Court* (1997) 15 Cal.4th 232, 243 [62 Cal.Rptr.2d 243, 933 P.2d 507].) Whether the Legislature intended retroactive application of a statute requires an exercise in statutory interpretation to ascertain if, by “ ‘express language or clear and unavoidable implication,’ ” the presumption of prospective application has been overcome. (*Evangelatos, supra*, 44 Cal.3d at p. 1208.) As this formulation in *Evangelatos* suggests, no talismanic word or phrase is required to establish retroactivity. Rather, the question is whether, from the language employed in the statute, there plainly emerges a legislative intent for the statute to operate retrospectively. Moreover, even in the absence of an express retroactivity provision, a statute may still be applied retroactively if the Legislature’s intention is sufficiently clear from such extrinsic sources as legislative history. (*Id.* at pp. 1208-1209.)

Contrary to the majority, I conclude that subdivision (f) of section 1714.45 (added by Stats. 1997, ch. 570, § 1; all references to the Repeal Statute are to the 1997 enactment) is a sufficiently unambiguous statement of the Legislature’s intent that the Repeal Statute be given retrospective effect. In reaching this conclusion, I rely on the familiar principle of statutory construction that requires, in the first instance, consulting the words of the statute itself to ascertain legislative intent. (*Steketee v. Lintz, Williams & Rothberg* (1985) 38 Cal.3d 46, 51 [210 Cal.Rptr. 781, 694 P.2d 1153].) “The court is required to give effect to statutes ’ ’ ’ according to the usual, ordinary import of the language employed in

framing them.’ [Citations.] ‘If possible, significance should be given to every word, phrase, sentence and part of an act in pursuance of the legislative purpose []’ [citation]; ‘a construction making some words surplusage is to be avoided.’ [Citation.]“ ’ ’ (*Id.* at p. 52.)

Subdivision (f) of section 1714.45 states: “It is the intention of the Legislature in enacting the amendments to subdivisions (a) and (b) of this section adopted at the 1997-98 Regular Session to declare that *there exists no statutory bar* to tobacco-related personal injury, wrongful death, or other tort claims against tobacco manufacturers and their successors in interest by California smokers or others who *have suffered or incurred* injuries, damages, or costs arising from the promotion, marketing, sale, or consumption of tobacco products. It is also the intention of the Legislature to clarify that those claims *that were or are brought shall be determined on their merits, without the imposition of any claim of statutory bar or categorical defense.*” (Italics added.)

A statute speaks from the day it takes effect. (*Hersh v. State Bar* (1972) 7 Cal.3d 241, 245 [101 Cal.Rptr. 833, 496 P.2d 1201].) The inclusion of *850 persons who “*have suffered or incurred injuries*” as among those to whom the abolition of the statutory immunity applies cannot be understood to mean anything other than that the Legislature, speaking as of January 1, 1998, intended to eliminate immunity for past injury-producing conduct by the tobacco industry. This construction of section 1714.45, subdivision (f) is further supported by the next sentence, which declares an intent that “those claims that *were* or are brought shall be determined, ... *without the imposition of any claim of statutory bar or categorical defense.*” (Italics added.) The ordinary meaning of this language plainly precludes assertion by the tobacco companies of a statutory bar or other categorical defense not only to claims which may be brought in the future (“are brought”) but those based on past conduct (“were ... brought”) as to which the original enactment (Stats. 1987, ch.

1498, § 3, p. 5778; hereafter the Immunity Statute) might otherwise have applied.

The majority is “not persuaded” that these “phrases in isolation” express the Legislature’s intent that the Repeal Statute should be retroactively applied. (Maj. opn., *ante*, at p. 843.) The majority asserts: “Neither the italicized phrases nor section 1714.45, subdivision (f) as a whole states anything more than that Repeal Statute rescinded any former statutory immunity for tobacco companies.” (*Ibid.*) This conclusory statement, however, fails to suggest an alternative interpretation of the statute. In this respect, the majority’s approach does not comport with the principle of statutory construction that requires a reviewing court to give significance, if possible, to every word and phrase of a statute and avoid a construction that renders some words surplusage. (*Steketee v. Lintz, Williams & Rothberg, supra*, 38 Cal.3d at p. 52.) The majority then goes on to state that, even “were we to accept that proposed reading of subdivision (f), the Repeal Statute is, at best, ambiguous on the question of retroactivity because of the Legislature’s reference in subdivision (e) (allowing public entities to sue tobacco companies) to ‘a prior version’ of the statute as possibly precluding suits against tobacco companies by individual smokers.” (Maj. opn., *ante*, at p. 843.) Having thus discerned this ambiguity, the majority would apply the rule that a statute ambiguous as to retroactive application is to be applied prospectively. As I point out elsewhere, however, subdivision (e) does not conflict with the legislative mandate in subdivision (f) that the Repeal Statute be applied retroactively but, rather, addresses another legislative concern entirely; the possibility that the courts might determine that constitutional considerations preclude retroactivity, in which event, the Legislature carved out in subdivision (e) an exemption for public entities. In my view, therefore, subdivision (e) does not create an ambiguity. I would also observe that, by construing these two subdivisions so as to create a apparent conflict between them, the majority’s interpretation is contrary to the fundamental *851 principle of statutory construc-

tion that requires us, in construing legislation, “to harmonize its various elements without doing violence to its language or spirit.” (*Wells v. Marina City Properties, Inc.* (1981) 29 Cal.3d 781, 788 [176 Cal.Rptr. 104, 632 P.2d 217].)

I find further support for my conclusion that the Legislature intended retroactive application of the Repeal Statute in the legislative history surrounding the addition of subdivision (f) to section 1714.45. This history strongly suggests that subdivision (f) was added in response to a concern that the statute might only apply prospectively.

Senate Bill No. 67, as originally proposed, did not contain what eventually became subdivision (f), nor any other declaration of legislative intent. (Sen. Bill No. 67 (1997-1998 Reg. Sess.) § 1, as introduced Dec. 11, 1996.) In anticipation of an April 1997 hearing on the bill, the Senate Judiciary Committee noted that “[s]ome concern has been expressed that [Senate Bill No.] 67 would apply *only to causes of action arising on or after January 1, 1998*, assuming it is enacted this year. In the absence of specific language in the legislature specifying retroactive application, a measure will operate prospectively only upon its enactment.” (Sen. Com. on Judiciary, Rep. on Sen. Bill No. 67 (1997-1998 Reg. Sess.) as amended Feb. 14, 1997, italics added.) One week after this acknowledgment of concern about a prospective-only application of amendments as then drawn, the bill was amended further by the insertion of what would become subdivision (f). (Sen. Bill No. 67 (1997-1998 Reg. Sess.) § 1, subd. (d), as amended Apr. 16, 1997.)

The proximity of these events suggests that subdivision (f) was added to section 1714.45 in response to the concern expressed in the committee report. At minimum, that “the retroactivity question was actually consciously considered during the enactment process” (*Evangelatos, supra*, 44 Cal.3d at p. 1211) supports a conclusion that retroactivity was intended.

28 Cal.4th 828, 50 P.3d 751, 123 Cal.Rptr.2d 40, Prod.Liab.Rep. (CCH) P 16,451, 02 Cal. Daily Op. Serv. 7019, 2002 Daily Journal D.A.R. 8796
(Cite as: 28 Cal.4th 828)

The majority, examining this legislative history, simply concludes that the addition of subdivision (f) "may have been" the product of legislative compromise that allowed legislators with "differing views on retroactivity to vote for the Repeal Statute." (Maj. opn., *ante*, at p. 845.) But no "differing views" are expressed in the committee report regarding retroactivity and I cannot agree with the majority's explanation of the report. The plain meaning of the language used in subdivision (f) and the legislative history seem to me to unmistakably document such intent.

To buttress the assertion that subdivision (f) does not mean what it says, the majority, like defendants, cites subdivision (e) of section 1714.45. *852 Subdivision (e) essentially reiterates an amendment to the Immunity Statute that exempted public entities from the statute. The original provision in the Immunity Statute stated that in an "action brought by a public entity, the fact that the injured individual's claim against the defendant may be barred by this section shall not be a defense." (§ 1714.45, former subd. (d), as amended by Stats. 1997, ch. 25, § 2, eff. June 12, 1997.) The current version in the Repeal Statute provides "[i]n the action brought by a public entity, the fact that the injured individual's claim against the defendant may be barred by a prior version of this section shall not be a defense." (§ 1714.45, subd. (e), italics added.)

The majority finds that the phrase "a prior version of this section" suggests that "even after the January 1, 1998, effective date of the Repeal Statute, 'a prior version' of that statute, namely the Immunity Statute, may continue to bar claims against tobacco companies brought by individual smokers." (Maj. opn., *ante*, at p. 842.) In my view, subdivision (e) of section 1714.45 simply reflects the Legislature's concern that, notwithstanding its intent that the Repeal Statute apply retroactively, the courts might decline to give retroactive effect to the statute based on due process or other constitutional concerns raised by retroactivity. (*Western Security*

Bank v. Superior Court, *supra*, 15 Cal.4th at p. 243 ["Of course, when the Legislature clearly intends a statute to operate retrospectively, we are obliged to carry out that intent *unless* due process considerations prevent us" (italics added)].) Indeed, the majority touches upon these constitutional issues and while, in my view, they provide no basis to deny retroactive application of the Repeal Statute, the Legislature could not have forecast with absolute certainty whether its intent to apply the statute retroactively would survive a court challenge. This uncertainty by the Legislature is demonstrated by its use of the word "may." Therefore, the Legislature chose to make it clear that, at minimum, suits by public entities would not be precluded by judicial fiat. This interpretation harmonizes subdivisions (e) and (f), which, notably, the majority's approach does not. (*Wells v. Marina City Properties, Inc.*, *supra*, 29 Cal.3d at p. 788 ["It is fundamental that legislation should be construed so as to harmonize its various elements without doing violence to its language or spirit."].)

Finally, the majority suggests that constitutional considerations reinforce its interpretation of the Repeal Statute as not having retroactive application. (Maj. opn., *ante*, at p. 845.) Specifically, the majority alludes to potential due process and ex post facto issues. The retroactive application of any statute must be vetted for constitutionality, but I do not agree that constitutional considerations support a conclusion of nonretroactivity. Nor are the cases cited by the majority persuasive in this respect. The concurring opinion of Justice Kennedy in *853 *Eastern Enterprises v. Apfel* (1998) 524 U.S. 498, 548-549 [118 S.Ct. 2131, 2158-2159, 141 L.Ed.2d 451], states little more than the truism that retroactive laws must meet the test of due process. The majority's citation to dictum in *Landgraf v. USI Film Products* (1994) 511 U.S. 244 [114 S.Ct. 1483, 128 L.Ed.2d 229] on the ex post facto issue is equally general.

Retroactive application of a statute may be unconstitutional if, inter alia, it deprives a person of a

vested right without due process of law. (*In re Marriage of Buol* (1985) 39 Cal.3d 751, 756 [218 Cal.Rptr. 31, 705 P.2d 354].) I am not convinced that the immunity conferred in this case, however, is a vested right. First, the immunity involved here was wholly a creation of statute, and its abolition does not affect the tobacco companies' right to assert common law defenses in product liability actions. (Cf. *Callet v. Alioto* (1930) 210 Cal. 65, 67-68 [290 P. 438] [statutory rights, unlike common law rights, not vested for purposes of retroactive application of a statute because "all statutory remedies are pursued with full realization that the legislature may abolish the right to recover at any time"].) Second, I question whether a statutory immunity secured in part by deceptive representations by the tobacco companies about the lethal nature of their product should be deemed a vested right under any circumstance. FN2

FN2 The majority asserts that there is no proof in the record that the 1987 legislation was the product of deception by tobacco companies. (Maj. opn., *ante*, at p. 845, fn. 6.) At the time the Repeal Statute was proposed its author explained the need for the legislation was due in part to evidence that "the tobacco companies may have deliberately manipulated the level of nicotine" and also that "evidence shows the tobacco companies have systematically suppressed and concealed material information and waged an aggressive campaign of disinformation about the health consequences of tobacco use." (Sen. Com. on Judiciary, Rep. on Sen. Bill No. 67 (1997-1998 Reg. Sess.) Apr. 8, 1997, p. 2.) In the same report, the California Medical Association, identified as "one of the main participants" in the 1987 legislation stated in support of the bill that "[o]ver the last decade we have learned much regarding the addictive nature of tobacco and the industry's intentional efforts to mislead the public on the health effects of tobacco. This, coupled

with the courts' broad interpretation of the California statute, has precipitated the need to change that statute and remove tobacco's liability protections.'" (*Ibid.*) I submit that these remarks, particularly the comments of the California Medical Association which was a participant in the 1987 legislation, suggest that the tobacco companies did deceive the other parties to the legislative effort that resulted in the Immunity Statute.

Even assuming, arguendo, that the Immunity Statute created a vested right, it is settled that "[v]ested rights are not immutable; the state, exercising its police power, may impair such rights when considered reasonably necessary to protect the health, safety, morals and general welfare of the people." (*In re Marriage of Buol*, *supra*, 39 Cal.3d at pp. 760-761.) "In determining whether a retroactive law contravenes the due process clause, we consider such factors as the significance of the state interest served by the law, the importance of the retroactive application of the law to the effectuation of that interest, the extent of reliance upon the former law, the legitimacy of that reliance, the extent of actions taken on the basis of that *854 reliance, and the extent to which the retroactive application of the new law would disrupt those actions." (*In re Marriage of Bouquet* (1976) 16 Cal.3d 583, 592 [128 Cal.Rptr. 427, 546 P.2d 1371].)

I submit that, if the due process issue actually arose, all these factors would weigh heavily in favor of finding that retroactive application of the Repeal Statute does not contravene the due process clause. The state has a substantial interest in seeing that victims of dangerous products are compensated for their injuries by the manufacturers of dangerous or defective products that are in the best position to provide such compensation. (*Safeway Stores, Inc. v. Nest-Kart* (1978) 21 Cal.3d 322, 330 [146 Cal.Rptr. 550, 579 P.2d 441] ["one of the principal social policies served by product liability doctrine is to assign liability to a party who possesses the

(Cite as: 28 Cal.4th 828)

ability to distribute losses over an appropriate segment of society ...”).) The state has an equally substantial interest in protecting and promoting the health of Californians. These interests would be significantly advanced by retroactive application of the Repeal Statute.

The Repeal Statute restores the right of Californians suffering from smoking-related illnesses to pursue product liability actions against the tobacco companies. Such meritorious actions would properly compensate the victims and would also shift the costs for their care from the public health system, to the extent the victims rely on public health care, to the tobacco companies. Furthermore, such actions expose the life-threatening consequences of tobacco use, as well as the tobacco companies' deceptive practices in promoting the use of their products. In the past, such suits have helped create a popular repugnance toward the tobacco companies and their products that has, in turn, contributed to a decline in the amount of consumption of tobacco products, thus promoting the health of the populace and reducing health costs associated with tobacco use. Retroactive application of the Repeal Statute would serve both goals of victim compensation and reduction of the use of tobacco products. By contrast, the tobacco companies can claim little reliance on the decade-old Immunity Statute, since the claims ordinarily advanced in these kinds of suits involve conduct stretching back decades. Furthermore, as I observed, retroactive application of the Repeal Statute does not strip the tobacco companies of their common law defenses.

Briefly, the majority also suggests that retroactive application of the Repeal Statute could implicate the prohibition against ex post facto laws because of the potential availability of punitive damages. Again, however, the majority does not engage in an in-depth analysis that demonstrates retroactive application of the Repeal Statute would in fact violate the prohibition against ex post facto laws. Furthermore, the brief discussion of this *855 point in the case cited by the majority, *Landgraf v. USI Film*

Products, supra, 511 U.S. 244, is dictum. (*Id.* at p. 281 [114 S.Ct. at pp. 1505-1506].) Assuming a punitive damages award might be deemed penal for purposes of the ex post facto clause, the clause applies only if the challenged law makes criminal conduct that was not criminal at the time the action was performed. (*Ibid.* [“Before we entertain [the ex post facto] question, we would have to be confronted with a statute that explicitly authorized punitive damages for preenactment conduct”]; *Collins v. Youngblood* (1989) 497 U.S. 37, 42 [110 S.Ct. 2715, 2719, 111 L.Ed.2d 30].)

The conduct engaged in by the tobacco companies that might support an award of punitive damages in the instant case stretches back far beyond the 10-year period during which the Immunity Statute was in effect. As the majority concludes elsewhere in the opinion, neither due process concerns nor the ex post facto clause shields the tobacco companies from liability, presumably including punitive damages, for conduct they engaged in prior to the enactment of the Immunity Statute in 1988. (Maj. opn., *ante*, at pp. 847-848.) The effect of the Repeal Statute in that case is simply to restore the status quo ante that existed before January 1, 1988. Since the tobacco companies' conduct that is the basis of the instant suit is a continuous course of action that encompasses several decades, I question whether a plausible ex post facto claim could be made. To do so the tobacco companies would be required to isolate specific acts that occurred during the immunity period and identify the percentage of a punitive damages award attributable to such conduct. This is not their position. Rather, they have argued that the Immunity Statute insulates them from *any* liability, including their pre-1988 conduct. (Maj. opn., *ante*, at p. 847.) Therefore, the ex post facto concern raised by the majority seems both theoretical and dubious and does not present a substantive reason for declining to carry out the Legislature's will by retroactively applying the Repeal Statute.

For all these reasons, therefore, I dissent. *856

28 Cal.4th 828, 50 P.3d 751, 123 Cal.Rptr.2d 40, Prod.Liab.Rep. (CCH) P 16,451, 02 Cal. Daily Op. Serv. 7019,
2002 Daily Journal D.A.R. 8796

(Cite as: 28 Cal.4th 828)

Cal. 2002.

Myers v. Philip Morris Companies, Inc.

28 Cal.4th 828, 50 P.3d 751, 123 Cal.Rptr.2d 40,
Prod.Liab.Rep. (CCH) P 16,451, 02 Cal. Daily Op.
Serv. 7019, 2002 Daily Journal D.A.R. 8796

END OF DOCUMENT

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)



United States District Court,
C.D. California.

R. Todd NEILSON as Trustee of the Bankruptcy Estate of Reed E. Slatkin, Wesley West Flexible Partnership, Stuart W. Stedman; Stedman West Family Partnership, Ltd. As Successor to Wesley West Long Term Partnership Ltd.; Stuart W. Stedman as Trustee of the Neva and Wesley West Foundation; Wesley West Minerals, Ltd.; George V. Kriste, John K. Poitras, Michael B. Azeez; Michael B. Azeez as Trustee of the Azeez Foundation; Michael B. Azeez as Trustee of the Betty Shapiro Trust; Michael B. Azeez as Trustee of the Thomas Di Maggio Trust; Michael B. Azeez as General Partner and on Behalf of Sazeez L.P.; Anthony Podell; Gregory B. Abbott, Fred Ockrim; Sheri L. Ockrim; And The Following Individuals In Their Individual and Representative Capacities On Behalf Of All Those Similarly Situated: Steven M. Besserman; Linda A. Besserman; Ric Jackson; Cynthia Jackson; Anita Kaplan; Michael Kaplan; Susan Safirstein; Jaroslav J. Marik; And California Community Foundation as Trustee of the Barbara L. Dewey Charitable Lead Annuity Trust, Plaintiffs,
v.
UNION BANK OF CALIFORNIA, N.A.; Comerica Bank-California; Imperial Management Incorporated; Bank of Orange County; Mary Catherine Leider; and Does 1 through 10, Defendants.

No. CV02-06942MMMCWX.

Oct. 20, 2003.

Investors brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors. On defendants' motions to dismiss and to strike, the District Court, Morrow, J., held that:(1) parent bank was not corporate alter ego of subsidiary bank; (2) investors adequately alleged banks' aider and abettor liability; (3) investors adequately pleaded claim for breach of fiduciary duty; (4) investors failed ad-

equately to plead claims for fraud, negligent misrepresentation and constructive fraud; (5) investors adequately pleaded claims for negligence, unfair business practices and fraudulent transfers; and (6) action was not barred by res judicata.

Motions granted in part, and denied in part.

West Headnotes

[1] Evidence 157  **43(1)**

157 Evidence

157I Judicial Notice

157k43 Judicial Proceedings and Records

157k43(1) k. In general. Most Cited Cases

Judicial notice can be taken only for limited purpose of recognizing judicial act that order represents on subject matter of litigation. Fed.Rules Evid.Rule 201, 28 U.S.C.A.

[2] Evidence 157  **43(4)**

157 Evidence

157I Judicial Notice

157k43 Judicial Proceedings and Records

157k43(4) k. Proceedings in other courts.

Most Cited Cases

District court would take judicial notice of documents filed in other court, for limited purpose of establishing fact of such litigation and related filings.

[3] Federal Civil Procedure 170A  **1832**

170A Federal Civil Procedure

170AXI Dismissal

170AXI(B) Involuntary Dismissal

170AXI(B)5 Proceedings

170Ak1827 Determination

170Ak1832 k. Matters considered

in general. Most Cited Cases

District court ruling on motion to dismiss may consider, on judicial notice, document which is not contested as to its authenticity, and upon which

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

plaintiff's complaint necessarily relies.

[4] Evidence 157 ↪1

157 Evidence

157I Judicial Notice

157k1 k. Nature and scope in general. Most Cited Cases

District court would take judicial notice of contracts between defendant and putative class members that provided foundation for class action.

[5] Evidence 157 ↪1

157 Evidence

157I Judicial Notice

157k1 k. Nature and scope in general. Most Cited Cases

District court would not take judicial notice of letter from plaintiff's counsel to defendant, since its contents were not alleged in complaint and its authenticity was not undisputed. Fed.Rules Evid.Rule 201, 28 U.S.C.A.

[6] Corporations and Business Organizations 101 ↪1039

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1039 k. Alter ego in general. Most Cited Cases

(Formerly 101k1.4(4))

When plaintiff comes into court claiming that opposing party is using corporate form unjustly and in derogation of plaintiff's interests under California law, court may, under "alter ego doctrine," disregard corporate entity and hold individual shareholders liable for actions of corporation.

[7] Corporations and Business Organizations 101 ↪1037

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1037 k. Justice and equity in general.

Most Cited Cases

(Formerly 101k1.4(4))

Corporations and Business Organizations 101 ↪1039

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1035 Reasons and Justifications

101k1039 k. Alter ego in general. Most Cited Cases

(Formerly 101k1.4(4))

Before "alter ego doctrine" may be invoked under California law to hold individual shareholders liable for corporation's actions, plaintiff must allege that: (1) there is such unity of interest and ownership between corporation and its equitable owner that separate personalities of the corporation and shareholder do not exist, and (2) there will be inequitable result if acts in question are treated as those of corporation alone.

[8] Corporations and Business Organizations 101 ↪1053

101 Corporations and Business Organizations

101II Disregarding Corporate Entity; Piercing Corporate Veil

101k1050 Separate Corporations; Disregarding Separate Entities

101k1053 k. Parent and subsidiary corporations in general. Most Cited Cases

(Formerly 101k1.5(3))

Mere fact that parent corporation owns stock of subsidiary will not suffice to prove that two entities are alter egos of one another, for purpose of imposing personal liability upon shareholders under California law for corporations' actions; rather, evidence must show that wholly-owned subsidiary is merely conduit for, or is financially dependent on, parent corporation.

[9] Corporations and Business Organizations

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

101 ↪ **1085(4)**

101 Corporations and Business Organizations
101III Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil

101k1085 Pleading

101k1085(4) k. Alter ego, instrumentality, or agency in general. Most Cited Cases

(Formerly 101k1.7(1))

Conclusory allegations of “alter ego” status are insufficient to state claim imposing personal liability upon shareholders under California law for corporation's actions; rather, plaintiff must allege specifically both elements of alter ego liability, as well as facts supporting each.

[10] Corporations and Business Organizations
101 ↪ **1085(10)**

101 Corporations and Business Organizations
101III Disregarding Corporate Entity; Piercing Corporate Veil

101k1079 Actions to Pierce Corporate Veil

101k1085 Pleading

101k1085(10) k. Separate corporations. Most Cited Cases

(Formerly 101k1.7(1))

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, failed to allege that parent bank engaged in bad faith conduct in its acquisition and management of subsidiary bank against whom substantive claims were brought, as required to state claims against parent bank under California law based upon “alter ego doctrine”; allegation that subsidiary bank lacked sufficient funds to pay judgment on prospective claim was inadequate to allege that inequitable result would follow if corporate veil were not pierced.

[11] Torts 379 ↪ **133**

379 Torts

379I In General

379k129 Persons Liable

379k133 k. Aiding and abetting. Most Cited Cases
(Formerly 379k21)

Under California law, liability may be imposed on one who aids and abets commission of intentional tort if person: (1) knows that other's conduct constitutes breach of duty and gives substantial assistance or encouragement to other to so act, or (2) gives substantial assistance to other in accomplishing tortious result, and person's own conduct, separately considered, constitutes breach of duty to third person.

[12] Fraud 184 ↪ **45**

184 Fraud

184II Actions

184II(C) Pleading

184k45 k. Falsity of representations and knowledge thereof. Most Cited Cases

Although rule that malice, intent, knowledge, and other states of mind may be averred generally within fraud claim obviates necessity of pleading detailed facts supporting allegations of knowledge, it does not relieve pleader of burden of alleging nature of knowledge that defendant purportedly possesses. Fed.Rules Civ.Proc.Rule 9, 28 U.S.C.A.

[13] Torts 379 ↪ **133**

379 Torts

379I In General

379k129 Persons Liable

379k133 k. Aiding and abetting. Most Cited Cases
(Formerly 379k26(1), 379k21)

In order to plead aider and abettor liability for intentional tort under California law, plaintiff must allege that party in question had actual knowledge of primary violation.

[14] Brokers 65 ↪ **34**

65 Brokers

65IV Duties and Liability to Principal

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

65k34 k. Fraud of broker or his agent. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, adequately alleged that banks had actual knowledge of primary violations committed by independent advisor, as required to plead aider and abettor liability against banks under California law; complaint alleged that banks utilized atypical banking procedures to service advisor's accounts, raising inference that they knew of scheme and sought to accommodate it by altering normal ways of doing business.

[15] Conspiracy 91 ⚡1.1

91 Conspiracy

91I Civil Liability

91I(A) Acts Constituting Conspiracy and Liability Therefor

91k1 Nature and Elements in General

91k1.1 k. In general. Most Cited Cases

"Agent's immunity rule" provides that duly acting agents and employees cannot be held liable under California law for conspiring with their principals.

[16] Conspiracy 91 ⚡1.1

91 Conspiracy

91I Civil Liability

91I(A) Acts Constituting Conspiracy and Liability Therefor

91k1 Nature and Elements in General

91k1.1 k. In general. Most Cited Cases

Agent's immunity rule does not apply under California law where agent acts for his own financial gain.

[17] Fraud 184 ⚡30

184 Fraud

184I Deception Constituting Fraud, and Liability Therefor

184k30 k. Persons liable. Most Cited Cases

Claim for aiding and abetting breach of fiduciary duty under California law does not require plaintiff to plead that defendant participated in alleged breach for financial gain or advantage.

[18] Brokers 65 ⚡34

65 Brokers

65IV Duties and Liability to Principal

65k34 k. Fraud of broker or his agent. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, failed to plead any facts averring that administrator substantially assisted independent advisor's theft of funds from non-account holders, as required to plead aider and abettor liability against administrator under California law.

[19] Fraud 184 ⚡43

184 Fraud

184II Actions

184II(C) Pleading

184k43 k. Statements, acts, or conduct constituting fraud. Most Cited Cases

Where aiding and abetting is gravamen of fraud claim, complaint must inform defendant of what he did that constituted substantial assistance to underlying fraud. Fed.Rules Civ.Proc.Rule 9, 28 U.S.C.A

[20] Brokers 65 ⚡34

65 Brokers

65IV Duties and Liability to Principal

65k34 k. Fraud of broker or his agent. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, adequately alleged that administrator substantially assisted independent advisor's theft of funds from account holders, as required to plead aider and abettor liability against administrator un-

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

der California law; complaint averred that administrator made statements that calmed potentially irate investors, allowing advisor to retain possession of their funds and continue scheme.

[21] Fraud 184 ↪41

184 Fraud

184II Actions

184II(C) Pleading

184k41 k. Allegations of fraud in general.

Most Cited Cases

Allegations of fraud or substantial assistance to fraud must be specific enough to give defendants notice of particular misconduct which is alleged to constitute charge, so that they can defend against charge and not just deny that they have done anything wrong. Fed.Rules Civ.Proc.Rule 9, 28 U.S.C.A.

[22] Torts 379 ↪133

379 Torts

379I In General

379k129 Persons Liable

379k133 k. Aiding and abetting. Most

Cited Cases

(Formerly 379k21)

Aider and abettor liability may properly be imposed under California law on one who knows that another's conduct constitutes breach of duty and substantially assists or encourages breach.

[23] Torts 379 ↪133

379 Torts

379I In General

379k129 Persons Liable

379k133 k. Aiding and abetting. Most

Cited Cases

(Formerly 379k21)

Act of aiding and abetting is distinct from primary violation; liability attaches because aider and abettor behaves in manner that enables primary violator to commit underlying tort.

[24] Conspiracy 91 ↪13

91 Conspiracy

91I Civil Liability

91I(A) Acts Constituting Conspiracy and Liability Therefor

91k12 Persons Liable

91k13 k. In general. Most Cited Cases

Conspirators are held liable for torts committed by their co-conspirators.

[25] Torts 379 ↪133

379 Torts

379I In General

379k129 Persons Liable

379k133 k. Aiding and abetting. Most

Cited Cases

(Formerly 379k21)

Causation is essential element of aiding and abetting claim, i.e., plaintiff must show that aider and abettor provided assistance that was substantial factor in causing harm suffered.

[26] Conspiracy 91 ↪2

91 Conspiracy

91I Civil Liability

91I(A) Acts Constituting Conspiracy and Liability Therefor

91k1 Nature and Elements in General

91k2 k. Combination. Most Cited

Cases

Plaintiff seeking to prove conspiracy claim need not adduce proof that purported conspirator did anything that caused or contributed to harm; all that is needed is proof of agreement to commit tort.

[27] Fraud 184 ↪44

184 Fraud

184II Actions

184II(C) Pleading

184k44 k. Contract, transaction, or circumstances connected with fraud. Most Cited Cases

Claim for aiding and abetting breach of fiduciary duty under California law does not require plaintiff to allege that defendant owed plaintiff in-

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

dependent fiduciary duty.

[28] Fraud 184 ↪7

184 Fraud

184I Deception Constituting Fraud, and Liability Therefor

184k5 Elements of Constructive Fraud

184k7 k. Fiduciary or confidential relations. Most Cited Cases

To state claim for breach of fiduciary duty under California law, complaint must allege existence of fiduciary duty, its breach, and damages resulting therefrom.

[29] Brokers 65 ↪28

65 Brokers

65IV Duties and Liability to Principal

65k28 k. Keeping and rendering accounts. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, adequately alleged that bank, as trustee of investment accounts, failed to perform its management and oversight obligations to investors, as required to plead claim for breach of fiduciary duty under California law; investment accounts were custodial in nature, and bank's obligations to investors were not contractually limited.

[30] Corporations and Business Organizations 101 ↪1957

101 Corporations and Business Organizations

101VII Directors, Officers, and Agents

101VII(E) Liability for Corporate Debts and Acts

101k1956 Nature and Grounds in General

101k1957 k. In general. Most Cited Cases

(Formerly 101k325)

Corporation's employees owe no independent fiduciary duty under California law to third party with whom they deal on behalf of their employer.

[31] Fraud 184 ↪3

184 Fraud

184I Deception Constituting Fraud, and Liability Therefor

184k2 Elements of Actual Fraud

184k3 k. In general. Most Cited Cases

To state cause of action for fraud under California law, plaintiff must allege: (1) misrepresentation; (2) knowledge of falsity; (3) intent to defraud; (4) justifiable reliance; and (5) resulting damage.

[32] Fraud 184 ↪13(3)

184 Fraud

184I Deception Constituting Fraud, and Liability Therefor

184k8 Fraudulent Representations

184k13 Falsity and Knowledge Thereof

184k13(3) k. Statements recklessly made; negligent misrepresentation. Most Cited Cases

Elements of cause of action for negligent misrepresentation are same as those of claim for fraud under California law, with exception that defendant need not actually know representation is false; rather, to plead negligent misrepresentation, it is sufficient to allege that defendant lacked reasonable grounds to believe representation was true.

[33] Brokers 65 ↪34

65 Brokers

65IV Duties and Liability to Principal

65k34 k. Fraud of broker or his agent. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, failed to allege that administrator or other bank employee made knowingly false representations to any named plaintiffs, or that administrator or other employee was authorized to do so by bank, as required to plead fraud claim under California law.

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

[34] Banks and Banking 52 ↪226

52 Banks and Banking
 52III Functions and Dealings
 52III(H) Actions
 52k226 k. Pleading. Most Cited Cases

Fraud 184 ↪45

184 Fraud
 184II Actions
 184II(C) Pleading
 184k45 k. Falsity of representations and knowledge thereof. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, failed to allege that administrator made representations to investors while lacking reasonable grounds to believe that they were true, as required to plead negligent misrepresentation claim under California law.

[35] Fraud 184 ↪6

184 Fraud
 184I Deception Constituting Fraud, and Liability Therefor
 184k5 Elements of Constructive Fraud
 184k6 k. In general. Most Cited Cases

To state cause of action for constructive fraud under California law, plaintiff must allege: (1) fiduciary or confidential relationship; (2) act, omission or concealment involving breach of that duty; (3) reliance; and (4) resulting damage.

[36] Brokers 65 ↪34

65 Brokers
 65IV Duties and Liability to Principal
 65k34 k. Fraud of broker or his agent. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, failed to allege that administrator owed independent fiduciary duty to investors, as required to

plead constructive fraud claim under California law.

[37] Banks and Banking 52 ↪100

52 Banks and Banking
 52III Functions and Dealings
 52III(A) Banking Franchises and Powers, and Their Exercise in General
 52k100 k. Torts. Most Cited Cases

Banks and Banking 52 ↪226

52 Banks and Banking
 52III Functions and Dealings
 52III(H) Actions
 52k226 k. Pleading. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, alleged that banks breached duty of reasonable care to ensure accuracy, legitimacy, and existence of assets of investment club, as required to state negligence claim under California law; complaint averred that banks breached duty by commingling assets of club accounts and by allowing independent investment advisor to accept funds, even though banks knew that he was not legally registered.

[38] Antitrust and Trade Regulation 29T ↪358

29T Antitrust and Trade Regulation
 29TIII Statutory Unfair Trade Practices and Consumer Protection
 29TIII(E) Enforcement and Remedies
 29TIII(E)5 Actions
 29Tk356 Pleading
 29Tk358 k. Particular cases. Most Cited Cases

(Formerly 92Hk38 Consumer Protection)

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, adequately alleged that banks' actions in

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

connection with scheme constituted unfair, illegal, and fraudulent business practices, as required to plead claim under California Business and Professions Code. West's Ann.Cal.Bus. & Prof.Code § 17200.

[39] Bankruptcy 51 ↪2724

51 Bankruptcy
51V The Estate
51V(H) Avoidance Rights
51V(H)2 Proceedings
51k2724 k. Pleading. Most Cited Cases

Investors who brought class action against banks and investment account administrator, stemming from purported Ponzi scheme to defraud investors, alleged that banks told investors they were deducting trustee fees from investors' individual accounts, and that investors relied on such representations to their detriment, as required to state claim for avoiding and recovering advisor's intentional fraudulent transfers under California Uniform Fraudulent Transfer Act; complaint averred that independent investment advisor concealed from his creditors fact that he had transferred money to banks within seven-year period, and that banks affirmatively misrepresented to investment club members that such transfers constituted trustee's fees. Bankr.Code, 11 U.S.C.A. § 544; West's Ann.Cal.Civ.Code §§ 3439.04, 3439.07.

[40] Bankruptcy 51 ↪2724

51 Bankruptcy
51V The Estate
51V(H) Avoidance Rights
51V(H)2 Proceedings
51k2724 k. Pleading. Most Cited Cases

Federal courts applying fraudulent transfer law at pleading stage generally require that complaint allege existence of actual creditor holding allowable unsecured claim who could avoid transfer under applicable state law in absence of bankruptcy proceeding. Bankr.Code, 11 U.S.C.A. § 544.

[41] Bankruptcy 51 ↪2724

51 Bankruptcy
51V The Estate
51V(H) Avoidance Rights
51V(H)2 Proceedings
51k2724 k. Pleading. Most Cited Cases

Plaintiff seeking to avoid and recover fraudulent transfers under California Uniform Fraudulent Transfer Act is required specifically to allege identity of any unsecured creditor whose rights he is asserting. Bankr.Code, 11 U.S.C.A. § 544; West's Ann.Cal.Civ.Code §§ 3439.04, 3439.07.

[42] Judgment 228 ↪584

228 Judgment
228XIII Merger and Bar of Causes of Action and Defenses
228XIII(B) Causes of Action and Defenses Merged, Barred, or Concluded
228k584 k. Nature and elements of bar or estoppel by former adjudication. Most Cited Cases
"Res judicata," also known as claim preclusion, bars litigation in subsequent action of any claims that were raised or could have been raised in prior action.

[43] Judgment 228 ↪540

228 Judgment
228XIII Merger and Bar of Causes of Action and Defenses
228XIII(A) Judgments Operative as Bar
228k540 k. Nature and requisites of former recovery as bar in general. Most Cited Cases
Doctrine of res judicata is applicable whenever there is: (1) identity of claims; (2) final judgment on merits; and (3) identity or privity between parties.

[44] Judgment 228 ↪955

228 Judgment
228XXIII Evidence of Judgment as Estoppel or Defense

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

228k955 k. Evidence as to identity of parties.

Most Cited Cases

Banks against whom class action was brought by investors, stemming from purported Ponzi scheme to defraud investors, failed to establish that they were in privity with any parties named in prior related claim brought by sole investor, and thus investors' present action was not barred by res judicata; banks did not offer any evidence to support assertion that they were successors in interest to prior named entities.

[45] Federal Civil Procedure 170A ↪1832

170A Federal Civil Procedure

170AXI Dismissal

170AXI(B) Involuntary Dismissal

170AXI(B)5 Proceedings

170Ak1827 Determination

170Ak1832 k. Matters considered

in general. Most Cited Cases

In deciding motion to dismiss for failure to state claim, court's review is limited to contents of complaint, exhibits attached thereto, and matters that are properly subject to judicial notice. Fed.Rules Civ.Proc.Rule 12(b)(6), 28 U.S.C.A.

[46] Federal Civil Procedure 170A ↪1103

170A Federal Civil Procedure

170AVII Pleadings and Motions

170AVII(N) Striking Pleading or Matter

Therein

170Ak1103 k. Discretion of court. Most

Cited Cases

Decision whether to grant motion to strike lies within sound discretion of district court. Fed.Rules Civ.Proc.Rule 12(f), 28 U.S.C.A.

[47] Federal Civil Procedure 170A ↪1145.1

170A Federal Civil Procedure

170AVII Pleadings and Motions

170AVII(N) Striking Pleading or Matter

Therein

170Ak1145 Determination of Motion

170Ak1145.1 k. In general. Most Cited

Cases

In exercising its discretion whether to grant motion to strike, district court views pleadings in light most favorable to non-moving party, and resolves any doubt as to relevance of challenged allegations in favor of plaintiff, particularly if moving party demonstrates no resulting prejudice. Fed.Rules Civ.Proc.Rule 12(f), 28 U.S.C.A.

[48] Federal Civil Procedure 170A ↪1126

170A Federal Civil Procedure

170AVII Pleadings and Motions

170AVII(N) Striking Pleading or Matter

Therein

170Ak1125 Immaterial, Irrelevant or Unresponsive Matter

170Ak1126 k. Particular allegations.

Most Cited Cases

District court would strike allegation within complaint alluding to business practices of banks other than those named in investors' action seeking recovery for purported Ponzi scheme, since such practices were immaterial to investors' specific allegations of misconduct, and would serve to prejudice named banks. Fed.Rules Civ.Proc.Rule 12(f), 28 U.S.C.A.

[49] Federal Civil Procedure 170A ↪1126

170A Federal Civil Procedure

170AVII Pleadings and Motions

170AVII(N) Striking Pleading or Matter

Therein

170Ak1125 Immaterial, Irrelevant or Unresponsive Matter

170Ak1126 k. Particular allegations.

Most Cited Cases

District court would strike allegation within complaint alluding to banks' purported motive of "greed" in participating in purported Ponzi scheme, since such statement was immaterial to specific allegations of misconduct. Fed.Rules Civ.Proc.Rule 12(f), 28 U.S.C.A.

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

*1107 R. Alexander Pilmer, Amanda Jane Wong, Christopher Thomas Casamassima, and Richard L. Wynne, Kirkland & Ellis, and Mary E. Newcombe, Caldwell, Leslie, Newcombe & Pettit, Los Angeles, CA, for plaintiffs.

A. William Urquhart, Christopher Tayback and Martin Howard Pritikin, Quinn, Emanuel, Urquhart, Oliver & Hedges, Arya Towfighi, David Lewis Hirsch, and Jamila A. Berridge, McDermott Will & Emery Los Angeles, CA, and Steven L. Bergh, Prenovost, Normandin, Bergh & Dawe, Santa Ana, CA, for defendants.

ORDER GRANTING DEFENDANT COMERICA'S MOTION TO DISMISS THIRD AMENDED COMPLAINT;

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT IMPERIAL'S MOTION TO DISMISS THIRD AMENDED COMPLAINT;

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT UNION BANK OF CALIFORNIA, N.A.'S MOTION TO DISMISS THIRD AMENDED COMPLAINT;

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT BANK OF ORANGE COUNTY'S MOTION TO DISMISS THIRD AMENDED COMPLAINT; AND

ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT CATHERINE MARY LEIDER'S MOTION TO DISMISS THIRD AMENDED COMPLAINT

ORDER GRANTING DEFENDANT UNION BANK OF CALIFORNIA, N.A.'S MOTION TO STRIKE

MORROW, District Judge.

This class action seeks damages from Union Bank of California, Comerica Bank *1108 of California, Imperial Management, Inc., and Bank of Orange County, each of which is alleged to have conspired with Reed Slatkin in effecting a Ponzi scheme that defrauded hundreds of investors out of hundreds of millions of dollars. Plaintiffs allege that these defendants knowingly participated in and facilitated the Ponzi scheme by providing Slatkin

with credit, allowing Slatkin to commingle personal and investor funds, and lending their name and prestige to his operations.

I. FACTUAL BACKGROUND

A. The Alleged Ponzi Scheme

Plaintiffs filed this action in federal court on September 5, 2002, alleging claims for aiding and abetting a breach of fiduciary duty, aiding and abetting fraud, breach of fiduciary duty, fraud, negligent misrepresentation, constructive fraud, negligence and violation of California Business and Professions Code §§ 17200 et seq. Plaintiffs filed a first amended complaint on October 23, 2002, that asserted identical causes of action. Defendants moved to dismiss the first amended complaint. On February 20, 2003, the court granted in part and denied in part defendants' motion to dismiss. Plaintiffs filed a second amended complaint on April 14, 2003. On May 20, 2003, the parties submitted a stipulation that plaintiffs be allowed to file a third amended complaint withdrawing Count XI as well as a request for statutory penalties under California Business & Professions Code § 17200. The court subsequently entered an order on the parties' stipulation.

The third amended complaint defines the putative class plaintiffs seek to represent as "all individuals or entities that (a) made claims in the bankruptcy of Reed E. Slatkin; and (b) received in return less money from Reed E. Slatkin than they entrusted to him to invest." ^{FN1} Additionally, the pleading identifies, by name and amount invested, eighteen individuals and/or entities allegedly defrauded by Slatkin and the banks. ^{FN2} It asserts that each of these "class representatives" falls within the class defined above.

FN1. Third Amended Complaint, ¶ 33.

FN2. *Id.*, ¶¶ 9-26.

Slatkin allegedly began his career as a full-time investment advisor during the mid-1980's, and invested money on behalf of a variety of individuals.

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

FN3 Soon after Slatkin began accepting money from others to invest, he allegedly developed and executed a scheme to defraud those who entrusted their funds to him. FN4 One artifice Slatkin used to carry out the scheme was a limited partnership called the Reed Slatkin Investment Club L.P. FN5 Slatkin was general partner of the Club; its limited partners were individuals who gave Slatkin money to invest on their behalf. FN6 Slatkin actively ran the Club until he filed for bankruptcy on May 1, 2001. FN7 Plaintiffs allege that Slatkin operated a classic Ponzi scheme, FN8 i.e., he used monies paid by later investors to pay artificially high returns to initial investors, with the ultimate goal of attracting still more investors. FN9 In reality, plaintiffs allege, Slatkin's investment portfolio bore little resemblance to the claims he made. FN10 Plaintiffs assert that Slatkin spent investors' money on a lavish lifestyle, commingled investors' funds, and *1109 paid false returns to some investors with the principal paid by others. FN11 Slatkin allegedly received nearly \$600,000,000 from investors; of this, approximately \$250,000,000 has never been returned, and is still owed to class members. FN12

FN3. *Id.*, ¶ 41.FN4. *Id.*, ¶ 41.FN5. *Id.*, ¶ 45.FN6. *Id.*FN7. *Id.*FN8. *Id.*, ¶ 42.FN9. *Id.*FN10. *Id.*FN11. *Id.*FN12. *Id.*, ¶ 44.

B. Allegations Against Defendants

Plaintiffs have sued four separate banking institutions—Union Bank of California, Comerica Bank-

California, Bank of Orange County, and Imperial Management, Inc. (collectively “the Banks”). Defendant Union Bank is sued in its individual capacity and as successor to the trust business of Imperial Trust, which it acquired in May 1999. FN13 Defendant Bank of Orange County is sued as the direct successor-in-interest to Pacific Inland Bank. FN14 Defendant Imperial Management, Inc. is sued as the direct successor-in-interest to Imperial Trust Company. FN15 Defendant Comerica Bank is sued as the successor by merger to Imperial Bank (the prior parent of Imperial Trust) and as the alter-ego of co-defendant Imperial Management, Inc., Comerica's wholly-owned subsidiary. FN16 The liability of all four defendants, therefore, hinges on the alleged conduct of Imperial Trust Company, Pacific Inland Bank and/or Union Bank. Plaintiffs have also sued one individual, Mary Catherine Leider, for wrongful acts and omissions allegedly committed as administrator of accounts that had investments in the Club, first at Pacific Inland, and later at Imperial. FN17

FN13. *Id.*, ¶ 27.FN14. *Id.*, ¶ 31.FN15. *Id.*, ¶ 29.FN16. *Id.*, ¶ 28.FN17. *Id.*, ¶ 32.

Plaintiffs allege that Slatkin's investment scheme depended for its success on the involvement of the defendant Banks. The Banks, or their predecessors-in-interest, allegedly provided Slatkin with three types of assistance: (1) a steady flow of new money; (2) a mechanism for managing investors' custodial accounts; and (3) an aura of legitimacy that allowed the scheme to flourish. FN18 Plaintiffs contend that Slatkin established accounts at the Banks, and induced dozens of investors to transfer millions of dollars to “custodial” or “trustee” accounts there. FN19 Upon receipt of the investors' cash, the Banks allegedly transferred the

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

money into accounts established in the name of the Club. With the Banks' alleged knowledge and assistance, Slatkin then commingled new investors' money with his own and other investors' money. Most of the accounts were held at Pacific Inland Bank, Imperial Trust, and commencing in May 1999, Union Bank. Santa Barbara Bank & Trust held the remaining Club accounts. Plaintiffs further allege that, due to the legitimacy conferred on the scheme by the Banks' involvement, Slatkin convinced individuals to give him money directly.^{FN20}

In addition to lending their prestige to Slatkin, the Banks allegedly vouched for his skill and trustworthiness when asked.^{FN21}

FN18. *Id.*, ¶ 43.

FN19. *Id.*, ¶ 47.

FN20. *Id.*, ¶ 48.

FN21. *Id.*, ¶ 49.

Plaintiffs make numerous specific allegations regarding the conduct of each of the Banks. As respects Imperial and Pacific Inland (Imperial's predecessor-in-interest), the complaint alleges that individual officers*1110 at both Banks acted as salespersons for Slatkin and encouraged individuals to invest with Slatkin.^{FN22} Plaintiffs also contend that individuals at Imperial and Pacific Inland represented to investors that the Club was audited annually, even though neither Bank ever conducted such an audit.^{FN23} They further allege that Imperial failed to certify investors' account statements despite an obligation to do so,^{FN24} and that it purportedly encouraged investors to rely on its official "certified" statements rather than Slatkin's unofficial reports.^{FN25} Plaintiffs allege that Imperial was aware of Slatkin's illegal activities due to the highly unusual nature of the Club.^{FN26} Finally, they assert that Slatkin bribed Mary Catherine Leider, the Club account manager at Imperial, to assist him in the operation of his Ponzi scheme.^{FN27}

FN22. *Id.*, ¶¶ 50-53.

FN23. *Id.*, ¶¶ 54-55.

FN24. *Id.*, ¶¶ 56-57.

FN25. *Id.*, ¶ 61.

FN26. *Id.*, ¶¶ 62-68.

FN27. *Id.*, ¶¶ 69-73.

As respects Union Bank (which acquired Imperial's trust business in May 1999), plaintiffs allege that, like Imperial, it failed properly to value the investments of the class members, and to audit the investments held in Slatkin accounts as it was required to do.^{FN28} They assert that, in violation of its own policies, Union Bank allowed Slatkin to overdraw the Club checking account by hundreds of thousands of dollars,^{FN29} and extended a \$4,000,000 unsecured line of credit to Slatkin in February 2000.^{FN30} Finally, they allege that Union Bank performed "inappropriate favors" for Slatkin to induce him to provide additional business to it.^{FN31} Plaintiffs allege generally that Union Bank knew or should have known of Slatkin's illegal activities.^{FN32}

FN28. *Id.*, ¶¶ 80-83.

FN29. *Id.*, ¶¶ 86-90.

FN30. *Id.*, ¶¶ 92-95.

FN31. *Id.*, ¶ 96.

FN32. *Id.*, ¶ 99.

Plaintiffs argue that all of the Banks "rubber-stamped" the false information Slatkin gave them, and treated the client accounts as "one common pool of fungible and liquid assets."^{FN33} They also allege that each of the Banks, in its own right or through a predecessor-in-interest, actively participated in Slatkin's Ponzi scheme with constructive and/or actual knowledge of his crimes.^{FN34} They maintain that each of the Banks knew or should have known that Slatkin was operating a Ponzi scheme,^{FN35} and that, without the assistance

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

provided by the Banks, Slatkin's Ponzi scheme could not have succeeded.^{FN36}

FN33. *Id.*, ¶¶ 100-103.

FN34. *Id.*, ¶¶ 104-105.

FN35. *Id.*, ¶¶ 106-116.

FN36. *Id.*, ¶ 116.

Based on these allegations, plaintiffs' third amended complaint pleads eleven claims for relief: (1) aiding and abetting a breach of fiduciary duty; (2) aiding and abetting fraud; (3) breach of fiduciary duty; (4) fraud; (5) negligent misrepresentation; (6) constructive fraud; (7) negligence; (8) violation of California Business and Professions Code §§ 17200 et seq.; (9) intentional fraudulent transfer (seven years); (10) intentional fraudulent transfer (four years); and (11) constructive fraudulent transfer (four years). The first two claims are brought by all plaintiffs except Neilson against all defendants. The third, fourth, fifth, sixth and seventh claims are *1111 brought by plaintiffs Fred Ockrim, Sheri Ockrim, and Jaroslav Marik against all defendants, and by plaintiffs Wesley West Flexible Partnership, Stedman Family Partnership, Ltd., Stedman as Trustee of the Neva and Wesley West Foundation, George Kriste, Fred Ockrim, Sheri Ockrim, Jaroslav Marik, and California Community Foundation ("CCF") against all defendants except Bank of Orange County. The eighth claim is brought by all plaintiffs against all defendants. The last three claims are brought by plaintiff Neilson against Union Bank, Comerica Bank and Imperial Management. Plaintiffs seek approximately \$200 million in damages on each of the first two claims, and approximately \$24 million on counts three through eight. As respects the fraudulent transfer claims, plaintiffs seek (a) to avoid any transfer of money by Slatkin to the Banks within a specified seven or four year period ("the Seven-Year Period" and "Four-Year Period" respectively); (b) to impose a constructive trust on any transfer of money from Slatkin within the Seven-Year Period or the

Four-Year Period, or any proceeds of the transfers; and (c) to require the Banks to convey to the Trustee the value of any transfer of money to them by Slatkin with the Seven-Year Period or Four-Year Period, as well as any proceeds of such transfers. Plaintiffs seek attorneys' fees on all counts.

All five defendants have moved to dismiss the third amended complaint. Defendant Comerica Bank asserts that the complaint fails adequately to allege its liability either as the alter ego of Imperial Management or as the successor-in-interest to Imperial Bank. Defendant Imperial Management contends that the aiding and abetting claims and the fraudulent transfer claim that invokes a seven-year reach back period must be dismissed. Defendant Union Bank challenges the aiding and abetting claims and all claims brought by plaintiff Ockrim. Defendant Bank of Orange County seeks dismissal of the claims for aiding and abetting, breach of fiduciary duty, fraud, negligent misrepresentation, constructive fraud, violation of Business & Professions Code § 17200, and all claims brought by Ockrim. Finally, defendant Leider asserts that the claims for aiding and abetting, breach of fiduciary duty, constructive fraud, fraud, and negligent misrepresentation are deficient. As all motions address similar issues, the court considers them jointly in this order.

II. DISCUSSION

A. Legal Standard Governing Motions To Dismiss

A Rule 12(b)(6) motion tests the legal sufficiency of the claims asserted in the complaint. FED.R.CIV.PROC. 12(b)(6). A court may not dismiss a complaint for failure to state a claim "unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45-46, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957). See also *Moore v. City of Costa Mesa*, 886 F.2d 260, 262 (9th Cir.1989); *Haddock v. Board of Dental Examiners*, 777 F.2d 462, 464 (9th Cir.1985) (stating that a court should not dismiss a complaint

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

if it states a claim under any legal theory, even if plaintiff erroneously relies on a different theory). In other words, a Rule 12(b)(6) dismissal is proper only where there is either a “lack of a cognizable legal theory” or “the absence of sufficient facts alleged under a cognizable legal theory.” *Balistreri v. Pacifica Police Dept.*, 901 F.2d 696, 699 (9th Cir.1988).

In deciding a motion to dismiss for failure to state a claim, the court's review is limited to the contents of the complaint. *Campanelli v. Bockrath*, 100 F.3d 1476, 1479 (9th Cir.1996); *1112 *Allarcom Pay Television, Ltd. v. General Instrument Corp.*, 69 F.3d 381, 385 (9th Cir.1995). The court must accept all factual allegations pleaded in the complaint as true, and must construe them and draw all reasonable inferences from them in favor of the nonmoving party. *Cahill v. Liberty Mutual Ins. Co.*, 80 F.3d 336, 337-38 (9th Cir.1996); *Mier v. Owens*, 57 F.3d 747, 750 (9th Cir.1995) (citing *Usher v. City of Los Angeles*, 828 F.2d 556, 561 (9th Cir.1987)); *NL Indus. Inc. v. Kaplan*, 792 F.2d 896, 898 (9th Cir.1986). It need not, however, accept as true unreasonable inferences or conclusory legal allegations cast in the form of factual allegations. *Western Mining Council v. Watt*, 643 F.2d 618, 624 (9th Cir.1981), cert. denied, 454 U.S. 1031, 102 S.Ct. 567, 70 L.Ed.2d 474 (1981).

In addition to the allegations of the complaint, a court may consider exhibits submitted with the complaint, documents whose contents are alleged in the complaint when authenticity is not questioned, and matters that may be judicially noticed pursuant to Federal Rule of Evidence 201.^{FN37} *Branch v. Tunnell*, 14 F.3d 449, 454 (9th Cir.1994), cert. denied, 512 U.S. 1219, 114 S.Ct. 2704, 129 L.Ed.2d 832 (1994), overruled on other grounds, *Galbraith v. County of Santa Clara*, 307 F.3d 1119 (9th Cir.2002); *Hal Roach Studios, Inc. v. Richard Feiner & Co.*, 896 F.2d 1542, 1555, n. 19 (9th Cir.1989).

FN37. Taking judicial notice of matters of public record does not convert a motion to

dismiss into a motion for summary judgment. *MGIC Indemnity Corp. v. Weisman*, 803 F.2d 500, 504 (9th Cir.1986).

B. Defendants' Requests For Judicial Notice

Four of the five defendants have requested that the court take judicial notice of various documents in ruling on their motions.

1. Union Bank

Union Bank has requested that the court take judicial notice of the following documents:

a. Declaration of Reed E. Slatkin in Support of Trustee's *Ex Parte* Application for a Right to Attach Order And Order for Issuance of Writ of Attachment, filed on August 28, 2002, in *In re: Reed Slatkin*, Case No. ND 01-11549-RR (Bankr.C.D.Cal.) (“*Slatkin*”);^{FN38}

FN38. Defendant Union Bank of California's Request for Judicial Notice (“*Union Bank's Req.*”), Exh. A.

b. Complaint for Disallowance (i.e., Objection) and Equitable Subordination of Claim Nos. 437 and 535, and Declaration of Jolynn Runolfson in support thereof, filed in *Slatkin* on April 23, 2003;^{FN39}

FN39. *Id.*, Exh. B.

c. The Second Amended Complaint, dated August 20, 2002, in *Wesley West Flexible Partnership, et al. v. Union Bank of California, et al.*, CV 02-964 RSWL (“*Wesley West*”);^{FN40}

FN40. *Id.*, Exh. C.

d. September 18, 2002, Order in *Christensen v. Union Bank of California, N.A.*, CV 02-608 MMM (CWx) (“*Christensen*”);^{FN41}

FN41. *Id.*, Exh. D.

e. January 6, 2003, Order in *Christensen*;^{FN42}

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

FN42. *Id.*, Exh. E.

f. Disclosure Statement to Accompany Chapter 11 Trustee and Creditors' Committee Joint Plan of Reorganization, dated January 30, 2003, filed in *Slatkin*.^{FN43}

FN43. Defendant Union Bank of California's Second Request for Judicial Notice ("Union Bank's Second Req."), Exh. A.

*1113 g. Stipulation Re: Briefing Schedule for Defendants' Motions to Dismiss Plaintiffs' First Amended Complaint; and [Proposed] Order Thereon, filed October 25, 2002, in this case; FN44

FN44. *Id.*, Exh. B.

h. Stipulation re Filing of Third Amended Complaint and [Proposed] Order, filed May 15, 2003, in this case;^{FN45} and

FN45. *Id.*, Exh. C.

i. Second Amended Complaint, dated October 15, 2002, in *Christensen*.^{FN46}

FN46. *Id.*, Exh. D.

Under the Federal Rules of Evidence, courts may take judicial notice of facts that are not subject to reasonable dispute, either because they are "(1) generally known within the territorial jurisdiction of the trial court or (2) capable of accurate and ready determination by resort to sources whose accuracy cannot be reasonably questioned." FED. R. EVID. 201.

[1][2] Court orders and filings are the type of documents that are properly noticed under the rule. Notice can be taken, however, "only for the limited purpose of recognizing the 'judicial act' that the order represents on the subject matter of the litigation." *United States v. Jones*, 29 F.3d 1549, 1553 (11th Cir.1994) (citing *Liberty Mut. Ins. Co. v. Rotches Pork Packers, Inc.*, 969 F.2d 1384, 1388

(2d Cir.1992)). See also *General Electric Capital Corp. v. Lease Resolution Corp.*, 128 F.3d 1074, 1082, n. 6 (7th Cir.1997) ("We agree that courts generally cannot take notice of findings of fact from other proceedings for the truth [of the matter] asserted therein because these findings are disputable and usually are disputed"); *Goetz v. Capital Factors, Inc.*, 120 F.3d 268, 1997 WL 415340, * 1-2 (9th Cir. July 22, 1997) (Unpub.Disp.) ("although a court may take judicial notice of its own records, it cannot take judicial notice of the truth of the contents of all documents found therein"); *San Luis v. Badgley*, 136 F.Supp.2d 1136, 1146 (E.D.Cal.2000) (quoting *Jones* for the proposition that a court "may take judicial notice of a document filed in another court not for the truth of the matters asserted in the litigation, but rather to establish the fact of such litigation and related filings"). Applying this standard, the court takes judicial notice of the existence and legal effect of the documents submitted by Union Bank.

2. Comerica Bank And Imperial Management, Inc.

Comerica and Imperial have requested that the court take judicial notice of the following documents:

a. The January 6, 2003 transcript of proceedings in *Christensen*;^{FN47}

FN47. Defendants Comerica Bank of California and Imperial Management, Inc.'s Request for Judicial Notice ("Comerica Banks' Req."), Exh. A.

b. The February 20, 2003 Order Granting Motions to Dismiss entered in this case;^{FN48}

FN48. *Id.*, Exh. B.

c. Plaintiff's Opposition to Imperial's Motion to Dismiss First Amended Complaint in this case;^{FN49}

FN49. *Id.*, Exh. C.

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

d. Plaintiff's Opposition to Motion to Strike Portions of the First Amended Complaint in this case;^{FN50}

FN50. *Id.*, Exh. D.

e. Reply of Comerica Bank in Support of Motion to Dismiss Plaintiffs' First Amended Complaint in this case;^{FN51} and

FN51. *Id.*, Exh. E.

*1114 f. The January 6, 2003 transcript of proceedings in this action.^{FN52}

FN52. *Id.*, Exh. F.

For the reasons discussed above, the court takes judicial notice of the existence and legal effect of the documents submitted by Comerica and Imperial.

3. Bank of Orange County

The Bank of Orange County has requested that the court take judicial notice of the following documents:

a. April 2, 2003, Civil Minutes, granting in part Bank of Orange County's Motion to Compel;^{FN53}

FN53. Defendant Bank of Orange County's Request for Judicial Notice ("BOC Req."), Exh. A.

b. April 21, 2003, letter from plaintiff's counsel, Kirkland & Ellis;^{FN54}

FN54. *Id.*, Exh. B.

c. Memorandum and Opinion, filed January 9, 2002, in *Wesley West*;^{FN55}

FN55. *Id.*, Exh. C.

d. Pacific Inland Contract dated December 30, 1992, signed by Joanne Christensen;^{FN56}

FN56. *Id.*, Exh. D.

e. Pacific Inland Contract dated December 16, 1991, signed by Paul Hawken;^{FN57}

FN57. *Id.*, Exh. E.

f. Pacific Inland Contract dated June 24, 1991, signed by Thomas Rook;^{FN58} and

FN58. *Id.*, Exh. F.

g. Order Granting in Part and Denying in Part Defendant Union Bank of California's Motion to Dismiss the Second Amended Complaint in *Christensen*.^{FN59}

FN59. *Id.*, Exh. G.

[3][4] For the reasons stated earlier, the court takes judicial notice of the existence and legal effect of the documents identified in paragraphs a, c, and g. The court may also take judicial notice of the documents identified in paragraphs d, e, and f, as these are contracts between Pacific Inland Bank and putative class members that provide the foundation for plaintiffs' claims. "[A] district court ruling on a motion to dismiss may consider a document the authenticity of which is not contested, and upon which the plaintiff's complaint necessarily relies." *Parrino v. FHP, Inc.*, 146 F.3d 699, 706 (9th Cir.1998). As the *Parrino* court explained: "Although we have yet to apply this rule to documents crucial to the plaintiff's claims, but not explicitly incorporated in his complaint, such an extension is supported by the policy concern underlying the rule: preventing plaintiffs from surviving a Rule 12(b)(6) motion by deliberately omitting references to documents upon which their claims are based." *Id.* See also *Cortec Indus., Inc. v. Sum Holding L.P.*, 949 F.2d 42, 47 (2d Cir.1991) ("... we have held that when a plaintiff chooses not to attach to the complaint or incorporate by reference a prospectus upon which it solely relies and which is integral to the complaint, the defendant may produce the prospectus when attacking the complaint for its failure to state a claim, because plaintiff should not

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

so easily be allowed to escape the consequences of its own failure”); *In re Northpoint Communications Group, Inc., Securities Litigation*, 221 F.Supp.2d 1090, 1095 (N.D.Cal.2002) (“In ruling on a motion to dismiss, a court may take judicial notice of a document if it is relied on in the complaint (regardless of whether it is expressly incorporated therein) and its authenticity is not disputed,” citing *Parrino*); *Springgate v. Weighmasters Murphy, Inc. Money Purchase Pension Plan*, 217 F.Supp.2d 1007, 1013 (C.D.Cal.2002) (“For *1115 purposes of this Motion to Dismiss, this Court takes judicial notice of documents (1) and (2) only because these documents’ contents are alleged in the Complaint, and their authenticity is not in question”).

[5] The April 21, 2003, letter from Kirkland & Ellis, however, identified in paragraph b, is not a proper subject of judicial notice. Its contents are not alleged in the third amended complaint and its authenticity is not undisputed. Compare *In re Amylin Pharmaceuticals, Inc., Securities Litigation*, No. 01CV1455BTM(NLS), 2002 WL 31520051, * 2 (S.D.Cal. Oct.10, 2002) (“Plaintiffs do not dispute the letter’s authenticity and rely upon it implicitly in their [consolidated complaint] and in their opposition papers. The court may therefore take judicial notice of the October, 2001 letter”). Nor does it concern matters generally known within the court’s territorial jurisdiction or capable of accurate and ready determination by resort to sources whose accuracy cannot be reasonably questioned. FED. R. EVID. 201. Accordingly, the Bank of Orange County’s motion for judicial notice of the Kirkland & Ellis letter is denied.

C. Comerica’s Motion to Dismiss

Comerica argues that the claims against it must be dismissed because plaintiffs fail adequately to allege that Comerica is the alter ego of, and successor-in-interest to, Imperial Management, its wholly owned subsidiary.

1. Legal Standards Governing The Alter Ego Doctrine

[6] “The alter ego doctrine arises when a

plaintiff comes into court claiming that an opposing party is using the corporate form unjustly and in derogation of the plaintiff’s interests. In certain circumstances the court will disregard the corporate entity and will hold the individual shareholders liable for the actions of the corporation.” *Mesler v. Bragg Management Co.*, 39 Cal.3d 290, 300, 216 Cal.Rptr. 443, 702 P.2d 601 (1985). The purpose of the doctrine is to bypass the corporate entity for the purpose of avoiding injustice. Its “essence... is that justice be done[,] ... [and t]hus the corporate form will be disregarded only in narrowly defined circumstances and only when the ends of justice so require.” *Id.* at 301, 216 Cal.Rptr. 443, 702 P.2d 601. See also *Roman Catholic Archbishop of San Francisco v. Superior Court*, 15 Cal.App.3d 405, 411, 93 Cal.Rptr. 338 (1971) (“The terminology ‘alter ego’ or ‘piercing the corporate veil’ refers to situations where there has been an abuse of corporate privilege, because of which the equitable owner of a corporation will be held liable for the actions of the corporation,” citing *Minton v. Cavaney*, 56 Cal.2d 576, 579, 15 Cal.Rptr. 641, 364 P.2d 473 (1961)).

[7] Before the doctrine may be invoked, two elements must be alleged: “First, there must be such a unity of interest and ownership between the corporation and its equitable owner that the separate personalities of the corporation and the shareholder do not in reality exist. Second, there must be an inequitable result if the acts in question are treated as those of the corporation alone.” *Sonora Diamond Corp. v. Superior Court*, 83 Cal.App.4th 523, 526, 99 Cal.Rptr.2d 824 (2000); *Mesler, supra*, 39 Cal.3d at 300, 216 Cal.Rptr. 443, 702 P.2d 601 (“There is no litmus test to determine when the corporate veil will be pierced; rather the result will depend on the circumstances of each particular case. There are, nevertheless, two general requirements: ‘(1) that there be such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist and (2) that, if the acts are treated as those of the corporation alone, an inequitable result *1116 will follow.’ ”

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

quoting *Automotriz Del Golfo De California S. A. De C. V. v. Resnick*, 47 Cal.2d 792, 796, 306 P.2d 1 (1957)). See also *AT & T v. Compagnie Bruxelles Lambert*, 94 F.3d 586, 591 (9th Cir.1996).

[8] “[O]nly a difference in wording is used in stating the ... concept where the entity sought to be held liable is another corporation instead of an individual.” *Las Palmas Associates v. Las Palmas Center Associates*, 235 Cal.App.3d 1220, 1249, 1 Cal.Rptr.2d 301 (1991). Like other shareholders, a parent company is presumed to have an existence separate from its subsidiaries. Accordingly, the mere fact that it owns the stock of the subsidiary will not suffice to prove that the two entities are alter egos of one another; rather, the evidence must show that the wholly-owned subsidiary is merely a conduit for, or is financially dependent on, the parent corporation. *Institute of Veterinary Pathology, Inc. v. California Health Laboratories, Inc.*, 116 Cal.App.3d 111, 119, 172 Cal.Rptr. 74 (1981) (“With increasing frequency, courts have demonstrated a readiness to disregard the corporate entity when a wholly owned subsidiary is merely a conduit for, or is financially dependent on, a parent corporation. In the interests of justice and to prevent fraud, the courts will ignore the existence of a corporate entity used to cut off either causes of action against or defenses by another corporate entity,” quoting 1A Ballantine & Sterling, CALIFORNIA CORPORATION LAWS, § 296.02, pp. 14-32.1-14-33 (4th ed.1980)).

[9] Conclusory allegations of “alter ego” status are insufficient to state a claim. Rather, a plaintiff must allege specifically both of the elements of alter ego liability, as well as facts supporting each. *In re Currency Conversion Fee Antitrust Litigation*, 265 F.Supp.2d 385, 426 (S.D.N.Y.2003) (“These purely conclusory allegations cannot suffice to state a claim based on veil-piercing or alter-ego liability, even under the liberal notice pleading standard”); *Wady v. Provident Life and Accident Ins. Co. of America*, 216 F.Supp.2d 1060, 1067 (C.D.Cal.2002) (“More pertinent for purposes of

the current discussion, none [of the allegations] contains any reference to UnumProvident being the alter ego of Provident. None alleges that UnumProvident treats the assets of Provident as its own, that it commingles funds with Provident, that it controls the finances of Provident, that it shares officers or directors with Provident, that Provident is undercapitalized, or that the separateness of the subsidiary has ceased. Without such allegations, the issue is not adequately raised, and UnumProvident was not put on notice that this was a theory against which it should be prepared to defend”); *Kingdom 5-KR-41, Ltd. v. Star Cruises PLC*, No. 01 Civ. 2946(AGS), 2002 WL 432390, * 12 (S.D.N.Y. Mar.20, 2002) (“[I]n order to overcome the presumption of separateness afforded to related corporations, [plaintiff] is required to plead more specific facts supporting its claims, not mere conclusory allegations”); *Hokama v. E.F. Hutton & Co., Inc.*, 566 F.Supp. 636, 647 (C.D.Cal.1983) (“Defendants further argue that plaintiffs cannot circumvent the requirements for secondary liability by blandly alleging that Madgett, Consolidated, and Frane are ‘alter egos’ of other defendants accused of committing primary violations. This point is well taken.... If plaintiffs wish to pursue such a theory of liability, they must allege the elements of the doctrine. Conclusory allegations of alter ego status such as those made in the present complaint are not sufficient”).

2. Whether The Complaint Sufficiently Alleges Liability Against Comerica

[10] Comerica does not dispute that the complaint adequately alleges the first element of alter ego liability—unity of interest or ownership. Rather, it asserts *1117 that the pleading fails adequately to allege that plaintiffs will suffer cognizable injustice if the court treats Imperial Management's acts as the acts of that entity alone. The third amended complaint plainly alleges that an inequitable result will follow if Imperial Management's acts are treated as its acts alone. It states: “[B]ecause Imperial Management is a mere instrumentality of Comerica Bank-California, an inequitable result would occur

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

if Comerica Bank-California is not a defendant in this action.”^{FN60} The complaint fails to allege facts supporting this statement, however.

FN60. *Id.*, ¶ 29.

Plaintiffs assert that the failure to join Comerica would be inequitable because Imperial Management does not have sufficient assets to pay the liabilities it will incur if plaintiffs prevail at trial. California courts have rejected the view that the potential difficulty a plaintiff faces collecting a judgment is an inequitable result that warrants application of the alter ego doctrine. *Virtualmagic Asia, Inc. v. Fil-Cartoons, Inc.*, 99 Cal.App.4th 228, 245, 121 Cal.Rptr.2d 1 (2002) (“[A]lter ego will not be applied absent evidence that an injustice would result from the recognition of separate corporate identities, and ‘[d]ifficulty in enforcing a judgment or collecting a debt does not satisfy this standard,’ ” quoting *Sonora Diamond Corp.*, *supra*, 83 Cal.App.4th at 539, 99 Cal.Rptr.2d 824); *Mid-Century Ins. Co. v. Gardner*, 9 Cal.App.4th 1205, 1213, 11 Cal.Rptr.2d 918 (1992) (“ ‘Certainly, it is not sufficient to merely show that a creditor will remain unsatisfied if the corporate veil is not pierced,’ and thus set up such an unhappy circumstance as proof of an ‘inequitable result. In almost every instance where a plaintiff has attempted to invoke the doctrine he is an unsatisfied creditor,’ ” quoting *Associated Vendors, Inc. v. Oakland Meat Co.*, 210 Cal.App.2d 825, 842, 26 Cal.Rptr. 806 (1962)). Rather, California courts generally require some evidence of bad faith conduct on the part of defendants before concluding that an inequitable result justifies an alter ego finding. *Mid-Century Ins. Co.*, *supra*, 9 Cal.App.4th at 1213, 11 Cal.Rptr.2d 918 (“ ‘The purpose of the doctrine is not to protect every unsatisfied creditor, but rather to afford him protection, where some conduct amounting to bad faith makes it inequitable, under the applicable rule above cited, for the equitable owner of a corporation to hide behind its corporate veil,’ ” quoting *Associated Vendors*, *supra*, 210 Cal.App.2d at 842, 26 Cal.Rptr. 806).

Here, the complaint fails to allege that Comerica engaged in any bad faith conduct in its acquisition and/or management of Imperial. While plaintiffs cite several cases in which the corporate veil was pierced due to the inadequate initial capitalization of an entity,^{FN61} or the draining of *1118 corporate assets after initial capitalization,^{FN62} the complaint does not allege that Comerica is guilty of either practice. Comerica was not involved in the incorporation of Imperial Management, and thus cannot be held liable for any initial undercapitalization of the company. Additionally, the complaint does not allege that Comerica deliberately drained Imperial Management of assets. Rather, plaintiffs allege only that Imperial does not presently have sufficient funds to pay a money judgment in this case. This is not adequate under California law to allege that an inequitable result will follow if the corporate veil is not pierced. Accordingly, the court finds that plaintiffs have failed adequately to allege that Comerica is liable as the alter ego of Imperial Management. Since the complaint does not sufficiently allege Comerica's liability on an alter ego theory, the claims against it must be dismissed. Moreover, since plaintiffs have had three opportunities to state claims against Comerica, the dismissal will be with prejudice.

FN61. See, e.g., *Slottow v. American Cas. Co. of Reading, Pennsylvania*, 10 F.3d 1355, 1360 (9th Cir.1993) (“FNT's initial capitalization of \$500,000 was woefully inadequate for a corporation that handled trust agreements of the magnitude involved here. The investors claimed damages in the range of \$10,000,000; the case settled for nearly half that. Under California law, inadequate capitalization of a subsidiary may alone be a basis for holding the parent corporation liable for acts of the subsidiary”); *Automotriz Del Golfo De California S.A. De C.V. v. Resnick*, 47 Cal.2d 792, 797, 306 P.2d 1 (1957) (“If a corporation is organized and carries on business without substantial capital in such a way that the

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

corporation is likely to have no sufficient assets available to meet its debts, it is inequitable that shareholders should set up such a flimsy organization to escape personal liability.... [E]ven if the court believed defendants' testimony in this regard, it could have inferred that \$5,000 was an insufficient capital investment in view of the volume of business conducted"); *United States v. Healthwin-Midtown Convalescent Hospital and Rehabilitation Center, Inc.*, 511 F.Supp. 416, 419 (C.D.Cal.1981) ("Zide himself testified that the corporation was undercapitalized. This testimony was confirmed by further evidence which established that although Healthwin consistently had outstanding liabilities in excess of \$150,000, its initial capitalization was only \$10,000"); *Linco Services, Inc. v. DuPont*, 239 Cal.App.2d 841, 844, 49 Cal.Rptr. 196 (1966) ("DuPont's participation did enable defendant corporation to return to active business, without capital stock and with inadequate financing. This resumption, in turn, invited the public generally to deal with the unsound corporation, and plaintiff did so to its loss").

FN62. *RRX Industries, Inc. v. Lab-Con, Inc.*, 772 F.2d 543, 546 (9th Cir.1985) ("TEKA transferred all of its software and licenses to Lab-Con for no consideration. Following the transfer, TEKA was simply an empty shell, which the district court properly disregarded").

D. Whether The Complaint Adequately Pleads Aiding And Abetting

[11] Plaintiffs' first and second claims for relief plead the aiding and abetting of a breach of fiduciary duty and the aiding and abetting of fraud respectively. Under California law, "[l]iability may ... be imposed on one who aids and abets the commission of an intentional tort if the person (a) knows

the other's conduct constitutes a breach of duty and gives substantial assistance or encouragement to the other to so act or (b) gives substantial assistance to the other in accomplishing a tortious result and the person's own conduct, separately considered, constitutes a breach of duty to the third person." See *Fiol v. Doellstedt*, 50 Cal.App.4th 1318, 1325-26, 58 Cal.Rptr.2d 308 (1996) (citing *Saunders v. Superior Court*, 27 Cal.App.4th 832, 846, 33 Cal.Rptr.2d 438 (1994), and REST. 2D TORTS, § 876).

Plaintiffs' aiding and abetting claims are brought against all defendants. Defendants collectively mount four attacks on the claims: (1) that the complaint fails adequately to plead that defendants knew of Slatkin's fraudulent scheme; (2) that it fails to plead defendants acted for financial gain as required by California law; (3) that it fails to allege substantial assistance by defendant Leider; and (4) that it fails to allege Leider owed plaintiffs an independent fiduciary duty. The court evaluates each argument in turn.

1. Whether The Complaint Adequately Pleads "Knowledge"

Defendants argue that plaintiffs' aiding and abetting claims are deficient because they fail adequately to allege that defendants had actual knowledge of Slatkin's fraudulent activities. In the first amended complaint, plaintiffs alleged that the Banks "knew or should have known" of Slatkin's fraud. The court found such an allegation insufficient because California law requires *1119 that a defendant have actual knowledge of tortious activity before it can be held liable as an aider and abettor, and federal courts have found that the phrase "knew or should have known" does not plead actual knowledge. The aiding and abetting claims were thus dismissed with leave to amend. Consistent with the court's earlier order, the third amended complaint deletes all references to defendants' constructive knowledge. It asserts, for example, that

"Pacific Inland and Imperial knew that Slatkin was in fact engaged in actions amounting to fraud

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

and breach of his fiduciary duty to all Class Members.” FN63

FN63. First Amended Complaint, ¶ 76.

“Each Bank, in its own right or through its predecessor in interest, actively participated in Slatkin’s Ponzi scheme with actual knowledge of Slatkin’s crimes.” FN64

FN64. *Id.*, ¶ 101.

“The Banks knew that Slatkin was violating his fiduciary duties to his clients and the Club and actively participated in his operation of the Ponzi scheme.” FN65

FN65. *Id.*, ¶ 124.

“The Banks knew that Slatkin was engaging in fraud.” FN66

FN66. *Id.*, ¶ 128.

“Ms. Leider knew that Slatkin was breaching fiduciary duties he owed to Club members and committing fraud.” FN67

FN67. *Id.*, ¶ 72.

Defendants contend these allegations do not cure the earlier deficiency, because they fail to allege actual knowledge of the underlying wrong Slatkin committed. Plaintiffs counter (1) that it is not necessary to plead actual knowledge of a specific underlying wrong; and (2) that even if such an allegation is required, the complaint adequately pleads actual knowledge of specific tortious conduct on Slatkin’s part.

[12][13] Under Rule 9(b) of the Federal Rules of Civil Procedure, while fraud must be pled with specificity, “[m]alice, intent, knowledge, and other condition of mind of a person may be averred generally.” FED.R.CIV.PROC. 9(b). Although this obviates the necessity of pleading detailed facts supporting allegations of knowledge, it does not relieve

a pleader of the burden of alleging the nature of the knowledge a defendant purportedly possessed. In the case of an aider and abettor under California law, this must be actual knowledge of the primary violation. *Howard v. Superior Court*, 2 Cal.App.4th 745, 749, 3 Cal.Rptr.2d 575 (1992) (“while aiding and abetting may not require a defendant to agree to join the wrongful conduct, it necessarily requires a defendant to reach a *conscious decision* to participate in tortious activity for the purpose of assisting another in performing a wrongful act” (emphasis added)); *Gerard v. Ross*, 204 Cal.App.3d 968, 983, 251 Cal.Rptr. 604 (1988) (“A defendant can be held liable as a cotortfeasor on the basis of acting in concert only if he or she *knew* that a tort had been, or was to be, committed, and acted with the intent of facilitating the commission of that tort”). See also *Cope v. Price Waterhouse*, 990 F.2d 1256, 1993 WL 102598, * 6 (9th Cir. Apr.7, 1993) (Unpub.Disp.) (“In a case of secondary liability for common law fraud, the California Supreme Court held that ‘[t]he words “aid and abet” ... have a well understood meaning, and may fairly be construed to imply an intentional participation with knowledge of the object to be attained.’ ... The Second Restatement of Torts also supports a finding that actual knowledge is the proper standard for a claim of aiding and abetting fraud. Section 876(b) provides for secondary liability for tortious conduct if a party ‘knows that the other’s conduct constitutes a breach of *1120 duty and gives substantial assistance or encouragement to the other so to conduct himself.’ ... Other subsections indicate that the term ‘knows’ does not include both actual knowledge and recklessness. When the drafters of the Restatement meant to include recklessness as an element of liability, they did so explicitly”); *Resolution Trust Corp. v. Rowe*, No. C 90-20114 BAC, 1993 WL 183512, * 5 (N.D.Cal. Feb.8, 1993) (“Under California law, actual knowledge and intent are required to impose aiding and abetting liability,” citing *Gerard, supra*, 204 Cal.App.3d at 983, 251 Cal.Rptr. 604); *Hashimoto v. Clark*, 264 B.R. 585, 598 (D.Ariz.2001) (holding under California law that “[t]he requisite degree of knowledge for an aid-

ing and abetting claim is actual knowledge. This means Trustee must come forward with evidence to show that Safrabank knew Clark was breaching a duty owed Sheffield”).

The question is whether plaintiffs' allegations satisfy this standard. Generally, courts have found pleadings sufficient if they allege generally that defendants had actual knowledge of a specific primary violation. See *Dubai Islamic Bank v. Citibank, N.A.*, 256 F.Supp.2d 158, 167 (S.D.N.Y.2003) (holding that a complaint asserting that “ ‘Citibank, through its officers and employees, ... actually knew of and participated in the unlawful scheme to steal from DIB and launder the money stolen from DIB’ ... sufficiently allege [d] that Citibank had actual knowledge”); *In re Sharp Intern. Corp.*, 281 B.R. 506, 513 (Bankr.E.D.N.Y.2002) (“To analyze the sufficiency of Sharp's pleading, it is necessary to identify precisely the breach of fiduciary duty for which Sharp seeks to hold State Street liable ... Sharp's pleading falls short of alleging that State Street had actual knowledge of the Spitzes' diversion of monies from Sharp”); *Bogart v. National Community Banks, Inc.*, Civ. A. No. 90-5032, 1992 WL 203788, * 8 (D.N.J. Apr.25, 1992) (holding that plaintiff had adequately pleaded the actual knowledge element of an aiding and abetting claim because “Rule 9(b) clearly provides that ‘intent, knowledge, and other condition of mind of a person may be averred generally.’ ... Rule 9(b) is satisfied where plaintiff ‘alleges generally that defendants had actual knowledge of the materially false and misleading statements and omissions ... or acted with reckless disregard for the truth.’ ... Plaintiff has met this standard”); *Smith v. Network Equipment Technologies, Inc.*, Nos. C-90-1138 DLJ, C-90-1281 DLJ and C-90-1372 DLJ, 1990 WL 263846, * 7 (N.D.Cal. Oct.19, 1990) (citing *In re Thortec Securities Litigation*, [1989 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 94,330, 1989 WL 67429 (N.D.Cal.1989), for the proposition that a “general averment of actual knowledge [is] sufficient to plead a claim of aiding and abetting liability”).

[14] Applying this standard, the complaint adequately pleads that defendants had actual knowledge of the primary violation committed by Slatkin. The complaint asserts that the Banks knew Slatkin was committing fraud and was breaching his fiduciary duties to class members. It also alleges that each bank actively participated in Slatkin's Ponzi scheme with knowledge of his crimes. Slatkin's crime, of course, was the operation of a Ponzi scheme that defrauded hundreds of investors and caused losses of hundreds of millions of dollars. The complaint details the manner in which the Ponzi scheme operated, describes Slatkin's fraudulent transactions, and outlines the Banks' involvement in these activities. It alleges, in particular, that the Banks utilized atypical banking procedures to service Slatkin's accounts, raising an inference that they knew of the Ponzi scheme and sought to accommodate it by altering their normal ways of doing business. This supports the general allegations of knowledge. See, e.g., *1121 *Aetna Casualty and Surety Co. v. Leahey Construction Co.*, 219 F.3d 519, 536 (6th Cir.2000) (“... although short-term lending may be ‘commonplace,’ the details of this particular loan (e.g., its four-day duration straddling the July 1996 month end) were highly unusual”); *Camp v. Dema*, 948 F.2d 455, 459 (8th Cir.1991) (“A party who engages in atypical business transactions or actions which lack business justification may be found liable as an aider and abettor with a minimal showing of knowledge,” citing *Woods v. Barnett Bank of Fort Lauderdale*, 765 F.2d 1004, 1010 (11th Cir.1985)); *Woodward v. Metro Bank of Dallas*, 522 F.2d 84, 97 (5th Cir.1975) (“Conversely, if the method or transaction is atypical or lacks business justification, it may be possible to infer the knowledge necessary for aiding and abetting liability”). While it is true the complaint does not directly state that the Banks knew Slatkin was running a Ponzi scheme and stealing investor funds, this is the net effect of allegations that the Banks knew of Slatkin's “fraud,” “actively participated” in the Ponzi scheme with knowledge of his “crimes,” and accommodated him by using atypical banking procedures to service his accounts.

The Banks argue that the pleading is insufficient because multiple types of “fraud” are alleged in the complaint. “Crimes,” they assert, could refer to Slatkin's failure to register as an investment advisor or to his overdrawing of accounts, both of which are alleged in the complaint. To the extent this is the reference, the Banks maintain, the allegations are wholly insufficient, as plaintiffs do not allege that they have suffered damage as a result of these misdeeds on Slatkin's part.^{FN68} The complaint, however, references “crimes” in the context of an allegation that directly concerns Slatkin's Ponzi scheme, and asserts the Banks actively participated in it. Read liberally, as it must be for purposes of a Rule 12(b)(6) motion, this allegation pleads that the Banks knew of the Ponzi scheme. See *Aetna Casualty and Surety Co.*, *supra*, 219 F.3d at 533-34 (“If one is aware that he has a role in an improper activity, ... then surely he knows that the primary party's conduct is tortious”). The Banks' reading to the contrary seeks to parse the pleading too finely for Rule 8 purposes.

FN68. Defendants assert that plaintiffs simply replaced allegations found in their earlier complaint that the Banks “knew or should have known” of various of Slatkin's activities with allegations of knowledge in this complaint. They find it suspicious that virtually all of the relevant allegations were amended in this fashion except one asserting that the Banks knew or should have known of Slatkin's Ponzi scheme, and make much of the fact that the current complaint contains no allegation that the Banks knew of the scheme. While the Banks' belief that plaintiffs cannot show actual knowledge may ultimately prove to be true, the allegation that the Banks “actively participated in Slatkin's Ponzi scheme with actual knowledge of his crimes” suffices to allege their knowledge of the Ponzi scheme.

This is particularly true when one considers the

detail with which Slatkin's underlying wrong and the Banks' substantial assistance is pled. See, e.g., *Cromer Finance Ltd. v. Berger*, 137 F.Supp.2d 452, 494 (S.D.N.Y.2001) (“To satisfy the knowledge requirement of these claims, New York law requires that a defendant have ‘actual knowledge’ of the underlying fraud. ... The defendant's knowledge and intent, however, need only be ‘averred generally.’ ... A plaintiff satisfies the scienter pleading requirement where it identifies ‘circumstances indicating conscious behavior by the defendant,’ ... or a clear opportunity and a motive to aid the fraud”). Defendants cite no cases to the contrary.^{FN69} *1122 Accordingly, the court finds that the complaint adequately pleads the Banks' actual knowledge of Slatkin's underlying fraud, and denies their motion to dismiss the aiding and abetting claims on this basis.^{FN70}

FN69. Defendants rely heavily on *In re Sharp Intern. Corp.*, *supra*, 281 B.R. 506, which dismissed an aiding and abetting claim for failure to plead the underlying breach of fiduciary duty specifically. *Sharp* is distinguishable, as there, the complaint as a whole failed to allege the nature of the underlying wrong. Here, by contrast, the complaint clearly sets forth the nature of the underlying wrong.

FN70. Defendants argued at the hearing that even if the complaint adequately alleges actual knowledge of Slatkin's defrauding of account holders, it fails to allege actual knowledge of Slatkin's defrauding of non-account holders. The court disagrees. The complaint specifically pleads that the Banks had actual knowledge of the fraudulent activities that Slatkin perpetrated on all of his clients, including non-account holders. (See Third Amended Complaint, ¶ 76) (“... Pacific Inland and Imperial knew that Slatkin was in fact engaged in actions amounting to fraud and breach of his fiduciary duty to *all Class*

Members ” (emphasis added)); *id.*, ¶ 124 (“The Banks knew that Slatkin was violating his fiduciary duties to *his clients* and the Club and actively participated in his operation of the Ponzi scheme” (emphasis added)). Moreover, the complaint alleges that the Banks had knowledge of Slatkin’s Ponzi scheme. *Id.*, ¶ 101 (“Each Bank, in its own right or through its predecessor in interest, actively participated in Slatkin’s Ponzi scheme with actual knowledge of Slatkin’s crimes”). Since the Ponzi scheme allegedly encompassed both account holders and non-account holders, the allegations in combination sufficiently plead knowledge of Slatkin’s defrauding of non-account holders. Cf. *LaSalle Nat. Bank v. Duff & Phelps Credit Rating Co.*, 951 F.Supp. 1071, 1093 (S.D.N.Y.1996) (“[T]he complaint alleges that Duff & Phelps participated in Towers’ Ponzi scheme by assigning the inflated rating of ‘AA’ (or ‘AA+’) to the Bonds.... Duff & Phelps argues that plaintiffs’ claim fails because plaintiffs have not alleged that Duff & Phelps had knowledge of the identity of each individual purchaser.... Knowledge of the identity of each particular plaintiff is not necessary, however, if the defendant’s representation is designed to target a ‘select group of qualified investors’ rather than ‘the public at large.’ ... Plaintiffs have adequately alleged that Duff & Phelps knew that a select group of qualified investors would rely on the inaccurate rating contained in the Offering Memoranda. Duff & Phelps expressly consented to the use of its Bond rating in the Offering Memoranda. Moreover, Duff & Phelps was in direct contact with at least some of the plaintiffs, and with the broker dealers selling the Bonds. Thus, Duff & Phelps knew that its misrepresentations were being circulated in a private placement memoranda to a select group of potential

investors,” quoting *Schwartz v. Michaels*, No. 91 CIV. 3538(RPP), 1992 WL 184527, * 32 (S.D.N.Y. July 23, 1992)). While it may ultimately prove to be the case that the Banks did not know Slatkin had investors other than the account holders, the court must, for purposes of this motion, accept as true the allegations to the contrary contained in plaintiffs’ third amended complaint.

2. Whether The Complaint Adequately Pleads “Financial Gain”

The Banks next argue that the claim for aiding and abetting a breach of fiduciary duty fails because it does not adequately plead that they participated in the breach for financial gain or advantage. California courts have generally held that, to hold a non-fiduciary liable for aiding and abetting a fiduciary’s breach of his duties, the non-fiduciary must have participated in the breach for personal gain or in furtherance of its own financial advantage. See *Doctors’ Co. v. Superior Court*, 49 Cal.3d 39, 47, 260 Cal.Rptr. 183, 775 P.2d 508 (1989).

In the first amended complaint, plaintiffs alleged that the Banks acted for their own financial advantage because they received substantial fees from Slatkin and his investors. The court found that this did not adequately plead financial gain, citing the fact that California courts uniformly hold that ordinary fees, even fees calculated on the basis of the amount of assets held in an account, do not satisfy the “personal gain or financial advantage” requirement. Consistent with the court’s order, plaintiffs amended the complaint to allege new facts regarding the financial *1123 gain defendants obtained through their dealings with Slatkin. Defendants assert that these new allegations remain inadequate.

Plaintiffs counter (1) that financial gain is not a required element for aiding and abetting liability under California law;^{FN71} (2) that the complaint nonetheless adequately alleges conduct by the Banks in furtherance of their own financial advantage.

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

age; and (3) that the bribes Slatkin allegedly paid to Leider are properly imputed to the Banks under the doctrine of respondeat superior, and constitute financial gain.

FN71. Plaintiffs' opposition to defendants' earlier motions to dismiss did not dispute that they were required to plead financial gain to state an aiding and abetting claim against a non-fiduciary under California law, and the court so held in its prior order. Plaintiffs' present assertion that financial gain is not an element of the tort essentially seeks reconsideration of the earlier ruling. Plaintiffs have not made a proper motion for reconsideration, nor have they shown that they are entitled to reconsideration. Before reconsideration is appropriate, a party must demonstrate

“(a) a material difference in fact or law from that presented to the Court before such decision that in the exercise of reasonable diligence could not have been known to the party moving for reconsideration at the time of such decision, or (b) the emergence of new material facts or a change of law occurring after the time of such decision, or (c) a manifest showing of a failure to consider material facts presented to the Court before such decision. No motion for reconsideration shall in any manner repeat any oral or written argument made in support of or in opposition to the original motion.” CA CD L.R. 7-18.

Plaintiffs have not shown a material difference in law or fact, the emergence of new law or facts, or a manifest failure by the court to consider material facts presented by plaintiffs, and the court could properly refuse to consider plaintiffs' new arguments as a consequence. To ensure that its initial decision was not infected by error as a res-

ult of plaintiffs' failure to raise the issue, however, the court has elected to address the argument on the merits. See also *School Dist. No. 1J, Multnomah County v. ACandS Inc.*, 5 F.3d 1255, 1263 (9th Cir.1993) (“reconsideration is appropriate if the district court (1) is presented with newly discovered evidence, (2) committed clear error or the initial decision was manifestly unjust, or (3) if there is an intervening change in controlling law”).

Plaintiffs argue first that financial gain is not a required element of all aiding and abetting claims. Rather, they assert that the need to plead and prove financial gain arises only in cases alleging wrongful conduct by an agent or employee of a fiduciary. Additionally, they maintain that including financial gain as an element of aiding and abetting a breach of fiduciary duty confuses that tort with conspiracy. Finally, plaintiffs contend that, because California has adopted the Restatement definition of aiding and abetting, which does not include a “financial gain” requirement, it is not an element of the tort. The court evaluates each argument in turn.

[15] Plaintiffs first argue that the financial gain requirement constitutes an exception to the agent's immunity rule, and thus does not apply where the defendant is not an agent of the party responsible for the underlying harm. The agent's immunity rule provides that duly acting agents and employees cannot be held liable for conspiring with their principals. *Doctors' Co.*, *supra*, 49 Cal.3d at 45, 260 Cal.Rptr. 183, 775 P.2d 508 (“This rule ... ‘derives from the principle that ordinarily corporate agents and employees acting for and on behalf of the corporation cannot be held liable for inducing a breach of the corporation's contract since being in a confidential relationship to the corporation their action in this respect is privileged,’ ” quoting *Wise v. Southern Pacific Co.*, 223 Cal.App.2d 50, 72, 35 Cal.Rptr. 652 (1963)).

[16] The rule does not apply where the agent

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

acts for his or her own financial gain. See *id.* at 47, *1124260 Cal.Rptr. 183, 775 P.2d 508 (the rule “does not preclude the subjection of agents to conspiracy liability for conduct which the agents carry out ‘as individuals for their individual advantage’ and not solely on behalf of the principal.... Since the nonfiduciary defendants ... acted not simply as agents or employees of the fiduciary defendants but rather in furtherance of their own financial gain, they could not have been relieved from liability under the [agent’s immunity rule]”). See also *Skarbrevik v. Cohen, England & Whitfield*, 231 Cal.App.3d 692, 710, 282 Cal.Rptr. 627 (1991) (applying *Doctors’ Co.* to reverse a verdict against an attorney where the facts at trial established that the attorney received no more than ordinary fees for legal work performed for the client company); *Wolf v. Mitchell, Silberberg & Knupp*, 76 Cal.App.4th 1030, 1040, 90 Cal.Rptr.2d 792 (1999) (holding that a beneficiary had standing to sue a trustee’s attorneys where the attorneys were alleged to have actively concealed the dissipation of trust assets in order to keep receiving a greater amount of the fees than they would have otherwise); *Pierce v. Lyman*, 1 Cal.App.4th 1093, 1104-06, 3 Cal.Rptr.2d 236 (1991) (applying *Doctors’ Co.* to reverse the dismissal of a complaint on demurrer where the complaint alleged that attorneys for a trust had engaged in misrepresentations, concealment and self-dealing for personal financial gain).

The question is whether these cases, which clearly applied the financial gain requirement as an exception to the agent’s immunity rule, mandate a finding that it is properly applied only in that context. None expressly limits the requirement in this manner. Plaintiffs assert, however, that *1-800 Contacts, Inc. v. Steinberg*, 107 Cal.App.4th 568, 132 Cal.Rptr.2d 789 (2003), and *Everest Investors 8 v. Whitehall Real Estate Limited Partnership XI*, 100 Cal.App.4th 1102, 123 Cal.Rptr.2d 297 (2002), support their argument in this regard. Both *1-800 Contacts* and *Everest Investors* are conspiracy cases, which based their holdings ultimately on the fact that defendants did not owe plaintiffs an inde-

pendent duty and thus could not conspire to breach that duty. See *1-800 Contacts, supra*, 107 Cal.App.4th at 592-93, 132 Cal.Rptr.2d 789 (“Breach of fiduciary duty is a tort that by definition may be committed by only a limited class of persons.... In the case of Conder’s fiduciary duty to plaintiff as its former attorney, that class did not include Steinberg. Plaintiff’s effort to hold him nevertheless liable for Conder’s alleged breach through the doctrine of conspiracy was legally unauthorized”); *Everest Investors, supra*, 100 Cal.App.4th at 1107-08, 123 Cal.Rptr.2d 297 (“Since the only duty allegedly breached as a result of the alleged conspiracy is a fiduciary duty owed by the General Partners but not by Whitehall, Whitehall cannot be held accountable to Everest on a conspiracy theory”).

In reaching this result, both the *1-800 Contacts* and the *Everest Investors* courts took pains to note that the “financial gain” requirement is an exception to the agent’s immunity rule and, in the context of a claim for conspiracy, cannot substitute for or create a duty where none otherwise exists. Both cited the “two independent principles” on which *Doctors’ Co.* was based—the fact that parties cannot be liable for conspiring to breach a duty they do not owe and the agent’s immunity rule, and noted that the exception for conduct undertaken for one’s own financial gain applies only to the agent’s immunity rule. See *1-800 Contacts, supra*, 107 Cal.App.4th at 592, 132 Cal.Rptr.2d 789; *Everest Investors, supra*, 100 Cal.App.4th at 1107-08, 1109, 123 Cal.Rptr.2d 297.

Each of *1-800 Contacts* and *Everest Investors* criticizes earlier California appellate decisions holding that agents of fiduciaries who act to further their own financial*1125 interests can be held liable for conspiring to breach or for aiding and abetting a fiduciary’s breach of duty. Among the decisions criticized are those on which the court earlier relied in holding that plaintiffs had to plead that the Banks acted for their own financial gain—*Pierce, supra*, 1 Cal.App.4th 1093, 3 Cal.Rptr.2d

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

236, and *City of Atascadero v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 68 Cal.App.4th 445, 80 Cal.Rptr.2d 329 (1998). See *Everest Investors, supra*, 100 Cal.App.4th at 1108-09, 123 Cal.Rptr.2d 297. See also *1-800 Contacts, supra*, 107 Cal.App.4th at 592, 132 Cal.Rptr.2d 789.

The *Pierce* court held that *Doctors' Co.* stated two exceptions to the rule that one cannot conspire to breach a duty he or she does not owe. The first of these, the court said, is where the party owes an independent duty to the plaintiff; the second, it held, is where a party participates in the breach of another's duty for his or her own financial gain. See *Pierce, supra*, 1 Cal.App.4th at 1104-05, 3 Cal.Rptr.2d 236 (“*Doctors' Co.*... cited several exceptions to this rule. Most notably, where an attorney conspires with a client to violate a statutory duty peculiar to the client, the attorney may be liable for his or her participation in the violation of the duty if the attorney was acting in furtherance of his or her own financial gain.... Also to be distinguished is the case where an attorney violates his or her own duty to the plaintiff...”). Concluding that the complaint adequately alleged that the attorney defendants had acted for their own personal gain, the court held that it stated a claim for breach of fiduciary duty against them. *Id.* at 1105-06, 3 Cal.Rptr.2d 236.

Relying on *Pierce* and *Doctors' Co.*, the *City of Atascadero* court held that “[u]nder California law, the right to sue a third party for participating in a fiduciary's breach of trust is limited to situations in which the third party was acting for personal gain or in furtherance of his or her own financial advantage.... As long as the third parties were acting to further their own individual economic interests, they may be liable for actively participating in a fiduciary's breach of his or her trust.” *City of Atascadero, supra*, 68 Cal.App.4th at 463, 80 Cal.Rptr.2d 329. The court discussed a recent appellate decision- *Kidron v. Movie Acquisition Corp.*, 40 Cal.App.4th 1571, 47 Cal.Rptr.2d 752 (1995)- which, citing the California Supreme Court's de-

cision in *Applied Equipment*, held that a party not in a fiduciary relationship with the plaintiff could not be held liable for conspiring to breach a fiduciary's duty to the plaintiff. *City of Atascadero, supra*, 68 Cal.App.4th at 464, n. 14, 80 Cal.Rptr.2d 329. The *Atascadero* court concluded that *Kidron* had overlooked the exception to this general rule created by *Doctors' Co.* for cases where the non-fiduciary acts for his or her own financial gain, and stated that non-fiduciaries could be held liable for aiding and abetting a breach of fiduciary duty where they acted for individual advantage. *Id.*^{FN72}

FN72. *Pierce* and *City of Atascadero* were followed in *Wolf, supra*, 76 Cal.App.4th 1030, 90 Cal.Rptr.2d 792.

As this brief summary of the cases makes clear, there appears to be a clear division among the California Courts of Appeal regarding the proper interpretation of the California Supreme Court's decisions in *Doctors' Co.* and *Applied Equipment*. The court must thus attempt to discern how the Supreme Court would itself decide the issue in the context of this case. See *Katz v. Children's Hosp. of Orange County*, 28 F.3d 1520, 1528 (9th Cir.1994) (“Our task is to predict how the *1126 California Supreme Court would interpret section 340.5”); *Estrella v. Brandt*, 682 F.2d 814, 817 (9th Cir.1982) (determining which of several conflicting intermediate state court decisions the state supreme court would adopt).

The court first notes that *Pierce*, *City of Atascadero*, and *Wolf* each applied section 326 of the Restatement (Second) of Trusts, which provides that “[a] third person who, although not a transferee of trust property, has notice that the trustee is committing a breach of trust and participates therein is liable to the beneficiary for any loss caused by the breach of trust.” While the holdings of the cases regarding breach of fiduciary duty are broader, it appears they were informed by the particular trust context in which the cases arose, as each court attempted to harmonize the common law trust principles reflected in the Restatement with the Califor-

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

nia Supreme Court's pronouncements in *Doctors' Co.* See *Wolf, supra*, 76 Cal.App.4th at 1039-40, 90 Cal.Rptr.2d 792 (addressing a complaint that alleged a claim for active participation in a trustee's breach of trust); *City of Atascadero, supra*, 68 Cal.App.4th at 463-64, 80 Cal.Rptr.2d 329 (stating that the common law rule set forth in the Restatement was limited by *Doctors' Co.*, but that the "basic principles" remained the same); *Pierce, supra*, 1 Cal.App.4th at 1103-04, 3 Cal.Rptr.2d 236 (discussing § 326 and stating that "[t]he right to sue attorneys, agents, or employees of a fiduciary for participation in the fiduciary's breach of trust has been circumscribed by the California Supreme Court in *Doctors' Co.*...").^{FN73} Perhaps because of the trust context in which they arise, and the non-specific language of the Restatement section they apply,^{FN74} the cases do not clearly distinguish between claims for breach of fiduciary duty, conspiracy to breach a fiduciary duty, and aiding and abetting the breach of a fiduciary duty. The instant case does not involve a breach of fiduciary duty by a trustee.^{FN75} Thus, to the extent *Pierce* and *City of Atascadero* were informed by the common law of trusts, and blurred the distinction between conspiracy and aiding and abetting liability as a result, they are inapposite to this case.

FN73. *Mosier v. Southern California Physicians Ins. Exchange*, 63 Cal.App.4th 1022, 1048, 74 Cal.Rptr.2d 550 (1998), did not arise in the trust context. There, the court stated: "We agree with SCPIE that the general rule is that a party who is not personally bound by the duty violated may not be held liable for civil conspiracy even though it may have participated in the agreement underlying the injury.... However, an exception to this rule exists when the participant acts in furtherance of its own financial gain." *Id.* at 1048, 74 Cal.Rptr.2d 550. In reality, the court had already found that the insurer, SCPIE, had a duty to the plaintiff. *Id.* Thus, this statement was not necessary to the court's de-

cision and is dicta.

FN74. The Restatement speaks of "participation" in a breach of trust, rather than "conspiracy" or "aiding and abetting."

FN75. While Slatkin was an investment advisor, there is no indication that he operated pursuant to a statutory or other species of trust. This distinguishes the case from *City of Atascadero*, which involved statutory investment trusts.

1-800 Contacts and *Everest Investors*, while conspiracy cases, address the applicability of the financial gain requirement outside the trust context. More fundamentally, these courts' interpretation of the *Doctors' Co.* and *Applied Equipment* decisions is correct. Both *Doctors' Co.* and *Applied Equipment* are conspiracy cases. The starting point for their analysis is the principle that a civil conspiracy is not an independent tort and gives rise to a cause of action only when a civil wrong has been committed that results in damage. See *Applied Equipment, supra*, 7 Cal.4th at 511, 28 Cal.Rptr.2d 475, 869 P.2d 454; *1127*Doctors' Co., supra*, 49 Cal.3d at 44, 260 Cal.Rptr. 183, 775 P.2d 508. Both cases articulate the doctrine that a conspiracy claim may not be asserted against one who did not owe the injured party a duty. *Applied Equipment, supra*, 7 Cal.4th at 511, 28 Cal.Rptr.2d 475, 869 P.2d 454; *Doctors' Co., supra*, 49 Cal.3d at 44, 260 Cal.Rptr. 183, 775 P.2d 508. While *Doctors' Co.* also relied on the agent's immunity rule, and discussed the financial gain exception to that rule (see 49 Cal.3d at 44, 260 Cal.Rptr. 183, 775 P.2d 508), the Supreme Court in *Applied Equipment* made clear that this issue was "independent" from the question of duty. To the extent, therefore, that *Pierce* and *City of Atascadero* read *Doctors' Co.* as permitting a conspiracy cause of action to proceed against a party who does not owe plaintiff a duty solely because the party acted for his or her own financial gain, the court concludes that they are incorrectly decided, and that the California Supreme Court would so hold.

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

This does not resolve the precise question that is presently before the court, however, as plaintiffs do not charge the Banks with conspiracy, but rather with aiding and abetting the breach of a fiduciary duty. Under California law, such a cause of action does not require that the aider and abettor owe plaintiff a duty so long as it knows the primary wrongdoer's conduct constitutes a breach of duty, and it substantially assists that breach of duty. See *Fiol, supra*, 50 Cal.App.4th at 1325-26, 58 Cal.Rptr.2d 308. Other than the *Pierce/City of Atascadero/Wolf* line of cases, the only case cited by either party that even remotely suggests that financial gain is an element of a claim for aiding and abetting the breach of a fiduciary duty is *Heckmann v. Ahmanson*, 168 Cal.App.3d 119, 214 Cal.Rptr. 177 (1985).^{FN76} There, the court stated:

FN76. Defendants contend that the Supreme Court's decision in *Bancroft-Whitney Co. v. Glen*, 64 Cal.2d 327, 49 Cal.Rptr. 825, 411 P.2d 921 (1966), imposed such a requirement. See *id.* at 353, 49 Cal.Rptr. 825, 411 P.2d 921 ("It is clear from the evidence set forth above that Bender was aware of or ratified Glen's breach of his fiduciary duties in all but a few respects, that he cooperated with Glen in the breach, and that he received the benefits of Glen's infidelity. It cannot be said here ... that Bender Co. did not 'reap where it had not sown.' Under all the circumstances, Bender and Bender Co. must be held liable for their part in Glen's breach of his fiduciary duties"). *Bancroft-Whitney* does not aid defendants' argument, as the claim there considered was an unfair competition claim, not an aiding and abetting claim. See *id.* at 330, 49 Cal.Rptr. 825, 411 P.2d 921.

"If the Disney directors breached their fiduciary duty to the stockholders, the Steinberg Group could be held jointly liable as an aider and abettor. The Steinberg Group knew it was reselling its

stock at a price considerably above market value to enable the Disney directors to retain control of the corporation. It knew or should have known Disney was borrowing the \$325 million purchase price. From its previous dealings with Disney, including the Arvida transaction, it knew the increased debt load would adversely affect Disney's credit rating and the price of its stock. If it were an active participant in the breach of duty *and reaped the benefit*, it cannot disclaim the burden." *Id.* at 127, 214 Cal.Rptr. 177 (emphasis added).

Having reviewed *Heckmann* carefully, the court concludes that it stands for the unremarkable proposition that one who knows of a fiduciary's breach of duty and substantially assists it is liable as an aider and abettor. The court's reference to "reaping the benefit," offhand as it is, cannot be seen as adding an element to the tort.^{FN77}

FN77. It should be noted, moreover, that the aider and abettor in *Heckmann* itself had a duty to shareholder plaintiffs, such that the second prong of the *Fiol* test probably applied. See *Fiol, supra*, 50 Cal.App.4th at 1325-26, 58 Cal.Rptr.2d 308 (one is liable as an aider and abettor if he "gives substantial assistance to the other in accomplishing a tortious result and the person's own conduct, separately considered, constitutes a breach of duty to the third person").

Rather, the *Heckmann* court cited financial gain as evidence that the aider and *1128 abettor knew of and substantially assisted the primary violator's breach of fiduciary duty. A review of the case law and scholarly literature regarding the tort indicates that this is the proper role to assign to financial gain, i.e., it should not be viewed as an element of the tort, but as evidence of knowledge, substantial assistance, or both. See Alan R. Bromberg & Lewis D. Lowenfels, Aiding and Abetting Securities Fraud: A Critical Examination, 52 ALB. L. REV. 637, 739-48 (1988) ("Benefit or gain derived by the

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

aider-abettor is not one of the three traditional elements of aiding-abetting-primary violation, knowledge, and substantial assistance. Benefit nonetheless has significance in aid-abet cases. The courts mention it with some frequency and attach varying weight to its presence or absence in deciding whether either the knowledge or the substantial assistance requirements (or both) are satisfied"). See also *Monsen v. Consolidated Dressed Beef Co., Inc.*, 579 F.2d 793, 799 (3d Cir.1978) (" 'The requirement of knowledge may be less strict where the alleged aider and abettor derives benefits from the wrongdoing but even in this situation the proof offered must establish conscious involvement in impropriety or constructive notice of intended impropriety,' ") quoting *Gould v. American-Hawaiian Steamship Co.*, 535 F.2d 761, 780 (3d Cir.1976); *Chem-Age Industries v. Glover*, 652 N.W.2d 756, 775 (S.D.2002) ("It has been suggested that an element of wrongful intent should be included as part of the 'substantial assistance' requirement.... One example of wrongful intent would be when a lawyer aids and abets the breach of a fiduciary duty in furtherance of the lawyer's own self-interest.... Although not an element in proving aiding and abetting the breach of a fiduciary duty, certainly [a lawyer's self-interest and receipt of fees] are circumstances to consider in gauging a lawyer's alleged knowing participation and substantial assistance," citing, *inter alia*, *Skarbrevik*, *supra*, 231 Cal.App.3d 692, 282 Cal.Rptr. 627). Cf. Bryan C. Barksdale, *Redefining Obligations in Close Corporation Fiduciary Representation: Attorney Liability for Aiding and Abetting the Breach of Fiduciary Duty in Squeeze-Outs*, 58 WASH. & LEE L. REV. 551, 572-73 (2001) (describing California's financial gain requirement as a substitute for intent).
FN78

FN78. Imperial argues that, at a minimum, the court should require that plaintiffs plead and prove that the banks benefited financially from assisting Slatkin to defraud investors who were not bank customers. Imperial asserts it did not know these

investors existed, and thus cannot have consciously aided and abetted Slatkin's efforts to defraud them. As noted *supra*, the complaint alleges that the Banks knew Slatkin was defrauding, and breaching his fiduciary duty to, all Class Members. The court must accept this allegation as true for purposes of ruling on defendants' motions. The court notes, however, that the Banks can have had no form of duty-fiduciary or otherwise-to investors who were not depositors. Given that the banks had no duty of any kind to this group, non-account holders should arguably be required to adduce stronger evidence that the banks knew the full extent of Slatkin's Ponzi scheme and intended to assist him in executing it than Club members who had accounts at the banks. See, e.g., *Edwards & Hanly v. Wells Fargo Securities Clearance Corp.*, 602 F.2d 478, 485 (2d Cir.1979) (" 'A remote party must not only be aware of his role, but he should also know when and to what degree he is furthering the fraud,' ") quoting *Woodward v. Metro Bank of Dallas*, 522 F.2d 84, 95 (5th Cir.1975)). The court need not decide this issue, however, as the question is not properly raised by the pending motions, which address only the sufficiency of the complaint.

*1129 [17] Accordingly, the court concludes that the California Supreme Court would not hold that personal financial gain is an element of aiding and abetting a breach of fiduciary duty. Thus, plaintiffs need not plead that the Banks, who were not Slatkin's agents, acted for their own financial gain in order to state a claim that they aided and abetted Slatkin's breach of a fiduciary duty.
FN79
Defendants' motion to dismiss on this basis is therefore denied.

FN79. Because it concludes that plaintiffs are not required to plead financial gain to state an aiding and abetting claim, the

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

court need not consider the parties' arguments regarding the adequacy of the pleading in this regard.

3. Whether The Complaint Adequately Pleads "Substantial Assistance"

Defendant Leider argues that the complaint fails to describe how she substantially assisted Slatkin's scheme and damaged plaintiffs. In the first amended complaint, plaintiffs alleged that the Banks substantially assisted Slatkin by giving him access to large sums of money that kept his scheme afloat for a significant period of time. The court found these allegations sufficient to allege that the Banks' participation was a "substantial factor" in bringing about the alleged injury suffered by the putative class members. In the third amended complaint, plaintiffs have added allegations that Leider substantially assisted Slatkin by "vouching" for his Club and "promoting" his skills as an investment advisor.

Leider argues that these allegations do not adequately plead substantial assistance. She asserts that (1) allegations the Banks extended funds to Slatkin do not demonstrate that she substantially assisted him since it is not alleged that she gave Slatkin money; (2) the complaint contains no allegations as to how she purportedly assisted Slatkin's theft of non-account holder investments; and (3) allegations that she "vouched" for Slatkin's investment club and "promoted" his skills as an investment advisor to account holders at Imperial and Pacific Inland Banks are not pled with the specificity required by Rule 9(b). The court evaluates each argument in turn.

Leider first argues that the court's earlier ruling that plaintiffs had adequately pled substantial assistance on the part of the Banks does not apply to her since the complaint does not allege that she gave Slatkin any funds. Plaintiffs do not dispute the absence of such an allegation. They argue, however, that "[b]ecause Ms. Leider was the administrator of the Club at both Pacific Inland and Imperial, the [first amended complaint's] allega-

tions in large part referred to Ms. Leider's actions," and thus the "court has already held, in effect, that the ... allegations as to Ms. Leider are sufficient."

In its prior order, the court cited an allegation in the first amended complaint asserting that "access to [the] large sums of cash the Banks gave Mr. Slatkin allowed Mr. Slatkin to pay fake returns to all of his investors," and "to prolong the longevity of [the] fraud."^{FN80} It concluded this sufficed to allege that the Banks' participation was a "substantial factor" in bringing about the injury purportedly suffered by the putative class members. See *Cromer Finance Ltd. v. Berger*, 137 F.Supp.2d 452, 470 (S.D.N.Y.2001) ("Substantial assistance requires the plaintiff to allege that the actions of the aider/abettor proximately caused the harm on which the primary liability is predicated"); *1130 *Mitchell v. Gonzales*, 54 Cal.3d 1041, 1052-53, 1 Cal.Rptr.2d 913, 819 P.2d 872 (1991) (endorsing a "substantial factor" test for proximate cause). This analysis is inapposite as respects Leider, however, since neither first nor the third amended complaints alleges that she personally advanced funds to Slatkin that were used in the scheme. Thus, the adequacy of plaintiffs' allegations that she substantially assisted the scheme must be found elsewhere in the complaint.

FN80. First Amended Complaint, ¶ 93.

[18] Leider bifurcates her discussion of this issue between account holder and non-account holder plaintiffs. As respects the latter, she argues correctly that the complaint contains no factual allegations regarding the manner in which she purportedly assisted Slatkin's theft of funds from this investor class. Rather, all of the allegations in the third amended complaint regarding Leider's conduct concern Club accounts at Pacific Inland and Imperial Management. Thus, the non-account holder plaintiffs' aiding and abetting claims against Leider fail adequately to allege "substantial assistance," and must be dismissed with leave to amend.

Leider next contends that allegations she

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

“vouched” for Slatkin and “promoted” his investment skills to account holders at the Banks are not pled with the requisite degree of specificity under Rule 9(b). Plaintiffs do not dispute that, when a claim alleges the aiding and abetting of a fraud, substantial assistance must be pled in accordance with Rule 9(b)'s heightened specificity requirements.^{FN81} They maintain, however, that their allegations regarding Leider's substantial assistance of Slatkin's fraud satisfy this standard.

FN81. Nor could plaintiffs make such an argument. Federal courts have held that the substantial assistance prong of a claim that defendant aided and abetted the commission of a fraud must be pled with heightened specificity. *FMC Corp. v. Boesky*, 727 F.Supp. 1182, 1200-01 (N.D.Ill.1989) (“The parties[] dispute whether FMC has alleged its aiding and abetting claims with enough detail. Federal Rule of Civil Procedure 9(b) obligates the plaintiff ‘to state each of the elements of aiding and abetting liability with sufficient particularity to give defendant[s] adequate notice of the exact nature of the fraud claimed so that [they] can formulate adequate responses. ... Unadorned allegations that [the defendants] knew of the primary violation and rendered substantial assistance ... will not suffice to satisfy the strictures of Rule 9(b),’ ” quoting *Kirshner v. Goldberg*, 506 F.Supp. 454, 458 (S.D.N.Y.1981), *aff'd.* without opinion, 742 F.2d 1430 (2d Cir.1983)); *Brant v. CCG Financial Corp.*, 693 F.Supp. 889, 894 (D.Or.1988) (“The acts or omissions that comprise the necessary substantial assistance must be pleaded with specificity pursuant to Fed.R.Civ.P. 9(b)"); *First Federal Sav. & Loan Ass'n of Pittsburgh v. Oppenheim, Appel, Dixon & Co.*, 634 F.Supp. 1341, 1353 (S.D.N.Y.1986) (“Memel Jacobs also contends that the supplemental third-party complaint is defi-

cient because its allegations of substantial assistance violate ‘the general rule that Rule 9(b) pleadings cannot be based on information and belief.’ ... It is true that OAD's complaint introduces the allegations of substantial assistance in conclusory terms and on information and belief; however, this language is followed by a more specific description, quoted above, of the nature of the acts by Memel Jacobs that are alleged to constitute the substantial assistance.... Although OAD's description of Memel Jacobs' conduct is not particularly detailed, we believe it is an acceptable ‘statement of facts upon which the [pleading on information and] belief is founded,’ ... so as to render the pleading sufficient, at least as to matters particularly within Memel Jacobs' knowledge, such as its dealings with Comark.... Dismissal on Rule 9(b) grounds is therefore not warranted” (citations omitted)).

The complaint contains numerous allegations concerning specific activities in which Leider engaged. It states that she recruited investors to liquidate existing investments and purchase shares in Slatkin's investment club, representing to them that Slatkin could obtain high rates of return and that he was a man of great integrity. It further alleges that, in at least one instance, Leider stated that all Club assets *1131 were marketable securities and that certificates would be held in the bank vault.^{FN82}

FN82. See Third Amended Complaint, ¶¶ 51, Ex. 4.

Plaintiffs assert that Leider “unitized” shares of the Club, and told investors the Club was regularly audited. They also contend that when Slatkin was slow to honor withdrawal requests, Leider explained to investors why it was taking longer than expected to obtain the funds.^{FN83} Finally, they allege that Leider falsely told investors the Banks deducted fees from liquid assets on deposit.^{FN84}

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

FN83. *Id.*, ¶¶ 53, 54, 71.FN84. *Id.*, ¶¶ 65, 74.

[19] Leider argues that these allegations do not sufficiently plead substantial assistance because plaintiffs do not specifically identify the individuals to whom she allegedly spoke, when she made the statements, and what she said.^{FN85} In assessing this argument, it is important to recall that Leider is not charged directly with fraud. Rather, she is charged with “substantially assisting” Slatkin’s fraud. Where aiding and abetting is the gravamen of the claim, Rule 9(b) requires that “the complaint ... inform [the] defendant ... what he did that constituted ... ‘substantial assistance.’ ” *Graziose v. American Home Products Corp.*, 202 F.R.D. 638, 642 (D.Nev.2001) (quoting *Arroyo v. Wheat*, 591 F.Supp. 136, 138-39 (D.Nev.1984)). See also *Securities and Exchange Commission v. Wexler*, No. 92 Civ. 2902(SWK), 1993 WL 362390, * 4 (S.D.N.Y. Sept.14, 1993) (finding that a complaint, which alleged that defendant complied with instructions not to accept unapproved sell orders and parked 3,000 units in a nominee account, adequately alleged substantial assistance because the “allegations [were] sufficiently specific to inform [the defendant] of the precise nature of the charges levied against him”); *National Fire Ins. Co. of Pittsburgh, Pa. v. Califinvest*, Nos. 90 CIV. 2476(LLS), 90 CIV. 6831(LLS), 1992 WL 35017, * 4-5 (S.D.N.Y. Feb. 14, 1992) (observing that “[d]efendants are not required to plead all of their proof in their counterclaims,” and concluding allegations that an insurer intentionally participated in a fraudulent limited partnership scheme by bonding the investments and prevailing upon banks to provide loans to the partnerships adequately alleged substantial assistance); *Harrison v. Enventure Capital Group, Inc.*, 666 F.Supp. 473, 477 (W.D.N.Y.1987) (“... the acts or omissions that comprise the necessary substantial assistance must be pleaded with specificity. Generalized and conclusory allegations that a defendant aided and abetted the principal wrongdoers will not suffice”).

FN85. The complaint alleges specific representations by Leider to five account holder plaintiffs: George Kriste, Fred Ockrim, Stuart Stedman, the trustee of the Dewey Trust and Jaroslav Marik.

[20] Here, the complaint adequately alleges what Leider did to assist Slatkin in defrauding the investors. The complaint pleads numerous specific statements by Leider to Club investors, and states why they were false. Fairly read, it pleads that Leider had a practice of making such statements to class members, commencing in 1992, when she began working at Pacific Inland Bank, and continuing until 1999, when the accounts were acquired by Union Bank.^{FN86} See *Bonilla v. Trebol Motors Corp.*, Civil No. 92-1795(JP), 1997 WL 178844, * 51 (D.P.R. Mar.27, 1997) (“ ‘If the fraud involved either a course of conduct occurring over an extended period of time or a series of transactions, it is not necessary to recite in detail the facts of each transaction of the fraudulent scheme,’ ” quoting *1132 *Federal Savings & Loan Ins. Corp. v. Shearson-American Express, Inc.*, 658 F.Supp. 1331, 1337 (D.P.R.1987)). rev’d in part, vacated in part on other grounds, 150 F.3d 88 (1st Cir.1998). While the complaint does not allege that Leider made the statements to each and every member of the putative class, or indeed to each named plaintiff, the inference to be drawn from the allegations is that her representations to various members of the class harmed all plaintiffs because the statements allowed Slatkin to retain possession of plaintiffs’ funds and continue the Ponzi scheme.

FN86. See Third Amended Complaint, ¶¶ 47, 50.

[21] Rule 9(b) is designed to ensure that defendants have notice of the specific conduct with which they are charged, and to guard against the filing of unsubstantiated charges that may harm an individual’s reputation. See *Bly-Magee v. State of California*, 236 F.3d 1014, 1018 (9th Cir.2001) (“ Rule 9(b) serves not only to give notice to defendants of the specific fraudulent conduct against

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

which they must defend, but also ‘to deter the filing of complaints as a pretext for the discovery of unknown wrongs, to protect [defendants] from the harm that comes from being subject to fraud charges, and to prohibit plaintiffs from unilaterally imposing upon the court, the parties and society enormous social and economic costs absent some factual basis,’ ” quoting *In re Stac Electronics Securities Litigation*, 89 F.3d 1399, 1405 (9th Cir.1996)). Thus, “[t]o comply with Rule 9(b), allegations of fraud [or substantial assistance] must be ‘specific enough to give defendants notice of the particular misconduct which is alleged to constitute the fraud charged so that they can defend against the charge and not just deny that they have done anything wrong.’ ” *Id.* at 1019 (quoting *Neubronner v. Milken*, 6 F.3d 666, 672 (9th Cir.1993)). Here, the complaint clearly identifies the misconduct with which Leider is charged, and provides sufficient information to enable her to prepare an adequate defense. More is not required.

Leider asserts that the allegations are insufficient because plaintiffs do not plead how these various activities substantially assisted Slatkin. Yet the complaint alleges that Leider was “a key factor in the growth of the Club and Mr. Slatkin's Ponzi scheme in general,” and that she “served as an important buffer between Mr. Slatkin and the Club members” by “cover[ing] for [his] delays” in payment and “calming potentially irate investors.”^{FN87} It further alleges that Leider's representation that the Banks audited the investor accounts “created a sense of security” in the investors.^{FN88} Coupled with the specific facts alleged, these allegations adequately plead that Leider's actions were a “substantial factor” in Slatkin's ability to perpetrate the fraudulent scheme. Accordingly, the court finds that plaintiffs have adequately alleged that Leider substantially assisted Slatkin's fraud and breach of fiduciary duty.

FN87. *Id.*, ¶¶ 50, 53.

FN88. *Id.*, ¶ 55.

4. Whether Plaintiffs Must Allege That Leider Owed Them An Independent Duty

Leider asserts finally that the aiding and abetting claims fail as a matter of law because she did not owe plaintiffs an independent fiduciary duty.^{FN89} Leider acknowledges that no California court has held that a defendant cannot be liable as an aider and abettor unless he or she had an independent duty to the plaintiff. She contends, however, that California courts have implicitly adopted such a rule, and that federal courts have expressly approved it.

FN89. See *infra* at 1134-35.

*1133 a. California Law

Leider first argues that an independent duty requirement is implicit in California law because California courts have analogized aiding and abetting to conspiracy, and California law requires that each conspirator owe the duty violated by the underlying tort before he or she can be held liable.

California courts have certainly recognized that conspiracy and aiding and abetting are closely allied forms of liability. See *Janken v. GM Hughes Electronics*, 46 Cal.App.4th 55, 78, 53 Cal.Rptr.2d 741 (1996) (“Conspiracy is a concept closely allied with aiding and abetting. A conspiracy generally requires agreement plus an overt act causing damage. Aiding and abetting requires not agreement, but simply assistance. The common basis for liability for both conspiracy and aiding and abetting, however, is concerted wrongful action”); *Howard, supra*, 2 Cal.App.4th at 749, 3 Cal.Rptr.2d 575 (“In the abstract, there may be a distinction between an aiding and abetting cause of action and one for civil conspiracy. However, while aiding and abetting may not require a defendant to agree to join the wrongful conduct, it necessarily requires a defendant to reach a conscious decision to participate in tortious activity for the purpose of assisting another in performing a wrongful act. A plaintiff's object in asserting such a theory is to hold those who aid and abet in the wrongful act responsible as joint tortfeasors for all damages ensuing from the wrong”).

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

California courts have also held that a claim for civil conspiracy does not arise unless the alleged conspirator owed the victim a duty not to commit the underlying tort. See *Applied Equipment Corp. v. Litton Saudi Arabia Limited*, 7 Cal.4th 503, 514, 28 Cal.Rptr.2d 475, 869 P.2d 454 (1994) (“Conspiracy is not an independent tort; it cannot create a duty or abrogate an immunity. It allows tort recovery only against a party who already owes the duty and is not immune from liability based on applicable substantive tort law”); *Doctors’ Company, supra*, 49 Cal.3d at 44, 260 Cal.Rptr. 183, 775 P.2d 508 (“A cause of action for civil conspiracy may not arise, however, if the alleged conspirator, though a participant in the agreement underlying the injury, was not personally bound by the duty violated by the wrongdoing and was acting only as the agent or employee of the party who did have that duty”).

[22] No California case, however, holds that a party must owe the plaintiff a duty before he or she can be held liable as an aider and abettor. Rather, California cases outlining the elements of aiding and abetting liability have consistently cited the elements of the tort as they are set forth in the Restatement (Second) of Torts, § 876, and have omitted any reference to an independent duty on the part of the aider and abettor. Under this formulation, liability may properly be imposed on one who knows that another’s conduct constitutes a breach of duty and substantially assists or encourages the breach. See *Fiol, supra*, 50 Cal.App.4th at 1325-26, 58 Cal.Rptr.2d 308; *Saunders, supra*, 27 Cal.App.4th at 846, 33 Cal.Rptr.2d 438; REST. 2D TORTS, § 876.^{FN90} See also *1134 *In Re First Alliance Mortgage Co.*, 298 B.R. 652, 668 (C.D.Cal.2003) (citing *Saunders*); *Wynn v. National Broadcasting Co., Inc.*, 234 F.Supp.2d 1067, 1114 (C.D.Cal.2002) (“Since neither [the FEHA nor New York’s Human Rights Law] provides a definition of aiding and abetting, courts have looked to the common law definition. ‘[O]ne is subject to liability if he ... (b) knows that the other’s conduct constitutes a breach of duty and gives substantial assistance or encour-

agement to the other so to conduct himself.’ Restatement (Second) of Torts § 876 (1979),” citing *Fiol, supra*, 50 Cal.App.4th at 1325-26, 58 Cal.Rptr.2d 308); *Perfect 10, Inc. v. Cybernet Ventures, Inc.*, 213 F.Supp.2d 1146, 1183 (C.D.Cal.2002) (“California has adopted the joint liability principle laid out in the Restatement (Second) of Torts § 876”).

FN90. Leider argued at the hearing that the court cannot rely on *Fiol* for the rule that aiding and abetting liability requires no independent duty because the question was not squarely presented in *Fiol*, and thus was not addressed by the court. The court cannot agree. The *Fiol* court articulated alternative tests for aiding and abetting liability and evaluated whether the defendant supervisor could be held liable for aiding and abetting the sexually harassing conduct of plaintiff’s co-worker under both. Under the actual knowledge and substantial assistance test, the court concluded that the supervisor’s failure to take action to prevent the harassment did not constitute substantial assistance. *Fiol, supra*, 50 Cal.App.4th at 1326, 58 Cal.Rptr.2d 308. Under the substantial assistance and breach of duty formulation, the court held that “a supervisory employee owes no duty to his or her subordinates to prevent sexual harassment in the workplace.” *Id.* Even if *Fiol* had not applied the first test for aiding and abetting liability, however, the court would find it appropriate to rely on the case. The court does not cite *Fiol* for its holding that there was no liability for aiding and abetting under the facts there presented. Rather, it relies on *Fiol*’s statement of the elements of an aiding and abetting claim, a formulation that is generally applicable, is also set forth in *Saunders*, and is drawn directly from the Restatement.

Leider argues nonetheless that such a result is

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

the natural extension of the principles enunciated by the California Supreme Court in *Applied Equipment*. After analyzing that decision carefully, the court concludes to the contrary. In *Applied Equipment*, the Court noted that conspiracy was “not a cause of action, but a legal doctrine that imposes liability on persons who, although not actually committing a tort themselves, share with the immediate tortfeasors a common plan or design in its perpetration.... By participation in a civil conspiracy, a coconspirator effectively adopts as his or her own the torts of other coconspirators within the ambit of the conspiracy.” *Applied Equipment*, *supra*, 7 Cal.4th at 511, 28 Cal.Rptr.2d 475, 869 P.2d 454. The Court further observed that “... the major significance of the conspiracy lies in the fact that it renders each participant in the wrongful act responsible as a joint tortfeasor for all damages ensuing from the wrong, irrespective of whether or not he was a direct actor and regardless of the degree of his activity.” *Id.* (quoting *Doctors' Co.*, *supra*, 49 Cal.3d at 44, 260 Cal.Rptr. 183, 775 P.2d 508). For this reason, the Court held, the “... tort liability arising from conspiracy presupposes that the coconspirator is legally capable of committing the tort, i.e., that he or she owes a duty to plaintiff recognized by law and is potentially subject to liability for breach of that duty.” *Id.*

[23][24] Unlike a conspirator, an aider and abettor does not “adopt as his or her own” the tort of the primary violator. Rather, the act of aiding and abetting is distinct from the primary violation; liability attaches because the aider and abettor behaves in a manner that enables the primary violator to commit the underlying tort. See *Halberstam v. Welch*, 705 F.2d 472, 478 (D.C.Cir.1983) (“Aiding-abetting focuses on whether a defendant knowingly gave ‘substantial assistance’ to someone who performed wrongful conduct, not on whether the defendant agreed to join the wrongful conduct.... There is a qualitative difference between proving an *agreement* to participate in a tortious line of conduct, and proving *knowing action* that substantially aids tortious conduct”); ^{FN91} *1135

Wenneman v. Brown, 49 F.Supp.2d 1283, 1290, n. 3 (D.Utah 1999) (“This Court recognizes fundamental and significant differences between aiding and abetting, by which a person gives aid to a criminal wrongdoer, and conspiracy, by which a person knowingly joins others in a criminal undertaking with a common criminal goal”). See also *Aetna Casualty & Surety Co.*, *supra*, 219 F.3d at 534 (quoting *Halberstam* and stating that “[t]he District of Columbia Circuit has succinctly identified the ... difference between the torts of conspiracy to commit fraud and aiding and abetting fraud”); *id.* at 538 (quoting *Halberstam* 's statement that there is a “qualitative difference” between “agreement to participate in a tortious line of conduct, and proving knowing action that substantially aids tortious conduct”); *In re Washington Public Power Supply System Securities Litigation*, MDL No. 155, 1988 WL 158948, * 15 (W.D.Wash. July 14, 1988) (“The court in *Halberstam* ... provides some guidance with its careful analysis of two theories of secondary tort liability. The *Halberstam* court distinguished conspiracy from aiding and abetting by observing that a conspiracy consists of concerted action by agreement while aiding and abetting is concerted action by substantial assistance”). Because aiders and abettors do not agree to commit, and are not held liable as joint tortfeasors for committing, the underlying tort, it is not necessary that they owe plaintiff the same duty as the primary violator. Conspirators, by contrast, are held liable for the tort committed by their co-conspirator. See *Applied Equipment*, *supra*, 7 Cal.4th at 510-11, 28 Cal.Rptr.2d 475, 869 P.2d 454. Because liability is premised on the commission of a single tort, it is logical that all conspirators must be legally capable of committing the wrong.

FN91. *Halberstam* was cited favorably in *Howard*, *supra*, 2 Cal.App.4th at 749, 3 Cal.Rptr.2d 575.

[25][26] Additionally, causation is an essential element of an aiding and abetting claim, i.e., plaintiff must show that the aider and abettor

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

provided assistance that was a substantial factor in causing the harm suffered. See *Metge v. Baehler*, 762 F.2d 621, 624 (8th Cir.1985) (a plaintiff seeking to prevail on an aiding and abetting claim must prove a “ ‘substantial causal connection between the culpable conduct of the alleged aider and abettor and the harm to the plaintiff[,]’ ... or a showing that ‘the encouragement or assistance is a substantial factor in causing the resulting tort’ ”), cert. denied, 474 U.S. 1057, 106 S.Ct. 798, 88 L.Ed.2d 774 (1986); *Cromer Finance Ltd.*, *supra*, 137 F.Supp.2d at 470 (“Substantial assistance requires the plaintiff to allege that the actions of the aider/abettor proximately caused the harm on which the primary liability is predicated”). A plaintiff seeking to prove a conspiracy claim, by contrast, need not adduce proof that the purported conspirator did *anything* that caused or contributed to the harm. All that is needed is proof of an agreement to commit the tort. See *Applied Equipment*, *supra*, 7 Cal.4th at 511, 28 Cal.Rptr.2d 475, 869 P.2d 454 (noting that alleged conspirators can be held liable as “ ‘... joint tortfeasor[s] for all damages ensuing from the wrong, irrespective of whether or not [they were] direct actor[s] and regardless of the degree of [their] activity,’ ” quoting *Doctors' Co.*, *supra*, 49 Cal.3d at 44, 260 Cal.Rptr. 183, 775 P.2d 508). This difference too demonstrates the distinction between the forms of liability, and argues in favor of a rule that permits the imposition of aider and abettor liability in the absence of a duty owed directly to the plaintiff.

[27] In sum, the court concludes that the analysis set forth in *Applied Equipment* does not mandate a finding that California law implicitly requires that a defendant owe plaintiffs a duty before she can be held liable for aiding and abetting. In the absence of an express holding by the *1136 California Supreme Court (or some other California court) to this effect, the court declines to apply such a rule in this case.

b. Federal Law

Leider next argues that federal courts interpret-

ing California law have required that plaintiffs prove that defendant owed them an independent duty as a prerequisite to the imposition of aider and abettor liability. Leider relies primarily on *Grosvenor Properties Ltd. v. Southmark Corp.*, 896 F.2d 1149 (9th Cir.1990). In *Grosvenor*, plaintiff alleged that defendant had conspired with his employer, and aided and abetted the employer's wrongful misappropriation of the benefits of a joint venture agreement. *Id.* at 1153. The Ninth Circuit held that the defendant owed plaintiff no independent duty and consequently that he could not be liable for “any tort in connection with his actions in regard to [plaintiff].” *Id.* at 1154. Citing this language, Leider contends the Ninth Circuit held that under California law, an aider and abettor must owe plaintiff an independent duty. The court disagrees. As described in *Grosvenor*, the district court granted the defendant's motion for directed verdict “on the ground that an officer of a defendant corporation acting within the scope of his authority cannot be held liable for conspiring with the corporation to commit a breach of fiduciary duty of the corporation.” *Id.* at 1151. This is the ruling that was appealed to the Ninth Circuit. *Id.* at 1153.

It is true that later in the opinion the circuit court stated that plaintiff alleged the corporate officer “conspired with [his corporate employer] and aided and abetted its wrongful misappropriation of the fruits of a joint venture.” *Id.* The court's discussion of the claim, however, is based entirely on California conspiracy law, and does not cite any California cases addressing liability for aiding and abetting. See *id.* at 1153-54 (citing *Gruenberg v. Aetna Ins. Co.*, 9 Cal.3d 566, 108 Cal.Rptr. 480, 510 P.2d 1032 (1973)). It was based on conspiracy law alone that the court determined that the defendant could not be liable for “any tort” because he owed no independent duty to the plaintiff corporation. *Id.* at 1154. The court's reliance on conspiracy law is consistent with its description of the ruling appealed, and supports the conclusion that the case does not articulate a rule applicable to liability for aiding and abetting as opposed to conspiracy.^{FN92}

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

Grosvenor, therefore, does not control this court's interpretation of aiding and abetting liability under California law.^{FN93}

FN92. The court's single reference to aiding and abetting in a case that otherwise concerns conspiracy liability is perhaps illustrative of the fact that “[c]ourts and commentators have frequently blurred the distinction between the two theories of concerted liability.” *Halberstam, supra*, 705 F.2d at 478.

FN93. Moreover, even if the court were to read *Grosvenor* as broadly as Leider contends, *Grosvenor* was decided in 1990. This was long before the California Courts of Appeal decided *Fiol* and *Saunders*. To the extent *Grosvenor* is inconsistent with these courts' interpretation of state law, the court concludes that it must follow the decisions of the California courts. See *Pershing Park Villas Homeowners Ass'n. v. United Pacific Ins. Co.*, 219 F.3d 895, 903 (9th Cir.2000) (“We are only ... bound [to follow Ninth Circuit interpretations of state law], however, ‘in the absence of any subsequent indication from the [state] courts that [the previous] interpretation was incorrect,’ ” quoting *Owen v. United States*, 713 F.2d 1461, 1464 (9th Cir.1983)).

Leider also cites *In re County of Orange*, 203 B.R. 983 (Bkrtcy.C.D.Cal.1996), aff'd. in part, rev'd. in part on other grounds, *In re County of Orange*, 245 B.R. 138 (C.D.Cal.1997), for its holding that aiding and abetting liability in California may *1137 only be imposed on those who owe an independent duty to the plaintiff. *Id.* at 997 (“S & P argues that recent California case law requires that the County's claim for aiding and abetting breach of a fiduciary duty be dismissed, because S & P does not have an independent fiduciary duty to the County.... After reviewing the history of California case law in this area, I am convinced that S & P is correct. A proper interpretation of *Applied Equip-*

ment requires that in order for the County to bring an aiding and abetting breach of a fiduciary duty suit against S & P, S & P must have owed the County an independent fiduciary duty.”). In *County of Orange*, the court grappled with precisely the same issue this court addressed above-i.e., whether under California law, the rule of *Doctors' Co.* and *Applied Equipment* is as applicable to aiding and abetting claims as it is to conspiracy. Noting that California courts have held that aiding and abetting and conspiracy are “closely allied,” and that both involve “concerted action,” the *County of Orange* court concluded that the same rule should apply. *Id.* at 999. For the reasons stated above, the court reaches a contrary conclusion, and declines to follow the reasoning set forth in *County of Orange*.

In sum, the court finds that under California law, a defendant may be found liable for aiding and abetting a breach of fiduciary duty even though the defendant owes no independent duty to the plaintiff, so long as the aider and abettor knows of, and substantially assists, the primary violator's breach of duty. Since this is the nature of the aiding and abetting claim plaintiffs have asserted against Leider, the claim is adequately pled despite plaintiffs' failure to allege that Leider owed them an independent fiduciary duty.

E. Whether The Complaint Adequately Pleads Breach Of Fiduciary Duty

[28] Plaintiffs' third cause of action alleges that defendants, “as custodians and/or trustees of the Club's accounts,” breached their fiduciary duties to Club members.^{FN94} To state a claim for breach of fiduciary duty, a complaint must allege the existence of a fiduciary duty, its breach, and damages resulting therefrom. *City of Atascadero v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 68 Cal.App.4th 445, 483, 80 Cal.Rptr.2d 329 (1998) (“The elements of a cause of action for breach of fiduciary duty are the existence of a fiduciary relationship, its breach, and damage proximately caused by that breach”); *Pierce v. Lyman*, 1 Cal.App.4th 1093, 3 Cal.Rptr.2d 236 (1991) (“In

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

order to plead a cause of action for breach of fiduciary duty, there must be shown the existence of a fiduciary relationship, its breach, and damage proximately caused by that breach. The absence of any one of these elements is fatal to the cause of action”). Although this claim is brought against all defendants, only Bank of Orange County and Leider challenge its validity. The court evaluates each challenge in turn.

FN94. Third Amended Complaint, ¶ 131.

1. The Bank of Orange County

The complaint alleges that the each of the Banks had a fiduciary duty “not to commingle assets; the duty to maintain accurate accounting records; the duty to refrain from accepting illegal investment directions; the duty to audit the assets of the Club; the duty to verify the assets of the Club; the duty to review the adequacy of internal controls; ... the duty to perform accurate valuations of the Club; ... the duty to supply each Club member with an accurate account statement ... [and] a fiduciary duty to provide market values of *1138 the Club members' accounts after audited financial statements of the Club had been completed.”^{FN95} The complaint further alleges that the Banks failed to perform and breached these duties,^{FN96} causing plaintiffs damage.^{FN97} Three of the named plaintiffs maintained accounts at Bank of Orange County's predecessor-in-interest, Pacific Inland Bank-Jaroslav Marik, Fred Ockrim, and Sheri Ockrim. The Bank contends these plaintiffs' breach of fiduciary duty claims fail because Pacific Inland Bank did not owe them a fiduciary duty, and because, even if it did, the custodial agreements plaintiffs executed demonstrate that it owed none of the duties alleged by plaintiffs in the complaint.

FN95. *Id.*, ¶ 132.

FN96. *Id.*, ¶ 133.

FN97. *Id.*

[29] California courts have generally held that

banks are not fiduciaries for their depositors. *Copesky v. Superior Court*, 229 Cal.App.3d 678, 693, 280 Cal.Rptr. 338 (1991). They have also held, however, that a fiduciary relationship may arise between a bank and its depositors where funds are deposited in a custodial account. *Van de Kamp v. Bank of America*, 204 Cal.App.3d 819, 859-60, 251 Cal.Rptr. 530 (1988) (“It may safely be said the deposit of securities into a custodial agency account creates a trust relationship”). See also *LaMonte v. Sanwa Bank California*, 45 Cal.App.4th 509, 517, 52 Cal.Rptr.2d 861 (1996) (same, quoting *Van de Kamp*). Bank of Orange County does not dispute that the three plaintiffs' funds were deposited into custodial accounts. Indeed, the court previously found that plaintiffs had adequately alleged the Club accounts were custodial in nature, and plaintiffs attach numerous documents to the complaint confirming this fact. Accordingly, Bank of Orange County's first argument-that Pacific Inland was not a fiduciary-fails.

As respects the bank's second argument-that Pacific Inland owed none of the fiduciary duties alleged in the complaint-California courts hold that a fiduciary's duties may be limited by contract. See *Van de Kamp, supra*, 204 Cal.App.3d at 860, 251 Cal.Rptr. 530 (a bank's duties as an agent under a custodial account are “limited to the scope of the agency set forth in the parties' agreement” and it “is a fiduciary [only] with respect to matters within the scope of the agency”). See also *LaMonte, supra*, 45 Cal.App.4th 509, 517, 52 Cal.Rptr.2d 861 (1996) (same); *Brown v. California Pension Administrators*, 45 Cal.App.4th 333, 337-38, 52 Cal.Rptr.2d 788 (1996) (“express provisions in documents governing the business relationship between the parties limited the duties of the trustee and the administrator. As a result, neither the trustee nor the administrator had an obligation to provide appellants with information about the performance of investments other than their own”).

Bank of Orange County cites one document attached to the complaint that it contends undermines

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

the fiduciary duty allegations of the Ockrims and Marik. The document, titled "Trustee Responsibilities With Respect to Assets Subject to Investment By Other Persons," was signed by plaintiff Jaroslov Marik on August 23, 1991. In relevant part, it states:

"The trustee shall not be under any obligation or duty ... to review any securities or other property of the Trust constituting assets thereof with respect to which another person possesses investment management responsibility." FN98

FN98. Third Amended Complaint, Exh. 34.

The bank argues that this document clearly limits the duties Pacific Inland owed the three plaintiffs. Specifically, it asserts, *1139 the agreement makes clear that Pacific Inland did not undertake to "audit the assets of the Club," "verify the assets of the Club" or perform any of the other tasks alleged in paragraph 132. For this reason, Bank of Orange County contends, it and its predecessor-in-interest, Pacific Inland, were merely non-discretionary custodians with no fiduciary duties to plaintiffs.

The contract proffered by Bank of Orange County is signed only by Marik, and the bank has not produced a similar agreement signed by the Ockrims. It is not clear on the present record, therefore, whether the duties the bank undertook with respect to the Ockrims' account were similarly limited. Moreover, although the contract limits the fiduciary duties of Pacific Inland Bank in certain respects, it contains no language limiting Pacific Inland's duty to issue accurate account statements. Additionally, it is unclear whether the contract's reference to "reviewing" the securities or other property held in a custodial account is intended to limit the bank's responsibility for auditing and/or accurately valuing accounts, or simply to limit its obligation to oversee the investment decisions being made by the investment manager. Given the

myriad fact questions that exist on the present record, the court finds that plaintiffs have adequately alleged a cause of action against Bank of Orange County for breach of fiduciary duty and denies the bank's motion to dismiss the claim.

2. Leider

Leider also argues that the breach of fiduciary duty claim against her must be dismissed. After alleging the nature of the fiduciary duties purportedly owed by the Banks, the complaint asserts that "[a]s the officer in charge of administering the Club, Ms. Leider owed each Club member the same duties." FN99

Leider argues that, as a matter of law, she owed plaintiffs no fiduciary duty independent of that owed by the Banks.

FN99. *Id.*, ¶ 131.

[30] It is well-established in California that " 'a corporation's employees owe no independent fiduciary duty to a third party with whom they deal on behalf of their employer.' " *Slottow v. American Cas. Co. of Reading, Pennsylvania*, 10 F.3d 1355, 1359 (9th Cir.1993) (quoting *Grosvenor Properties Ltd. v. Southmark Corp.*, 896 F.2d 1149, 1154 (9th Cir.1990) (citing *United States Liab. Ins. Co. v. Haidinger-Hayes, Inc.*, 1 Cal.3d 586, 594-95, 83 Cal.Rptr. 418, 463 P.2d 770 (1970), and *Wyatt v. Union Mortgage Co.*, 24 Cal.3d 773, 785, 157 Cal.Rptr. 392, 598 P.2d 45 (1979))).

Plaintiffs do not dispute that corporate officers in California generally have no fiduciary duty to third parties for acts performed on behalf of the corporation. Although they argue that there is an exception to this rule in the trust context, plaintiffs cite no authority supporting the proposition. FN100 Moreover, plaintiffs overlook the fact that *Slottow* involved a trust. *1140 In *Slottow*, a bank subsidiary served as trustee for loan pool investors. Slottow, who signed and supervised the trust agreements, was the subsidiary's president and also an officer and director of the parent bank. The investors sued the bank, the subsidiary and Slottow, alleging that the loan pool had been a Ponzi scheme

and that defendants were liable for breach of contract, negligence and breach of fiduciary duty. The trial court dismissed the contract claim against Slottow, and the parties later settled. In evaluating whether the settlement agreement adequately apportioned liability to Slottow on the negligence and breach of fiduciary duty claims, the Ninth Circuit concluded that Slottow faced no liability for breach of fiduciary duty, citing the rule announced in *Grosvenor*.^{FN101}

FN100. Plaintiffs cite several cases holding that officers of a corporate trustee have a fiduciary duty to trust beneficiaries and are liable to the beneficiaries when they know or should have known of a conversion of the trust property to the use of the corporation. See *Middlesex Ins. Co. v. Mann*, 124 Cal.App.3d 558, 572, 177 Cal.Rptr. 495 (1981) (“[A] corporate officer has a fiduciary duty to the beneficiary of a trust and is liable to the beneficiary for wrongful conversion of the trust property to the use of the corporation of which he knew or in the exercise of his fiduciary duties should have known,” citing *Knoblock v. Waale-Camplan Co.*, 141 Cal.App.2d 870, 874, 297 P.2d 765 (1956) (“Both being agents of the corporate trustee, when they thus relieved the corporation of its possession of the trust money, they, individually, were charged with the same duties and obligations as had been imposed upon the corporate trustee”). Plaintiffs do not allege that their investment monies were wrongfully used for bank purposes. Rather, they assert that Slatkin stole the money from them, and that the Banks' purported breaches of fiduciary duty assisted him in this regard. Accordingly, plaintiffs' reliance on *Middlesex* and *Knoblock* is misplaced.

Plaintiffs also cite cases holding that officers may be personally liable for the

torts of the corporation if they are personally involved in those torts. *Haidinger-Hayes*, *supra*, 1 Cal.3d at 594-95, 83 Cal.Rptr. 418, 463 P.2d 770 (“Directors or officers of a corporation do not incur personal liability for torts of the corporation merely by reason of their official position, unless they participate in the wrong or authorize or direct that it be done. They may be liable, under the rules of tort and agency, for tortious acts committed on behalf of the corporation”); *Wyatt v. Union Mortgage Co.*, 24 Cal.3d 773, 785, 157 Cal.Rptr. 392, 598 P.2d 45 (1979) (“Directors and officers of a corporation are not rendered personally liable for its torts merely because of their official positions, but may become liable if they directly ordered, authorized or participated in the tortious conduct”). These cases do not hold that officers owe third parties a “fiduciary duty” in connection with work they perform for their employers. Rather, consistent with the rule announced in *Slottow* and *Grosvenor*, they reaffirm that corporate officers cannot be held liable for breach of their duty to the corporation, but only for torts for which they would be independently liable to third parties. See *Haidinger-Hayes*, *supra*, 1 Cal.3d at 595, 83 Cal.Rptr. 418, 463 P.2d 770 (corporate officers “are not responsible to third persons for negligence amounting merely to nonfeasance, to a breach of duty owing to the corporation alone; the act must also constitute a breach of duty owed to the third person.... Liability imposed upon agents for active participation in tortious acts of the principal have been mostly restricted to cases involving physical injury, not pecuniary harm, to third persons.... More must be shown than breach of the officer's duty to his corporation to impose personal liability

to a third person upon him”). Here, Leider cannot be jointly liable with the Banks for breach of fiduciary duty because she did not independently owe such a duty to plaintiffs. Rather, she owed duties only to her employer.

FN101. Plaintiffs erroneously argue that “even the *Slottow* court would have held the employee in question personally liable had there been ‘personal direction or participation in the tort ...’ ” The excerpt they cite, however, refers only to the negligence claim, not the claim for breach of fiduciary duty. Moreover, as noted earlier, Leider cannot have personally have participated in a breach of fiduciary duty because she owed no duty to plaintiffs.

Here, plaintiffs seek to hold Leider liable for acts performed on behalf of her employer. Because, under California law, Leider owed plaintiffs no duty with respect to such conduct, the breach of fiduciary duty claim against Leider must be dismissed with leave to amend.

F. Whether The Complaint Adequately Pleads Fraud And Negligent Misrepresentation

[31] Plaintiffs' fourth and fifth causes of action, asserted against all defendants, are for fraud and negligent misrepresentation. Their adequacy is challenged by defendants Bank of Orange County and Leider. To state a cause of action for fraud, a plaintiff must allege “(a) misrepresentation (false representation, concealment, or nondisclosure); (b) knowledge of *1141 falsity (or ‘scienter’); (c) intent to defraud, i.e., to induce reliance; (d) justifiable reliance; and (e) resulting damage.” *Engalla v. Permanente Medical Group, Inc.*, 15 Cal.4th 951, 974, 64 Cal.Rptr.2d 843, 938 P.2d 903 (1997); *Lazar v. Superior Court*, 12 Cal.4th 631, 638, 49 Cal.Rptr.2d 377, 909 P.2d 981 (1996) (same); *Anderson v. Deloitte & Touche*, 56 Cal.App.4th 1468, 1474, 66 Cal.Rptr.2d 512 (1997) (same).

[32] The elements of a cause of action for neg-

ligent misrepresentation are the same as those of a claim for fraud, with the exception that the defendant need not actually know the representation is false. Rather, to plead negligent misrepresentation, it is sufficient to allege that the defendant lacked reasonable grounds to believe the representation was true. *B.L.M. v. Sabo & Deitsch*, 55 Cal.App.4th 823, 834, 64 Cal.Rptr.2d 335 (1997) (“ ‘Negligent misrepresentation is a form of deceit, the elements of which consist of (1) a misrepresentation of a past or existing material fact, (2) without reasonable grounds for believing it to be true, (3) with intent to induce another's reliance on the fact misrepresented, (4) ignorance of the truth and justifiable reliance thereon by the party to whom the misrepresentation was directed, and (5) damages,’ ” citing *Fox v. Pollack*, 181 Cal.App.3d 954, 962, 226 Cal.Rptr. 532 (1986)). See also *Glenn K. Jackson Inc. v. Roe*, 273 F.3d 1192, 1201, n. 2 (9th Cir.2001) (“The elements of negligent misrepresentation include: (1) misrepresentation of a past or existing material fact, (2) without reasonable ground for believing it to be true, (3) with intent to induce another's reliance on the misrepresentation, (4) ignorance of the truth and justifiable reliance on the misrepresentation by the party to whom it was directed, and (5) resulting damage”); *Firoozye v. Earthlink Network*, 153 F.Supp.2d 1115, 1128 (N.D.Cal.2001) (“The elements for a claim for negligent misrepresentation are similar [to the elements for fraud]; the plaintiff must show that the defendant made a misrepresentation without reasonable grounds for believing it to be true and that the representation was intended to induce the plaintiff to take some action in reliance upon it,” citing *B.L.M., supra*).

Both Bank of Orange County and Leider argue that the fraud and negligent misrepresentation claims fail to satisfy the heightened pleading standard set forth in Rule 9(b). It is well-established in the Ninth Circuit that both claims for fraud and negligent misrepresentation must meet Rule 9(b)'s particularity requirements. *Glen Holly Entertainment, Inc. v. Tektronix, Inc.*, 100 F.Supp.2d 1086,

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

1093 (C.D.Cal.1999) (“Claims for fraud and negligent misrepresentation must meet the heightened pleading requirements of Rule 9(b)”); *U.S. Concord, Inc. v. Harris Graphics Corp.*, 757 F.Supp. 1053, 1058 (N.D.Cal.1991) (“Defendant further asserts that the negligent misrepresentation claim fails to satisfy Rule 9(b)'s particularity requirements. The point is well-taken. Since the claim is based upon the same flawed allegations of misrepresentation as the fraud count, it, too, fails for lack of specificity”).

Rule 9(b) requires that the facts constituting the fraud or mistake be pled with specificity. Conclusory allegations are insufficient. FED.R.CIV.PROC. 9(b); *Moore v. Kayport Package Exp., Inc.*, 885 F.2d 531, 540 (9th Cir.1989) (“A pleading is sufficient under Rule 9(b) if it identifies the circumstances constituting fraud so that a defendant can prepare an adequate answer to the allegations. While statements of the time, place and nature of the alleged fraudulent activities are sufficient, mere conclusory allegations of fraud are insufficient”); *Walling v. Beverly Enters.*, 476 F.2d 393, 397 (9th Cir.1973) (concluding that allegations stating the time, place, and nature of allegedly fraudulent activities *1142 meet Rule 9(b)'s particularity requirement).

[33] Bank of Orange County and Leider contend that the fraud allegations against them must be dismissed because the third amended complaint fails to allege that either Leider or another Pacific Inland employee made knowingly false representations to any of the named plaintiffs, or that Leider or any other employee was authorized to do so by Pacific Inland. The court agrees. While plaintiffs cite numerous allegations that recite purportedly false statements by Leider,^{FN102} none specifically alleges that Leider knew the representation described was false.

FN102. See, e.g., Third Amended Complaint, ¶¶ 51-61, 67, 69-70, 72, 76, 104, 105 and 116.

[34] Bank of Orange County and Leider similarly argue that the negligent misrepresentation claim against them fails to plead that Leider made the representations alleged lacking reasonable grounds to believe that they were true. Once again, no such allegation appears in the complaint. Accordingly, plaintiffs' claims for fraud and negligent misrepresentation against Bank of Orange County and Leider must be dismissed with leave to amend.

G. Whether The Complaint Adequately Pleads Constructive Fraud

[35] Plaintiffs' sixth cause of action alleging constructive fraud is asserted against all defendants, and challenged by defendants Bank of Orange County and Leider. To state a cause of action for constructive fraud, a plaintiff must allege (1) a fiduciary or confidential relationship; (2) an act, omission or concealment involving a breach of that duty; (3) reliance; and (4) resulting damage. *Assilzadeh v. California Federal Bank*, 82 Cal.App.4th 399, 414, 98 Cal.Rptr.2d 176 (2000) (“Constructive fraud is a unique species of fraud applicable only to a fiduciary or confidential relationship. As a general principle constructive fraud comprises any act, omission or concealment involving a breach of legal or equitable duty, trust or confidence which results in damage to another even though the conduct is not otherwise fraudulent. Most acts by an agent in breach of his fiduciary duties constitute constructive fraud” (citations omitted)). See also *In re Harmon*, 250 F.3d 1240, 1249, n. 10 (9th Cir.2001) (citing *Assilzadeh, supra*).

[36] Bank of Orange County and Leider contend that plaintiffs' constructive fraud claim must be dismissed because neither Pacific Inland nor Leider owed plaintiffs a fiduciary duty. As discussed above, plaintiffs have adequately alleged that Pacific Inland owed them a fiduciary duty, and Bank of Orange County's motion to dismiss the constructive fraud count fails as a result. The court has found, by contrast, that the complaint does not sufficiently allege that Leider had a fiduciary duty to plaintiffs. Accordingly, her motion to dismiss

290 F.Supp.2d 1101
 (Cite as: 290 F.Supp.2d 1101)

this claim is granted with leave to amend.

H. Whether The Complaint Adequately Pleads Negligence

Bank of Orange County challenges the sufficiency of plaintiffs' seventh cause of action for negligence, which is asserted against all defendants. To state a negligence claim, plaintiffs must allege, *inter alia*, that defendants owed them a duty. See, e.g., *Whitfield v. Heckler & Koch, Inc.*, 82 Cal.App.4th 1200, 1217, 98 Cal.Rptr.2d 820 (2000) ("Actionable negligence is traditionally regarded as involving the following: (a) a legal duty to use due care; (b) a breach of such legal duty; (c) the breach as the proximate or legal cause of the resulting injury" (citations omitted)). *1143 Whether one owes another a duty is a question of law. See *Dutton v. City of Pacifica*, 35 Cal.App.4th 1171, 1175, 41 Cal.Rptr.2d 816 (1995).

[37] Bank of Orange County argues that the complaint fails to state a claim for negligence for "the same factual and legal grounds as the negligent misrepresentation count." The court fails to understand this argument. There is no requirement that negligence be pleaded with heightened specificity pursuant to Rule 9(b). Furthermore, the complaint has adequately alleged a negligence claim. It pleads that the Banks had a "duty of reasonable care to their clients to ensure the accuracy, legitimacy, and existence of the assets of the Club."^{FN103} It further alleges that the Banks breached this duty by failing to ensure accuracy, by commingling the assets of Club accounts, and by allowing Slatkin to accept the Club members' funds even though the Banks knew he was not a registered investment advisor.^{FN104} The complaint alleges that Club members suffered damages as a result, and that the damages were proximately caused by the Banks' conduct.^{FN105} Thus, the negligence claim against Bank of Orange County survives under Rule 12(b)(6).

^{FN103}. First Amended Complaint, ¶ 161.

^{FN104}. *Id.*

FN105. *Id.*

I. Whether The Complaint States a Claim For Violation Of California Business And Professions Code § 17200

Plaintiffs' final claim for relief is brought on behalf of the general public, and alleges that the Banks engaged in unfair business practices in violation of California Business & Professions Code §§ 17200 et seq. This claim is brought against all defendants, but once again, is challenged only by Bank of Orange County. To state a cause of action for violation of § 17200, a plaintiff must allege an "unlawful, unfair or fraudulent business act or practice." CAL. BUS. & PROF. CODE § 17200. See also *Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co.*, 20 Cal.4th 163, 180, 83 Cal.Rptr.2d 548, 973 P.2d 527 (1999) ("... as relevant here, [§ 17200] defines "unfair competition to include any unlawful, unfair or fraudulent business act or practice...." Its coverage is sweeping, embracing anything that can properly be called a business practice and that at the same time is forbidden by law.... By proscribing any unlawful business practice, section 17200 borrows violations of other laws and treats them as unlawful practices that the unfair competition law makes independently actionable.... However, the law does more than just borrow. The statutory language referring to any unlawful, unfair or fraudulent practice ... makes clear that a practice may be deemed unfair even if not specifically proscribed by some other law. Because Business and Professions Code section 17200 is written in the disjunctive, it establishes three varieties of unfair competition-acts or practices which are unlawful, or unfair, or fraudulent. In other words, a practice is prohibited as unfair or deceptive even if not unlawful and vice versa" (internal quotations omitted)).

[38] Bank of Orange County argues that plaintiffs' § 17200 claim must be dismissed because the complaint fails to plead an "unlawful, unfair or fraudulent business act or practice" by Pacific Inland. Count eight clearly incorporates the earlier factual allegations supporting counts one through

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

seven, however, and alleges that “[t]he Banks’ actions constitute unfair, illegal, and fraudulent business practices within the meaning of Cal. Bus. & Prof.Code sections 17200 et seq.”^{FN106} Accordingly,*1144 the court finds that the complaint alleges unlawful, unfair or fraudulent business acts or practices sufficient to survive dismissal under Rule 12(b)(6).

FN106. *Id.*, ¶ 163.

J. Whether The Complaint Adequately Pleads Fraudulent Transfer

The ninth cause of action is brought by Neilson pursuant to California’s Uniform Fraudulent Transfer Act (“CUFTA”), California Civil Code § 3439. The claim seeks to avoid and recover intentional fraudulent transfers allegedly made by Slatkin within the seven years preceding his filing of a bankruptcy petition on May 1, 2001. While the claim is asserted against Union Bank, Comerica and Imperial Management, only Imperial contests its sufficiency. Imperial argues that the claim must be dismissed because Neilson has not and cannot plead facts demonstrating that the claim is timely under the applicable four-year statute of limitations.

1. Legal Standards Governing Avoidance Of Fraudulent Transfers Under The California Uniform Fraudulent Transfer Act And 11 U.S.C. § 544(b)

A bankruptcy trustee’s authority to bring a fraudulent transfer claim under the CUFTA derives from section 544(b) of the Bankruptcy Code. *In re Commercial Acceptance Corp.*, 5 F.3d 535, 1993 WL 327833, * 3, n. 3 (9th Cir. Aug.27, 1993) (Unpub.Disp.) (“Section 544(b), 11 U.S.C. provides that a trustee ‘may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim.’ There is no dispute that California’s Uniform Fraudulent Transfer Act, Cal.Civ.Code § 3439, applies in this instance”); *Imperial Corp. of America v. Shields*, No. 92-1003-IEG (LSP), 1997 WL 808628, * 3 (S.D.Cal. Aug.20, 1997) (“Regarding applicable

state law for purposes of Durkin’s § 544 claim, California and Delaware have both enacted the Uniform Fraudulent Transfers Act”); *Durkin v. Shields*, No. 92-1003-IEG (LSP), 1997 WL 808651, * 11 (S.D.Cal. June 5, 1997) (“A trustee may assert state-law theories of fraudulent transfer under 11 U.S.C. § 544(b), which permits a trustee to ‘avoid any transfer of an interest of the debtor in property that is voidable under applicable law by an unsecured creditor with an allowable claim,’ ” quoting 11 U.S.C. § 544(b)).

Section 544(b) provides, in relevant part,

“The trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.” 11 U.S.C. § 544(b)(1).

Federal courts generally limit recovery under § 544(b)(1) to those claims that a creditor of the estate could avoid as fraudulent under applicable state law. See, e.g., *In re Cybergenics Corp.*, 226 F.3d 237, 243 (3rd Cir.2000) (“Section 544(b) is the operative avoidance power at issue here. Specifically, this provision authorizes the avoidance of ‘any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an [allowable] unsecured claim.’ ... The avoidance power provided in section 544(b) is distinct from others because a trustee or debtor in possession can use this power only if there is an unsecured creditor of the debtor that actually has the requisite non-bankruptcy cause of action”); *Sender v. Simon*, 84 F.3d 1299, 1304 (10th Cir.1996) (“If Mr. Sender is bringing claims *1145 belonging to HSA L.P. itself, we fail to see how he can satisfy § 544(b)’s requirements that he establish the existence of an actual unsecured creditor who could avoid the challenged transactions under the applicable law”); *Official Committee of Asbestos Claimants of G-I Holding, Inc. v. Heyman*, 277 B.R. 20, 35

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

(S.D.N.Y.2002) (“To prevail on any of its avoidance claims under § 544(b) the Committee must demonstrate that an actual unsecured creditor exists who could avoid the Transactions under New York law”).

2. Whether The Complaint Adequately Alleges Avoidance Of Fraudulent Transfers Under 11 U.S.C. § 544(b)

Neilson alleges that he is bringing the fraudulent transfer claim on behalf of the named plaintiffs as well as other unnamed unsecured creditors of Slatkin. As the complaint states, “[a]t all relevant times, the transfers of money from Mr. Slatkin to the Banks were voidable under Cal.Civ.Code §§ 3439.04(a) and 3439.07 by one or more of Mr. Slatkin's creditors. These creditors include, but are not limited to, the plaintiffs.”^{FN107} Imperial argues that this allegation is insufficient because, to the extent Neilson purports to act on behalf of the named plaintiffs, the claim is barred by the relevant statute of limitations. It asserts additionally that, to the extent the claim is brought on behalf of unsecured creditors not named in the complaint, it fails because the creditors are not identified. The court evaluates each proposition in turn.

FN107. *Id.*, ¶ 168.

a. Unsecured Claims Of Named Plaintiffs

Imperial argues first that, to the extent Neilson's fraudulent transfer claim is brought on behalf of plaintiffs named in the complaint, it fails because their claims are barred by the relevant statute of limitations. A claim for intentional fraudulent transfer under the CUFTA must be brought within four years after the transfer was made or, if later, one year after the transfer was or reasonably could have been discovered by the claimant. In no event may an action be commenced later than seven years after the date of the transfer. The seven-year reach back period is an exception to the four-year statute of limitations, and applies only where the claimant alleges that he did not discover, and could not reasonably have discovered, the transfer within the four-year period. CAL. CIV. CODE §§ 3439.09(a),

(c); *Cortez v. Vogt*, 52 Cal.App.4th 917, 919, 60 Cal.Rptr.2d 841 (1997) (“Section 3439.09, subdivisions (a) and (b) provide in part that an action by a creditor against a debtor for relief against a transfer or obligation under the UFTA is extinguished unless the action is brought ‘within four years after the transfer was made or the obligation was incurred.’ Section 3439.09, subdivision (a) also provides for a longer statute of limitations of one year after the transfer was or reasonably could have been discovered if the transfer was made with the intent to hinder, delay or defraud any creditor. Section 3439.09, subdivision (c) provides that notwithstanding any other provision of law an action with respect to a fraudulent transfer is ‘extinguished if no action is brought or levy made within seven years after the transfer was made or the obligation was incurred’ ”); *Monastra v. Konica Business Machines, U.S.A., Inc.*, 43 Cal.App.4th 1628, 1645, 51 Cal.Rptr.2d 528 (1996) (same). See also *Bresson v. C.I.R.*, 213 F.3d 1173, 1175 (9th Cir.2000) (“[P]ursuant to California Civil Code § 3439.09(b), claims under Section 3439.04(b) of the CUFTA are ordinarily ‘extinguished’ if they have not been *1146 brought within four years of the relevant fraudulent transfer”).

[39] Imperial contends the claims of the named creditor plaintiffs are time-barred because the third amended complaint fails to allege that they did not know, and could not have discovered, that Slatkin was paying their account fees. As a review of the pleading reveals, however, it clearly alleges that the Banks told investors they were deducting trustee fees from the investors' individual accounts, and that the investors relied on these representations to their detriment.^{FN108} The complaint further alleges that with the Banks' help, Slatkin concealed from his creditors, including plaintiffs, the fact that he had transferred money to the Banks within the seven-year period.^{FN109} Finally, the complaint alleges that the Banks affirmatively misrepresented to Club members that they, and not Slatkin, had transferred money to the Banks for “trustee's fees.”^{FN110} These allegations sufficiently plead that the

290 F.Supp.2d 1101
(Cite as: 290 F.Supp.2d 1101)

creditor plaintiffs did not know of the allegedly fraudulent transfers.

FN108. *Id.*, ¶¶ 74, 97.

FN109. *Id.*, ¶ 169.

FN110. *Id.*

Imperial next argues that, even if the complaint adequately pleads that the named plaintiffs did not know of the transfers within the four-year period, evidence attached to the complaint demonstrates otherwise. Specifically, it points to statements the Banks sent to investors that reflect a monthly entry for “Cash, Receipt, Reimbursement of Trustee Fees.”^{FN111} Defendant contends these monthly entries show that plaintiffs knew the fees were being paid by Slatkin. While the entries raise a question of fact regarding plaintiffs’ knowledge, the court cannot find that such evidence establishes, as a matter of law, that plaintiffs knew or should have known of the transfers at the time they occurred. Additionally, the referenced exhibit reflects only that the Neva and Wesley West Foundation received statements containing such entries. No similar evidence suggesting that other plaintiffs received identical statements is presently in the record. For this additional reason, the court is unable to find, as a matter of law, that the named plaintiffs knew, or should have known, of the allegedly fraudulent transfers within four years after they were made. Accordingly, Imperial’s motion to dismiss the claim on this basis and to the extent asserted on behalf of these creditors is denied.

FN111. *Id.*, Exh. 7 at 142-146.

b. Unsecured Claims Of Unidentified Individuals

Imperial also argues that to the extent plaintiffs assert the claims of individuals not joined in this suit, Neilson’s fraudulent transfer claim fails because the complaint does not identify the creditors for whom he purports to act. Plaintiffs do not dispute that the complaint does not name these individuals. They argue, however, that this is not re-

quired at the pleadings stage.

[40] Federal courts applying fraudulent transfer law at the pleading stage generally require that the complaint allege the *existence* of an actual creditor holding an allowable unsecured claim who could avoid a transfer under applicable state law in the absence of a bankruptcy proceeding. *XL Sports, Ltd. v. Lawler*, 49 Fed. Appx. 13, 23, n. 9, 2002 WL 31260355, * 9, n. 9 (6th Cir. Oct.8, 2002) (“[Section] 544(b) seemingly requires the trustee (or debtor in possession) to at least allege the existence of an unsecured creditor who could avoid the transfer under state law,” citing *1147 *In re Wintz Cos.*, 230 B.R. 848, 859 (8th Cir.BAP1999) (“[I]n order to avail himself of the benefits conferred by § 544(b), and concomitantly, of the MFTA, the Trustee ‘must first show that there is an actual unsecured creditor holding an allowable unsecured claim ... who, under [state] law, could avoid the transfers in question.’ ... Thus far, the Trustee has not only failed to identify such a creditor, but has failed even to allege that such a creditor exists, as he is required to do in order to meet this threshold burden. Accordingly, the Trustee presently lacks standing to pursue his fraudulent transfer actions”)); *In re Meadowbrook Estates*, 246 B.R. 898, 903-04 (Bankr.E.D.Cal.2000) (“Nor does the complaint state a claim for relief under 11 U.S.C. § 544. It does not assert that any pre-petition transfer is avoidable under any of the powers granted to the debtor in possession by section 544(a). Nor does the complaint allege that a pre-petition transfer could be avoided by an actual unsecured creditor under applicable non-bankruptcy law as permitted by section 544(b)”).

Courts are divided, however, as to whether a complaint must specifically allege the identity of the creditor to state a claim under § 544(b). Compare *Zahn v. Yucaipa Capital Fund*, 218 B.R. 656, 673-74 (D.R.I.1998) (“The Complaint clearly satisfies the requirements of Rules 8 and 9(b). ... Plaintiff’s failure to name an existing creditor is of no moment, for he is not required to prove his case

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

at this point; his allegation that such a creditor exists suffices”); *In re Healthco International, Inc.*, 195 B.R. 971, 980 (Bankr.D.Mass.1996) (“... the Trustee alleges he represents ‘at least one qualified, unsecured creditor holding an allowable unsecured claim which existed at the time of the LBO....’ Under the liberal rule of notice pleading, that allegation is enough. The Trustee need not name the creditor”) with *In re Sverica Acquisition Corp., Inc.*, 179 B.R. 457, 464-65 (Bankr.E.D.Pa.1995) (“In support of Count VII the Trustee baldly asserts that ‘[a]t the time of the 1990 leveraged buy-out, an unsecured creditor of the Debtor existed.’ ... Procedurally, this allegation is insufficient to satisfy even the minimal pleading requirements of Fed.R.Civ.P. 8 since it fails to adequately place Defendants on notice of whose rights the Trustee is claiming under. Such notice is imperative here because the Trustee’s rights under Code § 544(b) are derivative of whatever rights the alleged creditor had under state law. It is crucial therefore that Defendants have proper notice of the identity of the alleged creditor in order that they might confirm or deny the validity of that entity’s claim”); *In re Wingspread Corp.*, 178 B.R. 938, 945-46 (Bankr.S.D.N.Y.1995) (“The specific issue with which I must deal is whether the mere allegation of various unsecured creditors is sufficient to invoke section 544(b), or whether the Trustee must allege the existence of a specific unsecured creditor who would have standing to bring the action.... The Defendants contend that the Trustee must name an actual unsecured creditor who would have standing to challenge the transfer. I agree. ‘[B]efore a trustee is able to utilize applicable state or federal law referred to in Section 544(b), there must be an allegation and ultimately a proof of the existence of at least one unsecured creditor of the Debtor who at the time the transfer occurred could have, under applicable local law, attacked and set aside the transfer under consideration,’ ” quoting *Schaps v. Bally’s Park Place, Inc.*, 58 B.R. 581 (E.D.Pa.1986), *aff’d.*, 815 F.2d 693 (3d Cir.1987)); *In re Tri-Star Technologies Co., Inc.*, 260 B.R. 319, 329, n. 10 (Bankr.D.Mass.2001) (“This Court agrees with

those cases which hold that the estate representative must identify the existence of a relevant creditor.... Standing is an essential element of a § 544(b) action...”).

*1148 [41] The court finds these latter cases more persuasive. Rule 8(a) of the Federal Rules of Civil Procedure requires “a short and plain statement of the claim showing that the pleader is entitled to relief.” F ED. R. CIV. PROC. 8(a). Rule 8(a) is designed to ensure that a defendant has fair notice of the nature of the claim and of the facts on which it is based. *Conley, supra*, 355 U.S. at 47-48, 78 S.Ct. 99. See also *In re Marino*, 37 F.3d 1354, 1357 (9th Cir.1994) (noting that the federal courts’ liberal pleading policy “does not justify the conclusion that any document filed in a court giving some notice of claim satisfies the requirements of the Federal Rules”). “Effective pleading ... provide[s] the defendant with a basis for assessing the initial strength of the plaintiff’s claim, for preserving relevant evidence, for identifying any related counter- or cross-claims, and for preparing an appropriate answer.” *Grid Systems Corp. v. Texas Instruments Inc.*, 771 F.Supp. 1033, 1037 (N.D.Cal.1991). Unless Neilson is required to allege specifically the identity of the unsecured creditor(s) whose rights he is asserting, defendants will have no way to “assess[] the initial strength of [his] claim, ... preserv[e] relevant evidence, ... identify[] any related counter- or cross-claims, and ... prepar[e] an appropriate answer.” *Id.* Accordingly, the court grants Imperial’s motion to dismiss Neilson’s fraudulent transfer claim to the extent it relies on the existence of unidentified unsecured creditors who could avoid the transfers under state law in the absence of the bankruptcy proceeding. Neilson may amend to identify these creditors, or remove reference to them from the complaint.

K. Whether Plaintiff Fred Ockrim’s Claims Are Barred By Res Judicata

Union Bank and the Bank of Orange County contend that all of plaintiff Fred Ockrim’s claims are barred by res judicata. It is undisputed that

Ockrim was named as a plaintiff in the first amended complaint filed in a related case, *Christensen v. Union Bank*, CV 02-00608 MMM (CWx). The court dismissed all claims in the *Christensen* first amended complaint on September 18, 2002, and directed that the *Christensen* plaintiffs file any amended complaint within twenty days of the date of the order. This deadline was subsequently extended one week pursuant to stipulation of the parties. The *Christensen* plaintiffs timely filed a second amended complaint on October 15, 2002. Ockrim, however, did not join the second amended complaint. Instead, he withdrew from the *Christensen* case and became a plaintiff in this case. Union Bank accordingly moved to dismiss Ockrim's claims in *Christensen* pursuant to Rule 41(d) for failure to comply with the court's order. The court granted this motion and dismissed Ockrim's claims with prejudice on January 8, 2003. Union Bank and the Bank of Orange County argue that Ockrim's claims in the instant suit are now barred by res judicata.

[42][43] “Res judicata, also known as claim preclusion, bars litigation in a subsequent action of any claims that were raised or could have been raised in the prior action.” *Owens v. Kaiser Foundation Health Plan, Inc.*, 244 F.3d 708, 713 (9th Cir.2001) (quoting *Western Radio Servs. Co. v. Glickman*, 123 F.3d 1189, 1192 (9th Cir.1997)); *Robi v. Five Platters, Inc.*, 838 F.2d 318, 321 (9th Cir.1988) (“Claim preclusion ‘prevents litigation of all grounds for, or defenses to, recovery that were previously available to the parties, regardless of whether they were asserted or determined in the prior proceeding.’” quoting *Brown v. Felsen*, 442 U.S. 127, 137, 99 S.Ct. 2205, 60 L.Ed.2d 767 (1979)). The doctrine is applicable whenever there is “(1) an identity of claims, (2) a final judgment on the merits, and (3) identity or *1149 privity between parties.” *Owens, supra*, 244 F.3d at 713; *Western Radio, supra*, 123 F.3d at 1192 (same); *Robi, supra*, 838 F.2d at 324 (same).

[44] Ockrim's claims against the Bank of Or-

ange County are not barred by res judicata for the simple reason that Bank of Orange County was not, and is not, in privity with any of the parties in *Christensen*. The Ninth Circuit has recognized that a non-party who has succeeded to a party's interest in property is in privity with that party and bound by any prior judgment against it. See *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 322 F.3d 1064, 1082 (9th Cir.2003) (“Federal courts have deemed several relationships ‘sufficiently close’ to justify a finding of ‘privity’ and, therefore, preclusion under the doctrine of res judicata: ‘First, a non-party who has succeeded to a party's interest in property is bound by any prior judgment against the party,’” quoting *In re Schimmels*, 127 F.3d 875, 881 (9th Cir.1997)). Here, the third amended complaint alleges that Bank of Orange County is the direct successor-in-interest to Pacific Inland Bank.^{FN112} It also alleges that Union Bank is the successor-in-interest to the trust business of Imperial Trust.^{FN113} The remainder of Imperial Trust was merged into Imperial Management.^{FN114} While Bank of Orange County argues that Imperial Trust Company is the successor-in-interest to Pacific Inland Bank, the complaint does not so allege, and Bank of Orange County offers no evidence to support this assertion. Even accepting the truth of the bank's claim, the transfers and acquisitions are such that they are is not, without more, sufficient to support a finding that the Bank of Orange County a privy of Union Bank. Thus, Bank of Orange County cannot use affirmatively against Ockrim the dismissal with prejudice of his claims against Union Bank in the *Christensen* suit.^{FN115}

FN112. *Id.*, ¶ 31.

FN113. *Id.*, ¶ 27.

FN114. *Id.*, ¶ 30.

FN115. The court does not finally decide this issue because the record presently before it concerning the nature of the transfers of ownership is incomplete and am-

biguous. Bank of Orange County may, if it is able to demonstrate that it is in privity with Union Bank, raise the issue at a later point in the proceedings.

Union Bank, however, can invoke the doctrine of res judicata to bar Ockrim's claims in this action, as all prerequisites to the application of the doctrine have been met. First, there was clearly a final judgment on the merits in *Christensen* dismissing all of Ockrim's claims with prejudice. Second, this action involves the same claims Ockrim asserted in *Christensen*, as well as several new claims that Ockrim could have asserted there. Finally, there is an identity of parties, as Ockrim was a plaintiff and Union Bank a defendant in *Christensen*, and both are parties to the instant suit as well.

Plaintiffs do not dispute that the prerequisites to the application of claim preclusion have been satisfied as respects Union Bank. They argue, however, that Ockrim's claims against Union Bank are not barred by res judicata because Union Bank stipulated that Ockrim could be added as a named plaintiff in this case. Specifically, plaintiffs cite a stipulation regarding a briefing schedule on defendants' motions to dismiss the first amended complaint signed by all parties, and the order thereon entered by the court on October 28, 2002.^{FN116} The stipulation provides:

FN116. Declaration of Christopher Casamassima in Support of Plaintiff's Oppositions to Union Bank of California, N.A.'s, Comerica Bank-California's, and Bank of Orange County's Motions to Dismiss Plaintiff's Third Amended Complaint ("Casamassima Decl."), Exh. 3.

*1150 "... In the interest of providing a uniform and mutually agreeable briefing schedule on defendants' respective motions to dismiss the First Amended Complaint,

1. Plaintiffs' opposition papers to the motions filed by defendants on October 25, 2002 shall be

filed and served by November 18, 2002.

2. Defendants' reply papers shall be filed and served by December 9, 2002.

3. The hearing on the motions shall take place on January 6, 2003."^{FN117}

FN117. *Id.*

The stipulation also contains a footnote, which states: "Plaintiffs have represented to defendants that they would be filing their First Amended Complaint ("FAC") simultaneously with the filing of defendants' motions on October 25, 2002. Plaintiffs further represented that the FAC would be identical to the original complaint filed September 5, 2002 with the exceptions that: (1) a Mr. Fred Ockrim would be added as a named plaintiff; and (2) a single paragraph would be added describing Mr. Ockrim and his relation to the case."^{FN118}

FN118. *Id.*

Plaintiffs argue this pleading clearly demonstrates that the Banks stipulated to the joinder of Ockrim as a plaintiff in this case, and that they waived any res judicata objections they might otherwise have to his claims. Union Bank counters that the stipulation concerned a briefing schedule for the motions to dismiss. Neither interpretation is the only reasonable construction that could be given to the language of the stipulation. Rather, whether the stipulation was intended solely to set forth a briefing schedule or also to encompass an agreement regarding the addition of Ockrim as a plaintiff is unclear on the face of the document.

Several factors favor defendants' interpretation of the stipulation. The title of the stipulation suggests that it memorializes only an agreement regarding a briefing schedule on the motions to dismiss, and the bulk of the language found in the stipulation addresses this subject. The footnote that discusses Ockrim, moreover, does not directly recite Union Bank's agreement to have him added as a

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

plaintiff. It simply memorializes the fact that he will be named in the first amended complaint.

Other aspects of the stipulation, however, arguably favor plaintiffs' interpretation. While the footnote concerning Ockrim's addition as a plaintiff does not expressly waive any objections by Union Bank, for example, it also does not explicitly assert objections. Its silence on the point could be read as implicit acquiescence in the amendment described. Union Bank clearly knew that Ockrim was one of the *Christensen* plaintiffs. Given this fact, its failure to note a specific objection to his joinder as a plaintiff could be viewed as significant. Certainly, the matter is not entirely unambiguous.

Plaintiffs assert that Ockrim "never would have entered into the stipulation with defendants to join the *Neilson* action as a named plaintiff (and by doing so given up his opportunity to file an amended complaint in *Christensen*) if he believed defendants would assert *res judicata* to bar his claims." Union Bank labels this argument illogical, noting that Ockrim had already given up his opportunity to file an amended complaint in *Christensen* before he sought to join *Neilson* as a named plaintiff. The second amended complaint in *Christensen* was filed on October 16, 2003. Ockrim was not named as a plaintiff in that pleading. Union Bank has proffered evidence that it was not until October 17, *1151 2002—one day *after* Ockrim failed to join the second amended complaint in *Christensen*—that plaintiffs sought to add him as a party in this case. Union Bank's counsel declares: "The parties met and conferred on defendants' motion to dismiss Plaintiffs' original complaint on October 17, 2002. This was the first time Plaintiffs ... mentioned to Union Bank their intent to add Fred Ockrim as a named plaintiff in *Neilson*. It was also the first time Union Bank ... heard from any source that Ockrim intended to join *Neilson*." FN119 Given this chronology, Union Bank argues, Ockrim abandoned his *Christensen* claims before plaintiffs ever raised the idea of adding him as a plaintiff in *Nielson*. Plaintiffs do not dispute these facts, and proffer no evidence to

the contrary.

FN119. Declaration of Martin Pritikin, ¶ 6.

[45] While the weight of the evidence currently before the court supports Union Bank's position, the matter has been raised in the context of a motion to dismiss brought pursuant to Rule 12(b)(6). In deciding such a motion, the court's review is limited to the contents of the complaint, exhibits attached thereto and matters that are properly the subject of judicial notice. *Branch, supra*, 14 F.3d at 454; *Hal Roach Studios, supra*, 896 F.2d at 1555, n. 19. While the stipulation is the type of court document that can be judicially noticed, the parties' intent in entering into the stipulation is not. See *Jones, supra*, 29 F.3d at 1553 (court may take judicial notice of court documents only for the purpose of recognizing "the 'judicial act' that the order represents on the subject matter of the litigation"). This is particularly true where the parties dispute the import of the agreement memorialized in the stipulation and the document is not unambiguous on its face.

While the parties proffer evidence regarding the manner in which the stipulation should be interpreted, the court may not weigh evidence in deciding a motion to dismiss. See, e.g., *Official Committee of Unsecured Creditors of Color Tile, Inc. v. Coopers & Lybrand, LLP*, 322 F.3d 147, 158 (2d Cir.2003) ("A court's task 'in ruling on a Rule 12(b)(6) motion is merely to assess the legal feasibility of the complaint, not to assay the weight of the evidence which might be offered in support thereof,' " quoting *Cooper v. Parsky*, 140 F.3d 433, 440 (2d Cir.1998)); *County of Santa Fe, N.M. v. Public Service Co. of New Mexico*, 311 F.3d 1031, 1035 (10th Cir.2002) (" 'The court's function on a Rule 12(b)(6) motion is not to weigh potential evidence that the parties might present at trial, but to assess whether the plaintiff's complaint alone is legally sufficient to state a claim for which relief may be granted,' " quoting *Miller v. Glanz*, 948 F.2d 1562, 1565 (10th Cir.1991)); *Baird ex rel. Baird v. Rose*, 192 F.3d 462, 468, n. 6 (4th Cir.1999) ("[I]t is inap-

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

propriate in addressing the appropriateness of a dismissal under Rule 12(b)(6) to make a determination concerning the weight of the evidence that ultimately may be presented in support of these various positions,") citing Charles A. Wright & Arthur R. Miller, *FEDERAL PRACTICE & PROCEDURE*, § 1356 (2d ed.1990) (explaining that "[t]he purpose of a motion under Rule 12(b)(6) is to test the formal sufficiency of the statement of the claim for relief; it is not a procedure for resolving a contest about the facts or the merits of the case"); *Jones v. Johnson*, 781 F.2d 769, 772, n. 1 (9th Cir.1986) ("[A]ny weighing of the evidence is inappropriate on a 12(b)(6) motion"); *Glen Holly Entertainment, Inc. v. Tektronix, Inc.*, 100 F.Supp.2d 1086, 1089 (C.D.Cal.1999) ("On a motion to dismiss, the Court evaluates only the legal sufficiency of a complaint *1152 and not the weight of the evidence supporting it").

Since Ockrim has stated cognizable claims against Union Bank, and since the court is unable to determine, as a matter of law, whether those claims are barred by res judicata, it must allow them to proceed. Union Bank's motion to dismiss Ockrim's claims as barred by res judicata is therefore denied without prejudice to its right to renew the argument at a later stage of the litigation.

L. Union Bank's Motion To Strike

Rule 12(f) provides that a court "may order stricken from any pleading any insufficient defense or any redundant, immaterial, impertinent, or scandalous matter." FED.R.CIV.PROC. 12(f). Motions to strike are generally regarded with disfavor because of the limited importance of pleading in federal practice, and because they are often used as a delaying tactic. See *Lazar v. Trans Union LLC*, 195 F.R.D. 665, 669 (C.D.Cal.2000); *Bureerong v. Uvawas*, 922 F.Supp. 1450, 1478 (C.D.Cal.1996); *Colaprico v. Sun Microsystems, Inc.*, 758 F.Supp. 1335, 1339 (N.D.Cal.1991). Given their disfavored status, courts often require "a showing of prejudice by the moving party" before granting the requested relief. *Securities and Exchange Commission v.*

Sands, 902 F.Supp. 1149, 1166 (C.D.Cal.1995) (citations omitted). The possibility that superfluous pleadings will cause the trier of fact to draw "unwarranted" inferences at trial is the type of prejudice that will support the granting of a motion to strike. See *Fantasy, Inc. v. Fogerty*, 984 F.2d 1524, 1528 (9th Cir.1993) (holding that the district court properly struck lengthy, stale and previously litigated factual allegations to streamline the action), rev'd. on other grounds, *Fogerty v. Fantasy, Inc.*, 510 U.S. 517, 114 S.Ct. 1023, 127 L.Ed.2d 455 (1994).

[46][47] Ultimately, whether to grant a motion to strike lies within the sound discretion of the district court. *Fantasy, supra*, 984 F.2d at 1528. In exercising its discretion, the court views the pleadings in the light most favorable to the non-moving party (see *In re 2TheMart.com Securities Litigation*, 114 F.Supp.2d 955, 965 (C.D.Cal.2000)), and resolves any doubt as to the relevance of the challenged allegations in favor of plaintiff. This is particularly true if the moving party demonstrates no resulting prejudice. *Wailua Assocs. v. Aetna Casualty and Surety Co.*, 183 F.R.D. 550, 553-54 (D.Haw.1998) ("Matter will not be stricken from a pleading unless it is clear that it can have no possible bearing upon the subject matter of the litigation; if there is any doubt as to whether under any contingency the matter may raise an issue, the motion may be denied ...").

Union Bank moves to strike (1) allegations in paragraph 90 regarding corporate banking practices in general rather than practices of Union Bank in particular; (2) allegations in paragraph 102 referring to the Banks' alleged motive as "GREED". The court addresses each argument in turn.

[48] Union Bank first seeks to strike the sentence in paragraph 90 of the third amended complaint that states: "In a world where banks charge ever-increasing fees to customers who bounce \$10 checks, Union Bank's actions are all the more telling." Union Bank argues that allegations concerning the business practices of other banks are

290 F.Supp.2d 1101

(Cite as: 290 F.Supp.2d 1101)

immaterial to plaintiffs' specific allegations of misconduct in this case. Instead, Union Bank contends, they serve no purpose other than to confuse the issues and prejudice it. While plaintiffs argue that the allegations "are not only true, but it places Union Bank's actions into context," they are, in fact, immaterial and *1153 unnecessary. Furthermore, they serve to prejudice Union Bank since they seek to associate it with practices that are not at issue in this case. Because the matter is not material to the instant dispute and potentially prejudicial, the court grants the bank's motion to strike the referenced sentence in paragraph 90.

[49] Union Bank also seeks to strike the rhetorical question that appears in paragraph 102 of the third amended complaint—"Why then did the Banks lend Mr. Slatkin the hand he needed? *The Banks' motive: GREED.*" Union Bank argues this invective does nothing to inform it of the charges it must answer, but serves only to inflame and should be stricken. While plaintiffs contend the statement is true and places Union Bank's motives in context, the court agrees with the bank that the allegation is unnecessary. Accordingly, Union Bank's motion to strike this allegation is also granted.

III. CONCLUSION

For the reasons stated, the court grants Comerica Bank of California's motion to dismiss the third amended complaint with prejudice. The court grants with leave to amend (1) the motions of Bank of Orange County and Leider to dismiss plaintiffs' fraud and negligent misrepresentation claims; and (2) Leider's motion to dismiss plaintiffs' claims for breach of fiduciary duty and constructive fraud. The court grants in part and denies in part (1) Imperial's motion to dismiss plaintiffs' claim to avoid and recover intentional fraudulent transfers using a seven-year reach back period; and (2) Leider's motion to dismiss plaintiffs' claims for aiding and abetting. Plaintiffs are given leave to amend these claims to address the deficiencies noted in this order. The court denies (1) the motions of Imperial Management, Union Bank, and Bank of Orange

County to dismiss plaintiffs' claims for aiding and abetting; (2) Bank of Orange County's motion to dismiss plaintiffs' claims for breach of fiduciary duty, constructive fraud, negligence, and violation of Business & Professions Code § 17200; and (3) the motions of Union Bank and Bank of Orange County to dismiss all claims of plaintiff Fred Ockrim with prejudice. Finally, the court grants Union Bank's motion to strike the first sentence of paragraph 90 and the entirety of paragraph 102. Plaintiffs may file an amended complaint within twenty days of the date of this order.

This order disposes of Docket Nos. 138, 141, 142, 145, 150, 151, 152, 165, 166, 167, and related pleadings.

C.D.Cal.,2003.

Neilson v. Union Bank of California, N.A.

290 F.Supp.2d 1101

END OF DOCUMENT

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

▷
NORTHERN NATURAL GAS COMPANY OF
OMAHA, NEBRASKA, et al., Petitioners,
v.
THE SUPERIOR COURT OF FRESNO COUNTY,
Respondent; NED S. VAN DUYNÉ, Real Party in
Interest

Civ. No. 3176.

Court of Appeal, Fifth District, California.
December 17, 1976.

SUMMARY

A natural gas corporation and its wholly owned subsidiary, a propane gas corporation, sought relief by mandamus following denial by the superior court of their motions to quash service of summons on the ground that they were foreign corporations not engaged in business in the State of California and not otherwise subject to the jurisdiction of the California courts. The action against them was by a licensee alleging fraud and breach of the license agreement by a company, organized and controlled by the foreign subsidiary, that manufactured and marketed pool chlorination devices. The Court of Appeal granted the writ, directing the trial court to set aside its order denying the motion of the natural gas corporation, and holding that California jurisdiction was not established by the mere fact that its wholly owned subsidiary might be subject to California jurisdiction. The court further held, however, that its foreign subsidiary was subject to such jurisdiction in light of evidence showing that it was a member of a joint venture engaged in business in California through the pool chlorination manufacturer and marketer as its agent or instrumentality. (Opinion by Loring, J., ^{FN*} with Brown (G. A.), P. J., and Gargano, J., concurring.)

FN* Assigned by the Chairman of the Judicial Council.

HEADNOTES

Classified to California Digest of Official Reports (1a, 1b, 1c) Corporations § 53--Foreign Corporations--Subsidiary Subject to California Jurisdiction--Effect.

In a breach of contract and fraud action against two foreign corporations, the fact that one was the wholly owned subsidiary of the other did not render the parent corporation subject to California jurisdiction even though the subsidiary was so subject, having engaged with a third corporation in a joint venture in California. There was no showing that the parent was a party to or had imputed knowledge of such venture; moreover, the parent itself had done no intrastate business in California, and, though engaged in interstate commerce, was entitled to avoid suit in California, having filed its certificate of surrender more than two years before service in the action (Corp. Code, § 6504).

(2) Corporations § 53--Foreign Corporations--Parent and Subsidiary-- Jurisdiction.

Jurisdiction of a wholly owned subsidiary does not give a court jurisdiction of the parent corporation.

(3) Corporations § 40--Corporate Liability--Parent and Subsidiary.

A parent corporation is not liable on a contract, or for tortious acts, of its subsidiary simply by reason of its being a wholly owned subsidiary; some other basis of liability must be established.

(4a, 4b, 4c, 4d, 4e) Corporations § 53--Foreign Corporations-- California Jurisdiction--Effect of Joint Venture.

In an action, against a foreign parent and a foreign subsidiary corporation, by a licensee alleging breach of the license agreement and fraud, the subsidiary was subject to the jurisdiction of the California courts where there was uncontradicted evidence that it had specially organized a third corporation, as its agent, to engage in a joint venture in California and where the subsidiary's president was also president and chairman of the board of the

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

third corporation and was thus, under the doctrine of imputed knowledge, chargeable with knowledge of the inducements and representations made by the third corporation as to the joint venture relationship.

[See **Cal.Jur.3d**, Corporations, § 387; **Am.Jur.2d**, Foreign Corporations, § 347.]

(5) Agency § 27--Duties of Agents to Principal--Information.

An agent is under a duty to inform his principal of matters, in connection with the agency, that the principal would desire to know about.

(6) Agency § 30--Liabilities--Imputed Knowledge--Principal and Subagent.

The doctrine of imputed knowledge applies in the relationship of principal and subagent where the latter's employment by the agent is authorized or ratified.

(7) Corporations § 53--Foreign Corporations--Subsidiary Used as Agent-- Jurisdiction.

Where a foreign corporation uses a wholly owned subsidiary as a mere agent or instrumentality of the foreign parent corporation, then the state may exercise jurisdiction over the foreign corporation.

(8) Agency § 2--Distinctions--Alter Ego--Agency.

Agency and alter ego are two different and distinct concepts. In the case of an alter ego, the court pierces the corporate veil; in the case of an agency, the corporate identity is preserved but the principal is held liable for the acts of its agent.

(9) Courts § 10--Jurisdiction--In Actions for Fraud.

Where charges of fraud on California citizens are involved, jurisdictional principles should be liberally construed.

(10) Mandamus and Prohibition § 27--To Courts--Quashing Service of Summons--Mandamus.

When a trial court erroneously denies a motion to quash service of summons made on the ground that the court has no personal jurisdiction over the moving party, mandamus is the appropriate remedy to review the erroneous ruling.

COUNSEL

McCormick, Barstow, Sheppard, Coyle & Wayte and Michael W. Case for Petitioners.

No appearance for Respondent.

Kelly, Leal & Olimpia and Stanley F. Leal for Real Party in Interest. *986

LORING, J. ^{FN*}

FN* Assigned by the Chairman of the Judicial Council.

Northern Natural Gas Company of Omaha, Nebraska, a Delaware corporation (Natural Gas) and Northern Propane Gas Company of Minneapolis, Minnesota, a Delaware corporation (Propane Gas) were sued as defendants in respondent court in an action filed by Ned S. Van Duyne, (Van Duyne), real party in interest. Natural Gas and Propane Gas filed motions to quash service of summons on the ground that they were foreign corporations not engaged directly or indirectly in business in the State of California and not otherwise subject to the jurisdiction of California. The motions were opposed by Van Duyne and were denied by respondent court. Natural Gas and Propane Gas sought relief through mandamus. We granted an order to show cause.

We conclude that respondent court correctly denied the motion of Propane Gas to quash service of summons, but erroneously denied the motion of Natural Gas to quash service of summons. A peremptory writ will be issued accordingly.

The affidavits in connection with the motion before respondent court disclosed the following facts with reference to petitioners Natural Gas and Propane Gas:

Facts About Natural Gas Company

F. Vincent Roach, vice president and general counsel of Natural Gas made an affidavit filed in respondent court in which he stated that Natural

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

Gas is a Delaware corporation with offices in Omaha, Nebraska. It transacts business in certain midwestern and southwestern states, the business consisting of the operation of a 19,990-mile natural gas pipeline system in 12 states (excluding California), for the distribution of natural gas to 74 utility customers in 1,094 communities with a population of 5.9 million. These communities are located in 11 states in the upper midwest. Natural Gas's retail distribution system sells natural gas to residential, commercial, industrial and agricultural customers in eight states (excluding California). (1a) The affidavit alleges that the corporation is not qualified to *987 do business in the State of California^{FN1} and does not engage in business activities, maintain an office or offices, maintain books and records, own real property, own tangible personal property, manufacture products, perform services, make sales of goods, maintain a stock of goods, have full or part time salesmen or sales agents offering its products for sale, or conduct activities as a member of a partnership, joint venture or limited partnership, in the State of California.

FN1 Natural Gas was qualified to do business in California during the period of April 22, 1966 to December 18, 1973. However, service of process was made sometime after March 26, 1976. Under California Corporations Code section 6504, where a foreign corporation is engaged solely in *interstate* business, if it ceases to do business before service, the corporation can avoid suit in this state. (I Witkin, Cal. Procedure (2d ed. 1970) Jurisdiction, § 110, p. 641; *Detsch & Co. v. Calbar, Inc.* (1964) 228 Cal.App.2d 556 [39 Cal.Rptr. 626].) In the present case, there is no allegation of any *intrastate* business by Natural Gas in California at any time. Therefore, once Natural Gas filed its certificate of surrender on December 18, 1973, it was no longer subject to the jurisdiction of California courts based on its "doing business" in California.

Facts About Propane Gas Company

Gale M. Colburn, vice president of Propane Gas filed an affidavit in respondent court in which he stated that Propane Gas is a Delaware corporation. It has offices in Minneapolis, Minnesota, and transacts business in 21 midwestern and eastern states, the business consisting of the operation of 283 retail and bulk plant propane operations. It serves 265,000 customers in the midwest and eastern United States under the name "Norgas" and it is primarily a retail seller of propane gas with wholesale propane gas purchase and sales operations. Associated appliances are also marketed by the corporation at its retail outlets. It employs approximately 1,600 people throughout its area of service. The affidavit alleged that the corporation is not qualified to do business in the State of California and does not maintain an office or offices, maintain books and records, own real property, own tangible or intangible property, manufacture products, perform services, make sales of goods, maintain a stock of goods, have full or part time salesmen or sales agents, or conduct activities as a member of a partnership, joint venture or limited partnership, in the State of California.

The lawsuit pending before respondent court arose out of a "license agreement" between Van Duyne and Geni-Chlor International, Inc., a Delaware corporation (Geni-Chlor) dated April 12, 1974, which Van Duyne claimed had been breached to his damage. Van Duyne also alleged a cause of action for fraud against the defendants. The corporate*988 identity of Geni-Chlor as disclosed by such affidavits in support of the motion and in opposition of the motion may be briefly summarized as follows:

Facts About Geni-Chlor

The forerunner of Geni-Chlor was S. K. & A. Development Corporation. In 1970, Mr. Dan Tucker purchased S. K. & A. and commenced work to manufacture and market pool chlorination devices. Mr. Tucker's intention was to develop a pool purifier/chlorination unit operating on a principle of elec-

64 Cal.App.3d 983, 134 Cal.Rptr. 850
 (Cite as: 64 Cal.App.3d 983)

trollysis. After a period of testing, Mr. Tucker became satisfied with the unit and in early 1972 began to market the unit in the Concord, California area through Damoto Products, Incorporated. Also in 1972, S. K. & A. became associated with International Consolidated Industries of Oakland, California, for the purpose of developing a national marketing program.

On December 18, 1972, Geni-Chlor was formed under the laws of Delaware. On January 4, 1973, Geni-Chlor acquired the assets of S. K. & A. Geni-Chlor maintains offices and a manufacturing plant in Concord, California, and has a designated agent to receive service of process in California.

Geni-Chlor is a subsidiary of Propane Gas, which in turn is a wholly owned subsidiary of Natural Gas.^{FN2}

FN2 A "subsidiary corporation" is defined in California Corporations Code section 118:

"If a corporation, domestic or foreign, has power either directly or indirectly or through another corporation or series of other corporations, domestic or foreign, to elect a majority of the directors of another corporation, domestic or foreign, any of the corporations having controlling power is a 'holding corporation' in its relation to any corporation which it so controls, and any corporation which is subject to such control is a 'subsidiary' corporation in its relation to any such controlling corporation."

Darwin A. Larson is both president of Propane Gas and the president and chairman of the board of Geni-Chlor. Stephen Sulentic and Calvin Forbes are both directors of Geni-Chlor and officers of Propane Gas. Mr. Sulentic is also a director of Propane Gas.

In a bulletin entitled "The Geni-Chlor Story,"

issued by Geni-Chlor to its distributors, the distributors were informed that Geni-Chlor and Propane Gas had in 1972 entered into a joint venture agreement to build and market the Geni-Chlor pool purifier. Propane Gas was already a*989 distributor of Geni-Chlor, marketing Geni-Chlor pool purifiers on the west coast of Florida.

Also in the bulletin entitled "The Geni-Chlor Story," reference was made to Natural Gas and its financial position and that of its subsidiaries, including the fact that Natural Gas was traded on the New York Stock Exchange.

In another bulletin entitled "Selling the Company," it is stated that on December 18, 1969, Geni-Chlor became associated with Propane Gas, a wholly owned subsidiary of Natural Gas. Also, in November of 1974, Propane Gas bought controlling interest in Geni-Chlor. The same bulletin gives the following model question and answer from a sales training manual circulated among Geni-Chlor distributors:

"Objection No. 6: How do I know your company [Geni-Chlor] will be around when a part goes bad?

"Answer: ... First, let me reemphasis [*sic*] the credibility of Northern Natural Gas. This company has been in business for many years. I think it is quite safe to state that they are going to be around for a good many more years.

"As far as Geni-Chlor International is concerned, they have been operating successfully for about 5 years, and of course, they are owned by Northern Natural Gas."

In his affidavit in opposition to the motion Van Duynes stated:

"Employees of Geni-Chlor International, Inc., including J. Michael Walker who is vice president and general manager of Geni-Chlor and a member of the board of directors of Geni-Chlor, induced me to enter into the licensing contract attached to my

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

complaint by informing me that Geni-Chlor International and Northern Propane Gas Company had in 1972 entered into a joint venture agreement to both build and market the Geni-Chlor pool purifier. That as of this time (April, 1974) Northern Propane Gas Company held an option to purchase virtually all of the Geni-Chlor stock; that the defendant Northern Gas Company was standing behind Geni-Chlor; that the Northern Natural Gas companies were large and financially solvent companies listed on the New York Stock Exchange and that as a licensee with Geni-Chlor, I could rely*990 upon the money and prestige of the Northern Gas companies. At this time and in this regard, I was supplied with the Geni-Chlor Story, which is marked Exhibit A and attached hereto and incorporated herein.

“The consolidated financial position of Northern Natural Gas and its subsidiary companies, referred to in the 'Geni-Chlor Story,' were also supplied to me at this time so that I might appreciate the significant financial backing upon which I might expect to rely. The attached 'Geni-Chlor Story' also makes reference to the joint venture relationship between Geni-Chlor International and Northern Propane Gas Company.”

At another point in his affidavit, Van Duyne stated:

“At many sales meetings I was advised, as were other licensees in California to establish 'credibility' of the product by making people aware of the financial position, status and 'credibility' of Northern Propane Gas Company and of Northern Natural Gas Company. This advice was received by me from employees of Geni-Chlor who were operating under the direction and control of Mr. Lars Larson, who at all times was president of Geni-Chlor, chairman of its board of directors and also president of Northern Propane Gas Company.

“Northern Propane Gas Company was thereby aware of the inducements and representations made as to its responsibility for the product sold by its subsidiary.”

A bulletin from Geni-Chlor instructs its distributors not to associate the Geni-Chlor name with Propane Gas or Natural Gas in their *marketing* programs. Any such advertising was not to be made without the written authorization of Geni-Chlor who, in turn, was to have the written permission of Natural Gas. However, the distributors were also informed that Geni-Chlor was working with Propane Gas and Natural Gas to establish such an advertising policy, and that they would be notified when Geni-Chlor received authorization.

The allegations of the Van Duyne affidavit were not specifically denied.

Discussion

The propriety of the denial of the motion to quash service of summons is readily disposed of insofar as Natural Gas is concerned. Natural Gas, *991 a foreign corporation not engaged in business in California, was at most only a parent of Propane Gas, its wholly owned subsidiary. Regardless of whether or not Propane Gas was subject to the jurisdiction of California, it is clear that Natural Gas was not merely because Propane Gas was its wholly owned subsidiary. (2) It is well established that jurisdiction of a wholly owned subsidiary does not give a court jurisdiction of the parent corporation. (*Watson's Quality Turkey Products, Inc. v. Superior Court* (1974) 37 Cal.App.3d 360, 364 [112 Cal.Rptr. 345]; *Westinghouse Electric Corp. v. Superior Court* (1976) 17 Cal.3d 259, 274 [131 Cal.Rptr. 231, 551 P.2d 847]; *Cannon Mfg. Co. v. Cudahy Packing Co.* (1925) 267 U.S. 333, 336-338 [69 L.Ed. 634, 642-643, 45 S.Ct. 250]; 1 Witkin, *Cal. Procedure* (2d ed. 1970) *Jurisdiction*, § 106, pp. 636-637; *Code Civ. Proc.*, § 410.10 (com.); *Rest.2d Conf. of Laws*, § 52, com. b.)

(3) A parent corporation is not liable on the contract or for the tortious acts of its subsidiary simply because it is a wholly owned subsidiary. Some other basis of liability must be established. “*Stock ownership alone is not enough.*” (6 Witkin, *Summary of Cal. Law* (8th ed. 1974) *Corporations*, § 11, p. 4323 (italics in original).)

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

(1b) Natural Gas therefore was not subject to the jurisdiction of California courts solely by reason of the fact that Propane Gas was its wholly owned subsidiary. We can find no other basis for jurisdiction. The trial court therefore committed error in refusing to grant the motion of Natural Gas to quash service of summons. A peremptory writ will therefore issue as to Natural Gas.

(4a) The motion of Propane Gas to quash service of summons presents a different problem. There was uncontradicted evidence before the trial court that Geni-Chlor had been specially organized to carry out a joint venture association with Propane Gas. In his affidavit in opposition to the motion of Propane Gas to quash service of summons, Van Duyne stated: "Employees of Geni-Chlor International, Inc., including J. Michael Walker who was vice president and general manager of Geni-Chlor and a member of the board of directors of Geni-Chlor induced me to enter into the licensing contract attached to my complaint by informing me that Geni-Chlor International and Northern Propane Gas Company had, in 1972, *entered into a joint venture agreement* to both build and market the Geni-Chlor pool purifier." (Italics ours.)*992

Bearing in mind the contents of the document entitled "The Geni-Chlor Story" and the fact that Darwin A. Larson, the president and chairman of the board of Geni-Chlor was also the president of Propane Gas, the trial court was entitled to conclude that Propane Gas was aware of the representations by Geni-Chlor, particularly where the contents of the affidavit of Van Duyne were not denied at the time of the hearing on the motion of Propane Gas to quash service of summons.

Petitioners argue that the statement in Van Duyne's affidavit: "Northern Propane Gas Company was thereby aware of the inducements and representations made as to its responsibility for the product sold by its subsidiary" is pure speculation by Van Duyne not supported by competent evidence. Petitioners make a like argument regarding statements in Van Duyne's affidavit that Geni-Chlor

did various acts with "the obvious approval of the parent corporation." These arguments by petitioners disregard the legal principle of imputed knowledge.

Under the doctrine of imputed knowledge, Larson, as president and chairman of the board of Geni-Chlor, was chargeable with knowledge of the statements, representations, acts and conduct of the employees of Geni-Chlor. In 1 Witkin, Summary of California Law (8th ed. 1973) Agency and Employment, section 139, page 743, this elemental rule is stated as follows:

(5) "An agent is under a duty to inform his principal of matters in connection with the agency which the principal would desire to know about. (Rest.2d, Agency § 381.) Even if he fails to do so, the principal will in most cases be charged with such notice. 'As against a principal, both principal and agent are deemed to have notice of whatever either has notice of, and ought, in good faith and the exercise of ordinary care and diligence, to communicate to the other.' (C.C. 2332; see Rest.2d, Agency §§ 268, 272, 275, and Appendix, Rep. Notes, pp. 441, 446, 454, 461, 471, 475; *Davis v. Local No. 11, Int. Brotherhood, etc.* (1971) 16 Cal.App.3d 686, 695, 94 C.R. 562; *Capron v. California* (1966) 247 Cal.App.2d 212, 231, 55 C.R. 330; BAJI (5th ed.) No. 8.21 [knowledge of defective or dangerous condition of premises]; 4 A.L.R.3d 224 [imputation where agent acts for both parties to transaction]; 3 Am.Jur.2d, Agency § 273 et seq.)

"The court in *Columbia Pictures Corp. v. DeToth* (1948) 87 Cal.App.2d 620, 630, 197 P.2d 580, explained the doctrine of imputed knowledge as follows: 'The fact that the knowledge acquired by the agent was not*993 actually communicated to the principal ... does not prevent operation of the rule. ... The agent may have been guilty of a breach of duty to his principal, yet the knowledge has the same effect as to third persons as though his duty had been faithfully performed. The agent acting within the scope of his authority, is, as to the matters existing therein during the course of the

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

agency, the principal himself. ... This rule of law is not a rebuttable presumption. It is not a presumption at all."

(4b) Inasmuch as Larson was president and chairman of the board of Geni-Chlor and also president of Propane Gas, we think that Propane Gas was also chargeable with the same imputed knowledge that Larson was chargeable with as president of Geni-Chlor. (6) It is well established that the doctrine of imputed knowledge applies in the relationship of principal and subagent where the latter's employment by the agent is authorized or ratified. (*Trane Co. v. Gilbert* (1968) 267 Cal.App.2d 720, 727 [73 Cal.Rptr. 279].)

(4c) It would be unreasonable for the trial court to conclude that Larson as president of Geni-Chlor was chargeable with imputed knowledge of representations made by employees of Geni-Chlor to Van Duyne, but that Larson as president of Propane Gas had no such knowledge. The trial court had a right to conclude that Propane Gas as stockholder of Geni-Chlor elected Larson president of Geni-Chlor so that Larson as president of Propane Gas would be fully aware of what its wholly owned subsidiary was doing.

In view of the affidavit of Van Duyne and the other evidence in the case, the trial court could properly conclude therefore that Propane Gas organized and used Geni-Chlor as an instrumentality or agent to carry out a joint venture agreement in which Propane Gas was one of the joint venturers. The representations which Geni-Chlor made with imputed knowledge and consent of its president and chairman of its board of directors Darwin A. Larson, and therefore with the imputed knowledge and consent of Propane Gas of which Larson was also president, was tantamount to a representation that Propane Gas would be liable for Geni-Chlor's debts which it would be as a matter of law if there was a joint venture agreement as alleged in the uncontradicted declarations of Van Duyne. We hold that that conclusion was legally permissible by the trial court where the Van Duyne affidavit was not con-

tradicted. If the statements were untrue, Propane Gas at least had a duty to file a contradicting affidavit.*994

(7) The principle is well established that where a foreign corporation uses a wholly owned subsidiary as a mere agent or instrumentality of the foreign parent corporation, then the state may exercise jurisdiction over the foreign corporation. (6 Witkin, Summary of Cal. Law (8th ed. 1974) Corporations, § 11, p. 4323.) (8) Agency and alter ego are two different and distinct concepts. In the case of an alter ego, the court pierces the corporate veil. In the case of an agency the corporate identity is preserved but the principal is held liable for the acts of its agent. (4d) Here, in view of the fact that Larson was the president of Propane Gas and president and chairman of the board of Geni-Chlor, the court was justified in holding Propane Gas responsible for the declarations by Geni-Chlor that it had been formed to carry out a joint venture relationship with Propane Gas especially where Propane Gas has not seen fit to deny the allegations. Gale M. Colburn, vice president of Propane Gas, filed an affidavit which as a conclusion of law stated inter alia that Propane Gas was not a member of a partnership joint venture or limited partnership in California, but the specific declarations of Van Duyne in his affidavits were not denied. As a conclusion of law, the court was entitled to disregard the Colburn statement. At most, Colburn's affidavit merely created a conflict in the evidence which was impliedly resolved against Propane Gas by the trial court. The detailed statements by Van Duyne supported by some documentary evidence are certainly more persuasive than the legal conclusion by Colburn. We are bound by the trial court's implied resolution of this conflict in favor of the real party in interest where there was evidence to support it which there was.

It is likewise true that Geni-Chlor issued a bulletin to its distributors not to associate the name of Geni-Chlor with Propane Gas or Natural Gas in *marketing* operations. Since the bulletin refers to

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

marketing operations, the trial court had a right to interpret this bulletin as relating to the relationship between Geni-Chlor and the general public. By its own terms it did not relate to the relationship between Geni-Chlor and Geni-Chlor's distributors such as Van Duyne. Even interpreting the bulletin in the light most favorable to Propane Gas merely creates a conflict in the evidence which was resolved against Propane Gas.

(1c) The doctrine of imputed knowledge does not apply to Natural Gas because there is no comparable showing that the president of Natural Gas was the president of Propane Gas. In any event, even Van Duyne does not claim that anybody represented to him that Natural Gas was a party to any joint venture relationship with Geni-Chlor.*995

(4e) We note also that in the case at bar, Van Duyne complains that Geni-Chlor perpetrated a fraud on California citizens and that Geni-Chlor submitted to an injunction in a proceeding instituted by the district attorney enjoining certain alleged fraudulent conduct and false representations. Obviously such issue is not before us on the merits and we express no opinion other than to note that fraud was an issue in the case before respondent court. In *Empire Steel Corp. v. Superior Court* (1961) 56 Cal.2d 823, 833 [17 Cal.Rptr. 150, 366 P.2d 502], the court said:

“Such [fraudulent] conduct allegedly resulting in harm to persons doing business in this state may be considered as a factor to be weighed in determining whether Empire is subject to jurisdiction in the pending action. ...”

“Furthermore, this jurisdiction has a manifest interest in providing a forum for local creditors injured by alleged frauds effected through a California subsidiary.”

Quoting from another case, the court in *Empire Steel* said: “The essential thing is merely whether the corporations are present within the state, whether they operate through an independent contract,

agent, employee or in any other manner.” (*Id.* at p. 835.) (Italics by the court.)

Propane Gas is subject to the jurisdiction of California courts not because Geni-Chlor is its wholly owned subsidiary, but because there was evidence before respondent court upon which it could base an implied finding that Propane Gas was a member of a joint venture which was engaged in business in California through Geni-Chlor not as an alter ego, but as its agent or instrumentality. (9) Where charges of fraud on California citizens are involved, jurisdictional principles should be liberally construed and interpreted in order to accomplish substantial justice for California citizens.

We conclude therefore that the trial court properly denied the motion of Propane Gas to quash service of summons upon it.

(10) When a trial court erroneously denies a motion to quash service of summons made on the ground that the court has no personal jurisdiction over the moving party, mandamus is the appropriate remedy to review the erroneous ruling. (*Owens v. Superior Court* (1959) 52 Cal.2d 822, 827 [345 P.2d 921, 78 A.L.R.2d 388]; 5 Witkin, Cal. Procedure (2d ed. 1971) Extraordinary Writs, §§ 85, 187, pp. 3859, 3946.) The petition*996 here was filed within the time allowed by law as extended by the trial court. (Code Civ. Proc., § 418.10.)

The order to show cause heretofore issued herein is discharged and set aside insofar as it relates to Propane Gas.

Let a peremptory writ of mandate issue directing respondent court to vacate and set aside the denial of the motion of Natural Gas to quash service of summons on it and to grant such motion.

Brown (G. A.), P. J., and Gargano, J., concurred.

Cal.App.5.Dist.
Northern Natural Gas Co. v. Superior Court
64 Cal.App.3d 983, 134 Cal.Rptr. 850

64 Cal.App.3d 983, 134 Cal.Rptr. 850
(Cite as: 64 Cal.App.3d 983)

END OF DOCUMENT

643 F.3d 668, 11 Cal. Daily Op. Serv. 7982, 2011 Daily Journal D.A.R. 9655
(Cite as: 643 F.3d 668)

H

United States Court of Appeals,
Ninth Circuit.
REDEVELOPMENT AGENCY OF the CITY OF
STOCKTON, Plaintiff–Appellee–Cross–Appellant,
v.
BNSF RAILWAY COMPANY; Union Pacific
Railroad Company, Defendants–Appellants–Cross
Appellees.
Redevelopment Agency of the City of Stockton,
Plaintiff–Appellee–Cross–Appellant,
v.
BNSF Railway Company; Union Pacific Railroad
Company, Defendants–Appellants–Cross Ap-
pellees.
Redevelopment Agency of the City of Stockton,
Plaintiff–Appellee–Cross–Appellant,
v.
BNSF Railway Company; Union Pacific Railroad
Company, Defendants–Appellants–Cross Ap-
pellees.
Nos. 09–16585, 09–16739, 09–17640.
Argued and Submitted Feb. 14, 2011.
Filed June 28, 2011.

Background: City redevelopment agency filed state court action against railroads to recover costs incurred in remediating petroleum contamination of property. After removal, the United States District Court for the Eastern District of California, John A. Mendez, J., 2007 WL 1793755, granted in part and denied in part agency's motion for summary judgment. Parties filed cross-appeals.

Holdings: The Court of Appeals, Tallman, Circuit Judge, held that:

- (1) railroads' installation of underground french drain to remove water from roadbed did not create nuisance;
- (2) railroads were not liable for nuisance as possessors of property when contamination occurred; and

- (3) railroads were not liable under California's Polanco Act;
- (4) doctrine of equitable conversion did not render railroads equitable owners of property; and
- (5) railroads' easement over property did not render them owners of property under Polanco Act's CERCLA provision.

Affirmed in part, reversed in part, and remanded.

West Headnotes

[1] Federal Courts 170B  776

170B Federal Courts
170BVIII Courts of Appeals
170BVIII(K) Scope, Standards, and Extent
170BVIII(K)1 In General
170Bk776 k. Trial de novo. Most Cited
Cases
Court of Appeals reviews de novo district court's ruling on cross-motions for summary judgment.

[2] Nuisance 279  1

279 Nuisance
279I Private Nuisances
279I(A) Nature of Injury, and Liability
Therefor
279k1 k. Nature and elements of private nuisance in general. Most Cited Cases

Nuisance 279  4

279 Nuisance
279I Private Nuisances
279I(A) Nature of Injury, and Liability
Therefor
279k4 k. Nature and extent of injury or danger. Most Cited Cases
Under California law, to qualify as nuisance, interference must be both substantial and unreasonable.

(Cite as: 643 F.3d 668)

[3] Nuisance 279 ↪2

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability
Therefor

279k2 k. Intent. Most Cited Cases

Nuisance 279 ↪4

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability
Therefor279k4 k. Nature and extent of injury or
danger. Most Cited CasesUnder California law, intentional but not un-
reasonable act can give rise to nuisance liability if it
creates unreasonable interference.**[4] Nuisance 279** ↪9

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability
Therefor279k9 k. Persons creating or causing nuis-
ance. Most Cited Cases**Nuisance 279** ↪10

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability
Therefor279k10 k. Persons continuing nuisance.
Most Cited CasesUnder California law, if property owners did
not create or assist in creation of nuisance, they can
only be held liable if they acted unreasonably as
possessors of property in failing to discover and
abate nuisance.**[5] Nuisance 279** ↪9

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability
Therefor279k9 k. Persons creating or causing nuis-
ance. Most Cited CasesUnder California law, nuisance liability does
not necessarily hinge on whether defendant owns,
possesses, or controls property, nor on whether he
is in position to abate nuisance; critical question is
whether defendant created or assisted in creation of
nuisance.**[6] Nuisance 279** ↪9

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability
Therefor279k9 k. Persons creating or causing nuis-
ance. Most Cited Cases**Railroads 320** ↪108

320 Railroads

320VI Construction, Maintenance, and Equip-
ment320k106 Waters and Water Courses
320k108 k. Ditches, culverts, and bridges.
Most Cited Cases**Water Law 405** ↪1126

405 Water Law

405IV Groundwater: Subterranean and Percolat-
ing Waters405k1125 Pollution
405k1126 k. In general. Most Cited CasesUnder California law, railroads' installation of
underground french drain to remove water from
roadbed did not create nuisance, even though petro-
leum spilled at nearby industrial site migrated onto
neighboring property via drain, contaminating soil
and groundwater, where railroads did not spill pet-
roleum or otherwise release it into environment,
and did not affirmatively direct its flow or know-
ingly permit it to migrate into drain.**[7] Nuisance 279** ↪9

643 F.3d 668, 11 Cal. Daily Op. Serv. 7982, 2011 Daily Journal D.A.R. 9655

(Cite as: 643 F.3d 668)

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability Therefor

279k9 k. Persons creating or causing nuisance. Most Cited Cases

Under California law, passive but-for causation is not sufficient for nuisance liability to attach; conduct cannot be said to create nuisance unless it actively or knowingly generates or permits specific nuisance condition.

[8] Nuisance 279 ↪9

279 Nuisance

279I Private Nuisances

279I(A) Nature of Injury, and Liability Therefor

279k9 k. Persons creating or causing nuisance. Most Cited Cases

Railroads 320 ↪108

320 Railroads

320VI Construction, Maintenance, and Equipment

320k106 Waters and Water Courses

320k108 k. Ditches, culverts, and bridges.

Most Cited Cases

Water Law 405 ↪1126

405 Water Law

405IV Groundwater: Subterranean and Percolating Waters

405k1125 Pollution

405k1126 k. In general. Most Cited Cases

Under California law, railroads had no duty to inspect subsurface of property for contamination, and thus were not liable to subsequent owner for nuisance as possessors of property when soil and groundwater contamination occurred, even though property was near potential source of hazardous waste, and railroads had contractual obligation to maintain railroad tracks and drainage, where there was no evidence that they had actual knowledge of

contamination while they were in possession of property or that they failed to properly maintain drains, and contamination was not discovered by any subsequent owner or possessor of land until excavation began sixteen years after railroads sold it. Restatement (Second) of Torts § 839.

[9] Environmental Law 149E ↪445(1)

149E Environmental Law

149EIX Hazardous Waste or Materials

149Ek436 Response and Cleanup; Liability

149Ek445 Persons Responsible

149Ek445(1) k. In general. Most Cited

Cases

Under California law, railroads were not liable under Polanco Act for petroleum contamination of property owned by city redevelopment agency, even though petroleum was channeled onto property by underground french drain installed by railroads to remove water from roadbed, where petroleum originated from another site, and railroads were unaware of petroleum spill. West's Ann.Cal.Health & Safety Code § 25323.5; West's Ann.Cal.Water Code § 13304(a).

[10] Equitable Conversion 149T ↪110

149T Equitable Conversion

149Tk109 Conveyances and Contracts

149Tk110 k. In general. Most Cited Cases

Equitable Conversion 149T ↪112

149T Equitable Conversion

149Tk109 Conveyances and Contracts

149Tk112 k. Time of conversion. Most Cited Cases

Under California law, doctrine of "equitable conversion" generally provides that when valid executory land sales contract is entered into, purchaser becomes equitable owner of land.

[11] Vendor and Purchaser 400 ↪22

400 Vendor and Purchaser

400I Requisites and Validity of Contract

643 F.3d 668, 11 Cal. Daily Op. Serv. 7982, 2011 Daily Journal D.A.R. 9655

(Cite as: 643 F.3d 668)

400k20 Written Contracts

400k22 k. Description of property. Most Cited Cases

Under California law, essential requirement for valid land sales contract is that it contain description of land to be conveyed.

[12] Environmental Law 149E ↪445(1)

149E Environmental Law

149EIX Hazardous Waste or Materials

149Ek436 Response and Cleanup; Liability

149Ek445 Persons Responsible

149Ek445(1) k. In general. Most Cited

Cases

Equitable Conversion 149T ↪110

149T Equitable Conversion

149Tk109 Conveyances and Contracts

149Tk110 k. In general. Most Cited Cases

Under California law, doctrine of equitable conversion did not render railroads equitable owners of property upon execution of agreement to relocate existing railroad track from proposed interchange site to nearby state-owned parcel, and thus did not subject railroads to liability under Polanco Act's CERCLA provision for petroleum contamination of property, where agreement did not describe how wide or extensive rights-of-way were, or indicate that state intended to convey fee simple interest to railroads. Comprehensive Environmental Response, Compensation, and Liability Act of 1980, § 107(a), 42 U.S.C.A. § 9607(a); West's Ann.Cal.Health & Safety Code § 33459(h).

[13] Environmental Law 149E ↪445(1)

149E Environmental Law

149EIX Hazardous Waste or Materials

149Ek436 Response and Cleanup; Liability

149Ek445 Persons Responsible

149Ek445(1) k. In general. Most Cited

Cases

Railroads' easement over property did not render them owners of property, and thus did not

subject railroads to liability pursuant to California's Polanco Act's CERCLA provision for petroleum contamination of property, even though petroleum spilled at nearby industrial site migrated onto neighboring property via underground french drain installed by railroads to remove water from roadbed, where petroleum spill was unrelated to railroads' use of easement, and drain was not installed or operated for any purpose related to petroleum contamination. Comprehensive Environmental Response, Compensation, and Liability Act of 1980, § 107(a), 42 U.S.C.A. § 9607(a); West's Ann.Cal.Health & Safety Code § 33459(h).

*670 Morgan Gilhuly (argued), John F. Barg, Donald Sobelman, Barg Coffin Lewis & Trapp, LLP, San Francisco, CA, for defendants-appellants-cross-appellees BNSF Railway Company and Union Pacific Railroad Company.

William D. Brown (argued), Scott E. Patterson, Christine J. Gracco, Brown & Winters, Cardiff-by-the-Sea, CA, for plaintiff-appellee-cross-appellant Redevelopment Agency of the City of Stockton.

Kevin M. Fong, Margaret Rosegay, Pilsbury Winthrop Shaw Pittman LLP, San Francisco, CA, for amicus curiae California Council for Environmental and Economic Balance.

Benjamin G. Shatz, Fred L. Main, Manatt, Phelps & Phillips, LLP, Los Angeles, CA, for amicus curiae California Chamber of Commerce.

Appeal from the United States District Court for the Eastern District of California, John A. Mendez, District Judge, Presiding. D.C. No. 2:05-cv-02087-JAM-JFM.

671 Before: M. MARGARET McKEOWN^{FN} and RICHARD C. TALLMAN, Circuit Judges, and ARTHUR J. TARNOW,^{FN**} Senior District Judge.

FN* Due to the death of the Honorable David R. Thompson, the Honorable M. Margaret McKeown, United States Circuit Judge for the Ninth Circuit, was drawn to replace him. Judge McKeown has read the briefs, reviewed the record, and listened to the audio recording of oral argument held on February 14, 2011.

FN** The Honorable Arthur J. Tarnow, Senior United States District Judge for the Eastern District of Michigan, sitting by designation.

OPINION

TALLMAN, Circuit Judge:

Appellants BNSF Railway Company and Union Pacific Railroad Company (“the Railroads”) formerly maintained railroad tracks on a parcel of land in Stockton, California, that was contaminated by petroleum. The petroleum was spilled at a nearby industrial site and migrated onto the property via an underground french drain the Railroads had installed in order to remove water from the roadbed. We consider whether the Railroads are liable for the contamination of the property under the law of nuisance or under California’s Polanco Redevelopment Act (“Polanco Act”), Cal. Health & Safety Code § 33459 *et seq.* We hold that they are not.

There is no evidence that the Railroads actively or knowingly caused or permitted the contamination as required for nuisance liability and liability under the Polanco Act’s Water Code provision. Nor were the Railroads “owners” of the property under the Polanco Act’s CERCLA provision when the contamination occurred. Because the record establishes no genuine issue of material fact as to the Railroads’ liability, the Railroads are entitled to summary judgment. Therefore, we need not reach any of the damages issues on appeal or cross-appeal.

I

In 1968, in order to make room for the construction of a freeway interchange between Interstate 5 and State Highway 4 in Stockton, California, the State of California entered into a contract (“the Agreement”) with several railroad companies, predecessors-in-interest to the Railroads, to relocate existing railroad track from the proposed interchange site to a nearby State-owned parcel (“the Property”). Under the Agreement, the Railroads planned and approved grading and drainage improvements to the Property made by the State, including the installation of a “french drain” underneath the new roadbed. The french drain, a buried perforated pipe, was designed to improve soil stability by facilitating drainage. After these improvements were completed, the Railroads laid track on the Property. The Railroads agreed to maintain the track, roadbed and drainage, and the State agreed to convey to the Railroads all rights-of-way necessary for track operation. Although the Railroads began running trains over the track in 1970, the State did not actually transfer the deed to the underlying land to the Railroads until 1983.

In 1988, the Railroads sold their interest in the Property to Appellee, the Redevelopment Agency of the City of Stockton (“the Agency”), which planned to develop the site. In 2004, the Agency sold a portion of the Property known as “Area 3” to a commercial developer (while retaining those portions known as “Area 4” and “Area 24”) and indemnified the developer for costs incurred due to any then-existing *672 contamination discovered on the site. When site excavation began in preparation for development, petroleum contamination was found in the soil along the path of the french drain and in the groundwater. Testing indicated that the contamination was at least twenty years old, and its likely source was determined to be the nearby L & M bulk petroleum facility (“the L & M Site”) where there had been several spills in the early 1970s, including a spill of up to 6,000 gallons of diesel fuel in 1974. It is undisputed that the french drain served as a preferential pathway through which the petroleum contamination migrated underground

onto the Property.

After the contamination was discovered in July 2004, the developer and the Agency began to work with environmental consultants and regulators to develop a remediation workplan for Area 3. The Agency sent notices to the Railroads requesting that they prepare remedial action plans for Areas 3, 4, and 24, but the Railroads did not respond to any of them. In the fall of 2004, a trench approximately 300 feet long, 18 to 20 feet deep, and 15 to 20 feet wide was excavated on Area 3 to remove contaminated soil. The Agency incurred costs of over \$1.3 million for this work, plus additional costs of nearly one-half million dollars for investigation and remediation work on Areas 4 and 24 between 2005 and 2008.

On September 29, 2005, the Agency sued the Railroads in California Superior Court, seeking cost recovery and an injunction requiring the Railroads to remediate any remaining contamination at the Property. The Agency alleged that the Railroads were liable for the contamination under the Polanco Redevelopment Act as well as the common law of nuisance. The Railroads removed the action to the United States District Court for the Eastern District of California under diversity jurisdiction. The Railroads and the Agency filed cross-motions for summary judgment. On June 19, 2007, the district court ruled that the Railroads were liable for the contamination under the law of nuisance and under the Polanco Act's Water Code provision,^{FN1} but not under the Polanco Act's CERCLA provision. See Cal. Health & Safety Code § 33459(h). The Agency was awarded over eight hundred thousand dollars in damages and an injunction. The parties appeal and cross-appeal as to the findings of liability and the damages award.

FN1. The district court held that the Railroads were liable under the Polanco Act only for Areas 4 and 24, but not Area 3, because the Agency had failed to comply with the Act's notice provisions as to Area 3.

II

[1] We have jurisdiction under 28 U.S.C. § 1291. We review de novo a district court's ruling on cross-motions for summary judgment. *Trunk v. City of San Diego*, 629 F.3d 1099, 1105 (9th Cir.2011). We view the evidence in the light most favorable to the nonmoving party and determine "whether there are any genuine issues of material fact and whether the district court correctly applied the relevant substantive law." *Id.* (citation omitted). When the district court disposes of a case on cross-motions for summary judgment, we may review both the grant of the prevailing party's motion and the corresponding denial of the opponent's motion. *Id.*; see *Jones-Hamilton Co. v. Beazer Materials & Servs., Inc.*, 973 F.2d 688, 694 n. 2 (9th Cir.1992).

III

[2] California law defines a nuisance, in part, as "[a]nything which is injurious to *673 health ... or is indecent or offensive to the senses, or an obstruction to the free use of property, so as to interfere with the comfortable enjoyment of life or property...." Cal. Civ.Code § 3479. To qualify as a nuisance "the interference must be both *substantial* and *unreasonable*." *People ex rel. Gallo v. Acuna*, 14 Cal.4th 1090, 1105, 60 Cal.Rptr.2d 277, 929 P.2d 596 (1997) (emphasis in original); see also *San Diego Gas & Elec. Co. v. Superior Court*, 13 Cal.4th 893, 938-39, 55 Cal.Rptr.2d 724, 920 P.2d 669 (1996). It is undisputed that the soil and groundwater contamination in this case constitutes a nuisance. See *California v. Campbell*, 138 F.3d 772, 776 (9th Cir.1998) (citing *Carter v. Chotiner*, 210 Cal. 288, 291, 291 P. 577 (1930)); *Selma Pressure Treating Co. v. Osmose Wood Preserving Co. of Am.*, 221 Cal.App.3d 1601, 1619, 271 Cal.Rptr. 596 (1990). The question is whether the Railroads are liable for it.

[3] At the outset, we clarify how the concept of "unreasonableness" plays into nuisance liability. The Railroads invoke *Lussier v. San Lorenzo Valley Water District*, 206 Cal.App.3d 92, 253 Cal.Rptr. 470 (1988), for the proposition that nuisance liability

643 F.3d 668, 11 Cal. Daily Op. Serv. 7982, 2011 Daily Journal D.A.R. 9655
(Cite as: 643 F.3d 668)

ity requires an unreasonable act. *See id.* at 101, 253 Cal.Rptr. 470 (noting that nuisance liability can arise “only for such interferences as are intentional and unreasonable or result from negligent, reckless or abnormally dangerous conduct” (internal quotation marks and citation omitted)). However, this proposition confuses the concept of an unreasonable *interference*, which is required for nuisance liability, with an unreasonable or negligent *act*, which is not. An intentional but not unreasonable *act* can give rise to nuisance liability if it creates an unreasonable *interference*. *See id.* at 105–06, 253 Cal.Rptr. 470; *Shields v. Wondries*, 154 Cal.App.2d 249, 255, 316 P.2d 9 (1957) (noting that a private nuisance may result from “skillfully directed efforts,” such as the non-negligent construction of improvements on one’s property, which nonetheless infringe upon a neighbor’s property rights).

[4] If the Railroads created or assisted in the creation of the nuisance on the Property by installing and maintaining the french drain, they are liable, regardless of whether the installation and maintenance of the french drain was conducted in a reasonable manner or not. If the Railroads did not create or assist in the creation of the nuisance, they can only be held liable if they acted unreasonably as possessors of the Property in failing to discover and abate the nuisance. *See Lussier*, 206 Cal.App.3d at 104–05, 253 Cal.Rptr. 470 (noting the general view that “proof of negligence may be essential to a claim of nuisance where the alleged nuisance involves a failure to act”). We consider first whether the Railroads created the nuisance by installing the french drain; and second whether they unreasonably failed to discover and abate it.

A

[5] Nuisance liability does not necessarily “hinge on whether the defendant owns, possesses or controls the property, nor on whether he is in a position to abate the nuisance; the critical question is whether the defendant *created or assisted in the creation of the nuisance*.” *Cnty. of Santa Clara v. Atl. Richfield Co.*, 137 Cal.App.4th 292, 306, 40

Cal.Rptr.3d 313 (2006) (emphasis in original) (internal quotation marks and citations omitted). The district court concluded that the Railroads “created or assisted in the creation” of the nuisance because they were a but-for cause of the contamination of the Property: the contamination would not have migrated onto the Property but for the existence of the french drain, and the french drain *674 would not have been installed but for the Railroads.

[6][7] We cannot agree that such passive but-for causation is sufficient for nuisance liability to attach. Under California law, conduct cannot be said to “create” a nuisance unless it more actively or knowingly generates or permits the specific nuisance condition. For example, in *Selma Pressure Treating Co.*, the California Court of Appeal held that a company’s “direct involvement in the design and installation of unsafe disposal systems” for chemicals used in a wood treatment process, “coupled with its claimed knowledge of the dangers involved in such practices, clearly could support liability based upon a finding that it created or assisted in the creation of a public nuisance.” 221 Cal.App.3d at 1620, 271 Cal.Rptr. 596.

However, in *City of Modesto Redevelopment Agency v. Superior Court*, 119 Cal.App.4th 28, 13 Cal.Rptr.3d 865 (2004), the Court of Appeal declined to extend *Selma* to hold that “those who merely placed [hazardous substances] in the stream of commerce,” as opposed to those who “took affirmative steps directed toward the improper discharge of [hazardous] wastes,” could be liable for nuisance. *Id.* at 43, 13 Cal.Rptr.3d 865; *see also Atl. Richfield*, 137 Cal.App.4th at 310, 40 Cal.Rptr.3d 313 (holding that lead paint manufacturers could incur nuisance liability for their “intentional promotion of the use of lead paint on the interiors of buildings with knowledge of the public health hazard that this would create,” but not for their “mere manufacture and distribution of lead paint or their failure to warn of its hazards”).^{FN2}

FN2. As the Agency points out, the holdings in *Modesto* and *Atlantic Richfield* are

explained in part by the courts' recognition that manufacturing and distribution activity may be better addressed through the law of products liability. *See Atl. Richfield*, 137 Cal.App.4th at 308–09, 40 Cal.Rptr.3d 313. But these cases are also explained by the courts' recognition that nuisance liability requires more than a passive or attenuated causal connection to contamination. *See id.* at 309–10, 40 Cal.Rptr.3d 313 (“A public nuisance cause of action is not premised on a defect in a product or a failure to warn but on affirmative conduct that assisted in the creation of a hazardous condition.”).

Federal cases interpreting California nuisance law reflect this same understanding. *See Campbell*, 138 F.3d at 775 (defendant manufacturers created a nuisance at a property where they disposed of hazardous waste by dumping it on the ground); *W. Coast Home Builders, Inc. v. Aventis Cropscience USA Inc.*, 2009 WL 2612380 at *9 (N.D.Cal.2009) (defendant waste generators not liable for groundwater contamination at a landfill where their waste was disposed because their conduct was “too attenuated from the creation of the alleged nuisance,” even though it was a but-for cause of the contamination).

In short, we find no precedent suggesting that but-for causation suffices for nuisance liability, and we will not adopt such an expansive interpretation of California law here. Because the Railroads' conduct with regard to the specific nuisance condition—the contamination—was not active, affirmative, or knowing, the Railroads simply did not “create or assist in the creation” of the nuisance on the Property. They did not spill the petroleum or otherwise release it into the environment. They did not affirmatively direct its flow or knowingly permit it to migrate into the french drain and onto the Property. While the Railroads may have acted affirmatively with regard to the installation of the french drain, that conduct was wholly unrelated to

the contamination. The Railroads did not, for example, install the french drain as part of a system designed to move or dispose of hazardous waste, like *675 the defendants did in *Selma*. *See* 221 Cal.App.3d at 1620, 271 Cal.Rptr. 596. The drainage improvements on the site were designed to move water, not contaminants.

We decline to hold that an otherwise innocent party who builds or installs a conduit or structure for an unrelated purpose which happens to affect the distribution of contamination released by someone else is nonetheless liable for “creating or assisting in the creation” of a nuisance. Such a result defies semantics, the law, and common sense. “While liability for nuisance is broad ..., it is not unlimited.” *Modesto*, 119 Cal.App.4th at 39, 13 Cal.Rptr.3d 865. We decline to extend it here. The Railroads are not liable for creating a nuisance by virtue of their installation of the french drain.

B

We must also examine whether the Railroads are liable for nuisance as the possessors of the Property when the contamination occurred. Possessors of land can be liable for a nuisance on that land even when they did not create the nuisance. *See Leslie Salt Co. v. San Francisco Bay Conservation and Dev. Comm'n*, 153 Cal.App.3d 605, 619–20, 200 Cal.Rptr. 575 (1984) (noting that, under principles of nuisance, an occupier of land could be liable for fill dumped into a wetland by someone else without the occupier's knowledge). In such a situation, liability flows not from the possessor's “active responsibility for a condition of his land that causes widespread harm ... but rather, and quite simply, from his very possession and control of the land in question.” *Id.* at 622, 200 Cal.Rptr. 575; *see also* Restatement (Second) of Torts § 839 cmt. d (1979). California nuisance law conforms to the Restatement, *see City of Los Angeles v. San Pedro Boat Works*, 635 F.3d 440, 452 (9th Cir.2011), and under the Restatement,

[a] possessor of land is subject to liability for a nuisance caused while he is in possession by an

abatable artificial condition on the land, if the nuisance is otherwise actionable, and

(a) the possessor knows or should know of the condition and the nuisance or unreasonable risk of nuisance involved, and

(b) he knows or should know that it exists without the consent of those affected by it, and

(c) he has failed after a reasonable opportunity to take reasonable steps to abate the condition or to protect the affected persons against it.

Restatement (Second) of Torts § 839 (1979).

We assume, without deciding, that the soil and groundwater contamination on the Property is considered “abatable” under California law. *See Capogeannis v. Superior Court*, 12 Cal.App.4th 668, 682–83, 15 Cal.Rptr.2d 796 (1993) (holding that soil and groundwater contamination can be considered abatable); *but see Mangini v. Aerojet-Gen. Corp.*, 12 Cal.4th 1087, 1099–1100, 51 Cal.Rptr.2d 272, 912 P.2d 1220 (1996) (noting that “‘abatable’ means reasonably abatable” given considerations of cost and practicality); Restatement (Second) of Torts § 839 cmt. f (1979). We focus instead on whether the Railroads knew or should have known of the contamination.

[8] No evidence has been adduced that the Railroads had actual knowledge of the contamination while they were in possession of the Property. Whether the Railroads “should have known” about the contamination depends on whether they had a duty to inspect for it and whether it was discoverable by a reasonable inspection. *676 *See Leslie Salt*, 153 Cal.App.3d at 621, 200 Cal.Rptr. 575; Restatement (Second) of Torts § 839 cmt. i (1979). The Agency does not allege that the contamination should have been apparent to the Railroads based on their periodic visual inspections of the Property. This is not a case in which, for example, the nuisance was in any way manifest on the surface of the land. *Cf. Leslie Salt*, 153 Cal.App.3d at 621, 200

Cal.Rptr. 575 (holding that landowner “certainly” should have known of “the existence of several hundred tons of detritus and other fill materials on its land”). Indeed, the contamination was not discovered by any subsequent owner or possessor of the land, including the Agency itself, until excavation began at the Property some sixteen years after the Railroads sold it.

The Agency nonetheless implies that the Railroads had a duty to inspect the *subsurface* for contamination, because: (1) the Property was near the L & M Site, a potential source of hazardous waste; and (2) the Railroads were obligated by the Agreement to maintain the railroad tracks and drainage. Neither of these conditions is sufficient to establish such a duty. As to the first, it is untenable that a possessor of land, simply because his neighbor is a potential polluter, thereby becomes responsible for investigating the subsurface in order to discover and control his neighbor's pollution. Such a holding shifts too much of the cost of pollution control away from the parties who actually have the ability to affect whether a hazardous substance is released into the environment in the first place, and onto the innocent parties who have the misfortune of being “downstream.”

The law reasonably imposes a duty on a possessor of land to ensure that activities on that land—where the possessor has control—do not produce a nuisance. *See Leslie Salt*, 153 Cal.App.3d at 620–22, 200 Cal.Rptr. 575; Restatement (Second) of Torts § 838 (1979). This is not the same as a duty to ensure that activities on adjacent land—where the possessor has *no* control—do not produce a nuisance. It is this latter duty that the Agency essentially asks us to impose on the Railroads, and we decline to do so. The law of nuisance evolved to protect a person from his neighbor's activities, not to render him liable for them. *See Lussier*, 206 Cal.App.3d at 100, 253 Cal.Rptr. 470 (“The basic concept underlying the law of nuisances is articulated in the ancient maxim *sic utere tuo ut alienum non laedas*, that is, so use your own

643 F.3d 668, 11 Cal. Daily Op. Serv. 7982, 2011 Daily Journal D.A.R. 9655
(Cite as: 643 F.3d 668)

as not to injure another's property.” (citations omitted)).

Whether the Railroads had a duty to inspect the subsurface for contamination of the Property based on their responsibility under the Agreement to “maintain” the track and drainage is a closer question. We recently suggested in dicta that a possessor of land who was contractually obligated to “keep and maintain [the] premises in a safe, clean, wholesome, sanitary and sightly condition” might have a heightened duty to investigate for contamination. *San Pedro Boat Works*, 635 F.3d at 453. However, even assuming that this dicta should be applied as a rule of law, the Agreement simply cannot be construed to impose any comparable obligation on the Railroads. Unlike the contractual language in *San Pedro Boat Works*, the relevant language in the Agreement, which indicates that “the maintenance of all railroad facilities including track, roadbed, [and] railroad drainage ... shall be by [the] Railroads at their expense,” in no way implies any particular obligation to keep the Property pollution-free. Rather, this language merely imposes a duty to maintain certain structures on the Property. There is no indication that the Railroads did not fulfill this responsibility with *677 regard to the drainage: as the Railroads point out, the drainage functioned exactly as it was supposed to by channeling and dispersing water under the site. Nothing in the Agreement remotely suggests that the “maintenance” of the railroad facilities involved a duty to conduct a proactive subsurface investigation for contamination.

Because there is no basis on which to conclude that the Railroads knew or should have known of the contamination, they cannot be liable for nuisance by virtue of their status as possessors of the Property.

IV

In addition to its claim of nuisance, the Agency also claims that the Railroads are liable under California's Polanco Act, Cal. Health & Safety Code § 33459 *et seq.* Under the Polanco Act, a local re-

development agency can recover the costs it incurs for contamination remediation within a redevelopment project area from any “responsible party.” *Id.* § 33459.4(a); *Modesto*, 119 Cal.App.4th at 34, 13 Cal.Rptr.3d 865. The Polanco Act defines a “responsible party” as any person described in either: (1) California Health and Safety Code section 25323.5 (which, in turn, refers to persons described in the federal Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) at 42 U.S.C. § 9607(a)); or (2) California Water Code section 13304(a). Cal. Health & Safety Code § 33459(h). We now assess the Railroads' Polanco Act liability under both the Water Code provision and the CERCLA provision.

A

[9] The Polanco Act imposes liability on parties described in section 13304(a) of the California Water Code, which in turn refers to

[a]ny person ... who has caused or permitted, causes or permits, or threatens to cause or permit any waste to be discharged or deposited where it is, or probably will be, discharged into the waters of the state and creates, or threatens to create, a condition of pollution or nuisance....

Cal. Water Code § 13304(a). The district court held that the Railroads were liable under section 13304 because the channeling and emission of petroleum by the french drain was a discharge, and the Railroads were responsible for the design, installation and maintenance of the french drain. We disagree.

First of all, we take issue with the characterization of the emission of the contamination from the french drain as the relevant “discharge,” when the french drain merely acted as a conduit for the waste that had been initially released into the environment at the L & M Site. *Cf. Lake Madrone Water Dist. v. State Water Res. Control Bd.*, 209 Cal.App.3d 163, 169, 256 Cal.Rptr. 894 (1989) (noting that a dam that collected and discharged silt was “not a mere conduit through which a[hazardous substance]

passes”). It is undisputed that the Railroads did not in any way cause or permit the initial discharge of petroleum at the L & M Site. But even if the emission of contamination from the french drain is the appropriate “discharge” to consider, the Railroads are not liable.

As the district court recognized, section 13304 should be construed harmoniously with the law of nuisance. *See Modesto*, 119 Cal.App.4th at 37–38, 13 Cal.Rptr.3d 865. However, because the district court construed nuisance liability too broadly its section 13304 liability analysis reflects the same error. Just as but-for causation is insufficient to impose liability for a nuisance, it is insufficient to impose liability for a discharge under section 13304. The *678 California Court of Appeal has concluded that the words “causes or permits” within section 13304 were not intended “to encompass those whose involvement with a spill was remote and passive.” *Modesto*, 119 Cal.App.4th at 44, 13 Cal.Rptr.3d 865; *see also id.* at 43, 13 Cal.Rptr.3d 865 (“[T]hose who took affirmative steps directed toward the improper discharge of [hazardous] wastes ... may be liable under [section 13304].”). The Railroads’ involvement with the petroleum *spill* was not only remote, it was nonexistent; and their involvement with the emission of contamination from the french drain was entirely passive and unknowing. As explained in our nuisance analysis, the Railroads engaged in no active, affirmative or knowing conduct with regard to the passage of contamination through the french drain and into the soil. Therefore, the Railroads did not “cause or permit” the discharge under section 13304, and they are not liable under the Water Code provision of the Polanco Act.

B

The Polanco Act also imposes liability on persons described in CERCLA at 42 U.S.C. § 9607(a). Cal. Health & Safety Code § 33459(h). As relevant to this case, CERCLA refers to “any person who at the time of disposal of any hazardous substance owned or operated any facility at which such haz-

ardous substances were disposed of.” 42 U.S.C. § 9607(a)(2). The district court held that the Railroads were not liable under the Polanco Act’s CERCLA provision because they were not “owners” or “operators” within the meaning of CERCLA. The Agency has appealed only the district court’s ruling that the Railroads were not “owners” of the Property. We agree with the district court on this issue. FN3

FN3. We note that, prior to reaching the ownership issue, the district court determined that the migration of petroleum contamination onto the Property through the french drain constituted a “disposal” within the meaning of CERCLA at 42 U.S.C. § 9607(a)(2). We are skeptical of this aspect of the district court’s ruling. *See Carson Harbor Vill., Ltd. v. Unocal Corp.*, 270 F.3d 863, 879 (9th Cir.2001) (en banc) (holding that “the gradual passive migration of contamination through the soil” was not a “disposal” under CERCLA). However, because the “disposal” issue was not contested by the parties, and because we can affirm the district court’s holding that the Railroads were not liable under the Polanco Act’s CERCLA provision based on its finding that the Railroads were not “owners” of the Property, we decline to rule on the “disposal” issue.

It is undisputed that the Agency did not deed the Property to the Railroads until 1983, well after the petroleum release occurred in the 1970s. However, the Agency asserts that the Railroads were nonetheless “owners” of the Property within the meaning of CERCLA when the petroleum release occurred because: (1) the doctrine of equitable conversion rendered them equitable owners of the Property upon the execution of the Agreement in 1968; or (2) they held an easement or license to operate trains over the Property pursuant to the Agreement. Both arguments fail.

[10][11] The doctrine of equitable conversion generally provides that when a valid executory land sales contract is entered into, the purchaser becomes the equitable owner of the land. *See Parr-Richmond Indus. Corp. v. Boyd*, 43 Cal.2d 157, 166, 272 P.2d 16 (1954) (“An unconditional contract for the sale of land, of which specific performance would be decreed, grants the purchaser equitable title, and equity considers him the owner.”); *Alhambra Redevelopment Agency v. Transamerica Fin. Servs.*, 212 Cal.App.3d 1370, 1376, 261 Cal.Rptr. 248 (1989) (“By the *679 execution of a valid enforceable contract to sell real estate the vendee becomes the equitable owner of the title....” (internal quotation marks and citation omitted)). We must therefore inquire whether the Agreement functioned as a valid land sales contract. An essential requirement for a valid land sales contract is that it contain a description of the land to be conveyed. *See Corona Unified Sch. Dist. of Riverside Cnty. v. Vejar*, 165 Cal.App.2d 561, 564-66, 332 P.2d 294 (1958). That description must be sufficient to delineate the property on the ground without resort to parol evidence. *Id.* at 566, 332 P.2d 294.

[12] The Agreement provided that the State would convey to the Railroads “all rights of way necessary for the construction and operation of substitute trackage ... and for the construction and operation of all other railroad facilities required to be relocated or reestablished due to construction and relocation work herein contemplated.” However, nowhere did the Agreement describe how wide or extensive these rights-of-way would be. Although a map was incorporated into the Agreement as “Exhibit A,” that map, by its terms, depicted the location of the “trackage,” not the extent of the associated rights-of-way. Furthermore, there is no indication from the Agreement that the State intended to convey a fee simple interest to the Railroads. After all, a “right-of-way” is commonly defined as a lesser property interest. *See Black’s Law Dictionary* 1440 (9th ed.2009) (defining a “right-of-way” as “[t]he right to build and operate a railway line or

a highway *on land belonging to another*, or the land so used”) (emphasis added).

The Agreement simply did not describe the extent of the property to be transferred from the State to the Railroads sufficiently to be considered a valid land sales contract. *See Corona Unified*, 165 Cal.App.2d at 566, 332 P.2d 294 (noting that “ ‘a strip of land in front of Golden Rule Store and Stent Market’ ” was an insufficient description of land because “nothing [was] contained as to the width or length of the strip” (citation omitted)). Therefore, the Agreement’s execution did not establish the Railroads as equitable owners of the Property, and the Railroads are not CERCLA “owners” under this theory.

2

[13] The Agency also theorizes that the Railroads were “owners” of the Property for purposes of CERCLA because their construction and use of the track on the Property, as licensed by the Agreement, gave them an easement. *See Noronha v. Stewart*, 199 Cal.App.3d 485, 490, 245 Cal.Rptr. 94 (1988) (“[W]here a party has made substantial expenditures in reliance on a license, the license acts, for all purposes, as an easement, estopping the grantor and his successor from revoking it.”). However, even assuming the Railroads held an easement over the Property, the argument that their status as an easement holder is enough to render them “owners” under CERCLA is squarely foreclosed by our precedent. “Having an easement does not make one an ‘owner’ for purposes of CERCLA liability.” *Long Beach Unified Sch. Dist. v. Godwin Cal. Living Trust*, 32 F.3d 1364, 1370 (9th Cir.1994); *see also id.* at 1368 (“[W]e read [CERCLA] as incorporating the common law definition of its terms.... The common law does not regard an easement holder as the owner of the property burdened by it.”); *San Pedro Boat Works*, 635 F.3d at 451 (“In establishing ‘owner’ liability [under CERCLA], Congress did not say ‘de facto owner,’ or ‘possessor,’ or ‘person with some incidents or attributes of ownership,’ as it has in other

643 F.3d 668, 11 Cal. Daily Op. Serv. 7982, 2011 Daily Journal D.A.R. 9655

(Cite as: 643 F.3d 668)

legislation.... *680 Instead it used the unmodified term ‘owner’ which ... when used alone, imports an absolute owner.” (some internal quotation marks and citations omitted)).

In *Long Beach* we held that a holder of an easement for a non-polluting pipeline was not liable as an “owner” under CERCLA. 32 F.3d at 1368–69. The Agency points out, correctly, that *Long Beach* does not preclude imposing CERCLA liability on an easement holder when the contamination results from the use of the easement. *See id.* at 1367. But that is simply because, in such circumstances, the easement holder could be liable as an *operator* under CERCLA. *Id.* (“[W]hen a party uses the easement to operate a pipeline that releases hazardous materials, it is liable as an operator provided the other statutory elements [of CERCLA] are satisfied.”). Certainly, if the Railroads’ use of their right-of-way resulted in a contaminant release, the Railroads could be liable as “operators.” But that is not what happened here. The petroleum spill was entirely unrelated to the Railroads’ use of the easement, and the french drain was not installed or operated for any purpose related to the petroleum contamination.

The district court correctly held (and the Agency does not contest on appeal) that the Railroads were *not* “operators” under CERCLA because they did not “manage, direct, or conduct operations specifically related to [the] pollution, that is, operations having to do with the leakage or disposal of [the] hazardous waste.” *United States v. Bestfoods*, 524 U.S. 51, 66–67, 118 S.Ct. 1876, 141 L.Ed.2d 43 (1998). And there is absolutely nothing in our opinion in *Long Beach* that suggests that, if the Railroads are not liable as “operators,” they can nonetheless be liable as “owners” based solely on their status as easement holders. *See* 32 F.3d at 1368–69 (“[W]e see no basis for holding that easement holders are owners for purposes of CERCLA liability.”).

In *San Pedro Boat Works*, we recently explained that “the CERCLA framework holds liable

both the passive *title* owner of real property who acquiesces in another’s discharge of harmful pollutants on his real property ... (‘owner liability’), and the active (or negligent) operator of the facility who holds only a possessory interest in the real property but is in fact responsible for the discharge (‘operator liability’).” 635 F.3d at 451–52 (emphasis in original). The Railroads do not fall within either of these two categories: they did not hold title to the Property at the time of the contamination, and they are not in fact responsible for the discharge because they did not conduct operations related to the petroleum. Since the Railroads are not “owners” or “operators” under CERCLA, 42 U.S.C. § 9607(a)(2), they are not liable under the Polanco Act’s CERCLA provision.

V

The Railroads are not liable for the contamination at the Property under the common law of nuisance or under California’s Polanco Redevelopment Act. Therefore, we need not reach the damages issues raised on appeal and cross-appeal. We reverse the grant of summary judgment for the Agency on the nuisance and Polanco Act–Water Code provision issues and remand for entry of summary judgment for the Appellants. We affirm the grant of summary judgment to the Appellants on the Polanco Act–CERCLA provision issue.

Costs are awarded to the Appellants.

AFFIRMED in part; REVERSED AND REMANDED in part.

C.A.9 (Cal.),2011.

Redevelopment Agency of City of Stockton v. BNSF Ry. Co.

643 F.3d 668, 11 Cal. Daily Op. Serv. 7982, 2011 Daily Journal D.A.R. 9655

END OF DOCUMENT



FRED A. REINHARD, Appellant,

v.

LAWRENCE WAREHOUSE COMPANY (a Corporation) et al., Respondents.

Civ. No. 11372.

District Court of Appeal, First District, Division 2,
California.

November 28, 1940.

HEADNOTES

(1) Landlord and Tenant § 318 (3)--Rights and Liabilities as to Third Persons--Injuries to Third Persons--Actions--Trial.

In an action for personal injuries sustained when an employee of a glazing contractor fell through a skylight, a directed verdict for the landlord was proper where the plaintiff merely pleaded negligence in maintenance of the skylight and the undisputed evidence showed that the injuries resulted from a condition of the building which was unknown to both the landlord and the tenant, and could not have been discovered through ordinary inspection or care.

See 15 Cal. Jur. 742; 16 R. C. L. 1067.

(2) Trial § 269--Direction of Verdict--Proceedings--Review.

A motion for a directed verdict is made upon the case then before the trial court, based on the pleadings and the proof, and the only question for a reviewing court to determine is whether the trial court erred in granting the motion, since the case cannot be tried on appeal *de novo*.

(3) Appeal § 965--Review--Necessity That Matter be Considered or Decided Below.

No error as to an issue not presented in the trial court can be reviewed on appeal.

(4) Nuisances § 23--Particular Nuisances--Buildings.

A skylight over a portion of the business office

of a warehouse company is not shown to be a public nuisance where there is no evidence (a) that anyone worked under it, (b) that the office was open to the public, or (c) that anyone other than the employees and invitees of the firm were at any time in proximity to it.

(5) Negligence § 67--Exercise of Care Toward Particular Persons-- Trespassers or Licensees--Who are Trespassers and Licensees.

A glazing contractor employed by a lessee to repair a skylight, although an invitee of the lessee, is a trespasser as to the owner.

(6) Negligence § 73--Exercise of Care Toward Particular Persons--Invitees-- Duty Towards Invitees.

The owner or occupant of premises only owes due or ordinary care to an invitee; he is not an insurer.

(7) Negligence § 74--Exercise of Care Toward Particular Persons--Invitees-- Duty Towards Invitees--Knowledge of Danger.

The ground of liability of the owner or occupant of property to an invitee is his superior knowledge of the perilous instrumentality and the danger therefrom to persons going upon the property, there being no liability for injuries from dangers that are obvious, or as well known to the persons injured as to the owner or occupant.

(8) Nuisances § 9--Persons Liable--Notice.

One who was not the creator of a nuisance must have notice or knowledge thereof before he can be held liable for damages on account of injuries arising therefrom.

(9) Nuisances § 11--Persons Liable--Successive Owners.

Where the heirs of the owner of the building conveyed the property to a corporation and such transfer was confirmed in the final decree of distribution, the grantee did not take the property direct from the owner so as to be deemed to be the

“creator” of an alleged nuisance on the premises.

(10) Descent and Distribution § 39--Rights and Liabilities of Heirs--After Vesting--When Title Vests.

Immediately upon demise of the owner of realty, his heirs succeed to the property. (See Prob. Code, sec. 300.)

(11) Nuisances § 11--Persons Liable--Notice--“Neglect.”

In Civil Code, section 3483, providing that every successive owner of property who “neglects” to abate a continuing nuisance upon the property, created by the former owner, is liable therefor, the word “neglect” is not synonymous with the word “omit”, but imports an intent which presupposes knowledge.

See 20 Cal. Jur. 281; 20 R. C. L. 392.

(12) Nuisances § 11--Persons Liable--Notice--Presumption of Knowledge-- Proof.

While the creator of a nuisance is presumed to have knowledge of his own acts, there is no presumption that the successor to the title to the realty has knowledge of the acts of his predecessor in interest; and where heirs succeeded to the title of a warehouse property by operation of law and transferred it to a corporation without knowledge of an alleged nuisance thereon, the corporation cannot be held liable for resulting injuries in the absence of proof of notice or knowledge of the nuisance.

(13) Landlord and Tenant § 316, 317--Rights and Liabilities as to Third Persons--Injuries to Third Persons--Injuries Caused by Nuisance--Negligence.

A landlord cannot be held in damages for a nuisance of which he had no knowledge, nor for negligence because of a hidden defect in the premises of which he had no knowledge.

(14) Landlord and Tenant § 318(2)--Rights and Liabilities as to Third Persons--Injuries to Third Persons--Actions--Evidence.

In an action for personal injuries sustained when an employee of a glazing contractor fell through a skylight, plaintiff's proof that the defective condition of the skylight could not have been

discovered by him either by reasonable care or by reasonable inspection established nonliability of the landlord and the tenant in that it showed that the defect was hidden, not discoverable by reasonable care or reasonable inspection and that it was presumably unknown to defendants, and a directed verdict for the tenant of the building was properly granted.

SUMMARY

APPEAL from a judgment of the Superior Court of the City and County of San Francisco. Sylvain J. Lazarus, Judge. Affirmed.

COUNSEL

Thomas C. Ryan and George Olshausen for Appellant.

Hadsell, Sweet, Ingalls & Lamb, Myrick & Deering and Scott, James Walter Scott and J. LeRoy Wehr for Respondents.

Nourse, P. J.

In 1912 one John A. Lennon contracted for the construction of a four-story building at 37 Drumm Street in San Francisco. The building was erected by a contractor under the supervision of an architect. In 1923 Lennon leased the entire building to the Lawrence Warehouse Company for a term of twenty years. In 1924 Lennon died leaving as his only heirs ten children to whom this property descended. In 1926 one of these children conveyed his interest to the others, and, in 1927, the remaining children conveyed the Drumm Street property to the Estate Company, respondent herein. Thereupon the estate was closed, and a decree of final distribution to the company was entered in conformity with the conveyances from the heirs.

On December 20, 1938, the lessee engaged a glazing contractor to make some repairs to a skylight which was maintained in the rear of the building over a private office. Plaintiff, an employee of this contractor, while working on the skylight, fell and was injured. He sued the owner and the lessee

for damages caused by their alleged negligence in the maintenance of the skylight. The charging part of his complaint reads: "That on the 20th day of December, 1938, plaintiff was an invitee of the defendants in said building and was engaged in repairing a certain glass skylight maintained by said defendants on said premises; that the defendants carelessly and negligently maintained said skylight *744 in a dangerous and defective condition in this: that the cross bars of said skylight were not anchored or did not extend into the walls of said building; that said cross bars were not reinforced by rivets in order to prevent the galvanized metal surrounding said bars from buckling; that the defendants failed to have the hip joints of said skylight placed close together in order to render sufficient support to said skylight; that after said skylight was built the defendants carelessly and negligently installed a sprinkling and ventilating system in said building and used said skylight for support of both said sprinkling system and said ventilating system, thus adding greatly to the strain of said skylight; that for many years the iron ribs into which the glass in said skylight was fitted, were rusted and rotten; that as a result of all of said conditions said skylight became so weakened that it was unable to support the weight of plaintiff while working on said skylight and said skylight gave way and fell in and precipitated plaintiff a distance of approximately twenty (20) feet to the floor below."

At the close of plaintiff's case tending to show that the skylight had been constructed defectively and had since decayed, the trial court granted the motions of both defendants for a directed verdict. On his appeal from the judgment plaintiff seeks to hold the owner on the ground that the faulty construction of the roof was a nuisance; and seeks to hold the lessee on the further ground that it was negligent in failing to observe the dangerous condition of the roof. Before discussing these questions it should be stated that the plaintiff as a witness in his own behalf testified that he had had many years of experience as a glazier, had worked on numerous skylights, was familiar with the various types of

construction, had worked on a few of the types used in the Drumm Street building, and that it was impossible to tell whether the beams of this skylight were safely imbedded in the brick without tearing the brick out, or the metal off. In this respect the witness's statement was confirmed by his experts, and no conflicting testimony was given. The trial court was thus confronted with the undisputed evidence that plaintiff's injuries resulted from a condition of the building which was unknown to both landlord and tenant, and could not have been discovered through ordinary or usual inspection or care.

(1, 2) The directed verdict in favor of the landlord is sound for many reasons, but we will mention but a few.*745 In his complaint the plaintiff clearly and simply pleaded a cause of action for negligence in the maintenance of the skylight. He did not plead a nuisance, public or private. If any of his evidence tended to prove a nuisance he did not rely upon it as such and did not so inform the trial court. The motion for a directed verdict was made upon the case then before the trial court, based upon the pleadings and the proof. It is not a question of variance. It is a simple question whether the evidence proves the case which plaintiff tendered to the trial court. On this appeal the only question is whether the trial court erred. We cannot try the case or the issue *de novo*. (3) Since the plaintiff did not tender the issue to the trial court which he now argues for the first time on appeal, there was no error in that court in reference to that issue which can be reviewed here.

(4) Aside from the question of pleading, the evidence failed to prove a nuisance, either public or private. It is said in 46 C. J., page 646: "A nuisance is common or public where it affects the rights enjoyed by citizens as part of the public, that is, the rights to which every citizen is entitled. A private nuisance is one that affects a single individual or a determinate number of persons in the enjoyment of some private right not common to the public." Appellant proved that the skylight was over a portion

of the business office of the warehouse company. There was no evidence that anyone worked under it, or that any of the public entered these offices. There was no evidence that any customers entered the office, or that anyone other than the employees and invitees of the firm were at any time in proximity to the skylight. There was no evidence that these offices were at any time open to the public. Hence, none of the elements necessary to establish a public nuisance are present.

(5) But the appellant argues that the skylight might have been a private nuisance and that the owner should be held though free from negligence. The argument is not sound. Appellant pleaded that he was an invitee of the defendants for the purpose of repairing the skylight. He proved that he was the invitee of the lessee only. As to the owner he was as a trespasser. (6) The rule is settled in this state that the owner or occupant of premises only owes due or ordinary care to an invitee, and is not an insurer. (*Mautino v. Sutter Hosp. Assn.*, 211 Cal. 556, 560 [296 Pac. 76].)*746

(7) This doctrine is a simple corollary of the well accepted rule that knowledge is the basis upon which the liability to an invitee rests. In 20 Ruling Case Law, page 57, it is said: "The true ground of liability is the proprietor's superior knowledge of the perilous instrumentality and the danger therefrom to persons going upon the property. It is when the perilous instrumentality is known to the owner or occupant and not known to the person injured that a recovery is permitted. ... And, hence, there is no liability for injuries from dangers that are obvious, or as well known to the person injured as to the owner or occupant." (8) And there is no dispute in the authorities that one who was not the creator of a nuisance must have notice or knowledge of it before he can be held. (*Grigsby v. Clear Lake Water Works Co.*, 40 Cal. 396, 407; *Edwards v. Atchison, T. & S. F. R. Co.*, 15 Fed. (2d) 37, 38.) The same principle is clearly stated in 46 C. J., page 742, as follows: "It is a prerequisite to impose liability against a person who merely passively continues a

nuisance created by another that he should have notice of the fact that he is maintaining a nuisance and be requested to remove or abate it, or at least that he should have knowledge of the existence of the nuisance."

(9) To escape this rule appellant argues that the respondent Lennon Estate Co. having taken direct from the deceased must be deemed the "creator" of the alleged nuisance. The argument is faulty because based upon a wholly false premise. (10) The heirs of Lennon succeeded to the property immediately upon his demise. (Sec. 300, Prob. Code; *Johns v. Scobie*, 12 Cal. (2d) 618, 623 [86 Pac. (2d) 820, 121 A. L. R. 1404].) While the title rested in them they conveyed to the corporation. There was no privity between the corporation and the deceased; no organization calling for the application of the "alter ego" doctrine. The decree of distribution, made after the conveyance, merely confirmed the title in the corporation. This was not a transfer of title from the deceased to the corporation, that title was transferred from the deceased to the heirs by operation of law. (*Schade v. Stewart*, 205 Cal. 658, 660 [272 Pac. 567].)

(11) The sound principle that one who has not created a nuisance must be shown to have knowledge of its existence before he can be held finds expression in section 3483 of the Civil Code which reads: "Every successive owner of property*747 who neglects to abate a continuing nuisance upon, or in the use of, such property, created by the former owner, is liable therefor in the same manner as the one who first created it." The words "neglect" and "omit" are not synonymous. The former imports intent and intent presupposes knowledge. (12) The creator of a nuisance is presumed to have knowledge of his own acts. But there is no presumption that the successor to the title to realty has knowledge of the acts of his predecessor in interest. The only conclusion possible under the authorities is that the Lennon heirs, having succeeded to the title by operation of law, transferred to the corporation without knowledge of the alleged nuis-

ance, and the corporation took without notice, or, to be more precise, the appellant made no effort to prove knowledge in any of these parties and rests his case on the argument that such proof was not necessary, though the undisputed evidence is that the existence of the alleged nuisance was not discovered until some twenty-six years after the building was constructed.

(13) For the same reason that a landlord cannot be held in damages for a nuisance of which he had no knowledge, he cannot be held for negligence because of a hidden defect in the premises, of which he had no knowledge. (*Ayres v. Wright*, 103 Cal. App. 610, 618, 619 [284 Pac. 1077]; *Ellis v. McNeese*, 109 Cal. App. 667, 670 [293 Pac. 854].) And it is stated plainly in the latter case that, "It is not sufficient to show that by the exercise of reasonable care the landlord could have discovered the defective condition, but in order to hold him liable it must appear that he knew of such defect." (14) Here the undisputed evidence is that the defective condition of the premises could not have been discovered either by reasonable care or by reasonable inspection. Appellant made this proof in detail to show that the defect was not obvious and that he was free from negligence in not discovering it before the fall. Therein he sought to eliminate the three elements which would have relieved the defendants from legal liability—"actual notice of the danger by the invitee, obvious danger which should have been seen, and danger which might have been seen by reasonable diligence and care." (*Kessler v. Cudahy Packing Co.*, 38 Cal. App. (2d) 607, 610 [102 Pac. (2d) 362]; 20 R. C. L., p. 57.) But, in proving the absence of all these elements as to an expert workman actually on the premises, he at the same time proved the non-liability of the*748 defendants—that the defect was hidden, not discoverable by reasonable care or reasonable inspection, and that it was presumably unknown to the defendants.

Little further need be said in reference to the appeal from the judgment in favor of the warehouse

company. Appellant here rests his argument on a charge of negligence in failing to maintain the roof in a safe condition. He proved no lack of reasonable care on the part of the tenant. The appellant's argument that the defective condition might have been discovered through a reasonable inspection is based wholly upon an incorrect statement of the evidence. On this issue he called four witnesses. It was his theory that the skylight collapsed because the beams, or hip rafters, were not properly imbedded in the brick of the walls and that the hips, or ribs, had rusted and decayed. In his own behalf he testified that for twenty-two years he had been working for the same contractor in the construction and repair of skylights, had worked on some having the same type of construction, and had worked on this particular one several times before the accident. In answer to the question "Was it possible without tearing the thing down-by that I mean pulling the beams out, pulling the sheet metal off and taking it to pieces-to see whether or not those beams were embedded in the brick in any way?" he said, "It would be impossible to tell unless you tore the brick out." Appellant's co-worker was called as a witness, and we find these questions and answers given: "Q. There was nothing to indicate to you as you looked and examined that skylight that there was anything wrong with it that would cause it to let down? A. I didn't see anything. Q. The only way you could see it would be to tear it apart to find out how it was made, isn't that right? A. I would say so, yes." An expert engineer was called by appellant and testified as follows: "Q. What would have been necessary to do, what would it have been necessary to do in order to see whether or not that core bar was embedded in the wall of the building? A. It would have been necessary to lift up some flashing that is embedded in the brick work, take out two lights of glass, and split the sheet metal sash bar open so you could see the core bar." Another expert, a structural engineer engaged in his profession in San Francisco since 1910, testified that the design of this particular skylight was a usual and customary type. In response to the question "And looking*749 at such a skylight, without tearing it

apart to see how the lateral support was or to see the size of those hip rafters, or digging it out to see how far the end was embedded in the wall, without doing that you could not in any way tell that that skylight was unsafe, could you?" he answered, "No, I don't think you could."

Upon this state of the record counsel for appellant states the question involved as to the tenant's liability should be limited by the consideration "that witnesses testified they did not 'think' its condition could be ascertained without digging out the roof." A more careful examination of the undisputed evidence would have relieved all parties from a useless discussion of a question which is not an issue here since that evidence discloses that no reasonable or ordinary inspection would have enabled the tenant to discover the defective condition. Upon his own evidence the appellant has shown that the tenant exercised all the ordinary and reasonable care required of any reasonable person under the same circumstances, and failed to make any proof of facts from which the jury could have inferred negligence.

The judgment is affirmed.

Sturtevant, J., and Spence, J., concurred.

A petition by appellant to have the cause heard in the Supreme Court, after judgment in the District Court of Appeal, was denied by the Supreme Court on January 27, 1941. Carter, J., and Traynor, J., voted for a hearing.

Cal.App.1.Dist.
Reinhard v. Lawrence Warehouse Co.
41 Cal.App.2d 741, 107 P.2d 501

END OF DOCUMENT



REYNOLDS METALS COMPANY, Plaintiff and
Appellant,

v.

NORMAN O. ALPERSON et al., Defendants and
Respondents

L.A. No. 31045.

Supreme Court of California
August 31, 1979.

SUMMARY

Plaintiff brought an action against two shareholders and directors of two bankrupt corporations, seeking to hold them liable for the debts owed plaintiff by the corporations, claiming defendants were "alter egos" of the companies. One count was based on two unpaid promissory notes executed by one corporation with the other as endorser, which provided for recovery of collection cost, including attorney fees limited to 15 percent of the principal amount. Defendants had not signed the promissory notes. Two other causes of action were on common counts. The trial court rejected the alter ego theory and absolved defendants from personal liability for the obligations of the corporations. In addition, the trial court granted defendants 100 percent of their legal fees incurred in attachment proceedings, 75 percent of their fees incurred from the commencement of the lawsuit until certain tort causes of action were dismissed, and 100 percent of their remaining fees. (Superior Court of Los Angeles County, No. C61852, August J. Goebel, Judge.)

The Supreme Court reversed for redetermination of attorney fees. The court held that Civ. Code, § 1717, enacted to establish mutuality of remedy where contractual provision makes recovery of attorney fees available for only one party, is to be interpreted to further provide a reciprocal remedy for a nonsignatory defendant, sued on a contract as if he were a party to it, when a plaintiff would clearly be entitled to attorney fees should he prevail in en-

forcing the contractual obligation against defendant. Accordingly, the court held that, since defendants would have been liable for attorney fees pursuant to the fees provision in the promissory note had plaintiff prevailed, they could recover attorney fees pursuant to Civ. Code, § 1717, now that they had prevailed. The court further held that, because the promissory notes contained a provision limiting attorney fees to 15 percent of the amount of the notes, recovery of fees under Civ. Code, § 1717, must be similarly limited, and the trial court erred in failing to observe that limitation. (Opinion by Clark, J., expressing the unanimous view of the court.)

HEADNOTES

Classified to California Digest of Official Reports
(1) Costs § 7--Amount and Items Allowable--Attorney Fees.

Unless authorized by either statute or agreement, attorney fees ordinarily are not recoverable as costs.

(2) Damages § 11--Compensatory Damages--Attorney Fees--Contractual Provision--Mutuality--Nonsignatory.

Civ. Code, § 1717, enacted to establish mutuality of remedy where contractual provision makes recovery of attorney fees available for only one party and to prevent oppressive use of one-sided attorney fee provisions, is to be interpreted to further provide a reciprocal remedy for a nonsignatory defendant, sued on a contract as if he were a party to it, when a plaintiff would clearly be entitled to attorney fees should he prevail in enforcing the contractual obligation against defendant. Accordingly, in an action against two defendants on promissory notes executed by bankrupt corporations in which defendants were shareholders and directors, with defendants' liability predicated on an alter ego theory, even though defendants had not signed the notes, they were entitled to attorney fees where the notes provided for recovery of collection costs, including attorney fees. Because defendants would

have been liable for attorney fees pursuant to the fees provision had plaintiff prevailed, they could recover attorney fees pursuant to the statute when they prevailed. (Disapproving *Arnold v. Browne* (1972) 27 Cal.App.3d 386, 398-399 [103 Cal.Rptr. 775] and *Sain v. Silvestre* (1978) 78 Cal.App.3d 461, 476 [144 Cal.Rptr. 478], insofar as they are inconsistent.)

[See **Cal.Jur.3d**, Costs, § 64; **Am.Jur.2d**, Costs, § 79.]

(3) Damages § 11--Compensatory Damages--Attorney Fees--Contractual Provision.

Where a cause of action based on a contract providing for attorney fees is joined with other causes of action beyond the contract, the prevailing party may recover attorney fees under Civ. Code, § 1717, only as they relate to the contract action. A litigant may not increase his recovery of attorney fees by joining a cause of action in which attorney fees are not recoverable to one in which an award is proper. Accordingly, attorney fees incurred solely by defendants for defending causes of action not related to an action on promissory notes providing for recovery of attorney fees were not recoverable.

(4) Damages § 11--Compensatory Damages--Attorney Fees--Apportionment.

Attorney fees need not be apportioned when incurred for representation on an issue common to both a cause of action in which fees are proper and one in which they are not allowed. Accordingly, all expenses incurred by defendants with respect to an issue that was common to both an action on a promissory note providing for attorney fees and a cause of action not so providing, qualified for an award of attorney fees.

(5) Damages § 11--Compensatory Damages--Attorney Fees--Contractual Provision--Mutuality--Amount.

Because promissory notes contained provisions limiting attorney fees to 15 percent of the amount of the notes, recovery of fees by defendants who prevailed in an action on the notes under Civ. Code, § 1717, establishing a reciprocal right to attorney

fees, were limited to the same 15 percent of the face amount of the notes.

COUNSEL

Adams, Duque & Hazeltine, James L. Nolan and Margaret Levy for Plaintiff and Appellant.

Kranitz, Sarrow, Imerman & Sacks, Jerome H. Sarrow, Goodstein, Copes & Field, Donald A. Dewar and H. Walter Croskey for Defendants and Respondents.

CLARK, J.

Plaintiff appeals from judgment awarding defendants \$80,500 attorney's fees. We reverse. *127

Defendants, shareholders and directors of Titanium Metallurgical, Inc. (TMI), owned and operated a subsidiary, Turner Metals Supply, Inc. (Turner). Plaintiff supplied aluminum goods and products to Turner pursuant to a general line consignment agreement executed in 1971. TMI signed the agreement as guarantor of Turner's payments. The agreement contained no provision for recovery of attorney's fees in the event of breach.

In January 1973, Turner, with TMI as indorser, executed and delivered two promissory notes in the aggregate principal amount of \$60,794.12. The notes provided for recovery of collection costs, including attorney's fees limited to 15 percent of the principal amount of the notes, in the event of default.

In 1973, Turner and TMI became insolvent and bankruptcy proceedings commenced. Plaintiff, having extended credit of \$823,231.48 to Turner, filed a creditor's claim in the proceedings. Plaintiff also brought this suit seeking to hold defendants personally liable for the debts owed plaintiff by Turner and TMI, claiming defendants were "alter egos" of the two bankrupt companies. Trial proceeded on three causes of action, two on common count and the third upon the two unpaid promissory notes.

After lengthy trial, the court rejected the “alter ego” theory advanced by plaintiff, absolving defendants from personal liability for the obligations of Turner and TMI. In addition, the trial court granted defendants \$80,500 in attorney's fees.^{FN1}

FN1 Defendant Alperson sought to recover \$39,445 in attorney's fees and was awarded \$38,500. Defendant Blivas sought \$51,597.50 and was awarded \$42,000.

The court awarded defendants 100 percent of their legal fees incurred in attachment proceedings, 75 percent of their fees incurred from the commencement of the lawsuit until certain tort causes of action were dismissed, and 100 percent of their remaining fees.

I. Availability of Attorney's Fees

(1) Unless authorized by either statute or agreement, attorney's fees ordinarily are not recoverable as costs. (Code Civ. Proc., § 1021; *D'Amico v. Board of Medical Examiners* (1974) 11 Cal.3d 1, 24-27 [112 Cal.Rptr. 786, 520 P.2d 10]; *Freeman v. Goldberg* (1961) 55 Cal.2d 622, 625 [*12812 Cal.Rptr. 668, 361 P.2d 244]; *Young v. Redman* (1976) 55 Cal.App.3d 827, 834-835 [128 Cal.Rptr. 86].)

Civil Code section 1717 provides in part: “*In any action on a contract*, where such contract specifically provides that attorney's fees and costs, which are incurred to enforce the provisions of such contract, shall be awarded to one of the *parties, the prevailing party, whether he is the party specified in the contract or not*, shall be entitled to reasonable attorney's fees in addition to costs and necessary disbursements.”^{FN2} (Italics added.)

FN2 Section 1717 also provides: “Attorney's fees provided for by this section shall not be subject to waiver by the parties to any contract which is entered into after the effective date of this section. Any provision in any such contract which provides for waiver of attorney's fees is

void. [¶] As used in this section 'prevailing party' means the party in whose favor final judgment is rendered.”

The language of the statute is unclear as to whether it shall be applied to litigants who like defendants have not signed the contract. The section refers to “any action on a contract” thus including any action where it is alleged that a person is liable on a contract, whether or not the court concludes he is a party to that contract. Nevertheless the terms “parties” and “party” are ambiguous. It is unclear whether the Legislature used the terms to refer to signatories or to litigants.

(2) Section 1717 was enacted to establish mutuality of remedy where contractual provision makes recovery of attorney's fees available for only one party (*International Industries v. Olen* (1978) 21 Cal.3d 218, 223 [145 Cal.Rptr. 691, 577 P.2d 1031]; *System Inv. Corp. v. Union Bank* (1971) 21 Cal.App.3d 137, 163 [98 Cal.Rptr. 735]; Review of Selected 1968 Code Legislation (Cont.Ed.Bar) pp. 35-36), and to prevent oppressive use of one-sided attorney's fees provisions. (*Coast Bank v. Holmes* (1971) 19 Cal.App.3d 581, 596-597 [97 Cal.Rptr. 30].)

Its purposes require section 1717 be interpreted to further provide a reciprocal remedy for a nonsignatory defendant, sued on a contract as if he were a party to it, when a plaintiff would clearly be entitled to attorney's fees should he prevail in enforcing the contractual obligation against the defendant.

Attorney's fees were awarded pursuant to section 1717 to a person found not to be a signatory to a contract in *Babcock v. Omansky* (1973) 31 Cal.App.3d 625, 633-634 [107 Cal.Rptr. 512]. The defendant prevailed following the plaintiff's allegation she was liable as a coventurer or partner with another defendant who had executed a promissory note *129 providing for attorney's fees. Concluding that the nonsigning defendant was entitled to attorney's fees, the court reasoned the language of sec-

tion 1717 was sufficiently broad to include persons who had not signed the contract but were sued on the note and found not to be parties to it. (See *Pas v. Hill* (1978) 87 Cal.App.3d 521, 533-536 [151 Cal.Rptr. 98]; *Canal-Randolph Anaheim, Inc. v. Wilkoski* (1978) 78 Cal.App.3d 477, 486, fn. 2 [144 Cal.Rptr. 474]; *Schlocker v. Schlocker* (1976) 62 Cal.App.3d 921, 923 [133 Cal.Rptr. 485]; *Boliver v. Surety Co.* (1977) 72 Cal.App.3d Supp. 22, 29 [140 Cal.Rptr. 259].)

Arnold v. Browne (1972) 27 Cal.App.3d 386, 398-399 [103 Cal.Rptr. 775] and *Sain v. Silvestre*, (1978) 78 Cal.App.3d 461, 476 [144 Cal.Rptr. 478] are disapproved insofar as they are inconsistent with our holding here.

Had plaintiff prevailed on its cause of action claiming defendants were in fact the alter egos of the corporation. (*Kohn v. Kohn* (1950) 95 Cal.App.2d 708, 718 [214 P.2d 71]), defendants would have been liable on the notes. Since they would have been liable for attorney's fees pursuant to the fees provision had plaintiff prevailed, they may recover attorney's fees pursuant to section 1717 now that they have prevailed.

II. The Amount

(3) Where a cause of action based on the contract providing for attorney's fees is joined with other causes of action beyond the contract, the prevailing party may recover attorney's fees under section 1717 only as they relate to the contract action. (*McKenze v. Kaiser-Aetna* (1976) 55 Cal.App.3d 84, 88-90 [127 Cal.Rptr. 275]; see *Schlocker v. Schlocker, supra*, 62 Cal.App.3d 921, 923.) Describing the attorney's fees provision, section 1717 specifically refers to fees "incurred to enforce the provisions of [the] contract." A litigant may not increase his recovery of attorney's fees by joining a cause of action in which attorney's fees are not recoverable to one in which an award is proper. In this case, the two promissory notes contained contract provisions for attorney's fees, but no such provision existed in the general line consignment agreement. Accordingly, attorney's fees incurred

solely for defending causes of action based on the latter agreement and defending against the tort causes of action are not recoverable.

Conversely, plaintiff's joinder of causes of action should not dilute its right to attorney's fees. (4) Attorney's fees need not be apportioned when incurred for representation on an issue common to both a cause of *130 action in which fees are proper and one in which they are not allowed. All expenses incurred with respect to the alter ego issue - common to both the note and the general line consignment agreement - qualify for award.

(5) Because the promissory notes contained provision limiting attorney's fees to 15 percent of the amount of the notes (\$60,794.12) recovery of fees under section 1717 must be similarly limited. As we have seen, the section establishes a reciprocal right to attorney's fees, and the statutory right should be no greater than the contractual right. The statute refers to "reasonable attorney's fees," and reasonable falls within the fundamental principle of reciprocity.

The trial court erred in failing to observe the 15 percent limitation.

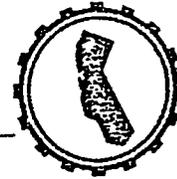
The judgment is reversed for redetermination of attorney's fees.

Bird, C. J., Tobriner, J., Mosk, J., Richardson, J., Manuel, J., and Newman, J., concurred. *131

Cal.
Reynolds Metals Co. v. Alperson
25 Cal.3d 124, 599 P.2d 83, 158 Cal.Rptr. 1

END OF DOCUMENT

California
Manufacturers Association



923 12th Street, P.O. Box 1138, Sacramento, California 95805 (916) 441-5420

June 4, 1980

Honorable Leo T. McCarthy
State Capitol, Room 3164
Sacramento CA 95814

Dear Leo:

Confirming a telephone conversation with Dian Julian of your staff yesterday, we are opposed to Section 3 of your bill AB 2700 and suggest it be deleted.

Section 3 would amend Section 13304 of the Water Code. If adopted it will represent a major change in legislative water quality policy, granting Regional Water Quality Boards significant increased arbitrary power over all waste dischargers in the State-agricultural, industrial and municipal.

Since 1949 regional boards have set requirements on waste discharges, designed to protect receiving water quality. Dischargers are required to meet those requirements and if they don't they are subject to punishment and corrective action.

Section 3 of your bill would give regional boards power to require any discharger who threatens to discharge waste in violation of requirements, or who threatens or has threatened to discharge any waste to state waters and threatens to create a condition of pollution or nuisance to take remedial action.

Thus a regional board could require a discharger to take remedial action even though that discharger was in complete compliance with requirements. That action would have to be something involving changes in plant equipment design and/or location and operating procedures. Thus the regional boards would be getting into the business of telling dischargers how to run their business, something we are strongly opposed to.

We are also opposed to the addition of the words "has discharged" and "has caused or permitted". We simply don't understand the need for those words since the power to abate conditions of pollution or nuisance already exists. What these words do is impose retroactive liability on dischargers covering events in past years which presumably have already been dealt with.

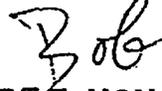
To repeat, we strongly recommend that Section 3 be deleted.

LEGISLATIVE INTENT SERVICE (800) 666-1977

SP-6

We recently received from your office a copy of a proposed Section 4 which would add Section 13362 to the Water Code dealing with recovery of civil damages. We have no problem with this section if it is amended to strike "this division", replacing those words with "Section 13350".

Very truly yours,



ROBERT T. MONAGAN
President

RTM:dd

cc: Members - Senate Health and Welfare Committee
Peter Weiner - Governor's Office
Mary Michel - State Water Resources Control Board

107 Cal.App.3d 456, 165 Cal.Rptr. 726
 (Cite as: 107 Cal.App.3d 456)

C

UNITED STATES FIRE INSURANCE COM-
 PANY, Plaintiff and Respondent,

v.

NATIONAL UNION FIRE INSURANCE COM-
 PANY OF PITTSBURGH, PENNSYLVANIA, De-
 fendant and Appellant.

Civ. No. 57922.

Court of Appeal, Second District, Division 3, Cali-
 fornia.

Jun 25, 1980.

SUMMARY

An insurance company sought to impose liability on a second insurance carrier for losses that resulted from an aircraft accident. The airplane had been piloted by the president of a corporation on company business and the resultant deaths and injuries from the crash were caused by his negligence. Plaintiff insurance company had provided a policy that insured both the corporation and the president, but defendant company's policy clearly did not make the president an insured under its coverage of the corporation. Both the president, personally, and his corporation, vicariously, were liable for the damages arising from the crash of the aircraft. The trial court found that defendant company was responsible to pay \$1 million, the policy limit, on the ground that defendant company was the primary insurer and that the corporation was merely an alter ego of the president. (Superior Court of Los Angeles County, No. C 175117, Robert P. Schifferman, Judge.)

The Court of Appeal reversed, holding the alter ego doctrine could not be applied in the absence of a showing that there was such unity of interest and ownership the separate personalities of the corporation and the individual no longer existed, and that, if the acts were treated as those of the corporation alone, an inequitable result would follow. The court observed that defendant insurer had had nothing to

do with the organization or operation of the corporation and its only relationship to the corporate entity was its contracting to provide insurance coverage. The court also held that, because primary liability for the president's negligence was his own personal liability, plaintiff insurer's policy was the primary policy to the extent of its policy limits. (Opinion by Potter, Acting P. J., with Cobey and Allport, JJ., concurring.)

HEADNOTES

Classified to California Digest of Official Reports
 (1) Insurance Contracts and Coverage §
 100--Extent of Loss of Insured and of Liability of
 Insurer--Coinsurance--Negligence of Corporate Of-
 ficer.

Primary liability for the negligence of a corporation president and director, who was killed in the crash of an airplane piloted by him while engaged in business activities on behalf of his corporation, was his own personal liability and any liability imposed on the corporation would be vicarious. Thus, as between two insurance companies providing coverage to the corporation and its president, a policy that expressly covered the president as an insured was the primary policy to the extent of its policy limits, and a second policy that provided coverage only to the corporation was secondary.

(2) Partnership § 13--Relations With Third Persons--
 Liability of Partner and Partnership--Vicarious Li-
 ability--Right of Indemnity.

The rule giving an employer a right of indemnity against a negligent employee who subjects him to vicarious liability is equally applicable where the negligent party is a partner and subjects the partnership to vicarious liability.

(3a, 3b) Corporations § 4--Power of Court to Dis-
 regard Corporate Entity--When Power Will or Will
 Not Be Exercised--Alter Ego--Liability for Negli-
 gence of Officer--Insurance Coverage.

For the alter ego doctrine to apply to a corporation, there must be shown not only such unity of in-

107 Cal.App.3d 456, 165 Cal.Rptr. 726
 (Cite as: 107 Cal.App.3d 456)

terest and ownership that the separate personalities of the corporation and the individual no longer exist but also that, if the acts are treated as those of the corporation alone, an inequitable result will follow; it may not be applied so as to prejudice the rights of an innocent third party who has dealt with the corporation as such. Thus, an insurance company that expressly provided coverage for a corporate president, who was killed when an airplane he was piloting while on corporate business crashed as a result of his negligence, was the primary insurer and liable for damages up to the limit of policy coverage. A second insurance company, which provided coverage only to the corporation, had had nothing to do with organizing or operating the corporation and its only relationship to the corporate entity was its contracting to provide insurance coverage. Because the second insurance company had not participated in an abuse of the corporation's privilege or been guilty of any inequity, the alter ego doctrine could not be applied to impose liability on it.

[See **Cal.Jur.3d**, Corporations § 19; **Am.Jur.2d**, Corporations, § 16.]

(4) Insurance Contracts and Coverage § 44--Coverage of Contracts--Right to Limit Coverage.

An insurance company has the right to limit the coverage of a policy issued by it and when it has done so, the plain language of the limitation must be respected.

COUNSEL

Kern & Wooley, John R. Johnson and Ralph S. LaMontagne, Jr., for Defendant and Appellant.

Clausen, Harris & Campbell, Kenneth H. Clausen and Arthur E. Schwimmer for Plaintiff and Respondent.

POTTER, Acting P. J.

Defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania (hereinafter National) appeals from a judgment in favor of plaintiff United States Fire Insurance Company (hereinafter

United). The judgment declared the respective parties' obligations as insurers in respect of an aircraft accident in which Philip Morgan, Jr., was the pilot. Claims for the resultant deaths and injuries were settled by United for \$1,527,000, with a contribution of \$300,000 from a nonparty carrier. The judgment decreed that with respect to the accident: "Defendant's policy AV 347207 covered Philip Morgan, Jr., as an insured and is underlying insurance as to Plaintiff's policy DCL 002799 which likewise covered Philip Morgan, Jr., as an insured. That Defendant's policy must be exhausted before Plaintiff's policy comes into play and/or before any payment is due under Plaintiff's policy, and that Plaintiff, having paid \$1,000,000 in settlements that should have been paid by Defendant, is entitled to reimbursement in the amount of \$1,000,000 from Defendant plus interest at *459 the legal rate from the date Plaintiff made its payment; to wit, from September 1, 1976."

The judgment also awarded United judgment against National in the amount of \$1 million plus interest.

The evidence before the trial court consisted of an oral stipulation of facts, documentary exhibits 1 through 5, and four depositions which were received in evidence though not marked as exhibits or numbered as such. The oral stipulation provided as follows: [Counsel for plaintiff]: "Mr. Clausen/ The following facts are stipulated to, for the purposes of this coverage dispute only, and are not binding and have no application in any other proceeding:

"That the accident giving rise to this coverage dispute occurred on October 18, 1974, on which date at Long Beach Airport, Philip Morgan, Jr., piloting a Piper Aztec aircraft, struck a gas storage tank shortly after takeoff. The Piper Aztec then crashed to the ground, all of which caused the death of Morgan and certain deaths and injuries.

"That Philip Morgan, Jr. was negligent; that such negligence approximately [*sic*] [caused] the accident the resulting deaths and injuries.

107 Cal.App.3d 456, 165 Cal.Rptr. 726
(Cite as: 107 Cal.App.3d 456)

“That the occupants of the Piper Aztec at the time of the accident were Philip Morgan, Jr. as pilot, Robert DeRobertis, John C. Whipperman, and Peter Tilson, all of whom sustained fatal injuries, and James Reynolds who sustained serious bodily injury, but who survived the crash.

“That at the time of the accident, Philip Morgan, Jr. was president and chairman of the directors of US West Investments, Golden Pacific Insurance and any and all other subsidiary corporations of US West Investments. That at the time of said accident, Philip Morgan, Jr. was engaged in business activities on behalf of said corporate entities, taking clients and [pro]spective clients on a hunting trip to promote the business of said corporations. That the accident thus arose out of the business of said corporations.

“That at the time of said accident, US West Investments was the record owner of a Beechcraft Bonanza aircraft which was described in the policy issued by defendant, which policy provided specific coverage for *460 said described Beechcraft Bonanza, and in addition, defendant's policy provided coverage for the operations of nonowned aircraft. Prior to the accident, the specific liability coverage on the Beechcraft Bonanza had been deleted because said aircraft was down for a major overhaul and at the time of the accident, said overhaul had not been completed and the liability coverage on this aircraft had not yet been reinstated. The Piper Aztec aircraft was being used by Philip Morgan, Jr. at the time of said accident instead of the Beechcraft Bonanza, because said overhaul had not been completed.

“That the Piper Aztec aircraft was owned by National Aviation Company and had been either rented or loaned to either Golden Pacific Insurance or US West Investments for use at the time of said accident.

“That the INA (Insurance Company of North America) policy listed in plaintiff's policy as specifically scheduled underlying primary insurance,

did not provide any coverage for the use of aircraft.

“The named insureds under plaintiff's policy were US West Investments, Golden Pacific Insurance and all other subsidiary operations of US West Investments and plaintiff's policy limits were \$2,000,000 combined single limit per accident or occurrence.

“The named insured under defendant's policy was US West Investments and defendant's policy limits were \$1,000,000 combined single limit per accident or occurrence.

“Coverage for any other entity or individual under both or either policy is left for the Court to decide. End of stipulation.”

The documentary exhibits included copies of the policies issued by United and National. United's policy was captioned a “Commercial Comprehensive Catastrophe Liability Policy.” The pertinent coverage was “to indemnify the insured for ultimate net loss in excess of the retained limit hereinafter stated, which the insured may sustain by reason of the liability imposed upon the insured by law...[f]or damages...because of personal injury, including death at any time resulting therefrom, sustained by any person or persons...” The retained limit provision, so far as here pertinent, was as follows:

“[T]he company's liability shall be only for the ultimate net loss in excess of the insured's retained limit defined as the greater of: ”(a) the *461 total of the applicable limits of the underlying policies listed in Schedule A hereof, and the applicable limits of any other underlying insurance collectible by the insured; or

“(b) an amount as stated in Item 4(C) ^{FN1} of the declarations as the result of any one occurrence not covered by the said policies or insurance;...”

FN1 The amount specified in item 4(C) of the declarations was \$10,000.

The definition of “insured” in the United policy

107 Cal.App.3d 456, 165 Cal.Rptr. 726
(Cite as: 107 Cal.App.3d 456)

included "any executive officer, director or stockholder of the named insured with respect to the use of an automobile or aircraft not owned by the named insured in the business of the named insured."

As a result of the above provision, it was apparent that Philip Morgan, Jr., individually, was an insured within the personal injury liability coverage of the United policy.

The National policy, on the other hand, clearly did not make Morgan an insured under its bodily injury coverage as of the date of the accident. As originally issued June 14, 1974, National's policy did extend bodily injury coverage to Morgan provided he was "using" the Beechcraft Bonanza aircraft of which U.S. West Investments was the record owner and which was described in the policy declarations, or was "legally responsible for its use." However, with respect to use of nonowned aircraft, such insured status was expressly withheld by an endorsement effective at the initiation of the policy. Coverage with respect to the operation of nonowned aircraft was limited to U.S. West Investments as named insured. The endorsement extending this coverage, for which an additional premium of \$175 was charged, deleted the definition of "Insured" which applied to the described aircraft liability coverage as well as special provisions providing automatic insurance for newly acquired aircraft and a special provision governing "Use of Other Aircraft." However, before the accident occurred, further endorsements deleted altogether the described aircraft liability coverage, thus eliminating any coverage under which Morgan was an insured. A substantial premium refund accompanied the subsequent endorsement whereby, in effect, National refunded approximately \$200 of a total liability premium of \$525 which included \$175 for the nonownership endorsement and \$350 for the described aircraft liability. Inasmuch as the nonownership endorsement remained in effect for the full policy term, it is apparent that *462 \$200 of the \$350 described aircraft liability coverage premium

was refunded after approximately one-fourth of the policy term had expired. In consideration of this refund, U.S. West Investments became the sole insured for liability purposes and was covered only for use of nonowned aircraft in its behalf.

The stipulated facts, of course, show that both Morgan, personally, and U.S. West, vicariously, were liable for the damages arising from the crash of the nonowned Piper aircraft due to Morgan's negligence. Morgan was also an insured under an owner's policy covering the Piper aircraft. This policy had policy limits of \$300,000 which sum was paid in full by the insurer, thus reducing the outlay for settlement to \$1,227,000. The issue between United and National thus related to the allocation of responsibility between them for the remaining liability.

United contended that National was responsible to pay \$1 million of the loss because National's policy constituted "underlying insurance collectible by the insured," making "the insured's retained limit" under United's policy \$1.3 million,^{FN2} so that United's indemnity agreement covered only the excess, or \$227,000, leaving National responsible for its full policy limits.

FN2 United treated the owner's \$300,000 liability policy as underlying insurance in respect of United's policy.

National, on the other hand, contended that whereas United's policy extended coverage both to Morgan, individually, and to U.S. West Investments, National's policy expressly excluded Morgan as an insured in respect of liability arising from the use of nonowned aircraft and covered only U.S. West Investments in that respect. In view of the stipulated fact that the sole cause of the accident was Morgan's negligence for which U.S. West Investments was only vicariously liable, National invoked the rule that a policy which covers the individual liability of a negligent employee as "an additional insured...is primary over a policy...which covers only the vicarious liability of the employ-

107 Cal.App.3d 456, 165 Cal.Rptr. 726
(Cite as: 107 Cal.App.3d 456)

er...under the doctrine of *respondeat superior*.” (*Hartford Accident & Indemnity Co. v. Transport Indemnity Co.* (1966) 242 Cal.App.2d 90, 92 [51Cal.Rptr. 168].)

In reply, United relied upon the testimony in the four depositions taken of four surviving principals of U.S. West Investments as showing: “Alter Ego Is Applicable. US West Investments and Golden Pacific Insurance *463 Were Alter Egos of Morgan, Anderson, Hammer and Kummer. Phil Morgan, Jr., Is Thus One of Defendant's Named Insureds.”^{FN3}

FN3 United's trial brief, page 8.

National, in turn, argued that even if the evidence supported a finding of alter ego, the alter ego doctrine was not applicable so as to rewrite its policy by adding an expressly excluded insured, because National was not a party to any inequitable conduct.

National further contended that if both policies were found to cover Morgan's individual liability, the coverage should be prorated in the ratio of the respective policy limits.

The trial court issued a written intended decision. In respect of the evidence concerning the alter ego claim, the court adopted “as its recital of the evidence,” pages 1 to 7 of United's trial brief. According to this recital, the principals, who “were separately engaged in the insurance business as agents and brokers” in 1971 “joined forces and merged their businesses into one.” “Phil Morgan, Jr., was the dominant, dominating factor. He conceived the idea of combining these various agencies into one business, sold the others on the idea, and thereafter dominated the new business, which the individuals thereafter conducted *substantially as partners* by utilizing several corporate alter egos.” (Italics added.)

The status of the twin-engine Bonanza aircraft referred to in National's policy was described by

United as follows: “He [Morgan] owned an aircraft before the merger which he brought with him... [A]s among the principals, Morgan alone flew this plane.... Morgan used this plane, as he always had, as his own.” However, though “Morgan flew the plane on many pleasure-business trips to such places as fishing spots in Mexico, [h]e never made such trips for only his own pleasure. His personal life and his business life were one and the same, and on all such trips clients accompanied him.”

One of the corporate alter egos utilized by the partners was U.S. West Investments which was made registered owner of the airplane to avoid a California use tax, and “[s]ince U.S. West Investments was the 'record' owner, the liability insurance policy on this plane, a 1958 twin engine Beechcraft Bonanza, was in the name of U.S. West Investments.” The activities of U.S. West Investments were allegedly confined to the above described record ownership and provision of insurance for *464 said aircraft. It “continued as before to neither receive nor disburse money. It had no bank account or assets, carried on no business and was nothing more than a 'paper entity.’”

The financial aspects of the merged business in the meantime were conducted in the name of another corporate alter ego, Golden Pacific Insurance. “All business continued to be done through Golden Pacific Insurance and the only money the principals received out of the business done came through the form of salary checks from Golden Pacific Insurance and expense reimbursements from Golden Pacific Insurance.” “All banking was done in the name of Golden Pacific Insurance.... For all practical purposes these men *did business as partners* under the name of Golden Pacific Insurance Agency.” (Italics added.) It was in the name of that corporation that the agency license was obtained.

Further facts detailed in United's recital included the issuance of shares in an original U.S. West Investments corporation in proportion to the agreed value of the respective principal's contributed business; and subsequent exchange of these

107 Cal.App.3d 456, 165 Cal.Rptr. 726
 (Cite as: 107 Cal.App.3d 456)

shareholdings by said principals for approximately 90 percent of the stock of an existing publicly held corporation (Protronics, Inc.), a New Jersey manufacturing enterprise which had ceased to do business. The name of Protronics was then changed to U.S. West Investments on dissolution of the original company of that name.

Finally, United claimed: "From the time the '*partners*' combined their businesses to the time of the accident, Phil Morgan, Jr., was president of U.S. West Investments, of Golden Pacific Insurance, and any and all other purported corporate entities utilized by the principals. The remaining '*partners*' were all corporate officers, holding the same title as to each purported corporate entity, and all such purported entities had the same board of directors who were the individuals previously named who had merged their businesses. No Golden Pacific stock was ever issued. Directors' meetings were ordinarily informal business conferences in Phil Morgan's offices, and these meetings usually purported to be directors' meetings of Golden Pacific Insurance.

"Subsequent to Mr. Morgan's death the business became insolvent, ceased operating, and Golden Pacific agency became involved in a bankruptcy. U.S. West Investments was not included in the bankruptcy. It never had assets, nor did it ever receive, hold or disburse any money. It was simply ignored." (Italics added.) *465

On the basis of the above alleged facts as claimed by United, the trial court opined that "the requisite unity of interest and ownership between Morgan and U.S." to invoke the alter ego doctrine was shown. The court further held that the second element necessary to the application of the alter ego doctrine, "fraud or inequity," was also present. The court referred in this connection to the insolvency of U.S. West Investments and of Golden Pacific and of an inference of inequitable purpose "to be drawn from the intermingling of funds, payment of personal obligations by the corporation, and deposit of the individual's private funds in the corporation's

bank account..." The court further relied in this connection upon National's assumed knowledge that Morgan would be flying the airplane so that "he should be deemed a named insured."

Findings of fact and conclusions of law were requested by National. The findings generally conformed to the stipulation and the recital of facts in United's trial brief, with one exception. Instead of finding that U.S. West Investments and Golden Pacific Insurance were alter egos of the several principals who were in effect partners, finding No. 9 stated "[t]hat said purported corporate entities, including U.S. West Investments and Golden Pacific Insurance, were the alter egos of Philip Morgan, Jr." so "[t]hat U.S. West Investments as an alter ego of Philip Morgan, Jr., is but another name for Philip Morgan, Jr., and Philip Morgan, Jr., was thus personally insured under [National's] policy at the time of said accident."

From its findings, the court concluded that "[National's] policy covers Philip Morgan, Jr., individually, as an insured; that [National's] share of said settlement was its full policy limit of \$1,000,000 which should have been paid by [National] toward said settlement." The judgment accordingly so declared and awarded United the judgment in the sum of \$1 million. This appeal followed.

Contentions

National contends that: (1) its policy does not cover Morgan individually as an insured and that its coverage of the vicarious liability of U.S. West Investments in respect of Morgan's negligence is secondary coverage following the primary coverage of United's policy which expressly makes Morgan an insured; (2) as an innocent third party, National cannot be subjected to liability on an alter ego theory; and (3) in any event, if National is held to have insured Morgan individually, *466 the liability for coverage should be prorated on the basis of the respective policy limits.

United contends that: (1) although it "has no

107 Cal.App.3d 456, 165 Cal.Rptr. 726
(Cite as: 107 Cal.App.3d 456)

quarrel with” the principle invoked in National's first contention, the court properly applied the alter ego doctrine to make Morgan an insured under National's policy; and (2) the United policy is by its terms excess coverage only in respect to any risk having “other underlying insurance collectible,” and therefore not subject to proration.

Discussion

Summary

The nonowned aircraft coverage under National's policy was expressly limited to the vicarious liability of the named insured, U.S. West Investments. As such, it was secondary to any coverage of Morgan individually as negligent operator of the aircraft. The claimed alter ego status of U.S. West Investments does not alter the coverage because (1) the rationale for the coverage rule remains fully operative, and (2) there is no fraud or inequity in its application.

Having concluded that United's policy is the primary coverage, it is unnecessary to reach National's contention that liability should be prorated.

Unless a Contrary Result Is Required Under the Alter Ego Doctrine, National's Coverage Was Secondary

(1)The provisions of both policies were perfectly clear. United's policy specifically extended coverage to Morgan as an insured because he was an “executive officer, director or stockholder of the named insured” and he was using an “aircraft not owned by the named insured in the business of the named insured.” On the other hand, under National's policy, the only insured with respect to the use of nonowned aircraft was the named insured, U.S. West Investments. Since the stipulated facts included the fact that at the time of the accident, Morgan “was engaged in business activities on behalf of said corporate entities [U.S. West Investments and Golden Pacific Insurance], taking clients and [pro]spective clients on a hunting trip to promote the business of *467 said corporations” of which he was president, it is apparent that the primary liability for Morgan's negligence was his own personal

liability. Liability imposed upon U.S. West Investments was vicarious liability for Morgan's fault.

The obligations of Morgan and of U.S. West Investments were, therefore, governed by the rule stated in *Continental Cas. Co. v. Phoenix Constr. Co.* (1956) 46 Cal.2d 423, 428-429 [296 P.2d 801, 57 A.L.R.2d 914]: “Where a judgment has been rendered against an employer for damages occasioned by the unauthorized negligent act of his employe, the employer may recoup his loss in an action against the negligent employe [Citations]; that is, as between employer and employe in such a situation, *the obligation of the employe is primary and that of the employer secondary....*”

“Under equitable principles of subrogation the insurer of the employer who has been compelled to pay the judgment against the employer may recover against the negligent employe or the employe's insurer. [Citations.]” (Italics added.) Since the policy covering the employee as an insured had policy limits sufficient to cover the loss, such policy was found to be the primary coverage.

Hartford Accident & Indemnity Co. v. Transport Indemnity Co., supra., 242 Cal.App.2d 90, relied upon *Continental Cas. Co.* to reach a like result, imposing all liability upon the vehicle owner's policy which made a permissive user an insured and relieving the carrier which covered only his employer on account of vicarious liability.

It is clear, therefore, that under the facts of this case, the United policy, which expressly covered Morgan as an insured, was the primary policy unless that result is avoided by the application of the alter ego doctrine.

The Alter Ego Relationship Shown by the Evidence Does Not Eliminate the Reason for Making U.S.

West Investment's Obligation Secondary

As pointed out above, the reason National's coverage of U.S. West Investments is secondary to United's coverage of Morgan is that U.S. West Investments was entitled to indemnity against Mor-

107 Cal.App.3d 456, 165 Cal.Rptr. 726
 (Cite as: 107 Cal.App.3d 456)

gan. Theoretically, if Morgan, as a sole proprietor, and U.S. West Investments were *468 alter egos, no such obligation to indemnify could arise, because Morgan could not have an obligation to indemnify himself. The evidentiary showing in the trial court, however, did not support any claim that Morgan was a sole proprietor. United in its brief concedes “[t]he fact that there were several men who in essence did business as partners through alter ego corporate shells...” This concession is consistent with the position taken by United in its trial brief where repeated reference was made to the fact that the principals “did business as partners.” There is no suggestion in the record that Morgan's flying activities did not promote the entire partnership business and the only possible meaning of the stipulation that at the time of the accident Morgan was flying in behalf of the insured corporations is that he was engaged in partnership activities if in fact such corporations were merely instrumentalities through which the partnership business was carried on.

(2)The rule giving an employer a right of indemnity against a negligent employee who subjects him to vicarious liability is equally applicable where the negligent party is a partner and subjects the partnership to vicarious liability.

“The law of partnership is the law of agency. Each partner is the agent of the other, and impliedly agrees that he will exercise reasonable care and diligence in the operation of the partnership business. When a loss is paid by a partnership, there is a right of indemnity against the partner whose negligence caused the loss. *Yorks v. Tozer*, 59 Minn. 78, 60 N.W. 846, 28 L.R.A. 86, 50 Am. St. Rep. 395. It is the same rule where the principal is held liable for the negligent act of his agent. Upon payment of the loss, the principal may bring action against his agent to be indemnified for the loss sustained: 2 C. J. 721. As stated in Rowley's 'Modern Law of Partnership,' vol. 2, § 983, 'Losses caused wholly by the negligence or misconduct of one party must be borne by him.' In 'The Law of Partnership' by Shu-

maker (2d Ed.) 160, it is said: 'A partner has no right to charge the firm with losses or expenses caused by his own negligence or want of skill....' Also see 33 C. J. 864.” (*United Brokers' Co. v. Dose* (1933) 143 Ore. 283 [22 P.2d 204, 205].)

68 Corpus Juris Secundum, section 83, page 522, states the rule as follows: “Where a partnership is liable for injuries to a third person, there is a right of indemnity against the partner whose negligence caused the injuries. [Fn. omitted.]” *469

It is thus apparent that United's claim that U.S. West Investments was the alter ego of its principals conducting business “substantially as partners” does not alter Morgan's indemnity obligation upon which the coverage question depends.

No Inequity Justifying Invocation of the Alter Ego Doctrine Has Been Shown

(3a)In order for the alter ego doctrine to apply, there must be shown not only “such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist,” but further “that, if the acts are treated as those of the corporation alone, an inequitable result will follow.” (*Automotriz etc. De California v. Resnick* (1957) 47 Cal.2d 792, 796 [306 P.2d 1].) In the trial court, National virtually conceded the existence of the first element. In its brief on appeal, however, National argues: “There was clearly a separate corporate existence.” We find it unnecessary to resolve this issue, however, since it is clear, in any event, that even if U.S. West Investments failed to achieve any separate existence, no fraud or other inequitable result will follow if it is recognized as the sole insured under the nonowned aircraft coverage of National's policy. “The *alter ego* doctrine is applied to avoid inequitable results not to eliminate the consequences of corporate operations.” (*Aladdin Oil Corp. v. Perluss* (1964) 230 Cal.App.2d 603, 614 [41 Cal.Rptr. 239].) Consequently, it may not be applied so as to prejudice the rights of an innocent third party who has dealt with the corporation as such.

107 Cal.App.3d 456, 165 Cal.Rptr. 726
(Cite as: 107 Cal.App.3d 456)

An example of this limitation is *Tarter, Webster & Johnson, Inc. v. Windsor Developers, Inc.* (1963) 217 Cal.App.2d Supp. 875 [31 Cal.Rptr. 452]. A trial court judgment allowing the plaintiff a materialman's lien against defendant's property was reversed. The defendant contracted with Cal-Mar, a corporation formed by Bailey, Butts and Procopio for the purpose of acting as framing contractors in the construction of buildings, to do the framing in defendant's housing project. Defendant also dealt with Trus-Span, another corporation formed by Bailey and Butts "for the purpose of buying and selling building materials" (*id.*, at p. 877) to furnish the necessary materials to be delivered in "built-up loads" appropriate to construct each house. Plaintiff, a building material supplier, sold Trus-Span built-up loads which were delivered to the property and utilized in the construction of the houses. To escape the consequences of the rule "that one who furnishes materials *470 to a person who is himself a materialman is not entitled to a lien" (*id.*, at p. 878), plaintiff showed facts upon which the trial court found that "Trus-Span and Cal-Mar, were but the *alter egos* of the individuals, Bailey, Butts and Procopio" (*id.*, at p. 879), and on this basis held that plaintiff was entitled to a materialman's lien. In reversing, the reviewing court said (*id.*, at pp. 879-881): "It would serve no useful purpose to review in detail the voluminous testimony which was received upon this feature of the case. It is sufficient for the purposes of this opinion to state that were this an action against these individuals to hold them personally liable for the obligations of these corporations upon the *alter ego* theory, the evidence introduced in this action would be sufficient to justify a judgment against them.

"The difficulty with this situation, however, is that neither Trus-Span nor Cal-Mar nor the individuals who organized them are parties to this action. It appears that the plaintiff, who was in the business of selling lumber at wholesale, sold the materials in question to Trus-Span at wholesale prices, plus an additional charge for making up the built-up loads. The materials thus sold were

charged to Trus-Span on an open account. The defendant made its contract with Trus-Span for the purchase of these materials for which defendant agreed to pay a larger price than that charged to Trus-Span. In other words, Trus-Span was making a profit from the purchase and sale of the material. There is no evidence in the record that there was any bad faith on the part of the defendant or that defendant knew of facts which would indicate that the corporations were but the *alter egos* of the individuals. It is the fact that no permit to issue stock was granted to either corporation and apparently no stock was actually issued. The fact remains, however, that both corporations were organized and charters were issued and filed for record.

"The general purpose of the *alter ego* theory is to look through the fiction of the corporation and to hold the individuals doing business in the name of the corporation liable for its debts in those cases where it should be so held in order to avoid fraud or injustice. (*D. N. & E. Walter & Co. v. Zuckerman*, 214 Cal. 418 [69 P.2d 839, 79 A.L.R. 329].)

"Generally speaking, in order to enforce the *alter ego* theory bad faith must be shown. (*Hollywood Cleaning & Pressing Co. v. Hollywood Laundry Service, Inc.*, 217 Cal. 124 [17 P.2d 709]; *Wilson v. Stearns*, 123 Cal.App.2d 472 [267 P.2d 59]; *Luis v. Orcutt etc. Co.*, 204 Cal.App.2d 433 [22 Cal.Rptr. 389].) *471

"

.....

"Referring then to the instant case, it appears from the evidence that the defendant had nothing whatever to do with the two corporations except to contract with them for materials and labor. Bills were rendered by the two corporations and were paid. Waivers of lien were executed and delivered to defendant. On the other hand, the plaintiff, a wholesaler of lumber, agreed to sell lumber to the Trus-Span Corporation as a dealer of materials. There were no representations to the plaintiff that Trus-Span was a contractor. Under such circum-

107 Cal.App.3d 456, 165 Cal.Rptr. 726
(Cite as: 107 Cal.App.3d 456)

stances plaintiff was in the position of selling materials at wholesale to a corporation holding itself out as a retailer and which was in turn selling at a profit to the property owner. Under such circumstances plaintiff would not be entitled to a lien. It is true that Trus-Span failed to pay plaintiff. Had there been either allegation or proof that the defendant in any way conspired to produce such result, defendant might be held liable or a lien might effectually be placed upon its property. Here, however, it is sought to use the *alter ego* theory, not as against the parties who conducted the business in the name of the corporations, but against an innocent third party who has already paid for the materials. It is clear from the prior decisions of the California courts that the *alter ego* theory may not be used for such purpose.”

The facts in *Tarter* are indistinguishable from those in the case at bench. Neither U.S. West Investments nor the principals who utilized it are parties to the action. National had nothing whatever to do with organizing or operating U.S. West Investments. Its only relationship to that entity was its contracting to provide insurance coverage relating to the use of aircraft in U.S. West Investment's behalf. Moreover, National had given full consideration in the elimination of Morgan's insured status by substantially reducing the premium.

A similar statement limiting the applicability of the doctrine appears in *Meyer v. Glenmoor Homes, Inc.* (1966) 246 Cal.App.2d 242, 260-261, where the court said: “Moreover, since the purpose of the doctrine of disregarding the corporate entity is to prevent fraud it cannot be used to inflict an obligation on an innocent corporation or its minority stockholders. (*Oakland Medical Bldg. Corp. v. Aureguy, supra.*, and *Commercial Lbr. Co. v. Ukiah Lbr. Mills, supra.*; *Dashew v. Dashew Business Machines, Inc.* (1963) 218 Cal.App.2d 711, 716 [32 Cal.Rptr. 682].)” *472

Tacit recognition of the same limitation of the doctrine is found in *Roman Catholic Archbishop v. Superior Court* (1971) 15 Cal.App.3d 405 [93

Cal.Rptr. 338], where the alter ego doctrine was held inapplicable to subject one subsidiary to liability for the obligations of another subsidiary controlled by the same parent. The court said (*id.*, at p. 412): “The purpose of the doctrine is not to protect every unsatisfied creditor, but rather to afford him protection, where some conduct amounting to bad faith makes it inequitable... for the equitable owner of a corporation to hide behind its corporate veil.” (*Associated Vendors, Inc. v. Oakland Meat Co., supra.*, 210 Cal.App.2d 825, at p. 842 [26 Cal.Rptr. 806].)”

The teaching of the foregoing cases is that the fraud or inequity, the elimination of which legitimately invokes the doctrine, must be that of the party against whom the doctrine is invoked, and such party must have been an actor in the course of conduct constituting the “abuse of corporate privilege” (15 Cal.App.3d at p. 411), or must be seeking some inequitable advantage based upon “the fiction of separate existence” (*ibid.*). No such circumstances exist in this case. There is no evidence in the record whatever that National participated in the abuse of U.S. West Investments' corporate privilege. The circumstance that U.S. West Investments and Golden Pacific Insurance both became insolvent is immaterial to the position of either National or United. As insurers who received their agreed premiums for coverage, they have no concern with the ability of their insureds to satisfy claims. In recognition of this fact, Insurance Code section 11580, subdivision (b), provides that the insurer's obligation is not affected by the insolvency or bankruptcy of the insured during the life of the policy.

The trial court's finding of inequity was premised on the assumption that if Morgan were not made an insured under National's policy, it “would be permitted to avoid its obligations and the risks which it voluntarily undertook under the subject insurance policy for which it had been duly compensated, thereby unfairly placing [United] in the position of a primary, rather than an excess, in-

107 Cal.App.3d 456, 165 Cal.Rptr. 726
 (Cite as: 107 Cal.App.3d 456)

suror." There are two faults with this premise. The first is the assumption that National voluntarily undertook to insure Morgan against personal liability, and the second is that it was compensated for any such coverage. As above pointed out, approximately \$200 of an original annual premium of \$350 for aircraft liability coverage which did cover Morgan was refunded when the described aircraft liability coverage was deleted after it had been in effect two and one-half months. Substantially, the only liability coverage *473 premium retained was the \$175 annual premium for the nonownership coverage which was limited to the named insured, U.S. West Investments. After this endorsement, National neither undertook coverage of Morgan nor received compensation therefor.

Though the effect of this withdrawal of coverage unquestionably increased United's exposure under its policy which expressly covered Morgan's individual liability, it is difficult to see how National is chargeable with any inequity in this respect. (4) "An insurance company has the right to limit the coverage of a policy issued by it and when it has done so, the plain language of the limitation must be respected." (*Continental Cas. Co. v. Phoenix Constr. Co.*, *supra.*, 46 Cal.2d at p. 432.) If Morgan was willing to rely upon the coverage provided by the owner's policies for the borrowed aircraft and thereby save U.S. West Investments premium dollars, the pro rata refund of the liability premium was reasonable if not obligatory. (Ins. Code, § 481, subd. (a)(2); *Jenson v. Allstate Ins. Co.* (1973) 32 Cal.App.3d 789, 793.)

(3b) In any event, there is nothing in the record in any respect suggesting that the deletion of individual coverage for Morgan violated any rights or expectations of United. United's policy expressly covered Morgan as an insured while he was operating a nonowned aircraft in the business of U.S. West Investments. There was, however, no evidence that United relied upon the existence of any underlying insurance, other than that usually carried by the nonowned aircrafts' owners, to reduce

its exposure under this coverage. The fact that the National policy was not scheduled, though provision was made for scheduling of policies upon which the premium was based, belies any inference that United acted on the assumption that there was underlying insurance carried by U.S. West Investments.

The record is equally devoid of any evidence that National had any reason to believe that there was an umbrella policy providing such unusual coverage as that specified in the United policy or that the National policy would not be scheduled in any such umbrella policy, should it exist. We are, consequently, unable to find any basis for accusing National of inequity of any kind; it simply provided the coverage which its insured was willing to pay for, and the alter ego doctrine cannot appropriately be applied to impose liability upon it. The United policy, therefore, was the primary coverage for liability caused by the negligence of Morgan while flying in the course of the business of U.S. *474 West Investments. Its policy limits were adequate to cover all the loss suffered by the injured parties. No occasion, therefore, arose for resort to National's coverage of the vicarious liability of U.S. West Investments.

The judgment is reversed and the cause remanded with directions to enter a judgment in favor of defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania.

Cobey, J., and Allport, J., concurred.

Respondent's petition for a hearing by the Supreme Court was denied August 20, 1980. *475

Cal.App.2.Dist.

United States Fire Ins. Co v. National Union Fire Ins. Co.

107 Cal.App.3d 456, 165 Cal.Rptr. 726

END OF DOCUMENT

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313

(Cite as: 881 F.2d 801)



United States Court of Appeals,
Ninth Circuit.

WILSHIRE WESTWOOD ASSOCIATES; Platt
Development Company, Plaintiffs–Appellants,

v.

ATLANTIC RICHFIELD CORPORATION; Peter
J. Ruddock; John Crawford; Thomas Crawford; and
Does 1 through 20, Defendants–Appellees.

No. 88–5708.

Argued and Submitted Dec. 9, 1988.

Decided Aug. 7, 1989.

Action was brought alleging claim for response costs under Comprehensive Environmental Response, Compensation, and Liability Act. The United States District Court for the Central District of California, Robert M. Takasugi, J., dismissed complaint. Appeal was taken. The Court of Appeals, Coyle, District Judge, sitting by designation, held that petroleum exclusion in Act applies to unrefined and refined gasoline.

Affirmed.

Reinhardt, Circuit Judge, filed a specially concurring opinion in which O'Scannlain, Circuit Judge, joined.

West Headnotes

[1] Federal Courts 170B ↪776

170B Federal Courts

170BVIII Courts of Appeals

170BVIII(K) Scope, Standards, and Extent

170BVIII(K)1 In General

170Bk776 k. Trial De Novo. Most

Cited Cases

Dismissal for failure to state a claim is a ruling on question of law and, as such, is reviewed de novo. Fed.Rules Civ.Proc.Rule 12(b)(6), 28 U.S.C.A.

[2] Environmental Law 149E ↪440

149E Environmental Law

149EIX Hazardous Waste or Materials

149Ek436 Response and Cleanup; Liability

149Ek440 k. Substances Covered. Most

Cited Cases

(Formerly 199k25.5(10) Health and Environment)

Petroleum exclusion in Comprehensive Environmental Response, Compensation and Liability Act applies to unrefined and refined gasoline, even though certain of its indigenous components and certain additives introduced during refining process have themselves been designated as hazardous substances within meaning of the Act. Comprehensive Environmental Response, Compensation, and Liability Act of 1980, § 101(14), 42 U.S.C.A. § 9601(14).

[3] Statutes 361 ↪196

361 Statutes

361VI Construction and Operation

361VI(A) General Rules of Construction

361k187 Meaning of Language

361k196 k. Relative and Qualifying

Terms, and Their Relation to Antecedents. Most

Cited Cases

“Doctrine of the last antecedent” states that qualifying words, phrases and clauses must be applied to words or phrases immediately preceding them and are not to be construed as extending to and including others more remote.

*801 Rene P. Tatro, San Francisco, Cal., for plaintiffs-appellants.

Patrick W. Dennis, Los Angeles, Cal., for Atlantic Richfield.

T. Emmet Thornton, Los Angeles, Cal., for Peter Ruddock.

Gary R. Ricks, Santa Barbara, Cal., for John Craw-

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313
(Cite as: 881 F.2d 801)

ford, defendants-appellees.

M. Alice Thurston, Washington, D.C., for amicus U.S.

Appeal from the United States District Court for the Central District of California.

Before REINHARDT and O'SCANNLAIN, Circuit Judges, and COYLE, District Judge.^{FN*}

FN* Honorable Robert E. Coyle, United States District Judge for the Eastern District of California, sitting by designation.

COYLE, District Judge:

Wilshire Westwood Associates and Platt Development Company appeal the district court's dismissal pursuant to F.R.Civ.P. 12(b)(6) of their complaint against Atlantic Richfield Corporation, Peter J. Ruddock, John Crawford and Thomas Crawford. The district court concluded that the petroleum exclusion set forth in Section 101(14) of the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), 42 U.S.C. § 9601(14), applies to leaded gasoline. We affirm.

***802 A. Background.**

On April 8, 1987 Wilshire Westwood Associates and Platt Development Company (hereinafter referred to as plaintiffs) filed a complaint against Atlantic Richfield Corporation, Peter J. Ruddock, John Crawford and Thomas Crawford (hereinafter referred to as defendants) alleging a claim for response costs from defendants pursuant to Section 107(a) of CERCLA, 42 U.S.C. § 9607(a)(2)(B).^{FN1}

The complaint alleges at paragraph 6 that "[t]he gasoline stored in leaking underground storage tanks ... contained additives with hazardous substances including, but not limited to, benzene, toluene, xylene, ethyl-benzene and lead [which] leaked from the underground storage tanks and contaminated soils...." Paragraphs 30 and 32 respectively allege that "[t]he substances identified in

paragraph 6 ... are hazardous substances within the meaning of Section 101(14) of CERCLA, 42 U.S.C. § 9601(14)" and that "[t]here have been releases or threatened releases of hazardous substances, including, but not limited to, those identified in paragraph 6 ... into the environment ... within the meaning of Section 101(22) of CERCLA, 42 U.S.C. § 9601(22).^{FN2}

FN1. 42 U.S.C. § 9607(a)(2)(B) provides in pertinent part:

Notwithstanding any other provision or rule of law, and subject only to the defenses set forth in subsection (b) of this section—

(2) any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of

(4) ... shall be liable for—

(B) any other necessary costs of response incurred by any other person consistent with the national contingency plan....

FN2. 42 U.S.C. § 9601(14) defines the term "hazardous substance" as:

(14) The term 'hazardous substance' means (A) any substance designated pursuant to section 1321(b)(2)(A) of Title 33, (B) any element, compound, mixture, solution, or substance designated pursuant to section 9602 of this title, (C) any hazardous waste having the characteristics identified under or listed pursuant to section 3001 of the Solid Waste Disposal Act [42 U.S.C.A. § 6921] (but not including any waste the regulation of which under the Solid Waste Disposal Act [42 U.S.C.A. § 6901 et seq.] has been suspended by Act of Congress), (D) any toxic pollutant listed under section

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313
(Cite as: 881 F.2d 801)

112 of the Clean Air Act [42 U.S.C.A. § 7412], and (F) any imminently hazardous chemical substance or mixture with respect to which the Administrator has taken action pursuant to section 2606 of Title 15. *The term does not include petroleum, including crude oil or any fraction thereof which is not otherwise specifically listed or designated as a hazardous substance under subparagraphs (A) through (F) of this paragraph*, and the term does not include natural gas, natural gas liquids, liquefied natural gas, or synthetic gas usable for fuel (or mixtures of natural gas and such synthetic gas). [emphasis added]

The district court initially denied motions made pursuant to Rule 12(b)(6), Federal Rules of Civil Procedure to dismiss plaintiffs' claim under CERCLA, ruling in pertinent part:

(1) CERCLA's petroleum exclusion covers gasoline as well as its hazardous constituents: benzene, ethylbenzene, toluene and xylene, although said constituents are specifically listed as hazardous substances under CERCLA. This is because whether or not these constituents are fractions of petroleum, to interpret the petroleum exclusion otherwise would render the exclusion meaningless since it would result in no petroleum products coming under the petroleum exclusion.

(2) CERCLA's petroleum exclusion does not cover leaded gasoline because

(a) Lead is an additive to gasoline; it is not 'petroleum, including crude oil or any fraction thereof ...'

(b) Lead is specifically listed as a hazardous substance under CERCLA.

(c) There is no reason to treat lead differently when it is released as a part of gasoline from when it is released in any other form. *See*

United States v. Carolawn Co., 14 Env'tl.L.Rep. 20696 (D.S.C. June 15, 1984) (lead is a hazardous substance when released in water-based paint).

The district court subsequently reconsidered this ruling upon motion because of a memorandum dated July 31, 1987 from the General Counsel of the Environmental Protection Agency to the Assistant Administrator for Solid Waste and Emergency Response.*803 Based on this memorandum, the district court ruled on reconsideration that CERCLA's petroleum exclusion applies to leaded gasoline and dismissed plaintiffs' claim under CERCLA. FN3

FN3. The district court simultaneously dismissed plaintiffs' pendent claims for lack of subject matter jurisdiction, thereby resulting in dismissal of the action. The dismissal of the pendent claims is not at issue in this appeal.

Plaintiffs appeal. The issue presented in this appeal is whether the exclusion from the definition of "hazardous substances" in CERCLA for "petroleum, including crude oil and any fraction thereof not specifically listed as a hazardous substance" includes refined gasoline and all of its components and additives.

B. Request for Judicial Notice.

Rule 201(b)(2), Federal Rules of Evidence, allows the court to take judicial notice of a fact not subject to reasonable dispute because it is "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned."

It is undisputable that benzene, toluene, xylene, ethylbenzene and lead are hazardous substances, having been specifically listed or designated pursuant to several of the statutes set forth in Section 9601(14)(a)-(F).

We take judicial notice that benzene, toluene,

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313
(Cite as: 881 F.2d 801)

xylene, ethylbenzene and lead also are all indigenous components of crude oil. We also take judicial notice of the meaning of the words "fraction" and "petroleum." Thus, "fraction" is defined in Webster's Third New International Dictionary Unabridged (1981) to mean "one of several portions (as of a distillate or precipitate) separable by fractionation and consisting either of mixtures or pure chemical compounds." "Petroleum" is defined in relevant part as:

[A]n oily flammable bituminous liquid ... that is essentially a compound mixture of hydrocarbons of different types with small amounts of other substances (as oxygen compounds, sulfur compounds, nitrogen compounds, resinous and asphaltic components, and metallic compounds) ... and that is subjected to various refining processes (a fractional distillation, cracking, catalytic reforming, hydroforming, alkylation, polymerization) for producing useful products (as gasoline, naphtha, kerosene, fuel oils, lubricants, waxes, asphalt, coke, and chemicals)

....

C. Standard of Review.

[1] A dismissal for failure to state a claim pursuant to Rule 12(b)(6) is a ruling on a question of law and as such is reviewed *de novo*. *Emrich v. Touche Ross & Co.*, 846 F.2d 1190, 1198 (9th Cir.1988). Interpretation of a statute is a question of law also subject to *de novo* review. *Trustees of Amalgamated Insurance Fund v. Geltman Industries, Inc.*, 784 F.2d 926, 928 (9th Cir.), *cert. denied*, 479 U.S. 822, 107 S.Ct. 90, 93 L.Ed.2d 42 (1986); *United States v. Horowitz*, 756 F.2d 1400, 1403 (9th Cir.), *cert. denied*, 474 U.S. 822, 106 S.Ct. 74, 88 L.Ed.2d 60 (1985).

D. Statutory Interpretation.

[2] As noted, the definition of hazardous substance in Section 9601(14) contains an exclusion therefrom commonly referred to as the "petroleum exclusion." The petroleum exclusion provides that the term hazardous substance "does not include pet-

roleum, including crude oil or any fraction thereof which is not otherwise specifically listed or designated a hazardous substance under subparagraphs (A) through (F) of this paragraph...." Neither the term "petroleum" nor "fraction" are defined in CERCLA.

1. Plain Meaning.

The plain language of a statute is the starting point for its interpretation. *American Tobacco Co. v. Patterson*, 456 U.S. 63, 68, 102 S.Ct. 1534, 1537, 71 L.Ed.2d 748 (1982). "A fundamental canon of statutory construction is that, unless otherwise defined, words will be interpreted as taking their ordinary, contemporary, common *804 meaning." *Perrin v. United States*, 444 U.S. 37, 42, 100 S.Ct. 311, 314, 62 L.Ed.2d 199 (1979). However, "[d]eparture from a literal reading of statutory language may ... be indicated by relevant internal evidence of the statute itself and necessary in order to effect the legislative purpose." *Malat v. Riddell*, 383 U.S. 569, 571-72, 86 S.Ct. 1030, 1032, 16 L.Ed.2d 102 (1966). "If the intent of Congress is clear, that is the end of the matter; for the court ... must give effect to the unambiguously expressed intent of Congress." *Chevron, U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43, 104 S.Ct. 2778, 2781-82, 81 L.Ed.2d 694 (1984). Because "CERCLA is essentially a remedial statute designed by Congress to protect and preserve public health and the environment [, courts] are ... obligated to construe its provisions liberally to avoid frustration of the beneficial legislative purposes ... 'in the absence of a specific congressional intent otherwise.'" *Dedham Water Co. v. Cumberland Farms Dairy, Inc.*, 805 F.2d 1074, 1081 (1st Cir.1986) (citations omitted). However, "[t]his court must look beyond the express language of a statute where a literal interpretation 'would thwart the purpose of the over-all statutory scheme or lead to an absurd result.'" *Brooks v. Donovan*, 699 F.2d 1010, 1011 (9th Cir.1983) (citations omitted). And "[s]tatutes should not be construed to make surplusage of any provision." *Pettis ex rel. United States v. Morrison-Knudsen Co.*, 577 F.2d 668, 673 (9th

(Cite as: 881 F.2d 801)

Cir.1978).

Plaintiffs contend that the petroleum exclusion's plain and unambiguous terms compel the construction that it does not apply to petroleum, crude oil or any fraction thereof containing any of the components which have been designated as hazardous pursuant to any one of the acts listed in Section 9601(14)(A)-(F).

In our view, however, the application of the standards governing statutory construction to the words of the petroleum exclusion requires us to exclude gasoline, even leaded gasoline, from the term "hazardous substance" for purposes of CERCLA. Any other construction ignores the plain language of the statute and renders the petroleum exclusion a nullity.

[3] Plaintiffs rely upon the canon of statutory construction known as the "doctrine of the last antecedent." The doctrine of the last antecedent states that qualifying words, phrases and clauses must be applied to the words or phrases immediately preceding them and are not to be construed as extending to and including others more remote. *First Charter Financial Corp. v. United States*, 669 F.2d 1342, 1350 (9th Cir.1982); *United States v. Metate Asbestos Corp.*, 584 F.Supp. 1143, 1147 (D.Ariz.1984). Plaintiffs contend that in the application of this doctrine "the limiting words 'which is not otherwise specifically listed' plainly modify the preceding words of Section 9601(14): '[t]he term [hazardous substance] does not include petroleum, including crude oil or any fraction thereof' and creates an exception." [emphasis added]

We cannot agree with plaintiffs' application of the doctrine of the last antecedent. As we apply it, the doctrine compels the construction that "hazardous substance" does not include any fraction of crude oil which has been listed or designated as a hazardous substance under Section 9601(14)(A)-(F). The word immediately preceding the qualifying phrase is "fraction."^{FN4} Plaintiffs' proposed application extends*805 to more remote

words and is ungrammatical. Plaintiffs' application of the doctrine of last antecedent necessarily requires a plural verb in the qualifying phrase while the actual grammar sets forth a singular verb.

FN4. In line with this construction, defendants contend that gasoline is the only fraction of crude oil alleged in the complaint to have been released onto the property. The other substances, including benzene, are all alleged to have been additives to the gasoline. Therefore, defendants argue: "The plain language of the statute is clear that *only* when the particular *fraction* of crude oil is separately listed will it be considered a hazardous substance. Gasoline does not appear on any of the lists identified in subparagraphs (A) through (F) of section 9601(14) and therefore is not a hazardous substance." Plaintiffs contend in their reply brief that benzene itself is a fraction of petroleum. Benzene is defined as "a colorless volatile flammable toxic liquid hydrocarbon ... that is usually obtained commercially from the carbonization of coal ... or from certain petroleum fractions by catalytic dehydrogenation, and that is used chiefly in organic synthesis ..., as a solvent, and as a motor fuel (as for blending with gasoline)." Webster's Third New International Dictionary Unabridged (1981). Therefore, plaintiffs argue: "Whether the benzene is pure or blended with gasoline is not the issue.... If the exception to the petroleum exclusion is to be interpreted by its plain meaning, it must apply to any listed fraction." However, as judicially noted, benzene also is an indigenous component of crude oil.

In further support of their construction of the plain meaning of the petroleum exclusion, plaintiffs point out that lead, benzene, ethyl-benzene and toluene are hazardous substances covered by CERCLA if released as part of chemical wastes, *United*

States v. Conservation Chemical Co., 619 F.Supp. 162, 182–83 (W.D.Mo.1985), that ethyl-benzene and xylene are hazardous substances when constituents of coal tar, *United States v. Union Gas Co.*, 586 F.Supp. 1522, 1523 (E.D.Pa.1984), and that lead is a hazardous substance when it is a component of water-based paint, *United States v. Carolawn Co.*, 21 E.R.C. 2124, 2125–26 (D.S.C.1984). Plaintiffs argue therefrom: “[That] those same specifically listed substances would not be considered hazardous if released as a result of leaking underground gasoline storage tanks ... cannot be what Congress intended. Such an interpretation would render meaningless the exception to the petroleum exclusion.”

However, there are no exclusions in CERCLA similar to the petroleum exclusion for chemical wastes, coal tar and water-based paints. Consequently, plaintiffs' reliance on these cases to support their construction is misplaced.

Moreover, because all of the substances complained of herein and designated as hazardous pursuant to other statutes are indigenous to crude oil, *see* discussion *supra*, the construction advocated by plaintiffs would have the effect of rendering the petroleum exclusion a nullity because all crude oil, petroleum and petroleum fractions, unrefined or refined, would fall outside its ambit. While plaintiffs contend that their construction of the plain meaning of the petroleum exclusion would still leave some substances within its scope, *e.g.*, unrefined oil and other petroleum products that do not contain constituents added or created during the refining process, the distinction between those substances which are added to a petroleum product and those substances which may be indigenous to petroleum is nonsensical because all of the substances plaintiffs allege were additives to the gasoline also exist as indigenous components of crude oil.^{FN5}

FN5. The United States argues that if the term petroleum in the exclusion does not include any standard industry additives to gasoline, almost every petroleum spill or

leak would be redressible under CERCLA, a circumstance which would vastly broaden the potential exposure of the limited CERCLA funds. However, if the petroleum exclusion is interpreted to remove from CERCLA coverage not only “unadulterated petroleum fractions but also those which have been contaminated during use,” the EPA's cleanup authority would be severely hampered and the agency would be effectively prevented from addressing many contaminated sites. Thus, the United States urges the court to interpret the petroleum exclusion as limited to releases of crude oil and refined petroleum and petroleum fractions. In our opinion, the statutory construction and the concern expressed by the United States relative to “unadulterated petroleum fractions [and] those which have been contaminated during use” is not necessary to the resolution of this appeal.

2. Legislative History.

Although our conclusion regarding the plain meaning of the scope of the petroleum exclusion makes unnecessary resort to the next step in statutory construction, legislative history, *Blum v. Stenson*, 465 U.S. 886, 896, 104 S.Ct. 1541, 1547, 79 L.Ed.2d 891 (1984), we are persuaded that the legislative history supports our plain meaning construction.

There is virtually no legislative history contemporaneous with the enactment of CERCLA directly relevant to the scope of the petroleum exclusion. This dearth is probably because CERCLA was enacted as a compromise among three competing bills, H.R. 7020, H.R. 85, and S. 1480, after very limited debate under a suspension of the *806 rules. *See Dedham Water Co.*, *supra*, 805 F.2d at 1080; *United States v. Mottolo*, 605 F.Supp. 898, 902–05 (D.N.H.1985); Grad, “A Legislative History of the Comprehensive Environmental Response, Compensation and Liability (“Superfund”) Act of

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 *Envtl. L. Rep.* 21,313

(Cite as: 881 F.2d 801)

1980,” 8 *Colum.J.Envntl.L.* 1–2 (1982).^{FN6} Of these three bills, only H.R. 85 addressed oil spills. H.R. 85 was reported to the Senate but no further action was taken on it. Grad, *supra* at 4.

FN6. H.R. 7020, 96th Cong., 2d Sess. (1980) (“Hazardous Waste Containment Act”); H.R. 85, 96th Cong., 1st Sess. (1979) (“Oil Pollution Liability and Compensation Act”); S. 1480, 96th Cong., 1st Sess. (1979) (“Environmental Emergency Response Act”).

In arguing that the legislative history of CERCLA supports their position that gasoline and its additives and constituents when refined are not included within the petroleum exclusion, plaintiffs quote from the Report of the Senate Committee on Environment and Public Works accompanying S. 1480 that “[t]he reported bill does not cover spills or other releases strictly of oil.” *I Superfund: A Legislative History*, Environmental Law Institute, Washington, D.C. (1982), 12–13, quoting from S.Rep. No. 96–848, 96th Cong., 2d Sess., July 11, 1980, 1980 U.S.Code Cong. & Admin.News 6119. This argument is disingenuous. The plain meaning and common use of “oil” includes not just crude oil but its various refined fractions. Moreover, one of the definitions for “oil” is “petroleum.” *See Webster’s Third New International Dictionary Unabridged* (1981).

That Congress had before it the statutory definition of hazardous substances and a list of the substances which had been designated as hazardous under other federal laws when CERCLA was enacted is contended by plaintiffs to mean that the phrase “not otherwise specifically listed or designated as a hazardous substance” in the petroleum exclusion “was not considered blindly without a referent” and that “the statute including the petroleum exclusion was passed with the substances about which plaintiffs complain specifically listed and, therefore, excepted from the definition.” In addition, plaintiffs contend: “A review of the legislative history shows that each time the term

‘hazardous substance’ was defined, Congress used the same words. The definition, including the final sentence—the petroleum exclusion—and its exception—remained unchanged.”

In our opinion, these arguments do not constitute an indication from the legislative history that Congress intended that the petroleum exclusion not encompass petroleum which contains any designated hazardous substances.

The contemporaneous legislative history concerning the scope of the petroleum exclusion being so sparse, we next examine congressional action when Congress was presented with opportunities to amend CERCLA.

Specifically, we refer to H.R. 1881, 99th Cong., 1st Sess. (1985). Defendants, citing [15 *Current Developments*] *Env’t Rep. (BNA)* 2191 (April 12, 1985), assert that Section 1(b) of H.R. 1881, introduced by Congressman Downey but never progressing beyond its introduction, would have amended CERCLA as follows:

The provisions of [CERCLA] ... shall apply to petroleum, including crude oil or any fraction or component or derivative thereof, in the same manner and to the same extent as such provisions apply to any hazardous substance referred to in paragraph (14) [42 U.S.C. Section 9601(14)], but only if such petroleum (or fraction, component or derivative thereof) is otherwise specifically listed or designated as a hazardous substance under [the subparagraphs of 42 U.S.C. Section 9601(14)]....

In addition, reference is made to the Hazardous and Solid Waste Amendments of 1984, Pub.L. No. 98–616, 98 Stat. 3221. Section 601(a) of the Amendments added Subtitle I, §§ 9001–9010, to the Solid Waste Disposal Act of 1965 (“SWDA” or “RCRA”) pertaining to the regulation of underground storage tanks. *See* 42 U.S.C. §§ 6991–6991i as amended by the Superfund Amendments and Reauthorization Act of 1986 (“SARA”), *807 Pub.L. No. 99–499, 100 Stat. 1613.^{FN7} An under-

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313
(Cite as: 881 F.2d 801)

ground storage tank is defined in Section 9001 as "any one or combination of tanks (including underground pipes connected thereto) which is used to contain an accumulation of regulated substances ..." with certain exceptions not pertinent here. Section 9001(2) defines "regulated substance" as:

FN7. The Solid Waste Disposal Act is also known as the Resource Conservation and Recovery Act of 1976 or "RCRA." According to *Grad, supra* at p. 2 n. 9, RCRA came into being as an amendment to the Solid Waste Disposal Act of 1965.

(A) Any substance defined in Section 101(14) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (but not including any substance regulated as a hazardous waste under Subtitle C), and

(B) Petroleum, including crude oil or any fraction thereof which is liquid at standard conditions of temperature and pressure (60 degrees Fahrenheit and 14.7 pounds per square inch absolute).

Senator Durenberger introduced the 1984 Amendment, stating as follows:

Underground storage tanks are seldom regulated. At present, Federal regulation of storage tanks covers only above-ground tanks containing chemical wastes. And, if a tank is leaking, the Federal Government cannot under Superfund authority respond or clean up a spill if it involves petroleum products.

The tank storage of one of the most common underground contaminants—gasoline—is unregulated because it is not a waste product (and thus not under the authority of the Resource Conservation and Recovery Act), and spills of the fuel cannot be cleaned up under the Superfund law because it is a petroleum product.

130 Cong.Rec. S2028, S2080 (daily ed. Feb. 29, 1984). Finally, in 1986, Congress, in Section 205 of the Superfund Amendments and Reauthoriz-

ation Act of 1986 ("SARA"), Pub.L. 99-499, 100 Stat. 1613, further amended Subtitle I of the Solid Waste Disposal Act by adding Section 9003(h), 42 U.S.C. § 6991b(h), to establish a separate response program for petroleum leaking from underground storage tanks, the response program being funded by a Leaking Underground Storage Tank Trust Fund financed by taxes on motor fuels. The Conference Report accompanying SARA, H.R.Rep. No. 962, 99th Cong., 2d Sess. 183, 263 (1986), *reprinted in* 1986 U.S.Code Cong. & Admin.News 2835, 3276, 3356 adopted the House provision for the definition of petroleum for purposes of Section 9003(c), the Senate Amendment containing no provision:

The response program established by this subsection is available only for tanks containing petroleum substances. The House amendment contains an explicit definition of the term petroleum. The definition is a restatement of the meaning of the term as established by current law in Section 9001(2) of the Solid Waste Disposal Act. The new definition does not add or remove from regulation any substance or underground tank subject to current law.

Representative Stangeland stated in the House debate on SARA:

Another bold initiative included in the bill is an expanded program for cleanup of leaking underground storage tanks. The 1984 amendments to the Solid Waste Disposal Act authorized a regulatory program to address the problem of leaking underground storage tanks, including petroleum tanks which are not covered by Superfund. Under the amendments included in the conference report, the existing regulatory program is expanded upon to authorize EPA to require the owner of underground petroleum tank to undertake cleanup if the tank should fail or allow EPA to undertake the work if the tank owner can't or won't clean up the leak.

132 Cong.Rec. H9572 (daily ed. Oct. 8, 1986). SARA left unchanged the petroleum exclusion set

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313
(Cite as: 881 F.2d 801)

forth in 42 U.S.C. § 9601(14). SARA did amend CERCLA by adding to CERCLA in Section 101(33), 42 U.S.C. § 9601(33), a definition of the term "pollutant or contaminant." This definition *808 contains a petroleum exclusion identical to the exclusion in Section 9601(14). During debate on SARA in the Senate, Senator Simpson stated in pertinent part:

This bill will not diminish the scope of the present petroleum exclusion. That provision, found in section 101(14) of the Act excludes from the definition of 'hazardous substances' all types of petroleum, including crude oil, crude oil tank bottoms, refined fractions of crude oil, and tank bottoms of such which are not specifically listed or designated as a hazardous substance under the other subparagraphs of that provision.

132 Cong.Rec. S14932 (daily ed. Oct. 3, 1986).

The rejection of H.R. 1881 in 1985 and the failure to amend the petroleum exclusion when CERCLA was amended by SARA in 1986 even though the EPA had already clarified its interpretation of the exclusion to cover gasoline and other refined products and their components and additives, *see discussion infra*, are asserted by defendants to constitute persuasive evidence that their interpretation of the petroleum exclusion is the one intended by Congress in 1980.

Although defendants' characterization of these two legislative events as "persuasive evidence" is too strong under the circumstances, these subsequent events are entitled to some weight:

Although postenactment developments cannot be accorded 'the weight of contemporary legislative history, we would be remiss if we ignored these authoritative expressions concerning the scope and purpose of Title IX....'

... Where 'an agency's statutory construction has been "fully brought to the attention of the public and the Congress," and the latter has not sought to alter the interpretation although it has amended

the statute in other respects, then presumably the legislative intent has been correctly discerned.'

North Haven Bd. of Educ. v. Bell, 456 U.S. 512, 535, 102 S.Ct. 1912, 1925, 72 L.Ed.2d 299 (1982) (citations omitted). *See also NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 274-75, 94 S.Ct. 1757, 1761-62, 40 L.Ed.2d 134 (1974). Because, however, the United States concedes that it is not clear that Congress was specifically aware of the EPA's prior interpretations of the petroleum exclusion in 1986, the failure of Congress to object to the EPA's interpretation is entitled to only modest weight. *National Wildlife Federation v. Gorsuch*, 693 F.2d 156, 167 and n. 33 (D.C.Cir.1982). Nonetheless, these postenactment developments lend credence to our plain meaning construction.

In any event, the more compelling indications of Congress's intent in 1980 concerning the scope of the petroleum exclusion are the amendments to the SWDA in 1984 and the amendments in 1986 to the SWDA and CERCLA enacted by SARA. While "it is well settled that 'the views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one[.]'" *Russello v. United States*, 464 U.S. 16, 26, 104 S.Ct. 296, 302, 78 L.Ed.2d 17 (1983), the very specificity of these amendments to cover leaking gasoline, when conjoined with the unchanged wording of the petroleum exclusion, cannot be disregarded in fathoming legislative intent in 1980.

3. Agency Interpretation.

After looking to the legislative history, courts also look to the interpretation given to a statute by its administering agency as an aid in interpreting Congress's intent. *Brock v. Writers Guild of America, West, Inc.*, 762 F.2d 1349, 1353 (9th Cir.1985). Although unnecessary to our opinion, the EPA's interpretation of the scope of the petroleum exclusion is entirely consistent with its plain meaning and legislative history and constitutes highly persuasive evidence that our interpretation is correct. ^{FN8}

FN8. The relevant documents include three

(Cite as: 881 F.2d 801)

memoranda issued to subordinates by the General Counsel of the EPA and respectively dated December 2, 1982, August 12, 1983, and July 31, 1987. Also relevant are EPA pronouncements at 46 *Fed.Reg.* 22145 (April 15, 1981), at 50 *Fed.Reg.* 13460 (April 4, 1985), and at 51 *Fed.Reg.* 8106 (March 10, 1986).

*809 As stated in *Chevron, U.S.A., supra*, 467 U.S. at 843-845, 104 S.Ct. at 2781-2783:

'The power of an administrative agency to administer a congressionally created ... program necessarily requires the formulation of policy and the making of rules to fill any gap left, implicitly or explicitly, by Congress.' ... If Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation. Such legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute. Sometimes the legislative delegation to an agency on a particular question is implicit rather than explicit. In such a case, a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency.

We have long recognized that considerable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer, and the principle of deference to administrative interpretations 'has been consistently followed by this Court whenever decision as to the meaning or reach of a statute has involved reconciling conflicting policies, and a full understanding of the force of the statutory policy in the given situation has depended upon more than ordinary knowledge respecting the matters subjected to agency regulations....

'... If this choice represents a reasonable accommodation of conflicting policies that were committed to the agency's care by the statute, we

should not disturb it unless it appears from the statute or its legislative history that the accommodation is not one that Congress would have sanctioned.' *United States v. Shimer*, 367 U.S. 374, 382, 383 [81 S.Ct. 1554, 1560, 1561, 6 L.Ed.2d 908] (1961).

" 'Particularly is this respect due when the administrative practice at stake "involves a contemporaneous construction of a statute by the men charged with the responsibility of setting its machinery in motion, of making the parts work efficiently and smoothly while they are yet untried and new." ' " *Udall v. Tallman*, 380 U.S. 1, 16, 85 S.Ct. 792, 801, 13 L.Ed.2d 616 (1965), quoting *Power Reactor Co. v. International Union of Electricians*, 367 U.S. 396, 408, 81 S.Ct. 1529, 1535, 6 L.Ed.2d 924 (1961). As further explained in *Process Gas Consumers Group v. United States*, 694 F.2d 778, 791 (D.C.Cir.1982) (en banc), cert. denied sub nom. *Louisiana v. Federal Energy Regulatory Comm'n*, 461 U.S. 905, 103 S.Ct. 1874, 76 L.Ed.2d 807 (1983) (footnotes omitted):

The extent to which courts should defer to agency interpretations of law is ultimately 'a function of Congress' intent on the subject as revealed in the particular statutory scheme at issue.' Thus, when Congress delegates full responsibility to an agency to implement a statute, but provides little guidance on how the governing statute should be interpreted, common sense suggests that Congress would wish courts to consider agency views on questions of law that are 'closely related ... to the everyday administration of the statute and to the agency's administrative or substantive expertise.'

Courts also consider the thoroughness of the agency's consideration, the validity of its reasoning, and the consistency of its position over time. *General Electric Co. v. Gilbert*, 429 U.S. 125, 141-42, 97 S.Ct. 401, 410-11, 50 L.Ed.2d 343 (1976); *Skidmore v. Swift & Co.*, 323 U.S. 134, 140, 65 S.Ct. 161, 164, 89 L.Ed. 124 (1944).

The United States argues that by implication

the EPA is empowered to render conclusive decisions on what should or should not be considered a hazardous substance under CERCLA. In support thereof the United States notes that it is clear that Congress intended the EPA to have substantial discretion in administering CERCLA generally and refers the court to 42 U.S.C. § 9602(a):

(a) The Administrator shall promulgate and revise as may be appropriate, regulations designating as hazardous substances, in addition to those referred to in section 9601(14) of this title, such elements,*810 compounds, mixtures, solutions, and substances which, when released into the environment may present substantial danger to the public health or welfare or the environment, and shall promulgate regulations establishing that quantity of any hazardous substance the release of which shall be reported pursuant to section 9603 of this title. The Administrator may determine that one single quantity shall be the reportable quantity for any hazardous substance, regardless of the medium into which the hazardous substance is released.

Plaintiffs argue that the court should not accord this deference to the memoranda issued by the EPA concerning the scope of the petroleum exclusion. Plaintiffs cite *United States v. Pennsylvania Indus. Chem. Corp.*, 411 U.S. 655, 93 S.Ct. 1804, 36 L.Ed.2d 567 (1973) and *Independent Bankers Ass'n v. Smith*, 534 F.2d 921 (D.C.Cir.), cert. denied sub nom. *Bloom v. Independent Bankers Ass'n*, 429 U.S. 862, 97 S.Ct. 166, 50 L.Ed.2d 141 (1976) as authority that the EPA's memoranda are not binding on the court. Neither of these decisions, however, provide support for the contention that the court may disregard the EPA memoranda because of either the purpose underlying their issuance or the informality of their issuance.

Noting that a party's right to advance "a private cause of action for damages under CERCLA is not dependent upon a previous governmentally authorized cleanup program, *Wickland Oil Terminals v. Asarco, Inc.*, 792 F.2d 887, 891-92 (9th Cir.1986),

plaintiffs further argue that no deference is due these memoranda in an action between private parties because the memoranda are issued informally to guide and assist the EPA in setting priorities for the implementation of CERCLA and the allocation of its resources.

However, the memoranda, while expressing concerns about allocation of resources, are not couched solely in those terms. Moreover, while a decision by the EPA to authorize under CERCLA a program for the cleanup of gasoline spills is not a prerequisite to this action, the EPA's opinion whether such spills are encompassed within CERCLA's statutory provisions is extremely relevant. Plaintiffs' apparent suggestion that the petroleum exclusion be interpreted differently by the court and the EPA depending upon whether the action is private or public does not make sense in the absence of clearly expressed language in the statute or legislative history. See *Skidmore, supra*, 323 U.S. at 140, 65 S.Ct. at 164 ("Good administration of the Act and good judicial administration alike require that the standards of public enforcement and those for determining private rights shall be at variance only when justified by very good reasons.")

We conclude that the EPA's interpretation of the scope of the petroleum exclusion should be accorded considerable deference, especially because of the virtual absence of contemporaneous legislative history. While the EPA's opinions are not exactly contemporaneous with the enactment of the petroleum exclusion, its consideration has been very thorough and consistent over time.

E. Conclusion.

We rule that the petroleum exclusion in CERCLA does apply to unrefined and refined gasoline even though certain of its indigenous components and certain additives during the refining process have themselves been designated as hazardous substances within the meaning of CERCLA.

AFFIRMED.

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313
(Cite as: 881 F.2d 801)

REINHARDT, Circuit Judge, specially concurring:

I concur in the court's opinion. I agree with the substance of the court's treatment of CERCLA'S legislative history and the interpretation accorded that statute by the EPA, and write separately only to emphasize that we need not go beyond the language of the statute itself in order to reach our result. In my view, the language of CERCLA'S "petroleum exclusion," contained in 42 U.S.C. § 9601(14), plainly applies to gasoline, even when, as here, that gasoline contains lead additives. The court *811 correctly examines the "plain language" of the statute, *ante* at 803–805, and applies the elementary rule that we give the words of a statute their "ordinary, contemporary, common meaning," unless doing so produces an absurd result, or one clearly contrary to the expressed intention of the statute's drafters. *Perrin v. United States*, 444 U.S. 37, 42, 100 S.Ct. 311, 314, 62 L.Ed.2d 199 (1979); *see also Pierce v. Underwood*, 487 U.S. 552, 108 S.Ct. 2541, 2547, 101 L.Ed.2d 490 (1988) (courts "turn first to the language and structure" of the relevant statute). In my view, the language of § 9601(14)'s petroleum exclusion flatly applies to gasoline, even if that gasoline may also contain a "hazardous substance" within the meaning of CERCLA (in this case, lead). To hold otherwise, as Wilshire Westwood seeks to have us do, would require us to construe the words Congress chose in something other than their ordinary meaning. Inasmuch as Wilshire Westwood has failed to offer any persuasive justification for doing so—either in the legislative history of the section or in the general policies served by CERCLA—the court rightly refuses to depart from the ordinary construction of the statute's words.

O'SCANNLAIN, Circuit Judge, concurs fully in the opinion authored for the court by Judge COYLE and also concurs in the special concurrence of Judge REINHARDT.

C.A.9 (Cal.), 1989.

Wilshire Westwood Associates v. Atlantic Richfield Corp.

881 F.2d 801, 30 ERC 1065, 58 USLW 2123, 19 Env'tl. L. Rep. 21,313

END OF DOCUMENT



VARETTA WOODS, Plaintiff and Appellant,
 v.
 WILLIAM YOUNG et al., Defendants and Re-
 spondents.

No. S005969.

Supreme Court of California
 Apr 4, 1991.

SUMMARY

In a medical malpractice action against doctors and a medical center, the trial court granted defendants summary judgment on the ground the complaint was barred by the statute of limitations. Plaintiff had filed her notice of intent to sue pursuant to Code Civ. Proc., § 364, subd. (a), more than ninety days prior to the running of the one-year statute of limitations for actions based on professional negligence of health care provider (Code Civ. Proc., § 340.5), but did not file her complaint until one year and three weeks after the commission of the alleged negligent act. Prior to plaintiff's filing of her action, several appellate court decisions held that Code Civ. Proc., § 364, subd. (d) (which provides that if the notice is served within 90 days of the running of the statute of limitations, the time for commencement of the action is extended for 90 days from the date of service), extends the statute of limitations by 90 days for all plaintiffs. (Superior Court of Los Angeles County, No. C510740, Jerry K. Fields, Judge.) The Court of Appeal, Second Dist., Div. Three, No. B026333, reversed.

The Supreme Court affirmed the judgment of the Court of Appeal. It held that the serving of the notice of intent to sue pursuant to Code Civ. Proc., § 364, subd. (a), tolls the one-year statute of limitations only when the plaintiff gives the notice of intent to sue in the last ninety days of the limitations period, but that the running of the statutory period is not otherwise affected by the service of the notice. It also held that considerations of fairness and

public policy required application of the decision be prospective only, and accordingly held that the rule did not apply to plaintiff bringing the appeal or to plaintiffs filing complaints no later than 90 days after the finality of the decision. (Opinion by Kennard, J., with Lucas, C. J., Panelli, Arabian, Baxter, JJ., and Kremer (Daniel J.), J., ^{FN*} concurring. Separate concurring opinions by Mosk and Baxter, JJ.)

FN* Presiding Justice of the Court of Appeal, Fourth Appellate District, Division One, assigned by the Chairperson of the Judicial Council.

HEADNOTES

Classified to California Digest of Official Reports
 (1) Healing Arts and Institutions § 30--Physicians, Surgeons, and Other Medical Practitioners--Duties and Liabilities--Medical Injury Compensation Reform Act--Purpose.

In enacting the Medical Injury Compensation Reform Act (MICRA), the Legislature attempted to reduce the cost and increase the efficiency of medical malpractice litigation by revising a number of legal rules applicable to such litigation.

(2) Healing Arts and Institutions § 47.6--Physicians, Surgeons, and Other Medical Practitioners--Duties and Liabilities--Actions--Notice of Intention to Commence Suit; Certificate of Merit--Purpose of Requirement.

Code Civ. Proc., § 364, subd. (a), requires that, before filing a medical malpractice action, a plaintiff give the defendant at least 90 days' notice of intent to sue. The purpose of this 90-day waiting period is to decrease the number of medical malpractice actions filed by establishing a procedure that encourages the parties to negotiate outside the structure and atmosphere of the formal litigation process.

(3) Statutes §
 29--Construction--Language--Legislative Intent.

In construing statutes, courts must determine and effectuate legislative intent. To ascertain intent, the court looks first to the words of the statutes. Words must be construed in context, and statutes must be harmonized, both internally and with each other, to the extent possible. Interpretations that lead to absurd results or render words surplusage are to be avoided.

(4a, 4b, 4c, 4d) Healing Arts and Institutions § 47--Physicians, Surgeons, and Other Medical Practitioners--Duties and Liabilities--Actions-- Statute of Limitations--Tolling--Notice of Action.

Code Civ. Proc., § 364, subd. (a), requires that, before filing a medical malpractice action, a plaintiff give the defendant at least 90 days' notice of intent to sue. Code Civ. Proc., § 364, subd. (d), provides that if this notice is served within 90 days of the statute of limitations, the time for commencement of the action is extended by 90 days from the date of service. Reading both provisions together, only when a plaintiff serves the notice in the last 90 days of the 1-year period of limitations in medical malpractice cases (Code Civ. Proc., § 340.5), is that statute of limitations tolled for 90 days. The running of the statutory period is not otherwise affected by the service of the notice. This interpretation best effectuates the legislative intent of § 364, subd. (a), which is to avoid litigation by attempting to settle matters by methods other than litigation. The tolling provision of Code Civ. Proc., § 356 (commencement of action stayed by statutory prohibition), does not apply to medical malpractice plaintiffs. (Disapproving to the extent inconsistent: *Grimm v. Thayer* (1987) 188 Cal.App.3d 866; 871 [233 Cal.Rptr. 687]; *Paxton v. Chapman General Hospital, Inc.* (1986) 186 Cal.App.3d 110 [230 Cal.Rptr. 355]; *Gilbertson v. Osman* (1986) 185 Cal.App.3d 308 [229 Cal.Rptr. 627]; *Hilburger v. Madsen* (1986) 177 Cal.App.3d 45 [222 Cal.Rptr. 713]; *Banfield v. Sierra View Local Dist. Hospital* (1981) 124 Cal.App.3d 444 [177 Cal.Rptr. 290]; *Braham v. Sorenson* (1981) 119 Cal.App.3d 367 [174 Cal.Rptr. 39]; and *Gomez v. Valley View Sanitorium* (1978) 87 Cal.App.3d 507 [151 Cal.Rptr.

97].)

[See **Cal.Jur.3d**, Healing Arts and Institutions § 179; 3 **Witkin**, Cal. Procedure (3d ed. 1985) Actions, §§ 165, 501; 6 **Witkin**, Summary of Cal. Law (9th ed. 1988) Torts, § 786.]

(5) Statutes § 45--Construction--Presumptions--Assumption That Every Provision Is Meaningful.

Every provision of a statute is assumed to have meaning and to perform a useful function.

(6) Statutes § 52--Construction--Codes--Conflicting Provisions--General and Specific Provisions.

A specific provision relating to a particular subject will govern a general provision, even though the general provision standing alone would be broad enough to include the subject to which the specific provision relates.

(7) Constitutional Law § 83--Equal Protection--Classification--Judicial Review--Standard--Personal Injury Plaintiffs.

In determining whether legislation violates equal protection principles, the "rational basis" standard, rather than the "compelling state interest" test, applies to legislative classifications among personal injury plaintiffs.

(8a, 8b, 8c) Courts § 35--Decisions and Orders--Judicial Discretion-- Prospective Application--Litigant's Reliance on Prior Appellate Court Holdings:Healing Arts and Institutions § 47--Physicians, Surgeons, and Other Medical Practitioners--Duties and Liabilities--Statute of Limitations--Notice of Action--Prospective Application of Tolling Rule.

In fairness to the plaintiffs who relied on several Court of Appeal rulings concerning the effect of the 90-day notice requirements for medical malpractice actions (Code Civ. Proc., § 364, subd. (a)) on the statute of limitations, the decision establishing the rule that only when a plaintiff serves the notice of intent to sue in the last 90 days of the 1-year period of limitations (Code Civ. Proc., § 340.5) is that statute of limitations tolled for 90 days, did not apply to the plaintiff whose appeal led to the decision or to plaintiffs filing complaints no later than

90 days after the finality of the decision.

(9) Courts § 36--Prospective and Retroactive Decisions--Judicial Discretion--Factors Considered.

Unlike statutory enactments, judicial decisions, particularly those in tort cases, are generally applied retroactively. But considerations of fairness and public policy may require that a decision be given only prospective application. Particular considerations relevant to the retroactivity determination include the reasonableness of the parties' reliance on the former rule, the nature of the change as substantive or procedural, retroactivity's effect on the administration of justice, and the purposes to be served by the new rule.

(10) Courts § 34--Prospective and Retroactive Decisions--Procedural Changes.

Retroactive application of an unforeseeable procedural change is disfavored when such application would deprive a litigant of any remedy whatsoever.

COUNSEL

Robert Wasserwald and William J. Cleary, Jr., for Plaintiff and Appellant.

Ian Herzog, Leonard Sacks, Robert Steinberg, Bruce Broillet, Evan Marshall, Richard D. Aldrich, Harvey R. Levine, Douglas DeVries, Robert E. Cartwright, Guy Saperstein, Gary Gwilliam, Sanford Gage and Roland Wrinkle as Amici Curiae on behalf of Plaintiff and Appellant.

Kirtland & Packard, Harold J. Hunter, Jr., Donna P. McCray, Herzfeld & Rubin, Michael A. Zuk, Roy D. Goldstein, Seymour W. Croft, Shield & Smith, Richard B. Castle and Douglas Fee for Defendants and Respondents.

Hassard, Bonnington, Rogers & Huber, David E. Willett, Musick, Peeler & Garrett, James F. Ludlam, Charles E. Forbes, Horvitz, Levy & Amerian, *319 S. Thomas Todd and Frederic D. Cohen as Amici Curiae on behalf of Defendants and Respondents.

KENNARD, J.

In 1975, the Legislature enacted the Medical Injury Compensation Reform Act (MICRA) in response to a health care crisis caused by a rapid increase in premiums for medical malpractice insurance. Among MICRA's many provisions is one that requires a plaintiff, before filing an action based on a health care provider's professional negligence, to give the defendant at least 90 days' notice of intent to sue.

The issue in this case is whether the 90-day notice provision tolls or extends the 1-year statute of limitations for medical malpractice actions,^{FN1} and, if so, under what circumstances.

FN1 Code of Civil Procedure section 340.5 provides for a limitations period in medical malpractice cases of three years after the injury or one year after the plaintiff's discovery of the injury, whichever occurs first. The three-year limitations period is not in issue here.

Two different views have developed in the Courts of Appeal that have addressed this issue. All of the decisions have concluded that the statute of limitations is tolled for 90 days regardless of when during the limitations period the plaintiff gives the requisite notice of intent to sue. Some, however, have held that when the notice is given in the last 90 days of the limitations period, the overall time for bringing the action is extended for a period ranging from 90 to 180 days.

We conclude that neither line of authority effectuates the legislative intent underlying MICRA's statutory scheme. We hold that the 1-year statute of limitations is tolled for 90 days when the plaintiff gives the notice of intent to sue in the last 90 days of the limitations period, but that the running of the statutory period is not otherwise affected by service of the notice. We further hold that considerations of fairness and public policy require prospective application of our decision.

I

(1) In enacting MICRA in 1975, the Legislature “attempted to reduce the cost and increase the efficiency of medical malpractice litigation by revising a number of legal rules applicable to such litigation.” (*American Bank & Trust Co. v. Community Hospital* (1984) 36 Cal.3d 359, 363-364 *320 [204 Cal.Rptr. 671, 683 P.2d 670, 41 A.L.R.4th 233].) The MICRA revision added to the Code of Civil Procedure three provisions that are relevant to a resolution of the issue presented here: Code of Civil Procedure section 364, subdivisions (a) and (d), and section 365.^{FN2} (All further statutory references are to the Code of Civil Procedure.)

FN2 Section 364, subdivision (a) provides: “No action based upon the health care provider’s professional negligence may be commenced unless the defendant has been given at least 90 days’ prior notice of the intention to commence the action.”

Section 364, subdivision (d) states: “If the notice is served within 90 days of the expiration of the applicable statute of limitations, the time for the commencement of the action shall be extended 90 days from the service of the notice.”

Section 365 reads: “Failure to comply with this chapter shall not invalidate any proceedings of any court of this state, nor shall it affect the jurisdiction of the court to render a judgment therein. However, failure to comply with such provisions by any attorney at law shall be grounds for professional discipline and the State Bar of California shall investigate and take appropriate action in any such cases brought to its attention.”

(2) Section 364, subdivision (a) (hereafter section 364(a)) requires that, before filing a medical malpractice action, a plaintiff give the defendant at least 90 days’ notice of intent to sue. The purpose of

this 90-day waiting period is to decrease the number of medical malpractice actions filed by establishing a procedure that encourages the parties to negotiate “outside the structure and atmosphere of the formal litigation process.” (*Jenkins & Schweinfurth, California’s Medical Injury Compensation Reform Act: An Equal Protection Challenge* (1979) 52 So.Cal.L.Rev. 829, 963, fn. omitted; see *Grimm v. Thayer* (1987) 188 Cal.App.3d 866, 871 [233 Cal.Rptr. 687]; *Gilbertson v. Osman* (1986) 185 Cal.App.3d 308, 317 [229 Cal.Rptr. 627].)

Section 365 states that a plaintiff’s failure to give the 90-day notice required by section 364(a) “shall not invalidate any proceedings of any court of this state, nor shall it affect the jurisdiction of the court to render a judgment therein.” It also provides, however, that an attorney who fails to comply with the notice requirement may be subject to disciplinary proceedings by the State Bar of California.

Unless the giving of the 90-day notice tolls or extends the statute of limitations, sections 364(a) and 365 pose a dilemma for the plaintiff’s attorney who serves the notice within the last 90 days of the 1-year limitations period. In that situation, the attorney must either comply with section 364(a)’s proscription against commencing the action during that statute’s 90-day waiting period, thereby forfeiting the client’s cause of action, or the attorney must file the lawsuit during the statutory 90-day waiting period, thereby “triggering” section 365’s provision of possible disciplinary action by the State Bar. In the absence of tolling or extension, a plaintiff’s attorney wishing to protect the client’s rights without risking disciplinary *321 proceedings would have to serve the 90-day notice within 9 months of the plaintiff’s discovery of the injury. This would, in effect, shorten the statutory limitations period from one year to nine months.

The Legislature attempted to resolve this problem through section 364, subdivision (d) (hereafter section 364(d)). That provision states that if section 364(a)’s 90-day notice of intent to sue is served dur-

ing the last 90 days of the statute of limitations, the limitations period is "extended 90 days from service of the notice." This additional time could give the plaintiff more, but never less, than the statutory one-year period in which to bring the lawsuit. Thus, section 364(d) reflects the Legislature's intent to allow a medical malpractice plaintiff at least a year in which to file the action.

A literal application of section 364(d), however, leads to incongruous results, as this example shows: A plaintiff serves the 90-day notice of intent to sue required by section 364(a) 50 days before expiration of the 1-year statute of limitations. Because section 364(d) would in that case extend the 1-year limitations period by 90 days, calculated from the date of service of the 90-day notice, the plaintiff has 1 year and 40 days in which to file the action.

If our hypothetical plaintiff were to file suit on the last day of the extension, the plaintiff would violate the 90-day waiting requirement of section 364(a), which requires the plaintiff to give the defendant health care provider *at least* 90 days' prior notice of intent to sue. If, however, the plaintiff were to file the action one day after the extended period, that is, one year and forty-one days after discovery of the injury, the action would be barred by the one-year statute of limitations because it was filed one day beyond the limitations period as extended.

Thus, when applied literally, section 364(d) accomplishes nothing. This is the problem that has confronted the Courts of Appeal in their efforts to resolve the dilemma that sections 364(a) and 365 present to a plaintiff's attorney who serves the 90-day notice of intent to sue in the last 90 days of the 1-year limitations period.

II

All of the Courts of Appeal that have attempted to resolve the difficulties presented by the MICRA provisions discussed above have resorted to the non-MICRA tolling provision of section 356. That

provision states that when "the commencement of an action is stayed by ... statutory prohibition," the time of the statutory prohibition "is not part of the time limited for the commencement of the action." The Courts of Appeal have *322 concluded that section 364(a)'s 90-day waiting period is a "statutory prohibition" within the meaning of section 356, thus resulting in a 90-day tolling of the 1-year limitations period regardless of when the notice of intent to sue is given. They have disagreed, however, whether the 90-day extension provided by section 364(d) is in addition to, or is included within, the 90-day tolling attributable to section 356, as the following cases illustrate.

In *Gomez v. Valley View Sanitorium* (1978) 87 Cal.App.3d 507 [151 Cal.Rptr. 97], the court, relying on section 356, concluded that the giving of the 90-day notice of intent to sue required by section 364(a) tolls the 1-year statute of limitations for a period of 90 days, and that, in addition, when the notice is served within 90 days of the expiration of the statute, section 364(d) operates to lengthen the statute by a period of between 1 day and 90 days.

The *Gomez* court noted that section 364(d), which applies only when the requisite notice of intent to sue is given in the last 90 days of the limitations period, extends the limitations period for 90 days from the date of service of the notice. The court observed that section 364(a) "incongruously" prohibited the commencement of the action during the limitations period as extended by section 364(d). In the court's view, the statutory scheme would "self-destruct" were it not for the tolling provided by section 356. For these reasons, the court concluded that section 356 interrupted the running of the limitations period upon the serving of section 364(a)'s 90-day notice of intent to sue, and that the period *as extended by section 364(d)* resumed upon expiration of section 364(a)'s 90-day waiting period. (*Gomez v. Valley View Sanitorium, supra*, 87 Cal.App.3d at p. 510.)

Therefore, under *Gomez v. Valley View Sanitorium, supra*, 87 Cal.App.3d 507, the 90-day

tolling resulting from the application of section 356 and the 90-day extension flowing from section 364(d) are consecutive, so that the time for bringing suit does not expire until up to 180 days after service of the 90-day notice required by section 364(a). Thus, under *Gomez*, the statute of limitations period can be extended for a period ranging from 90 days to 180 days, depending on when a plaintiff gives section 364(a)'s 90-day notice of intent to sue. At least two cases have followed *Gomez*. (*Paxton v. Chapman General Hospital, Inc.* (1986) 186 Cal.App.3d 110, 115 [230 Cal.Rptr. 355]; *Estrella v. Brandt* (9th Cir. 1982) 682 F.2d 814, 818-819.)

But in *Braham v. Sorenson* (1981) 119 Cal.App.3d 367 [174 Cal.Rptr. 39], another Court of Appeal adopted a different view. In *Braham*, the court focused on the express language in section 364(d) providing that its 90-day extension must be measured from the date of service of section 364(a)'s 90-day notice of intent to sue. The court concluded that this *323 language precluded adding the two 90-day provisions. (119 Cal.App.3d at p. 372 .)

The *Braham* court reasoned that section 364(d)'s extension of 90 days was concurrent with, and consequently subsumed by, the 90-day tolling that results from applying section 356's "statutory prohibition" provision to section 364(a)'s 90-day notice requirement. As interpreted by *Braham*, the application of sections 356, 364(a), and 364(d) results in all cases in changing the one-year limitations period into a total of one year and ninety days, but not more than that. (*Braham v. Sorenson, supra*, 119 Cal.App.3d at pp. 372-373.) Among the cases that have followed the *Braham* decision are *Grimm v. Thayer, supra*, 188 Cal.App.3d 866, 870; *Gilbertson v. Osman, supra*, 185 Cal.App.3d 308, 317; *Hilburger v. Madsen* (1986) 177 Cal.App.3d 45, 52 [222 Cal.Rptr. 713]; and *Banfield v. Sierra View Local Dist. Hospital* (1981) 124 Cal.App.3d 444, 459-460 [177 Cal.Rptr. 290].

As we shall explain, the Courts of Appeal's application of section 356, the general tolling provi-

sion, cannot be harmonized with section 364(d)'s extension provision. Under the interpretations adopted by the Courts of Appeal, section 364(d) is either rendered meaningless or given a meaning that its language will not support.

III

(3) In construing statutes, we must determine and effectuate legislative intent. (*People v. Woodhead* (1987) 43 Cal.3d 1002, 1007 [239 Cal.Rptr. 656, 741 P.2d 154]; *People ex rel. Younger v. Superior Court* (1976) 16 Cal.3d 30, 40 [127 Cal.Rptr. 122, 544 P.2d 1322].) To ascertain intent, we look first to the words of the statutes. (*Dyna-Med, Inc. v. Fair Employment & Housing Com.* (1987) 43 Cal.3d 1379, 1386-1387 [241 Cal.Rptr. 67, 743 P.2d 1323]; *People v. Woodhead, supra*, at p. 1007.) "Words must be construed in context, and statutes must be harmonized, both internally and with each other, to the extent possible." (*California Mfrs. Assn. v. Public Utilities Com.* (1979) 24 Cal.3d 836, 844 [157 Cal.Rptr. 676, 598 P.2d 836].) Interpretations that lead to absurd results or render words surplusage are to be avoided. (*Ibid.*)

(4a) To apply section 356's tolling provision to section 364, as the Courts of Appeal have done, extends the 1-year statute of limitations for either a period ranging from 90 to 180 days, as expressed in *Gomez v. Valley View Sanitorium, supra*, 87 Cal.App.3d 507, or for 90 days only, but not more than that, as held in *Braham v. Sorenson, supra*, 119 Cal.App.3d 367.

The *Gomez* court's construction, under which the section 364(d) extension commences only after the section 356 tolling is concluded, cannot be *324 reconciled with the language of section 364(d) stating that the 90-day extension is measured "from the service of the notice" that a plaintiff must give under section 364(a).

The *Braham* court's construction, on the other hand, is faithful to the language of section 364(d), but at the cost of rendering it substantively meaningless. Under the reasoning of *Braham*, the section

364(d) extension and the section 356 tolling are both “triggered” by the same act (service of the notice of intent to sue). Beginning at the same time, the two 90-day periods run in tandem and expire together. In other words, the section 364(d) extension is wholly subsumed within, and thus redundant of, the 90-day tolling attributable to sections 364(a) and 356. (5) Because this conclusion deprives section 364(d) of any meaning, it violates the rule that every provision of a statute is assumed to have meaning and to perform a useful function. (*White v. County of Sacramento* (1982) 31 Cal.3d 676, 681 [183 Cal.Rptr. 520, 646 P.2d 191]; *J. R. Norton Co. v. Agricultural Labor Relations Bd.* (1979) 26 Cal.3d 1, 36 [160 Cal.Rptr. 710, 603 P.2d 1306].)

(4b) The anomalies created by applying the tolling provision of section 356 to section 364 suggest that when the Legislature enacted MICRA it did not intend section 356, a non-MICRA provision, to apply to section 364, a MICRA statute. This conclusion is supported by the presence of section 365 in MICRA's statutory scheme. Section 365 states that a medical malpractice plaintiff's failure to comply with the 90-day notice requirement of section 364(a) does *not* invalidate court proceedings and is *not* jurisdictional, although failure to comply may subject the plaintiff's attorney to State Bar disciplinary proceedings. Therefore, as noted in *Toigo v. Hayashida* (1980) 103 Cal.App.3d 267, 268- 269 [162 Cal.Rptr. 874], section 365 does not legally prevent a plaintiff from commencing a medical malpractice action during the mandatory 90-day waiting period set forth in section 364(a). (Compare, e.g., *Cal. Cigarette Concessions v. City of L. A.* (1960) 53 Cal.2d 865, 868 [3 Cal.Rptr. 675, 350 P.2d 715] [§ 356 held to toll the statute of limitations during the pendency of a claim for refund of municipal business license taxes when the presentation of a claim to the city was a prerequisite to bringing court action]; *Eistrat v. Cekada* (1958) 50 Cal.2d 289, 291-292 [324 P.2d 881] [§ 356 held applicable to a restraining order in a bankruptcy proceeding that prevented the plaintiff from commencing an action].)

Our conclusion that section 356 does not apply to section 364 is also supported by the rule of statutory construction that a later, more specific statute controls over an earlier, general statute. Sections 364 and 365 were enacted in 1975 as part of MICRA, “an interrelated legislative scheme enacted to deal specifically with all medical malpractice claims.” (*325 *Young v. Haines* (1986) 41 Cal.3d 883, 894 [226 Cal.Rptr. 547, 718 P.2d 909].) Section 356, a non-MICRA provision, was enacted in 1872 (13A West's Ann. Code Civ. Proc. (1982 ed.) § 356, p. 594), and applies to tolling and to statutory prohibitions in general. (6) As we said in *People v. Tanner* (1979) 24 Cal.3d 514, 521 [156 Cal.Rptr. 450, 596 P.2d 328]: “A specific provision relating to a particular subject will govern a general provision, even though the general provision standing alone would be broad enough to include the subject to which the specific provision relates.”

(4c) The conclusion that the tolling provision of section 356 is inapplicable does not, however, resolve the problem presented by a literal application of section 364(d). That provision states that if section 364(a)'s 90-day notice of intent to sue is served during the last 90 days of the statute of limitations, the limitations period is “extended 90 days from service of the notice.” As mentioned previously, a literal application of section 364(d) would require a medical malpractice plaintiff to commence the lawsuit in the same period of time during which section 364(a) precludes the plaintiff from filing suit. To resolve the problem, we must therefore consider both the context in which section 364 was enacted and the legislative objective. (*Dyna-Med, Inc. v. Fair Employment & Housing Com.*, *supra*, 43 Cal.3d at p. 1387; see *People v. Woodhead, supra*, 43 Cal.3d at pp. 1007-1008.)

As we noted at the outset, in enacting MICRA the Legislature sought to “reduce the cost and increase the efficiency of medical malpractice litigation” by, among other things, changing the legal rules governing such litigation. (*American Bank & Trust Co. v. Community Hospital, supra*, 36 Cal.3d

at pp. 363-364.) One such change was to impose, through section 364(a), a 90-day "waiting" period on the plaintiff in an effort to encourage negotiated resolution of the medical malpractice dispute outside the formal litigation process. (*Grimm v. Thayer, supra*, 188 Cal.App.3d at p. 871.)

That legislative purpose is best effectuated by construing section 364(d) as tolling the one-year statute of limitations when section 364(a)'s ninety-day notice of intent to sue is served during, but not before, the last ninety days of the one-year limitations period. Because the statute of limitations is tolled for 90 days and not merely extended by 90 days from the date of service of the notice, this construction results in a period of 1 year and 90 days in which to file the lawsuit. In providing for a waiting period of at least 90 days before suit can be brought, this construction achieves the legislative objective of encouraging negotiated resolutions of disputes.

Moreover, this interpretation resolves the dilemma, discussed earlier, that sections 364(a) and 365 pose for a plaintiff's attorney who serves the 90-day notice of intent to sue required by section 364(a) in the last 90 days of the 1-year *326 limitations period. Our construction of section 364 as tolling, rather than merely extending, the statute of limitations, permits the plaintiff to commence the action after the 90-day "waiting" period has elapsed and before the limitations period has expired.^{FN3} The plaintiff who gives the 90-day notice before the last 90 days of the 1-year limitations period can still bring the lawsuit after the 90-day period has elapsed because in that situation the 1-year statute of limitations will not have expired at the end of the 90-day waiting period.

FN3 A plaintiff who serves the notice of intent to sue on the last day of the limitations period has one day after the ninety-day waiting period to file the complaint. Tolling may be analogized to a clock that is stopped and then restarted. Whatever period of time that remained when the

clock is stopped is available when the clock is restarted, that is, when the tolling period has ended. Because the law does not divide time periods into increments of less than one day (see, e.g., §§ 12, 1013) and because tolling takes effect immediately, the day of service of the notice is not part of "the time for the commencement of the action." (§ 340.5.)

Furthermore, this construction of section 364 harmonizes the statutory provisions at issue. It maintains the legislative mandate, as expressed in section 364(a), that a medical malpractice plaintiff give the defendant at least 90 days' notice of intent to sue before commencing an action. As explained earlier, by imposing this 90-day waiting period, the Legislature sought to encourage settlement outside the formal litigation process. Our construction also achieves section 364(d)'s purpose of preserving the 90-day negotiation period by allowing additional time to bring the lawsuit when the plaintiff serves the 90-day notice in the last 90 days of the limitations period. It further gives effect to the provision in section 365 that the failure to give section 364(a)'s 90-day notice of intent to sue is not jurisdictional and does not invalidate any proceedings.

We recognize that to grant additional time to a plaintiff who serves the notice of intent to sue required by section 364(a) in the last 90 days of the limitations period, but not to a plaintiff who more promptly gives such notice, appears to reward the dilatory plaintiff. But the Legislature drew this distinction when it enacted MICRA. Through section 364(d), the Legislature extended the statute of limitations "[i]f the notice is served within 90 days of the expiration of the applicable statute of limitations" Presumably the Legislature's reason for imposing this restriction was that plaintiffs who serve the notice before the final 90 days of the limitations period will still have time to file their actions after the 90-day waiting period is concluded, and so they do not need an extension. (See *Mutual Life Ins. Co. v. City of Los Angeles* (1990) 50

Cal.3d 402, 412 [267 Cal.Rptr. 589, 787 P.2d 996].) In matters of statutory construction, we may not ignore restrictions the Legislature has inserted. (§ 1858.) If the relief afforded by section 364(d) is to be provided also to plaintiffs who serve the section 364(a) notice *327 before the last 90 days of the 1-year limitations period, it must be the Legislature that provides it.

The distinction between a plaintiff who promptly gives notice and one who gives notice in the last 90 days of the limitations period does serve the legislative objective of allowing time for negotiations without the formal initiation of legal proceedings. Tolling the limitations period when the plaintiff serves the notice during the last 90 days of that limitations period allows MICRA plaintiffs to continue negotiating with the defendants for the full 90-day waiting period contemplated by MICRA before their actions must be filed to avoid the bar of limitations. At the same time, this construction of section 364(d), which restricts relief to plaintiffs who serve the notice of intent to sue during the last 90 days of the limitations period, avoids judicially converting the legislatively established 1-year statute of limitations (§ 340.5) into a 1-year-and-90-day statute of limitations in all cases. As we have seen, the alternative constructions render section 364(d) meaningless, reach anomalous results, or cannot be reconciled with the other statutory provisions at issue.

Invoking the constitutional guarantee of equal protection, plaintiff argues that the statutory scheme improperly favors those plaintiffs who serve the section 364(a) notice of intent during the last 90 days of the 1-year limitations period. These plaintiffs are favored, according to this argument, because they alone are granted extensions of the one-year limitations period. This distinction, plaintiff maintains, violates equal protection because it lacks a rational relationship to the legislative objective. We disagree.

The timing of the notice determines in which group the plaintiff falls. Because the plaintiff con-

trols the timing of the notice, it is the plaintiff who selects the group or classification. Under the one-year statute of limitations, a cause of action accrues on discovery. (§ 340.5.) Thus, upon discovery of the injury the medical malpractice plaintiff is aware of the cause of action and can decide when to give the statutory notice of intent to sue. Consequently, the plaintiff rather than the Legislature determines the plaintiff's group or classification.

Also without merit is plaintiff's assertion that the legislative classifications are not rationally related to the legislative objective. (7) The "rational basis" standard, rather than the "compelling state interest" test, applies to legislative classifications among personal injury plaintiffs. (*Young v. Haines*, *supra*, 41 Cal.3d at p. 899; *American Bank & Trust Co. v. Community Hospital*, *supra*, 36 Cal.3d at p. 373, fn. 12.) As noted earlier, the Legislature sought to decrease the number of medical malpractice actions filed by providing for a period of negotiation before commencement of the *328 lawsuit. Allowing additional time if the 90-day notice to sue is not given until the last 90 days of the statute of limitations directly relates to this legislative objective by providing time for negotiation without barring the plaintiff's claim. (See *Fein v. Permanente Medical Group* (1985) 38 Cal.3d 137, 161-164 [211 Cal.Rptr. 368, 695 P.2d 665]; *Roa v. Lodi Medical Group, Inc.* (1985) 37 Cal.3d 920, 930-933 [211 Cal.Rptr. 77, 695 P.2d 164]; *Barme v. Wood* (1984) 37 Cal.3d 174, 181-182 [207 Cal.Rptr. 816, 689 P.2d 446]; *American Bank & Trust Co. v. Community Hospital*, *supra*, 36 Cal.3d at pp. 370-374.)

(4d) For the reasons given above, we hold that when a plaintiff gives the 90-day notice of intent to sue required by section 364(a) in the last 90 days of the 1-year statute of limitations that statute is tolled for 90 days.^{FN4}

FN4 Statements in the following cases inconsistent with this holding are disapproved: *Grimm v. Thayer*, *supra*, 188 Cal.App.3d 866; *Paxton v. Chapman General Hospital, Inc.*, *supra*, 186 Cal.App.3d

110; *Gilbertson v. Osman*, *supra*, 185 Cal.App.3d 308; *Hilburger v. Madsen*, *supra*, 177 Cal.App.3d 45; *Banfield v. Sierra View Local Dist. Hospital*, *supra*, 124 Cal.App.3d 444; *Braham v. Sorenson*, *supra*, 119 Cal.App.3d 367; and *Gomez v. Valley View Sanitorium*, *supra*, 87 Cal.App.3d 507.

IV

In this case, plaintiff Varetta Woods was admitted to defendant Brotman Medical Center (Brotman) on May 10, 1983. Defendants Hiawatha Harris, M.D., and Alvin T. Trotter, M.D., agents and employees of Brotman, diagnosed plaintiff as suffering from schizophrenia, and provided treatment.

On June 29, 1983, plaintiff was transferred from Brotman to County-USC Medical Center (County-USC), where she was told she was suffering from encephalitis rather than schizophrenia. On July 21, 1983, plaintiff authorized Brotman to release her medical records to an attorney. After her discharge from County-USC on July 25, 1983, plaintiff changed attorneys.

In response to interrogatories, plaintiff stated that she learned of the alleged misdiagnosis upon admission to County-USC on June 6, 1983. Thus, that would have been the date on which plaintiff discovered her injury and the statute of limitations would have commenced running. (§ 340.5.) Hospital records, however, showed that Brotman discharged plaintiff on June 29, 1983, and that she was admitted on that same day to County-USC, where she remained until her discharge on July 25, 1983. Because of plaintiff's admission in her interrogatory response that she first learned of the misdiagnosis upon her admission to County-USC, the discrepancy between the date she said to be her admission date and hospital records showing a later date of admission suggests that the date given by *329 plaintiff may have been in error. In any event, as the Court of Appeal in this case concluded, "the date of such advice could not have been later than

July 25, 1983, the date of [plaintiff's] discharge from County-USC." For purposes of this decision, therefore, we will accept July 25, 1983—the latest possible date of plaintiff's discovery of the alleged malpractice—as the date on which the one-year statute of limitations started to run. (§ 340.5.)

In compliance with the 90-day notice requirement of section 364(a), plaintiff's new attorneys notified defendants on February 17, 1984, of her intent to file a malpractice action against them. The complaint was filed on August 16, 1984, one-year and three weeks after plaintiff's discovery of the injury. ^{FN5} It alleged medical malpractice based on negligent examination, diagnosis, and treatment. Each defendant answered, and alleged as an affirmative defense that the complaint was barred by the one-year statute of limitations.

FN5 Plaintiff did not file her complaint within one year of any of the possible dates (June 6, June 29, and July 25, 1983) of discovery of the injury. Nor did she serve the 90-day notice of intent to sue within the last 90 days of the 1-year limitations period regardless of which date is considered the date of discovery. Each of these possible dates leads to the same result.

Defendants moved for summary judgment on the ground that the filing of the complaint was untimely because it occurred after expiration of the statute of limitations. (§ 340.5.) The trial court granted the motions, and denied plaintiff's motion for reconsideration.

Plaintiff appealed, and obtained a reversal. The Court of Appeal held that the statute of limitations was tolled by the giving of the notice of intent to sue, regardless of when during the limitations period the notice was given. Although the court noted that the application of section 356's tolling provision to section 364 was questionable, it decided to follow the existing published decisions that had applied section 356 to section 364. Because plaintiff's

complaint was filed within one year and ninety days of the date her cause of action accrued, the Court of Appeal reversed the judgment of the trial court.

V

(8a) If the construction of the relevant statutes that we have adopted were applied retroactively to the facts of this case, plaintiff's action would be barred by the statute of limitations. Because she served the notice of intent to sue before the last 90 days of the limitations period, plaintiff would not be entitled to the benefit of the tolling provided by section 364(d). Her complaint, filed one year and three weeks after discovery of her cause of action, would be untimely. *330

(9) Unlike statutory enactments, judicial decisions, particularly those in tort cases, are generally applied retroactively. (*Newman v. Emerson Radio Corp.* (1989) 48 Cal.3d 973, 978, 981-982 [258 Cal.Rptr. 592, 772 P.2d 1059].) But considerations of fairness and public policy may require that a decision be given only prospective application. (*Id.* at pp. 983-984; see *Estate of Propst* (1990) 50 Cal.3d 448, 463 [268 Cal.Rptr. 114, 788 P.2d 628]; *Moradi-Shalal v. Fireman's Fund Ins. Companies* (1988) 46 Cal.3d 287, 305 [250 Cal.Rptr. 116, 758 P.2d 58]; *Peterson v. Superior Court* (1982) 31 Cal.3d 147, 152 [181 Cal.Rptr. 784, 642 P.2d 1305].) Particular considerations relevant to the retroactivity determination include the reasonableness of the parties' reliance on the former rule, the nature of the change as substantive or procedural, retroactivity's effect on the administration of justice, and the purposes to be served by the new rule. (*Newman v. Emerson Radio Corp.*, *supra*, at pp. 983-992; *Peterson v. Superior Court*, *supra*, at p. 152; *Neel v. Magana, Olney, Levy, Cathcart & Gelfand* (1971) 6 Cal.3d 176, 193 [98 Cal.Rptr. 837, 491 P.2d 421].)

(8b) Reliance by litigants on the former rule and the unforeseeability of change support prospective application of the rule adopted here. As we have observed, the issue presented in this case has

been addressed in seven published Court of Appeal decisions. Although the Courts of Appeal were divided on the interpretation and application of section 364(d),^{FN6} all seven opinions concluded that the one-year limitations period was tolled during section 364(a)'s ninety-day waiting period regardless of when during the limitations period the notice of intent to sue was served. This unanimous conclusion established a settled rule upon which plaintiff could reasonably rely in determining when to file her action.

FN6 Because the Courts of Appeal were divided on this issue, a plaintiff could not reasonably rely on the interpretation under which the time for bringing suit after discovery of the injury could exceed one year and ninety days. This interpretation, first advanced in *Gomez v. Valley View Sanitorium*, *supra*, 87 Cal.App.3d 507, was vigorously disputed by other appellate decisions.

Limiting the retroactivity of our decision is also indicated by the nature of the change effected by the new rule. The change is procedural, affecting only the calculation of the limitations period. Prospective application will not remove any substantive defense to which defendants would otherwise be entitled. Retroactive application of the change, on the other hand, would bar plaintiffs' actions regardless of their merits. (10) Retroactive application of an unforeseeable procedural change is disfavored when such application would deprive a litigant of "any remedy whatsoever." (*Chevron Oil Co. v. Huson* (1971) 404 U.S. 97, 108 [30 L.Ed.2d 296, 306, 92 S.Ct. 349]; *Newman v. Emerson Radio Corp.*, *supra*, 48 Cal.3d at pp. 990-991.)

(8c) Concern for the administration of justice further supports prospective application. Medical malpractice is one of the more common tort *331 actions; therefore, we anticipate that many pending cases will be affected by our decision. Justice is not served by barring so many actions that reasonably appeared timely when filed. (*Moradi-Shalal v.*

Fireman's Fund Ins. Companies, supra, 46 Cal.3d at p. 305; *Li v. Yellow Cab Co.* (1975) 13 Cal.3d 804, 829 [119 Cal.Rptr. 858, 532 P.2d 1226, 78 A.L.R.3d 393].)

The purposes of the new rule announced in this decision are to harmonize statutory provisions and to resolve a division of authority in the Courts of Appeal. These important objectives are not compromised by prospective application of the new rule.

Consideration of the relevant factors leads us to conclude that our primary holding in this case should be given only prospective application. Accordingly, this opinion's holding—that serving the notice of intent to sue tolls the one-year limitations period only when the notice is served during the last ninety days of the one-year period—shall apply only to complaints filed more than ninety days after this decision becomes final (see Cal. Rules of Court, rule 24(a)).^{FN7} All complaints filed no later than 90 days after the decision becomes final shall have the benefit of a 90-day tolling if a notice of intent to sue was served at any time during the 1-year limitations period.

FN7 Making the holding effective as soon as our decision becomes final would reduce the limitations period for those plaintiffs who served the notice of intent to sue before the final 90 days of the 1-year limitations period but have not yet filed suit. To provide a reasonable period within which such parties may commence their actions, we have determined that the effective date should be 90 days after the decision becomes final.

The judgment of the Court of Appeal is affirmed. Defendants are awarded their costs on appeal.

Lucas, C. J., Panelli, J., Arabian, J., Baxter, J., and Kremer, (Daniel J.), J.,^{FN*} concurred.

FN* Presiding Justice, Court of Appeal, Fourth Appellate District, Division One, assigned by the Chairperson of the Judicial Council.

MOSK, J.

I write a separate concurrence to emphasize some of the anomalies in the statutory scheme governing the time limitations applicable to actions for malpractice.

I concur reluctantly in the majority's holding that the 90-day tolling of the statute of limitations applies only to those who file the notice required by subdivision (a) of section 364 of the Code of Civil Procedure (hereinafter section 364(a))^{FN1} within the last 90 days of the 1-year limitations period set forth in section 340.5. The consequence of this ruling is to allow the dilatory malpractice plaintiff an additional 90 days to file a malpractice action—i.e., *332 1 year plus 90 days—while limiting the diligent plaintiff to 9 months or less from the date the notice period expires—i.e., 1 year minus 90 days. It is difficult to believe that the Legislature deliberately intended such an inexplicable result.

FN1 All statutory references in this opinion are to the Code of Civil Procedure.

Nevertheless, I can see no way to avoid the majority's holding in view of the statutory language. Sections 364(a) and 365, construed together, appear to prevent application of the tolling provision of section 356 to plaintiffs who file the required notice prior to the last 90 days of the limitations period. Section 356, which applies to actions generally, provides that when the commencement of an action is stayed by a statutory prohibition, the time of the continuance of the prohibition is not part of the limitation period. On its face, section 364(a) contains such a prohibition, i.e., it declares in the clearest terms that a malpractice action may not be commenced unless the plaintiff has given 90 days' prior notice of the intent to bring the action. But section 365 nullifies this prohibition against bringing the

action without the required notice: it provides that the failure to give notice is not jurisdictional, but, rather, that an attorney who fails to do so is subject to discipline.^{FN2}

FN2 Section 365 provides, "Failure to comply with this chapter [which includes section 364] shall not invalidate any proceedings of any court of this state, nor shall it affect the jurisdiction of the court to render a judgment therein. However, failure to comply with such provisions by any attorney at law shall be grounds for professional discipline and the State Bar of California shall investigate and take appropriate action in any such cases brought to its attention."

In view of the provisions of section 365, section 364(a) cannot be viewed as a statute which stays the commencement of an action within the meaning of section 356. Thus, section 364(a), in spite of its prohibitory language, does not provide the 90-day tolling period to plaintiffs in malpractice actions. While I doubt that the Legislature intended such a result, it appears to be compelled by the statutory language.

Another aspect of the majority opinion that troubles me is their departure from the language of section 364, subdivision (d). That provision states that in the case of a plaintiff who files notice within 90 days of the expiration of the limitations period, "the time for the commencement of the action shall be extended 90 days from the service of the notice." The majority holding tolls the statute of limitations rather than extending it, and it does so for a fixed 90 days beyond the 1-year limitation period for all such plaintiffs, rather than varying the time allowed for commencing the action according to the date of the service of summons.

Nevertheless, there seems to be no other way out of the dilemma posed by the language of section 364, subdivision (d), which requires an attorney to *333 either sacrifice a client's cause of ac-

tion to the bar of the statute of limitations or face disciplinary proceedings before the State Bar. If the statute were applied literally, as is pointed out in *Gomez v. Valley View Sanitorium* (1978) 87 Cal.App.3d 507, 510 [151 Cal.Rptr. 97], subdivision (d) of section 364 would "self-destruct." The choice, then, appears to be between applying the statute as written, which would not accomplish the Legislature's goal, or, as the majority have done, in effect rewriting it. The latter course is obviously unsatisfactory, but I reluctantly conclude that in this instance it may be the best way to resolve the anomalies caused by the contradictory and ineffectual statutory scheme.

BAXTER, J.

I concur in the judgment. I think it necessary, however, to point out that defendant Trotter failed to petition for review of the Court of Appeal decision or to join in the petition for review filed by defendant Harris. Rule 28(b) of the California Rules of Court clearly provides that, "A party seeking review *must* serve and file a petition" (Italics added.) Defendant Trotter's failure to do so raises the question of whether he is properly before this court. As a practical matter, we need not decide that question in light of our affirmance of the Court of Appeal decision against defendant Trotter. I believe a word of caution, however, is advisable. In future cases, each party who seeks our review should comply with rule 28(b) either by filing a petition for review or by filing an express written joinder in another party's petition. *334

Cal. 1991.
Woods v. Young
53 Cal.3d 315, 807 P.2d 455, 279 Cal.Rptr. 613

END OF DOCUMENT