



RECOVERING PROPERTY DAMAGES UNDER
CALIFORNIA LAW

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RECOVERING PROPERTY DAMAGES UNDER CALIFORNIA LAW:

Two General Categories

There are two general categories of damages:

(1) **Economic Damages** are objectively verifiable monetary losses such as past and future medical expenses, loss of past and future earnings, burial costs, loss of use of property, costs of repair or replacement, costs of obtaining domestic services, loss of employment and loss of business or employment opportunities; BAJI 14.00

(2) **Non-Economic Damages** are subjective, non-monetary losses such as pain, suffering, inconvenience, mental suffering, emotional distress, loss of society and companionship, loss of consortium, humiliation and injury to reputation. BAJI 14.76; Civil Code § 1431.2(b)(1) & (b)(2).

MEASURE OF DAMAGES GENERALLY

“**THE MEASURE OF DAMAGES [IN CALIFORNIA]** for the commission of a tort is that amount which will compensate the plaintiff for **ALL DETRIMENT SUSTAINED** as the proximate result of the defendant’s wrong, regardless of whether or not such detriment could have been anticipated by the defendant.” Civil Code § 3333.

DAMAGES TO A COMMERCIAL ENTERPRISE

A Review Of Real Property And Business Related Damages

Generally, there are no hard and fast rules for determining the measure of damages to property in California. Armitage v. Decker (1990) 218 CA3d 887. The measure of damages can be different in each case, depending on the kind of *real property* involved and the type of damage done to the property. Hancock v. GRC Paving Co. (1931) 114 CA 624, 628.

Damages to a Commercial Structure

The most basic and normal rule uses *diminution in value* as the measure of damages of destroyed property, which is the difference between the fair market value of the property immediately before and after the fire. Revis v. Chapman (I.S.) & Co. (1933) 130 C.A. 109, 115. However, this method is not the exclusive way of measuring damages and other methods may be substituted if the court finds them more appropriate. Natural Soda Products Company vs. City of Los Angeles (1943) 23 C2d 193, 200-201.

“If the damages have been repaired, or are capable of repair, so as to restore the fair market value as it existed immediately before the accident, at a cost less than the difference in value, then the measure of damage is the cost of the repair rather than the difference in value.” BAJI 14.20. Therefore, if the damage is repairable, the most-frequent measure of damages will be the *cost of repair*. Charles v. Reuck (1960) 179 CA2d 145, 147.

“If repairs have been made but the property cannot be completely repaired, the measure of damages is the difference in the fair market value of the property immediately before the fire and immediately after the repairs have been made, plus the reasonable cost of making the repairs.” BAJI 14.20.

The caveat is that the cost of repair as a measure of damages cannot be used (a) when the cost of repair exceeds the fair market value of the property destroyed, or (b) the cost of repair exceeds the difference in fair market before and after the loss. Green v. General (1928) 205 C. 328. In any of the above two situations, the value of the property itself immediately before the fire is the correct measure of damages. De Costa v. Massachusetts (1861) 17 C 613, 617.

Betterment

As related to property damage, the law of torts generally aims at placing the injured party in the place they were in prior to the injury. California Civil Code § 3333. Thus, the injured party is not entitled to be placed in a better position as the result of the accident.

Betterment denotes an addition to or enhancement of real property that increases its capital value and is designed to make the property more useful or have an increased market value. Betterment involves the expenditure of labor or money and is designed to make the property more useful or valuable as distinguished from ordinary repairs. Keller vs. Chowchilla Water District, [2000] 80 Cal.App.4th 1006, 32 Cal.Rptr. 2d 511.

Where the repairs to a Commercial structure includes enhancements or improvements that increase the market value of the property beyond the status pre-loss, the Courts are reluctant to attach liability to a tortfeasor for the cost of same. The issue generally involved in “betterment” cases is the qualification of the improvement as either a necessary or sole substitute for the damaged portion of the structure.

Code Upgrades

Code Upgrades are the cousin of “betterment” improvements to property. In the “betterment” arena, building materials or fixtures which replace existing or lost materials or fixtures, are an “enhancement” upon the “like kind and quality” of the materials and items that they are replacing. Hence, they are termed “betterments.”

Code Upgrades, on the other hand, are publicly mandated alterations in the building components, structure or materials, which are required by law or “code.” These are improvements for which there can be no deviation and are not necessarily requested by the insureds. Nonetheless, the cost to “bring a structure to code” can significantly increase the cost of repair and can result in placing the “insured’s property” in a “better circumstance” than it was before the loss ... and hence, a “betterment.”

Nationwide, the majority rule is that code enforcement damages are not recoverable in tort actions. Stinger v. Hope Natural Gas Co. (1954) 80 S.E.2d 889. The minority view, allowing for such recovery, is reflected in Peluso v. Singer General Precision, Inc. (1977) 365 N.E.2d 390. Although California cases have held that an *insurer* is not responsible to its insured for code upgrades, there are apparently no cases dealing with code upgrades in the context of third-parties (i.e. the insured or his subrogated insurer suing a negligent third party for damages and seeking to recover code upgrade costs). Although there are no California cases on point, if code upgrades and cost to repair do not exceed the diminution in value of the property they are recoverable. In addition, the damaged party can make the following arguments:

(1) “But for” analysis: The damaged party would not have incurred the expenses related to the code enforcement *but for* the negligence of the tortfeasor, which proximately caused the damages; and

(2) “Incomplete recovery”: The damaged party is effectively unable to restore its property until the code upgrade repairs or modifications are made. It is unrealistic to assume that the damaged party can replace its damaged property with those of like kind and quality when doing so without the necessary upgrades would be in violation of the law.

The Potential Measures of Recovery for Inventory Losses

Many insurance policies covering manufacturers and other commercial entities provide coverage for inventory destroyed in a covered event on the basis of selling price, less unincurred selling expenses. Liability adjusters and defense lawyers will rarely be prepared to settle an inventory claim on the basis, however, absent proof of actual sales lost with respect to the involved merchandise. Common sense might suggest that the manufacturer is placed in the same position that it existed in immediately before the loss by receiving its cost to remanufacture the goods, particularly if it is able to meet all orders out of inventory. After all, it is frequently argued, that manufacturers like Revco can simply “turn up the speed” of the manufacturing machines and replace the damaged goods at little, if any, additional expense.

While this argument may be initially appealing, in most jurisdictions, including California, a manufacturer is not limited to its “cost of replacement”. It can recover its selling price from a tortfeasor consistent with coverage under your policy. Wholesalers and retailers, however, are limited to their replacement cost, assuming the goods are still readily available on the market.

As in just about every case involving damage to personal property, the legal standard of recovery is the “fair market value” of the inventory at the time of its destruction. Bench Approved Jury Instruction (BAJI) 14.21. How is fair market value determined? It is the highest price that a willing seller would be willing to sell the inventory for to a willing buyer, neither being under any duress to engage in the transaction. BAJI 11.73. The other principle which is paramount in the area of damages is the goal to put the injured party in the same position it occupied immediately before the accident to the extent possible. Witkin, Summary of California Law, Torts §1319.

By following these two rules, the answer of who gets what as between a manufacturer, wholesaler and retailer should become relatively clear. A retailer can go back into the market as a willing buyer and repurchase the damaged inventory at its wholesale selling price at the time of the loss. If it is able to replace the inventory at the same price, it has been restored to the position it held before the loss. (Note: It is not what the retailer paid for the inventory originally

which controls, but what was its replacement cost or wholesale selling price within a reasonable time of the loss.) Similarly, a wholesaler can go back to the manufacturer and replace the destroyed inventory at the manufacturer's selling price. A manufacturer, however, cannot go back into the market to replace or repurchase the goods. The argument that the replacement cost of a manufacturer is equivalent to its cost to remanufacture ignores the reality that a manufacturer would never be a "willing" seller if it did not receive its profit for such merchandise. It is for this reason that the majority of jurisdictions considering the issue have held that a manufacturer is entitled to its selling price, assuming the destroyed goods had a readily available market and would have been sold but for the tortious event.

The following is a discussion of the leading cases which deal with the valuation of inventory losses for tort purposes.

In McMahan's of Santa Monica v. City of Santa Monica, 146 Cal.App.3d 683 (1983), a retail furniture store's stock was damaged as a result of a water main break. The owner of the store argued that it was entitled to recover the retail selling price of the merchandise, less any discounts. The Court of Appeals, however, held that McMahan's inventory which was damaged was not unique and readily replaceable. The plaintiff was only entitled to recover the wholesale cost of the furniture that was destroyed. In reaching this decision, the Court adopted the following Comment from the Restatement of the Law of Torts, Section 911:

From the time when a chattel is manufactured to the time of its actual use, there may be many markets in which it is sold. Thus, different prices are paid by the wholesaler, the retail dealer and the consumer. Since the measure of recovery is determined by the harm done, the market that determines the measure of recovery by a person whose goods have been taken, destroyed, or detained is that which he would have to resort in order to replace the subject matter. Thus, the consumer can recover the retail price, the retail dealer, and the wholesale price. The manufacturer, who does not buy in a market, receives his selling price. Damages for the profits which the wholesale dealer or the retail dealer would normally anticipate from a sale are not ordinarily allowed . . .

Comment d to Section 911, 146 Cal.App.3d at 701.

As McMahan's did not deal with a manufacturer's loss, some defense attorneys have argued that the Court was not necessarily adopting the Comment's conclusion that a manufacturer is always entitled to its selling price, but rather that recovery of selling price

requires proof of lost sales. The leading case directly on point on this issue is Simmons, Inc. v. Pinkerton's, Inc., 762 F.2d 591 (7th Cir. 1985). In Simmons, a well-known manufacturer of bedding material lost a portion of its inventory in a warehouse fire which was caused by the defendant's security guard. The jury awarded Simmons the fair market value of the inventory destroyed based upon its regular selling price. The defendant argued on appeal that because Simmons was a manufacturer and was able to replace the destroyed goods out of existing inventory and made no claim of lost sales or profits, damages should have been limited to Simmons' cost of remanufacturing the destroyed goods without any allowance for speculative future profit. The Court of Appeals summarily rejected this argument:

Pinkerton admits it can cite no Indiana law to buttress its imaginative argument that we should discard the fair market value – selling price measure in this case . . . Simmons deducted from the list price the cost of selling the inventory, thus taking account of the fact that the inventory was still at the manufacturer's level in the chain of distribution, not at the wholesaler's. The manufacturer's 'profit margin', on the other hand, seems properly attributable to the manufacturing process, not primarily to the process of distribution. The fact that Simmons can replace the goods by manufacturing should not affect a profit margin attributable to the manufacturing process. The profit margin is part of the value as inventory, even though, like the rest of the price, it is not realized until sale. Id. 726 F.2d at 606-607 (Emphasis supplied).

See also H.K. Porter Co. v. Halperin, 297 F.2d 442 (7th Cir. 1961) and Eastman Kodak Company v. Westway Motor Freight, Inc., 949 F.2d 317 (10th Cir. 1991).

The only case which we have found to date which does not award a manufacturer its selling price is Akro-Plastics v. Drake Industries, 115 Ohio App. 3d 221, 685 N.E. 2d 246 (1996). In that case, the plaintiff's medical stretcher boards were destroyed in a fire which occurred at a contractor's facility at which foam was injected into the boards prior to their return to the plaintiff for sale. The state court in Ohio held that the plaintiff manufacturer was only entitled to recover the cost to remanufacture the goods as opposed to their ultimate selling price. Had the boards been finished at the time of their destruction and a ready market were proven however, we believe the Court would have allowed the manufacturer to recover its selling price. The Akro-Plastics case illustrates that where the merchandise may not be immediately saleable at the time of loss, the plaintiff will not be awarded future profits in the nature of its selling price

In the retail setting, the retailer is also often insured for its selling price. The subrogating insurer, however, may only recover the wholesale price or cost to its insured. If the retailer can also show a loss of a specific sale which it could not meet by way of replacement merchandise, it would be entitled to its selling price by way of a supplemental award of loss of earnings. Similarly, a wholesaler may be able to recover the selling price if the destroyed goods are already sold and it can show a loss of a specific customer or sale. A manufacturer, having received its selling price, cannot recover on a business interruption basis as it has already received its built-in profit by way of its selling price.

What if the inventory is obsolete or not readily marketable at the manufacturer's listed selling price? In such a case, selling price does not represent what a willing buyer would pay and fair market value must be further analyzed. An appraisal may be required which would consider original cost to manufacture, age and all other relevant factors which would be considered by a knowledgeable buyer and seller.

Business Interruption

Upon the occasion of a loss in a commercial setting, not only does the insured suffer damage to its inventory but generally they are unable to conduct their trade or business for a period of time. As a result, while profits are not generated, the costs to maintain the business location and obligations continue.

California case law has interpreted Civil Code § 3333 to include recovery for the loss of anticipated profits where an established business has been injured. Natural Soda vs. City of Los Angeles [1943] 23 Cal.2d 193 Accordingly, courts have also allowed recovery for damages to commercial property to include lost past and future profits, in addition to increased operating expenses during repairs.

“The basis of this principle is that where the operation of an established business is prevented or interrupted by a tort, damages for loss of prospective profits, that otherwise might have been made from its operation, are ordinarily *recoverable for the reason that their occurrence and extent may be ascertained with reasonable certainty* from the working experience of the business, from the past volume of the business, and other provable data relevant to the probable future sales.” Lucky v. Turner (1966) 244 CA2d 872, 882.

As a general requirement, the owner must provide a satisfactory basis for estimating what the probable earnings would have been had there if the loss had not taken place; otherwise, the owner is denied recovery of an amount that would be uncertain, speculative, or remote. Furthermore, the owner may not recover both for *loss of business profits and loss of use* since this will lead to double recovery. Tremeroli v. Austin (1951) 102 CA2d 464, 482-483. However, an owner may recover for both loss of use of the property and a loss of profits that would have been made from the sale of the property (i.e. gains in the real estate value). These values are normally subject to qualification by each side’s expert witnesses who will shed light on financial records and other supporting evidence.

“While the courts have often noted the difficulty of proving the amount of loss of profit they have also recognized that a defendant cannot complain if the probable profits are of necessity estimated, the rationale being that it was the defendant himself who prevented the

plaintiff from realizing profits.... Accordingly, the general principle inherent in the recovery of damages for loss of prospective profits is that the evidence must make reasonably certain their nature, occurrence and extent. In sum, such evidence must be of reasonable reliability.” Lucky, supra, at 882-83.

Stigma Damages

Stigma is the identifying mark or characteristic permanently or temporarily associated with real or personal property. Stigma cases mostly revolve around real estate disclosure cases. For illustration purposes, imagine a house claimed to be haunted by its neighbors that was occupied by an AIDS patient who was later convicted of a heinous crime and eventually executed. The uninformed buyer of such a house may eventually sue the seller and/or realtors for having failed to disclose these facts and seek to recover stigma damages; namely, the difference is the fair market value of the property had it not been tainted with the undesirable characteristics.

Another source of plentiful litigation in stigma cases involves toxic torts, where the negative image of the post-clean up property adversely affects its fair market value. In one noteworthy case, a transportation company contaminated a piece of land with chemical pollutants. After successful clean-up efforts, the property owner sued the transportation company, arguing that the stigma attached to the contaminated land decreased its value. The court rejected the stigma claim and held that under California law, the property owner could have recovered damages only if the contamination been permanent and irreparable, posing a threat of future injury. Santa Fe Partnership v. ARCO (1996) 46 CA4th 967.

To a lesser extent, some cases have dealt with the stigma associated with real property due to construction defects. For example, a large commercial building with a defective foundation is properly repaired and put back on the market. To the owner's dismay, the entire business community has learned about the defect and potential tenants are unwilling to lease the premises for the fair market value of similar buildings. The owner's recourse is to make significant concession in overcoming the stigma, and suing the responsible parties (i.e. the developer and the contractor) for its damages. In such cases, stigma damages represent the residual loss of market value after repairs have been made.

In general, California case law does not permit the recovery of "stigma" damages in cases involving damage to real property. As a matter of public policy, the courts frown upon such damages as "simply too remote in the causal chain, too inherently speculative and too uncertain

of measurement to permit recovery.” Aas v. Superior Court (1998) 64 CA4th 916 citing Miller, California Construction Defect Litigation, § 10.7, p. 384. Therefore, in a hypothetical situation where a clothing store suffers partial fire damage and some of the clothing articles are soot damaged, the owner cannot recover under the theory that the *unaffected* articles carry the stigma of having been exposed to a fire. However, the owner may recover the fair market value of the *affected* articles, minus the salvage value, if any.

DAMAGES TO A PERSONAL RESIDENCE

A Review Of Real Property And Personal Property Related Damages

Damages for Repair or Restoration

California courts usually follow two formulas when determining how to compensate a injured party for damage caused to their personal residence. Generally when a defendant damages a home, the court awards the damaged party the difference in market value of the home immediately before and immediately after the harm, or the reasonable cost of repair if that cost is less than the diminution in value. This formula is generally followed unless the cost of repair exceeds the value of the residence. In that instance, a homeowner can be placed in a position where the cost to repair his home exceeds its value and thus he “cannot be made whole” if the only damages available to him is the diminution of value.

For example, a residence in Porterville, California is destroyed by fire. If the market value of the home before the loss is \$160,000.00 and the cost to rebuild is \$220,000.00, the standard formula would allow a tortfeasor to *pay the lesser of cost of repair or the diminution in value*. In such an instance, a homeowner would receive \$160,000.00 and *still not be able to replace the home!*

A personal reason exception allows a plaintiff the option of having the home repaired even though it would cost the defendant less to give the plaintiff the diminution in market value of the home. Orndorff v. Christiana Community Builders, (1990) 217 Cal. App.3d. In its ruling in Orndorff, the court noted that the plaintiffs should have the option to repair a defect caused by the defendant if they had a bona fide desire to repair and the damage caused by the defendant deprived the plaintiffs’ home of most of its value. The court noted that the personal reason exception should not apply when the defendant’s conduct improved the value of the plaintiffs’ home or only diminished the value slightly. If a defendant’s conduct only causes minor damage to a plaintiff’s home, the plaintiff most likely will be awarded the diminution in market value of the home because it is usually less then the cost of repair.

Additional Living Expense

The goal of awarding a injured party's damages is to compensate for all the detriment proximately caused by the tortfeasor's actions. An injured party who is entitled to repair cost or the loss in market value of her home because of the tortfeasor's actions can also be entitled to recover for further loss.

Further loss consists of any harm or cost suffered by the plaintiff that does not include the original damage to the home. The Second Restatement of the Law of Torts § 928, states, "...in addition to damages for the diminution of the value of the subject matter or other similar elements of damages, the plaintiff is entitled to recover for any loss of which the defendant's act is the legal cause, either because the plaintiff is unable to use the subject matter until it is repaired or replaced or otherwise." The language of the Restatement suggests that a plaintiff whose home is damaged by a defendant can ask the court to award her living expenses between the time of the loss and the repair, in addition to any money awarded for the damage caused to the home.

Contents

In a typical loss scenario, either by fire, flood or other calamity, the insured may lose use of or have destroyed significant personal property, including home furnishings, personal items and the like.

Damages to personal and real property are generally measured using the same formula. In both types of property cases, the plaintiff is usually entitled to the difference in the market value of the property immediately before or immediately after the injury, or the reasonable cost of repair if that cost is less. Although courts when measuring personal and real property damages adhere to the same damage calculations, the type of items covered by the two property definitions is drastically different. Personal property consists of any movable or intangible thing that is subject to ownership and real property consist of land or anything attached to land. An example of personal property would be someone's television and an example of real property would be the house where the television is located.

A case that provides a thorough explanation of how most courts arrive at a damage award for personal property damage is Hand Electronics, Inc. v. Snowline Joint Unified School District, (1994) 21 Cal. App.4th 862, 870. In Hand an electronics company claimed damages from the defendant school district when one of the district's buses collided with the company's truck and damaged some manufacturing equipment. The court in determining how the plaintiff should be compensated for its loss noted that the plaintiff would recover the depreciation in market value or repair cost for damage done to personal property. It explained how it decides to allocate a damage award to a plaintiff by stating:

“...if the cost of repairs exceeds the depreciation in value, the plaintiff may only recover the lesser sum. Similarly, if depreciation is greater than the cost of repairs, the plaintiff may only recover the reasonable cost of repairs. If the property is wholly destroyed, the usual measure of damages is the market value of the property.”

The language present in Hand Electronics concerning how to measure personal property damages is applicable to other cases because courts want to compensate plaintiffs for personal property damage caused by a defendant's actions but they do not want to award a plaintiff more than the value of the property destroyed.

Peculiar Value

The usual measure of damages for property which is totally destroyed is its market value. An exception to this general rule is, however, applied in cases involving damage to items with little or no market value which have special value to the owner. As indicated in Witkin on Torts § 1453:

“Where the market value is relatively small as compared with its special value to the owner, the value to the owner may sometimes be recovered, and resort may be had to such evidence as the value of time spent in producing it. This exception is applied, e.g., to books, manuscripts, etc.” (Emphasis in original). p. 928.

This point of law was squarely addressed by the California Supreme Court in Willard v. Valley Gas & Fuel Company (1915) 171 Cal.9. In Willard, the Court analyzed the damages recoverable for scrapbooks, other data and a rare book destroyed in a fire.

The Willard Court emphasized:

“It is clear that the scrapbooks could have no market value but that they might be of great value to a literary man. It was therefore proper for Mr. Willard to testify regarding their value to him. The same rule is applicable to the old book. p. 11.

The Court noted that:

“Ordinarily, where property has a market value that can be shown, such value is the criterion by which actual damages for its destruction for loss may be fixed. But if may be that property destroyed or lost has no market value. In such state of the case, while it may be that no rule which will be absolutely certain to do justice between the parties can be laid down, it does not follow from this, nor is it the law, that the plaintiff must be turned out of court with nominal damages merely. Where the article or thing is so unusual in its character that market value cannot be predicated of it, its value, or plaintiff’s damages, must be ascertained in some other rational way, and from such elements as are attainable. (Citation omitted) (Emphasis added). p. 12.

However, courts cannot award the “emotional” value of personal property, such as family photos and video-tapes and the like. There is no established method of valuing such property, although family photos and video tapes are worth more than the photographic paper and blank video tape. As stated in Mieske vs. Bartell Drug Company [1979] 92 Wash.2d 40, 593 P.2d 1308]:

“When determining damages based upon value to an owner, compensation for sentimental or fanciful values will not be allowed. The type of sentiment which is not

compensable as value to the owner is that which relates to indulging in feeling to an unwarranted extent or being affected or mawkishly emotional. [However] difficulty of assessment is not cause to deny damages to a plaintiff whose property has no market value and cannot be replaced or reproduced.”

An out-of-state decision, Doelger & Kirsten, Inc. v. National Union Fire Insurance Company of Pittsburgh, Pennsylvania (1969) 42 Wis. 2d 518; 167 N.W. 2d 198 is especially instructive.

That Court was asked to determine the proper measure of damages for wooden patterns used for production of castings for alligator shears. In commencing its analysis, the Court noted that alligator shears were items of heavy industrial equipment for which there was no longer much public demand.

The Doelger Court, in affirming a finding that plaintiff was entitled to replacement cost of the destroyed patterns, minus physical depreciation and obsolescence, stated:

“By the replacement test plaintiff would get \$12,100. By the present market value test, plaintiff would get nothing or very near that. The trial court adopted the measuring stick of replacement cost, minus physical depreciation and minus obsolescence. . . . This is in accord with the opinions of experts in valuation of a property. ‘For example, in the case of used patterns, molds, and designs used as equipment by a manufacturer it has been held that their replacement cost new is not a fair test and that their obsolescence as well as their physical depreciation must be taken into account.’” (Emphasis added.) p. 522.

The Court continued:

“Applied to the type of equipment here involved and the type of situation here presented, this appears to be a common sense approach to determining present ‘actual cash value.’ . . .”

Admittedly, this is no easy assignment. Under the fact situation here presented, the court could not be expected to ascertain the ‘actual cash value’ with exact mathematical precision. It was for the trier of fact to set the damages at a reasonable amount, using an acceptable measuring stick.” (Emphasis added) pp. 522-523.

EVIDENCE AND PROVING OF DAMAGES

Courts, when considering how to award damages to an insured who has suffered a loss from the actions of a defendant, usually rely on the testimony of the insured, the language found in documents obtained from the insured, the testimony of an insurance adjuster, and the testimony of an expert. This section discusses each of the four issues.

Testimony of Insured

It is well settled in California that the testimony of an insured regarding the expenses incurred for medical care and loss of work is some evidence of the reasonable value of the amount claimed absent any showing to the contrary. In Malison v. Black, (1948) 83 Cal. App.2d 375, 379, an injured driver sued another driver for his alleged negligence in operating an automobile. The injured driver, during his in court testimony, gave an estimate of the expenses he had incurred for medical care and loss of work, which the defendant believed were exaggerations. The defendant made two arguments to convince the court that the plaintiff should not be entitled to the damages he claimed as a result of the accident. First, the defendant argued that the damages in regard to the plaintiff's physical injury and loss of work could not be considered true unless the plaintiff provided medical documentation or past work receipts to verify his claims. Second, the defendant contended that the plaintiff should not be awarded the amount of damages he claimed because the plaintiff's own testimony on the subject of how much he should be awarded was uncertain and confused.

The court considering the evidence presented by both parties decided in favor of the plaintiff. Although the defendant's two arguments were quite convincing, the court believed that the plaintiff's evidence was more persuasive. It stated that, "...it is not surprising that a carpenter, did not describe the injuries to his shoulder with the same clarity that would be expected of a physician. [The plaintiff] was competent to testify to the fact that his shoulder was injured, that his arm was in a sling for a period of one month, that he was unable to work for about two months, {and} that he still suffered pain at night as a result of the injury." The court ruled that the amount the plaintiff claimed he paid for medical expenses and loss of work was

some evidence of the reasonable value of his claims. It also decided that without any showing to the contrary that the plaintiff's testimony was incorrect, the testimony would be sufficient to award the plaintiff the amount claimed if he won the case.

Thus Malinson provides sufficient precedent to establish that *an insured* may provide testimony as to the *market value, cost of goods*, or other *opinion evidence as it relates to items for which the insured would have personal knowledge*. This includes the value of the insured's real property. Any such testimony, of course, would be subject to cross-examination.

Documents

Documents are useful to corroborate the testimony of an insured regarding the price of a particular item. Although plaintiffs have prevailed on damage claims without providing documentation to validate their testimony, courts have become increasingly more reluctant to rely on a plaintiff's claims of damage if the defendant can present evidence that contradicts the plaintiff's testimony. An insured will have a greater likelihood of prevailing in court if they can provide evidence that describes how much their damaged property was worth when it was purchased. Below is a list of some items that a plaintiff can use to validate her testimony:

Bill of Sale

Receipt

Warranty

Contract

Testimony of Adjuster

An adjuster's in-court testimony regarding the amount of property damage suffered by a plaintiff because of the defendant's negligence or willful misconduct is admissible evidence to support a judgment for an insured or insurer. In Lakewood Engineering and Manufacturing v. Quinn, (Md. App. 1992) 604 A.2d 535, 537, buyers of a defective electric fan sued the manufacturer for fire damage to their house allegedly caused by defects in the fan. The in court testimony of an independent insurance adjuster working for the plaintiff's insurer provided the only evidence regarding the amount of property damage suffered by the plaintiff. The defendant argued that the insurer adjuster's testimony was insufficient evidence to prove the plaintiff's damage amounts. The Court noted that the evidence presented by the plaintiff through the adjuster whose interest were diametrically opposed to the plaintiff's interest was sufficient because the nature of an insurer is to pay as little as possible on any given claim. The court also stated that "...in light of the adversarial relationship that generally exists between an insurer and a claimant-insured, an inference may properly be drawn that the amount of damage to which the insurer concedes *is, at the very least, the lower boundary of the damage actually suffered.*"

An insurance adjuster who is sufficiently knowledgeable in determining the values of destroyed or lost property may be called as a witness at trial to give testimony on the values of such property. Maris v. H. Crumney, Inc. (1922) 55 Cal.App.573, 577-78; Feder v. Bryson, et al. (1931) 111 Cal.App. 448, 453.

Testimony of an Expert

Expert testimony is used when a person with common experience in a particular subject would have less knowledge on a particular subject than an expert. A person is qualified to testify as an expert if she has acquired a special knowledge of a subject through study or practical experience to a degree that she can give the jury guidance in solving a problem for which their own good judgment and average knowledge is inadequate. The determination of whether a person is an expert on a particular subject is a matter within the sound discretion of the court. If a witness does not possess sufficient familiarity with the subject on which he undertakes to testify as an expert, the court is justified in excluding his testimony.

In property damage cases, expert testimony is frequently used to determine the market value of an item that is no longer in public use or currently considered a rare antique. For example, in U.S. v. Kayne, (1st. Cir.) 90 F.3d 7, some coin dealers were being tried for fraud for selling coins to consumers that were substantially lower in quality and value than the prices they represented. The defendants argued that the jury should not rely on the expert testimony because it did not have to deal with a scientific subject matter but the court disagreed. The court noted that, "...opinions of value are a traditional subject of expert testimony. One could hardly expect a lay jury to form conclusions about such an esoteric subject as the value of rare coins without the help of experts."

Expert testimony can include the testimony of parties involved in a case. A plaintiff's testimony concerning the value of damaged or stolen goods can be considered expert testimony if the plaintiff has extensive experience in evaluating the particular item. Although a witness's lay opinion about an item is usually inadmissible as evidence, courts have made exceptions when the opinion comes from an expert in the particular field. In Frank v. Repp & Mott, (1945) 70 Cal. App.2d 407, the plaintiff testified to the court regarding the price of various items that were stolen from his furniture store by the defendant. The defendant argued the court should disregard the plaintiff's testimony because his testimony concerning the price of the furniture stolen was mere opinions and could not be validated by any evidence but the court disagreed. It noted that the plaintiff was an expert in the field of furniture prices because he had been in the furniture business for over 20 years and he had familiarized himself with the value of the furniture that

was stolen. Although the defendant argued that the plaintiff's testimony regarding the prices of the evidence stolen should not be admissible it failed to provide any evidence to contradict the plaintiff's calculations.

An expert's testimony regarding the market value of a particular item is not the only evidence that a jury can use to make a determination on how much to award a plaintiff. Juries can ignore expert testimony even if the testimony is uncontradicted. A jury, instead of relying on expert testimony to determine the proper amount of damages to award a plaintiff, can consider the nature of the property involved or any other facts within their knowledge in arriving at a verdict provided there are in evidence sufficient facts from which they may draw a legitimate conclusion. Although juries have the option to ignore expert testimony on the market value of rare or obsolete items, most juries rely heavily on the expert opinion of both parties when deciding how much to award a plaintiff for damages caused by the defendant.

ADDITIONAL TOPICS

Restitution for Criminal Acts

Direct victims of crime have a statutory right under California Penal Code section 1202.4 to restitution based on the full amount of their losses, regardless of full or partial reimbursement from other sources except the state Restitution Fund. Restitution is required for direct injury to both persons and property.

For example, the California court in People v. Hove, (1999) 76 Cal.App.4th 1266, found that when a drunk driver causes a car accident that injures another, the drunk driver will be responsible for paying restitution to the victim for the damages to the car and to the persons injured. This includes medical expenses despite the fact that the victim's medical expenses were covered by their insurance provider or Medicare.

An insured can also receive restitution for payment of their insurance deductible. This was the case in In re Brittany L., 2002 WL 1272848 (Cal.App.2d). There a homeowner's house was "egged" by a juvenile and the court order the juvenile defendant to repay the homeowner the \$500 deductible paid to his insurer. The insurer was not entitled to this restitution in subrogation.

According to the seminal case of People v. Birkett, (1999) 21 Cal.4th 226, the insurer of a victim of a criminal act generally does not have a right to any of the mandatory restitutionary award paid to the victim. The key to restitution awards is who is the "direct crime victim." In the case of a criminal act against an insured, the insurer is not a "direct" victim, but an indirect victim, and therefore is not entitled to any portion of the award. Thus, if the insurer has paid on a claim to the victim of a crime, the insurer has no right to be reimbursed when the insured receives a restitution award.

It is possible, however, for an insurer to receive restitution if it was the direct victim of the crime. For example, in a case such as People v. O'Casey, (2001) 88 Cal.App.4th 967, when an employee makes a fraudulent worker's compensation claim, the insurer is the direct victim of

the crime, and is thereby entitled to restitution. Also, where a criminal purposely caused minor car accidents and filed the fraudulent claims with the victim's insurer, the insurer was the "victim" for restitution purposes according to the judgment in People v. Moley, (2000) 84 Cal.App.4th 257. Thus, an insurer is entitled to a restitution award only if it is the "direct victim" of a crime.

Another typical example is an embezzlement scenario. If an employee embezzles from his company and is found criminally culpable the company is entitled to restitution from the employee. If the company has insurance for employee misconduct and is reimbursed under that policy they, the company, are still entitled to restitution. The insurance company can then subrogate what they paid under the policy through the company.

Restitution awards are treated as "civil judgments" for the purposes of execution. Criminal restitution awards are usually not covered by insurance because the criminal act was "willful" and therefore uninsurable under California Insurance Code Section 533. Accordingly, recovery on restitution awards can be extremely difficult.

The Economic Loss Doctrine

A new dump truck's brakes fail when it is parked and the truck rolls into a guard-rail. The truck is "in the shop" for repairs for three weeks. Can the truck's owner recover for his lost profit while the truck is being repaired? As a general rule, no. Recovery of such lost profits is barred by the "economic loss doctrine". This judicially crafted doctrine prohibits tort recovery for economic loss, generally defined as a loss resulting from product failure when there is no personal injury or damage to "other property".

Typically, the economic loss doctrine arises from product liability cases where the "injury" is limited to the product itself. East River Steamship Corporation v. Transamerica Delaval, Inc., 476 U.S. 858 (1986). In such cases, to recover for "economic losses," including damages for diminution or inadequate value, cost to repair or replacement of the defective product or consequent loss of use or profits, plaintiffs are limited to contract remedies. The policy behind the rule is that the loss of the value of a product that suffers physical harm is very much like the loss of the value of a product that does not work properly or at all. The complaining party has simply lost the benefit of its contractual bargain, and thus, "contract law, and the law of warranty in particular," is the appropriate remedy. Id. at 872-873.

According to the United States Supreme Court in East River, a plaintiff cannot recover for either the physical damage a defective product causes to the product itself, or those incidental or consequential damages flowing from damage to the product itself, i.e., lost profits, and cost of repair/replacement. A plaintiff can recover in tort for damage other than the product which the manufacturer placed in the stream of commerce and which was purchased by the initial user. For example, a large oven used in the manufacture of clay pots malfunctions, destroying itself and the plant it occupies. Under this scenario, damages caused by the malfunctioning oven (loss of plant, loss of profits, etc.) would not be subject to the economic loss doctrine. A majority of jurisdictions have adopted East River and prohibit tort recovery for economic damages where there is no personal injury or damage to property "other than the component that was the subject of the sale." See, *W. Dudley McCarter, The Economic Loss Doctrine in Construction Litigation.*

Recent Trends

A. RESTATEMENT OF TORTS

The American Law Institute adopted a new element of the Restatement 3d of Torts in 1997, entitled *Products Liability*. In restating the law of products liability after more than a quarter of a century, the Institute had to respond to many questions left unanswered, including those related to the economic loss doctrine. Under Restatement 3d of Torts: Products Liability, Section 21, the Institute provided that harm to persons or property subject to tort recovery may include economic loss, but only when one of the following is present:

- (1) Harm to the plaintiff's person;
- (2) Harm to the person of another when harm to the other interferes with an interest of the plaintiff protected by tort law;
- (3) Harm to the plaintiff's property other than the defective product itself.

Comment A to Section 21, provides the following rationale for the exception:

“First, products liability law lies at the boundary between tort and contract. Some categories of loss, including those often referred to as ‘pure economic loss’ are more appropriately assigned to contract law and the remedies set forth in Articles 2, and 2A of the Uniform Commercial Code. When a code governs a claim, its provisions regarding such issues as statute of limitation, privity, notice of claim, and disclaimer ordinarily govern the litigation. Second, some forms of economic loss have traditionally been excluded from the realm of tort law even when the plaintiff has no contractual remedy for a claim.”

B. MIDWEST

Beginning with the 1992 Michigan Supreme Court decision of Neibarger v. Universal Cooperatives, Inc. 439 Mich. 512, 486 N.W. 2d 612 (1992), a growing number of courts have used the economic loss doctrine to prohibit tort recovery for both losses to the product itself and “other property,” where the damage to the “other property” was foreseeable at the time of contracting.

In most instances where the courts have significantly narrowed the “other property” exception to the economic loss doctrine, there is an understandable connection between the defective product and the “other property” which permits an inference that the damage to the “other property” was within the “contemplation” of the parties at the time of contracting. For example, at the time of contracting for the construction of a plant, it is within the contemplation of the parties that if the plant collapses, the equipment and goods stored in the plant will be damaged. See, e.g., Crosica Co-Op Ass’n v. Behlen Manufacturing Co., 967 F. Supp. 382(D.S.D. 1997).

Despite Michigan’s harsh application of the economic loss doctrine, and the growing number of courts in the Midwest adopting Michigan’s position, there are ways to avoid application of the doctrine. For example, under Michigan law, the economic loss doctrine does not apply if: (1) the contract is for services as opposed to a sale of goods; (2) there exists the potential for serious injury or death; and (3) plaintiff is a consumer as opposed to a commercial entity.

C. MID-ATLANTIC STATES

The Pennsylvania Supreme Court has yet to address the economic loss doctrine, and as such, the status of the economic loss doctrine is still in question. However, the federal courts applying Pennsylvania law, and lower Pennsylvania state courts, have adopted a form of the economic loss doctrine in line with East River, where a plaintiff is prohibited from recovery in tort for economic losses which do not result in physical injury or damage to other property.

The New Jersey Supreme Court has recently held that the doctrine precludes both individual consumers and commercial entities from recovering in tort for economic losses which do not result in personal injury or damage to other property.

In 1995, the New York Court of Appeals, upon review of a question certified by the United States Court of Appeals for the Second Circuit, adopted the East River approach to the economic loss doctrine. Thus, under New York law, the tort recovery for economic loss is prohibited where there is no physical injury or damage to other property.

D. THE WEST

The economic loss doctrine, adopted by the California Supreme Court in Seely v. White Motor Company (1965) 63 Cal.2d 9, held a manufacturer may be liable in tort (strict

liability and negligence) for physical injuries to persons or property, but not for purely economic loss arising from a defective product. In California, economic loss includes lost profits, loss of prospective clients, repair expenses and lost earnings. Pisano v. American Leasing 146 Cal.App.3d 194 (1983). The California Supreme Court has recently extended the doctrine into the construction defect realm holding that the economic loss doctrine precludes recovery for the loss of repairs for defects which have yet to cause actual damages. Aas vs. Superior Court of San Diego County [2000] 24 Cal.4th 627. Recently, the California Legislature enacted SB800, the *Construction Defect Act*, which allows consumers the right to sue for prospective damage, thus avoiding the harsh preclusions of Aase. The exact extent of SB800 has yet to meet challenge in the Courts and thus the apparent conflict with Aase and SB800 is presently unresolved. Notwithstanding Aase and the newly enacted SB800, if a component of the home causes damage to other portions of the home the economic loss doctrine does not apply. Stearman vs. Centex Homes 78 Cal.App.4th 611 [2000].

Arizona courts follow the rules set forth in Salt River Project v. Westinghouse, 694 P.2d 198 (Ariz. 1984) and weigh three factors to determine whether a plaintiff can recover in tort for economic loss. If these elements are present:

- (1) Product posed an unreasonable danger to those who used it;
- (2) Loss must be from a sudden accident, such as violence, fire or collision;
- (3) Plaintiff can recover economic losses via tort law channels.

A plaintiff in Nevada may not recover in negligence or strict products liability for economic loss absent privity of contract or an injury to person or other property. Central Bit Supply v. Waldrop Drilling & Pump, 717 P.2d 35 (Nev. 1986).

E. PACIFIC NORTHWEST

The Washington Supreme Court in Washington Water & Power Company v. Graybar Electric Co. 774 P.2d 1199 (1989), held that the Washington Product Liability Act did not provide a cause of action for a claim of purely economic loss except where the product defect creates a “risk of harm.” A claim falling within this exception may be brought under the Product Liability Act. The court analyzed two tests to determine if the product created a “risk of harm” (1) the sudden and dangerous test, and (2) the evaluative approach, but declined to adopt either because the issue was moot.

In a subsequent case, Touchet Valley v. Opp & Seibold Construction (1992) 831 P.2d 724 (1992), the Washington Supreme Court discussed the exception and the two tests suggesting that under the “sudden and dangerous test,” if the failure is the result of a sudden and dangerous event, it is actionable under tort law principles. The evaluative approach proceeds on the theory that a product user should not have to suffer a calamitous event before earning his remedy in tort. This approach examines interrelated factors such as the nature of the defect, the type of risk and the manner in which the injury arose. Id. at 733.

The Oregon Supreme Court in Russell v. Ford Motor Co. 575 P.2d at 1383 (1978), held that “the loss must be a consequence of the kind of danger and occurred under the kind of circumstances, ‘accidental’ or not, that made the condition of the product a basis for strict liability” in order for a loss to fall outside the economic loss doctrine. Id. at 595. Such losses are to be distinguished from losses “due only to the poor performance or the reduced resale value of a defective, even dangerously defective product.” Applying this new rule to plaintiff’s strict product liability claim for damages to his truck incurred when a defective weld in an axle housing caused him to lose control of the vehicle and hit a rock pile, the court found that plaintiff’s claim sounded in products liability because the defect was “man-endangering” and the damages occurred in precisely the situation that made the product dangerous.

F. SOUTHEAST

Generally, the economic loss rule bars a tort claim for purely economic losses from an alleged product defect that does not damage other property in Alabama, Florida, Georgia, Mississippi and South Carolina. North Carolina does not have a well-defined rule but it appears that a party cannot bring a products liability claim under a negligence or intentional tort theory where it would be governed by the UCC or contract law for damages where the product damages itself or produces other intangible economic losses. In Virginia, however, case law holds that the economic loss rule does not bar a negligence claim so long as there is privity of contract between the parties.

G. COMPONENT PART EXCEPTION TO ECONOMIC LOSS DOCTRINE

Can a subrogating carrier recover under a strict products liability theory against a component part manufacturer whose component part caused damage/destroyed the manufacturing system to which it was incorporated?

Answer:

Generally, Yes.

A component part manufacturer will be held strictly liable for a defective part if the defect is not the result of a substantial change in later processing of the product. The economic loss doctrine would not apply in those states recognizing damage to “other property” because the manufacturing system to which the component part was incorporated would be considered “other property.” The California Court of Appeals Fourth Appellate District, most recently attempted to elucidate this issue in Stearman v. Centex Homes 78 Cal.App.4th 611 (2000).

Stearman arose in a construction defect context. The gravamen of the underlying case was that defective construction of a tract home caused severe slab movement and deformation. Extensive cracks ultimately manifested themselves throughout the home’s interior and exterior as a result of those defects.

The primary issue on appeal was whether a strict liability cause of action was appropriate when a defect in one component part of the home caused damage to other component parts of the residence without damaging persons or property separate from the structure. Relying heavily on the landmark decision in Seely v. White Motor Co. (1965) 63 Cal.2d 9. Centex Homes contended that a strict liability cause of action was barred by the “economic loss rule” since the subject damage involved nothing more than “injury to the product (home) itself.” The Stearman Court rejected that argument, holding that strict liability was applicable since defects in the home had caused physical damage to the property (i.e., other component parts of the house).

Interest Rules

Amount, Timing and Authority

Under the California Civil Code § 3287, “[e]very person who is entitled to recover damages certain, or capable of being made certain by calculation” can also recover interest, which is calculated from the date she gains the right to recover. Prejudgment interest should be computed from the earliest date that the defendant knew, or from the available information could have reasonably computed the amount owed on plaintiff’s claim. Ferrellgas, Inc. v. American Premier Underwriters, Inc. (1999) 79 F.Supp.2d 1160. Accordingly, the test for the recovery of prejudgment interest is whether the defendant *has actual notice* the amount of damages owed the plaintiff, or could have computed that amount from reasonably available information. KGM Harvesting Co. v. Fresh Network (1995) 36 CA4th 376.

Estimates of an expert are appropriate in determining damages for the purposes of prejudgment interest. Levy-Zenner Co. v. Southern Pacific Transportation Co. (1977) 74 CA3d 762.

“Damages are deemed certain or capable of being made certain within the provisions of § 3287 where there is essentially no dispute between the parties concerning the basis of computation of damages if any are recoverable but where their dispute centers on the issue of liability giving rise to damage.” Esgro Central, Inc. v. General Ins. Co. of America (1971) 20 CA3d 1054.

California Constitution Article XV § 1 (usury) sets an **annual interest rate of 7 percent** on “the loan or forbearance of any money, goods, or things in action, **or on accounts after demand.**” However, parties can agree to a different interest rate in a written contract; under California’s usury law, this rate may not exceed the higher of 10 percent per year, or 5 percent per year plus the prevailing Federal Reserve rate on 25th day of the month.

Attorney's Fees

Under California Code of Civil Procedure section 1033.5, subdivision (a)(10), attorney's fees, when authorized by contract, statute, or law, are recoverable as an element of costs, not as an element of damages. The prevailing party in any action or proceeding is entitled to a recovery of costs as a matter of right under Code of Civil Procedure section 1032(b). Also, Code of Civil Procedure § 1021 provides that, unless specifically provided for by statute, the measure and mode of compensation of attorneys is controlled by the agreement, express or implied, of the parties. Thus, in the absence of an express statute or contractual provision, attorney fees are generally paid by the party employing the attorney.

Statute

There are many statutes providing for awards of attorney's fees. Some statutes authorize recovery of attorney's fees in particular types of litigation, such as retail installment contracts, condemnation proceedings, inverse condemnation proceedings, and partition proceedings.

Inverse Condemnation

California Code of Civil Procedure section 1036 allows a successful inverse condemnation plaintiff to recover reasonable costs, disbursements, and expenses, including reasonable attorney, appraisal, and engineering fees, actually incurred because of such proceeding. Prejudgment interest is awarded in inverse condemnation cases to provide the constitutionally required "just compensation" to persons whose property has been taken or damaged.

For instance, if an insured's property is flooded due to the state damming a river, the insured has a claim for inverse condemnation against the state. Should the insurer pay on the insured's property policy, the insurer would have a subrogation action against the state. In such a subrogation action the insurer has no greater or less rights than the insured would have. Thus, if an insurer is successful in subrogating against the state in the above scenario, attorney's fees would be awarded to the insurer as well as prejudgment interest.

Contract

Provisions for attorney's fees may be included in a contract and such provisions will be applicable in a legal action instigated by either party to the contract. The purpose of upholding an attorney's fees provision in a contract is to allow the recovery of the full amount due to the plaintiff without diminishing that amount by attorney's fees.

A standard clause in a contract providing for the recovery of attorney's fees provides indemnity for fees at trial as well as on appeal. Although most awards of attorney's fees have rested on contract language expressly providing for such fees in the event of suit to enforce the contract, the contract may impliedly as well as expressly permit their recovery. For example, in Citizens Suburban Co. v. Rosemont Development Co., (1966) 244 Cal.App.2d 666, the court found that the phrase "costs and expenses" in an indemnity clause of a contract impliedly authorized an award of attorney's fees as damages though there was no express provision for attorney's fees.

Of course, though a court may find that an attorney's fee provision is implied, if such a provision is desired, it is always best to use language that is free from ambiguity. Language used in a contract providing "should legal action be necessary to enforce or interpret any phase of this contract the losing party therein shall pay to the prevailing party reasonable attorney's fees" was ruled to be a clear allowance for attorney fees in Heidt v. Miller Heating & Air Conditioning Co., (1969) 271 Cal.App.2d 135.

Parties may validly claim an award of attorney's fees even though the lawsuit brought by one of the parties is not based on breach of the that contract. In Allstate Ins. Co. v. Loo, (1996) 46 Cal.App.4th 1794, an insurer attempted to subrogate against a landlord based on the insurer's payment for fire damage to its insured tenant's personal property. The lease between the tenant/insured and the landlord provided that that the prevailing party was entitled to attorney fees "in any legal action . . . to enforce the terms hereof or relating to the demised premises." The insurer's claim against the landlord was, however, for negligence, failure to disclose a latent defect, and breach of an implied warranty of habitability. Of these claims, only breach of an implied warranty is a claim based on the lease contract. The court found that it did not matter if

the lawsuit was filed directly in regards to the lease contract. Instead the court opined that the only question is the intent of the parties. In this case it was clear that the intent of the parties was to award attorney's fees to the prevailing party in *any* legal action . . . *relating* to the premises. Because the landlord was successful in defending the subrogation action, the insurer was forced to pay the attorney's fees of the landlord.

Finally, in California all contractual attorneys fees are reciprocal, despite any written expressions to the contrary. *California Civil Code Section 1717*. There are also restrictions on contractual attorneys' fees limited "to certain claims." In general, such limitations are valid only if both parties *were represented by counsel* at the time of entering into the agreement. *California Civil Code Section 1717*.

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