

Ordered Not Published Previously published at: 24 Cal.App.4th 1632(Cal. Rules of Court, Rules 976, 977, 979)

(Cite as: 30 Cal.Rptr.2d 163)

[Ron Leaf](#), Law Offices of Martin & Leaf, San Mateo, for respondents, Robert and Nita Kyle.

Court of Appeal, First District, Division 5, California.

Robert H. KYLE and Nita F. Kyle, Plaintiffs and Respondents,

v.

UNITED SERVICES AUTOMOBILE ASSOCIATION, Defendant and Appellant.

No. A057408.

May 16, 1994.

Certified for Partial Publication. [\[FN*\]](#)

[FN*](#) Pursuant to [rules 976](#) and [976.1, California Rules of Court](#), this opinion is certified for publication except for parts III and IV.

Review Denied Aug. 11, 1994. [\[FN**\]](#)

[FN**](#) In denying review, the Supreme Court ordered that the opinion be not officially published. (See California Rules of Court Rules 976 and 977.)

Insurer appealed from judgment of the Superior Court, San Mateo County, No. 323725, Clarence B. Knight, J., which entered judgment on jury verdict in favor of insureds in action for bad faith. The Court of Appeal, Haning, J., held that: (1) court could consider challenge to sufficiency of evidence even though insurer did not object to legal conclusions and other testimony of insurance adjuster; (2) evidence did not establish that insurer acted in bad faith; (3) insureds were entitled to recover as damages for breach of contract the cost of stabilizing their insured home.

Affirmed in part and reversed in part.

***165** [Pamela W. Levin](#), Michael F. Scully, Thornton, Taylor, Downs, Becker, Tolson & Doherty, San Francisco, [Michael J. Brady](#), [Susan H. Handelman](#), Ropers, Majeski, Kohn, Bentley, Wagner & Kane, Redwood City, for appellant, USAA.

[HANING](#), Associate Justice.

Appellant United Services Automobile Association appeals a judgment by jury trial in favor of its insureds, respondents Robert H. and Nita F. Kyle, in their action for breach of contract, bad faith and violations of [Insurance Code section 790.03](#) (hereafter, unreferenced statutes are to the Insurance Code). [\[FN1\]](#) Appellant contends the trial court committed instructional error, erred in refusing to allow it to amend its answer, and that the finding of bad faith is not supported by substantial evidence.

[FN1.](#) This case was filed prior to the Supreme Court's decision in [Moradi-Shalal v. Fireman's Fund Ins. Companies \(1988\) 46 Cal.3d 287, 250 Cal.Rptr. 116, 758 P.2d 58](#), which held that a violation of [section 790.03](#) does not create a private cause of action under the Unfair Practices Act. ([Ins.Code, § 790](#), et seq.) [Moradi-Shalal](#) was a third-party case, but its elimination of private causes of action under the Unfair Practices Act applies equally to first-party cases. ([Zephyr Park v. Superior Court \(1989\) 213 Cal.App.3d 833,262Cal.Rptr.106.](#)) [Moradi-Shalal](#) further held that it did not operate retrospectively to bar cases filed prior to its finality. (See also, [Rangel v. Interinsurance Exchange \(1992\) 4 Cal.4th 1, 6, fn. 4, 14 Cal.Rptr.2d 783, 842 P.2d 82.](#))

The specific claims of bad faith asserted in this action under [section 790.03](#) are coextensive with those duties inherent in the implied covenant of good faith and fair dealing. Consequently, our discussion of bad faith includes both contractually and statutorily based claims.

FACTS

Respondents' Portola Valley home was built in 1958. A converted garage and laundry room were added between May 1965 and June 1973. Respondents purchased and moved into their house in July 1973. Appellant had insured the property under an all-***166** risk homeowner's policy since respondents purchased

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the property.

By 1975 respondents noticed a slope in the kitchen floor. In 1980 when the kitchen floor linoleum was changed, the flooring contractor noticed the slope and informed respondents it would involve major work to level the floor. Specifically, the contractor said he would have to remove the existing boards and replace the imperfect ones at a cost of about \$6,000. He did not suggest that the floor was moving and needed stabilizing.

In 1981 cracks in the patio and pool area became more noticeable. In 1983 the linoleum cracked between the kitchen and laundry room. In December 1983 respondents had the property appraised in conjunction with efforts to refinance it. The appraisal did not indicate any problems with the property. At about the same time, respondents received a realtor's market analysis of the property prepared in conjunction with its possible sale. The report stated, in part: "Regarding your liability, and our major concern, we were also unanimous ... the sloping floors in the kitchen and laundry area and the effect it will have on the salability of the house. You have lived there happily for ten years and grown used to the sloping, and may not even give it a thought. [¶] In those ten years, geological concerns, consumer concerns, real estate regulations have changed. A seller avoids so many problems by having the corrective work done prior to listing the property. And that is what we all recommend to you." The report recommended two firms that performed foundation corrections and suggested that by contacting them respondents would "accurately learn: [] the cause and extent of your sloping [and] how it can be corrected."

In July 1986 respondents noticed a crack in the master bathroom tile and in September 1986 observed screws protruding from the laundry room ceiling. They regarded all the defective conditions as normal wear and tear and not an insurable damage, until September 1986 when they met with a contractor, Philip Hartman. Hartman noted that the problems were probably due to slippage of the hill upon which the house was located. He suggested that respondents contact their insurer, which they did. Appellant assigned the investigation of respondents' claim to Robert Byrne, an independent insurance adjuster. On September 11, 1986 Byrne inspected the property and took a statement from Nita Kyle. Byrne's report to appellant stated that "[respondents] would make good to excellent witnesses on their own

behalf."

Byrne retained a geotechnical engineer, Dr. Rexford Upp, to determine the cause of the damage. Upp estimated that the converted garage and laundry room were added sometime between May 1965 and June 1973. The house showed evidence of foundation movement, indicated by the floor slope. Upp concluded that "the distress to the house and pool is the result of the settlement and lateral movement of the fill placed before the addition of the converted garage and the laundry room." Appellant provided respondents with a copy of Upp's report and a transcript of Nita Kyle's statement.

The HO-3 policy in effect specifically excluded loss caused by "Earth Movement, meaning ... landslide; mudflow; earth sinking, rising or shifting...." It also excluded loss caused by "Water Damage[.]" including surface water and "water below the surface of the ground," and "Faulty, inadequate or defective: [¶] (1) planning, zoning, development, surveying, siting; [¶] (2) design, specifications, workmanship, repair, construction, renovation, remodeling, grading, compaction; [FN[2]] [¶] (3) materials used in repair, construction, renovation or remodeling; or [¶] (4) maintenance [.]" and excluded coverage for "settling, cracking, shrinking, bulging or expansion." The policy states: "Suit Against Us. No action can be brought unless the policy provisions have been complied with and the action is started within one year after the date of loss."

FN2. This third-party negligence exclusion was added to respondents' policy in 1985.

In January 1987 appellant sent respondents a written denial of their claim. [\[FN3\]](#) It *167 informed them that the claimed damage was caused by settlement of the foundation, movement of fill soils and improper construction, which, it contended, were excluded by the policy. Appellant also determined that because respondents became aware of a problem with their kitchen floor in 1980, the claim was barred by the one-year contractual limitation period.

[FN3.](#) The denial letter states: "Dear Mr. and Mrs. Kyle: [¶] We have concluded our investigation into your loss, and our investigation indicates that the damages sustained are caused by settlement of the

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foundation, the movement of fill soils, and improper construction. Your Homeowner's policy, HO-3 (4-84 Edition), contains specific exclusions for these perils. The specific exclusions can be found on pages five and seven of your policy. On page five, please refer to 2. f. (6). On page seven, the applicable policy language is 1. b., 1. c., and 2. c. [¶] As you indicated in your recorded statement, you were advised by a flooring contractor in 1980 that you had a problem with your kitchen floor. The policies in force during the time that these damages became apparent also contained exclusionary language for earth movement, and settling and cracking. These policies require that any action under the policy be initiated within one year after the date of loss. Accordingly, coverage would not be available under these policies. [¶] There is also a four-year Statute of Limitation in the State of California which is applicable to this loss. [¶] If you have any questions concerning this letter or your policy language, or if there is any additional information which you feel should be considered in the presentation of your claim, please do not hesitate to contact me. [¶] Very truly yours, [¶] Stephen Ringer [¶] Property Claims Examiner [¶] Western Region[.]"

Respondents filed this action in October 1987, alleging breach of contract, breach of the implied covenant of good faith and fair dealing, breach of fiduciary duties, fraud and Insurance Code violations, seeking both compensatory and punitive damages. The case was tried in January 1992.

Respondents' expert, Joseph Michelucci, testified that the predominant cause of the damage to respondents' house was inadequately compacted fill under the added-on garage and laundry room. He also opined that the fill compaction was below construction industry standards in existence at the time the house was constructed. He noted that other contributing causes were the soil's moisture content, the weight of the house, and perhaps earthquakes. The fill has moved approximately one quarter inch per year since the addition was built. At the time respondents purchased the house it was not stable, due to the moving fill.

Appellant's expert, Charles Allen, testified that the damage to respondents' house was mainly caused by earth movement due to soil moisture from rain water. He agreed that part of the fill was not compacted correctly, but opined that inadequate compaction did not cause the house to move until rain water and gravity acted upon the soil to make it move. Thus, without water acting on it, inadequate compaction would not have caused the earth movement or damage to the house.

Dr. Upp testified that the predominant cause of the damage was movement of the fill caused mainly by gravity. He had no opinion as to whether the fill was "constructed negligently."

Appellant's motion for nonsuit was denied and by special verdict the jury found appellant liable for breach of contract, bad faith and Insurance Code violations. It found that September 5, 1986 was the "date of loss or manifestation of loss for [respondents'] claim[.]" and that negligence (improperly compacted fill) was the predominant cause of respondents' loss. The jury awarded respondents both compensatory and punitive damages.

DISCUSSION

I

Appellant contends its decision to deny benefits was reasonably made as a matter of law, thus barring tort liability. In essence, appellant is asserting a lack of substantial evidence to support respondents' claims of bad faith and fraud. In particular, it argues that its denial of respondents' claim was a reasonable decision based on its determination that (1) the claim was barred by the policy's one-year limitation provision, and (2) there was no coverage under the policy's earth movement and water exclusions, which it believed constituted the predominant cause of the loss.

[1][2][3] In the broad field of insurance law, the phrase "bad faith" has evolved as shorthand legal jargon to describe a breach of the implied covenant of good faith and fair dealing *168 inherent in every contract of insurance. Its significance in first-party insurance claim cases is that violation of the covenant by an insurer is a tort and thus entitles the insured to tort damages. ([Gruenberg v. Aetna Ins. Co. \(1973\) 9 Cal.3d 566, 581, 108 Cal.Rptr. 480, 510 P.2d 1032](#); [Crisci v. Security Ins. Co. \(1967\) 66 Cal.2d 425, 433, 58 Cal.Rptr. 13, 426 P.2d 173](#); [Comunale v. Traders](#)

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& General Ins. Co. (1958) 50 Cal.2d 654, 663, 328 P.2d 198. Although "good faith" has not attained a precise or all-encompassing definition (see, e.g., Walbrook Ins. Co. v. Liberty Mutual Ins. Co. (1992) 5 Cal.App.4th 1445, 1455, 7 Cal.Rptr.2d 513), it is well established that the covenant of good faith and fair dealing requires insurers to exert reasonable-effort attempts to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear.

[4][5] In cases such as this, where the insured is suing on a claim the insurer has denied, the test of bad faith is whether the denial of the claim was unreasonable (Gourley v. State Farm Mut. Auto. Ins. Co. (1991) 53 Cal.3d 121, 127, 3 Cal.Rptr.2d 666, 822 P.2d 374; Opsal v. United Services Auto. Assn. (1991) 2 Cal.App.4th 1197, 1205, 10 Cal.Rptr.2d 352), or without proper cause. (Opsal v. United Services Auto. Assn., supra, at p. 1205, 10 Cal.Rptr.2d 352; California Shoppers, Inc. v. Royal Globe Ins. Co. (1985) 175 Cal.App.3d 1, 54-55, 221 Cal.Rptr. 171.) An erroneous, but reasonable belief that the claim is barred under the policy or as a matter of law does not of itself constitute bad faith, i.e., create a tort liability. (Opsal v. United Services Auto. Assn., supra, 2 Cal.App.4th at pp. 1205-1206, 10 Cal.Rptr.2d 352; see also Austero v. National Cas. Co. (1978) 84 Cal.App.3d 1, 32, 35-36, 148 Cal.Rptr. 653.)

[6] The determination of whether an insurer's denial of a claim constituted bad faith is measured against the background of the totality of the circumstances existing at the time the insurer's disputed conduct occurred. (Walbrook Ins. Co. v. Liberty Mutual Ins. Co., supra, 5 Cal.App.4th at pp. 1455-1456, 7 Cal.Rptr.2d 513.) Thus, an assessment of appellant's conduct in denying respondents' claim in this case requires analysis of the terms of the policy under which the claim was made, the law in existence during the period the claim accrued and was denied, and whether appellant's interpretation of the law and the policy provisions were reasonable.

Appellant contends its denial of respondents' claim was reasonable for the two basic reasons set forth in its denial letter (*ante*, at p. 166, fn. 3): Its reasonable belief that (1) the claim was not timely made within the period required by the policy, and (2) the loss was predominately caused by an excluded peril, i.e., a peril for which respondents were not insured under the policy.

It is not subject to reasonable dispute that respondents' loss was caused by at least two perils. The statutory foundation for insurance coverage in cases of concurrent causation is contained in sections 530 and 532, which state, respectively: "An insurer is liable for loss of which a peril insured against was the proximate cause, although a peril not contemplated by the contract may have been a remote cause of the loss; but he is not liable for a loss of which the peril insured against was only a remote cause." (§ 530.)

"If a peril is specially excepted in a contract of insurance and there is a loss which would not have occurred but for such peril, such loss is thereby excepted even though the immediate cause of the loss was a peril which was not excepted." (§ 532.)

Sabella v. Wisler (1963) 59 Cal.2d 21, 27 Cal.Rptr. 689, 377 P.2d 889, analyzed sections 530 and 532 and explained that in first-party cases involving concurrent causation by both covered and excluded perils, the "efficient proximate cause" determines coverage: "[I]n determining whether a loss is within an exception in a policy, where there is a concurrence of different causes, the efficient cause--the one that sets others in motion--is the cause to which the loss is to be attributed, though the other causes may follow it, and operate more immediately in producing the disaster." [Citation.] (*Id.*, at pp. 31-32, 27 Cal.Rptr. 689, 377 P.2d 889, quoting 6 Couch (1930) Insurance, § 1466.)

In Sabella, a contractor built the insured's house on uncompacted fill and negligently installed a sewer line. The sewer line ruptured, *169 causing water to saturate the filled ground surrounding the house, thereby causing subsidence. The negligent installation of the sewer line was a covered peril under the insureds' homeowners policy, but subsidence was not. When their claim was denied, the insureds sued their insurer for property loss. The Supreme Court held that even though the damage to the house would not have occurred "but for" the excluded peril of subsidence, the loss was covered because the escaping water was the "proximate cause" under sections 530 and 532. The Court reasoned that to construe section 530 as exempting coverage whenever the loss would not have occurred but for the operation of an excluded cause would be contrary to section 530, which renders an insurer liable for coverage when the peril insured against proximately causes the loss.

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Notwithstanding *Sabella's* establishment of the concurrent-causation rule for first-party cases in 1963, some confusion arose following *State Farm Mut. Auto. Ins. Co. v. Partridge* (1973) 10 Cal.3d 94, 109 Cal.Rptr. 811, 514 P.2d 123. In *Partridge* a third party was injured while riding in the insured's car over rough terrain off the road, when a pistol the insured was holding as he drove, accidentally fired as the car struck a bump. The insured had modified the pistol to give it a "hair trigger" action, which caused it to discharge. The insured had liability coverage through an automobile policy and a homeowners policy, but the homeowners policy excluded coverage for injuries arising out of the use of a motor vehicle. (*Id.*, at p. 97, 109 Cal.Rptr. 811, 514 P.2d 123.) The Supreme Court rejected the homeowner carrier's attempt to deny coverage under that policy. The Court concluded that both negligent driving, which was covered under the auto policy, and the modification of the pistol, which constituted negligence under the homeowners policy, contributed to the injury. (*Id.*, at pp. 105-106, 109 Cal.Rptr. 811, 514 P.2d 123.) *Partridge* held generally that coverage under *aliability* policy is available if *any* covered risk contributed to the third party's injury, regardless of other concurrent causes. (*Id.*, at p. 102, 109 Cal.Rptr. 811, 514 P.2d 123.)

Although *Partridge* itself did not address the issue, several cases decided later declined to recognize a first-party/third-party distinction and applied *Partridge's* concurrent-causation analysis in first-party property insurance cases. (See *Farmers Ins. Exchange v. Adams* (1985) 170 Cal.App.3d 712, 722, 216 Cal.Rptr. 287; *Premier Ins. Co. v. Welch* (1983) 140 Cal.App.3d 720, 727-728, 189 Cal.Rptr. 657; *Safeco Ins. Co. of America v. Guyton* (9th Cir.1982) 692 F.2d 551, 554-555.)

The confusion generated by *Partridge* was clarified in *Garvey v. State Farm Fire & Casualty Co.* (1989) 48 Cal.3d 395, 257 Cal.Rptr. 292, 770 P.2d 704. *Garvey* involved a claim under an "all-risks" homeowner's insurance policy for damage which occurred when a house addition began to pull away from the main structure. Although the policy excluded coverage for damage due to settling or earth movement, the insureds claimed the loss was covered because negligent construction, which was not specifically excluded, was a concurrent cause. (*Id.*, at pp. 399-401, 257 Cal.Rptr. 292, 770 P.2d 704.) *Garvey* reaffirmed *Sabella's* analysis: "... *Sabella* ... sets forth a workable rule of coverage that provides a fair result within the reasonable expectations of both

the insured and the insurer whenever there exists a causal or dependent relationship between covered and excluded perils. In multiple cause cases, a proximate cause analysis, focusing on the efficient proximate cause, could be employed to determine whether or not the insured was covered for the loss under the property portion of the homeowner's insurance policy." (*Id.*, at p. 404, 257 Cal.Rptr. 292, 770 P.2d 704.) (*Garvey* also referred to the "efficient proximate cause" as the "predominant cause" [*id.*, at p. 403, 257 Cal.Rptr. 292, 770 P.2d 704] which is the phrase used by the parties and the trial court here.) *Garvey* further held that third-party negligence is a covered risk unless specifically excluded by the policy. (*Id.*, at p. 408, 257 Cal.Rptr. 292, 770 P.2d 704.)

In addition to the foregoing causation decisions, in September 1990 *Davis v. United Services Auto Assn.* (1990) 223 Cal.App.3d 1322, 1332-1333, 273 Cal.Rptr. 224, held that *170 United Services Auto Assn. failed to adequately inform its insureds of a change in its renewal policy that excluded coverage for losses resulting from contractors' negligence, thereby rendering the exclusion ineffective. *Davis* involved a claim under an all-risks homeowner's policy due to soil subsidence. The foundation slab was not properly reinforced and the fill soil supporting it was improperly compacted. (*Id.*, at pp. 1331-1332, 273 Cal.Rptr. 224.)

In November 1990 *Prudential-LMI Com. Insurance v. Superior Court* (1990) 51 Cal.3d 674, 274 Cal.Rptr. 387, 798 P.2d 1230, held that in first-party progressive property loss cases, the one-year limitation period begins to run on the date of inception of the loss, defined as "that point in time when appreciable damage occurs and is or should be known to the insured, such that a reasonable insured would be aware that his notification duty under the policy has been triggered." (*Id.*, at p. 687, 274 Cal.Rptr. 387, 798 P.2d 1230.) The Court also held that this limitation period should be equitably tolled from the time the insured files a timely notice, pursuant to policy notice provisions, to the time the insurer issues a formal denial of the claim. (*Id.*, at p. 693, 274 Cal.Rptr. 387, 798 P.2d 1230.)

It is against this backdrop of precedent that this case was tried and we conduct our review. As we previously noted, appellant's initial denial in 1986 of respondents' claim was based on the policy's one-year limitation period and the exclusions for loss due to earth movement, water, and third-party negligence.

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Respondents submitted their bad faith case solely on the testimony of Raymond Charleston, a licensed insurance adjuster and consultant. In reviewing respondents' bad faith case as presented through Charleston, we note that with this witness the parties disregarded the rules of evidence, and Charleston, who is not an attorney, was permitted to state his *personal* opinions on issues of law. Those legal opinions concerned a general overview of insurance law, the legal import of specific cases, and the legally imposed duty owed by appellant to respondents. Charleston's testimony was preceded by a cautionary instruction by the court in response to appellant's request: "... Ladies and gentlemen, the law that applies to this case will be given to the jury by the court, that's me, at the end of the case. We're going through the various legal questions here to get opinions from these witnesses and to determine the knowledge of certain witnesses, et cetera, et cetera. But the law that you are to apply to the case will be given to you by the court at the end of the case."

[7] Charleston is not a party to this case and his conduct and state of mind are not at issue. Consequently, his *personal* opinions of the state of the law and the legal impact of various appellate decisions are irrelevant, even if he were qualified to render such opinions. Although *appellant*'s understanding of the law may be relevant to determine whether its claims practices constituted bad faith, respondents did not purport to elicit Charleston's testimony for the purpose of establishing appellant's corporate state of mind, even assuming Charleston was able to so testify. Rather, the legal opinions Charleston rendered were clearly his own, and were offered to demonstrate that appellant failed to follow the law as he saw it and breached its legal duty to respondents, although on occasion Charleston appeared to testify about what the insurance industry in general believed the law to be during certain time periods.

[8][9][10] Ordinarily, when litigants engage in this sort of evidentiary free-for-all and permit the introduction of evidence which would be inadmissible over objection, they are not in a favorable position to argue insufficiency of the evidence after the fact, either in post-trial motions or on appeal. (3 Witkin, Cal.Evidence (3d ed. 1986) Introduction of Evidence at Trial, § 2012, pp. 1971-1972; *Estate of Silverstein* (1984) 159 Cal.App.3d 221, 225, 205 Cal.Rptr. 294.) However, appellant's claim of error challenges not the admissibility of the

evidence, but its legal sufficiency, and in our review of a claim of insufficiency of the evidence Charleston's personal legal opinions are not entitled to consideration. Issues of law are for the court, especially when they involve a determination of duty. (See, e.g., *171Ann M. v. Pacific Plaza Shopping Center (1993) 6 Cal.4th 666, 678, 25 Cal.Rptr.2d 137, 863 P.2d 207; *Ballard v. Uribe* (1986) 41 Cal.3d 564, 572-573, 224 Cal.Rptr. 664, 715 P.2d 624.)

The gist of Charleston's testimony is that appellant acted in bad faith by (1) relying on the policy's third-party negligence exclusion, (2) relying on the policy's one-year time period for bringing legal action, and (3) relying on *Sabella's* predominant-cause test, and subsequently refusing to accept third-party negligence as the predominant cause of the loss. Ordinarily, whether the insurer has acted unreasonably, and hence in bad faith, is a question of fact for the trier of fact. (*Walbrook Ins. Co. v. Liberty Mutual Ins. Co.*, supra, 5 Cal.App.4th at p. 1454, 7 Cal.Rptr.2d 513.) However, the question is one of law when there are no conflicting inferences and reasonable minds could not differ. (*Ibid.*) In essence, we must determine whether, on the entire record, there is any substantial evidence, contradicted or uncontradicted, which will support the jury's conclusions. (*Kruse v. Bank of America* (1988) 202 Cal.App.3d 38, 51, 248 Cal.Rptr. 217.) To be "substantial," the evidence must be "reasonable in nature, credible, and of solid value; it must actually be "substantial" proof of the essentials which the law requires in a particular case." [*Citations.*] (*Id.*, at pp. 51-52, 248 Cal.Rptr. 217, quoting *Estate of Teed* (1952) 112 Cal.App.2d 638, 644, 247 P.2d 54.)

[11] First, as to the policy's third-party negligence exclusion, Charleston admitted that appellant acted reasonably in relying on this exclusion up to the time when the opinion was announced in *Davis v. United Services Auto Assn.*, supra, 223 Cal.App.3d 1322, 273 Cal.Rptr. 224. He further agreed, as the record reveals, that appellant did not rely on this exclusion to deny respondents' claim after *Davis*. Consequently, the evidence is insufficient to support a bad faith claim on the theory that appellant acted in bad faith by relying on the negligence exclusion.

[12] Second, as to the policy's one-year limitation period, Charleston's testimony was equivocal--during cross-examination he said reasonable minds could differ on all issues; on redirect he contended reasonable minds could not differ over the date of

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inception of the loss. He admitted, however, that respondents' claim was barred if the inception of the loss occurred prior to 1986. Prudential-LMI Com. Insurance v. Superior Court, *supra*, 51 Cal.3d 674, 274 Cal.Rptr. 387, 798 P.2d 1230, held: "The insured's suit on the policy will be deemed timely if it is filed within one year after 'inception of the loss,' defined as that point in time when appreciable damage occurs and is or should be known to the insured, such that a reasonable insured would be aware that his notification duty under the policy has been triggered. To take advantage of the benefits of a delayed discovery rule, however, the insured is required to be diligent in the face of discovered facts. The more substantial or unusual the nature of the damage discovered by the insured (e.g., the greater its deviation from what a reasonable person would consider normal wear and tear), the greater the insured's duty to notify his insurer of the loss promptly and diligently. [Citation.] [¶] Determining when appreciable damage occurs such that a reasonable insured would be on notice of a potentially insured loss is a factual matter for the trier of fact." (*Id.*, at pp. 686- 687, 274 Cal.Rptr. 387, 798 P.2d 1230.)

Respondents moved into their home in 1973. By 1975 they noticed a definite slope in their kitchen floor, and in 1980 they were advised by a flooring contractor that major work was necessary to level it. By 1981 cracks in the patio and pool area became more pronounced, and in 1983 the floor covering cracked between the kitchen and laundry room, i.e., between the original structure and the addition. Also in 1983 they received a real estate appraisal that suggested they contact a contractor to correct foundational problems. For purposes of determining whether respondents were diligent in pursuing their claim, the jury found they were not aware and could not reasonably have been aware that appreciable damage occurred prior to 1986. However, for purposes of determining whether the record supports a finding of bad faith, we conclude that although appellant may have been mistaken, respondents failed to establish that appellant acted *unreasonably* in concluding that the inception of *172 the loss occurred well before 1986. As we stated earlier, a reasonable (although erroneous) belief that a claim is barred does not ipso facto constitute bad faith. (Opsal v. United Services Auto Assn., *supra*, 2 Cal.App.4th at pp. 1205-1206, 10 Cal.Rptr.2d 352.) Even Charleston admitted that a mere mistake in judgment does not constitute bad faith.

[13][14] Finally, Charleston's opinion that appellant acted in bad faith in relying on Sabella's "efficient proximate cause" analysis was based on his opinion that prior to Garvey, most of the insurance industry was applying the Partridge third-party concurrent causation rule. Therefore, he concluded, appellant committed bad faith by refusing to abide by industry custom and standard, even though Garvey subsequently validated appellant's analysis. Charleston concluded it was inappropriate to use "hindsight," i.e., the Garvey decision, to justify appellant's pre-Garvey position. In short Charleston contended that even though appellant's legal analysis was correct, it acted in bad faith by following the law, i.e., ruling on Sabella.

This is a novel approach to liability that finds no support in the law. Industry custom and standard is relevant in tort litigation on the issue of standard of care. (See 1 Witkin, Cal.Evidence (3d ed. 1986) Circumstantial Evidence, § 394, pp. 368-369, and cases cited therein.) However, "the duty of an insurer to deal fairly with its insured is prescribed by law and cannot be delineated entirely by customs of the insurance industry." (Silberg v. California Life Ins. Co. (1974) 11 Cal.3d 452, 462, 113 Cal.Rptr. 711, 521 P.2d 1103; 1 Witkin, *op. cit. supra*, § 394.) If appellant had failed to follow the law, its belief that it was in compliance, and its reliance on custom and practice in the industry, would have been relevant on the issue of bad faith to show state of mind or intent. (See, e.g., Anaheim Bldrs. Supply, Inc. v. Lincoln (1965) 233 Cal.App.2d 400, 412-413, 43 Cal.Rptr. 494; Hanson v. Prudential Ins. of America (9th Cir.1985) 772 F.2d 580, 584.) However, since appellant's analysis of the law accorded with the Supreme Court's earlier pronouncement in Sabella, the fact that a portion of the industry followed a different course is irrelevant. (Silberg v. California Life Ins. Co., *supra*, 11 Cal.3d at p. 462, 113 Cal.Rptr. 711, 521 P.2d 1103.) The ultimate inquiry is whether appellant's conduct conformed to the law. As Garvey pointed out, Sabella announced the correct rule in 1963, and appellant's reliance on Sabella cannot, as a matter of law, constitute bad faith.

[15] In apparent recognition of the weakness of this position, respondents also attack appellant's predominant cause analysis based on Charleston's testimony that reasonable minds could not differ over the fact that negligence was the predominant cause of their loss, and therefore appellant acted in bad faith by denying their claim. The record does not support

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the contention that reasonable minds could not differ. The evidence as to what constituted the predominant cause of the loss was closely balanced. Appellant had substantial evidence from experts that the contractor's negligence in compacting the landfill was too remote, and that the earth movement was caused by surface and subsurface water, both of which were excluded perils along with earth movement itself. The fact that negligence may have been found to be the predominant cause establishes that appellant was mistaken, but not necessarily unreasonable or guilty of bad faith in relying on credible evidence to the contrary. (See California Shoppers, Inc. v. Royal Globe Ins. Co., *supra*, 175 Cal.App.3d at p. 55, 221 Cal.Rptr. 171; Hanson v. Prudential Ins. Co. of America, *supra*, 772 F.2d at p. 584.)

[16][17] To summarize, the evidence is clearly sufficient to support a breach of contract, but not a tort. As we stated earlier in this opinion, to be substantial, evidence must be of ponderable legal significance, reasonable in nature, credible, and of solid value. (Braewood Convalescent Hospital v. Workers' Comp. Appeals Bd. (1983) 34 Cal.3d 159, 164, 193 Cal.Rptr. 157, 666 P.2d 14; People v. Johnson (1980) 26 Cal.3d 557, 576, 162 Cal.Rptr. 431, 606 P.2d 738; Kruse v. Bank of America, *supra*, 202 Cal.App.3d at 51-52, 248 Cal.Rptr. 217; Estate of Teed, *supra*, 112 Cal.App.2d at p. 644, 247 P.2d 54.) The expression of erroneous legal principles and concepts of duty are not of ponderable legal significance, reasonable in nature, credible, *173 nor possessed of solid value. (See, e.g., Zemke v. Workmen's Comp. App. Bd. (1968) 68 Cal.2d 794, 798, 69 Cal.Rptr. 88, 441 P.2d 928.) Consequently, we give them no weight in our search for substantial evidence.

[18] At appellant's request we asked the parties to address this issue more specifically by supplemental briefing. Respondents contend that appellant waived the right to appeal the issue by failing to object at trial. The obvious answer, as we previously stated, is that appellant is contesting not the admissibility of the evidence, but its legal significance. In addition, appellant moved for nonsuit in the trial court and thereby preserved the substantial evidence issue for appeal. (Gettemy v. Star House Movers (1964) 225 Cal.App.2d 636, 647-648, 37 Cal.Rptr. 441.)

Respondents also contend that appellant has not properly raised the issue on appeal. Again, although respondents framed its assignment of error in terms of its right to judgment as a matter of law, as we

previously indicated, appellant is in effect raising the lack of substantial evidence. In any event, this court can raise the issue on its own motion and request additional briefing, and we have afforded respondents that opportunity. Respondents' contention that there is no authority for this procedure is mistaken. (See Myers Building Industries, Ltd. v. Interface Technology, Inc. (1993) 13 Cal.App.4th 949, 957, fn. 3, 17 Cal.Rptr.2d 242, and cases cited therein; see also, Gov.Code, § 68081.)

[19] Regardless of whether the jury accepted it, there is also substantial evidence to support a finding that the inception of the loss occurred well before 1986 and that the predominant causes of the loss were excluded perils. An insurer's reasonable reliance on credible evidence supporting its position that a claim is barred does not alone constitute a breach of the implied covenant of good faith and fair dealing. (See generally, Opsal v. United Services Auto. Assn., *supra*, 2 Cal.App.4th at pp. 1205-1206, 10 Cal.Rptr.2d 352; Austero v. National Cas. Co., *supra*, 84 Cal.App.3d at pp. 31-32, 148 Cal.Rptr. 653.) This was a close case and there was no smoking gun here; respondents did not produce any evidence that appellant was *not* relying on the evidence supporting its position, or that it denied the claim for some unreasonable, improper or unlawful reason. They simply argued that appellant was wrong, based on their nonlawyer expert's personal and frequently erroneous opinions of what the law required.

[20] Charleston also opined that appellant's intention to deny the claim without regard to the facts or the law was manifested by the initial claim investigation report of Robert Byrne, appellant's independent adjuster, who stated in his report that respondents would make good witnesses on their own behalf. From this remark, Charleston inferred that appellant must have planned on litigation from the outset. He testified that in his entire 24- year career he had never seen such a statement in an adjuster's report to an insurance carrier. The record indicates that Byrne, like many adjusters, handled both first-party and third-party claims, which involve interviews with witnesses as well as parties.

In contrast to Charleston's experience, we routinely run across adjuster's reports that assess the witness potential of the persons interviewed. The record does not clearly indicate whether appellant requested this information or whether Byrne supplied it on his own initiative, although the latter appears more

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likely. However, in either event, there is nothing improper in receiving or obtaining such information. When an insurer has reason to believe it will not be able to resolve a claim to the satisfaction of its insured, it would be naive in this day and age not to consider the possibility, if not probability, of a lawsuit--insurance carriers are our largest institutional civil litigants, usually at the defense table. The mere fact that an insurer is aware of the possibility of litigation does not constitute evidence of bad faith. (Cf. Opsal v. United Services Auto. Assn., *supra*, 2 Cal.App.4th at pp. 1205-1206, 10 Cal.Rptr.2d 352.)

We do not imply that insurers are able to grasp any evidence, no matter how weak or remote, to contradict substantial or reasonable factors indicating that a claim should be paid. The duty of good faith and fair dealing *174 requires that the insurer act reasonably and give equal "consideration to the interests of its insured[s] as it gives to its own interests." (Egan v. Mutual of Omaha Ins. Co. (1979) 24 Cal.3d 809, 818, 169 Cal.Rptr. 691, 620 P.2d 141.) We interpret this as meaning that the first response to a notice of claim from the insured should not be a search for a policy defense, or retention of the sort of expert who always comes forth with a helpful opinion as soon as the client's needs are understood. By the same token, if reasonable investigation reveals a credible dispute over coverage, the insurer does not act in bad faith by denying a claim for which it can reasonably believe it has no obligation. (Opsal v. United Services Auto. Assn., *supra*, 2 Cal.App.4th at pp. 1205-1206, 10 Cal.Rptr.2d 352; Austero v. National Cas. Co., *supra*, 84 Cal.App.3d at pp. 31-32, 148 Cal.Rptr. 653.)

II

[21] In addressing appellant's attack on the damages, we note that the compensatory damages sought and awarded were measured by the cost of repair, a contract measure, and did not include any amount for emotional distress or other elements of tort damages. The court's instruction on the measure of contract indemnity stated: "... If you find that [respondents'] loss is covered, you will be asked to decide the amount owed to [respondents] under the policy. That amount is the reasonable cost of stabilizing and repairing [respondents'] property." Appellant contends that by requiring payment of stabilization costs, the instruction erroneously compelled it to do more than indemnify respondents for the actual

damage which occurred during the policy period; it also required appellant to provide them with a stable lot which they did not possess at any time during the policy period.

The loss settlement clause of respondents' policy provides that in the event of a covered loss, appellant will pay not more than the least of the following amounts: "(a) the limit of liability under this policy that applies to the building; [¶] (b) the replacement cost of that part of the building damaged for like construction and use on the same premises; or [¶] (c) the necessary amount actually spent to repair or replace the damaged building."

In Michelucci's opinion, the fill would not have moved had it been properly compacted, and it will continue to move at a rate of approximately one quarter inch per year if no work is performed to retain it. Michelucci suggested that a retaining wall should be built to retain the fill and prevent further movement; further, the settled portion of the house should be underpinned and the house should be releveled. The end result of such work would be a stable and level house. Michelucci opined that cosmetic repairs, i.e., fixing cracks and leveling floors, would give respondents a temporarily functional house subject to some movement, which would sustain further damage sometime in the future. At its current settlement rate, the house would be significantly damaged again within a decade.

The instruction given was derived from Strickland v. Federal Ins. Co. (1988) 200 Cal.App.3d 792, 246 Cal.Rptr. 345, and the cases cited therein. In Strickland, the insureds' house was damaged by earth movement of an ancient massive landslide in the Big Rock Mesa area of Malibu. The insureds purchased their home in 1982, unaware of the fact that continual earth movement had occurred in that area since the late 1970's. They suffered structural damage in 1983, and at that point first became aware of the landslide movement. Significant interior and exterior cracking occurred, several gas leaks occurred from the pipes pulling apart, and the house appeared to be tilted. The house moved approximately two feet in two years, and movement had since been reduced to a very slow rate. The experts agreed that the house could not be protected from further damage unless the entire landslide area was stabilized. The Court of Appeal held that the cosmetic repairs proposed by the insurer were inadequate to compensate for the loss to the insureds due to the landslide and continuing instability of the land, and that the insurer was liable

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for the cost of stabilizing the land underneath the house, up to the policy limit. (*Id.*, at pp. 801-802, 246 Cal.Rptr. 345.)

*175 *Strickland* relied on three cases which addressed the scope of insurance coverage for loss due to landslide: *Pfeiffer v. General Insurance Corporation* (N.D.Cal.1960) 185 F.Supp. 605, *Hughes v. Potomac Ins. Co.* (1962) 199 Cal.App.2d 239, 18 Cal.Rptr. 650 and *Snapp v. State Farm Fire & Cas. Co.* (1962) 206 Cal.App.2d 827, 24 Cal.Rptr. 44. *Pfeiffer* held that a policy covering a "dwelling" impliedly covers the soil underlying it. *Pfeiffer* also held that because the land underlying the insureds' home was unstable, making only cosmetic repairs would be an erroneous interpretation of the policy, since further landslide damage to the house was possible. (*Pfeiffer v. General Insurance Corporation, supra*, at p. 608.)

In *Snapp*, the experts agreed it would be pointless to restore a house damaged by a landslide to its original form due to the altered condition of the land. The *Snapp* court agreed with *Pfeiffer*, that until the earth was stabilized the house would continue to suffer damage and the occupants would be imperiled. Consequently, since the risk insured against materialized when the soil moved during the policy period, the insurer had a duty to restore the premises by stabilizing the soil up to the limits of the policy. (*Snapp v. State Farm Fire & Cas. Co., supra*, 206 Cal.App.2d at p. 833, 24 Cal.Rptr. 44.)

In *Hughes*, a portion of the land underlying the insureds' house slid into a creek, leaving the house partially overhanging a newly formed 30-foot cliff. However, cosmetic damage to the house amounted to only \$50. In essence, the insurer interpreted the policy such that the building was not damaged as long as its paint and walls remained intact. The Court of Appeal disagreed and held that until the land beneath the house was stabilized, the structure could not be considered a "dwelling" that reasonable people would be content to inhabit. (*Hughes v. Potomac Ins. Co., supra*, 199 Cal.App.2d at pp. 248-249, 18 Cal.Rptr. 650.)

Appellant argues that *Strickland* and the cases cited therein are distinguishable from this case in that they all deal with insureds who were residing in apparently safe homes which became unsafe during the policy period, thus requiring stabilization to return them to their position before the damage occurred. Appellant relies on *McCorkle v. State*

Farm Ins. Co. (1990) 221 Cal.App.3d 610, 270 Cal.Rptr. 492, which held that the insurer was not required to pay the additional costs necessary to comply with upgraded building codes where the loss settlement clause limited coverage to replacement using "equivalent" construction. (*Id.*, at pp. 614-615, 270 Cal.Rptr. 492.)

Unlike the house in *McCorkle*, the repair of respondents' residence does not require building code upgrades. Here, the jury found that respondents' loss was predominantly caused by third-party negligence, for which they were covered. Consequently, respondents are entitled to a stable dwelling. (See *Strickland, supra*, 200 Cal.App.3d at pp. 801-802, 246 Cal.Rptr. 345.) It is impossible or impractical now to stabilize the fill underlying respondents' house by recompacting it, which would require the removal and rebuilding of a portion of the house. The only practical way to provide respondents with a stable dwelling is to construct a retaining wall around the unstable portion. As the aforementioned cases demonstrate, stabilizing the fill under the house will allow respondents to retain a stable dwelling and prevent further damage.

III & IV [FN***]

[FN***] See footnote *, *ante*.

DISPOSITION

As we previously stated, the compensatory damages in this case were entirely contractual; the only portion of the judgment containing tort damages lies in the punitive award. In light of our conclusion that the evidence does not support a tort claim, but does establish respondents' right to policy benefits, that portion of the judgment awarding punitive damages and attorney fees is reversed. [FN4] The *176 judgment is otherwise affirmed. The parties shall bear their own costs.

[FN4] It was stipulated that if respondents prevailed on their bad faith claim they would be entitled to attorney fees as damages due to the tort of another. (*Brandt v. Superior Court* (1985) 37 Cal.3d 813, 817, 210 Cal.Rptr. 211, 693 P.2d 796.) At oral argument the parties agreed that the stipulated attorney fee award was dependent upon and derivative of the tort actions, and

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not contractually based.

PETERSON, P.J., and [POCHE, J.](#) [\[FN****\]](#), concur.

[FN****](#) Assigned by the Chairperson of the
Judicial Council.

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