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ARROWOOD INDEMNITY COMPANY AND BEL AIR MART

BINDING FEE ARBITRATION PURSUANT TO CC §2860, SUB C

ARROWOOD INDEMNITY COMPANY, a Delaware corporation formerly known as ROYAL INDEMNITY COMPANY, as successor to GLOBE INDEMNITY COMPANY, Plaintiff, v. BEL AIR MART, a California corporation; R. GERN NAGLER, as Trustee of the John W. Burns Testamentary Trust; ROBERT GERN NAGLER, an individual, Defendants.	US DISTRICT COURT Case No. 2:11-CV-00976-JAM-DAD JW Case No. A189741-27 Judge: Hon. John A. Mendez **NOTICE OF INTERIM AWARD IN 2860 FEE ARBITRATION, PHASE THREE** DATE: 09/29/2014 10:00 AM LOCATION: Judicate West ARBITRATOR: Hon. Robert J. Polis (ret.) Case filed: August 20, 2013 [JW] Date Submitted: January 12, 2015

TO ALL PARTIES AND TO THEIR ATTORNEYS OF RECORD:

I. PREAMBLE

Arrowood was ordered[1] to "submit all issues concerning the amount of fees it owes for the work of BAM's independent counsel to binding arbitration pursuant to California Civil Code § 2860 (c).[2]

ARROWOOD INDEMNITY COMPANY, *et al.,* is represented by Mr. Bruce D.

[1] Order Granting Bel Air Mart's Motion to Compel Fee Arbitration, Exhibit E-4, pg. 12, lines 7-10.
[2] See FN 1 above.

Celebrezze, Esq., and Mr. Alexander "Alex" E. Potent, Esq., [appearing] and Jason Chorley, Esq., of the law offices of SEDGWICK LLP [hereinafter ARROWOOD]. BEL AIR MART, *et al*., is represented by Mr. Gary W. Osborne, Esq.,[appearing] and Mr. Dominic Nesbitt, Esq., of the law offices of OSBORNE & NESBITT LLP [hereinafter BAM].

II. PROCEDURAL BACKGROUND

A. Arbitration

The arbitration was heard at the Santa Ana Offices of Judicate West on September 29, 2014 from 10:00 to 7:00 PM for a total hearing time of approximately 8[3] hours from a time estimate of 8 (+) hours. BAM appeared through counsel Gary Osborne, Esq. and Dominic Nesbitt, Esq.; also present was Helen Singmaster, Esq., and Steve Goldberg, Esq. ARROWOOD appeared through counsel Alex Potente, Esq. and Jason Chorley, Esq. The Subpoena issues were argued and submitted [See *C*. below]. BAM previously filed its Letter Brief [14 pages] and attached Exhibits [2-3], Declarations of Gary W. Osborne, Esq., Steven Goldberg, Esq., Robert Soran, Esq., Olivia Wright, Esq., and Douglas R. Anderson, Esq., Reply Brief [9 pages and Compendium of cited cases] and Sur-Reply Brief [6 pages], as well as two loose leaf volumes of Exhibits A-1 to K-3 [approximately 850 pages] and upon the request of the Neutral Arbitrator the written contents of two Power-Point presentations, i.e., Opening Statement and Closing Argument. Also received was the Second Amended Counterclaim of Nagler as D-11. BAM called as witness Steven Goldberg, Esq. ARROWOOD previously filed its Letter Brief [20 pages], Declaration of Alexander E. Potente with attached Exhibits 1-3, Declaration of Allison M. Low, Esq., with attached Exhibits 4-13, and Compendium of cited cases Exhibits 14-18, Reply Brief [9 pages] with Compendium of cited cases, Sur-Reply Brief [6 pages], as well as a loose-leaf binder of Exhibits 1-19. ARROWOOD called as witnesses Eric Garner, Esq., [who was examined under oath via telephone], and Helen Singmaster [See *C* below].

The matter was argued but not submitted for decision due to a number of unresolved evidentiary issues for which it was originally thought would take up to three-weeks to produce; accordingly, the parties each came to a qualified "rest," but, it was not until early December that the final promised piece of evidence was received. All of the above evidence and cited

[3] After a generous deduction for time spent on lunch break.

cases was read and considered [list of cases in Appendix, Item Five]; due to the nature of the claims involving a significant number of pages of evidence read and considered, the Neutral Arbitrator put in 100 or so hours in reviewing all the Exhibits in evidence, briefing, cited cases and in drafting the Interim Award, not all of which shall be billed out of professional courtesy. [Reaching 52 hours, time records ceased to be accumulated until January when it was taken up again, as reflected in the Billing Memorandum].

B. Scope of the Arbitration.

1. All issues concerning the amount of fees owed for the work of BAM's independent counsel are submitted to binding arbitration pursuant to California Civil Code § 2860 (c) [see FN 1 above], but limited by agreement to the years 2011, 2012 and 2013.

2. Determination of the appropriate hourly rate to be by paid by Arrowood. [Order Granting Motion to Compel Arbitration, Exhibit E-4, pg. 4, lines 19-22]. [See Exhibit F-2, Notice of Interim Award, Phase Two, April 14, 2014].

3. Reasonableness of the Fees [Order Granting Motion to Compel Arbitration, Exhibit E-4, pg. 8, lines 22-24].

4. Allocation of costs between offensive and defensive tasks [Order Granting Motion to Compel Arbitration, Exhibit E-4, pg. 10, lines 5-7].

5. Only the unpaid *Cumis* fees from 2011, 2012 and 2013 are at issue [see FN 1 BAM's Opening Letter Brief of May 27, 2014, pg. 1, hereinafter OLB].

6. There is no issue of attorney fees for this arbitration [see FN 1 BAM's OLB, pg. 1].

7. The finding by the District Court that ARROWOOD owed BAM a duty to defend is already the law of the case. [Order Granting BAM's Summary Judgment, Exhibit E-5, pg. 15, lines 20-22, March 3, 2014].

C. Issues regarding trial subpoenas, evidentiary rulings and additional evidence.

In Limine Motions:

(1) Motion to quash subpoena of Helen Singmaster, Esq. and *in limine* motion re relevance. ARROWOOD called as a witness Helen Singmaster, Esq. with an offer of proof. BAM objected and argued that the fees incurred "pre-tender" and for the "year of 2014" were

outside the scope of the subpoena issued by ARROWOOD and were irrelevant. The matter was argued, offers of proof were made about ARROWOOD's inquiry into "any demands for settlement made by counterclaimants" to which the mediation privilege was raised. The tentative ruling was to sustain the mediation privilege regarding mediation demands, but in lieu of testimony, it was stipulated that there were "no demands made to BAM outside of the mediation." Accordingly, Helen Singmaster was not called to testify nor sworn as a witness. In discussion, it was determined that any settlement payment to be made by Ralph Armstrong had already been agreed upon but was yet within the mediation privilege as the settlement papers were not executed—Mr. Alex Potente, Esq., of ARROWOOD agreed to provide all the information on the settlements.

(2) Subpoena of Mr. Lassner, Esq. Rather than be called as a witness, the parties stipulated WFI paid attorney fees from January 1, 2012 to December 13, 2013 of $85,000; and incurred investigation and remediation costs to date of $237,000.

Jason Chorley, Esq. During the arbitration, ARROWOOD called as a witness Jason Chorley, Esq., to testify and to present an exhibit he prepared regarding the number of hours billed and allocated to specific legal functions. BAM objection was argued, submitted and sustained because the exhibit itself had not previously been produced as agreed between the parties and as being presented too late; however, the ruling permitted ARROWOOD to make any closing argument they wished based upon the evidence produced and admitted, i.e., the invoiced amounts from Exhibits K1-3, but the document prepared by Mr. Chorley and his testimony about the allocations were not themselves received in evidence. [See FN 20 herein].

Settlement Figures. On December 1, 2014, the Neutral Arbitrator granted one last extension to January 12, 2015, within which the information requested regarding settlement figures could be provided either by stipulation or with executed hard copies of the settlement agreements. Before submission of the case for award, on December 8, 2014, in an e-mail, Mr. Gary Osborne, Esq., on behalf of BAM[4] agreed to stipulate to the settlement figures, to wit. On December 9, 2014, Mr. Alex Potente, Esq., accepted the stipulation and on December 14, he

[4] Quite promptly on December 9, 2014, Mr. Alex Potente, Esq. accepted the stipulation on the settlement figures.

forwarded two of the three written settlement agreements in his possession, not received in evidence as the figures were already admitted. See below, Finding No. 2, Settlement Figures.

[Neutral Arbitrator note: These matters were vigorously pursued by the parties at the arbitration; therefore, it was necessary to set forth the issues and resolutions in this Interim Award by way of incorporating this note and the Notice of Evidentiary Rulings and Orders in re matter of Subpoenas which was issued on October 3, 2014, attached as Exhibit One].

Mediation Costs. On November 20, 2014, the Neutral Arbitrator asked for additional briefing regarding mediations and settlement discussions as being included in services for which fees could be recovered as defense costs by *Cumis* counsel. Both parties responded with supplemental letter briefing filed, read and considered. See Finding No. 16.

Submission Date. The matter was deemed submitted as of January 12, 2015.

III. NOTICE OF INTERIM AWARD

BAM IS HEREBY AWARDED THE SUM OF $545,778.58 PLUS PRE-JUDGMENT INTEREST IN THE SUM OF $81,781.94 FOR A TOTAL AWARD OF $627,560.52.

IV. ANALYSIS, DISCUSSION AND FINDINGS

A. REGARDING THE RELEVANT FUNDAMENTAL PRINCIPLES TO BE APPLIED TO THE ISSUES PRESENTED

Conclusion No. One. The principles of *Aerojet-General* and *Buss v. Superior Court* apply to recovery of defense costs for *Cumis* counsel, as requested in this case.

Finding No. 1. The principal recovery issue presented in this matter is for attorney-fees as defense costs, not site investigation costs, *per se,* as in *Aerojet-General*.

The focus of the dispute in the instant case is nearly a generation of cases away from the issue initially framed and decided in the now famous cases of *Aerojet-General* and *Buss*. ARROWOOD raised no controversy about BAM recovering “site investigation costs” *per se*. But ARROWOOD does contest BAM’s claim for the expenditure of attorney’s fees as defense costs incurred by BAM’s *Cumis* counsel Downey Brand for the three specific years the parties stipulated were to be resolved in Phase III. ARROWOOD’s status as these cases go, is as a non-

breaching insurer for whom a duty to defend BAM in the multiple cross-complaints filed by cross-complaining parties to the CLERCLA action BAM and WFI filed against counterclaimants has already been determined; further, this is not a "mixed action" as discussed in *Buss, id*, where the court is faced with and must distinguish between "covered" and "non-covered" claims in the traditional sense of being within the policy or not. As such, the principles of *Aerojet-General*, *Buss*, and other cases, apply. All well known to the parties, these principles are both cited and paraphrased below, with some editorial license taken.

> (1). The court in *Aerojet* established three requirements for analysis. It follows that the insured's **site investigation expenses** constitute defense costs that the insurer must incur in fulfilling its duty to defend if, and only if, the following requirements are satisfied. First, the site investigation must be conducted within the **temporal limits** of the insurer's duty to defend, i.e., between tender of the defense and conclusion of the action. Second, the site investigation must amount to a **reasonable and necessary** effort to avoid or at least minimize liability. Third and final, the site investigation expenses must be **reasonable and necessary for that purpose**. *Aerojet,* 17 Cal.4th 38, 61-62. Under *Aerojet* the facts must be determined objectively, not subjectively.
>
> (2). Duty to defend arises as soon as tender is made (e.g., *ibid*.), before liability is established and apart therefrom (e.g., *Montrose Chemical Corp. v. Admiral Ins. Co.*, *supra*, 10 Cal.4th at p. 659, fn. 9), and is discharged when the action is concluded. (E.g., *Buss v. Superior Court*, *supra*, 16 Cal.4th at p. 46.) *Aerojet* 17 Cal.4th 38, 60.
>
> (3). It is manifest that this analysis applies, as it were, not only between *claims* but also between *parts* of a single claim. Thus, when all the parts of a claim are at least potentially covered because each may possibly embrace some triggering harm of the specified sort within the policy period caused by an included occurrence, the insurer has a duty to defend. It has " 'contract[ed] to pay the entire cost of defending' " a claim of this sort. (*Buss v. Superior Court*, *supra*,

16 Cal.4th at p. 47.)

(4). *Reasonable and necessary.* Whether the insured's site investigation amounts to a reasonable and necessary effort to avoid or at least minimize liability must also be assessed under an objective standard. What matters here is whether the site investigation would be conducted against liability by a reasonable insured under the same circumstances.

(5). *Reasonable and necessary for that purpose.* Lastly, whether the insured's site investigation expenses are reasonable and necessary to avoid or at least minimize liability must be assessed under an objective standard as well. What matters here is whether the site investigation expenses would be incurred against liability by a reasonable insured under the same circumstances. Were it not, this question too would require a discernment of motive. Why is the insured incurring the site investigation expenses at issue? To resist liability? For that reason and some other? For a reason altogether different? "Motive," again, "is 'hard ... to discern.' " (*Buss v. Superior Court*, *supra*, 16 Cal.4th at p. 52, fn. 14.) *Aerojet* 17 Cal.4th 38, 63.

(6). *The burden of proof lies with BAM.* "In the general case [where the insurer is non-breaching], it is the insured that must carry the burden of proof on the existence, amount, and reasonableness and necessity of the site investigation expenses as defense costs, and it must do so by the preponderance of the evidence. *Buss v. Superior Court*, *supra*, 16 Cal.4th at pp. 53-54. *Aerojet,* 17 Cal.4th 38, 64.

(7). *BAM has the burden of making a good faith effort to separate its costs between defense and prosecution costs, or prove they were inextricably intertwined. KLA-Tencor Corp. v. Travelers Indemnity Company of Illinois*, 2004 WL 1737297, did not concern contamination but allegations of patent infringements '055 and '406, and counterclaims against KLA for disparaging and untrue statements. The Court found insured KLA had the burden of proving the

existence and amount of the expenses involved in defending the disparagement counterclaims, which KLA met in the '055 case by "demonstrating the hours worked and testimony that all the work was related to the defense, but subject to the requirement that such work must be reasonable and necessary to defense of the disparagement counterclaims" [*KLA*, *supra* HN #6]. Further, the Court held, to the extent that the costs related to the disparagement counterclaims cannot be separated from the costs unrelated to those claims, the insurer bears the burden of showing which costs are in fact unreasonable or unnecessary [Citing *Barratt*, *id* at 1548—see above].

(8). Negotiated claims. The court in *Aerojet* found it did not matter that the governmental actions were different from others, i.e., not litigation, not leading to judgment, but were "negotiated" and "aimed at settlement." The court reasoned: "What matters is the legal "essence," as it were, of any site investigation and any site investigation expenses, and not their factual "accidents." *Aerojet,* 17 Cal.4th 38, 65.

(9). *Site investigation costs can do double duty, both as defense costs and indemnification*. In *Barratt American v. Transcontinental Insurance Company* (2002) 102 Cal.App.4th 848, the Appellate Court made two findings that are pertinent to the instant case, i.e., (1) defense costs may serve the insured in dual capacities[5], and (2) the Appellate Court found that Barratt did not prove facts sufficient to recover their defense costs from insurer.

B. REGARDING RELEVANT FOUNDATIONAL FACTS FOUND TO BE TRUE

Conclusion No. Two. Certain Uncontested Facts are true.

Finding No. 2. The basic facts and procedural issues are the "law of the case."

A. The Underlying Action—basic facts uncontested.

[Arbitrator's note. Rather than tease the relevant facts from the materials presented,

[5] See *KLA –Tencor Corp v. Travelers Indem. Co. of Illinois,* 2004 WL 1737297. [Exhibit 15, ARROWOOD's Compendium of cited cases].

attached hereto as Exhibit Two to this Interim Award are the underlying facts found in the (partial) Order Granting Bel Air's Motion for Summary Judgment etc., Exhibit E-5]

B. The Procedural Matters are uncontested.

COURT ORDER of June 3, 2013.

Arbitrability of Rates [Exhibit E-4, pg. 4][6]

Notice of Interim Award §2860 Arbitration, Phase Two [Exhibit F-2]

Partner $275; Counsel $240; Associate $225, Paralegal $115.

Arbitrability of reasonableness of Fees is not in dispute [Exhibit 4, pg. 4].

Arbitrability of Allocation is ordered [Exhibit 4, pg. 9].

COURT ORDER. Submit all issues concerning the amount of fees ARROWOOD owes for the work of BAM's independent counsel to binding arbitration pursuant to CC § 2860 (c).

COURT ORDER of March 3, 2014.

The Court grants Bel Air Mart's motion for Summary Judgment on the duty to defend.

Stipulations between the Parties as to uncontested facts.

Only the unpaid *Cumis* fees from 2011, 2012, and 2013 are presented in Phase III.

WFI spent $87,000 from 01/01/2012 to 12/31/2013.[7]

WFI paid for site investigation and remediation to date $237,170.[8]

BAM paid pre-tender fees/costs of $69,677 for Downey Brand from July to December of 2010, which is one-half of the total of the total amount of $129,997. [See FN 9 below]

BAM incurred fees/costs of $236,854 for Downey Brand from January to October of 2014, which is 70% of the total $338,183 [not recoverable in Phase III]. [See FN 9 below]

Settlement Figures. On 12/08-09/2014, the parties stipulated as to the settlement figures as follows: (2)[9] Glen Nagler [Industrial Indemnity] is paying $95,000 as "net settlement" of BAM and WFI's claims and Nagler's claims against BAM, WFI, Gene Wong, Paul Wong and Lillie Fong; (3) Ronald Armstrong [Century] is paying BAM and WFI the "net amount" of $550,000; (4) Joo Parties are paying $20,000 to BAM and WFI; and (5) Panattoni settled with

[6] Accomplished in Order Granting Bel Air mart's Motion to Compel Fee Arbitration Pursuant to §2860.
[7] Stipulation at hearing.
[8] Stipulation in November 18, 2014 e-mail.
[9] (1) is intentionally deleted.

BAM and WFI for a net payment of $85,000; (6) Burns Party [ARROWOOD] did not settle—CERCLA actions remains active; (7) BEL AIR's excess/umbrella insurer Industrial Indemnity paid $205,000 for remediation; and (8) ARROWOOD has paid $401,793 toward costs for environmental consultant Kleinfelder as defense and response costs

Fees and costs for this 2860 Arbitration are not presented in Phase III.

Finding No. 3. The actual numbers submitted to ARROWOOD are uncontroverted.

It is uncontroverted that BAM submitted to ARROWOOD the Downey Brand monthly invoices on behalf of BAM in the CERCLA Action from January 1, 2011 to December 2013. [See Exhibits J-1 to J-36]. The actual amount of the figures is not disputed. BAM submitted invoices totaling $831,970[10] for which ARROWOOD has paid $286,192 leaving an unpaid but contested balance of $545,779[11] broken down by pertinent year: **2011:** $150,690.30; **2012:** $389,009.12; and **2013:** $292,271.00.

BAM allocated the fees submitted into categories called "covered" and "not covered."

It is uncontroverted that before submitting each invoice, knowledgeable attorneys for Downey Brand reviewed and made adjustment reducing the amount of fees billed. The adjustments were based upon an "allocation analysis" for time spent only on BAM's defense of the counterclaims, that is, tasks which were identified as reasonable and necessary to the defense—the covered costs—versus those that were thus non-covered, which figures were then redacted from the invoices. Only for the year 2011 was the total invoiced amount split between WFI and BAM pursuant to a cost sharing agreement before being submitted to ARROWOOD, but not thereafter in the years 2012 and 2013. Conclusion. The actual numbers are not controverted, only the right to recover them as defense costs.

Conclusion No. Three. Contested Facts found to be true.

Finding No. 4. No adverse discovery inference drawn in favor of ARROWOOD.

In footnote 8, of Response Brief, ARROWOOD requested an adverse inference from BAM's refusal to produce its attorney invoices from prior to the filing of the counterclaims based upon BAM's assertion of the attorney-client privilege. First, BAM never offered the

[10] The parties stipulated at trial permitting a "rounding-up" of the figures.
[11] Rounded up to nearest dollar.

argument that its litigation strategy or purpose changed following the filing of the counterclaims, for which ARROWOOD now seeks the adverse inference. Secondly, the refusal to comply with ARROWOOD's RFP No. 2 seeking the fee invoices was justified by the finding and ruling of the Neutral Arbitrator based upon the most sacrosanct of all privileges, the attorney-client privilege. Therefore, it cannot be said that BAM "willfully refused to comply" with a relevant discovery request which would justify an adverse evidentiary inference. Conclusion. No such adverse inference is justified.

Finding No 5. BAM has made a good faith effort to allocate its costs between defense of the counterclaims and prosecuting the affirmative CERCLA action.

BAM had the burden of making a good faith effort to separate its costs between defense and prosecution, or prove they were inextricably intertwined and therefore impossible to separate. *KLA-Tencor Corp. v. Travelers Indemnity Company of Illinois*, 2004 WL 1737297, did not concern contamination but alleged patent infringements '055 and '406, and counterclaims against KLA for disparaging and untrue statements. See Finding No. 1 (7) above. The case law establishes that in cases of a non-breaching insurer, it is the insured who has the burden to prove the fees are reasonable and necessary to the defense; but once a prima facie case is made, or it has been determined that the prosecution and defense fees are impossible to separate, the burden shifts to insurer to prove which costs are unreasonable and unnecessary.

The Instant Case. It is uncontradicted that before submitting them, each invoice was reviewed by knowledgeable attorneys and adjustments were made reducing the amount of fees billed by Downey Brand to those claimed reasonable and necessary. The adjustments were based upon an "allocation analysis" for time spent only on BAM's defense of the counterclaims, that is, tasks which were identified by the reviewers as being reasonable and necessary to the defense—the covered costs, so-to-speak—versus those that were non-covered, which were then redacted from the invoices presented in evidence. Conclusion. It is uncontradicted that Downey Brand performed an "allocation analysis" of what was "reasonable and necessary" to BAM's defense of the counterclaims, designating that amount as being "covered," versus "non-covered." Only "covered" fees were presented for reimbursement. [OLB, pages 4-5].

Documentary Evidence.

BAM Presented as documentary evidence Exhibit K1-3, being the Allocation Spreadsheets for the years 2011, 2012 and 2013; these exhibits have been redacted by occluding the non-covered line items. Also, admitted in evidence are the actual invoices for 2011, 2012 and 2013, marked Exhibit J1-36. These, too, have been redacted by occluding line items consistent with the initial task of allocation between covered and non-covered efforts. The Neutral Arbitrator spot-checked Exhibit K1-3 for accuracy against Exhibit J1-36. Then, the entirety of Exhibit K1-3, all 6,353 line items, has been reviewed at least twice, once at the outset of evidence review and the second time right before final re-write and re-draft.

Declarations of Downey Brand lawyers.

Attorney Robert Soran. The allocation analysis was performed by Robert P. Soran, Esq., who reviewed five specific tasks, i.e., investigation, procedure, communications, settlement and research and analysis in determining the allocations [Soran Declaration ¶ 26] but making further relevant subdivisions, each explained at ¶¶ 27, 28, 29, 30, 31, 32, and 34, of his declaration. It was his opinion that the tasks identified amounted to objectively reasonable and necessary efforts to avoid or minimize BAM's liability against the four counterclaims [See Soran Declaration, ¶ 33]. He further declared, a plaintiff's defense of counterclaims will usually overlap with the prosecution of an original CERCLA complaint, to wit, by litigating the relative fault and responsibility for the contamination. [Soran Declaration, BAM's Exhibit 2, ¶¶ 3, 23, 25, 26, & 36].

Attorney Steven H. Goldberg. From May of 2013, Mr. Goldberg took over for Robert Soran, who retired. [Goldberg Declaration, ¶4]. In his Declaration, he repeated many paragraphs from the Declaration of Robert Soran about this process and his findings/opinions.

Attorney Olivia Wright. Olivia Wright worked closely with both Messrs. Robert Soran and Steve Goldberg on the CERCLA matter, and she reviewed every single fee entry for purposes of determining whether the tasks were reasonable and necessary to BAM's defense, and declared so by rendering favorable opinions. [Declaration, ¶¶ 4 & 6].

Conclusion. BAM has met its burden of making a good faith effort to allocate its costs

between defense of the counterclaims and prosecuting the affirmative CERCLA action.

C. EACH OF THE *AEROJET* THREE-FACTOR ANALYSIS HAS BEEN MET.

Conclusion No. Four. The first factor of *Aerojet's* analysis has been met--*Temporal limits.*

Finding No. 6. It is uncontroverted all claimed defense costs arose within the temporal limits as defined by *Aerojet.*

The *Aerojet* definition is: [See Finding No. 1]

> "It follows that the insured's site investigation expenses constitute defense costs that the insurer must incur in fulfilling its duty to defend if, and only if, the following requirements are satisfied. First, the site investigation must be conducted within the temporal limits of the insurer's duty to defend, i.e., between tender of the defense and conclusion of the action. *Aerojet,* 17 Cal.4th 38, 61.

This element of the three-part test is uncontroverted: it is uncontested that ARROWOOD's duty to defend commenced on January 6, 2011, and it has not yet concluded [Burns party has not yet settled]. [OLB, pg. 7][See ARROWOOD Opposition Brief, pg. 8:7-12 AOB hereinafter][BAM Reply Brief, pg. 1, hereinafter BRB].

Temporal Limits Timeline Worksheet.

12/09/2010	FAC filed [Exhibit D2]
01/19/2011	R. Armstrong First Amended counterclaim filed [D3]
02/02/2011	Nagler First Amended counterclaim filed [D5]
04/15/2011	Panattoni counterclaim filed [D7]
04/22/2011	Answer to Nagler filed [D6]
04/29/2011	Answer to R. Armstrong filed [D4]
06/11/2011	Answer to Panattoni filed [D8]
07/12/2012	Century Indemnity cross and counterclaim filed [D9]
05/14/2013	Answer to Century Indemnity filed [D10]
06/04/2014	Compel Arbitration Order
10/12/2014	Settlement of all but Burns Party.
12/10/2014	Settlement executed by all but Burns Party

Conclusion. The Neutral Arbitrator finds the first factor of the *Aerojet* analysis was met.

Conclusion No. Five. The second factor of *Aerojet's* analysis has been met.

Finding No. 7. BAM met its evidentiary burden to show defense costs were reasonable and necessary to avoid or at least minimize liability.

The second factor of *Aerojet's* analysis is that BAM must show the defense costs were in

a reasonable and necessary effort to *avoid or at least minimize liability*.

The *Aerojet* definition is: [See Finding No. 1].

> "Second, the site investigation must amount to a reasonable and necessary effort to avoid or at least minimize liability." *Aerojet,* 17 Cal.4th 38, 61.

Before launching into a discussion of and application of the facts to the above stated *Aerojet* principle, a few comments are in order. *Aerojet* was the target of the contamination litigation and was defending the suit after tendering the defense under its general liability policy. In the instant case, BAM brought the CERCLA action in the first place, so unlike *Aerojet*, BAM was not initially defending a contamination lawsuit and therefore unable to rely upon its CGL policy to prosecute its case against those sub tenants BAM sued believing them 100% responsible for the contamination. These now sued former dry cleaning tenants became the counterclaimants. When the same target defendant parties in the CERCLA litigation action conveniently brought their own counterclaims against BAM as sub lessor of the property, BAM was placed in the same position of *Aerojet-General*, that is, BAM was now defending against the liability for contamination now aimed at BAM by all four counterclaimants, who were deflecting their own liability by pointing at BAM as the 100% responsible party. Thus, in defending the counterclaims, BAM was trying to "avoid, or at least minimize" its own liability from the counterclaimants, while at the same time trying to establish and maximize liability against the same subtenants now in their counterclaimant capacity.

Finding No. 8. "Site investigation costs may do double duty, both as defense costs and indemnification."

In *Barratt American v. Transcontinental Insurance Company* (2002) 102 Cal.App.4th 848, the Court made a finding pertinent to the instant case, i.e., (1) defense costs may serve the insured in dual capacities,[12] and, incidentally, the Court also found that Barratt did not prove facts sufficient to recover their defense costs from insurer. Recall in *Barratt,* a developer incurred repair costs for homes whose owners did not join in the underlying construction defect litigation in which insurer had a duty to defend and was being defended. At trial, the jury found

[12] See *KLA –Tencor Corp v. Travelers Indem. Co. of Illinois,* 2004 WL 1737297. [Exhibit 15, ARROWOOD's Compendium of cited cases].

Barratt's costs were recoverable defense costs. On appeal, the Court found the principles announced in *Aerojet General* applied to the *Barratt* case, in that, even if CERCLA "response costs" which are considered "damages" were sought, (See *AIU Ins. Co. v. Superior Court* (1990) 51 Cal.3d 807), it does not mean those expenses cannot also be characterized as defense costs; the Court went on to explain that site investigation expenses can do double duty—indemnification and defense costs. Further noted in *Barratt* from *Aerojet*, the court stated: just because the insured gains collateral benefits from the defense investigation expenditures does not mean the costs lose their character as recoverable defense costs. *Barratt* 102 Cal.App.4th 848, 858. While the Court in *Barratt* recognized that developer Barratt's costs incurred in repairing non-plaintiff homes were not recoverable under Transcontinental's indemnity obligation under *Foster-Gardner*[13] and *Powerine,* this did not mean that Barratt could not recover investigation expenses to defend the construction defect lawsuit. *Barratt*, 102 Cal.App.4th 848 859. Thus, the court in *Barratt* found those expenses were not barred from recovery as a matter of law under *Aerojet General* or *Foster-Gardner*. *Barratt supra*, 848, 861. We know, of course, Barratt failed to meet it burden, and these costs were denied.

This same dual purpose concept placed BAM in the position that its best defense to the counterclaims would be having the best offense it can muster in favor of establishing the 100% liability of all the former owners/tenants, not itself, thus avoiding or at least minimizing its own liability. All of the evidence marshaled in the investigative stage for its own CERCLA action surely falls into this dual-purpose offensive/defensive category. Thus, it can be concluded that the site investigation costs [as in *Aerojet,* but here defense costs]—served a dual purpose—the defense costs were reasonable and necessary to "avoid or at least minimize" BAM's liability against the counterclaims, even though the very same evidence and same efforts would be utilized to establish and maximize the liability of each and every counterclaimant "at the same time." "That the same costs may do double duty as both indemnification costs and defense costs does not mean that they do not do duty as the latter as well as the former." *Aerojet, id* 17 Cal.4th 38, 66. Of course, it is acknowledged that ARROWOOD contended from the outset its

[13] *Foster-Gardner Inc. v National Union Fire Ins. Co.* (1998) 18 Cal.4th 857; *Certain Underwriters at Lloyd's of London v Superior Court,* (2001) 24 Cal.4th 945, 960 (*Powerine*).

"subjective belief" that such a tactic amounted to a "scheme" to achieve coverage where coverage would not otherwise lie, and that BAM's "motive" all along was to prosecute its own affirmative claims against the sub-tenants. This argument has not been accepted herein. Conclusion. The Neutral Arbitrator finds the "double-duty" concept applied as seen in both *Aerojet* and *Barratt,* that is, the defense costs served a dual purpose, i.e., for BAM's best defense to the counterclaims to avoid or at least minimize BAM's liability by establishing 100% liability of the counterclaimants; and, by so doing, the defense costs do not lose their characterization as recoverable defense costs as in *Barratt*.

Finding No. 9. The Pleadings themselves establish BAM's CERCLA claims and counterclaimants' counterclaims were essentially identical. .

First Amended Complaint. In 2010, the Complaint was filed [FAC Exhibit D2—December 09, 2010] by BAM and WFI against Arnold Cleaners and all prior owners and operators, i.e., Han Joo, Chang Joo [breach of lease], Peter Kim, Estate of Ronald Armstrong, Ralph Armstrong, M. Carrington, Y. Panattoni, R. Gern Nagler, Estate of John Burns and others, in 13 causes of action, to wit, CERCLA, Health & Safety Code, Declaratory Relief, Equitable Indemnification, Contribution under Common Law, Negligence, Negligence Per Se, Private Nuisance, Trespass and Breach of Contract. The gist of the 70-page Complaint is that WFI as owner and BAM as sub lessor initiated and paid for subsurface investigations, which resulted in finding contamination by PCE and TCE that were present in soil vapor samples, and VOCs in groundwater samples; and further, it alleged all defendant subtenants released hazardous substances and wastes during their operation of dry cleaning facilities resulting in plaintiffs' continuing need for response and remediation costs. [Complaint, Exhibit D-2, pgs. 9-11, ¶¶ 42-51; pgs. 12-17, ¶¶ 56-70. Specifically, ¶ 75 alleged all defendants intentionally or negligently released hazardous substances into the environment under the dry cleaning facility and the property, for which plaintiffs have incurred response costs. In ¶ 85, WFI and BAM alleged neither plaintiff caused or contributed to the release of hazardous substances. Plaintiffs thereby alleged subtenants were 100% responsible and Plaintiffs were not responsible at all.

The Counterclaims. The allegations of the counter complaints filed by the subtenants

against BAM reflect their own assertion that BAM's negligence was the cause of the contamination, the same as BAM alleged against the subtenant dry cleaning operators, the counterclaimants. Counterclaimant Ralph Armstrong [Exhibit K3] alleged plaintiff WFI and BAM caused and contributed to the contamination with inadequate maintenance of the property, sewer conveyances, flooring and parking lot, such that PCE, HVOCs or VOCs escaped [Exhibit K3, pg. 4, ¶ 10] in causes of action for Negligence, Declaratory Relief, Equitable Indemnity, Contribution and Public Nuisance all arising from plaintiffs' culpability, to which BAM asserted three Affirmative Defenses alleging Acts of Others. Counterclaimants Nagler [Exhibit K5], Panattoni [Exhibit K7], Century Indemnity Company [on behalf of Ronald Armstrong vis-à-vis Probate Code § 550] [Exhibit K9], and Estate of Burn all filed counterclaims that mirrored that of Ralph Armstrong, with the exception of the claim for fees and costs asserted by Gern Nagler for the Tort of Another. The gist of each of the allegations of the complaint, each of the counterclaims, and the affirmative defenses is to the same effect: "the other guy did it, not me." Plaintiffs assert the defendants caused the harm, defendants deny causing harm, but as counterclaimants, they assert that plaintiffs caused the harm, which plaintiffs as counter-defendants deny. The arguments are the same, and the issues are the same. Conclusion. The Neutral Arbitrator finds the pleadings demonstrate that the claims of the parties against each other are the same.

Finding No. 10. BAM's Evidence at Hearing established the defense costs claimed were all to avoid or at least minimize BAM's liability.

Mr. Goldberg and Ms. Wright identified as associated with the defense against the counterclaims the following five relevant general categories to be utilized in determining whether the line item fees were reasonable and necessary to avoid or at least minimize liability: investigation, procedure, communications, settlement, and research and analysis. [Goldberg Decl. ¶ 8., Exhibit 2]. Included in the investigation category also were determining the nature, scope and sources of contamination, evaluating remediation options, identifying potentially responsible parties, litigating equitable factors that bear on the parties' respective contribution claims against each other, procedural, communication and settlement tasks associated with the

defense—all found enumerated in the 6,353 line items of Exhibit K1-3. [Goldberg Decl. ¶ 11]. Further, Mr. Goldberg stated the counterclaims to a CERCLA action will usually overlap the prosecution of the original complaint [Goldberg Decl., ¶ 13].

In his declaration, attorney Soran discussed in ¶¶ 26-32 his sub-categories of legal procedures and activities which comprise reasonable and necessary efforts to avoid or at least minimize liability, including litigating equitable factors that bear on the parties' respective contribution claims against each other [Soran Decl., ¶ 34]. It was also his experience that there was an overlap of prosecuting a CERCLA claim and defending counterclaims [*id*].

(1) Investigation. [Soran Declaration, ¶¶ 26--32]. In addition to the seven factors discussed by Mr. Soran in ¶ 27, by way of argument, BAM offered [OLB, pg. 9] various other logical factors that would further define the "investigative period." For example, BAM offered as factors to be considered: discovery, expert analysis, consultants, testing, preparation of the Remedial Action Plan [RAP], all client documentation, collection, review and analysis of third party documents, witness interviews, depositions of parties and witnesses, and damage analysis; again, all found enumerated amid the 6,353 line items of Exhibit K1-3.

(2) Procedure. [Soran Declaration, ¶¶ 26, 29]. Mr. Soran suggested traditional procedural matters here are important like pleadings, motions, notices, and the like, are reasonable and necessary; likewise all found enumerated in the 6,353 line items of Exhibit K1-3.

(3) Communications. [Soran Declaration, ¶¶ 26, 30]. Mr. Soran suggests all forms of communication as being reasonable and necessary.

(4) Settlement and Mediation. [Soran Declaration, ¶¶ 26, 31]. Mr. Soran suggests all work on settlement inside and outside mediation is reasonable and necessary. Specifically, both Messrs. Soran and Goldberg both declared as going to the defense was the task of "litigating equitable factors that bear on the parties' respective contribution claims against each other." What is in the litigation pot, is also the food for mediation. [See Finding No. 16—Mediation and Settlement fees]

(5) Research and Analysis. [Soran Declaration, ¶¶ 26, 32]. Mr. Soran suggests all legal analysis associated with shifting legal liability is reasonable and necessary.

<u>Testimony of Attorney Goldberg</u>. Mr. Stephen H. Goldberg, J.D., a lead partner at Downey Brand since May of 2013, testified he was thoroughly acquainted with CLERLA cases (25-30) and dry cleaner litigation.[14] His conclusion was that by way of the counterclaims, BAM was exposed to the entire cost of investigation and clean up, including the proposed RAP [Remedial Action Plan] and future remediation—the cost of which was 1.6 million for remediation, which cost may be exceeded. The cost of investigation was approximately $900,000, he testified. In addition, counterclaimants Ralph Armstrong, Panattoni and Nagler prayed for attorney fees but Century Indemnity did not. The counterclaimants alleged that BAM was negligent and mismanaged the property, failed to maintain the property as master tenant (relating to sewer lines that were a source of contamination), failed to maintain and repair the parking area pavement, failed to abate the problems when discovered, continued to lease to dry cleaners who used these same toxic chemicals, and then exacerbated the contamination by demolishing the dry cleaner building. Under CERCLA, in his opinion, both the money already paid and the allocation for future costs of clean up would be determined along with the "orphan shares" [for those who were liable but are now judgment proof—e.g., Carrington, *et. al*.] would get allocated between the parties. Thus BAM's potential exposure was high for past and future costs of clean up—that is, for 100% of the damages. While it is true that no one sued BAM under CERCLA—BAM argued that BAM prevented that lawsuit by its voluntary action, and that the Water Board anyway would have issued to plaintiffs a "clean up and abatement order."

In his opinion, CERCLA cases are complex, involving multiple parties, much evidence, multiple experts—with extensive battles between experts—and such cases are document intensive, making CERCLA very expensive to both prosecute and defend. Downey Brand was required to respond to lots of pleadings issues and motions filed against BAM including a "dispositive-seeking" spoliation motion asking for terminating sanctions brought by Century Indemnity that was difficult; experts were consulted, and most were deposed. BAM did the site investigation and paid for the expert Kleinfelder for $237,000—no one else paid or incurred investigation costs. Mr. Goldberg further testified that usually all parties "point their fingers at

[14] Evidentiary objection as legal conclusion argued, submitted and overruled.

each other," thus, in his opinion, the investigation facts were related to defending the counterclaims. Further, he testified about the allegations of the counterclaims against BAM re lack of maintenance, mismanagement of the property, lack of sewer line maintenance which was alleged to be a source of the contamination, failure to maintain the parking lot pavement, failure to abate the nuisance upon knowledge thereof, negligence in leasing to cry cleaning tenants who used hazardous chemicals in the process, and exacerbation of the entire contamination process by demolishing the building [not spoliation]. BAM's evidence was that its response costs were reasonable and necessary to avoid or at least minimize its liability. BAM was at considerable risk for past and future costs of clean up—up to 100% of the damage, he testified. This evidence was persuasive. He further testified in these actions, the claim of both BAM and counterclaimants were the same—they were all for contribution, with everybody taking the position that they are not liable but all faced exposure for the cost of clean up [including the orphan shares]. BAM further offered into evidence the declarations of experienced CERCLA lawyers [Attorneys Goldberg and Soran][15] about various factors encountered in prosecuting and defending CERCLA actions, laying out a considerable laundry list of what factors, in their opinion, should be considered in determining that the defense costs amounted to a reasonable and necessary effort to avoid or at least minimize BAM's liability to the counterclaimants causes of action.

ARROWOOD did not offer any expert opinions or a list of what factors should or should not be considered for a determination of what was reasonable and necessary [except the offer of testimony from Jason Chorley, Esq. about the hours spent in certain categories but not their lack of relevance]. That is to say, ARROWOOD has vigorously argued that all of the claimed expenses were for prosecution of its CERCLA action, and not in defense of the counterclaims, citing cases which support their views which have been reviewed and resolved herein---ARROWOOD's contention has been that ALL of the defense costs are not reasonable and not necessary as the counterclaims were "almost exclusively defensive" in nature. Conclusion. The Neutral Arbitrator found BAM's evidence persuasive.

[15] Not to denigrate the considerable experience of attorney Olivia Wright in any way.

Finding No. 11. ARROWOOD's evidence found not persuasive.

ARROWOOD's evidence at hearing was noted but ultimately found not controlling. ARROWOOD called as a witness Eric Garner, Esq.[16] Mr. Garner, an attorney, testified he represented Nagler who owned the property in the 1980-88 timeframe before selling it to the Panattoni family, but did not operate any business there.[17] He testified that counterclaimant Nagler spent nothing on investigating or remediating the contamination problem at the property, and his Nagler's only claim was for attorney fees under contract and for the tort of another, which now totaled almost $166,000, which Nagler was trying to recover against BAM as an offset to any damage claim. Mr. Garner admitted under the CERCLA actions, there could be a judgment imposing liability against some parties for the cost of clean up, but he did not recall seeking liability against BAM. Nagler settled within a week of this arbitration. ARROWOOD argues this evidence in support of its claim that the counterclaims were defensive only.

ARROWOOD called as a witness Helen Singmaster, Esq. with the offer of proof regarding pre-tender costs and 2014 fees. BAM correctly objected that the fees incurred "pre-tender" and for the "year of 2014" were outside the scope of the subpoena issued by ARROWOOD and irrelevant. The matter was argued and an offer of proof was made about whether there were "any demands for settlement made by counterclaimants." The confidentiality of mediation was raised by way of an objection as a bar to this evidence. The tentative ruling was to sustain the mediation confidentiality; in lieu of testimony then, it was stipulated between the parties that there were "no demands" made to BAM outside of the mediations—hence the confidentiality of mediation prevailed regarding demands, and no evidence of demands/offers was admitted. Helen Singmaster did not testify. At the same time, evidence of settlement payments to be made by Ralph Armstrong was also determined to be within the mediation confidentiality, as the settlement papers were not executed yet or made public—but ARROWOOD [Alex Potente] agreed to provide all the settlement information when able—and he did. There is no evidence of any of the substantive claims made by any of the parties due to the mediation confidentiality and evidentiary ruling thereon. There is no evidence of the nature

[16] Who by prior agreement testified telephonically.
[17] Relevancy objection was made, argued, submitted and overruled.

of any of the considerable negotiations and mediation which must have occurred that lead to a settlement between so many parties in such a complex case as this.

ARROWOOD contended strenuously throughout that BAM's attorney fees are not reasonable and necessary to BAM's defense. [AOB, pg. 14 *et seq*.] ARROWOOD argued that BAM's fees are "almost exclusively" incurred to maximize their own recovery, not to defend the counterclaims [AOB, pg. 15:1-3]. The Neutral Arbitrator found that the counterclaims against BAM are not "exclusively defensive." See Finding No. 18.

ARROWOOD argued BAM is transmuting prosecution costs into covered defense costs [AOB, pg. 17:7-8], citing *James 3 Corp*, *supra*, and *Larkin*, *supra*. But, the facts of the instant case do not fit into the rulings enunciated in *James 3 Corp* or *Larkin,* both of which are inapposite. ARROWOOD argued that the scope of Downey Brand's legal work has not changed since the inception of the problem in 2007, and that mere filing of "defensive" counterclaims seeking offset did not transmute BAM's voluntary cleanup and prosecution of the recovery action into fees reasonable and necessary to BAM's defense. ARROWOOD's argument is not persuasive. Not only is BAM prosecuting its action, as claimed, it is defending against claims against its own liability in four counterclaims. ARROWOOD does not controvert that it owed BAM a complete defense under *Buss v Superior Court*, *supra*, which case ARROWOOD argued has no application here. Conclusion. In the end, ARROWOOD's evidence was not found controlling.

Finding No. 12. Defense costs were reasonable and necessary on their face.

The Invoices. Exhibits K1-3. The Neutral Arbitrator reviewed each of the 6,353 line items in a mind-numbing exercise,[18] viewing each column, paying attention to the date, the author, the amount billed and hourly rate, but more particularly, the "block-billing" narrative backup for each individual charge. ARROWOOD argued [though no evidence by Mr. Chorley was admitted other than this one opinion] that of the total hours, 2,659 hours were not

[18] Actually reviewed twice: once at the outset examining for *Aerojet* 2 factors, and once again at the end of the re-write at which time the author was far more familiar with attorneys, issues, contentions and factors in order to identify them in the block billing narratives to *Aerojet* 3 factors—there will be only a partial billing for the first review and none for the first two Advil tablets.

"defensive" hours, but were in specific categories,[19] to wit, for spoliation, settlement (mediation), RAP, site investigation, stay of the CERCLA action, insurance matters, and intra office communication. In general, ARROWOOD offered no legal or logical rationale why any of these specific categories were not reasonable and necessary in avoiding or at least minimizing liability, or were not reasonable and necessary to the defense of the counterclaims. Each of the activities [insurance matters, intra office communications, and a stay of action], on their face alone amounts to reasonable and necessary legal activity confronted in normal litigation, much less considering the difficulty of this litigation and the number of moving-parts involved. Spoliation and mediation are dealt with elsewhere. RAP and site investigations are an integral part of any CERCLA action—See Goldberg. Furthermore, ARROWOOD failed to cite specifically to any particular line item that could be reviewed in the context of this argument to give body to the objection. The Neutral Arbitrator found none on its own, with some minor quibbles here and there. It seems that ARROWOOD's argument is only that the number of hours expended on these subject were excessive. They were not, considering the evidence offered by BAM—not countered by ARROWOOD—that CERCLA cases (with multiple parties) are difficult to defend and prosecute, both of which fell upon Downey Brand in fulfilling their duty to defend immediately and fully.

In response to the arguments made by ARROWOOD, the Neutral Arbitrator reviewed extensively all of the line items, paying attention to the seven special categories enumerated above to the extent that the block-billing narrative made it possible. The results of the review are not so specific as to number of hours spent in each of the individual categories of effort as argued by ARROWOOD, but the results came by way of generalized statements.

Year of 2011. There were 1190 line items, resulting in 1,251 hours of "covered" activity resulting in reduction of the bill to $150,690 of adjusted covered fees from the amount invoiced. This calculated out to about 49 percent covered. In the opinion of the compiler of this document, 1,251 hours were attributable to the defense of the counterclaims, not the prosecution of the

[19] Though not evidence, the categories were: spoliation 251, mediation 456, RAP 261, stay of action 33, insurance matters 523 and intra-office communication 857; the Neutral Arbitrator ran rough figures of its own in each of these categories as well as others from the reviews of Exhibit K1-3.

CERCLA action. Of the five categories posited by BAM in evidence, i.e., "investigation, procedure and communication," in the review of Exhibit K1, the category of "communication" showed a very high number, as would be expected at the outset of a significant lawsuit, while research would be low, analysis, settlement and spoliation of evidence were all also lower, but site investigation and discovery began at this stage if not before. At the commencement of a lawsuit, this allocation of services is about right, even though the numbers of hours expended for these categories, viewing major litigation generically, were on the high side if this were not a CERCLA case. But these figures otherwise comport with the expert testimony that CERCLA cases are more complex and more difficult to manage.

In 2011, as in every year, the category of "communications" was on the high side for generic litigation matters. The total of the communication hours was roughly subdivided by the Neutral Arbitrator into sub-parts, i.e., communication with clients, infra office, opposing counsel (of which there were many), and the court and mediation services.[20] One could quibble about so much time spent communicating, but when one considers that the main complaint of most litigation clients is never hearing from their attorneys, this, too, falls away. And with two plaintiffs, four counterclaimants and many other active parts of the case including expert consultants, Regional Board, Water Board, SACTO County, this number is reasonable and necessary. And, certainly under the keystone cases, defense costs themselves serve a dual-purpose, and go right to the heart of the question of liability.

Year of 2012. Much of what is said above about 2011 also pertains to 2012. There were a total of 2,536 line items, resulting in 1,430 hours of "covered" activity reduced to $389,009 of adjusted covered fees, which calculated out to roughly 89 percent covered [expended on defense of the counterclaims], in the opinion of the compiler of this document. In addition, now the costs of arranging a mediation crept into the time keeping, and grew with time with many settlement strategy discussions and meetings, coordination, pre-negotiations, costs, concerns about who was not going to pay for mediation, who was to participate, and whatnot. None of these costs was unreasonable or unnecessary.

[20] The calculations are far to rough and scribbled to be shared or made an exhibit.

Year of 2013. There were 2,627 line items, resulting in 1,740 hours of "covered" activity and $292,271 of adjusted covered fees, which calculated out to between 79 to 77 percent covered activities, in the opinion of the compiler of this document. Mediation and settlement activities categories showed very high in this year, as well as the very high number of hours in the defense of the terminating sanctions sought by Century Indemnity's Spoliation Action, defendant pleading issues with G. Nagler, many hours spent on discovery and deposition issues, not surprisingly for this later stage of the case. These all were reasonable and necessary.

Year of 2014. Per stipulation and not relevant herein for arbitration purposes, BAM incurred fees for Downey Brand in 2014 of $338,123 of which $236,854 is for covered purposes, resulting in a calculated percentage of 70% which is consistent with prior years. Further stipulated, the attorney fees for WFI and BAM in 2010 is $129,997—this is pre tender, thus there is no calculated break down, as pre-tender costs are not temporally linked to BAM's contractual right to recover from ARROWOOD.

Conclusion. The Neutral Arbitrator finds the totality of the 2011, 2012, and 2013 allocation of hours and fees contained in Exhibit K1-3 to be reasonable and necessary to avoid or at least minimize liability under *Aerojet* 2 any liability raised by the counterclaimants. Furthermore, it is likewise found that the incurred expenses served a dual purpose between the defense of the counterclaims and prosecution of BAM CERCLA Action. The Neutral Arbitrator from the totality of the evidence that the second of the *Aerojet* factors has been met, that is, the claimed defense costs were all reasonable and necessary to avoid or at least minimize liability.

Conclusion No. Six. The third factor of *Aerojet's* analysis has been met.

Finding No. 13. BAM has met its evidentiary burden to show defense costs were reasonable and necessary for the purpose of the defense of the counterclaims.

> "Third and final, the site investigation expenses must be reasonable and necessary for that purpose." *Aerojet,* 17 Cal.4th 38, 61.

Not only does the proposed expense need to be reasonable and necessary as lawsuits go, it also must be reasonable and necessary for that purpose—which means "reasonably related to the defense," so argued ARROWOOD correctly [AOB, pg. 9:14-15].

In the first place, if the defense costs are a reasonable and necessary in the effort to avoid or minimize liability [as in *Aerojet* factor two] as already found to be true, in this case where the defense costs serve a dual purpose, and where the boundaries between prosecuting costs and defendant costs are indistinguishable, and, where it has been determined that the defense costs are "not almost all defensive" because the same efforts overlap both offense and defense, then, by force of logic and definition, those same *Aerojet* 2 costs are also meet the burden for BAM in the *Aerojet* 3 category. Conclusion No. Five, and Finding Nos. 7-12 are incorporated herein as if fully set forth.

Defense costs serve a dual purpose. See Finding No. 8.

Defendant costs not almost exclusively defensive. See Finding No. 18.

Conclusion. BAM has met its burden here.

Finding No. 14. Overlap in defense costs between prosecuting and defending amounts to reasonable and necessary defense costs.

Mr. Goldberg, Esq., stated in his declaration at ¶ 13:

> ". . . a plaintiff's defense of a counterclaim filed against it in a CERCLA action will usually **overlap** with the prosecution of its original complaint. In both prosecuting the original action, and defendants the counterclaim, a plaintiff will be litigating issues of relative fault and responsibility for the contamination."

Mr. Soran, Esq., stated in his declaration at ¶ 33, about defending a CERCLA lawsuit, it may encompass identifying responsible parties, litigating equitable factors that bear on the parties respective contribution claims against each other. And in ¶ 34, in his experience, defense of a counterclaim will usually **overlap** the prosecution of the original complaint—in litigating issues of relative fault and responsibility for contamination. ARROWOOD offered no evidence or expert opinion on the issue of the overlapping of prosecuting and defending a CERCLA claim. Overlapping of prosecuting and defending efforts does not make the defense costs not reasonable and necessary for that purpose, i.e., of defending. Conclusion. The Neutral Arbitrator finds that an overlap of the prosecution costs with the defense costs, so long as the defense costs are reasonable and necessary to avoid or at least minimize liability and/or

1 reasonable and necessary to the defense, the defense costs are recoverable.

2 **Finding No. 15**. Evidence of Defense Costs analysis supports the allocation.

3 The diary of day-to-day events that circumscribe first the birth and then the passing of a
4 litigated case can surely be found in the history provided by the invoices. In fact, a review of
5 three years of just such block billing accounts of daily activities was indeed a window on the life
6 of this case with each period having its special character. Each day of each month, of each of
7 three years was reviewed line-by-line a second time to confirm the reasonableness and necessity
8 of the function reported therein including whether or not the function was in the defense of the
9 counterclaims. They are summarized below, and all support the conclusion that all but a
10 smattering were reasonable and necessary to avoid or at least minimize liability as well as
11 reasonable and necessary to that end.

12 **2011.** In the year of infancy to puberty of the CERCLA Action, the litigation focused
13 upon site investigation and initial discovery concerns about the counterclaims, with attention to
14 pleading, site investigations, consultants, strategy sessions involving experts and counsel,
15 governmental bodies and with heavier emphasis on discovery as the case grew older toward the
16 end of the year.

17 **2012.** From adolescence to middle age, the litigation matured into the more serious side
18 of discovery with identification and preparation of documents, witnesses, exchange of exhibits in
19 response to requests, making requests for discovery, depositions, and with a heavier focus on the
20 counterclaimants Joo and Armstrong, while the site investigations sharpened into questions of
21 boring sites, groundwater explorations, consultant reports, much contact with expert Kleinfelder,
22 attorneys for counter claimants, then maturing into depositions and preparation for them.
23 Meanwhile, the site investigation activities increased, with Regional Board concerns, RAP,
24 surveys, identification of contaminants, and a growing focus on response costs, and later, the
25 damage claims. Later that year, the focus turned to allocations and costs, and the parties began
26 discussing mediation; the spoliation motion began to infect the atmosphere, raising new
27 discovery issues, privilege claims, and contests over depositions. Counterclaimant names
28 showed up frequently toward the end of the year associated with pleading and questions about

stay of litigation, and probate code § 550 interests.

2013. From middle age to settlement, the focus of the litigation matured even more with a higher focus on discovery matters—heavily—including depositions, which included the spoliation witnesses, and a great many hours spent upon the Spoliation Motion defense filed by Century Indemnity. Regular discovery continued including site investigations, ascertainment of costs of remediation, discovery into allocation of fault between contaminators, and then focusing upon the many, many motions made by the counterclaimants, particularly G. Nagler, seeking an amendment of the counterclaim. The mediation occurred October 9, 2013—the preparation leading up to the mediation is reflected in many hours in meetings, marshaling of information and preparation of various mediation documents and preparation, once the mediator vendor and mediator was selected.

Randomized daily reports. In addition to the survey of daily activities, as a further delineation of the evidence that supports this view, a randomized review of one day each month was performed making special note of "keywords" that appeared in the block billing narrative, which would give a snap-shot the focus for that day only, with special attention being paid to the involvement of counterclaims. [The target day moved forward one day each month to make the selection random starting with January 6, 2011].

January 6. Armstrong, telecom with counterclaimant [hereinafter CCX].
February 7. Status report, discovery, litigation strategy, site investigation, RFPD.
March 8. Site status report, Nagler's RFPD, response costs, counterclaims.
April ~~9~~ 8. Joo, disclosures, documents and witnesses, depo preparation, Cooley Manion.
May 10. Site inspect/testing, Arnolds, cost estimates, site map, groundwater, evidence.
June 10 ~~11~~. Store profiles, Regional Board, Kleinfelder, invoices.
July 12. Kleinfelder, hole boring, work plan, site investigation, stay, strategy.
August ~~13~~ 14. Due diligence reports.
September 14. Site investigation, discovery issues.
October ~~15~~ ~~16~~ 17. Discovery and site investigation, Kleinfelder, EFS.
November 16 ~~17~~. Status of budget, discovery requests.
December ~~17~~ ~~18~~ 19. WCAB, discovery, soils.

January of 2012.

January 18 ~~19~~ ~~20~~. Soil vapor, SACTO Sanitation Dist., Joo depo, RFPD.
February ~~19~~ ~~20~~ 21. Investigation, expert consultant, Nagler.
March 20. Wong, site investigation, depositions.
April ~~21~~ ~~22~~ 23. Site investigation, depositions.
May 22. Time line, document lists, status, remediation.

June ~~23~~ ~~24~~ 25. RFPD, admissions, documents.
July 24. RAP, ground water investigation, remediation.
August ~~25~~ ~~26~~ 27. Kleinfelder, damages.
September 26. Site investigations, Panattoni, Joo, Nagler, mediation.
October ~~27~~ ~~28~~ 29. RAP, discovery, spoliation, stay of litigation.
November 28. Mediation, spoliation, discovery, site investigation.
December 28~~-29~~. Groundwater, pleadings, RAP.

January of 2013.

January 30. Century Insurance, Regional Board, discovery issues.
February 1. Discovery, Century Insurance.
March ~~2~~ 4. Kleinfelder, response costs, discovery, Century, privilege log.
April 3. Court order, mediation, stay, CCX, RAP, groundwater, Kleinfelder, discovery.
May ~~4~~ ~~5~~ 6. Stay, RAP, CCX Armstrong, settlement, discovery.
June 5. Stay, RAP.
July ~~6~~ ~~7~~ 8. Deposition, mediation.
August 7. Depositions, mediation, evidence, CCXs.
September ~~8~~ 9. Mediation, CCX, depositions.
October 9. MEDIATION!
November ~~10~~ 11. Regional Board, Pleadings, RAP, CCX, Spoliation.
December 11. Nagler motions-discovery, RFPD, admissions/interrogs, CCX.

Conclusion**.** The totality of this close evidentiary review of each of the 6,353 line item entries overwhelmingly demonstrated that the efforts expended on behalf of the defense of the counterclaims was not only reasonable and necessary for litigation, in general, to avoid or at least minimize liability [*Aerojet* 2] but, as well "for that purpose" to wit, "reasonably related" to the defense of the counter claims [*Aerojet* 3].

Finding No. 15. Spoliation costs are reasonable and necessary, and, reasonably related to the defense of the counterclaims**.**

In closing argument, ARROWOOD argued that at least 251 hours[21] were spent in the spoliation matter raised by Century Indemnity by way of a dispositive motion. The Neutral Arbitrator did not tally the exact number of hours, but the mediation and settlement expenditures were found to be substantial upon review, that is, either the figure suggested by Mr. Chorley, or greater. It was argued by ARROWOOD that this was a part of 2,659 hours asserted by ARROWOOD that should not be attributed as defense costs.[22] Regardless of the number of hours expended and allocated by BAM to defense costs and sought to be recovered by way of

[21] Received only as argument, not evidence due to a prior ruling.
[22] See FN 18 above.

attorney fees in this action, the question is: Is the defense of the Spoliation Action a reasonable and necessary expenditure to avoid or at least minimize liability and for the purpose of defense against the counterclaims.

The answer to both inquiries is YES. Little evidence of the spoliation issue has been presented—mercifully so. Attorney Goldberg testified that the spoliation action "was difficult" but it was successfully defended and involved up to seven different depositions and much pleading—obviously made more difficult because there were multiple parties involved. Suffice it to say, the Spoliation Motion was brought as a dispositive motion against BAM's CERCLA action, which, in the worst case scenario if successful, would have resulted in a dismissal of BAM's CERCLA action against all counterclaimants, or at the very least, it may have crippled BAM's effort to show 100% responsibility upon the subtenants through the imposition of issue and/or evidentiary sanctions against BAM's efforts in the CERCLA case to establish 100% liability upon the defendants/counterclaimants. A spoliation motion is not the same as a separate suit involving a third party affecting liability as seen in some of the cases cited by the parties, but it is brought within the present action and pertains specifically to it. In this case, it was brought about by plaintiffs decision to demolish the subject premises [Arnold's Cleaners], causing counterclaimants to argue that the destruction of premises was the '"intentional destruction of exculpatory evidence" thereby preventing subtenants from proving their affirmative case against BAM. A dismissal of BAM's CERCLA case would have been fatal to BAM's action to recover investigation and remediation damages. It is not necessary to correctly tally up the number of hours spent by Downey Brand in the defense of the Spoliation Action to determine if that expenditure of attorney time and costs was both reasonable and necessary [*Aerojet* issue 2] or reasonable and necessary for the defense of the counterclaims [*Aerojet* issue 3]. The defense costs so expended met the test. Conclusion. These spoliation expenditures were reasonable and necessary to avoid or at least minimize liability and reasonable and necessary, that is, reasonably related to mounting a defense, and, the Neutral Arbitrator finds the number of hours attributed to that effort was not excessive.

Finding No. 16. Mediation and settlement expenditures are reasonable and necessary for

the defense of the counterclaims.

In closing argument, ARROWOOD argued that at least 456 hours[23] were spent in the mediation and related matters—this is a truly high figure. On November 20, 2014, a question was posed to both counsel, raised from a confusing and contradictory quote in *obiter dictum* by the Court in *Aerojet*, *id* at 67, also found cited in *KLA-Tencor Corp.*, *id*, regarding settlement costs, and therefore, by implication, addressed to the costs of mediation as not being a legitimate and recoverable defense cost. The parties responded, as promised, filing supplementary briefs on November 26, 2014, and December 5, 2014.[24]

In ARROWOOD's supplementary briefs[25] on this specific issue, it is asserted as fact [erroneously so] that in each of the mediations and settlement discussions "BAM acted prosecutorily, demanding money from the other parties…" all of whom, "…in turn, offered to pay BAM in an attempt to settle the CERCLA action in exchange for appropriate releases from BAM. ARROWOOD further asserted, none of the counterclaimants demanded that BAM or WFI pay any money in exchange for dismissal of the counterclaims (except Nagler)" re attorney fees, and BAM never offered to pay any counterclaimant. None of these exact statements were elicited from any witness or admitted anywhere into evidence. The evidence testified to by Mr. Eric Garner, Esq., attorney for the Nagler parties, does not support ARROWOOD's exuberant arguments. First, it was stipulated that, if called, General Counsel Helen Singmaster, Esq., would have testified that all demands and offers that occurred in the case came within the mediation confidentiality, and there were none outside the mediation context—therefore none of the demands or offers came into evidence. It is true, Mr. Garner testified that Nagler had no investigation or remediation expenses and was making a claim for recovery of attorney fees [almost $166,000] but, he testified, Nagler was trying to recover as an *offset* to the CERCLA action any damage claim assessed against Nagler—through claims for contribution and indemnity, he testified. ARROWOOD offered other evidence that counterclaimants' response to discovery showed no site investigation costs. But, no other counterclaimant offered testimony

[23] Received only as argument, not evidence due to a prior ruling.
[24] All 30 pages read and considered.
[25] First, 11/26/2014, pg. 1 and again, 12/05/2014, pg. 2.

on this issue. ARROWOOD's "arguments" in this regard are accepted as just that—argument within fair comment as to what might be expected to have occurred in a series of mediations between all these parties and their insurance carriers, but none of it is supported directly by any evidence. It is recognized by the Neutral Arbitrator from the evidence offered by ARROWOOD that none of the counterclaimants may have had claims for any cost of investigation or remediation as they did, it appears, the nothing of the sort, as they were all out of possession of the premises with the CERCLA matter arose. There were certainly claims for attorney fees as in Gern Nagler's instance—it appears Nagler fought hard over amending his counterclaim at the end. According to BAM's arguments, which, in fact, carries the day, whether or not counterclaimants had investigative costs is irrelevant, because they were each claiming they were devoid of liability under the CERCLA Action, and BAM was 100% at fault, and each sought affirmative relief in their counterclaims against BAM should they, the counterclaimant, be found responsible for the contamination. See Finding No. 18 below on "almost exclusively defensive."

Evidence the mediation minimized liability. In both briefs [See FN 16] ARROWOOD argued that BAM presented no evidence about "…how 400 hours in attorney time…" minimized its potential liability. No so! The declaration of Robert Soran, Esq., who determined the allocation of fees by category stated in ¶¶ 26, 31 & 33, that settlement, as one of the categories, was identified as an objectively reasonable and necessary effort to avoid or minimize BAM's liability against the four counterclaims. Specifically noted in ¶ 11, was delineated by him the task of "litigating equitable factors that bear on the parties' respective contribution claims against each other." Both attorneys Steven Goldberg, Esq., and Olivia Wright, Esq., mirrored these assertions in their declarations. See Goldberg, ¶¶ 8, 10, 11, & 16. Specifically noted in ¶ 34, and others, was the task of "litigating equitable factors that bear on the parties' respective contribution claims against each other." See Finding No. 5.

BAM made out a prima facie case with this evidence supporting the conclusion that mediation and settlement were a reasonable and necessary effort to avoid or minimize BAM's liability. The burden shifted to ARROWOOD, who failed to offer any evidence to the contrary -- the aberrant and unsupported-by-rationale comments in *Aerojet* and *KLA Tencor* to the contrary

notwithstanding. Nothing goes more directly to the heart of "liability" than a good-faith mediation, about liability, about comparative negligence and about the expert-driven fact scenarios of contamination sources and costs of remediation along with discussions of the equitable factors that bear on all parties' contribution claims against each other. Mr. Goldberg testified at arbitration, in CERCLA actions, it is the judge as trier of fact who determines each party's responsibility under a section 113 claim for allocation. If not tried, the only other way these difficult issues can be resolved is by way of mediation or settlement discussions—those discussions surely go to liability and BAM's effort to avoid or minimize it. Of course, we have no evidence of what was demanded or offered by whom or what arguments were set forth to support those positions.

BAM's real and significant monetary exposure. In both briefs, ARROWOOD repeated its contention that BAM's exposure was limited. Again, the testimony of the CERCLA expert Attorney Goldberg at hearing supported BAM's claim of exposure for future cost of remediation of 1.6 million, or more, and that their cost of investigation was approximately $900,000; and the cost proposed by the Water Board might be in the $100,000 range. In his declaration at ¶ 37, he noted the Regional Board estimated the costs at $2,600,000.

Aerojet and *KLA Tencor*. Finally, ARROWOOD addressed briefly the issue that initiated the inquiry, the *Aerojet* comment and the *KLA Tencor* ruling, with the obvious note that the *Aerojet* Court did not explain its comment, and the court in *KLA Tencor* did not grant settlement costs in the reimbursement. In a one-paragraph headnote in *KLA Tencor*, the court cited *Aerojet* without explanation and denied recovery for settlement activities. BAM, in its November 26, 2014 letter brief explained that in *Aerojet*, "settlement" costs" meant "…settlement payment made after a settlement has been reached." BAM argued persuasively, settlement activities "…are quite obviously aimed at trying to 'minimize' an insured's liability." The Neutral Arbitrator agrees. Secondly, BAM argued cogently that the court held that "work prosecuting and obtaining an *adjudication* of patent infringement in Therma-Wave I was reasonable and necessary to establish the "truth" of the defense to the disparagement allegations in Therma-Wave II" but the actual settlement of Therma-Wave I was of no help in establishing such a

"truth" defense, and thereby, the fees for settlement activities were not recoverable.[26] This explanation make sense about the "stray" and unconnected finding in *KLA Tencor* that garnered this attention in the first place. Based upon this analysis, BAM argued that it "…makes no sense that legal fees associated with trying to reach a settlement are, as a matter of law, not 'defense costs.'" The Neutral Arbitrator agrees—having thought from the outset that the *Aerojet obiter dictum* comment simply made no sense at all, aided by no *per se* explanation in *KLA Tencor*. Nothing ARROWOOD argued changed this initial view, though the efforts by both parties in this regard were appreciated.

Finally, ARROWOOD falls back upon its unsupported-by-evidence argument that only BAM demanded money of the counterclaimants—while this may well be accurate, it was not proved in evidence, nor is it a reasonable inference that can be drawn from the evidence in the case. Conclusion. The Neutral Arbitrator finds that mediation and settlement expenditures were reasonable and necessary for the defense.

Other claimed unreasonable or excessive expenditures.

In closing argument, ARROWOOD argued that at least 33 hours were spent in the Stay of Action, 523 hours for insurance matters, and 857 hours for intra-office communications. See FN 20 herein. The purpose for the second review of all 6,353 line item entries was to independently evaluate BAM's claim that all invoiced hours were reasonable and necessary as well as reasonable and necessary to the defense, and determine whether all of the hours attributed to these sub-categories was reasonable and necessary. They were.

The Stays. In that review of the totality, the Neutral Arbitrator found the Motions to Stay the action were reasonable and necessary sufficient for both *Aerojet* 2 and 3 purposes based upon the reasons given for the stay in the block billing narrative. See Oppo., pg. 7, lines 1-6.

Insurance Matters. So long as the insurance matters claimed did not relate to the BAM – ARROWOOD insurance coverage suit but were within the framework of the CERCLA action and counterclaims, they too were reasonable and necessary for both *Aerojet* 2 and 3 purposes.

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[26] This same persuasive argument can and will be made for the reasonableness and necessity for the defense of the "spoliation" action, which if it had been successful, would have adversely resolved BAM's liability in favor of counterclaimants.

There were few such entries but each was too equivocal without back up documents to make a finding that they concerned the instant case and may have been overlooked by the author of Exhibit K1-3. ARROWOOD and Sedgwick were actively involved in the Burns Probate Code § 550 action themselves as a party, making any definitive determination difficult. No specific line items were brought to the fore by ARROWOOD.

Intra-office communications. No specific line items were offered into evidence to support the contention that 857 hours expended in this category was unreasonable, unnecessary or excessive. The general review of all line items failed to reveal any palpable or significant evidence that any of the alleged claims were unreasonable or unnecessary. In general, in reviewing for reasonable attorney fees, the time allocated to intra-office communications may be suspect as a dumping ground for stray hours, but in this complex case with so many moving parts and multiple lawyers, it was found not to be so.

Conclusion. These allocation of expenditures was reasonable and necessary to avoid or at least minimize liability and reasonable and necessary in mounting a defense, and, the Neutral Arbitrator finds the number of hours allocated to each category was not excessive; ARROWOOD has failed to meet it burden to show these expenditures were unreasonable and unnecessary.

Finding No. 17. BAM's exposure is considerable.

ARROWOOD argued that BAM's fees are not reasonably related to defense of the counterclaims because BAM's exposure from the counterclaims is very limited [Response, pg. 9:14-15]. It cannot be that the expense of almost "seven figures" is reasonable or necessary for the defense when BAM's exposure was so very little, argued ARROWOOD. [AOB, pg. 9:14-18]. Thus, urged ARROWOOD, the gross expenditures must have been for recovery of its own voluntary site investigation and remediation, not to defend the counterclaims that merely seek a setoff [AOB, pg. 9:19-23]. This syllogistic argument does not follow, because the argument is unsupported by evidentiary findings.

At first, ARROWOOD posited BAM's potential damages were only the sum of $165,000 attorney fees for the "Tort of Another" prayed for by counterclaimant Nagler, but then, later in

oral argument, ARROWOOD stated that at most, BAM's exposure can be is one-half of the total site investigation and remediation costs of 2.6 million, which figure is thus 1.3 million, due to the 50/50 cost sharing plan with the WFI plaintiffs in the underlying CERCLA action. ARROWOOD has sought to lessen this potential liability by offering proof with discovery responses [Response, pg. 6, fn. 3] that demonstrate no hard monetary damages were incurred by counterclaimants. The evidence offered by ARROWOOD about the purported lack of damages on behalf of the various counterclaimants is not persuasive. In Nagler's Response to BAM's Interrogatories [ARROWOOD Exhibit 8, Responses Nos. 7 and 18], Nagler admitting incurring "attorney fees" and "expert witness costs" and was seeking reimbursement for attorney fees, indemnification and contribution with respect to any judgment against Nagler. R. Armstrong's Response to BAM's Interrogatories [Exhibit 9, Response Nos. 9 and 20], Armstrong asserted it engaged environmental professions, attorneys, insurance, archeologists and others, and yet denied seeking specific damages from BAM. In Responses to Request for Admissions, [Exhibit 10, Response Nos. 56-57] they admitted not performing any voluntary investigation and remediation, but denied not incurring Response costs. This discovery is equivocal at best. Further, it has been determined that the total pass-through exposure by BAM to the counterclaimants in the CERCLA action is considerable--at least the figure argued by ARROWOOD, to wit, 1.3 million, and more, based upon the actual evidence presented.

Further, ARROWOOD argued that due to a series of expense sharing agreements with co-plaintiff WFI, BAM "cannot pay more than half" of all the costs incurred in site investigation and remediation, and that diminution of total value of the case ought to be a factor in determining the reasonable and necessary expenses according to the risk/analysis argument. [Oral Argument]. That may well be so. However, for purposes of evaluating the risk potential of the counterclaims in light of the duty to defend, the cost sharing agreements are irrelevant. BAM argued that its exposure was $867,000 for total site investigation and 1.6 million for remediation for a total exposure of about 2.6 million—that figure is uncontroverted [but not agreed upon]. ARROWOOD argued that BAM's maximum exposure under ARROWOOD's argument would

be half of that figure at best, due to the cost sharing agreements with WFI.[27] For purposes of the determination that the counterclaims were either offensive not "almost exclusively defensive" these figures are irrelevant. But they are substantial numbers in either case--as either the whole amount [2.6 million] or half of it, is substantial. ARROWOOD also argued in Oral Argument that BAM has already paid the investigating costs and started remediation of the site, hence, there can be no more liability imposed upon BAM. This argument ignores the fact that through the CERCLA action, BAM is attempting to recover this very same economic burden from the responsible parties by suing them, and they are suing back claiming BAM itself caused the negligence which caused the harm for the entire amount—even if BAM had a cost sharing agreement with WFI. Conclusion. The Neutral Arbitrator finds that BAM's exposure to the counterclaims is significant. See Finding No. 19.

Finding No. 18. The counterclaims are not "almost exclusively defensive."

This is the crux of the case. ARROWOOD contended that the "counterclaimants almost[28] exclusively seek to *offset* any amounts they may owe BAM." [Response, pg. 5:22-24]. This argument and use of he word "offset" is clearly an attempt by ARROWOOD to bend the instant facts in favor of the holdings in *James 3*, *CDM* and *Chang*. To be sure, BAM made the contrary arguments just as strongly [the Yin and Yang of the adversarial system and good lawyering, if you will] that is, the counterclaims are not defensive but are offensive, which argument is in the nature of the same attempt to bend[29] the instant facts toward the line of cases represented by *Aerojet*, *Barratt*[30], *TIG*, and *State*. As with every ardently litigated case, the instant facts may not so easily deflect as does the futbol into one or the other edge of the goal, as so vigorously contended by each party, but the true circumstances, the "sweet-spot" may lie somewhere along the spectrum---but where? That is what required an extensive analysis of the facts and law.

In the Sur-Reply [09/08/2014], ARROWOOD made its bottom-line argument abundantly

[27] This argument by ARROWOOD flies in the face of the argument made in the Sur-Reply at page 3, lines 26-28 wherein it was contended that the cost sharing arrangements "guts" the effect of any indemnity counterclaim liability to co-plaintiff. Reducing the potential claim from 2.6 to 1.3 is hardly "gutting" it.

[28] While never explained or defined by ARROWOOD, "almost" more than likely refers to the fact that in the Nagler counterclaim, ARROWOOD acknowledges the claim for attorney fees attributable to the "tort of another."

[29] Not meant in the pejorative sense, but as in "bending" the soccer ball by putting a spin on it—as in "Beckham." This is the stuff of good advocacy.

[30] For the construction defect lawsuit, not the voluntary repairs to non-plaintiffs.

clear: BAM and WFI did not sue each other, but together, voluntarily investigated and sought to remediated the property in order to develop it for commercial purposes in light of there being no CGL coverage for the preexisting pollution and contamination; thus, to recover these same costs, BAM and WFI sued the prior owners and operators of the dry cleaners who timely and conveniently counterclaimed against BAM and WFI, giving rise to BAM's attempt to "morph" its prosecutorial fees and costs in the CERCLA action [not otherwise covered by ARROWOOD's CGL policy] into "defense" and response costs through the counterclaims, which seek "offset" against BAM's action against the counterclaimants. [Sur-Reply, 1:10-2:14]. Offset or affirmative action? At least ARROWOOD is not shy about its subjective belief—calling this scenario "a scheme[31] hatched" by BAM to circumvent the language and exclusions of the policy. [See also, Sur-Reply, 5:6-8].

After close consideration of the unique facts of this case and the considerable amount of law that has evolved over the years, it was inevitable that ARROWOOD would make this challenging argument. And as appealing as this "motive" argument of ARROWOOD may be, the case cannot be decided upon ARROWOOD's subjective beliefs—it must be objectively decided from the evidence and by the law. In the end, the Neutral Arbitrator finds nothing nefarious about any part of the "arguments" posited by ARROWOOD or, on the other hand, about the "scheme" hatched by BAM. But it is not ARROWOOD's subjective belief and arguments thereon, or BAM's subjective motives, that carry the day—the court in *Aerojet-General* mandated that the "objective" test for everything be applied, not the subjective intent of the parties. So it is!

As the non-property owner plaintiff, BAM contended that the counterclaims are "offensive" in nature, as counterclaimants were also sued by the property owner WFI, who sought to recover for property damage WFI suffered from the pollution and contamination caused by the sub-tenants, cross-complaining parties herein. As a plaintiff, the WFI suit also exposed each of the counterclaimants to liability for the entire cost of the site investigation and remediation costs through the CERCLA action, whereupon each counterclaimants sued BAM,

[31] See Response, 12:8.

the master-tenant, for its BAM's negligence and contribution and for equitable indemnity, thereby exposing BAM to the very same degree of liability counterclaimants were themselves facing in the property owner WFI's suit against them. [Reply, pg. 5].

The counterclaims may well be both offensive AND defensive claims, derived from the claims WFI is prosecuting, but they are not almost "exclusively defensive" as argued by ARROWOOD. BAM cited *State of California v. Indemnity Company, supra* where the Court found the insurer was obligated to defend the counterclaims in their entirety but insurer could seek reimbursement for claims not even potentially covered. This finding alone changes the bend-it-vector in counsels' arguments more to a trajectory favoring a corner goal by BAM.

The Neutral Arbitrator finds that the counterclaims are NOT "almost exclusively defensive." Looking at them individually, each counterclaim contained the affirmative causes of action sounding in negligence and nuisance while also containing causes for indemnity and contribution—these very defenses may be intertwined with the prosecution of the contamination action by BAM as to be inextricably intertwined with BAM's offensive CERCLA suit. Indeed, as argued by BAM, the gist of the all of the counterclaims is all sub-tenants are seeking recovery against WFI and BAM for ALL potential damages claimed against the counterclaimants by plaintiffs. As BAM was the master leaseholder, it should be noted that the negligence causes of action are aimed at plaintiff BAM, as Cross Defendant, of whom it is alleged in the counterclaims "inadequately maintained the property, sewers, flooring and parking lot," among other things. See [R. Armstrong, Exhibit D-3, ¶10], [G. Nagler, Exhibit D-5, ¶21], [Y. Panattoni, Exhibit D-7, ¶22] and [Century, Exhibit D-9, ¶¶22, 35, 36]. The Hon. John A. Mendez articulated that BAM met its initial burden of establishing there is a potential for coverage under the Pre-1985 Policies. [Exhibit E-5, page 12, lines 24-25; page 11, lines 10 to page 13]. ARROWOOD had the opportunity in court to get a ruling that there was NO potential for coverage, but that failed. [Exhibit E-5, page 11:4-7][32]. While the conundrum facing the trier-of-fact under these circumstances would have raised some interesting questions about assessing liability and/or comparative fault, we here are only focusing upon the reasonableness and

[32] Interestingly, the court also granted ARROWOOD's motion for summary judgment as to he Post 1985 Policies, finding no potential for coverage.

necessity of BAM as plaintiff to both prosecute its own action seeking 100% liability against one or all of the counterclaimants while at the same time, defending against the counterclaimants who are seeking 100% liability against BAM in their own in defense of the WFI [and BAM] CERCLA complaint against them. BAM is acting both affirmatively and defensively at the same time. That circumstance alone makes the counterclaims per force of logic not "exclusively defensive." More importantly to the analysis under the cases, had BAM alone dismissed its own claims against the counterclaimants, counterclaimants would still have grounds to maintain all of their own counterclaims against BAM, so long as WFI maintained its CERCLA suit against counterclaimants.

Were it the intention of all counterclaimants to seek only an "offset" against BAM and WFI, they might have said so by taking the less expensive way out by simply pleading an offset; but they did not, selecting the more pervasive and positive action of filing a comprehensive counterclaims instead. Conclusion. The Neutral Arbitrator finds the counterclaims are not "almost exclusively defensive." The evidence supports BAM's contention that the counterclaims are offensive in nature, and are independently sustainable as it relates to shifting the CERCLA potential liability from the counterclaimants to BAM.

Finding No. 19. The "Reasonable-insured-under-the-same-circumstances" test is met.

ARROWOOD contended BAM's attorney's fees are grossly disproportionate to its exposure. [Oppo. pg. 15, line 20 *et seq*.]. Therefore, they argued, the fees aren't reasonable. Of course, this argument is postulated on ARROWOOD's version of the facts not found to be true. These arguments have been rejected. See Conclusion Nos. Five and Six, Finding No. 17.

The Court in *Barratt* also found [*Barratt,* 102 Cal.App.4th 848, 862]:

> "Instead, a developer seeking reimbursement for repair costs to homes not the subject of a lawsuit must present evidence that a reasonable insured would have engaged in a similar defense strategy, which necessarily involves a consideration of **whether the benefits of the strategy are worth the cost**. (*Aerojet-General*, *supra*, *id* at p. 62.) [Emphasis added]

Evidence of Experts.

Neither Mr. Soran, Mr. Goldberg nor Ms. Wright were asked directly to express their expert opinion as to whether or not a "reasonable insured under the same circumstances" facing potential liability of 2.6 million in remediation costs would expend the defense costs BAM is now seeking to recover from insurer ARROWOOD. Without restating all of the testimony given by Mr. Goldberg at hearing, the bottom line of his expressed opinions is that the fees he reviewed and certified were reasonable and necessary to avoid or at least minimize liability [*Aerojet* 2] and reasonable and necessary for the defense of the counterclaims [*Aerojet* 3]. He also answered the question the same way when he was asked about the exposure BAM faced to the counterclaims. He was aware of the cost of investigation so far and the estimated cost of remediation when he expressed that opinion. Mr. Goldberg further justified the high defense costs as being consistent with his experience with 25-30 CERCLA actions in the past. Finally, it was his opinion that the counterclaims actually sought 100% of the costs of remediation from BAM. In his declaration, Mr. Goldberg declared [¶ 14] that BAM's exposure was significant, facing total costs of approximately 2.6 million, and given this exposure, the total fees of "832,970.42," he declared were "…objectively reasonable and necessary for the purpose of defending Bel Air against that exposure." [Decl., ¶ 16]. Mr. Soran declared [Decl., ¶ 37] "The potential exposure facing Bel Air in the CERCA Action was an is significant." And "…estimated to be approximately $2,600,000 [*id*]. Further, he declared, "…the fees are in my opinion objectively reasonable and necessary for the purpose of defendant Bel Air against that exposure." [supra]. While arguing the point unflinchingly, ARROWOOD presented no evidence to the contrary by way of expert opinion direct or circumstantial.

Where the benefits worth the cost? YES! The actual settlement figures are irrelevant. See below. What is significant about the numbers in this case lay with the ratio between the defense costs compared to the exposure to potential liability.

The total fees recoverable in Phase III are $545,779 from total defense costs for the pertinent period of $831,970. For purpose of this analysis, one might add in the expenditures the pre-tender costs, and those of WFI, and incurred fees with Downey Brand from January to October of 2014 in order to arrive at a total attorney fee as defense cost of about $950,000.

Compared to the 2.6 million of estimated potential exposure, the comparison ratio is favorable toward the conclusion that the benefit was worth the cost. Even if the figure were one-half the 2.6 million, to wit 1.3 million, as urged by ARROWOOD [Oppo., pg. 18, line 21], while less favorable, the ratio is still worth the benefit, particularly considering the uncertainty of and high cost of actual litigation today. Conclusion. The Neutral Arbitrator finds the reasonable insured under the same circumstances test set forth in *Barratt* has been met.

Finding No. 20. The holdings and finding of *CDM* and *Chang* are inapposite.

The factual findings made in both the *Chang* and *CDM* cases, relied upon by ARROWOOD, are significantly and factually distinguishable as argued by BAM [Reply, pgs. 3-6]. In neither case did the defendants there, claiming an offset, have an independent action which would have resulted in an independent lawsuit that could have been brought against plaintiffs Chang or CDM who sued then initially—a fact which differentiates and distinguishes *Chang* and *CDM* from the instant matter.

BAM makes two additional arguments, which distinguish the holdings in *Chang* and *CDM,* both of which are supported by the facts. (1) BAM argues persuasively [Reply, pg. 5], had either plaintiff in *Chang* or *CDM* dismissed their affirmative lawsuits, none of the defendants filing cross-complaints would have had any independent actions against either, whereas, argued BAM, if BAM dismissed its complaint against the counterclaimants, the surviving WFI action would leave untouched the counterclaims against BAM [with affirmative relief plead by way of negligence, indemnity and contribution against BAM (and WFI)]. That this did not happen after many years of litigation does not affect ARROWOOD's duty to defend, which can only be viewed prospectively, not retroactively, or our analysis about it. Furthermore, (2) BAM argued persuasively [Reply, pg. 6] there was no order that BAM incur remediation costs by the Water Board as in the *CDM* case, where it was said by the court that the counterclaims "functioned only to re-impose upon CDM for what CDM was already legally obligated. *CDM*, *supra* at 1269. Not so here. There was no order that BAM pay anything—an uncontroverted argument continually made by ARROWOOD on another issue. Certainly, as orally argued by ARROWOOD, BAM may have been subject to allocation of responsibility in

the CERCLA action, but that, too, did not happen. BAM argued persuasively that the counterclaims facing BAM presented potential liability for the "entire cost of clean up at the Arden Way Property." As BAM is not the owner of the property, argued BAM, BAM would not have been exposed to this potential liability without the counterclaims having been filed. BAM's arguments carry the day. Conclusion. The Neutral Arbitrator finds *CDM v. Travelers* and *Chang* are inapposite under their own facts and the factual findings made herein.

See Appendix One, Item Four for further discussion of *Chang*, *CDM*, and *TIG*, relocated for sake of brevity.

Finding No. 21. Settlement figures are essentially irrelevant except for application of the *Barratt* "reasonableness" test.

As the good advocates they are, counsel for BAM and ARROWOOD did not miss their last chance to argue their respective positions—all in the last exchange of e-mails on or about December 9 and 10, 2014. These were in response to the Neutral Arbitrator's comment that the settlement figures may have "some" relevance to the issues to be decided [a cagey comment if ever one were devised]. Of course, the Neutral Arbitrator had in mind but did not wish to "tip-his-hand" about the ancillary question posed in *Barratt* regarding applying the "reasonable insured in the same circumstances" analysis for which some mile markers were needed, to wit, the approximate total amount spent against the approximate or potential liability, on which issue the actual settlement "may have some relevance." As it turned out, there is no relevance found in the final figures.

To this, ARROWOOD argued the settlement is relevant to show that the CERCLA action is really about BAM collecting money, not about BAM's exposure to the counterclaimants and the attorney fees claimed are not reasonable and necessary to the defense of BAM's "limited and theoretical exposure." It has been found that the BAM's exposure was considerable, being approximately 2.6 million. And, the total amount of fees claimed as defense costs bore a reasonable relationship to the exposure, that is, objectively, and not with hindsight, thus, it would not be unreasonable for a party in the same circumstances to expend $800,000 plus in defense costs defending a potential recovery of more than three times that amount. That is the finding.

1 BAM's arguments as to lack of relevancy are cogent and bears comment. The view is
2 not retroactive, but prospective, not knowing as we now know that the case would actually settle.
3 And further, the actual settlement, the Neutral Arbitrator agrees, as in most settlements, has little
4 to say about the amount of or the reasonableness of the fees. Lastly, regardless of the amount of
5 the settlement, the reasonableness of the amount spent on defense costs would be the same,
6 except in meeting the *Barratt* test of the reasonable insured in the same circumstances, which in
7 this case, has been done successfully. See Finding No. 19 above.
8 ARROWOOD filed an e-mail response, first objecting to the claim that $2,540,865 was
9 the amount of clean up costs in the RAP—noted before but with a supporting factual finding
10 about the evidence offered. ARROWOOD repeated its previous contentions that
11 counterclaimants have no affirmative claims for remediation against BAM, BAM voluntarily
12 agreed to remediate with no governmental suit, the estimated costs of clean up are not the proper
13 basis for calculating BAM's exposure (but show BAM's economic interest in pursuing its
14 affirmative claims), the *Chang* case applies, the counterclaims are only an offset, all of which
15 have been resolved herein. But thanks for the reminder by way of a check list.
16 **Finding No. 22.** The allocation of fees between prosecution and defense was correct.
17 Incorporated herein as if fully set forth are Finding Nos. 6-22, but specifically Finding
18 No. 16. Conclusion. Based upon the totality of the evidence, the Neutral Arbitrator finds the
19 allocation of fees made by Downey Brand between prosecution costs and defense costs to have
20 been supported by a preponderance of the the evidence, and accordingly, the allocation is found
21 appropriate.
22 **Finding No. 23.** ARROWOOD is not entitled to reimbursement of what was paid.
23 ARROWOOD contended in it remarks in conclusion that it is entitled to reimbursement
24 of a substantial portion of the $297,066 already paid to BAM because the fees were not
25 reasonable and necessary, were almost exclusively defensive, and not reasonably related to
26 BAM's limited exposure. [Oppo. pg. 20, lines 9-15]. Incorporated herein as if fully set forth are
27 Finding Nos. 7, 10, 12, 13, 14, 17, 18, and 19. Conclusion. The Neutral Arbitrator's findings on
28 each of the arguments made by ARROWOOD preclude a award in its favor reimbursing any of

the amounts already paid.

D. DISCUSSION OF SOME OF THE CASES REVIEWED.

No Affirmative counterclaims or cross-complaints under *James 3*.

See discussion of *James 3 Corp. v. Truck Insurance Exchange,* 91 Cal.App.4th 1093 (2001) at Item One, Appendix One [relocated for sake of brevity].

No Separate actions under *Larkin*.

See discussion of *Larkin v. ITT Hartford*, (ITT Hartford Insurance Group), 1999 WL 459351, at Item Two, Appendix One [relocated for sake of brevity].

No cross actions where *"no potential for coverage."*

See discussion of *Continental Casualty Company v Superior Court (Paragon),* (2001) 92 Cal.App.4th 430, at Item Three, Appendix One [relocated for sake of brevity].

Some addition comments derived from a review of cases not cited by the parties.

Block billing. A cursory reading of some of the cases read but not cited by the Parties [nor was the issue was raised by anyone] is the issue of block billing. This has to do with a "negative lode-star" reduction made by some courts for vacuous block billing. In the hundreds of block billing invoice line items reviewed, these are among the most legible, cogent and complete billing narratives seen recently by the Neutral Arbitrator in reviewing attorney billing to establish reasonable attorney fees. Accordingly, there is no percentage diminution assigned by way of incomplete block billing.

Hour increments. Similarly, some courts were negatively influenced by reason of overly large [and unexplained] hourly increment used in the block billing. Not so here. Consistent with modern billing practice, the one-tenth of one-hour (or six minutes) was utilized by Downey Brand—entirely appropriately. Accordingly, there is no percentage diminution assigned by way of excessively high increment billing.

E. REGARDING PRE JUDGMENT INTEREST

Conclusion No. Seven. BAM is awarded $81,781.94 for pre-judgment interest.

Finding No. 24. BAM's claim for pre-judgment interest meets the test under C.C. § 3287 and the cases.

BAM contended that unreasonable delay in paying policy benefits or paying less than the amount due may be actionable as a breach of the contract as bad faith which gives rise to tort damages. [OLB, pg. 14]. Further, BAM claimed pre-judgment interest [OLB, pg. 14] now in the sum of $81,781.94 . BAM argued [Reply Letter Brief, pgs. 7-8] that § 3287 is to be liberally construed to permit recovery of prejudgment interest citing *Chesapeake Indus. Inc. v. Togova Enterprises, Inc*. (1983) 149 Cal. App.3rd 901, 907, and ARROWOOD's argument was rejected in *Safeway Stores Inc. v National Union Fire Ins. Co* (9th Cir. 1995) 64 F. 3d 1282, 1291. In turn, ARROWOOD argued no pre-judgment interest is owed for an amount of defense expenses "not certain" until a ruling in this arbitration [Oppo. pg. 19, line 15, *et seq*.]. ARROWOOD argued the sum was not rendered certain until the arbitration is concluded, relying on *St. Paul Mercury Ins. Co. v Mountain West Farm Bureau Mut. Ins. Co*. (2012) 210 Cal.App.4th 645, 665 [*id*, pgs. 19-20].

The test applied by all three courts in their opinions is: "(1) did the defendant actually know the amount owed or (2) from reasonably available information could the defendant have computed that amount. Regarding ARROWOOD, the answer to both tests is YES. ARROWOOD knew of the amounts owed, as it is uncontroverted that each invoice, after redactions, was timely sent and received by ARROWOOD. Secondly, each monthly invoice sent was redacted by Downey Brand showing the allocation analysis consistent with efforts designated as "covered" opposed to those that were non-covered. That the parties had a dispute as to liability over the invoices does not make the exact sums not certain, pursuant to the cases. Conclusion. The Neutral Arbitrator finds from the evidence that ARROWOOD knew the actual amounts owed contemporaneously in each invoice submitted and had the exact information asserted by Downey Brand as being a "covered" versus a non-covered expense, and accordingly, finds BAM is entitled to recover prejudgment interest as calculated.

V. POSTSCRIPT ONE

This Notice of Interim Award was electronically transmitted to all counsel in the late evening hours of January 31, 2015, and will be served regular mail by Judicate West with Proof of Service sometime thereafter. It is not a tentative ruling, but an Interim Final Award on the

issues presented and resolved, joining the previous two Interim Awards, all as agreed by the parties at the outset.

[Neutral Arbitrator's note: having spent an large amount of time in producing this Final Interim Award, the actual hours expended [about 100 hours] was reduced by approximately 80% out of an expression of courtesy and acknowledgement of your patience in permitting a complete and thorough understanding and analysis of the complex factual and legal issues before making a decision. See Billing Memorandum].

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IT IS RULED AND ORDERED AS AN INTERIM AWARD.

DATED: JANUARY 31, 2015

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Hon Robert J. Polis (Ret.)
Neutral Arbitrator
Judicate West