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Research on good-faith determination of settlement under California Law

Introduction

Client, a subcontractor, along with other subcontractors, was hired by a general contractor to build a hospital on Winnebago tribal territory. The tribe sued the contractors for taxes due on the construction revenues. The general contractor then sued the subcontractors. Client had a contractual indemnity agreement with the general contractor, and was being sued under the theory of joint and several liability. However, client entered into a settlement agreement with the tribe. The judge refuses to make a determination that the settlement agreement was made in good faith because of the two outstanding issues of (i) joint and several liability, and (ii) contractual indemnity.

Questions Presented

1. Under California law, should a settlement agreement be deemed to have been made in good faith despite the fact that the non-settling entities are still being sued under joint and several liability?
2. Does the existence of an indemnity agreement preclude a party from settling in good faith?

Short Answers

1. Yes, if the settlement was entered into for a reasonable amount, the settlement should be deemed to have been made in good faith notwithstanding the fact that other defendants are sued under the theory of joint and several liability.
2. No, the existence of an express indemnity agreement does not preclude a party from settling in good faith

Discussion

I. DEFENDANTS BEING SUED UNDER A THEORY OF JOINT AND SEVERAL LIABILITY ARE NOT PRECLUDED FROM INDIVIDUALLY ENTERING INTO A GOOD FAITH SETTLEMENT WITH THE CLAIMANT.

Far from being a bar to a determination of a good-faith settlement, the existence of the issue of joint and several liability is the very reason why such a determination would be necessary in the first place. Under common law, there was no right of contribution among tortfeasors. *Tech-Bilt Inc. v. Woodward-Clyde & Assoc.*, 38 Cal. 3d 488, 492 (Cal. 1985). If one joint tortfeasor settled, all the others would be released from liability, creating a powerful disincentive to settle. *Id.* *Cal Code Civ Proc* § 877 was passed to ameliorate these harsh effects. *Id.* It provides that a “good-faith” settlement does not discharge other joint tortfeasors from liability, but does reduce their liability by the amount of the settlement. “The good faith language was added to give the courts occasion to review settlements between a plaintiff and one of several joint tortfeasors to determine whether they prejudiced the interests of a nonsettling tortfeasor.” *Id.* at 495 n. 4. Thus the existence of joint tortfeasors is not a bar to the “good-faith” determination, but rather the purpose for it.

After California adopted comparative negligence, the legislature responded by passing *Cal Code Civ Proc* § 877.6, which provides that a section 877 settlement bars claims for partial or comparative indemnity or for contribution. “It also specifically reiterates the proviso that a settlement must be made in good faith before it will operate as a bar and clarifies the procedures for judicial determination of the good faith issue.” *Id.* at 496. Section 877.6 provides the framework under which a settlement in a multiparty litigation can be determined to be in good faith and the amount by which plaintiff’s claim has been diminished can be precisely calculated. *Dillingham Construction, N.A., Inc. v. Nadel Partnership, Inc.*, 64 Cal. App. 4th 264 (Cal. Ct. App. 1998). The statute permits any party to an action where the parties are sued as joint tortfeasors to enter into a good faith settlement with the plaintiff or claimant. There is nothing in the language of the statute that precludes a joint tortfeasor from individually settling his liability with the claimant/plaintiff. However, client’s settlement agreement with the tribe will be valid only if it is made “in good faith.”

Because the “good faith” determination of a settlement is intended to protect non-settling joint tortfeasors, the issue of joint and several liability is by no means a bar to the determination. Any potential joint tortfeasor, even those not named in a suit at the time of the settlement, has a due process right to be heard on the issue of whether the settlement is in good faith. *Singer Co. v. Superior Court*, 179 Cal. App. 3d 875, 896 (Cal. Ct. App. 1986). Twin safeguards protect non-settling defendants against unfair results or violation of their due process rights: (1) the adverse nature of the settlement negotiations; and (2) the requirement of court approval of the settlement elements before they may be given full effect.” *Dillingham Construction, N.A., Inc.*, 64 Cal. App. 4th 264, 281 (Cal. Ct. App.

1998). Although all joint tortfeasors have a right to be heard, settlements are presumed to be in good faith and the party asserting the lack of good faith bears the burden of proof. (§ 877.6, subd. (d).) *Standard Pacific of San Diego v. A. A. Baxter Corp.*, 176 Cal. App. 3d 577, 581 (Cal. Ct. App. 1986).

In determining whether a settlement was made in good faith or not, courts must look at whether the settlement amount is reasonable in light of the settling tortfeasor's proportionate share of liability. *Standard Pacific of San Diego v. A. A. Baxter Corp.*, 176 Cal. App. 3d 577, 588 (Cal. Ct. App. 1986). A determination of good faith involves questions of whether the settlement (1) was proportional, (2) took into consideration the financial condition of the settling tortfeasor, and (3) did not evidence tortious conduct toward non-settling tortfeasors. *Singer Co. v. Superior Court*, 179 Cal. App. 3d 875, 896 (Cal. Ct. App. 1986). Factors relevant to determining whether a settlement was made in good faith under section 877.6 include: a rough approximation of plaintiffs' total recovery and the settlor's proportionate liability, the amount paid in settlement, the allocation of settlement proceeds among plaintiffs, and a recognition that a settlor should pay less in settlement than he would if he were found liable after a trial. *Standard Pacific of San Diego*, 176 Cal. App. 3d 577, 583 (Cal. Ct. App. 1986). Other relevant considerations include the financial conditions and insurance policy limits of settling defendants, as well as the existence of collusion, fraud, or tortious conduct aimed to injure the interests of the nonsettling defendants. Finally, practical considerations require that the evaluation be made on the basis of information available at the time of settlement. *Id.* A "good faith" settlement does not call for perfect or even nearly perfect apportionment of liability. What is required is simply that the settlement not be grossly disproportionate to the

settlor's fair share. See *Abbott Ford, Inc. v. Superior Court*, 43 Cal. 3d 858, 877 (Cal. 1987). Thus, if the client has paid the tribe a proportionate amount in settlement, then there is no reason for the court to withhold a determination that the client's settlement agreement is in good faith.

A good-faith settlement cuts off the right of other defendants to seek contribution or comparative indemnity from the settling defendant, and the non-settling defendants obtain in return a reduction in their ultimate liability to the plaintiff. See *Mayer v. Bryan*, 139 Cal. App. 4th 1075 (Cal. Ct. App. 2006). Under Code of Civil Procedure section 877.6, subdivision (c), if a court determines a tortfeasor made a settlement in good faith, then any other joint tortfeasor is barred from any claims against the settling tortfeasor for equitable comparative contribution, or partial or comparative indemnity, based on comparative negligence or comparative fault. However, the non-settling defendants obtain in return a reduction in their ultimate liability to the plaintiff. *Regan Roofing Co. v. Superior Court*, 21 Cal. App. 4th 1685, 1700 (Cal. Ct. App. 1994). The plaintiff's recovery from non-settling tortfeasors is diminished only by the amount that the plaintiff has actually recovered in a good faith settlement, rather than by an amount measured by the settling tortfeasor's proportionate responsibility for the injury. *Dillingham Construction, N.A., Inc.*, 64 Cal. App. 4th 264, 278 (Cal. Ct. App. 1998). Thus, under the terms of section 877, a settlement -- if found to be in "good faith" -- has *two* interrelated consequences: (1) it discharges the settling tortfeasor from all liability to other defendants for contribution or indemnity, and (2) it reduces the plaintiff's claims against the other defendants by "the amount of consideration paid for it." *Abbott Ford, Inc.*, 43 Cal. 3d 858, 877 (Cal. 1987). Thus, the consequences of a settlement by one joint tortfeasor on

the non-settling ones are carefully provided for by a statutory scheme, under which a determination of good faith is integral. There is simply no legal justification for the proposition that the existence of joint and several liability in any way bars a good-faith settlement approval.

II. THE EXISTENCE OF AN EXPRESS INDEMNITY AGREEMENT IS NOT A BAR TO GOOD FAITH SETTLEMENT BECAUSE THE SETTLEMENT HAS NO AFFECT ON THE CONTRACTUAL INDEMNITY RIGHT.

Because the general contractor's express contractual right to be indemnified by client is unaffected by client's settling with the tribe, the issue of indemnity is not a bar to a finding that the parties settled in good faith. If the Court determines that a settlement was made in good faith, the other joint tortfeasors or co-obligors are barred from making any claims against the settling party for partial or comparative indemnity under *Cal Code Civ Proc* § 877.6 (c), which reads in relevant part:

(c) A determination by the court that the settlement was made in good faith shall bar any other joint tortfeasor or co-obligor from any further claims against the settling tortfeasor or co-obligor for equitable comparative contribution, or partial or comparative indemnity, based on comparative negligence or comparative fault.

However, this provision only applies to equitable indemnity and does not affect the right to sue for contractual indemnity. *Bay Development, Ltd. v. Superior Court*, 50 Cal. 3d 1012, 1032 (Cal. 1990). A contractual right of indemnity will survive a good-faith settlement. *C. L. Peck Contractors v. Superior Court*, 159 Cal. App. 3d 828, 834 (Cal. Ct. App. 1984). The Legislature, by specifying equitable comparative indemnity in *Cal Code Civ Proc* § 877.6 (c), evidenced its intention to exclude contractual indemnity from the purview of that section. *Id.* In *C. L. Peck Contractors*, a worker was injured while working at a construction site. He sued the general contractor, the owner of the property,

and a subcontractor. Plaintiff settled his claim against the subcontractor, and the trial court dismissed all cross-claims for indemnification, holding that a under *Cal Code Civ Proc* § 877.6, a good-faith settlement extinguishes all claims for indemnity, even those provided for by contract. The appellate Court reversed the decision, holding that when parties by express contractual provision establish a duty in one party to indemnify another, the extent of that duty must be determined from the contract and not from the doctrine of equitable indemnity. The court found that the provisions of *Cal. Civ. Proc. Code* § § 877 and 877.6 do not operate to bar otherwise valid claims of express contractual indemnity, and that such claims survive a good faith § 877.6 settlement:

We hold that an indemnity claim against a codefendant based on express contract survives a good faith section 877.6 settlement. The Legislature, by specifying equitable comparative indemnity, evidenced its intention to exclude contractual indemnity. The language of section 877.6 is clear, and we are not free to depart from it.

Id. at 834.

Thus in general, the settlement agreement cannot affect contractual indemnity. Clever parties, however, may be able to construct a settlement agreement that indirectly defeats the indemnity right. Even in such cases, the settlement is not necessarily in bad faith. For example, in *Bobrow/Thomas & Assocs v. Superior Court*, 50 Cal. App. 4th 1654 (Cal. Ct. App. 1996), subcontractors settled a case with plaintiff in return for an agreement that the plaintiff would not seek recovery in the ongoing suit with the contractor for any claims based on derivative liability based on the performance of the settling parties, thus limiting the claims against the contractor to professional negligence that would not be covered under the express indemnity agreement with the settling subcontractors. *Id.* at 1659. The Court noted that the settlement agreement was

“ingenious.” *Id.* at 1661. It was constructed in such a way as to cut off the contractual indemnity right, which would otherwise have survived a settlement. *Id.* at 1662. Even in these circumstances, the settlement was not automatically deemed to be in bad faith, however. The Court ruled as follows:

We conclude that the court erred in confirming the settlement. This does not mean the settlement itself is void. Upon presentation of the full details of the settlement, including how the continuing trial is to proceed and what commitments Sutter has made about recovery, the court may confirm the settlement again if it meets the requirements for good faith.

Id. at 1664.

Thus, a contractual indemnification will not bar a finding that a settlement was made in good-faith. Generally, the contractual indemnification right is completely unaffected by a settlement. Even in rare cases where the parties are able to tailor their settlement agreement to defeat indemnity, the court may still make a determination of good-faith.

Conclusion

1. Code of Civil Procedure section 877.6 permits any party to an action where the parties are sued as joint tortfeasors on a contract debt, to enter into a good faith settlement with the plaintiff or claimant. The settlement would be deemed valid only if it is made in good faith. If the client’s liability has been settled for a reasonable amount, the settlement agreement would be deemed to have been made in good faith.
2. The existence of an indemnity agreement does not preclude a party from settling in good faith. An indemnity claim against a codefendant based on express contract will survive a good faith section 877.6 settlement. Because the

indemnity right is unaffected, the issue should not be a bar to a determination that a settlement was made in good faith.