IN THE SUPREME COURT OF THE STATE OF OREGON

MONTARA OWNERS ASSOCIATION, an Oregon non-profit corporation,
Plaintiff,

v.

LA NOUE DEVELOPMENT, LLC, an Oregon limited liability company; et al.,
Defendants.

LA NOUE DEVELOPMENT, LLC, an Oregon limited liability company,
Third-Party Plaintiff-Appellant,
Respondent on Review,

and

MARK LA NOUE, an individual,
Third-Party Plaintiff,

v.

SUTTLES CONSTRUCTION, INC., an Oregon corporation; and GORDON HARDING, an individual, dba Gordon Harding Construction, and MCM ARCHITECTS, PC, an Oregon professional corporation; et al.,
Third-Party Defendants,

and

VASILY A. SHARABARIN, an individual, dba Advanced Construction,
Third-Party Defendant-Respondent,
Petitioner on Review.

September 2014

EVANS CONSTRUCTION SIDING CORPORATION, an Oregon corporation,
Fourth-Party Plaintiff,

v.

DAVE BURGESS CONSTRUCTION, INC., an Oregon corporation; et al.,
Fourth-Party Defendants.

DAVE BURGESS CONSTRUCTION, INC., an Oregon corporation,
Fifth-Party Plaintiff,

v.

RAUL HERNANDEZ and CARLOS HERNANDEZ, individuals, dba
Hernandez Brothers, a partnership; et al.,
Fifth-Party Defendants.

LA NOUE DEVELOPMENT, LLC, an Oregon limited liability company; and
MARK LA NOUE, an individual,
Plaintiffs,

v.

MCM ARCHITECTS, PC, an Oregon professional corporation,
Defendant.

Multnomah County Circuit Court
051213487, 061213628

Court of Appeals
A140771

S062120

APPELLANT LA NOUE DEVELOPMENT, LLC'S BRIEF ON THE MERITS

Date of Decision:	December 4, 2013
Author:	Wollheim, J.
Concurring:	Schulman, P.J.
Concurring Separately:	Nakamoto, J.

Appeal from the General Judgment of the Multnomah County Circuit Court,
By the Honorable Jean K. Maurer, Judge

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I. INTRODUCTION AND SUMMARY OF THE ARGUMENT

Initially, this case started as a construction defect case. By the time it got to trial, however, it was a breach of contract case. The trial court and Court of Appeals viewed this case as a construction defect case, analyzing issues as though the general contractor was a homeowner. Thus, the analysis and rulings of the trial court and Court of Appeals were flawed.

La Noue Development, LLC ("La Noue") is the developer and general contractor of the Montara Townhomes, a thirteen building townhome project located in the Forest Heights neighborhood of Portland, Oregon. La Noue was named as a defendant in a multi-million dollar construction defect lawsuit brought by the Montara Owners Association (the "HOA").

La Noue pursued third-party claims against a number of subcontractors, including third-party defendant Vasily A. Sharabarin ("Sharabarin"), an installer of siding, trim, and related components on four of the townhome buildings.

Prior to trial, La Noue settled the HOA's claims for $5 million. Although La Noue was able to recoup some of the settlement dollars it paid to the HOA from most of the third-party defendants, it could not reach a settlement with Sharabarin. La Noue proceeded to trial against Sharabarin and a jury rendered a verdict in favor of LaNoue.

This appeal is focused on four key issues that plague similar cases in Oregon and prejudiced La Noue's ability to fully recoup its losses from Sharabarin. Those issues are: (1) whether Oregon statutory law requires contractual indemnification provisions to be read so that they do not violate ORS 30.140(1); (2) whether monies paid by a general contractor in settlement of a homeowner's claims are properly classified as economic losses and, therefore, for purposes of the general contractor's claims against its subcontractors, considered contract expectation damages; (3) whether the party offering an alternative theory of damages bears the burden of proof on those damages; and (4) whether attorney fees incurred by a party defending third party claims caused by another party's breach are recoverable as consequential damages against the breaching party even though they were incurred in the same action.

II. PROCEDURAL HISTORY AND FACTS MATERIAL TO DETERMINATION OF REVIEW

This appeal arises out of what was initially a construction defect lawsuit brought in 2005 by the HOA against La Noue, the developer and general contractor of the Montara Townhomes. *Montara Owners Ass'n v. La Noue Development, LLC,* 259 Or App 657, 660-63, 317 P3d 257 (2013). In the lawsuit, the HOA sought more than $7 million as compensation for personal injuries and property damage to the townhomes. *Id*. at 661.

La Noue pursued third-party claims against a number of its subcontractors, including Sharabarin. La Noue alleged each subcontractor was responsible for some part of the HOA's damages. *Id*. at 661-62. Prior to trial, one of the subcontractors brought a motion for partial summary judgment on La Noue's contractual indemnification claim. *Id*. at 662. Other subcontractors, including Sharabarin, joined in the motion, which was granted by the trial court. *Montara Owners Ass'n*, 259 Or App at 661 and n 1. As a result, La Noue's contractual indemnification claim was dismissed by the trial court pursuant to ORS 30.140. *Id*.

La Noue and the HOA settled the HOA's claims before trial for $5 million. *Id*. at 661.

Trial began in September of 2007 against five subcontractors. Two settled after opening statements, leaving three subcontractors, including Sharabarin, remaining through trial. *Id*. at 662. As a result of various pre-trial rulings, the only claim submitted to the jury was La Noue's breach of contract claim. *Montara Owners Ass'n*, 259 Or App at 662. Ultimately, the jury found that all three subcontractors breached their contracts with La Noue. *Id*. The jury awarded damages against the other two subcontractors in the amount of $102,101. *Id*. The jury awarded only $43,711 in damages against Sharabarin, despite evidence that Sharabarin's breach of contract caused more than $2 million in damages. *Id*. Following trial, the trial court ruled that La Noue

could not recover, as consequential damages, its attorney fees incurred in defending the HOA's claims. *Montara Owners Ass'n*, 259 Or App at 662.

La Noue filed a motion for new trial pursuant to ORCP 64. *Id*. The trial court denied La Noue's motion and La Noue appealed. *Id*. at 663. While the appeal was pending, the other two subcontractors settled with La Noue, leaving La Noue's claims against Sharabarin as the sole focus of the appeal. *Id*.

On appeal, La Noue filed a motion for remand pursuant to ORS 19.420(3). *Appellant's Motion to Reverse and Remand for New Trial Pursuant to ORS 19.420(3)*. The motion was filed due to the loss or destruction of portions of the trial transcript dealing with argument on the jury instructions. *Id*.

On December 4, 2013, the Court of Appeals reversed and remanded La Noue's indemnity claim and remanded for a new trial on breach of contract damages. *Montara Owners Ass'n*, 259 Or App at 683-84. The Court of Appeals also affirmed the trial court's denial of attorney fees. *Id*. Specifically, the Court of Appeals found: (1) the trial court had erred in giving a jury instruction on damages based on diminished value when there was no evidence in the record to support the instruction; (2) the trial court erred in holding the indemnity clause in the parties' contract was void; and (3) upheld the trial court's ruling that La Noue could not recover attorney fees because La Noue brought Sharabarin in via a third-party complaint instead of bringing a discrete

lawsuit. *Id*. The Court of Appeals also denied La Noue's motion to remand on ORS 19.420(3) grounds. *Id*. at 664, n 2.

In March of 2014, Sharabarin sought review of the Court of Appeals' decision and La Noue filed a response and contingent request for review. On May 29, 2014, this Court allowed review. Sharabarin filed his *Brief on the Merits* on July 8, 2014, and La Noue now hereby submits its merits brief.

III. FIRST QUESTION PRESENTED

A. Question

Does ORS 30.140 allow a contractual indemnity provision to be enforced to the extent that it allows for indemnity for damages caused by an indemnitor?

B. Proposed Rule

An indemnity clause that offends ORS 30.140(1) because it requires a subcontractor to indemnify a contractor for the contractor's own negligence remains enforceable only to the extent that it requires the subcontractor to indemnify the contractor for the subcontractor's own negligence.

C. Discussion

ORS 30.140 states in relevant part:

> (1) *Except to the extent provided under subsection (2) of this section,* any provision in a construction agreement that requires a person or that person's surety or insurer to indemnify another against liability for damage arising out of death or bodily injury to persons or damage to property caused in whole or in part by the negligence of the indemnitee is void.

> (2) This section does not affect any provision in a construction agreement that requires a person or that person's surety or insurer to indemnify another against liability *for damage arising out of* death or bodily injury to persons or *damage to property to the extent that the death or bodily injury to persons or damage to property arises out of the fault of the indemnitor, or the fault of the indemnitor's agents, representatives or subcontractors.*

(Emphasis added.)

In this case, La Noue and Sharabarin entered into a construction contract containing the following indemnification provision:

> SUBCONTRACTOR SPECIFICALLY AND EXPRESSLY agrees to indemnify and save harmless the CONTRACTOR, its officers, agents and employees, from and against any and all suits, claims, actions, losses, costs, penalties and damages, of whatsoever kind or nature, including attorney's fees, arising out of, in connection with, or incident to the SUBCONTRACTOR'S performance of the SUBCONTRACT, *whether or not caused in part by OWNER or CONTRACTOR, their employees or agents, but* excepting that caused by the sole negligence of the OWNER or CONTRACTOR, their employees or agents.

ER-2 (emphasis added). Before trial, Sharabarin joined a motion for partial summary judgment filed by other subcontractors. The motion asserted that La Noue's contractual indemnity claims against the subcontractors must be dismissed pursuant to ORS 30.140. The trial court granted the motion for partial summary judgment. ER-31-32, Tr 162-183. The Court of Appeals reversed the trial court, finding that ORS 30.140 rendered only the offending

portion of the contract provision between Sharabarin and La Noue void, leaving the remaining agreement intact and enforceable:

> *** [W]e must decide whether an indemnity clause that includes provisions allowed by ORS 30.140(2) is nonetheless unenforceable because it also includes provisions prohibited by ORS 30.140(1).
>
> ***
>
> An indemnity clause that offends ORS 30.140(1) because it requires a subcontractor to indemnify a contractor for the contractor's own negligence remains enforceable to the extent that it also requires the subcontractor to indemnify the contractor for the subcontractor's negligence. Because the indemnity clause in the La Noue/Sharabarin contract requires Sharabarin to indemnify La Noue for claims based on its own fault, it is enforceable to that extent.

Montara Owners Ass'n, 259 Or App at 682-83. The Court of Appeals is correct.

1. *The plain language of ORS 30.140 permits indemnification provisions in contracts that require a subcontractor to indemnify another for damages arising from the subcontractor's actions.*

In construing a statute, a court examines the text and context of the statute and considers legislative history, giving that history the weight the court "considers to be appropriate." *State v. Gaines*, 346 Or 160, 168-69, 206 P3d 1042 (2009). There is no more persuasive evidence of the intent of the legislature than "the words by which the legislature undertook to give expression to its wishes." *Id.* at 171 (*quoting State ex rel Cox v. Wilson*, 277 Or 747, 750, 562 P2d 172 (1977) (*quoting United States v. Am. Trucking Ass'ns.*, 310 US 534, 542–44, 60 S Ct 1059, 84 LEd 1345 (1940)). A court strives to

give effect to each word in a statute and non-technical words are given their "plain, natural, and ordinary meaning." *Portland Gen. Elec. Co. v. Bureau of Labor and Indus.*, 317 Or 606, 611, 859 P2d 1143 (1993), *superceded by statute*, ORS 174.020; ORS 174.010. Apparent conflicts in a statute are harmonized if possible. *Friends of Neabeack Hill v. City of Philomath*, 139 Or App 39, 48, 911 P2d 350 (1996), *rev den*, 323 Or 136 (1996).

By its express terms, ORS 30.140(1) applies "[e]xcept to the extent provided under subsection (2) of this section." "Except" means "with the exclusion of" and "otherwise, elsewhere, or for other reason than: other than." *Webster's Third New Int'l Dictionary* 791 (2002) (unabridged ed). "Extent" in this context means "the range (as of inclusiveness or application) over which something extends," "scope," "compass," "comprehensiveness," and "the point or degree to which something extends." *Id*. at 805. "Provision" in this context means "a stipulation," which is "a condition, requirement, or item specified in a contract ***." *Id*. at 1827, 2245. In other words, to the extent ORS 30.140(2) applies, ORS 30.140(1) does not. Applying the plain meaning of the words to the statute, subsection one of ORS 30.140 means:

> *[Other than what is included under]* subsection (2) of this section, *[any condition, requirement, or item]* in a construction agreement that requires a person or that person's surety or insurer to indemnify another against liability for damage arising out of death or bodily injury to persons or damage to property caused in whole or in part by the negligence of the indemnitee is void.

And subsection two means:

> This section does not affect *[any condition, requirement, or item]* in a construction agreement that requires a person or that person's surety or insurer to indemnify another against liability for damage arising out of death or bodily injury to persons or damage to property to the extent that the death or bodily injury to persons or damage to property arises out of the fault of the indemnitor, or the fault of the indemnitor's agents, representatives, or subcontractors.

Subsection one uses the singular for "provision," thus limiting its application. The ordinary dictionary definitions for the words in the statute demonstrate that subsection one excepts subsection two from the rule that a condition violating subsection one's terms is void. Subsection two confirms that conditions requiring a subcontractor to indemnify another for the subcontractor's own fault are unaffected by the rule set forth in subsection one.

To endorse Sharabarin's interpretation of the statute, one must replace or interpret words in the statute so as to go beyond the plain meaning of the words. Sharabarin, for example, replaces "provision" with "agreements" in order to assert that the entire "agreement" at issue here is void, even though the plain meaning of the statute makes only the one condition void. *See Respondent Sharabarin's Brief on the Merits*, p 7 (stating that ORS 30.140 "voids agreements to indemnify a general against injury or damage 'caused in whole *or in part'* by the general[.]") (Emphasis in original.)

But courts do not reject entire paragraphs or entire contracts simply because one part is unenforceable, void, or illegal. "[The] rule respecting the

sanctity of contracts is so firmly fixed in our system of jurisprudence that even where the agreement is partly legal and partly illegal, the legal part will be enforced." *Eldridge v. Johnston*, 195 Or 379, 405, 245 P2d 239 (1952); *Hagen v. O'Connell, Goyak & Ball, P.C.*, 68 Or App 700, 704, 683 P2d 563 (1984) (*citing W.J. Seufert Land Co. v. Greenfield*, 262 Or 83, 87, 496 P2d 197 (1972)). In *Hagen*, the court examined an unenforceable penalty provision in paragraph 5 of a contract. It found that the penalty provision could be severed from the other provisions in paragraph 5, thus only the offending provision was severed, not the entire paragraph. *Hagen*, 68 Or App at 704. Similarly, here, the offending provision can be severed, while the remaining provisions of the paragraph remain in force.

2. *The purpose of ORS 30.140 is to ensure fairness between the parties to construction contracts.*

When the legislation related to ORS 30.140 was first introduced in 1995, the bill's proponents explained the impetus of the legislation to the Senate Judiciary Committee. "[W]hat we would like to propose is that there be a sense of fair play *** and that those that have negligence, in fact, defend and pay for that negligence ***." App-26-27.

Fairness is ensured by protecting a person entering a construction contract from a requirement that the person indemnify another for the other's own negligence. *Walsh Constr. Co. v. Mut. Of Enumclaw*, 338 Or 1, 104 P3d 1146 (2005). But Sharabarin seeks to do more than protect itself from this

outcome. Instead, he interprets the statute as though the purpose of the statute were to penalize one party to the contract. He asserts that without reading such penalty into the statute, "there would be nothing to stop generals from continuing to draft overbroad provisions ***." *Respondent Sharabarin's Brief on the Merits*, p 12. Sharabarin does not cite to any legislative history or other source for reading this purpose into the statute. Only the legislature can alter the statute to create punitive rules, and it has not done so here.

The statute's plain terms do not suggest any punitive intent. Instead, they suggest a balance, allowing the parties to contract freely for the inclusion of indemnity provisions while ensuring the intended protection otherwise limits construction agreements.

Case law supports this outcome. Pursuant to *Hays v. Centennial Floors, Inc.*, 133 Or App 689, 695, 893 P2d 564 (1995), the entire indemnification provision is not void, even if the language of the indemnification contract between Sharabarin and La Noue is sufficiently broad to require indemnification for injury caused by La Noue, as is precluded by ORS 30.140. "Instead, it is only unenforceable in part." *Richardson v. Howard S. Wright Constr. Co.*, CV-05-1419-ST, WL 1467411*5 (D Or May 18, 2007) (discussing impact of ORS 30.140(1) on contracts) (*citing Hays*, 133 Or App at 695).

In *Hays*, the Court of Appeals considered an earlier version of ORS 30.140, which also voided a contractual indemnification provision

requiring a subcontractor to indemnify a contractor for negligence that was the sole fault of the contractor. Although the Court found that the contractual indemnification clause at issue was partially void, it held that ORS 30.140 only "voids the clause to the extent that its application would require [the indemnifying party, the indemnitor,] to indemnify [the party seeking indemnity, the indemnitee,] for its own sole negligence." *Hays*, 133 Or App at 695.

The *Hays* court therefore considered whether the party seeking indemnity had met its burden of proof in establishing "the extent to which the amounts, including settlement payments, for which it sought indemnity pertained to claims other than those relating to [the indemnitee's] sole negligence – *i.e.*, [claims] for which [the indemnitor] could have been at least partly liable * * *." *Id*. at 697. The Court found that this burden had not been met at trial, and the trial court had therefore appropriately entered judgment for the defendant. *Id*.

The plain, natural, and ordinary meaning of the statute allows conditions in contracts to stand when they require a subcontractor to indemnify another for the subcontractor's own negligence. The Court of Appeals correctly ruled that the trial court erred on this issue. Remand on La Noue's indemnification claim is appropriate.

3. *La Noue should have been allowed to offer proof of facts giving rise to a duty on the part of Sharabarin to indemnify La Noue.*

By its clear terms, ORS 30.140(2) allows parties to a construction agreement to contractually require one party to indemnify another for damage

arising out of "the fault of the indemnitor, or the fault of the indemnitor's agents, representatives or subcontractors." At the time of the trial court's ruling, there was no evidence that La Noue was seeking contractual indemnification from Sharabarin for damages La Noue caused, either in whole or in part. To the contrary, La Noue sought only contractual indemnity from Sharabarin to the extent that the damage to the townhomes arose out of Sharabarin's fault.

Sharabarin further argues that La Noue cannot seek indemnity because the HOA did not allege that Sharabarin was negligent when the HOA asserted claims against La Noue. *Respondent Sharabarin's Brief on the Merits*, p 15. Sharabarin does not provide any statutory or case law support for this proposition. In practice, homeowners may bring many claims against a general contractor. The general contractor may implead subcontractors who are liable to it for these damages. The claims will not perfectly align and La Noue is not aware of a requirement that the claims of the homeowner allege that the subcontractors are at fault.

Instead, the focus is on whose actions caused the damages. The homeowner asserts La Noue caused the damages. La Noue asserts Sharabarin caused the damages. If La Noue proves its allegations, that the homeowner may not have made those allegations does not change the outcome that Sharabarin is liable for damages he caused.

La Noue should have been afforded an opportunity, as the party seeking indemnification, to prove facts giving rise to a duty on the part of Sharabarin to indemnify La Noue. The Court of Appeals correctly held that the trial court erred in dismissing La Noue's indemnification claim. Remand of La Noue's indemnification claim is appropriate.

IV. SECOND QUESTION PRESENTED

A. Question

When a general contractor reaches a settlement with a homeowner to resolve claims for personal injuries and property damages, is the settlement payment considered an economic loss and, if so, is the general contractor entitled to seek breach of contract / expectation damages from a subcontractor on whose behalf the general contractor settled the homeowner's claims?

B. Proposed Rule

Settlement payments are economic losses. When a party's breach of contract causes another's economic loss, expectation or reliance damages are the appropriate measure of damages. The economic waste doctrine has no applicability to lawsuits involving a general contractor's economic losses caused by a subcontractor's breach of contract.

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C. Discussion

1. *La Noue preserved its objection to the jury instruction.*

The Court of Appeals summed up the threshold preservation issue as follows:

> There is some dispute relating to preservation of [La Noue's arguments concerning the jury instruction on damages]. Sharabarin contends that the only exception on the record is a post-instructional objection by La Noue's attorney to "Instruction No. 26 on damages." La Noue contends that the issue was in fact raised but, because of a problem with the record on appeal (a recording device problem not caused by La Noue), a portion of the record concerning the parties' objections and argument on jury instructions is missing. To the extent that preservation is an obstacle, La Noue asks this court to order a new trial. See ORS 19.420(3) ***. Under the unique circumstances in this case, we conclude that the correctness of the jury instruction was sufficiently raised and neither the trial court nor Sharabarin will be surprised by this court's consideration of the jury instruction issue on appeal. Therefore, we deny La Noue's motion under ORS 19.420(3) to remand for a new trial. We proceed to the merits of La Noue's first assignment of error.

Montara Owners Ass'n, 259 Or App at 664-65, n 2. Sharabarin now claims to be "very surprised" that the Court of Appeals considered the merits on this issue, claiming, "There is nothing in the record to support the conclusion that Sharabarin and the trial judge were somehow aware that La Noue would challenge the instruction *on the grounds that it did*" and claiming to be "confused" by the Court's characterization of the recording malfunction as "unique." *Respondent Sharabarin's Brief on the Merits*, pp 21-22 (emphasis in original). Sharabarin's position is disingenuous.

First, Sharabarin's counsel concedes La Noue made a general exception to Instruction Number 26 (*Respondent Sharabarin's Brief on the Merits*, p 17), the instruction at issue.

Second, consequently, it is disingenuous for Sharabarin to now claim that neither he nor the trial court could possibly know the grounds for La Noue's challenge or claim surprise that in the later filed appeal "La Noue would challenge the instruction for lack of evidence to support the instruction." *Respondent Sharabarin's Brief on the Merits*, p 22. Following trial, La Noue moved the trial court for a new trial pursuant to ORCP 64. Supp ER-5-7 and 13-14. In support of that motion, La Noue's counsel declared that she "objected at trial to the jury instruction provided by the court regarding the proper measure of damages, and requested that the court instruct the jury that the cost of replacement or repair is the correct measure of damages for construction work done by subcontractors that is so deficient as to be in breach of contract." Supp ER-7. *Also* s*ee, e.g.*, Supp ER-14 ("Because there was absolutely no evidence in this case of economic waste, or of a reasonable method for the jury to calculate damages if they did find economic waste, the instruction mislead the jury ***."). Sharabarin responded to the ORCP 64 motion. Supp ER-8.

Third, at a 2010 hearing before the trial court on La Noue's request to correct the record to address the recording malfunction, Sharabarin's counsel also acknowledged that there was "an unreported afternoon, during which

instructions were discussed" before the trial court. *Declaration of Emilie K. Edling in Support of Appellant's Motion to Reverse and Remand for New Trial Pursuant to ORS 19.420(3)*, ¶ 4, Ex. 4, p 15:10-12. And, counsel for La Noue declared under penalty of perjury:

> I recall arguing at length regarding La Noue's objection to the proposed economic waste jury instruction, which the trial court ultimately provided to the jury in the Jury Instruction No. 26 at trial. My objections to that instruction were made in the courtroom during the time and place that the court designated for discussion of jury instructions. *My objections to Jury Instruction No. 26 specifically stated that the provision of the economic waste instruction was in error because economic waste was not an appropriate measure of damages in this case. I further argued that the provision of the economic waste instruction was in error because the instruction was not supported by evidence from which the jury could determine the alternative measure of damages.*

Declaration of Leta E. Gorman in Support of Appellant's Motion to Reverse and Remand for New Trial Pursuant to ORS 19.420(3), ¶ 3, p 1 (Emphasis added.)

Moreover, the recording malfunction that occurred while the parties argued the jury instructions before the trial court in this case is precisely the sort of unique or extraordinary circumstances that should inform whether or not an appellate court exercises its discretion under ORS 19.420(3). *State v. Shumate*, 262 Or App 109, 122, 330 P3d 29 (2014) (under "extraordinary circumstances" presented by destruction of record, appellant's failure to make *prima facie* showing of trial court error does not preclude remand).

The Court of Appeals correctly exercised its discretion in denying La Noue's ORS 19.420(3) motion for remand and proceeding to the merits of this assignment of error. Alternatively, if this Court should find that the Court of Appeals erred in denying La Noue's ORS 19.420(3) motion, the only appropriate outcome is reversal and remand for a new trial on damages.

2. *Settlement payments are economic losses.*

Oregon case law is clear that amounts paid in settlement are economic losses. *See, e.g., Harris v. Suniga,* 209 Or App 410, 418, 149 P3d 224 (2006) (describing types of economic losses) (*citing Indian Creek Dev. Co. v. City of Hood River,* 203 Or App 231, 125 P3d 50 (2005), *rev den.,* 340 Or 158, 130 P3d 787 (2006) (lost profits); *Miller v. Mill Creek Homes, Inc.*, 195 Or App 310, 97 P3d 687 (2004) (loss of flood insurance proceeds); *SFG Income Fund, LP v. May,* 189 Or App 269, 274, 75 P3d 470 (2003) (loss of expected proceeds resulting from negligent misinformation that property was buildable); *Lewis-Williamson v. Grange Mut. Ins. Co.,* 179 Or App 491, 39 P3d 947 (2002) (undervaluation of plaintiff's residence in homeowners insurance policy); *Portland Trailer & Equip., Inc. v. A-1 Freeman Moving & Storage, Inc.*, 166 Or App 651, 5 P3d 604 (2000), *adh'd to as modified on recons*, 168 Or App 654, 4 P3d 741 (2000) (attorney fees incurred as result of defendants' initiation of predicate civil proceeding); *Roberts v. Fearey,* 162 Or App 546, 556, 986 P2d 690 (1999) (failed loan transactions); *Oregon Life & Health Ins. Guar. Ass'n v.*

Inter-Reg'l Fin. Grp, Inc., 156 Or App 485, 967 P2d 880 (1998) (loss of investment); *Allstate Ins. Co. v. Tenant Screening Servs., Inc.*, 140 Or App 41, 914 P2d 16 (1996) (money paid in settlement of personal injury claim).

The fundamental flaw in the Court of Appeals' decision is that it viewed the damages La Noue sought from Sharabarin as property damage, to which an economic waste / diminution of value argument may apply. The Court failed to recognize that La Noue was seeking reimbursement for amounts it paid in settlement, *i.e.*, its economic losses, on behalf of Sharabarin.

3. *When a subcontractor breaches its contract with a general contractor and the general contractor makes a settlement payment on behalf of the subcontractor, the general contractor is entitled to its expectancy damages.*

The goal of damages for breach of contract is compensation. *Carter v. Wolf Creek Hwy.*, 54 Or App 569, 573, 635 P2d 1036 (1981). That loss may be expressed in terms of different legally cognizable interests. One such interest is "expectation interest." Contract remedies designed to protect an injured party's "expectation interest" are often expressed as the party's interest in receiving the benefit of the bargain. *Shook v. Travelodge of Oregon*, 63 Or App 137, 144, 663 P2d 1280, *rev den* 295 Or 541, 668 P2d 384 (1983); *see also Restatement (Second) Contracts* § 344(a) (1979). Expectation interest damages put the injured party in the position he or she would have been in had the contract not been breached. *Siler v. Turnbull*, 71 Or App 787, 790, 693 P2d 1323 (1985).

In the present case, there is no rational reason for not protecting La Noue's expectation interest. This measure of damages is mandated by the weight of authority, the interest of justice, and the need for a reasonable rule of law designed to adequately compensate the injured party. La Noue's expectancy is clear, and its efforts to mitigate liability and cap damages should not be subjected to a hindsight review under the guise of the economic waste doctrine. Given that La Noue's expectation damages had already been established by the amount of the settlement payment, there was no basis for allowing a diminution of value assessment of damages. The sole question for the jury at trial should have been what *portion* of the settlement amount paid by La Noue was Sharabarin's responsibility.

The damages instruction given by the trial court was a misstatement of the law. The instructional error was not because it was speculative and not supported by the evidence. *Wallach v. Allstate Ins. Co.*, 344 Or 314, 329, 180 P3d 19 (2008). For this reason, La Noue's breach of contract claim should be reversed and remanded for a new trial on damages.

4. *The economic waste doctrine does not apply when there is no risk of windfall.*

The economic waste doctrine traces back to Judge Benjamin Cardozo's opinion in *Jacob & Youngs v. Kent*, 230 NY 239, 129 NE 889 (1921). In that case, a builder contracted to build a home. The plans called for a specific brand of plumbing pipe to be used. Due to an error of the builder, a different brand of

pipe was used. The owner discovered the error after the home was completed but demanded the pipes be removed and replaced, even though the removal and replacement would cause substantial damage to the home. The builder refused to replace the pipe and the owner refused to pay. The builder sued. After a directed verdict in favor of the owner at trial, the New York Supreme Court, Appellate Division, reversed and ordered a new trial. The owner then appealed to the New York Court of Appeals, which affirmed the Appellate Division and ordered judgment in favor of the builder.

Judge Cardozo drafted the majority opinion and acknowledged that "in most cases the cost of replacement is the measure [of damages]***." *Id*. at 891. That measure is inappropriate, however, when "the cost of completion is grossly and unfairly out of proportion to the good to be attained." *Id*. Judge Cordozo concluded that damages the owner was entitled to recover should be limited to the difference in the value of the home if it had been built to the specifications and the value of the home as it was built. *Id*.

The goal of the doctrine is sometimes expressed as attempting to avoid providing the homeowner with a windfall – compensation for defects the homeowner is never likely to fix. *See, e.g.*, comment c to *Restatement (Second) Contracts* § 348 (1981)[1] (term "economic-waste" is something of a misnomer,

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[1] *Restatement (Second) Contracts* § 348 (1981) provides:

> (1) If a breach delays the use of property and the loss in value to the injured party is not proved with

because typically doctrine is not invoked to prevent an imprudent use of resources; rather, it is used to avoid granting owner windfall); and *Tru-Built Garage & Lumber Co., Inc. v. Mays*, 13432, WL 15664 *4 (Ohio Ct App Jan 27, 1993) ("[W]hen the total cost to remedy a defect is grossly disproportionate to the good to be attained, a different measure of damages must be applied to avoid *** economic waste as well as a windfall to the plaintiff").

The economic waste doctrine simply does not apply to the facts of this case. First, La Noue is not a homeowner. Second, when a general contractor seeks to recover of amounts it paid in settlement of a homeowner's claims, there is no risk of windfall to the general contractor. Indeed, the situation is

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> reasonable certainty, he may recover damages based on the rental value of the property or on interest on the value of the property.
>
> (2) If a breach results in defective or unfinished construction and the loss in value to the injured party is not proved with sufficient certainty, he may recover damages based on
>
> (a) the diminution in the market price of the property caused by the breach, or
>
> (b) the reasonable cost of completing performance or of remedying the defects if that cost is not clearly disproportionate to the probable loss in value to him.
>
> (3) If a breach is of a promise conditioned on a fortuitous event and it is uncertain whether the event would have occurred had there been no breach, the injured party may recover damages based on the value of the conditional right at the time of breach.

more likely to be a windfall to a subcontractor who refuses to settle and forces the matter to trial – banking on being able to convince a judge or jury that it did not breach its contract and/or cause any of the general contractor's financial losses.

A jury should not have been given an instruction providing it with an alternative way to measure damages. The Court of Appeals and the trial court should be reversed.

5. *Lack of evidence at trial made instruction on the economic waste doctrine erroneous.*

Even though the Court of Appeals erred in concluding that the economic waste instruction was a correct statement of the law in this case, it correctly determined that the jury instruction was given in error because there was no evidence at trial of the diminished value of the townhomes as a result of the defects:

> ***La Noue argues that, even if the instruction correctly stated the law in the abstract, it was erroneous to give it in this case in light of the evidence at trial. La Noue contends that there was no evidence at trial from which the jury could determine economic waste or diminished value. Viewing the evidence "in the light most favorable to the establishment of the facts necessary to require giving the requested instruction," we conclude that La Noue is correct.
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> ***
>
> Sharabarin does not, and cannot, argue that there was evidence at trial establishing the difference between the value of the buildings as constructed and as they should have been constructed. *** Without such evidence, Sharabarin was not

> entitled to an instruction on the diminished value of the buildings or units as an alternative measure of damages. Because there was no evidence of the diminished value of the Montara buildings as a result of Sharabarin's breach of contract, the trial court erred in giving a damages instruction that was not supported by evidence in the record.

Montara Owners Ass'n, 259 Or App at 669-70 (internal citations omitted).

There was absolutely no evidence at trial of the diminished value of the buildings as a result of Sharabarin's breach of contract. There was therefore no evidence from which the jury could establish any form of recovery based on economic waste or diminished value.

The economic waste doctrine states, "*** the cost of replacement or repair is the correct measure of damage for defects in work unless that remedy generates undue economic waste." *Beik v. Am. Plaza Co.*, 280 Or 547, 555, 572 P2d 305 (1977). The doctrine relies upon the comparison of two different things – the cost of repair and the value of the project. "Only if the cost of repair is disproportionate does the standard of difference in value become applicable at all." *Id.* at 310, *citing* McCormick, *Damages*, 647, 650, s. 168 (1935). At trial, Sharabarin failed to produce any evidence of the alleged diminution of value of the townhomes, let alone compare such diminution with the cost of repair. Both of those are key facts that are fundamental to application of this doctrine. Such comparison is *only* done *if* the cost of repair is disproportionate to the value of the project, again requiring that evidence

must have been shown by which a comparison of proportionality could be assessed.

Because there was no evidence in this case of economic waste, or of a reasonable method for the jury to calculate diminution in value damages if they did find economic waste, the instruction misled the jury into impermissibly speculating as to a measurement of damages for which no evidence had been presented. The damages awarded by the jury were necessarily arbitrary and capricious and were not based on any evidence, prejudicing La Noue. The instructional error was not harmless. *Montara Owners Ass'n*, 259 Or App at 670 (*citing Wallach*, 344 Or at 329). The trial court should be reversed and La Noue's breach of contract claim remanded for a new trial on damages.

V. THIRD QUESTION PRESENTED

A. Question

Which party has to burden to prove an alternative theory of damages?

B. Proposed Rule

If a party proposes an alternative measure of damages, it has the burden to prove those damages.

C. Discussion

The Court of Appeals correctly held:

> Assuming that Sharabarin might have been able to present to the jury an alternative to normal expectation damages based on the economic waste doctrine, he bore the burden of proving the amount of damages the jury should award if it applied that

> doctrine, namely, the diminished value of the townhouses. Sharabarin did not meet his burden due to a lack of evidence, and there was, consequently, no basis in the evidence to give the instruction concerning economic waste or diminished value.

Montara Owners Ass'n, 259 Or App at 665 (citations omitted). Even if the economic waste doctrine could apply here, Sharabarin bore the burden of proof in establishing diminution in value and failed to do so at trial, thus rendering the jury instruction purely speculative and improper. The Oregon Court of Appeals and several other jurisdictions hold that once a party has proven its cost of repair or replacement, the burden shifts to the defendant to prove that the cost would result in economic waste and the amount of diminution in value. *See Pac. Erectors, Inc. v. Westinghouse Elec. Corp.*, 61 Or App 1, 655 P2d 613 (1982) (court finding burden was on subcontractor to show amount of charges incurred were unreasonable); *Panorama Vill. Homeowners Ass'n v. Golden Rule Roofing, Inc.*, 102 Wash App 422, 10 P3d 417, 422 (2000) (stating "[o]nce the injured party has established the cost to remedy the defects, the contractor bears the burden of challenging this evidence in order to reduce the award, including providing the trial court with evidence to support an alternative award."); and *Andrulis v. Levin Constr. Corp.*, 331 Md 354, 628 A2d 197, 208 (1993) (holding "authorities *** agree that the burden to show that the cost of correction constitutes economic waste is on the party breaching the contract.")

Sharabarin's argument that the burden should be on the plaintiff to produce evidence to support an award of an *alternative* measure of damages,

which it is not seeking, is simply inconsistent with well established law and the general principles of the burden of proof. *See* 5 Arthur Linton Corbin, *Contracts* §1089 (1964) ("[A]ll substantial doubt as to the usefulness and value of the defective structure should be resolved against the building contractor."); *Andrulis,* 628 A2d at 207 (noting "economic waste is a limitation on the ordinary rule of contract damages," and therefore the burden of proving economic waste is on the party that breached the contract and that invokes the doctrine in an effort to limit expectation damages."); *Reutemann v. Lewis Aquatech Inc., CIV.A DKC* 2004-0063, WL 1593473 *5 (D Md Jul 5, 2005) (holding that it was the breaching contractor's burden to "present evidence necessary to take the market value approach.") (*quoting Stangl v. Todd*, 554 P2d 1316 (Utah 1976)).

Invoking the doctrine of economic waste is an alternative theory of damages to the ordinary rule of contract expectation damages. To require plaintiff to put on evidence, and meet a burden of proof, for a theory of damages, which a defendant may not even argue to a jury, simply does not make logical sense. In other jurisdictions, this has been widely accepted and courts have held that the party proposing the deviation from the normal "cost of repair" damages has the burden of proof.[2]

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[2] *See Cashman Equip Corp. v. U.S. Fire Ins. Co.,* 368 Fed Appx 288, 295 (3d Cir 2010) (holding that it, along with "vast majority of authorities that have considered the question" concur that, "without question," party that breaches

Sharabarin cites to *McComb v. Cogswell*, 140 Or 676, 15 P2d 716 (1932) as the "one case directly on point" to support its position. *Respondent Sharabarin's Brief on the Merits*, p 28. The Court of Appeals cited to *McComb* to stand for the exact opposite position, however. Indeed, the Court in *McComb* stated that it was defendants who failed to establish the amount of their damages, *i.e.*, the value of the building as constructed and what its value would have been had it been built according to the plans and specifications. *Id.* at 665 and n 3.

Because it was defendant's burden to clearly and convincingly prove that the cost to repair the townhomes would involve an unreasonable economic waste, and having failed to meet this burden of proof, the jury instruction was in error and prejudiced La Noue by being entirely speculative and unsupported by the evidence. As a result, La Noue's breach of contract claim should be remanded for a new trial on damages.

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contract should have burden of proving that "cost of curing a construction defect is disproportionate to the probable loss in value."); *Cf. Andrulis*, 628 A2d at 197; *P.G. Lake, Inc. v. Sheffield*, 438 SW2d 952, 956 (Tex Civ App 1969) ("[t]he minimization of damages is a defensive matter," and "[i]f the defendant desires to avail himself of such defense, the burden rests upon him to raise such issue by pleadings and proof"); *John Thurmond & Associates, Inc. v. Kennedy*, 284 Ga 469, 668 SE2d 666, 669 (2008) (burden on contractor guilty of breach to prove that award of repair costs constitutes economic waste).

VI. FOURTH QUESTION PRESENTED

A. Question

Are attorney fees incurred by a party defending third party claims recoverable as consequential damages even though they were incurred in the same action?

B. Proposed Rule

Where breach of contract triggers litigation with a third party, the attorney fees incurred in defending that litigation are recoverable as consequential damages arising out of the breach even if they are incurred in the same action.

C. Discussion

There is no dispute that where a breach of contract triggers litigation with a third-party, the attorney fees, costs, and expenses incurred in the litigation are recoverable as damages arising out of the breach. *Huffstutter v. Lind*, 250 Or 295, 301, 442 P2d 227 (1968); *Osborne v. Hay*, 284 Or 133, 142, 585 P2d 674 (1978); *Hoage v. Westlund*, 43 Or App 435, 439-42, 602 P2d 1147 (1979); *Braught v. Granas*, 73 Or App 488, 493-94, 698 P2d 1012 (1985); *Raymond v. Feldmann*, 124 Or App 543, 546, 863 P2d 1269 (1993); *Acushnet Co. v. G.I. Joe's, Inc.*, CV 05-764-HU, WL 2729555 *7 (D Or 2006).

The authority for attorney fees in such situations arises from the *Restatements of Torts* and *Contracts*. *See, e.g., Hoage*, 43 Or App at 439

("Although the trial court did not so state, the [attorney fee] award *** was necessarily by authority of Restatement (Second) of Torts 914(2) (1977)"); *Raymond*, 124 Or App at 546 and n 1 (*citing Restatement (Second) of Torts* § 914 (1977), *Restatement (Second) of Contracts*, § 351, comment c (1979), and *Restatement of Contracts*, § 334 (1932)); *Osborne*, 284 Or at 141; and *Huffstutter*, 250 Or at 301 (*citing* "Restatement, Torts, 591 914 (1939).").

Restatement (Second) of Torts, § 914 (1977) provides:

> (2) One who through the tort of another has been required to act in the protection of his interests by bringing or defending an action against a third person is entitled to recover reasonable compensation for loss of time, attorney fees and other expenditures thereby suffered or incurred *in the earlier action*.[3]

(Emphasis added.)

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[3] *Restatement (Second) of Contracts* § 351, comment c (1979) provides:

> Sometimes a breach of contract results in claims by third persons against the injured party. The party in breach is liable for the amount of any judgment against the injured party together with his reasonable expenditures in the litigation, if the party in breach had reason to foresee such expenditures as the probable result of his breach at the time he made the contract.

Restatement (First) of Torts, § 914 (1939) provides, "A person who through the tort of another has been required to act in the protection of his interests by bringing or defending an action against a third person is entitled to recover compensation for the reasonably necessary loss of time, attorney fees and other expenditures thereby suffered or incurred."

And *Restatement (First) of Contracts*, § 334 (1932) states, "If a breach of contract is the cause of litigation between the plaintiff and third parties that the defendant had reason to foresee when the contract was made, the plaintiff's reasonable expenditures in such litigation are included in estimating his damages."

In this case, the trial court ruled that La Noue could not recover attorney fees as part of its consequential damages on the breach of contract claim because it chose to bring its claims against Sharabarin *via a third-party complaint*, rather than through "earlier or separate litigation." Tr 3377. The Court of Appeals agreed: "Because the fees do not originate from prior litigation with a third party, the court did not err in denying La Noue's request for attorney fees." *Montara Owners Ass'n*, 259 Or App at 683.

In other words, had La Noue foregone the third-party complaint, and instead opted to dismiss its lawsuit with the HOA after settling, and then filed a separate action against Sharabarin and the other subcontractors, then and only then would La Noue's fees be recoverable. But no authority requires § 914(2) of the *Restatement (Second) of Torts* to be read so literally as to preclude recovery of fees when third-party practice is utilized instead of a discrete suit.

The Court of Appeals cited to *State v. O'Brien*, 96 Or App 498, 774 P2d 1109 (1989) *rev den*, 308 Or 466 (1989), in support of its holding against La Noue on this issue. But that case is distinguishable in that it doesn't involve third-parties. The issue in *O'Brien* was the absence of third-party claims, not whether or not a discrete suit was filed. The difference is best articulated in *Raymond,* 124 Or App at 543. Ms. Raymond was injured in a motor vehicle accident. A few days later, she settled her personal injury claim with an agent of the driver's (Mr. Feldmann) insurance company. Ms. Raymond believed she

had sustained minor injuries, so accepted a small settlement. When it later became apparent that her injuries were more severe, she returned the small settlement check and filed a personal injury action against Mr. Feldmann in Deschutes County Circuit Court. Mr. Feldmann counterclaimed for attorney fees. The court held Mr. Feldmann's attorney fees were not recoverable because no third-party was involved:

> [T]his case does not involve a claim for damages arising from "separate" litigation with a third party. *** [Feldmann's] counterclaim is for attorney fees incurred in defending the claim of negligence brought by plaintiff. The claim arises out of the same action, not a separate one involving defendant and a third party.

Raymond, 124 Or App at 549. The Court of Appeals in the *Raymond* case specifically distinguished the facts of cases like *Huffstutter* and *Braught*, where third-parties were involved, from the facts of cases like *O'Brien*, where they were not:

> Defendant and the dissent fail to distinguish between litigation involving the parties to the agreement, such as in this case, from cases involving litigation between the nonbreaching party and a third party. It is essential to the application of this exception that the claimed attorney fees arise from litigation involving a third party.
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> ***
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> In light of [the facts in *Braught*], we held that plaintiffs were entitled to recover damages from defendant, including attorney fees, resulting from the litigation with the third party.
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> When third parties are not involved, the other side of the coin is reflected by such holdings as *Samuel v. Frohnmayer*, 95 Or

> App 561, 770 P2d 914, *rev'd on other grounds*, 308 Or 362, 779 P2d 1028 (1989), and *State v. O'Brien*, 96 Or App 498, 774 P2d 1109, *rev den* 308 Or 466, 781 P2d 1214 (1989).

Raymond, 124 Or App at 546-548.[4] (Citations omitted. Emphasis in original.)

The rule of law as proposed by Sharabarin and endorsed by the trial court and Court of Appeals thwarts the policy behind third-party practice and will dramatically increase the number of suits filed in the state of Oregon. Judicial economy has long been favored in Oregon. *See, e.g., Huson v. Portland & S.E. Ry. Co.*, 107 Or 187, 208, 211 P 897 (1923), *citing Alderman v. Tillamook Cnty*, 50 Or 48, 91 P 298 (1907) ("It was necessary to bring in all the associates in the undertaking as new parties to the litigation in order to avoid a multiplicity of suits."). The lower court decisions would thwart judicial economy if separate lawsuits are required for a party to be able to recover attorney fees as consequential damages.

ORCP 22 C(1) governs third-party practice in Oregon. It provides:

> After commencement of the action, a defending party, as a third party plaintiff, may cause a summons and complaint to be served upon a person not a party to the action who is or may be liable to the third party plaintiff for all or part of the

[4] The Court of Appeals also cited to the fact that the *Hoage* case predates ORCP 68. *Montara Owners Ass'n*, 259 Or App at 683, n 8. But ORCP 68 did not overrule *Hoage*, it simply "provides a procedure for assessing *** fees no matter what source is relied upon as providing the right to such fees" and excludes "pre-existing attorney fees which are actually claimed as damages" from that *procedure*. *See, Appellant's Reply Brief and Combined Supplemental Excerpt of Record and Appendix*, p 15, n 3, and App-8. In any event, *Raymond* and *Braught* post-date ORCP 68. *Also see, Acushnet Co.*, 2006 WL 2729555 at *7.

> plaintiff's claim against the third party plaintiff as a matter of right ***.

This closely tracks the federal third-party rule counterpart, FRCP 14 (a)(1), which states, "A defending party may, as a third-party plaintiff, serve a summons and complaint on a nonparty who is or may be liable to it for all or part of the claim against it."

The very purpose behind third-party practice is to facilitate judicial economy.[5] And the goal of judicial economy is reflected in decisions across multiple jurisdictions where courts have evaluated the "prior proceeding" issue

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[5] *See, e.g., First Nat. Bank of Santa Fe v. Espinoza*, 95 NM 20, 618 P2d 364, 365 (1980) ("The purpose of [New Mexico] Rule 14 is to facilitate judicial economy by allowing a defendant to bring in a party would who be liable to him in the event the original plaintiff prevails" *citing* C. Wright and A. Miller, *Federal Practice and Procedure* § 1442 (1971); *Bonaparte v. Neff*, 116 Idaho 60, 773 P2d 1147, 1155 (Ct App 1989) ("Fundamental purpose" of Idaho Rule 14 "is to promote judicial efficiency by eliminating circuity of actions or piecemeal litigation," *citing* Wright & Miller § 1442); *Pizani v. St. Bernard Parish*, 125 So 3d 546, 554-55 (La Ct App 2013) *writ den*, 131 So 3d 863 (La 2014) (Allowing third party demand "promotes judicial economy by avoiding a 'circuity of proceeding,' *i.e.* a multiplicity of suits."); *Farm Bureau Mut. Ins. Co. v. Riverside Marine Remanufacturing, Inc.*, 278 Ark 585, 647 SW2d 462, 464 (1983) ("[T]he purpose of [Arkansas] Rule 14 [is] to promote judicial economy and avoid multiplicity of suits."); *Franklin Cty. Dist. Bd. of Health v. Paxson*, 152 Ohio App 3d 193, 787 NE2d 59, 64-5 (2003) (Third party complaint was consistent with purposes of Ohio rule, including promoting judicial efficiency by avoiding circuity of actions, avoiding duplication of testimony and evidence, and avoiding inconsistent ruling); *Long Island Women's Health Care Associates v. Haselkorn-Lomansky*, 10 Misc 3d 1068(A), 814 NYS2d 562 (Sup Ct 2005) (objectives underlying New York third party practice rule are to "promote judicial economy and to avoid multiplicity of actions." (Citations omitted)); *Kerschner v. Weiss & Co.*, 282 Ill App 3d 497, 667 NE2d 1351, 1357-58 (1996).

in the third-party exception to recovery of fees. In *Prentice v. N. Am. Title Guar. Corp., Alameda Div.*, 59 Cal2d 618, 620-21, 381 P2d 645 (1963), the California Supreme Court held:

> In the usual case, the attorney's fees will have been incurred in connection with a prior action; but there is no reason why recovery of such fees should be denied simply because the two causes (the one against the third person and the one against the party whose breach of duty made it necessary for the plaintiff to sue the third person) are tried in the same court at the same time.

(Citations omitted.)

The Massachusetts Supreme Court agreed in *M.F. Roach Co. v. Town of Provincetown*, 355 Mass 731, 247 NE2d 377, 378 (1969):

> This case deviates from the usual in that the plaintiff, instead of first suing the third party and then recovering counsel fees incurred in that action from the tort-feasor in a second action, has joined both claims in one lawsuit. A similar situation was faced by the Supreme Court of California in *Prentice v. North Am. Title Guar. Corp.*, 59 Cal2d 618, 30 CalRptr 821, 381 P2d 645.
>
> ***
>
> We feel that the result reached by the California court was correct. *It would be unjust to deprive the plaintiff of its damages from the tortfeasor merely because it has conserved judicial resources by bringing one suit instead of two*.

(Emphasis added.)

The Fifth Circuit Court of Appeals similarly held in *Wood v. Old Sec. Life Ins. Co.*, 643 F2d 1209, 1218-19 (5th Cir 1981): "Plaintiff's claim for

attorney fees in this case is not precluded by the fact that they were not incurred in a prior action."

The Colorado Court of Appeals, applying New York law, examined the issue at length in *Prospero Associates v. Redactron Corp*., 682 P2d 1193, 1199 (Colo App 1983):

> [Defendant] urges the inapplicability of [the] exception, premising its argument on the requirement that the third-party litigation be a prior, [separate] litigation. [Defendant] suggests that since the rights of all three parties here were litigated in one action, no attorneys' fees may be awarded.
>
> *There is no reason why attorneys' fees should be recoverable when the aggrieved party files separate lawsuits against the contract breacher and the tortfeasor, but should be denied when he consolidates both into one lawsuit. [Defendant's] assertion that attorneys' fees are recoverable only for a separate lawsuit is without basis in New York law. While some New York cases refer to separate litigation, others do not.*
>
> ***
>
> The Restatement notes that this rule applies: "[w]hen a cause of action or an alleged cause of action against the defendant in a proceeding exists only because of the tort of another ***."
>
> *Thus, while New York law recognizes that separate lawsuits frequently result from tortuous interference, we find no requirement that a plaintiff sue the breaching party and the tortfeasor in separate actions*.

(Citations omitted. Emphasis added.)

Similarly, in Michigan, "The fact that the 'prior action' is tried with the action in which the legal expenses are claimed has no significance. *** '[T]he fact that a number of claims are brought in a single lawsuit does not mean that

one or some of the claims cannot be considered prior litigation for the purpose of applying the exception.'" *Michigan Nat. Bank v. Kroger Co.*, 619 F Supp 1149, 1159 (ED Mich 1985), *citing Larson v. Van Horn*, 110 Mich App 369, 313 NW2d 288, 285 (1981). (Other citations omitted.)

The Fifth Circuit followed the First Circuit in *Mut. Fire, Marine & Inland Ins. Co. v. Costa*, 789 F2d 83, 89-90 (1st Cir 1986), where the Court noted:

> It is true that, in some cases that have discussed the third-party exception to counsel fees, courts have referred to a requirement that the litigation involving the third party take place in a "prior proceeding". *More recently, however, courts have clarified that it is not necessary for the litigation against the third party to have been separate from the litigation between the plaintiff and defendant*.

(Emphasis added.)

The Indiana Supreme Court summed up the policy behind allowing attorney fees under the exception without requiring multiple suits:

> It is also not a requirement that the litigation with the third party caused by the defendant's wrongful act be in a separate action. *The test of recoverability of attorney fees is not whether they were incurred in a separate action, but whether they were incurred in an action against a third party. In light of our rules and case law which encourage the disposition of all related issues in a single litigation, it would surely be inappropriate to permit the recovery of counsel fees to turn on the existence of a separate and discrete proceeding*.[6]

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[6] *Masonic Temple Ass'n of Crawfordsville v. Indiana Farmers Mut. Ins. Co*., 837 NE2d 1032, 1039-40 (Ind Ct App 2005) (Citations omitted. Emphasis added.) *Also see, Troutman v. Erlandson*, 287 Or 187, 204, 598 P2d 1211 (1979):

The Colorado Supreme Court came to the same conclusion in *Rocky Mountain Festivals, Inc. v. Parsons Corp*., 242 P3d 1067, 1072-73 (Colo 2010):

> The court of appeals has recognized that it is sometimes appropriate for a plaintiff alleging wrong-of-another damages to seek to recover his litigation costs with respect to a distinct subset of claims as opposed to an entire litigation. Specifically, the court in [*Swartz v. Bianco Family Trust*, 874 P2d 430, 434-35 (Colo App 1993)] held that *a party may recover attorneys' fees incurred during litigation in which the underlying dispute is litigated alongside the dispute with the third*-party wrongdoer. As the court of appeals noted, "*[t]o conclude otherwise would require that separate lawsuits be filed involving the same subject matter and parties with the attendant expense to the litigants and the resultant burden upon the judicial system.*"

(Citations omitted. Emphasis added.)

There is no authority in Oregon requiring that third-party practice be avoided and discrete lawsuits filed when attorney fees are sought under the third-party exception. Judicial economy has long been the public policy in Oregon. The rule of law proposed by Sharabarin, and endorsed by the trial court and Court of Appeals would result in multiple unnecessary lawsuits being filed in every case where a breach of contract triggers litigation with a third-party – unless the nonbreaching party chooses not to seek recovery of the

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> The legislature of this state has been steadily liberalizing the rules of joinder of causes of action and of suit. Related thereto is the abolishment of the distinction between law and equity. It is reasonable to conclude that the public policy of this state

attorney fees incurred as a result of the breach. This would either be inequitable or, more inevitably, result in added expense to parties and a tremendous additional burden on the courts. On this issue, the Court of Appeals erred and the trial court must be reversed.

VII. CONCLUSION

For the reasons set forth above, this Court should affirm the Court of Appeals with regard to the indemnity clause and the decision that the exception to the jury instruction on damage was properly preserved. This Court should reverse the Court of Appeals with regard to the measure of damages, including the entitlement to attorney fees as consequential damages. The case should be remanded to the trial court for a new trial on breach of contract damages and indemnity.

The trial court should be reversed and this matter remanded for trial as noted above.

Dated this 16th day of September, 2014.

Respectfully submitted,

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encourages the disposition in one proceeding of claims between parties litigant. (Citations omitted.)

CERTIFICATE OF COMPLIANCE WITH BRIEF LENGTH AND TYPE SIZE REQUIREMENTS

Brief length

I certify that this brief complies with the 14,000 word limit for Supreme Court briefs in ORAP 9.17(3)(c), and that the word count of this brief as described in ORAP 5.05(2)(b)(i) is 11,157 words.

Type size

I further certify that the size of the type in this brief is not smaller than 14 point for both the text of the brief and footnotes as required by ORAP 5.05(4)(g).

DATED: September 16, 2014.

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CERTIFICATE OF FILING AND SERVICE

I certify that on the date shown below, I **electronically filed** the attached BRIEF ON THE MERITS by using the Oregon e-Filing System.

I further certify that on the date shown below, I **electronically served** the attached BRIEF ON THE MERITS on the following person(s) by using the Oregon Appellate e-Filing system:

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