No. S280598

IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

OSCAR J. MADRIGAL and AUDREY MADRIGAL,
Plaintiffs and Respondents,
v.
HYUNDAI MOTOR AMERICA,
Defendant and Appellant.

California Court of Appeal, Third District, Civil No. C090463
Appeal from Placer County Superior Court
Case No. SCV0038395
Honorable Michael Jones

REPLY BRIEF ON THE MERITS

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INTRODUCTION

Code of Civil Procedure section 998 penalizes plaintiffs who "fail to obtain a more favorable judgment or award" than a prior 998 offer, by requiring the plaintiffs to pay the defendant's post-offer costs out of "any damages awarded." (Subds. (c) & (e).)[1]

Section 998's purpose in doing so is "to encourage the settlement of lawsuits *prior to trial*" given the "time delays and economic waste *associated with trials*." (*Martinez v. Brownco Construction Co.* (2013) 56 Cal.4th 1014, 1017, 1019, italics added.)

The question presented is whether section 998's cost-shifting provisions nevertheless "apply if the parties ultimately negotiate a pre-trial settlement." (Order Granting Review.)

Hyundai says those penalty provisions obviously apply to cases that settle, because they don't expressly *exempt* such cases. But the penalty's application to settlements is far from obvious.

Until the decision here, no appellate court in section 998's 170-year history had ever held that section 998's penalty provisions apply to cases that settle. The dissenting justices in this case and in *Ayers v. FCA US, LLC* (2024) 99 Cal.App.5th 1280, 1311-1318 (dis. opn. of Viramontes, J.) certainly didn't consider the penalty's application to cases that settle a foregone conclusion. Each of those dissents would have held that section 998's penalty *doesn't* apply, just as the trial courts in those cases

[1] All statutory references are to the Code of Civil Procedure.

ruled, too. The absence of any reference to "settlement" on the face of section 998 thus signals only that the Legislature never contemplated that it would be used to penalize parties who settle.

A closer examination of the text, legislative history, public policy, and other tools of interpretation ends all doubt. They *all* indicate that section 998's penalties don't apply where parties negotiate a pre-trial settlement.

Plain Text. The language in section 998(c)(1) is a bad fit for cases that settle. It penalizes plaintiffs for "fail[ing]" to obtain a more favorable "judgment or award" by awarding a defendant's post-offer costs out of any "damages awarded." These terms are all consistent with applying penalties following *adjudications,* not settlements. Hyundai's contrary reading erases the words "judgment or award" and inserts the word "result." But if the Legislature wanted section 998's penalties to apply to any "result"—as opposed to a "judgment or award"—it could've said so. It didn't. That choice must be given effect.

Surely, the Legislature was aware that the overwhelming majority of cases end in settlement, yet it chose words that presuppose section 998's application only to *adjudications*. By its word choice, the Legislature directed penalties at certain types of conclusions of lawsuits (namely, adjudicatory results) that are distinct from the most common type of "result" of a lawsuit—a *settlement* in which *proceeds* are *negotiated* and not *awarded*.

Legislative History. Legislative materials dating back to section 998's inception signal that the Legislature has long

contemplated that penalties would apply to adjudications—such as when a party "fail[s] to settle [and] the result *after trial* is less favorable than the offer that was made to settle the case *before trial*." (MJN-664, italics added.)[2] Those materials show that the California Bar and other stakeholders have taken the same view. Applying section 998 to pre-trial settlements would thus go beyond anything the Legislature contemplated. Hyundai has not cited to *any* legislative materials showing otherwise, and instead, insists this Court should close its eyes to the legislative history because, according to Hyundai, it's "unnecessary." (Answering Brief on the Merits (ABM)-9, 23, 34.)

Section 998's Purposes. Section 998's purpose is to encourage pre-trial settlements that "reliev[e] the crowded trial calendars." (MJN-189.) Penalizing parties who settle after rejecting a 998 offer will deprive parties of "flexibility" to settle in light of "new evidence bearing on the plaintiff's injuries or the defendant's culpability," or any other new developments that arise during litigation. (See *Martinez, supra,* 56 Cal.4th at p. 1021.) Hyundai doesn't argue otherwise. Nor could it. Requiring parties to settle around 998's penalties makes it harder to settle. After all, in some cases, applying those penalties would wipe out a plaintiff's recovery and cause her to owe money to the defendant. Plus, a significant benefit to settlement—the parties' ability to fashion a settlement in whatever way they

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[2] MJN cites refer to appellant's concurrently filed motion for judicial notice and the exhibits attached thereto.

compromise—disappears if the law imputes a non-stated term in the form of possible section 998's penalties into every settlement.

Additionally: Because courts generally haven't applied section 998 to cases that settle, affirming the majority's novel ruling will result in a sea change in the law that threatens to inundate courts with complex motions on whether a rejected 998 offer is more favorable than the settlement offer that was ultimately accepted. And since that analysis requires assessment of non-financial terms, courts will have to determine whether a settlement was more favorable than a prior offer based on matters that are *subjective* to the parties—such as where a settlement is for a lower amount than a prior offer, but includes non-monetary terms that a plaintiff may find more favorable than any monetary difference (i.e., where the later offer has better enforcement mechanisms).

The Opening Brief elaborated on each of these points (except on *Ayers*, which was decided after that brief filed). Hyundai's Answering Brief doesn't persuasively refute them.

ARGUMENT

I. The Recent *Ayers* Dissent Cogently Explains Why Section 998's Penalty Provision Should Be Interpreted As Not Applying When Cases Settle.

The Opening Brief showed that the *Madrigal* dissenting opinion is better-reasoned than the majority opinion. After our brief filed, another dissent in another published opinion—*Ayers, supra,* 99 Cal.App.5th 1280—concluded that section 998's penalty doesn't apply to cases that settle. Hyundai highlights the *Ayers* majority opinion, while wholly ignoring the dissent. But the dissent's analysis applies equally to this case. We summarize it for the Court's benefit.

The plain text of section 998's penalty provisions can reasonably be read as inapplicable to cases that settle. The *Ayers* dissent concluded that although section 998's penalty provisions *can* be interpreted to apply to cases that settle because the text doesn't expressly exempt such cases, that "is not the only" reasonable interpretation. (99 Cal.App.5th at p. 1313.) The penalty provisions applies where the plaintiff ""*fails to obtain* a judgment more favorable than a previously rejected or withdrawn offer to compromise."" (*Ibid.*, quoting *Madrigal v. Hyundai Motor America* (2023) 90 Cal.App.5th 385, 413 (dis. opn. of Robie, acting P.J.), italics in *Madrigal.*) "[A] settlement is not a failure of either party, rather, it is a voluntary resolution of a dispute…." (*Id.* at p. 1313.) "Further, settlements are not always 'functionally the equivalent of judgments, such that reference to one infers or includes the other.'" (*Ibid.*) Thus, "'fails to obtain'

may reasonably be understood to refer to the result flowing from the plaintiff's *unilateral* action rather than a result flowing from a compromise between opposing parties." (*Ibid.,* original italics.) "[A]t the very least, the statute's use of those words calls into question whether a settlement for less that the unaccepted offer equates to a failure to obtain a more favorable judgment under section 998(c)(1)." (*Id.* at p. 1314.) The text, thus, is "equally susceptible to" multiple interpretations—and a review of the legislative history and section 998's purpose are necessary to determine which one the Legislature intended. (*Ibid.*)

Legislative history suggests that section 998 doesn't apply. "Although nothing in the legislative history definitively" answers the question, the history "tends to support the conclusion that the Legislature did not intend to have section 998(c)(1) apply to" cases resolved through settlement. (*Ayers, supra,* 99 Cal.App.5th at p. 1314.) That history reflects an intent to "conserve precious court resources by incentivizing settlements that would circumvent *a full adjudication of the merits*," and legislative analyses of an amendment to expand section 998 to arbitration "repeatedly stated" that the penalty applies "when a party rejects a settlement offer and subsequently fails to do better *at trial*." (*Id.* at pp. 1314, 1316, first italics added, second italics in original.)

Applying section 998 penalties to cases that settle undermines the statute's purpose of avoiding trials. This Court has previously recognized section 998's penalty provision is designed to avoid delays and waste associated *with trials*. (*Ayers,*

supra, 99 Cal.App.5th at p. 1316, citing *Martinez*, *supra*, 56 Cal.4th at p. 1019.) Indeed, "'our public policy in favor of settlement primarily is intended to reduce the burden on the limited resources of the trial courts.'" (*Id.* at pp. 1316-1317, quoting *Wilson v. Wal-Mart Stores, Inc.* (1999) 72 Cal.App.4th 382, 390-391.) Applying section 998's cost-shifting penalty to cases that settle will discourage parties from settling, and instead "encourage them to take their chances at trial…." (*Id.* at p. 1317.) While parties theoretically can address cost issues in their settlements, the burden of attempting to do that "injects additional complications and difficulties to resolving the case, which is contrary to the statute's purpose." (*Ibid*.)

The Madrigal and Ayers majority opinions upset the status quo. Some version of section 998's penalty "has been California law for at least 170 years," yet "only in the last year has an appellate court reached the issue." (*Ayers, supra,* 99 Cal.App.5th at p. 1317.) "When we consider the fact that the overwhelming majority of civil cases resolve in settlements, and that only two recent California appellate courts, including the case at bar, have ever had to address the issue may reflect a general understanding by the trial courts and the parties that section 998(c)(1)'s cost-shifting provision does not apply to settlements." (*Id.* at pp. 1317-1318.)

II. None Of Hyundai's Arguments Overcome The Reasoning In The *Madrigal* and *Ayers* Dissents, Or The Other Points In Plaintiffs' Opening Brief.

Section 998's penalties are imposed to encourage parties to reach settlements that avoid the time and expense of trial. The Opening Brief and the dissenting opinions in *Madrigal* and *Ayers* showed that all interpretative aids support the logical conclusion that follows: section 998's penalties don't apply where parties settle before trial. Hyundai's responses don't refute that showing or even address the *Ayers* dissent.

A. Section 998's text signals that the Legislature has long presupposed that section 998's penalties would apply following adjudications, not following negotiated, pre-trial settlements.

Hyundai says section 998's penalty unambiguously applies to settled cases because section 998 doesn't expressly *exclude* settlement. (ABM-17.) But the fact that section 998's penalty provision doesn't mention settlements is hardly dispositive. The omission of any mention of settlement could merely reflect that the Legislature *never so much as considered* that the penalty would apply to settlements—a conclusion that's supported by section 998's plain text. That text penalizes a plaintiff's "*failure*" to secure a more favorable "*judgment or award*" by requiring her to pay the defendant's post offer costs out of "any *damages awarded*" to her. (§ 998, subd. (c)(1), italics added.) Although section 998 doesn't expressly say so, its language signals that its

penalties apply only to cases that end in adjudications, and not where parties reach a pre-trial settlement.

Nothing that Hyundai says comes close to showing that section 998(c)(1)'s terms clearly encompass settlements—let alone that the text so clearly makes section 998's penalties applicable to settlements that the Court should affirm a split-decision, novel holding applying penalties to settlements *without even considering* legislative history or public policy. (ABM-25-33.)

"Judgment or award" As shown (OBM-27-28), if the Legislature wanted section 998(c)(1) to apply to settlements, it would've drafted section 998(c)(1) to apply whenever a plaintiff fails to obtain a more favorable "result"—a word that Hyundai uses repeatedly though it is found nowhere in the statute—instead of requiring a more favorable "judgment or award." (See also *Ayers, supra*, 99 Cal.App.5th at p. 1315 [dis. opn.: 1997 amendment adding "award" "shows an intent to apply section 998(c)(1)'s cost-shifting provision only in those instances where the litigation ends after an adjudication"].)

Hyundai responds by citing cases that have interpreted "judgment" to encompass settlements. (ABM-26, 28-29, 60-61.)

But we already addressed this point (OBM-58-59), including the exact cases Hyundai cites—*DeSaulles v. Community Hospital of Monterey Peninsula* (2016) 62 Cal.4th 1140 and *Goodstein v. Bank of San Pedro* (1994) 27 Cal.App.4th 899. *DeSaulles* and *Goodstein* didn't consider whether section 998(c)(1)'s penalty applies to cases that settle. They addressed

the meaning of "judgment" in a *different* subdivision of section 998 (subdivision (b)) that articulates the criteria for a valid 998 offer and that states *in that context* that an offer must "allow judgment to be taken" against the offeror. (See OBM-58-59.) Cases are not authority for propositions not considered. (*Gonzalez v. Mathis* (2021) 12 Cal.5th 29, 45.) And there's no "inflexible rule" that a word has "precisely the same meaning" throughout a statute. (See OBM-59, quoting *People v. Superior Court* (2018) 6 Cal.5th 457, 467.)

Hyundai says plaintiffs haven't shown why "judgment" should be interpreted differently in section 998(c)(1) than in section 998(b)—i.e., why section 998(c)(1)'s penalty doesn't apply to cases that settle. (ABM-61.) Nonsense. Our entire Opening Brief is directed at that point.

In a nutshell: The goal of statutory interpretation is to effectuate the Legislature's intent—which, as to section 998, is to encourage settlements that help clear trial court calendars. (*Mendoza v. Fonseca McElroy Grinding Co., Inc.* (2021) 11 Cal.5th 1118, 1125, cited at OBM-25.) "Judgment" in section 998(c)(1) shouldn't be interpreted to encompass settlements, because section 998(c)(1)'s wording, legislative history, and pro-settlement purposes all signal that the Legislature did *not* intend section 998(c)(1) to encompass settlements. (OBM-25-73.)

Nor does it matter that the settlement in this case contemplated the court entering a judgment under Code of Civil Procedure section 664.6. (See ABM-59, 63-65.) As shown (OBM-63-64), the question isn't whether a settlement would result in

the entry of a document titled "judgment"; it's whether the Legislature intended section 998's penalty to apply to cases resolved through a pretrial settlement. Pretrial settlements achieve the Legislature's goal of avoiding trials equally well regardless of whether they result in a section 664.6 judgment or not. As the *Ayers* dissent observed, that "'a party to a settlement may seek to transform it into a judgment *for enforcement purposes* [citation] does not mean that the one is necessarily the equivalent of the other…." (*Ayers, supra*, 99 Cal.App.5th at p. 1313, italics added, quoting *Mares v. Baughman* (2001) 92 Cal.App.4th 672, 676-677, italics and brackets in *Ayers*.) Simply put: the fact that a judgment may be entered after a settlement doesn't mean that it's an *adjudicatory* judgment for purposes of triggering section 998's penalty provisions. (See OBM-63-64.)

"Fails to obtain" Building on the *Madrigal* dissent's reasoning, the Opening Brief argued that a negotiated settlement isn't a "fail[ure] to obtain" a certain judgment or award (section 998(c)(1)'s trigger), because "fail" means *involuntarily* falling short of a purpose, and a settlement is a voluntary compromise with no winner and no loser. (OBM-28-29; 90 Cal.App.5th at pp. 413-415 (dis. opn.).) Hyundai summarily declares that there's no need for interpretation, because "fails to obtain" plainly just means any instance where a plaintiff doesn't obtain a judgment better than the 998 offer. (ABM-29-31.) But, in making this argument, Hyundai neglects to mention that a plaintiff must've *tried* to get a judgment in order to have *failed* to get a judgment. When a plaintiff *compromises*—e.g., he accepts less than he

wanted in exchange for finality and certainty—he's no longer pursuing a judgment at trial.

The *Madrigal* and *Ayers* dissents show that section 998's reference to a "fail[ure]" is either inconsistent with a settlement, or at least "call[s] into question" whether the Legislature intended section 998(c)(1) to apply to settlements. (90 Cal.App.5th at pp. 413-415 [*Madrigal* dissent]; 99 Cal.App.5th at pp. 1313-1314 [*Ayers* dissent, agreeing plain language indicates that section 998 doesn't apply to settlements because "a settlement is not a failure of either party"].) In light of those well-reasoned dissents, Hyundai's ipse dixit insistence that "fails" is unambiguous—i.e., can *only* be read to encompass settlements—rings hollow.

"*Compromise settlement*" As shown (OBM-29-30), section 998 treats formal judgments entered in the wake of a settlement differently from *adjudicated* judgments in that section 998 subdivision (f) assigns a special name to a judgment entered as part of an accepted 998 offer: a "compromise settlement."

Hyundai says this shows that dispositions entered after settlements are "judgments." (ABM-31-32.) But that ignores the key point: "Judgment" is not a monolithic term for purposes of section 998. A judgment resulting from an accepted 998 offer is treated as legally different from other types of judgments. This is a strong indication that the Legislature likewise intended *settled resolutions* to be treated different from *adjudicated resolutions* when it comes to triggering the section 998(c)(1)'s penalty.

"*Any damages awarded*" As another indicator that the Legislature had adjudicatory resolutions rather than settlements in mind when drafting section 998(c)(1), the Opening Brief noted that where the penalty applies, section 998 dictates that costs "'shall be deducted from any *damages awarded in favor of the plaintiff*.'" (OBM-30, quoting § 998, subd. (e), italics added in OBM.) Hyundai argues that the penalty doesn't always come out of a damages award, because sometimes the plaintiff subject to cost-shifting won *no* damages *at trial*. (ABM-32-33.)

But that's irrelevant. Subdivision (e) plainly makes a plaintiff pay a defendant's post-offer costs out of "any damages awarded" to ensure that where a plaintiff recovers, a defendant can immediately recover its post-offer costs. This concern would apply equally to cases that end in settlements (if section 998's penalties apply to settlements). Thus, had the Legislature intended section 998 to penalize settling parties, section 998(e) would've captured both scenarios by referring to any "proceeds the *plaintiff recovers*"—as the Legislature did in section 1032, a related provision. (OBM-30-31, citing Code Civ. Proc., § 1032(a)(4); *DeSaulles, supra,* 62 Cal.4th at p. 1153.) The Legislature's choice to instead penalize plaintiffs by awarding defendants post-offer costs to be paid out of any "damages awarded" signals that the Legislature wasn't considering penalizing plaintiffs who settle for *proceeds* that are *negotiated* for *consideration*.

Plus: It makes no sense that a plaintiff could compromise on a settlement to achieve finality and certainly, only to be on the

hook for a then-unknown sum of a defendant's costs that the plaintiff would have *to pay back to the defendant*. That amount could eclipse the negotiated settlement proceeds, rendering a plaintiff owing a defendant even after a compromise is reached. (See OBM-48-49.)

"***Prior to commence[ment] of trial***" The Opening Brief noted that 998 offers can be made until 10 days before trial, and accepted before "the commence of trial" likewise shows a focus on avoiding *trials*. (OBM-31.)

Hyundai *agrees* that the Legislature intended section 998 to avoid resource-intensive trials. (ABM-33.) Hyundai argues, however, that the Legislature also intended section 998's penalty to avoid *pre-trial* proceedings by encouraging *early* settlement. (*Ibid.*) But Hyundai doesn't provide support for that claim. And, as the Opening Brief showed, Hyundai's interpretation of section 998(c)(1) would *discourage* rather than encourage settlements. (See also § II.C, *post*.)

B. Legislative materials are relevant in deciding a novel question that may dramatically change how section 998 has operated for years.

Legislative history shows the Legislature contemplated penalties following trial, arbitrations, or other adjudications—not in cases where parties avoid trial by reaching a negotiated settlement. Hyundai hasn't shown otherwise.

1. The Legislature, the State Bar, and other stakeholders have long presumed that section 998 applies only following trials or other adjudications, and not where parties moot the need for adjudication by settling.

Materials across several decades show that individual legislators, the Legislature as a whole, the State Bar, and other practitioners have always contemplated that penalties would apply only following adjudications—that is, where the party rejecting the 998 offer: "does not get a more favorable judgment *at the trial*" (1969); secured a "*[v]erdict* [l]ower" than the rejected offer (1971); fails to secure "a more favorable result *at trial or arbitration*" (1999); or "fail[s] to settle [and] the result *after trial* is less favorable than the offer that was made to settle the case *before trial*" (2015). (MJN-131, 226, 580, 664, italics added.) Hyundai cites *no legislative materials* indicating that the Legislature ever contemplated that section 998's penalties would apply where the parties reach a settlement that makes further adjudication unnecessary.

Hyundai instead argues that the legislative history is irrelevant because section 998(c)(1)'s text *unambiguously* requires applying penalties to cases that settle. (ABM-34-35.) To make this point, Hyundai posits that "judgment or award" is unambiguously synonymous with the word "result," and that a settlement is clearly a case-ending "result."

But Hyundai's circular reasoning doesn't work. The statue never even references settlements, which suggests that the Legislature never contemplated that penalties would apply to parties who settle before trial. Nor does the statute use the word "result," which Hyundai tries to add to the statute. Plus, the *Madrigal* and *Ayers* dissents both found section 998's legislative history to be a relevant and persuasive interpretive tool. (90 Cal.App.5th at pp. 416-417; 99 Cal.App.5th at pp. 1314-1316.) This Court should do the same.

The legislative history would be an important interpretive aid even if section 988's language appeared unambiguous at first blush: "[L]anguage that appears clear and unambiguous on its face may be shown to have a latent ambiguity," and legislative history is relevant to determine what the Legislature intended. (*Spotlight on Coastal Corruption v. Kinsey* (2020) 57 Cal.App.5th 874, 891-892 [collecting cases where statute was found to have a *latent* ambiguity because literal interpretation would frustrate legislative purpose]; *Varshock v. California Department of Forestry & Fire Protection* (2011) 194 Cal.App.4th 635, 644, 647 [finding a *latent* ambiguity and looking to legislative history to "'resolve the question of [statutes'] intended meaning'"]; *Union Bank of California v. Superior Court* (2004) 115 Cal.App.4th 484, 488 ["language that appears unambiguous on its face may be shown to have a latent ambiguity; if so, a court may turn to customary rules of statutory construction or legislative history for guidance"].) There's no possible basis to adopt a rule that would

radically change how section 998 has operated for over 170 years *without even scanning* the legislative history.

Equally unavailing is Hyundai's attempt to downplay the substance of the legislative history—namely, the materials showing that the Legislature viewed section 998's penalty as applying only following an adjudication. Hyundai dismisses references to "verdicts" and "trials" as "stray remarks." (ABM-36.) But the references to "trials" and "verdicts" are far more pervasive than Hyundai's disparaging characterization suggests: They appear in multiple materials dating back to the 1848 Field Code and continue through *seven* amendments to section 998 enacted between 1969-2015. (See OBM-32-41.)

Hyundai emphasizes that the legislators and other stakeholders who made the comments were not specifically addressing whether section 998 penalties apply to settlements. (ABM-36-39.)[3] That's beside the point. As the *Madrigal* and *Ayers* dissents concluded, the comments are relevant to show that the Legislature was focused on avoiding *trials*. (90 Cal.App.5th at pp. 416-417; 99 Cal.App.5th at pp. 1314-1316; see also, e.g., MJN-198 [section 998's purpose is "reliev[ing] the crowded trial

[3] Hyundai also takes aim at the *type* of legislative history materials Plaintiffs submitted. (ABM-35.) Hyundai's argument on this point is in a separately-filed opposition to the motion for judicial notice filed with our Opening Brief. (*Ibid.*) We follow suit, addressing Hyundai's argument in our concurrently-filed reply in support of that motion for judicial notice.

calendars of our courts"].)[4] By contrast, Hyundai has not cited any legislative history showing the Legislature intended section 998's penalty to apply in cases that settle.

The clues from the legislative history point in only one direction—and it's the same direction indicated by the Legislature's word choice: The Legislature didn't intend section 998 to apply to cases that settle before trial. (See *Ayers, supra*, 99 Cal.App.5th at p. 1314 [dis. opn.: even if not "definitive[]," the legislative history "tends to support the conclusion that the Legislature did not intend to have section 998(c)(1) apply to the circumstances before us where the litigation ends in a mutually agreed-upon settlement"].)

2. The Legislature's choice to *not* dramatically expand how section 998 has been applied is entitled to deference.

Lacking any affirmative support in the legislative history, Hyundai attempts to justify the *Madrigal* majority's reliance on legislative *silence*. (ABM-61-63.) But silence surely doesn't outweigh the decades of *legislative materials* indicating that the Legislature has always contemplated that section 998's penalties apply to *adjudicated* cases. Hyundai's position that the Court

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[4] Hyundai argues that the settlement here occurred *at trial*, not before. (ABM-27.) But the settlement was before opening statements, which is what section 998 defines as commencing trial. (§ 998, subd. (b)(3).) And it avoided a trial that was scheduled to last up to three weeks (1-RT-78), thus achieving the Legislature's priority of conserving trial resources.

should on the one hand shut its eyes to these materials, and on the other hand, interpret something from purported legislative silence, makes no sense.

More importantly, both Hyundai and the *Madrigal* majority have it backwards. "Even though the vast majority of civil cases resolve in settlements," until the *Madrigal* decision, not one court had held that "section 998(c)(1)'s cost-shifting provision applies to a negotiated settlement." (*Madrigal, supra,* 90 Cal.App.5th at pp. 417-418 (dis. opn.), internal citations omitted.) Thus, for the 170+ years during which section 998 has existed in one form or another, virtually everyone presumed that it only applies to adjudications. Practitioners confirm this: The *Madrigal* majority's ruling was a dramatic change to existing understandings as to how section 998's penalties functioned. (Consumer Attorneys of California Letter ISO Review at 1; Dreyer Babich Letter ISO Review at 2; Wirtz Law Letter ISO Review at 1.) Hyundai hasn't pointed to a single practitioner who said otherwise. Against this backdrop, the Legislature's choice not to amend section 998(c)(1) to add a reference to settlements indicates that the Legislature *agrees* with how section 998 had been applied until the recent decision in this case—that is, the Legislature *doesn't want* section 998 to apply beyond the trials or other adjudications to which the statute has long been applied.

Indeed, in amending section 998 to add the word "award" to clarify that 998's penalties apply to arbitration awards just like they do to trial judgments, the Legislature made clear that the penalty provisions' application is *narrow*. After all, if the word

"judgment" was already as all-encompassing as Hyundai claims, then there would've been no need to add the word "award."

The Legislature's choice *not* to expand the penalty provision's application to cases that settle should be given effect. It's not an invitation for the courts to unilaterally expand section 998 by ruling that it penalize parties merely for reassessing a prior reluctance to settle—i.e., the very conduct that section 998 is supposed to encourage. (See *Murillo v. Fleetwood Enterprises, Inc.* (1998) 17 Cal.4th 985, 1001 [section 998 is supposed to push "parties to assess realistically their positions prior to trial," internal quotations omitted].)

Hyundai's observation (ABM-62) that the Legislature didn't amend section 998 following *Goodstein* is unpersuasive, too. *Goodstein* didn't address whether section 998(c)(1)'s penalty applies in cases that settle. And, in fact, no court read *Goodstein* as relevant to that question for almost *two decades* after it was decided, i.e., until this case. (OBM-61-63.)

Hyundai has no response to the key point: *Goodstein* didn't address the scope of section 998(c)(1)'s penalty, so nothing about *Goodstein* would've signaled a need to amend that penalty provision. Hyundai's reliance on the absence of a post-*Goodstein* amendment to section 998(c)(1) is therefore misguided.

Decades of legislative materials show that the Legislature long contemplated that section 998's penalty would apply only following a trial or other adjudication—and not where, as here, parties negotiate a settlement that avoids the need for further

adjudication. Consistently, parties and courts have generally presumed the same thing. If the Legislature thought that virtually everyone had been misled in such a consequential way, it surely would've stepped in to clarify that section 998 prioritizes forcing early settlements so much that its penalties apply even where the parties settle later on. The Court should respect the Legislature's choice to *not* dramatically alter how section 998 has operated for nearly two centuries.

C. Plaintiffs' interpretation furthers section 998's purpose of avoiding trials, while Hyundai's interpretation encourages parties to roll the dice at trial rather than settling.

The *Madrigal* and *Ayers* dissents concluded that applying section 998(c)(1) to cases that settle would undermine section 998's purpose of encouraging pre-trial settlements, and "come at the expense of the parties' ability to settle later as the litigation progresses." (90 Cal.App.5th at pp. 418, 422-424; 99 Cal.App.5th at pp. 1316-1317.) The Opening Brief discussed these points, demonstrating that the specter of penalties imputed into every settlement (1) deprives parties of flexibility to settle as a case progresses, (2) causes friction to negotiations, (3) can wipe out the injured party's settlement, and (4) would create post-settlement litigation in any cases where parties settle on non-financial terms. (OBM-41-56.) Hyundai's responses are unavailing.

1. Section 998's primary purpose is to avoid *trials*, not to force the earliest possible settlement.

Hyundai challenges our premise that section 998's goal is to avoid trials. Hyundai says the Legislature *also* independently had a goal of promoting *early* settlement, and that section 998 therefore should be read to punish parties who settle before trial but after foregoing an earlier 998 offer. (ABM-41-42.)

But Hyundai cites nothing suggesting the Legislature sought to push early settlement even at the cost of discouraging later pre-trial settlements. Rather, this Court has repeatedly recognized that section 998's purpose is "to encourage the settlement of lawsuits *prior to trial*." (*Martinez, supra*, 56 Cal.4th at p. 1019, italics added; see also *Heimlich v. Shivji* (2019) 7 Cal.5th 350, 356 [998's penalties applicable "when the opponent rejects the offer and obtains a lesser result at trial"].) That's consistent with the legislative history. (See OBM-32-41.) And as the *Ayers* dissent concluded, it's also consistent with California's broader public policy favoring settlement: "'Although settlements achieved earlier rather than later are beneficial to the parties and thus to be encouraged, our public policy in favor of settlement *primarily is intended to reduce the burden on the limited resources of the trial courts*.'" (99 Cal.App.5th at p. 1316, citation omitted, italics in *Ayers*.)

The Legislature's focus is on avoiding *trials* because "'trial of a lawsuit that should have been resolved through compromise and settlement uses court resources that should be reserved for

the resolution of otherwise irreconcilable disputes.'" (99 Cal.App.5th at pp. 1316-1317, citation omitted.) The statute should be interpreted to promote this goal. (*Mendoza, supra*, 11 Cal.5th at p. 1125 ["fundamental task" in statutory interpretation is to "effectuate the law's purpose"].)

2. Hyundai has not persuasively refuted that its rule deprives parties of flexibility, and thereby impedes pre-trial settlements once a 998 offer has not been accepted.

As shown (OBM-42-50, 67-69), Hyundai's interpretation undermines section 998's goal of avoiding trials by encouraging parties to roll the dice at trial rather that attempting to settle as trial approaches. The *Ayers* dissent makes this point, characterizing the majority's position as "com[ing] at the expense of the parties' ability to settle later as the litigation progresses." (99 Cal.App.5th at p. 1316.)

Hyundai doesn't articulate any persuasive argument that cases would continue to settle as trial approaches if Hyundai's interpretation prevails; indeed, Hyundai shrugs at the very real possibility that penalizing parties who settle will yield fewer settlements. (ABM-69 ["Take first the concern that a plaintiff who previously rejected a 998 may be discouraged from entering into a settlement for less than that in response to newly discovered evidence or a change in the law. Maybe, maybe not"].)

Hyundai argues that its interpretation is necessary to drive plaintiffs to accept *early* settlement offers. (ABM-41-49.) But the

legislative history shows the Legislature was focused on *avoiding trials*—a goal achieved through *any* pre-trial settlement, not just early settlements. Hyundai hasn't cited anything indicating that the Legislature intended to privilege early settlements—let alone at the expense of the flexibility that *this Court* has recognized is necessary for the parties to settle later on. (See OBM-42-43, discussing *T.M. Cobb Co. v. Superior Court* (1984) 36 Cal.3d 273, 276, 281; *Martinez, supra,* 56 Cal.4th at p. 1021 ["[c]ourts look favorably upon applications [of section 998] that provide flexibility when parties discover new evidence"].)

Hyundai hasn't refuted our showing (OBM-41-57) that Hyundai's interpretation will discourage later settlements. Generally, many cases that don't settle during discovery or other early litigation will settle as trial approaches: "Experience shows many cases can be settled 'on the courthouse steps,' notwithstanding earlier unsuccessful settlement conferences." (Hanning et al., Cal. Practice Guide: Personal Injury (The Rutter Group 2023) ¶ 4:1378.) This makes sense. It's difficult for parties to reach agreements early on. Settling becomes easier as litigation progresses and parties become better able to assess their claims and reassess their willingness to settle—without nearly as much concern that a settlement offer may grossly undervalue or overvalue a claim. A plaintiff tries to obtain damaging evidence—often resorting to discovery motions—while a defendant tries to limit the claims through, for example, demurrers or summary judgment motions. A plaintiff tries to establish their damages, while a defendant tries to limit

recoverable damages. This process must be allowed to play out so that the parties know the value of their case and assess the risks of a zero-sum trial.

As we showed through hypotheticals (OBM-46-50), there are many scenarios where parties won't reach a pre-trial settlement if section 998 penalties are in the mix—parties will opt to roll the dice on trial in the hope of beating a 998 offer rather than agreeing to a settlement that will certainly trigger 998 penalties. (See Korobkin & Guthrie, *Psychological Barriers to Litigation Settlement: An Experimental Approach* (1994) 93 Mich. L.Rev. 107, 136 ["Losers were more likely to risk an uncertain trial verdict than to accept a settlement offer that appeared to leave them in a 'worse' position"].)

Giving courts the power to weigh the relative value of non-economic terms only heightens this problem. For example, a settlement term that gives a plaintiff more certainty of being paid may be a must-have term, given a plaintiff's sincere distrust of the defendant who wronged her. But the threat that this plaintiff could face section 998 penalties if *a court* doesn't agree with how much she genuinely valued a term for earlier-payment, liquidated damages, or other enforcement mechanisms will effectively doom any hope of a later pre-trial settlement.

The *Madrigal* and *Ayers* dissents agree that applying section 998's penalties will result in fewer cases settling before trial. (90 Cal.App.5th at pp. 423-424; 99 Cal.App.5th at p. 1317.) Indeed, the *Ayers* dissent pointed out that the parties had been

unable to reach an agreement on costs/fees as part of their settlement and instead had reserved that issue for future decision. (*Ayers*, at p. 1317.) That inability "is evidence that the additional burden of necessarily including fees and costs into every settlement injects additional complications and difficulties to resolving the case, which is contrary to the statute's purpose." (*Ibid.*) Hyundai has no meaningful answer.

3. There's no merit to Hyundai's portrayal of Plaintiffs as unreasonable, and of Hyundai's rule as necessary to achieve the Legislature's purpose.

Hyundai argues that the facts of this case illustrate why section 998's penalties must apply to settlements—Hyundai portrays plaintiffs as unreasonably "ignor[ing]" a 998 offer and dragging it through litigation, and argues that it should not be "punished" for having made an early settlement offer. (ABM-50-51, 66-67.) There are multiple problems with this argument.

First, plaintiffs didn't "ignore" the 998 offers. Just the opposite: Upon receiving each offer, plaintiffs *invited Hyundai to mediate*—and Hyundai declined. (2-AA-660.) Had Hyundai agreed to mediate, the case may well have been resolved sooner. Yet, the *Madrigal* majority's decision would punish a *plaintiff* for a defendant's refusal to even try to address plaintiff's concerns via mediation—in some circumstances, even if the parties settled in that mediation (i.e., if *the court* thinks the plaintiff settled for

less, without regard to whether *the plaintiff* prefers the ultimate settlement to the rejected offer).

Second, Hyundai's argument assumes that section 998's purpose is to incentivize *early* settlement, as opposed to incentivizing *any settlement that avoids the need for a trial*. As shown, that assumption is wrong.

Third, a holding that section 998's penalties *don't apply* to settlements doesn't "punish" Hyundai. Indeed, it's unclear how Hyundai would be "punished" by refusing to put its first offer back on the table, and then either securing a settlement for less than the amount previously offered or proceeding to a trial where the plaintiff must beat each of Hyundai's 998 offers. What *is* clear is that section 998 worked in this case—it operated to make plaintiffs think twice before burdening the court with a three-week trial. Moreover, plaintiffs' decision to end this case was premised on trial-court rulings on evidentiary matters that materially changed the anticipated trial on the day before the jury was summoned. (See OBM-15.) That's exactly the type of sober decision-making that section 998 seeks to compel.

Section 998 imposes penalties in specific circumstances as a way to incentivize certain behavior. The question is whether the Legislature intended pre-trial settlements to be one of those circumstances. A conclusion that the Legislature didn't intend section 998's penalties to operate in cases that settle doesn't punish Hyundai; it simply recognizes that this isn't the type of situation where the Legislature intended penalties to apply.

Nor does honoring the Legislature's intent that section 998 not apply to settlements strip Hyundai or other parties of the value of making an early 998 offer. A party who makes an early 998 offer will still have the "stick" that comes with such an offer—the offer gives that party extra leverage to push the other side to reach a settlement agreement. After all, if a settlement isn't reached, the party who rejected the early 998 offer may not only lose at trial. If she loses or wins but not by enough to beat *every 998 offer made*, she also risks her entitlement to costs and any statutory or contractual fees available, and will have to cover the other side's post-offer costs.

It makes no sense that a plaintiff would be able to agree to a settlement of a sum certain, only to have to pay defendant back a then-unknown sum to cover costs of litigation.

Hyundai doesn't dispute that even if section 998 applied in cases that settle, defendants would still generally continue to make additional 998 offers after the first one was rejected. Indeed, Hyundai did exactly that here—its series of settlement offers show that section 998 already gives defendants flexibility to make offers of varying amounts and terms, sometimes better than prior offers, sometimes worse.

Hyundai says adopting Plaintiffs' interpretation of section 998 would "incentivize" one class of defendants "not to settle at all after making an initial 998 offer, and instead to opt to go to trial:" those who are "confident that the other side would be 'unlikely to secure a more favorable judgment through continued

litigation" after fear of "los[ing] the benefit (and leverage) of cost-shifting by settling." (ABM-68.) Hyundai says plaintiffs' arguments "are not directed" at that assertion. (ABM-68.) But that isn't true. As shown (OBM-70-71), even defendants who *know* they'll secure a more favorable judgment at trial will still have reasons to settle after an unaccepted 998 offer, but before trial—among them, the immense leverage such defendants would have in subsequent settlement negotiations. (See OBM-70-71 [also discussing other reasons].)

It makes no sense to force parties in all cases to negotiate around section 998's penalties. Hyundai's response? Silence.

4. Hyundai hasn't shown that its rule is necessary to avoid gamesmanship.

As shown (OBM-68-69), there's no basis for the *Madrigal* majority's concerns that if section 998's penalties aren't applied to pre-trial settlements, plaintiffs will reject early 998 offers so they can rack up fees that they'll recover if they settle later.

Hyundai responds that it's not accusing plaintiffs of gamesmanship in this case, but that "the opportunity for gamesmanship is clearly present" unless 998 penalties apply to cases that settle. (ABM-66.)

But this assertion is completely ipse dixit: Hyundai doesn't actually respond to the substance of our argument. Nor could it. Plaintiffs/their counsel have no incentive to drive up costs and fees after rejecting a 998 offer with a plan of settling later:

Plaintiffs cannot unilaterally dictate whether a defendant will be willing to settle closer to trial. Thus, defendants still hold the proverbial "stick" since they can decide whether to compromise.

Moreover, even if plaintiffs do subsequently settle and become entitled to a cost award, Code of Civil Procedure section 1033.5 only allows costs (defined to include fees recoverable by statute) that are *reasonable*. (§ 1033.5, subd. (c) ["allowable costs shall be reasonably necessary to the conduct of the litigation" and "reasonable in amount"].) There's no incentive to unreasonably incur fees and costs, which won't be recoverable regardless of whether section 998 applies to pre-trial settlements.

5. Hyundai hasn't refuted that its rule punishes plaintiffs who do what the Legislature wanted—settle before trial.

As shown (OBM-51-53), Hyundai's interpretation would subvert section 998's goal of compensating the injured plaintiff, even though she settled before trial as the Legislature wanted. Again, Hyundai's responses are unavailing.

Hyundai says plaintiffs could've gotten more compensation in this case by accepting the 998 offer than they did in the later settlement. (ABM-52.) But the issue isn't the amount of the settlement, it's the impact of section 998's *penalty* on plaintiffs' recovery. It's undisputed that applying section 998's penalty in some cases will entirely wipe out a plaintiff's recovery (including to the point of obligating a plaintiff who settled for a positive recovery having to *owe the defendant*). Hyundai points out that

the same thing could happen at trial. (ABM-52.) But this makes sense where the plaintiff *never settles*, and instead requires a court to adjudicate the case; it doesn't make sense where the plaintiff does exactly what the Legislature wanted by reassessing his willingness to settle in the course of litigation and reaching a settlement before trial. (See OBM-51-52.) Applying section 998's penalties in this context isn't just unduly harsh; it defeats section 998's purpose since it will likely preclude settlement in most such cases. (See OBM-51-52.)

Hyundai says pre-trial proceedings burden courts as much as trials. (ABM-53-54.) But Hyundai offers no evidence that discovery proceedings consume nearly the resources of trials. Section 998's wording and legislative history signal Legislative intent to avoid *trials*. The Legislature didn't intend to inhibit a party from merely trying to investigate his case or from trying to stave off pleading or evidentiary challenges.

D. The burden on courts from having to decide 998 motions after cases settle isn't "overblown."

Hyundai dismisses as "overblown" the Opening Brief's showing that imposing 998 penalties in cases that settle would create voluminous new work for the courts. (ABM-54-55, 70-71.)

But Hyundai doesn't dispute the statistics: More than 200,000 unlimited civil case are filed in California each year, and 95% of California civil cases settle. (OBM-53.) Nor does Hyundai dispute that until this case, courts weren't imposing section 998 penalties to settled cases. (90 Cal.App.5th at pp. 417-418

[*Madrigal* dissent noting an "overall historical understanding" that 998 penalties don't apply to settlements]; 99 Cal.App.5th at p. 1317 [*Ayers* dissent noting "some indication that the majority's decision is upsetting the status quo"].)

If penalties are now available in settled cases, the number of section 998 fee-shifting motions will increase exponentially. Those motions will involve complex questions about the value of non-monetary terms in the unaccepted 998 offer as compared to those in the eventual settlement—questions that courts didn't have to deal with until the Court of Appeal decision in this case and that they're unequipped to deal with. (OBM-53-56.) While courts have dealt with the *validity* of non-monetary terms in a 998 offer, they've not had to weigh the *value* of the terms that may appear *in an executed settlement*—whose value to the plaintiff may be entirely subjective. How do you value a settlement that includes an apology from a defendant versus a prior offer that did not?

Comparing a 998 offer to a judgment for a sum certain is easy. That analysis becomes much more complicated when comparing an offer to an executed settlement that may have been reached only because the parties agreed to certain terms that are only subjectively quantifiable. For instance, let's say a defendant rejected a 998 offer that would've required him to pay a smaller amount immediately, but later reached a settlement that required a larger payment amount to be paid over a long time period. How is a court supposed to decide whether the settlement is more or less favorable than the rejected offer? Does the

defendant have to show that he wasn't financially well off enough to (comfortably) make the lump sum payment the first offer required—or that he had verifiable concerns that if he paid the plaintiff immediately, he'd lose any leverage to get the plaintiff to fulfill her settlement obligations? And at what point does the monetary difference between the offers matter?

In other contexts, courts simply presume that a defendant had good reason to insist on these terms. (See pp. 40-41, *post*.) There's no reason to believe the Legislature nevertheless would've wanted to replace the time that courts spent on trials by answering these types of complex questions—questions that will make it so much harder for the parties to later settle in the likely event that the first 998 offer is rejected. (OBM-53-55.)

Hyundai says parties will simply reach an agreement about whether section 998's penalties apply to the case. (ABM-70.) But that requires the parties to negotiate to *extract* an unnecessarily *imputed* term. Even assuming parties are willing to try to negotiate around section 998's penalties, the uncertainty about whether those penalties might still apply will likely doom many would-be settlements.

E. General contract principles further support the interpretation that section 998 penalties don't apply to settled cases.

As shown (OBM-56-58), construing section 998(c) to not apply to settlements is consistent with general contract

principles, including the merger doctrine. (OBM-56-58.) Hyundai's responses lack merit.

First, Hyundai says the merger doctrine applies only to interpreting or enforcing a contract, and that we aren't concerned here with interpreting the settlement agreement. (ABM-55-56.) But this doesn't make general contract principles irrelevant to how section 998 is interpreted. After all, contract principles inform how *everyone*—including the Legislature—understands how offers and contracts are supposed to function. Courts look to general contract principles when section 998's text is silent because if the Legislature wanted offers and contracts to work differently in the section 998 context, it would've said so. (See *T.M. Cobb, supra*, 36 Cal.3d at pp. 279-280 [general contract-law principles apply where section 998 is silent].) Section 998 is silent on whether or not a settlement agreement supersedes prior rejected prior offers. So, general contract principles apply. This means a rejected 998 offer is treated the same under section 998 as it would in any other context—namely, that the rejected offer is rendered a *legal nullity* that's subsumed within the final contract. (See *Bradford v. Southern California Petroleum Corp.* (1944) 62 Cal.App.2d 450, 461; Civ. Code, § 1625.)

Second, Hyundai says it "agrees with" the *Madrigal* majority's holding that the merger doctrine doesn't apply to the oral settlement agreement at issue here, only to written contracts. (ABM-56.) But the mere fact of Hyundai's agreement has no independent weight in the analysis. Hyundai doesn't explain *why* it agrees—nor does it even attempt to refute our

showing that the merger doctrine applies because oral settlements memorialized in a transcript and minute order are treated the same as signed writings. (Compare ABM-56 with OBM-57.) Hyundai ignores this flaw in the majority's conclusion.

Third, Hyundai says it couldn't have revoked its 998 offer by agreeing to a settlement on different terms. (ABM-57-58.) But even apart from the merger doctrine, it's well established that contracting parties "have the utmost liberty of contract to arrange their affairs according to their own judgment so long as they do not contravene positive law or public policy." (*Series AGI West Linn of Appian Group Investors DE, LLC v. Eves* (2013) 217 Cal.App.4th 156, 164, internal quotation marks omitted.) "The nonpaternalistic corollary to this freedom is that courts assume that each party to a contract is alert to, and able to protect, his or her own best interests." (*Ibid*.) Applying 998's penalties to cases that settle defies the principle that when parties enter into a contract, they've necessarily acted in their best interest—instead, a *court* will be charged with determining whether the rejected offer is more or less favorable than another offer that may contain entirely different terms. In contrast with the deference afforded to contracting parties in all other cases, *a court* would be substituting its judgment for the judgment of the parties who may have been happy to accept a lesser settlement amount in exchange for better enforcement mechanisms, a broader release, or other non-monetary terms.

The *Ayers* majority's reasoning underscores the problem; *Ayers* held that a plaintiff who settled for less money, but better

enforcement mechanisms was subject to section 998's penalties because "*[w]e think* the differences between [the offer and settlement] are immaterial as a matter of law." (99 Cal.App.5th at pp. 1308-1309, italics added.) Thus, *Ayers* broadly declared a rule that after rejecting a prior 998 offer with weak enforcement mechanisms, a plaintiff *can't* agree to less money but better enforcement mechanisms without subjecting herself to section 998's penalties.

Given section 998's pro-settlement purposes—and the "bedrock principle of contract law" that parties act in their best interest when reaching any contract (*Series AGI*, *supra*, 217 Cal.App.4th at p. 164)—there's no reason to believe the Legislature sought to (1) limit the parties' ability to reach a later, pre-trial settlement based on how *a court* might view a settlement that the parties chose for themselves relative to a rejected prior offer, or (2) to punish a party for not accepting a prior offer even though the parties have subsequently succeeded in negotiating a mutually-agreeable settlement.

CONCLUSION

All interpretative tools show the Legislature didn't intend section 998 penalties to apply to cases that settle before trial. The Court should reverse.

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CERTIFICATION

Pursuant to California Rules of Court, rule 8.504(d)(1), (d)(4), I certify that this **REPLY BRIEF ON THE MERITS** contains 8,397 words, not including the tables of contents and authorities, the caption page, signature blocks, or this Certification page.

Dated: June 28, 2024

/s/ Cynthia E. Tobisman
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PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the County of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business and email addresses are 6420 Wilshire Boulevard, Suite 1100, Los Angeles, California 90048, mallen@gmsr.com.

On January 8, 2024, I hereby certify that I electronically served the foregoing **REPLY BRIEF ON THE MERITS** through the Court's electronic filing system, TrueFiling. I certify that all participants in the case who are registered TrueFiling users and appear on its electronic service list will be served pursuant to California Rules of Court, rule 8.70. The filing of this document through e-Filing will also satisfy the requirements for service on the Court of Appeal rule 8.212(c)(2):

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Executed on January 8, 2024 at Los Angeles, California.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

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