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SUMMARIES

Contractual Disputes

Musicians’ reasonable interpretation of music publishing contract precluded entry of summary judgment against them (Zelon, J.)

**Brown v. Goldstein**

C.A. 2nd; March 27, 2019; B278949

The Second Appellate District reversed a judgment. The court held that plaintiffs’ interpretation of their contract with their music publisher Gerald Goldstein and related entities had failed to pay them a share of the royalties generated from public performances of the band’s songs. Goldstein moved for summary judgment, arguing that the parties’ music publishing agreement did not require it to pay the band any royalties derived from song performances. Plaintiffs argued the agreement was ambiguous, and filed extrinsic evidence in support of their interpretation.

The trial court concluded the agreement was not reasonably susceptible to plaintiffs’ proposed interpretation, and granted summary judgment in Goldstein’s favor.

The court of appeal reversed, holding that the parties agreement was reasonably susceptible to plaintiffs’ interpretation. In arguing that they were entitled to a share of the revenues generated from public performances, plaintiffs relied on paragraph 22 of the parties’ agreement, which states that plaintiffs are entitled to a share of revenues from all “composition gross receipts,” defined as “all monies actually earned and received from the sale, lease, license, disposition or other turning to account of rights in the compositions…” In arguing to the contrary, defendants relied on paragraph 7, which states that plaintiffs were not entitled to share in any sums defendants received from a “performing rights organization” for performance royalties. The court rejected defendants’ contention that the language in paragraph 7 rendered plaintiffs’ proposed interpretation of the Agreement unreasonable. Paragraph 7 and paragraph 22 address two distinct types of payments that defendants must pay to plaintiffs: royalty payments (paragraph 7) and a revenue-sharing payment (paragraph 22). The language in paragraph 7 that precludes plaintiffs from sharing in “performance income” can be reasonably interpreted as applying only to royalty payments. Paragraph 7 does not include any language stating that the exclusion of “performance fees” extends to paragraph 22’s revenue-sharing provision. Moreover, paragraph 22 specifically directs that the revenue-sharing payment described therein is to be paid “In addition to the royalties provided for in Paragraph 7.” The fact that plaintiffs are not entitled to receive royalty payments on performance income thus does not necessarily preclude them from receiving a portion of performance income based on the revenue-sharing payment described in paragraph 22. Further, plaintiffs’ interpretation of the agreement is thus not only plausible, but more reasonable than defendants’ interpretation.

**Copyrights**

Copyright owner’s claim of vicarious infringement not supported by showing of direct financial benefit to alleged infringer (Hawkins, J.)

**Erickson Productions, Inc. v. Kast**

9th Cir.; April 16, 2019; 15-16801

The court of appeals affirmed in part, reversed in part, and vacated in part a judgment. The court held that the record failed to support a finding that defendant obtained a direct financial benefit from his alleged vicarious infringement of plaintiff’s copyrights.

Kraig Kast hired a website developer to design a website for a business he owned. He asked that the website mimic, to the extent possible, the website of one of his competitors, Wells Fargo Private Bank. Three photos from Wells Fargo’s website were eventually incorporated into the website designed for Kast. Copyright owner Erickson Productions discovered the infringement and demanded that Kast remove the photos and pay damages. Kast promptly directed its website developer to remove the photos, but refused to pay damages.

Erickson filed suit, alleging direct, vicarious, and contributory copyright infringement. The case was tried to a jury, which found both vicarious and contributory infringement, and found that the infringement was willful. Erickson was awarded $450,000 in damages.

The court of appeal reversed in part, holding that the record failed to support the jury’s finding of vicarious liability. To prevail on a vicarious liability claim, a plaintiff must prove that the alleged infringer had both the right and ability to supervise the infringing conduct and a direct financial interest in the infringing activity. Here, although the evidence established Kast’s right and ability to supervise the website design, there was no showing of a causal relationship between the posting of Erickson’s photos and any direct financial benefit to Kast. Although the photographs argueable “drew” visitors to his website, this was insufficient, standing alone, to establish a direct financial benefit. That Kast avoided license fees was also insufficient to establish the requisite financial benefit—a direct infringer necessarily saves money by failing to obtain a license. Finally, Kast’s alleged ability to “rush” the completion of his website by using the infringing photos was also not shown to have conferred on him any direct financial benefit. The jury’s finding of vicarious liability was thus unsupported by the evidence. The
district court’s instruction on willfulness, which allowed the jury to find willfulness based on a finding that Kast “should have known” his conduct infringed Erickson’s copyrights, was also error. Willful conduct requires actual knowledge, willful blindness, or recklessness, and not merely negligence. The court vacated the finding of vicarious liability, reverse the finding of willfulness, and remanded.

**Employment Litigation**

Lack of specificity in compensation order issued under Longshore and Harbor Workers’ Compensation Act precluded district court enforcement (Hurwitz, J.)

**Grimm v. Vortex Marine Construction**

9th Cir.; April 16, 2019; 18-15104

The court of appeals affirmed a district court judgment of dismissal. The court held that the district court lacked jurisdiction to enforce a nonspecific compensation order that obliged the claimant’s former employer to pay for “necessary medical treatment” without stating the specific expenses for which the employer was liable.

Grimm worked as a pile driver for Vortex Marine Construction. After leaving work, Grimm filed a claim against Vortex under the Longshore and Harbor Workers’ Compensation Act, seeking workers’ compensation and medical benefits. A Department of Labor administrative law judge found that Grimm had sustained work-related injuries and ordered Vortex to pay or reimburse the Grimm for all medical expenses arising from Grimm’s work-related injuries, and to pay for all necessary treatment going forward. The Benefits Review Board affirmed the ALJ’s order. Grimm later filed suit to enforce that order, alleging that Vortex had refused to pay for required medical treatment. Grimm also asserted a claim under the Medicare Secondary Payer Act (MSP), seeking double damages for the amounts Medicare had paid for his treatment.

The district court granted Vortex’s motion to dismiss, finding it lacked jurisdiction to enforce the ALJ’s order because it was not final and the MSP claim was premature.

The court of appeals affirmed, holding that the district court did not err in dismissing the enforcement claim for lack of subject matter jurisdiction. In order to be “final” for purposes of enforcement under 33 U.S.C. §921(d), an order must “at a minimum specify the amount of compensation due or provide a means of calculating the correct amount without resort to extra-record facts which are potentially subject to genuine dispute between the parties.” The district court’s enforcement power does not extend to determining whether specific medical care is appropriate, or even whether the fees charged by a treating physician are reasonable. It thus stands to reason that a district court’s limited jurisdiction over a compensation order extends only to orders whose monetary sweep cannot be disputed. The district court also correctly rejected Grimm’s MSP claim as premature. The gravamen of that claim was that Medicare was forced to pay Grimm’s medical expenses after Vortex wrongfully refused to do so. Resolution of that claim would require the district court to determine in the first instance whether Vortex was obliged to pay for the treatment received by Grimm. Until such time as Vortex is found liable for specific medical expenses, the district court cannot make such a determination. Judge Watford concurred, opining that Grimm, in order to obtain an enforceable compensation order, must first receive the medical care he requires and then seek an additional order directing Vortex to pay his medical bills.

**Insurance Litigation**

Triable issues of fact as to cause of insured’s loss precluded summary judgment (Pregerson, J.)

**Ingenco Holdings, LLC v. Ace American Insurance Company**

9th Cir.; April 15, 2019; 16-35792

The court of appeals affirmed in part and reversed in part a district court judgment and orders and remanded. The court held that triable issues of fact regarding both the cause of an insured’s loss and the prejudice that allegedly resulted from the insured’s noncompliance with policy terms precluded summary judgment.

Ingenco Holdings, LLC operates a gas purification plant. On October 1, 2010, an internal component in the purification system broke, causing thousands of pounds of dust to be released into the system. Ingenco repaired the damage and restarted the facility on October 10, believing it had removed all the dust. Its cleanup efforts had been inadequate, however. Dust infiltrated other parts of the system, causing a second system-wide failure in March 2011. Operations did not resume until August 2012. Ingenco filed property damage and business interruption insurance claims with Ace American Insurance Company. Ace denied coverage, citing Ingenco’s failure to notify it of the October shutdown and also contending that the claimed loss was not covered because it did not result from an “external” cause. Ingenco filed suit.

The district court granted summary judgment in favor of Ace, finding that Ingenco’s losses did not result from an “external cause,” but rather from an “inherent problem in the system.” The court of appeals reversed the grant of summary judgment, holding that there were triable issues of fact as to (1) whether Ingenco’s loss was the result of an external cause and (2) whether Ace was prejudiced by Ingenco’s failure to notify it of the October 2010 shutdown and repairs. Ace ar-
gued that Ingenco’s failure to give notice of the initial failure and shutdown violated a condition precedent to coverage under Ingenco’s policy. Ace further argued that Ingenco’s remedial actions deprived it of the ability to reconstruct the system and fully investigate Ingenco’s claims about how the failure occurred. Conflicting testimony regarding these claims precluded summary judgment. Further, with regard to the cause of the failure, Ingenco argued that the internal component that failed was not inherently defective but failed instead due to forces outside the system. Conflicting evidence as to cause also precluded summary judgment. The court found no error, however, either in the district court’s determination that Washington law applied or in its imposition of sanctions for discovery violations by Ingenco.

Tax

Common law mailbox rule not applicable in determining timeliness of tax filing with IRS (Watford, J.)

**Baldwin v. United States**

9th Cir.; April 16, 2019; 17-55115

The court of appeals reversed a district court judgment. The court held that the common law mailbox rule no longer applies in determining whether a tax document was timely delivered to the Internal Revenue Service.

Howard and Karen Baldwin prepared an amended 2005 tax return, claiming entitlement to a refund of some $167,000. They deposited the return in the mail on June 21, 2011. The IRS never received it. Upon learning that their amended return was never received, the Baldwins sent a second return, but it was neither postmarked nor received by the October 15, 2011 deadline, and the IRS denied their refund claim as untimely. The Baldwins filed suit, arguing that under the common law mailbox rule, their original return should have been deemed to have been received shortly after it was mailed in June 2011.

The district court agreed and rendered judgment in the Baldwins’ favor, crediting their employees’ testimony that the return was delivered to the post office on June 21.

The court of appeals reversed, holding that the common law mailbox rule did not apply. Under Internal Rev. Code §7502, a tax document will be deemed to have been timely filed if (1) the document is actually delivered to the IRS, even if after the deadline, and (2) the document is postmarked on or before the deadline. If the document is never delivered at all, it cannot be deemed to have been timely filed absent proof of the postmark date. At issue here was whether §7502 supplemented or supplanted the common law mailbox rule. The statute itself is silent as to its effect on the common law mailbox rule. The treasury Department, however, was not silent. It adopted Treasury Regulation §301.7502-1(e)(2), in
FULL TEXT OPINION

Ninth Circuit Court of Appeals

Cite as 19 C.D.O.S. 3431

ERICKSON PRODUCTIONS, INC.; JIM ERICKSON, Plaintiffs-Appellees,
v. KRAIG RUDINGER KAST, Defendant-Appellant.

No. 15-16801
United States Court of Appeals for the Ninth Circuit
D.C. No. 5:13-cv-05472-HRL
Appeal from the United States District Court for the Northern District of California
Howard R. Lloyd, Magistrate Judge, Presiding
Argued and Submitted March 25, 2019
San Francisco, California
Filed April 16, 2019
Before: Sidney R. Thomas, Chief Judge, and Michael Daly Hawkins and M. Margaret McKeown, Circuit Judges.

COUNSEL
Christopher J. Cariello (argued), Margaret Wheeler-Frothingham, and Paul M. Fakler, Orrick Herrington & Sutcliffe LLP, New York, New York, for Defendant-Appellant.
Kevin P. McCulloch (argued) and Nathaniel A. Kleinman, New York, New York, for Plaintiffs-Appellees.

OPINION

HAWKINS, Senior Circuit Judge:

Defendant-Appellant Kraig Kast (“Kast”) appeals a jury verdict finding that he vicariously and contributorily infringed Plaintiffs-Appellees Erickson Productions, Inc. and Jim Erickson’s (collectively, “Erickson”) copyrighted images by displaying them on his website and did so willfully. We vacate the jury’s vicarious liability verdict but affirm its contributory liability verdict, so we uphold the judgment against Kast. We vacate the jury’s willfulness finding and remand for a determination of whether Kast’s infringement was willful on the existing record.

This opinion addresses Kast’s appeal of the judgment against him, Case No. 15-16801. The panel will address Kast’s related appeal of the district court’s amendment of the judgment against him, Case No. 17-17157, in a separate memorandum disposition.

FACTS AND PROCEEDINGS BELOW

I. FACTUAL BACKGROUND

Kast is a California resident who owns and operates various business entities and websites. One such business is Atherton Trust, a real estate wealth management company. In 2010, an opportunity arose for Atherton Trust to be appointed by the State of California to manage the estates of disabled persons. Kast thought a revamped website would enhance Atherton Trust’s prospects; so, he hired a website developer, Only Websites, to redevelop the site. Among other things, Kast “agree[d] to provide content and other material … throughout the development process.” Kast’s approval would be required on all work, “including the design, development and finalization of the website.”

To facilitate development, Kast completed a questionnaire outlining his goals for the revamped website. Kast identified Wells Fargo Private Bank (“Wells Fargo”) as one of Atherton Trust’s competitors and highlighted certain features of Wells Fargo’s website he found appealing. Kast also stated in emails that he wanted to mimic Wells Fargo’s website. Further, Kast noted that he “need[ed] to choose photos from options” provided by Only Websites.

Kast closely managed the development process. For instance, after reviewing an early draft of the developmental website, Kast stated that he “like[d] what [Only Websites did] with the home page layout.” On the other hand, Kast wanted the logo “to be warmer like” Wells Fargo’s and the photos “to be more casual like” Wells Fargo’s. Likewise, Kast later requested that Only Websites move the placement of Atherton Trust’s logo and company name.

Eventually, three photos from Wells Fargo’s website—which were taken by Jim Erickson and licensed to Wells Fargo through his company, Erickson Productions, Inc.—were incorporated into Atherton Trust’s developmental website.1 Neither Atherton Trust, Kast, nor Only Websites licensed the photos. Erickson discovered the infringement via Picscout, a “software that tracks imagery online” by running nightly internet-wide searches. In July 2011, Erickson demanded that Atherton Trust “cease and desist infringing its copyright” and pay damages. Kast promptly directed Only Websites to remove the photos, which was done the next morning, but refused to pay.

II. PROCEDURAL BACKGROUND

a. The trial and the jury’s verdict against Kast

Erickson filed suit in the Central District of California, alleging direct, vicarious, and contributory copyright infringement.2 Erickson contended that the infringement was willful, 1. Neither the record nor the trial transcript reveals whether Kast directed Only Websites to include the photos or whether Only Websites did so unilaterally.
2. Erickson initially sued Kast in the Southern District of New York, but his complaint was dismissed for lack of personal jurisdiction. See Erickson Prods., Inc. v. Atherton Trust, No. 12 Civ. 1693 (PGG), 2013 WL 1165346 (S.D.N.Y. March 20, 2013). Erickson obtained a default judgment against Only Websites. Order of Default, Erickson
and therefore subject to enhanced damages under 17 U.S.C. § 504(c)(2).

The case was transferred to the Northern District of California, where it proceeded to trial by consent before a magistrate judge.

Two divergent narratives emerged at trial. Erickson portrayed Kast as an opportunistic, cost-cutting businessman who rushed completion of Atherton Trust’s developmental website in an effort to generate additional income through state-appointed estate management. Erickson’s counsel elicited testimony from Kast at trial that he first became aware that the photos in question were on Atherton Trust’s website in January 2011, and the photos remained there until Kast received the July 2011 demand letter. Erickson claimed that including the unlicensed photos not only allowed Kast to continue pursuing the business opportunity he so desired, but also avoided the required developmental licensing fee.

Kast painted a different picture. He agreed “the Atherton Trust website included unauthorized copies of [Erickson’s] photos that were copied from” Wells Fargo’s website. But, according to Kast, Only Websites copied the photos without his consent. Kast also pointed to a provision in his contract with Only Websites, which stated that “Client [Kast] is responsible for obtaining copyright releases and licenses on all photographs it sends to Provider. Limit of 2 photographs provided by Provider for every page except the home page.” Kast testified he understood this provision to mean that “[a] nything that I sent to them had to be licensed,” but that “if they provided the photos, [they] had to provide licensed photos.” Similarly, Kast asserted that had he known he needed to license photos for the developmental site, he would have done just that; in fact, he later and on his own licensed two stock photos for the site’s “live” version. Separately, Kast argued he lacked control over Only Websites: Only Websites published the website without his consent and ignored multiple requests to replace the infringing photos. Finally, Kast contended that he did not reap a financial benefit from the infringing photos because “[h]e made no money off the website” and “avoid[ing] a license fee” is not a direct financial benefit.

At the charging conference, the parties wrangled over the wording of the willfulness jury instruction. Erickson sought an instruction that Kast acted willfully if he knew he infringed Erickson’s copyrights, acted with reckless disregard for Erickson’s copyrights, or “should have known” his actions infringed Erickson’s copyrights. Kast objected to the “should have known” prong, arguing that it set the standard “much lower than recklessness.” The district court agreed with Erickson and included the “should have known” prong.

The jury found by special verdict that Kast vicariously and contributorily (but not directly) infringed Erickson’s copyright on each of the photos and did so willfully. Pursuant to 17 U.S.C. § 504(c)(2), the jury awarded Erickson $150,000 in damages per photograph, for total damages of $450,000.

b. The instant appeal

Kast timely appealed the district court’s judgment against him. Kast initially briefed his case without the assistance of counsel. We appointed pro bono counsel to assist Kast with two of the issues he raised in his opening brief: (1) whether the avoidance of licensing fees constitutes a direct financial benefit for purposes of imposing vicarious copyright liability; and (2) whether a “should have known” willfulness instruction is proper under 17 U.S.C. § 504(c). The parties submitted supplemental briefing on these issues, the former an issue of first impression in this circuit. We now consider whether to affirm (1) the jury’s vicarious liability verdict, (2) the jury’s contributory liability verdict, and (3) the jury’s willfulness finding. We also address (4) some additional evidentiary and procedural matters.

STANDARDS OF REVIEW

“We review the district court’s denial of a motion for directed verdict de novo.” Allstate Ins. Co. v. Herron, 634 F.3d 1101, 1109 (9th Cir. 2011). Legal questions are reviewed de novo so long as they are “raise[d] … at some point before the judge submitted the case to the jury[,]” F.B.T. Prods., LLC v. Aftermath Records, 621 F.3d 958, 962–63 (9th Cir. 2010).

Jury instructions “must fairly and adequately cover the issues presented, must correctly state the law, and must not be misleading.” Gantt v. City of Los Angeles, 717 F.3d 702, 706 (9th Cir. 2013) (quotation marks and citation omitted). If a jury instruction is incorrect, reversal is appropriate “unless the error is more probably than not harmless.” Chuman v. Wright, 76 F.3d 292, 294 (9th Cir. 1996). If a party fails to object to a jury instruction in the district court, it can still be reviewed on appeal for plain error. See Hoard v. Hartman, 904 F.3d 780, 786 (9th Cir. 2018). “We may exercise our discretion to correct a district court on plain error review when the following factors are met: (1) the district court erred; (2) the error was obvious or plain; (3) the error affected substantial rights; and (4) the error seriously impaired the fairness, integrity, or public reputation of judicial proceedings.” Id. at 787 (quotation marks and citation omitted).

“We review the district court’s rulings concerning discovery and evidentiary issues for an abuse of discretion and reverse only if the district court’s ruling more likely than not affected the verdict.” Kulas v. Flores, 255 F.3d 780, 783 (9th Cir. 2001) (citations omitted).

DISCUSSION

I. THE VICARIOUS LIABILITY VERDICT

The jury found that Kast vicariously infringed Erickson’s copyright through his employment of Only Websites, the direct infringer. “To prevail on a vicarious liability claim, [plaintiff] must prove [defendant] has (1) the right and ability
to supervise the infringing conduct and (2) a direct financial interest in the infringing activity.” VHT, Inc. v. Zillow Group, Inc., 918 F.3d 723, 745 (9th Cir. 2019) (citing Perfect 10, Inc. v. Giganews, Inc., 847 F.3d 657, 673 (9th Cir. 2017) (internal quotation marks omitted).

Kast argues the judge erred in denying his motion for a directed verdict on vicarious liability because Erickson presented no evidence that could constitute a direct financial benefit as a matter of law. We agree and vacate the jury’s vicarious liability verdict.

“The essential aspect of the ‘direct financial benefit’ inquiry is whether there is a causal relationship between the infringing activity and any financial benefit a defendant reaps . . . .” Ellison v. Robertson, 357 F.3d 1072, 1079 (9th Cir. 2004). Erickson claims Kast received three “direct financial benefits” from Only Websites’ infringement: (1) the photographs drew customers to purchase his services; (2) he avoided paying licensing fees to Erickson; and (3) he was able to “rush” the launch of his website. Each one fails.

**a. Enhanced attractiveness of Kast’s website**

A website owner can receive a direct financial benefit from the presence of infringing material on his or her website, but only “where the availability of infringing material acts as a draw for customers.” Ellison, 357 F.3d at 1078 (internal quotation marks and citation omitted). If the infringing material is “just an added benefit,” rather than a draw, it does not confer a direct financial benefit on the website owner. See id. at 1078–79.

Erickson claims the photographs enhanced the general attractiveness of Kast’s website to customers, and thereby “drew” visitors to purchase his services. Erickson argues that, because the whole purpose of the website was to advertise Kast’s wealth management company, Kast had a direct financial interest in everything on the website that enhanced its appeal to potential customers. However, a financial benefit is not “direct” unless there is a “causal relationship between the infringing activity and [the] financial benefit.” Ellison, 357 F.3d at 1079. Erickson does not contend that anyone visited Kast’s website in order to view his photographs or purchased his services because they saw the photographs. The parties agree that no one visited the website or purchased anything after doing so. If Kast had a direct financial interest in every piece of content on this website that arguably made the website marginally more attractive or presentable, then the requirement of a causal link would be erased. Erickson does not argue the photographs were anything more, at best, than an “added benefit” to visitors of Kast’s website, so the infringement did not confer a direct financial benefit on Kast as a matter of law. See id.

**b. Avoidance of licensing fees**

Erickson claims “Kast enjoyed a direct [financial] benefit from the illegal copying of Erickson’s works by avoiding the license fees he would have otherwise been required to pay[.]” Whether a vicarious infringer’s avoidance of licensing fees constitutes a direct financial benefit as a matter of law is a question of first impression in this circuit. No other circuit appears to have addressed it, either. We hold that it does not.

As an initial matter, Erickson’s avoidance of fees claim cannot be premised on any unlicensed use by Kast of Erickson’s copyrighted photographs. That would result in direct liability, a theory the jury rejected. See A&M Records, Inc. v. Napster, Inc., 239 F.3d 1004, 1013 (9th Cir. 2001) (“[D]irect infringers violate at least one exclusive right granted to copyright holders under 17 U.S.C. § 106.”). Additionally, to the extent Erickson suggests Kast owed licensing fees as a result of his vicarious infringement, his argument is plainly circular.

Instead, Erickson’s argument must be that Kast received a direct financial benefit when Only Websites avoided Erickson’s licensing fee. Only Websites surely owed Erickson a licensing fee, and saved money by failing to pay it, but the direct infringer’s avoidance of fees alone cannot satisfy the requirement of a direct financial benefit to the vicarious infringer. Otherwise, the requirement of a direct financial benefit would be rendered meaningless, since—at least where, as here, licenses are for sale—a direct infringer necessarily saves money by failing to obtain a license. See Worldwide Church of God v. Phila. Church of God, Inc., 227 F.3d 1110, 1114 (9th Cir. 2000) (“The existence of a license creates an affirmative defense to a claim of copyright infringement.”).

Nor did Kast receive any other direct financial benefit as a result of Only Websites’ failure to pay. In some circumstances, a direct infringer’s avoidance of fees may prove financially advantageous to a vicarious infringer. For instance, Kast would have benefitted if Only Websites turned its lower

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3. Kast also argues that the jury’s vicarious liability verdict was not supported by sufficient evidence. Kast failed to renew his motion for a directed verdict in the trial court, so his sufficiency of the evidence argument is forfeited. See Ntico Holding Corp. v. Boujikian, 491 F.3d 1086, 1089 (9th Cir. 2007) (“[A] post-verdict motion under Rule 50(b) is an absolute prerequisite to any appeal based on insufficiency of the evidence.”) (citing Unitherm Food Sys., Inc. v. Swift-Eckrich, Inc., 546 U.S. 394 (2006)). Insofar as Kast’s arguments address whether certain alleged benefits were “direct financial benefits” as a matter of law, rather than whether the evidence established that Kast received those benefits, they are unaffected by this rule. See Cochran v. City of Los Angeles, 222 F.3d 1195, 1200 (9th Cir. 2000) (failure to renew post-verdict a motion for judgment as a matter of law made at the close of evidence does not prevent our review of an “issue [that] does not concern the sufficiency of the evidence presented to the jury.”).

costs from fee avoidance into lower prices for its website design services. See In re Aimster Copyright Litig., 334 F.3d 643, 654 (7th Cir. 2003). But this benefit would not be “direct,” since it would reach Kast only incidentally, via Only Websites’ intervening decision to cut prices. See id. (noting in dicta that a dance hall operator benefitted only indirectly from an orchestra’s avoidance of licensing fees). In any event, Erickson never claimed that Only Websites and Kast were able to offer services more cheaply or quickly because Only Websites infringed Erickson’s copyright.

Erickson’s alternative theory that Only Websites avoided the licensing fee in its capacity as Kast’s agent, such that Kast himself is liable for its failure to pay, is also unpersuasive. Kast employed Only Websites to develop the website, but the latter’s decision to infringe Erickson’s copyright would have exceeded the scope of any agency relationship that may have existed between them. See Restatement (Third) of Agency § 2.02 cmt. h (illegal or tortious acts exceed the scope of an agency relationship).

Thus, Only Websites’ avoidance of licensing fees did not confer a direct financial benefit on Kast as a matter of law.5

c. The “rush” completion of the website

Finally, Erickson contends Kast received a direct financial benefit because the photographs enabled Kast to “rush” the launch of his website. Indeed, Kast conceded that he “rushed” the site out before it was finished in order to seek appointment to manage certain estates. But Kast received no money, clients, business inquiries, or website visitors by rushing the website’s completion before removing Erickson’s photos. Erickson never explained how using the photos allowed Kast to launch the website more quickly, or how the rushed launch enabled him to realize any profits at all. Thus, the alleged rush conferred no financial benefit on Kast at all and fails as a matter of law. See Ellison, 357 F.3d at 1079.

II. THE CONTRIBUTORY LIABILITY VERDICT

The jury also found that Kast contributorily infringed Erickson’s copyright. A party engages in contributory copyright infringement when it “[1] has knowledge of another’s infringement and (2) either (a) materially contributes to or (b) induces that infringement.” VHT, 918 F.3d at 745 (citing Perfect 10, Inc. v. Visa Int’l Serv., Ass’n, 494 F.3d 788, 795 (9th Cir. 2007)). On appeal, Kast challenges the jury instructions on the contributory liability claim.6 We find his argument unpersuasive and affirm the contributory liability verdict.

6. Kast claims the trial judge erred by instructing the jury that “knowledge” for contributory infringement purposes includes having a “reason to know” of the infringement. According to Kast, only “actual knowledge” or “willful blindness” are sufficient.

Preliminarily, we note that Kast raised this issue for the first time in his supplemental opening brief, with the assistance of pro bono counsel. This argument exceeds the scope of the issues pro bono counsel was instructed to brief and argue. Kast himself did not object to this element of the jury instructions, so we ordinarily would not address it. See Galvan v. Alaska Dep’t of Corr., 397 F.3d 1198, 1204 (9th Cir. 2005) (“Courts generally do not decide issues not raised by the parties.”).

However, even if we were to reach this issue, we would still uphold the contributory liability verdict. Kast did not raise this objection at trial, so it is reviewed for plain error.7 “[I]n the civil context… plain errors should ‘encompass only those errors that reach the pinnacle of fault envisioned by [the plain error standard].’” C.B. v. City of Sonora, 769 F.3d 1005, 1018 (9th Cir. 2014) (quoting Hemmings v. Tidyman’s Inc., 285 F.3d 1174, 1193 (9th Cir. 2002) (internal alterations omitted)).

Here, even if the “should have known” instruction was erroneous, the error was not plain. Inconsistency in our case law on the “knowledge” element of contributory liability precludes a finding of plain error. For instance, in Luvdarts, LLC v. AT & T Mobility, LLC, 710 F.3d 1068, 1072–73 (9th Cir. 2013), we held that “actual knowledge of specific acts of infringement” and “[w]illful blindness of specific facts” are the only two mental states that satisfy the “knowledge” element of contributory infringement. Id. But in Louis Vuitton Malletier, S.A. v. Akancor Solutions, Inc., 658 F.3d 936, 943 (9th Cir. 2011), we cited with approval a “know or have reason to know” instruction for contributory liability. Id. (citing Napster, 239 F.3d at 1020). Neither case is close to Kast’s on the facts.8 While Luvdarts was decided after Louis Vuitton, it did not explicitly overrule it. And both cases were decided several years after Metro-Goldwyn-Mayer Studios, Inc. v. Grokster, Ltd., 545 U.S. 913 (2005), the case in which Kast claims the Supreme Court settled the matter in favor of an “actual knowledge” requirement. Without resolving the apparent tension between Luvdarts and Louis Vuitton, we hold

5. We find the parties’ attempts to fit Kast’s alleged avoidance of licensing fees into Ellison’s “draw” inquiry unmoving. The “draw” inquiry assumes that the financial benefit in question is an increase in potential customers on the vicarious infringer’s website or in his place of business. By contrast, the supposed benefit of avoiding a licensing fee does not depend on how many people visit the website or buy anything when they are there.

6. Kast also claims insufficient evidence supports the contributory liability verdict. As with all his other sufficiency of the evidence challenges, this argument is waived. See Nico, 491 F.3d at 1089.

7. Erickson’s claim that Kast waived even plain error review of this jury instruction is incorrect. Erickson is right that both parties stipulated to the relevant instruction. However, merely submitting an erroneous instruction does not waive a later challenge, so long as there is no evidence that the appellant considered and rejected a correct instruction “for some tactical or other reason.” See United States v. Perez, 116 F.3d 840, 845–46 (9th Cir. 1997); see also Crowley v. Epicent Corp., 883 F.3d 739, 748 (9th Cir. 2018). Here, there is no such evidence.

8. In Luvdarts, the alleged contributory infringer was a wireless carrier whose network was used to send infringing multimedia content, see 710 F.3d at 1070, while in Louis Vuitton, it was a company that hosted websites that sold infringing goods, see 658 F.3d at 940.
that Kast has not demonstrated that the jury instructions were plainly erroneous.

Nor are we persuaded by Kast’s other arguments against the contributory liability jury instructions. Kast challenges the instruction requiring the jury to find that “Only Websites did not have permission to copy or publish copies of [Erickson’s] Photos and thus infringed [Erickson’s] copyrights by doing so[,]” He insists this instruction “ask[ed] the jury to make a finding not in evidence.” Kast failed to object to this instruction below, and, in any case, he is wrong on the merits. The parties stipulated that Only Websites designed the infringing website, which “included unauthorized copies of [Erickson’s] Photos” copied from Wells Fargo’s website. And Erickson elicited unrefuted testimony that neither Only Websites nor Kast had permission to use the photos. Thus, these facts were in evidence.

III. THE WILLFULNESS FINDING

The jury also found Kast’s vicarious and contributory infringement were willful. Kast claims the district court erred when it instructed the jury that it could find that Kast’s infringement was willful if Kast “should have known that [his] acts infringed plaintiffs’ copyright.” We agree and remand the issue of willfulness to the district court on the existing record.

a. Whether the willfulness instruction was erroneous

The jury’s willfulness finding is relevant to its award of statutory damages. Absent a finding of willfulness, the jury may award statutory damages “in a sum of not less than $750 or more than $30,000” per work infringed. 17 U.S.C. § 504(c)(1). However, if the copyright owner proves that the infringement was “willful,” the court may increase the statutory damage award to $150,000 per work infringed. Id. § 504(c)(2).

At Kast’s trial, the judge instructed the jury: “Infringement is considered willful when . . . (1) the defendant knew that those acts infringed plaintiffs’ copyrights; or, (2) the defendant should have known that those acts infringed plaintiffs’ copyright; or, (3) the defendant engaged in conduct that was reckless or demonstrated a reckless disregard for plaintiffs’ copyrights.” The jury found that Kast’s contributory and vicarious infringement was willful and awarded Erickson $450,000 in statutory damages. Had the jury not made this finding, Erickson’s statutory damages could not have exceeded $90,000.

“A determination of willfulness requires an assessment of a defendant’s state of mind.” Friedman v. Live Nation Merch., Inc., 833 F.3d 1180, 1186 (9th Cir. 2016). “[T]o prove willfulness under the Copyright Act, the plaintiff must show (1) that the defendant was actually aware of the infringing activity, or (2) that the defendant’s actions were the result of reckless disregard for, or willful blindness to, the copyright holder’s rights.” Unicolors, Inc. v. Urban Outfitters, Inc., 853 F.3d 980, 991 (9th Cir. 2017) (quoting Wash. Shoe Co. v. A-Z Sporting Goods, Inc., 704 F.3d 668, 674 (9th Cir. 2012)) (alteration in original).

A “should have known” instruction does not fit within this framework because it is a negligence standard. To say that a defendant “should have known” of a risk, but did not know of it, is to say that he or she was “negligent” as to that risk. See Global-Tech Appliances, Inc. v. SEB S.A., 563 U.S. 754, 770 (2011); see also BMG Rights Mgmt. (US) LLC v. Cox Commc’ns, Inc., 881 F.3d 293, 310 (4th Cir. 2018) (“The formulation ‘should have known’ reflects negligence”); Swinton v. Potomac Corp., 270 F.3d 794, 803 (9th Cir. 2001) (noting that “should have known” is a negligence standard).

Negligence is a less culpable mental state than actual knowledge, willful blindness, or recklessness, the three mental states that properly support a finding of willfulness. See Global-Tech Appliances, 563 U.S. at 770; Unicolors, 853 F.3d at 992. “[A] willfully blind defendant is one who takes deliberate actions to avoid confirming a high probability of wrongdoing and who can almost be said to have actually known the critical facts. By contrast, a reckless defendant is one who merely knows of a substantial and unjustified risk of such wrongdoing, and a negligent defendant is one who should have known of a similar risk but, in fact, did not.” Global-Tech Appliances, 563 U.S. at 769–70 (citations omitted). Thus, Kast is correct that the judge permitted the jury to find willfulness on the basis of a lesser mental state than our cases demand.9

Erickson’s alternative interpretation of the jury instructions is unpersuasive. Erickson claims that an infringer who “should have known” of the infringing activity has “constructive knowledge” of the infringement, and that constructive knowledge is sufficient for willfulness.

Erickson is correct that a “should have known” instruction conveys the concept of “constructive knowledge.” See Knowledge. Black’s Law Dictionary (10th ed. 2014) (“Constructive knowledge” is “[k]nowledge that one using reasonable care or diligence should have, and therefore that is attributed by law to a given person.”). The problem for Erickson is that “constructive knowledge” is distinct from, and less culpable than, any of the mental states that support a finding of willfulness. Erickson cites extensively from non-binding, out-of-circuit, and district court authorities indicating that constructive knowledge can support a willfulness finding, but all are incompatible with our repeated requirement of actual knowledge, willful blindness, or recklessness.10 We

9. The jury instruction was phrased in the disjunctive, that is, the jury was asked whether Kast “knew” of, should have known of, or was reckless with regard to Only Websites’ infringement. Thus, implicit in a finding under the “should have known” prong would be a conclusion that Kast did not, in fact, know of the risk or fact of infringement. See Global-Tech Appliances, 563 U.S. at 770 (explaining that a negligent defendant, by definition, does not know of a risk).

10. Erickson relies heavily on our “see also” citation, in Washington Shoe, to a statement by a New York district court: “[t]o prove willfulness, plaintiffs must show that the infringer had actual or construc-
have never held merely negligent conduct to be willful, and we decline to do so now.

**b. Whether the error requires reversal**

The erroneous willfulness instruction was likely prejudicial to Kast, so remand is required. See *Chuman*, 76 F.3d at 294. While the evidence may have established that Kast was negligent, it is much less clear that it established recklessness, willful blindness, or actual knowledge. Kast presented evidence that he did not know Only Websites was or might be infringing. Kast’s contract with Only Websites suggests that Kast reasonably believed it was Only Websites’ responsibility to obtain licenses for Erickson’s photos. See *VHT*, 918 F.3d at 748 (“[C]ontinued use of a work even after one has been notified of his or her alleged infringement does not constitute willfulness so long as one believes reasonably, and in good faith, that he or she is not infringing.” (citing *Evergreen Safety Council v. RSA Network Inc.*, 697 F.3d 1221, 1228 (9th Cir. 2012)). Several of Kast’s other actions also suggest that he was not reckless with respect to Erickson’s rights: he obtained licenses for the photos that he supplied to Only Websites, and promptly removed the infringing photos when Erickson asked. If the jury had been properly instructed, it might well have refused to find Kast willful on this record.

We are unpersuaded by Erickson’s contention that the jury’s contributory infringement verdict indicates that the jury would have found willfulness even without the “should have known” instruction. Erickson claims that a contributory infringer has “knowledge” of the direct infringer’s conduct if he “know[s] or ha[s] reason to know” of the direct infringement. See *Louis Vuitton*, 658 F.3d at 943 (citing *Napster*, 239 F.3d at 1020). Erickson contends that, if Kast had “knowledge” for purposes of contributory infringement, then he had “knowledge” for purposes of the willfulness inquiry. However, a “knew or had reason to know” instruction could be satisfied by a negligence finding via its second prong, so the contributory infringement finding does not necessarily mean the jury would have found that Kast was actually aware of, or willfully blind or reckless with respect to, Only Websites’ infringement. In any case, *Louis Vuitton* is inapposite because it addressed a contributory infringer with actual, rather than constructive, knowledge. See *id.* at 944.

Accordingly, we remand the issue of willfulness to the district court. We disagree with Kast’s claim that “the record permits only one resolution of the factual issue” of willfulness, see *Pullman-Standard v. Swint*, 456 U.S. 273, 292 (1982), and decline his invitation to enter judgment in his favor.

**IV. KAST’S REMAINING EVIDENTIAL AND PROCEDURAL ARGUMENTS**

Kast makes several additional evidentiary and procedural arguments, primarily in his pro se briefs. We summarize these below. None are persuasive.

Kast claims he was an improper defendant because “Erickson should have sued Atherton, not Kast.” Even if Atherton Trust is also liable for the infringement, Kast would be jointly and severally liable, so he is a proper defendant. See *Range Road Music, Inc. v. E. Coast Foods, Inc.*, 668 F.3d 1148, 1151, 1155 (9th Cir. 2012) (imposing joint and several liability in copyright infringement case on corporate entity and its sole officer and director).

Kast also argues that the district court made numerous discovery and evidentiary errors, including that it should have excluded information about Kast’s finances, it permitted Erickson to withhold evidence relating to his finances, and it permitted Erickson to introduce improper character evidence. None of these alleged errors call for reversal. For instance, Erickson’s questions regarding Kast’s finances explored the ownership of various businesses and trusts, not his personal wealth. Because such questions arguably related to both vicarious liability and willfulness, see *Amazon*, 508 F.3d at 1173 (requiring control for vicarious liability); *Castle Rock Entm’t v. Carol Publ’y Grp., Inc.*, 955 F. Supp. 260, 267 (S.D.N.Y. 1997) (considering whether “the defendants are sophisticated” in determining willfulness), allowing it was not an abuse of discretion. Likewise, although Kast points to billing line items to suggest that Erickson withheld evidence, nothing suggests any documents resulted from those communications. Finally, even assuming Erickson’s prior-relationship questioning was improper, Kast fails to show that this error—or, in fact, any of the other alleged evidentiary errors—was prejudicial. *Kulas*, 255 F.3d at 783.

**CONCLUSION**

We vacate the jury’s finding of vicarious liability. We affirm the jury’s finding of contributory liability and therefore affirm the judgment. See *Hopkins v. Dow Corning Corp.*, 33 F.3d 1116, 1119, 1126, 1128 (9th Cir. 1994) (affirming judgment because jury’s verdict on at least one theory of liability was upheld); *DeWitt v. W. Pac. R.R. Co.*, 719 F.2d 1448, 1451 (9th Cir. 1983) (same). We reverse the jury’s finding of
willfulness and remand the issue of statutory damages to the trial court.

AFFIRMED IN PART, REVERSED IN PART, AND REMANDED. EACH PARTY TO BEAR ITS OWN COSTS.

INGENCO HOLDINGS, LLC, a Delaware limited liability company; BIO ENERGY (WASHINGTON), LLC, a Delaware limited liability company, Plaintiffs-

v.

ACE AMERICAN INSURANCE COMPANY, Defendant-Appellee.

No. 16-35792
United States Court of Appeals for the Ninth Circuit
D.C. No. 2:13-cv-00543-RAJ
Appeal from the United States District Court for the Western District of Washington
Richard A. Jones, District Judge, Presiding
Argued and Submitted June 12, 2018
Seattle, Washington
Filed April 15, 2019
Before: Dorothy W. Nelson and Paul J. Watford, Circuit Judges, and Dean D. Pregerson,* District Judge.
Opinion by Judge Pregerson

COUNSEL

OPINION
PREGERSON, District Judge:

Appellants operate a gas purification plant in King County, Washington. In 2010, metal brackets securing a crucial component broke, resulting in damage to other components and an eventual shutdown of the entire facility. Appellants’ insurance carrier Appellee ACE American Insurance Company (“Ace”), denied coverage, and Appellants sued. The district court, applying Washington law, granted summary judgment in Ace’s favor and sanctioned Appellants for discovery violations.

We have jurisdiction under 28 U.S.C. § 1291. We affirm the district court’s application of Washington law and its dis-
covery sanctions against Appellants, but reverse its grant of summary judgment in Ace’s favor and remand for trial.

FACTUAL AND PROCEDURAL BACKGROUND

A. Damage to the gas purification plant

Appellants, Ingenco Holdings, LLC and its wholly owned subsidiary, Bio Energy (Washington), LLC (collectively, “Ingenco”) operate a gas purification plant at the Cedar Hills landfill in King County, Washington. The plant converts raw landfill gas into usable natural gas. The final step of the purification process involves the removal of excess nitrogen from the landfill gas in a nitrogen rejection unit, or “NRU”. The gas is directed through adsorbent beads, to which nitrogen adheres, contained within pressure vessels. The beads, which are essentially a filter medium, cannot withstand the direct pressure of the landfill gas inflow, which, if unmediated, can grind the beads down into dust. To reduce the force of the gas flow on the beads, a “diffuser basket” is suspended from the top of, and surrounds, each bead-filled pressure vessel. The diffuser basket, in particular its perforated bottom plate, acts as a shield that prevents the full force of the incoming landfill gas from striking the beads directly. Instead, the incoming stream of gas strikes the diffuser basket’s bottom plate first, is diffused, and then passes through the beads in the pressure vessel with reduced force.

The diffuser basket bottom plate, or shield, is secured to the rest of the diffuser basket by metal straps, or brackets. On October 1, 2010, the metal straps securing the bottom plate of pressure vessel number thirty-two’s (“V32”) diffuser basket broke and the bottom plate fell away, leaving the beads in V32 unprotected. The parties dispute the reason for the breakage. Ace maintains that the bottom plate flexed, leading to excess stress upon, fractures in, and ultimately failure of, the metal straps. Ingenco contends that the bottom plate could not flex unless subjected to pressures far greater than those present within the nitrogen rejection unit. Instead, Ingenco posits, the flow of landfill gas caused the bottom plate’s metal straps to vibrate at a frequency that coincidentally matched the straps’ natural vibration frequency, or resonant frequency.¹ These unforeseeable vibrations, Ingenco argues, caused the metal straps to change shape and break.

Whatever the cause of the strap breakage, once the diffuser basket’s bottom plate fell away from the assembly, there was no longer any shield in place to protect the adsorbent beads from the full pressure of the incoming stream of landfill gas. The unmediated gas flow pulverized the 30,000 pounds of beads in V32 into dust, resulting in an automatic total shutdown of the facility on October 5, 2010.

Ingenco thought it had removed, or would be able to remove, the dust from all gas processing systems, and re-started the facility on October 13, 2010. Unbeknownst to Ingenco, however, dust from the pulverized beads in V32 had infiltrated other parts of the system, including other bead-containing pressure vessels. Dust from the V32 beads abraded against undamaged beads in the other pressure vessels, degrading those beads as well. Eventually, the accumulation of bead dust forced an automatic shutdown of the plant in March 2011. The plant remained idle for several months as Ingenco investigated alternative nitrogen filtration options and undertook repairs. Ingenco did not begin cleanup or repair operations until November 2011. The plant resumed operation in August 2012.

B. The insurance coverage dispute

Ingenco filed a property damage and business interruption insurance claim with Ace in May 2011. Ingenco’s all risks insurance policy, issued by Ace, covered against “all risks of direct physical loss or damage occurring . . . from any external cause.” The policy, however, excluded “[f]aulty or defective material, faulty workmanship, faulty methods of construction, [or] errors or omissions in plan or specification or designs . . . unless loss by a peril not otherwise excluded ensues . . . .” The policy also excluded “[g]radual deterioration, depletion, inherent vice, [or] latent defect . . . unless such loss is caused directly by physical damage not otherwise excluded . . . .” A separate Boiler and Machinery endorsement (“the Endorsement”) covered property damage and business losses “resulting from an Accident” to a pressure vessel. The Endorsement’s definition of “Accident,” however, excluded “deletion, deterioration[,] . . . and wear and tear.”

Ace denied coverage on several grounds. Ace claimed that, as a threshold matter, Ingenco failed to comply with a notification provision that required Ingenco to notify Ace of all losses. Specifically, Ace claimed that Ingenco failed to notify Ace of both the October diffuser shield failure and the resulting loss of beads in V32 until May 11, when the plant shut down for the second time. With respect to coverage, Ace took the position that Ingenco’s losses were not caused by any “external” force, but rather from defects in the diffuser basket and the overly delicate adsorbent beads. Thus, Ace reasoned, without an “external cause” there was no covered loss, and even if there were an external cause, coverage would nevertheless be lacking under the “defective material,” “wear and tear,” “deterioration,” and other, similar exclusions.

C. Procedural history

Ingenco brought suit in the Western District of Washington, alleging causes of action for breach of contract and declaratory relief, as well as statutory claims under Washington’s Consumer Protection Act and Insurer Unfair Conduct Act. The parties eventually filed cross motions for summary judgment. The district court granted Ingenco’s motion insofar as Ingenco argued that Washington law should apply to all claims, and that, under Washington law, Ingenco’s alleged failure to comply with the policy’s notice provision did not preclude coverage absent prejudice to Ace. The court ruled

¹ Every material has a natural, or resonant, frequency at which it will vibrate if disturbed. See, e.g. https://www.scientificamerican.com/article/fact-or-fiction-opera-singer-can-shatter-glass/
for Ace, however, that Ingenco’s losses did not result from an “external cause,” but rather from an “inherent problem in the system,” which system had been designed to withstand the “external” force at issue, i.e., the landfill gas.

The district court also ruled that the “ensuing loss” exception to the “defective material” exclusion did not apply to create coverage because there was no covered loss in the first place. In a similar vein, the district court concluded that Ingenco’s losses were caused by wear and tear resulting from normal operation, and therefore fell outside the Endorsement’s definition of covered “Accident.” Lastly, the district court ruled that, even in the event of coverage, business interruption losses would be limited to the “hypothetical” reasonable repair period, regardless of the actual time necessary to complete repairs.

In a separate order, the district court found that Ingenco had failed to timely disclose or produce evidence related to its state law bad faith claims. As a discovery sanction, the district court precluded Ingenco from introducing any such evidence and, accordingly, dismissed Ingenco’s statutory claims for lack of proof of damages.

Ingenco now appeals the district court’s orders.

**STANDARD OF REVIEW**

We review grants of summary judgment, and partial grants of summary judgment, de novo. *Flores v. City of San Gabriel*, 824 F.3d 890, 897 (9th Cir. 2016). Discovery rulings, including the imposition of discovery sanctions, are reviewed for abuse of discretion. *R & R Sails, Inc. v. Ins. Co. of Pennsylvania*, 673 F.3d 1240, 1245 (9th Cir. 2012). A district court abuses its discretion if it bases its decision “on an erroneous view of the law or on a clearly erroneous assessment of the evidence.” *Holgate v. Baldwin*, 425 F.3d 671, 675 (9th Cir. 2005); *Marchand v. Mercy Med. Ctr.*, 22 F.3d 933, 936 (9th Cir. 1994).

**ANALYSIS**

In resolving this appeal, we must first determine whether Washington or Virginia law applies to this insurance coverage dispute. Only then can we proceed to analyze the coverage issues, including whether Ingenco violated a condition precedent to coverage. We address these questions before turning to the remaining damages and discovery issues.

**A. Choice of Law**


The parties do dispute, however, whether the district court correctly concluded that Washington law applies. The Restatement provides that the local law of the state with the “most significant relationship to the transaction and parties” should control, and that the most significant relationship can be determined by reference to five factors: (1) the place of contracting; (2) the place of negotiation; (3) the place of performance; (4) the “location of the subject matter of the contract[;]” and (5) the residence, place of incorporation, and place of business of the parties. Restatement (Second) of Conflict of Laws §P 188(2) (1971). Notably, the Restatement further provides that “[t]hese contacts are to be evaluated according to their relative importance with respect to the particular issue.” *Id.*

1. The place of contracting

The Restatement defines “the place of contracting” as “the place where occurred the last act necessary … to give the contract binding effect … .” Rest. (Second) Conflict of Laws § 188, cmt. e; see, e.g., *First Commerce, LLC v. Sheldon*, No. 213 CV 01915 RFB GWF, 2016 WL 5791542, at *2 (D. Nev. Sept. 29, 2016). The parties dispute whether the insurance contract, or at least the addition of the Washington gas processing plant (the “Cedar Hills facility”) to an existing insur-
 ance policy, was entered into in Washington or Virginia. Both sides, however, conflate the “place of contracting” factor with the “place of negotiation” factor. Indeed, all of the parties’ citations to the record appear to pertain more to negotiation of the insurance contract than to its execution. Given that Ingenco’s risk manager, Raymond Yerly, and Ace’s managing agent, Tim Drag, met in Virginia and were both located in Virginia, it seems likely that the contract was executed in Virginia. In any event, however, “standing alone, the place of contracting is a relatively insignificant contact.” Rest. (Second) Conflict of Laws § 188, cmt. e.

2. The place of negotiation

The record is also somewhat unclear with respect to the place of negotiation. Yerly and Drag did have in-person meetings in Virginia. Ingenco’s broker, who communicated with Drag, also appears to have been located in Virginia. Drag acknowledged, however, that prior to the addition of the Washington Cedar Hills facility to the policy, Ace investigated the Washington plant, presumably in person, and that up to fifty percent of Ace’s due diligence may have occurred in Washington. Furthermore, some of the negotiations may have occurred by telephone from different states. Neither Yerly nor Drag could recall having a substantive, in-person meeting regarding the Washington facility.3 Thus, the place of negotiation factor is either neutral, or perhaps weighs slightly in favor of Ace and Virginia, See Rest. (Second) Conflict of Laws § 188, cmt. e (“This contact is of less importance when there is no single place of negotiation and agreement, as … when the parties do not meet but rather conduct their negotiations from separate states by mail or telephone.”).

3. The place of performance

With respect to the place of performance, neither party identifies where Ingenco performed, either by paying premiums or otherwise. Ace asserts that its own place of performance was Virginia because the policy states that any loss is to be “adjusted with” and payable to Ingenco, and Ingenco’s mailing address is in Virginia. The meaning of the policy’s “adjusted with” language is not entirely clear, but suggests that Ace will adjust any claim in collaboration with Ingenco. Ace’s managing agent, however, acknowledged that roughly fifty percent of the adjustment of Ingenco’s claim took place in Washington, and that the rest took place in New York, not Virginia.

With respect to payment of insurance benefits, some courts have held that the place of performance is the place where payment under a policy would be made. See, e.g., Pinnacle Realty Mgmt. Co. v. Nat’l Union Fire Ins. Co. of Pittsburgh, PA, No. CIVA 06 cv 02063 WDMCB, 2007 WL 1970275, at *3 (D.Colo. July 3, 2007). Other courts applying Section 188 have concluded, however, that “[w]hen the contract is one of payment, the place of performance seems, in truth, of no particular consequence.” State Farm Fire & Cas. Co. v. Miraglia, No. 4:07-CV-013-A, 2008 WL 11350060, at *3 (N.D. Tex. Jan. 30, 2008) (quoting Houston Cas. Co. v. Certain Underwriters at Lloyd’s London, 51 F. Supp. 2d 789, 797 (S.D. Tex. 1999)). Here, the place of performance factor is neutral, as payment took place in Virginia but adjustment took place in Washington. In any event, this factor merits little weight.

4. The location of the subject matter of the contract

Ace argues that the location of the subject matter of the contract “mostly covers Virginia property.” This argument depends entirely on the fact that the policy at issue here covers thirteen locations in Virginia and only one in Washington. That emphasis is misplaced, however. The policy in question covers eighteen separate facilities across five states. Although Virginia is home to the largest number of insured facilities, the coverage amount for the lone Washington facility dwarfs the combined coverage amounts of all seventeen other facilities, let alone the amounts of the thirteen Virginia facilities. The Cedar Hills facility is insured for $35 million in property losses and $12 million in business interruption losses, while the other seventeen facilities are insured for a total of approximately $31.3 million.4 Thus, it cannot be said that the policy covers “mostly” Virginia property.

Furthermore, to the extent Ace argues that Section 188 factors look to a jurisdiction’s relationship with a contract, rather than with a specific property, Ace cites no authority, and ignores the language of Section 188 itself, which states that contacts “are to be evaluated according to their relative importance with respect to the particular issue.” Rest. (Second) Conflict of Laws § 188(2) (emphasis added); see also Hartford Underwriters Ins. Co. v. Found. Health Servs., Inc., 524 F.3d 588, 595 (5th Cir. 2008); Hammersmith v. TIG Ins. Co., 480 F.3d 220, 234 (3d Cir. 2007). The commentary to the Restatement also counsels:

When the contract deals with a specific physical thing …the location of the thing or of the risk is significant (see §§ 189–193). The state where the thing or the risk is located will have a natural interest in transactions affecting it. Also the parties will regard the location of the thing or of the risk as important. Indeed, when the thing or the risk is the principal subject of the contract, it can often be assumed that the parties, to the extent that they thought about the matter at all, would expect that the local law of the state where the thing or risk was located would be applied to determine many of the issues arising under the contract.

3. To the extent Yerly referenced discussions regarding finding “a permanent place” for the gas facility, he appears to have meant a proper insurance vehicle rather than a physical, geographical location. 4. The Cedar Hills facility in Washington appears to be the only facility with business interruption coverage. Even excluding the business interruption coverage, the Cedar Hills facility is insured against a greater amount of property damage than all of the other seventeen facilities combined.
Rest. (Second) Conflict of Laws § 188, cmt. e.

Thus, in light of the particular issue here and the fact that the Washington facility is, by insured value, far and away the primary subject matter of the policy, the location of the subject matter factor weighs heavily in favor of Washington, and is significant.

5. The residence, place of incorporation, and place of business of the parties

With respect to residence, place of incorporation, and place of business, only the latter appears to be relevant. It is undisputed that Ingenco’s principal place of business is in Virginia. Ingenco represented to the district court both that its subsidiary, Bio Energy (Washington), LLC, has a principal place of business in Virginia and that its offices, records, and personnel are located in Washington. Ingenco, however, is the named insured. This factor weighs in favor of Virginia law, but is not particularly significant. See Rest. (Second) Conflict of Laws § 188, cmt. e (“The fact that one of the parties is domiciled or does business in a particular state assumes greater importance when combined with other contacts, such as that this state is the place of contracting or of performance or the place where the other party to the contract is domiciled or does business.”).

6. The balance of the Restatement factors weighs in favor of the application of Washington law

Looking, then, to the totality of the relevant Section 188 factors, only the fifth weighs significantly and unequivocally in favor of Ace and the application of Virginia law. The first, second, and third factors (place of contracting, place of negotiation, and place of performance, respectively) are either neutral or, to the extent they weigh in favor of Virginia law, are not particularly important. See Rest. (Second) Conflict of Laws § 188(2) (“These contacts are to be evaluated according to their relative importance with respect to the particular issue.”)). The fourth factor, the location of the subject matter of the contract, weighs heavily in favor of Washington law, and with respect to the particular issue here, is by far the most important factor. Accordingly, Washington law applies.

B. Whether Ingenco’s Failure to Notify Violated a Condition Precedent to Coverage

Having concluded that Washington law applies to this insurance coverage dispute, we now turn to the particular coverage provisions and exclusions at issue.

It is undisputed that although the diffuser basket straps failed on October 1, 2010 and the entire facility was shut down between October 5 and October 13, Ingenco did not notify Ace of the October diffuser shield malfunction and the resulting loss of beads in V32 until May 11, 2011, when the plant shut down for the second time. Ace argues that Ingenco’s failure to give notice of the initial failure and shutdown violated a condition precedent to coverage under the all risks policy.

As stated above, under Washington law, an insurer contending that an insured violated a condition precedent to coverage, such as by failing to comply with a notice provision, must demonstrate prejudice from the insurer’s failure. Mut. of Enumclaw, 164 Wash. 2d. at 424–25; MacLean Townhomes, 138 Wash. App. at 190. Ace contends that the uncontested evidence demonstrates that it was prejudiced by Ingenco’s failure to notify Ace of the October 1 diffuser basket failure or the October 5 shutdown. Specifically, Ace points to undisputed evidence that Ingenco discovered the shield failure on October 5, 2010, shut down the facility until October 13, discovered dust throughout the pressure vessels, and replaced all four vessels’ diffuser baskets, all without notifying Ace until after the second total shutdown on March 11.

Although Ingenco does not dispute this evidence, it does argue that the evidence is insufficient to demonstrate any prejudice to Ace. Indeed, Ace’s entire argument is premised on the assertion that Ingenco’s remedial actions “depriv[ed] Ace of the ability to reconstruct the system and fully investigate Ingenco’s claims about how the failure occurred and why it fell within the Policy’s coverage terms.” Ace’s argument, however, conflicts with the testimony of its own expert, Dr. Michael Casey. Dr. Casey testified at his deposition that he was able to determine the cause of the diffuser basket failure based on photographs of the failed basket and straps. To the extent Dr. Casey testified that Ace was able to evaluate the gas purification system from photographs alone, there is at least a triable issue of fact as to whether Ace was prejudiced by Ingenco’s remedial actions.

C. Whether Ingenco’s Losses Resulted From an “External Cause”

1. Background

Ingenco’s all risks policy, issued by Ace, insured against “all risks of direct physical loss or damage occurring … from any external cause.” Ingenco asserts, somewhat inconsistently, that “gas flow-induced vibrations,” the “pressure from the process gas,” and the “undiffused, high velocity landfill gas” were “external” causes of Ingenco’s adsorbent bead losses.

5. The district court looked beyond the Section 188 factors to Washington’s interest in protecting its insureds and maintaining the health and safety of its residents. Although not strictly relevant to a Section 188 analysis, these factors, insofar as they relate to the “particular issue” of damage to a potentially hazardous facility, may be more properly considered as relevant to the “relative importance” attributable to the Section 188 factors, particularly the fourth, “location of the subject matter” factor. Rest. (Second) Conflict of Laws § 188(2).

6. Ingenco also admits that it replaced V32’s adsorbent beads, but claims that it did not notify Ace because the bead manufacturer did not charge Ingenco for the replacement beads, and therefore Ingenco suffered no loss.

7. Ingenco did not appeal the district court’s conclusion that Ingenco failed to comply with the policy’s notice provision.
Ace argues that, as the district court concluded, the unmediated stream of landfill gas that destroyed V32’s adsorbent beads does not qualify as an “external” force, and that Ingenco’s losses are therefore not covered by the all risks policy.

There is no dispute about the generally applicable principles of insurance policy interpretation. Policies should be construed as a whole and given the type of sensible construction that an average insurance purchaser would give. Kitsap Cry. v. Allstate Ins. Co., 136 Wash. 2d 567, 575 (1998). Undefined terms must be given their “plain, ordinary, and popular meaning,” and any ambiguities should be construed against the insurer. Id. at 576.

The policy does not define the term “external cause.” Ingenco argues, briefly, that under the plain and ordinary meaning of “external,” landfill gas that originated outside the Ingenco facility was, by definition, not internal to the covered facility and, thus, qualifies as an “external” force. Although that argument has some appeal, Ingenco also contends, without explaining why any meaning other than the plain meaning should apply, that, in the absence of a definition of “external cause” in the policy, courts may look to judicial interpretations of that phrase, including the district court’s decision in Standard Structural Steel Co. v. Bethlehem Steel Corp., 597 F. Supp. 164, 193 (D. Conn. 1984). Both parties cite the Standard Structural Steel court’s explanation that, in the context of an all risks policy such as that at issue here, “a cause is external if damage which arises from it does not result wholly from an inherent defect in the subject matter or from the inherent deficient qualities, nature and properties of the subject matter.” Standard Structural Steel, 597 F. Supp. at 193 (internal quotation marks omitted). Other courts, including the district court here, have applied essentially this same definition of “external cause.” See, e.g., Delta Nat. Gas Co. v. Nat’l Union Fire Ins. Co. of Pittsburgh, Pennsylvania, No. CIV.A. 11-57-KSF, 2011 WL 2007706, at *2 (E.D. Ky. May 23, 2011).

8 In some cases, conflicting dictionary and industry (or judicially-crafted) meanings may create ambiguities that can only be resolved, if at all, through extrinsic evidence. See Queen City Farms, Inc. v. Cent. Nat. Ins. Co. of Omaha, 126 Wash. 2d 50, 83 (1994). Here, although Ingenco argues both that the plain meaning of “external cause” should apply and that the Standard Structural Steel-type definition applies, Ingenco does not contend that there is any ambiguity in the term “external cause.” See also Enron Oil Trading & Transp. Co. v. Walbrook Ins. Co., 132 F.3d 526, 530 (9th Cir. 1997) (looking to other provisions of insurance contract to determine that parties intended industry usage, rather than the plain meaning, of a term).

9 The Standard Structural Steel court also stated that all risks insurance policies implicitly require an external cause, even if the language of the policy is not so limited. Standard Structural Steel, 597 F. Supp. at 192. Thus, as the Standard Structural Steel court explained, “[t]he label ‘all risk’ is essentially a misnomer. All risk policies are not ‘all loss’ policies; all risk policies … contain express written exclusions and implied exceptions which have been developed by the courts over the years.” Standard Structural Steel, 597 F. Supp. at 192 (internal quotation and citation omitted).

2. Fortuity

The parties hew closely to the Standard Structural Steel definition of external cause and argue at length about whether the V32 diffuser basket and the adsorbent media were “inherently defective.” The parties’ arguments largely ignore, however, the concept of “fortuity,” which operates “as a sort of partnership” with the external cause requirement. Standard Structural Steel, 597 F. Supp. at 191–92; see also Koppers Co. v. Aetna Cas. & Sur. Co., 98 F.3d 1440, 1446 (3d Cir. 1996) (citing “the generally accepted principle that every ‘all risk’ contract of insurance contains an unnamed exclusion—the loss must be fortuitous in nature.” (internal quotation omitted)); Underwriters Subscribing to Lloyd’s Ins. Cert. No. 80520 v. Magi, Inc., 790 F. Supp. 1043, 1046 (E.D. Wash. 1991) (“Regardless of its express terms, every all-risk policy contains an unnamed exclusion—the loss must be fortuitous in nature.” (internal quotation and citation omitted)). Indeed, some courts have used the word “fortuitous” as an alternative to “external cause.” See, e.g., Dow Chem. Co. v. Royal Indem. Co., 635 F.2d 379, 386, (5th Cir. 1981) (stating, in reference to an all risks policy using the term “external cause,” that “recovery under an all-risk policy will be allowed for all fortuitous losses not resulting from misconduct or fraud, unless the policy contains a specific provision expressly excluding the loss from coverage.”).

The Washington Supreme Court has not addressed the concept of fortuity as it relates to all risks insurance policies. It is our task, therefore, to predict how the Washington Supreme Court would decide the issue. Dimidowich v. Bell & Howell, 803 F.2d 1473, 1482 (9th Cir. 1986). In so doing, we may look to other courts’ decisions for guidance, as well as to treatises, restatements, and other data. Id.; Astaire v. Best Film & Video Corp., 116 F.3d 1297, 1300 (9th Cir. 1997), amended, 136 F.3d 1208 (9th Cir. 1998).

Courts, often drawing upon the Restatement of Contracts, have typically defined a fortuitous event as one that is dependent upon chance, taking into account the knowledge of the parties. See, e.g., Compagnie des Bauxites de Guinee v. Ins.
Co. of N. Am., 724 F.2d 369, 372 (3d Cir. 1983); Magi, Inc., 790 F. Supp. at 1047–48 (collecting cases). Courts have further concluded that a fortuity inquiry should look to, among other things, whether a particular loss was certain to occur; the parties’ perception of risk at the time the policy issued, and whether the loss could reasonably have been foreseen. 13 Magi, Inc., 790 F. Supp. at 1048; Churchill v. Factory Mut. Ins. Co., 234 F. Supp. 2d 1182, 1188 (W.D. Wash. 2002); Frank Coluccio Const. Co. v. King Cty., 136 Wash. App. 751, 768 (2007). We conclude that the Washington Supreme Court would adopt a definition of fortuity consistent with this trend. 14

With this concept of fortuity in mind, we turn to the facts of this case. Here, the fortuity analysis is complicated somewhat by Ingenco’s inconsistent references to both “flow induced vibrations” and “the process gas” as the cause of its losses, as discussed above. Were the inquiry focused on the fortuity of “the process gas,” Ingenco could not possibly succeed, as it is undisputed that all parties fully expected the stream of landfill gas to enter the Cedar Hills facility and, as Ingenco concedes, the incoming stream of gas never exceeded expected tolerances. The focus of our fortuity analysis, however, is not on the fortuity of the process gas or some other cause, but rather on whether Ingenco’s loss was fortuitous. There is no evidence in the record that the failure of the diffuser basket cover plate straps, or the subsequent obliteration of the adsorbent media, was inevitable. Nor is there any evidence in the record that either party had reason to believe, at the time the policy issued, that the diffuser basket cover would fail under normal gas pressures, or that the adsorbent media would ever be exposed to an unmediated stream of high pressure gas. Lastly, Ingenco’s expert opined that the resonant vibrations in the metal straps were not, and could not have been, reasonably foreseen. See Magi, Inc., 790 F. Supp. at 1047–48; see also City of Burlington v. Indem. Ins. Co. of N. Am., 332 F.3d 38, 49 (2d Cir. 2003) (recounting Third Circuit’s conclusion in Compagnie Des Bauxites that “while in hindsight [...] structural defects might appear inevitable, [the court] had to credit the insured’s statements that it had no knowledge of the design defects and that the loss was therefore fortuitous,” and explaining that “an intrinsically caused loss may be just as unexpected as an extrinsically caused one.”). Thus, it appears that Ingenco’s loss was indeed fortuitous, or that there is, at the very least, a triable issue of fact regarding the issue.

### 3. External Cause

A determination that a particular loss is fortuitous could obviate the need to examine whether that loss was caused by an external force. Although the policy language here un-

doubtedly applies only to losses resulting from an “external cause,” some courts, interpreting nearly identical policy language, have held that an insured need only demonstrate that a fortuitous loss has occurred, notwithstanding “external cause” policy language. See, e.g., Atl. Lines Ltd. v. Am. Motorists Ins. Co., 547 F.2d 11, 12 (2d Cir. 1976). The Fifth Circuit addressed one such situation, explaining:

As has been recognized in other circuits, it would appear that all risks insurance arose for the very purpose of protecting the insured in those cases where difficulties of logical explanation or some mystery surround the (loss of or damage to) property. It would seem to be inconsistent with the broad protective purposes of “all risks” insurance to impose on the insured . . . the burden of proving the precise cause of the loss or damage. It is not surprising, therefore, that courts which have considered claims under insurance policies with essentially the same insuring language as the policy before us have consistently refused to require the insured to demonstrate that the loss or damage was occasioned by an external cause. We similarly refuse to impose such a burden in this case.


Although we find this reasoning persuasive, the Washington Supreme Court has not spoken on the issue. We need not predict, however, whether the Washington Supreme Court would read “external cause” policy language to require an insured to make a separate showing of external causation. Even assuming that the Washington Supreme Court would, unlike the Morrison Grain court, require an insured to show not only a fortuitous loss, but also an “external cause” in the all risks context, and would adopt the Standard Structural Steel definition of “external cause” as dependent on whether resulting damage arises “wholly from an inherent defect in the subject matter,” there nevertheless remains a triable issue of fact here. 15 Standard Structural Steel, 597 F. Supp. at 191.

As an initial matter, the district court appears to have conflated, or at the very least applied, two different definitions of “external cause.” To the extent that the district court concluded that “the incoming landfill gas was necessary and internal to the gas purification system,” it appears to have applied a plain and ordinary meaning of “external.” Whether it did so correctly is debatable. On the one hand, landfill gas was certainly essential to the operation of the Cedar Hills facility. At the same time, however, landfill gas was not an essential

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15. Although we refrain from concluding that the Washington Supreme Court would follow a Morrison Grain-like approach, neither do we suggest that the court would adopt the Standard Structural Steel court’s view of external causation. To the contrary, although the Washington Supreme Court has not addressed the precise issue, it has, in the all risks context, suggested that an external cause can exist even in circumstances involving latent defects. See Dickson v. U.S. Fid. & Guar. Co., 77 Wash. 2d 785, 793–94 (1970).
component of the facility or of the machinery itself, which existed before the first inflow of gas was ever piped in.\textsuperscript{16} Furthermore, although the landfill gas indisputably “arose” from outside the insured facility, whether it “acted” internally or externally depends on whether the borders of the insured subject matter begin at the property line or at the edge of the pressure vessel.\textsuperscript{17} These conflicts are difficult to resolve on the record before us, and perhaps, more than anything, illustrate the advantages of avoiding the “external cause” question altogether. See \textit{Morrison Grain}, 632 F.2d at 430.

The district court also, however, applied the \textit{Standard Structural Steel} definition of “external cause,” concluding that because there was an inherent problem in the gas purification system, “the landfill gas was not an external cause.” See \textit{Standard Structural Steel}, 597 F. Supp. at 193. The district court based that conclusion on its determination that because the purification system, and in particular the diffuser basket, was (1) designed to withstand landfill gas and (2) failed to do so, it must have suffered from an inherent defect. This logic, which Ace essentially reiterates on appeal, is difficult to square, particularly in the all risks context. Although, in general, system failures of any kind can conceivably result from an inherent defect, so too might failures occur for some other, justifiably unexpected reason. See, e.g., \textit{City of Burlington}, 332 F.3d at 49 (“[I]n hindsight[, ] structural defects might appear inevitable, … [b]ut an intrinsically caused loss may be just as unexpected as an extrinsically caused one.”); \textit{Morrison Grain}, 632 F.2d at 430 (“[A]ll risks insurance arose for the very purpose of protecting the insured in those cases where difficulties of logical explanation or some mystery surround the (loss of or damage to) property.”).

Even putting that logic aside, the district court’s conclusion that an inherent defect, and therefore an internal cause, was responsible for Ingenco’s losses fails to account for material evidence and, indeed, is inconsistent with the district court’s own determinations. The district court stated that the V32 diffuser basket was “not necessarily defective,” and acknowledged that Ingenco presented “some evidence that the [diffuser] basket may not have been defectively designed.” This observation is impossible to reconcile with the district court’s conclusion on summary judgment that an inherent defect nevertheless existed. Ingenco’s expert opined not only that resonant vibrations caused the V32 shield failure, but also that such failure was rare, that the vibrations were unforeseeable and, perhaps for that reason, that the relevant design codes do not require testing for resonant vibrations.

\textsuperscript{16} Indeed, King County, which controls the Cedar Hills landfill, has the ability to completely shut down the inflow of gas.

\textsuperscript{17} Ingenco’s argument that the object of the insurance claim, which in this case is limited to the diffuser beads, defines the physical borders relevant to an externality inquiry is not persuasive. Although Ingenco argues that Ace’s characterization of the subject matter of the policy is so comprehensive as to render any damage “internal,” Ingenco’s characterization is no less extreme, being so fine-grained as to render virtually any damage to any particular component, such as adsorbent beads, “external.”

Although Ace’s experts certainly disagree, that genuine dispute of fact is material to the questions whether (1) the gas purification system, or V32’s diffuser basket and its adsorbent beads, did, in fact, suffer from an inherent defect and (2) accordingly, whether the cause of Ingenco’s loss was internal or external.

We therefore conclude that the district court’s grant of summary judgment to Ace on the question of whether Ingenco’s loss was the result of an “external cause” must be reversed. The district court, and to some extent, the parties, failed to consider the role of fortuity in all risks insurance disputes. There is, at least, a dispute of fact as to whether Ingenco’s loss here was fortuitous. We take no position at this juncture on the question whether the Washington Supreme Court would require a separate showing of external causation. Even assuming, however, that Ingenco must make such a showing, and even assuming that “external cause” is coterminous with “inherent defect,” there is a triable issue of fact as to whether Ingenco’s purification system, and/or its components, suffered from such a flaw.

D. The Ensuing Loss Exception

Ingenco’s all risks policy excluded losses resulting from “[f]aulty or defective material, faulty workmanship, faulty methods of construction, [or] errors or omissions in plan or specification or designs . . . unless loss by a peril not otherwise excluded ensues . . . .” \textsuperscript{16} Ingenco argues that, even if V32’s diffuser basket was defectively designed, and even if its failure therefore constitutes an uncovered “internal” cause of loss, the “ensuing loss” exception quoted above preserves coverage for the post-failure damage to the adsorbent beads throughout the purification system. Ace’s opposition is based largely upon the contention, discussed at length above, that the damage at issue here did not result from an “external cause.”

As Ingenco points out, the Washington Supreme Court discussed ensuing loss exclusions in \textit{Vision One, LLC v. Philadelphia Indem. Ins. Co.}, 174 Wash. 2d 501 (2012). As the \textit{Vision One} court explained, ensuing loss clauses ensure that, where an uncovered event takes place, any ensuing loss which is otherwise covered by the policy remains covered, even though the uncovered event itself is never covered. \textit{Vision One}, 174 Wash.2d at 515. For example, if a homeowner’s policy excluded losses from faulty workmanship, an electrician’s wiring mistakes would not be covered, even if the policy included an ensuing loss exception. \textit{Id.} If, however, those uncovered wiring mistakes subsequently caused a fire that then caused additional damage, the fire damage would be covered under the ensuing loss clause. \textit{Id.} Conversely, for example, if a policy contained an ensuing loss provision but specifically excluded both faulty construction and mold losses, the ensuing loss provision would not preserve coverage where defective construction led to mold damage, because the ensuing mold damage was not “otherwise covered.” \textit{Id.} “[T]he dispositive question in analyzing ensuing loss clauses
is whether the loss that ensues from the excluded event is covered or excluded. If the ensuing loss is also an excluded peril or an excluded loss under the policy, there is no coverage.” Id. at 516.

The bulk of the dispute here appears to center on whether Ingenco’s bead-related loss ensued from some other, prior, uncovered loss, or itself constituted the loss. Ingenco concedes that the loss of the V32 diffuser shield was not covered.18 Ingenco argues, however, that because the destruction of the adsorbent beads occurred subsequent to the shield failure, the ensuing loss provision should operate to cover the bead-related loss, regardless of the fact that the shield failure itself is excluded. In response, Ace argues that “nobody is concerned with damage to the diffuser basket itself,” and thus the bead-related damage is not an ensuing loss, but rather the excluded loss itself.

Ace’s argument appears to be inconsistent with its prior assertion that the high-pressure stream of landfill gas was the internal cause of Ingenco’s loss. Vision One counsels that the key question is whether “the loss that ensues from the excluded event is covered or excluded.” Vision One, 174 Wash.2d at 516 (emphasis added). Ace’s understanding of the “excluded event” is difficult to pin down. In the external cause context, Ace argues that the stream of landfill gas was an internal, causative event, and was thus excluded. In the ensuing loss context, in contrast, Ace appears to suggest a different precipitating “excluded event,” suggesting that the breakdown of the adsorbent beads is the primary event. At the same time, however, Ace also states that the loss of the beads was “caused by the diffuser basket’s defective design,” suggesting yet a third potential preliminary, excluded cause. Ace cannot have it both (or all three) ways.

Proceeding, therefore, with the understanding that the loss of the adsorbent beads did ensue from some prior, but excluded loss or event, whether it be the stream of gas or the failure of the diffuser shield, the question remains whether the loss of the beads was itself excluded. Vision One, 174 Wash.2d at 516. In other words, to compare these facts to the examples cited in Vision One, is the loss of the beads more akin to the fire damage in the mis-wiring example or to the mold in the defective construction case? We conclude that the answer is the former. Although in the latter example, the mold did ensue from faulty construction, the ensuing loss provision nevertheless did not preserve coverage because mold itself was an excluded peril. Id. Here, there was no specific exclusion regarding the loss of the beads, just as in the mis-wiring example, there was no specific exclusion for fire.19 Thus, even if it were conclusively established that the diffuser shield suffered from some inherent defect, the subsequent destruction of the adsorbent beads would be covered under the policy’s ensuing loss exception.

E. The Endorsement’s “Accident” coverage

Ingenco also argues that the separate Boiler and Machinery endorsement to the policy independently confers coverage for Ingenco’s losses. The Endorsement covered “Accident[s],” defined as a “sudden and accidental breakdown of an Object,” exclusive of “depletion, deterioration, … [and] wear and tear ….” As discussed above, Ingenco’s experts opined that the “truly sudden” breakdown of V32’s diffuser shield, which resulted in the destruction of the adsorbent beads in V32 and throughout the system, was the “unexpected” result of unanticipated resonant vibrations that were “not foreseeable.” Thus there is a genuine dispute of material fact as to whether the Endorsement applies.

F. Actual Time of Repair

Assuming, for the sake of argument, that there is coverage, the policy covers business interruption losses for “only such length of time … as would be required with the exercise of due diligence and dispatch to rebuild or replace” damaged property. Ingenco did not resume operations at Cedar Hills for approximately sixteen months after the second, March 2011 shutdown. Nor did Ingenco perform any remedial work at the facility for approximately nine months, during which time Ingenco evaluated alternative options for nitrogen removal. Nevertheless, Ingenco seeks to recover for the entire sixteen-month shutdown period. Ace argues that Ingenco’s business interruption recovery should be limited to the “theoretical period of restoration.” The district court largely agreed with Ace, concluding that the applicable period “is limited to the hypothetical period of restoration.”

Some courts have held that the applicable period for an insured to reenter business is the “theoretical replacement time.” Vermont Mut. Ins. Co. v. Petit, 613 F. Supp. 2d 154, 161 (D. Mass. 2009); W. & Clay, LLC v. Landmark Am. Ins. Co., No. C09-1423 MJP, 2011 WL 321740, at *5 (W.D. Wash. Jan. 28, 2011); SR Int’l Bus. Ins. Co. v. World Trade Ctr. Properties, LLC, No. 01 CIV.9291(MBM), 2005 WL 827074, at *9 (S.D.N.Y. Feb. 15, 2005). Nevertheless, Ingenco argues, based largely upon our memorandum disposition in Alevy v. All. Gen. Ins. Co., No. 95-56034, 1996 WL 623065 (9th Cir. Oct. 24, 1996), that the “actual replacement time” is relevant to the measure of Ingenco’s losses. The Alevy court observed that although theoretical replacement time would be an appropriate measure of actual insured losses where payment was to be made before rebuilding was complete, actual replacement time is a more logical “starting point in the analysis” where rebuilding has already occurred. Alevy, 1996 WL 623065, at *2–3; see also SR Int’l, 2005 WL 827074, at *7. Other courts have agreed that it makes “per-

18. It is not entirely clear whether Ingenco’s concession is based upon the fact that the basket failed for some excluded reason, the fact that the basket was not an integral part of the nitrogen rejection vessel, or some other reason.

19. To the extent Ace argues that there was such an exclusion because the beads themselves suffered from an inherent defect, there is a triable issue of fact regarding the integrity of the beads.

20. Ingenco’s citation to the unpublished disposition in Alevy runs counter to Ninth Circuit Rule 36-3. See CTA9 Rule 36-3(a), (c).
fect sense” to look first to actual time of repair in cases where businesses have completed repairs or resumed operations by
the time a court is presented with the task of interpreting coverage provisions. See, e.g. SR Int’l, 2005 WL 827074, at *7.
Here, as in Alevy, repairs had already been made by the
time Ace denied Ingenco’s claim. We conclude that under
such circumstances, the actual time of repair has some bear-
ning on what period “would be required with the exercise of
due diligence and dispatch to rebuild or replace” damaged
property. We further observe, however, that Ingenco does not
argue, nor does any authority appear to state, that the applicable
repair period should be measured by “actual replacement
time” even where the actual time to repair is unreasonable.21
Thus, although Ingenco’s actual time to repair might be rel-
evant to the question whether a sixteen-month shutdown was
consistent with “the exercise of due diligence and dispatch,”
it is by no means dispositive.

G. Sanctions

The district court determined that Ingenco willfully with-
held evidence of damages on its state law statutory claims.
The district court then, as a sanction, precluded Ingenco from
introducing such evidence.22 See Fed. R. Civ. P. 37(c). In-
genco argues that the district court abused its discretion in
finding willful misconduct because (1) Ingenco responded to
Ace’s request for damages information within one day of
Ace’s request, and (2) the district court refused to consider sanctions other than dismissal.

We afford district courts “particularly wide latitude” to
impose discovery sanctions, and will not reverse absent a
“definite and firm conviction that the district court commit-
ted a clear error of judgment.” R&R Sails, 673 F.3d at 1245;
Marchand, 22 F.3d at 936. The district court observed that
Ace requested damages information in written interroga-
tories several months before Ingenco ultimately, after an ad-
ditional request from Ace, provided the information at a
Rule 30(b)(6) deposition. Furthermore, Ace points out, as
did the district court, that Federal Rule of Civil Procedure
26(a)(1)(A)(iii) requires the disclosure of “a computation of
each category of damages claimed by the disclosing party—
who must also make available . . . the documents or other
evidentiary material . . . on which each computation is based,
including materials bearing on the nature and extent of inju-
ries suffered,” regardless whether the opposing party requests such information. Fed. R. Civ. P. 26(a)(1)(A)(iii). The dis-
ctrict court concluded that Ingenco’s initial disclosures, which
were never supplemented, never disclosed any damages in-
formation related to statutory claims. Here, on appeal, In-
genco has not presented any argument explaining this failure
to meet its affirmative obligations under Rule 26.

When a party fails to disclose information required by
Rule 26, Rule 37(c)(1) provides that the improperly withheld
information should be excluded, unless the failure to disclose
is “substantially justified or harmless.” Fed. R. Civ. P. 37(c)
(1). Here, the district court found that Ingenco’s eleventh hour disclosure was not substantially justified, and was not harmless
because it disrupted both Ace’s and the court’s schedules.
Although the court’s prejudice explanation was not particularly
detailed, its conclusion was not clearly erroneous.

The district court also recognized that, because exclusion
of Ingenco’s statutory damages evidence as a Rule 37(c)
sanction would be dispositive of Ingenco’s statutory claims,
which require a showing of damages, the court was required
to consider (1) whether Ingenco’s noncompliance involved
willfulness, fault, or bad faith, and (2) whether lesser sanc-
tions were available. See R&R Sails, 673 F.3d at 1247. The
district court made the required findings of willfulness, fault,
and bad faith, supported by evidence that Ingenco (1) ig-
nored Ace’s written interrogatories, (2) never complied with
its Rule 26 obligations, or even attempted to do so until one
day before the discovery cutoff, and then (3) attempted to
blame Ace for those failures instead of justifying or explain-
ing them. The district court also explained that a lesser sanc-
tion would not be appropriate because (1) Ingenco had not
put forth any viable alternative and (2) any lesser sanction
requiring the reopening of discovery would have interfered
with the impending trial date.

Accordingly, the district court did not abuse its discre-
tion in sanctioning Ingenco for failure to disclose statutory
claims information to Ace, even though those sanctions resulted in the dismissal of Ingenco’s statutory claims.

CONCLUSION

For the reasons stated above, we AFFIRM the district
court’s orders in part, insofar as they apply Washington law
and exclude evidence of damages for purposes of state law
claims as a discovery sanction. We REVERSE, however, the
district court’s grant of summary judgment against Ingenco
and REMAND to the district court for trial. Each party shall
bear its own costs.

AFFIRMED IN PART; REVERSED IN PART; and
REMANDED.
Because the merits of the underlying tax dispute are irrelevant to our disposition, we provide only a brief summary of the facts. The Baldwins’ 2007 tax return reported a net operating loss of approximately $2.5 million from their movie production business. They wanted to carry that loss back to the 2005 tax year in order to offset their 2005 tax liability. Based on that carryback, the Baldwins prepared an amended 2005 tax return claiming entitlement to a refund of approximately $167,000.

To obtain a refund, the Baldwins were required to file their amended 2005 tax return by October 15, 2011—three years from the extended due date for their 2007 tax return. See 26 U.S.C. § 6511(b)(1), (d)(2)(A). The Baldwins assert that they sent their amended 2005 tax return to the IRS by U.S. mail in June 2011, well before the October 15th deadline. But the IRS never received that return, or any other return postmarked by the October 15, 2011, deadline. The IRS did eventually receive an amended 2005 return from the Baldwins in July 2013, but it was postmarked after the statutory deadline had passed. The IRS accordingly denied the Baldwins’ refund claim as untimely.

The Baldwins then brought this action against the United States in the district court. Although the doctrine of sovereign immunity would ordinarily bar such a suit, the United States has waived its immunity from suit by allowing a taxpayer to file a civil action to recover “any internal-revenue tax alleged to have been erroneously or illegally assessed or collected.” 28 U.S.C. § 1346(a)(1). Under the Internal Revenue Code (IRC), though, no such action may be maintained in any court “until a claim for refund or credit has been duly filed” with the IRS, in accordance with IRS regulations. 26 U.S.C. § 7422(a); see United States v. Dalm, 494 U.S. 596, 609 (1990). To be “duly filed,” a claim for refund must be filed within the time limit set by law. Yuen v. United States, 825 F.2d 244, 245 (9th Cir. 1987) (per curiam). Here, as noted above, the Baldwins had to file their refund claim (i.e., their amended 2005 tax return) by October 15, 2011.

At this point, before proceeding further, a detour is necessary to explain when a document, such as a tax return, is deemed “filed” with the IRS.

Before 1954, the law treated tax documents as timely filed only if they were physically delivered to the IRS by the applicable deadline. Anderson v. United States, 966 F.2d 487, 490 (9th Cir. 1992); see United States v. Lombardo, 241 U.S. 73, 76 (1916). This physical-delivery rule left taxpayers who mailed their documents vulnerable to the vagaries of the postal service; documents could be delayed or not delivered at all through no fault of the taxpayer. To mitigate the harshness of the physical-delivery rule, some courts responded by applying the common-law mailbox rule. See, e.g., Detroit Automotive Products Corp. v. Commissioner of Internal Revenue, 203 F.2d 785, 785–86 (6th Cir. 1953) (per curiam); Arkansas Motor Coaches, Ltd. v. Commissioner of Internal Revenue, 198 F.2d 189, 191 (8th Cir. 1952). Under the common-law mailbox rule, proof of proper mailing—including by testimonial or circumstantial evidence—gives rise to a rebuttable presumption that the document was physically delivered to the addressee in the time such a mailing would
ordinarily take to arrive. *Philadelphia Marine Trade Association v. Commissioner of Internal Revenue*, 523 F.3d 140, 147 (3d Cir. 2008); *Anderson*, 966 F.2d at 491.

In 1954, Congress addressed some of the problems caused by the physical-delivery rule by enacting IRC § 7502. Section 7502(a)(1) carves out an exception to the physical-delivery rule for tax documents sent and delivered by U.S. mail. It provides that if a document is received by the IRS after the applicable deadline, it will nonetheless be deemed to have been delivered on the date that the document is postmarked:

> If any return, claim, statement, or other document required to be filed, or any payment required to be made, within a prescribed period or on or before a prescribed date under authority of any provision of the internal revenue laws is, after such period or such date, delivered by United States mail to the agency, officer, or office with which such return, claim, statement, or other document is required to be filed, or to which such payment is required to be made, the date of the United States postmark stamped on the cover in which such return, claim, statement, or other document, or payment, is mailed shall be deemed to be the date of delivery or the date of payment, as the case may be.

26 U.S.C. § 7502(a)(1). This exception means that a document will be deemed timely filed so long as two things are true: (1) the document is actually delivered to the IRS, even if after the deadline; and (2) the document is postmarked on or before the deadline. If the document is never delivered at all—say, because it gets lost in the mail—the exception by its terms does not apply. *Miller v. United States*, 784 F.2d 728, 730 (6th Cir. 1986) (per curiam).

To protect against a failure of delivery, some taxpayers choose to send documents by registered mail. Section 7502(c)(1) provides an exception to the physical-delivery rule applicable to documents sent in that manner. It provides that when a document is sent by registered mail, the registration will serve as prima facie evidence that the document was delivered, and the date of registration will be treated as the postmark date:

> For purposes of this section, if any return, claim, statement, or other document, or payment, is sent by United States registered mail—

(A) such registration shall be prima facie evidence that the return, claim, statement, or other document was delivered to the agency, officer, or office to which addressed; and

(B) the date of registration shall be deemed the postmark date.

26 U.S.C. § 7502(c)(1). Subsection (B) provides, in effect, that the same exception to the physical-delivery rule afforded under § 7502(a)(1) for documents sent by regular mail extends to documents sent by registered mail, with the registration serving the same function as the postmark. Subsection (A), however, goes further. It provides a presumption that a document sent by registered mail was delivered even if the IRS claims not to have received it, so long as the taxpayer produces the registration as proof.1

In the decades following the enactment of IRC § 7502, the courts of appeals reached conflicting decisions as to what effect, if any, the statute had on application of the common-law mailbox rule. On one side of the split, some courts held that § 7502 supplies the exclusive exceptions to the physical-delivery rule, thereby displacing the common-law mailbox rule altogether. See *Miller*, 784 F.2d at 730–31; *Deutsch v. Commissioner of Internal Revenue*, 599 F.2d 44, 46 (2d Cir. 1979). These courts noted that § 7502 evinces a preference “for an easily applied, objective standard”—a preference incompatible with the common-law mailbox rule, which tolerates testimonial and circumstantial evidence to prove when a document was mailed (and thus presumptively delivered). *Deutsch*, 599 F.2d at 46.

On the other side of the split, some courts reasoned that because § 7502 was meant to mitigate the harshness of the physical-delivery rule, it is best read as providing a safe harbor, not as limiting resort to alternative exceptions to the physical-delivery rule. See *Sorrentino v. IRS*, 383 F.3d 1187, 1193 (10th Cir. 2004); *Estate of Wood v. Commissioner of Internal Revenue*, 909 F.2d 1155, 1161 (8th Cir. 1990). Courts on this side of the split relied on the principle that statutes should not be read as displacing the common law unless Congress clearly so intended, while noting that Congress did not clearly state in § 7502 that it intended to displace the common-law mailbox rule. See *Estate of Wood*, 909 F.2d at 1160. Our circuit adopted this latter line of reasoning. In *Anderson v. United States*, 966 F.2d 487 (9th Cir. 1992), we “decline[d] to read section 7502 as carving out exclusive exceptions to the old common law physical delivery rule.” Id. at 491.

This circuit split left the law in an undesirable state, as it allowed similarly situated taxpayers to be treated differently depending on where they lived. In August 2011, the Treasury Department sought to resolve the split by promulgating an amended version of Treasury Regulation § 301.7502-1(e). The amended regulation interprets § 7502 as creating the exclusive exceptions to the physical-delivery rule:

> Other than direct proof of actual delivery, proof of proper use of registered or certified mail, and proof of proper use of a duly designated [private delivery service], are

1. Although not at issue here, IRC § 7502(c)(2) and (f)(3) authorize the Treasury Secretary to establish, by regulation, equivalent exceptions to the physical-delivery rule for documents sent by certified mail, electronic filing, and private delivery services. 26 U.S.C. § 7502(c)(2), (f)(3).
the exclusive means to establish prima facie evidence of delivery of a document to the agency, officer, or office with which the document is required to be filed. No other evidence of a postmark or of mailing will be prima facie evidence of delivery or raise a presumption that the document was delivered.

26 C.F.R. § 301.7502-1(e)(2)(i) (emphasis added). The regulation makes clear that, unless a taxpayer has direct proof that a document was actually delivered to the IRS, IRC § 7502 provides the exclusive means to prove delivery. In other words, recourse to the common-law mailbox rule is no longer available.

With that background in mind, we can now return to the facts of this case. In the district court, the Baldwins did not dispute that the amended 2005 tax return they claim to have mailed in June 2011 was never received by the IRS. The Baldwins therefore sought to rely on the common-law mailbox rule to establish that the document was presumptively delivered to the IRS in June 2011, shortly after they mailed it. They offered the testimony of two of their employees, who had been tasked with mailing the document on the Baldwins’ behalf. The employees explained that they deposited the amended 2005 return in the mail at the post office in Hartford, Connecticut, on June 21, 2011. Under the common-law mailbox rule, that testimony, if credited by the court, would give rise to a rebuttable presumption that the amended return was delivered to the IRS well before the October 15, 2011, deadline.

The district court credited the testimony of the Baldwins’ employees and found, on the basis of the common-law mailbox rule, that the Baldwins’ claim for a refund had been timely filed. The court rejected the government’s argument that Treasury Regulation § 301.7502-1(e)(2) barred application of the common-law mailbox rule. The court viewed IRC § 7502 as unambiguously supplementing, rather than supplanting, the common-law mailbox rule, thus leaving no room for the agency to adopt the construction of the statute reflected in Treasury Regulation § 301.7502-1(e)(2). Whether the district court correctly declared that portion of the Treasury Regulation invalid is the principal focus of the government’s appeal.

II

In deciding whether Treasury Regulation § 301.7502-1(e)(2) is valid, we employ the familiar two-step analysis under Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984). We ask first whether “Congress has directly spoken to the precise question at issue.” Id. at 842. If it has, Congress’ resolution of the issue controls and the agency is not free to adopt an interpretation at odds with the plain language of the statute. But if the statute is silent or ambiguous on the question at hand, we then ask whether the agency’s interpretation is “based on a permissible construction of the statute.” Id. at 843.

At step one of the analysis, we conclude that IRC § 7502 is silent as to whether the statute displaces the common-law mailbox rule. In particular, with respect to the question relevant here, the statute does not address whether a taxpayer who sends a document by regular mail can rely on the common-law mailbox rule to establish a presumption of delivery when the IRS claims not to have received the document. The statute does afford a presumption of delivery when a taxpayer sends a document by registered mail, 26 U.S.C. §§ 7502(c)(1)(A), and it authorizes the creation of similar rules for certified mail, electronic filing, and private delivery services. §§ 7502(c)(2), (f)(3). But as to documents sent by regular mail, the statute is conspicuously silent.

At step two of the Chevron analysis, the remaining question is whether Treasury Regulation § 301.7502-1(e)(2) is based on a permissible construction of the statute. We conclude that it is. As reflected by the circuit split that developed on this issue, Congress’ enactment of IRC § 7502 could reasonably be construed in one of two ways: as intended merely to supplement the common-law mailbox rule, or to supplant it altogether. The Treasury Department chose the latter construction by interpreting IRC § 7502 to provide the sole means by which taxpayers may prove timely delivery in the absence of direct proof of actual delivery. That construction of the statute is reasonable in light of the principle that “where Congress explicitly enumerates certain exceptions to a general prohibition, additional exceptions are not to be implied, in the absence of evidence of a contrary legislative intent.” Hillman v. Maretta, 569 U.S. 483, 496 (2013) (alteration omitted); see also Syed v. M-I, LLC, 853 F.3d 492, 501 (9th Cir. 2017). Given that the purpose of enacting IRC § 7502 was to provide exceptions to the physical-delivery rule, it is reasonable to conclude that “Congress considered the issue of exceptions and, in the end, limited the statute to the ones set forth.” United States v. Johnson, 529 U.S. 53, 58 (2000).

In arguing that the Treasury Department unreasonably construed IRC § 7502 as having displaced the common-law mailbox rule, the Baldwins invoke a different principle of statutory interpretation, which provides that “the common law … ought not to be deemed repealed, unless the language of a statute be clear and explicit for this purpose.” Norfolk Redevelopment and Housing Authority v. Chesapeake & Potomac Telephone Co., 464 U.S. 30, 35 (1983) (alteration and internal quotation marks omitted). But the mere fact that dueling principles of statutory interpretation support opposing constructions of a statute does not prove, without more, that the agency’s interpretation is unreasonable. The question remains whether the agency has adopted a permissible construction of the statute, taking into account all of the interpretive tools available. As is true in this case, an agency’s

2. The statute is also silent as to whether any evidence other than the objective evidence described in the statute—the registration for registered mail, and equivalents for certified mail, electronic filing, and private delivery service—may raise a presumption of delivery.
construction can be reasonable even if another, equally permissible construction of the statute could also be upheld.

Finally, our prior interpretation of IRC § 7502 in Anderson does not bar our decision to defer to the agency’s conflicting, but nonetheless reasonable, construction of the statute. As noted above, before the relevant amendment of Treasury Regulation § 301.7502-1(e), we “decline[d] to read section 7502 as carving out exclusive exceptions to the old common law physical delivery rule.” Anderson, 966 F.2d at 491. But “[a] court’s prior judicial construction of a statute trumps an agency construction otherwise entitled to Chevron deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion.” National Cable & Telecommunications Association v. Brand X Internet Services, 545 U.S. 967, 982 (2005). We did not hold in Anderson that our interpretation of the statute was the only reasonable interpretation. In fact, our analysis made clear that our decision filled a statutory gap. Under Brand X, the Treasury Department was free to fill that gap by adopting its own reasonable interpretation of the governing statute.

III

The Baldwins contend that even if Treasury Regulation § 301.7502-1(e)(2) is valid, it does not apply in this case. They offer two arguments to that end, both of which we reject.

First, the Baldwins argue that IRC § 7502 and Treasury Regulation § 301.7502-1(e)(2) apply only when a tax document was sent before, but received after, the applicable due date. In their view, these provisions do not apply when, as here, a tax document was never received at all. The Baldwins thus contend that even if Treasury Regulation § 301.7502-1(e)(2) prohibits recourse to the common-law mailbox rule, that prohibition does not apply to them because they used the mailbox rule not to prove that a late-received document was mailed in time, but instead to prove that a document that the IRS apparently never received was in fact delivered.

The Baldwins are mistaken. To be sure, § 7502 addresses situations in which tax documents are mailed before, but not received until after, the due date. Subsection (a)(1) provides that in such instances the document will be deemed timely filed so long as it was postmarked before the due date. 26 U.S.C. § 7502(a)(1). But § 7502 also addresses situations in which the IRS claims not to have received a tax document at all. Subsection (c)(1)(A) provides that, for documents sent by registered mail, the registration will be treated as “prima facie evidence that the [document] was delivered.” § 7502(c)(1)(A). That provision can apply only when the IRS claims not to have received a document. The Baldwins are therefore wrong in contending that IRC § 7502 and Treasury Regulation § 301.7502-1(e)(2)—which interprets the statute to prohibit recourse to the common-law mailbox rule—do not apply to situations like theirs in which a document was never delivered to the IRS.

Second, the Baldwins argue that Treasury Regulation § 301.7502-1(e)(2) does not apply in this case because it was promulgated in August 2011, two months after they allegedly mailed their amended 2005 return in June 2011. This argument also fails. See Maine Medical Center v. United States, 675 F.3d 110, 118 n.14 (1st Cir. 2012) (rejecting identical argument). The regulation expressly provides that “Section 301.7502-1(e)(2) will apply to all documents mailed after September 21, 2004,” the date that the current text of the regulation was proposed. 26 C.F.R. § 301.7502-1(g)(4); Timely Mailed Treated as Timely Filed, 69 Fed. Reg. 56,377-01 (Sept. 21, 2004). That retroactivity provision complies with IRC § 7805(b), which authorizes the Treasury Secretary to make regulations retroactively applicable as far back as the date of their proposal. 26 U.S.C. § 7805(b)(1)(B); see Bowen v. Georgetown University Hospital, 488 U.S. 204, 208 (1988). Our prior decision in Anderson is irrelevant to the issue of retroactivity, as § 7805(b) does not contain an exception barring the retroactive application of a valid regulation in judicial circuits where the regulation contravenes a prior circuit decision.

Because Treasury Regulation § 301.7502-1(e)(2) is valid and applicable in this case, and because timely filing is a mandatory requirement for maintaining tax refund suits, see 26 U.S.C. § 7422(a), we reverse the judgment below and remand with instructions to dismiss this case. As the Baldwins are no longer prevailing parties, we also reverse the award of litigation costs.

REVERSED and REMANDED.
Cite as 19 C.D.O.S. 3451

TERRY GRIMM, Plaintiff-Appellant, v. VORTEX MARINE CONSTRUCTION; SIGNAL MUTUAL INDEMNITY ASSOCIATION; ACCLAIM RISK MANAGEMENT, INC.; EDWARD PAUL MARTIN; DALE ANN MARTIN; CASSANDRA LANE, Defendant-Appellee.

No. 18-15104
United States Court of Appeals for the Ninth Circuit
D.C. No. 3:17-cv-03103-EDL
Appeal from the United States District Court for the Northern District of California
Elizabeth D. Laporte, Magistrate Judge, Presiding
Argued and Submitted March 12, 2019
San Francisco, California
Filed April 16, 2019

OPINION

HURWITZ, Circuit Judge:

The central issue in this case is whether a Department of Labor administrative law judge (“ALJ”) found that Grimm had sustained work-related injuries while employed by Vortex. The ALJ therefore ordered Vortex to “pay or reimburse the Claimant for all medical expenses arising from the Claimant’s work-related injuries,” and to “provide treatment going forward, including the diagnostic procedures and therapies his treating physicians judge appropriate.” The Benefits Review Board (“BRB”) affirmed the ALJ’s order. Vortex petitioned this Court for review of the BRB decision, but withdrew the petition.

In this action, Grimm alleges that Vortex refused to pay for required medical treatment and he was therefore forced to rely on Medicare to pay his expenses. The operative amended complaint sought to enforce the ALJ’s order and also asserted a claim under the MSP, seeking double damages for the amounts Medicare paid for the services. See 42 U.S.C. § 1395y(b). 1

The district court granted Vortex’s motion to dismiss, finding it lacked jurisdiction to enforce the ALJ’s order because it was not final and that the MSP claim was premature. This timely appeal followed.

II

A

“The Longshore Act is a worker’s compensation plan under which employers subject to the Act are required, within statutory limits, to compensate their employees for job-related injuries or deaths.” Thompson v. Potashnick Constr. Co., 812 F.2d 574, 575 (9th Cir. 1987). Compensation claims are “filed with the deputy commissioner in the compensation district in which such injury or death occurred,” 33 U.S.C. § 913, and disputes requiring a hearing referred to an ALJ, id. § 919(c)–(d). The ALJ can issue a “compensation order,” either “rejecting the claim or making the award.” Id. § 919(e); 20 C.F.R. § 702.348. Appeals from compensation orders go to the BRB. 33 U.S.C. § 921(b)(3). “Final orders of the BRB are reviewable by the United States Courts of Appeals.” Thompson, 812 F.2d at 576 (citing 33 U.S.C. § 921(c)).

If an employer “fails to comply with a compensation order … that has become final,” the beneficiary may bring an enforcement action in the district court. 33 U.S.C. § 921(d). “Unlike the BRB and court of appeals, the district court has no jurisdiction over the merits of the litigation.” Thompson, 812 F.2d at 576. A district court accordingly “cannot affirm, modify, suspend or set aside the order.” Id. Rather, its “jurisdiction extends only to the enforcement of compensation orders.” Id.

1. The defendants are Vortex; Signal Mutual Indemnity Association; Vortex’s insurer; Acclaim Risk Management, Inc., third party administrator for Vortex’s Longshore Act claims; an Acclaim insurance adjuster; and two Acclaim officers.
The district court dismissed Grimm’s enforcement action because it found the ALJ’s order not final under § 921(d). We previously have not addressed when an order becomes final under that statute. However, several of our sister Circuits have done so, and we join them in holding that to be “final” for purposes of § 921(d), an order must “at a minimum specify the amount of compensation due or provide a means of calculating the correct amount without resort to extra-record facts which are potentially subject to genuine dispute between the parties.” Severin v. Exxon Corp., 910 F.2d 286, 289 (5th Cir. 1990); see also Stetzer v. Logistec of Conn., Inc., 547 F.3d 459, 463–64 (2d Cir. 2008) (adopting Severin’s analysis).2

The Longshore Act does not specify when a “compensation order” becomes “final” under § 921(d). But the Act defines “compensation” as “the money allowance payable to an employee,” 33 U.S.C. § 902(12), suggesting that a final order must either specify the “money allowance” or provide a ready method for determining it. And, the governing regulations define “medical care” as that which is “recognized as appropriate by the medical profession for the care and treatment of the injury.” 20 C.F.R. § 702.401(a). The district court’s enforcement power does not extend to determining whether specific medical care is appropriate, or even whether the fees charged by a treating physician are reasonable. See 20 C.F.R. § 702.413 (requiring the agency to determine the reasonableness of disputed fees). It thus stands to reason, as Severin holds, that a district court’s limited jurisdiction over a compensation order extends only to orders whose monetary sweep cannot be disputed.

Under the Severin rubric, the district court correctly found that it lacked jurisdiction over Grimm’s § 921(d) enforcement claim. The ALJ’s order stated “Vortex … must pay or reimburse the Claimant for all submitted medical expenses … .” It did not list an amount to be paid or a means of calculating what Vortex would be called on to resolve disputes about whether the services Grimm received were for work-related injuries, and perhaps over the charges incurred for those services. Resolution of that dispute plainly turns on “extra-record facts which are potentially subject to genuine dispute between the parties.” Severin, 910 F.2d at 289. Those disputes must be addressed in the first instance to the agency.3

Moreover, the amended complaint improperly requested modification of the ALJ’s order. For example, it sought issuance of three LS-1 forms authorizing payment for medical services, as well as an order requiring Vortex to pay timely for future medical care and hold Grimm harmless against claims brought by others. Issuance of these forms would modify, rather than enforce, the ALJ’s order and a district court lacks jurisdiction under § 921(d) to “modify” orders. See Thompson, 812 F.2d at 576.

Grimm correctly notes that the central purpose of the Longshore Act is “to place the compensation award in the hands of the entitled claimant as soon as possible.” Sea-Land Serv., Inc. v. Barry, 41 F.3d 903, 907 (3d Cir. 1994). That purpose might be furthered if Congress had seen fit to empower district courts to resolve disputes over whether a specific service should be paid for by the employer. But Congress did not do so, instead in § 921(d) limiting the district court to enforcement of final agency orders. The district court therefore did not err in dismissing the enforcement claim for lack of subject matter jurisdiction.

B

The gravamen of Grimm’s MSP claim is that Medicare was forced to pay his medical expenses after Vortex wrongfully refused to do so. The district court correctly rejected that claim as premature.

“The MSP makes Medicare insurance secondary to any ‘primary plan’ obligated to pay a Medicare recipient’s medical expenses ….” Parra v. PacifiCare of Ariz., Inc., 715 F.3d 1146, 1152 (9th Cir. 2013) (citing 42 U.S.C. § 1395y(b)(2)(A)). The term “primary plan” includes “workmen’s compensation law[s] or plan[s],” 42 U.S.C. § 1395y(b)(2)(A); see § 1395y(b)(8)(F); 42 C.F.R. § 411.40(a) (interpreting “primary plan” to include the Longshore Act). The MSP authorizes Medicare to make conditional payment for services if a primary plan “has not made or cannot reasonably be expected to make payment … promptly.” Id. § 1395y(b)(2)(B)(i). Medicare

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2. Other courts of appeal have also reached identical conclusions in suits under 30 U.S.C. § 932, the Black Lung Benefits Act (“BLBA”). Section 932 expressly incorporates the enforcement scheme in the Longshore Act. See, e.g., Connors v. Amax Coal Co., 858 F.2d 1226, 1228–29 (7th Cir. 1988) (“A claimant … does not possess a compensation order extending only to orders whose monetary sweep cannot be disputed.”) (internal quotations omitted); Connors v. Bethlehem Mines Corp., 862 F.2d 461, 463 (3d Cir. 1988) (requiring “the Secretary of Labor to make an initial determination of benefits before the district court has jurisdiction to enforce a final order”); Connors v. Oglebay Norton Co., 848 F.2d 84, 85 (6th Cir. 1988) (holding that a plan could not “proceed directly” in district court to recover BLBA payments made to miners “since it has never been determined administratively that the miners are entitled to any specific award”).

3. While this appeal was pending, the Office of Workers’ Compensation Programs issued a Memorandum of Internal Conference, recommending that Vortex (1) pay or reimburse Grimm for all submitted chiropractic bills; (2) authorize Grimm’s medical group to treat him with all appropriate medical care; and (3) review and resolve all outstanding non-chiropractic provider bills within 90 days. We GRANT Vortex’s motion for judicial notice of the Memorandum.
care can then seek reimbursement “if it is demonstrated that such primary plan has or had a responsibility to make payment.” Id. § 1395y(b)(2)(B)(ii).

The MSP’s private right of action allows a beneficiary to recover double the amount of Medicare payments made when a plan “fails to provide for primary payment (or appropriate reimbursement).” Id. § 1395y(b)(3)(A); see Parra, 715 F.3d at 1152. A primary payment includes a “payment [that] has been made, or can reasonably be expected to be made” by a primary plan. 42 U.S.C. § 1395y(b)(2)(A).

But, “the defined term ‘primary plan’ presupposes an existing obligation (whether by statute or contract) to pay for covered items or services.” Humana Med. Plan, Inc. v. W. Heritage Ins. Co., 832 F.3d 1229, 1237 (11th Cir. 2016). Grimm’s MSP claim would require the district court to determine in the first instance whether Vortex was obliged to pay for the items and services covered by a Medicare conditional payment. Until an ALJ, subject to review by the BRB and court of appeals, has found an employer liable for specific medical expenses, a plaintiff cannot demonstrate the employer’s responsibility as required by the MSP. Absent a final compensation order requiring that specific services either be paid for or reimbursed, Grimm has failed to state a claim for recovery under the MSP.

III

For the reasons above, we AFFIRM the judgment of the district court.

WATFORD, Circuit Judge, concurring:

I agree that the district court lacks jurisdiction to hear the Longshore Act claim. But while the court casts the jurisdictional issue as one of finality, in my view there is a more basic deficiency. The Longshore Act limits the jurisdiction of the district court to enforcing “compensation orders.” 33 U.S.C. § 921(d). What Terry Grimm seeks to enforce here is the portion of an administrative order directing Vortex Marine Construction to pay or reimburse Grimm in the future “for all medical expenses arising from [his] work-related injuries.” That is not a compensation order within the meaning of the Longshore Act. The Act defines “compensation” as “the money allowance payable to an employee or to his dependents as provided for in this chapter.” § 902(12). That definition does not include an employer’s obligation to furnish future medical care. Marshall v. Pletz, 317 U.S. 383, 390–91 (1943). To obtain an enforceable compensation order, Grimm must first receive the medical care he requires and then seek an additional order directing Vortex to pay for the medical bills he has incurred. Id. at 391; see 33 U.S.C. § 907(d)(1). The Longshore Act does not permit a district court to issue an injunction under § 921(d) prospectively ordering an employer to pay for future medical benefits, no matter how specific the administrative order may be.
A music publishing agreement is a contract between a songwriter and a publishing company that sets forth the ownership of the copyright in the subject musical compositions, and the division of revenue generated from the use of those compositions. Under the traditional form of music publishing agreement, the songwriter assigns his or her copyright interest in the composition to the publisher. In return, the publisher agrees to promote and exploit the composition on the market, and pay the songwriter his or her share of royalties. (See generally Broadcast Music, Inc. v. Roger Miller Music, Inc. (6th Cir. 2005) 396 F.3d 762, 765 (Roger Miller) [describing the “basics of the music industry”].)

There are four primary categories of royalty income generated from music publishing: (1) “mechanical royalties,” consisting of income from the sale of records, audiocassettes, compact discs, etc.; (2) “synchronization royalties,” consisting of income from music that is synchronized with a visual image, such as a movie, television show or commercial; (3) “song book and folio royalties,” consisting of income from the sale of printed music; and (4) “public performance royalties,” consisting of income from public performances of the music composition, including, for example, radio broadcasts, streaming broadcasts and live performances in music venues. In standard publishing agreements, the publisher is responsible for collecting the first three categories of royalties from third parties who have licensed the composition, and then paying the songwriter his or her contracted share of those royalties, typically 50 percent. However, the writer and publisher normally agree to affiliate with a “performing rights organization” (PRO) to collect and distribute public performance royalties (hereafter performance royalties or performance income). “Broadcast Music, Inc. (BMI) and the American Society of Composers, Authors and Publishers (ASCAP) are the two principal [PROs] operating in the United States.”

“Commonly, writers and publishers agree to be paid their respective shares of performing rights directly by the

1. “ASCAP was created in 1914 by music creators and publishers as an unincorporated membership association. BMI was founded by broadcasters in 1939. Each represents hundreds of thousands of songwriters, composers, and publishers who hold copyrights in millions of musical works. They negotiate, implement, and enforce agreements with licensees that grant the right to perform their members’ copyrighted songs. . . . Together, ASCAP and BMI license the music performance rights to most domestic copyrighted music in the United States.” (Broadcast Music, Inc. v. DMX Inc. (2d Cir. 2012) 683 F.3d 32, 36.)
[PRO].” (Ibid.) As with most other forms of music publishing income, the songwriter is typically entitled to 50 percent of the performance royalties, and the publisher is entitled to the remaining 50 percent.

B. Summary of the Parties’ Agreements

1. The 1970 Agreement

In 1970, each member of the band WAR entered into an identically-worded music publishing agreement with Far Out Music (FOM), then owned by Gerald Goldstein and his now-deceased partner, Stephen Gold. In exchange for each band member’s copyrights to the music compositions he had written (or co-authored), FOM agreed to pay the following royalties, set forth in paragraph 9: (1) 4 cents per copy of sheet music, and 10 percent of income generated from sale of music folios; and (2) 50 percent of the net sums received from mechanical royalties, synchronization royalties and foreign income (income generated from the sale or license of the compositions outside the United States). Paragraph 7 of the Agreement, however, directed that the writer “shall receive his public performance royalties … directly from his own affiliated performing rights society and shall have no claim whatsoever against publisher for any royalties received by publisher as a distribution from any performing right society which makes payment directly … to writers authors and composers.”

The 1970 Agreement did not entitle the band members to any form of payment other than the royalties set forth in paragraph 9.

2. The 1972 Memorandum of Understanding

Following the publication of a successful album in 1971, the band retained attorney Nicholas Clainos to represent them in litigation against FOM and several FOM-related entities. As part of the litigation, the band sought to terminate the 1970 Agreement, and negotiate a new agreement that included more favorable terms.

After extensive negotiations between Clainos and Stephen Gold, the parties signed a “Memorandum of Agreement” on August 22, 1972 (the MOA) that included the following preface: “Prior to the preparation of formal contracts between [the band members] and [FOM], this memorandum of agreement will confirm the agreements we have reached with respect to the subject matter contained herein.” The MOA further provided that each band member would “enter into an exclusive songwriter agreement upon the terms and conditions hereinafter set forth, as well as those standard terms which are customary in the entertainment industry in the agreements of this type.”

Paragraph 3(b) of the MOA described the royalties FOM had agreed to pay the band, which were essentially identical to the royalties set forth in paragraph 9 of the 1970 Agreement:

“The songwriter will receive $.04 for sheet music; 10% of the wholesale selling price for other printed copies; 50% of all net sums received from the utilization of mechanical, electrical transcriptions, and synchronization rights; and 50% of all foreign monies received. It is acknowledged that the writer will receive directly from his own performing rights society the writer’s portion of any and all performance monies which shall become due.”

In addition to the royalties described in paragraph 3(b), however, the MOA included a new provision, set forth at paragraph 3(e), that entitled the band to a share of the income FOM received from the exploitation of the compositions: “In addition to the foregoing, the writer shall receive with respect to those songs which he has written, a sum equal to 30% … share of publisher’s income (after deduction for collection fees, direct costs and administration fees).”

The final paragraph of the MOA reiterated that the terms set forth therein “correctly reflect[ed] [the signatories’] mutual understanding. . . . Until formal contracts are entered into . . . reflecting the agreements set forth above, this memorandum of agreement shall for all purposes govern and bind the parties hereto.”

3. The 1972 Agreement

Shortly after signing the MOA, the parties signed the 1972 Agreement, which was to take effect as of August 22, 1972, the same date the MOA was signed.3

Paragraph 7 of the 1972 Agreement set forth the royalties FOM agreed to pay the band, which were the same amounts set forth in paragraph 3(b) of the MOA. The 1972 Agreement however, contained modified language regarding the payment of performance royalties. Paragraph 7(c), for example, stated that the writer was to receive “50% of any and all net sums actually received by the Publisher from the mechanical rights, electrical transcriptions, . . . synchronization and . . .

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3. As with the 1970 Agreement, each member of the band signed a separate, identically-worded agreement that assigned FOM the copyrights to the musical compositions he wrote (or co-wrote) in exchange for the payments described therein. The individual 1972 Agreements likewise included language clarifying that the payments described therein were to be paid solely to the writer “in instances where Writer is the sole author and composer of the composition,” and “with regard to compositions where there are other writers, the Writer shall be paid only a portion of said [payments] which shall be determined by dividing the total [payments] payable by the number of writers for such composition, unless a different division … is agreed upon by all such writers. . . .”
and all other rights (except as otherwise specifically provided for herein) … except that the Writer shall not be entitled to share in any sum or sums received by the Publisher from [a PRO].” Paragraph 7(d) similarly provided that band members were entitled to 50 percent of the net sum of any foreign income “other than public performance uses for which Writer is paid by any [PRO].”

Finally, paragraph 7(f) confirmed that “the publisher shall not be required to pay royalties earned by reasons of the public performances of the composition; said royalties being payable only by the [PRO] with which Writer is or may in the future become affiliated.”

As with the MOA, the 1972 Agreement included an additional provision, set forth at paragraph 22, that entitled the writer to receive a 30 percent share of FOM’s revenue after the deduction of certain administrative costs and fees:

22. In addition to the royalties provided for in Paragraph 7 above, all monies actually earned and received from the sale, lease, license, disposition or other turning to account of rights in the Compositions, including all monies received in connection with the infringement by third parties of rights in the Compositions (“Composition Gross Receipts”) shall be treated as follows:

(a) Publisher shall be entitled first to deduct any and all administration and related fees from the Composition Gross receipts. . . .

(b) Publisher shall then deduct from Composition Gross Receipts . . . the royalties due to the composers of the composition in accordance with any agreement the Publisher may have with such composers;

(c) From the balance of the Composition Gross Receipts remaining . . . Publisher shall be entitled to deduct and retain amounts equal to the following direct costs actually advanced or incurred by Publisher in realizing Composition Gross Receipts (Composition Costs): All costs of copyrighting the composition; . . . legal fees [relating to any claim of copyright infringement]; Accounting fees. . . . [etc.];

(d) 30% of the balance of the Composition Gross Receipts remaining after the deductions provided for in Paragraphs 22(a), 22(b) or 22(c) hereof . . . shall belong to Writer and be paid to Writer . . . .”

4. The 1975 Agreement and subsequent litigation

In 1975, FOM and the band members signed a new agreement (the 1975 Agreement) that modified the payout formula set forth in paragraph 22 of the 1972 Agreement. The new revenue sharing provision provided that, after the deductions of certain administrative costs and fees, FOM would be entitled to 25 percent of the Composition Gross Receipts, and the writer would be entitled to the remaining balance. The 1975 Agreement did not alter the definition of Composition Gross Receipts, or otherwise affect the categories of revenue that FOM was to include when calculating the amount due under paragraph 22. Instead, the new agreement only altered the formula used to determine the band member’s share of Composition Gross Receipts.

In 2009 and 2011, several band members brought multiple lawsuits in connection with FOM’s payment of royalties under the parties’ publishing agreements. The litigation resulted in two settlement agreements, both of which contained language confirming that the 1972 Agreement and 1975 Agreement remained in effect.

C. The Current Litigation

1. Summary of plaintiffs’ claims

In October 2014, several current and former band members (or their successors-in-interest) (collectively plaintiffs or the band) filed the current breach of contract action against FOM, Gerald Goldstein and numerous FOM-related entities (collectively FOM). The complaint alleged FOM had violated the terms of the 1972 Agreement by excluding public performance royalties from “Composition Gross Receipts” described in paragraph 22, denying plaintiffs their right to share in that category of income.

The complaint alleged paragraph 22 defined Composition Gross Receipts to include “all moneys” FOM had received from the sale, lease or license of the compositions, which necessarily included any performance royalties FOM had received from its PRO. The complaint further alleged FOM had consistently “paid [plaintiffs] royalties on [its share] of ‘performance income’ without fail for nearly four decades.” In December of 2013, however, FOM “suddenly . . . , [and] without any basis for doing so, eliminated [its] share of public performance as a category of income for which [it] w[as] paying participant royalties . . . .”

In their prayer for relief, plaintiffs sought a declaration that FOM’s “share of public performance revenue is to be included in the revenue base upon which [FOM] account[s] to and pay[s] Plaintiffs pursuant … to paragraph 22 of the [1972 Agreement].” They also sought contract damages for any accounting period during which FOM had excluded its performance royalties from Composition Gross Receipts.4

4. Plaintiffs’ complaint included an additional claim alleging that FOM had breached the terms of the written agreements by failing to use the revenue sharing formula set forth in the 1975 Agreement, and instead continuing to use the formula set forth in the 1972 Agreement. During the trial court proceedings, however, plaintiffs voluntarily dismissed that portion of their complaint. The parties agree that any continuing disputes they may have regarding the 1975 Agreement are not relevant to the issues in this appeal.
2. FOM's motion for summary judgment
   a. Summary of FOM's motion

FOM filed a motion for summary judgment arguing that the
plain and unambiguous language of the 1972 Agreement
made clear that the publisher's performance royalties were
to be excluded from paragraph 22's revenue-sharing provi-
sion. In support, FOM cited language in paragraphs 7(c) and
(f) of the agreement stating that the writer was not "entitled
to share in any … sums received by the Publisher from [any
PRO]." and that "the publisher shall not be required to pay
royalties earned by reasons of the public performances of the
composition." According to FOM, this language unambigu-
ously "exclude[d] … all public performance royalties as a
source of revenue which must be included in the formulæ
[set forth in paragraph 22]."

FOM further asserted that paragraph 22 could not be
read to "grant rights [to plaintiffs] that [were] specifically
excluded by Paragraph 7." FOM explained that the revenue-
sharing payment described in paragraph 22 was to be made
"in addition to" whatever royalties were due under paragraph
7, which expressly excluded any type of payment for perfor-
mance royalties. FOM contended that because paragraph 7
excluded performance royalties, such royalties were neces-
sarily excluded from paragraph 22. According to FOM, any
other interpretation would render paragraph 7's exclusion of
performance royalties meaningless.

FOM did not submit any extrinsic evidence in support of
its interpretation of the 1972 Agreement. Instead, it relied
solely on the text of the agreement, and declarations authen-
ticating the document.

b. Plaintiffs' opposition and extrinsic evidence

Plaintiffs, however, argued the 1972 Agreement should
be interpreted to require FOM to include performance roy-
alties in the base amount used to calculate the revenue-sharing
payment due under paragraph 22. Plaintiffs noted that para-
graph 22 specifically defined Composition Gross Receipts
to include "all moneys" FOM had received from the sale or
lease of the compositions, and contained no language ex-
cluding performance royalties. Plaintiffs further asserted the
language FOM had cited in paragraph 7 was merely intended
to clarify that FOM had no duty to pay plaintiffs' royalties
for performance revenue because the band was to receive
all of its performance royalties directly from its PRO. Para-
graph 22, in contrast, described a separate and distinct type
of payment consisting of a share of all revenue FOM received
from the exploitation of the music, including performance
royalties.

In support of their opposition, plaintiffs submitted copies
of all the parties' prior written agreements, and declarations
from several witnesses, including: (1) Nicholas Clainos, the
attorney who negotiated the 1972 Agreement on the band's
behalf; (2) Michael Perlstein, an attorney specializing in the
music industry; and (3) Fred Wolinsky, a certified public ac-
countant specializing in music industry accounting.

i. Declaration of Nicholas Clainos

Nicholas Clainos's declaration stated that his primary con-
tact at FOM during the negotiation of the 1972 Agreement
was Steven Gold, who Clainos described as a co-owner of
the company. Clainos asserted that he had told Gold the band
would drop its legal claims regarding the 1970 Agreement if
FOM agreed to enter into a new agreement that contained a
provision entitling the band to participate in "the pool of the
publisher's share of money," which was to include "the entire
pot of money collected by the publisher for all sources, in-
cluding the publisher's share of public performance monies."

According to Clainos, "[Gold] agreed to the participation
concept," and then "prepared the 1972 [MOA] as a tempo-
rary document and foundation for drafting a long form. . . .
Subparagraphs (a) through (d) of paragraph 3 of the 1972
[MOA] reiterate FOM's previously existing obligation to pay
the band royalties] . . . . . Paragraph 3(e) is the lan-
guage that [Gold] prepared based upon our discussion and
our agreement for payment to my clients of a percentage of
30% of all the publisher's share of income in addition to the
monies payable solely for their [royalties]."

Clainos further stated that before the parties signed the
1972 MOA, he reaffirmed with Gold that the band's 30 per-
cent participation in FOM's share of revenue "was to include
100% of all revenue the publisher received, including the
publisher's public performance revenue. [Gold] acknowled-
ged that such was the agreement . . . . " Clainos also as-
serted that when drafting the 1972 Agreement, he and Gold
"specifically . . . discuss[ed]" that paragraph 22 was intended
to apply to all forms of revenue that FOM actually received,
"including the publisher's share of public performance rev-
emens, less only specifically delineated deductions."

ii. Declaration of Michael Perlstein

Michael Perlstein's declaration stated that he had over 50
years of experience representing clients in the music industry,
and was "very familiar" with "the standard music publishing
industry practices of [the 1970s], the customs and practices
in connection with such contracts . . . and the customary us-
age of terminology in such contracts." Perlstein provided an
overview of the music publishing industry, explaining the
various forms of revenue derived from musical compositions,
the origins of performing rights organizations and how pub-
lishing agreements had evolved during the 20th Century.

According to Perlstein, the plaintiffs' 1970 and 1972
Agreements reflected the favorable changes that more suc-
cessful songwriters were able to impose on publishers dur-
ing that era. Specifically, Perlstein explained that the original
1970 Agreement merely provided the band members tradi-
tional royalty payments, while the 1972 Agreement, negoti-
ated after the band had become more successful, contained a
new and additional paragraph entitling them to "receive from
FOM, a portion of the publisher's share [of revenue]."

Perlstein further asserted that, "as used in publishing con-
tracts of the period, i.e., usage of trade, the word 'all' used
here in this new arrangement set forth in paragraph 22 meant what it says – all monies actually earned and received by a publisher such as FOM from all sources, including the publisher’s share of performance royalties paid to FOM by its PRO (in this case ASCAP). This customary usage also was customarily defined by terms such as ‘Composition Gross Receipts’ which was used at that time (and at present) as an all-encompassing reference subject only to deductions specified directly in connection with such definition.”

Perlstein contended that in his “nearly 50 years of experience of drafting and negotiating music publishing agreement[s] and evaluating them for [his] publishing catalogue clients . . . [he had] never seen a music publishing contract which provided for songwriters to be paid a portion of the publisher’s share of . . . income that did not include in its base amount, the publisher’s share of public performance income.”

iii. Declaration of Frederick Wolinsky

Frederick Wolinsky’s declaration stated that he had “more than 35 years of experience in royalty and forensic accounting in the music industry,” and had personally participated in an audit between the parties in 2007. Wolinsky further asserted that he had reviewed the parties’ prior publishing agreements, and “at least 30 years of statements issued by defendants.” Based on his review of those materials, Wolinsky concluded that until May of 2014, FOM had “consistently included [its] share of . . . public performance revenue in . . . calculate[ing] . . . and pay[ing] Plaintiffs’ . . . ‘participant’s share’ under paragraph 22 of the 1972 [Agreement].”

Wolinsky’s declaration identified and attached as exhibits five accounting statements that were “consistent with the [other statements] he had reviewed in rendering his opinion. The five statements were from six-month accounting periods in 1982, 2007, 2011 and 2013. Three of the statements (from 1982, 2007 and 2011) did not specifically reference performance royalties; instead the statements only showed the total amount of income FOM had paid to the band members for each song during that accounting period. The two other statements, which covered six-month periods in 2011 and 2013, used a different format that included a separate line item showing FOM had paid band members a share of performance royalties during that period.

Wolinsky further stated that in May of 2014, FOM sent plaintiffs a letter asserting that they were “not entitled to share in the publisher’s share of performance royalties,” and that some prior statements reflected an “overpayment in connection with performance royalties.” The letter further explained that FOM intended to offset those overpayments against future royalty payments owed to plaintiffs. According to Perlstein, “[t]his reversed [FOM’s] decades-old course of performance,” and was “inconsistent with at least 30 years of prior statements.”

3. FOM’s reply brief

In its reply brief, FOM asserted that “the words of the [1972 Agreement] plainly and clearly manifest the intentions of the parties in 1972 that the publisher’s public performance royalties would not be included in the calculation of royalties to plaintiffs.” FOM further asserted that the trial court should not consider any of the plaintiffs’ extrinsic evidence because the 1972 Agreement was not reasonably susceptible to their proposed interpretation. According to FOM, the extrinsic evidence was instead admitted for an improper purpose: “to create for the parties a contract which they did not make and . . . insert language which one party now wishes were there.”

FOM also attacked the relevancy and credibility of the extrinsic evidence. First, it contended the 1972 MOA was not relevant to the interpretation of the 1972 Agreement because the MOA had been “superseded by the 1972 Agreement.” Second, FOM argued that Clainos’s declaration was “irrelevant” because his statements merely asserted that he and Gold had “discussions” about certain aspects of the 1972 Agreement without explaining “what the parties said to one another and what was expressly agreed between them.” FOM argued Perlstein’s declaration was likewise of “no value” because his customs and usage testimony conflicted with the plain language of the 1972 Agreement, which expressly excluded any form of payment for performance royalties.

Finally, FOM argued that Wolinsky’s “course of performance” testimony was “irrelevant” and inadmissible because it lacked “factual and evidentiary foundation.” FOM explained that although Wolinsky claimed the materials he had reviewed showed FOM had paid plaintiffs a share of performance royalties for decades, his declaration failed to “disclose how [he had] divined [t]his conclusion.” FOM noted that only two of the five accounting statements Wolinsky had included with the declaration actually referenced performance royalties, which was insufficient to establish a “course of performance.” FOM further asserted that the letter Wolinsky had referenced in his declaration made clear that the inclusion of performance royalties in these two statements was the result of an accounting mistake.

FOM’s reply brief was accompanied by evidentiary objections seeking to exclude substantial portions of the declarations and documents plaintiffs had filed in support of their opposition, including all of Wolinsky’s testimony related to FOM’s past payment of performance royalties.

D. The Trial Court’s Ruling and Judgment

After a hearing, the trial court issued an order granting FOM’s motion for summary judgment. In its analysis, the court agreed with FOM that paragraph 7 impliedly excluded performance royalties from the payment due under paragraph 22: “The language of paragraph 7 . . . specifically excludes, in three separate subparagraphs, public performance royalties from being shared with the ‘writer,’ i.e., plaintiffs. It would be difficult to imagine a more clear mutual intention of the
On September 16, 2016, the court entered judgment in FOM’s favor.

**DISCUSSION**

Plaintiffs argue that the trial court erred in concluding the 1972 Agreement is not reasonably susceptible to their proposed interpretation. Plaintiffs assert that the text of the document and the uncontroverted extrinsic evidence demonstrate that their proposed interpretation is not only reasonable, but also the correct interpretation of the parties’ agreement.

**A. Standard of Review and Applicable Law**

1. **Standard of review**

“Summary judgment is appropriate ‘if all the papers submitted show that there is no triable issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.’ [Citation.] . . . [¶] Our review is de novo. [Citation.] We liberally construe the opposing party’s evidence and resolve all doubts in favor of the opposing party. [Citation.] We consider all evidence in the moving and opposition papers, except that to which objections were properly sustained.” *(Jacobs v. Coldwell Banker Residential Brokerage Co. (2017) 14 Cal.App.5th 438, 443.)*

2. **Rules governing the interpretation of contracts**

“The rules governing the role of the court in interpreting a written instrument are well established. The interpretation of a contract is a judicial function. [Citations.] In engaging in this function, the trial court ‘giv[es] effect to the mutual intention of the parties as it existed’ at the time the contract was executed. [Citation.] Ordinarily, the objective intent of the contracting parties is a legal question determined solely by reference to the contract’s terms. [Citation.]” *(Wolf v. Walt Disney Pictures & Television (2008) 162 Cal.App.4th 1107, 1125-1126 (Wolf).)*

“The court generally may not consider extrinsic evidence of any prior agreement or contemporaneous oral agreement to vary or contradict the clear and unambiguous terms of a written, integrated contract. [Citations.] Extrinsic evidence is admissible, however, to interpret an agreement when a material term is ambiguous. [Citations.]” *(Wolf, supra, 162 Cal.App.4th at p. 1126; see also Pacific Gas & Electric Co. v. G.W. Thomas Drayage & Rigging (1968) 69 Cal.2d 33, 39-40 [if extrinsic evidence reveals that apparently clear language in the contract is, in fact, “susceptible to more than one reasonable interpretation,” then extrinsic evidence may be used to determine the contracting parties’ objective intent].)*

“The interpretation of a contract involves ‘a two-step process: First the court provisionally receives (without actually admitting) all credible evidence concerning the parties’ intentions to determine “ambiguity,” i.e., whether the language is “reasonably susceptible” to the interpretation urged by a party. If in light of the extrinsic evidence the court decides...”
the language is “reasonably susceptible” to the interpretation urged, the extrinsic evidence is then admitted to aid in the second step – interpreting the contract. [Citation.] [Citation.]” (Wolf v. Superior Court (2004) 114 Cal.App.4th 1343, 1351 (Wolf II) [citing and quoting Winet v. Price (1992) 4 Cal.App.4th 1159, 1165 (Winet); see also Wolf, supra, 162 Cal.App.4th at p. 1126.)

“When there is no material conflict in the extrinsic evidence, the trial court interprets the contract as a matter of law. [Citation.] This is true even when conflicting inferences may be drawn from the undisputed extrinsic evidence [citations] or that extrinsic evidence renders the contract terms susceptible to more than one reasonable interpretation. [Citations.] If, however, there is a conflict in the extrinsic evidence, the factual conflict is to be resolved by the jury. [Citations.]” (Wolf, supra, 162 Cal.App.4th at pp. 1126-1127; see id. at p. 1134 (“that extrinsic evidence may reveal an ambiguity subjecting a contract to more than one reasonable interpretation does not mean resolution of that ambiguity is necessarily a jury question. Absent a conflict in the evidence, the interpretation of the contract remains a matter of law”).)

On appeal, a “trial court’s ruling on the threshold determination of ‘ambiguity’ (i.e., whether the proffered evidence is relevant to prove a meaning to which the language is reasonably susceptible) is a question of law, not of fact. [Citation.] Thus[,] the threshold determination of ambiguity is subject to independent review. [Citation.]” (Winet, supra, 4 Cal. App.4th at p. 1165)

“The second step – the ultimate construction placed upon the ambiguous language – may call for differing standards of review, depending upon the parol evidence used to construe the contract.” (Winet, supra, 4 Cal.App.4th at pp. 1165-1166.) However, where no extrinsic evidence was admitted, or the extrinsic evidence is not conflicting, “the appellate court will independently construe the writing.” (Id. at p. 1166; see also Department of Forestry & Fire Protection v. Lawrence Livermore National Security, LLC (2015) 239 Cal.App.4th 1060, 1066 [“On appeal from a summary judgment based on a trial court’s interpretation of a contract, we are not bound by that interpretation . . . if there is no extrinsic evidence concerning its interpretation, [or] . . . if there is no conflict in such evidence”].)

B. The 1972 Agreement is Reasonably Susceptible to Plaintiffs’ Interpretation

The first question we must address is whether the 1972 Agreement “is ‘reasonably susceptible’ to the interpretation urged by [plaintiffs]. If it is not, the case is over. [Citation.]” (Southern Cal. Edison Co. v. Superior Court (1995) 37 Cal. App.4th 839, 847 (Southern Cal. Edison.) After provisionally allowing plaintiffs’ extrinsic evidence (except for those portions to which objections were sustained), the trial court concluded that the revenue-sharing provision in paragraph 22 could not be reasonably interpreted to include income FOM had received from performance royalties. In support, the court relied on language in paragraph 7 stating that plaintiffs were not entitled to share in any sums FOM had received from a PRO for performance royalties.

We disagree with the trial court’s threshold determination. As the plaintiffs note, paragraph 22 of the agreement does not contain any language indicating that performance royalties are to be excluded from “Composition Gross Receipts,” which defines the pool of income that is subject to plaintiffs’ revenue sharing rights. Instead, paragraph 22 states that Composition Gross Receipts consists of “all monies actually earned and received from the sale, lease, license, disposition or other turning to account of rights in the Compositions . . . .” FOM does not dispute that performance royalties are a form of “money . . . earned” from the sale or license of the compositions that are subject to the 1972 Agreement. Thus, considered in isolation, the language of paragraph 22 supports the plaintiffs’ interpretation of the agreement.

FOM contends, and the trial court agreed, that despite the absence of any exclusionary language in paragraph 22, the text of paragraph 7 nonetheless shows the parties intended to exclude performance royalties from paragraph 22’s revenue-sharing provision. Paragraph 7 sets forth the “royalties” FOM must pay plaintiffs “with respect to each composition.” The paragraph requires FOM to pay a 50 percent royalty for most forms of income generated from the exploitation of the composition, including mechanical rights, synchronization rights and foreign income, but clarifies “that the Writer shall not be entitled to share in any sum or sums received by the Publisher from [any PRO] which pays performance fees directly to songwriters.” Paragraph 7(f) then reiterates that FOM shall not be required to pay “royalties earned by reasons of the public performances of the composition; said royalties being payable only by [the Writer’s PRO].”

The language in paragraph 7 does not render plaintiffs’ proposed interpretation of the 1972 Agreement unreasonable. Paragraph 7 and paragraph 22 address two distinct types of payments that FOM must pay to plaintiffs: royalty payments (paragraph 7) and a revenue-sharing payment (paragraph 22). The language in paragraph 7 that precludes plaintiffs from sharing in FOM’s “performance income” can be reasonably interpreted as applying only to the type of payment described in paragraph 7, namely royalty payments. Paragraph 7 does not include any language stating that the exclusion of “performance fees” extends to paragraph 22’s revenue-sharing provision. Moreover, the first clause of paragraph 22 directs that the revenue-sharing payment described therein is to be paid “in addition to the royalties provided for in Paragraph 7.” The fact that plaintiffs are not entitled to receive royalty payments on FOM’s performance income does not necessarily preclude them from receiving a portion of FOM’s performance income based on the revenue-sharing payment described in paragraph 22, which is to be paid “in addition to” whatever royalties are due under paragraph 7.

FOM argues that plaintiffs’ proposed interpretation of paragraph 22 would render “paragraph 7’s specific exclusion
of . . . public performance royalties . . . meaningless.” As explained above, however, under plaintiffs’ interpretation, the exclusionary language in paragraph 7 serves to clarify that while FOM must pay plaintiffs a 50 percent royalty on most forms of income, the performance income FOM receives from its PRO is not subject to that requirement. Paragraph 22, in turn, provides that “in addition to” the royalties described in paragraph 7, plaintiffs are entitled to a certain share (30 percent after various administrative costs and fees are deducted) of “all monies [FOM] actually earned and received” from the sale or licensing of the music compositions. Thus, the language in paragraph 7 and 22 are both given effect: the former provision establishes that FOM does not have to pay plaintiffs a 50 percent royalty on the performance income it receives from its PRO, while the latter provision establishes that such income is nonetheless subject to the revenue-sharing formula set forth in paragraph 22.

Plaintiffs’ proposed interpretation is also supported by their extrinsic evidence. First, as explained in Clainos’s declaration, prior to signing the 1972 Agreement, the parties entered into a MOA that summarized the terms of what they had agreed to. The MOA expressly states that the signatories agreed that it “reflect[ed]” the terms of the agreement that were to be included in their “formal contract[].” Paragraph 3(b) of the MOA sets forth the royalties FOM agreed to pay plaintiffs, and includes language clarifying that plaintiffs were to obtain “any and all performance moneys” from ASCAP, and not from FOM. Paragraph 3(e) of the MOA sets forth the revenue participation payment, directing that “in addition to the foregoing, the writer shall receive . . . 30% of [FOM’s] share of publisher income (after deduction for collection fees, direct costs and administration fees).” Paragraph 3(e) has no language excluding income that FOM received from performance royalties. Considered together, paragraph 3(b) and 3(e) support plaintiffs’ assertion that the parties intended FOM would not be required to pay royalties on performance income, but would nonetheless be required to include such income when calculating the revenue-sharing payment.

Nicholas Clainos’s declaration lends further support to plaintiffs’ interpretation. Clainos asserted that during his negotiations of the 1972 Agreement with Steve Gold, then a co-owner of FOM, Gold specifically acknowledged that the parties had agreed the revenue-sharing provision would apply to “100% of all revenue the publisher received, including the publisher’s public performance revenue.” Clainos further asserted that he and Gold discussed that, as used in paragraph 22, the term “‘all monies’ in the definition of ‘Composition Gross Receipts’ … encompassed [FOM’s] share of public performance revenues that were otherwise excluded in connection with the calculations under paragraph 7.”

Michael Perlstein’s expert testimony regarding industry usage and custom also provides support for plaintiffs’ interpretation. According to Perlstein, at the time the 1972 Agreement was negotiated, it was customary in the music publishing industry that a provision entitling a writer to a share of the publisher’s income would include income generated from performance royalties. Indeed, Perlstein noted that in his 50 years of drafting, negotiating and evaluating music publishing agreements, he had never seen a single agreement that contained a revenue sharing provision that excluded performance royalties. This testimony suggests plaintiffs’ proposed interpretation accords with the industry customs and practices that were in effect at the time the contract was negotiated.

Finally, the plaintiffs submitted accounting statements showing that, as recently as 2011 and 2013, FOM had paid plaintiffs a share of the income it derived from performance royalties. These accounting statements provide circumstantial evidence that FOM believed the 1972 Agreement entitled plaintiffs to share in performance royalties, which again accords with plaintiffs’ proposed interpretation. (See Universal Sales Corp. v. California Press Mfg. Co. (1942) 20 Cal.2d 751, 761 [“when a contract is ambiguous, a construction given to it by the acts and conduct of the parties with knowledge of its terms, before any controversy has arisen as to its meaning, is entitled to great weight”]; Enos v. Armstrong (1946) 75 Cal.App.2d 663, 669 [“where the terms are . . . capable of more than one reasonable construction, the practical construction put upon the instrument by the parties thereto, as evidenced by their conduct under it, furnishes one of the most reliable means of arriving at its meaning and their intention when executing it”].)

In sum, contrary to the trial court’s conclusion, the language of the 1972 Agreement, considered in conjunction with plaintiffs’ extrinsic evidence, demonstrates that the contract is reasonably susceptible to the plaintiffs’ proposed interpretation.

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7. In its written order, the trial court concluded Perlstein’s testimony amounted to his own “legal opinions as to the meaning of paragraph 22,” and was therefore not relevant to the interpretation of the contract. Perlstein, however, did not merely relate his subjective interpretation of paragraph 22. Rather, he provided expert testimony regarding the music publishing industry’s customs and usage pertaining to revenue-sharing provisions such as the one set forth in paragraph 22. Specifically, Perlstein asserted that such provisions customarily applied to all forms of publisher revenue, including performance royalties the publisher obtains from a public rights organization. This custom and usage evidence was relevant to aid in the interpretation of the contract. (See Howard Entertainment, Inc. v. Kudrow (2012) 208 Cal.App.4th 1102, 1119-1121 [trial court erred in excluding expert declaration stating that management agreements in the entertainment industry customarily entitled managers to post-termination compensation for any engagements that were entered into while the agreement was in effect]; Heyter Trucking, Inc. v. Shell Western E&P, Inc. (1993) 18 Cal.App.4th 1, 20 ["parol evidence of custom and usage is similarly admissible to interpret the written words"]).

8. As discussed above (see ante, pp. 15-16, 18), plaintiffs’ expert in music accounting, Fred Wolinsky, submitted these accounting statements in support of his declaration stating that FOM had paid plaintiffs a share of performance royalties for decades, before suddenly changing course in 2014. The trial court sustained objections to Wolinsky’s “course of performance” testimony, but overruled objections to the actual accounting statements he submitted with the declaration.
C. Plaintiffs’ Interpretation Is More Reasonable than the Interpretation FOM Has Proposed

Having concluded that the parties’ agreement is reasonably susceptible to plaintiffs’ proposed interpretation, we move to the “second step – interpreting the contract.” (Wolf II, supra, 114 Cal.App.4th at p. 1351; see also Southern Cal. Edison, supra, 37 Cal.App.4th at pp. 847-848 (“If the court decides the language is reasonably susceptible to the interpretation urged, the court moves to the second question: what did the parties intend the language to mean?”).) Because the parties’ summary judgment materials do not contain any conflicting extrinsic evidence (FOM having elected not to submit any extrinsic evidence), we interpret the contract as a “question of law subject to our independent construction.” (Winet, supra, 4 Cal.App.4th at p. 1160; Wolf, supra, 162 Cal.App.4th at p. 1134 (“Absent a conflict in the evidence, the interpretation of the contract remains a matter of law”).)

“The goal of contractual interpretation is to determine and give effect to the mutual intention of the parties. [Citations.]” [Citation.] Thus, “a court’s paramount consideration ... is the parties’ objective intent when they entered into [the contract].” [Citations.]” [Citation.] ‘A contract must be so interpreted as to give effect to the mutual intention of the parties as it existed at the time of contracting, so far as the same is ascertainable and lawful.’ [Citation.] “‘If a contract is capable of two constructions courts are bound to give such an interpretation as will make it lawful, operative, definite, reasonable, and capable of being carried into effect...’” [Citations.]’ [Citation.]” (Khavarian Enterprises, Inc. v. Commline, Inc. (2013) 216 Cal.App.4th 310, 318.) “In sum, courts must give a ‘“reasonable and commonsense interpretation”’ of a contract consistent with the parties’ apparent intent. [Citation.]” (Department of Forestry & Fire Protection v. Lawrence Livermore National Security, LLC (2015) 239 Cal.App.4th 1060, 1066.)

Based on the language of the parties’ agreement, and aided by the extrinsic evidence in the record, we conclude that plaintiffs’ interpretation of the 1972 Agreement is the most reasonable. As explained above, paragraph 22 does not include any language indicating that income derived from performance royalties is to be excluded from “Composition Gross Receipts,” the base amount used to determine plaintiffs’ revenue sharing payment. Instead, Composition Gross Receipts is specifically defined to include “all monies actually earned and received” in connection with the sale and licensing of the music compositions. Had the parties intended to exclude performance royalties from Composition Gross Receipts, we expect that they would have included language to that effect.

Paragraph 7’s exclusion of performance-based income from FOM’s royalty payment requirements does not compel a different result. Paragraph 7 describes the royalties FOM is required to pay plaintiffs on various types of income, and expressly excludes royalties on performance-based income. Paragraph 22, in contrast, describes a separate revenue partic-