Riverisland Cold Storage, Inc. v. Fresno-Madera Production Credit Association

The California Supreme Court overrules seventy-five year old precedent and holds that a litigant may offer evidence of a prior oral agreement that contradicts a written contract.

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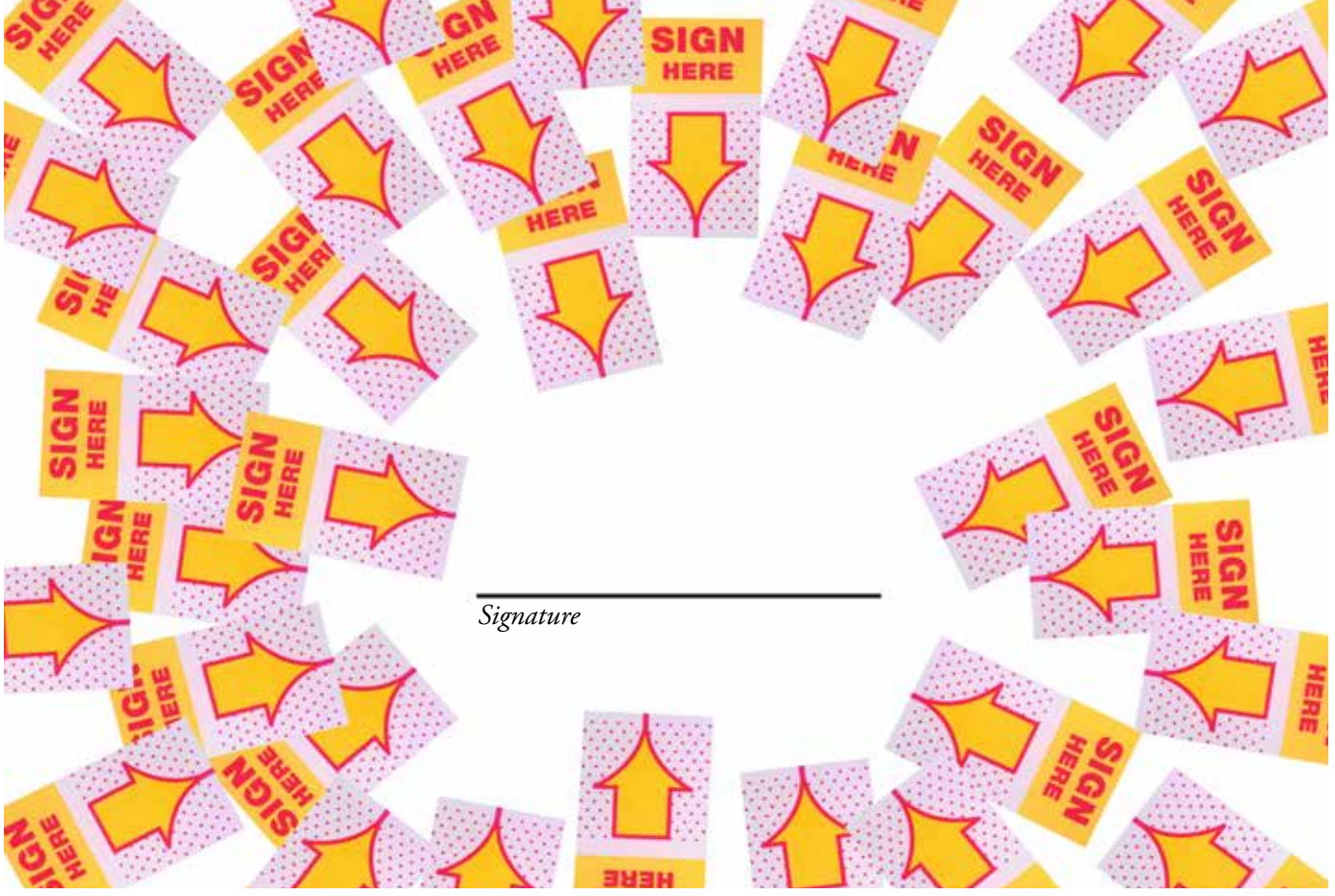
We have all heard the old adages, "get it in writing" and "read the fine print." What they mean is that when we sign a contract, we are bound by its terms. Nothing more, nothing less. In law, this concept is represented by the parol evidence rule. The rule is based on the principle that a written contract supersedes statements made during negotiations. Under the rule, if a litigant is a party to a valid written contract, he or she cannot offer evidence of a prior or oral agreement to contradict it: "The parol evidence rule protects the integrity of written contracts by making their terms the exclusive evidence of the parties' agreement." *Riverisland Cold Storage, Inc. v. Fresno-Madera Production Credit Assn.*, 55 Cal. 4th 1169, 1171 (2013); Cal. Civ. Proc. Code § 1856; Cal. Civ. Code § 1625. But under the fraud exception, if the issue is whether the written contract is valid or tainted by fraud, the parol evidence rule does not apply. Cal. Civ. Proc. Code § 1856 (f) and (g). In other words, a litigant may generally offer evidence to prove a contract is not valid or the result of fraud.

Can a litigant who seeks to invalidate a written contract offer evidence of a prior or oral agreement that contradicts it? The California Supreme Court recently addressed this question in *Riverisland Cold Storage, Inc. v. Fresno-Madera Production Credit Association*. 55 Cal. 4th at 1172, 1182.

In *Riverisland*, the plaintiff borrowers filed a case against the defendant lender for fraud, negligent misrepresentation, recission, and reformation. The plaintiffs admitted that they did not read, but signed, a contract with the defendant. The plaintiffs claimed that, at the time of the signing, the defendant lied about the terms contained in the contract, which induced the plaintiffs to sign. The Fresno County Superior Court granted the defendant's summary judgment motion. The court found that the plaintiffs' oral evidence of misrepresentation was inadmissible pursuant to the parol evidence rule. The court rejected the plaintiffs' argument that the evidence was admissible because it was offered to prove fraud and thus invalidate the written contract.



The Fifth District Court of Appeal reversed. The court held that under the fraud exception, parol evidence of a contemporaneous factual misrepresentation of the terms contained in a written agreement is admissible. The court acknowledged the case of *Bank of America National Trust and Savings Association v. Pendergrass*, 4 Cal. 2d 258, 263–64 (1935), in which the California Supreme Court held that oral evidence that directly contradicts a provision in an agreement does not fall under the fraud exception to the parol evidence rule and is not admissible. However, the Fifth District concluded that *Pendergrass* was not controlling in *Riverisland*. The court found that the evidence discussed in *Pendergrass* was distinguishable from that in *Riverisland*. According to the court, *Pendergrass* addressed promissory fraud, but *Riverisland* concerned factual misrepresentation of terms of an agreement.

The California Supreme Court affirmed. However, rather than distinguish *Pendergrass* like the Fifth District did, the California Supreme Court overruled it.

For More Than Seventy-Five Years, a Litigant Could Not Offer Evidence That Contradicted a Written Contract

In 1935, in *Pendergrass*, the California Supreme Court placed a limit on evidence that could be used to prove fraud. *Id.* The court held that a litigant could not offer any evidence that contradicted a term in a written contract, even to prove fraud:

> Our conception of the rule which permits parol evidence of fraud to establish the invalidity of the instrument is that it must tend to establish some independent fact or representation, some fraud in the procurement of the instrument or some breach of confidence concerning its use, and not a promise directly at variance with the promise of the writing. *Id.* at 263.

The court explained that to hold otherwise would be to nullify the parol evidence rule. The court was concerned that anytime a litigant wanted to invalidate a written con-

tract he or she would simply claim that there had been a prior oral agreement to the contrary. At the time, the court believed it was preventing future "frauds and perjuries" on and in the court. *Id.*

Now a Litigant May Offer Any Evidence to Prove Fraud, Even If It Contradicts a Written Contract

This year, in *Riverisland*, the California Supreme Court removed the limit on fraud evidence. 55 Cal. 4th at 1172, 1182. The court overruled *Pendergrass* and held that a litigant may offer any evidence, including a prior oral agreement, to prove fraud, even if it contradicts a term in a written contract: "[W]e overrule *Pendergrass* and its progeny . . . . '[I]t was never intended that the parol evidence rule should be used as a shield to prevent the proof of fraud.'" *Id.* at 1182.

The court explained that *Pendergrass* was bad public policy. The court found that *Pendergrass* ignored that fraud invalidates a written contract:

> *Pendergrass* failed to account for the fundamental principle that fraud undermines the essential validity of the parties' agreement. When fraud is proven, it cannot be maintained that the parties freely entered into an agreement reflecting a meeting of the minds. *Id.*

The court further found that rather than preventing "frauds and perjuries," *Pendergrass* may have encouraged fraud:

> Underlying the objection that *Pendergrass* overlooks the impact of fraud on the validity of an agreement is a more practical concern: its limitation on evidence of fraud may itself further fraudulent practices. . . . "Oral promises made without the promisor's intention that they will be performed could be an effective means of deception if evidence of those fraudulent promises were never admissible merely because they were at variance with a subsequent agreement.'" *Id.* at 1177.

The court also explained that *Pendergrass* was bad law. According to the court, "*Pendergrass* departed from established California law at the time it was decided, and neither acknowledged nor justified the abrogation." *Id.* at 1172. Moreover, the court pointed out that when *Pendergrass* was decided, the governing statute did not limit fraud evidence the way that *Pendergrass* did, and when the legislature subsequently revised the statute, it did not include the *Pendergrass* limitation. *Id.* at 1174–76; 1178–80 (referring to Cal. Civ. Proc. Code § 1856). The court noted that *Pendergrass* "conflicts with the doctrine of the Restatements, most treatises and the majority of our sister-state jurisdictions." Id. Finally, the court found that *Pendergrass* "is difficult to apply. . . . The functionality of the *Pendergrass* limitation has been called into question by the vagaries of its interpretations in the Courts of Appeal." *Id.* 1172–80.

Significance

Riverisland permits a litigant who wants to invalidate a written contract to claim fraud and prove it with a contradictory prior oral agreement. Under the opinion, a party to a contract will not necessarily be held responsible for understanding its written terms before signing it and may be protected if the drafter misrepresents the terms. However, the court did not address to what extent a party to a contract is responsible for its contents nor to what extent the party is protected from the drafter. The court merely noted that fraud requires justifiable reliance on a misrepresentation and declined to discuss how failure to read a contract might affect reliance.

More importantly, *Riverisland* shows litigants how to defeat old precedent against them. Litigants should argue that the case law, no matter how longstanding, is bad policy, poorly reasoned, and inconsistent with governing statutes, the restatements, treatises, and case law in most other states, as well as difficult for courts to consistently interpret. A good case for reconsideration is one where "a decision departed from an established general rule without discussing the contrary authority." *Id.* at 1180.

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