NO. 90351-4
SUPREME COURT
OF THE STATE OF WASHINGTON

NO. 42864-II
COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION II

BULLIVANT HOUSER BAILEY, P.C., and RICHARD G. MATSON,

Defendants / Respondents,

v.

CLARK COUNTY FIRE DISTRICT NO. 5 and AMERICAN ALTERNATIVE INSURANCE CORPORATION,

Plaintiffs / Petitioners.

DEFENDANTS' / RESPONDENTS' ANSWER TO PETITION FOR REVIEW

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I. IDENTITY OF THE RESPONDENTS

Respondents, defendants below, are Bullivant Houser Bailey, P.C., a Washington Professional Services corporation, and Richard G. Matson, a shareholder of the Bullivant firm (hereinafter "defendants," "attorney defendants" or "respondents").

II. THE COURT OF APPEALS DECISION

Petitioners request this Court to deny review of the decision terminating review by Division II of the Washington Court of Appeals in Appeal No. 42864-4-II, *Clark County Fire District No. 5, et. al., Appellants v. Bullivant Houser Bailey, P.C. and Richard G. Matson, Respondents* (---- Wn.2d ----, 324 P.3d 723, (2014)). The court's opinion was entered for publication on April 24, 2014. A copy of the published opinion was included in the Appendix attached to the Petition.

III. STATEMENT OF THE CASE

This case was initially filed in Clark County Superior Court in August 2009. [CP 295-302.] The complaint asserted claims for professional negligence. [CP 300-301.]

Defendants Bullivant Houser Bailey and Richard Matson filed an Answer responding to the complaint. [CP 304-311.] Noting that one of the plaintiffs, AAIC, was the liability insurer of its clients, and recognizing that Washington law does not impose a legal duty on insurance defense

attorneys to the insurer who assigns them to represent and defend the insurer's insureds defendants alleged an affirmative defense of lack of standing in their Answer. [CP 310.]

In September 2011, plaintiffs filed a motion for partial summary judgment requesting in part, that the trial court dismiss the defendants' affirmative defense of AAIC's lack of standing. [CP 327, *et seq.*]

Defendants thereafter filed a Response including a request for summary judgment dismissal of AAIC's claims based on a lack of standing. [CP 346, *et seq.*]

Oral Argument was heard in Clark County Superior Court in October 14, 2011. The Trial Court entered an order dismissing the claims of AAIC against the defendants on the ground that AAIC has no legal standing as the insurance carrier of Clark County Fire District No. 5 to bring claims for legal malpractice against the defendants. [CP 695-699.]

The order of the trial court was certified under CR 54(b), and AAIC filed this Appeal prior to the commencement or conclusion of trial in the Superior Court.

On December 5, 2011, plaintiffs/respondents filed an appeal of the trial court decision in Division II of the Washington Court of Appeals on the issues relating to defendants' affirmative defense of AAIC's lack of standing. Briefs were submitted in early 2012.

Briefing was completed and oral arguments on the consolidated appeal were heard in Division II of the Court of Appeals on January 16, 2014.

On April 24, 2014, the Court of Appeals entered its ruling and certified its opinion for publication.

IV. ARGUMENT

A. The Lower Court Dismissals of AAIC's Claim Were Proper

Division II of the Washington Court of Appeals, as the trial court before it, fully considered the extensive arguments brought by plaintiff/ petitioner American Alternative Insurance Co. ("AAIC") on the question of its lack of standing to pursue a claim for legal malpractice against the defendant/respondent attorneys in this case.

Both the Court of Appeals, as the trial court before it, dismissed AAIC's complaint for legal malpractice holding, as a matter of law, that in Washington, an attorney representing an insured defendant has no legal duty relating to legal services, to the insurance carrier who assigns that attorney to defend its insured as required by the terms of its insurance contract with the insured defendant.

The Court of Appeals dismissed the complaint in recognition of and in compliance with with the clear governing law recently established by this Court in *Stewart Title Guar. Co. v. Sterling Sav. Bank* 178 Wn.2d

561, 311 P.3d 1 (2013).

Having unsuccessfully argued its positions twice below, the petitioner now urges this Court to ignore those determinations and conduct a third review of the matter, on the erroneous grounds that the lower court rulings implicate provisions of RAP 13.4, which establishes the criteria for Washington Supreme Court review.

B. Petitioner Does Not Establish That the Provisions of RAP 13 Which Establish the Basis for Supreme Court Review Are Satisfied, and the Petition Must Be Denied

Petitioners erroneously contend that the Court of Appeals ruling upholding the trial court dismissal on the basis of this Courts' unambiguous rule articulated in *Stewart Title*, satisfy the following provisions of RAP 13.4(b) in that the decision:

> (1) . . . is in conflict with a decision of the Supreme Court (specifically *Stewart Title, supra,* and *Trask v. Butler,* 123 Wash.2d 835, 872 P.2d 1080 (1994));
>
> (4) . . . involves an issue of substantial public interest that should be determined by the Supreme Court (but nothing that has not been previously disposed of by the holding in *Stewart Title).*

Neither of those elements, which are required to establish grounds for such discretionary review, are established by the Petition. Petitioner's continued dissatisfaction with the Trial Court and Court of Appeals' resolutions of the case does not qualify the case for discretionary review under RAP 13.4(b).

C. The Court of Appeals Decision Based on the Rule Recently Established by This Court in *Stewart Title v. Sterling Savings* Bank Does Not Conflict with That Decision, the Decision in *Trask v. Butler*, or Any Other Washington Supreme Court Case

Petitioner's contention that Division Two's ruling is in conflict with this Court's decision in either *Stewart Title v. Sterling Bank* or *Trask v. Butler* is demonstrably erroneous, if only by a simple reading of the *Stewart Title* opinion.

In *Stewart Title*, this Court determined that the "tri-partite" relationship between insurance carrier, insured and counsel assigned by the carrier to defend the insured from a third-party claim, is fundamentally legally incompatible with the existence of legal duty on the part of the assigned defense attorney to the "non-client" insurer necessary to support a claim for legal malpractice by the carrier against the attorney. This Court held that "[t]he fact that an insurer's and insured's interests happen to align in some respects—though perhaps not in all respects ... — does not by itself show that the attorney or client intended the insurer to benefit from the attorney's representation of the insured." *Stewart Title Guar. Co. v. Sterling Sav. Bank*, at 178 Wn.2d 567.

The petitioner re-argues its positions that were rejected by the lower courts in this case on a number of issues related to the analysis of whether a "non-client" can claim that a lawyer who does not represent it,

owes it a legal duty to the "non-client" so as to support a claim for malpractice based on the legal services performed. These issues include: the status of a carrier as a claimed "beneficiary" of an assigned defense counsel's legal services provided to its actual client, the insured; a mis-directed argument that if the insurer in the tri-partite relationship has no right to sue the assigned defense counsel for acts involved in the attorney's representation of the insured there exists no "remedy"; and, disingenuously, that forcing an attorney who is representing an insured while simultaneously responsible to the insured's carrier under a separate legal duty, to weave through the resultant minefield of potential, or actual, conflicts of interest, "does not burden the profession."

Petitioner's arguments ignore the principal foundation of this Court's resolution of the same issues in *Stewart Title* and are, in effect, nothing more than red herrings designed only to expand the focus of the Court's review here beyond its superseding precedential ruling in *Stewart Title*.

The lower court rulings in this case, and the decision in *Stewart Title* are all consistent with the axiomatic rule affecting the tri-partite relationship expressed by this Court many years ago, that in providing a defense to its insured an insurer holds a separate legal obligation of good faith which prohibits it from placing its own interests – whatever the

nature – above the interests of the insured. *Tank v. State Farm Fire & Cas. Co.* 105 Wn.2d 381, 387-88, 715 P.2d 1133 (1986).

In *Stewart Title,* this Court specifically examined the fundamental aspects of the "tri-partite" relationship in the context of its prior decision in *Trask v. Butler* which articulated a test for determining the existence of a lawyer's duty to a non-client. *Trask v. Butler*, 123 Wn.2d at 842-843.

The first of the six *Trask* factors is the most significant and represents the "threshold" inquiry; if the attorney's representation was not specifically intended to benefit the non-clients, or if any "benefit" derived by the non-client was merely "incidental" in nature, the non-client has no legal standing to sue the attorney for malpractice based on his representation of actual client. *Leipham v. Adams*, 77 Wn. App. 827, 832, 894 P.2d 576 (1995) (citing *Trask*, at 123 Wn.2d 842-43).

In *Stewart Title*, the court said:

> [In *Trask*] we explained that the first factor is the "primary inquiry" in determining an attorney's liability to third parties. [citation omitted]. We further explained that "under the modified multi-factor balancing test, the threshold question is whether the plaintiff is an intended beneficiary of the transaction to which the advice pertained" and that "no further inquiry need be made unless such an intent exists." [123 Wn. 2d] at 843, 872 P.2d 1080."

Stewart Title Guar. Co. v. Sterling Sav. Bank at 178 Wn.2d 566.

The *Stewart Title* court specifically concluded that an insurer could not be held to be the "intended beneficiary" of legal services provided by the counsel the insurer assigned to defend its own insured, if only because to do so would violate "the settled rule of law" as articulated in the Washington Rules of Professional Responsibility (hereinafter "RPC"), that, "A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services." *Id.* at 178 Wn.2d 568 [citing RPC 5.4(c)]

There is nothing new, novel or groundbreaking in the facts of this case which separates it from, or places it in conflict with the prior holdings of this Court in either *Stewart Title*, or *Trask v. Butler*. Distilled to its meaningful content, Petitioner's argument here is based on the single idea that because AAIC did not issue a "reservation of rights" to its insured Clark County Fire District No. 5, the interests of AAIC and its insured were purportedly so "aligned," that there must be no conflict of interest to a lawyer representing both the insured and the insurer which would necessarily preclude a finding under *Trask* that the insurer is an "intended beneficiary". Thus, petitioner blithely rejects the specific contrary holding by the *Stewart Title* court which categorically rejected the same argument.

> "The alignment of interests is insufficient to find a duty running from [the assigned defense attorney] to [the non-client insurer] for purposes of a malpractice claim. [The non-client] argues, ... that as long as there is no actual conflict of interest between an insurer and its insured, a non-client insurer is presumed to be an intended beneficiary and "can bring a claim for malpractice" against its insured's attorney. [Appellate citation omitted] Under [the non-client insurer's] analysis, unless there is an actual and demonstrable conflict of interest, an insurer may always sue its insured's attorney for malpractice under *Trask*.
>
> **We reject that analysis**."

Stewart Title Guar. Co. v. Sterling Sav. Bank, 178 Wn.2d 561 at 567 (emphasis added).

The salient facts of this case are no different than the principal facts forming the basis of this Court's decision in *Stewart Title*, which in and of itself, incorporated an analysis of *Trask v. Butler* as applied to the fundamental relationships and policies affecting the "tri-partite" relationship.

D. *Stewart Title* Correctly Determined That the Tri-Partite Relationship Precludes the Insurer as an "Intended Beneficiary" of the Defense Counsel's Representation of Its Client, the Insured

Stewart Title established that the fundamental relationships between an insurer, its insured, and, counsel assigned to defend the insured are inimical to the creation of a duty by the attorney to the insurer. Petitioner's attempt to create some unique factual relationship here between insurer AAIC and respondents in their role as defense counsel for

insured Clark County Fire District No. 5 completely ignore the decision of this Court in *Stewart Title* that because of the inherent conflicting interests in the relationship, such factual distinctions are irrelevant to the question of the existence of duty.

In making its decision, the Court of Appeals noted that AAIC is an insurer, that AAIC insured a party who was the object of a liability claim, and that respondents were assigned by AAIC to represent the insured as its client – the Court of Appeals acknowledged the existence of the classic "tri-partite" relationship. The Court of Appeals then read the clear holdings of this Court in *Stewart Title* and applied its rule of Washington law that the tri-partite relationship inherently precludes the idea that the carrier is an "intended beneficiary" of the attorneys' representation of the insured (even where there the carrier did not issue a "reservation of rights" to dispute coverage).

E. Petitioner's Argument Asserting That the *Stewart Title* Rule Creates an "Empty Remedy" Is Invalid, Illogical and Does Not Govern This Court's Determination Whether to Grant This Petition

Finally, AAIC argues is that this Court should accept review because the Court of Appeals' decision is wrong because it supposedly allows a situation where there is a "right" with no "remedy". This argument is mis-directional at best. First, in lamenting that if the

insurance carrier is unable to "cash in" by not being entitled under existing law to sue the lawyer it appointed to defend its insured, the petitioner again pre-supposes that the carrier is legally entitled to a recovery from any third party for its contractually required performance under the insurance contract. This disingenuously puts "the cart before the horse."

The *Stewart Title* rule conclusively decides the issue of whether the insurer has a "right" against the assigned defense attorney to claim a breach of a representational duty, in the negative. This lack of any legal "right" against the defense attorney is the basis of petitioner's true aggravation. AAIC apparently made a poor risk-analysis decision in insuring Clark County Fire District No. 5, the result of which was that it had to make indemnity payments to the underlying plaintiffs because of that decision. Now AAIC wants someone else to pay for its mistaken risk analysis.

To the extent it has any merit, petitioner's theory is founded on the idea that a "remedy" is for the purpose of making an injured party whole. The fact is, if there was any professional negligence, respondents' client, Clark County Fire District No. 5, is whole. It is whole because of its foresight in making a contractual agreement with AAIC to be made whole and the fact that it can bring a claim for malpractice against its lawyers.

Petitioner's breathless argument that the lawyers "will receive a windfall" unless the carrier is allowed to attempt to recover its contractually agreed indemnity payments paid on behalf of its insured, from a third party, is a misconstruction of reality. The attorney recovers nothing if a carrier is obligated to perform its separate contractual responsibilities on behalf of its insured. The attorney is not a "winner" and perhaps more fundamentally, the insurer is not a "loser" – at least in the sense that petitioner asserts.

If the carrier were allowed to bring a claim against the defense counsel to recover monies it paid due to its separate contractual obligations to the insured, any "windfall" goes to AAIC. AAIC simply wants a source to replace the "loss" which they had willingly previously contracted to lose. Paying for the liabilities incurred by their insured is what AAIC contracted to do. "It must not be forgotten that the purpose of insurance is to insure...." *Phil Schroeder, Inc. v. Royal Globe Ins. Co.*, 99 Wn.2d 65, 69, 659 P.2d 509 (1983).

The simple fact that this appeal is being made in an effort to create new law demonstrates that AAIC knew at the time it issued an insurance policy to Clark County Fire District No. 5 that in Washington, there was no prospective remedy against its insured's attorneys to recoup its

payments of settlements or judgments made to satisfy its contractual obligations to indemnify Clark County for its liabilities.

The law in Washington has never been that the insurance defense carrier has the standing to recover in malpractice from the assigned attorney. As a sophisticated commercial entity, AAIC knew or should have known that it had no legal standing to recover any monies paid on behalf of their insured to a third party due to an adverse judgment.

Petitioner has inverted the issue of "rights and remedies." A tort plaintiff is entitled to compensation based only on the defendant's tortious act. Where there is no duty there is no tort. Where there is no tort there is no right to compensation. Petitioner's talk of an "empty" remedy ignores the reality that the lawyer's actual client (as opposed to the third party to which the attorney has no legal duty) does have a right to pursue his counsel for the sum of money that will put himself in the position but for the defendant's tortious act.

AAIC has not suffered compensable damage because of anything the respondents did or did not do. In paying for Clark County Fire District No. 5's liabilities AAIC is simply "losing" what it contracted to lose. In the end, this case is focused solely on the idea of an insurance company trying to relieve itself from its own faulty risk analysis. In considering "equities" here, it should be fully noted that AAIC's insured, Clark

County Fire District No. 5, was the bad actor. It was their conduct which led to the claims against them. Despite the fact that Clark County Fire District No. 5 was the bad actor, it has been made whole.

Plaintiffs' citation to the Arizona decision of *Paradyme Ins. Co. v. Langerman Law Offices*, 200 Ariz. 146, 24 P.3d 593 (Ariz. 2001) on the issue of a "lack of remedy" is problematical and irrelevant – that case is from a jurisdiction which holds that defense counsel does have a duty to its assigning carrier, and further, that duty is based on an analysis entirely different from *Trask*.

Petitioner's legal citations arguing that the *Stewart Title* rule leaves the carrier "an empty remedy" are misleading and inapplicable. The citation to *Stangland v. Brock*, 109 Wn.2d at 681 [Petition, p. 14] takes that court's discussion concerning "third-party beneficiary" theories of duty applied in other states, and uses it to inaccurately imply that the *Stangland* court was articulating the petitioner's argument. *Stangland* recognized that not every duty will provide a basis for compensation. " . . . even if a duty is owed, the law will give it recognition and effect only as it is defined by a particular standard of conduct." *Stangland v. Brock*, 109 Wn.2d 675, 682, 747 P.2d 464, 468 (1987).

The Texas case cited by petitioner, *American Centennial Ins. Co. v. Canal Ins. Co.*, 843 S.W.2d 480 (Tex., 1992), does not validate the

petitioner's argument. The Texas case involves issues of contractual relations and issues of equitable subrogation between excess insurers who each have similar obligations to the insured, issues specifically not applicable here. See, *Stewart Title v. Sterling Sav. Bank*, 178 Wn.2d at 570, fn. 4.

F. Petitioner's Assertion of "Public interest" Appears to Be Based on Circumstances That Are Not Entirely Independent to Petitioner's Claim

AAIC asserts, with little analysis, that a "substantial public interest" will be served if this Court accepts review of this matter. This contention appears largely based on the existence of another pending appellate case.

The criteria generally considered to determine if an issue is of "substantial public interest" are the public or private nature of the question presented, the desirability of an authoritative determination for the future guidance of public officers, and the likelihood of future recurrence of the question." *Sorenson v. City of Bellingham*, 80 Wn.2d 547, 558, 496 P.2d 512 (1972). Rather than address these factors, however, AAIC asserts an argument that because a separate single case with similar issue has been recently presented to this Court, there must be a substantial public interest.

Petitioner's initial statement to the Court that this other case which involves an assertion of a carrier's right to recover moneys paid to

indemnify the bad acts of its insured, from the attorney who represented the insured, [Petition, p. 6] had been "accepted" for review by this Court[1] - the implication being that because this Court has "accepted" the second case, there is some "significant groundswell" of public interest is incorrect. The fact is that this Court has not accepted review of the other matter and second, the "groundswell" of interest seemingly rises only on the part of petitioner's trial court expert (the second case was apparently filed by the same attorney specializing in representing plaintiffs in legal malpractice proceedings who acts as the petitioner's paid expert in the trial court).

The fact that the 2013 *Stewart Title* decision is the first decision of record in Washington addressing the issues surrounding the duty of a defense counsel to the insurer who appointed it to defend its insured, in and of itself demonstrates the tepid, "unsubstantial" nature of any "public interest" in the issue.

G. The Myriad of Possible Conflicts of Interest Created in Finding a Duty by a Defense Attorney to Its Client's Insurer Are Significant Burdens on the Profession

Petitioner's attempt to parse the Rules of Professional Responsibility to the end of demonstrating a lack of possible conflicts of interest in the tri-partite relationship is unavailing.

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[1] Petitioner later realized the inaccuracy of its statement and filed an "*errata*" acknowledging the correct facts.

The possibility of creating conflicting loyalties is, of course, directly relevant to whether this Court would recognize a duty from a lawyer to a non-client. An attorney owes a duty of care only to the client. *See Bohn v. Cody*, 119 Wn.2d 357, 364-65, 832 P.2d 71 (1992); *Stangland v. Brock*, 109 Wn.2d 675, 679, 747 P.2d 464 (1987). No Washington appellate decision has *ever* applied *Trask* to impose a duty of care on the part of an insured's lawyer to the insurer under any circumstances. As *Stewart Title* recognized, establishment of such a duty would create intolerable potential conflicts, contrary to *Trask*.

Petitioner's arguments ignore the overarching potential for impermissible conflict between the insurance carrier and its insured which precludes a lawyer to represent both. Even if not initially apparent at the time that a defense assignment is accepted, a conflict situation (even over the insured's rights to coverage) can subsequently arise. Numerous circumstances can be envisioned in the tri-partite relationship where potential or actual conflicts of interest could arise for the insurance defense attorney even where an insurer has not "reserved its rights" under its contract of insurance with the attorney's client. These would include but are not necessarily limited to (1) representation of the insured which becomes more complex than anticipated, resulting in financial hardship for the attorney; (2) policy and/or coverage defenses discovered by either the

carrier or the attorney and insured while the attorney represents the insured; (3) disagreement between the insured and the insurer with regard to settlement negotiations.

A potential conflict that is virtually impossible to negate simply because the carrier has accepted the defense of its insured without any "reservation of rights," is when a third-party claimant offers to settle with the defense counsel's client, the insured, within the indemnity limits of the insurance policy. Washington's preeminent insurance expert, Thomas Harris, described the situation:

> When a claimant offers to settle within the insured's policy limit, an insurer's natural inclination would be to consider its own interest first. If the duty to pay only included the duty to indemnify, the insurer would face no risk beyond its policy limits. Allowing an insurer to interpret its contractual duty to pay in such a narrow fashion "would be akin to asking the cat to guard the canary."

HARRIS, THOMAS, WASHINGTON INSURANCE LAW 18-3 (3d ed.).

While an insured and its insurer may share some "common" interests, the two parties are subject to complete divergence at any time. Where a subsequent conflict rises, the rule is clear, "If a lawyer accepts dual representation and the client's interests thereafter come into actual conflict, the lawyer must withdraw." *Gustafson v. City of Seattle*, 87 Wn. App. 298, 303, 941 P.2d 701 (1997) (citing *Eriks v. Denver*, 118 Wn.2d 451, 459, 824 P.2d 1207 (1992)).

According to the petitioner itself, there is "in every case" a "significant risk that a lawyers' ability to consider, recommend or carry out an appropriate course of action for the client will be materially limited as the result of the lawyer's other responsibilities to its insured necessarily fail the test." [Court of Appeals, Appellant's Opening Brief, p. 35].

The situation where the attorney assigned by an insurer to adequately and zealously represent the interests of the insured is fraught with ethical perils for the lawyer. Even in "intended beneficiary" cases, Washington courts take the position that "the mere potential for a conflict of interest which potentially compromises the attorney's duty of undivided loyalty to the client ... imposes an untenable burden upon the attorney-client relationship. *Parks v. Fink* 173 Wn. App. 366, 384, 293 P.3d 1275 (2013).

V. CONCLUSION

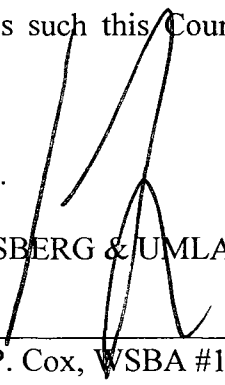
Based on the foregoing arguments, defendants/respondents respectfully request that this Court deny the Petition for Review of this Appeal insofar as it relates to the trial court summary judgment and the Court of Appeals affirmance of that dismissal of Petitioner/Plaintiff AAIC's complaint, for lack of standing. Petitioner has failed to show that review of the issue of an insurer's standing to bring a claim of legal

malpractice against the attorney it assigns to defend its own insured is appropriate under RAP 13.4(b).

The record and applicable law show that the Court of Appeals decided the issues presented correctly. As such this Court should deny further review of AAIC's case.

DATED this 20th day of June, 2014.

FORSBERG & UMLAUF, P.S.



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DECLARATION OF SERVICE

I, Elizabeth Sado, declare under penalty of perjury that I am over the age of 18 and competent to testify as to service in this matter.

On the date given below, I caused a copy of Defendants'/ Respondents' Answer to Petition for Review to be hand-delivered on June 23, 2014 by 4:30 p.m. to:

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DATED this 20th day of June, 2014, at Seattle, Washington.

Elizabeth Sado