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No. 95604-9

Court of Appeals, Division I No. 75674-5-I

IN THE SUPREME COURT
OF THE STATE OF WASHINGTON

NATIONAL SURETY CORORATION,

Respondent,

v.

IMMUNEX CORPORATION,

Appellant.

RESPONDENT NATIONAL SURETY CORPORATION'S RESPONSE TO BRIEF OF *AMICI CURIAE*

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I. INTRODUCTION

When an insurer issues a reservation of rights ("ROR"), it takes on an obligation to pay defense fees incurred by the insured up until the time a court determines there is no coverage. But the insurer's payment obligation is not unqualified: To the extent the insured's conduct results in actual and substantial prejudice, the insurer need not pay.

In cases like this one, where the prejudice caused by the insured is so obvious and pervasive, it is impossible to say prior to trial whether any amount of defense fees ultimately will be owed. Indeed, Immunex's own counsel judicially admitted that fact in open court, and as it turned out, the jury ended up discounting Immunex's claimed damages by nearly 100 percent.

Had Immunex timely tendered to National Surety Corporation ("NSC"), and as the jury concluded after weighing the highly unique facts of this case, NSC would have obtained a judicial declaration of no coverage years earlier, cutting off any supposed defense obligation long before the overwhelming majority of Immunex's $15.4 million legal bill was ever incurred.

An insurer does not lose the benefits afforded to it under an ROR simply because the insured engaged in a prejudicial course of conduct that

necessitates a jury trial. Indeed, because it issued an ROR, NSC became legally obligated to pay whatever portion of Immunex's $15.4 million legal bill the jury determined to be appropriate, after factoring in the impact of the prejudice caused by Immunex. In exchange for undertaking that potentially massive obligation – one the jury ultimately determined to be $670,000 – Washington law affords NSC a substantial benefit: insulation from extracontractual liability. Without such protection, no insurer would ever issue an ROR and agree to pay fees.

Amici take issue with the timing of NSC's $670,000 payment, but completely ignore the sequence of events leading up to that payment. Perhaps most notably, *Amici* ignore that the trial court, Court of Appeals, and this Court all recognized, prior to trial, that Immunex's extraordinarily late notice and tender presented questions of fact that needed to await resolution by the jury, and that NSC's payment obligation, if any, could not be determined (let alone paid) prior to that time.

That isn't to say, as *Amici* now imply, that NSC paid no attention to Immunex's legal fees prior to trial. In fact, at the time NSC issued the ROR in March of 2008, it asked Immunex to submit copies of all bills it wanted NSC to pay. It took Immunex more than a year to begin providing those invoices to NSC, by which time the trial court had already determined there was no coverage.

This was not, in other words, a situation in which a helpless insured was left to fend for itself. Instead, Immunex strategically waited until it had incurred every last penny of its $15.4 million legal bill before submitting even a single invoice to NSC for reimbursement, by which time the trial court had already determined there was no coverage.

There may be some other case, involving different parties and circumstances, in which some amount of defense fees are not subject to reasonable dispute, for which the insured timely submitted legal bills to the insurer, and for which payment need not await a jury determination at trial. This is not such a case.

The Court of Appeals correctly recognized that a jury trial on the issue of prejudice was necessary before any payment under the ROR could be paid or even ascertained under the circumstances presented here, and that NSC did not forfeit the important rights afforded to it under the ROR simply because the prejudicial course of conduct engaged in by Immunex necessitated such a trial. That was a proper application of Washington law to the highly unique facts of this case. There is no basis to review that ruling.

II. SUPPLEMENTAL STATEMENT OF THE CASE

In the interest of judicial economy, NSC respectfully incorporates by reference the Statement of the Case included in NSC's Answer to

Immunex's Petition for Discretionary Review, and refers to that document herein as the "Answer." In the section that follows, NSC also makes reference to additional facts and evidence that are relevant to the arguments presented herein.

III. ARGUMENT

A. The Court of Appeals' Ruling Does Not Transform the Duty to Defend into a Duty to Reimburse; It Merely Applies Washington Law to the Unique Facts of This Particuar Case

Amici first argue that the Court of Appeals' ruling "transforms the duty to defend into a mere duty to reimburse years later." Brief at 7. *Amici* are wrong. In its ruling, the Court of Appeals merely applied settled Washington law, including the law of this case, to the unique facts before it, including the fact that Immunex never made any request that NSC defend it in the AWP Litigation, and instead made the extremely prejudicial decision to seek reimbursement of $15.4 million of legal fees long after-the-fact.

In support of its argument, *Amici* note that the duty to defend entitles the insured to a "'prompt and proper defense' from its insurer." Brief at 8 (quoting *N.H. Indem. Co. v. Budget Rent-A-Car Sys., Inc.*, 148 Wn.2d 929, 938, 64 P.3d 1239 (2003)). *Amici* go on to argue that NSC's reimbursement of defense fees after-the-fact categorically

precludes it from mounting a "prompt" defense, and thus categorically precludes NSC from receiving any benefits under the ROR. *Id.*

Stated differently, in order to receive the benefits conferred under the ROR, *Amici* argue that NSC was required to "promptly mount[ ] a defense and continu[e] to defend until it obtaine[d] a ruling of no coverage." Brief at 11. Because it did not do so, *Amici* argue, NSC is not entitled to any protection (and instead only an obligation to pay) under the ROR.

That cannot possibly be correct, legally or logically, as Immunex never even asked NSC to defend it in connection with the AWP Litigation. Indeed, the jury was presented with undisputed evidence that, over a course of years, Immunex unilaterally defended itself in the AWP Litigation without ever seeking NSC's assistance or involvement. Answer at 2.

For example, Immunex's corporate representative confirmed that the company knew it was not being defended by NSC in 2002, when the AWP Litigation arose, or at any point thereafter, notwithstanding the fact that it was incurring (and actively paying) legal fees in the AWP Litigation – fees that ultimately exceeded $15.4 million:

Q. Was National Surety defending Immunex in the year 2002?

A. No.

Q. Was National Surety defending Immunex in the year 2003?

A. No.

Q. 2004?

A. No.

Q. 2005?

A. No.

Q. 2006?

A. No.

Q. And you knew it?

A. We knew that National Surety was not defending Immunex in those years.

CP 4551. Clearly, this testimony demonstrates Immunex's knowledge that the company had not tendered any claim to NSC.

At trial, Immunex's broker went on to confirm that, when an insurance company is defending a lawsuit, it is the insurance company – not the insured – who hires and pays the lawyers. RP 15:17-20, 39:9-23 (May 11, 2016 a.m.). The opposite happened here: Over the course of years, Immunex incurred and paid all of the legal fees itself, and not a single witness testified that Immunex directly or indirectly submitted a single legal bill to NSC or any other insurer for payment. RP 320:7-23

(May 10, 2016); RP 39:9-23 (May 11, 2016 a.m.); RP 291:3-17 (May 17, 2016); RP 488:3-19 (May 24, 2016).

Underscoring the point even further, Immunex's lead national counsel, David Burman, confirmed that he and his colleagues likewise knew there were no insurance companies involved in Immunex's defense, and that they had instead been retained and paid by Immunex alone:

> Q. And you weren't dealing with any insurance companies in this case and you knew it?
>
> A. Correct.

RP at 294:4-6 (May 17, 2016).

Had Immunex timely tendered the AWP Litigation, Immunex would have, among other things, (1) sought to work with NSC in the selection of defense counsel, (2) kept NSC apprised of events in the AWP Litigation, (3) sent NSC legal bills in connection with the twenty lawsuits filed against it, and (4) inquired into to the status of NSC's coverage position at some point over the course of more than five years. RP 489:12-493:12 (May 24, 2016). The jury heard unrefuted testimony that Immunex did none of those things.

As the jury concluded, timely tender would have permitted NSC to move for declaratory judgment back in 2002, before the vast majority of Immunex's $15.4 million legal bill was ever incurred. The fact that Immunex gave NSC no such opportunity was highly prejudicial, which in

turn resulted in the jury reducing the amount owed to Immunex under the ROR by nearly 100 percent.

Indeed, the jury heard unrefuted evidence that Immunex did not even begin submitting legal bills to NSC until May 29, 2009, the same day Immunex received its last and final bill in connection with the AWP Litigation. *Compare* CP001682 at ¶ 43 (admitting that Immunex did not begin sending invoices to NSC until May 29, 2009) *with* TX 304A (showing last batch of invoices to Immunex dated May 29, 2009).

In other words, rather than asking NSC to defend it in the AWP Litigation, as the NSC policies unambiguously required Immunex to do as a condition of coverage, Immunex merely asked NSC to reimburse $15.4 million in legal fees years after-the-fact.

Having denied NSC any opportunity to even consider defending it in connection with the AWP Litigation, Immunex and *Amici* obviously cannot fault NSC for "failing" to provide a "prompt" defense. Indeed, reimbursement was the only choice Immunex ever presented to NSC, which was an act that resulted in significant prejudice.

In applying Washington law to these unique facts, the lower courts did not "transform[ ] the duty to defend into a mere duty to reimburse years later," but instead appropriately acknowledged the context in which

Immunex made its extraordinarily late and inappropriate request for NSC's assistance.

Like Immunex, *Amici* completely ignore that context, which was critical to the Court of Appeals' ruling. The assertion that the Court of Appeals' ruling somehow transforms the duty to defend into a duty to reimburse is clearly misplaced, and simply ignores the pertinent evidence underlying the Court of Appeals' analysis.

B. The Court of Appeals' Ruling Does Not Disturb Existing Incentives Between Insurers and Insureds

Amici next argue that the Court of Appeals' ruling improperly disturbs the incentives between insurers and insureds by permitting NSC to claim the benefits of the ROR without actually undertaking any corresponding burden. Brief at 12. *Amici* are wrong, both as to the facts and applicable law.[1]

NSC accepted the full burden that comes with issuing an ROR when it undertook a legal obligation to pay whatever amount the jury deemed appropriate, up to $15.4 million. Indeed, even after the trial court determined that none of the policies issued by NSC afford a penny of

[1] As noted above, *Amici's* argument is perverse. Indeed, *Amici* argue that Immunex should receive all of the benefit under the ROR (*i.e.*, $670,000 in legal fees not otherwise covered under any NSC policy) while simultaneously maintaining its right to bring extracontractual claims. It is Immunex – not NSC – who is impermissibly attempting to have the best of both worlds.

coverage, NSC continued to be bound by its obligation to pay those potentially massive defense fees.

As this Court acknowledged in remanding the case for trial, the only remaining questions concerned the extent of the prejudice Immunex's extraordinarily late tender caused to NSC, and the amount by which NSC's payment obligation under the ROR would be reduced as a result of that prejudice: "[A]n insurer may avoid or minimize its responsibility for defense costs when an insured belatedly tenders a claim and the insurer demonstrates actual and substantial prejudice as a result." *Nat'l Sur. Corp. v. Immunex Corp.*, 176 Wn.2d 872, 875, 297 P.3d 688, 689 (2013). The Court remanded the case for trial to resolve those issues. *Id.* at 891.

At trial, the jury determined that NSC was obligated to pay $670,000, and NSC paid that amount in full with applicable interest. Answer at 13; CP 4506-7.

In exchange for taking on that obligation, and in accordance with settled Washington law, the Court of Appeals correctly recognized that the law affords NSC a substantial benefit: insulation from extracontractual liability. Without such protection, insurers would have no incentive to undertake the potentially massive obligations that flow to them under an ROR, and no insurer would ever do so.

On the flip side of the coin, and as *Amici* point out, the existence of extracontractual liability incentivizes insurers to avoid acting in bad faith, and Washington law furthers that goal by ensuring that the "worst case scenario" for an insurer entails payment of some amount that exceeds whatever the insurer is already obligated to pay under its policies. Brief at 10.

This case epitomizes those competing incentives in motion, working exactly as they should under Washington law. Indeed, it was those very incentives that caused NSC to issue an ROR, under which it agreed to pay up to $15.4 million under policies that ultimately were determined to afford no coverage whatsoever. Stated differently, the ROR placed NSC on the hook for up to $15.4 million more than what it was required to pay under its policies. NSC accepts that, because it issued the ROR, it ultimately was required to pay more than what its policies actually cover, but NSC obviously is entitled to the corresponding benefit of the bargain: insulation from extracontractual liability. *Woo v. Fireman's Fund Ins. Co.*, 161 Wn.2d 43, 54, 164 P.3d 454 (2007).

The Court of Appeals' ruling, which upheld and recognized the important benefits and burdens each party receives under the ROR, perfectly implemented the incentives this Court has established between insurers and insureds, and should not be disturbed.

C. The Court of Appeals' Ruling Does Not Permit Insurers to Escape Extracontractual Liability "Simply by Reserving Their Rights"

Amici next argue that the Court of Appeals' ruling permits insurers to escape extracontractual liability "simply by reserving their rights." Brief at 14. But this case does not involve a situation in which an insurer simply reserved its rights and did nothing more. On the contrary, NSC paid $670,000 to Immunex under the ROR, even though none of the policies it issued afford a penny of coverage, and did so precisely when this Court said it should: following the jury's determination on the issue of prejudice. *Nat'l Sur. Corp.*, 176 Wn.2d at 875, 891.

Simply ignoring the six-figure payment made by NSC, along with the fact that this Court remanded the case for trial on the issue of prejudice, *Amici* argue that "this Court has refused to extend immunity from bad faith liability to insurers who *promise* a defense under a reservation of rights, but then do not keep that promise." Brief at 14 (*citing Safeco Ins. Co. v. Butler*, 118 Wn.2d 383, 823 P.2d 449 (1992)).

But NSC indisputably kept the promise it made under the ROR by paying the full amount of defense fees incurred by Immunex in the AWP Litigation, subject to the jury's determination on the issue of prejudice.

Moreover, the cases cited by *Amici* on this issue are inapposite, as each one of those cases involves an insured who, unlike Immunex, timely

requested a defense during the course of an active litigation. In those cases, the courts recognized that an insurer who begins defending under an ROR can still be liable for bad faith in the event it fails to continue defending in an appropriate manner, such as by prematurely withdrawing its defense or not defending in an appropriate manner. *Butler*, 118 Wn.2d at 392; *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 387, 715 P.2d 1133 (1986).

This is not such a case: Immunex never asked NSC to defend it in the AWP Litigation at all. In fact, and as noted above, Immunex decided to defend itself throughout the entirety of the AWP Litigation, and began sending its AWP-related bills to NSC on the same day it received the very last of those bills from its own counsel – invoices relating to 20 separate lawsuits incurred over the course of more than seven years of litigation. *Compare* CP001682 at ¶ 43 *with* TX 304A.

The jury was presented with substantial evidence that Immunex could have provided those invoices to NSC at any time during the course of the AWP Litigation, but strategically decided not to do so. *See supra* Section III.A.

By proceeding in such a manner, Immunex made it impossible for NSC to defend it in the AWP Litigation, and instead left NSC in a situation in which its only option was to reimburse Immunex's legal fees

after-the-fact. In issuing the ROR, that is precisely what NSC agreed to do, subject to a jury determination on the issue of prejudice. As soon as the jury resolved that issue in accordance with this Court's remand instructions, NSC timely paid Immunex all that was owed. In short, NSC did not "simply reserve its rights," but reserved its rights and then timely paid the full amount promised under the ROR.[2]

Moreover, no one was capable of saying prior to trial what amount, if any, NSC was obligated to pay, which is precisely why this Court remanded the case for trial. That is what Immunex's own counsel judicially admitted in open court. RP at 14:19 – 15:4 (Oral Argument Transcript of April 28, 2016). And that is what Immunex's own insurance expert conceded. CP 3160 at 12:3-8. NSC obviously does not forfeit the protections afforded to it under the ROR because Immunex created a situation in which it was impossible to know what amount, if any, NSC would end up owing under the ROR prior to trial.

D. The Court of Appeals' Ruling is Perfectly Consistent With the Enhanced Duty of Good Faith and Fair Dealing Insurers Owe When Defending Under a Reservation of Rights

Amici next point out that insurers who defend under a reservation of rights owe an "enhanced duty of good faith to the insured," and argue

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[2] If NSC had failed to pay that amount following trial, then Immunex would have been entitled to immediately collect upon its judgment without the need for further litigation. That is precisely the framework established by Washington law.

that NSC violated that enhanced duty by allegedly "failing" to provide a "prompt and proper" defense. Brief at 16.

Amici specifically argue that, "[w]hen an insurer promises an immediate defense but then abandons its insured to fend for itself while a court resolves a coverage dispute, it has not given 'equal consideration' to the insured's interest with respect to that dispute, nor has it vindicated 'the elevated level of trust' insureds place in their insurers." Brief at 16.

But as noted, Immunex never asked NSC to defend it in connection with the AWP Litigation at all. In fact, as the evidence presented to the jury made clear, there was nothing left to defend by the time Immunex decided to provide its AWP-related bills to NSC. The case was over. All legal expenses had been incurred, and Immunex was merely looking for NSC to reimburse the $15.4 million of fees it unilaterally incurred over the preceding seven years. *See supra* Section III.A. The idea that NSC "abandoned" Immunex or left the company to "fend for itself" is demonstrably incorrect: Immunex was exceptionally careful to ensure that it tightly controlled its own defense, over the course of many years, without the involvement of NSC.

As the trial court, Court of Appeals, and this Court have all ruled, and as Immunex's own counsel judicially admitted in open court, it was not possible to know what amount, if any, NSC owed under the ROR

before the jury determined the extent of the prejudice Immunex caused by proceeding in such an untenable manner. *Nat'l Sur. Corp. v. Immunex Corp*, 162 Wn. App. 762, 782 (n.14) 297 P.3d 688 (2013); *Nat'l Sur. Corp.*, 176 Wn.2d at 875. As soon as the jury determined that amount, NSC timely paid it, which was all NSC was obligated to do under the ROR.

E. The Court of Appeals' Ruling Will Have Little to No Impact Upon Small Businesses and Individuals of Limited Means

Amici next argue that the Court of Appeals' ruling will disproportionately impact policyholders who, unlike Immunex, lack the resources to mount and fund their own defense. Brief at 16-18. In making that argument, Immunex implies that small businesses and individuals of limited means might one day find themselves in the same situation Immunex and its army of in-house lawyers, brokers, and risk managers created for themselves in connection with the AWP Litigation.

That will not happen. Insureds who lack the means to mount and fund their own defense do not pay millions of dollars in legal fees over the course of several years, only to seek reimbursement from an insurer years after-the-fact.

Indeed, the unique facts underlying this case would arise again only with respect to an insured who, like Immunex, (1) does have the

resources to hire its own lawyers to defend it in multiple complex cases over the course of several years, and (2) is able to assume the risk that, in demanding reimbursement of its legal fees well after-the-fact, and in violation of the unambiguous obligations it has under its policies of insurance, a jury might reasonably conclude that the insurer has been unfairly prejudiced.

Small businesses are highly unlikely to engage in such ill-advised activity, but if anyone were to follow the poor example set by Immunex in this case, then perhaps the Court of Appeals' ruling may have some impact upon the outcome of that particular case. With that being said, the type of conduct engaged in by Immunex here is not the type of conduct any small business could, would, or should ever engage in, and the idea that the Court of Appeals' ruling will have any impact upon small businesses and individual insureds – let alone a "widespread" impact – is clearly misplaced.

F. The Scope of the Court of Appeals' Ruling is Limited to the Particular Facts of This Case

Amici next argue that, "if the Court of Appeals' decision stands, insurers will be able to stand on *any* colorable defense to coverage, and still enjoy blanket immunity from extra-contractual claims." Brief at 19. Nothing in the decision below suggests that the Court of Appeals intended

for its ruling to have any application beyond the specific factual pattern before it.

Indeed, the Court of Appeals specifically noted that

> [t]he case was remanded to the trial court to determine factually if, and to what extent, the late tender of defense by Immunex prejudiced National Surety with respect to defense costs. Until the reasonableness of the defense costs was resolved by the jury and reduced to judgment, tender of payment in this case was not required.

App'x A to Petition for Review at 7.

The Court of Appeals did not rule, as *Amici* suggests, that an insurer who issues an ROR may avoid paying defense fees thereunder based upon "*any* colorable defense." Instead, the Court of Appeals merely recognized what this Court expressly acknowledged in its own prior ruling remanding this case for trial – namely, that the amount of NSC's payment obligation, if any, was a question of fact that needed to await resolution by the jury. In following that ruling, NSC obviously did not forfeit the substantial rights afforded to it under the ROR, and the Court of Appeals did not err in upholding dismissal of Immunex's extra contractual claims.

G. When Applied to These Unique Facts, *Amici's* Position Would Turn Washington Law on its Head and Promote Gamesmanship on the Part of Sophisticated Insureds

Finally, if the Court were to adopt *Amici's* position with respect to the unique facts of this case, doing so would turn Washington law on its

head, unfairly deny insurers their right to pursue an early declaratory judgment action, read the early notice provision entirely out of insurance contracts, and otherwise promote gamesmanship on the part of sophisticated insureds such as Immunex.

Indeed, if an insurer could receive the benefit of an ROR only by reimbursing 100 percent of the insured's legal fees up-front, and without awaiting a determination on the issue of prejudice, sophisticated insureds would have little or no incentive to tender their claims in a timely fashion, and would instead be tempted to follow the untenable approach adopted by Immunex here – namely, to defend themselves over the course of a prolonged period of time, to deny insurers any ability to be involved in the selection of counsel, the management of legal fees, or decisions in the litigation, and to then belatedly tender those fees for reimbursement only after the underlying litigation is already over.

Permitting such an approach would put insurers in an unfair and untenable position: In order to enjoy the benefits of an ROR, the insurer effectively would be forced to waive its right to seek a reduction in fees based upon the insured's untimely tender.

Such an approach would unfairly deprive insurers the right to seek an early declaratory judgment action, and would render meaningless the

early notice provision contained in most insurance policies, including the ones at issue here.

Permitting such an approach also would be inconsistent with settled Washington law, including the law of this case, which requires a reduction in fees to the extent an insured's untimely notice and tender results in prejudice. *See*, *e.g.*, *Mut. of Enumclaw Ins. Co. v. USF Ins. Co.*, 164 Wn.2d 411, 417, 191 P.3d 866, 871 (2008); *Unigard Ins. Co. v. Leven*, 97 Wn. App. 417, 427, 983 P.2d 1155, 1161 (1999), *as amended* (Apr. 24, 2000); *Nat'l Sur. Corp.*, 176 Wn.2d at 891. Nothing in law or logic suggests that, as a condition to issuing an ROR, insurers must waive their right to seek such a reduction of fees in an appropriate case such as this one.

IV. CONCLUSION

For all of the foregoing reasons, in addition to the reasons set forth in its previously-submitted Answer, NSC respectfully requests that the Court deny Immunex's Petition for Discretionary Review and finally bring this case to an end after more than a decade of expensive and time-consuming litigation.

DATED THIS 25th day of May, 2018.

McNAUL EBEL NAWROT & HELGREN PLLC

By: ______________________

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DECLARATION OF SERVICE

The undersigned declares under penalty of perjury under the laws of the State of Washington that on May 25, 2018, I caused a copy of the foregoing **Respondent/Plaintiff's Answer to Petition for Review** to be served by electronic mail on:

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Respondent National Surety Corporation's Response to Brief of Amici Curiae

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