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NO. 63667-7

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

RICHARD BANKSTON and SUSAN BANKSTON, husband and wife and the marital community composed thereof, d/b/a AAROHN CONSTRUCTION,

Appellants,

v.

DEVELOPER'S SURETY AND INDEMNITY COMPANY, a foreign corporation,

Respondent.

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BRIEF OF APPELLANT

David B. Jensen, WSBA #21284
Holly E. Hinterberger, WSBA #37281
Facsimile: (206) 467-2689
Attorneys for Appellants

MERRICK, HOFSTEDT & LINDSEY, P.S.
3101 Western Ave., Suite 200
Seattle, WA 98121
Telephone: (206) 682-0610
Facsimile: (206) 467-2689

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I. INTRODUCTION

This case arises from an indemnity claim against Appellant Richard and Susan Bankston, d/b/a Aarohn Construction ("Aarohn Construction") brought by their bonding company, Developer's Surety and Indemnity Company ("Developer's"). Developer's posted a performance bond in connection with the performance of a public works contract between Aarohn Construction and Pierce County ("the County") for landscaping at a facility known as the Pierce County Annex. After wrongfully terminating Aarohn Construction, the County sought payment from Developer's under the bond.

Rather than investigating the claim, Developer's made an expedient self-serving business decision and paid the County. It then sued its own principal Aarohn Construction for indemnity rather than risk litigating with the County. Although Developer's was within its rights to pay the County, under the language of indemnity agreement ("Agreement"), it did not have a right to seek indemnity against Aarohn Construction. Accordingly, the trial court erred when it failed to grant Aarohn Construction's Motions to Dismiss after the close of Developer's case and after the verdict.

II. ASSIGNMENT OF ERROR

1. The trial court erred when it failed to grant Defendant's Motion for Directed Verdict and Motion Notwithstanding the Verdict where under the most reasonable reading of the subject agreement, construed in favor of Aarohn Construction, Developer's had no right to pursue an indemnity claim against Aarohn Construction.

2. The trial court erred when it failed to grant Defendant's Motion for Directed Verdict and Motion Notwithstanding the Verdict where Developer's failed to present any evidence supporting the conclusion that the indemnity obligation had been triggered.

3. The trial court erred when it failed to grant Defendant's Motion for Directed Verdict and Motion Notwithstanding the Verdict where the subject Agreement was unconscionable.

4. The trial court erred when it failed to grant Defendant's Motion for Directed Verdict and Motion Notwithstanding the Verdict where the trial court lacked subject matter jurisdiction.

5. The trial court erred when it awarded Developer's prejudgment interest for its disputed unliquidated indemnity claim.

III. STATEMENT OF CASE

A. *Background Facts.*

1. The Formation of the Indemnity Agreement.

Richard Bankston was the owner of Aarohn Construction, a sole proprietorship. Report of Proceedings ("RP") 636, 638. His father, John Bankston was the company's project superintendant and on-site manager. RP 670, 672. He had speaking authority for Richard and for Aarohn Construction.[1] RP 672, 797-98. He was also a signatory for the company and was authorized to sign documents on its behalf. RP 797-98.

Pierce County issued a request for bids for an extensive tree replacement and irrigation project at the Pierce County Annex Facility. Clerk's Papers ("CP") 447-52; RP 786. Aarohn Construction submitted a bid for the Project, which the County accepted. RP 679.

Aarohn Construction purchased the subject bond from Developer's as required under its contract for a public works project with the County. Supplemental Designation of Clerk's Papers ("SCP"), Trial Exhibit No. 1. The County required that Aarohn Construction obtain a performance bond. CP 451, 480, 529. If it failed to do so, Aarohn Construction would not be allowed to perform the contract with the County. *Id.*

---

[1] We use first names for ease of reading and to avoid confusion. We mean no disrespect.

Aarohn Construction purchased the bond and paid a premium to Developer's. SCP, Trial Exhibit No. 1; CP 403. Developer's then required Aarohn Construction to sign a form indemnity agreement that was developed solely by Developer's. RP 557-58. Aarohn Construction was not allowed to negotiate the terms of the agreement and was required to sign it in order to obtain the bond. RP 559. According to Developer's corporate counsel Lou White:

> Q. Okay. Is this a document [the indemnity agreement] that -- that's a DSI [Developer's Surety] document?
>
> A. If you're asking if the bonding company created this, yes, I believe we did.
>
> Q. Okay. So this is actually an agreement that DSI drafted, right?
>
> A. To the best of my knowledge, yes.
>
> Q. Okay. Did -- so I'm assuming Mr. [Richard] Bankston, then, didn't have any role in negotiating the terms of this contract, correct?
>
> A. I would assume not.
>
> Q. Yeah. I'm assuming that's not Surety's practice to negotiate indemnity agreements with principals, correct?
>
> A. That is correct.

RP at 558-59.

Mr. White agreed that Aarohn Construction held no bargaining power to negotiate the terms of the agreement. Aarohn Construction was

nevertheless required to sign the agreement in order to obtain the bond or it would lose the contract with the County. CP 480-81. It is clear that Richard did not read the bond application when he signed the Agreement and that he signed it with no understanding of the potential liability exposure.

2. Subject Project.

The subject Project involved the removal of trees and extensive landscaping of the Pierce County Annex Facility. CP 529-30, 539. During the course of the work, Aarohn Construction encountered multiple unforeseen obstacles preventing the timely completion of the work. CP 561-64; RP 801. For example, the County provided inaccurate and incomplete plans for the Project, which caused Aarohn Construction to inadvertently damage portions of a sprinkler system that was not shown on the plans. CP 561-64; RP 796-97, 801-03. Aarohn Construction's performance was further complicated because multiple sprinkler systems and wiring were located in areas not shown in the plans. This further delayed Aarohn Construction. CP 561-64; RP 801, 803. Additionally, Aarohn Construction had problems accessing the site because the County failed to keep the area clear of parked cars. RP 801.

These issues required Aarohn Construction to request additional time and money to complete the Project. SCP, Trial Exhibit 70; RP 803-

04. The County terminated its contract with Aarohn Construction and ultimately retained an alternate contractor (Serpanok) to complete the Project. CP 516-17. The County then requested payment from Developer's for the difference between the amount paid to Serpanok and the alleged portion of the contract remaining after deducting the payment to Aarohn Construction. CP 444.

Developer's paid the County $65,759.79 without conducting any investigation of the County's claims or Aarohn Construction's defenses, including its request for additional time and compensation. CP 419; RP 568. It then filed this action against its own principal and sought the full amount paid as well as its attorney fees. CP 3-6. After trial, the jury refused to award Developer's its full alleged damages. CP 695-96.

In fact, Developer's even conceded at trial that there were significant issues with the County's claim, but it made no investigation or determination as to the merits of that claim. *See, e.g.*, RP 568-69, 582. Developer's also failed to make any investigation regarding Aarohn Construction's request for additional time or compensation under the contract. RP 568. Developer's did not even review the contract between Aarohn Construction and the County. RP 567. In short, it simply paid the County without making any determinations as to whether the County had a valid claim, or whether Aarohn Construction had valid defenses.

Developer's corporate counsel unequivocally stated that Developer's decision to pay Pierce County was a "business decision" and was not based upon an investigation supporting a determination of liability or contingent liability. RP 555, 588. He further admitted that the business decision, based solely on Developer's own self-serving interests, fit within the definition of expediency. *See, e.g.*, RP 485-87, 555, 564.

Developer's was unwilling to assume any responsibility for investigating the claim and potential defenses. *Id.* Instead, it requested that Aarohn Construction post collateral as a precondition for Developer's to investigate the County's claim and evaluate Aarohn Construction's defenses. RP 868. This requirement is found nowhere in the bond application or indemnity agreement. SCP, trial exhibit 2; RP 868.

Rather than incur any risk, Developer's made the business decision to expediently resolve the claim and pay the County:

> Q. Any my question to your is whether that decision [to pay] was, in fact, a **business decision** by [Developer's Surety]. Is that accurate?
>
> A. Generally yes.

RP 555 (emphasis added) (testimony of Mr. White). Payment was not made based upon liability or contingent liability. It was based upon expediency:

> Q. Would you agree that expediency would include a business decision by the surety to pay based on a lot of things that you talked about in your direct examination, attorneys' fees, exposure, bad faith exposure? Would you agree that that is a business decision that would fit within the definition of "expediency"?
>
> A. Yes.

RP 564 (emphasis added).

B. ***Terms of the Parties' Indemnity Agreement.***

The terms of the subject indemnity agreement allows Developer's to seek indemnity in certain instances. However, the Agreement was limited in scope and only authorized Developer's to seek indemnity where the surety "**was liable or contingently liable**" for demands or losses. CP at 403 (emphasis added); SCP, trial exhibit 2. Specifically, the agreement states:

> 1. To reimburse Surety, upon demand for all payments made for and to indemnify and keep indemnified Surety from:
>
> a) all demands, loss, contingent loss, liability and contingent liability claim, expense, including attorney's fees, for which Surety shall become liable or shall become contingently liable by reason of such suretyship, whether or not Surety shall have paid same at the time of demand; . . . .
>
> 2. Surety shall have the exclusive right to determine whether any claim or suit shall, on the basis of liability, expediency or otherwise, be denied, paid, compromised, defended or appealed. . . .

Id. (Emphasis added). The terms "liability," "contingent liability," and "expediency" are not defined anywhere in the Agreement or the bond itself. RP 565.This omission is critical because the triggering event for Developer's right of indemnity is liability or contingent liability. RP 561; CP 403.

Developer's conceded that it had not conducted any investigation of the County's claim and that it had not determined whether Aarohn Construction was liable or contingently liable for the amount demanded by the County. *See* RP 555, 588. The surety's liability to the County was based on Aarohn Construction's liability under its contract. There was never any determination of liability, instead the surety simply concluded that payment of the claim was "expedient" based on its own business interests. *See* RP 564. Although it may be a basis for payment, expediency does not give rise to a right to seek indemnity. CP at 403; SCP, trial exhibit 2.

C. *Procedural History*.

After Developer's presented its case in chief, Aarohn Construction moved for a directed verdict based upon Developer's failure to present evidence supporting its claim that the indemnity obligation had been triggered. CP 631-36. The trial court denied the motion. Aarohn

Construction renewed its motion after the verdict. CP 698-708. The trial court again denied the motion. CP 790.

The jury was tasked with determining whether Developer's was entitled to reimbursement of the funds paid under the indemnity agreement. CP 665. The jury awarded Developer's damages in the amount of $60,759.79, but awarded less than the amount claimed by Developer's. CP 695-97.

The trial court subsequently awarded Developer's prejudgment interest on the verdict amount over Aarohn Construction's objection that the damages were not liquidated and therefore, did not warrant such an award. CP 695.

Aarohn Construction timely appealed.

IV. LEGAL ANALYSIS

I. STANDARD OF REVIEW

This Court reviews a trial court's decision to grant or deny a motion for directed verdict de novo. *Guijosa v. Wal-Mart Stores*, 144 Wn.2d 907 , 914, 32 P.3d 250 (2001). A trial court should grant a motion for directed verdict if, as a matter of law, no evidence or reasonable inference exists to sustain a verdict for the nonmoving party. *Harris v. Drake*, 158 Wn.2d 480, 493, 99 P.3d 872 (2004).

II. THE TRIAL COURT ERRED WHEN IT DENIED AAROHN'S MOTION TO DISMISS.

A. *The Uncontroverted Evidence at Trial Established that Developer's Surety's Right to Indemnity Never Arose.*

When interpreting indemnity provisions, courts apply fundamental rules of contract construction. *MacLean Townhomes, LLC v. American First Roofing and Builders, Inc.,* 133 Wn. App. 828, 830, 138 P.3d, 155 (2006). The court differentiates between contract interpretation and contract construction. Interpretation is the "process whereby one person gives a meaning" to the document whereas contract construction is "the process by which legal consequences are made to follow from the terms of the contract...." *Berg v. Hudesman*, 115 Wn.2d 657, 663, 801 P.2d 222 (1990). To construe a contract, the court looks to its context. *Id.*

Where a contract is ambiguous on its face, the court looks to evidence of the parties' intent as "shown by the contract as a whole, its subject matter and objective, the circumstances of its making, the subsequent conduct of the parties, and the reasonableness of their interpretations." *Berg*, 115 Wn.2d at 666. Extrinsic evidence is admissible to illustrate the entire circumstances under which the contract was formed so as to aid in determining the parties' intent. *Id.* at 667. A contract need not be ambiguous for the court to look to evidence outside its four corners. *Id.* at 669.

Developer's Complaint includes only a claim under the indemnity agreement and no other theory was pled or pursued. CP 3-6. Mr. White did not even read his own company's Complaint and did not know if there was another basis for the claim. RP 567. Notwithstanding Mr. White's confusion about his company's own lawsuit, it is undisputed that the Agreement is the sole basis of Developer's claim. The Agreement provides in pertinent part that Richard and Susan Bankston agree:

> 1. To reimburse Surety, upon demand for all payments made for and to indemnify and keep indemnified Surety from:
>
> a) all demands, loss, contingent loss, liability and contingent liability claim, expense, including attorney's fees, **for which Surety shall become liable or shall become contingently liable** by reason of such suretyship, whether or not Surety shall have paid same at the time of demand; . . . .
>
> 2. Surety shall have the exclusive right to determine whether any claim or suit shall, on the basis of liability, expediency or otherwise, be denied, paid, compromised, defended or appealed. . . .

CP 403; SCP, trial exhibit 2 (emphasis added.)

Paragraph 1(a) sets forth the triggering event for indemnity: "liability" or "contingent liability." The most reasonable reading of the Agreement is that Developer's may seek indemnity where non-performance by the contactor that makes the surety legally liable to the

County – not where payment by Developer's was "expedient" under the circumstances. By the admission of its in-house attorney in charge of the claim, no serious inquiry was ever made by Developer's regarding Aarohn Construction's actual liability under the contract, or its defenses. In fact, Mr. White did not even read the contract between Aarohn Construction and the County:

> Q. Now, am I correct that as part of your investigation or part of Developer's Surety's investigation in this case that neither you or Mr. Wozney looked at the complete contract between Bankston Construction and Pierce County?
>
> A. Did you say, "Is that true?" Is that what your question was?
>
> Q. Correct.
>
> A. Almost assuredly that is true, since usually contracts are a whole lot of different papers and documents. I would say yes.

RP 567. He further testified that he did not review any change orders submitted by Aarohn Construction to the County asking for additional time. RP 568. It was primarily this request for additional time that caused the dispute between the County and Aarohn Construction. RP 416. The contract and change orders were crucial documents to this alleged dispute and they were simply ignored by Developer's.

Mr. White admitted that Developer's decision to pay Pierce County was a "business decision" that fit within the definition of "expediency":

> Q. And my question to you is whether that decision [to pay] was, in fact, a **business decision** by [Developer's]. Is that accurate?
>
> A. Generally yes.
>
> ***
>
> Q. Would you agree that that is a business decision that would fit within the definition of "expediency?
>
> A. Yes.

RP 555, 564 (emphasis added).

Developer's expedient business decision was made without any determination by Developer's as to whether it was "liable" or "contingently liable" to the County as a result of Aarohn Construction's performance of the contract:

> Q. Did you ... do any determination regarding whether Aarohn Construction should have obtained additional time for this contract?
>
> A. Well, if you mean by that if we came to some final determination based on everything, no, no.
>
> ***
>
> Q. Okay. And again, as part of your claim investigation process, you, on behalf of Developer's Surety, made no determination as to whether there should have been an extension of time on this contract; is that correct?

> A. I think -- well, I think that's fair. We didn't -- we didn't weigh and make some ultimate decision, if that's what you're asking. That is true.

RP 569, 583.

Developer's paid the County under the incorrect premise that it could then claim indemnity against its principal without regard to any actual or contingent liability. RP 610-11. As Mr. White put it, Developer's believed its right to indemnity from Aarohn Construction was near "absolute." RP 610. Mr. White testified that the indemnity provision entitled Developer's to sue its principal at any time for almost any reason:

> Q. Okay. So any time your company decides that it should pay a claim, there is a near absolute right to sue your principal? Or I guess that indemnity or contribution or however you want to characterize it.
>
> A. If we acted completely irresponsibly, I suppose there would be something, but I don't think we're anywhere close to that here.
>
> Q. Okay. So your opinion is that the surety's right to seek indemnity is absolute, even though the indemnity agreement itself sets out in paragraph 1A when the right to indemnity is actually triggered?
>
> A. First of all, I didn't say it was absolute. I said it was close to it. And -- but it's very, very broad. Okay?
>
> Q. Is -- or does paragraph 1A in this indemnity agreement that Developer's Surety is suing my client under, is it your

> opinion that 1A gives your business, Developer's Surety, an absolute or near absolute right to sue its principal?
>
> A. It is a very wide berth and wide discretion to act in a responsible, but -- a responsible way. But very wide berth to do so.

RP at 610-11. Mr. White's testimony regarding his company's right to seek indemnity ignores the language contained in Developer's own agreement. RP 458; *See also* CP 403.

This testimony also reflects Developer's intent to simply pursue its principal regardless of any determination of liability and without any reasonable investigation.

Developer's senior claims analyst Conrad Wozney – who was the only Developer's employee who was onsite – also did not review change orders, the contract, or otherwise make a determination about liability:

> Q. So but do you have any recollection of seeing any change orders submitted by Mr. Bankston?
>
> A. I don't really remember. I might have seen something at the office later on, but I'm not sure.
>
> Q. Okay. Am I correct <u>you never developed any sort of opinion as to whether Mr. Bankston should have obtained more time under these changes orders</u>?
>
> A. <u>No</u>. Because without seeing all the documentation, I wouldn't make that judgment.
>
> Q. Okay. <u>So you made no judgment regarding whether Mr. Bankston -- excuse me -- Aarohn Construction should have gotten more time on this</u>

project?

A. Correct.

***

Q. Well, I'm just asking generally about your review of this contract, the contract between Aarohn Construction and Pierce County. And that should be Exhibit 4 of the plaintiff's notebook.

A. Let's see.

Q. Now, does that appear to be the contract –

A. (Inaudible) –

Q. -- that Mr. Friedrich (inaudible) before?

A. I believe that's what he showed me. I didn't read it or anything.

Q. So, again, you've never seen that contract before today?

A. No.

RP 324-27 (emphasis added).

By his own admission, Mr. Wozney, did not actually investigate Aarohn Construction's performance on the Project. He spent time speaking with the County and less than an hour with John Bankston. RP 322-23. He certainly made no determination as to whether the surety was liable or contingently liable as a result of a breach of the underlying contract with the County. Furthermore, Developer's settlement agreement

with the County makes no mention of a determination of liability or contingent liability. CP 419-20.

As it made no determination of liability or contingent when paying the County's claim, Developer's has no right to indemnity. Accordingly, the trial court erred when, pursuant to an incorrect construction of the Agreement, it failed to grant Aarohn Construction's Motions to Dismiss. The verdict in Developer's favor should be set aside and the claims against Aarohn Construction dismissed.

B. *When Read Together, the Terms "Liability" and "Expediency" Render the Indemnity Agreement Ambiguous and it Therefore, Must be Construed Against the Drafter.*

When interpreting indemnity provisions, courts apply fundamental rules of contract construction. *MacLean Townhomes, LLC*, 133 Wn. App. at 828. An agreement is ambiguous if it is subject to at least two reasonable interpretations. *Kaplan v. N.W. Mut. Life Ins. Co.,* 115 Wn. App. 791, 804, 65 P.3d 16 (2003). "[T]he contract as a whole is examined, and if, on the face of the contract, two reasonable and fair interpretations are possible, an ambiguity exists." *Id.* If an indemnity agreement is ambiguous, any ambiguity is construed against the drafter. *Nunez v. Am. Bldg. Maint. Co. W.*, 144 Wn. App. 345, 351, 190 P.3d 56, *rev. denied*, 165 Wn.2d 1008 (2000) (construing an indemnity agreement against its drafter to determine whether the indemnity obligation had been

triggered). "Whether a written instrument is ambiguous is a question of law for the court," *Carlstrom v. Hanline*, 98 Wn. App. 780, 784, 990 P.2d 986 (2000).

Moreover, where a contract contains different words, those terms should be construed to have different meanings. *See, e.g. Bellevue Sch. Dist. No. 405 v. Bentley*, 38 Wn. App. 152, 159, 684 P.2d 793 (1984). In *Bellevue School District*, supra, the Court evaluated an employment contract to determine whether a former teacher was required to pay back her salary and benefits she received during a sabbatical. *Id.* at 154. The agreement specifically required that teachers who failed to return to work after a paid sabbatical were required to reimburse the district for the "salary" they received while away. *Id.* The agreement also contained the term "benefits," but the provision regarding reimbursement only stated that teachers must pay back their salary. *Id.* The court held that the terms should be construed to have different meanings because they were used separately in the agreement, and shall be construed to have different meanings. *Id.* at159.

Further, "[w]hen interpreting a document, the preferred interpretation gives meaning to all provisions and does not render some superfluous or meaningless." *Bogomolov v. Lake Villas Condominium Ass'n of Apartment Owners*, 131 Wn. App. 353, 361-62, 127 P.3d 762

(2006). Developer's reading of the Agreement does not give any meaning at all to the word "expediency."

While paragraph 1 of the Agreement requires liability or contingent liability to trigger indemnity, paragraph 2 grants Developer's "the exclusive right" to decide whether to make a payment "on the basis of liability, expediency or otherwise." (Emphasis added). If the Court accepts that Developer's has advanced a reasonable consideration of the Agreement, the interplay between these two paragraphs is at least ambiguous. The law requires that ambiguity must be construed against the Agreement's drafter, Developer's. *Nunez*, 144 Wn. App. 351.

Developer's advanced the position that it was entitled to indemnity under paragraph 1 regardless of why it paid a claim under paragraph 2. This construction conveniently ignores the word "expediency" in the Agreement. In spite of the terms of the Agreement and of the much more reasonable construction advocated by Aarohn Construction, the trial court presumably accepted Developer's theory by denying both the Motion after the Plaintiff's Case and in denying the Motions to dismiss. This ruling was clearly in error.

The reasonable interpretation that should be accepted by the Court is that Developer's is entitled to indemnification under paragraph 1 *only* when it pays a claim based on liability or contingent liability under

paragraph 2. If Developer's chooses to pay a claim under paragraph 2, not on the basis of liability, but rather on the basis of "expediency or otherwise," then a right to indemnification does not arise under paragraph 1. This gives meaning to all terms in the subject Agreement, including the term "expediency." *See Bogomolov*, 131 Wn. App. at 361-62. Significantly, the testimony at trial by Mr. White was that Developer's decision to pay the claim was a business decision based upon "expediency."

According to the testimony of Developer's own in-house counsel, the language of this agreement was confusing. Mr. White was clearly hesitant to construe any parts of the parts of the Agreement, and in fact agreed that its terms were difficult to understand:

> Q. Okay. I'd like to direct your attention to subparagraph B. And it's an additional -- it goes on to describe, again, what the indemnifier's obligations are, is that "Pay surety any additional premium upon execution of each bond computed under the basis of contract rights regardless of the amount of any such bond in accordance with rates in effect at the time such bond is issued and pays Surety or receives from Surety, as the case may be, a premium computed of a difference in contract price occurring in progress or upon completion of the project or operation for which a bond is executed."
>
> So would you agree that that's at least a mouthful?
>
> A. Yeah, absolutely. As I said, <u>we don't normally use English, unfortunately</u>. Yes, it is a mouthful.

RP 559-60 (emphasis added).

He even described his own documents as "gobbledygook speak." RP 464. In fact, Mr. White himself could not state why the indemnity agreement contained the term "expediency":

> Q. (By Mr. Jensen) Do you know why Developer's Surety decided to use the term "expediency" in paragraph 2 of the indemnity agreement? Do you know why? It's my only question. Yes or no.
>
> A. I did not draft this. In the great abstract, no, I don't know why -- what their thinking was, but I know what it means in my view.

RP 589.

Mr. White admitted that the language used in the Agreement was not even "English" and suggested to counsel that one should reference a dictionary in order to clarify the meaning of words contained in Developer's own documents. RP 592. Mr. White was correct in this point. Washington law also requires that where the terms to an agreement are not defined, the court should look to their ordinary meaning. *Bellevue Sch. Dist.*, 38 Wn. App. at 159. The American Heritage Dictionary defines "expediency" as "[a]ppropriateness to the purpose at hand" and "[a]dherence to self serving means." American Heritage College Dictionary, 1993 Edition. In this instance, Developer's decision to pay the County was profoundly self serving and reflected Developer's choice to

litigate against its own principal rather than the County. *See* RP 485-87. These actions precisely fit the dictionary definition of "expediency."

The Agreement in this case is clearly ambiguous based on the use of the terms "liability" and "contingent liability" in paragraph 1, which sets out when indemnity is available and use of the term "expediency" in paragraph 2, which allows for payment by the surety of a claim under nearly any circumstance. It is a well established rule of construction that if a contract is equally susceptible to two or more constructions, it shall be construed against the drafter of the contract. *Nunez*, 144 Wn. App. at 351; *See Also Seattle First National Bank v. Hawk,* 17 Wn. App. 251, 562 P.2d 260 (1977); *N. Pac. Ry. v. Sunnyside Valley Irrigation Dist.,* 85 Wn.2d 920, 922, 540 P.2d 1387 (1975).

The Agreement at issue was admittedly drafted by Developer's and was considered confusing by Developer's own claim counsel.[2] RP 558-59. In construing the Agreement, under its most reasonable reading, the term "expediency" would include a business decision such as the one made by Developer's when it paid the County. Thus, no right to indemnity arose, as a matter of law.

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[2] As briefed below, the evidence in this case also demonstrates that the Agreement at issue is an unconscionable adhesion contract, and as such, the enforcement of it should be discouraged a matter of public policy.

Mr. White even conceded at trial that Developer's decision to pay was a business decision, and that a business decision would fall within the definition of expediency:

> Q. And my question to you is whether that decision was, in fact, a business decision by DSI. Is that accurate?
>
> A. Generally, yes.
>
> ***
>
> Q. Would you agree that expediency would include a business decision by the surety to pay based on a lot of things that you talked about in your direct examination, attorneys' fees, exposure, bad faith exposure? Would you agree that that is a business decision that would fit within the definition of "expediency"?
>
> A. Yes.

RP 555, 564.

Incredibly, Mr. White's testimony is the most compelling evidence that Developer's decision to pay the claim was based on expediency, not liability or contingent liability. There was no conflicting evidence on this point. It should be accepted as a verity on appeal.

Under these definitions accepted by Developer's, the Agreement must be construed to grant no indemnity rights to Developer's.

Given Mr. White's testimony, the construction advanced by Aarohn Construction must be accepted as the only reasonable

interpretation of the Agreement. Developer's drafted this agreement and Developer's payment was characterized by its own counsel as expedient.

Even if the Court determines that the Agreement is susceptible to the interpretation advanced by Developer's, the conclusion is the same. It remain ambiguous and the Agreement must be construed against its drafter and in favor of Aarohn Construction. *Nunez*, 144 Wn. App. at 351. *See also Luna v. Gillingham*, 57 Wn. App. 574, 579-80, 789 P.2d 801 (1990).

In *Luna*, the Court found the term "gross recovery" in a contingent attorney fee agreement to be ambiguous because it did not state whether gross recovery included court-awarded attorney fees. 57 Wn. App. at 579-80. The attorney's client argued that the agreement did not require the attorney fees to be calculated to include the court-awarded fees. This Court agreed and found that because the term "gross recovery" was ambiguous, the agreement must be construed against the drafter, the attorney, and in favor of the client. *Id.* 57 Wn. App. at 581.

Under Aarohn Construction's reading of the Agreement, when Developer's decided to pay a claim under paragraph 2 based on "expediency" rather than "liability" or "contingent liability," it had no right to indemnity under paragraph 1 as a matter of law.

Under Developer's construction, however, it can pay the underlying claim and then seek indemnity whenever it wants, and the word expediency has no meaning.

The evidence at trial including Developer's own admissions, supported only the conclusion that Developer's right to indemnity was never triggered. When the trial court accepted Developer's unreasonable, or less reasonable construction, it committed reversible error by denying the motions to dismiss brought after Developer's case and after trial.

C. *A Surety that Pays a Doubtful Claim Based on Expediency Forfeits its Right to Indemnification.*

Wholly apart from any ambiguity in the Agreement, case law supports the proposition that where a surety that pays a doubtful claim based on expediency or otherwise, it forfeits its right to indemnity from the principal.

The Supreme Court has Recognized That a Surety Forfeits Its Right to Indemnification by Paying Doubtful Claim. The Washington Supreme Court recently reaffirmed that "[i]f a surety pays a doubtful claim, it may forfeit its right to indemnification." *Colo. Structures, Inc. v. Ins. Co. of the West*, 161 Wn.2d 577, 629, 167 P.3d 1125 (2007) (Madsen, J., dissenting). The majority and the dissent in *Colorado Structures*

agreed on this one principle, even though they were otherwise divided. Justice Chambers elaborated on this point in the majority opinion:

> **Indemnity, however, is not a foregone conclusion. A surety who wrongfully pays an obligee may, as the dissent notes, 'forfeit its right to indemnification.'** [Dissent] at 629. Thus, the dilemma facing the surety is not to balance its duty to the principal with its duty to the obligee. Rather, it must balance its duty to the obligee against its own self-interest. The surety must choose whether a principal has or has not defaulted and thus whether payment is owed the obligee. **But the risk of a wrongful decision falls on the surety, not the principal.**

Id., at 605 n. 15. Justice Madsen correctly noted in her dissent, that a surety has a "divided loyalty to the obligee and the principal." *Id.*, at 629 (Madsen, J., dissenting).

The *Colorado Structures* opinion makes clear that if a surety decides to pay a doubtful claim, the consequences of the surety's decision fall not on the principal (here, Aarohn Construction), nor on the obligee (the County), but rather on the surety itself. Such is the risk that sureties take when they pay doubtful claims, a risk for which they are compensated by their principal's own premiums paid in advance.

The idea that a surety that pays a doubtful claim may forfeit its right to indemnity from the principal is recognized in the *Restatement (Third) of Suretyship & Guaranty* (1996). Section 24(2) of the *Restatement* states that the duty of a principal obligor (Aarohn

Construction) to reimburse a secondary obligor (Developers) does not arise if the secondary obligor fails to conduct a "reasonable" inquiry into whether the primary obligor has any defenses to the underlying obligation (the contract between Aarohn Construction and the County).[3]

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[3] The *Restatement* provides;

> § 24 **When the Duty to Reimburse Does Not Arise**
>
> (1) Notwithstanding § 22, **the principal obligor has <u>no duty to reimburse the secondary obligor</u> to the extent that**:
>
> (a) if the underlying obligation is contractual, the principal obligor is not liable because of its lack of capacity to enter into that obligation;
>
> (b) the principal obligor had a defense to the underlying obligation that, pursuant to the terms of the secondary obligation, was not available to the secondary obligor;
>
> ***
>
> (c) **at the time of performance or settlement of the secondary obligation, <u>the secondary obligor had notice of a defense of the principal obligor to the underlying obligation</u> that was available to the secondary obligor as a defense to the secondary obligation** (§ 34), **<u>unless it was a reasonable business decision for the secondary obligor to perform or settle the secondary obligation in light of factors, amounting to business compulsion</u>**, of which the principal obligor had notice at the time it incurred the underlying obligation; or
>
> (2) For purposes of subsection (1)(e), **a secondary obligor has notice of a defense of the principal obligor to the underlying obligation available to the secondary obligor**

In this regard, the testimony at trial was that Developer's did not undertake a reasonable inquiry into whether Aarohn Construction had any defenses to the County's claim that Aarohn Construction had defaulted. Rather, according to Lou White, Developer's decision to pay the secondary obligation (to Pierce County) was entirely a "business decision." RP at 555.

The evidence was uncontroverted that Developer's conducted no investigation as to any defenses Aarohn Construction may have had. Instead, it opted to pay the County and litigate against its principal rather than the much more substantial adversary, the County:

> Q. And you talked about why you made that decision to pay Pierce County.
>
> A. Right.
>
> ***
>
> Q. It was a factor in making the business decision, right?
>
> A. Yes, sure.

RP 578-79 (Mr. White testimony).

> **as a defense to the secondary obligation if that defense would be revealed to the secondary obligor <u>by making such inquiry of the principal obligor as is reasonable under the circumstances to ascertain whether the principal obligor claims any defenses</u>.**

Developer's received a demand letter from the County, which threatened to sue Developer's for bad faith if it failed to pay the claim. CP 444-45. Developer's determined that it faced the risk of incurring its own attorney fees, additional damages, and the County's attorney fees. RP 485-87. It was unwilling to incur this risk and made the business decision to pay the claim. *Id.*

In the absence of any evidence of an investigation by Developer's into Aarohn Construction's defenses, Developer's is not entitled to indemnity from Aarohn Construction as a matter of law.

D. *The Trial Court's Interpretation of the Indemnity Provision Renders it Unconscionable.*

An unconscionable contract is unenforceable *Walters v, A.A.A. Waterproofing*, 151 Wn. App. 316, 329-30, 211 P.3d 454 (2009) (holding that the unconscionable provisions of an employment contract were unenforceable). In determining whether a contract is unconscionable, the court must scrutinize "all of the circumstances surrounding the transaction in question." *Christiansen Bros. v. State of Washington*, 90 Wn.2d 872, 877, 586 P.2d 840 (1978), *overturned on other grounds in, Scoccolo Construction, Inc. v. City of Renton*, 158 Wn.2d 506, 145 P.3d 371 (2006).

There are two forms of contractual unconscionability – substantive and procedural. *Christiansen Bros.*, 90 Wn.2d at 878. Substantive

unconscionability occurs when a clause or term in the contract is one sided or overly harsh. Procedural unconscionability exists where there is impropriety during the bargaining process. *Id.* This occurs when one side has a lack of a meaningful choice. To make this determination, the court looks to the manner in which the contract was entered; whether each party had reasonable opportunity to understand the terms of the contract; and whether the important terms were conspicuous. *Id. See also Schroeder v. Fageol Motors, Inc.*, 86 Wn.2d 256, 260, 544 P.2d 20 (1975). An unconscionable contract is not enforceable. *Walters*, 151 Wn. App. at 329-30.

In *Walters v. A.A.A. Waterproofing*, the court found an arbitration agreement substantively unconscionable in an employment contract where it contained a reciprocal attorney fee provision. 151 Wn. App. at 324-25. The court held that such a provision would deter an employee from suing his employer because the risk of having to pay his employer's attorney fees would present an "enormous deterrent" to pursuing a claim. *Id.* Accordingly, the court refused to enforce the provision. *Id.* at 325.

Here, the indemnity agreement, it is both substantively and procedurally unconscionable. Under the construction advanced by Developer's, Aarohn Construction's termination itself would trigger liability regardless of how arbitrary or unfounded the termination was.

Not only is a key term of the Agreement stripped of any meaning, Aarohn Construction now faces the overly harsh result of having to pay a claim no matter what happened. According to the testimony of Developer's own witnesses, its rights are absolute and Aarohn Construction has none. RP 610-11; *See also* RP 458 (Mr. White testified that "[i]f the surety or bonding company loses money, that contractor agrees to pay the bonding company back. That's in the simplest terms."). As discussed above, Developer's claims attorney admitted that its terms were "gobblegook." The interpretation of the Agreement that the trial court accepted resulted in the enforcement of an unconscionable contract.

Further, Aarohn Construction lacked a meaningful choice in entering into the Agreement, which constitutes procedural unconscionability. Aarohn Construction was presented with a form contract of adhesion to sign. Presumably, if it failed to sign the Agreement, Developer's would not provide the bond. If Aarohn Construction did not procure the bond, it lost the contract with the County. CP 480. Aarohn Construction was not able to negotiate the terms of the Agreement nor was it entitled to make any changes to the form Agreement. RP 558-59. Rather, it had two choices – sign or lose the job.

The trial court erred when it failed to dismiss Developer's claims under the Agreement where that Agreement was both procedurally and

substantively unconscionable as a matter of law and was therefore, unenforceable. *See Walters*, 151 Wn. App. at 329-30. Accordingly, there is another independent basis for reversing the trial court's decision.

E. *The Trial Court Erred When it Failed to Dismiss Developer's Complaint for Lack of Subject Matter Jurisdiction.*

At trial, Aarohn Construction also based its Motions to Dismiss on a lack of jurisdiction. Under Washington law, the trial court lacked subject matter jurisdiction over this matter because it was not filed in the same county as the real property out of which the case arises:

> Actions for the following causes shall be commenced in the county in which the subject of the action, or some part thereof, is situated:
>
> (1) For the recovery of, for the possession of, for the partition of, for the foreclosure of a mortgage on, or for the determination of all questions affecting the title, or for any injuries to real property.

RCW 4.12.010 (emphasis added.) Actions described in RCW 4.12.010, which must be brought in the county where the property is located, are called "local." "Transitory" actions are those described in RCW 4.12.025, which may be brought where the defendant resides.

RCW 4.12.010 is mandatory and jurisdictional, and its requirements cannot be waived. A tribunal's lack of jurisdiction may be raised by a party or the court at any time. *Okanogan Wilderness League, Inc. v. Town of Twisp*, 133 Wn.2d 769, 788, 947 P.2d 732 (1997).

In the present case, Developer's claims attorney admitted that the claims arise out of injury to real property, in this case the Pierce County Annex:

> Q. Okay. So would you agree that part of the claim of Pierce County was for injury to this physical property, including the Pierce County Annex property?
>
> A. Yeah. Damage, injury, yes.
>
> Q. Okay. So injury to the property, right?
>
> A. Yeah. Broadly speaking, right.

RP 554 (testimony of Mr. White) (emphasis added).

These allegations of injury to the real property include damages to the Annex Building, breakage of underground irrigation pipes, and injury to the vegetation. *See, e.g.,* CP 568-69. The use of "any injuries to real property" contained in the statute establishes that the requirement is mandatory. RCW 4.12.010 (emphasis added). Thus, the trial court's failure to dismiss for lack of jurisdiction was in error and should be reversed.

III. DEVELOPER'S WAS NOT ENTITLED TO PREJUDGMENT INTEREST FOR UNLIQUIDATED DAMAGES.

A party is only entitled to prejudgment interest where the claim is "liquidated or readily determinable." *Hansen v. Rothaus*, 107 Wn.2d 468, 472, 730 P.2d 662 (1986). An unliquidated claim does not enable a party to collect prejudgment interest. *Id.*

A liquidated claim is one in which "the evidence furnishes data, which, if believed, makes it possible to compute the amount with exactness, without reliance on opinion or discretion." *Id.* (quoting *Prier v. Refrigeration Eng'g Co.*, 74 Wn.2d 25, 32, 442 P.2d 621 (1968)). In contrast, an unliquidated claim is one in which:

> [T]he exact amount of the sum to be allowed cannot be definitely fixed from the facts proved, disputed or undisputed, but must in the last analysis **depend upon the opinion or discretion of the judge or jury** as to whether a larger or a smaller amount should be allowed.

Id. (Emphasis added).

Here, the jury was required to determine the sum, if any, that Developer's was entitled to. This was based upon a consideration of whether Developer's was reasonable in its investigation of the County's claim and upon whether the amount paid under the bond was justified or should be reduced in some fashion. Conflicting evidence was presented on both sides regarding the amount the County should have been paid, if anything. This was not a claim involving a fixed, calculated amount.

There were significant issues regarding the County's claim, including whether or not Aarohn Construction was entitled to more time to complete the Project for the County. According to construction expert Mark Lawless, Aarohn Construction was reasonable in its requests for additional time. RP 1208-09. Moreover, the amount paid was in

controversy as the scope of Serpanok's repair work exceeded the scope of the original contract. *See* RP 1222-23.

Significantly, the jury in this case did not award the full amount Developer's paid to the County because in its discretion, that amount was not supported by the facts. Rather, it concluded that a discount was warranted in light of the facts. *See* CP 695-97. The award itself is evidence of the discretion exercised by the jury and of the fact that the damages in this case were unliquidated. Thus, Developer's is not entitled to prejudgment interest.

IV. AAROHN CONSTRUCTION REQUESTS THIS COURT AWARD COSTS ON APPEAL

Under RAP 14.2, this Court may award costs to the prevailing party on appeal. Aarohn Construction respectfully requests an award of its costs incurred for this Appeal.

V. CONCLUSION

The trial court erred when it failed to grant Aarohn Construction's Motion for Directed Verdict and Motion to Dismiss after Developer's case. Developer's failed to present evidence regarding its entitlement to seek indemnity where the contract contained an express triggering event and payment was made for the sake of expediency, a non-triggering event. Additionally, even if the Developer's construction of the Agreement is

considered, the only reasonable interpretation compels the conclusion that there was no indemnity available to Developer's. The Agreement was also unconscionable and thus unenforceable. Further, the trial court erred when it failed to dismiss for lack of jurisdiction and allowed Developer's pre-judgment interest for unliquidated damages.

RESPECTFULLY SUBMITTED this 28 day of October, 2009.

MERRICK, HOFSTEDT & LINDSEY, P.S.

By _____
David B. Jensen, WSBA #21284
Holly E. Hinterberger, WSBA #37281
Attorneys for Appellants