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No. 86535-3

SUPREME COURT  
OF THE STATE OF WASHINGTON

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NATIONAL SURETY CORPORATION,

Petitioner,

v.

IMMUNEX CORPORATION,

Respondent.

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ANSWER OF PETITIONER NATIONAL SURETY CORPORATION  
TO AMICUS CURIAE BRIEF OF WSAJ FOUNDATION

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## I. INTRODUCTION

The amicus brief submitted by Washington State Association for Justice Foundation (WSAJ) rests on several unfounded assumptions about the nature of an insurer's good faith duty to defend subject to a reservation of rights that is at issue in this case. First, contrary to WSAJ's argument (WSAJ 5, 10-11), the good faith duty to defend is intended to protect, not fulfill, the contractual duty to defend. Second, there is no support for WSAJ's claims that a *contractual* duty to defend "applies until a court determines that the underlying claim is clearly not covered" (WSAJ 8) or that "a court declaration that the duty to defend does not apply is prospective only." (WSAJ 13) Finally, WSAJ's argument why an insurer should not be allowed to *recoup* costs it previously paid in defending an uncovered claim (WSAJ 14-15), actually proves why an insurer should not be required to *reimburse* its insured for the costs of defending an uncovered claim, and particularly for costs the insured incurred before tender.

National Surety agrees with WSAJ that a reservation of rights is "mere *notice*" (WSAJ 14, emphasis in original) that an insurer is asserting its contractual rights under the policy, and does not *create* a right to recoup defense costs. But that does not

answer the question raised by this case: whether an insurer that has no duty under its policy to defend its insured, that never waived its right to assert the terms of that contract, and that met its good faith obligation to protect the insured's interests under the policy, must nevertheless reimburse its insured for the cost of the defense as though it had contracted to do so after the courts have confirmed that it had no duty to defend under the clear and unambiguous terms of the policy. Consistent with this Court's prior case law, public policy, and the statutory duty of both insured and insurer to "preserv[e] inviolate the integrity of insurance," RCW 48.01.030, the answer to this question must be "no."

## **II. ARGUMENT IN RESPONSE TO AMICUS**

### **A. The Good Faith Duty To Defend Is Intended To Protect, Not Fulfill, The Contractual Duty To Defend.**

Amicus WSAJ Foundation asserts that the "contractual duty to defend is unaltered" when an insurer defends under a reservation of rights (WSAJ 5), and that as a consequence the Court should hold in this case that the insured Immunex is entitled to reimbursement of the cost of defending itself against uncovered claims, including costs voluntarily incurred years before any tender to National Surety. But the good faith duty to defend pending a

determination of coverage is intended only to protect, not to fulfill, the contractual duty to defend. Imposing a duty to retroactively pay defense costs voluntarily incurred by an insured in the absence of a contractual duty to defend, as proposed by WSAJ, would rewrite the parties' contract.

As explained in National Surety's Supplemental Brief at 2-3, insurers have a good faith duty to defend tendered claims as a matter of public policy pending a resolution of disputes about coverage under *Woo v. Fireman's Fund Ins. Co.*, 161 Wn.2d 43, 164 P.3d 454 (2007) and *American Best Food, Inc. v. Alea London, Ltd.*, 168 Wn.2d 398, 229 P.3d 693 (2010). The duty is not "free-floating" (WSAJ 11), but is intended to protect the insured's right to a defense under the policy if a court determines that the claim is potentially covered, and to alleviate the harm of depriving the insured of "one of the principal benefits of the liability insurance policy," *Woo*, 161 Wn.2d at 54, ¶ 19, if a court determines that the insurer has a contractual duty to defend.

But the good faith duty to defend is not itself a contractual duty. Nor does it change the parties' obligations under the insurance policy. Here, while it is undisputed that National Surety fulfilled its *good faith* duty to defend, it is also undisputed that the

policies at issue did not impose upon National Surety a *contractual* duty to defend Immunex against the AWP claims.

An insurance policy is interpreted as a contract, and will be enforced pursuant to its clear and unambiguous terms:

The criteria for interpreting insurance contracts in Washington are well settled. We construe insurance policies as contracts. *Weyerhaeuser Co. v. Commercial Union Ins. Co.*, 142 Wn.2d 654, 665, 15 P.3d 115 (2000). We consider the policy as a whole, and we give it a “ ‘fair, reasonable, and sensible construction as would be given to the contract by the average person purchasing insurance.’ ” *Id.* at 666 (quoting *Am. Nat’l Fire Ins. Co. v. B&L Trucking & Constr. Co.*, 134 Wn.2d 413, 427-28, 951 P.2d 250 (1998) (quoting *Key Tronic Corp. v. Aetna (CIGNA) Fire Underwriters Ins. Co.*, 124 Wn.2d 618, 627, 881 P.2d 201 (1994))). Most importantly, if the policy language is clear and unambiguous, we must enforce it as written; we may not modify it or create ambiguity where none exists. *See id.*

***Quadrant Corp. v. Am. States Ins. Co.***, 154 Wn.2d 165, 171, ¶10, 110 P.3d 733, 737 (2005). Contrary to these long-established principles, amicus WSAJ asks this Court to rewrite the parties’ contract to impose obligations on National Surety that were never part of the insurance policy, and that National Surety unambiguously did not undertake.

The policy at issue here gave National Surety the right to defend suits alleging covered claims – *not* the obligation to

reimburse its insured Immunex for the cost of defending uncovered claims that its insured had independently and voluntarily incurred, largely without notice and long before tender to its insurer National Surety. Under the policy, National Surety had “the right and duty to . . . defend any Insured against any Suit, seeking damages . . . to which Coverage B applies.” (CP 630-31) (emphasis in original omitted). But under the terms of the policy, National Surety had no other obligation to defend Immunex, or to pay its defense costs for uncovered claims. The policy expressly stated that National Surety would “have no duty to defend any insured against any Suit seeking damages . . . to which Coverage B does not apply.” (CP 631)

This Court denied Immunex’s petition for review of Division One’s decision that there was no basis for Immunex’s (belated) claim that the AWP litigation was potentially encompassed by Coverage B, and that consequently National Surety could have any contractual duty to defend those claims. 162 Wn. App. at 770-73, ¶¶ 11-20. There is therefore no question that “the duty to defend never existed under the policy.” (WSAJ 10) And far from leaving the parties’ contractual duties “unaltered” (WSAJ 5), WSAJ’s argument for imposing an obligation on an insurer to reimburse its insured for the voluntarily incurred costs of defending uncovered

claims after a final determination has been made that the claims were, indeed, uncovered, would significantly change the parties' obligations under the policy and rewrite the insurance contract.

**B. There Is No Support For WSAJ's Claim That A Court's Determination That An Insurer Has No Contractual Duty To Defend Is Only "Prospective."**

As WSAJ rightly concedes (WSAJ 4), National Surety had no duty to defend any of the claims tendered by Immunex under the policy. WSAJ nevertheless argues that National Surety had a *contractual* duty to defend "until a court determine[d] that the underlying claim [was] clearly not covered" (WSAJ 8), and that "a court declaration that the duty to defend does not apply is prospective only." (WSAJ 13). These arguments are unsupported in WSAJ's briefing and do not bear reasoned analysis.

WSAJ cites *Alea*, 168 Wn.2d at 405, for the first proposition, that "[t]he duty to defend applies until a court determines that the underlying claim is clearly not covered." (WSAJ 8) But neither *Alea* nor any of the authority it cites says that. Instead, the cited page from *Alea* sets out an insurer's good faith obligation to defend under a reservation of rights, ending with a quotation from *Truck Ins. Exchange v. VanPort Homes, Inc.*, 147 Wn.2d 751, 760, 58 P.3d 276 (2002), quoting *Kirk v. Mt. Airy Ins. Co.*, 134 Wn.2d 558,

563 n.3, 951 P.2d 1124 (1998), that makes clear that if an insurer takes “that course of action,” “the insured receives the defense promised and, *if coverage is found not to exist, the insurer will not be obligated to pay.*” (emphasis added)

This Court’s reasoning in ***Alea*** thus supports not WSAJ’s argument, but National Surety’s position that it has no obligation to pay the cost of defending uncovered claims. WSAJ claims that “[t]his language from ***Kirk*** seems to refer to the duty to indemnify.” (WSAJ 14 n.5) But there is nothing in ***Kirk***, or in ***VanPort*** or ***Alea***, that supports that gloss. Indeed, there was a *contractual* duty to defend in each of these cases, and the quoted language relies on the insured’s right to receive “the defense promised.” ***Kirk***, 134 Wn.2d at 563 n.3.

Here, however, in its contract with Immunex National Surety did not “promise” to defend, but expressly disavowed the obligation to defend, uncovered claims. It is not National Surety, but WSAJ, that conflates the duty to defend with the duty to indemnify (WSAJ 12) in arguing that National Surety nevertheless could have a contractual duty to pay the cost of defending uncovered claims pending a determination of coverage.

WSAJ cites *no* authority for its second proposition that '[u]nder Washington law, a court declaration that the duty to defend does not apply is prospective only." (WSAJ 13) Nor is there any authority for such a proposition in the law governing the interpretation of insurance contracts. Instead, "the court cannot rule out of the contract language which the parties thereto have put into it, nor can the court revise the contract under the theory of construing it, nor can the court create a contract for the parties which they did not make themselves, nor can the court impose obligations which never before existed." ***Farmers Ins. Co. v. Miller***, 87 Wn.2d 70, 73, 549 P.2d 9 (1976).

Courts interpret contracts; they do not create them. The good faith duty to defend pending a determination of coverage provides important benefits to the insured, but the duty is one imposed as a matter of public policy, not by contract. There is no support for WSAJ's claim, critical to its analysis, that the court's determination that National Surety never had a contractual duty to defend Immunex applied only prospectively.

**C. A Reservation Of Rights That Notifies The Insured That The Insurer Intends To Assert Its Right Under The Policy Not To Defend Uncovered Claims Does Not Violate The "Equal Consideration" Rule.**

All National Surety seeks here is confirmation of its contractual right not to pay for the defense of uncovered claims now that a determination of non-coverage has been made. Contrary to WSAJ's arguments (WSAJ 14), National Surety does not claim that its reservation of rights letter creates or governs that right. All National Surety's reservation of rights did was reserve its right to rely upon the express terms of its contract with Immunex.

Just as the parties' contract did not obligate National Surety to pay, and National Surety expressly disavowed the obligation to pay, for the defense of uncovered claims, the parties' insurance contract did not prevent National Surety from offering to pay defense costs and asserting its right to recoup any payments made once a court determined that National Surety had no contractual duty to defend. Nothing in the parties' insurance contract, or elsewhere, prevented National Surety from limiting its offer to pay defense expenses to those incurred after tender. And there has been no suggestion, by either Immunex or WSAJ, that National Surety failed to fulfill its contractual or good faith duties in

responding to Immunex's untimely tender of the uncovered AWP claims by asserting its contractual rights.

Imposing an obligation to reimburse an insured for defense costs in these circumstances, in the absence of a contractual duty to defend, would undermine the reciprocal duty of good faith imposed upon both insureds and insurers under Washington law:

The business of insurance is one affected by the public interest, requiring that all persons be actuated by good faith, abstain from deception, and practice honesty and equity in all insurance matters. Upon the insurer [and] the insured . . . rests the duty of preserving inviolate the integrity of insurance.

RCW 48.01.030. Worse, extending that obligation to include costs incurred by an insured before tender would discourage an insured from promptly notifying and tendering the defense of claims to its insurer, and undermine the ability of an insurer to obtain a prompt resolution of the issue of coverage by filing a declaratory judgment action.

"Certainly breach of the duty to defend cannot occur before tender. The scope of a duty, however, is defined not by its breach, but by the contract." *Griffin v. Allstate Ins. Co.*, 108 Wn. App. 133, 141, 29 P.3d 777, 36 P.3d 522 (2001) (citing *Public Utility Dist. No. 1 v. International Ins. Co.*, 124 Wn.2d 789, 804-05, 881

P.2d 1020 (1994)), *rev. denied*, 146 Wn.2d 1005 (2002). Here, National Surety had no obligation to defend Immunex under the terms of their contract. And it could have had no good faith duty to defend before Immunex tendered the uncovered AWP claims in October 2006.

Nor does an insurer's assertion of its right to rely on the terms of the parties' contract violate the "equal consideration" rule adopted in *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986). The "equal consideration" rule does not change the terms of the policy, and it does not require an insurer (or authorize the court) to disregard those terms, even when they do not favor coverage. To invoke the rule, an insured must show "actual harm" as a result of the insurer's conduct. *St. Paul Fire and Marine Ins. Co. v. Onvia, Inc.*, 165 Wn.2d 122, 133, ¶ 24, 196 P.3d 664 (2008). Here, Immunex indisputably has suffered no harm. It had no right to a defense under the policy, and it controlled its defense of the uncovered AWP claims throughout. Neither National Surety's assertion of its contractual right not to defend uncovered claims nor its offer to pay defense costs after tender violated the "equal consideration" rule.

**D. Under WSAJ's Reasoning, An Insurer That Has Not Had The Opportunity To Exercise Its Contractual Right To Control The Defense Should Have No Obligation To Reimburse Its Insured For The Cost Of Defending Uncovered Claims.**

In limiting its argument to an insurer's right to recoup costs it has actually incurred in defending an insured after prompt tender of a claim by its insured (WSAJ 2),<sup>1</sup> amicus WSAJ also disavows any analysis of the real issue in this case – whether Immunex is entitled to be reimbursed for the cost of defending uncovered claims. WSAJ addresses an issue this Court need not resolve to hold that Immunex has no right to be reimbursed for the costs that it incurred in defending uninsured claims, in large part years before its October 2006 tender to National Surety. But WSAJ's reasoning supports National Surety's argument against reimbursement.

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<sup>1</sup> That is not the situation here. Immunex defended itself, without tender to its insurer National Surety, for at least six years, until shortly after Immunex (and its obligations) were purchased by Amgen. (CP 1059) In its October 2006 "tender" letter, Amgen announced that it was close to finalizing a settlement of the California AWP litigation against Immunex, identified nine of the 23 suits for which it now claims defense costs, under policies dating back to 1997, and demanded payment of "reasonable defense expenditures incurred, and to fund reasonable settlements. . . ." (CP 1059-60) Thus, Immunex controlled its defense for many years without tender to National Surety, and only sought reimbursement of defense costs after it had fully litigated and reached a settlement of significant portions of the AWP litigation.

In arguing that the insurer's duty to defend its insured should not be subject to a right to recoup the cost of defending uncovered claims (WSAJ 11-15), WSAJ relies heavily on Thomas V. Harris, *Washington Insurance Law* (3d ed. 2010). Harris reasons that "[a]n insurer's *duty* to defend is one of the 'main benefits' that an insured receives when he purchases a policy. Because of its duty to pay covered losses, the *right* to control the defense is equally important to an insurer." Harris, § 17.01, at 17-5-17.6 (emphasis in original) (footnote omitted).

Harris explains that recoupment of expenses actually paid by an insurer that controls the defense of a claim is inappropriate because "[p]rior to withdrawing its defense, an insurer has managed and controlled the defense, selected counsel, agreed to counsel's billing rate, made all decisions regarding the proportionality of attorney fees to the amounts at issue, and decided whether or not to seek early settlement rather than incur disproportionate fees and defense costs." Harris, § 17.01, at 17-2. The premise of Harris' and WSAJ's argument that "retroactive reimbursement for attorney fees and defense costs already incurred by the insurer" should not be allowed thus is that the insurer has exercised a contractual right to control the defense.

(See WSAJ 11, addressing “the insurer’s selection of defense counsel, negotiation of the terms of engagement, and management and control of the defense”).

Here, however, none of the litigation decisions important to the *right* to defend were left to National Surety. National Surety did not select counsel, did not approve the hiring of experts, and had no say in the litigation strategy that Immunex’s defense counsel pursued for years before Immunex, on the eve of settling them, belatedly tendered defense of the AWP claims. Nor did National Surety actually incur the expenses that Immunex now demands it to retroactively reimburse – *not* because it refused to defend its insured, but because Immunex did not tender, and instead retained control of its defense until it was ready to settle the (uncovered) claims, which it only then demanded National Surety pay.

WSAJ argues that Immunex’s late tender is of no consequence to the issues on appeal, citing this Court’s cases holding that a late tender may relieve an insurer of the duty to defend and cover otherwise covered claims only if the insurer can establish prejudice. (WSAJ 6 n.3, citing *Mutual of Enumclaw Ins. Co. v. USF Ins. Co.*, 164 Wn.2d 411, 417-26, 191 P.3d 866 (2008)) That argument ignores the obvious – that Immunex’s claims are not

now, and never have been, covered claims. National Surety should not be ordered to pay defense costs not just because the claims were outside the scope of its contractual duty to defend, but because its insured Immunex's late tender prevented National Surety from exercising its good faith duty to defend and its contractual right to control that defense.<sup>2</sup>

It is Immunex, not National Surety, that improperly seeks "retroactive reimbursement" of uncovered defense costs under the analysis in Harris upon which WSAJ relies. In arguing against an insurer's right to recoupment, WSAJ disengages an insurer's *obligation* to defend from its *right* to control the defense – a right that is the underpinning of cases in other jurisdictions that restrict an insurer's right to seek recoupment of the costs of a defense that the insurer provided and controlled. See, e.g., ***American and***

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<sup>2</sup> Immunex's late tender violated not just the "prompt notice" requirements of the parties' contract. Under the policy, Immunex was obligated not only to provide National Surety with prompt notice of any claim, but to refrain from incurring any "expense, other than first aid," to "assume no obligation" without the consent of National Surety, and to "cooperate with [the insurer] in . . . defense of any Insured against any Suit." (CP 639) (emphasis in original omitted). This Court has recognized that, even in consideration of a covered claim, in the "extreme case" prejudice may be presumed if an insured violates the "cooperation" and "no action" provisions of the policy. ***Public Utility Dist. No. 1 v. International Ins. Co.***, 124 Wn.2d 789, 804-05, 861 P.2d 1020 (1994). Surely being called upon to pay the insured's pre-tender costs of defending uncovered claims presents such an "extreme case."

*Foreign Ins. Co. v. Jerry's Sport Ctr., Inc.*, 606 Pa. 584, 595, 2 A.3d 526 (2010) (“[B]y undertaking the right to defend Insured, Royal benefited by preserving its right to control the defense and to take actions to mitigate any future indemnification responsibilities”); and other cases cited at Immunex Supp. 14-16.

The distinction between reimbursement of costs an insured paid years before tender to its insurer and recoupment of expenses actually paid by an insurer is also apparent from an analysis of *Minnesota Mutual Life Ins. Co. v. Fraser*, 128 Wash. 171, 222 P. 228 (1924), the case relied upon by the Court of Appeals in holding that National Surety could be obligated to reimburse Immunex for the cost of defending uncovered claims. 162 Wn. App. at 777, ¶ 29. This Court held in *Fraser* that a life insurance company had no right to recoup advances made to its agent/salesman under the parties' contract, which made no provision for recoupment, because the insurance company's advances against earnings “were such as benefited the company generally, promoted its welfare, tended to increase its business, and in the absence of some provision in the contract from which such intent can be clearly inferred, such as that such advances were distinctly for the benefit of the agent, they were not loans . . . . and to the extent that they exceeded the

earnings under the contract are not recoverable." *Fraser*, 128 Wash. at 175.

In *Fraser*, the contract with its agent expressly required the insurance company to pay advances to the agent. Because the contract did not contain a provision requiring repayment by the agent of unearned advances, the Court recognized the insurance company was not entitled to repayment. Here, in contrast, National Surety's contract with Immunex never obligated National Surety to pay expenses incurred in defending claims that were not potentially covered. Instead, the policies at issue expressly provide that National Surety will *not* defend such claims. Accordingly, because National Surety never contractually agreed to pay the costs incurred by Immunex in defending the AWP claims, it cannot be liable for such costs, regardless of the absence of a specific recoupment provision in the policies.

By rejecting the insurance company's claim for repayment in *Fraser*, this Court left the parties where they were under the terms of their contract. That is the result National Surety proposes here as well. Because Immunex had no right to a defense under the parties' contract, National Surety has no obligation to retroactively reimburse Immunex for its costs of defending uncovered claims.

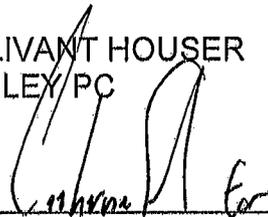
WSAJ to the contrary would obligate National Surety to pay millions of dollars in Immunex's independently incurred defense costs in the absence of either a contractual duty to defend or timely tender.

### III. CONCLUSION

No principle of law or social utility supports a multi-million dollar judgment against an insurer for defense costs previously incurred by the insured that the insurer was not contractually obligated to pay. This Court should reject WSAJ's arguments, which are not directed to the true issues before this Court, and hold that National Surety has no obligation to reimburse Immunex's costs of defending uncovered claims.

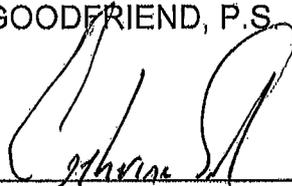
Dated this 24<sup>th</sup> day of April, 2012.

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## DECLARATION OF SERVICE

The undersigned declares under penalty of perjury, under the laws of the State of Washington, that the following is true and correct:

That on April 24, 2012, I arranged for service of the Answer of Petitioner National Surety Corporation to Amicus Curiae Brief of WSAJ Foundation, to the Court and to the parties to this action as follows:

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**DATED** at Seattle, Washington this 24<sup>th</sup> day of April, 2012.



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**Subject:** RE: National Surety v. Immunex, Cause No. 865335-3

Attached for filing in .pdf format is the Answer of Petitioner National Surety Corporation to Amicus Curiae Brief of WSAJ Foundation, in *National Surety Corporation v. Immunex Corporation*, Cause No. 86535-3. The attorney filing this document is Catherine W. Smith, WSBA No. 9542, e-mail address: [cate@washingtonappeals.com](mailto:cate@washingtonappeals.com).

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