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No. 67663-6-I

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IN THE COURT OF APPEALS DIVISION ONE  
OF THE STATE OF WASHINGTON

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WISTERIA CORPORATION, et al.,

Appellants,

v.

BOND SAFEGUARD INSURANCE COMPANY, a foreign corporation,

Respondent.

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APPELLANTS' REPLY BRIEF TO BOND  
SAFEGUARD'S RESPONSIVE BRIEF

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## I. INTRODUCTION

Comes now Appellants Chris Hatch, Stacie Hatch, and Wisteria Corporation (collectively “Wisteria”) and reply to Bond Safeguard’s Responsive Brief (“Response Brief”), filed herein. The matter on review arises from an order granting summary judgment and denial of reconsideration thereof, and concerns an open question of Washington Law. The motion for summary judgment was brought by Respondents/Plaintiffs Bond Safeguard (“Bond Safeguard”) shortly after the filing of the complaint, and arguably before Wisteria had any significant opportunity to perform discovery. *See* Response Brief at 1 (“Not long after filing its Complaint...”); *see also*, CP 165-166, 247-259; Lynn Webber Transcript, at 16:1 (July 29, 2011). The motion for Reconsideration was brought by Wisteria thereafter. *See* CP 12-13. Whether the rulings of the lower court are proper are the issues on appeal.

Bond Safeguard attempts to recast Wisteria’s argument in an effort to be dismissive of it. *See* Response Brief at 2, 12, 23 (“Best summarized as follows: [\*\*\*] miss the mark [\*\*\*] [b]ecause Wisteria has no evidence to show bad faith” they urge this Court to apply reasonableness standard); *see also*, Response Brief at 14 (assessing arguments made below and not on review). Wisteria has appealed this matter to determine the narrow

questions of: (1) what standard should be applied to a surety with respect to investigation and settlement; and having established such standard, (2) whether there is a genuine issue of material fact as to Bond Surety meeting the standard. *See* Appellants Opening Brief at 1, 12-20. Wisteria has made no argument (nor does Bond Safeguard cite to any relevant portion of Appellants Opening Brief stating such) that the success or failure of Wisteria appeal depends solely on finding the minority rule to be the standard.

**A. Reply to Respondents Statement of the Facts.**

What actions Bond Safeguard took prior to settling the case, and whether such meet the standard of a surety in Washington State are in dispute. To this end, Bond Safeguard bolsters its position by colorful adjectives and adverbs and the telling and retelling what amounts to be the same list of actions purported to have been taken by the Respondent for both Turtle Pole and Wombat DNR Claims. *See e.g.*, Response Brief at 3, 6-10. Based on Bond Safeguard's Response Brief, those actions are:

- Hoping Wisteria and DNR negotiate and claiming to participate in negotiations (*See* Response Brief at 3, 6, 7, 9, 10); *but see*, 6 (“Bond Safeguard [\*\*\*] took a more passive role”);
- “remaining optimistic” that the parties to resolve their claims; (*See* Response Brief at 3, 6, 7);

- arranging one meeting (*See* Response Brief at 7, 9);
- reviewing some emails; (*See* Response Brief at 7); see also CP 82-83 and,
- delaying payment of DNR’s claims. (*See* Response Brief at 3, 6, 7-8, 9).<sup>1</sup>

Wisteria’s fact based explanation is that there is little to no evidence in the record to support a proper investigation occurred. CP 148-149 (Hayes Letter), 159; CP 160; *see also*, CP 248:18-19; CP 250:26-251:12, 253:7-8. In fact, Bond Safeguard admits it had little knowledge, e.g., settlement was not reached “[f]or reasons unknown to Bond Safeguard” (Response Brief at 7, 10) and this lack of knowledge is precisely the point raised by Wisteria. *See* Appellants Opening Brief at 7-9; CP 148-149 (Hayes Letter), CP 159. Furthermore evidence of Bond Safeguard’s failure to investigate appears in DNR’s complaints to the Washington Office of Insurance. *See* CP 54-55 (Chronology between Dec. 26, 2006 and April 23, 2007); *see also*, CP 56 (August 1, 2007 Maas Email). Additionally, settlement was lodged over the protest of the Wisteria; and the Bond Safeguard knew of such. CP 108, 151 (Hayes letter). Had an investigation occurred, rather than passive encouragement or optimism, Wisteria asserts

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<sup>1</sup> Noticeably absent from the statement of the facts, but appearing later in the brief, is what Bond Safeguard describes as the “reality” of Bond Safeguard’s decision. *See* Response Brief at 25-26. This reality is an inflation of what is stated in Mr. Friedrich’s declarations (CP 20-33, CP 167-246) and exhibits thereto, and in factual dispute.

Bond Safeguard would know whether DNR's claims should or should not have been paid and/or Wisteria defenses prevail. CP 251:15-252:2, 253:12-14. Instead the reason Bond Safeguard settled the claim, not based on knowledge or information, but rather out of fear, convenience, or collusion with DNR. *Id. See also*, Response Brief at 3. Wisteria argues herein that such ignorance or improper motive constitutes a breach of the implied standards of care imposed on Bond Safeguard.

Bond Safeguard also utilizes its Statement of the Facts to interpret certain contract provisions and make arguments. For e.g., Wisteria had a "contractual duty to 'save the Company harmless from and against every claim'" and therefore, "[i]t was Wisteria that was duty bound to investigate and resolve the claim, not Bond Safeguard." *See* Response Brief at 6. This is neither a fair statement of the facts nor supported by the record. *See* RAP 10.3.

Finally, Bond Safeguard resorts to speculation and unsupported fact in its Statement; e.g., the assertion that had Bond Safeguard not settled, all parties would be "[m]ired down in a morass of costly litigation with DNR that would no doubt exceed the cost of DNR's original claim." Response Brief at 4.

## II. ARGUMENT

### A. Standard of Review.

In reviewing an order to grant or deny summary judgment, the Court enters into the same inquiry as the trial court, i.e., the court must consider the facts submitted and draw all reasonable inferences from the facts in the light most favorable to the nonmoving party. *Hisle v. Todd Pac. Shipyards Corp.*, 151 Wn.2d 853, 860-61, 93 P.3d 108 (2004); *Davis v. West One Automotive Group*, 140 Wn. App. 449, 456, 166 P.3d 807 (2007). Questions of fact may be determined on summary judgment as a matter of law only where reasonable minds could reach but one conclusion. *Owen v. Burlington Northern and Santa Fe R.R. Co.*, 153 Wn.2d 780, 108 P.3d 1220 (2005); *Alexander v. County of Walla Walla*, 84, Wn. App. 687, 692, 929 P.2d 1182 (1997); *see also, Moore v. Pacific Northwest Bell*, 34 Wn. App. 448, 456, 662 P.2d 398 (1983) (where there is a genuine issue as to any material fact, however, a trial is not useless, but is absolutely necessary). Here the arguments and facts show a genuine dispute concerning (1) law and (2) fact over whether Bond Safeguard properly investigated before settling its claims. Where reasonable minds could reach different conclusions, it would not be proper for the Trial Court to grant Bond Safeguard's Motion for Summary Judgment and deny Wisteria's Motion for Reconsideration.

**B. Reply to Response Brief's Contract Arguments.**

Bond Safeguard initially focuses on the role of the contract and “broad rights” afforded it under the Indemnity Agreement, including the “conclusive and binding,” “indemnification for claims paid,” and “right to settle” provisions of the contract. *See e.g.*, Response Brief at 12-16, 19, 24 (“viewed in light of the broad rights [\*\*\*] contractual rights in mind [\*\*\*] right to indemnification for claims paid to protect its own interests [\*\*\*] binding and conclusive”). Without citation to Wisteria’s Opening brief, Bond Safeguard recasts Wisteria’s Opening brief as a “threefold” argument. *See* Response Brief at 13. But these statements mischaracterize those arguments raised by Wisteria on appeal. *Compare, Id.* at 13; *with, generally,* Opening Brief at 12-20. Further, despite Bond Safeguard’s assertions otherwise, Wisteria does not advance or depend on an argument of an explicit clause in the contract to defend. *See e.g.*, Response Brief at 14-16 (Most erroneous of all [\*\*\* is Wisteria’s argument at CP 151 \*\*\*] True to Form, Wisteria asserts contract rights [\*\*\*] Wisteria cannot point to any language in the Indemnity Agreement”). Wisteria does not dispute that the contract says what it says and intends what it intends.

Instead, the arguments on appeal concern the common law exceptions to the surety’s right to indemnify. These common law exceptions derive from surety’s role of a judicial substitute, and

appropriate strategy to take when confronted with observability problems, asymmetries of information, and active protest. The freedom to contract is a social value, but it is not absolute, it is limited, as recognized even by the surety in this matter. *See* Response Brief at 17-20.

**C. Reply to Response Brief's Exception to Right of Indemnity.**

Despite contractual language, both Wisteria and Bond Safeguard recognize an implied exception to the right of a surety to seek indemnification. *See* Response Brief at 17-20, 23; Appellants Opening Brief at 16-20. At the very least, Washington implies a duty of good faith and fair dealing into all contracts. *Coventry Assocs. v. Amer. States Ins. Co.*, 136 Wn.2d 269, 961 P.2d 933 (1998); *Lonsdale v. Chesterfield*, 99 Wn.2d 353, 662 P.2d 385 (1983). However, at issue in this appeal, is whether that exception is stated or phrased under a majority (e.g., that the surety did not perform or settle in good faith) or minority rule (e.g., that the surety did not act in a reasonable and prudent manner) with respect to investigation. *See* CP 67, 71 (recommendation that the surety carefully investigates the issue of default); *compare, e.g., PSE Consulting, Inc. v. Frank Mercede and Sons, Inc.*, 267 Conn. 279, 304 (2004); *and, U.S. Fid. & Guar. Co. v. Feibus*, 15 F. Supp. 2d 579, 587 (M.D. Pa. 1998); *with, e.g., City of Portland v. Ward & Associates*, 89 Or. App. 452, 458, 750 P.2d 171, 175 (1988); *and, Hartford v. Tanner*, 22 Kan. App.2d 64, 76,

910 P.2d 872, 880-881 (1996); *and, Hawaiian Ins. & Guar. Co., Ltd. v. Higashi*, 67 Haw. 12, 13, 675 P.2d 767, 769 (1984); *and, Fidelity & Dep. Co. of Md. v. Davis*, 22 Kan. 790, 800-801, 284 P. 430 (Kan. 1930).

While the analysis may be different under each standard, it appears either standard may be breached by a surety's failure to conduct some investigation or fact-based determination (which Wisteria argues facts in the record show as much to proceed to further discovery and trial).

**1. Bad Faith May Arise from Failure to Investigate.**

Bond Safeguard argues that Wisteria is not entitled even to the minority "bad faith" standard. However, in Washington, an insurer has already been found to have acted in "bad faith," even when correctly denying a claim, if the denial was made without a reasonable investigation first. *See Coventry Assocs. v. Amer. States Ins. Co.*, 136 Wn.2d 269, 961 P.2d 933 (1998). The same can and should be said of the tri-partied relationship here.

**2. Unreasonableness May Arise from Failure to Investigate.**

In reply to the mutual protections of the surety and obligee argument (see Response Brief at 24), it is reasonable that Bond Safeguard would expect timely investigation prior to settlement, and it would be reasonable for DNR to expect the same had Bond Safeguard chosen not to settle.

**3. Reasons Why Standards Applied to Insurance Industry Should Also Apply Here, and Reply to Argument That IFCA Applies Only to First-Party Claimants.**

The business of insurance, which Wisteria asserts includes surety insurance, affects the public interest:

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

RCW 48.01.030. Washington desires that Surety's perform a reasonable and timely investigation prior to settlement of a claim. *See Industrial Indem. Co. of the Northwest v. Kallevig*, 114 Wn.2d 907, 792 P.2d 520 (1990)(the failure to conduct a good faith insurance investigation constitutes unfair and deceptive practice).

In reply to "DNR is the only party that is the functional equivalent of a first party claimant" (Response Brief at 22), and subsequent citations to the *Tank v. State Farm* case, Bond Safeguard misses the mark. *See Tank v. State Farm*, 105 Wn.2d 381, 386-387, 715 P.2d 1133 (1986)("The imposition of an insurer's duty of good faith by *both the courts* and the Legislature of this state has resulted in lawsuits *alleging breach of that duty in both nondefense and defense settings*" [emphasis supplied]).

Once again Bond Safeguard misconstrues Wisterias policy argument that the “common strategies to prohibit such practices include emphasis on information gathering; discouraging length separation from the process” in a closely related business of insurance (Appellants Opening Brief at 14-15). Had Wisteria sought a specific cause of action under WAC 284-30-300 through -600 it would have alleged so. In sum, Wisteria’s argument in its opening brief, and herein, is that this Court’s selecting of a standard should be influenced by the policies behind Insurance Commissioner’s regulation of the very relatable Insurance Industry, the common law, and prior weighing in of the legislature support the desire to have an investigation for both first party claimants and principals.

Further, with respect to Bond Safeguard’s “important function” to “construction industry” argument, the use of the surety in this case, was to circumvent the dispute resolution procedures of the contract. Both Wisteria and Bond Safeguard have a financial and economic interest in keeping DNR happy. But, the Government/Claimant’s favoring of one judicial substitute (that of the claim against the surety) over another (that of arbitration or mediation process) (*see* CP 184-186, 222), means that equivalent standards of information gathering, fairness, neutrality, and reasonableness should be followed by the favored substitute before

resolution. This means, at a minimum, a review of the facts and neutrality. Further, where the motive of the judicial substitute is based purely on self-preservation, it should not be favored.

**D. There is Evidence that Bond Safeguard Failed to Investigate.**

Bond Safeguard intersperses arguments throughout its brief concerning Wisteria's evidence of failure to investigate which are best considered in one analysis of the facts concerning investigation. (*See* Response Brief at 12, 17, 25-27).

Wisteria argues that a duty of care to investigate may be found under either the good faith or reasonableness standard. Wisteria alleges no investigation had been performed prior to settlement, as evidenced by DNR's records, Maas' correspondence, and Hayes' letter, other evidence and assertions in the record. CP 54-55 (Chronology between Dec. 26, 2006 and April 23, 2007); CP 56 (August 1, 2007 Maas Email); CP 148-149 (Hayes Letter); CP 159-160; *see also*, CP 248:18-19; CP 250:26-251:12, 253:7-8; *c.f.*, Response Brief at 1 (Summary Judgment was pursued "not long after" Bond Safeguard filed its complaint depriving Wisteria of a chance to perform further investigation). Further emphasizing that this fact is in dispute, Bond Safeguard itself effectively both admits and denies it investigated in its response brief. *See e.g.*, Response Brief at 6-7, 25 (cycling between passive encouragement, lack

of knowledge of outcome, and exhaustive internal deliberations). When read in the light most favorable to Wisteria, a reasonable person may find Bond Safeguard failed to investigate.

**E. Facts Show Wisteria Had Defenses.**

In Reply to Bond Safeguards arguments about defenses against DNR's claim (Response Brief at 24-25) and defenses being revealed (Response Brief at 27), there is evidence in the record and further determinable (had Bond Safeguard performed a reasonable investigation) that DNR was in the wrong in the alternative dispute resolution process and the underlying claims. *See* CP 145-147, 158 (that pursuant to paragraph G-240 a request to regional manager to seek other relief was made, and tersely refused); CP 184-186, 222 (violations and dispute resolution) CP 148-149, 159 (Hayes letter where Wisteria notified Bond Surety); CP 202 ("the surety intends to do nothing")

Further, argument about the existence of defenses is post hoc rationalization of Bond Safeguard's actions. Rather than perform an investigation within 30 days, Bond Safeguard chose instead to passively refrain from participation and instead settled solely to protect itself rather than as a result of an investigation.

**F. Response to Motion to Strike.**

In defense of its tardiness, Wisteria's efforts to secure representation in this technical matter have been hampered by the withdrawal of prior counsel and successful efforts by Bond Safeguard to collect upon its judgment by garnishing Wisteria's bank account. Bond Safeguard's request to strike Wisteria's opening brief is not supported by citation to any case or rule supporting such a harsh result.

To the extent Bond Safeguard is asking to strike Wisteria's appeal as some sort of sanction, it and this Court are required to make a record for doing so. *Blair v. TA-Seattle E. No. 176*, 171 Wn.2d 342, 348-49, 254 P.3d 797 (2012) (Reversing the Court of Appeals finding that the trial court did not need to set forth its reasons for imposing harsh sanction which goes to the ability of a party to present his case); *Burnet v. Spokane Ambulance*, 131 Wn.2d 484, 494, 933 P.2d 1036 (1997).<sup>2</sup>

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<sup>2</sup> The Supreme Court stated therein:

[\*\*\*] it must be apparent from the record that the trial court explicitly considered whether a lesser sanction would probably have sufficed," and whether it found that the disobedient party's refusal to obey a discovery order was willful or deliberate and substantially prejudiced the opponent's ability to prepare for trial. *Snedigar v. Hodderson*, 53 Wn. App. 476, 487, 768 P. 2d 1 (1989) (citing to due process considerations).

*Burnet*, 131 Wn.2d at 494. Other decisions establishing due process concerns with regard to a court issuing the harshest of sanctions without discussion of its reasoning for doing so: *See e.g., Hovey v. Elliott*, 167 U.S. 409, 17 S. Ct. 841, 42 L. Ed. 215 (1897); *Mitchell v. Watson*, 58 Wn.2d. 206, 361 P.2d 744 (1961). Because the harsh sanction contained no statement of grounds and had insufficient rationale for this Court to review the propriety of the COA's order dismissing claims and parties there was obvious and/or probable error and/or a such a departure from the accepted and usual course of judicial proceedings so as to call for review by this Court.

**III. THIS COURT SHOULD DENY BOND SAFEGUARD'S  
REQUEST FOR ATTORNEY FEES.**

Bond Safeguard is only entitled to fees if it is the prevailing party.  
RAP 14.2. As Wisteria should prevail, it should not be required to any  
attorney fees.

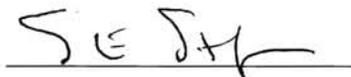
**IV. CONCLUSION**

For the aforementioned reasons, this Court should: (1) rule with  
regard to the standard of care for surety in Washington regarding a  
protested claim; (2) reverse the Superior Courts order granting summary  
judgment in favor of Bond Safeguard; and, (3) reverse the Superior  
Court's order denying Wisteria's motion for reconsideration.

DATED this 8th day of June, 2012 at Arlington, WA.

Respectfully Submitted,

By



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