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COURT OF APPEALS
DIVISION II

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No. 37194-4-II

STATE OF WASHINGTON
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DEPUTY

**COURT OF APPEALS - DIVISION II
OF THE STATE OF WASHINGTON**

TERRANCE S. COX and JULIE K. COX,

Appellants,

vs.

JAMES H. O'BRIEN, et ux, et al.,

Respondents.

APPELLANTS' REPLY BRIEF

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pm 4/24/08

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I. INTRODUCTION

Appellants Terrance and Julie Cox (Buyers) contracted to purchase a house from Respondents Danny and Mary DeMers (Sellers) in June of 2000. Sellers agreed to have a pest inspection prior to closing and hired O'Brien Home Inspection Services to perform the pest inspection. After the home sale had closed, Buyers discovered that the pest inspection had failed to reveal significant structural pest damage inside the walls of the home. Buyers settled with O'Brien and sought to have O'Brien's indemnification rights, which were assigned to buyers as part of the settlement, enforced against the sellers.

Sellers convinced the trial court in a summary judgment motion that an action in tort was barred by the economic loss rule. The trial court also ruled that the indemnification provision was barred by public policy.

In their complaint, Buyers also brought a claim of unjust enrichment against the sellers. That claim was resolved at trial by a directed verdict entered in favor of the sellers. The trial court reasoned that the sellers were not in a position where they knew or should have known about the damage to the house.

The trial court's reasoning in granting the summary judgment and the directed verdict in favor of the seller was erroneous and should be reversed.

II. RESTATEMENT OF ISSUES

- A. When the economic loss rule is applied to bar tort claims, should a contractual indemnification provision allowing the shifting of the assumption of risk for economic loss be nullified as contrary to public policy?
- B. Did the trial court incorrectly construe the indemnification language at issue when it denied buyers' cross-motion for summary judgment?
- C. Did the trial court correctly rule as a matter of law that the indemnification language was not rendered void by RCW 4.24.115?
- D. Did the trial court err in finding a directed verdict in favor of sellers was appropriate on the buyers' unjust enrichment claims?
- E. Are buyers entitled to attorneys' fees based on MAR 7.3 and damages per the indemnification provision in the inspection contract?

III. RESPONSE TO SELLERS' RESTATEMENT OF THE CASE

Home buyers Terrance and Julie Cox found the need to purchase a larger house for their growing family and sought to purchase one from Danny and Mary DeMers that had previously been used as a rental. *CP 170-202; RP 7*

After Mr. and Mrs. Cox made a cursory inspection of the home (which was occupied at the time by renters) they agreed on a price and entered into a Purchase and Sale Agreement with sellers. *RP 8, 10.* A condition of the sale was for the sellers DeMers to provide a pest inspection on the home. *RP 14-15.* DeMers selected and hired O'Brien Home Inspection Services. *RP 14.* Unfortunately, O'Brien failed to detect insect infestation and structural damage inside the walls of the home in his report dated July 31, 2000. *CP 170-202*

In his contract, O'Brien required DeMers to sign an inspection contract which included an indemnification provision. *CP 170-202* A copy of the agreement signed by the sellers is attached as Exhibit A to the appellants' opening brief. O'Brien also requested home buyers Cox to sign the agreement which they did. *CP 170-202*

After the buyers took possession of the home, they discovered significant damage to the home. *CP 170-202* They filed a lawsuit against home inspector O'Brien who tendered defense of the claim to the sellers pursuant to the indemnification agreement. *CP 161-169* The sellers did not respond to the tender but notified their insurance company. *RP 13-14, 32-33* Pest inspector O'Brien named the sellers as third party defendants and they were defended by their insurance carrier. *CP 11-15*

Home buyers Cox ultimately settled with O'Brien. *CP 170-202* As part of the settlement, O'Brien signed and conveyed to Cox his claims against the home sellers. *CP 83-84, 161-202*

An arbitration was held with a decision entered in favor of home buyers Cox. A trial de novo was demanded by the home sellers.

Following the de novo appeal from the mandatory arbitration, both parties moved for summary judgment. *CP 96-210* The trial court granted summary judgment to the home sellers and denied summary judgment to the home buyers, finding that the indemnification provision was violative of public policy. *CP 212-214*

At trial, the only issue remaining was the claim of the home buyers for unjust enrichment. *CP 212-214* At the close of the Buyers' case, a directed verdict was entered in favor of home sellers. *CP 215-220*

IV. SUMMARY OF ARGUMENT

The economic loss rule bars tort claims for purely economic losses between parties that contractually allocated risk for such loss or had an opportunity to do so in order to protect the parties from disproportionate risk. *Alejandre v. Bull*, 159 Wn.2d 674, 153 P.3d 864 (2007). As plaintiffs' claims are limited to economic losses, the economic loss rule applies. *Id.* The pest inspector allocated his risk to the sellers by an indemnification provision requiring the sellers to protect him in the event there was undetected pest damage. *RP 37-49*. By invalidating the indemnification provision, the trial court improperly interfered in the allocation of risk provided for in the agreements between the buyers, sellers and pest inspector. Where parties have contracted for their potential economic liability, those agreements need to be respected. Otherwise, the rationale behind the economic loss rule becomes

meaningless. *Alejandre v. Bull*, 159 Wn.2d 674, 153 P.3d 864 (2007),
Berschauer/Phillips Construction Co. v. Seattle School Dist. 124 Wn. 2d
816, 881 P. 2d 986 (1994).

The home sellers procured insurance to protect them from this loss.
RP 27. In finding for the sellers, the court invalidated the agreements
between the parties to shift the cost of the defective pest inspection from
the sellers' insurance carrier to the buyers. Should this result be allowed to
stand it will result in a windfall for the insurance carrier.

V. ARGUMENT

**A. Application of the economic loss rule requires that the
contractual indemnification provision stand as not void under public
policy.**

When the economic loss rule is applied to bar tort claims, a
contractual indemnification provision shifting the assumption of risk for
economic loss should be allowed by public policy.

The economic loss rule was developed to prevent disproportionate
liability and allow parties to allocate risk by contract. *Berschauer/Phillips
Const. Co. v. Seattle School Dist. No. 1*, 124 Wn.2d 816, 822, 881 P.2d
986 (1994). The economic loss rule is a conceptual device used to classify
damages deemed more properly remediable only in contract. *Id.*

Respondent sellers are correct that the economic loss rule bars buyers from recovering under a theory of negligent misrepresentation. However, the economic loss rule does not bar an indemnification claim allowed for in the contract between the pest inspector and the sellers. In fact, the application of the economic loss rule makes it essential that all risk shifting provisions in the bargained for contract be enforced.

The trial court left buyers with no possible remedy when it declared the indemnification void because it was contrary to public policy. A commenter on Washington court's embrace of the economic loss rule in *Berschauer/Phillips* stated:

A bright line distinction between the remedies offered in contract and tort with respect to economic damages encourages parties to negotiate a desired or customary allocation of risk. Without a bright line, a contractor might seek in tort to recover benefits it was unable to obtain in contractual negotiations. The Washington Supreme Court has eliminated the contractor's end run around the burdens of its contract with the owner.

Public policy requires that a party be bound by the reasonable terms of its contract. Several important contract obligations would become essentially meaningless if the economic loss rule was not applied in this context.

Michael J. Bond, *Rebuilding the Citadel of Privity*, 30 Gonz. L. Rev. 221, 231 (1995) (citations omitted).

In the case at hand, the buyers are attempting to recover the pest inspector's contractual right to be indemnified against losses stemming

from his defective inspection, which was assigned to the buyers. There is no dispute that the buyers' loss due to the deficient inspection falls under the economic loss rule. The buyers looked to the pest inspector responsible for their loss. The pest inspector in turn had shifted the risk by contract to the sellers. The sellers had shifted their risk to their insurance company by contract.

By ruling that the loss indemnification provision of the pest inspector's contract was void as violative of public policy, the trial court has abrogated the Washington Supreme Court's ruling that the risk of economic loss be allocated by contract. At the same time the trial court determined that claims for the buyers' loss was barred by the economic loss rule. The trial court's position that economic loss risk allocation be done by contract is not consistent with its ruling that such shifting of risk is void as violative of public policy.

The sellers rely on *Aljendre v. Bull*, 159 Wn.2d 674, 153 P.3d 864 (2007), to demonstrate that the buyers cannot sue the sellers for economic damages when the remedy is not set out in the contract. Sellers would be correct if the buyers were suing them directly for damages as buyers under the purchase and sale agreement. The court in *Aljendre* stated "[t]here is no question that the parties' relationship is governed by contract. Thus, unless there is some recognized exception to the economic loss rule that

applies, the plaintiffs' claim of negligence cannot stand because they are limited to their contract remedies." *Id* at 685-686.

However, the instant case is distinguishable from *Aljandre* in that the suit against the seller comes partially under a contract between the pest inspector and the seller whereas there were no contractual remedies available to the parties in *Aljandre*. The buyers in this case are placed "in the shoes" of the pest inspector and are simply seeking relief under the contract which was entered into by the parties, which the Supreme Court of Washington has ruled to be the proper theory under which to seek relief in a case involving economic loss.

B. The contract must be interpreted in a way that does not produce a nonsensical result.

The trial court incorrectly construed the indemnification language at issue when they denied buyers' cross-motion for summary judgment

Contracts should be given a fair, reasonable and sensible construction which fulfills the apparent object of the contract rather than a strained, forced construction which leads to an absurd conclusion which renders a contract nonsensical or ineffective. *Transcontinental Ins. Co. v. Washington Public Utilities Districts' Utility System*, 111 Wn.2d 452, 457, 760 P.2d 337 (1988); *McDonald Industries, Inc. v. Rollins Leasing Corp.*, 95 Wn.2d 909, 913, 631 P.2d 947 (1981). Yet if the contract were to be

construed the way the seller proposes, the result would be a nonsensical, ineffective provision of the contract.

Sellers rely on their contention that the indemnification clause of the pest inspection contract indemnifies some company or person that is not party to the contract. Interpreting the contract as the sellers propose results in an absurdity, an outcome barred by Washington case law.

The limitation of liability provision of the contract reads:

The above inspecting firm endeavors to perform its services in a professional manner consistent with the care and skill ordinarily exercised by similar pest control professionals. No warranty, express or implied, other than as set forth herein, is made or... by performing the work identified in this agreement. Should this firm, or its employees, be found to have been negligent in their performance of services, it is agreed that the maximum total recovery against us or our employees shall be limited to our fee for the services provided under this agreement.

In the event any person or company makes a claim for any alleged error, omission, or other act arising out of **their** performance of professional services under this contract, each signer of this agreement agrees to defend and hold us harmless from any such claim, including reasonable attorney's fees and costs incurred in defending against the claim.

(Emphasis added.) The sellers' contention is that the "their" in the second paragraph renders the contract ambiguous or that the pronoun refers to the person or company making a claim against their own performance.

Under the sellers' interpretation, the contract indemnifies a person or company who is not a signatory to the contract but who is suing themselves for their own performance under the contract even though no one but the pest inspector would be performing services under the contract. That is precisely the kind of nonsensical result rejected by the case law.

Even if the buyers' contention that the "their" should be a "the" is rejected, the contract can still be construed to indemnify the pest inspector when it is read in context of the entire limitation of liability provision. In the paragraph preceding the indemnification provision, the same phrase, "their performance of services," is used and the "their" refers to the pest control firm or its employees. It is a reasonable assumption that the drafter continued to have "their" refer to the pest control firm and employees after the paragraph break, especially since that avoids a nonsensical result.

Regardless if the "their" in question is read as "their" or "the" the result must be the same in order to avoid a nonsensical result: the indemnification of the pest inspector by the seller.

C. RCW 4.24.115 does not apply to indemnity agreements in inspection contracts.

The trial court correctly rule as a matter of law that the indemnification language was not rendered void by RCW 4.24.115

Sellers contend that the indemnity provision in the pest inspection contract is barred by RCW 4.24.115, the applicable portion of which states:

A covenant, promise, agreement or understanding in, or in connection with or collateral to, a contract or agreement relative to the construction, alteration, repair, addition to, subtraction from, improvement to, or maintenance of, any building, highway, road, railroad, excavation, or other structure, project, development, or improvement attached to real estate, including moving and demolition in connection therewith, purporting to indemnify against liability for damages arising out of bodily injury to persons or damage to property:

(1) Caused by or resulting from the sole negligence of the indemnitee, his agents or employees is against public policy and is void and unenforceable.

Sellers attempt to force the services of a professional home inspector into the category of “maintenance” in order that they may escape the consequences of the indemnification agreement. Sellers did not cite any cases demonstrating that a pest inspection is maintenance, but rather simply asked that the court assume that an inspection is maintenance. However, both the context of the statute and case law have demonstrated that “maintenance,” as used in the statute refers to physically engaging in the upkeep of a property rather than a passive, one-time inspection.

The court must look to the plain meaning of a statute to construe the intent of the legislature. *Christensen v. Ellsworth*, 162 Wn.2d 365, 372-373, 173 P.3d 228 (2007). The word “maintenance” has a plain and ordinary meaning of “the labor of keeping something... in a state of repair or efficiency; care, upkeep,” or “the work of keeping something in proper condition; upkeep.” *Mower v. King County*, 130 Wn. App. 707, 716, 125 P.3d 148 (2005). The action of “labor” or “work” being performed on a piece of property in the act of maintenance is consistent with the other terms in the statute - construction, alteration, repair, addition to, subtraction from, improvement to – all of which suggest some change being made to the physical properties of the property rather than a simple inspection.

Additionally, case law related to RCW 4.24.115 demonstrates that “maintenance” as used in the statute is meant as physical work done to the property. The cases where RCW 4.24.115 was applied in the context of maintenance do not include inspection services, but do include pipefitters performing maintenance on a refinery furnace in *Stocker v. Shell Oil Co.*, 105 Wn.2d 546, 716 P.2d 306 (1986), and the performance of steam cleaning by a subcontractor in *Kaiser Aluminum & Chemical Co. v. Finrow Painting Co., Inc.*, 10 Wn. App. 178, 516 P.2d 798 (1973).

While RCW 4.24.115 prohibits the enforcement of indemnification agreements in cases of sole negligence in the *construction setting*, *Gilbert H. Moen Co. v. Island Steel Erectors, Inc.*, 128 Wn.2d 745, 747, 753-754, 912 P.2d 472 (1996), it does not apply to the case at hand. The statute's rule makes sense in the high-risk arena of construction, where public policy demands that each contractor strive for a safe work environment and carry insurance. However, as discussed above, when the economic loss rule bars recovery for negligence, the ability to enforce a contracted indemnity provision is essential.

D. The sellers, and in turn the sellers' insurance carrier, were unjustly enriched.

The trial court erred in directing a verdict in favor of sellers on the buyers' unjust enrichment claims.

A person has been unjustly enriched when he has profited or enriched himself at the expense of another contrary to equity. *Farwest Steel Corp. v. Mainline Metalworks Inc.*, 48 Wn. App. 719, 731-32, 741 P.2d 59 (1987). . Unjust enrichment should can be viewed as a legal remedy in the form of restitution. *Ducalon Mechanical Inc. v. Schinstine/Forness Inc.*, 77 Wn. App. 707, 893 P.2d 1127 (1995).

As the sellers point out, the trial court determined that there was no evidence that the sellers should have known that the home was damaged

and therefore there could be no unjust enrichment. However, the sellers provided a pest inspection as part of the purchase and sale agreement. Had the pest inspector not been negligent he sellers *should* have and would have known from the inspection that there was pest damage.

If the pest inspection had revealed the damage, buyers either would have negotiated a lower price or the sellers would have remedied the situation at the expense of their insurance carrier. As it occurred, the sellers' insurance company is retaining money that should have been a price break for the buyer because of an ineffective pest inspection.

It is of no consequence that the buyers could have purchased a full house inspection. The damage in question is pest damage for which the home was inspected, not damage from another source that could have been found in a full home inspection. While the buyers took the risk of unknown damage from some sources, they did not assume the risk of pest damage.

E. Buyers are entitled to attorneys' fees.

Buyers are entitled to attorneys' fees based on MAR 7.3 or the indemnification provision in the inspection contract.

If the trial court awarded summary judgment to the buyers, sellers would have failed to improve their position from the Mandatory Arbitration Award and buyers would be entitled to attorneys' fees. MAR

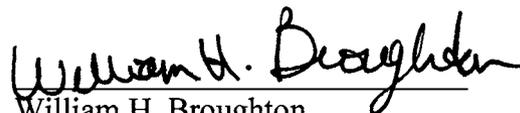
7.3. If this court reverses the order granting summary judgment in favor of the sellers and the order denying the cross-motion for summary judgment in favor of the buyers, the sellers have not improved their position and fees should be awarded on appeal.

Additionally, the buyers are entitled to attorneys' fees under the indemnification rights assigned to them by the pest inspector pursuant to the inspection contract.

VI. CONCLUSION

For the reasons above stated, the buyers ask that the summary judgment and directed verdict orders in favor of the sellers be reversed.

Respectfully submitted this 24th day of September, 2008.



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STATE OF WASHINGTON

BY _____
DEPUTY

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

TERRANCE S. COX and JULIE K. COX, husband
and wife,

Appellants/Plaintiffs,

vs.

JAMES H. O'BRIEN and JANE DOE O'BRIEN,
husband and wife, dba **O'BRIEN HOME**
INSPECTION SERVICES,

Respondents/ Defendants.

No. 317194-4-II

DECLARATION OF MAILING

O'BRIEN HOME INSPECTION SERVICE,

Respondent/Third Party Plaintiff

vs.

DANNY D. DEMERS and MARY I. DEMERS,
husband and wife, and the marital community
composed thereof,

Respondents/Third Party Defendants

DANNY D. DEMERS and MARY I. DEMERS,
husband and wife, and the marital community
composed thereof,

Respondents/Fourth Party Plaintiffs

vs.

TERRANCE S. COX and JULIE K. COX, husband
and wife,

Appellants/Fourth Party Defendants.

Sandra Rivas, under penalty of perjury under the laws of the State of Washington,
hereby declares as follows:

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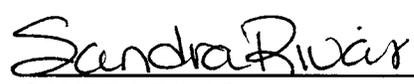
1. That I am over the age of eighteen (18) years, not a party to this action, and am competent to make this Declaration;
2. That on 24 Sept. 2008, I sent via first class mail, a copy of the Appellants Reply Brief, together with a copy of this Declaration to the Court of Appeals, Division II, and to the attorneys for Respondents.

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Division II
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DATED this 24th day of September, 2008.


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