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NO. 86109-9

SUPREME COURT
OF THE STATE OF WASHINGTON

JAMES BIRD,
Respondent,

v.

BEST PLUMBING GROUP, L.L.C.
Defendant,

FARMERS INSURANCE COMPANY OF WASHINGTON,
Petitioner.

FILED
SUPREME COURT
STATE OF WASHINGTON
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ON APPEAL FROM THE WASHINGTON STATE COURT OF
APPEALS, DIVISION I

AMICI CURIAE BRIEF OF NATIONAL ASSOCIATION OF
MUTUAL INSURANCE COMPANIES, AMERICAN INSURANCE
ASSOCIATION, AND PROPERTY CASUALTY INSURERS
ASSOCIATION OF AMERICA

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I. INTRODUCTION

Where an insured defendant whose insurer has allegedly acted in bad faith settles directly with a claimant for a reasonable amount and assigns its right to pursue a bad faith claim, the amount of that settlement becomes the presumptive measure of damages in the bad faith claim brought by the claimant. A practice has developed in Washington where the insured and the claimant have the trial court in their underlying case determine the reasonableness of the settlement under the *Glover* test. Under that practice, upon a determination that the settlement is reasonable, the insurer, as the defendant in the subsequent bad faith action, is liable for that full settlement amount unless it can prove that the settlement was the product of fraud or collusion; the reasonableness of the settlement under *Glover* is deemed resolved by the reasonableness determination.

The authority and reasons for using this method for determining the amount of damages in an insurance bad faith action have become obscured over time. Whatever the reasons, the practice manifestly conflicts with an insurer's constitutional rights to trial by jury and due process. This Court should take the opportunity of this case to clarify the basis and reasons for this method of determining damages, and in a way that safeguards these important rights.

II. IDENTITY AND INTEREST OF AMICI CURIAE

The American Insurance Association ("AIA"), the National Association of Mutual Insurance Companies ("NAMIC"), and the

Property Casualty Insurers Association of America (“PCI”) (collectively referred to as “*amici*”) move to file an *amici curiae* brief in this appeal. A copy of the proposed *amici* brief is attached hereto.

Amici are the leading national associations of property and casualty insurers in the United States. Members of *amici* range in size from small companies to the largest insurers with global operations. On issues of importance to the insurance industry and marketplace, *amici* advocate sound public policies on behalf of their members in legislative and regulatory forums at the state and federal levels and file amicus curiae briefs in significant cases before federal and state courts, including this Court. *Amici*’s members write a majority of the property and casualty insurance in Washington (totaling some \$9 billion in premiums) and nationwide and thus are vitally interested in the resolution of the issues in this case.

III. STATEMENT OF THE CASE

For the purposes of this brief, *Amici* rely upon the statement of facts set forth by Farmers in its appellant’s brief, petition for review, and supplemental Supreme Court briefing.

IV. ARGUMENT

A. No Statute or Holding of This Court Authorizes a Trial Court to Preside Over a Hearing Convened for the Purposes of Determining the Amount of Tort Damages Binding on the Insurer in a Subsequent Bad Faith Action, Where the Insurer Invokes its Right to Have a Jury Determine Those Damages.

Respondent James Bird argues that the procedure for having a trial court determine the reasonableness of a covenant judgment is well-established by Washington case law. Supplemental Brief of Respondent James Bird, at 6, citing *Glover v. Tacoma Gen. Hosp.*, 98 Wn.2d 708, 715-716, 658 P.2d 1230 (1983), overruled on other ground by *Crown Controls, Inc. v. Smiley*, 110 Wn.2d 695, 756 P.2d 717 (1988); *Chaussee v. Md. Cas. Co.*, 60 Wn. App. 504, 512, 803 P.2d 1339 (1991). But a review of Washington case law does not reveal any decisions from this Court blessing such a procedure *when the insurance company objected that its use violates its right to a jury trial*. Nor does the language of RCW 4.22.060 show a legislative intent to effect such a result.

Under the 1981 Tort Reform Act, a "hearing shall be held on the issue of the reasonableness" of a partial settlement reached. RCW 4.22.060(1). Nothing in the text of chapter 4.22 RCW provides for a reasonableness hearing in cases where no nonsettling, potentially-at-fault defendants remain in the action. Instead, under the 1981 Tort Reform Act, there "are only two tort litigation settings in which a reasonableness hearing should be conducted. A hearing must be conducted (1) to fix the amount of an unreleased, non-settling defendant's credit *or* (2) to set the reasonable amount that will be apportioned between a settling defendant

and a released non-settling defendant when the settling defendant's contribution claim is subsequently litigated." Thomas V. Harris, *Washington's Unique Approach to Partial Tort Settlements: The Modified Pro Tanto Credit and the Reasonableness Hearing Requirement*, 20 GONZ. L. REV. 69, 106, 113 (1984/85). "If there is only a single defendant, neither of the two contexts calling for a hearing can possibly arise." *Id.*, at 114, n.161.

Indeed, "[o]ne of the primary purposes of the hearing is to 'protect the *nonsettling defendant* from paying more than his or her share of the damages.'" *Price v. Kitsap Transit*, 125 Wn.2d 456, 467-68, 886 P.2d 556 (1994) (emphasis added), quoting *Adams v. Johnston*, 71 Wn. App. 599, 604, 860 P.2d 423 (1993) (citing Senate Journal, 47th Legislature (1981), at 636-37). See also Harris, 20 GONZ. L. REV. at 113 ("[A] reasonableness hearing would serve no purpose when a litigation has been fully settled."). Thus, where the claimant settles with the insured defendant and then sues the insurer for bad faith in a separate action under an assignment of rights, conducting a reasonableness hearing does not serve the purpose of RCW 4.22.060.

Case law on the notice provision of RCW 4.22.060 further demonstrates that the section was never intended to authorize a hearing that would impact the rights of an entity, such as an insurer, that is not a party to the action culminating in the settlement. The notice provision in RCW 4.22.060(1) requires five days notice of intent to settle only to "parties" to the action. In the case of a settlement between a claimant and

the insured, courts have ruled that the insurer is not a “party” and is thus not guaranteed to receive notice of the settlement according to RCW 4.22.060’s requirements. *See Sharbono v. Universal Underwriters Ins. Co.*, 139 Wn. App. 383, 407, 161 P.3d 406 (2007) (rejecting insurer’s argument that it did not receive the required notice since the insurer was not a “party” to the settlement between the claimant and insured and RCW 4.22.060(1) “requires that all *parties* receive notice of the settlement.”) (emphasis in original); *Villas at Harbour Pointe Owner’s Ass’n v. Mut. of Enumclaw Ins. Co.*, 137 Wn. App. 751, 761-62, 154 P.3d 950 (2007) (insurance company not entitled to notice as required by RCW 4.22.060(1) since it was not a party to the settlement).

It strains credulity to find in a statute requiring no notice to an insurer of the intent to settle, a legislative intent to create a procedure whose outcome would displace an insurer’s right to have a key issue of fact—damages, as measured by the reasonable amount of a covenant judgment—decided by a jury in the trial of the follow-on bad faith action.

This Court’s decisions under RCW 4.22.060 offer no more support for a trial court to convene a reasonableness hearing outside of the joint tortfeasor context:

- ***Glover v. Tacoma General Hospital.*** In *Glover*, a medical malpractice case with multiple defendants, most of whom settled, this Court recognized that the reasonableness determination required by RCW 4.22.060 is of “great importance to *both settling and nonsettling defendants*” because it determines what offset the nonsettling defendant

would be allowed against the judgment at trial. 98 Wn.2d at 716 (emphasis added). Notably, this Court said nothing about the importance, or lack thereof, of a reasonableness hearing when the settlement occurs between a single claimant and single defendant. *Glover* does not provide any authority for the trial court to conduct a reasonableness hearing that would have a preclusive effect in a subsequent action between the claimant and the defendant's insurer. If anything, *Glover* implies the opposite, that reasonableness hearings are not important in the absence of nonsettling defendants.

- *Schmidt v. Cornerstone Investments*. The next case from this Court to address reasonableness hearings under RCW 4.22.060, *Schmidt v. Cornerstone Investments*, is similarly silent on whether a reasonableness hearing was authorized or advised outside of the context involving the partial settlement of a case with at least one nonsettling defendant remaining potentially at fault. 115 Wn.2d 148, 795 P.2d 1143 (1990). In *Schmidt*, two defendants settled, and *a jury determined the damages* and liability of the remaining nonsettling defendants. The jury's award was offset by the settlement amount found reasonable under RCW 4.22.060. *Schmidt* thus offers no guidance regarding the propriety of conducting a reasonableness hearing in a liability action between a claimant and an insured to determine the amount of damages in a subsequent bad faith action.

Whatever this Court may have said in support of the reasonableness process, and the role it may legitimately play in

relationship to covenant judgment settlements and follow-on bad faith actions, this Court has never expressly held that the result of a reasonableness determination trumps an insurer's right to have a jury determine reasonableness, if that insurer has insisted on such a trial on that issue.

• *Chaussee v. Maryland Casualty Co.* While not a decision from this Court, *Chaussee v. Maryland Casualty* warrants discussion because it provides the first example of a case where a reasonableness hearing was conducted outside of the context of RCW 4.22.060. 60 Wn. App. 504. In *Chaussee*, the reasonableness hearing was required by *guardianship law* before the guardian could compromise the minor's claim against the insured. After the settlement was approved, the guardian sued the insurance company, as an assignee of the insured, for bad faith and brought the case to trial. Because the guardian failed to offer sufficient evidence to prove the insured's damages, the trial court granted a judgment n.o.v. The Court of Appeals affirmed, holding that the bad faith plaintiff failed to satisfy the burden of proving that the settlement amount was reasonable. 60 Wn. App. at 510. The reason for this burden remaining on the claimant was the possibility that an insured would "settle for an inflated amount to escape exposure[.]" 60 Wn. App. at 510. *Chaussee* endorsed using the *Glover* factors to determine the settlement's reasonableness, but did not provide any guidance on whether the trial court, in the action preceding the bad faith action could by its

determinations preclude the insurer's right to a determination of reasonableness by the jury in the bad faith action.

- *Besel v. Viking Insurance Co. of Wisconsin.* In *Besel*, this Court agreed with the Court of Appeals in *Chaussee* that the *Glover* factors apply to determine reasonableness where such a hearing was held to approve a covenant judgment. 146 Wn.2d 730, 738, 49 P.3d 887 (2002). But *Besel*, like *Chaussee*, sheds no light on the authority to conduct a reasonableness hearing outside of RCW 4.22.060.

In *Besel*, the insured and the claimant made the settlement contingent on a reasonableness determination. The trial court entered an order finding the settlement reasonable. The insurance company did not object to the procedure even though it had notice of the hearing. 146 Wn.2d at 739. The claimant sued the insurance company for bad faith. On appeal, the insurance company did not dispute the reasonableness of the settlement. 146 Wn.2d at 739. This Court, thus, did not have occasion to examine the authority for the procedure underlying the trial court's order approving the settlement. Further, *Besel* did not involve any discussion of the trial court's authority to conduct an effectively preclusive hearing over an intervening insurer's request for a jury to determine the issue. And, in *Besel*, there would have been no basis to disapprove of the procedure under article 1, section 21, since interested parties may waive their rights under that section, which is essentially what the *Besel* insurer did by not objecting on appeal to the reasonableness of the settlement as determined by the trial court.

• *Mutual of Enumclaw Insurance Co. v. T & G Construction, Inc.* *T & G Construction, Inc.* is this Court's most recent case involving a covenant judgment preceding a bad faith action. 165 Wn.2d 255, 199 P.3d 376 (2008). There, the insurance company did not participate in a final round of settlement talks under the belief that the insured had an affirmative defense and should not be obligated to pay the claimant (and, by extension, that the insurance company was under no obligation). 165 Wn.2d at 260-61. The parties settled and requested a reasonableness hearing for the settlement. 165 Wn.2d at 261. The insurer appeared and unsuccessfully objected to the settlement at the hearing. 165 Wn.2d at 261. The Court held that if the coverage question in the separate action turns on the same law or facts at issue in the underlying dispute between the claimant and the insured, the insurer will be bound by the results of settlement approved as reasonable. 165 Wn.2d at 267.¹

As for the hearing procedure, *T & G Construction* states that the "parties *may ask* the trial court to determine whether the settlement is reasonable." 165 Wn.2d at 264 (emphasis added). This does not resolve

¹ This holding could effectively make the presumption of damages from the reasonableness hearing irrebuttable. This is because one of the *Glover* issues to be addressed in making the reasonableness determination is the issue of bad faith, collusion, or fraud. Thus, if the trial court in the underlying action determines the settlement is reasonable, the insurer theoretically could be bound by the fact determination that the settlement is not the product of bad faith, collusion or fraud. And this would preclude the insurer's ability to rebut the presumption of reasonableness in the bad faith action through a showing of fraud or collusion.

whether the trial court has the authority to hold such a hearing where the parties ask for one but the intervening insurer invokes its right to have the jury determine whether the settlement is reasonable. Nor does *T & G Construction* explain the basis for such a procedure outside RCW 4.22.060 and the guardianship statute when, unlike in *Besel*, the insurer invokes its right to a jury trial. Finally, although the insurer in *T & G Construction*, unlike the insurer in *Besel*, was disputing the reasonableness of the settlement amount, there is no indication in *T & G Construction* that the insurer raised the issue of its right to a jury trial, and certainly this Court did not address the issue.

B. The Absence of Clear Authority Has Led to Confusion in the Lower Courts Regarding Whether a Reasonableness Hearing Procedure Is Allowed or Recommended When an Insured Settles With a Claimant in Anticipation of a Bad Faith Action.

In *Werlinger v. Warner*, the trial court properly expressed skepticism about a trial court's authority under RCW 4.22.060 to hold a reasonableness hearing in a case without multiple defendants. 126 Wn. App. 342, 348, 109 P.3d 22 (2005). The trial court nevertheless held the hearing (based in part on assurances from the insurance company that the hearing was appropriate) and found the settlement unreasonable, in which case the Court of Appeals held that the amount of damages could be proved in the "ordinary way." 126 Wn. App. at 348, 352. This of course begs the question as to why, if damages against an insurer alleged to have acted in bad faith can be determined through normal means, a trial court should preside over a reasonableness hearing. *Chaussee*, in fact, shows

the ordinary procedure that would (and should) be used. There, the issue of damages was tried to a jury as part of the trial on the insurance company's liability for bad faith. While the bad faith plaintiff in that particular trial failed to present sufficient evidence to show that the settlement was reasonable, *Chaussee* shows that the issue of reasonableness is eminently triable. 60 Wn. App. at 515.

As another example of uncertainty as to the authority for the trial courts to hold effectively preclusive reasonableness hearings, in *Red Oaks Condominium Owners Association v. Sundquist Holdings, Inc.*, the Court of Appeals did not identify the authority for the hearing to determine the reasonableness of a covenant judgment and assignment of rights. The court instead simply stated that it was "common for parties to move for a hearing" following a covenant judgment in contemplation of a bad faith action and cited to other cases where a hearing had been conducted. 128 Wn. App. 317, 322, 116 P.3d 404 (2005). And at least one court has simply assumed that RCW 4.22.060 provides the authority, even in settings not covered by the 1981 Tort Reform Act and where the purpose of the reasonableness hearing under that act would not have been furthered. See *Howard v. Royal Specialty Underwriting, Inc.*, 121 Wn. App. 372, 377-78, 89 P.3d 265 (2004) (stating that "RCW 4.22.060 provides for a reasonableness hearing after a settlement has been

reached[]” even when there were not any defendants remaining in the underlying action.)²

The effect of this lack of clear authority is apparent in Court of Appeals decision under review. For example, the court appeared to assume that *Schmidt*'s holding about a reasonableness hearing conducted under RCW 4.22.060 would also apply here, as if the hearing in this case had been properly held under the authority of RCW 4.22.060. But in this case, unlike in *Schmidt*, there were not any nonsettling defendants. See *Bird v. Best Plumbing Group*, 161 Wn. App. 510, 520, 260 P.3d 209 (2011). The Court of Appeals also repeatedly referred to the reasonableness hearing as an equitable proceeding, but this characterization begs the question of how the result of such an equitable proceeding can displace an insurer's right as a defendant in a bad faith action, which sounds in tort *at law*, to have damages (reasonableness) decided by a jury in the bad faith action.

² Respondent Bird, before the Court of Appeals, all but conceded that RCW 4.22.060 provides no direct authority for holding a reasonableness hearing in cases like this one involving a covenant judgment with an assignment of bad faith and no nonsettling defendants. See Respondent's Brief at 25-27. Instead, Bird argued that the practice should be upheld because it had become "entrenched" and because the legislature had not yet reacted to decisions incorrectly citing to RCW 4.22.060 as authority. *Id.*

C. There Is No Reason to Conduct a Hearing to Determine the Reasonableness of a Settlement Between an Insured and a Claimant Before the Issue Is Litigated in the Bad Faith Action, Particularly Where Doing So Violates the Insurer's Right to a Jury Trial.

However "entrenched" the practice of giving binding effect to reasonableness hearing determinations in follow-on bad faith actions, whether a settlement between a defendant insured and a plaintiff was reasonable still indisputably remains a *question of fact*. And whatever authority there may be for a trial judge holding a hearing at which the court determines reasonableness (*e.g.*, under RCW 4.22.060), an insurance bad faith action is a tort action at law, and there should be no question that an insurer defendant in such an action, under well-established principles of Washington law, has a constitutional right to have all material issues of fact decided by a jury. "Damage" is one of those material questions of fact, and *Sofie v. Fibreboard Corp.*, 112 Wn.2d 636, 771 P.2d 711 (1989), leaves no doubt that there is a constitutional right to have a jury decide all fact questions pertaining to damage in a tort action.

This Court is committed to the protection of the right to jury trial enshrined in the Washington Constitution, and allowing a determination of reasonableness by a judge in some other proceeding to bind an insurer defendant in a bad faith case, in the face of that insurer's insistence on its right to have the jury in that bad faith action make that determination, is a

blatant violation of the right to jury trial.³ Further, allowing the insured and the claimant to invoke a reasonableness hearing before the insurance company's full involvement as a defendant effectively allows those parties to set in motion the process by which the insurance company's right to a jury trial will be lost. This Court should not authorize such a procedure allowing the insured and the claimant the ability to effectively waive the insurance company's jury trial rights.

Respondent Bird argues that trial court judges are in a superior position to evaluate the reasonableness of a settlement, which amount becomes the presumptive measure of harm in the later bad-faith case. Supplemental Brief of Respondent James Bird, at 8-10. Respondent Bird, citing case law from another jurisdiction, argues this is so because the kind of proof submitted in a reasonableness hearing would be best understood and weighed by the trial court judge. *Id.* But this cannot possibly be a valid basis for denying an insurer its right to a jury trial. Article 1, section 21 rights do not turn on whether the trial court or the jury would be better situated to decide the question at issue. *See Endicott v. Icicle Seafoods, Inc.*, 167 Wn.2d 873, 884-885, 224 P.3d 761 (2010) (test for determining whether Washington Constitution confers right to a jury trial).

³ An insurer can, of course, waive that right by agreeing to the submission of the issue to a reasonableness determination by a trial court. Farmers, however, did not waive its right, and qualified its participation in the reasonableness proceeding here by asserting its jury trial right.

Moreover, a jury is perfectly competent to decide how much damage an insurer's bad faith, if any, has caused the insured and to award compensation in that amount. Determining the amount of damages caused by an alleged tortfeasor is a traditional fact-finding function of the jury. *Sofie*, 112 Wn.2d at 645-46; *Werlinger*, 126 Wn. App. at 352 (allowing damages to be determined the "ordinary way," ostensibly involving a jury, in bad faith action where no reasonableness finding made as to settlement). Determining reasonableness is another traditional function of the jury, and one that a jury is well-equipped to handle.

Respondent Bird also invokes the risk of delay as a reason to deny a jury trial. *See* Supplemental Brief of Respondent James Bird, at 1. But, again, a litigant's rights under article 1, section 21 do not turn on whether the trial court or the jury would be quicker able to decide the question at issue. And having a jury determine the amount of bad faith damages will not add an unnecessary trial because the issue of liability for bad faith, if any, still must be proved to a jury. With that issue remaining to be decided in the subsequent bad faith action between the claimant and the insurer, there is no reason to effectively determine the amount of damages immediately following the settlement between the insured and the claimant.

This Court has never held that an insurer's jury trial rights in a bad faith action must yield in the face of a finding by a judge in a reasonableness proceeding that the settlement—and particularly, the amount of a covenant judgment—between the defendant insured and a

plaintiff is reasonable. Whatever rebuttable presumption of reasonableness may arise when the insurer does not assert its jury trial rights, the clear mandate of our constitution and decades of this Court's jury trial jurisprudence compel the conclusion that such a finding has no relevance to and should be given no weight in any bad faith action in which an insurer stands on its right to a jury trial. Such was the case here, and the Court of Appeals should be reversed for failing to honor this fundamental constitutional imperative.

D. As Conducted, the Reasonableness Hearing Procedure Is Unfair to Insurance Companies.

The procedures required for a reasonableness determination do not require the insured and the claimant to provide fair notice to the insured, or assure the insured a fair opportunity to be heard on the myriad issues raised by a claim of reasonableness. As it is, there is no guarantee that the insurer will be allowed sufficient time to intervene in the action between its insured and the claimant to ensure that the settlement is truly reasonable and not the product of collusion between the insured and the claimant. In *Red Oaks*, for example, the insurer was given only six days notice to determine whether the settlement was reasonable. 128 Wn. App. at 326. And in *Howard*, the trial court was allowed the discretion to refuse to reopen discovery and to deny the insurer's request to continue the hearing. 121 Wn. App. at 379. See also *Sharbono*, 139 Wn. App. at 407, 161 P.3d 406 (2007) (notice requirements under RCW 4.22.060(1) do not apply to insurer); *Villas at Harbour Pointe Owner's Ass'n*, 137 Wn. App.

at 761-62 (insurance company not entitled to notice required by RCW 4.22.060(1)).

As a practical matter, the insurance company is not likely to have counsel representing its interests in the case at the time of the settlement. That the insurer had been handling the liability claim against the insured does not necessarily mean the insurer would have knowledge of the laws and fact relevant to protecting its interests under the *Glover* factors. And, at the time of settlement, the insurer would not have had the opportunity to investigate and conduct discovery into facts relating to collusion or fraud.

Where the claimant still must prove its bad faith claim against the insurer in a separate action, there is no reason for this Court to condone a procedure by which insurers are unfairly and unnecessarily rushed into court to defend their interests under the multi-factor *Glover* test. Especially if this Court decides to authorize a reasonableness hearing over an insurer's request for a jury trial, this Court should at least require a procedure that protects an insurer's due process rights. This means the insurer should be provided with adequate notice of the hearing to sufficiently evaluate and plan its course of action. The insurer should also be provided with sufficient opportunity to conduct discovery on the reasonableness of the settlement, relevant to the *Glover* factors. The facts of *Chaussee* illustrate just how complex a determination of reasonableness can be, and should be ample proof of the need for something far more rigorous than the five day motions practice on papers that too often passes for "due process" in such situations today.

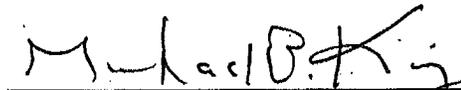
V. CONCLUSION

Unsettled questions regarding the authority for conducting a reasonableness hearing could be simply resolved in this case through a holding that the insured and claimant *and* insurer may agree to have a trial court make a reasonableness determination with respect to a settlement. But where the insurance company does not waive its right to a jury trial, there is no reason (and no authority under the Washington Constitution) to allow a trial court to determine the amount of damages that will be effectively binding on the insurance company in the subsequent bad faith action, especially where the insurer does not receive adequate notice of the hearing and is not allowed full discovery. That this state's court system may have for many years tolerated a practice that has failed to respect an insurer's jury trial rights is no reason for this Court to sanction it now.

RESPECTFULLY SUBMITTED this 23rd day of December, 2011.

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