

No. 42217-4

COURT OF APPEALS, DIVISION II
STATE OF WASHINGTON

STATE OF WASHINGTON,
Department of Transportation,

Respondent,

v.

JAMES RIVER INSURANCE COMPANY,

Appellant.

BRIEF OF APPELLANT

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I. INTRODUCTION

This appeal concerns whether mandatory arbitration provisions in insurance policies are enforceable under Washington law. James River Insurance Company issued two relevant insurance policies under which the State of Washington, State Department of Transportation (“WSDOT”) claims coverage for liabilities related to a fatal vehicular accident. After a dispute concerning James River’s coverage obligations arose, James River issued a valid arbitration demand to WSDOT pursuant to its policies’ arbitration provisions.

WSDOT opposed the arbitration and filed a declaratory judgment action, arguing the arbitration provisions are contrary to two Washington statutes that make no mention of “arbitration.” In response, James River sought a declaratory judgment validating the provisions. The trial court ultimately agreed with WSDOT and ruled James River’s arbitration clauses were unenforceable under Washington law.

The trial court erred in denying James River’s contractual right to arbitrate. The statutes relied upon by the trial court (RCW 48.18.200 and 48.15.150) have no effect on arbitration clauses in insurance policies, or otherwise, and the trial court misconstrued the statutory history behind those laws in making its ruling. The statutes further fail to trigger “reverse preemption” under the McCarran-Ferguson Act (15 U.S.C. 1012).

Moreover, the trial court failed to appreciate the strong preference given to arbitration provisions under Washington law and the preemptory effect of the Federal Arbitration Act (9 U.S.C. § 2). Since WSDOT failed to meet its burden of proof in challenging James River's arbitration clauses, the trial court's order should be reversed.¹

II. ASSIGNMENT OF ERROR

The trial court erred in entering the Order Granting Plaintiff's Motion to Bar Initiation of Arbitration Proceedings; Denying Defendant's Motion for Summary Judgment and Order for Compelling Arbitration; and Denying Defendant's Motion to Strike on May 20, 2011, thereby denying James River's contractual right to an arbitration.

III. ISSUES PERTAINING TO ASSIGNMENT OF ERROR

1. Does RCW 48.18.200 prohibit arbitration provisions in insurance contracts subject to Washington law?
2. Does RCW 48.15.150 prohibit arbitration provisions in surplus lines insurance contracts subject to Washington law or otherwise affect arbitration agreements under such insurance contracts?

¹ *Verbeek Props., LLC v. Greenco Envtl., Inc.* 159 Wn. App. 82, 87-88, 246 P.3d 205 (2010) (citing *Otis Housing Ass'n v. Ha*, 165 Wn.2d 582, 165 Wn.2d 582, 586-87, 201 P.2d 309 (2009) (confirming the burden of proof is on the party seeking to void an arbitration provision and the issue is reviewed under a de novo standard on appeal).

3. Does the McCarran-Ferguson Act (15 U.S.C. § 1012) “reverse preempt” the Federal Arbitration Act (9 U.S.C. § 2) based on RCW 48.18.200 or RCW 48.15.150?

IV. STATEMENT OF THE CASE

A. Factual Background—Chronology

James River issued two relevant insurance policies to Scarsella Brothers, Inc. (“Scarsella”) effective from April 4, 2008, to April 4, 2011: (1) Owners and Contractors Protective Liability Policy No. 00030980-0 (“primary policy”); and (2) Commercial Excess Policy No. 00030967-0 (“excess policy”). (CP 8-9, 313, 66-67, 250-280, 281-311). The policies provided coverage for certain liability related to Scarsella’s work on a highway project for WSDOT. (CP 66-67).

Pursuant to Scarsella’s contract with WSDOT, Scarsella asked James River to add WSDOT as an insured under the policies for certain liabilities associated with the highway project. (CP 66-67). WSDOT and James River dispute certain aspects of the coverage afforded by the policies to WSDOT, but those disputes are unrelated to the Assignment of Error. For purposes of this appeal, the Court may assume WSDOT was an insured under the policies and the arbitration clauses applied to WSDOT. (RP 05/20/11, 4-5, 34).

The underlying claims against WSDOT arose out of a traffic accident that allegedly occurred at or near Scarsella's ongoing construction project. (CP 10). On April 15, 2009, representatives of the individuals injured or killed in the accident sued WSDOT in King County Superior Court under Cause No. 09-2-15949-1 KNT ("underlying lawsuit"). The plaintiffs in the underlying lawsuit later amended their complaint, asserting claims against Scarsella. (CP 10-11).

On January 29, 2010, WSDOT sent a letter to Scarsella tendering WSDOT's request for a defense in response to the underlying lawsuit under Scarsella's insurance policies. (CP 11, 67). The tender was then forwarded to James River. James River accepted WSDOT's tender under a reservation of all rights under the policies. (CP 12, 67-68). James River further informed WSDOT in a separate letter that the policies contained mandatory arbitration provisions and demanded arbitration of the parties' coverage disputes. (Id.) The arbitration provisions in each policy are the following:

BINDING ARBITRATION

Should we and the insured disagree as to the rights and obligations owed by us under the policy, including the effect of any applicable statutes or common law upon the contractual obligation otherwise owed, either party may make a written demand that the dispute be subjected to binding arbitration.

When such a request is made, The American Arbitration Association shall be used, with each party selecting an arbitrator from the list of qualified arbitrators for insurance coverage disputes provided by that Association. The two chosen arbitrators shall select a third arbitrator from the same list, if they cannot agree to a selection, the American Arbitration Association shall make the selection for them. Each party shall bear the costs of its arbitrator and shall share equally the costs of the third arbitrator and of the arbitration process. A decision agreed to by two of the arbitrators will be binding.

In the event you prevail in the arbitration and we promptly offer to you costs and reasonable attorney fees incurred in connection therewith, in addition to the disputed contract benefit, you shall have no right to sue us for breach of implied covenants or unreasonable withholding of contract benefits.

To the extent that we prevail in the arbitration, the arbitrators may award us any expenses and/or damages incurred or paid under a reservation of rights in excess of our contract obligations as determined by the arbitrators.

(CP 10, 67, 250-280, 281-311).

On September 1, 2010, James River attempted to initiate arbitration proceedings pursuant to its policies' arbitration provisions.

(CP 68). WSDOT objected to the demand and filed the subject declaratory judgment action against James River on September 9, 2010.

(CP 7-15). WSDOT reached a settlement with the plaintiffs in the underlying lawsuit on October 22, 2010. (CP 315).

B. Procedural History

WSDOT filed its declaratory judgment action against James River in the trial court on September 9, 2010, expressly seeking a declaration that the arbitration provisions were void. (CP 7-15). On November 10, 2010, following WSDOT's settlement with the underlying plaintiffs, WSDOT filed its First Amended Complaint, adding claims James River wrongfully failed to fund the settlement. (CP 18-29). James River denied WSDOT's allegations of wrongdoing. (CP 45-59). In addition, James River asserted a counterclaim for declaratory judgment, requesting that the trial court find the arbitration provisions in James River's policies are binding and enforceable. (CP 57-58).

On January 28, 2011, James River filed its Motion for Summary Judgment and for Order Compelling Arbitration with the trial court. (CP 65-84). Later the same day, WSDOT filed its Motion to Bar Initiation of Arbitration Proceedings. (CP 312-336). The trial court heard the parties' arguments related to both motions on May 20, 2011. (RP 05/20/11, 1-40). The trial court entered an order from the bench granting WSDOT's motion and denying James River's motion. (RP 05/20/11, 34-40). The trial court held the arbitration clause at issue was barred by RCW 48.18.200 and RCW 48.15.150(1), which, according to the trial court, are not preempted by the Federal Arbitration Act based

on “reverse preemption” by the McCarran-Ferguson Act. (Id.) On June 14, 2011, James River timely filed its Notice of Appeal to this Court. (CP 1163-1170).

V. ARGUMENT

A. **The Trial Court Misconstrued RCW 48.18.200 and the History Behind It, Erroneously Concluding the Statute Renders Unenforceable Arbitration Provisions Within Insurance Policies Based on the Trial Court’s Misinterpretation of the Term “Jurisdiction of Action”**

James River’s policies contain unambiguous, binding arbitration provisions. WSDOT incorrectly argued before the trial court Washington law voids such provisions. The trial court adopted WSDOT’s incorrect reasoning that was based, in part, on a misunderstanding of how Washington courts viewed arbitrations and their effect on the courts’ jurisdiction when the insurance code was enacted in 1947. (RP 05/20/11, 38). The erroneous ruling and the core of WSDOT’s argument against the arbitration provisions were founded on the following statute:

48.18.200 Limiting actions, jurisdiction.

(1) No insurance contract delivered or issued for delivery in this state and covering subjects located, resident, or to be performed in this state shall contain any condition, stipulation, or agreement

...

(b) depriving the courts of this state of jurisdiction of action against the insurer[.]

(2) Any such condition, stipulation, or agreement in violation of this section shall be void, but such voiding shall not affect the validity of the other provisions in the contract.

The plain language of RCW 48.18.200 contains no reference to arbitration, much less a prohibition on binding arbitration clauses in insurance policies. In addition, no authority in this state suggests the statute was intended to void such arbitration provisions. WSDOT, however, claims the portion of the statute prohibiting any policy provision “depriving the courts of this state of jurisdiction of action against the insurer” bars arbitration clauses. According to WSDOT, and the trial court’s erroneous oral Order, arbitration, in effect, removes disputes from the “jurisdiction” of Washington’s courts. (CP 317-322; RP 05/20/11, 35-38).

WSDOT concedes, however, the notion that arbitration deprives the courts’ of jurisdiction over controversies is contrary to the “modern view” of arbitration. (RP 05/20/11, 6). In fact, WSDOT’s interpretation is contrary to Washington statutory authority, which expressly vests jurisdiction over arbitrations in the courts of this state.² In response to the “modern” and statutory confirmation that jurisdiction remains with the courts, WSDOT asserted in its briefs and at oral argument that when

² RCW 7.04A.260. Federal law similarly vests jurisdiction in the courts to review and revise arbitration awards. 9 U.S.C. § 2.

RCW 48.18.200 was originally enacted, courts uniformly viewed arbitration as a threat to their jurisdiction and were opposed to it. (CP 628-629).

WSDOT crafted its argument regarding the courts' *general* historic attitude toward arbitration around scant out-of-state authority. (Id.) Nevertheless, WSDOT cited no Washington authority from the time of RCW 48.18.200's original enactment, much less before its enactment. In fact, Washington authority from that period reveals this state was ahead of its time with respect to arbitration, and that the term "arbitration," like the term "jurisdiction," was subject to more than one meaning in the courts of the day.

Washington's statutory authority and case law confirm no confusion existed between "jurisdiction" and "arbitration." By the time RCW 48.18.200 was enacted in 1947, arbitration had been codified and placed under the sound discretion of this state's courts, unlike its precursor, common law arbitration. Moreover, arbitration in Washington remains under the jurisdiction of the state's courts, which have substantial statutory power over arbitration proceedings.³

³ See RCW 7.04A.260; *Everett Shipyard, Inc. v. Puget Sound Environmental Corp.*, 155 Wn. App. 761, 231 P.3d 200 (2010) (review denied, 170 Wn.2d 1006, 245 P.3d 227 (2010)).

WSDOT's arguments concerning the judicial suspicion of arbitration are flawed, in part because they are premised on an inaccurate assumption that all dispute resolution procedures referred to as "arbitration" are, and were historically, the same. WSDOT's characterization of arbitration as something derided by the courts until "modern" times fails appreciate when and why the "modern" view changed in Washington and elsewhere. In turn, the trial court adopted WSDOT's flawed legal and historical analysis, using it to deny James River's right to rely on the valid, legally-enforceable arbitration provisions in its policies.

1. The characteristics of arbitration evolved from antiquity to codification, from extrajudicial to a fully-accepted dispute resolution mechanism under the jurisdiction of the courts.

Just as "jurisdiction" has more than one meaning,⁴ "arbitration" has referred to more than one form of dispute resolution. Moreover, the characteristics of an arbitration that is subject to statutory authority differ from older forms of arbitration, which operated outside of the official legal system and beyond the jurisdiction of the courts. Arbitration, in the broad

⁴ *DiMercurio v. Sphere Drake Ins. Co.*, 202 F.3d 71, 78 (1st Cir. 2000).

sense, can be traced to antiquity.⁵ Arbitration was used as early as the thirteenth century by English merchant guilds, which imposed a “law of the shop” dispute resolution that operated wholly outside of the courts.⁶ In England, arbitration predated the common law courts, beginning with use by the Ecclesiastical courts.⁷

Early English common law courts opposed arbitration based on its extrajudicial nature.⁸ In early common law, “arbitration was entirely a matter of private arrangement for which there was no authority except the personal authority of the parties to the agreement[.]”⁹ The courts’ early opposition to arbitration is attributed to the belief that arbitration “ousted” the courts of their jurisdiction.¹⁰ Scholars have also attributed early judicial opposition to arbitration as a means of protecting court revenues and jobs, as well as a general mistrust of the fairness of early arbitration procedures.¹¹ Gradually, English law permitted certain forms of arbitration with safeguards over the courts’ jurisdiction, and the method

⁵ Philip J. Bruner & Patrick J. O’Connor, Jr., 6 Bruner & O’Connor on Construction Law § 20:2 (2011); Paul L. Sayre, *Development of Commercial Arbitration Law*, 37 Yale L.J. 595, 597-98 (1927).

⁶ Bruner, *supra* note 3.

⁷ Sayre, *supra* note 3, at 597.

⁸ Bruner, *supra* note 3.

⁹ Sayre, *supra* note 3 at 598.

¹⁰ *See, e.g., id.* at 603.

¹¹ Bruner, *supra* note 3; Sayre, *supra* note 3, at 597.

gained greater acceptance as codification of arbitration procedures developed.¹²

In the United States, courts initially viewed arbitration with the same mistrust as the early English courts.¹³ This mistrust of what became known as “common law” arbitration remained well after England passed arbitration statutes and its courts widely accepted arbitration proceedings.¹⁴ United States jurisdictions first began passing arbitration statutes in the late nineteenth century and early twentieth century.¹⁵ As those statutes expanded and the federal government passed its own arbitration statute, arbitration gained wider acceptance. Today, arbitration is routinely practiced. Moreover, as Washington courts recognize, “[e]ncouraging parties voluntarily to submit their disputes to arbitration is an increasingly important objective in our ever more litigious society.”¹⁶

¹² *Sayer, supra* note 3, *passim*.

¹³ *Bruner, supra* note 3.

¹⁴ *See, e.g., Tacoma Ry. & Motor Co. v. Cummings*, 5 Wash. 206, 208, 31 P. 747 (1892).

¹⁵ *Bruner, supra* note 3.

¹⁶ *Godfrey v. Hartford Cas. Ins. Co.*, 142 Wn.2d 885, 892, 16 P.3d 617 (2001) (quoting *Boyd v. Davis*, 127 Wn.2d 256, 262, 897 P.2d 1239 (1995)).

2. Washington's arbitration statutes have vested jurisdiction over arbitration in the state's courts since the late-nineteenth century, when common law arbitration was abolished in this state.

Among United States jurisdictions, Washington was ahead of its time when it first created statutory arbitration. Until codification, arbitration procedures in this state were largely extrajudicial. In 1892, the Washington Supreme Court addressed the status of arbitration in this state, comparing the historic nature of arbitration with Washington's new and atypical statutory arbitration:

An arbitration, at common law, was of such a nature that the decision of the arbitrators was not subject to control by the courts, excepting by a formal action brought for that purpose; but it is perfectly clear from our statute [(Rem. & Bal. Code § 420 et seq.)] that the arbitration therein authorized is entirely different, so far as the question of control of the award by the court in which it is required to be filed is concerned. Under our statute the award is not so far a finality that in itself it can be in any manner enforced against the defeated party until it has been acted upon by the court.^[17]

In 1916, the Washington Supreme Court again addressed the state's unusual (for the time) statutory arbitration and the jurisdiction held over arbitrations in this state by its courts:

Much confusion has been brought into our arbitration practice by common-law doctrines and decisions under statutes of other states, nor have the opinions of this

¹⁷ *Tacoma Ry.*, 5 Wash. at 208.

court been entirely harmonious. The present seems a suitable occasion to review them.

That common-law arbitration was excluded by our [arbitration] statute [(Rem. & Bal. Code § 420 et seq.)] is plain. For instance, either party under the former could repudiate the proceedings before an award was actually returned, and even afterwards, should he refuse to pay it, there was nothing left the prevailing party but to bring a suit upon it. Both these burdensome rights are in express terms swept away, for the statute makes the arbitration a preliminary part of judicial hearing; the award in a sense automatically passing into judgment unless the losing party can persuade the court to modify or set it aside.

Most distinctly too does the change appear from the common law where this statute gives the [arbitration] board a right to compel the attendance of witnesses or to punish for contempt. Nowhere is there recognized or suggested the right of revoking the award at any stage, of independent suit to cancel it, or of proceedings that ignore it. On the contrary, the act directly provides, as we have seen, for excellent internal review. There is indeed a provision that the agreement may impose a bond that the party will abide by the award, but this is not made indispensable *nor does it in any event override positive provisions giving the court jurisdiction to adopt, modify, and enforce the award.* The bond is to secure payment to the winner as well as additional attorneys' fees or damages from delay.^[18]

The court noted its most significant previous arbitration-related decision was *Tacoma Railway & Motor Co. v. Cummings*.¹⁹ In that earlier opinion, the Supreme Court confirmed Washington's unique arbitration statute granted the state's courts jurisdiction to confirm the arbitration

¹⁸ *Dickie Mfg. Co. v. Sound Constr. & Eng'g Co.*, 92 Wash. 316, 319, 159 P. 129 (1916). (Emphasis added.)

¹⁹ *Id.* at 319-20 (discussing 5 Wash. 206, 31 P. 747 (1892)).

award, contrary to common law arbitration.²⁰ The Supreme Court further noted Washington’s arbitration statute was “peculiar” and, as it previously stated in *Tacoma Railway*, “we can get but little aid from the citation of authorities” in interpreting the terms of the statute.²¹ More important, the court confirmed, three years before the original RCW 48.18.200 was enacted, in this state, “Those who enter into arbitration *accept in advance the jurisdiction* of the superior court. . . . Common law arbitration has ceased to exist.”²²

Later, in 1927, the U.S. Ninth Circuit Court of Appeals reiterated:

The Legislature of the State of Washington has prescribed a comprehensive and exclusive scheme for the settlement of disputes by arbitration. Section 420 et seq., Rem. provide that any controversy, suit, or quarrel, except such as respects the title to real estate, may be submitted to arbitration; that the submission shall be in writing; that the award of the arbitrators shall be filed in the office of the clerk of the superior court; that the party against whom the award is made may except thereto in writing, for certain causes; that if, upon exceptions filed, it shall appear to the court that the arbitrators have committed error in fact or law, the court may refer the cause back to them, directing an amendment of the award forthwith, returnable to the court, and on failure to so correct the proceedings, the court shall be possessed of the cause and proceed to its determination; and that the award, when affirmed, shall be in all respects like any other judgment of the Superior Court.

²⁰ *Id.* at 320.

²¹ *Id.* at 321 (quoting *Tacoma Ry.*, 5 Wash. at 206).

²² *Id.* at 321. (Emphasis added.)

As already stated, the *Supreme Court of the State has repeatedly held that the remedy thus prescribed is exclusive of all others.*^[23]

In 1939, the Washington Supreme Court again addressed the nature of the state's statutory arbitration and the jurisdiction held by the courts over it:

Contrary to the practice and procedure in the vast majority of the states, this jurisdiction does not recognize or permit common law arbitration, one of the distinguishing features of which is that an agreement for such arbitration is revocable. In this state, the proceeding is wholly statutory and the rights of the parties thereto are governed and controlled by statutory provisions.^[24]

The understanding that arbitration is subject to the jurisdiction of the courts of this state, based on clear statutory authority, has continued unabated to the present.²⁵

Washington's current arbitration statute, like its predecessor, vests jurisdictional authority over arbitrations in the state's courts.

Washington's Uniform Arbitration Act (UAA), RCW 7.04A, applies to all agreements to arbitrate, with the exception of employment contracts and

²³ *Fisher Flouring Mills Co. v. United States*, 17 F.2d 232, 234 (9th Cir. 1927). (Emphasis added.)

²⁴ *Puget Sound Bridge & Dredging Co. v. Lake Wash. Shipyards*, 1 Wn.2d 401, 404, 96 P.2d 257 (1939) (citing, *inter alia*, *Dickie Mfg. Co.*, 92 Wash. at 316). (Emphasis added.)

²⁵ See, e.g., *Boyd v. Davis*, 127 Wn.2d 256, 286, 897 P.2d 1239 (1995) (discussing the statutory nature of arbitration in this state and fact common law arbitration does not exist in Washington).

mandatory (i.e., court-ordered) arbitration of small claims under RCW 7.06.²⁶ The UAA, like Washington's previous arbitration statute, vests jurisdiction over arbitrations in the state's courts. Concerning this jurisdiction, the UAA provides:

7.04A.260 Jurisdiction.

(1) A court in this state having jurisdiction over the dispute and the parties may enforce an agreement to arbitrate.

(2) An agreement to arbitrate providing for arbitration in this state confers exclusive jurisdiction on the court to enter judgment on an award under this chapter.

Washington's UAA further contains numerous provisions and mechanisms by which the courts of this state may enforce, modify, and review arbitration procedures and awards.²⁷ Moreover, the Washington

²⁶ RCW 7.04A.030. The current version of Washington's Uniform Arbitration Act applies to all agreements to arbitrate entered into on or after January 1, 2006, which includes the policies at issue in this appeal. RCW 7.04A.030(a).

²⁷ *See, e.g.*, RCW 7.04A.220 (the court, not arbitrators, finally confirms the arbitration award); RCW 7.04A.230 (court's broad power to vacate an arbitration award); RCW 7.04A.240 (court's power to modify or correct an award); RCW 7.04A.250 (court's entry of judgment on the award); RCW 7.04A.290 (right of an appeal from a judgment on an arbitration award); RCW 7.04A.170 (court enforcement of subpoenas and discovery issued in arbitrations); RCW 7.04A.180 (court enforcement of pre-award rulings by arbitrator); RCW 7.04A.100 (court's power to consolidate arbitrations); RCW 7.04A.110 (court appointment of arbitrators where the parties' agreed method fails); RCW 7.04A.060 (court review of the validity of an agreement to arbitrate); RCW 7.04A.080 (right of a party to seek a court order for "provisional remedies to protect the effectiveness of an arbitration proceeding to the same

Supreme Court has recently reconfirmed that under Washington’s arbitration statute, “[t]he parties . . . in all arbitrations, affirmatively invoke the *jurisdiction* of Washington courts to facilitate and enforce the arbitration.”²⁸ The Supreme Court has also noted, “Washington State . . . has a strong public policy favoring arbitration of disputes.”²⁹

3. The Federal Arbitration Act applied the principles of Washington’s original arbitration act to the nation as a whole and controls over the arbitration provisions at issue.

In 1925, Federal Arbitration Act (FAA) became law.³⁰ The FAA, which *followed* Washington’s original arbitration statute, was designed “to ensure the validity and enforcement of arbitration agreements in contracts involving maritime transactions or interstate commerce.”³¹ Under the FAA, in any contract concerning interstate commerce, “an agreement in writing to submit to arbitration an existing controversy arising out of such

extent and under the same conditions as if the controversy were the subject of a civil action”); RCW 7.04A.070 (court’s power to compel arbitration).

²⁸ *Godfrey v. Hartford Cas. Ins. Co.*, 142 Wn.2d 885, 896 (2001) (addressing RCW 7.04, et seq., the immediate precursor to the current RCW 7.04A, et seq.). (Emphasis added.)

²⁹ *Zuver v. Airtouch Commc’ns*, 153 Wn.2d 293, 201, 103 P.3d 753 (2004).

³⁰ Arbitration Act of Feb. 12, 1925, ch. 213, 43 Stat. 883 (codified at 9 U.S.C. § 2).

³¹ Preston D. Wigner, *The United States Supreme Court’s Expansive Approach to the Federal Arbitration Act: a Look at the Past, Present, and Future of Section 2*, 29 U. Rich. L. Rev. 1499, 1499 (1995).

contract . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of the contract.”³²

The FAA further ensures “judicial enforcement of privately made agreements to arbitrate.”³³ As Washington courts have recognized, “the FAA ‘create[s] a body of federal substantive law of arbitrability. . . . [that] is enforceable in both state and federal courts.’”³⁴ Based on the FAA:

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had and in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.³⁵

The written agreements (insurance policies) at issue in this appeal were issued by James River, an undisputed surplus lines (i.e., “unauthorized” or out-of-state) insurer, and WSDOT, an agency of the State of Washington is seeking coverage under them. (CP 7-15). Interstate commerce, therefore, is implicated, and the provisions of the FAA apply over any other Washington state statute (including

³² 9 U.S.C. § 2.

³³ *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219 (1985).

³⁴ *Walters v. A.A.A. Waterproofing, Inc.*, 120 Wn. App. 354, 85 P.3d 389 (2004) (quoting *Perry v. Thomas*, 482 U.S. 483, 489 (1987)).

³⁵ 9 U.S.C. § 3.

Washington's UAA), unless a federal statute carves out an exception. As we discuss in Section C., *infra*, no such exception applies.

Furthermore, the United States Supreme Court recently held that the Federal Arbitration Act preempts California's judicial rule regarding the unconscionability of class arbitration waivers in consumer contracts, and upheld an arbitration clause in a cellular telephone contract.³⁶ The Court specifically found that "[w]hen state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA."³⁷

Thus, James River properly requested that the trial court compel arbitration pursuant to 9 U.S.C. § 3, and that request was improperly denied. (CP 65-84, 1159-1162).

4. No authority holds RCW 48.18.200 to void arbitration provisions in insurance policies, and Washington law strongly favors arbitration in general.

Washington law strongly favors arbitration, and the courts of this state have expressly held arbitration is essential to handling disputes in our litigious society.³⁸ In its briefing before the trial court, WSDOT cited no Washington authority holding that mandatory arbitration provisions in

³⁶ *AT&T Mobility LLC v. Concepcion et ux.*, 131 S. Ct. 1740 (2011).

³⁷ *Id.*, 131 S.Ct. at 1747 (citing *Preston v. Ferrer*, 552 U.S. 346, 353 (2008)).

³⁸ *See, e.g., Godfrey*, 142 Wn.2d at 892; *Perez v. Mid-Century Ins. Co.*, 85 Wn. App. 760, 765, 934 P.2d 731 (1997).

insurance contracts are treated any differently, much less any authority specifically holding that RCW 48.18.200 bars such provisions. Contrary to WSDOT's arguments, and the trial court's Order, parties to arbitrations in this state are unquestionably under the "jurisdiction" of its courts.³⁹ Moreover, the courts of this state routinely enforce arbitration provisions in insurance contracts.⁴⁰

The only case WSDOT found that analyzed RCW 48.18.200 was *Keesling v. Western Fire Ins. Co. of Fort Scott Kansas*, which addressed the validity of an *appraisal* provision in an insurance policy under the statute.⁴¹ In *Keesling*, Division One held: "A provision in a fire insurance policy calling for the appraisal of the actual amount of the fire loss in the event a demand for appraisal is made by either the insurer or the insured does not deprive the courts of the state of jurisdiction of action against the insurer."⁴² The court then cited various authorities in favor of appraisal clauses, including a Montana case from 1891.⁴³

³⁹ *Godfrey*, 142 Wn.2d at 896.

⁴⁰ *See, e.g., id.*; *Price v. Farmers Ins. Co. of Wash.*, 133 Wn.2d 490, 493-97, 946 P.2d 388 (1997).

⁴¹ 10 Wn. App. 841, 520 P.2d 622 (1974).

⁴² *Id.* at 845.

⁴³ *Id.* at 846 (citing *Randall v. Am. Fire Ins. Co.*, 10 Mont. 340, 25 P. 953 (1891)).

In a footnote, the *Keesling* opinion quotes from the Montana court’s discussion of why, under late-nineteenth century Montana law, an appraisal of the value or quantity of a dispute was different from a “contract requiring all differences or controversies arising out of their rights and liabilities be submitted to arbitration[.]”⁴⁴ The early Montana court’s statement was based on the old concept of arbitration being wholly extrajudicial. Borrowing from that older reasoning, the Montana opinion even states the appraisal provision “does not oust the jurisdiction of the courts[.]” using the same “ouster” language seen in pre-statutory arbitration opinions.⁴⁵

Contrary to WSDOT’s and the trial court’s conclusions, *Keesling* provides no support for WSDOT’s “ouster” claims related to arbitration under Washington law. *Keesling* contains no analysis of RCW 48.18.200 with respect to arbitration. Aside from the quotation from the Montana court, the word “arbitration” is used only once in the *Keesling* opinion, in its discussion of a Washington Supreme Court case from 1896 (*Davis*), four years after statutory arbitration was passed in this state.⁴⁶

⁴⁴ *Id.* at 846 (quoting *Randall v. Am. Fire Ins. Co.*, 10 Mont. at 340).

⁴⁵ *Id.*

⁴⁶ *Id.* at 847 (citing *Davis v. Atlas Assurance Co.*, 16 Wash. 232, 47 P. 436, 47 P. 885 (1896)).

In its discussion of *Davis*, an insurance matter, the *Keesling* court notes the Washington Supreme Court held an appraisal provision was valid, “but not a condition precedent to a right of action on the policy.” The *Davis* court did, however, also hold “when a demand for appraisal has been made pursuant to the policy provisions, the insured’s refusal thereof might be pleaded as a bar to recovery.”⁴⁷ After an appraisal procedure “collapsed,” the *Davis* court determined that the jury had to decide if this “collapse” was the insured’s fault (barring recovery) or the insurer’s fault (permitting the suit against it). The *Keesling* court described the result as follows: “The jury verdict found the [insurance] company at fault in not completing the appraisal and entering into a new arbitration.”⁴⁸ WSDOT made no mention before the trial court of this implicit *validation* of arbitration clauses in insurance contracts under Washington law within the *Keesling* opinion.

WSDOT’s motions before the trial court also rely on *Kruger Clinic Orthopaedics, LLC v. Regence BlueShield* for various propositions.⁴⁹ *Kruger*, however, addresses a specific, inapposite Washington statute and

⁴⁷ *Id.*

⁴⁸ *Id.* (Emphasis added.)

⁴⁹ 157 Wn.2d 290, 138 P.3d 936 (2006).

related regulation applying exclusively to health care insurance.⁵⁰

Moreover, Washington courts have expressly confirmed *Kruger* applies only in the context of the health care laws it addressed.⁵¹ The trial court's finding that *Kruger* was "persuasive authority, if not exactly binding precedent," therefore, was in error. (RP 05/20/11, 39).

B. The Trial Court Misconstrued RCW 48.15.150, Erroneously Concluding the Venue Statute Operates to Preclude Arbitration Provisions in Insurance Policies.

The trial court accepted WSDOT's erroneous argument that RCW 48.15.150 precludes arbitration provisions in insurance policies, either individually or in concert with RCW 48.18.200. The plain language of RCW 48.15.150 reveals the trial court's error. The statute states:

48.15.150 Legal process against surplus line insurer.

(1) An unauthorized insurer shall be sued, upon any cause of action arising in this state under any contract issued by it as a surplus line contract, pursuant to this chapter, in the superior court of the county in which the cause of action arose.

(2) Service of legal process against the insurer may be made in any such legal process either by person competent to serve a summons or by registered mail or certified mail with return receipt requested. At the time of such service the plaintiff shall pay to the commissioner ten dollars, taxable as

⁵⁰ *Id.* at 295 (noting the issue before the court was whether the FAA preempted RCW 48.43.055 and WAC 284-42-322).

⁵¹ *Verbeek Props.*, 159 Wn. App. at 92.

costs in the action. The commissioner shall forthwith mail the documents of process served, or a true copy thereof, to the insurer at its principle place of business last known to the commissioner, or to the person designated by the insurer for that purpose in the most recent document filed with the commissioner, on forms prescribed by the commissioner, by prepaid registered or certified mail with return receipt requested. The insurer shall have forty days from the date of service upon the commissioner within which to plead, answer, or otherwise defend the action. Upon service of process upon the commissioner in accordance with this provision, the court shall be deemed to have jurisdiction in personam of the insurer.

(3) An unauthorized insurer issuing such policy shall be deemed to have authorized service of process against it in the manner to and to the effect as provided in this section. Any such policy shall contain a provision designating the commissioner as the person upon whom service of process may be made.

Rather than viewing the statute as a whole and in its proper context within the insurance code, WSDOT extracted the words “shall be sued . . . in the superior court” and argued the statute is not a venue statute for surplus line insurers, but a bar to arbitration provisions in insurance contracts. WSDOT’s argument was premised on no authority whatsoever and is contrary to language of the statute, which makes no mention of “arbitration.” Instead, WSDOT simply argued the provision specifying suit in the superior court would be “superfluous” if it were a venue provision. (CP 630). That is, WSDOT claimed the insurance code has

other general (i.e., not specific to surplus line insurers) venue-related provisions, rendering a provision specific to suits against surplus line insurers unnecessary. (Id.) Moreover, as with RCW 48.18.200, WSDOT also created a new name for 48.15.150, calling it the “jurisdictional statute” and ignoring the statute’s title of “Legal process against surplus line insurer,” which makes clear that RCW 48.15.150 delineates the *process* by which a surplus line insurer shall be served, as well as the venue in which it is to be sued.

No matter what moniker WSDOT ascribes the statute, the words “shall be sued . . . in the superior court” relate to *venue* only, and WSDOT can point to no authority to the contrary.⁵² The term appears in a section of the statute addressing how a surplus line insurer should be sued, the manner for serving process, the number of days for the surplus line insurer’s response, and various other venue, jurisdictional, and procedural issues.⁵³ Furthermore, the statutory section is within RCW 48.15, which contains a total of twenty-two sections applicable to surplus line or

⁵² The trial court’s relevant Order also denied James River’s Objection and Motion to Strike Plaintiff’s Statement of Additional Authorities. (CP 1159-1162). Specifically, James River asked the trial court to consider the version of RCW 48.15.150 applicable to the parties’ dispute, not a later version submitted by WSDOT. The only change in the later version, however, is non-substantive. The word “shall” is replaced with “must,” and is ultimately a distinction without a difference. Nevertheless, the trial court’s consideration of the subsequent statute was in error. (See CP 1160).

⁵³ RCW 48.15.150(2)-(3).

“unauthorized” insurers only. These provisions are similar, and in some cases nearly identical, to numerous provisions throughout the insurance code applicable to other types of insurers or insurers in general. The fact that similar provisions are repeated in different places in the insurance code does not render them “superfluous” as WSDOT’s argued below.

For example, RCW 48.05.215 defines the jurisdiction of state courts, service of process and procedure on surplus lines carriers. Comparing RCW 48.05.215 to RCW 48.15.150 side-by-side reveals numerous completely duplicative provisions applicable to “unauthorized” or surplus line insurers and suits against them. Plaintiffs are even twice informed they must pay “ten dollars” to the commissioner as “taxable as costs in the action.” RCW 48.05.215(2); RCW 48.15.150(2). The existence of duplicative provisions in the insurance code alone, therefore, is not evidence the legislature had some special purpose in repeating itself. The duplications are better explained by the numerous additions and revisions the code has received over the course of more than sixty years and its evolution from various statutes predating its 1947 adoption.

WSDOT cannot establish that the term “shall be sued . . . in the superior court” has some special meaning related to arbitration provisions. The plain language of RCW 48.15.150 neither states nor hints at a bar on

arbitration provisions. Moreover, no authority expresses such an intent by the legislature.

The trial court also seemed to find no specific bar to arbitration provisions in RCW 48.15.150 alone. Instead, the trial court read the statute in conjunction with RCW 48.18.200 to reach its conclusion. (RP 05/20/11, 37). Its conclusion was in error. No authority states the two statutes have such a purpose or effect. In addition, the trial court's opinion regarding this combined effect is based on its mistaken view of the history behind RCW 48.18.200 and WSDOT's unilateral transformation of that statute into a "judicial action provision." Thus, RCW 48.15.150 provides no basis for voiding the arbitration provision within James River's policies, either alone or in combination with RCW 48.18.200.

C. The Trial Court Erroneously Determined The McCarran-Ferguson Act Applies to "Reverse Preempt" the Federal Arbitration Act Since No Insurance Statute Precluding Arbitration Exists in the State of Washington.

As demonstrated *supra*, no statute in Washington voids arbitration provisions in insurance policies. Moreover, the FAA ensures arbitration provisions are given their full legal force.⁵⁴ The trial court, therefore,

⁵⁴ See, 9 U.S.C. §§ 2-3.

erred in holding the McCarran-Ferguson Act⁵⁵ “reverse preempted” the FAA because the criteria for reverse preemption are unmet.

The McCarran-Ferguson Act states, in relevant part: “No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance . . . unless such Act specifically relates to the business of insurance[.]”⁵⁶ The McCarran-Ferguson Act, therefore, imposes two key criteria for “reverse preemption”: (1) the Act of Congress at issue (here, the FAA) must not “specifically relate to the business of insurance,” and (2) the application of the federal law (the FAA) would “invalidate, impair, or supersede” a state statute “enacted for the purpose of regulating the business of insurance.”⁵⁷

In this case, the FAA is not a federal insurance-specific statute. The second criterion, therefore, is the core issue on appeal. WSDOT cannot establish that “reverse preemption” applies because neither statute at issue is affected by the FAA. In addition, neither Washington statute at issue in this appeal relates to “the business of insurance,” as that term applies in relevant contexts.

⁵⁵ 15 U.S.C. § 1012.

⁵⁶ 15 U.S.C. § 1012(b).

⁵⁷ *Id.*

1. No Washington state insurance statute is invalidated, impaired, or superseded by the Federal Arbitration Act.

WSDOT cannot meet the second criterion for “reverse preemption” because neither RCW 48.18.200 nor RCW 48.15.150 are affected by the FAA. That is, the FAA’s validation of James River’s arbitration provisions in no way “invalidate[s], impair[s], or supersede[s]” those state statutes, based on the analysis above -- the arbitration provision does not divest the Washington Courts of jurisdiction, nor does it affect how an action is brought against a surplus lines insurer. As such, the FAA’s support of this arbitration provision does not affect those statutes either.

In 2005, Hon. John C. Coughenour expressly ruled RCW 48.18.200 has no effect on arbitration clauses in Washington insurance policies.⁵⁸ In its Motion to Bar Initiation of Arbitration Proceedings, WSDOT claimed Judge Coughenour did not understand the history of the statute, based on WSDOT’s flawed understanding of the same. (CP 325-333). Judge Coughenour specifically assessed the

⁵⁸ *Boeing Co. v. Agric. Ins. Co.*, No. C05-921-C, 2005 WL 2276770 (W.D. Wash. 2005) (unpublished opinion). GR 14.1(b) allows the citation of such an unpublished decision if citation to that opinion is permitted under the law of the jurisdiction of the issuing court. As there is no rule in the United States District Court for the Western District of Washington prohibiting the citation of an unpublished order from that court, and the court’s analysis in *Boeing* provides valuable legal authority, James River references it here. *See also* FRAP 32.1(a); CP 433-444.

argument WSDOT put forward in the trial court, that RCW 48.18.200 “depriv[es] the courts of this state of the jurisdiction of action against the insurer.”⁵⁹ Additionally, Judge Coughenour found that “because neither section 48.18.200 nor Washington case law interpreting and applying that section (or Washington's insurance statutes generally) bars the enforcement of express agreements to arbitrate coverage disputes, the McCarran-Ferguson Act” did not apply.⁶⁰

The U.S. First Circuit Court of Appeals analyzed in detail Massachusetts statutory language identical to RCW 48.18.200, finding the statute to specifically fail to trigger the McCarran-Ferguson “reverse preemption” protection. In *DiMercurio v. Sphere Drake Ins. Co.*, the court analyzed a state statute voiding “any condition, stipulation or agreement [in an insurance policy] depriving the courts of the commonwealth of *jurisdiction of actions* against [the insurer].”⁶¹ The court concluded that an agreement to arbitrate did not “oust” jurisdiction from the relevant courts.⁶² The court acknowledged the “modern” view of arbitration had indeed changed from historical judicial suspicion and fear

⁵⁹ *Boeing*, 2005 WL 2276770 at *3.

⁶⁰ *Id.*, 2005 WL 2276770 at *3.

⁶¹ 202 F.3d 71, 73-74 (1st Cir. 2000).

⁶² *Id.* at 75-76.

of “ouster” of jurisdiction.⁶³ The “modern view,” of course, is that an agreement to arbitrate does not deprive or divest courts of their jurisdiction over the parties’ dispute.⁶⁴

The *DiMercurio* court also noted the term “jurisdiction” was “chameleon-like” and had a “wide variety of meanings” beyond a court’s authority to issue a specific type of remedy[.]”⁶⁵ The Massachusetts statute, therefore, did not clearly implicate “arbitration” on its face.

The *DiMercurio* court conceded, however, that the statute was enacted in 1856, at a time when Massachusetts’s jurists were still suspicious of arbitration.⁶⁶ This suspicion was expressed in Massachusetts opinions dating to at least to 1944, long after Washington passed its first arbitration statute and its courts readily upheld arbitration clauses.⁶⁷ In fact, according to the *DiMercurio* court, “[i]t was not until 1960 when Massachusetts adopted the Uniform Arbitration Act for Commercial Disputes that the old ‘ouster of jurisdiction doctrine,’ at least as applied to

⁶³ *Id.* at 76-78.

⁶⁴ *Id.* at 75 (citing, e.g., *Vinar Seguros Y Reaseguros, S.A. v. M/V Sky Reefer*, 29 F.3d 727 (1st Cir. 1994), *aff’d*, 515 U.S. 428 (1995)).

⁶⁵ *Id.* at 78 (quoting *Prou v. United States*, 199 F.3d 37, 45 (1st Cir. 1999)).

⁶⁶ *Id.* at 79.

⁶⁷ *Id.* (discussing *Bauer v. Int’l Waste Co.*, 201 Mass. 197, 87 N.E. 637 (1909); *Sanford v. Boston Edison Co.*, 316 Mass., 631, 636, 56 N.E.2d 1 (1944)).

arbitration was finally put to rest [in Massachusetts].”⁶⁸ It was put to rest in Washington long before that time, even before RCW 48.18.200 was enacted. Thus, the *DiMercurio* finding that arbitration in no way deprives the courts of “jurisdiction of actions” is even more applicable to RCW 48.18.200 than the Massachusetts statute it addressed.

2. The Washington statutes at issue fail to relate to the “business of insurance,” as the term is used in the McCarran-Ferguson Act.

The McCarran-Ferguson Act relates only to the “business of insurance.” As such, courts have clarified that not everything relating to insurance qualifies as the “business of insurance.” In enacting the McCarran-Ferguson Act, “Congress was mainly concerned with the relationship between insurance ratemaking and the antitrust laws, and with the power of the States to tax insurance companies.”⁶⁹

The United States Supreme Court has held:

[The McCarran-Ferguson Act] did not purport to make the States supreme in regulating all activities of insurance companies; its language refers not to the persons or companies who are subject to state regulation, but to laws “regulating the business of insurance.” Insurance companies may do many things which are subject to

⁶⁸ *Id.* at 80.

⁶⁹ *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453,458-59 (1969) (citing, e.g., 91 Cong.Rec. 1087-1088 (remarks of Congressmen Hancock and Celler)).

paramount federal regulation; only when they are engaged in the “business of insurance” does the statute apply.”^{70]}

Other courts have opined on what qualifies as the “business of insurance” under the McCarran-Ferguson on Act:

A disputed claim is not the business of insurance. The business of regulating the insurance industry focuses on the underwriting and spreading of the policyholder's risk. *Group Life & Health Ins. v. Royal Drug Co.*, 440 U.S. 205, 99 S.Ct. 1067, 59 L.Ed.2d 261 (1979). “[S]tate regulation of a practice of an insurance company does not mean that the practice is the ‘business of insurance.’ ” *Id.* at 230, 99 S.Ct. at 1082.^[71]

Similarly, in the present appeal, at issue is a policy provision relating to a claim dispute. Consequently, the relevant Washington statutes, RCW 48.18.200 and 48.15.150, fall outside the scope of the McCarran-Ferguson Act and its “reverse preemption” power. Inasmuch as these statutes do not relate to the “business of insurance,” the FAA continues to ensure that arbitration provisions are given their full legal force.⁷²

⁷⁰ *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453,459-60 (1969)

⁷¹ *Triton Lines, Inc. v. S.S. Mut. Underwriting Ass'n*, 707 F. Supp. 277, 279 (S.D. Tex 1989); *accord, Organ v. Conner*, 792 F. Supp. 693, 696 (D. Alaska 1992); *see also, Hamilton Life Ins. Co. v. Republic Life Ins. Co.*, 408 F.2d 606, 611 (2d Cir. 1969) (arbitration statutes do not regulate the business of insurance).

⁷² *See*, 9 U.S.C. §§ 2-3.

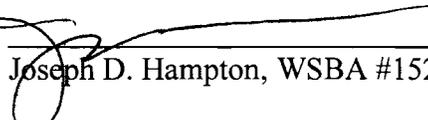
VI. CONCLUSION

James River is entitled to rely upon the arbitration provisions in its policies. No law in this state voids those provisions, and the trial court erred in its conclusion to the contrary. Since no Washington law affects the provisions, the McCarran-Ferguson Act is inapplicable and fails to “reverse preempt” the strong validation the Federal Arbitration Act gives arbitration clauses, including those in insurance policies. Based on the foregoing, James River requests that the trial court’s order denying James River’s arbitration demand be reversed and that the parties be ordered to arbitrate in accordance with the policies’ terms.

DATED: October 27, 2011.

BETTS PATTERSON & MINES, P.S.

By



Joseph D. Hampton, WSBA #15297

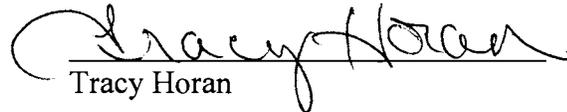
Attorney for Appellant James River Insurance
Company

CERTIFICATE OF SERVICE

I hereby certify that on October 28, 2011, a true and correct copy of the foregoing document was served on the following:

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Dated this 28th day of October, 2011, at Seattle, Washington.


Tracy Horan

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TIME: 10:00 AM
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