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COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

RICHARD BANKSTON and SUSAN BANKSTON, husband and wife
and the marital community composed thereof, d/b/a AAROHN
CONSTRUCTION,

Appellants,

v.

DEVELOPERS SURETY AND INDEMNITY COMPANY, a foreign
corporation,

Respondent.

BRIEF OF RESPONDENT

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I. INTRODUCTION

This case arises out of an indemnity claim brought by Plaintiff Developers Surety and Indemnity Company (“Developers”) against Defendant Richard and Susan Bankston, d/b/a Aarohn Construction (“Aarohn Construction”). Developers brought this action to enforce the terms of the Indemnity Agreement signed by Aarohn Construction on April 25, 2006, to recover losses sustained by Developers as a result of having furnished a Public Works Contract Bond on behalf of Aarohn Construction in connection with a public works contract between Aarohn Construction and Pierce County (“the County”) for landscaping at a facility known as the Pierce County Annex. On August 30, 2006, the County properly terminated Aarohn Construction’s right to continue work on the project, citing numerous construction failures. Soon thereafter, Developers sought reimbursement from Aarohn Construction pursuant to the unambiguous language of the Indemnity Agreement.

Defendants Richard and Susan Bankston, d/b/a Aarohn Construction, signed an unambiguous Indemnity Agreement with Plaintiff Developers. Developers executed a performance bond with Pierce County as beneficiary. Aarohn Construction was terminated for multiple defaults, including but not limited to (1) damage to the sprinkler system, (2)

flooding the interior of the Annex building; (3) failure to provide schedule meeting contract requirements; and (4) failure to conform to schedule.

Developers properly investigated the claim despite Aarohn Construction's attempt to obstruct the investigation. In fact, Developer's investigation was significantly impeded by John Bankston's unwillingness to cooperate with Developers. Developers honored its Performance Bond obligations to the County and sustained a loss in the amount of \$64,259,79. Aarohn Construction is contractually bound to fully reimburse Developers. Accordingly, the trial court properly denied Aarohn Construction's Motion to Dismiss after the close of Developer's case and after the verdict.

II. STATEMENT OF THE CASE

A. BACKGROUND FACTS

On March 23, 2006, John Bankston d/b/a Aarohn Construction submitted a bid to Pierce County for completion of work on the Tree Replacement Project at Annex (“the project”). Report of Proceedings (“RP”) 679; RP 786; Clerk’s Papers (“CP”) 447-452. The bidding requirements and the provisions of RCW 18.27.et seq., specifically provide that contractors are required to be registered with the State of Washington Department of Labor and Industries. On April 13, 2006, the registration of John Bankston, d/b/a Aarohn Construction, was suspended by the State of Washington Department of Labor and Industries. CP 147. At the direction of his father, John Bankston, and without knowledge of Pierce County, Richard Bankston, d/b/a Aarohn Construction – a construction company newly registered with the Department of Labor and Industries on April 25, 2006 – entered into a contract with Pierce County. CP 147.

Without Pierce County’s informed consent, Richard Bankston, d/b/a Aarohn Construction, entered into a construction contract with Pierce County in which Richard Bankston, d/b/a Aarohn Construction, agreed to furnish all labor and material and perform all work for the project. CP 147. Developers issued a Public Works Contract Bond in the

penal sum of \$144,254.65 on behalf of Aarohn Construction in connection with the contract. Supplemental Designation of Clerk's Papers ("SCP"), Trial Exhibit No. 1.

Aarohn Construction, began work on the project and was paid \$37,003.98 by the County. RP 537. The County defaulted Aarohn Construction, and terminated its right to continue work on the project on August 30, 2006, citing numerous construction failures. RP 546.

After defaulting and terminating Aarohn Construction, the County was hired Serpanok Construction to complete the remaining work required under the contract, including repair of property damage caused by Aarohn Construction, for a total of \$169,728.00, including tax. RP 536-539. Subsequently, a demand was made upon Developers and its Performance Bond. RP 519. The County demanded \$64,259.79 from Developers to reimburse it for the difference between the Serpanok amount and the portion of the contract amount remaining after deducting the Aarohn Construction payment. RP 535-536.

Prior to making payment on the bond, and in the course of investigating the claim, representatives of Developers met on-site with County officials and John Bankston, the company's project superindendant and on-site manager, to see if the County would allow Aarohn Construction to finish the job. RP 307; RP 670; 672. In fact, from

the outset, Developers sincerely hoped the County would allow Aarohn Construction to finish the job because “it was best for Mr. Bankston and the surety company.” RP 308. Toward that end, Developers representatives examined several means by which Aarohn Construction could finish the job under a new schedule, and, if necessary, with additional manpower. RP 308. However, in order to facilitate an alternative strategy for completion of the project, Developers needed John Bankston to provide documentation supporting the feasibility of a new plan. RP 469 – 470. Despite numerous written requests, that information was never provided. RP 490-491.

On March 8, 2007, based on “its studied and prudent opinion,” Developers paid the County \$64,259.79, and subsequently filed a Complaint for Indemnification against personal indemnitors, Richard and Susan Bankston, d/b/a Aarohn Construction, to recover all losses, including attorney’s fees and costs. RP 604; RP 536; CP 3-6. Throughout this entire process, **Pierce County was totally unaware and the Bankstons failed to disclose**, that the original bid was submitted by John Bankston, d/b/a Aarohn Construction, while the actual construction contract was executed with Richard Bankston, d/b/a Aarohn Construction. RP 988-990 (emphasis added). In fact, John Bankston and Richard Bankston had created two separate entities, each with separate UBI

numbers and separate Department of Labor and Industries registration numbers. CP 148.

B. THE UNAMBIGUOUS TERMS OF THE INDEMNITY AGREEMENT

Under the terms of the Public Works Performance Bond, indemnitors Richard and Susan Bankston, d/b/a Aarohn Construction, promised that in the event of any loss they would fully reimburse surety for all loss, cost, and expense. CP 403; RP 634. The indemnification clause signed by Aarohn Construction covers any loss sustained by Developers as a result of having furnished bonds on behalf of Aarohn Construction. RP 458. The General Indemnity Agreement signed and agreed to by Richard Bankston specifically provides as follows:

1. To reimburse Surety, upon demand for all payments made for and to indemnify and keep indemnified Surety from:
 - a) All demands, loss, contingent loss, liability and contingent liability claim, expense, including attorney's fees, for which Surety shall become liable or shall become contingently liable by reason of such suretyship,...

Moreover, Richard Bankston further agreed pursuant to Paragraph 2 of the Indemnity Agreement that:

2. Surety shall have the exclusive right to determine whether any claim or suit shall, on the basis of liability, expediency or otherwise, be denied, paid, compromised defended or appealed. An itemized statement of payments made by Surety for loss, contingent loss, liability, and/or expense, sworn to by an officer of Surety, or the vouchers for such payments, shall be prima facie evidence of the obligation of the undersigned to reimburse Surety.

CP 403 (emphasis added); SCP, trial exhibit 2.

Based on the terms of the Indemnity Agreement, Developers had broad discretion to settle claims made against the performance bond, even over the objection of its principal Richard Bankston. RP 606. Here, Richard Bankston agreed to reimburse Surety for “all payments” made for which Surety shall become “liable” or “contingently liable.” CP 403 (emphasis added). The Indemnity Agreement goes on to say that Surety shall have the “exclusive right” to determine the propriety of payments made. *Id.* (emphasis added). Put simply, if Aarohn Construction was contingently liable (possibly liable) under paragraph 1, Developers had the discretion to make payment if based on “liability, expediency or otherwise” under paragraph 2. *Id.* Furthermore, the Indemnity Agreement expressly states that itemized statements of payments made by Surety shall be prima facie evidence of Developer’s right to indemnity. *Id.* (emphasis added).

C. PROCEDURAL HISTORY

After Developers presented its case in chief, Aarohn Construction moved for a directed verdict. CP 631-636. The trial court denied the motion. Aarohn Construction renewed its motion after the verdict. CP 698-708. The trial court again denied the motion. CP 790.

The jury carefully considered whether Developers was entitled to reimbursement of the funds paid under the Indemnity Agreement. CP 665. The jury awarded Developers damages in the amount of \$60,759.79. CP 695-697. The trial court subsequently awarded Developers prejudgment interest on the verdict amount. CP 695.

Aarohn Construction timely appealed.

III. LEGAL ARGUMENT

A. STANDARD OF REVIEW

This Court reviews a trial court's decision on a motion for directed verdict and a motion for judgment n.o.v. using the same standard as the trial court. *Mega v. Whitworth Coll.*, 138 Wn. App. 661, 668, 158 P.3d 1211 (2007); *RWR Mgmt., Inc. v. Citizens Realty Co.*, 133 Wn. App. 265, 274, 135 P.3d 955 (2006). In reviewing a motion for judgment as a matter of law, the court must interpret the evidence most strongly against the moving party and in the light most favorable to the opponent. *RWR Mgmt.*,

Inc. v. Citizens Realty Co., 133 Wn. App. at 274. Moreover, a judgment as a matter of law admits the truth of the nonmoving party's evidence and all inferences that can be reasonably drawn from it. *Mega v. Whitworth Coll.*, 138 Wn. App. at 668. The court must deny the motion if any justifiable evidence exists on which reasonable minds might reach conclusions consistent with the verdict. *Id* (emphasis added).

B. THE TRIAL COURT PROPERLY DENIED AAROHN'S MOTION FOR DIRECTED VERDICT AND JUDGMENT N.O.V.

a) Developers is Entitled to Indemnification Because it Paid the County After a Reasonable Investigation Showed that Aarohn Construction was Liable or Contingently Liable

Courts have repeatedly upheld Indemnity Agreements subject only to the condition that payment by the surety is not the product of bad faith. *U.S. Fid. & Guar. Co. v. Feibus*, 15 F. Supp. 2d 579, 585 (M.D. Pa. 1998), *aff'd* 185 F.3d 864 (3rd Cir. 1999); *Gen. Accident Ins. Co. of Am. v. Meritt-Meridian Constr. Co.*, 975 F. Supp. 511, 516 (S.D.N.Y. 1997). Thus, to recover under its General Indemnity Agreement, a surety need only have made payments in good faith; the surety need not prove the actual validity of the claims paid. *Int'l Fid. Ins. Co. v. Spadafina*, 192 A.D. 2d 637, 639, 596 N.Y.S. 2d 453 (N.Y.App.Div. 1993). As such, contingent or possible liability is a sufficient basis for indemnity.

At trial and on appeal, Aarohn Construction maintains that Developer's right of indemnity under the contract never arose because Developers paid the claim without a determination as to whether Aarohn Construction was actually liable. *Appellant's Brief* 16-17. Aarohn contends that Developers must demonstrate actual liability of its principal before making payment. Here, Aarohn's argument is based on an erroneous reading of the Indemnity Agreement, which, if read carefully, expressly states that Developers is entitled to indemnification if the principal is "contingently liable" – in other words, possibly liable. CP 403. In fact, Lou White, Developer's in-house attorney in charge of claims, confirmed this interpretation:

Q. (By Mr. Friedrich) [U]nder what circumstances does the surety have right to make a payment?

A. If there's a claim and the claim has some, in the surety's opinion, some legitimacy and there's some reasonable possibility of loss.

RP 606. Nowhere in the Indemnity Agreement are the words actual liability used. Therefore, Developer's decision to pay based on Aarohn Construction's contingent liability is consistent with established surety law, which entitles surety to indemnity without having to prove actual liability on claims paid. *Int'l Fid. Ins. Co. v. Spadafina*, 192 A.D. 2d at

639. Nevertheless, Developers did, in fact, find actual liability on the part of Aarohn Construction after investigation.

Notwithstanding the fact that actual liability was not required for indemnification, Aarohn further contends that there was no reasonable inquiry into Aarohn's contingent liability, and therefore, Developers right to indemnity is prohibited. *Appellant's Brief* 18. However, the evidence at trial shows that Developers sent Conrad Wozney, a claims investigator, to meet on-site with representatives of Aarohn Construction and Pierce County to assess the situation. RP 308. In addition to an on-site investigation of the claim, Developers gathered documentary evidence from both parties to assist in making an informed determination as to the validity of the claim. RP 481-482; RP 490-491. Moreover, the testimony of Mr. Wozney demonstrates that Aarohn Construction was liable or possibly liable:

Q. Again, just go on with what you observed in terms of where you thought he was not being efficient.

A. Yeah. That was all in the irrigation...he cut some of the wires and --

Q. Wires to what?

A. Wires to the irrigation. And he cut some wires to irrigation that was outside the scope of work he was to do. So now they had areas within the county grounds that wouldn't get any water. They were concerned that

they were going to have to water it manually and it was going to be an extra expense for the county.

They also complained that some – there was a (inaudible) that was dropping material onto the asphalt. I don't remember if it was diesel fuel or some other type of fuel. And they were concerned because there was a small stream by the job site and they didn't want to get that contaminated into the stream.

RP 306-307 (emphasis added). Additional testimony from Mr. Wozney

based on the County's letter of termination shows why Aarohn

Construction was liable or contingently liable to the County:

Q. What is the number – what's the first item on the list?

A. "You (Aarohn Construction) failed to provide schedules meeting contract requirements, and you failed to conform even to the inadequate schedule you did provide."

RP 365 (emphasis added). Finally, Mr. White's testimony further explains

why Aarohn Construction was potentially liable to the County:

Q. Okay. And also, again, reading the first sentence of the heading, it's No. 3. And apparently, was there also an allegation by the county that he flooded the interior building?

A. Yes.

RP 544 (emphasis added). As demonstrated above, based on the information discovered in the course of Developer's investigation, there was a reasonable possibility that Aarohn Construction was liable to the County. Thus, under the unambiguous language of the Indemnity

Agreement, Developer's was entitled to indemnification for payments made on the basis of Aarohn Construction's contingent liability.

In addition to conducting a reasonable inquiry into Aarohn Construction's liability, one of the most important factors considered by courts in evaluating the surety's reasonableness in paying a claim is whether the contractor has cooperated with the surety and provided information and documentation supporting its defenses. *U.S. Fid. & Guar. Co. v. Feibus*, at 586. If a contractor does not indicate its desire to defend a claim or fails to cooperate with surety's investigation, the surety is entitled to pay and seek reimbursement. Lawrence R. Moelmann & John T. Harris, *The Law of Performance Bonds* 198 (1999). As to this point, Mr. White testified that Developers provided Aarohn Construction countless opportunities to demonstrate that it was not liable or contingently liable to the County for, among other things, flooding the interior of the Pierce County Annex building:

Q. You then requested information from John Bankston did you not?

A. Yes. Oh, yeah.

Q. Now did that information ever come?

A. Not in any substantive form, no.

Q. Did he ever provide you with documentation supporting his

defenses?

A. No, not to me.

RP 490-491.

As demonstrated above, Developers made reasonable efforts to investigate the claim and afford Aarohn Construction an opportunity to show that it had been wrongfully terminated before it exercised its right to pay the County. Throughout the course of the investigation, Mr. White implored John Bankston to furnish exculpatory documentation to assist in Developer's investigation of the claim. RP 608-609. Unfortunately, to Aarohn Construction's own detriment, John Bankston never provided documentation to support its position, and ultimately, Developers exercised its exclusive contractual right to make payment:

Q. So the fact that you didn't get any documentation was one of the factors you considered?

A. Ultimately, it was a major factor, that he couldn't – he couldn't put – put up what he was telling me what he had to support. I mean, he couldn't support what he had – what his claim was.

Q. Did that factor into your decision?

A. When I was figuring out what I was going to do, you know, on this thing and whether we were going to pay or not, the fact that he didn't support what he said was certainly a factor.

Q. Now, was one of the considerations, then, if there was, let's say, the lack of documentation – that's what you're saying, correct?

A. Right.

RP 608-610.

Contrary to Aarohn Construction's claims that Developers paid based entirely on expediency, the trial record provides substantial evidence that Developers decided to pay the County only after conducting a reasonable investigation that revealed Aarohn Construction's liability or contingent liability. After receiving notice of the claim from the County, Developers sent Conrad Wozney to investigate the claim. Based on Mr. Wozney's investigation and the documentary evidence gathered by Developers, surety believed there was a reasonable basis for liability. Subsequently, and pursuant to the express language of the Indemnity Agreement, Developers exercised its exclusive right to decide whether to make payment. RP 606. In accordance with those rights, Developers satisfied the claim. As a result, Developers has a right to indemnity under the contract.

Upon review, when viewing the evidence in the light most favorable to the nonmoving party and admitting the truth of the nonmoving party's evidence and all inferences that can be reasonably drawn from it, the trial court properly denied Aarohn Construction's

Motion for a directed verdict. In addition, because the trial court must deny the motion if any justifiable evidence exists on which reasonable minds might reach conclusions consistent with the verdict, the trial court properly denied Aarohn Construction's Motion to Dismiss after the verdict. Accordingly, the jury verdict in Developer's favor should be affirmed.

b) The Unambiguous Language of the Indemnity Agreement Grants Developers a Right to Indemnity Consistent with the Contract's Plain Intent

Generally, the terms of a General Indemnity Agreement will be enforced as written. *U.S. Fid. & Guar. Co. v. Napier Elec. & Constr. Co.*, 571 S.W.2d 644, 646 (KY.App. 1978). Specifically, that Court stated as follows:

The right of an indemnitee to recover of the indemnitor under a contract of indemnity according to the terms of such contract is well recognized. Such contract is not against public policy and will be enforced if the indemnitee has suffered loss thereunder and has complied with its terms.

Id. Moreover, Indemnity Agreements are valid and enforceable contracts. *See Cont'l Cas. Co. v. Seattle*, 66 Wn.2d 831, 405 P.2d 581 (1966); *New Amsterdam Cas. Co. v. Hamilton*, 123 Wn. 147, 212 P. 147 (1923).

In absence of fraud or bad faith on the part of the surety, the indemnitor is held to the reimbursement terms of the express Indemnity

Agreement. *Commercial Ins. Co. v. Pac./Peru Constr.* 558 F.2d 948 (9th Cir. 1977).

The Indemnity Agreement signed by Richard and Susan Bankston, d/b/a Aarohn Construction, provides in pertinent part that Richard and Susan Bankston agree:

1. To reimburse Surety, upon demand for all payments made for and to indemnify and keep indemnified Surety from:
 - a) All demands, loss, contingent loss, liability and contingent liability claim, expense, including attorney's fees, for which Surety shall become liable or shall become contingently liable by reason of such suretyship,...

Moreover, Richard Bankston further agreed pursuant to Paragraph 2 of the Indemnity Agreement that:

2. Surety shall have the exclusive right to determine whether any claim or suit shall, on the basis of liability, expediency or otherwise, be denied, paid, compromised defended or appealed. An itemized statement of payments made by Surety for loss, contingent loss, liability, and/or expense, sworn to by an officer of Surety, or the vouchers for such payments, shall be prima facie evidence of the obligation of the undersigned to reimburse Surety.

CP 403; SCP, trial exhibit 2 (emphasis added).

Here, Richard Bankston agreed to reimburse Surety for all payments made for which Surety shall become liable or contingently

liable. CP 403 (emphasis added). As such, Developers need only show possible liability, not actual liability, as argued by Aarohn Construction. Further, once contingent liability was established, Developers had the sole discretion to make payment whether motivated by “liability, expediency or otherwise.” *Id.* Moreover, the Indemnity Agreement expressly states that itemized statements of payments made by Surety shall be prima facie evidence of Developer’s right to indemnity. *Id.* (emphasis added). As outlined above, the Indemnity Agreement is unambiguous and the terms of the Agreement should be enforced as written. Pursuant to its terms, if possible liability exists, the Indemnity Agreement expressly grants Developers wide discretion to make payment and seek indemnification. *Int’l Fid. Ins. Co. v. Spadafina*, 192 A.D. 2d at 639.

Predictably, in interpreting the Indemnity Agreement, Aarohn Construction deliberately reads paragraph 1 and paragraph 2 out of sequence in order to bolster its claim that the Indemnity Agreement is ambiguous. First, Aarohn Construction asserts that Developer’s is entitled to indemnification under paragraph 1 only when it pays a claim based on liability or contingent liability under paragraph 2. *Appellant’s Brief* 24. Second, Aarohn Construction contends that if Developers pays a claim under paragraph 2 on the basis of “expediency,” then a right to

indemnification does not arise under paragraph 1. *Id* at 25. Aarohn Construction's reading of the Indemnity Agreement is fraught with error.

Here, Aarohn Construction advances a backwards and illogical interpretation of the Indemnity Agreement by reading the paragraph 1 and paragraph 2 out sequence and treating paragraphs 1 and 2 as mutually exclusive, which Developer's in-house counsel pointed-out was an incorrect reading of the contract. RP 564. In doing so, Aarohn Construction violates fundamental principles of contract interpretation, which hold that a contract, including a bond, should be construed as a whole, and, if reasonably possible, in a way that effectuates all its provisions. *Colo. Structures, Inc. v. Ins. Co. of the W.*, 161 Wn.2d 577, 588, 161 P.3d 1125 (2007).

A simple reading of the Indemnity Agreement, beginning with paragraph 1 and proceeding to paragraph 2, reveals that the contract is easily understandable. First, Developer's right to indemnity is initially triggered under paragraph 1 on the basis of "liability" or "contingent liability," the threshold requirement for indemnity. CP 403. Once Developers finds "liability" or "contingent liability" under paragraph 1, the reader must proceed to paragraph 2, which grants Developers "the exclusive right" to decide whether to make to make payment and seek reimbursement from Aarohn Construction on the basis of "liability,

expediency, or otherwise.” CP 403. This construction is simple, straightforward, and unambiguous.

In plain terms, once Developers recognizes possible liability under paragraph 1, the Indemnity Agreement allows Developers to make payment with the added safeguard of paragraph 2, which grants Developers the sole discretion to either investigate the claim further to establish “liability” or simply pay the claim on the basis of “expediency or otherwise.” This interpretation gives meaning to both paragraphs in the order they were intended to be read, and most importantly, supports the intended purpose of the contract between the parties. *Colo. Structures, Inc. v. Ins. Co. of the W.*, at 588. That is, if the principal exposes itself and surety to possible liability, Developers is entitled to protect itself and the beneficiary of the bond, in this case, Pierce County, by making payment on the basis of “expediency.” Mr. White, in-house counsel for Developers, explained that paragraphs 1 and 2 were meant to be interpreted in conjunction with each other because choosing to pay a claim based on “expediency” under paragraph 2 does not mean there isn’t “liability” or “contingent liability” under paragraph 1. RP 564. According to his testimony, liability and expediency are not “mutually exclusive.” *Id.*

This construction advances the express intent of the Indemnity Agreement and the purpose of the surety-beneficiary relationship, which calls for the surety to make reasonably prompt payment in order to allow the construction project to proceed unimpeded. *Gen. Accident Ins. Co. of Am. v. Meritt-Meridian Constr. Co.*, at 516. Nevertheless, Aarohn Construction advances an interpretation that undermines Developer's ability to settle claims in accordance with established surety law.

Aarohn Construction asserts that Developers right to indemnification never arose because it paid the County without any determination as to actual liability. Here, Aarohn Construction advocates an interpretation of the Indemnity Agreement that would require Developers to prove actual liability before paying claimants. Such an interpretation is contrary to the intent of the Indemnity Agreement and the role of surety in facilitating a construction project. *Gen. Accident Ins. Co. of Am. v. Meritt-Meridian Constr. Co.*, at 516.

For example, courts have consistently held that the surety need not prove the validity of the claims it paid. *Gen. Ins. Co. of Am. v. Singleton*, 40 Cal. App. 3d. 439 (1974). There, an indemnitor challenged a surety's decision to settle a bond claim. The indemnitor argued that, in order to recover, the settling surety must prove it was, in fact, liable for the amount paid. Expressly rejecting that argument, the court noted as follows:

To require plaintiff [surety] to establish a case against the defendants [the indemnitors] in the same manner that a claimant against the indemnitee would have been obligated to do, would defeat the purpose of the clauses in the indemnity agreement allowing the indemnitee to settle claims. “The purpose of clauses of the type here is to facilitate the handling of settlements by sureties and obviate unnecessary and costly litigation.”

Id. at 294, quoting *Transamerica Ins. Co. v. Bloomfield*, 401 F.2d 357, 363 (6th Cir. 1968).

Indeed, a number of courts have gone as far as to observe that in enforcing a surety’s right to indemnify for losses incurred in good faith, “it is irrelevant whether [the principal] was actually liable on the underlying debt[.]” *Int’l Fid. Ins. Co. v. Spadafina*, 192 A.D. 2d at 639 (emphasis added).

Not surprisingly, Aarohn Construction conveniently misconstrues the terms of the Indemnity Agreement which specifically provides that Developer’s right to indemnity is triggered by “contingent liability,” not actual liability. In accordance with its express rights under the Indemnity Agreement, Developers exercised its right to pay the County because it saw contingent or possible liability under paragraph 1, and then proceeded to make payment as authorized under paragraph 2 on the basis of “liability, expediency or otherwise.” CP 403. Accordingly, because Developers complied with its obligations under the Indemnity Agreement, Developers is entitled to indemnification.

Next, Aarohn Construction argues in its Appellate Brief that Developer's right to indemnity never arose because it paid the County based entirely on "expediency," and not on "liability" or "contingent liability." *Id.* at 27. Aarohn Construction's assertion that Developer's made an election to pay based entirely on expediency is without merit. The testimony of Mr. White at trial demonstrates that Developers paid the County only after careful consideration of Aarohn Construction's liability:

Q. (Referring to Paragraph 1) All right. Now, in your – in your opinion, -- what does – what does this mean?

A. Well, the way I interpreted that language was that we had a claim against us, which we surely did. We had a realistic potential for liability, which in my opinion, we did; that we had, number one, the right to pay that, and number two, to seek reimbursement for that. It didn't need to go to trial or anything like that.

There was a possibility – a reasonable possibility of loss. And the claim had a reasonable basis, we could have, in our studied and prudent opinion make payment and seek reimbursement.

RP 603-604.

As demonstrated above, Developer's decision to pay the County began with a determination of Aarohn Construction's "contingent liability" under paragraph 1. Once the threshold requirement for indemnification was established under paragraph 1, Developers, pursuant to the express terms paragraph 2, was granted the broad discretion to pay

claims based on “liability, expediency or otherwise.” *Id.* Thus, Aarohn Construction’s assertion that Developer’s decision to pay was based entirely on expediency is false.

Moreover, the record is replete with testimony that Developer’s decision to pay was grounded in Aarohn Construction’s liability. The testimony of Mr. White demonstrates that Developers initially made a determination as to “contingent liability” under paragraph 1, which then granted Developers the discretion to make payment under paragraph 2. RP 603-604. Mr. White testified that after finding the threshold requirement of “contingent liability” under paragraph 1, Developers then proceeded to use its discretion under paragraph 2 to settle the claim on the basis of “liability, expediency or otherwise”:

Q. [I]f you look at paragraph 2, under what circumstances does the surety have a right to make a payment?

A. The surety has a very broad right to make payments, which in its best judgment are warranted.

In other words, once Developers saw contingent liability, the Indemnity Agreement granted Developers broad discretion to make payment, which included payment on the basis of “expediency or otherwise.” The interpretation of the Indemnity Agreement advanced by Developers is anything but ambiguous; rather, it reinforces the clear and fundamental purpose of General Indemnity Agreements, which is to allow

surety to effectively and efficiently resolve claims and seek reimbursement without costly and unnecessary litigation. Edward G. Gallagher, *The Law of Suretyship* 496 (2000).

It has been suggested by at least one court that imposing any stricter duty on sureties would create reluctance on their part to satisfy valid claims under their bonds, *See e.g., Associated Indem. Corp. v. CAT Contracting, Inc.*, 964 S.W.2d 276, 282, (Tex. 1998). Further, as one court explained:

Sureties enjoy such discretion to settle claims because of the important function they serve in the construction industry, and because the economic incentives motivating them are a sufficient safeguard against payment of invalid claims.

Gen. Accident Ins. Co. of Am. v. Meritt-Meridian Constr. Co., at 516.

The evidence at trial conclusively demonstrates that the Indemnity Agreement was unambiguous and that Developer's right to indemnity was triggered based on Aarohns Construction's contingent liability. In fact, to characterize Aarohn Construction's liability as contingent is an understatement. Further, the jury found that Developer's interpretation of the Indemnity Agreement entitled Developers to indemnity and that the contract was unambiguous. The court properly denied Aarohn Construction's motion to dismiss before and after the verdict. In reviewing the trial court's decision this court must interpret the evidence

most strongly against the moving party and in the light most favorable to the opponent. Accordingly, the court's denial of Aarohn Construction's motion to dismiss should be affirmed.

c) Developers is Entitled to Indemnification When it Reasonably Believed a Claim Should Have Been Paid

Courts have consistently held that sureties are entitled to indemnification when they paid claims on a reasonable belief that the claims should be paid. *U.S. ex rel. Trs. of Elec. Workers Local Pension Fund v. D Bar D Enters., Inc.*, 772 F. Supp 1167 (D.Nev 1991). Among the factors considered by courts in evaluating a surety's reasonable belief are whether the principal (Aarohn Construction) has cooperated with the surety and provided information and documentation supporting defenses to the claim. *U.S. Fid. & Guar. Co. v. Feibus*, at 586.

Aarohn Construction contends that Developer's right to indemnity is precluded because Developers paid the County on a doubtful claim. *Appellant's Brief* 30. Incredibly, in support of this contention Aarohn cites the *Restatement (Third) of Suretyship and Guaranty* (1996), which undoubtedly supports Developer's right to indemnity. Section 24(1) of the *Restatement* states that a principal (Aarohn Construction) is precluded from asserting that a right to indemnity did not arise if the principal

obligor (Aarohn Construction) does not disclose to the secondary obligor (Developers) its defenses. The *Restatement* Provides:

§ 24 When the Duty to Reimburse Does Not Arise:

(1) Notwithstanding § 22, the principal obligor has no duty to reimburse the secondary obligor to the extent that:

(e) at the time of performance or settlement of the secondary obligation, the secondary obligor had notice of a defense of the principal obligor to the underlying obligation that was available to the secondary obligor as a defense to the secondary obligation (§ 34), unless it was a reasonable business decision for the secondary obligor to perform or settle the secondary obligation in light of factors, amounting to business compulsion, of which the principal obligor had notice at the time it incurred the underlying obligation; or

(2) For the purposes of subsection (1)(e), a secondary obligor has notice of a defense of the principal obligor to the underlying obligation available to the secondary obligor as a defense to the secondary obligation if that defense would be revealed to the secondary obligor by making such inquiry of the principal obligor as is reasonable under the circumstances to ascertain whether the principal obligor claims any defenses.

Comment on Subsection (2): If a notice is given or inquiry made, and the principal obligor does not disclose within a reasonable time a defense available to it, subsection (2) does not deem the secondary obligor to have notice of the defense.

In this regard, the testimony at trial shows that Developer's made a reasonable inquiry into whether Aarohn Construction had any defenses to

the County's claim and that Aarohn Construction failed to notify Developers of any defenses available to it, which, under the *Restatement*, affirmatively foreclosed Aarohn Construction's ability to assert that the duty to reimburse did not arise. According to the testimony of Mr. White, Developers made several inquiries into the defenses available to Aarohn Construction; however, John Bankston, for reasons unknown to Developers, failed to cooperate in the investigation and never disclosed Aarohn Construction's defenses:

Q. You then requested information from John Bankston, did you not?

A. Yes. Oh, yeah.

Q. Now did that information ever come?

A. Not in any substantive form, no.

Q. Did he ever provide documentation supporting his defenses?

A. No, not to me.

RP 490-491.

The evidence was uncontroverted that Developer's conducted an investigation into the defenses that Aarohn Construction may have had. RP 608-610. The evidence shows that Aarohn Construction deliberately thwarted the investigation by failing to provide Developers with

documentation supporting its defenses. RP 490-491. Ultimately, Aarohn's lack of cooperation played a significant role in Developers reasonable belief that the claim should be paid:

Q. Did that factor into your decision? (Referring to lack of documentation supporting Aarohn Construction's defenses).

A. Yes, absolutely. When I was figuring out what I was going to do, you know, on this thing and whether we were going to pay or not, the fact that he didn't support what he said was certainly a factor.

RP 609 (Mr. White testimony).

Aarohn Construction's contention that Developers paid a doubtful claim based entirely on expediency is erroneous on all accounts. The evidence at trial unequivocally establishes that Developers paid on the reasonable belief that Pierce County was entitled to payment after Aarohn Construction was unable to provide any documentary evidence supporting its claim that it was wrongfully terminated. Accordingly, this court should affirm the jury's verdict that Developers properly paid the County and is entitled to indemnification.

d) Indemnity Agreements are Valid and Enforceable Contracts

Indemnity Agreements are valid and enforceable contracts. *See e.g., Cont'l Cas. Co. v. Seattle*, 66 Wn.2d 831, 405 P.2d 581 (1966); *New Amsterdam Cas. v. Hamilton*, 123 Wn. 147, 212 P. 147 (1923). As noted,

it is standard for a surety in today's marketplace to demand that its principal (Aarohn Construction) enter into an express written Indemnity Agreement prior to the issuance of a surety bond. Lawrence R. Moelmann & John T. Harris, *The Law of Performance Bonds* 95 (1999). The right to compel the indemnitors (Aarohn Construction) to reimburse the surety under the terms of an Indemnity Agreement continues to be reaffirmed on a regular basis. *Cont'l Cas. Co. v. Guterman*, 708 F.Supp. 953 (N.D.Ill. 1989). Accordingly, Aarohn Construction should be held to the terms of the Indemnity Agreement.

Aarohn Construction asserts that the Indemnity Agreement knowingly and willingly signed by Richard Bankston is unconscionable because it is both substantively and procedurally unconscionable. With regard to substantive unconscionability, Aarohn Construction argues that the Indemnity Agreement forces Aarohn Construction to reimburse Developers regardless of how arbitrary or unfounded the termination was. *Appellant's Brief* 35. This is plainly false. Mr. White testified that Developer's carefully considered whether termination was warranted by reviewing evidence in support of both parties' position:

Q. And did you give any – what did you do as a result of his concerns? What did you request, if anything? (Referring to John Bankston).

A. I believe I asked him to provide me with as much backup information as he could to help support his position. And if his position was strong enough, I would certainly want to take that into account before I did anything further, at least try to.

RP 469-470. As demonstrated above, Developers did not decide to pay arbitrarily. Developers took reasonable steps to ensure that each party to the contract was heard before deciding to pay the claim. Further, Aarohn Construction was afforded ample opportunity to present its defenses to Developers, but elected not to. RP 469-470. Accordingly, the Indemnity Agreement is not substantively unconscionable.

Aarohn Construction also asserts that the contract is procedurally unconscionable because it lacked any meaningful choice in entering into the Agreement. This is confounding for several reasons. First, Richard Bankston testified that he voluntarily entered into the Agreement:

Q. And you signed it voluntarily, did you not?

A. Yes.

Q. Did anyone – no one from Developers forced you to sign that document?

A. No.

RP 635. Second, if Aarohn Construction did not like the terms of the Indemnity Agreement, they had every right and opportunity to procure a surety bond elsewhere. There was no coercion or duress of any sort to

sign the Agreement. *Id.* Finally, if Aarohn Construction lacked any meaningful choice in entering into this Agreement, it is because RCW 18.27.040 and RCW 39.08.010 mandate that all licensed contractors obtain a surety bond when performing work for a county. Thus, the Washington State legislature provided Aarohn Construction with a choice – comply with the law or operate its business illegally. Surely, a contract is not deemed procedurally unconscionable because the law requires it.

The trial court properly enforced the terms of the Indemnity Agreement as they are a necessary component of every surety bond between licensed contractors and surety companies. Absent Indemnity Agreements, the business of surety underwriting would be financially unsustainable. Accordingly, the Indemnity Agreement should be enforced as written.

e) The Trial Court Properly Denied Aarohn Construction's Motion to Dismiss for Lack of Subject Matter Jurisdiction

At trial, Aarohn Construction based its motion to dismiss on a lack of subject matter jurisdiction. Aarohn Construction bases this assertion on the erroneous characterization of this matter as an action for injury to real property, despite stating on numerous occasions throughout its Appellate Brief that this action is a suit for indemnity arising from Aarohn

Construction's breach of contract. *Appellant's Brief* 5, 10; CP 3-6. RCW

4.12.010 provides:

Actions for the following causes shall be commenced in the county in which the subject of the action, or some part thereof is situated:

(1) For the recovery of, for the possession of, for the partition of, for the foreclosure of a mortgage on, or for the determination of all questions affecting the title, or for any injuries to real property.

Although the statutes do not employ the terms "local" and "transitory," the actions described in RCW 4.12.010, which must be brought in the county where the property is located, are "local," while "transitory" actions are those described in RCW 4.12.025, which may be brought where the defendant resides. *Wash. State Bank v. Medalia Healthcare L.L.C.*, 96 Wn. App. 547, 557, 984 P.2d 1041 (1999).

Washington courts unanimously hold that actions for monetary recovery (indemnity) and breach of contract are "transitory," not "local," and may be brought in the county of the defendant's residence under RCW 4.12.025. *Wash. State Bank v. Medalia Healthcare L.L.C.*, 96 Wn. App. at 557. Washington courts support the view that transitory actions for monetary recovery are not subject to the requirements of RCW 4.12.010 for local actions, specifically where the connection to real property is merely incidental. *Id.*

Aarohn Construction advances the proposition that this is a case arising out of damage to real property. Aarohn Construction is wrong. Although Pierce County's claim on the proceeds of the bond arises out of damage to real property, the litigation itself is based entirely in contract. Developers brought suit to recover money under the terms of an Indemnity Agreement. The subject matter of this litigation is purely contractual. In fact, Developers, having no interest in the real property that was damaged in this matter, lacks standing to bring an action under RCW 4.12.010 for damage to the Pierce County Annex building.

Therefore, the trial court properly denied Aarohn Construction's motion to dismiss for lack of subject matter jurisdiction because where the plaintiff seeks monetary recovery under the terms of an Indemnity Agreement the action is deemed transitory in nature and is therefore not subject to the requirement of RCW 4.12.010. Accordingly, the trial court's denial of Aarohn Construction's motion to dismiss should be affirmed.

C. DEVELOPERS WAS ENTITLED TO PREJUDGMENT INTEREST FOR LIQUIDATED DAMAGES

A trial court's award of prejudgment interest is reviewed for abuse of discretion. *Hornback v. Wentworth*, 132 Wn. App 504, 513, 132 P.3d 778 (2006). A trial court abuses its discretion when its decision is

manifestly unreasonable or based on untenable grounds. *State v. Osman*, 147 Wn. App. 867, 879, 197 P.3d 1198 (2008). The rule in Washington is that interest prior to judgment is allowable (1) when an amount claimed is “liquidated” or (2) when the amount is readily determinable. *Prier v. Refrigeration Eng’g Co.*, 74 Wn.2d 25, 33, 442 P.2d 621 (1968). A liquidated claim is one where the evidence furnishes data which, if believed, makes it possible to compute the amount with exactness, without reliance on opinion or discretion. *Id.*

Here, the money Developers sought to recover from Aarohn Construction was liquidated and readily calculable because it was the exact amount paid by Developers to the County to settle the claim. The Indemnity Agreement supports the view that the amount was readily determinable because it requires Aarohn Construction to reimburse surety for “all payments made.” At trial, Mr. White testified as to the fixed amount paid by Developers:

Q. Which was what? (Referring to amount paid to Pierce County).

A. It was \$64,259.79.

RP 536.

Nevertheless, Aarohn Construction argues that the amount paid was unliquidated because there was a dispute over whether Developers should have paid the County at all. However, Washington courts

uniformly hold that existence of a dispute over the claim does not change the character of the claim from liquidated to unliquidated. *Prier v. Refrigeration Eng'g Co.*, 74 Wn.2d at 33. Washington courts are in agreement that difference of opinion as to whether someone legally ought to pay at all does not change the character of the claim. *Id.*

In this suit for indemnity, there was never any dispute as to the amount paid by Developers or the amount Developers sought to recover under the Indemnity Agreement because that amount was fixed as to “all payments made.” CP 403. At no stage in the litigation did Aarohn Construction dispute the amount Developers paid to the County. If anything, all parties were in agreement that Developers disbursed \$64,259.79 to the County. Although Aarohn Construction argues that it may have been wrongfully terminated or that it should have been afforded more time to complete the project, there was never a disagreement over the fact that Developers wrote a check for \$64,259.79 to Pierce County. Accordingly, the trial court did not abuse its discretion in awarding prejudgment interest to Developers.

D. DEVELOPERS REQUESTS THAT THIS COURT AWARD ATTORNEY’S FEES AND COSTS ON APPEAL

Under RAP 14.2, this Court may award costs to the prevailing party on appeal. Developers respectfully requests an award of its costs

incurred on this Appeal. Furthermore, pursuant to RAP 18.1, this Court may award reasonable attorney's fees or expenses on review. Developers is legally entitled to attorney's fees pursuant to the terms of the Indemnity Agreement which require Aarohn Construction to reimburse Developers for attorney's fees and expenses incurred by reason of such suretyship. Accordingly, Developers respectfully requests an award of its attorney's fees and expenses incurred on this Appeal.

E. CONCLUSION

In reviewing the issues on appeal, this Court must interpret the evidence most strongly against Aarohn Construction and in the light most favorable to Developers. In addition, if any justifiable evidence exists on which reasonable minds might reach conclusions consistent with the verdict, the trial court's ruling must be affirmed.

The trial court properly denied Aarohn Construction's Motion for Directed Verdict and Motion to Dismiss after Developer's case. Developers presented substantial evidence at trial regarding its express right to seek indemnity where the Indemnity Agreement specifically allowed Developers to seek reimbursement when it paid based on Aarohn Construction's liability or possible liability to the County. As long as possible liability was present, the contract granted Developers the exclusive right to decide whether to pay for a variety of reasons including

“liability, expediency or otherwise.” Aarohn Construction is contractually bound to reimburse Developers because it knowingly signed an unambiguous Indemnity Agreement. Further, the trial court had subject matter jurisdiction over this contractual suit for reimbursement and prejudgment interest was warranted because all parties agree that Developers paid \$64,259.79 to the County.

RESPECTFULLY SUBMITTED this 20 day of January, 2010.

YUSEN & FRIEDRICH

By 
Alexander Friedrich, WSBA # 6144

THIS IS TO CERTIFY that a copy of the Brief of Respondent was sent for filing on January 20, 2010 with the Court of Appeals, Division I; and was mailed January 20, 2009 to the following individuals:

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I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

RESPECTFULLY SUBMITTED the 20th day of January, 2010.

YUSEN & FRIEDRICH



Alexander Friedrich,
WSBA #6144
Attorney for Respondent