Case No. 70504

IN THE SUPREME COURT OF NEVADA

JAMES NALDER, Guardian Ad Litem
on behalf of CHEYANNE NALDER;
GARY LEWIS, Individually,

Appellants,

v.

UNITED AUTOMOBILE INSURANCE
COMPANY,

Respondent.

BRIEF OF AMICUS CURIAE OF UNITED POLICYHOLDERS IN SUPPORT OF APPELLANTS

Ninth Circuit Case No. 13-17441
U.S.D.C. No. 2:09-cv-01348-RCJ-GWF

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NRAP 26.1 DISCLOSURE

The undersigned counsel of record hereby certifies that the following are persons and entities as described in NRAP 26.1(a), and must be disclosed. These representations are made in order that the judges of this Court may evaluate possible disqualification or recusal:

United Policyholders ("UP") is a non-profit 501(c) (3) organization founded in 1991 that is an information resource and a voice for insurance consumers in Nevada and throughout the United States. The organization assists and informs disaster victims and individual and commercial policyholders with regard to every type of insurance product. Grants from community foundations and government, donations from individuals and businesses and volunteer attorneys, insurance professionals, and disaster survivors support the organization's work. UP does not sell insurance or accept funding from insurance companies.

UP did not appear in the underlying action and has submitted to this Court a motion for leave to file this brief. It is represented in the pending appeal, as amicus curiae, by David T. Pursiano, Esq. of the firm Pursiano Barry Bruce Lavelle, LLP and Mark A. Boyle, Esq., of the firm of Boyle & Leonard, P.A., who is pending admission upon the Court's approval of the Amended Motion to Associate.

DATED January 9, 2017.

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STATEMENT IDENTIFYING AMICUS, ITS INTEREST IN CASE, AND SOURCE OF AUTHORITY OF AMICUS CURIAE

UP is a non-profit 501(c)(3) organization founded in 1991 that is an information resource and a voice for insurance consumers in Nevada and throughout the United States. The organization assists and informs disaster victims and individual and commercial policyholders with regard to every type of insurance product. Grants from community foundations and government, donations from individuals and businesses and volunteer attorneys, insurance professionals, and disaster survivors support the organization's work. UP does not sell insurance or accept funding from insurance companies.

UP's work is divided into three program areas: Roadmap to Recovery™ (disaster recovery and claim help), Roadmap to Preparedness (disaster preparedness through insurance education), and Advocacy and Action (advancing pro-consumer laws and public policy). UP hosts a library of informational publications and videos related to personal and commercial insurance products, coverage and the claims process at www.uphelp.org.

A diverse range of individual and commercial policyholders throughout the United States regularly communicate their insurance concerns to UP which allows UP to submit *amicus curiae* briefs to assist state and federal courts in deciding cases involving important insurance principles. UP has filed more than 400 cases throughout the United States since the organization's founding in 1991. UP's amicus

curiae brief was cited in the United States Supreme Court's opinion in *Humana, Inc. v. Forsyth*, 525 U.S. 299 (1999). Arguments from UP's amicus curiae brief were cited with approval by the California Supreme Court in *Vandenburg v. Superior Court*, 982 P.2d 229 (Cal. 1999) and many other courts.

UP has been assisting policyholders, regulators and courts since the organization was founded in 1991 after the Oakland-Berkeley Hills Firestorm and has assisted many victims of natural disasters and individual policyholders across the country. Accordingly, in this brief, UP seeks to fulfill the "classic role *of amicus curiae* by assisting in a case of general public interest, supplementing the efforts of counsel, and drawing the court's attention to law that escaped consideration." *Miller-Wohl Co. v. Comm'r of Labor & Indus*., 694 F.2d 203, 204 (9th Cir. 1982). UP's 25 years of experience advocating for the interests of insureds makes it well suited to aid this Court in this case.

SUMMARY OF THE ARGUMENT

United Policyholders seeks to assist the Court in answering the certified question issued by the Ninth Circuit Court of Appeals. UP respectfully request that this Court answer the certified question holding that an insurer is liable for all losses consequential to an insurer's breach.

Under contract principles, a party that breaches a duty owed under a contract is liable for losses consequential for that breach when there is a special circumstance present. Contracts of insurance present a special circumstance given the special relationship between the parties and nature of the contract. As such, a breach of that contractual duty should result in a rule that allows insureds to recover an excess judgment amount as consequential damages.

Moreover, other courts have concluded that an insurer is liable for consequential damages resulting from its refusal to defend its insured—i.e. its breach of contract. As such, there is no justification for making a special rule about consequential damages for insurers. Nevada's usual rule that any party that breaches a contract is liable for consequential damages should apply to insurers as well.

ARGUMENT

On June 1, 2016, the Ninth Circuit Court of Appeals asked this Court to answer the following question:

> Whether, under Nevada law, the liability of an insurer that has breached its duty to defend, but has not acted in bad faith, is capped at the policy limit plus any costs incurred, or is the insurer liable for all losses consequential to the insurer's breach?

Nalder v. United Auto. Ins. Co, 824 F.3d 854, 855 (9th Cir. 2016).

Given the importance of this issue nationwide, UP respectfully request that this Court answer the certified question holding that an insurer is liable for all losses consequential to an insurer's breach.

A. An Insurer Who Breaches Its Duty to Defend Should Be Liable for All Losses Consequential for that Breach Under Contract Principles.

In today's world, insurance is required on virtually any kind of property one owns. Given the mandatory nature of insurance, courts and legislators across the county have enacted rules, statutes and regulations in providing safeguard to consumers and policyholders. Absent explicit rules, courts rely upon basic contracting common law principles in the insurance context. Once such basic contract principle is the concept of consequential damages. The concept of consequential damages traces back to *Hadley v. Baxendale*, Ex. 341, 156 Eng. Rep. 145 (1854). Many will recall from their first year of law school that *Hadley* set forth that consequential damages will only be available as compensation for a breach of contract if they were within the reasonable contemplation of both parties at the time

they entered into the contract. The *Hadley* court described general or direct damages which would arise in the usual course of events without regard to any special circumstances of the non-breaching party. In contrast, consequential damages were defined as secondary consequences of nonperformance resulting from the special circumstances of the non-breaching party. Importantly, consequential damages, which represent additional risks due to unusual circumstances of the non-breaching party, are not awarded unless the non-breaching party can establish that the parties were aware of the special circumstances at the time they entered into the contract and therefore intended to allocate to the breaching party the extra risks resulting from the non-breaching party's unusual position.

Once such special circumstance is the contract of insurance. This Court, and virtually all courts across the nation, recognize that an insurer hold a special relationship with an insured which is described as a fiduciary relationship. *Powers v. United Servs. Auto. Ass'n*, 962 P.2d 596, 603 (Nev. 1998). Under liability policies, insurance companies took on the obligation of defending the insured, which, in turn, made insureds dependent on the acts of the insurers; insurers had the power to settle and foreclose an insured's exposure or to refuse to settle and leave the insured exposed to liability in excess of policy limits. *Allstate Indem. Co. v. Ruiz*, 899 So. 2d 1121, 1125 (Fla. 2005) citing Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions: Refining the Standard of Culpability and*

Reformulating the Remedies by Statute, 26 U. Mich. J.L. Ref. 1 (Fall 1992). This placed insurers in a fiduciary relationship with their insured similar to that which exists between an attorney and client. *Id.* As a result, courts began to recognize that insurers "owed a duty to their insured to refrain from acting solely on the basis of their own interest in settlement." *Id.*

Consequently, control of the defense also means insurers are also able to control the form of their policies (i.e. policy language). Because of this control, insurers are able to contract around provisions and shift risk, subject to some limitations. Because of this one sided control, contracts of insurance are also contracts of adhesion. This Court has succinctly summed up this as the following:

> … an insurance policy is not an ordinary contract. It is a complex instrument, unilaterally prepared, and seldom understood by the assured. . . . The parties are not similarly situated. The company and its representatives are expert in the field; the applicant is not. *A court should not be unaware of this reality and subordinate its significance to strict legal doctrine*.

Prudential Ins. Co. of Am. v. Lamme, 425 P.2d 346, 347 (Nev. 1967) (emphasis added); *see also Allen v. Metro. Life Ins. Co.*, 208 A.2d 638, 644 (N.J. 1965) ("When members of the public purchase policies of insurance they are entitled to the broad measure of protection necessary to fulfill their reasonable expectations. They should not be subjected to technical encumbrances or to hidden pitfalls and their policies should be construed liberally in their favor to the end that coverage is afforded to the

full extent that any fair interpretation will allow.") (Quoting *Kievit v. Loyal Protect Life Ins. Co.*, 170 A.2d 22 (N.J. 1961)

The insurer is in control of the form of the policy and its language. Thus, by virtue of the common law, if an insurance policy fails to include an express term, coverage is read in favor of the policyholders. *Vitale v. Jefferson Ins. Co.*, 5 P.3d 1054, 1057 (Nev. 2000). If an insurer is unhappy with these interpretative rules, it has many options in the marketplace to allocate the risk in the manner insurers prefer. Many courts have applied these rules with particular vigor when language which would have accomplished insurer's purported purpose is available in the marketplace. *See Auto-Owners Ins. Co. v. Anderson*, 756 So. 2d 29, 36 (Fla. 2000).

In fact, in most contracts involving construction, it is not uncommon for a contract to include a provision which waive consequential damages. In fact, most type of these contracts explicitly waive consequential damages by listing the specific risk involved. For example, in *Costa v. Brait Builders Corp.*, 972 N.E.2d 449, 459 (Mass. 2012), the court examined the following waiver of consequential damages provision: "The Contractor waives Claims against the Owner for consequential damages arising out of or relating to this Contract. This includes: (1) damages incurred by the Contractor for ... losses of financing, business and reputation, and for loss of profit except anticipated profit arising directly from the Work." Often, provisions in contracts that waive consequential damages are permissible. 972 N.E.

2d at 459. As such, an insurer has the ability to contract for this specific provision. Its absence should be read in favor of policyholders.

An insurer's contractual duty to defend provides complete control to the insurer. As such, a breach of that contractual duty should result in a rule that allows insureds to recover an excess judgment amount as consequential damages.

B. Other Jurisdictions Recognize that Consequential Damages are Recoverable for an Insurer Who Breaches Its Duty to Defend.

Other jurisdictions recognize that consequential damages are recoverable for an insurer who breaches its duty to defend. In *Thomas v. Western World Ins. Co.*, 343 So. 2d 1298 (Fla. 1977), Florida's Second District Court of Appeal considered the exact same issue the Ninth Circuit certified to this Court: "whether appellants who are insureds are entitled to seek recovery against their liability carrier for an amount in excess of the policy limits where their insurance carrier has wrongfully refused to defend a negligence action against them." *Id.* at 1300. There, the plaintiff sued the insureds for negligence after the insureds' agent allegedly threw acid on him. *Id.* The insureds tendered the claim to their insurer. *Id.* The insurer, however, denied the claim based on an assault and battery exclusion and that the allegations did not fall within the policy's definition of occurrence. *Id.* The plaintiff eventually obtained a final judgment against the insureds in the sum of $18,459.73. *Id.*

The insureds then brought suit against their insurer and sought to recover the full amount of the plaintiff's judgment based on the insurer's wrongful denial of a

defense. *Id.* The insurer eventually conceded it wrongfully refused to defend the insureds. *Id.* at 1301. Then, back in the underlying action brought by the plaintiff, the insurer paid the policy limits to the plaintiff pursuant to a garnishment order. *Id.* After it paid the garnishment order, the insurer moved for summary judgment in the lawsuit brought by the insureds. *Id.* The trial court granted the motion for summary judgment and found that absent bad-faith, the insurer could not be liable for the entire judgment. *Id.*

The appellate court disagreed and reversed the trial court. *Id.* In doing so, the court analyzed two issues: (1) the necessity of an offer to settle and (2) the necessity of the existence of bad faith. *Id.* at 1301-04. In addressing the first issue, the court differentiated between an insurer's liability when it performs its contractual obligations and an insurer's liability when the insurer breaches its contract. *Id.* at 1301 (citing *Communale v. Traders & Gen. Ins. Co.*, 328 P. 2d 198 (Cal. 1958)). The court, in agreement with *Communale*, reasoned that an insurer's performance of its contractual obligations restricts its liability to the policy limits. *Id.* at 1302. The court continued and stated the limits of liability do not restrict an insurer's liability when it breaches the contract. *Id.* Specifically, the court reasoned that an insurer is liable for an amount in excess of the policy limits where: (1) the insurer's actions caused the insured to suffer a default or final judgment without benefit of an attorney,

or (2) the insured proves the final judgment would have been lower had the suit been properly defended. *Id.*

The difference between an insurer defending its insured and an insurer not defending its insured formed the underlying rationale of the court's bad-faith analysis. *Id.* at 1303-04. In analyzing the bad-faith issue, the court stated the concept of bad-faith comes about where the insurer defends its insured and measures the judgment exercised by the insurer in providing that defense. *Id.* However, where an insurer refuses to defend its insured "there is no threshold question of 'good faith' vs. 'bad faith'…[because] the [insurer] exercised no faith at all." *Id.* at 1304.

Accordingly, the court, in recognition of the basic legal premise that an insurance policy is simply a contract, held that an insurer is liable for all foreseeable damages the insurer's breach caused to be assessed against its insureds:

> An insurer which denies coverage does so at its own risk. This has been held to be true even where such denial is on a mistaken but honest belief that coverage did not exist. It seems only fair that an insurer whose contracts are by their very nature 'adhesive' should be held to at least the same standard of damages applicable to other contracting parties. One purchasing coverage should be able to rely upon this. An insurer at least impliedly represents it will be responsible for damages if it fails to provide the contracted for coverage and defense.

Id. (internal citations omitted).

Florida is not alone in employing this rule. Indeed, other courts have concluded that an insurer is liable for consequential damages resulting from its

refusal to defend its insured—i.e. its breach of contract. For example, in *Space Conditioning, Inc. v. Ins. Co. of N.A.*, 294 F. Supp. 1290 (E.D. Mich. 1968), the court held "[a]n insurance company which refuses to defend believing there to be no policy coverage, does so at its peril, *even if in good faith*, and must bear the legal consequences of its breach of contract." *Id.* at 1295 (citations omitted) (emphasis added). Accordingly, the court, similar to the *Thomas* Court, held the insurer is liable for all foreseeable damages caused by the insurer's breach of contract. *Id.* The court's reasoning makes clear that the existence of bad-faith by the insurer in denying the insured a defense is irrelevant because, similar to the *Thomas* Court's reasoning, bad-faith only applies where the insurer actually defends its insured. *Id.*

Moreover, the U.S. District Court for the District of Nevada addressed this issue in the case *Andrew v. Century Sur. Co.*, No. 2:12-cv-00978, 2015 WL 5691254 (D. Nev. Sept. 28, 2015) and examine other jurisdictions for guidance[1]. Once such

[1] The *Andrew* Court also examined **Georgia**'s *Khan v. Landmark Am. Ins. Co*., 757 S.E. 2d 151, 156 (Ga. 2014) (stating that "the possible damages at issue are not merely those within the indemnity coverage of the policy, but are those further damages that may flow from breach of the contract to defend" as consequential damages); **Delaware**'s *Delatorre v. Safeway Ins. Co.*, 989 N.E. 2d 268 (Del. App. Ct. 2013) (holding insurer's failure to defend caused default and insurer therefore was liable for judgment in excess of policy limits as consequential damages); **Illinois**' *Reis v. Aetna Cas. & Sur. Co. of Ill.*, 387 N.E .2d 700, (Ill. App. Ct. 1978) (stating that "damages for a breach of the duty to defend are not inexorably imprisoned within the policy limits, but are measured by the consequences proximately caused by the breach"); **Florida**'s *Thomas v. W. World Ins. Co.*, 343 So. 2d 1298, 1302 (Fla. Ct. App. 1977) (discussed above); **Michigan**'s *Stockdale v. Jamison*, 330 N.W. 2d 389 (Mich. 1982)(holding that when an insurer "breached its

case is *Maxwell v. Hartford Union High Sch. Dist.*, 814 N.W. 2d 484 (Wis. 2012). In *Maxwell*, the Supreme Court of Wisconsin held that when an insurer breaches a duty to defend its insured, the insurer is on the hook for all damages that result from that breach of its duty. *Id.* at 496. The *Maxwell* court relied upon its earlier case *Newhouse v. Citizens Security Mutual Insurance Co.*, 501 N.W. 2d 1 (Wis. 1993), which stated as follows:

> a party aggrieved by an insurer's breach of its duty to defend is entitled to recover all damages naturally flowing from the breach.... Damages which naturally flow from an insurer's breach of its duty to defend include: (1) the amount of the judgment or settlement against the insured plus interest; (2) costs and attorney fees incurred by the insured in defending the suit; and (3) any additional costs that the insured can show naturally resulted from the breach.

Id. at 830, 838, 501 N.W. 2d 1.

As the *Andrew* court stated: there is no justification for making a special rule about consequential damages for insurers. 134 F. Supp. 3d 1249, 1257. Nevada's usual rule is that any party that breaches a contract is liable for consequential damages. *Id.* Insurers should be held to the same standard.

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duty to defend, it became liable for any damages arising 'naturally from the breach. . . .").

CONCLUSION

For the foregoing reasons, Amicus Curiae, United Policyholders respectfully requests that this Court adopt a rule of law that an insured may recover all consequential damages caused by an insurer's contractual breach of its duty to defend, including judgments in excess of policy limits.

DATED December 20, 2016.

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CERTIFICATE OF COMPLIANCE

1. I hereby certify that this proposed brief complies with the formatting requirements of NRAP 32(a)(4), the typeface requirements of NRAP 32(a)(5) and the type style requirements of NRAP 32(a)(6) because this brief was prepared in a proportionally-spaced typeface (14-point Times New Roman font) using Microsoft Word.

2. I further certify that this brief complies with the page-or type-volume limitations of NRAP 32(a)(7) because excluding the parts of the brief exempted by NRAP 32(a)(7)(C), it is proportionally spaced, has a typeface of 14 points or more and contains 3,262 words.

3. I hereby certify that I have read this amicus curiae brief, and to the best of my knowledge, information, and belief, it is not frivolous or interposed for any improper purpose. I further certify that this brief complies with all applicable Nevada Rules of Appellate Procedure, in particular NRAP 28(e)(1), which requires every assertion in the brief regarding matters in the record to be supported by a reference to the page and volume number, if any, of the transcript or appendix where the matter relied on is to be found. I understand that I may be subject to sanctions in the event that the accompanying brief is not in conformity with the requirements of the Nevada Rules of Appellate Procedure.

CERTIFICATE OF SERVICE

Pursuant to NRAP 31, I hereby certify that I am an employee of Pursiano Barry Bruce Lavelle, LLP, and on this date, I electronically filed and served a true and correct copy of the foregoing BRIEF OF AMICUS CURIAE OF UNITED POLICYHOLDERS IN SUPPORT OF APPELLANTS via eFlex Program, which will send a notice of electronic filing to the following:

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