Case No. 73756

In the Supreme Court of Nevada

CENTURY SURETY COMPANY,

Appellant,

vs.

DANA ANDREW, as Legal Guardian on Behalf of RYAN T. PRETNER; and RYAN T. PRETNER,

Respondents.

CERTIFIED QUESTION

from the United States District Court for the District of Nevada
The Honorable ANDREW P. GORDON, District Judge
District Court Case No. 2:12-CV-00978

AMICUS CURIAE BRIEF OF THE FEDERATION OF DEFENSE & CORPORATE COUNSEL

IN SUPPORT OF APPELLANT

DANIEL F. POLSENBERG (SBN 2376)
J CHRISTOPHER JORGENSEN (SBN 5382)
LEWIS ROCA ROTHGERBER CHRISTIE LLP
3993 Howard Hughes Parkway, Suite 600
Las Vegas, Nevada 89169
(702) 949-8200

Attorneys for the Federation of Defense & Corporate Counsel

NRAP 26.1 DISCLOSURE

The undersigned counsel of record 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.

The Federation of Defense & Corporate Counsel (FDCC) is an Illinois not-for-profit corporation. The FDCC is represented by Daniel F. Polsenberg and J Christopher Jorgensen of Lewis Roca Rothgerber Christie LLP.

Dated this 18th day of October, 2017.

LEWIS ROCA ROTHGERBER CHRISTIE LLP

By: ______________________

DANIEL F. POLSENBERG (SBN 2376)
J CHRISTOPHER JORGENSEN (SBN 5382)
3993 Howard Hughes Parkway, Suite 600
Las Vegas, Nevada 89169
(702) 949-8200

Attorneys for the Federation of Defense & Corporate Counsel

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STATEMENT OF INTEREST

The Federation of Defense & Corporate Counsel (FDCC) formed in 1936 and has international membership of 1,400 defense and corporate counsel. FDCC members work in private practice, as in-house counsel, and as insurance-claims executives. Membership is limited to attorneys and insurance professionals nominated by their peers for having achieved professional distinction and demonstrated leadership in their respective fields. The FDCC is committed to promoting knowledge and professionalism in its ranks and has organized itself to that end.

The FDCC constantly strives to protect the American system of justice. Its members have established a strong legacy of representing the interests of civil defendants. Through its amicus curiae efforts, the FDCC seeks to assist courts in addressing issues of importance to its membership, including the interests of insurers—and ultimately of the commercial marketplace—in fair, predictable, contract-based remedies.

All time and cost for the preparation of this brief have been borne solely by the FDCC, with no contribution by any party.

SUMMARY OF THE ARGUMENT

The FDCC offers the Court a summary of other states' law on the certified 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 by the insured in mounting a defense, or is the insurer liable for all losses consequential to the insurer's breach?

Research reveals 25 states that have not yet decided this question.

Among the states with precedential opinions on point, 13 have reached the conclusion that Appellant Century Surety Company asks this Court to reach, **capping damages at the policy limit** (sometimes adding defense costs incurred by the insured)—and another 4 states have case law closely supporting that view. In comparison, we have identified only 8 states that appear to allow an insured in this situation to recover an excess judgment entered against it. Two of those courts say so only in dicta, and most require clear proof that the insurer's breach caused the excess judgment.

ARGUMENT

A MAJORITY OF STATES WITH LAW ON THIS QUESTION SUPPORT APPELLANT CENTURY SURETY

Half of all states have yet to address the question before this Court. Most of the rest favor the rule urged by Century Surety (which was also the district court's initial view): the liability of an insurer for breaching its duty to defend, absent any bad faith, is capped at the policy limit plus any costs incurred by the insured in mounting a defense. For ease of reference we will sometimes call this "the policy-limits rule."[1]

Even among the states allowing excess liability (two of which say so only in dicta), case law demands clear evidence that breach of the duty to defend caused the insured to suffer that result.

I.

<u>SEVENTEEN STATES WOULD REVERSE THE JUDGMENT HERE</u>

A. Ten State Courts Have Direct <u>Precedent for the Policy-Limits Rule</u>

Following are the most recent and authoritative cases on point with the certified question from ten state courts.

Arizona

The court in *State Farm Mutual Auto. Ins. Co. v. Paynter*, 593 P.2d 948, 954-955 (Ariz. Ct. App. 1979), **reduced a judgment against the insurer to the policy limit**, holding that an insurer's liability for refusing to defend "should be confined to the limits of the policy.

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[1] As Century's brief explains, one basis for many courts' determination that an insurer acted in bad faith has been that the insurer unreasonably declined an opportunity to settle the insured's exposure for an amount within policy limits. That did not happen here, as set forth in the District Court's April 2014 order at page 15, footnote 9.

Appellee Paynter has not cited any cases to us in which the court has held an insurer liable for an amount in excess of the policy limits in the absence of proof that there was, in addition to the refusal to defend, a refusal to entertain an offer of settlement." *See also Desert Mountain Props. Ltd. P'ship v. Liberty Mut. Fire Ins. Co.*, 236 P.3d 421, 444 (Ariz. Ct. App. 2010) ("An insurer's wrongful failure to indemnify or defend its insured does not expose the insurance carrier to greater liability than that contractually provided in the policy.").

Connecticut

The state supreme court has hewed to the policy-limits rule both times it has addressed the issue. In *Schurgast v. Schumann*, 242 A.2d 695, 705 (Conn. 1968), the insurer "refuse[d] to defend and, in so doing, breached its contract with Schumann. It [was] therefore under a duty to pay the judgment obtained against Schumann by Schurgast up to the limit of liability fixed by its policy," and **the court ordered a declaratory judgment so limiting the insurer's liability**. *See also Black v. Goodwin, Loomis & Britton, Inc.*, 681 A.2d 293, 302 (Conn. 1996).

Kansas

The leading case of *George R. Winchell, Inc. v. Norris*, 633 P.2d 1174 (Kan. Ct. App. 1981), resembles this case. The insured Norris caused an accident that injured the driver of a tractor-trailer. When that driver sued Norris, his insurer declined in good faith to defend, and default was entered against Norris. *Id.* at 1175-76. As here, the case went up on appeal with no challenge to the insurer's good faith. *Id.* at 1176.

The *Winchell* court **affirmed the trial court's judgment capping the damages at the policy limit**, noting that the insurer did not reject a reasonable settlement offer. *Id.* at 1176-77 ("Absent a settlement offer, the plain refusal to defend has no causal connection with the amount of the judgment in excess of the policy limits."). Following what it deemed "the majority rule," *Winchell* held: "As a general rule, a finding of bad faith is required for a finding of liability of amounts in excess of the policy limits." *Id.* at 1178.

Maryland

Maryland's highest court has likewise **affirmed capping a judgment against the insurer at the policy limit**, rejecting tort liability for a contract breach. In *Mesmer v. Maryland Auto. Ins. Fund*, 725 A.2d 1053 (Md. 1999), that court held: "A liability insurer's mistaken refusal to provide any defense whatsoever, on the grounds that there is no valid insurance contract or that there is no coverage under an insurance contract, gives rise to a breach of contract action against the insurer." *Id.* at 1058. Accordingly, the Maryland high court rejected the same contention Respondents make here, "that the amount of the excess judgment in the underlying tort case is recoverable in this contract action." *Id.* "Instead, the circuit court correctly held that the damages for breach of contract are limited to the policy limits and the costs of defending the underlying tort action." *Id.*; *see also id.* at 1064 ("There is utterly no support in our cases for the plaintiffs' argument that the damages for a liability insurer's breach of the promise to defend include the amount of the excess judgment.")

Minnesota

The state supreme court held almost a century ago, and more recently reaffirmed, that "the refusal of [an] insurance company to conduct the defense of an action [for vehicular injury to a third party] does not expose it to greater liability to the insured for injuries to the persons complaining than the amount stated in the policy." *Mannheimer Bros. v. Kan. Cas. & Sur. Co.*, 184 N.W. 189 (Minn. 1921). Minnesota's "measure of liability for a breach of the contract in that respect" is: "(1) The amount stated as for injuries to third persons [within the policy limit, *id.*]; and (2) all necessary costs and expenses incurred by the insured in defending the action." *Id.*

The high court "reaffirm[ed]" *Mannheimer* in *Engeldinger v. State Auto. & Cas. Underwriters*, 236 N.W.2d 596, 602 (Minn. 1975). While noting that "[c]onceivably, there exist situations where the insurer must bear the entire financial settlement, even in excess of policy limits, when it fails to defend" (*id.*)—by which it meant only "an insurer's breach of the duty to consider a settlement in good faith, rather than suggesting a more general liability for excess Judgments"[2] — the *Engeldinger* court "**limit[ed] damages to the policy limits plus interest and costs** including the reasonable cost of legal services

[2] *Ortega-Maldonado v. Allstate Ins. Co.*, 519 F. Supp. 2d 981, 990 (D. Minn. 2007) ("*Engeldinger* stands for the legal principle that a Court, which applies Minnesota law, can only enforce a Judgment, which is in excess of an insurance policy, against an insured when the insurer failed to consider a settlement in good faith.").

employed to defend the action, as spelled out in *Mannheimer*." *Id.* (emphasis added).

Missouri

The Missouri Supreme Court just last year **reduced a judgment against the insurer to the policy limit**. *Allen v. Bryers*, 512 S.W.3d 17, 39 (Mo. 2016). Like Century, the insurer in *Allen* was held to have breached its duty to defend, but the trial court "did not find that Insurer acted in bad faith. Consequently, the [trial] court exceeded its authority in awarding Allen the full amount of the underlying tort judgment because Allen was only entitled to the $1 million policy limits . . . ." *Id.* at 39.

The court quoted with approval the measure of damages previously set forth by Missouri's intermediate court: "'[A]n insurance company is liable to the limits of its policy plus attorney fees, expenses and other damages where it refuses to defend an insured who is in fact covered.' 'This is true even though the company acts in good faith and has reasonable ground[s] to believe there is no coverage under the policy.'" *Allen*, 512 S.W.3d at 38-39 (quoting *Landie v. Century Indemnity Co.*, 390 S.W.2d 558, 562 (Mo. Ct. App. 1965)).

Pennsylvania

Absent "a refusal to settle or other mishandling of the claim," the Pennsylvania Supreme Court holds that "the amount of recovery for breach of the [defense] obligation is the cost of hiring substitute counsel and other costs of the defense, and not the judgment obtained against the insured." *Gedeon v. State Farm Mut. Auto. Ins. Co.*, 188 A.2d 320, 322 (Pa. 1963). Where, as in the case at bar, the insured incurred a default judgment with no defense costs, there are "no damages resulting from this breach." *Id.* at 323, 321 (affirming trial court's refusal to award excess judgment).

Tennessee

An older Tennessee decision remains authoritative, again **reducing a judgment against the insurer to the policy limit**. *Nat'l Serv. Fire Ins. Co. v. Williams*, 454 S.W.2d 362, 372 (Tenn. Ct. App. 1969). The court explained : "In the absence of a 'bad faith' refusal to compromise the claim against the insured or to accept a reasonable settlement, the damages and the consequent liability of the insurer for breach of the contractual duty to defend an insured ordinarily is limited to the amount of the policy plus reasonable costs incurred in providing a defense for the insured." *Id*. at 365.

Texas

In *United Services Auto. Ass'n v. Pennington*, 810 S.W.2d 777 (Tex. App. 1991), *writ denied* (Oct. 23, 1991), the court directly addressed the measure of damages for a breach of the duty to defend in the absence of any bad faith. *Id*. at 783. Relying on the Texas Supreme Court's decision in *Southwestern Bell Tel. Co. v. Delanney*, 809 S.W.2d 493, 494 (Tex. 1991), *Pennington* declared: "If the defendant's conduct would impose liability on him only because it breaches the parties' agreement, the claim is contractual." 810 S.W.2d. at 783. While recognizing that any breach of contract "may give rise to liability for all damages directly and foreseeably resulting from the breach" (internal quotation marks omitted), the court held that "damages in a contract claim for the wrongful failure to defend do not include damages in excess of the policy limits." *Id.* at 784 (citations omitted).

Instead, the Texas measure of damages follows the policy-limits rule:

> In the absence of a showing either that the claim could have been resolved for the policy limits

> [citation] or that the insurer breached its duty of good faith and fair dealing [citation], the insured's damages generally will be limited to the policy limits, expenses of the insured in defending the suit (including reasonable attorney fees and court costs), and reasonable and necessary attorney fees and costs incurred in the suit to enforce the judgment against the insurer. [Citation]

Pennington, 810 S.W.2d at 784. The court then **reduced judgment against the insurer to the policy limit**. *Id.*

Washington

The Washington Supreme Court has twice applied the policy-limits rule. In *Waite v. Aetna Cas. & Surety Co.*, as here, there was "no showing nor any claim of bad faith." 467 P.2d 847, 851 (Wash. 1970). Accordingly: "The rule is that where an insurer wrongfully refuses to defend, it will be required to pay the judgment or settlement **to the extent of its policy limits** and also to reimburse the insured for his costs reasonably incurred in defense of the action." *Id.* at 853 (emphasis added). Seventeen years later, the same court rejected an invitation to abandon the "majority rule" it had adopted in *Waite*, and **reduced a judgment against the insurer to the policy limit**. *Greer v. Nw Nat'l Ins. Co.*, 743 P.2d 1244, 1250-51 (Wash 1987).

B. Four More States Have Precedents Strongly <u>Suggesting They Would Adopt The Policy-Limits Rule</u>

The courts of four additional states have announced holdings that closely support the policy-limits rule at issue here.

New Jersey

In *Radio Taxi Service, Inc. v. Lincoln Mutual Ins. Co.*, 157 A.2d 319 (N.J. 1960), the <u>**New Jersey**</u> Supreme Court held that an insurer that rejects a settlement demand reasonably and in good faith is **not liable for the portion of a verdict exceeding the policy limits**.

> The ultimate question is not whether a verdict in excess of the policy limits should have been anticipated but whether the insurer lacked good faith in deciding not to meet the settlement demand. … [S]uch a mistake when resulting from a decision made with good faith regard for its own and the insured's interests does not confer a cause of action on the insured for the excess.

Id. at 326. Because New Jersey rejects excess liability even where an insurer declines to settle a claim within limits (absent any bad faith), it appears clear New Jersey would also reject excess liability where an insurer declines in good faith to defend a claim.

Oregon

The **<u>Oregon</u>** Court of Appeals, sitting *in banc*, has held that an insurer's breach of the duty to defend does not give rise to a duty to indemnify unless the underlying claim is covered. That court's rationale illuminates why ***it is improper to rely on the claimed "foreseeability" of an excess judgment at the time an insurer declines a defense***:

> Consequential damages are, by definition, those that the parties to a contract reasonably contemplate at the time of execution, not at some later date. [Citations] Thus, whether it is reasonable to include as consequential damages settlement costs in excess of the provisions of an insurance policy must be examined by reference to what was reasonably contemplated by the parties at the time of the execution of the policy. As in any contract, the intentions of the parties are expressed in the terms of the insurance policy itself, which contains express limitations on coverage. [Citations]

Nw. Pump & Equip. Co. v. Am. States Ins. Co., 925 P.2d 1241, 1244–45 (Or. Ct. App. 1996).

New York / Idaho

The highest courts of **<u>Idaho</u>** and **<u>New York</u>** have likewise held that breach of the duty to defend does not result in liability to pay a judgment against the insured, if the insurer can show its policy doesn't cover the judgment. *Deluna v. State Farm Fire and Cas. Co.*, 233 P.3d 12, 16 (Idaho 2008); *K2 Inv. Grp.,* LLC *v. Am. Guarantee & Liab. Ins. Co.*, 6 N.E.3d 1117 (N.Y. 2014). In light of New York's statute on the subject of insurer liability to the judgment creditor—**which *does* cap exposure at policy limits**—it is especially likely that New York would adopt the policy-limits approach to the certified question here.[3]

C. Federal Courts Predicting the Law of Three Additional States Adopt or Support the Policy-Limits Rule

Virginia

The **Virginia** court system confers no right to appeal civil cases, and there is no state appellate decision on the certified question. But federal district courts in Virginia have clearly adopted the policy-limits rule: "If [the insurer] is ultimately found not to have acted in bad faith, then [the insured] may only recover up to the policy's relevant coverage limitations . . . ." *Field v. Transcon. Ins. Co.*, 219 B.R. 115, 123 (E.D. Va. 1998), *aff'd*, 173 F.3d 424 (4th Cir. 1999) (internal quotations

[3] *See* New York Ins. L. § 3420(a)(2) (requiring liability policies to contain a provision entitling judgment creditors to enforce their rights against an insurer only "under the terms of the policy or contract for the amount of such judgment not exceeding the amount of the applicable limit of coverage under such policy or contract").

omitted, modifications in *Field*); *see also Safeway Moving & Storage Corp. v. Aetna Ins. Co.*, 317 F. Supp. 238, 246 (E.D. Va. 1970) (damages for breach of defense duty include "the amount of the judgment up to the policy limits" along with reasonable defense costs and interest).

Mississippi

Likewise the Fifth Circuit has held that the policy-limits rule applies as a matter of **Mississippi** law:

> With respect to excess judgments, an insurer is not liable for the amount in excess of the policy limit so long as the insurer has not acted in bad faith and has not wrongfully refused to settle the claim within its policy limits. The rationale is that the excess judgment was not caused by either a breach of the duty to defend or a breach of the duty to settle. That is, the insurer's defense of the insured would not have prevented a judgment in excess of the policy limit.

Liberty Mut. Fire Ins. Co. v. Canal Ins. Co., 177 F.3d 326, 336–337 (5th Cir. 1999) (footnoted citations omitted). The court went on to carve out *exceptional situations*, such as where "the insurer leads the insured to believe he will provide a defense, but does not, the insurer may be liable for a default judgment entered in excess of the policy limits. Also, if an insurer wrongfully withdraws from the defense too close to trial such that the insured is precluded from providing an adequate defense, the insurer may be liable for an excess judgment." *Id.* at 337. These examples illustrate the causation element lacking in the present case, militating against allowing damages in excess of Century's policy limit—whether viewed through a lens of contract *or* tort.

South Dakota

Finally, in a case arising in **South Dakota**, the Eighth Circuit held after reviewing authorities on both sides: "As a general rule, … the insurer's liability will be limited by the policy's coverage provisions." *Triple U Enters., Inc. v. N.H. Ins. Co.*, 766 F.2d 1278, 1282 (8th Cir. 1985). While not addressing limits specifically, the court reversed a judgment against the insurer that included uncovered parts of the judgment, and remanded for recalculation of an award that hewed to the parties' contract. *Id.* at 1281, 1283.

II.

EIGHT STATES APPEAR TO ALLOW LIABILITY OVER LIMITS, UPON CLEAR PROOF THAT AN INSURER'S BREACH CAUSED IT

Illinois

Illinois' most recent case on point summarized state law as allowing an insured to "recover an excess judgment based on its insurer's breach of duty to defend" even absent bad faith, "as a compensatory measure, where the insured's damages are proximately caused by the insurer's breach of duty." *Delatorre v. Safeway Ins. Co.*, 989 N.E.2d 268, 275 (Ill. App. Ct. 2013). But the *Delatorre* court found such proximate causation on facts unlike Century's case: "[T]he entry of neither the default order nor the default judgment was of [the insured's] instigating or choosing, or even known to him until years later." *Id.* at 276. And the court "expressly limit[ed its] decision on the suitability of the default judgment entered against the insured as the measure of damages to the precise facts of this case . . . ." *Id.* at 276–277.

Wisconsin

The **Wisconsin** Supreme Court has also "conclude[d] that an excess judgment is properly included in the damages for breach of an insurer's duty to defend, if the excess judgment was a natural or proximate result of the breach." *Newhouse by Skow v. Citizens Sec. Mut. Ins. Co.*, 501 N.W.2d 1, 7 (Wis. 1993). But as that court explained last year, "*Newhouse* is explicit that the insured must show that he was made worse off by the breach than he would have been had the breach not occurred." *Burgraff v. Menard, Inc.*, 875 N.W.2d 596, 608 (Wis. 2016) (internal quotation marks omitted) (holding insured not entitled to recover judgment in excess of policy limits because no evidence showed his insurer's denial of defense caused that result).

Georgia

Georgia too allows case-specific proof that a judgment in excess of the policy limits can be "traced directly" to the insurer's breach of the duty to defend. *Khan v. Landmark Am. Ins. Co.*, 757 S.E.2d 151, 156 (Ga. Ct. App. 2014) (citing *Leader Nat. Ins. Co. v. Kemp & Son, Inc.*, 380 S.E.2d 458, 459 (Ga. 1989)).

California

Likewise in **California**, "damages for breach of the duty to defend are not inexorably imprisoned within the policy limit but are measured by the consequences proximately caused by the breach." *State Farm*

Mut. Auto. Ins. Co. v. Allstate Ins. Co., 88 Cal. Rptr. 246, 259 (Cal. Ct. App. 1970).

Michigan / Montana

The high courts of **Michigan** and **Montana** have also allowed damages in excess of the policy limit regardless of an insurer's good or bad faith. *See Stockdale v. Jamison*, 330 N.W.2d 389, 393 (Mich. 1982); *Lee v. USAA Cas. Ins. Co.*, 86 P.3d 562, 565 (Mont. 2004)).

North Carolina / Kentucky

The high courts of two states, **Kentucky** and **North Carolina**'s has so stated in dicta. *See Wilson v. State Farm Mut. Auto. Ins. Co.*, 394 S.E.2d 807, 811 (N.C. 1990) ("This [case] is not the same as a case in which a carrier wrongfully refuses to defend its insured . . . and damages are recovered against the insured in excess of the coverage. In such a case *[which the FDCC has not found in North Carolina]* the insured has been damaged and has a claim against the insurer."); *Cincinnati Ins. Co. v. Vance*, 730 S.W.2d 521, 523 (Ky. 1987) (similar language, but court reinstated trial court judgment absolving the insurer entirely). Moreover, the **Kentucky** Supreme Court has more recently held: "An insurer is liable for a judgment against its insured in excess of the policy limits only if it refused in 'bad faith' to pay a settlement demand within its policy limits." *American Physicians Assur. Corp. v. Schmidt*, 187 S.W.3d 313, 318 (Ky. 2006).

III.

IN 25 STATES, FDCC HAS FOUND NO PRECEDENT ADDRESSING THE QUESTION

The following state courts appear to have no decision on point with the certified question[4]: Alabama, Alaska, Arkansas, Colorado, Delaware, Florida, Hawaii, Indiana, Iowa, Louisiana, Maine, Massachusetts, Nebraska, Nevada, New Hampshire, New Mexico, North Dakota, Ohio, Oklahoma, Rhode Island, South Carolina, Utah, Vermont, West Virginia, Wyoming.

Nevertheless, as Century's brief explains, Nevada does have substantial case law *supporting adoption* of a policy-limits rule, based

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[4] Some states have no precedent anywhere near the point. Some have cases standing for related points, but they do not discuss policy limits, or address whether such limits cap an insurer's liability for breach of the defense duty. Only one state, **Florida**, appears here because it has *too many* conflicting intermediate-court precedents on or near the point to say what its law is, with no resolution by its highest court. *See Robinson v. State Farm Fire & Cas. Co*. 583 So.2d 1063, 1068 (Fla. Dist. Ct. App. 1991) (collecting cases); *State Farm Mut. Auto. Ins. Co. v. Horkheimer*, 814 So.2d 1069, 1071 (Fla. Dist. Ct. App. 2001) ("Absent a showing of bad faith, a judgment cannot be entered against an insurer in excess of its policy limits.")

on contract principles and related rules. The foregoing summary of state law further supports this Court's resolution of the certified question in favor of the policy-limits rule.

CONCLUSION

For the reasons set forth above and in Century's opening brief, this Court should hold that the liability of an insurer that denies a defense in good faith, and does not unreasonably decline a settlement offer within policy limits, is capped at the policy limit plus any costs incurred by the insured in mounting a defense.

Dated this 18th day of October, 2017.

LEWIS ROCA ROTHGERBER CHRISTIE LLP

By: ______________________________

DANIEL F. POLSENBERG (SBN 2376)
J CHRISTOPHER JORGENSEN (SBN 5382)
3993 Howard Hughes Parkway, Suite 600
Las Vegas, Nevada 89169
(702) 949-8200

Attorneys for the Federation of Defense & Corporate Counsel

CERTIFICATE OF COMPLIANCE

1. I certify that this brief complies with the formatting, typeface, and type-style requirements of NRAP 32(a)(4)–(6) because it was prepared in Microsoft Word 2010 with a proportionally spaced typeface in 14-point, double-spaced Century Schoolbook font.

2. I certify that this brief complies with the type-volume limitations of NRAP 32(a)(7) because, except as exempted by NRAP 32(a)(7)(C), it contains 4,096 words.

3. I certify that I have read this brief, that it is not frivolous or interposed for any improper purpose, and that it complies with all applicable rules of appellate procedure, including NRAP 28(e). I understand that if it does not, I may be subject to sanctions.

Dated this 18th day of October, 2017.

LEWIS ROCA ROTHGERBER CHRISTIE LLP

By: ______________________________

DANIEL F. POLSENBERG (SBN 2376)
J CHRISTOPHER JORGENSEN (SBN 5382)
3993 Howard Hughes Parkway, Suite 600
Las Vegas, Nevada 89169
(702) 949-8200

Attorneys for the Federation of Defense & Corporate Counsel

CERTIFICATE OF SERVICE

I certify that on October 18, 2017, I submitted the foregoing *AMICUS CURIAE* BRIEF for filing *via* the Court's eFlex electronic filing system. Electronic notification will be sent to the following:

Martin J. Kravitz
CHRISTIAN, KRAVITZ, DICHTER, JOHNSON & SLUGA
8985 South Eastern Avenue
Suite 200
Las Vegas, Nevada 89123

Attorneys for Appellant

Dennis M. Prince
Robert T. Eglet
Tracy A. Eglet
EGLET PRINCE
400 South 7th Street, Suite 400
Las Vegas, Nevada 89101

Attorneys for Respondents

I further certify that I served a copy of this document by mailing a true and correct copy thereof, postage prepaid, at Las Vegas, Nevada, addressed as follows:

James Ric Gass
Michael S. Yellin
GASS WEBER MULLINS LLC
241 N. Broadway Avenue
Suite 300
Milwaukee, Wisconsin 53202

Marie Louise Cousineau
COZEN O'CONNOR
601 South Figueroa Street
Suite 3700
Los Angeles, California 90017

Attorneys for Appellant

Eric Tran
LISPON, NEILSON, COLE, SELTZER, GARIN, P.C.
9900 Covington Cross Drive
Suite 120
Las Vegas, Nevada 89144

Attorneys for Respondents

An Employee of Lewis Roca Rothgerber Christie LLP