IN THE SUPREME COURT OF THE STATE OF NEVADA

CENTURY SURETY COMPANY, Appellant, v. DANA ANDREW, as LEGAL GUARDIANS OF RYAN T. PRETNER; AND RYAN T PRETNER, Respondents.	No. 73756 United States District Court Case No. 2:12-CV-00978

CERTIFIED QUESTION FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEVADA

APPELLANT'S REPLY BRIEF

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INTRODUCTION

Respondents devote half of their answering brief to providing a survey course in insurance law and quibbling with alleged "factual inaccuracies" in Century's brief. (*See* Respondents' Answering Brief ("Opp. Br.") at 1-37.)[1] What Respondents do not do much of in their brief is meaningfully address the arguments and authority presented in Century's opening brief. But even when they do, they fail to offer a persuasive parry to the thrust of Century's arguments. While Respondents provide a lengthy—and unnecessary—tour of insurance law, they only glancingly grapple with the certified question presented: Whether, under Nevada law, the liability of an insurer that has breached its duty to defend, but has

[1] While Respondents claim that there are "important factual inaccuracies" in Century's brief, they fail to specifically identify any alleged inaccuracies. (Opp. Br. at 1.) In any event, the purported disputes do not appear relevant to the resolution of the certified question. For instance, Respondents concede that the District Court granted summary judgment in Century's favor on Respondents' bad faith claims, but nonetheless argue that the Court "never concluded Century acted reasonably or in 'good faith' when it refused to defend." (Opp. Br. at 42.) Yet, the District Court unequivocally held that "Century did not act in bad faith in denying coverage" and that "Plaintiffs have failed to provide evidence to show a genuine dispute of material fact as to the reasonableness of Century's decision." *Andrew v. Century Sur. Co.*, No. 2:12-cv-00978, 2014 WL 1764740, at *10 (D. Nev. Apr. 29, 2014); *see also* Order Certifying Question at 3 ("Century did not act in bad faith."). These holdings are unaltered by the Court's subsequent decisions. In any event, why the Respondents dispute this point is unclear given that the certified question presumes, as the Court held, that there is no bad faith.

not acted in bad faith, is capped at the policy limit plus any costs incurred by the insured in mounting a defense.[2]

As Century explained in its opening brief, the majority of jurisdictions to address the certified question presented here have answered ***yes*** and limit the measure of damages for breach of the duty to defend—in the absence of bad faith—to the costs of defense plus indemnity up to policy limits. Under this majority rule, an insured's damages for an insurer's reasonable refusal to defend are limited to the policy limit plus any costs incurred by the insured in mounting a defense. To recover damages in excess of the policy limit under this rule, most jurisdictions hold that an insured must establish that the insurer failed to reasonably settle the claim or otherwise acted in bad faith. Thus, under the majority approach, the liability of an insurer that denied a defense in good faith—though later judicially determined to be in error—and did not decline a settlement within policy limits is capped at the policy limit plus any costs incurred by the insured in mounting a defense.

Respondents' brief simply disagrees with the majority rule, but does not provide this Court with any cogent reason to depart from this rule. Indeed, while

[2] For instance, Respondents spend five pages of their brief arguing that an insurer's breach of the duty to defend is a material breach of the insurance contract, an argument that was not raised in Century's opening brief, and which has no bearing on the resolution of the certified question here. (Opp. Br. at 25-29.)

Respondents expound at length on the background and nature of insurance law, jurisdictions adopting the majority rule recognize these same general insurance law principles upon which Respondents purport to rely.[3] Consequently, this Court should adopt the majority rule and expressly hold that the liability of an insurer that acted in good faith and did not decline a within-limits settlement opportunity is capped at the contracted for policy limit plus any costs incurred by the insured in mounting a defense.

ARGUMENT

I. This Court should adopt the majority rule, which holds that the liability of an insurer that has breached its duty to defend, but has acted in good faith, is capped at the policy limit plus any costs incurred by the insured in mounting a defense.

A. Respondents fail to meaningfully dispute or distinguish the majority rule.

Again, the majority rule holds that a liability insurer's good faith but mistaken refusal to provide a defense does not create liability beyond the contracted for policy limits. *See Wilcox* v. *Am. Home Assurance Co.*, 900 F. Supp. 850, 856 (S.D. Tex. 1995) ("The damages recoverable on a contract claim for breach of the duty to defend do not include damages in excess of the policy

[3] *See, e.g.*, *Mesmer v. Md. Auto Ins. Fund*, 725 A.2d 1053, 1064 (Md. Ct. App. 1999); *State Farm Mut. Auto Ins. Co. v. Paynter*, 593 P.2d 948, 950 (Ariz. Ct. App. 1979) (recognizing "the broad duty of the insurer to defend").

limits."); *Paynter*, 593 P.2d at 954 (recognizing the rule that "a refusal to defend in and of itself does not expose the insurance carrier to greater liability than that contractually provided in the policy."). The overwhelming weight of authority makes clear that, under the majority rule, where an insurer breaches its duty to defend, damages for the breach are ordinarily capped at the policy limit plus any costs incurred by the insured in mounting a defense. *See, e.g.*, *Desert Mountain Props. Ltd. P'ship v. Liberty Mut. Fire Ins. Co.*, 225 Ariz. 194, 217, 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.'") (quoting *Paynter*, 593 P.2d at 954 (App.1979)); *Waite v. Aetna Cas. & Sur. Co.*, 467 P.2d 847, 851-52 (Wash. 1970) ("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."); *Miller v. Secura Ins. & Mut. Co. of Wis.*, 53 S.W.3d 152, 155 (Mo. Ct. App. 2001) ("By breaching a contract by refusing to provide a defense to an insured under the policy, an insurance company is liable to its insured for any judgment recovered against [the insured] up to the limits of the policy plus attorney fees, costs, interest and any other expenses incurred by the insured in conducting the defense of the

suit") (citation and quotation marks omitted) (alteration in original); *Mesmer*, 725 A.2d 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. Instead, the damages for breach of the contractual duty to defend are limited to the insured's expenses, including attorney fees, in defending the underlying tort action").

Unable to blunt the force of the majority rule by distinguishing these cases on their facts, Respondents advance two lines of attack on the majority rule, both of which fall flat. First, Respondents apparently dispute the fact that there is a majority rule, employing the term "so-called majority rule." Second, Respondents essentially argue in a circle that the majority rule cases are wrongly decided because they reach the wrong (from Respondents' perspective) result. Neither argument has merit.

First, Respondents concede, as they must, "that there are cases that hold an insured may only recover up to the indemnity limit plus attorney's fees and costs in defending the underlying action when an insurer breaches its duty to defend in the absence of bad faith," but contend that "characterizing this as a majority rule is factually inaccurate." (Opp. Br. at 46.) The apparent basis for this argument is that the FDCC *amicus* brief identifies "only" ten states with a clear rule that, absent

bad faith, liability for the breach of the duty to defend is capped at the policy limits. (*Id.*) It is Respondents, not Century, that mischaracterize and distort the state of the law. Notwithstanding Respondents' attempt to muddy the waters, the FDCC *amicus* brief makes clear that of the 25 jurisdictions to address the question presented here, 17 would hold that a liability insurer's good faith but mistaken refusal to provide a defense does not create exposure to liability beyond the contracted-for policy limits. (*See* FDCC *Amicus* Br. at 3-16.) 17 of 25 is a majority.[4] Thus, there is no inaccuracy in referring to this as the majority rule.[5] Indeed, other courts have routinely referred to this rule as the majority rule. *See, e.g.*, *Greer v. Nw. Nat'l Ins. Co.*, 743 P.2d 1244, 1250 (Wash. 1987); *George R. Winchell, Inc. v. Norris*, 633 P.2d 1174, 1178 (Kan. Ct. App. 1981) (recognizing the "majority rule" that "a finding of bad faith is required for a finding of liability of amounts in excess of the policy limits.").

[4] This court has determined a majority rule by including only those states that have considered a question. *See Hulett v. State*, 546 P.2d 1293, 1294 (1976) (determining the "majority rule" using the 21 jurisdictions "that have considered and resolved the issue" as the denominator and adopting the majority rule).

[5] Even using Respondents' skewed math, under which 10 states have such a rule and 8 states do not, it is still the majority rule because 10 out of 18 is a majority. Or to put it differently, 8 is less than 10 (and certainly less than 17). Thus, viewed under any formula, the rule that Respondents attempt to foist upon this Court has been accepted by only a minority of jurisdictions to consider the rule.

Respondents' second argument fares no better. Respondents' attempt to refute the majority rule cases is nothing more than an argument that these cases were wrongly decided because the outcome is at odds with the position articulated by Respondents here—*i.e.*, the majority rule that liability is capped at the policy limits absent bad faith is wrong because Respondents should be able to recover damages in excess of the policy limits. (*See* Op. Br. at 46-51.) This argument from circularity simply begs the question.[6]

For instance, Respondents assert that "many of the decisions from these jurisdictions are not persuasive because they *overlook* the legal distinction between the remedies available for a breach of contract and the tort of bad faith." (Opp. Br. at 46-47 (emphasis added).) But Respondents offer nothing to substantiate their assertion that the courts in these cases "overlook[ed]" this distinction (or any other argument). Rather, like most courts to consider the issue, these courts considered the measure of damages that Respondents ask this Court to adopt and rejected it. Thus, these cases do not, as Respondents posit, "undermine[]" the majority rule, they undermine Respondents' position.

[6] Curiously, Respondents appear to cite to Judge Gordon's decision in *Andrew* to support their position. (*See* Opp. Br. at 48.) Of course, Judge Gordon did not answer the question at issue here; he asked this Court to do so.

Respondents assert that the majority rule is wrong. (*See* Op. Br. at 49 (arguing that "these cases incorrectly conflate the contractual duty to defend a lawsuit with the duty to indemnify and fail to acknowledge the distinction"); *id.* at 50 (arguing that the cases are not "reliable" and that the analysis is "flawed").) But Respondents' argument simply begs the question. (*See* Opp. Br. at 51 ("The existence of bad faith, or lack thereof, is not relevant to this Court's inquiry. Therefore, the [majority rule] decisions outlined above should be rejected.").) This tautology—the majority rule is wrong because it's wrong—does not give this Court any reason to depart from the majority rule and this Court should decline to do so.

B. The authority upon which Respondents purport to rely is entirely consistent with the majority rule.

After failing to address the legal reasoning of the majority rule, Respondents next contend that "[n]umerous jurisdictions do not follow the so-called majority rule." (Op. Br. at 52.) Tellingly (and for good reason), nowhere do Respondents attempt to argue that the position they ask this Court to adopt is the majority rule. In addition to (at least implicitly) conceding that the weight of applicable authority does not support their argument, the authority Respondents do cite is entirely

consistent with the majority rule and, in any event, does not provide this Court with a foundation upon which to depart from the majority rule.[7]

Respondents begin by asserting that "[t]he California Court of Appeals, California Supreme Court, and the Ninth Circuit all concluded that an insurer that breached its duty to defend is liable for the full amount of a resulting judgment, default or otherwise, against its insured." (Opp. Br. at 52 (citing *Gray v. Zurich Ins. Co.*, 419 P.2d 168 (Cal. 1966); *Pershing Park Villas Homeowners Ass'n v. United Pacific Ins. Co.*, 219 F.3d 895 (9th Cir. 2000); *Amato v. Mercury Casualty Co.*, 53 Cal. App. 4th 825 (Cal. Ct. App. 1997); *Archdale v. Am. Int'l Specialty Lines Ins. Co.*, 154 Cal. App. 4th 449 (Cal. Ct. App. 2007)).) As an initial matter,

[7] Respondents assert that that the "Nevada Supreme Court looks to persuasive authority for guidance regarding issues of first impression." (Opp. Br. at 52.) Century agrees, and made the same point in its opening brief. (*See* Br. at 19 ("In deciding questions of first impression under Nevada law, this Court has looked to other jurisdictions and found persuasive where a rule or approach was adopted by the majority of other jurisdictions.").) Given that Respondents appear to concede that they are advocating a minority position (adopted, at best, in only eight jurisdictions), Respondents understandably fail to explain how this proposition helps them here. (*See* FDCC *Amicus* Br. at 2-19.) To the extent that Respondents intended to suggest that this Court looks to California, as set forth below, the majority rule is consistent with the California decisions relied upon by Respondents here. Moreover, in looking to other states for guidance, this Court has looked to the very states that have adopted the majority rule here. *See*, *e.g.*, *Camco, Inc. v. Baker*, 113 Nev. 512, 517, 936 P.2d 829, 832 (1997) (adopting majority rule, looking to Arizona and Washington law); *Erickson v. State*, 821 P.2d 1042, 1043 (1991) (adopting majority rule, citing decisions from Arizona and Washington).

while Respondents appear to present these cases as examples of multiple jurisdictions that have adopted the minority view, each of these cases applied California law. *Id.* Thus, these cases represent only one "jurisdiction" for purposes of Respondents' efforts to show that "numerous jurisdictions" have adopted the minority approach that they ask this Court to adopt. More importantly, however, none of these cases actually supports Respondents' argument.

While *Gray* "acknowledges the general rule that an insurer that wrongfully refuses to defend is liable on the judgment against the insured," there is no suggestion that the judgment at issue in the case was an excess judgment—*i.e.*, one that exceeded the policy limits—or that the Court was ever presented with, or considered, that issue. *See id.* at 279-80 (noting that "defendant urges that our holding should require only the reimbursement of the insured's expenses in defending the third-party action but not the payment of the judgment."). In other words, *Gray* did not consider the specific question before this Court. Thus, because there is no indication that the judgment in *Gray* exceeded the policy limit, *Gray* does not conflict with the majority rule that damages for the breach of the duty to defend include expenses incurred in defending the underlying action and a judgment covered by the policy (capped at the policy limit), and the case does not help Respondents here.

The same is true with respect to Respondents' citation to *Pershing Park*. (Opp. Br. at 53.) In Respondents' recitation of the facts of *Pershing Park*, they fail to mention that the case turned on a finding of bad faith. *See* 219 F.3d at 902 (holding that insurer was liable for the default judgment because "it breached the covenant of good faith and fair dealing when it wrongly withdrew the [insured's] defense.").[8] While Respondents cite *Pershing Park* for the proposition that "automatic liability" attaches to an insurer's failure to defend, they fail to acknowledge the Court's clear pronouncement that such "automatic liability" springs from the insurer's ***bad faith***. *See id.* 901 (discussing whether insurer's "***bad faith*** rendered it automatically liable") (emphasis added). The Court concluded that the insurer "acted unreasonably and in bad faith," *id.* at 905, and made clear that tort damages were at issue. *See id.* at 902 ("The tort of bad faith is not predicated on negligence, . . . but on the bad faith failure to provide any defense at all."). Thus, like *Gray*, *Pershing Park* is entirely consistent with the majority rule, which requires a finding of bad faith before imposing liability beyond the policy limits.

Respondents' purported reliance on *Amato* is equally misplaced. Here, too, the case turned on a finding of bad faith—*i.e.*, a tortious breach. *See Amato*, 53

[8] In addition, as in *Gray*, there is no indication that the judgment at issue was in excess of the policy limits.

Cal. App. 4th at 829 (considering the damages available "where an insurer ***tortiously*** breaches the duty to defend") (emphasis added); *id.* at 831 (recognizing that the insurer "had no good cause to refuse to defend, and [it] therefore ***tortiously*** breached the covenant of good faith and fair dealing.") (emphasis added); *id.* at 833 (recognizing that "where the insurer ***tortiously*** refuses to defend and as a consequence the insured suffers a default judgment, the insurer is liable on the judgment") (emphasis added); *id.* at 834 (recognizing that "an insurer who wrongfully refuses to defend may ***tortiously*** breach the covenant of good faith and fair dealing and should be liable for consequential damages") (emphasis added).

Strangely, Respondents highlight that the *Amato* Court distinguished between contract damages and tort damages, but fail to recognize (or acknowledge) that the damages ultimately allowed in *Amato* were tort damages that resulted from the breach of the duty of good faith. *See id.* at 835 (holding that "the trial court was correct in its initial judgment that [the insurer] is liable for the default judgment, which constitutes the detriment to [the insured] proximately caused by [the insurer's] ***tortious*** breach of the duty to defend.") (emphasis added); *id.* at 837 ("The essence of the trial court's decision and our affirmance . . . is that [the insurer] breached its implied covenant of good faith and fair dealing by failing to provide a defense."); *see also id.* at 831 ("Breach of an insurer's duty to defend

violates a contractual obligation and, ***where unreasonable***, also violates the covenant of good faith and fair dealing, for which tort remedies are appropriate.") (emphasis added). Thus, *Amato* has no bearing on the question certified here, which asks this Court to determine the measure of damages absent tortious bad faith conduct.[9]

Respondents' citation to *Archdale* is equally wide of the mark and does not help them here. The claims at issue in *Archdale* involved an insurer's bad faith refusal to settle a claim within policy limits. *See* 154 Cal. App. 4th at 461 (plaintiffs "seek recovery only in contract for [the insurer's] ***bad faith conduct in failing to accept multiple reasonable settlement offers***; and they contend that such contract claim will support recovery of the amount of the excess judgment.") (emphasis added); *id.* at 463 ("The essence of the plaintiffs' claims is that [the insurer] ***rejected multiple reasonable settlement offers*** to resolve the underlying action for a sum within the coverage limit of the [insurance] policy.") (emphasis added). Thus, in the context of a bad faith failure to accept a reasonable settlement offer—two foundational premises that are absent from the certified question here—the *Archdale* Court found that an insurer could be liable for an excess judgment. *Id.* at 469 (concluding that "an insurer can be held liable for a judgment

[9] In addition, unlike Century here, the insurer in *Amato* had reasonable opportunities to settle the claim and failed to do so. *Id.* at 838.

against the insured in excess of its policy limits if the insurer has breached this implied covenant [of good faith and fair dealing] by failing to accept a settlement offer within the policy limits.").

Moreover, the *Archdale* Court expressly tethered its holding to the two foundational facts not at issue here: a bad faith failure to accept a reasonable settlement offer. *See id.* at 471, n. 24 ("We emphasize that our conclusion and its supporting analysis may not have application to an insured's effort to obtain a contract recovery for an insurer's breach of the implied covenant of good faith and fair dealing in factual contexts other than the one presented by this case (i.e., a liability insurer's failure to accept a reasonable settlement offer to resolve a claim against its insured).").[10] Because these are not the facts presented by the certified question, *Archdale*, like the other California cases cited by Respondents, is of no moment here.

Far from showing that these California cases require this Court to adopt the minority rule, the cases cited by Respondents establish that California law is in

[10] The same is true with respect to Respondents' citation to *Delatorre v. Safeway Insurance Co.*, 2013 IL App (1st) 120852, 989 N.E.2d 286 (Ill. App. Ct. 2013), *see* Opp. Br. at 56, which expressly limited its holding to the specific facts before the court and disclaimed the decision as precedent upon which to base other decisions. *Id.* at ¶ 37, 276-77 ("We expressly limit our decision on the suitability of the default judgment entered against the insured as the measure of damages to the precise facts of this case, and do not decide its applicability to future cases.").

accord with the majority rule that, absent bad faith or a failure to settle, liability is capped at the policy limits. *See Nalder v. United Auto. Ins. Co.*, 824 F.3d 854, 857 (9th Cir. 2016) ("In California, '[w]here there is no opportunity to compromise the claim and the only wrongful act of the insurer is the refusal to defend, the liability of the insurer is ordinarily limited to the amount of the policy plus attorneys' fees and costs.'") (citing *Communale v. Traders & Gen. Ins. Co.*, 328 P.2d 198, 201 (Cal. 1958)). The same is true with respect to Respondents' citation to *Robinson v. State Farm Fire & Casualty Co.*, 583 So.2d 1063 (Fla. Ct. App. 1991), (Op. Br. at 55), in which the Court adopted the approach taken by other Florida courts that "there can be no excess judgment in the absence of bad faith even where there was a breach of the duty to defend" and identifying factors relevant to the bad faith

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inquiry.[11] *Robinson*, 583 So.2d at 1068. The remaining cases upon which Respondents purport to rely are equally inapposite. (*See* Op. Br. at 55-56.)[12]

At bottom, the authority upon which Respondents purport to rely is entirely consistent with the majority rule. As Century explained in its opening brief, the majority rule is not an absolute bar to recovering damages in excess of the policy limit. (*See* Br. at 15-19.) Rather, like the cases upon which Respondents rely, the

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[11] As the FDCC *amicus* brief explains, Florida law is not settled, (*see* FDCC *Amicus* Br. at 20, n. 4), and numerous Florida cases have relied upon and adopted the majority rule. *See, e.g.*, *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."); *Seward v. State Farm Mut. Auto. Ins. Co.*, 392 F.2d 723, 726 (5th Cir. 1968) (Florida law); *Am. Fid. Fire Ins. Co. v. Johnson*, 177 So. 2d 679, 683 (Fla. 1st DCA 1965) ("Where there is no opportunity to compromise the claim and the only wrongful act of the insurer is the refusal to defend, the liability of the insurer is ordinarily limited to the amount of the policy plus attorneys' fees and costs.").

[12] *See, e.g., Bucci v. Essex Ins. Co.*, 323 F. Supp. 2d 84, 93 (D. Me. 2004) (holding that insurer that breached duty to defend was not liable for full amount of stipulated judgment entered into by insured because it was not a natural consequence of insurer's breach); *Polaroid Corp. v. Travelers Indem. Co.*, 610 N.E.2d 912, 920 (Mass. 1993) (holding that insurer was not liable for settlement costs where it breached its duty to defend, no discussion of liability for excess judgments); *Stockdale v. Jamison*, 330 N.W.2d 389, 394 (Mich. 1982) (holding that "ordinarily an insurer's liability for breach of its contractual duty to defend its insured is limited to an amount equal to the insured's assets not exempt from legal process."). Numerous courts have rejected the unworkable damages formulation set forth in *Stockdale*. *See*, *e.g.*, *Greer*, 743 P.2d at 1250 (recognizing that "Stockdale conflicts with the majority rule" and that "the *Stockdale* measure of damages violates the fundamental principle of contract damages that we mentioned at the outset of this section: an insured should be put in only as good a position as he would have occupied had the contract not been breached.").

rule requires that to recover damages in excess of the policy limit, an insured must establish that the insurer failed to reasonably settle the claim or otherwise acted in bad faith. (*See* Br. at 11-20.) Under any interpretation of the majority rule, the liability of an insurer that denied a defense in good faith and did not reject a within-limits opportunity to settle a claim is limited to the policy limit plus any costs incurred by the insured in mounting a defense. *See Emp'rs Nat'l Ins. Corp. v. Zurich Am. Ins. Co. of Ill.*, 792 F.2d 517, 518 (5th Cir. 1986) (holding that insurer is not liable for excess judgment beyond policy limits absent "bad faith or opportunity to settle within policy limits"); *Paynter*, 593 P.2d at 954 (recognizing that "the decisive factor in extending liability beyond the policy limit was not the refusal to defend, but the refusal to accept an offer of settlement within the policy limits" and holding that because insurer "never refused such an offer," insurer's "liability stemming from its refusal to defend the action should be confined to the limits of the policy."); *George R. Winchell, Inc.*, 633 P.2d at 1178 (recognizing the "majority rule" that "a finding of bad faith is required for a finding of liability of amounts in excess of the policy limits.").[13] Respondents fail to demonstrate that the majority rule is incorrect or should not apply here.

[13] Respondents attempt to distinguish *George R. Winchell, Inc*. and similar authority on the grounds that the cases discuss a bad faith failure to settle within

II. The Court should adopt the majority rule because it is consistent with Nevada law concerning breach of contract damages and this Court's decisions suggesting that a showing of bad faith is required to recover consequential damages in the insurance context.

Respondents contend that adopting the majority rule would somehow be at odds with longstanding Nevada contract law. (*See* Op. Br. at 29-37.) This is simply not so.

Again, under Nevada law, damages for breach of contract "should place the plaintiff in the position he would have been in had the contract not been breached." *Road & Highway Builders v. N. Nev. Rebar*, 284 P.3d 377, 382 (2012); *Col. Env'ts* v. *Valley Grading Corp.*, 105 Nev. 464, 470, 779 P.2d 80, 84 (1989). Here, if the contract had not been breached, Blue Streak would have been entitled to: 1) a defense, and 2) indemnity (if the claim was covered), up to the $1 million policy limit. In other words, had the duty to defend not been breached, the insured would have been entitled under the policy to the cost of defense and potential indemnification in an amount up to the policy limit. Thus, by awarding damages in the form of such costs and expenses as the insured may have incurred in defending the underlying tort action, a court places the insured in the position that it would have been in had the insurer properly performed its duty to defend.

In contrast, allowing recovery of a judgment in excess of the policy limit would put the insured in a better position than it would have been if the contract had not been breached and, accordingly, would run afoul of well-settled Nevada law concerning breach of contract damages. *See Road & Highway Builders*, 284 P.3d at 382; *see also Greer*, 743 P.2d at 1250 (recognizing that "an insured should

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policy limits. (*See* Op. Br. at 49-50.) But that's the point: absent bad faith or the failure to reasonably settle a claim, damages cannot exceed policy limits.

be put in only as good a position as he would have occupied had the contract not been breached."). Moreover, while Respondents suggest that the majority rule is inconsistent with general contract damages, jurisdictions that have adopted the majority rule follow the same general rules of contract damages adopted in Nevada. *See, e.g.*, *Dees v. Allstate Ins. Co.*, 933 F. Supp. 2d 1299, 1306, n. 4 (W.D. Wash. 2013) (applying Washington law) (noting general rule that "[c]onsequential damages are sustainable if they flow naturally and inevitably from a breach of contract and are so related to it as to have been within the contemplation of the parties when they entered into it," but recognizing that "even if [insured] is ultimately entitled to consequential damages for [insurer's] alleged breach of the Insurance Contract, total damages, including actual, incidental, and consequential damages for that breach, cannot exceed the Insurance Contact's policy limits"); *Miscione v. Bishop*, 130 Ariz. 371, 374, 636 P.2d 149, 152 (Ariz. Ct. App. 1981) ("Consequential damages are recoverable only where they arise naturally from the breach of a contract and where they were in the contemplation of the parties."). Unsurprisingly then, a majority of jurisdictions have declined to adopt the rule advocated by Respondents here, and this Court should follow suit.

In addition to being entirely consistent with general Nevada contract damages law, the majority rule is also consistent with this Court's articulation of damages in the specific context presented by the certified question. This Court has suggested that an insurer is not liable for consequential damages absent a finding of bad faith. *See U.S. Fid. & Guar. Co. v. Peterson*, 540 P.2d 1070, 1071 (1975) ("We approve and adopt the rule that allows recovery of consequential damages ***where there has been a showing of bad faith by the insurer***.") (emphasis added); *see also Allstate Ins. Co. v. Miller*, 212 P.3d 318, 327 (2009) ("If an insurer violates its duty of good faith and fair dealing . . . , the insurer's actions can be a

proximate cause of the insured's damages arising from a foreseeable settlement or excess judgment."). Thus, as under the majority rule, this Court has indicated that bad faith is required before an insurer can be held liable for an excess judgment. Similarly, this Court has recognized the general rule that "[a]n insurer who has no opportunity to settle within policy limits is not liable for an excess judgment for failing to settle the claim." *Miller*, 212 P.3d at 328 (citation and quotation marks omitted) (alteration in original). This too comports with those majority rule decisions holding that an insurer may be liable for an excess judgment beyond the policy limit if it had an opportunity to settle the claim and failed to do so in good faith.[14]

At bottom, Respondents ask this Court to adopt a minority rule that would impose extra-contractual liability on an insurer not due to willful or malicious actions taken in bad faith, but where, as here, a court has determined that the insurer proceeded in good faith and had a reasonable basis for its actions. The Court should decline Respondents' invitation to veer from the majority rule discussed above to create a new rule for Nevada, which would hold an insurer responsible for the entire judgment against an insured, including any amounts in

[14] Respondents attempt to distinguish this Court's prior decisions by arguing that this Court "did not hold, in either case, that without bad faith conduct, an insurer could never be liable for consequential damages above the indemnity limit for not providing a defense." (Opp. Br. at 51.) But Century never argued that this Court had expressly so *held*. Of course, if the Court had so held, there would be no question to certify because the issue would be conclusively decided. Rather, Century argues only that the reasoning of this Court's prior rulings supports adoption of the majority rule here. Respondents' arguments do nothing to suggest otherwise.

excess of the insurance policy's stated limits, regardless of the fact that the insurer acted reasonably and in good faith.

III. Even if the Court determines that consequential damages are recoverable in the insurance context absent a showing of bad faith—which it should not—damages from a default judgment in excess of the policy limit are not consequential damages as a matter of law.

Respondents contend that "Century improperly requests a legal conclusion from this Court that a default judgment is not a foreseeable consequential damage that stems from a breach of the duty to defend" because, they argue, the "question certified to this Court, [sic] is narrowly tailored and only asks to determine whether an insurer that breaches its duty to defend, in the absence of bad faith, is liable for all foreseeable consequential damages."[15] (Opp. Br. at 57.) Thus, the argument goes, this question is beyond the scope of the certified question. (*Id.*) Not so.

Contrary to Respondents' rendering, the precise question certified is stated as follows: "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?" (*See* Order Accepting

[15] Strangely, Respondents also posit that "Century cannot dispute that a foreseeable consequence of breaching the duty to defend is that insureds will be subject to a judgment, default or otherwise, in excess of the policy limit." (Opp. Br. at 37.) Of course, as Respondents' argument shows, Century does indeed dispute this point.

Certified Question, Directing Briefing and Directing Submission of Filing Fee.) Century agrees that if, as Century urges, this Court concludes that 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, it need not consider this point. If, however, the Court concludes otherwise—and again, it should not—then the question of whether damages from a default judgment in excess of policy limits are consequential as a matter of law are squarely within the question certified here.

Respondents' substantive argument on this point appears to be that Century discusses proximate cause, "however, the standard for determining whether damages are recoverable as a consequence of a breach of contract is foreseeability," which presents a question of fact. (Opp. Br. at 57.) Respondents are wrong on both accounts.

First, it is well-established that consequential damages must be both foreseeable *and* proximately caused by the breach.[16] *See Miller*, 212 P.3d at 327; *Goodrich & Pennington Mortg. Fund, Inc. v. J.R. Woolard, Inc.*, 120 Nev. 777, 784, 101 P.3d 792, 796 (2004) (affirming district court refusal to award

[16] Indeed, cases relied upon by Respondents recognize that consequential damages must be proximately caused by the breach. *See Delatorre*, 2013 IL App (1st) 120852, at ¶ 33, 989 N.E.2d at 275.

"consequential damages under a proximate-cause analysis."); *see also Finney v. First Tenn. Bank*, No. 12-cv-01249, 2016 WL 825836, at *5 (D. Ariz. Mar. 3, 2016) (consequential damages "must be 'proximately caused' by the breach"); 24 Williston on Contracts, § 64:12 (4th ed., May 2017 update) ("Consequential damages . . .. must be proximately caused by the breach"); *F.D.I.C. v. Commonwealth Land Title Ins. Co.*, 902 F. Supp. 2d 1048, 1071 (N.D. Ohio 2012) ("Consequential damages . . .. must be proximately caused by the breach and must be proven by the party seeking them.") (citation and internal quotation marks omitted).

Moreover, proximate cause and foreseeability may be determined as a matter of law. *See Humphries v. New York-New York Hotel & Casino*, 403 P.3d 358, 362 (Nev. 2017) (recognizing that "foreseeability is a question of law."); *Pac. Pools Const. Co. v. McClain's Concrete, Inc.*, 101 Nev. 557, 561, 706 P.2d 849, 852 (1985) (damages were not foreseeable as a matter of law). Indeed, under similar facts, courts have routinely held that damages from a default judgment in excess of the policy limit that is entered against an insured following the insured's failure to defend against the underlying tort action is not, as a matter of law, a consequential loss caused by said breach because a default judgment in excess of the policy limit is not a foreseeable consequential loss proximately caused by the breach of the

duty to defend. *See Liberty Mut. Fire Ins. Co. v. Canal Ins. Co.*, 177 F.3d 326, 336-37 (5th Cir. 1999) (holding that in the absence of bad faith, an insurer is not liable for a settlement or judgment in excess of the policy limits, explaining 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."); *see also* Allan D. Windt, 1 Insurance Claims and Disputes § 4.36 (6th ed. 2013) ("The amount of the judgment in excess of the policy limit would constitute an unforeseeable consequential damage"); Allan D. Windt, 1 Insurance Claims and Disputes § 4.36 (6th ed. 2013) (recognizing that "it cannot be said that the detriment suffered by the insured as a result of a judgment in excess of the policy limits was proximately caused by the insurer's refusal to defend.").

Here, if the contract had not been breached, Blue Streak would have been entitled to: 1) a defense, and 2) indemnity (if the claim was covered), up to the $1 million policy limit. Thus, the foreseeable damages proximately caused by Century's breach are any defense costs incurred in the underlying action, together with any indemnity (up to the policy limit). This is the appropriate measure of damages that were reasonably foreseeable and within the contemplation of the parties at the time the contract was entered. This measure of damages puts the

policyholder in "as good a position as he would have been had the contract not been breached," *Greer*, 743 P.2d at 1250, and is consistent with established Nevada law. *See, e.g.*, *Hornwood*, 807 P.2d at 211.

CONCLUSION

For the reasons set forth above and in Century's Opening Brief, this Court should adopt the majority rule and expressly hold that the liability of an insurer that acted in good faith and did not have an opportunity to settle a claim is limited to the policy limit plus any costs incurred by the insured in mounting a defense.

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Dated: January 25, 2018

Respectfully submitted,

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ATTORNEY'S CERTIFICATE

1. I certify that this 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 it has been prepared in a proportionally spaced typeface using 14 point Times New Roman font.

2. I further certify that this brief complies with the type-volume limitations of NRAP 32(a)(7) because, excluding the parts of the brief exempted by NRAP 32(a)(7)(C), it is proportionately spaced, has a typeface of 14 points and contains 6,684 words.

3. Finally, I certify that I have read this appellate 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 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 the accompanying brief is not in conformity with the requirements of the Nevada Rules of Appellate Procedure.

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