IN THE SUPREME COURT OF THE STATE OF NEVADA

* * *

NAUTILUS INSURANCE COMPANY,

Appellant,

v.

ACCESS MEDICAL, LLC ROBERT CLARK WOOD, II; AND FLOURNOY MANAGEMENT, LLC,

Respondents,

Supreme Court Case No. 79130

United States District Court,
for the District of Nevada,
Case No. 2:15-cv-00321

United States Court of Appeals for the Ninth Circuit
Case Nos. 17-16265
17-16272
17-16273

RESPONDENTS ACCESS MEDICAL, LLC AND ROBERT CLARK WOOD, II'S ANSWERING BRIEF

JORDAN P. SCHNITZER (#10744)
THE SCHNITZER LAW FIRM
9205 W. Russell Road, Suite 240
Las Vegas, Nevada 89148
Telephone: (702) 960-4050
jordan@theschnitzerlawfirm.com

Attorneys for Respondents Access Medical, LLC and Robert Clark Wood, II

NRAP 26.1 CORPORATE DISCLOSURE STATEMENT

The undersigned counsel of record certifies that the following are persons and entities as described in NRAP 16.1(a) and must be disclosed.

1. Defendants/Respondents Access Medical, LLC and Robert Clark Wood II ("Access") hereby declare Access is a limited liability corporation that there is no corporation which is a parent corporation of Access Medical or that owns 10% or more of stock belonging to Access Medical.

2. Jordan P. Schnitzer of The Schnitzer Law Group has represented Access in this litigation.

3. Martin J. Kravitz and L. Renee Green of Kravitz, Schnitzer, and Johnson, Chtd. have represented Access in this litigation.

These representations are made in order that the judges of this court may evaluate possible disqualification or recusal. A supplemental disclosure statement will be filed upon any change in the information provided herein.

DATED this 22 day of January 2020.

BY: s/Jordan P. Schnitzer, Esq.
JORDAN P. SCHNITZER, ESQ.

Nevada Bar No. 10744
THE SCHNITZER LAW FIRM
9205 W. Russell Road, Suite 240
Las Vegas, Nevada 89148
Attorney for Respondents

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Other Authorities

Secondary Sources

JURISDICTIONAL STANDARD FOR CERTIFICATION

This case presents a legal question certified to this Court under NRAP 5 by the United States Court of Appeals for the Ninth Circuit in *Nautilus Insurance Company v. Access Medical, LLC et al.* No. 17-16264, No. 17-16272, No. 17-16273, and D.C. No. 2:15-cv-00321-JAD-GWF (hereafter *Nautilus v. Access Medical*).

On September 20, 2019, this Court issued its Order Accepting the Certified Question.

STATEMENT OF THE ISSUE

This Court has accepted certification of a question from the United States Court of Appeals for the Ninth Circuit. The Ninth Circuit presented the certified question as follows:

> Is an insurer entitled to reimbursement of costs already expended in defense of its insureds where a determination has been made that the insurer owed no duty to defend and the insurer expressly reserved its right to seek reimbursement in writing after defense has been tendered but where the insurance policy contains no reservation of rights.

See Order Accepting Certified Question, directing Briefing and Directing Submission of Filing Fee.

This Court should rephrase the question presented by the Ninth Circuit to ask: Can an insurer unilaterally revise the terms an insurance policy through a reservation of rights letter to create a right to reimbursement, in effect retroactively increasing the insurance premium?

LEGAL BRIEF

I. STATEMENT OF THE FACTS

A. Introduction

Access Medical, LLC and Robert "Sonny" Wood, II (collectively the "Insureds") purchased an insurance policy from Nautilus Insurance Company ("Nautilus") and paid the requisite premiums with the expectation that Nautilus would defend them in claims asserted against them unless Nautilus knew with absolute certainty there was no coverage under the insurance policy (hereinafter "Policy"). However, when a third-party brought legal action against the Insureds in a California State action (hereinafter the "Underlying Action"), Nautilus delayed and strategized to use every tactic possible to disclaim its duty to defend the Insureds. Four months after the Insureds tendered defense in the Underlying Action, Nautilus agreed to defend the Insureds.

Nautilus filed a declaratory relief action seeking a declaration that it had no duty to defend the Insured in the Underlying Action under the policy. Nautilus prevailed in its initial declaratory relief action (litigation remains concerning additional evidence discovered that triggered the duty to defend), but the district court denied Nautilus' request for reimbursement of the attorneys' fees and costs expended in defending the Underlying Action.

B. The Policy

Access Medical, LLC ("Access") purchased a policy from Nautilus which was effective from January 15, 2011 to January 15, 2012. Joint Appendix, Vol. IV Pages 00683 – 733 (hereafter "Jt. App'x, Vol. __, p. __"). The provisions of the policy pertinent to this litigation are as follows:

> Insurance Agreement
>
> All Coverage Parts included in this policy are subject to the following conditions.
>
> …
>
> B. Changes
>
> ***This policy contains all the agreements between you and us concerning the insurance afforded***. The first Named Insured shown in the Declarations is authorized to make changes in the terms of this policy with our consent. ***This policy's terms can be amended or waived only by endorsement issued by us and made a part of this policy.***
>
> …
>
> COMMERCIAL GENERAL LIABILITY COVERAGE FORM
>
> …
>
> 1. Insuring Agreement
>
> We will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" or "property damage" to which this insurance applies. ***We will have the right and duty to defend the insured against any "suit"*** seeking those damages. However, we will have no duty to defend the insured against any "suit" seeking damages for "bodily injury" or "property damage" to

which this insurance does not apply. ***We may, at our discretion, investigate any "occurrence" and settle any claim or "suit" that may result.*** But.

(1) The amount we will pay for damages is limited as described in Section III – Limits of Insurance; and

(2) Our **right and duty** to defend ends when we have used up the applicable limit of insurance in the payment of judgments or settlements under Coverages A or B or medical expenses under Coverage C.

No other obligation or liability to pay sums or perform acts or services is covered unless explicitly provided for under Supplementary Payments – Coverages A and B.

…

COVERAGE B PERSONAL AND ADVERTISING INJURY LIABILITY

1. Insuring Agreement

a. We will pay those sums that the insured becomes legally obligated to pay as damages because of "personal and advertising injury" to which this insurance applies. ***We will have the right and duty to defend the insured against any "suit"*** seeking those damages. However, we will have not duty to defend the insured against any "suit" seeking damages for "personal and advertising injury" to which this insurance does not apply. We may, at our discretion, investigate any offense and settle any claim or "suit" that may result. But:

(1) The amount we will pay for damages is limited as described in Section III – Limits of Insurance; and

(2) Our **right and duty to defend** end when we have used up the applicable limit of Insurance in the payment of judgments or settlements under Coverages A or B or medical expenses under Coverage C.

No other obligation or liability to pay sums or perform acts or services is covered unless explicitly provided for under Supplementary Payments – Coverages A and B.

…

SUPPLEMENTARY PAYMENTS – COVERAGES A AND B

1. We will pay, with respect to any claim we investigate or settle, or any "suit" against an insured we defend:

a. All expenses we incur.

b. Up to $250 for cost of bail bonds required because of accidents or traffic law violations arising out of the use of any vehicle to which the Bodily Injury Liability Coverage applies. We do not have to furnish these bonds.

c. The cost of bonds to release attachments, but only for bond amounts within the applicable limit of insurance. We do not have to furnish these bonds.

d. All reasonable expenses incurred by the insured at our request to assist us in the investigation or defense of the claim or "suit", including actual loss of earnings up to $250 a day because of time off from work.

e. All costs taxed against the insured in the "suit".

f. Prejudgment interest awarded against the insured on that part of the judgment we pay. If we make an offer to pay the applicable limit of insurance, we will not pay any prejudgment interest based on that period of time after the offer.

g. All interest on the full amount of any judgment that accrues after entry of the judgment and before we have paid, offered to pay, or deposited in court the part of the judgment that is within the applicable limit of insurance.

These payments will not reduce the limits of insurance.

2. If we defend an insured against a "suit" and an indemnitee of the insured is also named as a party to the "suit", we will defend that indemnitee if all of the following conditions are met:

a. The "suit" against the indemnitee seeks damages for which the insured has assumed the liability of the

indemnitee in a contract or agreement that is an "insured contract"

b. This insurance applies to such liability assumed by the insured;

c. The obligation to defend, or the cost of the defense of, that indemnitee, has also been assumed by the insured in the same "insured contract";

d. The allegations in the "suit" and the information we know about the "occurrence" are such that no conflict appears to exist between the interests of the insured and the interests of the indemnitee;

e. The indemnitee and the insured ask us to conduct and control the defense of that indemnitee against such "suit" and agree that we can assign the same counsel to defend the insured and the indemnitee; and

f. The indemnitee:

(1) Agrees in writing to:

(a) Cooperate with us in the investigation, settlement or defense of the "suit";

(b) Immediately send us copies of any demands, notices, summonses or legal papers received in connection with the "suit";

(c) Notify any other insurer whose coverage is available to the indemnitee; and

(d) Cooperate with us with respect to coordinating other applicable insurance available to the indemnitee; and

(2) Provides us with written authorization to:

(a) Obtain records and other information related to the "suit"; and

(b) Conduct and control the defense of the indemnitee in such "suit".

So long as the above conditions are met, attorneys' fees incurred by us in the defense of that indemnitee, necessary

litigation expense incurred by us and necessary litigation expenses incurred by the indemnitee at our request will be paid as Supplementary Payments. Notwithstanding the provisions of Paragraph 2.b.(2) of Section I – Coverage A – Bodily Injury And Property Damage Liability, such payments will not be deemed to be damages for "bodily injury" and "property damage" and will not reduce the limits of insurance.

Our obligation to defend an insured's indemnitee and to pay for attorneys' fees and to pay for attorneys' fees and necessary litigation expenses as Supplementary Payments ends when:

a. We have used up the applicable limit of insurance in the payment of judgments or settlements; or

b. The conditions set forth above, or the terms of the agreement described in Paragraph f above, are no longer met.

…

SECTION IV – COMMERCIAL GENERAL LIABILITY CONDITIONS

1. Bankruptcy

Bankruptcy or insolvency of the insured or of the insured's estate will not relieve us of our obligations under this Coverage Part.

2. Duties In The Event of Occurrence, Offense Claim Or Suit

a. ***You must see to it that we are notified as soon as practicable of an "occurrence" or an offense which may result in a claim. To the extent possible, notice should include:***

(1) How, when and where the "occurrence" or offense took place;

(2) The names and addresses of any injured persons and witnesses; and

(3) The nature and location of any injury or damage arising out of the "occurrence" or offense.

b. If a claim is made or "suit" is brought against any insured, you must:

(1) Immediately record the specifics of the claim or "suit" and the date received; and

(2) Notify us as soon as practicable.

You must see to it that we receive written notice of the claim or "suit" as soon as practicable.

c. You and any other insured must:

(1) Immediately send us copies of any demands, notices, summonses or legal papers received in connection with the claim or "suit";

(2) Authorize us to obtain records and other information;

(3) Cooperate with us in the Investigation or settlement of the claim or defense against the "suit"; and

(4) Assist us, upon our request, in the enforcement of any right against any person or organization which may be liable to the insured because of injury or damage to which this insurance may also apply.

d. ***No insured will, except at that insured's own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than for first aid, without our consent.***

…

8. If the insured has rights to recover all or part of any payment we have made under this Coverage Part those rights are transferred to us. The Insured must do nothing after loss to impair them. At our request, the insured will bring "suit" or transfer those rights to us and help us enforce them.

…

SECTION V – DEFINITIONS

…

13. “Occurrence” means an accident, including continuous or repeated exposure to substantially the same general harmful conditions.

14. “Personal and advertising injury” means injury, including consequential “bodily injury” arising out of one or more of the following offenses:

a. False arrest, detention or imprisonment;

b. Malicious prosecution;

c. The wrongful eviction from, wrongful entry into or invasion of the right of private occupancy of a room, dwelling, or premises that a person occupies, committed by or on behalf of its owner landlord or lessor;

d. Oral or written publication, in any manner, of material that slanders or libels a person or organization or disparages a person’s or organization’s goods, products or services;

e. Oral or written publication in any manner of material that violates a person’s right of privacy;

f. The use of another’s advertising idea in your “advertisement”, or

g. Infringing upon another’s copyright, trade dress or slogan in your “advertisement”.

…

18. “Suit” means a civil proceeding in which damages because of “bodily injury”, “property damage” or “personal and advertising injury” to which this insurance applies are alleged. “Suit” includes:

a. An arbitration proceeding in which such damages are claimed and to which the insured must submit or does submit with our consent; or

> b. Any other alternative dispute resolution proceeding in which such damages are claimed and to which the insured submits with our consent.
>
> …

Id. (emphasis added).

Nautilus unilaterally drafted the entire Policy. The Policy's language did not indicate that Nautilus had any right to reimbursement of costs and fees if it chose to exercise its right to defend the Insureds in a legal action where a court later determined that Nautilus did not have a duty to defend.

II. SUMMARY OF THE ARGUMENTS

Nevada Public Policy and fundamental fairness support refusing to allow insurers to unilaterally change insurance contracts through reservation of rights letters.

The recent trend of states favors precluding insurers from recovering costs expended in defending uncovered claims unless the insurance policy contains an express provision allowing recoupment. Nevada should not allow insurers to amend insurance contracts unilaterally through reservation of rights letters. This rule is especially applicable when the insurance policy contains an express provision regarding policy amendments prohibiting modification through reservation of rights letters.

Standard Policy Language, including the policy at issue here, expressly state in plain and unambiguous language that insurers will bear all fees and costs incurred

in suits they defend. Nevada public policy favors construing insurance contracts to meet the reasonable expectations of the layperson, the insured, which would mean precluding recoupment actions. There can be no implicit right to reimbursement of defense costs when the policy explicitly states the insurer will bear fees and costs in cases it chooses to defend.

Nevada should adopt the default rule of the Restatement of Liability Insurance that insurers cannot seek reimbursement for fees and costs incurred in defending a suit when a court later determined there was no coverage under the policy absent an express policy provision.

III. ARGUMENT

A. Nevada Public Policy Favors Common Law Adopting the Default Rule as Detailed in the Restatement of Liability Insurance Prohibiting Recoupment Absent a Specific Policy Provision Allowing Recoupment.

1. The Duty to Defend is an Expansive Contractual Obligation Intended to Meet the Reasonable Expectations of Insureds by Helping Them Proceed Through the Litigation Process

A liability insurance policy creates a hierarchy of contractual duties. *Allstate v. Miller*, 125 Nev. 300, 309 (2009) The primary duties of an insurer are the duty to defend (*i.e.*, liability insurance) and the duty to indemnify (*i.e.*, pay claims). *Id.* This arrangement, chosen by insurers, subjects them to various consequences that stem not only from their power over insureds, but also from their ability to dictate

the insurance policy, and its language, on their terms. *Gray v. Zurich Ins. Co.*, 419 P.2d 168, 171 (Cal. 1966).

An insurance policy creates two contractual duties between the insurer and the insured: the duty to indemnify and the duty to defend. *Miller*, 125 Nev. at 309. An insurer's duty to defend is contractual in nature. *Id.* The insurer's duty to defend is, by definition "separate from and broader than the duty to indemnify. *Century Sur. Co. v. Andrew*, 124 Nev. Adv. Op 100 at 6 (citing 1 Barry R. Ostrager & Thomas R. Newman, *Handbook on Insurance Coverage Disputes* §5.02[a], at 327 (17th ed. 2015) (internal quotation marks omitted in original).

The duty to indemnify provides insureds financial protection against judgments. The duty to defend protects insureds from the financial burden of litigation. *Id.* The insured pays a premium with the expectation that insurers will defend "if facts [in a lawsuit] are alleged which if proved would give rise to the duty to indemnify." *Id.* at 7 (citing *Rockwood Ins. Co. v. Federated Capital Corp.*, 694 F. Supp. 772, 776 (D. Nev. 1988).

If there is any doubt as to whether the insurer must defend, the doubt should be resolved in the insured's favor. *United Nat'l Ins. Co. v. Frontier Ins. Co.*, 120 Nev. 678, 687 (2004). Even a failure to provide a defense under the erroneous belief there is no coverage is wrongful. *Howard v. Nat'l Fire Ins. Co.*, 115 Cal. Rptr. 3d 42, 69 (Cal. Ct. App. 2010).

The duty to defend gives the insurer the right to control litigation against the insured. *Miller*, 125 Nev. at 309. The right to control litigation creates the contractual duty to defend insureds from lawsuits that contain any allegations that fall within the scope of the policy's insurance coverage. *Id.* This Court recently clarified that an insurer cannot look to facts beyond a Complaint for justification to deny its duty to defend. *Andrew* 134 Nev. Adv. Op at 7 n.4. An insurer's duty to defend commences upon notice of a demand against the insured. *Miller*, 125 Nev. at 309.

In Nevada, an insurer has an ***absolute duty*** to defend an action brought against its insured that potentially seeks damages within the coverage of the policy, even if the claims are false, fraudulent, or unprovable. *Rockwood Ins. Co.*, 694 F. Supp. 772, 776 (D. Nev. 1988).

One of the reasons why the duty to defend is so broad is because it applies not only to claims for which an insured is likely liable but also to claims for which an insured may potentially be found liable. *Id.* The duty to defend is defined so expansively to meet the objectives and expectations of the insured. *Id.* In *Gray*, a California Court explained the duty as follows:

> When we test the instant policy by these principles, we find that its provisions as to the obligation to defend are uncertain and undefined; ***in light of the reasonable expectation of the insured, they require performance of that duty.*** At the threshold we note that the nature of the

> obligation to defend is itself uncertain. Although insurers have often insisted that the duty arises only if the insurer is bound to indemnify the insured, this very contention creates a dilemma. No one can determine whether the third party suit does or does not fall within the indemnification coverage of the policy until that suit is resolved…[.] The carrier's obligation to indemnify inevitably will not be defined until the adjudication of the very action which it should have defended. ***Hence the policy contains its own seeds of uncertainty; the insurer has held out a promise that by its very nature is ambiguous***.

Gray 419 P.2d at 173 (emphasis added).

Nevada, like California, construes insurance contracts to achieve the reasonable expectations of the insureds. *Powell v. Liberty Mut. Fire Ins. Co.*, 127 Nev. 156, 162 (2011). This interpretation derives from the fact that insurers have reserved unto themselves the exclusive power to manage and control the litigation and settle third-party claims. Insured have essentially no input into this reserved power decision-making. As such, insurers understand that insureds' reasonable expectation is that the insurer will defend even if the claim is baseless, false, or even fraudulent unless litigation is irrefutably beyond the scope of the policy. *Rockwood*, 694 F. Supp. at 776. To hold otherwise would allow insurers to profit from their superior bargaining position to the detriment of their insureds and the public. Insurers alone must face the uncertainties that arise from insurance policies they unilaterally drafted, and insurers are better equipped to deal with uncertainties by design:

> The insured is unhappily surrounded by concentric circles of uncertainty: the first, the unascertainable nature of the insurer's duty to defend; the second, the unknown effect of the provision that the insurer must defend even a groundless, false, or fraudulent claim; the third, the uncertain extent of the indemnification coverage. Since we must resolve uncertainties in favor of the insured and interpret the policy provisions according to the layman's reasonable expectations, and since the effect of the exclusionary clause is neither conspicuous, nor plain, nor clear, we hold that in the present case, the policy provides for an obligation to defend…

Gray, 419 P.2 at 174-75.

The duty to defend is of critical importance to insureds because most individuals and businesses have never been through the litigation process. Insureds look to insurers to protect their interests from the time the insured receives a demand through the completion of litigation. Insurers, in turn, protect their, and the insureds', interest by selecting competent counsel to oversee the insureds' defense throughout the litigation, approve and hire expert witnesses, and pay the costs of litigation. *Griffin Dewatering Corp. v. N. Ins. Co. of N.Y.*, 97 Cal. Rptr. 3d 568, 586 (Cal. Ct. App. 2009).

The lack of resolution regarding coverage (i.e. duty to indemnify) does not absolve an insurer of its duty to provide a defense to its insured. *United States Fire Ins. Co. v. Green Bay Packaging, Inc.*, 66 F. Supp. 2d 987, 995 (E.D. Wis. 1999). This result is justified because insurers' failure to provide a defense places the

unsophisticated insured at a significant disadvantage that can be disastrous to both the insured and insurer.

As a professional litigant with significant expertise and considerable power in litigating liability claims, liability insurers know that the scope of their duty to defend is broad. A contracting party with this level of power and sophistication does not need the benefit of a special rule allowing it to tilt the scales further and unilaterally revise the policy through a reservation of rights letter.

2. The Restatement of Liability Insurance's Recommended Default Rule

Justice Douglas cited to the Restatement of Liability Insurance when this Court clarified that an insurer could not consider facts outside the Complaint in making a determination to deny the duty to defend. *See Andrew*, 134 Nev. Adv. Op. 100 n. 4. This Court should again adopt the rule recommended by the Restatement regarding an insured's protection from a recoupment action. The Restatement provides as follows on the issue of recoupment:

> **§ 21. Insurer Recoupment of the Costs of Defense**
>
> **Unless otherwise stated in the insurance policy or otherwise agreed to by the insured, an insurer may not seek recoupment of defense costs from the insured, even when it is subsequently determined that the insurer did not have a duty to defend or pay defense costs.**

RESTATEMENT OF LIABILITY INSURANCE § 21 (Am. Law Inst., Proposed Final Draft No. 2, 2018).

The Restatement recognizes that precluding recoupment absent a specific policy provision allowing recoupment as the emerging state-court majority rule. The restatement contradicts the claim by Nautilus and *Amici Curiae* that the rule as adopted by the *Buss* court is the majority rule. *Id*. at cmt. a p. 183. The Restatement rule is there is no right to recoupment of defense costs as the default rule for insurance policies because:

> the duty to defend includes the obligation to defend the insured from all of the causes of action and remedies sought in the action, including those not covered by the liability insurance policy, the insurer has a contractual duty to defend the entire action whenever the action includes a potentially covered cause of action. Similarly, any time an insurer is defending under a reservation of rights because of a *factual* uncertainty related to a ground for contesting coverage, courts generally agree the insurer has a contractual duty to defend until that duty is terminated [through a declaratory relief action].

Id. at 182-83. The Restatement follows the emerging majority that the law precludes recoupment unless the insurer states the right in the insurance policy or is otherwise agreed to by the parties. The reasoning behind the rule, at least in part, is that the insurer should present it's desire for recoupment in a setting where the transaction costs were minimal and the parties had the time and the inclination to reach a bargain. *Id*. at 183.

The Restatement provides several bases for recoupment preclusion as the default and more sensible rule:

> First, the default rule followed in this Section would likely result in lower overall litigation costs than would the alternative rule of recoupment. For example, in cases involving covered and noncovered causes of action, under a recoupment rule there would often have to be a subsequent litigation over the question whether, or to what extent, the defense costs were incurred by the insurer in connection with noncovered causes of action. The rule followed in this Section entails no such secondary litigation. Second, because this rule is merely a default, if it turns out the recoupment rule would be relatively easy to administer or that the costs justify the expense, insurers can incorporate an express right of recoupment in their policies. Third, situating the right to recoupment in the insurance policy carries significant advantages; it puts the legal basis of the insurer's entitlement beyond dispute, and it specifies the contours of that entitlement in advance of a dispute, making it easier to evaluate for all parties concerned. Fourth, a default rule of no recoupment places the burden of contracting around the rule on the party best able to do so.

Id. at 183-84.

Nautilus' choice not to insert a recoupment provision in the policy acquires contractual significance under the Restatement's default rule. The Restatement further proffers that recognizing the insurer has made a choice not to insert a recoupment provision into the policy brings the default rule within the principle of disfavoring the use of unjust enrichment when the parties are in a position to address the issues by contract. *Id*. at 184. The risk of defending a noncovered legal action is a known uncertainty the insurer can address in the insurance contract, as is

frequently done in many other types of policies such as "Directors' and Officers' Liability Insurance policies. *Id*.

3. Sound Public Policy and Fundamental Fairness Weigh in Favor of Precluding Recoupment Absent an Express Policy Provision

Nevada construes insurance contracts to achieve the reasonable expectations of the insured. *Powell*, 127 Nev. at 162. This interpretation is necessary because insurers have reserved unto themselves the exclusive power to manage and control the litigation and settle third-party claims. Insureds, often unsophisticated and unaware of the substantial details of a complex liability insurance policy, have virtually no input into this reserved power decision-making. To allow recoupment would allow insurers to profit from their superior bargaining position to the detriment of their insureds. Therefore, insurers understand that the insureds' reasonable expectation is insureds will not face further litigation as a result of the insurers' choice to exercise their right and duty to defend the insureds in litigation should it later be determined there was no duty to defend. It would be an error to assume Access, and other insureds, did not purchase the right ***not to face a recoupment action*** when purchasing the policy.

In *Gen. Agents Ins. Co. v. Midwest Sporting Goods Co.* (hereafter "*Gainsco*"), the Illinois Supreme Court declined to follow *Buss*, embracing the position that refuses "to allow an insurer to receive reimbursement of its defense costs even

though the underlying claim was not covered by the insurance policy and the insurer had specifically reserved its right to reimbursement." 828 N.E.2d 1092, 1101 (Ill. 2005).

The *Gainsco* Court found that allowing recoupment absent an insurance policy provision authorizing it was equivalent "to allowing the insurer to extract a unilateral amendment to the insurance contract." 828 N.E.2.d at 1102 (quoting *Shoshone First Bank v. Pac. Emp'rs Ins. Co.*, 2 P.3d 510, 516 (Wyo. 2000) and *Am. States Ins. Co. v. Ridco, Inc.*, Civ. No. 95CV158D, 1996 WL 33401184, at 2 (D. Wyo. Feb. 8, 1996). An insurer cannot reserve a right not in the policy. *Gainsco*, 828 N.E.2d at 1103 (citing *First Ins. Co. v. State*, 665 P.2d 648, 654 (Haw. 1983)).

Litigation surrounding an insurer's right to reimbursement of defense costs has been active for more than twenty years. *See* 1-7 RANDY MANILOFF & JEFFREY STEMPEL, GENERAL LIABILITY INSURANCE COVERAGE: KEY ISSUES IN EVERY STATE § 7 (3d e. 2015). By way of specific example, the *Buss* decision was issued in 1997. The questions certified to this Court arises from a dispute centering around a policy issued from January 15, 2011, through January 15, 2012. Jt. App'x Vol. IV p.684. As such, Nautilus knew for more than twelve years of the potential for a suit arising against the Insureds where Nautilus would not be sure enough about its coverage decision to outright deny coverage with no risk, before issuing the policy at issue;

Nautilus had twelve years where it could have inserted a right to recoupment provision into its standard liability insurance language. Rather than proactively resolve this dispute, Nautilus now attempts to sandbag the Insureds nearly ten years after the Insureds purchased the policy with an additional policy premium of more than $500,000.

Nautilus cannot argue that the Insureds could ever have anticipated that the purchase of Nautilus' insurance policy would include an additional premium payment other than the amount expressly identified in the policy. Conversely, Nautilus and *Amici Curiae* cannot, in good faith, argue they could not have contemplated the need for a recoupment provision as part of its standard liability policy language because recoupment provisions are expressly included in other liability policies issued. Specifically, Directors and Officers Standard Liability Policies often include a specific recoupment provision allowing the insurer not only the right to control the defense of the litigation but also to recoup costs related to defending a suit later determined not to be covered by the policy.

4. Other Courts Precluding Recoupment

As detailed above, the majority of States recently making a recoupment determination have adopted the Restatement's default rule and rejected an insurer's recoupment claims.

a. State Courts

Texas was the first state to reject recoupment in 2000. *See Cf. Tex. Ass'n of Countie Cnty. Gov't Risk Mgmt. Pool v. Matagorda Cnty.*, 52 S.W. 3d 128, 131 (Tex. 2000) (refusing to permit recoupment of settlement costs, stating that a "unilateral reservation-of-rights letter cannot create rights not contained in the insurance policy").

In 2005, Illinois rejected *Gainsco*'s recoupment claim as detailed throughout this brief. 828 N.E.2d at 1097. ("[insurer's] reservation of rights letter could only reserve the rights contained within the insurance policy and could not create new rights.").

In 2008, Arkansas rejected the insurers recoupment efforts in *Med. Liab. Mut. Ins. Co. v. Alan Curtis Enters. Inc.* 285 S.W.3d 233, 237 (Ark. 2008) ("[W]ithout statutory or rule authority allowing for such, an insurer may not recoup attorney's fees under a unilateral reservation of rights.").

In 2010, Pennsylvania's Supreme Court rejected the recoupment right the insurer tried to preserve through a reservation of rights letter. *See Am. & Foreign Ins. Co. v. Jerry's Sport Ctr., Inc.*, 2 A.3d 526, 546 (Pa. 2010) ("We therefore hold that an insurer may not obtain reimbursement of defense costs for a claim for which a court later determines there was no duty to defend, even where the insurer

attempted to a claim a right to reimbursement in a series of reservation of rights letters.")

In 2013, Washington precluded recoupment of defense costs expended while the insurer's duty to defend was uncertain pre-litigation. *See Nat'l Sur. Corp. v. Immunex Corp.*, 297 P.3d 688, 695 (Wash. 2013) ("[I]nsurers may not seek to recoup defense costs incurred under a reservation of rights defense while the insurer's duty to defend is uncertain.").

Alaska rejected recoupment even when the policy contained a recoupment provision. *See Attorneys Liab. Prot. Soc'y, Inc. v. Ingaldson Fitzgerald, P.C.*, 370 P.3d 1101 (Alaska 2016) (holding that the Alaska independent-counsel statute means that an insurer cannot obtain recoupment for defense costs even if the insurance policy contains a recoupment provision).

In 2017, the Massachusetts' Superior Court rejected recoupment relying upon the rationale of the *Jerry's Sport* court. *See Holyoke Mut. Ins. Co. in Salem v. Vibram USA, Inc.*, NO. SUCV20152321BLS1, 2017 WL 1336600, at *5 (Mass. Super. Ct. Mar. 21, 2017) (discussing law nationwide and concluding "the Pennsylvania Supreme Court's decision in *Jerry's* comports with Massachusetts law").

b. Erie Rejections of Recoupment

Multiple Federal District Courts have made Erie predictions that a state would reject recoupment absent an express provision allowing it within the policy. *See*

> *Westchester Fire Ins. Co. v. Wallerich*, 563 F.3d 702, 719 (8th Cir. 2009) (applying Minnesota law) ("Here, [insurer] could have included in the policy an express provision for such reimbursement. [Insurer] cannot now unilaterally amend the policy by including the right to reimbursement in its reservation-of-rights letter."); *Perdue Farms, Inc. v. Travelers Cas. & Sur. Co. of Am.*, 448 F.3d 252, 259 (4th Cir. 2006) (applying Maryland law) (noting that "[a] partial right to reimbursement of defense costs would … undermine the bargain that Maryland courts describe insurers reaching with their insureds…[and] would significantly tip the scales in favor of the insurer"); *Evanston Ins. Co. v. Bosski, Inc.*, No. 1:14-cv-0022'7-EJL, 2017 WL 1158245 (D. Idaho Mar. 28, 2017) (following Idaho-law prediction of three prior district-court opinions); *James River Ins. Co. v. Arlington Pebble Creek, LLC*, 188 F. Supp. 3d 1246 (N.D. Fla. 2016) (predicting Alabama law); *Great Am. Assurance Co. v. PCR Venture of Phoenix LLC*, 161 F. Supp. 3d 778, 788 (D. Ariz. 2015) (predicting Arizona law, not acknowledging contrary prediction made in *Phillips & Assocs, P.C. v. Navigators Ins. Co.*, 764 F. Supp.2d 1178 (D. Ariz. 2011)); *Gen. Star Indem. Co. v. Driven Sports, Inc.*, 80 F. Supp. 3d 442, 460 (E.D.N.Y. 2015) (predicting New York law, acknowledging earlier, contrary predictions and a contrary decision by intermediate appellate court in New York and explaining why they are unpersuasive); *Pekin Ins. Co. v. Tysa, Inc.*, No. 3:05-cv-00030-JEG, 2006 WL 3827232, at *19 (S.D. Iowa Dec. 27, 2006) (predicting Iowa law).

RESTATEMENT OF LIABILITY INSURANCE § 21 p. 188.

B. Standard Liability Policy Language, Including the Provisions of the Nautilus Policy Do Not Comport with Recoupment.

1. Insurers are Bound by a Special Relationship of Confidence and Trust with Their Insureds

The State of Nevada heavily regulates the insurance industry because it is an important ***public trust.*** *Ainsworth v. Combined Ins. Co.*, 104 Nev. 587, 592 (1988) (emphasis added). The important role insurance plays in society serves as the requisite foundation for an insurer's relationship with an insured to be one of special confidence. *Id*. at 592, 676.

Insurance contracts are unlike ordinary bilateral contracts. *Goodson v. Am. Std. Ins. Co.*, 89 P.3d 409, 414 (Colo. 2004). Insureds enter into insurance contracts for financial security obtained by protecting themselves from unforeseen calamities and for peace of mind, rather than to secure a commercial advantage. *Id.* This Court has recognized this special relationship between an insurer and insured as being akin to a fiduciary relationship. *Powers v. United Servs. Auto Ass'n.*, 114 Nev. 690, 700 (1998). The nature of this relationship requires that the insurer adequately protect the insureds' interests and requires the insurer to equally consider the insureds' interests to its own in decision-making. *Miller*, 125 Nev. at 311. Insureds always remain the more vulnerable party because of the inequality in, not only bargaining power but also sophistication:

> It is a matter of almost common knowledge that a very small percentage of policy holders are actually cognizant

> of the provisions of their policies and many of them are ignorant of the names of the companies issuing said policies. The policies are prepared by the experts of the companies, they are highly technical in their phraseology, they are complicated and voluminous and in their numerous conditions and stipulations furnishing what may be veritable traps for the unwary.

United States Fid. & Guar. Co. v. Ferguson, 698 So.2d 77, 81 (Miss. 1997).

Liability insurers are in the business of managing risks, and they promise to provide litigation insurance against the costs of those risks. *Elliot v. Donahue*, 485 N.W.2d 403, 407 (Wis. 1992). As Justice Douglas recently stated, "The duty to defend is a valuable service paid for by the insured and ***one of the principal benefits of the liability insurance policy.***" *Andrew*, 134 Nev. Adv. Op. at 7 (citing *Woo v. Fireman's Fund Ins. Co.*, 164P.3d 454, 459-60 (Wash. 2007)). Individuals and businesses contract to purchase liability insurance policies to secure the insurers' sophistication to navigate the uncertainties of litigation. Indeed, litigation insurance is a primary reason individuals and businesses buy insurance,

> The insured's desire to secure the right to call on the insurer's superior resources for the defense of third-party claims is, in all likelihood, typically as significant a motive for the purchase of insurance as is the wish to obtain indemnity for possible liability.

Montrose Chem. Corp. v. Superior Ct., 861 P.2d 1153, 1157 (Cal. 1993).

The Insureds purchased the Policy with the expectation that Nautilus' expertise included the ability to evaluate coverage under the policy in the event a "suit" occurred. Nautilus could not make a determination with certainty as to

whether the Underlying Action invoked the "duty to indemnify." So, Nautilus invoked its right to defend the Underlying Action, protect itself from the Insureds self-defending the suit, and seek declaratory guidance as to the potential duty to indemnify. After having reaped all the benefits it bargained for, Nautilus now seeks to reap additional benefits while diminishing the benefits the Insureds thought they had procured when purchasing the policy.

2. The Contractual Relationship Between Insurer and Insured is One of Unequal Bargaining Power

This Court has recognized that liability insurance companies hold tremendous power over insureds because they draft insurance policies without providing an opportunity to negotiate the terms. *Benchmark Ins. Co. v. Sparks*, 122 Nev. 407, 412 (2011). Liability insurance companies present these policies to their insured on a "take it or leave it" basis. *Farmers Ins. Exch. v. Young*, 108 Nev. 328, 334 (1992). This is the defining trait that makes an insurance policy a contract of adhesion. *Frontier Ins. Co.*, 120 Nev. at 684. The adhesive nature of the insurance policy is primarily why this Court has interpreted policies broadly to afford the greatest possible coverage and protection to Nevada insurance consumers. *Id.*

Given the unequal bargaining power between insured and insurer, this Court has repeatedly approached the construction of liability insurance policies with a keen eye towards equalizing this imbalance. Any ruling that allows insurers to extract additional rights from this unequal bargaining power would be a significant

departure from Nevada's jurisprudence construing liability insurance policies fairly to protect Nevada insurance consumers.

3. Nevada Insurance Contracts are Interpreted Strictly with Ambiguities Resolved in Favor of the Insured

"An insurance policy is a contract between a policyholder and an insurer which the policyholder agrees to pay premiums in exchange for financial protection from foreseeable, yet preventable events." *Sparks*, 127 Nev. at 422 (citing New Appleman Insurance Law Practice Guide §1.03). In Nevada, the courts treat insurance policies like other contracts and thus, legal principles applicable to contracts generally are applicable to insurance policies. *Andrew* 134 Nev. Adv. Op. at 5 (citing *Century Sur. Co. v. Casino W., Inc.*, 130 Nev. 395, 398 (2014); *Frontier Ins. Co.*, 120 Nev. at 684; *Farmers Ins. Exch. v. Neal*, 119 Nev. 62, 64 (2003).

Specifically, any ***ambiguity or uncertainty*** as to an obligation in an insurance policy must be construed against the insurer and in favor of the insured. *Vitale v. Jefferson Ins. Co.*, 116 Nev. 590, 594 (2000). As the insurer is the drafter of an insurance policy and thus can limit its contractual obligations, any ambiguities in a policy of insurance are "interpreted against the insurer and in favor of the insured. *Frontier Ins. Co.*, 120 Nev. at 123. Construing any uncertainty in an insurance policy against the insurer is appropriate because the insurer is in a "… superior bargaining position to the insured." *United Rentals Highway Techs. Inc. v. Wells Cargo, Inc.*, 1128 Nev. 666, 677 (2012).

In *Sparks*, the liability insurance policy contained an ambiguous provision regarding the termination of the insurer's duty to defend upon the exhaustion of its liability limits. *Sparks*, 127 Nev. At 414. This Court affirmed the trial court's denial of the insurance company's motion for summary judgment that it no longer had a duty to defend its insured once it deposited the policy's limits with the trial court. *Id*. at 411. This Court reasoned that the exhaustion provision was ambiguous, as the insureds reasonably expected that the insurer would continue to provide him with a legal defense until the indemnity limit procured a settlement or satisfied a judgment. *Id*. at 254.

4. Recoupment Contravenes the Plain Language of the Nautilus Policy

In Nevada, contracts are construed from the written language and enforced as written. *Ellison v. Cal. State Auto. Ass'n*, 106 Nev. 601 (1990). Where a contract is clear, the court must construe the document from its language. *S. Trust Mortg. Co. v. K& B Door Co., Inc.*, 104 Nev. 564 (1988). Here, under the plain terms of the Policy, Nautilus expressly promised to bear all defense costs for claims and suits it defends. The promise remains whether Nautilus' choice to defend a suit arises because the duty to do so is evident or the question of coverage is close enough such that it would be dangerous to refuse to defend.

The Policy provides in pertinent part as follows:

SUPPLEMENTARY PAYMENTS – COVERAGES A AND B

1. ***We will pay, with respect to*** any claim we investigate or settle, or ***any "suit" against an insured we defend***:

a. All expenses we incur.

...

d. All reasonable expenses incurred by the insured at our request to assist us in the investigation or defense of the claim or "suit", including actual loss of earnings up to $250 a day because of time off from work.

e. All costs taxed against the insured in the "suit".

…

These payments will not reduce the limits of insurance.

2. ***If we defend an insured against a "suit"*** and an indemnitee of the insured is also named as a party to the "suit", we will defend that indemnitee if all of the following conditions are met:

a. The "suit" against the indemnitee seeks damages for which the insured has assumed the liability of the indemnitee in a contract or agreement that is an "insured contract"

b. This insurance applies to such liability assumed by the insured;

…

So long as the above conditions are met, attorneys' fees incurred by us in the defense of that indemnitee, necessary litigation expense incurred by us and necessary litigation expenses incurred by the indemnitee at our request will be paid as Supplementary Payments. Notwithstanding the provisions of Paragraph 2.b.(2) of Section I – Coverage A – Bodily Injury And Property Damage Liability, such payments will not be deemed to be damages for "bodily injury" and "property damage" and will not reduce the limits of insurance.

Our obligation to defend an insured's indemnitee and to pay for attorneys' fees and to pay for attorneys' fees and necessary litigation expenses as Supplementary Payments ends when:

a. We have used up the applicable limit of insurance in the payment of judgments or settlements; or

> ***b. The conditions set forth above, or the terms of the agreement described in Paragraph f above, are no longer met.***

Jt. App'x, Vol. IV p.696 – 97. There can be no dispute that the Policy expressly and unambiguously promises Nautilus will pay all expenses it occurs in connection with **any suit it chooses to defend**.

This Court should hold where a policy contains the "Supplementary Payments" clause contained within the Policy, if the insurer defends it must bear the costs of defense under the express terms of the policy. This Court has consistently bound insurers to the express terms of the insurance policy. This Court should not reverse course and allow insurers to contravene the supplementary payments clause's express promise to bear the cost of defending a suit.

Other Courts have rejected the *Buss* holding by looking to the policy language to determine if recoupment is expressly allowed. As detailed above, in *Gainsco*, the Illinois Supreme Court declined to allow an insurer to receive reimbursement of its defense costs even though the underlying claim was found to be not covered by insurance policy and the insurer had attempted to reserve a right to reimbursement. 828 N.E.2,d 1092, 1101 (Ill. 2005). In *Emp'rs Cass. Co. v. Indus. Rubber Prods., Inc.*, a federal district court found Minnesota law does not allow an insurer "reimbursement of defense costs expended prior to the determination of coverage, unless specifically provided for in the policy. No. Civ. 04-3839, 2006 WL 453207

9d. Minn. Feb. 23, 2006);*see also L.A. Weight Loss Ctrs., Inc. v. Lexington Ins. Co.*, 2006 WL 689109 (Pa. Ct. C.P.Phildelphia County Ct. Mar. 1, 2006) (a reservation of rights letter does not create a contract but rather is a means to assert defense and exclusions which the policy already contains).

While these courts found a lack of policy language supporting a right to recoupment as a basis to deny the *Buss* holding, here permitting Nautilus to recoup its attorneys' fees and litigation costs would violate the express provisions of the "Supplementary Payments" clause. The "Supplementary Payments" provision of the Policy is inconsistent with the allocation of defense costs to an insured.

The instant facts and circumstances are entirely distinguishable from the *Buss* case and its progeny, as the *Buss* court decided that a right of recoupment could be implied from the policy's basic terms. The *Buss* court could not have properly implied a right of allocation and reimbursement directly conflicting the policy's express promise that the insurer would bear all defense costs. This Court should find the promise to bear all expenses in suits defended by Nautilus precludes the right of recoupment created through implication by the *Buss* court.

Here, the policy not only expressly promises that Nautilus will bear the cost of all suits it chooses to defend, but also expressly prohibits the Insureds from paying for their own defense while retaining the possibility of reimbursement from Nautilus.

In addition to the "Supplementary Payments" provision, the Nautilus Policy contains the following language regarding Access' duties in the event of a lawsuit:

> 2. Duties In The Event of Occurrence, Offense Claim Or Suit
>
> a. You must see to it that we are notified as soon as practicable of an "occurrence" or an offense which may result in a claim. To the extent possible, notice should include:
>
> (1) How, when and where the "occurrence" or offense took place;
>
> (2) The names and addresses of any injured persons and witnesses; and
>
> (3) The nature and location of any injury or damage arising out of the "occurrence" or offense.
>
> b. If a claim is made or "suit" is brought against any insured, you must:
>
> (1) Immediately record the specifics of the claim or "suit" and the date received; and
>
> (2) Notify us as soon as practicable.
>
> You must see to it that we receive written notice of the claim or "suit" as soon as practicable.
>
> c. You and any other insured must:
>
> (1) Immediately send us copies of any demands, notices, summonses or legal papers received in connection with the claim or "suit";
>
> (2) Authorize us to obtain records and other information;
>
> (3) Cooperate with us in the Investigation or settlement of the claim or defense against the "suit"; and
>
> (4) Assist us, upon our request, in the enforcement of any right against any person or organization which may be liable to the insured because of injury or damage to which this insurance may also apply.
>
> d. ***No insured will, except at that insured's own cost, voluntarily make a payment, assume any obligation,***

> ***or incur any expense, other than for first aid, without our consent.***

Jt. App'x Vol. IV p. 699 (emphasis added). Pursuant to the Nautilus policy, the Insureds could not incur any expense relating to their own defense in the underlying suit without Nautilus' consent unless they intended to forego the ability to recover those expenses. Allowing recoupment would contravene not only the plain language of the policy but also the rules of fundamental fairness considering Access could not pay its own attorneys' fees and seek repayment from Nautilus without consent under the policy.

C. Nevada's Public Policy Favors a Common Law that Furthers the Insurer/Insured Confidential Relationship and Stands for the Principal that Consumer's Purchase Insurance for Peace of Mind. This Court Should Preclude a Unilateral Amendment to the Policy Through a Reservation of Rights Letter and Reject the Position Expounded by the Buss Court

1. A Reservation of Rights Letter Can Only Preserve Rights Already Provided by the Policy

It is "well settled that an action based on an implied-in-fact or quasi-contract cannot lie where there exists between the parties a valid express contract covering the same subject matter." *Morawski v. Lightstorm Entm't, Inc.*, 559 F.App'x 779, 780 (9th Cir. 2015) (cert denied) (internal citations omitted). This Court has held, "[s]uch a claim is not available when there is an express, written contract, because no agreement can be implied when there is express agreement." *Leasepartners*

Corp. v. Robert L. Brooks Trust Dated Nov. 12, 1975, 942 P.2d 182, 187 (Nev. 1997).

This Court has never held that a unilateral reservation of rights letter can change the terms of an insurance policy. This Court should find that a reservation of rights letter can only reserve rights already expressly provided for by the policy. Several other courts have held a unilateral reservation of rights letter cannot assert rights not contained within the insurance policy itself. *Jerry's Sport Ctr. Inc.*, 2 A.3d at 539. *See Shoshone First Bank*, 2 P.3d at 510 (Wyo. 2000); *Excess Underwriters at Lloyd's, London v. Frank's Casing Crew & Rental Tools, Inc.*, 246 S.W.3d 42 (Tex. 2008). The rationale behind this holding is "an insurer benefits unfairly if it can hedge on its defense obligations by reserving its right to reimbursement while potentially controlling the defense and avoiding a bad faith claim." *Jerry's Sport Ctr. Inc.*, 2 A.3d at 539 (citing *Excess Underwriters*, 246 S.W.3d at 68).

This Court should reject Nautilus' unilateral attempt to modify the policy through a reservation of rights and reject recoupment absent a new contract arising through Nautilus' reservation of rights letters. The Policy provides in pertinent part as follows:

> B. Changes
>
> This policy contains all the agreements between you and us concerning the insurance afforded. The first Named Insured shown in the Declarations is authorized to make changes to the terms of this policy with our consent. ***This***

> ***policy's terms can be amended or waived only by endorsement issued by us and made a part of this policy.***

Jt. App'x Vol. IV p. 687 (emphasis added).

Here, the policy outlines a binary choice for the insurer when a potential duty to defend arises. If the insurer determines the claim is potentially covered, it "has the right and duty to defend the insured" in that suit. *Id.* at 690. If the insurer determines the claim is not even potentially covered, then the insurer has "no duty to defend the insured." *Id.* The policy makes clear that "no other obligation [to] performs acts or services is covered…." *Id.* Thus, the policy governs how Nautilus may respond to claims and its related rights, and the mere fact that a court made a no-coverage determination does not allow Nautilus to depart from other contractual provisions.

Because the insurance contract did not authorize a defense subject to a reservation of rights, Nautilus could not reserve that right through unilateral correspondence. If Nautilus desired this contractual benefit, it should have bargained for it. Nautilus did not. Instead, it sought to unilaterally seize the benefit by asserting its alleged rights in an informal letter, a modification procedure expressly prohibited by the contract. This Court should reject Nautilus' attempt to retroactively modify the insurance contract because a reservation of rights letter does not comply with the modification procedures expressly detailed in the contract.

Multiple courts have consistently held that an insurer is not entitled to reimbursement of defense costs for non-covered claims because courts have been unwilling to grant insurers a substantial rebate on their duty to defend." *Perdue Farms, Inc. v. Travelers Cas. & Sur. Co. of Am.*, 448 F.3d 252, 259 (4th Cir. 2006); *Immunex Corp.*, 297 P.3d at 694 (holding that an insurer defending under a reservation of rights may not require reimbursement of defense costs if a court ultimately declares no coverage exists because it creates an impermissible "all reward, no risk" proposition that renders the defense portion of a reservation of rights defense illusory); *Jerry's Sport Cit. Inc.*, 2 A.3d at 539(the insurer was not entitled to reimbursement of defense costs due to a unilateral reservation of rights letter, which could not create rights not contained in the policy itself).

The rationale for courts' precluding an insurer from recouping defense costs from its insureds in these instances is as follows:

> ***It is the insurer that decides whether to defend (with or without a reservation of rights) before any judicial determination of coverage. Providing a defense benefits the insurer by giving it the ability to monitor the defense and better limit its exposures.*** When an insurer defends under a reservation of rights, it insulates itself from potential claims of breach and bad faith, which can lead to significant damages, including coverage by estoppel. In turn, the insured receives the benefit of a defense until a court declares none is owed. Conversely when an insurer declines to defend altogether, it saves money on legal fees but assumes the risk it may have breached its duty to defend or committed bad faith.

Immunex Corp., 297 P.3d at 693-94 (footnote and citations omitted). Moreover, if an insurer "were allowed to recover defense costs, it's 'offer' to defend would serve solely to protect itself from claims of breach while placing the full risk of a determination of noncoverage on its insured. ***This provides no security to the insured.***" *Id*. at 686 (emphasis added).

The Cases relied upon by Nautilus do not stand for the proposition that Nevada upholds the legitimacy of unilateral reservation of rights letters from the insurer to insured, as asserted in Nautilus' brief. *See*; Nautilus' Brief at p. 6-8. Nautilus cites of *Havas v. Atl. Ins. Co.*, *Las Vegas Metro. Police Dept. v. Coregis Ins. Co.*, and *NGA # 2 Ltd. Liab. Co. v. Rains*. *Id.* None of these cases support Nautilus' assertion for unilaterally allowing an insurer to make material revisions to the policy through a reservation of rights letter. *Havas* has nothing to do with reservation of rights letters at all but instead addresses the issue of whether an insurer waived its untimely notification defense when it agreed to investigate the claim if the insured signed a non-waiver release; this Court found there was no waiver because of the release signed by the insured. *Havas v. Atl. Ins. Co.*, 96 Nev. 586 (1980).

Las Vegas Metro. Police Dept. v. Coregis Ins. Co. had nothing to do with reservation of rights and the same is not discussed or mentioned throughout the case. Rather, this Court found that an insurer raising an untimely notice defense was

required to show it had suffered prejudice from the untimely notice of a claim. 127 Nev. 548 (2011).

Similarly, *NGA #2* was not a case about a reservation of rights letter, but rather about whether one party to a contract was estopped from terminating a contract that did not close by the stated close of escrow date when he continued to participate in the efforts to effectuate the contract's terms. 113 Nev. 1151 (1997).

2. Precluding Recoupment Does Not Unjustly Enrich Insureds Like Access but Unjustly Enriches Insurers Where, as Here, The Insurer Has the Right to Defend a Questionable Case

An insurer who chooses to defend a questionable coverage case receives substantial benefits from exercising that choice. This Court's recent decision in *Andrew* demonstrates that the insurer avoids the risk of enhanced liability in the event of a default resulting from no defense. However, the benefits conferred to an insurer defending a questionable coverage case go beyond avoiding the risk of enhanced liability. These benefits include maintaining control over the cost, quality and direction of the defense. By way of specific example, during the case underlying this dispute Nautilus changed defense counsel on multiple occasions because it was unhappy with the defense provided. In addition to control of the litigation, insurers obtain access to privileged defense-related litigation materials and get to participate in settlement discussions.

The fallacy of unjust enrichment to insureds from receiving defense for uncovered claims arises from the self-assuming conclusion that the only contractual rights for the insured are indemnity and defense. The unjust enrichment fallacy falls apart with just a slight shift in perspective; if the insured bargained for the insurers' expertise in being able to determine coverage questions, then the defense costs are nothing more than the consequential result of the insurers' inability to meet the expectation of definitive coverage evaluation.

The briefing of Nautilus and *Amici Curiae* inaccurately proffer defense solely as a duty under the policy; whereas, the policy provides that Nautilus has the right and duty to defend cases where the possibility of triggering the duty to indemnify exists. Jt. App'x. Vol IV p. 690. Nautilus has "no duty to defend the insured against any "suit" seeking damages for "bodily injury" or "property damage" to which this insurance does not apply." *Id*. However, Nautilus has "the ***right and duty to defend*** the insured against any "suit" seeking [damages which trigger Nautilus' duty to indemnify…[and] ***may, at [Nautilus'] discretion, investigate any "occurrence" and settle and claim or "suit" that may result.***" *Id*. (emphasis added).

Here, Nautilus had three choices: (1) to accept coverage and defend the case; (2) to deny coverage and deny the duty to defend or indemnify were triggered and face the uncertain consequences of an adverse finding that there was coverage; or (3) exercise its right to defend the case, receive the benefits of controlling the

litigation and being kept in the loop of potential exposure, and seek certainty on the issue of coverage. Nautilus chose option three and received substantial benefit from defending the case. Nautilus now seeks to receive additional unjust enrichment in the form of recouping defense costs.

For a thorough discussion of the benefits conferred to insurers who defend a suit rather than risking being wrong on a coverage decision, *see* KENNETH S. ABRAHAM & DANIEL SCHWARCZ, INSURANCE LAW AND REGULATION 584-586 (6th ed. 2015). Professors Schwarcz and Abraham identify the following benefits conferred to insureds:

> (a) the insurer can defer its determination of coverage issues, thus avoiding being estopped to deny its indemnity obligation if it later turns out that it did have a duty to defend;
>
> (b) the insurer can control defense expenditures;
>
> (c) the insurer can ensure the claim is effectively defended, thus minimizing its potential indemnity exposure;
>
> (d) the insurer can participate in, and perhaps control, settlement negotiations; and
>
> (e) the insurer gains access to otherwise-privileged communications.

Id.

The fallacy of unjust enrichment to the insured assumes that whenever litigation arises, an insured would be in a position to hire competent defense counsel to defend the suit. The more logical assumption is that more often than not, an

insured would not be able to hire any defense counsel absent the insurer exercising its right to defend the litigation and the insured and insurer would be bound by ineffective assistance of counsel or no counsel at all.

By way of specific example, in the *Andrew* case, the insured defaulted, and the insurer faced a judgment exceeding the policy limits by a factor of nearly twenty. Insurers defend close coverage cases to protect themselves. Insurers reap the overwhelming benefit of defending a close coverage case and should not be allowed to further tip the scales of bargaining power in their favor through recoupment.

Nautilus and *Amici Curiae* rely upon the RESTATEMENT THIRD, RESTITUTION AND UNJUST ENRICHMENT ("R3RUE") to support arguing insureds are unjustly enriched when courts preclude recoupment. The R3RUE expresses a general approach that allows an insurer that defends or settles a wholly noncovered legal action could be understood to confer benefits beyond the scope of its obligation and permits an obligor to seek restitution. The Restatement of Liability Insurance proffers that the R3RUE approach lacks a fundamental understanding of special considerations of insurance law. RESTATEMENT OF LIABILITY INSURANCE p.185.

IV. CONCLUSION

For the reasons set forth above, Respondents respectfully request that this Court conclude, in response to the Ninth Circuit's certified question of law, that absent an express provision in the policy an insurer cannot reserve a right to

reimbursement and cannot seek recoupment of fees and costs paid in defending litigation even if a court later determined there was no duty to defend the underlying lawsuit.

DATED this 22 day of January 2020.

BY: s/Jordan P. Schnitzer, Esq.
JORDAN P. SCHNITZER, ESQ.
Nevada Bar No. 10744
THE SCHNITZER LAW FIRM
9205 W. Russell Road, Suite 240
Las Vegas, Nevada 89148
Attorney for Respondents

CERTIFICATE OF COMPLIANCE

1. I hereby 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 this brief has been prepared in a proportionally spaced typeface using Microsoft Word in 14-point Times New Roman font.

2. I further certify that this brief complies with the type-volume limitations of NRAP 32(a)(7)(A) because, excluding the parts of the brief exempted by NRAP 32(a)(7)(c), it contains fewer than 12,000 words (9,980).

3. I hereby certify that I have read this 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 Nevada Rules of Appellate Procedure, in particular NRAP 28€(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.

4. I understand I may be subject to sanctions in the event the accompanying brief is not in conformity with the requirement of the NRAP.

DATED this 22 day of January 2020.

BY: s/Jordan P. Schnitzer, Esq.
JORDAN P. SCHNITZER, ESQ.

Nevada Bar No. 10744
THE SCHNITZER LAW FIRM
9205 W. Russell Road, Suite 240
Las Vegas, Nevada 89148
Attorney for Respondents

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I am an employee of The Schnitzer Law Firm and on the 22nd day of January, 2020, a true and correct copy of the above and foregoing document was filed electronically and e-served on all registered parties to the Supreme Court's electronic filing system and by United States First-Class mail to all parties as listed below:

Gil Glancz
Linda Wendell Hsu
Selman Breitman, LLP
3993 Howard Hughes Parkway, Suite 200
Las Vegas, Nevada 89169
Telephone: 702.228.7717
Attorneys for Appellant

James E. Harper
Taylor G. Selim
Harper Selim
1707 Village Center Circle, Suite 140
Las Vegas, Nevada 89134
Telephone: 702.228.7717
Attorneys for Flournoy Management Company, LLLC

s/ Melisa Gabhart
_____
Melisa Gabhart
An Employee of The Schnitzer Law Firm