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S211645

IN THE SUPREME COURT OF CALIFORNIA

HARTFORD CASUALTY INSURANCE COMPANY,
Defendant, Cross-Complainant, and Appellant,

vs.

J.R. MARKETING, LLC, *et al.*,
Plaintiffs, Cross-Defendants, and Respondents.

After a Decision By the Court of Appeal, First Appellate District, Division Three Case No. A133750 (Following an Order by the Trial Court, San Francisco County Superior Court, Judge Loretta Giorgi, Case No. CGC-06449220)

RESPONDENTS' ANSWER TO PETITION FOR REVIEW

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and Proposed Cross-Defendants and Respondents
SQUIRE SANDERS (US) LLP and SCOTT HARRINGTON

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I. INTRODUCTION

In its Petition for Review, Hartford fails to identify ***any*** split of authority in California on the question that it invites this Court to accept: whether an insurer that breaches its duty to defend can directly sue ***independent counsel*** over disputed legal fees. To the contrary, California law is clear that an insurer's remedy, if any, is against its ***insured.*** And while Hartford insists that the issue here "is likely to recur frequently," such predictions are exaggerated, to say the least, given that it cites no similar authority in the history of California jurisprudence.

Hartford does its best to mask the reason why this case is unique—in virtually all other instances, the insurer complies with the requirements of Civil Code Section 2860, which provides an insurer protection and remedies relating to legal fees. Here, despite employing a number of euphemisms about the "unavailability" of Section 2860, Hartford could not seek the protection of that statute because Hartford had repeatedly breached its duty to defend its insureds—a fact affirmed in prior appeals and that is now the law of the case. Indeed, Hartford's breach was instrumental to the appellate decision that it asks this Court to review, and yet Hartford refuses to admit (or even reveal to this Court) that it did, in fact, breach its duty. Hartford's refusal to acknowledge that fact reflects its misunderstanding of why the appellate court reached the result that it did.

For all of the public policy discussion contained in Hartford's Petition, conspicuously absent is any rationalization for why California law would want to reward a party that breached its duty to defend, affording it greater rights than insurers that actually comply with their duty. Hartford's position simply cannot be squared with Section 2860 or the policy underlying that statute.

An excellent illustration is Hartford's attempt to seek refuge in this Court's decision in *Buss*. Despite Hartford's efforts to contort the holding

in that case, *Buss* lends no support to Hartford's proposition that a breaching insurer should be able to directly sue independent counsel over legal fees. To the contrary, *Buss* took pains to emphasize the narrowness of its holding concerning an insurer's ability to seek reimbursement of defense costs, and specifically limited reimbursement to a claim against the ***insured.*** *Buss* also did not consider the effects of a breaching insurer, so it is certainly not a springboard for creating new rights heretofore unrecognized by any California court.

This case arises against a unique factual backdrop and complicated procedural history, which appropriately prompted the court of appeal to note that its holding was "quite limited." As a result, particularly in light of there being no split of authority, this Court should deny Hartford's Petition.

II. RELEVANT FACTS AND PROCEDURAL HISTORY

Hartford asks this Court to review the appellate court's decision, and yet its Petition systematically omits and obscures the facts on which that decision was based. Most notably, Hartford never acknowledges the fact that it repeatedly breached its duty to defend its insureds. Hartford instead turns a blind eye to an entire phase of the proceedings below in its Statement of the Case, and resorts to a series of carefully-worded phrases designed to avoid any reference to its breaches.

This case has a tortured procedural history that involves three trips to the court of appeal.[1] That court, duly cognizant of Hartford's repeated misconduct and efforts to avoid its obligations to its insureds, understood

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[1] (*See J.R. Marketing, L.L.C., et al. v. Hartford Casualty Ins. Co.* (Oct. 30. 207, A115472) [nonpub. opn.] (affirming denial of Hartford's motion to disqualify Squire Sanders); *J.R. Marketing, L.L.C., et al. v. Hartford Casualty Ins. Co.* (Nov. 30, 2007, A115846) [nonpub. opn.] (affirming order finding Hartford breached its duty to defend and forfeited the protections of Section 2860); *Hartford Casualty Ins. Co. v. J.R. Marketing, L.L.C., et al.* (May 17, 2013, A13375) 216 Cal.App.4th 1444 (affirming dismissal of Hartford's claims against Squire Sanders).)

what Hartford was trying to orchestrate by directly suing independent counsel over legal fees. As a result, to properly understand Hartford's present Petition, it is likewise necessary to review at least part of the complicated history of the case, all of which reinforces that this case is unsuitable for this Court's review.

A. Hartford Denies Coverage, Forcing Its Insureds To Hire Independent Counsel.

In July and August of 2005, Hartford issued policies to the insureds, and in September of that year the insureds were sued by Meir Avganim and others in Marin County Superior Court (the "Marin Lawsuit"). (Court of Appeal 5/17/2013 Decision ("Decision") at 2-3). The insureds immediately tendered the defense of the Marin Lawsuit to Hartford. (*Ibid.*)

From September 2005 to January 2006, Hartford did not provide any response to the insureds' request for coverage. As a result, the insureds hired their own attorneys to represent them in the Marin Litigation and to pursue coverage from Hartford (eventually, Squire Sanders (US) LLP).

When Hartford finally responded, it denied coverage on the basis that, among other things, the claims in the Marin Litigation arose prior to the policy period. (Appellant's Appendix ("AA"), Vol. 1 at 060 (top).) The insureds provided Hartford with additional information demonstrating that the claims arose during the policy period, but to no avail. (*Ibid.*)

B. The Insureds Sue Hartford, But Hartford Still Refuses To Provide A Complete Defense.

Faced with Hartford's refusal to provide coverage for the Marin Lawsuit, the insureds sued Hartford in February 2006 for breach of contract and bad faith. (*Supra.*) In response, Hartford eventually offered to "defend" its insureds under a reservation of rights, but even that offer proved illusory because: (1) Hartford refused to pay defense fees incurred before January 2006; and (2) Hartford required the insureds to transfer the

defense to Hartford's panel counsel—despite the fact that Hartford's reservation of rights created a conflict of interest that entitled the insureds to retain independent counsel. (*Ibid.*) In fact, Hartford threatened that any failure to transfer the defense from Squire Sanders would result in "forfeiture by the Insured of any policy benefits." (2 AA at 351).

C. Hartford Defies The Trial Court's Order To Defend Its Insureds.

Because of Hartford's continued refusal to provide a complete defense, the insureds moved in April 2006 for summary adjudication of Hartford's duty to defend and their right to independent counsel. In July 2006, the trial court granted the insureds' motion in full, finding that: (1) Hartford's duty to defend arose upon the insureds' tender of the claim in September 2005; and (2) that Hartford was required to allow the insureds to select their own counsel and Hartford was obligated to pay that counsel's fees. (1 AA at 060.)

Hartford ignored the trial court's July order. Not only did Hartford still refuse to pay defense fees prior to January 2006, Hartford refused to recognize or pay for its insureds' independent counsel—Squire Sanders. (*Supra* at 003:10–004:7, 075-077). Hartford instead maintained that its panel counsel continued to control the insureds' defense. (*Id.* at 077, n.11).

D. When The Insureds Seek To Enforce Hartford's Duty To Defend, Hartford Moves To Disqualify Squire Sanders.

In the face of Hartford's refusal to comply with the trial court's order, the insureds filed a motion in August 2006 to enforce Hartford's duty to defend. In its opposition to that motion, Hartford maintained, among other things, that it need not pay any fees because Squire Sanders should be disqualified from both the Marin Lawsuit and the coverage action against Hartford. (Respondents' Appendix ("RA") at 13-17; *see also* 1 AA at 161:20-25 and n.4).

Then, on August 16, 2006, the day before the court's tentative ruling on the enforcement motion was due, Hartford moved to disqualify Squire Sanders. (1 AA at 182 and 148, *et seq.*) As a result, the trial court was forced to put off the hearing on the insureds' enforcement motion—further delaying any relief for the insureds.

E. The Trial Court Finds That Hartford Repeatedly Breached Its Duty To Defend And Sought Disqualification For Disingenuous Reasons.

The trial court held a hearing on the enforcement and disqualification motions on September 14, 2006. It denied Hartford's motion to disqualify Squire Sanders, finding the motion premised on a "disingenuous argument." (*Supra* at 105:3-5.) Hartford requested a stay of the court's decision so that it could file an immediate appeal. (*Id.* at 111:1-116:19). The trial court, however, denied the stay request, noting Hartford's ongoing refusal to pay defense costs, even after the July summary adjudication order. (*Id.* at 140:14-18.)

The trial court then entered an order on September 27, 2006 granting the insureds' motion to enforce Hartford's duty to defend. In its Order, the court again found that Hartford had repeatedly breached its duty to defend: "by (1) failing to pay all reasonable and necessary defense costs incurred by the insured and by (2) failing to provide *Cumis* counsel." (*Supra* at 003:10-14.)

F. The Trial Court Holds That Hartford Forfeited Its Rights Under Section 2860 By Breaching Its Duty To Defend.

As part of its September 27 order, the trial court also held that "Hartford is [ ] not permitted to take advantage of section 2860, which is designed to protect insurers that honor their obligations of providing (and paying for) independent counsel." (*Supra.*)

California Civil Code Section 2860 generally governs the relationship between an insurer and independent (so-called "*Cumis*") counsel. Section 2860(a) provides that when a conflict of interest arises between the insurer and insured (such as when the insurer agrees to defend under a reservation of rights) the insured has a right to select independent counsel. In those circumstances, independent counsel represents only the ***insured***—not the insurer—and independent counsel has only limited duties to the insurer, such as providing certain non-privileged information. (*See* Civ. Code § 2860(d).)

Section 2860 also provides protections for the insurer, including the ability to require minimum qualifications for independent counsel, limitations on the rates paid to independent counsel, and the right to arbitrate "[a]ny dispute concerning attorney's fees." (Civ. Code § 2860(c).) These protections, however, are only available to an insurer that honors its obligations and fulfills its duty to defend, subject to a reservation of rights. (*Truck Ins. Exchange v. Superior Court* (1996) 51 Cal.App.4th 985, 998; *Atmel Corp. v. St. Paul Fire & Marine* (N.D. Cal. 2005) 426 F.Supp.2d 1039, 1047.)

Therefore, in light of Hartford's repeated breaches of its duty to defend, the trial court found that Hartford was not entitled to the protections of Section 2860, including the limitations on rates and the right to arbitrate fee disputes.

G. The Court Of Appeal Affirms The Enforcement And Disqualification Orders.

Hartford appealed the trial court's decisions on the enforcement and disqualification motions. In affirming both decisions, the court of appeal recognized the legal implications of Hartford's misconduct.

First, in affirming the trial court's enforcement order, the Court found that Hartford had "failed to timely pay all reasonable and necessary

defense costs incurred by respondents and had failed to provide independent counsel." (1 AA at 077). The court underscored these facts, stating that, while Hartford had paid several invoices, Hartford "failed to pay ***all*** outstanding bills ***in full*** . . . [and] failed to provide and pay for independent counsel for respondents following issuance of the order. Indeed, the evidence shows that, as of August 8, 2006, Hartford's panel counsel still understood itself to be lead defense counsel in the *Avganim* matter." (*Id.* at 077, n.11 (emphasis in original)).

Second, the court of appeal affirmed the trial court's denial of Hartford's disqualification motion. In doing so, the appellate court noted that Harford had likely brought that motion "for tactical reasons," as part of its effort to avoid paying independent counsel's fees. (*Supra* at 182 and 077 n.11).

The court of appeal considered all of Hartford's arguments on both issues, and soundly (and unanimously) rejected them.

H. Hartford Moves To Dissolve The Enforcement Order.

Unwilling to accept the court of appeal's decision, Hartford moved to "dissolve" the enforcement order in February 2010. Hartford argued that under Section 2860 it was entitled to arbitrate the defense fees incurred and hourly rates charged by its insureds' independent counsel. (*Supra* at 239:25-28.) In support of its argument, Hartford cited *Long v. Century Indem. Co.*, but as Respondents pointed out, *Long* did not apply where the insurer breaches its duty to defend. (2 AA at 325:10-328:5).

While Hartford's motion was pending, the court of appeal issued a decision confirming the inapplicability of *Long* in the face of an insurer's breach of the duty to defend. (*Intergulf Development LLC v. Superior Court* (2010) 183 Cal.App.4th 16, 21.) The trial court therefore denied Hartford's motion to dissolve the enforcement order. Hartford again

appealed the trial court's ruling (2 AA at 491), but later abandoned its appeal.

I. Hartford Brings A Direct Claim Against Squire Sanders, Which The Trial Court Dismisses.

Despite the length of the proceedings in the underlying Marin Lawsuit, Hartford waited until February 2011 to attempt to amend its cross-complaint to assert a claim against Squire Sanders (finally amending in July 2011).[2] (*Supra* at 502.) Respondents demurred to Hartford's claim against Squire Sanders, arguing (among other things) that Hartford could not seek rescission of the policy from non-insureds or reimbursement from non-insureds. (1 AA at 021, *et seq.*)

The trial court sustained the demurrer without leave to amend. In doing so, the trial court emphasized the importance of the "the legal analysis and policy considerations, protecting the integrity of the attorney-client relationship between the insured and their counsel . . . ." (2 AA at 430.)

J. The Court Of Appeal Unanimously Affirms The Trial Court's Dismissal Of Hartford's Direct Claim Against Squire Sanders.

Hartford appealed the trial court's decision and attempted to persuade the court of appeal that it has a common-law right to seek reimbursement of attorney's fees directly from the independent counsel hired by its insureds.[3] The court of appeal rejected Hartford's argument

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[2] Hartford also brought a reimbursement claim against another non-insured, Scott Harrington. The trial court dismissed that claim, and Hartford has abandoned any appeal regarding that claim. As such, it is not addressed further in this Answer.

[3] While Hartford's claim against Squire Sanders was on appeal, the trial court proceeded with the first phase of the remaining claims, including the insureds' breach of contract claim against Hartford. On December 12,

and found that such a claim was inconsistent with: (1) California law governing the relationship of insurer, insured, and independent counsel; and (2) California law governing the consequences of an insurer's breach of its duty to defend.

First, the court of appeal focused on Section 2860. As noted above, Section 2860 specifies the rights and responsibilities of an insurer with respect to independent counsel and provides protections to the insurer regarding fees. (*See* Decision at 9.) The appellate court emphasized, however, that "these protective rules come with an important caveat," and that in order to take advantage of the protections of Section 2860, the insurer had to fully accept the defense of its insureds under a reservation of rights. (*Id.* at 9-10.) If the insurer breaches its duty to defend, "the insurer forfeits the protections of section 2860, including its statutory limitations on independent counsel's fee rates and resolution of fee disputes." (*Ibid.*)

The court also looked beyond Section 2860 and found that California law imposes serious consequences on an insurer's breach of its duty to defend. In particular, the court noted that when an insurer breaches its duty to defend it "loses all right to control the defense," including "the right to control financial decisions such as the rate paid to independent counsel or the cost-effectiveness of any particular defense tactic or approach." (*Supra* at 13). The court was duly concerned about a breaching insurer's effort to control or manage litigation despite the existence of a conflict of interest necessitating independent counsel.

The appellate court ruled that Hartford's attempt to sue Squire Sanders was foreclosed by this settled law. Allowing such a claim would impermissibly allow a breaching insurer to "[r]etroactively impos[e] the insurer's choice of fee arrangement for the defense of the insured by means

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2012, the jury awarded damages to the insureds for Hartford's breach. (December 12, 2012 Rough Draft Trial Transcript at 2:9-24.)

of a post-resolution quasi-contractual suit for reimbursement against the insured's separate counsel." (*Supra* at 13.) Such a claim would also be inconsistent with Section 2860 because it "would effectively afford the insurer that has waived the protections of section 2860 through its own wrongdoing ***more*** rights in a fee dispute with independent counsel than the insurer that has not waived such protections." (*Id.* at 14 (emphasis added).) The appellate court concluded that "[t]he law does not sanction this inequitable result," (*ibid.*), and that "[t]here simply is no legal basis here for the restitution claim that Hartford has asserted against Squire." (*Id.* at 15.)

As such, the fact that Hartford breached its duty to defend—the precise fact that Hartford does its best to avoid mentioning in its Petition—greatly influenced the court of appeal's decision. That fact was not only critical to the court's ultimate holding, but the court also noted that due to Hartford's misconduct and the specific type of claim it attempted to bring, the scope of its decision was "quite limited." (*Supra.*) The court therefore declined to consider other potential circumstances in which an insurer might be able to bring a claim directly against independent counsel. (*Ibid.*)

It is this "quite limited" holding—turning on specific facts that Hartford fails to disclose—that Hartford now asks this Court to review.

III. LEGAL ARGUMENT

Hartford devotes the bulk of its Petition arguing the merits of its appeal, effectively dancing around the question of whether the decision below warrants this Court's review at all. That is because Hartford does not have much to say on this score—it cannot identify any split of authority and instead only presents a question of application of settled law to a unique factual scenario. Such matters do not warrant this Court's intervention.

A. There Is No Conflict In The Law Warranting This Court's Review.

This Court generally does not exercise jurisdiction except when "necessary to secure uniformity of decision or to settle an important question of law." (Cal. Rules of Court, rule 8.500(b)(1).) Yet in the few paragraphs that Hartford devotes to arguing why this Court should hear this case, Hartford does not even attempt to argue that the appellate court's decision creates any conflict in the law—nor could Hartford plausibly do so. Hartford does not cite a single case in its entire Petition in which an insurer that breached its duty to defend was permitted to bring a claim directly against its insured's independent counsel for reimbursement of allegedly "unnecessary or unreasonable" fees. As such, there is no conflict that might necessitate review by this Court.

B. Hartford Does Not Present Any Important Question Of Law.

Recognizing that there is no conflict in the law warranting this Court's review, Hartford instead seeks to portray the issues in the appellate court's decision as presenting an "important question of law." But there is no important legal question in the appellate court's "quite limited" decision—only the application of settled law to the facts of this case.

1. The Issue Hartford Proposes Is Not Likely To Recur Because It Can Only Arise In Limited Factual Circumstances.

As a cornerstone to its Petition, Hartford posits that the reimbursement issue it presents for this Court's review is important because it "is likely to recur frequently." (Petition at 4.) That notion is broadly dispelled by the fact that Hartford fails to identify—in the nearly thirty years since *Cumis* was handed down—***any*** other California cases where its argument was raised (much less endorsed). The lack of any other caselaw

illustrates the fallacy of Hartford's contention that this case presents an issue likely to recur.

It is not surprising that Hartford identifies no other case addressing this issue because the new type of reimbursement claim that Hartford seeks to fashion can only arise in the specific constellation of facts that exist in this case. Specifically, Hartford's new reimbursement claim can—by definition—only arise where ***all*** of the following occur:

(1) an insurer breaches duty to defend and thereby forfeits the protections of Section 2860;

(2) the insureds separately hire independent counsel;

(3) the insurer is ordered to pay independent counsel's fees on an ongoing basis (rather than the insured waiting until after the underlying litigation concludes to recover the fees it has incurred, through a coverage action or otherwise);

(4) the insurer seeks to recover fees that were allegedly "unnecessary or unreasonable" to the insured's defense (as opposed to fees incurred on non-covered claims or fees arising out of fraudulent billing practices); and

(5) the insurer seeks to recover such fees directly from independent counsel (as opposed to the insured).

Even where these factual prerequisites happen to align, the odds of the issue in Hartford's Petition arising are further diminished if any potential fee disputes happen to be wrapped up in a "global" settlement of the underlying litigation. Finally, few insurers would be brazen enough to bring a reimbursement claim that so clearly runs afoul of *Buss*, which as discussed further below narrowly defined the right to reimbursement as

arising ***only*** against the insured and ***only*** for claims that are not potentially covered by the policy. All of this explains why Hartford cannot identify any other relevant cases besides this one.

Indeed, the only support Hartford offers for its assertion that the issues in this case are likely to recur is a footnote reference to the handful of third-party requests for publication of the appellate court's opinion. (*See* Petition at 4 n.1.) Those requests, however, reinforce the rarity of the circumstances in this case. All but one of the requests were submitted by ***insureds*** who were frustrated with insurers' escalating attempts to delay and avoid their duties to defend. They sought publication of the appellate court's decision because it reinforced the longstanding California law that an insurer who breaches its duty to defend loses the right to select independent counsel and to control its defense strategy.[4] As such, the circumstances that could potentially give rise to the issue that Hartford asks this Court to review are indeed "quite limited" as the appellate court recognized, and unlikely to recur frequently.

2. The Appellate Court's Application Of Settled Law Does Not Warrant This Court's Review.

The appellate court recognized that this case did not blaze any new legal trails—it was simply an example of an insurer trying to escape the consequences of breaching its duty to defend. The court applied settled California law regarding the consequences of an insurer's breach to the facts of this case, and concluded that Hartford could not bring a reimbursement claim against Squire Sanders. That application, which

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[4] With respect to the sole request for publication submitted by an attorney, Hartford's Petition omits a telling fact. That attorney was sued in federal court by an insurer for reimbursement of fees, and the court dismissed the claim as unauthorized under California law. (*See* Exhibits to Newmeyer & Dillion's June 4, 2013 Request for Publication.)

Hartford largely elects to disregard in its Petition, does not present any important issue warranting this Court's review.

The appellate court began its analysis by surveying California law regarding the consequences of an insurer's breach of its duty to defend. It noted, for example, that a breaching insurer waives the protections of Section 2860, which includes limitations on hourly rates and the right to arbitrate disputes regarding the amount of fees. (Decision at 9-10, 13-14.) It also discussed the principle that an insurer who breaches its duty to defend "loses all right to control the defense, including, necessarily, the right to control financial decisions such as the rate paid to independent counsel or the cost-effectiveness of any particular defense tactic or approach." (*Id.* at 13; *see also id.* at 14 ("[I]t is clear California law bars an insurer, like Hartford, in breach of its duty to defend from thereafter imposing on its insured its own choice of defense counsel, fee arrangement or strategy.").)

In light of this settled law and the indisputable fact that Hartford breached its duty to defend, the appellate court ruled that Hartford could not sue Squire Sanders to recover fees that it claimed were "unreasonable or unnecessary" to the insureds' defense. First, the appellate court determined that such a claim would improperly allow a breaching insurer to retroactively control the insureds' defense. (*Supra* at 13.) As the court noted, it was the insureds—not Hartford—who hired Squire Sanders and had the right to choose how to defend against the claims in the Marin Litigation:

> Recall Hartford, an insurer in breach of its duty to defend, chose not to align its interests with the insured cross-defendants for purposes of the Marin defense and thereby forfeited all right to control that defense. Placed in this position, ***cross-defendants, not Hartford, hired Squire as independent counsel to represent their***

> ***interests in the defense, negotiated the relevant fee arrangement with Squire, and oversaw all matters of defense strategy including, presumably, deciding with Squire the cost/benefit of various litigation pursuits.*** It is within this context that Hartford claims the legal right to bring a reimbursement action against Squire for allegedly charging excessive, unreasonable or unnecessary fees for their provision of legal services in the name of cross-defendants' defense. We think not.

(*Id.* at 13-14 (emphasis added).)

Indeed, the specific complaints Hartford raises about Squire Sanders' fees substantiate the appellate court's concern. Among other things, Hartford protests that Squire Sanders should not have filed certain motions, pursued certain discovery measures, conducted certain legal research, or had certain attorneys working on the matter.[5] As the appellate court observed, California law does not allow a breaching insurer to control and second-guess independent counsel's decisions in these ways while litigation is underway—much less after the fact through a claim for reimbursement. To hold otherwise would essentially require counsel to seek advance approval from the insurer for certain litigation decisions, effectively placing counsel in an untenable position if its client directs the action but the insurer balks.

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[5] In its Motion for Judicial Notice, Hartford asks the Court to consider the trial court's June 24, 2013 Statement of Decision, in which it held that Hartford was entitled to reimbursement of approximately $5 million from the insureds. The insureds filed extensive objections to that Statement of Decision and moved the court to reconsider or vacate its decision. (*See* July 23, 2013 Respondents' Response to Hartford's Motion for Judicial Notice.) That matter is now subject to the insureds' objections, and if necessary, an appeal. But regardless of how those proceedings unfold, they illustrate the peril of allowing a breaching insurer to complain about the implementation of basic litigation strategy and management years after the fact.

Second, the appellate court ruled that Hartford's reimbursement claim "would effectively afford the insurer that has waived the protections of section 2860 through its own wrongdoing ***more*** rights in a fee dispute with independent counsel than the insurer that has not waived such protections'" including the right to sue independent counsel in court rather than arbitrate any fee disputes. (*Id.* at 14.) Section 2860 also provides certain protection concerning counsel's hourly rate, which breaching insurers should not be able to obtain through the backdoor by criticizing hourly rates of independent counsel (as Hartford seeks to do here).

Hartford does not, and cannot, dispute the well-settled law regarding an insurer's breach of its duty to defend that formed the legal basis for the decision that it now asks this Court to review. Instead, Hartford goes to great lengths to avoid this issue. On nearly every page of its Petition, Hartford engages in linguistic gymnastics and uses a conspicuously passive voice to avoid referring to the reason ***why*** the protections of Section 2860 did not apply in this case. (*See, e.g.*, Petition at 1 ("Where an insurer ***has been denied*** the protection of Civil Code section 2860 . . . ."); *id.* at 2 ("The Court of Appeal held in a published opinion that . . . the provisions of Civil Code section 2860 regulating independent *Cumis* counsel ***do not apply*** . . . ."); *id.* at 2-3 (". . . whether the restitutionary principles in *Buss* apply only to insureds, and not to *Cumis* counsel, when the statutory protection of ***section 2860 is unavailable.***") (emphases added)). The fact that Hartford cannot even be candid about its breach is a reflection on how instrumental that breach was to the outcome below.

3. Hartford's Reliance On *Buss* Does Not Create Any Important Issue Of Law.

Hartford tries to pique the Court's interest by citing to its decision in *Buss v. Superior Ct.* (1997) 16 Cal.4th 35, and arguing that the Petition presents "an issue that *Buss* implicitly decided but has not directly

addressed." (Petition at 2.) But Hartford's argument in this regard rests on a serious distortion of *Buss*.

In *Buss*, this Court held that an insurer may "seek reimbursement from ***the insured***" for fees related to claims "that are not even potentially covered." (16 Cal.4th at 49-50 (emphasis added).) And even with respect to such actions, this Court appreciated that the insurer must "accomplish a task that, if ever feasible, may be extremely difficult." (*Id.* at 58 (internal quotations omitted).) The Court further appreciated that insurers would only bring such claims in "exceptional" circumstances "where the defense costs the insurer may obtain in reimbursement are clear and substantial *and* where the assets ***the insured*** has available for reimbursement are themselves of the same sort." (*Id.* (first emphasis in original, second added).)

Hartford's assertion that this Court "implicitly" decided that insurers could bring direct actions against independent counsel for allegedly "unnecessary and unreasonable" fees thus finds no support in the actual words this Court used in *Buss*. The Court was careful to define the right of reimbursement of fees on uncovered claims as available only against ***the insured***, and to describe how limited it is. In doing so, the Court explicitly insulated independent counsel from the effects of reimbursement claims, noting that reimbursement would not undermine the insured's defense because "[t]he insured's counsel remains free to represent the insured as he sees fits, ***subject only to generally applicable legal provisions and professional standards***." (*Supra* at 58 (emphasis added).) Hartford seeks to expand *Buss* far beyond its narrow confines, which explains its inability to locate any other California cases validating its proffered interpretation of *Buss*.

Furthermore, the Court explicitly reserved judgment on how an insurer's breach of its duty to defend would impact the right of

reimbursement, because "[w]hether such a rule is sound is a question for another day, when we are faced with an insurer that has so misconducted itself." (*Supra* at 60 n.25.) In that regard, it is notable that the Court based the right of reimbursement, in part, on the need to encourage insurers to fulfill their duty to defend. (*Id.* at 52 ("Without a right of reimbursement, an insurer might be tempted to refuse to defend an action in any part . . . .").) But Hartford's proposed reimbursement claim against independent counsel would actually encourage insurers to ***ignore*** their obligations, knowing they could always second-guess independent counsel's defense after the underlying litigation concludes. *Buss* in no way supports such a result, and the irony of a breaching insurer looking to *Buss* to expand its legal remedies seems lost on Hartford.

Hartford goes further astray by asserting that it has a "quasi-contractual" relationship with Squire Sanders and therefore has a right to seek reimbursement directly from the law firm. (*See, e.g.*, Petition at 10 ("The inapplicability of section 2860 does not and should not limit the common law and equitable claims that arise from an insurer's quasi-contractual relationship with *Cumis* counsel.").) But the Court in *Buss* made it clear that it is the ***insured*** that has "quasi-contractual" relationship with the insurer, potentially giving rise to a claim of reimbursement "from the ***insured***." (16 Cal.4th at 39-40.) Squire Sanders has absolutely no relationship with Hartford, either factual or legal. As the appellate court recognized, it was the insureds—not Hartford—that independently hired Squire Sanders after Hartford refused to honor its duty to defend. (Decision at 13-14.)

Moreover, it bears emphasizing that California law provides that *Cumis* counsel owes no duties to the insurer apart from the statutory duties contained in Section 2860 (and those only apply in situations, unlike the present one, where the insurer does not breach its duties). (*See, e.g., Truck*

Ins. Exchange v. Superior Court (1996) 51 Cal.App.4th 985, 998; *Assurance Co. of America v. Haven* (1995) 32 Cal.App.4th 78 (rejecting insurer's action against independent counsel beyond the reporting requirements in section 2860).)

For this reason, a long line of cases has strictly prohibited insurers from bringing claims directly against independent counsel. (*See, e.g., Unigard Ins. Group v. O'Flaherty & Belgum* (1995) 38 Cal.App.4th 1229, 1235 (limiting insurer's ability to sue independent counsel for malpractice to situations where "the interests of the insurer and insured are not in conflict"); *Jackson v. Rogers & Wells* (1989) 210 Cal.App.3d 336 (prohibiting assignment to insurer of malpractice claim for allegedly excessive attorney's fees); *Assurance Co. of America v. Haven* (1995) 32 Cal.App.4th 78, 92 (prohibiting insurer's attempted malpractice claims against independent counsel); *Employers Insurance of Wausau v. Albert D. Seeno Constr. Co.* (N.D. Cal. 1988) 692 F.Supp. 1150 (prohibiting insurer from suing independent counsel for alleged ethical violations).)

In the same vein, Hartford's attempt to directly sue Squire Sanders also ignores the fact that the legal standards that apply to a fee claim between insurer and insured are not the same as those that apply to a fee claim between attorney and client. While fees in the insured-insurer relationship are typically governed by the terms of the insurance policy, the attorney-client relationship is governed by the California Rules of Professional Conduct, which prohibit an attorney from charging an "illegal or unconscionable fee" (unless the contract between attorney and client provides for a different, ethical fee standard). (Rule 4-200(A).) Hartford's attempt to sue Squire Sanders for allegedly "unreasonable or unnecessary" fees seeks to impose liability under insurance law standards that simply do not apply to Squire Sanders' relationship with its clients.

Moreover, even if Hartford tried to limit its claim to reimbursement of fees that violated Rule 4-200, Hartford would still be prohibited from bringing such a claim. California law is clear that ***only the client*** can sue an attorney for a violation of its ethical obligations—a third party cannot be permitted to intrude into the attorney-client relationship even if the client does not object. (*See, e.g., Jackson v. Rogers & Wells* (1989) 210 Cal.App.3d 336 (prohibiting assignment to insurer of malpractice claim for allegedly excessive attorney's fees).) Hartford is not Squire Sanders' client and is, in fact, adverse to Squire Sanders' clients in virtually every way possible. There is simply no legal basis under California law for an adverse, non-client such as Hartford to sue independent counsel for allegedly improper fees, and Hartford's effort to collapse two very different types of fee claims into one obliterates the vital distinctions between them.

Therefore, it is hardly surprising that this Court in *Buss* limited reimbursement to situations where the insurer could proceed against the insured. To hold otherwise would create a heretofore unrecognized duty between *Cumis* counsel and the breaching insurer, and it would contravene this settled body of law.

4. Hartford's Appeal To Equity Or Public Policy Presents No Important Issue Of Law.

Hartford spends the remainder of its Petition trying to knit together equitable or policy reasons for justifying a direct suit against *Cumis* counsel. Hartford's appeal to equity strains credulity and Hartford's policy-based arguments ignore the policy implications described by the court of appeal.

First, Hartford has no right to appeal to equity—Hartford breached its duty to defend, and in order to appeal to equity a litigant must ***do*** equity. (*See Dool v. First Nat'l Bank* (1929) 207 Cal. 347, 352.) Likewise, as the appellate court observed, a claim for reimbursement will only lie where it would be ***unjust*** to allow a party to retain a benefit. (Decision at 12.) Here,

California enacted a statute that specifically provides a remedy for Hartford's complaints—but only if the insurer has honored its duty to defend. Hartford offers no explanation why the law of equity should intervene to provide such a remedy when it disavowed its duty to defend.

Second, Hartford incorrectly argues that it would be unfair to hold an insured responsible for reimbursing for any "unreasonable or unnecessary" fees. (Petition at 2-3; *see also* Motion for Judicial Notice.) Putting aside the perverse irony of Hartford expressing concern over the supposed unfairness to the insureds who it abandoned, Hartford's real concern is not for the insureds but rather for itself, and the possibility that if the insureds cannot satisfy a reimbursement judgment Hartford will be left "holding the bag." But that is simply a risk that the breaching insurer assumes when it forsakes its duty to defend its insured and forfeits its rights and remedies under section 2860. Equity will not intervene to protect a breaching insurer from the consequences of its breach.

A third error in Hartford's line of equitable and policy-based arguments is its theory that allowing an insurer to bring a claim directly against independent counsel furthers judicial economy. Hartford's theory starts from the notion that (1) an insurer can bring a claim against its insured for "unreasonable or unnecessary" fees, and (2) its insured can bring an action against independent counsel for such fees. Hartford then suggests that it would be more efficient to allow the insurer to bring a claim directly against independent counsel (thereby bypassing the insured).

But Hartford acknowledges that there is actually no added efficiency because—under its view of the law—an insurer's direct action against independent counsel would likely be followed by an action between counsel and the insured. (Hartford Appellate Reply Br. at 11 (explaining that if Hartford were to recover against Squire Sanders, then "Squire Sanders may have a claim for reimbursement against the insureds for fees

that Squire Sanders believes the insureds should be required to pay").) In either scenario, therefore, the potential exists for two separate proceedings, so the notion that judicial economy would be furthered by Hartford's position rings hollow.

Not only does Hartford's proposed reimbursement claim fail to offer any added efficiency, but it also has serious legal flaws. As noted above, the legal standards governing a fee dispute between insurer and insured are different than in an attorney-client fee dispute. Thus, the two claims cannot simply be collapsed into one.

Hartford's proposal also creates serious concerns regarding the attorney-client privilege, while unfairly constraining the defense of *Cumis* counsel. Assume, for instance, than an insurer brings a direct action against *Cumis* counsel, second-guessing litigation strategy and staffing decisions (as Hartford desires to do here). Part of *Cumis* counsel's defense may well be that the client instructed counsel to take the challenged actions. But such communications would be shielded by the privilege, which counsel does not have the ability to waive. As a result, the direct action by the insurer would materially prejudice counsel's defense because it would not be able to fully explain its actions without risking a privilege waiver. If, however, the insurer recovered against the insured, and then the insured decided to sue counsel, counsel could rely on such communications as part of its defense. (*See* California Evid. Code § 958 (privilege inapplicable "as to a communication relevant to an issue of breach, by the lawyer or by the client, of a duty arising out of the lawyer-client relationship"); *Carlson, Collins, Gordon & Bold v. Banducci* (1967) 257 Cal.App.2d 212, 227-228 (finding privilege inapplicable under § 958 in fee dispute).) The result ordained by the court of appeal is therefore the only way to fully protect the privilege.

The equity and policy arguments advanced by Hartford therefore do not warrant review. To the contrary, they highlight why this Court should not intervene to protect a breaching insurer from the legal consequences of its breach.

IV. CONCLUSION

For the reasons stated above, Respondents respectfully request that the Court deny Hartford's Petition for Review.

Dated: July 31, 2013

Respectfully submitted,

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CERTIFICATE OF WORD COUNT

Pursuant to California Rules of Court, rule 8.204(c), I certify that this Answer contains 6,723 words as counted by the Microsoft Word 2010 word-processing program used to prepare this brief.

Dated: July 31, 2013

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Hartford Casualty Insurance Company v. J.R. Marketing, LLC, et al.
Supreme Court of the State of California
Case No. S211645

PROOF OF SERVICE

I am a citizen of the United States and employed in San Francisco County, California. I am over the age of eighteen years and not a party to the within-entitled action. My business address is 275 Battery Street, Suite 2600, San Francisco, California 94111.

On July 31, 2013, a copy of the following document:

RESPONDENTS' ANSWER TO PETITION FOR REVIEW

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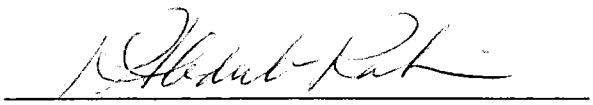

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