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SUPREME COURT
OF THE STATE OF WASHINGTON

SEATTLE TUNNEL PARTNERS,
WASHINGTON STATE DEPARTMENT OF TRANSPORTATION,
and HITACHI ZOSEN U.S.A.,

Petitioners,

vs.

GREAT LAKES REINSURANCE (UK) PLC,
a foreign insurance company, et al.,

Respondents.

AMICUS CURIAE MEMORANDUM OF VULCAN LLC

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I. ARGUMENT

A. The Court of Appeals Confused the Distinct Property Insurance Concepts of "Loss" and "Damage." Unless Corrected, the Decision Will Have Profound Consequences for Washington Policyholders.

The insuring agreement construed by the Court of Appeals provides: "Insurers will indemnify the Insured in respect of direct physical loss, damage *or* destruction … not specifically excluded herein." Despite the use of the disjunctive "or" separating "loss" from "damage," the Court of Appeals concluded the "plain language of the Policy does not provide coverage for loss of use of the tunnel." It continued:

> Washington case law shows that if a policy provides coverage for "physical" loss, it does not provide coverage for loss of use unless that loss of use arises out of or as a result of the physical loss.

COA Opinion at 22.

There are myriad problems with this conclusion. *First*, it relies on two cases concerning the duty to defend homeowners sued by their neighbors for obstructing scenic views. How

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these small *liability* cases bear on a multi-million dollar *property* insurance loss is a mystery.

Second, it overlooks Washington property insurance precedent distinguishing "loss" from "damage." In *Nautilus Grp., Inc. v. Allianz Glob. Risks US*, 2012 WL 760940 (W.D. Wash. Mar. 8, 2012), the director of the insured's Shanghai branch refused to return certain items following his termination. *Id.* at *2-3. The insured sought business interruption coverage, which was available if it suffered "direct physical loss or damage to Insured Property." The insurer argued coverage was not triggered unless the property was "physically altered." *See id.* at *6-7. The court rejected this argument, ruling that "physical loss" is distinct from "damage":

> [I]f "physical loss" was interpreted to mean "damage," then one or the other would be superfluous. The fact that they are both included in the grant of coverage evidences an understanding that ***physical loss means something other than damage.***

Id. at *7 (emphasis added). Under *Nautilus*, (i) "physical loss" does not require physical alteration or perceptible damage to

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property, and (ii) even a temporary deprivation of the ability to use property can constitute "physical loss."

Third, the Court of Appeals should have engaged in the policy interpretation exercise called for by Supreme Court precedent. Both "physical" and "loss" are undefined in the policy. They must thus be interpreted "as [they] would be understood by the average lay person." *Boeing Co. v. Aetna Cas. & Sur. Co.*, 113 Wn.2d 869, 876 (1990). The "plain, ordinary, and popular meanings" of "physical" and "loss" include loss of use of property for its intended purpose. *Id.* ("To determine the ordinary meaning of an undefined term, our courts look to standard English language dictionaries."). "Physical" means "having material existence: perceptible especially through the senses and subject to the laws of nature." *Physical*, MERRIAM-WEBSTER, https://www.merriam-webster.com/dictionary/physical (last visited November 15, 2021). "Loss" means "the act of losing possession: deprivation." *Id.*, *Loss*. "Loss" thus includes "the state of

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being kept from … using something." *Id.*, *Deprivation*. It follows that property suffers "physical loss" when an insured is deprived of the ability to use it for its primary function.

Keeping the distinction between "loss" and "damage" alive is critical for Washington policyholders. There are several ways in which property can suffer "loss" (and cannot be used for its intended purpose) without suffering tangible damage or alteration, including from odors, airborne chemicals, smoke, bacteria, blockades by protestors, civil authority shutdowns, and on and on. In each case, an insured property may not have suffered tangible "damage," yet the property itself suffered "loss" by being rendered uninhabitable or economically useless.

The Supreme Court should accept review because the Court of Appeals' ruling has implications for every business that purchases property and business interruption insurance and suffers physical "loss" but not physical "damage."

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B. The Holding That a Mechanical Breakdown Exclusion Precludes Coverage for Design Defects Imperils Coverage for All Washington Policyholders.

The Court of Appeals concluded that the following unintelligible exclusion excludes coverage for design defects:

> Loss of or Damage in respect any item by its own explosion mechanical or electrical breakdown, failure breakage or derangement.

The rationale was that: (i) some persuasive authority from sister jurisdictions "appears consistent" with the notion that machinery breakdown exclusions preclude recovery for damage caused by "internal causes," (ii) a "design defect" is an internal cause, hence (iii) the machinery breakdown exclusion "excludes coverage for design defects." This expansive interpretation of an exclusion imperils coverage for Washington policyholders.

1. The Court of Appeals' Decision Runs Afoul of Longstanding Rules of Policy Construction

The Supreme Court has set forth several foundational principles of Washington insurance law. For decades these principles have served as guideposts for policyholders and insurers alike. The Court of Appeals' decision inexplicably

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departs from several of these principles. The result is that (i) insurers get exclusions they did not include in their policies and (ii) Washington policyholders lose coverage they paid for. Policyholders pay thousands—and, in Vulcan's case, millions—of dollars in premiums with the reasonable expectation that the policy (i) means what it says and nothing more, and (ii) any uncertainty in what the policy says will be resolved in favor of coverage. Unless the Supreme Court accepts review, these settled expectations will be recast to the detriment of all policyholders.

a. Exclusions Must be Narrowly Construed

Exclusions "are contrary to the fundamental protective purpose of insurance" and are "not extend[ed] … beyond their clear and unequivocal meaning." *Vision One LLC v. Philadelphia Indem. Ins. Co.*, 174 Wn.2d 501, 512 (2012); *Int'l Marine Underwriters v. ABCD Marine, LLC*, 179 Wn.2d 274, 288 (2013) ("Exclusionary clauses are narrowly construed for the purpose of providing maximum coverage for the insured.");

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Stuart v. Am. States Ins. Co., 134 Wn.2d 814, 819 (1998) ("Exclusions should also be strictly construed against the insurer."). These and a litany of other Supreme Court decisions leave no doubt that an exclusion must be construed narrowly and will not eliminate or reduce coverage absent clear and specific language. The Court of Appeals violated this rule by holding that an exclusion that says nothing whatsoever about "design defects" nevertheless excludes coverage for defective design.

b. Unwritten Exclusions Cannot Be Implied into Insurance Policies

A second established rule ignored by the Court of Appeals is that "Court[s] may not read unwritten limitations into an insurance policy:"

> After all, "it is a matter of common knowledge that insurance companies prepare their own contracts of insurance .... The policies are prepared by skilled lawyers retained by the insurance companies, who through years of study and practice have become experts upon insurance law." Charter Oak's drafters were capable of inserting such a limitation into the insuring provision. In the

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> absence of such an express limitation, the Court must interpret the policy in favor of coverage.

King Cnty. v. Travelers Ins. Co., 1996 WL 257135, at *5 (W.D. Wash. Feb. 20, 1996). *Accord Pub. Empl. Mut. Ins. v. Mucklestone*, 111 Wn.2d 442, 444 (1988) (court will not rewrite policy "to make it read so as to provide the exclusion [the insurer] wishes it had drafted.").

The Court of Appeals—despite conceding "no design defect expressly appears in Section 2"—departed from this precedent by holding that an exclusion that is entirely silent on "design defects" excludes coverage for defective design. This holding is impossible to square with the rule prohibiting courts from adding words to a policy that allow insurers to avoid liability. *In re Feature Realty Litig.*, 468 F. Supp. 2d 1287, 1304 (E.D. Wash. 2006) ("[The insurer] is attempting to read an exclusion into the policy which does not exist. The Court will not add words to the language of the contract of insurance to either create or avoid liability.").

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The Supreme Court should accept review and confirm that exclusions cannot be implied into insurance policies. Such a confirmation is in keeping with longstanding precedent that it is incumbent upon insurers to draft exclusions in a clear and precise manner. *See Lynott v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 123 Wn.2d 678, 688 (1994) ("courts necessarily consider whether alternative or more precise language, if used, would have put the matter beyond reasonable question."). If their drafting efforts fall short, the insurers—not, as the Court of Appeals would have it, the policyholders—must live with the consequences. *See Am. Nat. Fire Ins. Co. v. B & L Trucking & Const. Co., Inc.*, 134 Wn.2d 413, 430 (1998) ("[The insurer] drafted the policy language; it cannot now argue its own drafting is unfair.").

c. Insurance Policies Are Interpreted as an Average Lay Person Would

Yet more rules of Washington insurance law underscore the Court of Appeals' error. "Courts in Washington construe insurance policies as the average person purchasing insurance

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would." *Vision One*, 174 Wn.2d at 512. No average person would understand "mechanical breakdown" to encompass "defective design." These phrases do not mean the same thing in common parlance. They are also not the same thing in practice. A well-designed machine can break down due to improper maintenance, overuse, or operator error, to name a few. *E.g.*, *Assoc. Aviation Underwriters v. George Koch Sons, Inc.*, 712 N.E.2d 1071, 1073-74 (Ind. Ct. App. 1999) (breakdown caused by failure to monitor engine oil level). Review should be accepted so Washington policyholders can continue to rely on the "average consumer of insurance" rule.

d. Ambiguities Are Construed in Favor of Coverage

The Court of Appeals also violated Washington's rule of ambiguities. That rule dictates that "[w]here a provision of a policy of insurance is capable of two meanings, or is fairly susceptible of two constructions, the meaning and construction most favorable to the insured must be employed." *Greer v. Nw. Nat. Ins. Co.*, 109 Wn.2d 191, 201 (1987). The rule applies

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"with added force to exclusionary clauses which seek to limit policy coverage." *Am. Star Ins. Co. v. Grice*, 121 Wn.2d 869, 874-75 (1993).

Here, the Court of Appeals was faced with two possible constructions of a machinery breakdown exclusion. The first was the expansive interpretation it ultimately adopted: the exclusion extends to design defects. The second was the narrower interpretation in keeping with how exclusions are supposed to be construed: the exclusion applies only to the clearly excluded cause of loss. At minimum, the narrower construction was reasonable, mandating a construction that favored coverage. *See Queen Anne Park Homeowners Ass'n v. State Farm Fire & Cas. Co.*, 183 Wn.2d 485, 489 (2015) ("Contractual terms are ambiguous if they are subject to more than one reasonable interpretation.").[1]

[1] This was the result compelled by Washington law even if the Insurers' expansive interpretation was more reasonable than the narrow one. *See Kaplan v. Nw. Mut. Life Ins. Co.*, 115 Wn. App. 791, 808 (2003) (to benefit from the ambiguity rule,

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2. A Design Defect Is Not an Internal Cause

Faced with the absence of any Washington case holding that design defects are internal causes, the Court of Appeals cherry-picked some decisions from sister jurisdictions and ignored others in order to arrive at its insurer-friendly conclusion. This exercise runs counter to Washington insurance law. In the absence of controlling precedent, the insured—not the insurer—should be given the benefit of the doubt. *Robbins v. Mason Cty. Title Ins. Co.*, 195 Wn.2d 618, 633 (2020) ("uncertainty in the law must be construed in favor of the insured"); *Am. Best Food, Inc. v. Alea London, Ltd*., 168 Wn.2d 398, 410-11 (2010) (the lack of Washington authority together with out-of-state case law supporting coverage meant that an exclusion was ambiguous and must be construed in favor of coverage); *Webb v. USAA Cas. Ins. Co*., 12 Wn. App.

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the insured "does not need to show that his list of possible interpretations, or any one of them, is more reasonable than that espoused by [the insurer], but only that there is more than one reasonable interpretation.").

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2d 433, 444-46 (2020) ("we must give the insured the benefit of the doubt" and "any 'legal ambiguity' must be resolved in favor of the insured."). Here, rather than giving the insured the benefit of the doubt, the Court of Appeals tilted the scales in favor of the insurer.

The Court of Appeals' reliance on *Acme Galvanizing* is all the more troubling because that California case concerned a latent defect exclusion rather than a design defect exclusion. The Court of Appeals found *Acme Galvanizing* helpful because "'Latent defect,' 'inherent defect,' and internal cause have been used interchangeably." *See* COA Opinion, n. 12. *Accord* Respondents' Opposition at 21 ("As Division I recognized, the term 'latent defect' is synonymous and interchangeable with 'inherent defect' and internal cause."). This is wrong as a matter of Washington law.

In Washington, "latent defect" means "those [defects] that would not be discovered by a reasonable inspection." *Babai v. Allstate Ins. Co.*, 2013 WL 6564353, at *3 (W.D.

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Wash. Dec. 13, 2013). A latent defect is simply not the same thing as an inherent vice or a design defect. *Cf. Port of Seattle v. Lexington Ins. Co*., 111 Wn. App. 901, 909-910 (2002) ("inherent vice" means "any existing defects, diseases, decay or the inherent nature of the commodity which will cause it to deteriorate with a lapse of time"). If these phrases were indeed interchangeable, there would be no reason for insurers to draft separate exclusions for design defects, latent defects, and inherent vices (to say nothing of machinery breakdowns). *Cf. Ibrahim v. AIU Ins. Co*., 177 Wn. App. 504, 515 (2013) ("the preferred interpretation gives meaning to all provisions and does not render some superfluous or meaningless.").

Even if the Court of Appeals were correct to look at "latent defect" cases, it should have relied on *Dickson v. U.S. Fid. & Guar. Co.*, 77 Wn.2d 790 (1970) rather than *Acme Galvanizing*. *Dickson* involved a property policy containing an exclusion for "latent defect." The Washington Supreme Court held that "the policy covers this loss, even if the exclusion were

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construed to include a loss caused by latent defects, since an insured external cause was responsible for this loss." 77 Wn.2d at 791. That is, an insured external cause can exist for Washington policyholders even if an excluded latent defect contributed to the loss. *Id*. at 793-94. *Accord Ingenco Holdings, LLC v. Ace Am. Ins. Co.*, 921 F.3d 803, 816 n.5 (9th Cir. 2019) (addressing "external" versus "internal" causes, citing *Dickson*, and observing "although the Washington Supreme Court has not addressed the precise issue, it has, in the all risks context, suggested that an external cause can exist even in circumstances involving latent defects."). It makes no sense for the Court of Appeals to have ignored Washington "latent defect" precedent in favor of *Acme Galvanizing*.

II. CONCLUSION

"It must not be forgotten that the purpose of insurance is to insure, and that construction should be taken which will render the contract operative, rather than inoperative." *Phil Schroeder, Inc. v. Royal Globe Ins. Co.*, 99 Wn.2d 65, 68

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(1983). The Court of Appeals' erroneous decision should be overturned because it renders insurance contracts inoperative for Washington policyholders.

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Respectfully submitted this 19th day of November, 2021.

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s/ DocuSigned by: Jennifer Bucher E7A95ECFD2A141B...

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VULCAN INC.

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