

NO. 64516-1-I

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION I

MUTUAL OF ENUMCLAW INSURANCE COMPANY,
a Washington corporation,

Appellant,

v.

UNIGARD INSURANCE COMPANY,
a Washington corporation,

Respondent.

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REPLY BRIEF OF APPELLANT

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I. INTRODUCTION

Respondent Unigard Insurance Company (“Unigard”) has missed the point of appellant Mutual of Enumclaw Insurance Company’s (“MOE”) argument on the primary issue on appeal. The issue is framed at page one of the Brief of Appellant as follows:

The trial court erred by ruling that *MOE* was liable for 100% of Newmarket’s cleanup costs, even though *Engelmann* did not assume 100% liability under the terms of the Agreement.

(Italics added.) Unigard’s trial brief argued that the court’s summary judgment ruling on bad faith meant that MOE was responsible for 100% of the clean up and investigation costs, as follows:

The Court has already determined that MOE is estopped from denying coverage as a result of its bad faith. MOE is thus liable for **all** investigation and clean-up costs, past and future, as well as all other damages sustained by the Engelmanns.

CP 70, ln. 13-15 (emphasis added). The trial court *agreed with Unigard* and ruled that “liability issues are not a part of this case.” VRP II 95, ln. 12-13.¹ A trial was held solely for the purpose of determining the *amount* of investigation and cleanup costs to be imposed on MOE.

¹ “VRP II” refers to volume II of the Verbatim Report of Proceedings recorded on July 16, 2009. “VRP I” refers to volume I of the Verbatim Report of Proceeding recorded on July 15, 2009. MOE failed to differentiate between the two volumes in the Brief of Appellant and apologizes for any resulting confusion or inconvenience. MOE will promptly file a corrected brief if requested by the Court.

Even though it was estopped from asserting coverage defenses, however, MOE's liability under the Settlement Agreement and Assignment ("Agreement") is no larger than that of its insured Engelmann. *See, e.g., Besel v. Viking Ins. Co.*, 146 Wn.2d 730, 736, 49 P.3d 887 (2002) (applying bad faith rule to settlements). The trial court erred by either (1) construing the Agreement as an assumption of 100% liability by Engelmann (Assignment of Error No. 1), or (2) by misapplying bad faith law to find that MOE was not entitled to address the issue of Engelmann's liability (which had not yet been determined) on the merits (Assignment of Error No. 2). MOE need not prevail on both assignments of error for this Court to reverse the trial court's judgment.

The trial court record shows that MOE presented its theory of the case before trial and opposed adverse rulings, but was rejected by the court. Unigard's reliance on instruction no. 7, which stated that MOE is "liable for all damages contemplated by the Settlement Agreement and Assignment," is unavailing because when viewed in its entirety the instruction only allowed MOE to defend Unigard's claim as to the *amount* of damages related to the assigned claims. Instruction no. 7 expressly stated that the "Court has already determined that the defendant is liable to plaintiff for damages." CP 658. The only issue submitted to the jury was the amount of investigation, cleanup and other costs related to the claims

in the underlying lawsuit, *i.e.*, the “damages contemplated by the Settlement Agreement and Assignment,” for which the trial court had already decided to impose liability on MOE.

While the remaining issues are moot if the Court reverses the trial court’s judgment for the reasons identified above, MOE continues to disagree with Unigard’s position regarding (1) the purpose and necessity of a reasonableness hearing in the event the Court concludes that Engelmann did accept liability for 100% of Newmarket’s investigation and cleanup costs, (2) the prejudicial effect of needlessly telling the jury that MOE had been found to have acted in bad faith, and (3) the propriety of awarding pre and post judgment interest at the contract rate of 12%.

II. ARGUMENT

A. **MOE’s Liability Depends On the Settlement Agreement and Assignment Entered Into By Engelmann.**

Unigard persuaded the trial court that MOE was precluded from presenting any liability defenses to its assigned claim because of bad faith. Unigard asserted in its trial brief that MOE was liable for “all clean-up and investigation costs” because of the bad faith ruling. CP 70, ln. 13-15. Unigard stated during pre-trial motions that “the only issue to be presented to the jury is the amount of damages.” VRP I 3, ln. 23-25. Unigard told the court that MOE’s defenses were limited to whether the Agreement

itself was the product of fraud or collusion and whether the investigation and cleanup costs were reasonable and related to the underlying lawsuit. VRP I 48, ln. 7-17.

The trial court *agreed with Unigard* and concluded that issues pertaining to Engelmann's liability to Newmarket (and MOE's corresponding liability to Unigard) would not be addressed at trial. VRP I 57, ln. 5-16. MOE argued on pre-trial motions and in its trial brief that Engelmann's actual liability to Newmarket *under the Agreement* had never been determined. VRP I 21-22; CP 116-118. MOE's position was rejected, and instead the trial court instructed the jury that it had "already determined" that MOE was liable to Unigard "for all damages contemplated by the Settlement Agreement and Assignment unless you find that the settlement is the product of fraud and collusion." CP 658. Unigard got what it wanted – a trial where MOE's liability was already established with the only issue being the amount of damages incurred in connection with the underlying lawsuit.

The problem with the trial court's rulings and instructions, however, is that while MOE is bound to the Agreement entered into by Engelmann, the Agreement is not ambiguous and did *not* impose liability on Engelmann beyond the \$20,000 he agreed to pay Newmarket, as follows:

5.1 This Agreement is the result of compromise and accord, and shall not be considered an admission of liability or responsibility by any party hereto, who continue to deny any liability for any and all claims related to the Site, the Facility and the Contribution Action.

CP 25. There is *no* language in the Agreement by which Engelmann assumed responsibility for all of Newmarket's cleanup costs.

MOE is not contesting on appeal that the Agreement was intended to *preserve* Engelmann's liability (if any) to the extent of available insurance. Nonetheless, as in *Kagele v. Aetna Life & Cas. Co.*, 40 Wn. App. 194, 698 P.2d 90 (1985),² the question of Engelmann's liability to Newmarket beyond \$20,000 was left *unresolved*. MOE is bound to the Agreement because of the court's bad faith ruling, but is nonetheless *only liable to the extent Engelmann could be found liable* under the express terms of the Agreement or otherwise. *See, e.g., Besel v. Viking Ins. Co.*, 146 Wn.2d 730, 736, 49 P.3d 887 (2002) (insurer's liability based on settlement entered into by insured).

Newmarket could have asked Engelmann to enter into an Agreement accepting liability for all of the investigation and cleanup costs, past and future, but did not. MOE explained to the trial court that even though it was bound by the Agreement, the issue of Engelmann's

² "First, the agreement between the Currys and Kageles does not determine the Currys' liability." 40 Wn. App. at 196-197.

liability beyond \$20,000 still had to be decided, but its position was rejected. VRP I 21-22; CP 116-118. The trial court's bad faith ruling estopped MOE from denying *coverage* for the settlement entered into by its insured, but should *not* have had the effect of enlarging Engelmann's liability under the Agreement or MOE's corresponding obligation to pay. In fact, that is what happened at trial in spite of MOE's objections.

MOE is not trying on appeal to avoid responsibility for Engelmann's liability under the Agreement. Rather, MOE seeks a *determination* of Engelmann's liability beyond \$20,000 under the Agreement, which remains unresolved. Whether the trial court found Engelmann to be responsible for 100% of the investigation and clean up costs under Agreement, or simply concluded that the bad faith ruling precluded any inquiry into the extent of Engelmann's liability under Agreement, it committed an error of law that requires a new trial.

If the trial court did *not* conclude that Engelmann accepted 100% liability under the Agreement, it misapplied bad faith law by refusing to allow MOE to stand in the shoes of its insured and defend the liability issue. There is no basis in bad faith law for imposing greater liability on MOE than that agreed to by its insured. *See, e.g., Truck Ins. Exch. v. VanPort Homes, Inc.*, 147 Wn.2d 751, 765-766, 58 P.3d 276 (2002) (insurer that commits bad faith is bound by settlement entered into by

insured). Unigard's successful argument to the trial judge that MOE is responsible for 100% of the investigation and cleanup costs based solely on the bad faith ruling simply skips over this critical step.

B. If Engelmann Accepted 100% Liability Under the Agreement the Trial Court Must Make A Determination Whether that Portion of the Settlement Is Reasonable.

Engelmann did not accept 100% liability for Newmarket's investigation and cleanup costs. Rather, the Agreement is unambiguous and demonstrates the parties' intent to leave the issue of Engelmann's liability undetermined. *See Kagele v. Aetna Life & Cas. Co.*, 40 Wn. App. 194, 196-198, 698 P.2d 90 (1985) (settlement without admission of liability did not release insurer *or* determine the liability of the insured). Although it is the trial court's function to interpret the Agreement as a matter of law,³ it never made any finding that the Agreement was ambiguous – it simply concluded at Unigard's urging that MOE was liable for all of the investigation and cleanup costs at issue in the underlying lawsuit because of the bad faith ruling.

Even the Court were to conclude that the Agreement shifted liability for *all* of the investigation and cleanup costs to Engelmann,

³ *See Queen City Farms, Inc. v. Central Nat'l Ins. Co.*, 126 Wn.2d 50, 65, 882 P.2d 703, 891 P.2d 718 (1995) (settlement agreements subject to contract rules of interpretation); *Riley Pleas, Inc. v. State*, 88 Wn.2d 933, 938, 568 P.2d 780 (1977) (interpretation of a contract is a question of law) .

however, MOE is responsible for those costs only if the acceptance of 100% liability was “reasonable.” See, e.g., *Truck Ins. Exch. v. VanPort Homes, Inc.*, 147 Wn.2d 751, 765, 58 P.3d 276 (2002) (burden of proof shifts to insurer *after* settlement has been approved as reasonable per *Chaussee* factors). MOE explained to the trial court before trial that a reasonableness hearing would be required to impose liability on MOE in the event that the Agreement itself was determinative of Engelmann’s liability.⁴ VRP I 22-23. Unigard disagreed. VRP I 23, ln. 9-10.

Without a determination that the settlement terms were reasonable under the *Chaussee* factors, Unigard has failed to establish an essential element of its claim against MOE. See *Truck Ins. Exch. v. VanPort Homes, Inc.*, *supra* (insurer that commits bad faith is liable for *reasonable* settlement by insured); *Chaussee v. Maryland Casualty Co.*, 60 Wn. App. 504, 803 P.2d 1339 (1991) (judgment *n.o.v.* for insurer affirmed based on

⁴ The factors the court must consider in a reasonableness hearing are (1) the releasing person's damages; (2) the merits of the releasing person's liability theory; (3) the merits of the released person's defense theory; (4) the released person's relative faults; (5) the risks and expenses of continued litigation; (6) the released person's ability to pay; (7) any evidence of bad faith, collusion, or fraud; (8) the extent of the releasing person's investigation and preparation of the case; and (9) the interests of the parties not being released. *Chaussee v. Maryland Casualty Co.*, 60 Wn. App. 504, 512, 803 P.2d 1339, 812 P.2d 487 (1991). The trial court limited the scope of the issues at trial to only the amount of damages and evidence of fraud or collusion. MOE was not permitted to address the seven other *Chaussee* factors at trial, including factors pertaining to liability.

claimant's failure to address all of the reasonableness factors adopted by the Court). Instead, Unigard persuaded the trial court to give an instruction that shifted the burden of proof to MOE, without establishing the necessary foundation for that ruling.⁵

Unigard seeks to avoid this fatal flaw by arguing that MOE did not request a reasonableness hearing. It was not up to MOE to request a reasonableness hearing in order to establish an essential element of Unigard's claim. Rather, Unigard had the burden of submitting evidence that would allow a determination that the settlement was reasonable. *See Chaussee v. Maryland Casualty Co., supra.*

Unigard argues on appeal that reasonableness hearings are limited to ensuring that the "dollar amount" of the judgment is reasonable and not the product of fraud and collusion, and that in this case no such determination is necessary because the jury decided the *amount* of investigation and cleanup costs. But determining the amount of damages related to the underlying lawsuit is at best only half the equation for a reasonableness determination. The other half is the defendant's potential liability for those damages including defenses. *See Chaussee v. Maryland Casualty Co.*, 60 Wn. App. 504, 512, 803 P.2d 1339, 812 P.2d 487 (1991)

⁵ The trial court acknowledged that it agreed with Unigard that there was no need to address issues concerning the basis of Engelmann's liability to Newmarket in the underlying lawsuit. VRP I 57, ln. 5-16.

(listing factors, including to the insured's potential liability and liability defenses). Unigard persuaded the trial court to ignore any issues pertaining to Engelmann's liability or defenses because of the bad faith ruling and conduct a trial on damages only. What that means is that issues pertaining to the *relative* responsibility of Engelmann and Newmarket for the investigation and cleanup costs have *never* been addressed under the Agreement or otherwise.⁶

Chaussee provides the methodology for binding an insurer to a settlement entered into by its insured because of bad faith and shifting the burden of proof. Instead of relying on that methodology, the trial court ignored liability issues and conducted a trial addressing only the amount of damages. MOE was given *less* of an opportunity at trial to defend itself from Unigard's claim than it would have received in the context of a summary hearing to determine reasonableness! Failure to address the basis for Engelmann's liability *in any way* before imposing liability on MOE raises concerns about due process that the *Chaussee* methodology presumably is intended to prevent. The trial court clearly erred when it ruled that "liability issues are not a part of this case." VRP II 95, ln. 12-13.

⁶ This is not a case where, for example, the defendant injured the plaintiff in a rear end auto accident such that the reasonableness of a settlement essentially depends on the amount to be paid in relation to the plaintiff's damages. In this case Engelmann and Newmarket *each* had potential liability for investigation and cleanup costs.

MOE was prepared to show at trial that Engelmann only owned the property for nineteen months and did not do anything to cause a “release” of hazardous substances at the site. Unigard’s assertion that Engelmann would have been found liable under the Model Toxics Control Act or under other legal theories simply illustrates that the issue has not been determined.⁷ Unigard’s position that liability issues have nothing to do with the judgment entered by the trial court is contrary to Washington bad faith law. Even if Engelmann is liable under the Agreement for all investigation and cleanup costs, Unigard and the trial court both failed to address whether the *liability* portion of the Agreement is “reasonable” as required to impose liability on MOE.

C. MOE Opposed Adverse Rulings at the Trial Court and Preserved Its Objections for Appeal.

It is at least somewhat surprising that after having successfully persuaded the trial court that MOE was responsible for “all” of the investigation and cleanup costs related to the claims in the underlying lawsuit, Unigard is apparently arguing on appeal that MOE was free to address liability issues based on instruction no. 7, which stated that it is “liable for all damages contemplated by the Settlement Agreement and

⁷ Regardless of the number of legal theories Newmarket may have had against Engelmann, it is difficult at best to conclude that *any* cause of action could have resulted in a complete and total shifting of liability to Engelmann.

Assignment,”⁸ when in fact it is quite clear that MOE was precluded from addressing liability issues in any way.⁹

Jury instructions must be viewed as a whole and are sufficient if they allow a party to argue its theory of the case, are not misleading, and correctly state the law. *See, e.g., State v. Pittman*, 134 Wn. App. 376, 381, 166 P.3d 720 (2006). Instruction no. 7 first states that the trial court “has already determined that the [MOE] is liable to [Unigard] for damages.” CP 658. MOE’s offer of Engelmann’s deposition testimony to address liability issues was rejected by the trial court. VRP II 44-46; CP 227-312. If there is one thing that is exceedingly clear about the trial court’s rulings, it is that the court was persuaded by Unigard’s incorrect legal argument that the bad faith ruling not only estopped MOE from denying coverage, but also precluded it from seeking a determination of Engelmann’s liability *under the terms of the Agreement*.¹⁰

As a result, the trial court instructed the jury that MOE was liable for all of the investigation and cleanup costs at issue in the underlying lawsuit, *i.e.*, “all of the *damages* contemplated by the Settlement

⁸ CP 658.

⁹ “[L]iability issues are not a part of this case.” VRP II 95, ln. 12-13.

¹⁰ MOE made clear that it was not seeking to relitigate or obtain a “do over” on the issue of Engelmann’s liability to Newmarket, because that liability had *not yet been determined* by the Agreement or otherwise. VRP I 21, ln. 22-25; VRP I 52, ln. 11-14.

Agreement and Assignment.”¹¹ CP 658 (italics added). MOE was not allowed to put on evidence or argue to the jury about whether it could be found liable for only a portion of the reasonable investigation and cleanup costs incurred in connection with the claims in the underlying lawsuit. Instruction no. 7 did not allow MOE to argue its theory of the case. Rather, instruction no. 7 boxed MOE into a trial limited to the issue of the amount of investigation and cleanup costs related to the underlying lawsuit, exactly as requested by Unigard.

Unigard’s argument that MOE did not adequately object to instruction no. 7 or preserve error for appeal is belied by the record. Instruction no. 7 was the product of the trial court siding with Unigard after a lengthy and contested argument on pre-trial motions. VRP I 20-57. Recall that Unigard’s position was that as a consequence of the bad faith ruling, “the only issue to be presented to the jury is the amount of damages.” VRP I 3, ln. 23-25. Unigard argued that at most MOE “could rebut some things, but not the dollar value of things actually relating to the suit that was not defended.” VRP I 48, ln. 12-17. In spite of MOE’s opposition, the trial court stated that it “did agree with plaintiff’s position

¹¹ MOE again points out that it is the trial court’s function, and not the jury’s, to interpret the Agreement as a matter of law. See *Queen City Farms, Inc. v. Central Nat’l Ins. Co.*, 126 Wn.2d 50, 65, 882 P2d 703, 891 P2d 718 (1995).

on the settlement agreement” when it advised the parties that it was giving instruction no. 7. VRP II 89, ln. 9-16.

MOE consistently and continuously expressed its opposition to Unigard’s position to the trial court. For example:

THE COURT: What about Butler and Truck Insurance Exchange, why wouldn’t they be applicable?

MR. BRANOM: Because in those cases, the liability of the – of the insured had been determined and it has not been determined here, so that’s an issue that still remains to be tried

THE COURT: But it seems like the ultimate question for the Court is even if it hasn’t been determined, whether through the principle of estoppel it can’t be raised at this point.

MR. BRANOM: The estoppel goes to coverage defenses your Honor. It goes to Mutual of Enumclaw’s ability to raises defenses under the insurance contract. They can’t assert exclusions under the policy. That’s what the estoppel goes to. It doesn’t go to the essential element of the case, which is the liability of Mr. Engelmann, if any, that has not been determined, it has never been determined.

VRP I 21-22.

THE COURT: Mr. Branom, the other side of the coin is how can you be permitted to raise these defenses that you’ve mentioned in your brief in light of the language of Safeco v. Butler?

MR. BRANOM: Safeco v. Butler was – had actually a covenant judgment in it. They had agreed to an amount, it had passed the reasonableness test, therefore you can’t come in and overturn that if you are in bad faith, that’s one of the consequences of the bad faith ruling. We don’t have that here. . . .

VRP I 48-49. When the trial court rejected MOE's proposed jury instructions and instead chose to give instruction number 7, it stated as follows:

THE COURT: All right. And the reason for the Court's denial of all these instructions is based on the prior ruling that the issues of liability have already been determined, and once there is a finding of bad faith, and the insured reaches a settlement agreement, the law appears to be quite clear that the insurer who's been found to be in bad faith is bound by the settlement agreement, unless the insurer can show that the settlement is the product of fraud or collusion, and that is the standard that stated in Instruction No. 7.

VRP II 97, ln. 9-18. As a result, MOE was bound to liability under a settlement agreement that itself left the issue of liability undetermined!

The trial court was well aware of MOE's objections to its conclusion that the bad faith ruling precluded any inquiry into liability issues. Instruction no. 7 is based on the court rejecting MOE's position, and instead agreeing with Unigard that MOE is "liable for all of the damages contemplated by the Settlement Agreement and Assignment," *i.e.*, all of the investigation and cleanup costs related to the claims in the underlying lawsuit, because of the bad faith ruling.¹²

¹² Unigard's example to the trial court of the type of damages *not* contemplated by the Settlement Agreement and Assignment was the cost of repairing damage to a condominium on Maui entirely unrelated to the claims in the underlying lawsuit. VRP I 48, ln.12-14.

The purpose of making objections to jury instructions is to enable the trial court to correct any mistakes in time to prevent unnecessary expense associated with a second trial. *See Nelson v. Mueller*, 85 Wn.2d 234, 238, 533 P.2d 383 (1975). In order to preserve error, “counsel must call the alleged error to the court's attention at a time when the error can be corrected.” *State of Washington v. Ray*, 116 Wn.2d 531, 540, 806 P.2d 1220 (1991), quoting *State of Washington v. Fagalde*, 85 Wn.2d 730, 731, 539 P.2d 86 (1975).¹³ The substance of instruction no. 7, *i.e.*, that MOE was liable for all damages related to the underlying lawsuit, had already been opposed and decided against MOE. The trial court told the parties when it chose the instruction that it “did agree with plaintiff’s position on the settlement agreement.” VRP II 89, ln. 9-16. The purpose of objecting to proposed instructions in order to afford the court an opportunity to correct errors was satisfied by MOE’s continuing opposition to Unigard’s position at trial.

D. MOE Was Needlessly Prejudiced by References to Bad Faith In a Trial Limited to Determining the Amount of Investigation and Cleanup Costs.

Unigard asserts that advising the jury that MOE had been found guilty of bad faith was not prejudicial. The trial court’s decision to allow

¹³ In at least some circumstances, objections may also be made in a motion for new trial. *Id.*

that information to be presented to the jury is reviewed for abuse of discretion. *See State v. Myers*, 133 Wn.2d 26, 34, 941 P.2d 1102 (1997). When making that determination the trial court should have weighed the probative value of the evidence against its prejudicial effect.¹⁴ The fact that MOE's liability was premised on bad faith had *no* probative value, however, in a trial essentially limited to the amount of environmental investigation and cleanup costs and/or other expenses incurred in connection with the underlying lawsuit. As a result, it was error to allow the information if doing so was prejudicial.

MOE asked the trial court to preclude references to bad faith, Consumer Protection Act violations or estoppel during trial. VRP I 34, ln. 9-14. MOE's concern was that the jurors would become close minded to its arguments upon hearing it had been found guilty of bad faith towards its insured. VRP I 37, ln. 1-9. Instead, the trial court chose to tell the jury during *voir dire* about claims against MOE for bad faith, violation of the Consumer Protection Act and estoppel. VRP I 40, ln. 18-24.¹⁵

¹⁴ *See State v. Acosta*, 123 Wn. App. 424, 433, 98 P.3d 503 (2004)

¹⁵ Unigard took full advantage of the trial court's refusal to grant MOE's motion *in limine* and itself made certain that the jury was told that MOE "did act in bad faith" and "did violate [Washington] statutes." VRP I 72, ln. 1-2. Obviously, Unigard understood that this information had significant potential to cause a negative impact on the jury with respect to MOE.

MOE also unsuccessfully objected to instruction no. 6, which again advised the jury that MOE had “acted in bad faith” and violated the Consumer Protection Act, on grounds that the instruction was prejudicial. VRP II 92, ln. 15-20; CP 657. As a result, the jury was repeatedly told without further explanation that MOE was guilty of bad faith and violating Washington statutes in a case where the only issue it was required to decide was the *amount of investigation and clean up costs* incurred in connection with the underlying lawsuit.

Unless telling the jury that MOE had been found guilty of bad faith and violating Washington statutes was not prejudicial, the trial court abused its discretion by giving the jury that information in circumstances where doing so had *no* probative value. Unigard’s purposeful emphasis on the bad faith ruling in its opening statement, as well as common understanding, belies any such conclusion. VRP I 72, ln. 1-2. In fact, Unigard recovered 100% of its incurred damages without one cent of reduction.

The trial court could have instructed the jury that MOE was liable for the damages contemplated by the Settlement Agreement and Assignment, *i.e.*, the investigation and cleanup costs related to the underlying lawsuit, *without* stating the basis for that liability. Instead, it abused its discretion by needlessly telling the jury MOE had been found to

have acted in bad faith, which is prejudicial on its face. Doing so is grounds for a new trial.

E. MOE's Motion for New Trial Should Have Been Granted.

Unigard's assertion that the trial court correctly denied MOE's motion for a new trial under CR 59(8)(a) is a re-argument of the issues pertaining to the effect of the bad faith ruling and related issues. MOE offers the same response, *i.e.*, the Settlement Agreement and Assignment did not determine Engelmann's liability to Newmarket beyond \$20,000 and that the bad faith ruling did not have the effect of enlarging MOE's liability beyond that of the insured.

F. The Trial Court Erred by Awarding Prejudgment Interest and by Applying a 12% Interest Rate to the Award.

MOE's has appealed with respect to the propriety of awarding prejudgment interest for the incurred investigation and cleanup costs and the trial court's decision to apply the 12% contract rate to amounts charged as pre and post-judgment interest.

1. Prejudgment interest for incurred investigation and cleanup costs.

Unigard correctly cites *Endicott v. Icicle Seafoods, Inc.*, 167 Wn.2d 873, 224 P.3d 761 (2010), for the proposition that an award of pre-judgment interest is reviewed for abuse of discretion, but concedes that an award based on an erroneous legal interpretation is an abuse of discretion

as a matter of law. 167 Wn.2d at 886. Whether reviewed *de novo* or on the basis that the decision to award prejudgment interest was “manifestly unreasonable” or “exercised on untenable grounds or for untenable reasons,” however, the trial court erred by awarding prejudgment interest in circumstances where the purpose of the trial itself was to determine the amount of investigation and cleanup costs related to the underlying lawsuit.

Unigard’s responsive argument relies on *Weyerhaeuser Co. v. Commercial Union Insurance Co.*, 142 Wn.2d 654, 15 P.3d 115 (2000), and is unavailing because in that case the contested issue at trial was liability and not damages. The *Weyerhaeuser* Court held that amounts claimed as damages are liquidated and therefore subject to prejudgment interest if “the evidence furnishes data which, if believed, make it possible to compute the amount due with exactness, without *reliance on opinion or discretion.*” 142 Wn.2d at 685, *citing Prier v. Refrigeration Engineering Co.*, 74 Wn.2d 25, 33, 442 P.2d 621 (1968) (emphasis added). The Court also explained that “[t]he questions before the jury were simply ones of liability and did not involve opinion or an exercise of discretion regarding the amount of the award, as would be the case with general damages.” 142 Wn.2d at 686. Here, the trial court made its *liability* determination before trial and the jury’s function was to determine the *amount of*

damages to be awarded based on, among other things, the expert opinion testimony offered by Unigard. As a result, the trial court made a legal error by awarding prejudgment interest on the incurred damages as determined by the jury.

2. Application of the tort remedy of estoppel requires applying the tort rate of interest under RCW 4.56.110(3) to the judgment entered by the trial court.

The trial court also erred by awarding interest to Unigard at the contract rate of 12%. This decision clearly involves a legal question that is reviewed *de novo*, *i.e.*, was the judgment against MOE primarily based on contract or tort liability? Unigard does not dispute that only one rate of interest applies to a “mixed” judgment or that the controlling factor is whether the judgment is primarily based on tort or contract. *See Woo v. Fireman’s Fund Ins. Co.*, 150 Wn. App. 158, 162, 208 P.3d 557 (2009).

In *Woo, supra*, the Court explained that the remedy of estoppel arises from the *tort* of bad faith, citing *Safeco v. Butler*, 118 Wn.2d 383, 823 P.2d 499 (1992). 150 Wn. App. at 169. The Court also explained that a recovery “based on the jury’s finding of bad faith of Fireman’s Fund and application of the remedy of insurance coverage by estoppel” was a remedy that “sounds in tort.” *Id.* at 172. In such a case, the entire judgment is subject to the interest rate for tort claims provided by RCW 4.56.110(3). *Id.* at 173.

In this case MOE was *estopped* from asserting any coverage defenses to Unigard's claim as a result of the trial court's bad faith ruling. That is a *tort* remedy under *Woo, supra*. There has never been a determination that *any* portion of Engelmann's liability arising from the sale of commercial property to Newmarket was actually covered by the homeowners policy he purchased from MOE. MOE also was not allowed to rely on its \$300,000 "each occurrence" liability limit in defense of Unigard's claim.¹⁶ While the basis for the bad faith finding itself was that MOE breached the contractual duty to defend, the same was true in *Woo*. Without the bad faith ruling and application of the tort remedy of estoppel, Unigard does not obtain a judgment for \$1,345,988.99 by simply proving the amount of investigation and cleanup costs related to the underlying lawsuit and a few other *de minimus* expenses.

Unigard's argument that some of the damages awarded, like Engelmann's defense costs and/or Olympic Steamship attorney's fees could have been awarded based on contract grounds alone means that this is a *mixed* judgment. Beyond dispute, however, is the fact that

¹⁶ Unigard's argument that MOE could have had liability for more than \$300,000 if there were "multiple occurrences" again misses the point. The fact that the homeowners policy includes a liability limit and/or the issue of whether there was more than one "occurrence" (which MOE disputes) were *irrelevant* at trial because the trial court applied the *tort remedy of estoppel*.

\$1,322,689.79 of the \$1,345,988.99 jury verdict was for past and future investigation and cleanup costs that were awarded *without* regard to policy limits *or* coverage defenses based on the bad faith ruling and application of estoppel.¹⁷ Regardless of the fact that Unigard choose to not seek general damages, the primary basis for the vast majority of the mixed judgment entered against MOE is the *tort remedy of estoppel*. The trial court erred as a matter of law by applying the 12% contract rate of interest to the judgment in this circumstance.

III. CONCLUSION

The record on review shows that Unigard convinced the trial court that MOE is responsible for 100% of the investigation and cleanup costs related to the underlying lawsuit because of a prior bad faith ruling. The trial court either (1) concluded that MOE's insured Engelmann had assumed 100% liability under the Settlement Agreement and Assignment with Unigard's insured Newmarket, or (2) simply refused to address the issue of Engelmann's liability under the Agreement because of bad faith. In either case it committed a fundamental error of law, because MOE's liability can be no greater than that to be imposed by the settlement

¹⁷ Unigard sought \$1,010,189.79 for past investigation and cleanup expenses plus Engelmann's defense and settlement payment for a total of \$1,033,488.79. VRP II 106-107. The jury awarded this entire amount, plus \$312,500 for future investigation and cleanup costs. CP 319.

entered into by its insured, which in this case was left undetermined by the terms of the Agreement itself. Even if Engelmann had accepted liability for 100% of Newmarket's cleanup and investigation costs under the Agreement, Unigard and the trial court failed to address whether shifting 100% liability to Engelmann was reasonable, as would be required to impose liability for such a settlement on MOE. This means that the trial court failed to adhere to the methodology adopted by Washington courts for imposing liability on an insurer that commits bad faith.

Instead, the trial court instructed the jury that MOE was liable to Unigard for *all* damages contemplated by the Settlement Agreement and Assignment. Read as a whole this instruction advised the jury that MOE is liable for all of the reasonable investigation and cleanup costs incurred in connection with the underlying lawsuit. The trial court considered and specifically ruled against MOE on the issues presented by the instruction, which did not allow MOE to argue its theory of the case. The trial court also abused its discretion by telling the jury that MOE had been found to have acted in bad faith and violated Washington statutes.

Finally, the trial court erred as a matter of law by awarding prejudgment interest where the sole issue at trial was the amount of reasonable and necessary damages, and by awarding pre and post-judgment interest at the contract rate of 12% to a judgment based

primarily on the tort remedy of estoppel. MOE was not allowed to present coverage defenses to Unigard's claim. MOE was not entitled to the protection of its policy limits. Instead, liability for over \$1 million in investigation and cleanup costs was imposed on MOE without regard to contract defenses because the trial court's bad faith ruling and application of estoppel. In the event that the trial court's award of pre and/or post-judgment interest stands on appeal, the correct rate of interest is the rate applied to tort judgments under RCW 4.56.110(3).

Respectfully submitted this 8th day of July, 2010.

RONALD S. DINNING

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of Attorneys for Respondent

CERTIFICATE OF SERVICE

Linda Voss, declares under penalty of perjury under the laws of the State of Washington that on July 8, 2010 a copy of the foregoing REPLY BRIEF OF APPELLANT was delivered via ABC Legal Messengers to: Karen Weaver, SOHA & LANG, 1325 Fourth Avenue, Suite 2000, Seattle, WA 98101-2570, attorney for Respondent.

Signed in Seattle, Washington this 8th day of July, 2010.

Linda Voss
Linda Voss