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COURT OF APPEALS
DIVISION III
STATE OF WASHINGTON
By _____

No. 319041

COURT OF APPEALS OF THE
STATE OF WASHINGTON, DIVISION III

DOUG and DUSTY CANNON, individuals,

Plaintiffs/Respondents,

v.

COOK CUSTOM HOMES, a Washington corporation; and HOWES
QUALITY DEVELOPMENT COMPANY, a Washington
corporation,

Defendants,

and

WESTERN HERITAGE INSURANCE COMPANY,

Intervener/Appellant.

RESPONDENTS DOUG AND DUSTY CANNON'S BRIEF

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I. INTRODUCTION

Since having Defendant Cook build their home, Respondents Doug and Dusty Cannon (“the Cannons”) have endured their home falling apart and years of litigation. Western Heritage continues to subject the Cannons to further litigation. After taking possession of their home, the Cannons began to notice what they believed to be minor settlement cracks. Over an extensive period, Cook made repairs to the home and the Cannons believed the repairs resolved the issue. Soon after, Doug Cannon was diagnosed with brain cancer and had to undergo several operations and chemotherapy treatments for the disease while simultaneously battling to save his home. At the same time the problems with the home increased as the lot it was built upon continued to settle and pull the house apart. Eventually, Cook admitted he could do nothing further and the Cannons were forced to initiate litigation to seek the damages being suffered.

During litigation, the Cannons learned that the damage was caused by the way the lot had been filled. Both the developer Howe and Cook had placed fill material in the lot. The Cannons ended up

being caught in the middle of an expensive and protracted fight between the developer and the contractor over who caused the damages that destroyed the Cannon home.

The Cannons home had severe cracks that developed through the home and it continued to shift during the litigation. Structural Engineers all agreed that significant repair work is necessary to make the home habitable. Due to extensive settlement that has occurred, the home is in danger of literally falling from its foundations. The engineers further agreed that even after repair work is performed, much of the damage can never be repaired.

After lengthy litigation, the Cannons were able to enter into settlement agreements with both Howe and Cook. Now, after participating in the litigation and refusing to participate in numerous reasonable settlement proposals, Appellant Western Heritage Insurance Company (“Western Heritage”) claims settlement with Cook is not reasonable. However, the Trial Court considered all of the relevant factors, evidence, and the arguments of Western Heritage. After doing so, it exercised its discretion and properly found the settlement reasonable.

II. RE-STATEMENT OF THE ISSUES

A. Reasonableness Determination/Motion For Reconsideration.

1. Did the Trial Court properly exercise its discretion in determining that the amount of the Settlement was reasonable?
2. Did the Trial Court properly exercise its discretion by determining the Settlement was not the product of collusion?
3. Did the Trial Court properly exercise discretion by denying Western Heritage's Motion to re-open discovery to depose the parties and their respective counsel?
4. Was Western Heritage precluded from seeking attorney-client privilege and work product?

III. STATEMENT OF THE CASE

A. Cannon's Home.

In 2005, the Cannons decided to build a home for their family. CP 781. The Cannons purchased a lot and hired Cook Custom Homes, Inc. ("Cook") to build a house on the premises. CP 782; CP 1150-1159. During construction, Cook brought in several hundred yards of fill soil to expand the home's foundation. CP 782. The Cannons moved into the home during the month of March 2006 and soon noticed cracks in the walls, foundation,

basement slab, ceilings, and driveway. CP 782-783. Michael Cook, Cook's president, returned several times to attempt repairs, but the cracks only intensified over time. CP 783. Ultimately, Mr. Cook admitted he was unable to remedy the problem. CP 783. Unfortunately, also during this time period Doug Cannon was diagnosed with brain cancer and endured chemotherapy treatment in the midst of the crisis facing the family home. CP 292.

On December 23, 2012, Lewis Construction & Development, Inc. provided an estimate to perform repairs as directed by Mark Aden of DCI Engineering. CP 558. It estimated that the repairs would cost \$396,478.00. CP 736-737. Doug Cannon testified his family lost the use of at least 49% of his home due to the subsidence damages. CP 784-785. Mr. Cannon calculated the loss-of-use damages by multiplying the 49% loss by the Cannons' monthly mortgage from the period between March 2006 through April 2013. CP 785. Mr. Cannon also testified that he and his family expected to incur \$15,793.99 to move out of the house during the repair process. CP 784.

During the discovery phase of the proceedings, Cook's expert appraiser assessed the fair market value of the Cannon's residence at \$585,000.00, without considering the damages that had occurred to the property. CP 738-740. Jim Powers, an expert for the Cannons, professionally estimated that the Cannons' residence would suffer a decrease in fair market value of 40-50% as a result of the stigma of disclosing the subsidence, even after the damages were repaired. CP 554-555.

B. Procedural History.

The Cannons filed suit against Cook on December 29, 2010. CP 5-12. In bad faith, Cook's insurance company, Western Heritage, denied coverage of the Cannons' claims against Cook, but did provide Cook a defense in the lawsuit subject to a Reservation of Rights. CP 1203-1223. Cook retained a geotechnical expert, GN Northern, Inc., which took several boring samples beneath the surface of the property and concluded the subsidence was the result of "*poorly compacted artificial fill soils*" to a depth of approximately 35-38 feet. CP 583-634.

After this discovery, the Cannons added defendant Howes Quality Development Company, Inc. (“Howes”), the developer of the lot upon which the home is situated. CP 20-32. Howes retained its own geotechnical expert, Strata, a Professional Services Corporation, which attributed the subsidence to the upper layers of fill placed by Cook. CP 635-735. The conflicting expert evidence left the Cannons in the middle of a contentious battle between Cook and Howes over whose fill caused the damage. It was undisputed that the Cannons were not at fault in any way.

The parties, including Western Heritage’s adjuster, unsuccessfully attempted to mediate the dispute on January 28, 2013. CP 835. The Trial Court later denied Howes’ Motion for Summary Judgment. CP 545-550. The Cannons were able to reach a settlement with Howe. CP 1229-1237. The Cannons tried to settle with Cook as well, but Western Heritage refused to offer a reasonable settlement on Cook’s behalf, leaving Cook with no choice but to pursue settlement to protect his interests. CP 986-1014.

On or about April 4, 2013, with the July Trial approaching, the Cannons entered into a “*Settlement Agreement (Consent*

Judgment, Assignment and Covenant not to Execute)” with Cook. Cook consented to entry of judgment against it in favor of the Cannons in the amount of \$1,293,892.81, and assigned its rights to pursue an action for coverage and bad faith against Western Heritage in exchange for the Cannons’ covenant not to execute the judgment against Cook. CP 787-793. The \$1,293,892.81 considered part of the damages being sought, includes repair costs in the amount of \$396,478.00, \$15,793.99 in moving expenses, \$74,229.16 in loss-of-use damages, \$292,500.00 in stigma damages, and \$308,052.49 in prejudgment interest accruing on the loss-of-use and stigma damages at a rate of 12% per annum over seven years. CP 796-797. Also included in the total were attorney fees in the amount of \$185,733.61 and legal costs in the amount of \$21,105.56 incurred in the litigation. CP 797, 1274.

On April 12, 2013, the Cannons moved for the Trial Court’s determination that the Settlement was reasonable and for entry of judgment against Cook. CP 551-553. Western Heritage requested and the Cannons stipulated to Western Heritage intervening for the hearing. CP 811-812. The Cannons also agreed to delay their

hearing to provide Western Heritage the opportunity to be heard. Prior to the reasonableness hearing, Western Heritage moved to re-open discovery for the purpose of deposing Michael Cook, Todd Startzel (Cook's insurer-provided counsel), and John Black (attorney for the Cannons). CP 813-814. The Trial Court denied the motion on June 21, 2013. 6/21/13 RP 12, ll. 3-5; CP 1028-1030. However, Western Heritage was provided access to all of Cook's files and records on the case. CP 816, 919-985.

On July 12, 2013, the Trial Court held the Reasonableness Hearing in which the Court found the Cook Settlement to be reasonable in its entirety. 7/12/13 RP 30-40. During oral argument, the Court noted that the underlying land is not usable, refuting the claims of Western Heritage's counsel that the Cannons' loss of value was limited to the \$475,000 structure rather than the \$585,000 value of the entire property. 7/21/13 RP 19, ll. 24-25. After hearing Western Heritage's arguments against Mr. Cannon's 49% loss-of-use testimony, the Court also took notice of remarks contained in the Lewis Construction & Development, Inc. bid that the basement was rendered unsafe due to presence of a steel structural beam that was

installed in the basement. 7/21/13 RP 18-19; CP 736. Finally, the Court also agreed that a claim may be liquidated even though it is disputed, and held that prejudgment interest was appropriate based on the simple computations involved and that it was a proper consideration as part of the Settlement. 7/21/13 RP 34, ll. 8-24.

The Trial Court entered Findings of Fact and Conclusions of Law in accordance with its ruling. CP 1428-1436. The following month, the Court denied Western Heritage's Motion for Reconsideration of the Court's reasonableness determination. CP 1697-1698.

IV. ARGUMENT

A. Standard Of Review.

In the context of covenant judgments, a Trial Court's determination of reasonableness is reviewed for abuse of discretion. Bird v. Best Plumbing Group, LLC, 175 Wn.2d 756, 774 (2012). Under this standard, a Trial Court's determination is entitled to deference unless the "*decision is manifestly unreasonable or is based on untenable grounds or untenable reasons.*" Id. (quoting

Water's Edge Homeowners Ass'n v. Water's Edge Assocs., 152 Wn. App. 572, 584 (2009)).

Western Heritage incorrectly asks the Court to engage in de novo review. See e.g., Brief of Appellant, pp. 22, 39. The function of a reasonableness determination is for the Trial Court to use its discretion to “*address the viability*” of the damages “*based on what was known to the parties at the time of settlement.*” Bird v. Best Plumbing Group, LLC, 175 Wn.2d 756, 775-76 (2012). As the Bird court discussed, “[t]rial courts **retain broad discretion in determining reasonableness, [and are reviewed] under an abuse of discretion standard.**” Id. at 774 (emphasis added). Here, Western Heritage asks this Court to re-weigh the issues and second guess the Trial Court that had a history with this case.

The Bird court upheld a trial court’s reasonableness determination of a covenant judgment that included statutory treble damages. Id. at 775. Despite arguments from the intervenor-insurer that the treble damage statute was inapplicable, the court declined to decide its reach, noting that “*even if we interpreted the treble damages provision as [the insurer] wished, it would not change the*

*outcome of this case. The precise question before us is whether the trial court **abused its discretion** in determining the covenant judgment was reasonable.” Id. (emphasis added). Therefore, the entirety of the Trial Court’s reasonableness determination is reviewed from an abuse of discretion standard, regardless of which components constitute findings of fact or conclusions of law. In other words, the issue is whether the Trial Court abused its discretion in finding that, as a whole, the Settlement was reasonable.*

Likewise, both the CR 59 motion for reconsideration and for discovery are also reviewed for abuse of discretion. See McCallum v. Allstate Property and Cas. Ins. Co., 149 Wn. App. 412, 428 (2009) (citing Rivers v. Washington State Conference of Mason Contractors, 145 Wn.2d 674, 685 (2002)); and Howard v. Royal Specialty Underwriting, Inc., 121 Wn. App. 372, 379 (2004); see also Nakata v. Blue Bird, Inc., 146 Wn. App. 267, 277 (2008) (“*A trial court has broad discretion under CR 26 to manage the discovery process and, if necessary, to limit the scope of discovery.*”).

B. The Trial Court Did Not Abuse Its Discretion By Finding The Settlement Reasonable.

When an insured defendant consents to judgment and assigns its rights against its insurer “[t]he presumptive measure of an insured’s damages in a bad faith action is the settlement amount, so long as the amount is reasonable and not the product of fraud or collusion.” Howard v. Royal Specialty Underwriting, Inc., 121 Wn. App. 372, 375 (2004). In determining whether covenant judgments against insured defendants are reasonable, courts apply the factors in Glover v. Tacoma Gen. Hosp., 98 Wn.2d 708, 717 (1983) by weighing:

- (1) the releasing party's damages;
- (2) the merits of the releasing party's liability theory;
- (3) the merits of the released party's defense theory;
- (4) the released party's relative fault;
- (5) the risks and expenses of continued litigation;
- (6) the released party's ability to pay;
- (7) any evidence of bad faith, collusion, or fraud;
- (8) the extent of the releasing party's investigation and preparation; and
- (9) the interests of the parties not being released.

Mut. of Enumclaw Ins. Co. v. T&G Constr. Inc., 165 Wn.2d 255, 264 (2008). In evaluating these criteria, “[n]o one factor controls and **the trial court has discretion** to weigh each case individually.” Chausee v. Maryland Cas. Co., 60 Wn. App. 504, 512 (1991)

(emphasis added). Once the court determines a settlement to be reasonable, the burden shifts to the insurer “*to show the settlement was the product of fraud or collusion.*” Besel v. Viking Ins. Co. of Wisconsin, 146 Wn.2d 730, 739 (2002).

1. The Settlement Was Reasonable Based On The Cannons’ Damages And Cook’s Risks At Trial.

The \$1,293,892.81 Settlement considered \$396,478.00 in repair costs, \$15,793.99 in moving expenses, \$74,229.16 in loss-of-use damages, \$292,500.00 in stigma damages, \$308,052.49 in prejudgment interest on the loss-of-use and stigma damages, and \$206,839.17 in attorney fees and costs. CP 796-797. Of these amounts, in its Appeal Western Heritage does not dispute the amounts for the expenses or loss-of-use damages.

a. Repair Costs And Stigma Damages.

In measuring damages for breach of construction contracts, Eastlake Constr. Co., Inc. v. Hess., 102 Wn.2d 30, 47-48 (1984) adopted the RESTATEMENT (SECOND) OF CONTRACTS § 348, allowing recovery of “*the reasonable cost of completing performance or remedying the defects if that cost is not clearly disproportionate to the probable loss in value to him.*” The purpose

of the Eastlake/RESTATEMENT test is to “*prevent[] a windfall in cases where the cost to remedy a construction defect is clearly disproportionate to any loss in value.*” Park Avenue Home Owners Ass’n v. Buchanan Dev., LLC, 117 Wn. App. 369, 385-86 (2003). However, “*it is better that [the plaintiff] receive a small windfall than that he be undercompensated by being limited to the resulting diminution in the market price of his property.*” Eastlake, 102 Wn.2d at 48 (quoting RESTATEMENT (SECOND) OF CONTRACTS § 348, cmt c). While Western Heritage initially insisted that the Cannons should have based their damages on the diminution of value of their property (CP 1037-1038), the Cannons’ counsel pointed out that doing so would have resulted in a greater amount of liquidated damages and pre-judgment interest, which would have increased the Cannons’ damages by more than \$100,000.00 above the Covenant Judgment amount. 7/21/13 RP 5-6. On appeal, Western Heritage now takes the position that “[t]he proper measure of damages is restoration costs and loss of use,” but claims stigma damages would have been unawardable. (Brief of Appellant, p. 21.)

It is well established that stigma damages arising from defects which must be disclosed to future prospective buyers constitute a “*permanent loss*” that is awardable “*in addition to the repairs.*” Mayer v. Sto. Indus., Inc., 156 Wn.2d 677, 695 (2006) (emphasis added). Western Heritage, for the first time on appeal, cites Pugel v. Monheimer, 83 Wn. App. 688 (1996), claiming that stigma damages and repair costs are mutually exclusive. (Brief of Appellant, pp. 20-21.) In fact, the Pugel court held the exact opposite and awarded the plaintiff repair costs as well as damages for the permanent loss of the property’s market value. Pugel, 83 Wn. App. at 693.

Like the case at hand, Pugel involved subsidence of the plaintiff’s property, causing cracks and instability. Id. at 690. The plaintiff also introduced expert testimony to explain that “*\$120,500 of permanent depreciation remained ‘after repairs had been made to restore the property to its prior condition.’*” Id. While the Pugel court acknowledged that diminution of value damages are typically awarded for permanent injury to property, whereas restorable injuries normally warrant restoration costs and loss-of-use damages, the court recognized an exception where the plaintiff “*established*

the loss of market value remaining after he had [repaired the subsidence damages.]” Id. at 692-93 (emphasis added). Thus, Pugel only bolsters the authority already cited by the Cannons at the Trial Court supporting the availability of stigma damages.

Here, even if Western Heritage had presented plausible arguments against Cannons’ right to recover repair costs and stigma damages, which it did not and has not, the question is whether the Trial Court abused its discretion in determining that the Covenant Judgment was reasonable based on the circumstances facing the parties at the time of settlement. In evaluating the damages, the Trial Court weighed expert testimony as to the Cannons’ repair costs and the diminution of the value of their home after completion of the repairs, as well as Cook’s own expert appraisal of the home’s fair market value without damage. CP 1429-1430. Based on these considerations, the Trial Court exercised its discretion.

b. Prejudgment Interest.

Prejudgment interest is awardable “(1) *when an amount claimed is ‘liquidated’* or (2) *when the amount of an ‘unliquidated’ claim is for an amount due upon reference to a fixed standard*”

contained in a contract.” Prier v. Refrigeration Eng.’r Co., 74 Wn.2d 25, 32 (1968). A claim is liquidated where “*the evidence furnishes data which, **if believed**, makes it possible to compute the amount with exactness, without reliance on opinion or discretion.*” Id. (emphasis added). “*The fact that the parties disputed the amount owed does not affect this result. **Mere difference of opinion as to the amount is... no more a reason to excuse [a party] from interest than difference of opinion whether he legally ought to pay at all,** which has never been held an excuse.*” Taylor v. Shigaki, 84 Wn. App. 723, 732 (1997) (emphasis added); see also Prier, 74 Wn.2d at 34 (“*It may be safely said that the tendency has been in favor of allowing interest rather than against it, and that the degree of certainty or ease with which the approximate amount can be ascertained has grown less and less stringent.*”). Even outside the context of a reasonableness determination, the allowance of prejudgment interest is reviewed for abuse of discretion. Curtis v. Security Bank of Washington, 69 Wn. App. 12, 20 (1993).

Western Heritage misconstrues the holding of Coulter v. Asten Group, Inc., 155 Wn. App. 1 (2010), and argues that a court

can never treat a covenant judgment as reasonable if it awards prejudgment interest. (Brief of Appellant, pp. 24-25.) In Coulter, however, uncertainty remained regarding amounts the plaintiffs would receive from one of the co-defendants, leaving the trial court with discretion to adjust the damages award. 155 Wn. App. at 13-14. Moreover, the Coulter plaintiffs sought prejudgment interest on their entire damages. Id. at 12-13. That is not the case here. Instead, in reaching a settlement the parties considered the fact that one of the risks Cook faced at trial was a potential award of prejudgment interest. Thus, Coulter has no relevance to the case at hand.

Here, by contrast, the Settlement considered prejudgment interest only upon the Cannons' loss-of-use and stigma damages. CP 797. The Trial Court correctly found that these damages were liquidated because they were readily calculable through simple formulae. CP 1430. Specifically, the amount of loss-of-use damages consisted of a 49% loss of use (per Mr. Cannon's undisputed testimony) multiplied by the relevant number of months and the monthly mortgage amount. 7/12/13 RP 34, ll. 20-24. The

stigma damages were computed by multiplying the house's original fair market value, as determined by an expert appraiser hired by Western Heritage on Cook's behalf, by the 50% market value diminution as determined by uncontroverted expert testimony. CP 797, 1430. Therefore, the loss-of-use and stigma damages were liquidated claims regardless of whether they were also disputed claims. It was not an abuse of discretion to regard these damages to be reasonable.

c. Attorney Fees Were Properly Considered In Reaching a Settlement.

The Contractor Agreement between the Cannons and Cook provides:

To the fullest extent permitted by law, the Contractor shall indemnify, defend and hold harmless Doug & Dusty Cannon and its agents and employees, from and against claims, damages, losses and expenses, including but not limited to attorney's fees, arising out of or resulting from performance of the work or providing of materials to the extent caused in whole or in part by negligent or wrongful acts or omissions of, or a breach of this agreement by, the contractor, a subcontractor, anyone directly or indirectly employed by them or anyone whose acts they are legally responsible.

CP 1150-1151 (emphasis added).

Western Heritage incorrectly relies on Newport Yacht Basin Ass'n of Condominium Owners v. Supreme Northwest, Inc., 168 Wn. App. 86 (2012), to claim the above clause does not provide for an award of attorney fees. However, the purchase and sale agreement in Newport Yacht Basin contained two separate attorney fee clauses, one for actions, “*by either party against the other*” and another for “*any and all liabilities or claims.*” Id. at 98, 100. These clauses were “*distinguish[able]*” because the first-party clause expressly limited attorney fees to the “*substantially prevailing party*” whereas the general indemnity clause contained no such limitation. Id. and n. 6. Because the party seeking attorney fees did not prevail in its fourth party complaint against the other contracting party, the court denied the award. Id. at 99. However, Newport Yacht does not affect the Cannons’ attorney fee claim since the contract at issue here differs.

Here, the contract does not contain a separate prevailing party provision and indemnification provision. Thus, unlike Newport Yacht, the only basis for attorney’s fees here is limited to the language of the sole attorney fee provision of the contract between

the Cannons and Cook. Based on that provision, the parties intended for Cook to compensate the Cannons for attorney's fees "*arising out of...negligent or wrongful acts or omissions of, or a breach of this agreement by, the contractor....*" At best, Western Heritage's self-serving interpretation of this provision would merely confirm that it was ambiguous. Since it is Cook's contract, any ambiguity would be interpreted in favor of the Cannons. Newport Yacht, 168 Wn. App. at 100. Indeed, Western Heritage apparently interprets the clause to preclude the application of attorney's fees in actions between the parties, whereas Cook, the Cannons, and the Trial Court all interpret it otherwise. The only provision for attorney's fees in the contract does not support Western Heritage's interpretation or otherwise indicate a limitation of attorney's fees in an action between the parties. Consequently, Newport Yacht is inapposite and the Trial Court did not abuse its discretion in finding the attorney fee provision applicable.

Likewise, Jones v. Strom Constr. Co., 84 Wn.2d 518 (1974), also has no bearing on the Cannons' right to attorney fees. That case consisted of a general contractor's claim against its subcontractor for

indemnification of a worker's jobsite injury. Id. at 519. The Jones court merely denied "*attorneys' fees attributable solely to litigation of the indemnity issue itself.*" Id. at 523. Similarly, Tri-M Erectors, Inc. v. Donald M. Drake Co., 27 Wn. App. 529, 538 (1980), only addressed "*attorneys' fees and costs expended in an action to establish indemnification.*"

None of Western Heritage's cases denied attorney fees in a first-party action against the indemnitor for negligence and breach of contract.

Although no Washington precedent addresses the issue, other jurisdictions have awarded attorney fees in liability actions against an indemnitor by way of attorney fee clauses similar to the one at issue. The Ninth Circuit, for instance, construed an indemnification clause to award attorney fees in an action between the indemnitor and the indemnitee where the clause did not expressly exclude such actions. Atari Corp. v. Ernst & Whinney, 981 F.2d 1025, 1031-32 (9th Cir. 1992). The court noted, "[t]he plain, unambiguous meaning of 'indemnify' is not 'to compensate for losses caused by third parties, but merely 'to compensate.'" Id.

In a case strikingly similar to the matter at hand, the Virginia Supreme Court granted attorney fees in a first-party suit by a property owner against an indemnitor excavation-grading contractor who failed to adequately compact a building's underlying soils. Chesapeake and Potomac Telephone Co. v. Sisson, 362 S.E. 2d 723, 724-25, 728-29 (Va. 1987). The Montana Supreme Court likewise considered an agreement to “*indemnify and hold the other parties harmless from and against all liability, claim loss, damage or expense, including reasonable attorneys' fees, incurred or required to be paid by such other parties by reason of any breach*” to allow attorney fees in the event the non-breaching party prevailed, even though the clause “*did not expressly provide that the “prevailing party” or “successful party” shall recover reasonable attorney's fees.*” Transaction Network, Inc. v. Wellington Tech., Inc., 7 P.3d 409, 413 (Mont. 2000) (abrogated on other grounds by Boyne USA, Inc. v. Lone Moose Meadows, LLC, 235 P.3d 1269 (Mont. 2010)). Taking these authorities into account along with the general rule cited in Jones, 84 Wn.2d at 520, that ambiguities in indemnity clauses are construed against the drafter (which was Cook), the Trial

Court did not abuse its discretion in finding that considering the attorney fees in reaching the Settlement was reasonable.

2. There Was No Evidence Of Collusion Between The Cannons And Cook.

In its unfounded accusations of collusion, Western Heritage placed lopsided emphasis on the Cannons' covenant not to execute its judgment against Cook. (Brief of Appellant, p. 40). This is a common characteristic of nearly all covenant judgments, and our courts refuse to recognize these arrangements as "*collusive as a matter of law.*" Bird v. Best Plumbing Group, LLC, 161 Wn. App. 510, 526 (2011). Moreover, case law makes clear that courts "*cannot infer bad faith, collusion or fraud merely based on innuendo and speculation alone.*" Martin v. Johnson, 141 Wn. App. 611, 622-23 (2007). As previously explained, the amount of the judgment reflects recoverable and proven damages suffered by the Cannons. In contrast to cases where collusion was found, Cook does not stand to recover any portion of the proceeds from the Cannons' pending bad faith action against Western Heritage. See Water's Edge Homeowners Ass'n v. Water's Edge Associates, 152 Wn. App. 572, 595-96 (2009).

The Cannons' prior settlement offers also have no bearing on the existence of collusion. Offering to settle a case in exchange for cash-in-hand is obviously preferable to an assignment of Cook's rights to pursue yet another lawsuit, this time against Western Heritage. Indeed, Western Heritage was offered the opportunity to settle for a payment and refused to do so. Greatly exacerbating the financial and emotional burdens of additional litigation was Doug Cannon's continuing battle with brain cancer. Under such circumstances, the Cannons' offer to settle the case for a lump sum cash payment of \$553,406.00 is completely irrelevant to their actual damages, their likelihood of prevailing at trial, and whether the amount of the Covenant Judgment was collusive. The settlement with Cook merely guaranteed another lawsuit with Western Heritage¹ and the expense of future litigation had to be considered in determining what the Cannons would accept as a Covenant Judgment.

The record also clearly shows that the Trial Court gave due consideration to Cook's alleged inability to pay a judgment, but that

¹ Which has happened. Western Heritage filed suit in Federal Court against Cannons and Cook. Western Heritage Insurance Company v. Cook Custom Homes, Doug and Dusty Cannon, Case No. CV-13-204-TOR, filed May 31, 2013 (E.D. Wash).

Western Heritage failed to establish its pertinence to the reasonableness determination. CP 1433. Other than a citation to a non-binding case, Aspen Grove Owners Ass'n v. Park Promenade Apartments, LLC, 842 F. Supp. 2d 1298 (W.D. Wash. 2012), Western Heritage has yet to offer any explanation as to why Cook would be less motivated to enter into a covenant judgment (and escape personal liability) if it was wealthy and ineligible for bankruptcy protection. CP 1040-1042; (Brief of Appellant, p. 40). The Trial Court apparently accorded this factor little weight in its reasonableness determination.

The Cannons' settlement with Howes was also irrelevant to the Trial Court's reasonableness determination. Under the rule set forth in Washburn v. Beatt Equipment Co., 120 Wn.2d 246, 295-96 (1992), defendants against whom judgment is entered are not entitled to offsets for pre-judgment settlements by other co-defendants. The Washburn court acknowledged that its holding could allow plaintiffs to receive more than "*one full recovery*," but also noted that pre-judgment settlements carry the opposite risk:

If the plaintiff settles for more than what a trier of fact might ultimately determine total damages are, plaintiff

has more than 'one full recovery'. Similarly, a plaintiff suing only one defendant may receive less than total damages as a result of the settlement, also a possibility under our holding here.

Id. at 297. Here, a windfall to the Cannons is not even a possibility since their settlement agreement with Howes requires them to reimburse its insurer out of a portion of their recovery from Western Heritage in their pending bad faith action. CP 1229-1237. Cook, meanwhile, remained potentially liable for the Cannons' entire damages, which a jury could not have accurately apportioned among the defendants. Faced with Western Heritage's intransigent refusal to offer coverage or settle the case, Cook was left with no reasonable choice except to consent to judgment.

Far more relevant to the Covenant Judgment's reasonableness were Cook's risks and expenses of continuing the litigation. Western Heritage cites to its own Reservation of Rights letter to Cook for the proposition that "*Cook's expert costs and attorney fees were borne by Western Heritage... they were not a risk to Cook.*" (Brief of Appellant, p. 42). However, its argument is disingenuous since the very same Reservation of Rights letter wrongfully reserved "[t]he right to reimbursement [from Cook] of all defense fees/costs

paid to defend the subject suit should it be established that the suit never presented a potential for covered liability.” CP 1205. Given Western Heritage’s coverage position, Cook potentially faced yet another lawsuit, this time from its insurer, for the substantial attorney fees, costs, and expert witness fees incurred in defending the Cannon suit. The ensuing trial could have exponentially increased these expenses resulting in an aggregate liability far in excess of the Covenant Judgment amount. In light of these considerations, the Trial Court rightly declined to adopt Western Heritage’s argument that collusion should be broadly inferred. In turn, the Trial Court’s reasonableness determination as well as its denial of reconsideration were not abuses of discretion.

C. The Trial Court Did Not Abuse Its Discretion By Denying Western Heritage’s Request For Depositions.

1. The Court Properly Refused To Re-Open Discovery For Depositions.

Western Heritage sought additional discovery “*in order to obtain evidence as to whether the settlement was made in good faith.*” CP 816. Yet no “*smoking gun*” circumstances transpired to imply any bad faith, collusion, or fraud that would necessitate such

discovery. Western Heritage makes no allegations that Cook and its insurer-appointed counsel were ever uncooperative, evasive, or hostile to Western Heritage. Unlike the insureds in Water's Edge Homeowner's Ass'n v. Water's Edge Associates, 152 Wn. App. 572, 579 (2009) and Bird v. Best Plumbing Group, LLC, 161 Wn. App. 510, 516 (2011), Cook did not obtain additional counsel or engage in settlement negotiations without the participation of its insurer-appointed counsel. Indeed, Western Heritage was included during the settlement process. Furthermore, Western Heritage had actively participated in the case and mediation. It also was fully informed of the fact that Cook was being offered a settlement by the Cannons including a Consent Judgment.

The Cannons' prior settlement offers also did not warrant additional discovery. As previously discussed, the Cannons' \$553,406.00 settlement offer was for an upfront cash payment as an alternative to more costly and stressful litigation on top of the multiple years that had already transpired. Doug Cannon's battle with cancer exacerbated these considerations. Unbelievably, Western Heritage continues to insist that his unfortunate illness was

“*irrelevant*” to evaluating the settlement. (Brief of Appellant, p. 46). There is simply nothing unusual about offers to settle based upon factors other than the underlying case. Western Heritage’s speculation and innuendo provided no basis to suspect collusion. Martin v. Johnson, 141 Wn. App. 611, 622-23 (2007).

In lieu of evidence indicating misconduct by the settling parties, Western Heritage claimed depositions were necessary because it claimed Cook had “*no incentive to minimize the amount*” of the Covenant Judgment. CP 818. This concern, which could be said of almost all covenant judgments, did not warrant a fishing expedition. In fact, our courts reached the opposite conclusion in Howard v. Royal Specialty Underwriting, Inc., 121 Wn. App. 372, 379 (2004) where the court refused to reopen discovery in anticipation of a reasonableness hearing. The court noted:

[The insurer] was not a complete ‘stranger to the case.’ [The insurer] provided counsel for its insured [who] had the opportunity to participate in discovery. [The insurer] had access to all of [the Plaintiff’s] medical records and copies of the correspondence between the settling parties.

Id. Red Oaks Condominium Owners Ass’n v. Sundquist Holdings, Inc., 128 Wn. App. 317, 326 (2005) held similarly, also observing:

[The insurer] was not a stranger to the case. It was notified of the claims against [the insured] almost a year in advance of the hearing, defended [the insured] under a reservation of rights, agreed to the tolling of the statute of limitations, paid for an investigation into the claims, and was aware of ongoing settlement negotiations.

Furthermore, an insured faced with denial of coverage has discretion “to settle a lawsuit defended under a reservation of rights.” Tank v. State Farm Fire & Cas. Co., 105 Wn.2d 381, 389 (1986).

Similarly, here Western Heritage was not a “stranger to the case.” Cook kept Western Heritage apprised of all settlement correspondence conducted by its insurer-appointed counsel, who routinely reported to Western Heritage. CP 986-1014. Western Heritage’s adjuster took part in an attempted mediation on January 28, 2013, and was given every opportunity to step up and settle the case. CP 835. Cook’s counsel granted Western Heritage unfettered access to its files relating to the lawsuit, including settlement evaluation and negotiation. CP 816. Western Heritage supplied Cook’s experts and had access to their reports, as well as all discovery conducted over more than two years’ time. CP 919-985. Nonetheless, Western Heritage has shown nothing to indicate that

Cook engaged in any misconduct beyond exercising its discretionary right to settle a claim that Western Heritage refused to indemnify.

2. The Depositions Sought Information Protected By The Attorney-Client Privilege/Work Product.

Western Heritage's requested depositions of the Cannons' counsel and Cook's counsel would have also violated the attorney-client privilege and work product doctrines. Attorneys are protected from discovery "as to any communications made by the client to him or her, or his or her advice given thereon in the course of professional employment," as to all "mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation," as well as to all work product "prepared in anticipation of litigation [absent] substantial need." RCW § 5.60.060(2)(a); CR 26(b)(4).

Washington case law does not define the boundaries and limitations of attorney depositions. Federal courts, however, commonly utilize the Eighth Circuit's test in Shelton v. Am. Motors Corp., 805 F.2d 1323, 1327 (8th Cir. 1986), which requires a showing that "(1) no other means exist to obtain the information than to depose opposing counsel, (2) the information sought is

relevant and nonprivileged, and (3) the information is crucial to the preparation of the case.” In this instance, Cook’s counsel already provided copies of the written settlement communications with the Cannons’ counsel. CP 986-1014. Western Heritage also actively participated in the January 28, 2013 mediation. CP 835. There are no facts to indicate the occurrence of any other significant settlement correspondence between Cook’s and the Cannons’ respective counsel. Western Heritage failed to establish the depositions of counsel were appropriate.

In arguing that no privilege applies, Western Heritage cited Pamida v. E.S. Originals, Inc., 281 F.3d 726, 730 (2002), which held that “*Shelton was not intended to provide heightened protection to attorneys who represented a client in a completed case and then also happened to represent the same client in a pending case where the information known only by the attorneys regarding the prior concluded case was crucial.*” Pamida, however, is inapposite because Western Heritage sought to depose attorneys in connection with the pending action between the Cannons and Cook, which did not conclude until the Trial Court determined the Covenant

Judgment to be reasonable and entered judgment in favor of the Cannons. Accordingly, the Trial Court did not abuse its discretion in denying Western Heritage's Motion for depositions which would not have uncovered any non-privileged information that had not already been disclosed.

V. **RAP 18.1 MOTION FOR ATTORNEY FEES**

A prevailing party is entitled to attorney fees on appeal if a private agreement, statute, or recognized ground of equity so provides. RAP 18.1. The Contractor Agreement between the Cannons and Cook provides that "*the Contractor shall indemnify, defend and hold harmless Doug & Dusty Cannon . . . and its agents and employees, from and against claims, damages, losses and expenses, **including but not limited to attorney's fees**, arising out of or resulting from performance of the work or providing of materials to the extent caused in whole or in part by negligent or wrongful acts or omissions of, or a breach of this agreement....*" CP 1150-1151 (emphasis added).

Here, Western Heritage intervened and seeks to avoid the Settlement by arguing application of this agreement. Accordingly,

based on RAP 18.1 and a private agreement which provides for attorney's fees, the Cannons respectfully request an award of reasonable attorney fees and costs Western Heritage forced the Cannons to incur on appeal.

VI. CONCLUSION

Pursuant to the foregoing, Respondents Doug and Dusty Cannon respectfully request the Trial Court's Reasonableness Determination, denial of Reconsideration, and denial of Discovery in this matter be affirmed.

DATED this 24th day of March, 2014.

DUNN BLACK & ROBERTS, P.S.



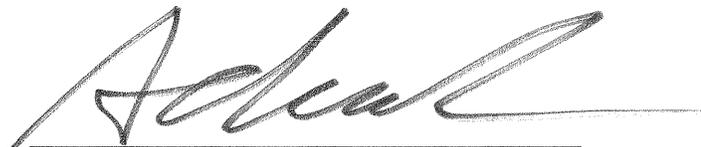
KEVIN W. ROBERTS, WSBA #29473
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ADAM J. CHAMBERS, WSBA #46631
Attorneys for Respondents

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 24th day of March, 2014, I caused to be served a true and correct copy of the foregoing document to the following:

<input type="checkbox"/>	HAND DELIVERY	Andrew Bohrnsen
<input checked="" type="checkbox"/>	U.S. MAIL	Bohrnsen, Stocker, Smith, Luciani & Staub, PLLC
<input type="checkbox"/>	OVERNIGHT MAIL	312 W. Sprague
<input type="checkbox"/>	FAX TRANSMISSION	Spokane, WA 99201
<input type="checkbox"/>	EMAIL	

<input type="checkbox"/>	HAND DELIVERY	Mark Thorsrud
<input checked="" type="checkbox"/>	U.S. MAIL	1300 Puget Sound Plaza
<input type="checkbox"/>	OVERNIGHT MAIL	1325 Fourth Avenue
<input type="checkbox"/>	FAX TRANSMISSION	Seattle, WA 98101
<input type="checkbox"/>	EMAIL	



KEVIN W. ROBERTS

RCW 5.60.060

Who is disqualified — Privileged communications.

(1) A spouse or domestic partner shall not be examined for or against his or her spouse or domestic partner, without the consent of the spouse or domestic partner; nor can either during marriage or during the domestic partnership or afterward, be without the consent of the other, examined as to any communication made by one to the other during the marriage or the domestic partnership. But this exception shall not apply to a civil action or proceeding by one against the other, nor to a criminal action or proceeding for a crime committed by one against the other, nor to a criminal action or proceeding against a spouse or domestic partner if the marriage or the domestic partnership occurred subsequent to the filing of formal charges against the defendant, nor to a criminal action or proceeding for a crime committed by said spouse or domestic partner against any child of whom said spouse or domestic partner is the parent or guardian, nor to a proceeding under chapter [70.96A](#), [70.96B](#), [71.05](#), or [71.09](#) RCW: PROVIDED, That the spouse or the domestic partner of a person sought to be detained under chapter [70.96A](#), [70.96B](#), [71.05](#), or [71.09](#) RCW may not be compelled to testify and shall be so informed by the court prior to being called as a witness.

(2)(a) An attorney or counselor shall not, without the consent of his or her client, be examined as to any communication made by the client to him or her, or his or her advice given thereon in the course of professional employment.

(b) A parent or guardian of a minor child arrested on a criminal charge may not be examined as to a communication between the child and his or her attorney if the communication was made in the presence of the parent or guardian. This privilege does not extend to communications made prior to the arrest.

(3) A member of the clergy, a Christian Science practitioner listed in the Christian Science Journal, or a priest shall not, without the consent of a person making the confession or sacred confidence, be examined as to any confession or sacred confidence made to him or her in his or her professional character, in the course of discipline enjoined by the church to which he or she belongs.

(4) Subject to the limitations under RCW [70.96A.140](#) or [71.05.360](#) (8) and (9), a physician or surgeon or osteopathic physician or surgeon or podiatric physician or surgeon shall not, without the consent of his or her patient, be examined in a civil action as to any information acquired in attending such patient, which was necessary to enable him or her to prescribe or act for the patient, except as follows:

(a) In any judicial proceedings regarding a child's injury, neglect, or sexual abuse or the cause thereof; and

APPENDIX A

(b) Ninety days after filing an action for personal injuries or wrongful death, the claimant shall be deemed to waive the physician-patient privilege. Waiver of the physician-patient privilege for any one physician or condition constitutes a waiver of the privilege as to all physicians or conditions, subject to such limitations as a court may impose pursuant to court rules.

(5) A public officer shall not be examined as a witness as to communications made to him or her in official confidence, when the public interest would suffer by the disclosure.

(6)(a) A peer support group counselor shall not, without consent of the law enforcement officer or firefighter making the communication, be compelled to testify about any communication made to the counselor by the officer or firefighter while receiving counseling. The counselor must be designated as such by the sheriff, police chief, fire chief, or chief of the Washington state patrol, prior to the incident that results in counseling. The privilege only applies when the communication was made to the counselor while acting in his or her capacity as a peer support group counselor. The privilege does not apply if the counselor was an initial responding officer or firefighter, a witness, or a party to the incident which prompted the delivery of peer support group counseling services to the law enforcement officer or firefighter.

(b) For purposes of this section, "peer support group counselor" means a:

(i) Law enforcement officer, firefighter, civilian employee of a law enforcement agency, or civilian employee of a fire department, who has received training to provide emotional and moral support and counseling to an officer or firefighter who needs those services as a result of an incident in which the officer or firefighter was involved while acting in his or her official capacity; or

(ii) Nonemployee counselor who has been designated by the sheriff, police chief, fire chief, or chief of the Washington state patrol to provide emotional and moral support and counseling to an officer or firefighter who needs those services as a result of an incident in which the officer or firefighter was involved while acting in his or her official capacity.

(7) A sexual assault advocate may not, without the consent of the victim, be examined as to any communication made between the victim and the sexual assault advocate.

(a) For purposes of this section, "sexual assault advocate" means the employee or volunteer from a community sexual assault program or underserved populations provider, victim assistance unit, program, or association, that provides information, medical or legal advocacy, counseling, or support to victims of sexual assault, who is designated by the victim to accompany the victim to the hospital or other health care facility and to proceedings concerning the alleged assault, including police and prosecution interviews and court proceedings.

(b) A sexual assault advocate may disclose a confidential communication without the consent of the victim if failure to disclose is likely to result in a clear, imminent risk of serious physical injury or death of the victim or another person. Any sexual assault advocate participating in good faith in the disclosing of records and communications under this section shall have immunity from any liability, civil, criminal, or otherwise, that might result from the action. In any proceeding, civil or criminal, arising out of a disclosure under this section, the good faith of the sexual assault advocate who disclosed the confidential communication shall be presumed.

(8) A domestic violence advocate may not, without the consent of the victim, be examined as

to any communication between the victim and the domestic violence advocate.

(a) For purposes of this section, "domestic violence advocate" means an employee or supervised volunteer from a community-based domestic violence program or human services program that provides information, advocacy, counseling, crisis intervention, emergency shelter, or support to victims of domestic violence and who is not employed by, or under the direct supervision of, a law enforcement agency, a prosecutor's office, or the child protective services section of the department of social and health services as defined in RCW 26.44.020.

(b) A domestic violence advocate may disclose a confidential communication without the consent of the victim if failure to disclose is likely to result in a clear, imminent risk of serious physical injury or death of the victim or another person. This section does not relieve a domestic violence advocate from the requirement to report or cause to be reported an incident under RCW 26.44.030(1) or to disclose relevant records relating to a child as required by *RCW 26.44.030(12). Any domestic violence advocate participating in good faith in the disclosing of communications under this subsection is immune from liability, civil, criminal, or otherwise, that might result from the action. In any proceeding, civil or criminal, arising out of a disclosure under this subsection, the good faith of the domestic violence advocate who disclosed the confidential communication shall be presumed.

(9) A mental health counselor, independent clinical social worker, or marriage and family therapist licensed under chapter 18.225 RCW may not disclose, or be compelled to testify about, any information acquired from persons consulting the individual in a professional capacity when the information was necessary to enable the individual to render professional services to those persons except:

(a) With the written authorization of that person or, in the case of death or disability, the person's personal representative;

(b) If the person waives the privilege by bringing charges against the mental health counselor licensed under chapter 18.225 RCW;

(c) In response to a subpoena from the secretary of health. The secretary may subpoena only records related to a complaint or report under RCW 18.130.050;

(d) As required under chapter 26.44 or 74.34 RCW or RCW 71.05.360 (8) and (9); or

(e) To any individual if the mental health counselor, independent clinical social worker, or marriage and family therapist licensed under chapter 18.225 RCW reasonably believes that disclosure will avoid or minimize an imminent danger to the health or safety of the individual or any other individual; however, there is no obligation on the part of the provider to so disclose.

[2012 c 29 § 12; 2009 c 424 § 1; 2008 c 6 § 402; 2007 c 472 § 1. Prior: 2006 c 259 § 2; 2006 c 202 § 1; 2006 c 30 § 1; 2005 c 504 § 705; 2001 c 286 § 2; 1998 c 72 § 1; 1997 c 338 § 1; 1996 c 156 § 1; 1995 c 240 § 1; 1989 c 271 § 301; prior: 1989 c 10 § 1; 1987 c 439 § 11; 1987 c 212 § 1501; 1986 c 305 § 101; 1982 c 56 § 1; 1979 ex.s. c 215 § 2; 1965 c 13 § 7; Code 1881 § 392; 1879 p 118 § 1; 1877 p 86 § 394; 1873 p 107 § 385; 1869 p 104 § 387; 1854 p 187 § 294; RRS § 1214. Cf. 1886 p 73 § 1.]