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No. _____

SUPREME COURT
OF THE STATE OF WASHINGTON

No. 64712-1-1

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

NATIONAL SURETY CORPORATION,

Petitioner,

v.

IMMUNEX CORPORATION,

Respondent.

PETITION FOR REVIEW

BULLIVANT HOUSER
BAILEY PC

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A. Identity of Petitioner.

National Surety Corporation, plaintiff in the Superior Court and respondent/cross-appellant in the Court of Appeals, asks the Court to accept review of Parts II through IV of the Court of Appeals decision designated in Part B holding that National Surety may have an obligation to pay costs incurred by its insured Immunex Corporation in defending claims that were not covered by National Surety's CGL policy.

B. Court of Appeals' Decision.

Division One's published decision was filed July 25, 2011. The panel denied National Surety's timely motion for reconsideration on August 24, 2011. A copy of the decision is attached as Appendix A and is published at 162 Wn. App. 762, 256 P.3d 439 (2011). A copy of the Order Denying Motion for Reconsideration is attached as Appendix B.

C. Issues Presented For Review.

1. Whether an insurer's good faith duty to defend under *Woo* and *Alea* can extend to require the insurer to reimburse an insured for its independently-incurred costs of defending a claim that the insurer has no contractual obligation to defend under the terms of its policy?

2 Whether an insurer that does not have a contractual duty to defend can be liable for costs incurred by its insured in defending itself prior to the insured's tender of the uncovered claim?

D. Statement Of The Case.

Drug manufacturers' "average wholesale price" (AWPs) are intended to be based on the actual wholesale prices paid by health care providers. AWP's are used to determine the rate at which health care providers will be reimbursed for the drugs. Between 1997 and 2005, Immunex and many other drug manufacturers were named as defendants in at least 23 complaints, filed mostly by states and counties, claiming that the defendant drug manufacturers had fraudulently overstated the AWP's of prescription drugs, thereby increasing the cost of these drugs to plaintiff health care benefit payors who paid artificially inflated prices to health care providers for the drugs ("the AWP suits"). CP 361-62; **National Surety Corp. v. Immunex Corp.**, 162 Wn. App. 762, 767 ¶ 3, 256 P.3d 439 (2011)(Appendix A).

In the AWP suits the plaintiff health care benefit payors alleged a variety of claims, including RICO, state unfair trade and protection statutes, civil conspiracy, fraud, and breach of contract,

against Immunex and the other drug manufacturer defendants. See, e.g., CP 376, 492, 520-21; 162 Wn. App. at 767, ¶ 2. None of the AWP suits alleged “discrimination,” and none of the AWP suits alleged that Immunex had caused damage by selling drugs at different prices to differently-placed persons or entities. See, e.g., CP 377, 493-94, 523-24, 559, 579.

Immunex defended itself in the AWP suits, and did not tender defense to its CGL insurer petitioner National Surety, for at least six years, until October 3, 2006, after Immunex (and its obligations) were purchased by Amgen. CP 1059; 162 Wn. App. at 768, ¶ 5. In its October 2006 “tender” letter, Amgen announced that it was close to finalizing a settlement of the California AWP suit against Immunex, identified nine (of the 23 suits for which it now claims coverage) other lawsuits in which Immunex had been sued on similar fraudulent misrepresentation claims, and demanded that National Surety pay “reasonable defense expenditures incurred, and . . . fund reasonable settlements . . .”. CP 1059-60.

Amgen asserted that National Surety had a duty to defend Immunex under Coverage B of CGL policies that provided coverage for personal injury “arising out of . . . discrimination (unless insurance thereof is prohibited by law).” CP 647, 654; 162

Wn. App. at 770, ¶ 11. The CGL policy gave National Surety the “right and duty to . . . defend” claims covered by Coverage B, but also expressly provided that National Surety would “have no duty to defend” any claim that was not covered:

B. COVERAGE B – WHEN WE WILL HAVE A DUTY TO DEFEND.

We will have the right and duty to investigate any claim, or defend any insured against any Suit, seeking damages . . . to which Coverage B applies . . . *However, we will have no duty to defend any insured against any Suit seeking damages to which Coverage B does not apply.*

CP 630-31 (emphasis added).

National Surety responded less than a month after the belated tender, asking that any suit papers be submitted for review. CP 1062-63. Immunex first forwarded copies of complaints, motions, and orders, in only some of the cases for which it now seeks reimbursement of defense costs, in December 2006. CP 1065. After many months of negotiating access to information about the AWP suits, National Surety finally obtained sufficient facts about the claims to make a determination that the AWP suits were not covered by its CGL policy. CP 1067. In its March 31, 2008 reservation of rights, National Surety offered to reimburse reasonable defense fees and costs from October 3, 2006, the date

of tender,¹ subject to a right to recoup any amounts paid when a court determined that there was no coverage or duty to defend.² 256 P.3d at 442, ¶ 6.

National Surety commenced this action for a declaratory judgment simultaneously with its reservation of rights. CP 1-9. Immunex resisted resolution of the coverage dispute, claiming it was “inappropriate” for National Surety to attempt to establish whether it had a duty to defend the belatedly tendered AWP suits until the underlying litigation was finally concluded, and that this action would prejudice *Immunex’s* control of the defense of the AWP suits.³ CP 590, 592; 162 Wn. App. at 768-69 ¶ 7. Immunex obtained a stay of this declaratory judgment action, which was lifted over Immunex’s objection on December 16, 2008, solely to allow

¹ “The lawsuits were tendered to [National Surety] for defense on October 3, 2006 . . . , and that is the date from which [National Surety] is prepared to reimburse reasonable defense fees and costs.” CP 1074.

² “[National Surety] reserves the right to recoup the amounts paid in defense if it is determined by the court that there is no coverage or duty to defend and that [National Surety] is entitled to reimbursement.” CP 1075.

³ Contrary to Immunex’s position, the parties’ agreement required Immunex not only to provide prompt notice of a claim but to refrain from incurring “any expense, except first aid,” to “assume no obligation” without the permission of National Surety, and to “cooperate with [the insurer] in . . . defense of any Insured against any Suit.” CP 1103 (emphasis in original omitted).

the parties to present motions on the issue of National Surety's duty to defend. CP 1025.

The trial court granted National Surety's motion for summary judgment confirming that it had no duty to defend under its policy on April 14, 2009. CP 1025. The stay was again lifted on June 24, 2009, so that the court could determine whether National Surety was responsible for defense costs, whether National Surety had a duty to indemnify, and whether National Surety was prejudiced as a matter of law by late notice of the AWP suits. CP 1028. Even though National Surety had no contractual duty to defend, the trial court held that National Surety had an obligation to pay defense costs until April 14, 2009, the date of the court's determination that National Surety had no duty to defend under its CGL policy, unless National Surety could prove at trial that it had been prejudiced by late notice of the AWP suits. CP 1359. The trial court certified its order as a final judgment pursuant to CR 54(b). CP 1118-20.

On Immunex's appeal, Division One concluded that National Surety had no contractual duty to defend the AWP suits because "the offenses alleged in the AWP complaints do not arise out of discrimination." 162 Wn. App. at 773, ¶ 20. Division One correctly rejected Immunex's claims based on this Court's direction in *Kitsap*

County v. Allstate Ins. Co., 136 Wn.2d 567, 580, 964 P.2d 1173 (1998), that “to determine whether coverage exists, we must look to the type of offense that is alleged rather than the nature of the injury.” 162 Wn. App. at 772, ¶ 18.

On National Surety’s cross-appeal, Division One held that National Surety must nonetheless pay Immunex’s defense costs, including defense costs incurred by Immunex prior to its tender of the AWP-suits to National Surety six years after Immunex was first sued, unless National Surety prevails at trial in establishing that it was prejudiced by the delayed tender. 162 Wn. App. at 782, ¶ 41. National Surety seeks review only of Parts II through IV of Division One’s published opinion holding that it may be liable for defense costs it was not contractually obligated to pay, including defense costs independently incurred by Immunex before tender.

E. Argument Why This Court Should Accept Review.

- 1. Division One Erroneously Held That An Insurer’s Good Faith Duty To Defend Uncovered Claims Under a Reservation Of Rights Can Extend To Reimbursement Of Defense Costs Independently Incurred By A Sophisticated Corporate Insured.**

Immunex controlled defense of the AWP suits for over six years without tender to its insurer National Surety. It then demanded that National Surety pay millions of dollars for fees and

indemnity on the eve of its independent settlement of many of the claims. The Court of Appeals' published decision presents an issue of substantial public concern to insurers and their insureds state-wide. This Court should accept review under RAP 13.4(b)(4) to determine whether an insurer's good faith duty to defend under a reservation of rights can extend to an obligation to reimburse an insured for its independently-incurred costs of defending a claim that is not covered by the insurer's policy.

Any obligation to pay defense costs in this case is not contractual, but arises from the good faith duty to defend imposed by this Court in *Woo v. Fireman's Fund Ins. Co.*, 161 Wn.2d 43, 164 P.3d 454 (2007) and *American Best Food, Inc. v. Alea London, Ltd.*, 168 Wn.2d 398, 229 P.3d 693 (2010). National Surety acknowledged and complied with this good faith duty imposed by Washington law. Upon tender, it made a good faith offer to defend Immunex by paying post-tender defense costs that was expressly conditioned on a right to reimbursement of amounts that National Surety was not contractually obligated to pay. CP 1074-75. Division One's published decision dramatically expands National Surety's obligation in a manner that is both contrary to the parties' insurance contract (which imposed *no* obligation on

National Surety to defend an uncovered claim), and that is an unprecedented extension of an insurer's good faith duty to defend under a reservation of rights pending judicial resolution of coverage.

In **Woo**, this Court held that an insurer must in good faith provide a defense to its insured until a court determines whether the insurer had contractual duty to defend whenever there is an arguable basis that an insurer owes a contractual duty to defend. 161 Wn.2d at 54, ¶ 19. In **Alea**, this Court held that an insurer's failure to provide such a defense under a reservation of rights was bad faith as a matter of law. 168 Wn.2d at 413, ¶ 20. In both **Woo** and **Alea**, however, the insurers had a contractual duty to defend their insureds. 161 Wn.2d at 57, ¶ 27; 168 Wn.2d at 411, ¶ 16.⁴ Thus, as Division One recognized, 162 Wn. App. at 774-77, ¶¶ 24-29, this Court has never decided the issue here, which is whether the insured or the insurer bears ultimate responsibility to pay for the cost of a defense that the insured did *not* contract to receive and

⁴ That was also the case in **Truck Ins. Exchange v. VanPort Homes, Inc.**, 147 Wn.2d 751, 58 P.3d 276 (2002), in which the insurer breached its *contractual* duty to defend and consequently was obligated to pay the reasonable costs incurred by the insured in defending itself. **VanPort** is discussed more extensively in National Surety's second argument why review should be accepted, *infra* at 16-17.

the insurer did *not* contract to provide. This Court should accept review to resolve that question.

There is no basis in law or policy to require an insurer to reimburse its insured for defense costs where, as here, the insurer properly reserves its rights, files a declaratory judgment action, and a court correctly determines the policy does not obligate the insurer to defend the tendered claims. An insurer cannot be required to pay defense costs it has no contractual obligation to pay. See ***Scottsdale Ins. Co. v. MV Transp.***, 36 Cal.4th 643, 31 Cal.Rptr.3d 147, 154, 115 P.3d 460, 466 (2005) (judicial determination that insurer had no contractual duty to defend triggered right to recoup defense costs paid under reservation of rights). If an insurer in good faith protects its insured's interests by offering to pay defense costs under a reservation of rights until the coverage dispute is resolved, as National Surety did here, such conduct cannot change the terms of the parties' insurance contract, because the insurer's obligation arose outside the terms of its policy. The insured is not entitled to benefits that the insurer did not contract to provide and that the insured paid no premium to receive.

Imposing an obligation to reimburse an insured for defense costs in the absence of a contractual duty to defend undermines

the reciprocal duty of good faith imposed upon both insureds and insurers by Washington law. RCW 48.01.030. As argued below, it discourages an insured from promptly tendering the defense of claims to its insurer and undermines the ability of an insurer to obtain a prompt resolution of the issue of coverage by filing a declaratory judgment action, contrary to ***Mutual of Enumclaw Ins. Co. v. USF Ins. Co.***, 164 Wn.2d 411, 420-23, ¶ 14-22, 191 P.3d 866 (2008); ***Woo***, 161 Wn.2d at 54, ¶ 19; and ***Truck Ins. Exchange v. VanPort Homes, Inc.***, 147 Wn.2d 751, 761, 58 P.3d 276 (2002).

There is no authority, anywhere, for the proposition that an insurer that does not have a contractual duty to defend can nevertheless be obligated to reimburse defense costs if it has not refused a tender of defense. In fact, most courts have held that the policy of encouraging an insurer to promptly provide a defense justifies giving an insurer who has defended under a reservation of rights an affirmative right to *recoup* defense costs from an insured,

even in the absence of express contractual language.⁵ See, e.g., ***Buss v. Superior Court***, 16 Cal.4th 35, 65 Cal.Rptr.2d 366, 378, 939 P.2d 766, 778 (1997) (without a right of reimbursement, an insurer might be tempted to refuse to defend an action); see *generally* 16 COUCH ON INSURANCE 3d § 226:123 (2005).

There is a split of authority in the United States regarding the circumstances under which an insurer may *recoup* defense costs it has actually paid, with some courts allowing recoupment only where the policy expressly provides that right, others where there has been a judicial determination that there is no duty to defend, and others where there is a determination of no coverage, even though the insurer may have had a duty to defend until that determination was made. See *generally* Couch, § 226.123; Marick, *An Insurer's Right to Recoup Non-Covered Defense Costs and*

⁵ Below, Immunex and Division One relied heavily on ***Minnesota Mutual Life Ins. Co. v. Fraser***, 128 Wash. 171, 222 P. 228 (1924) for the proposition that National Surety could not "rewrite" the policy to seek recoupment. 162 Wn. App. at 777, ¶ 29. First, as discussed *supra* at 10, because National Surety had no contractual obligation to pay the cost of defending uncovered claims under its CGL policy, its claim for recoupment of defense costs payable under the terms of its reservation of rights does not "rewrite" the policy. Second, ***Fraser*** does not consider the terms of an insurance policy, but instead addressed whether an employer could recoup advances that had actually been paid to its employee. The case has nothing to do with the duty to defend or with an insurer's good faith obligations to its insured that are at issue in this case.

Indemnity Payments, NEW APPLEMAN ON INSURANCE: CURRENT CRITICAL ISSUES IN INSURANCE LAW (July 2007) (collecting cases). Division One's holding in this published decision goes far beyond establishing the circumstances under which an insurer has the right to recoup costs it has paid in defending an uncovered claim, however. Here, Immunex seeks an unprecedented affirmative right to require an insurer to pay defense costs that it independently incurred in defending lawsuits that the insurer not only had no contractual obligation to defend, but which for years the insured asserted no claim that the insurer was obligated to defend. Under these circumstances, no court has required an insurer to *reimburse* its insured for the cost of defending uncovered claims.

Division One correctly held that National Surety had no contractual duty to defend Immunex. But its published decision fails to recognize the distinction between the contractual duty to defend potentially covered claims and the good faith duty to defend under a reservation of rights that is at issue here. Contrary to Division One's analysis, where a court makes an insurer potentially liable for the cost of an insured's *voluntarily undertaken* defense of uncovered claims, it impermissibly rewrites the parties' contract and modifies the language of the insurance policy. This Court should

accept review under RAP 13.4(b)(4) and hold that an insurer's good faith duty to defend under a reservation of rights cannot extend to an obligation to reimburse an insured for its independently-incurred costs of defending a noncovered claim.

2. Division One Erroneously Held That The Good Faith Duty To Defend Can Require An Insurer To Pay Costs Independently Incurred By The Insured In Defending Uncovered Claims Prior To The Insured's Tender.

National Surety should not in any event be liable for the defense costs incurred by Immunex prior to its tender of some of the AWP suits in October 2006. No authority supports Division One's imposition of an obligation to pay defense costs incurred prior to tender where, as here, there is no contractual duty to defend. This Court should accept review under RAP 13.4(b)(4) and hold that the good faith duty to defend imposed by *Woo* and *Alea* cannot extend to requiring an insurer to pay the costs of defending an uncovered claim incurred by a sophisticated corporate insured prior to tender of defense.

"An insured may choose not to tender a claim to its insurer for a variety of reasons:"

Like a driver involved in a minor accident, an insured may choose not to tender in order to avoid a premium increase. The insured may also want to preserve its

policy limits for other claims, or simply to safeguard its relationship with its insurer. Whatever its reasons, an insured has the prerogative not to tender to a particular insurer.

USF, 164 Wn.2d at 422, ¶ 17. As this Court recognized in **USF**, the one certain consequence of such “selective tender” of a third-party claim is that an insurer to whom no tender has been made by its insured should have no obligation to defend or indemnify the claim. 164 Wn.2d at 420-23, ¶¶ 15-22.

Even where claims fall within the scope of a policy, an insurer’s contractual duty to defend cannot arise unless and until it is asked to defend. See **USF**, 164 Wn.2d at 421 ¶15, (“the duties to defend and indemnify do not become *legal obligations* until a claim for defense or indemnity is tendered”) (emphasis in original; footnote omitted). “[A]n insurer’s duty to defend does not arise unless the insured specifically asks the insurer to undertake the defense of the action.” **Unigard Ins. Co. v. Leven**, 97 Wn. App. 417, 426-27, 983 P.2d 1155 (1999) (“an insurer cannot be expected to anticipate when or if an insured will make a claim for coverage; the insured must affirmatively inform the insurer that its participation is desired”) (footnote omitted), *rev. denied*, 140 Wn.2d 1009 (2000).

“Subject to policy-based defenses,” an insurer that has a *contractual* duty to defend may then be “liable for fees and costs incurred before the insured tenders defense of a *covered* claim.” ***Griffin v. Allstate Ins. Co.***, 108 Wn. App. 133, 136, 29 P.3d 777, (2001), (emphasis added) *rev. denied*, 146 Wn.2d 1005 (2002). But neither ***Griffin*** nor any other authority supports imposing upon an insurer the obligation to pay for the insured’s independently-incurred cost of defending *uncovered* claims before tender.

This Court considered a CGL insurer’s wrongful refusal to defend negligence claims its insured had tendered shortly after being sued in ***VanPort***. The insurer waited almost four years after denying coverage before filing a declaratory judgment action; the insured’s principals went bankrupt in incurring the burden of defending the insured during that delay. In noting that “[a]n insurer may be responsible for defense costs prior to tender,” 147 Wn.2d at 760 n.5, the ***VanPort*** Court pointed out that the insurer could “defend under a reservation of rights while seeking a declaratory judgment that it had no duty to defend.” 147 Wn.2d at 761, *citing* ***Grange Ins. Co. v. Brousseau***, 113 Wn.2d 91, 93-94, 776 P.2d 123 (1989). This Court then confirmed, however, that where “that course of action is taken, the insured receives the defense

promised and, if coverage is found not to exist, *the insurer will not be obligated to pay.*” **VanPort**, 147 Wn.2d at 761, quoting **Kirk v. Mt. Airy Ins. Co.**, 134 Wn.2d 558, 563 n. 3, 951 P.2d 1124 (1998) (emphasis added).

The Court made these statements where the insurer had breached its contractual duty to defend in **VanPort**. 147 Wn.2d at 763. The issue in **Kirk** was the insurer’s duty to indemnify in light of its bad faith in breaching its contractual duty to defend. 134 Wn.2d at 564. These cases anticipate but do not decide the issue presented here, which is whether an insurer should ever be obligated to pay the costs of defending an *uncovered* claim prior to tender, when it has fulfilled its good faith duties by offering to pay the cost of defense under a reservation of rights. In the instant case, National Surety took the correct course of action, offering Immunex a defense as soon as the claims were tendered and Immunex gave it information sufficient to make a coverage determination, while properly reserving its right to contest whether those claims fell within its policy’s coverage for discrimination, all as contemplated by both **VanPort** and **Woo**. National Surety then promptly sought a declaratory judgment, in which the trial court correctly held that it had no contractual duty to defend. No

authority supports Division One's decision requiring an insurer to reimburse its insured for pre-tender defense costs of uncovered claims under these circumstances.

Immunex's delay in tender prevented National Surety from obtaining a determination that the AWP suits were not covered by its CGL policy for over six years. Indeed, Immunex continued to resist resolution of the coverage dispute even after this action was commenced, obtaining a stay of the determination whether the claims were covered because it wanted to continue to control the defense and settlement of the AWP litigation. CP 590; see CP 1025. Yet at the same time Immunex was delaying the coverage determination, it asserted a right to reimbursement of defense costs that it had independently incurred years before tender until the lack of coverage was confirmed by the court.

Neither the good faith obligation of an insurer to pay defense costs until the lack of coverage is confirmed, nor the requirement that an insurer must prove prejudice to invoke contractual defenses to coverage, can be construed to encourage both an insured's late tender and its insistence on a delay of the coverage determination. Actual prejudice includes "some advantage lost or disadvantage suffered as a result of the delay, which has an identifiable

detrimental effect on the insurer's ability to evaluate or present its defenses to coverage. . . ". **Canron, Inc. v. Federal Ins. Co.**, 82 Wn. App. 480, 490-91, 918 P.2d 937 (1996), *rev. denied*, 131 Wn.2d 1002 (1997), *cited with approval in USF*, 164 Wn.2d at 429, ¶¶ 34-35. Such actual prejudice is indisputably present here, where National Surety's potential liability for the cost of defending uncovered claims has been extended for many years, and by many millions of dollars, by Immunex's late tender and delay.

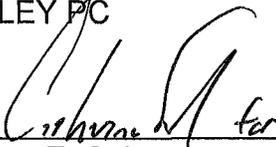
Division One's published decision gives insureds – particularly sophisticated corporate insureds such as Immunex – powerful incentive to delay tender, and especially to belatedly tender uncovered claims contrary to their contractual obligations and public policy. This Court should accept review under RAP 13.4(b)(4) and hold that an insurer cannot be obligated to pay pre-tender defense costs of an uncovered claim and that prejudice to the insurer is established as a matter of law when, as here, an insured in violation of its obligations under the policy delays tender of an uncovered claim for years in order to control the defense and settlement of the claims without the consent of its insurer.

F. Conclusion.

This Court should accept review of Parts II through IV of Division One's published decision, specify the issues for review as those raised in this petition, RAP 13.6, and hold that National Surety has no obligation to reimburse Immunex for its voluntarily incurred defense of the uncovered AWP claims, or that in no event can National Surety have an obligation to reimburse costs incurred by Immunex in defending uncovered claims prior to the insured's tender of defense in October 2006.

Dated this 23rd day of September, 2011.

BULLIVANT HOUSER
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By: 

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Howard M. Goodfriend
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Attorneys for Petitioner

DECLARATION OF SERVICE

The undersigned declares under penalty of perjury, under the laws of the State of Washington, that the following is true and correct:

That on September 23, 2011, I arranged for service of the Petition For Review, to the court and to the parties to this action as follows:

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DATED at Seattle, Washington this 23rd day of September, 2011.



Carrie L. Steen

256 P.3d 439
Court of Appeals of Washington,
Division 1.

NATIONAL SURETY CORPORATION,
Respondent/Cross Appellant,
v.
IMMUNEX CORPORATION,
Appellant/Cross Respondent.

No. 64712-1-I. July 25,
2011. Reconsideration Denied Aug. 29, 2011.

Synopsis

Background: Umbrella and excess liability insurer brought declaratory judgment action seeking determination as to whether it owed duty to defend insured, a drug manufacturer, in underlying lawsuits regarding insured's alleged use of inflated average wholesale price. The Superior Court, King County, Steven C. Gonzalez, J., ruled that insurer owed not duty to defend, but ordered insurer to compensate insured for defense costs until the time of the court's ruling on the duty to defend. Insured appealed and insurer cross-appealed.

Holdings: The Court of Appeals, Appelwick, J., held that:
1 underlying litigation did not arise out of discrimination;
2 insurer was required to reimburse defense costs;
3 insurer was liable for pre-tender defense costs if prejudice was not shown; and
4 genuine issue of material fact existed regarding prejudice.

Affirmed.

West Headnotes (28)

1 Insurance

☞ Personal Injury

Underlying litigation alleging that insured, a drug manufacturer, artificially inflated the average wholesale price (AWP) of drugs did not arise out of discrimination, and therefore umbrella and excess liability insurer did not have duty to defend insured in lawsuits pursuant to personal injury clause of policy; while it was true that some complaints alleged that consumers of certain groups paid a higher price as a result of insured's actions, the offenses originated not from discriminatory actions but from fraudulently

inflating the AWP, and, although the effect of that action might have impacted some consumers and providers more than others, that did not mean the offenses originated from discrimination.

2 Appeal and Error

☞ Cases Triable in Appellate Court

A motion for summary judgment presents a question of law reviewed de novo.

3 Insurance

☞ Application of rules of contract construction

The court construes insurance policies as contracts.

4 Insurance

☞ Construction as a whole

When construing an insurance policy, the court considers the policy as a whole, and the Court gives it a fair, reasonable, and sensible construction as would be given to the contract by the average person purchasing insurance.

5 Insurance

☞ Construction or enforcement as written

If the language of an insurance policy is clear and unambiguous, the court must enforce it as written.

6 Insurance

☞ Function of, and limitations on, courts, in general

Insurance

☞ Ambiguity in general

When construing an insurance policy, the court may not modify it or create ambiguity where none exists.

7 Insurance

☞ Ambiguity in general

A clause in an insurance policy is only considered ambiguous if it is susceptible to two or more reasonable interpretations.

8 Insurance

☞ Ambiguity, Uncertainty or Conflict

If an ambiguity exists in a clause of an insurance policy, the clause is construed in favor of the insured.

9 Insurance

☞ Plain, ordinary or popular sense of language

The expectations of the insured cannot override the plain language of an insurance policy.

10 Insurance

☞ Advertising Injury

Insurance

☞ Personal Injury

To determine whether coverage exists under the personal and advertising injury provisions of a liability insurance policy, the court must look to the type of offense that is alleged rather than the nature of the injury.

11 Insurance

☞ Termination of duty; withdrawal

Umbrella and excess liability insurer was required to reimburse insured, a drug manufacturer, for defense costs paid by insured for purposes of underlying action arising out of insured's alleged fraudulent inflation of drug prices until point when trial court determined that insurer owed insured no duty to defend under policy; although insurer was ultimately found not to have a duty to defend, the duty to defend attached at the point that a complaint was filed alleging a potentially covered claim and duty to defend continued to exist up until point when trial court declared that the duty did not exist, and insurer benefited by providing initial defense as it insulated itself from a bad faith claim and possible coverage by estoppel.

12 Insurance

☞ Insurer's Duty to Indemnify in General

The duty to indemnify exists only if the policy actually covers the insured's liability.

13 Insurance

☞ Pleadings

The duty to defend arises when a complaint against the insured, construed liberally, alleges facts which could, if proven, impose liability upon the insured within the policy's coverage.

14 Insurance

☞ Pleadings

An insurer is not relieved of its duty to defend unless the claim alleged in the complaint is clearly not covered by the policy.

15 Insurance

☞ Pleadings

If a complaint is ambiguous, a court will construe it liberally in favor of triggering the insurer's duty to defend.

16 Insurance

☞ Insurer's Duty to Indemnify in General

The duty to indemnify hinges on the insured's actual liability to the claimant and actual coverage under the policy.

17 Insurance

☞ Termination of duty; withdrawal

An insurer must defend until it is clear that the claim is not covered.

18 Insurance

☞ In general; nature and source of duty

Payment of defense costs for claims that are potentially covered is part of the bargained-for exchange between the insurer and the insured.

19 Implied and Constructive Contracts

↔ Unjust enrichment

To establish a theory of unjust enrichment, a party must show: (1) a benefit conferred upon the defendant by the plaintiff; (2) an appreciation or knowledge by the defendant of the benefit; and (3) circumstances that would make it inequitable for the defendant to retain the benefit without the payment of its value.

20 Insurance

↔ Pre-tender expenses

Insurance

↔ Tender or other notice

Umbrella and excess liability insurer was liable for pre-tender defense costs in underlying lawsuits against insured, a drug manufacturer, in which it was alleged that insured fraudulently inflated drug prices, unless insurer could show substantial and actual prejudice from late tender; even though the policy required tender as a condition precedent to the duty to defend, a showing of actual and substantial prejudice was required before an insured's breach would release an insurer from its duty to defend.

21 Insurance

↔ Tender or other notice

The insured must affirmatively inform the insurer that its participation is desired in order to trigger the duty to defend.

22 Insurance

↔ Tender or other notice

Breach of the duty to defend cannot occur before tender.

23 Insurance

↔ Tender or other notice

Even if the policy requires tender as a condition precedent to the duty to defend, a showing of actual and substantial prejudice is required before an insured's breach will release an insurer from its duty to defend.

24 Judgment

↔ Insurance cases

Genuine issue of material fact existed regarding whether insurer was substantially and actually prejudiced as a result of insured's allegedly late tender for purposes of insurer's duty to defend insured, a drug manufacturer, in underlying lawsuits alleging that insured fraudulently inflated drug prices, and therefore summary judgment in favor of insurer was precluded on claim that insurer did not owe pre-tender defense costs.

25 Insurance

↔ Pre-tender expenses

Insurance

↔ Tender or other notice

In order to show prejudice due to an insured's late tender so as to avoid liability for pre-tender defense costs, the insurer must prove that an insured's breach of a notice provision had an identifiable and material detrimental effect on its ability to defend its interests.

26 Insurance

↔ Pre-tender expenses

Insurance

↔ Tender or other notice

If the insurer claims that its own counsel would have defended differently, it must show that its participation would have materially affected the outcome, either as to liability or the amount of damages in order to show prejudice from an insured's late tender so as to avoid liability for pre-tender defense costs.

27 Insurance

⚡ Pre-tender expenses

Insurance

⚡ Tender or other notice

If the insurer claims that it was deprived of the ability to investigate, it must show that the kind of evidence that was lost would have been material to its defense in order to show prejudice due to an insured's late tender so as to avoid liability for pre-tender defense costs.

28 Insurance

⚡ Questions of law or fact

Insurance

⚡ Questions of law or fact

Whether or not late notice prejudiced an insurer so as to permit insurer to avoid liability for pre-tender defense costs is a question of fact, and it will seldom be decided as a matter of law.

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Opinion

APPELWICK, J.

¶ 1 Immunex challenges the trial court ruling that National Surety does not have a duty to defend in several lawsuits challenging Immunex's use of an inflated average wholesale price. National Surety cross appeals the trial court's order that it compensate Immunex for defense costs until the time of the court's ruling on the duty to defend unless it can show prejudice at trial. We affirm.

FACTS

¶ 2 Immunex¹ Corporation and many other drug manufacturers were sued in at least 23 complaints (AWP litigation) alleging several claims relating to Immunex artificially inflating its average wholesale price (AWP). The claims included RICO (Racketeer Influence and Corrupt Organizations Act, 18 U.S.C. §§ 1961–1968) claims, state unfair trade and protection statutes violations, civil conspiracy, fraud, and breach of contract.

¶ 3 To summarize the underlying litigation, physicians and other providers of drugs are reimbursed by Medicare and other third party *442 payors based on the AWP of the drug. Manufacturers periodically report the AWP of drugs to publishers, who then list that price. Immunex and other drug manufacturers allegedly engaged in a scheme to fraudulently manipulate the AWP of their drugs. As part of this scheme, the claims allege that Immunex reported inflated AWP's which materially misrepresented the actual prices paid to Immunex for prescription drugs by drug providers such as hospitals, pharmacies, and physicians. As a result, drug providers were reimbursed significantly more money than they paid for Immunex manufactured drugs. Also, the claims allege Immunex advertised the difference or "spread" in prices as a reason why those in the distribution chain should sell its drugs, thus increasing its share of the generic drug market. The plaintiffs in the AWP cases include consumers, third party payors, government entities, and consumer rights groups.

¶ 4 National Surety Corporation insured Immunex under an umbrella and excess liability insurance policy. The policy periods at issue are from September 1, 1998 to September 1, 2002. On August 21, 2001, Immunex informed National Surety that potential claims had arisen against Immunex, specifically a qui tam investigation² by the United States Department of Health and Human Services, as well as government investigations initiated by several states. Immunex also notified National Surety that the federal investigation related to a 1995 lawsuit. But, Immunex stated that it could not release information about the investigations because the government required a signed confidentiality agreement. National Surety acknowledged receipt of that notice on October 17, 2001. National Surety asked Immunex to send copies of the suit papers to determine coverage when available. On February 14, 2003, Immunex sent a status report, updating National Surety on the status of

the investigations but not notifying National Surety of the AWP lawsuits or forwarding documentation related to those lawsuits. The first AWP litigation complaint was filed on November 27, 2001.

¶ 5 On October 3, 2006, Immunex tendered defense of the AWP suits to National Surety and sought payment for the defense expenditures it had incurred. On October 30, 2006, National Surety responded, disclaiming the duty to defend based on failure to provide suit papers and requesting the necessary documentation. On December 12, 2006, Immunex sent copies of complaints, motions, and orders for some AWP cases.

¶ 6 The parties continued to discuss coverage. In March 2008, National Surety denied coverage but agreed under a reservation of rights to provide a defense with the right to obtain reimbursement of the amounts paid if it was determined by a court that there was no coverage or no duty to defend. Immunex alleges that National Surety has not paid any defense costs incurred in the AWP litigation.

¶ 7 Also in March 2008, National Surety filed this action, seeking a declaratory judgment that National Surety owed no duties to Immunex under the policy. In June 2008, the trial court granted Immunex's motion for a stay to prevent National Surety's declaratory action from proceeding until the underlying litigation had been resolved. The stay was apparently granted before the parties conducted any discovery. On December 16, 2008, the stay was lifted solely to permit the parties to present motions on the issue of National Surety's duty to defend.

¶ 8 Both parties presented motions for partial summary judgment on the issue of National Surety's duty to defend Immunex in the AWP litigation. On April 15, 2009, the trial court granted National Surety's motion for summary judgment, determining that National Surety had no duty to defend.

¶ 9 After stipulating to again lifting the stay, National Surety filed a motion for summary judgment regarding indemnity,³ an *443 alternative motion for summary judgment regarding late notice, and a motion for summary judgment regarding the payment of defense costs in July 2009. Immunex also filed a motion for partial summary judgment regarding the payment of defense fees and costs. The trial court denied National Surety's motion regarding payment of defense fees and costs and granted Immunex's motion regarding same, finding that that unless National Surety could prove prejudice from late

notice at trial, it could be obligated to pay defense costs until the date the court confirmed the claims were not covered. The trial court denied National Surety's motion to reconsider. The trial court then entered partial final judgment pursuant to CR 54(b) in order to permit this appeal to proceed.

¶ 10 Immunex appeals. National Surety cross appeals.

DISCUSSION

I. Duty to Defend

1 ¶ 11 Immunex alleges that the trial court erred when it granted summary judgment to National Surety on the basis that National Surety had no duty to defend Immunex in the AWP litigation. Immunex contends that National Surety owed a duty to defend Immunex against the AWP litigation under the "discrimination" provision of the policy.

2 ¶ 12 A motion for summary judgment presents a question of law reviewed de novo. *Osborn v. Mason County*, 157 Wash.2d 18, 22, 134 P.3d 197 (2006). A trial court grants summary judgment if there is no genuine issue as to any material fact and the moving party is entitled to a judgment as a matter of law. CR 56(c).

¶ 13 Pursuant to the "personal injury" coverage within the policy at issue as modified by the endorsement,⁴ National Surety was required to provide coverage for "Personal and Advertising injury that is caused by an offense arising out of [Immunex's] business but only if the offense was committed during our Policy Period."⁵ The policy defined "Personal and Advertising injury" as "injury, including consequential Bodily Injury, arising out of one or more of the following offenses[, including] Discrimination." Neither the policy nor the endorsement defined "offense" or "discrimination."

¶ 14 The trial court found:

"Discrimination" means more than a distinction or difference. The AWP complaints do not allege damages caused by discrimination. The complaints claim that Immunex, with or without the complicity of providers, gave false pricing information to those who paid the providers for drugs.

The trial court granted partial summary judgment in favor of National Surety, concluding that National Surety did not have a duty to defend Immunex in the AWP litigation.

¶ 15 Immunex alleges that a “predominant theme” of the underlying AWP litigation is discrimination, taking three forms: discrimination in pricing between AWP plaintiffs and providers, discrimination in pricing among providers, and a disparate impact on older Americans. National Surety contends that the policy was not triggered because no AWP plaintiff alleged “discrimination” claims and each complaint sought recovery based solely on fraudulent overstatement of AWP. Interpretation of an insurance policy is a question of law reviewed de novo. *Woo v. Fireman's *444 Fund Ins. Co.*, 161 Wash.2d 43, 52, 164 P.3d 454 (2007).

3 4 5 6 7 8 9 ¶ 16 The criteria for interpreting insurance policies in Washington are well settled. We construe insurance policies as contracts. *Weyerhaeuser Co. v. Commercial Union Ins. Co.*, 142 Wash.2d 654, 665, 15 P.3d 115 (2000). We consider the policy as a whole, and we give it a “ ‘fair, reasonable, and sensible construction as would be given to the contract by the average person purchasing insurance.’ ” *Id.* at 666, 15 P.3d 115 (quoting *Am. Nat'l Fire Ins. Co. v. B & L Trucking & Const. Co.*, 134 Wash.2d 413, 427–28, 951 P.2d 250 (1998)). Most importantly, if the policy language is clear and unambiguous, we must enforce it as written; we may not modify it or create ambiguity where none exists. *Quadrant Corp. v. Am. States Ins. Co.*, 154 Wash.2d 165, 171, 110 P.3d 733 (2005). A clause is only considered ambiguous if it is susceptible to two or more reasonable interpretations. *Id.* If an ambiguity exists, the clause is construed in favor of the insured. *Id.* at 172, 110 P.3d 733. However, “the expectations of the insured cannot override the plain language of the contract.” *Id.*

¶ 17 The trial court found, “The AWP complaints do not allege damages caused by discrimination.”⁶ Immunex argues that the trial court incorrectly required the AWP complaints to allege injuries directly caused by discrimination in order for National Surety's duty to defend to be triggered. Immunex alleges that the AWP plaintiffs' claims “arise out of” discrimination, and therefore the duty to defend was triggered.

10 ¶ 18 Immunex claims that the policy requires a duty to defend “as long as the claimants allege injury potentially and loosely based at least in part upon ‘discrimination.’ ” But, under *Kitsap County v. Allstate Ins. Co.*, 136 Wash.2d 567, 580, 964 P.2d 1173 (1998), to determine whether coverage exists, we must look to the type of offense that is alleged rather than the nature of the injury.⁷ See also *Cle Elum Bowl, Inc. v. N. Pac. Ins. Co.*, 96 Wash.App. 698, 707,

981 P.2d 872 (1999) (“[The insured] misunderstands a basic tenet of *Kitsap County*: the theory underlying the claim against the insured, not the nature of the alleged injury, determines whether personal injury coverage or bodily injury and property damage coverage applies.”). Unlike the claims in *Kitsap County*, the claims here for violations of consumer protection statutes and other similar claims are not analogous to claims of discrimination.

¶ 19 Therefore, we must look to the type of offense that is alleged and determine whether that offense is arising out of discrimination. Immunex seeks too broad of an interpretation of the term “arising out of.” Washington courts have previously defined “arising out of” as meaning “ ‘originating from,’ ‘having its origin in,’ ‘growing out of,’ or ‘flowing from.’ ” *Austl. Unlimited, Inc. v. Hartford Cas. Ins. Co.*, 147 Wash.App. 758, 774, 198 P.3d 514 (2008); *Toll Bridge Auth. v. Aetna Ins. Co.*, 54 Wash.App. 400, 404, 773 P.2d 906 (1989); *Avemco Ins. Co. v. Mock*, 44 Wash.App. 327, 329, 721 P.2d 34 (1986). Following those cases, we limit coverage to offenses originating from discrimination; the injuries here do not. While it is true that some AWP complaints alleged that consumers of certain groups paid a higher price as a result of Immunex's actions, the offenses originate not from discriminatory actions but from fraudulently inflating the AWP. Although the effect of that action might have impacted some consumers and providers more than others, that does not mean the *445 offenses originated from discrimination. The theories underlying the offenses are not that the consumers and providers paid higher prices as compared to others, but that the price itself was fraudulently inflated.

¶ 20 Because we agree that the offenses alleged in the AWP complaints do not arise out of discrimination, we need not address Immunex's other arguments that the trial court incorrectly interpreted the terms “discrimination” and “offense.” The trial court did not err in concluding that no coverage existed here.

II. Reimbursement of Defense Costs to Immunex

11 ¶ 21 The trial court found that National Surety had an obligation to pay defense costs until April 14, 2009, the date of the court's determination, unless National Surety could prove at trial that it had been prejudiced by the late notice of the AWP claims. National Surety argues on cross appeal that this was error.

¶ 22 The policy gave National Surety “the right and duty to ... defend any Insured against any Suit, seeking damages ... [t]o which Coverage B applies.” On March 31, 2008, National

Surety denied coverage but agreed to defend Immunex in the AWP litigation under a reservation of rights. Specifically, National Surety agreed to reimburse reasonable defense fees and costs from October 3, 2006, the alleged date of tender. National Surety expressly stated in that letter that it reserved the right to recoup amounts paid in defense if a court ultimately determined that National Surety had no duty to defend. The policy contained no provision permitting recoupment of defense costs paid on behalf of the insured.

¶ 23 The issue here is whether an insurer must reimburse an insured for defense costs paid by the insured when it is determined that the insurer owed no duty to defend or indemnify the insured and the insurance policy does not expressly provide for a right of recoupment. This is an open question in Washington.

12 13 14 15 16 17 ¶ 24 Our Supreme Court has long held that the duty to defend is different from and broader than the duty to indemnify. *Am. Best Food, Inc. v. Alea London, Ltd.*, 168 Wash.2d 398, 404, 229 P.3d 693 (2010). The duty to indemnify exists only if the policy actually covers the insured's liability. *Id.* In contrast, the duty to defend arises when a complaint against the insured, construed liberally, alleges facts which could, if proven, impose liability upon the insured within the policy's coverage. *Id.* An insurer is not relieved of its duty to defend unless the claim alleged in the complaint is "clearly not covered by the policy." *Truck Ins. Exch. v. VanPort Homes, Inc.*, 147 Wash.2d 751, 760, 58 P.3d 276 (2002). Moreover, if a complaint is ambiguous, a court will construe it liberally in favor of "triggering the insurer's duty to defend." *Id.* In contrast, the duty to indemnify "hinges on the insured's actual liability to the claimant and actual coverage under the policy." *Hayden v. Mut. of Enumclaw Ins. Co.*, 141 Wash.2d 55, 64, 1 P.3d 1167 (2000). In sum, the duty to defend is triggered if the insurance policy conceivably covers the allegations in the complaint, whereas the duty to indemnify exists only if the policy actually covers the insured's liability. *Woo*, 161 Wash.2d at 53, 164 P.3d 454; *Hayden*, 141 Wash.2d at 64, 1 P.3d 1167. Therefore, an insurer must defend until it is clear that the claim is not covered. *Woo*, 161 Wash.2d at 53-54, 164 P.3d 454.

18 ¶ 25 The duty to defend attached here at the point that a complaint was filed against Immunex alleging a potentially covered claim.⁸ *446 *Am. Best Food*, 168 Wash.2d at 404, 229 P.3d 693. As other courts have reasoned, payment of defense costs for claims that are potentially covered is part of the bargained-for exchange between the insurer and the insured. *See e.g., Buss v. Superior Court*, 16 Cal.4th 35, 49,

939 P.2d 766, 65 Cal.Rptr.2d 366 (1997) (explaining that an insurer contracts to pay the entire cost of defending claims that are at least potentially covered). The trial court did not err in holding that National Surety had a duty to defend until the trial court declared that the duty did not exist.

¶ 26 This holding is supported by dicta in *Woo*. In that case, the court held that coverage existed and the insurer had a duty to defend. 161 Wash.2d at 66-67, 164 P.3d 454. In dicta, the court reminded insurers that if the insurer is uncertain of its duty to defend, it may defend under a reservation of rights and seek a declaratory judgment that it has no duty to defend, stating: "Although the insurer must bear the expense of defending the insured, by doing so under a reservation of rights and seeking a declaratory judgment, the insurer avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach." *Id.* at 54, 164 P.3d 454.

¶ 27 This proposition derives from a footnote in *Kirk v. Mount Airy Insurance Co.*, 134 Wash.2d 558, 563 n. 3, 951 P.2d 1124 (1998). After holding that the remedy for an insurer's bad faith refusal to defend is a presumption of harm and coverage by estoppel, our Supreme Court suggested: "The insurer can easily avoid all of these issues by defending with a reservation of rights. When that course of action is taken, the insured receives the defense promised and, if coverage is found not to exist, the insurer will not be obligated to pay."⁹ *Id.* This language was quoted later in *Truck Insurance*, where the court held that where an insurer acts in bad faith in refusing to defend, the settlements entered into by insureds with third parties and approved by a court as reasonable will be presumed reasonable. 147 Wash.2d at 755, 761, 58 P.3d 276. This was discussed in dicta in *Holly Mountain Resources, Ltd. v. Westport Insurance Corporation*, 130 Wash.App. 635, 104 P.3d 725 (2005). Relying on *Truck Insurance*, the court defined "reservation of rights" as "a means by which the insurer conditionally defends its insured, subject to potential reimbursement by the insured upon later discovery that there was no duty to defend." *Id.* at 652 n. 8, 104 P.3d 725 (citing *Truck Ins.*, 147 Wash.2d at 761, 58 P.3d 276); *see also Tank v. State Farm Fire & Cas. Co.*, 105 Wash.2d 381, 391, 715 P.2d 1133 (1986) ("We also recognize that insurers, when faced with defending under a reservation of rights, are not without alternatives. They may sue for a declaratory judgment before they undertake a defense, to determine their liability. The company may also instruct an insured to pay for his own defense, reimbursing him for defense costs if the final judgment establishes the company's liability." (citations omitted)).

¶ 28 The cases underlying the statement in *Woo*, 161 Wash.2d at 54, 164 P.3d 454, that “the insurer must bear the expense of defending the insured” discussed the issue of reimbursement only in dicta. Like in *Woo*, no case provides a substantive analysis of the issue of reimbursement raised here. Any discussion to the contrary does not foreclose affirming the trial court's grant of reimbursement to Immunex for the cost of the defense.

¶ 29 We note that the policy at issue did not expressly authorize National Surety to offer a defense under a reservation of rights subject to recoupment. This court cannot rewrite the policy to so allow. In *Minnesota Mutual Life Insurance Co. v. Fraser*, 128 Wash. 171, 175, 222 P. 228 (1924), the Supreme Court held that advances against income earned made to an employee for expenses were not recoverable from the employee when he did not earn the full amount. The court reasoned that there was no indication in the agreement that the advances were intended to be a loan and that the advances benefited the *447 employer. *Id.* Similarly here, where no language in the agreement between the parties permits recoupment, Immunex, the party receiving the benefit, cannot be liable for reimbursement.

¶ 30 National Surety argues that *Fraser* is not analogous and relies on the fact that in that case the employer had actually paid the advances and used them to its benefit. In contrast, here National Surety did not pay out defense costs, act to its benefit, or control the defense. But, the fact that National Surety had not, at the time of the trial court ruling, actually paid the costs of Immunex's defense cannot support a different result here than in a case where the insurer had already provided a defense. It would be unfair to refuse recoupment to an insurer who actually provided a defense while excusing an insurer from reimbursing an insured who undertook its own defense. Such a holding would encourage insurers to avoid payments and would interfere with the policy goal of defending the insured. National Surety argues that to require insurers to reimburse insureds would discourage insurers from providing a defense. But, the risk of a bad faith claim and coverage by estoppel will prevent resistance to provision of a defense.

¶ 31 We also decline to permit insurance companies to assert a unilateral implied contract that would modify the language of the policy. See THOMAS V. HARRIS, WASHINGTON INSURANCE LAW § 17.01, at 17–2 (3d ed. 2010)¹⁰ (“A reservation of rights will never allow an insurer to seek retroactive reimbursement for attorney fees and defense costs

already incurred by the insurer.”). If the policy does not permit an insurer to recoup costs paid under an offer to defend its insured with a reservation of rights, this court will not read such a provision into the policy.

19 ¶ 32 We also decline to require Immunex to pay its own costs for the defense under an equitable theory such as unjust enrichment.¹¹ As recognized by other courts, the offer of a defense under a reservation of rights benefits the insurer as well as the insured, as it allows the insurer to protect its rights and avoids the risk of a poor defense exposing it to liability. See Michael M. Marick, *An Insurer's Right to Recoup Non-Covered Defense Costs and Indemnity Payments*, NEW APPELMAN ON INSURANCE: CURRENT CRITICAL ISSUES IN INSURANCE LAW, July 2007, at 10–11 (quoting *Gen. Agents Ins. Co. of Am., Inc. v. Midwest Sporting Goods Co.*, 215 Ill.2d 146, 163–64, 293 Ill.Dec. 594, 828 N.E.2d 1092 (2005)); *Terra Nova Ins. Co. v. 900 Bar, Inc.*, 887 F.2d 1213, 1219–20 (3d Cir.1989), criticized as dicta in *Cincinnati Ins. Co. v. Grand Pointe, LLC*, 501 F.Supp.2d 1145, 1164 n. 3 (E.D.Tenn.2007). Although here that National Surety has not yet taken on the actual defense of Immunex, National Surety had the benefit of insulating itself from a bad faith claim and possible coverage by estoppel. Therefore, the payment of the defense costs is not purely a gratuity to the insured and no unjust enrichment occurs if National Surety covers the cost of the defense until the trial court ordered otherwise.

¶ 33 We hold that the trial court did not err in ordering National Surety to reimburse Immunex for defense costs until the date that the trial court resolved the disputed coverage.

III. Pre-tender Defense

20 ¶ 34 National Surety additionally argues that, at minimum, it cannot be liable for costs incurred by Immunex prior to tender of some of the AWP lawsuits in October 2006.¹²

*448 21 22 ¶ 35 As previously discussed, an insurer's duty to defend arises when a complaint against the insured alleges facts which could impose liability upon the insured within the policy's coverage. *Mut. of Enumclaw Ins. Co. v. USF Ins. Co.*, 164 Wash.2d 411, 420–21, 191 P.3d 866 (2008). However, “[a]n insurer cannot be expected to anticipate when or if an insured will make a claim for coverage; the insured must affirmatively inform the insurer that its participation is desired.” *Id.* at 421, 191 P.3d 866 (quoting *Griffin v. Allstate Ins. Co.*, 108 Wash.App. 133, 140,

29 P.3d 777, 36 P.3d 552 (2001)). Thus, “ ‘breach of the duty to defend cannot occur before tender.’ ” *Id.* (quoting *Griffin*, 108 Wash.App. at 141, 29 P.3d 777, 36 P.3d 552).

23 ¶ 36 This court in *Griffin* refused to hold that pre-tender fees and costs are not recoverable. 108 Wash.App. at 136, 29 P.3d 777, 36 P.3d 552 (“Subject to policy-based defenses, an insurer is liable for fees and costs incurred before the insured tenders defense of a covered claim.”). In *Griffin*, the insureds tendered their defense to their insurer only after hiring a lawyer themselves. *Id.* at 136–37, 29 P.3d 777, 36 P.3d 552. This court required the insurer to provide pre-tender defense costs. *Id.* at 149, 29 P.3d 777, 36 P.3d 552. We distinguished the breach of a duty to defend, which cannot, under *Leven*, occur prior to tender, and the duty to reimburse an insured for costs incurred prior to tender. *Id.* at 141, 29 P.3d 777, 36 P.3d 552 (“The scope of a duty, however, is defined not by its breach, but by the contract.”). Under *Griffin*, even if the policy required tender as a condition precedent to the duty to defend, as the policy did here,¹³ a showing of actual and substantial prejudice is required before an insured's breach will release an insurer from its duty to defend. *Id.* at 141, 29 P.3d 777, 36 P.3d 552.

¶ 37 National Surety alleges that *Truck Insurance* and *Woo* eroded the rule in *Griffin* by expressly permitting an insurer to defend under a reservation of rights while seeking a declaratory judgment. National Surety distinguishes this case from *Griffin* on the basis that in that case the court found that the insurer actually had an obligation to defend. But, as discussed above, National Surety may be liable for the duty to defend even if this court ultimately agrees that there was no coverage for the AWP litigation. This is still true under *Truck Insurance* and *Woo*. Similarly, National Surety's attempts to rely on *Truck Insurance* makes the assumption that a prompt declaratory judgment action absolves it of the duty to defend. As discussed above, *Truck Insurance* does not support that argument. *Griffin* is still good law.

¶ 38 Unless it can show substantial and actual prejudice, National Surety is liable for pre-tender defense costs. Also, a question of material fact remains regarding whether Immunex's tender of the lawsuit was in fact late. These are issues for trial. The trial court did not err in denying National Surety's motion for summary judgment based on pre-tender costs.

IV. Prejudice As a Matter of Law

24 25 26 27 28 ¶ 39 National Surety argues that prejudice should be presumed in this case as a matter of law as a result of Immunex's allegedly late tender. In order to show prejudice, the insurer must prove that an insured's breach of a notice provision had an identifiable and material detrimental effect on its ability to defend its interests. *Mut. of Enumclaw*, 164 Wash.2d at 430, 191 P.3d 866. If the insurer claims that its own counsel would have defended differently, it must show that its participation would have materially affected the outcome, either as to liability or the amount of damages. *Id.* If the insurer claims that it was deprived of the ability to investigate, it must show that the kind of evidence that was lost would have been material to its defense. *Id.* In *Mutual *449 of Enumclaw*, the court articulated a non-exclusive, illustrative list of factors that courts may use to evaluate prejudice, including: Were damages concrete or nebulous? Was there a settlement or did a neutral decision maker calculate damages; what were the circumstances surrounding the settlement? Did a reliable entity do a thorough investigation of the incident? Could the insurer have eliminated liability if given timely notice? Could the insurer have proceeded differently in the litigation? *Id.* at 429–30, 191 P.3d 866. Whether or not late notice prejudiced an insurer is a question of fact, and it will seldom be decided as a matter of law. *Id.* at 427, 191 P.3d 866; *Tran v. State Farm Fire & Cas. Co.*, 136 Wash.2d 214, 228, 961 P.2d 358 (1998).

¶ 40 National Surety relies on *Leven* to prove that prejudice resulting from late notice can be found as a matter of law. In that case, the insurance company showed that had tender been timely, it would have argued that the insured was not personally liable and precluded the insured in question from being named as a potentially liable party. *Unigard Ins. Co. v. Leven*, 97 Wash.App. 417, 427, 431, 983 P.2d 1155 (1999). This court held that the lost opportunity to refute *Leven*'s liability resulted in prejudice. *Id.* at 431, 983 P.2d 1155. National Surety makes no comparable argument here.

¶ 41 National Surety here alleges prejudice as a matter of law resulting from late tender and from Immunex's motion for a stay in the declaratory action. In its motion for summary judgment on this issue, National Surety sought complete relief from any obligation to pay defense costs based on the theory that Immunex forfeited its right to those payments through breach of the contract terms. But, National Surety failed to allege an “identifiable prejudicial effect on [its] ability to evaluate, prepare or present its defenses to coverage or liability.” *Id.* at 427, 983 P.2d 1155. National Surety successfully defended on coverage and liability in the

declaratory action. National Surety seeks to avoid the defense costs assumed under reservation of rights up to the point of that order. Whether and to what extent it may have been prejudiced by the delay in notice is a question distinct from coverage and liability. Mere alleged late tender is not enough to prove as a matter of law it could or would have avoided all defense costs had timely tender been made. The trial court did not err in finding an issue of material fact remained regarding

prejudice and refusing to grant summary judgment on this issue.¹⁴

¶ 42 We affirm.

WE CONCUR: SPEARMAN and ELLINGTON, JJ.

Parallel Citations

256 P.3d 439

Footnotes

- 1 We refer to the party as “Immunex,” although Immunex merged with Amgen Inc. in July 2002.
- 2 A qui tam action refers to the False Claims Act, 31 U.S.C. §§ 3729–3733, which prohibits persons from presenting false or fraudulent claims for payment to the federal government, 31 U.S.C. § 3729(a), and permits civil actions alleging such fraud to be filed either by the Attorney General, 31 U.S.C. § 3730(a), or by private persons acting in the government’s name, 31 U.S.C. § 3730(b)(1).
- 3 On August 25, 2009, the trial court granted National Surety’s Motion regarding indemnity and denied its alternative motion regarding late notice. Immunex stipulated to withdrawing its claim for indemnity with respect to settlements or judgments entered in the AWP litigation, while reserving its right to reassert the claim if the April 15, 2009 order is overturned on appeal.
- 4 An endorsement to the Immunex policy in effect between September 1, 2001, and September 1, 2002, changed the policy. The original policy required National Surety to “pay on behalf of [Immunex] those sums that [Immunex b]ecomes legally obligated to pay as damages because of ... Personal Injury or Advertising Injury that is caused by an offense committed during our Policy Period.” The policy defined “personal injury” as “injury other than Bodily Injury caused by one or more of the following offenses[, including] Discrimination.” We will interpret the language used in the endorsement, as we conclude that even under that language no coverage existed for the AWP litigation.
- 5 All boldface emphasis contained in the policy has been omitted throughout this opinion.
- 6 The trial court’s conclusion tracks the original policy provision, which states that personal injury means “injury ... caused by ... [d]iscrimination.” (Emphasis added.) The endorsement changed that definition to “injury ... arising out of ... discrimination.” (Emphasis added.)
- 7 Similar to National Surety’s policy, the Kitsap County policy defined personal injury as injury arising from the offenses of “ ‘wrongful entry or eviction or other invasion of the right of private occupancy.’ ” *Kitsap County*, 136 Wash.2d at 573, 964 P.2d 1173. The question before the Washington Supreme Court was “whether the claims against the county for trespass, nuisance, and interference are equivalent to claims for wrongful entry or eviction or other invasion of the right of private occupancy.” *Id.* at 586, 964 P.2d 1173. The court concluded claims alleging trespass, nuisance, and interference constitute personal liability under policies that provide coverage for personal injury arising from wrongful entry or invasion. *Id.* at 571, 964 P.2d 1173.
- 8 We note that the reservation of rights method is employed by insurers in at least two contexts: where a question of fact exists that will determine coverage that will only be decided by the trier of fact at the end of the underlying litigation, and where a question of law exists regarding coverage, for example whether the terms of the policy cover the claims. See THOMAS V. HARRIS, WASHINGTON INSURANCE LAW § 17.01, at 17–3 (3d ed. 2010). Although the reasoning for the attachment of the duty to defend more logically applies to the case where a factual determination needs to be made, the same principles regarding the duty to defend were applied by the Supreme Court in *Woo*, which involved a question of coverage as a matter of law. See 161 Wash.2d at 52–54, 164 P.3d 454. Prior Washington cases on the duty to defend appear to make no meaningful distinction between the two contexts.
- 9 It is unclear whether the statement “obligated to pay” refers to the obligation to pay a third party under a duty to indemnify or to the obligation to pay defense costs.
- 10 The Washington Supreme Court has relied on the Harris treatise as authority. See, e.g., *Woo*, 161 Wash.2d at 54, 164 P.3d 454; *Mul. of Enumclaw Ins. Co. v. Dan Paulson Constr., Inc.*, 161 Wash.2d 903, 914 n. 8, 169 P.3d 1 (2007).
- 11 To establish a theory of unjust enrichment, a party must show a benefit conferred upon the defendant by the plaintiff; an appreciation or knowledge by the defendant of the benefit; and circumstances that would make it inequitable for the defendant to retain the benefit without the payment of its value. *Young v. Young*, 164 Wash.2d 477, 484, 191 P.3d 1258 (2008).
- 12 We agree with Immunex that National Surety did not expressly raise this argument before the trial court. But, we agree to address it in our discretion under RAP 2.5.

- 13 National Surety's policy required that Immunex notify it as soon as practicable "[o]f any Occurrence which may result in a claim under this policy, when the Occurrence is known to [y]our officer or insurance manager" and "[i]f a claim is made or Suit is brought against any Insured." The policy also required that Immunex not incur any "expense, other than first aid," to "[a]ssume no obligation" without the permission of the insurer, and to "[c]ooperate with [the insurer] in ... defense of any Insured against any Suit."
- 14 This holding does not preclude National Surety from arguing to the fact finder that prejudice resulted as a matter of fact and that it should be excused from some or all of its obligation to pay defense costs.

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

NATIONAL SURETY CORPORATION,)
)
Respondent/Cross Appellant,)
)
v.)
)
IMMUNEX CORPORATION,)
)
Appellant/Cross Respondent.)
_____)

No. 64712-1-1

ORDER DENYING MOTION
FOR RECONSIDERATION

The cross appellant, National Surety Corporation, having filed its motion for reconsideration herein, and a majority of the panel having determined that the motion should be denied;

Now, therefore, it is hereby

ORDERED that the motion for reconsideration is denied.

DATED this 24th day of August, 2011.


Judge

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STATE OF WASHINGTON
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