

NO. 88673-3
SUPREME COURT
OF THE STATE OF WASHINGTON

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EXPEDIA, INC., a Washington Corporation; EXPEDIA, INC., a Delaware Corporation; HOTELS.COM, L.P., a Texas Limited Liability Partnership; HOTELS.COM, GP, LLC, a Texas Limited Liability Company; HOTWIRE, INC., a Delaware Corporation; TRAVELSCAPE, a Nevada Limited Liability Company,

Plaintiffs/Petitioners,

v.

STEADFAST INSURANCE COMPANY, a Delaware Corporation;
ZURICH AMERICAN INSURANCE COMPANY, a New York Corporation; ROYAL & SUN ALLIANCE, a Foreign Corporation;
ARROWPOINT CAPITAL CORP., a Delaware Corporation;
ARROWOOD SURPLUS LINES INSURANCE COMPANY, a Delaware Corporation; ARROWOOD INDEMNITY COMPANY, a Delaware Corporation,

Defendants/Respondents.

PLAINTIFFS/PETITIONERS' REPLY BRIEF

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I. INTRODUCTION

The duty to defend is a critical, broad, and highly protected obligation under Washington law. It protects policyholders from the burdens of litigation by ensuring that when litigation does arise, the insurer will step in and fund the defense while litigation is ongoing. The rules this Court has adopted concerning the duty to defend further that protective purpose. Contrary to those well-established rules, the trial court permitted Zurich to a) refuse to defend Expedia even though Zurich has already failed to meet its burden of proving there is no potential for coverage, b) delay adjudication of Expedia's duty to defend while Zurich pursues discovery extrinsic to the policies and complaints, and c) pursue discovery into issues that overlap with matters at issue in the underlying lawsuits against Expedia, potentially prejudicing Expedia in direct contravention of Zurich's duty of good faith.

Where, as here, the insurer fails to meet its burden to demonstrate the absence of coverage under the "eight corners" of its policy and the underlying complaint and, as a consequence, the trial court has held that coverage is possible, the insurer necessarily has a duty to defend. Discovery extrinsic to the policies and the complaints cannot be used to delay adjudication of the duty to defend or deny that it has arisen. And an insurer may not seek to litigate coverage defenses that overlap with, or are

contrary to its policyholder's interests in, the underlying cases.

Zurich's response to Expedia's appeal primarily focuses on procedure, rather than substance, arguing that this Court should decline to review the trial court's refusal to order Zurich to defend Expedia or even to adjudicate whether the duty to defend has arisen without the completion of overlapping and potentially prejudicial discovery. Those arguments betray the lack of any substantive support for Zurich's continued refusal to defend Expedia. They also reflect a fundamental misunderstanding of the insured's substantive rights under Washington law to both an ongoing defense and to a prompt adjudication of the right to a defense when an insurer initially denies coverage. Expedia's right to an order establishing that the duty to defend has arisen, or, at the very least, an order directing the trial court to adjudicate the duty to defend immediately based upon the policies and complaints, is properly before this Court. This Court should reverse the trial court's orders and uphold Expedia's right to defense coverage during the pendency of the underlying lawsuits.

II. ARGUMENT

A. The Trial Court's Refusal to Order Zurich to Defend Expedia is Properly Before This Court.

Expedia's appeal arises from the trial court's fundamental misapplication of Washington law governing the duty to defend, resulting in a series of erroneous rulings, all of which denied Expedia the ongoing

defense coverage to which it is entitled. The trial court first erroneously refused to enter an order confirming that Zurich’s inability to negate coverage as a matter of law established instead that coverage was possible and thus necessarily established a duty to defend. But for that error, Expedia’s summary judgment motion, the improper continuance, and the resulting dispute concerning when Expedia’s right to a defense would be heard would never have happened.

Expedia noticed discretionary review from the final link in the chain of errors—the trial court’s order refusing to adjudicate Expedia’s duty to defend motion—and from “all orders related to [that] order.” CP 4911. RAP 2.4(b) has only two requirements for an order to be reviewable: “(1) the order or ruling prejudicially affects the decision designated in the notice, and (2) the order is entered, or the ruling is made, before the appellate court accepts review.” Zurich concedes that the second requirement is met. The interrelated nature of the challenged orders, and the prejudicial effect of the first order on the later rulings in the chain, satisfies the first requirement as well. Consistent with this Court’s guidance, “any related order” that meets RAP 2.4(b) is reviewable. *Clark Cnty. v. W. Wash. Growth Mgmt. Hearings Review Bd.*, 177 Wn.2d 136, 145, 298 P.3d 704 (2013); *see also State v. Olson*, 126 Wn.2d 315, 322-23, 893 P.2d 629 (1995) (appellate court should “exercise

its discretion to consider cases and issues on their merits” unless there are “compelling reasons not to do so”); *Hwang v. McMahill*, 103 Wn. App. 945, 949, 15 P.3d 172 (2000) (undesignated order reviewable when appellant “argue[d] why the order was incorrect in her brief on appeal”).

Even if Expedia’s notice of discretionary review did not encompass the trial court’s refusal to enter an order confirming that Zurich’s failure to eliminate coverage established its defense obligation (which is not the case), that technical violation would not prevent this Court from considering that order now. “RAP 1.2(a) makes clear that technical violation of the rules will not ordinarily bar appellate review, where justice is to be served by such review.” *Daughtry v. Jet Aeration Co.*, 91 Wn.2d 704, 710, 592 P.2d 631 (1979).¹ Where, as here, the petitioner assigns error to the ruling in its brief and the opposing party has the opportunity to respond, this Court will consider the matter on appeal. *Id.*; accord *Olson*, 126 Wn.2d at 322-23 (“[E]very case in which we have considered a technical noncompliance with the rules concerning appellate briefing or notice of appeal in light of RAP 1.2(a), we have decided to reach the merits of the case or issue.” (citing cases)).²

¹ The rule provides, in relevant part, that “[c]ases and issues will not be determined on the basis of compliance or noncompliance with these rules except in compelling circumstances where justice demands.” RAP 1.2(a).

² Zurich relies on *In re Marriage of Wixom*, (Unpublished) 174 Wn. App. 1020, 2013 WL 1164308 (2013), an unpublished Court of Appeals decision that may not be cited as

B. The Trial Court's Refusal to Order Zurich to Defend Expedia Violated Well-Established Law Governing the Duty to Defend.

There is no dispute that Zurich failed to prove, in its motion for summary judgment, that there was no possibility for coverage under the two policies that remain at issue. Instead, the parties dispute the consequence of that failure. Zurich's argument that the denial of its motion effectively has no bearing on its duty to defend is contrary to Washington law.

Courts applying the same duty to defend principles that Washington follows have concluded that an insurer's inability to prove that coverage is not possible necessarily confirms that the potential for coverage exists. *See Am. Cyanamid Co. v. Am. Home Assurance Co.*, 30 Cal. App. 4th 969, 975, 35 Cal. Rptr. 920 (1994); *Montrose Chem. Corp. v. Super. Ct.*, 6 Cal. 4th 287, 301, 24 Cal. Rptr. 2d 467, 861 P.2d 1153 (1993); *Horace Mann Ins. Co. v. Barbara B.*, 4 Cal. 4th 1076, 1084, 17 Cal. Rptr. 2d 210, 846 P.2d 792 (1993); *Amazon.com Inc. v. Atl. Mut. Ins. Co.*, No. 05-719, 2005 WL 1711966, at *5 (W.D. Wash. July 21, 2005).³

authority. *See* GR 14.1; *Johnson v. Allstate Ins. Co.*, 126 Wn. App. 510, 519-20, 108 P.3d 1273 (2005) (“[U]npublished opinions are not part of Washington’s common law.”).

³ *See also Anthem Elecs., Inc. v. Pac. Empr's Ins. Co.*, 302 F.3d 1049, 1060 (9th Cir. 2002) (holding that “summary judgment for [the policyholder] is required unless the insurers are able . . . conclusively to negate coverage as a matter of law”); *MGA Entm't v. Hartford Ins. Grp.*, No. 5:08-cv-00457, slip op. at 3(C.D. Cal. Feb. 14, 2012) (awarding summary judgment to non-moving policyholder because the “legal effect of

Zurich had no answer to these cases in its opposition brief because this bedrock principle of insurance law—the inability to eliminate the possibility of coverage confirms that coverage is possible—is beyond dispute. Not only did Zurich fail to eliminate the possibility of coverage, but the trial court affirmatively concluded that the underlying complaints asserted potentially covered claims. When a trial court has decided “that there is a possibility of coverage” and the insurer “did not eliminate that possibility,” the insurer must defend. *Vann v. Travelers Cos.*, 39 Cal. App. 4th 1610, 1619, 46 Cal. Rptr. 2d 617 (1995).

Similarly beyond dispute is the longstanding Washington approach to the duty to defend as the paramount duty owed under a liability policy. The policyholder is entitled to a defense for so long as “the insurance policy *conceivably covers* the allegations in the complaint” while the insurer cannot avoid its duty to defend until it affirmatively proves that there is no possibility for coverage. *See Am. Best Food, Inc. v. Alea London, Ltd.*, 168 Wn.2d 398, 404-05, 229 P.3d 693 (2010); *Woo v. Fireman’s Fund Ins. Co.*, 161 Wn.2d 43, 52-53, 164 P.3d 454 (2007). Once a potential for coverage exists, the insurer bears the burden of proving that exclusions to coverage apply and must defend until it can so prove. *See Mut. of Enumclaw Ins. Co. v. T&G Constr., Inc.*, 165 Wn.2d

[the] denial” of the insurers’ motion as to the duty to defend “is to *establish* the existence of the duty”).

255, 268, 199 P.3d 376 (2008) (citing *Am. Star Ins. Co. v. Grice*, 121 Wn.2d 869, 875, 854 P.2d 622 (1993)).

In the face of these undisputed legal principles, Zurich makes two unavailing arguments: (1) regardless of what the trial court said, it did not actually rule on the question of whether the underlying cases potentially sought damages; and (2) facts related to individual underlying cases were not before the trial court. Both of these arguments ignore the record.

First, Zurich does not dispute that the trial court ruled that, in light of the theories of liability alleged in the underlying complaints, “one of those theories, at least, would put this more in the category of damages.” Jan. 13, 2012 RP 81:22-24. Zurich contends that this ruling is incomplete because the trial court did not consider the definition of damages in its policies. The record refutes this argument.

Zurich’s lead argument below was that the claims against Expedia did not seek damages within its policies’ definition of that term. CP 116-18. The parties discussed that definition at length during oral argument. *See, e.g.*, Jan. 13, 2012 RP 46:11-14 (“Zurich argues . . . that its definition of damages changes this exclusion or this conclusion. Not so.”); *id.* 46:15-49:3 (discussing the impact of the definition of damages).

In holding that the underlying complaints sought “damages,” the trial court correctly applied the burdens of proof applicable to the duty to

defend under Washington law. It observed that the burden first falls on the insured to demonstrate the possibility that the underlying claim comes within the insuring agreement, after which the burden shifts to the insurer to prove an exclusion from coverage. *Id.* 80:7-13. The court then considered Expedia's burden first, asking whether the underlying cases made "claims for damages within the meaning of the policy." *Id.* 81:4-5. In delivering its ruling, the trial court expressly recognized that the relevant policies "did provide a definition of damages," and then proceeded to rule in Expedia's favor on those policies. *Id.* 79:7-8.

The trial court was directed to the definition of damages and necessarily considered it in rejecting Zurich's argument and finding that the underlying complaints potentially sought damages. That ruling was correct. Washington law broadly views damages as "sums of money" owed when a policyholder's "acts or omissions affected adversely the rights of third parties." *Boeing Co. v. Aetna Cas. & Sur. Co.*, 113 Wn.2d 869, 879, 784 P.2d 507 (1990); *see also Fluke Corp. v. Hartford Accident & Indem. Co.*, 145 Wn.2d 137, 147, 34 P.3d 809 (2004) ("damages" encompasses all sums a policyholder becomes liable to pay). As the trial court correctly concluded, the underlying complaints potentially sought damages, not "disgorgement or restitution," and not penalties or fines, the items potentially excluded by the definition in the Zurich policies. Jan.

13, 2012 RP 81:14-15, 19-24, 82:9-12; *see* Opp'n at 26.⁴

Second, Zurich contends that the record does not establish Expedia's entitlement to defense coverage for each underlying case. Again, Zurich is wrong as to what the record shows and wrong as to the scope of the trial court's ruling. Considering all of the underlying cases and all of the relevant policies, the trial court held that the claims against Expedia potentially came within the insuring agreement. Having so held, it then proceeded to consider whether "*these underlying lawsuits are nevertheless excluded* under the exclusionary language in the insurance policies." Jan. 13, 2012 RP 84:16-18 (emphasis added). For the two Zurich policies at issue, the trial court held that the "policies' exclusions would not assist the insurer" and "do not exclude coverage." *Id.* 85:15-16. As to the remaining policies, the trial court found that the particular exclusions applied to bar coverage as to each underlying lawsuit. *Id.* 85:17-87:19. The trial court could not have granted summary judgment in the insurers' favor on those policies without concluding that the exclusion applied to the claims made in each underlying case.

Expedia meets its burden in connection with the duty to defend when the evidence shows that the underlying complaints raise potentially

⁴ As an exclusion, Zurich's definition of damages was given a narrow reading by the trial court, consistent with Washington law. *See Stuart v. Am. States Ins. Co.*, 134 Wn.2d 814, 818-19, 953 P.2d 462 (1998). Zurich never sought reconsideration of the trial court's ruling on the ground that the trial court allegedly misunderstood the policy terms.

covered claims under the policies' insuring agreements. *See Grice*, 121 Wn.2d at 875. Expedia is *not* required to negate every possible defense raised in the insurer's answer before obtaining the benefit of a duty to defend. For example, in connection with the late notice defense, the "duty to defend remains unless [the insurer] proves actual and substantial prejudice." *Mut. of Enumclaw Ins. Co. v. USF Ins. Co.*, 137 Wn. App. 352, 360-61, 153 P.3d 877 (2007), *aff'd* 164 Wn.2d 411, 191 P.3d 866 (2008); *see also Nat'l Sur. Co. v. Immunex Corp.*, 176 Wn.2d 872, 889, 297 P.3d 688 (2013) ("[A]n insured's late tender . . . does not relieve the insurer of its duty to defend unless it proves *actual and substantial prejudice* from late notice.").

Zurich has conceded that Expedia raised the issue of its entitlement to summary judgment upon the denial of Zurich's motion in Expedia's original summary judgment opposition. CP 1730. Zurich also does not dispute that all of the relevant underlying complaints and relevant policies were in the record,⁵ or that the parties briefed—and the trial court considered—the particular aspects of individual underlying complaints to demonstrate the potential for coverage in each. CP 18-134, 752-99, 969-94. The trial court's consideration of the record on the Zurich's motion necessarily involved analysis of the various underlying complaints, each

⁵ *See* Declaration of Russell C. Love (Sub No. 65), provided to this Court as an original CD with the Clerk's Papers.

of which involves the same essential claim: due to Expedia's conduct, the municipality did not receive the revenues to which it asserts it is entitled. The trial court was not required to mention each underlying case in order to conclude, as it did in its ruling, that the underlying complaints, asserting that same essential claim, gave rise to the potential for coverage. The only way to reject Zurich's arguments that Expedia failed to meet its burden to prove that each action conceivably sought damages for negligent conduct (e.g., CP 123) was for the trial court to conclude instead, as it did, that Expedia demonstrated that coverage was possible.

Zurich's contentions as to why certain underlying complaints are not covered, notwithstanding the trial court's ruling, are unavailing. Zurich attempts to exclude every lawsuit "filed outside the policies' inception and termination dates." Opp'n at 29. But Zurich's policies are occurrence based, not claims made (CP 2104) and thus broadly cover liability arising out of any occurrence during the policy periods, not just claims filed during the policy period. *See Ellis Court Apartments Ltd. P'ship ex rel. Woodside Corp. v. State Farm Fire & Cas. Co.*, 117 Wn. App. 807, 815, 72 P.3d 1086 (2003).⁶ Essentially all of the underlying actions seek damages for conduct occurring during the policy periods.

Declaratory judgment actions brought by Expedia to prevent or

⁶ Only lawsuits already pending when the first policy inceptioned are outside the scope of Zurich's insuring agreement because they involve conduct pre-dating the policies.

overcome the assessment of monetary damages are similarly covered. If Expedia loses those actions, it faces liability to the municipalities for damages (which would be covered under Zurich's policies). The procedural details by which that dispute is litigated do not rob Expedia of a defense. *See Boeing*, 113 Wn.2d at 878 (holding that "coverage does not hinge on the form of action taken or the nature of relief sought"); *APA-Engineered Wood Ass'n v. Glens Falls Ins. Co.*, 94 Wn. App. 556, 972 P.2d 937 (1999) (ordering defense coverage for lawsuit seeking discovery because it could lead to the assertion of a claim for damages).⁷

The record before the trial court at the time it denied Zurich's summary judgment motion established the potential for coverage. Having found that the underlying complaints potentially sought damages for negligent conduct, the trial court should have ordered Zurich to defend Expedia. Its refusal to do so was legal error.

C. The Trial Court's Orders Denied Expedia's Right Under the Policies and Washington Law to Defense Coverage During the Pendency of the Underlying Lawsuits.

The trial court refused to adjudicate Expedia's right to an ongoing defense until Expedia provided discovery that overlaps with, and potentially prejudices Expedia in, the underlying lawsuits. The trial court's

⁷ A policyholder may recover the costs of an affirmative action taken to avoid the imposition of potentially covered liability. *See, e.g., Citadel Holding Corp. v. Roven*, 603 A.2d 818, 824 (Del. 1992); *Safeguard Sci., Inc. v. Liberty Mut. Ins. Co.*, 766 F. Supp. 324, 333-34 (E.D. Pa. 1991), *aff'd in part, rev'd in part*, 961 F.2d 209 (3d Cir. 1992).

ruling effectively deprives Expedia of its bargained-for defense while the underlying lawsuits remain pending. Essentially, the trial court converted the ongoing defense Expedia purchased from Zurich into a mere obligation to reimburse after the fact. This result is the opposite of what the policies and Washington law governing the duty to defend require.

The defense obligation is “a valuable service paid for by the insured and one of the principal benefits of the liability insurance policy,” and the policies are priced to reflect this service. *Woo*, 161 Wn.2d at 54. The policy Expedia purchased from Zurich contained an ongoing defense obligation, not just a right to reimbursement. Using standard form language, the policy requires Zurich to “defend any Suit against [Expedia] seeking” damages; it does not say that Zurich will not affirmatively defend a suit but only reimburse Expedia for the costs of defense at its conclusion. CP 2104. Had Zurich wanted to limit its contractual obligation to the mere provision of reimbursement, it could have added such language to the policy; having failed to do so, Zurich cannot “unilaterally disavow its financial responsibility.” *Immunex*, 176 Wn.2d at 891; *see also Lynott v. Nat’l Union Fire Ins. Co. of Pittsburgh, Pa.*, 123 Wn.2d 678, 688, 871 P.2d 146 (1994) (“In evaluating the insurer’s claim as to the meaning of language used, courts necessarily consider whether alternative or more precise language, if used, would have put the matter beyond reasonable

question.” (internal quotation marks omitted)). Instead, Zurich’s obligation under Washington law and its contract with Expedia was to provide an immediate defense for any potentially covered claim, as determined from the eight corners of the relevant policy and relevant complaint, until such time as Zurich could prove, as a matter of law, that there is no potential for coverage.

The duty to defend is an ongoing duty—one that must be provided during the pendency of the underlying litigation for so long as the potential for coverage exists—rather than reimbursement many years later after the insured has borne the burdens of its defense. An insurer may not “desert policyholders and allow them to incur substantial legal costs while waiting for an indemnity determination.” *Am. Best*, 168 Wn.2d at 405 (quoting *Truck Ins. Exch. v. VanPort Homes, Inc.*, 147 Wn.2d 751, 761, 58 P.3d 276 (2002)). The “immediate imposition” of the duty to defend is not simply a procedural nicety that a trial court can ignore; it is “necessary to provide to an insured the full benefits due under the policy.” *Haskel v. Super. Ct.*, 33 Cal. App. 4th 963, 968, 39 Cal. Rptr. 2d 520 (1995).

The procedural requirements that this Court has imposed on insurers faced with a tender of defense reflect these policies. The insurer must make its defense determination based only on the eight corners of the relevant policy and complaint. *Woo*, 161 Wn.2d at 54; *VanPort*, 147

Wn.2d at 760. An insurer must resolve disputed issues of fact and law in favor of the policyholder and must provide a defense for so long as those disputed questions exist. *Am. Best*, 168 Wn.2d at 404-05. Disputed issues of fact confirm the existence of the duty to defend; they do not defeat the duty or permit an insurer to avoid its defense obligation while those issues remain unresolved. *Id.*; *Anthem*, 302 F.3d at 1060.

Zurich does not dispute these principles but instead argues that these they may simply be cast aside when the insurer refuses a tendered defense based on unspecified “policy conditions or certain threshold matters.” Opp’n at 40. Zurich’s argument is wrong, for two reasons.

First, this Court already has rejected Zurich’s argument in connection with the so-called “threshold matters” on which Zurich relies. For example, Zurich contends that it may refrain from defending Expedia based on Zurich’s unresolved late notice defense while it takes discovery into matters related to Expedia’s tender of defense and any prejudice to Zurich. But Washington law is precisely to the contrary. Late notice does not excuse an insurer from defending unless and until it proves actual and substantial prejudice from late notice. *Immunex*, 176 Wn.2d at 889; *USF*, 137 Wn. App. at 360-61 (the insurer “*must* demonstrate actual prejudice *before* it will be relieved from its duties to its insured” (emphasis added)).

Zurich’s argument that *Immunex* is inapplicable when an insurer

refuses to defend rather than undertakes its defense under a reservation of rights (Opp'n at 42) lacks support in Washington law or public policy. Zurich does not cite, and Expedia is not aware of, any case drawing this distinction. If insurers who refused to defend were subject to more liberal standards in determining when their duty to defend arises than insurers who defend under a reservation of rights, insurers would be encouraged to refuse to defend any time they intend to assert the late notice defense (or any other of the myriad defenses an insurer might choose to interpose). This Court has repeatedly held that the proper course for an insurer that is unsure of its coverage obligations is to “defend under a reservation of rights” to ensure that policyholders receive the promised security that their insurance was intended to provide. *See Am. Best*, 168 Wn.2d at 405 (quoting *VanPort*, 147 Wn.2d at 761)).

Second, the authority on which Zurich relies does not go nearly as far as Zurich attempts to take it. Far from adopting a categorical rule that an insurer is entitled to discovery into facts relating to coverage defenses and a resolution of disputed issues relating to those coverage defenses before a policyholder's right to defense coverage can be adjudicated, each of Zurich's cases simply rule in favor of an insurer on its ultimate coverage obligation based upon the unique and indisputable facts present in those cases. For example, Zurich's lead case, *Overton v. Consolidated*

Insurance Co., 145 Wn.2d 417, 38 P.3d 322 (2002), involved insurers' motions for summary judgment addressed to the entirety of their coverage obligations: whether knowledge "precludes coverage." 145 Wn.2d at 423-24. As with any motion addressed to the duty to indemnify, the evidence presented by the insurers included evidence beyond the policies and complaints. This Court relied on that evidence to conclude that the insurer met its burden of proving that coverage was unavailable as a matter of law.⁸ The majority opinion does not even mention the duty to defend, what is relevant to that determination, when it may be adjudicated, and whether discovery may be conducted before determining if the duty to defend has arisen.⁹ Nor does any of Zurich's other authority.¹⁰

⁸ The bulk of the Court's opinion focused on the insuring agreement and the question of whether the policyholder could show that there had been an "occurrence." *Id.* at 424-33. The Court does not discuss the known loss defense other than to say that the absence of an occurrence, under the language of the policy at issue, also meant that "coverage was properly denied under the known-loss principle." *Id.* at 433.

⁹ Zurich argues that the discussion of the duty to defend in the dissent means that the majority necessarily disagreed with the approach advocated by the dissenting justice. Opp'n at 32. Not so. The majority offered no opinion on whether an insurer must defend while disputes related to coverage remain unresolved. *See generally Overton*, 145 Wn.2d 417. It simply held that the insurers met their burden to prove that they had no duty to indemnify. *Id.* This Court need not overrule *Overton*, as Zurich suggests (Opp'n at 39), to rule in Expedia's favor. Indeed, Washington courts already follow the procedure Expedia urges. *See, e.g., Time Oil Co. v. Cigna Prop. & Cas. Ins. Co.*, 743 F. Supp. 1400 (W.D. Wash. 1990) (enforcing ongoing duty to defend while insurer litigates, and pursues discovery relevant to, coverage defenses).

¹⁰ At most, *Overton* and the Court of Appeals' decision in *Unigard Ins. Co. v. Leven*, 97 Wn. App. 417, 983 P.2d 1155 (1999), suggest that if the court can conclude there is no possibility of coverage as a matter of law the first time the coverage question is posed to it, it need not consider whether the duty to defend was triggered earlier. That is not the case here, where Zurich already has tried and failed to eliminate coverage and seeks

Indeed, *none* of Zurich’s cases relies on extrinsic evidence to deny a policyholder’s standalone request for summary adjudication of the duty to defend. More critically, *none* of the cases endorses the procedure the trial court followed here: refuse to order the insurer to defend following an adjudication that coverage is possible and then delay the policyholder’s duty to defend motion while the insurer pursues overlapping discovery designed to create disputed issues of fact as to its coverage defenses. To uphold the trial court effectively would overrule *Woo* and *VanPort*.

The only case either party cites addressing this issue—whether an insurer may delay adjudication of a policyholder’s duty to defend motion to pursue extrinsic discovery—supports Expedia. Zurich has no answer to *Haskel*, 33 Cal. App. 4th 963, which is entirely consistent with Washington law. Under *Haskel* and Washington law, insurers *may not* “delay an adjudication of their defense obligation until they develop sufficient evidence to retroactively justify their refusal to provide that defense” because such delay would be “directly contrary” to duty to defend principles. *Id.* at 977. The trial court in *Haskel* “erred by effectively conditioning Haskel’s right to have its summary adjudication motion heard upon the satisfaction of all of the insurers’ discovery

through discovery to merely create questions of fact as to its coverage obligations. Even if questions of fact were present, they would only confirm that the duty to defend exists.

demands.” *Id.* at 978.¹¹ The trial court here committed the same error.

Zurich already has tried, and failed, to prove that there is no possibility that the underlying complaints are covered under Zurich’s policies. The discovery it seeks from Expedia, by Zurich’s own admission, would at most create issues of fact concerning Zurich’s ultimate coverage obligations, which do not negate a duty to defend. CP 3831; *Anthem*, 302 F.3d at 1060. Yet Zurich continues to refuse to defend Expedia while those issues remain unresolved, in derogation of its duties under the policies and longstanding Washington law, leaving Expedia without the ongoing defense coverage for which it bargained. The trial court should have adjudicated the duty to defend immediately, without allowing extrinsic discovery into Zurich’s coverage defenses. Its failure to do so is legal error.

D. The So Called “Unique” Circumstances of this Case Are Common to Insurance Coverage Litigation and Cannot Justify the Trial Court’s Departure from Washington Law.

The trial court refused to adjudicate Expedia’s right to a defense, reasoning that Expedia waited too long to tender the claims (even though

¹¹ *Haskel* also confirms that Zurich’s reliance on the abuse of discretion standard of review is incorrect. *Haskel* rejected the argument, made by Zurich here, that this issue is merely a procedural matter because that argument “confuses the principles surrounding the creation of a defense obligation.” *Id.* at 977., The trial court committed errors of law that, as Zurich does not dispute, this Court should review de novo. *Id.*; *Ino Ino, Inc. v. City of Bellevue*, 132 Wn.2d 103, 114, 937 P.2d 154 (1997). Nonetheless, Expedia prevails even under the abuse of discretion standard because the trial court made an “application of an incorrect legal analysis or other error of law.” *State v. Tobin*, 161 Wn.2d 517, 523, 166 P.3d 1167 (2007).

many were tendered within weeks or months after filing (CP 2170-84)) and had the financial means to defend itself prior to requesting Zurich's assistance. Even if these reasons were supported by the record, which they are not, they are neither unique to Expedia nor grounds for refusing Expedia's right to ongoing defense coverage.

Refusing to hear Expedia's duty to defend motion because of the timing of Expedia's tender effectively denies the duty to defend based on alleged late notice. The trial court, however, made no finding of actual and substantial prejudice to Zurich caused by any late notice. Nor could it, as no such evidence was in the record.¹² An allegation of late notice is not unique. To the contrary, the Washington courts have opined on the impact of that defense on an insurer's duty to defend on multiple occasions and consistently held that an insurer *may not* refuse to defend based on late notice alone, but instead must continue to defend unless and until it bears its burden of proving actual and substantial prejudice caused by such late notice. *See, e.g., Immunex*, 176 Wn.2d at 889; *USF*, 137 Wn. App. at 360-61. Thus, the supposedly "unique" circumstances of Expedia's tender are so common to insurance litigation that they have already spawned a body of coverage law compelling the opposite result

¹² Zurich's Opposition did not dispute that prejudice cannot be shown in the absence of evidence that Zurich would have done something differently had it been notified earlier. *See* Expedia Br. at 27-28. Zurich's steadfast refusal to defend at every turn confirms the absence of any prejudice.

from what the trial court ordered. If insurers could deny the duty to defend based on policy-based defenses requiring evidence beyond the eight corners of the complaint and policy, insurers would routinely invoke the need for discovery before providing a defense, undermining this Court's insistence that the insurer defend first, and litigate coverage later.

Similarly, the trial court's reliance on Expedia's financial wherewithal to refuse it the defense it bargained for has no support in Washington law, nor does Zurich argue to the contrary. The needs-based test adopted by the trial court would be unworkable and would convert a straightforward duty to defend analysis, made based on the plain language of the policy and underlying complaint, into a searching review of the policyholder's financial status. Moreover, Expedia's status as a corporate policyholder is not unique. Countless Washington businesses, large and small, purchase liability insurance to ensure that their resources are not depleted by burdensome litigation, but instead can remain directed toward their intended corporate, charitable, or other designated uses.

Zurich makes no attempt to defend a financial means-based test or explain how it would be consistent with Washington law on the duty to defend, because it cannot. Indeed, one of the two cases Zurich cites (Opp'n at 44) rejects the argument that sophisticated policyholders should

be treated differently under Washington law.¹³ Zurich cites the dissenting opinion in *Weyerhaeuser Co. v. Commercial Union Insurance Co.*, 142 Wn.2d 654, 15 P.3d 115 (2000), in which Justice Talmadge urged a “context” based approach, including consideration of policyholder sophistication, to construing the language of an insurance policy. *Id.* at 706-10 (Talmadge, J., dissenting). The majority opinion rejected this approach, ruling instead that policies must be given the same construction “as would be given to the contract by the average person purchasing insurance.” *Id.* at 669-70 (internal quotation marks omitted). As in *Weyerhaeuser*, the trial court should have refused to consider Expedia’s financial means. The trial court’s reliance on those means to delay adjudication of Expedia’s right to a defense until the underlying lawsuits have concluded was legal error.

E. **Expedia’s Right to Defense Coverage Cannot Be Conditioned Upon its Completion of Overlapping and Potentially Prejudicial Discovery.**

The trial court refused to adjudicate Expedia’s right to ongoing defense coverage until Expedia completes discovery that the trial court itself found to be “dangerous” and “injurious.” June 15, 2012 RP 31:10-

¹³ The other discusses policyholder sophistication outside of the duty to defend context and on a narrow factual issue. In *Grange Insurance Ass’n v. Great American Insurance Co.*, 89 Wn.2d 710, 575 P.2d 235 (1978), this Court relied on the City of Tacoma’s bidding process, including creation of bid proposals that it sent to insurers asking for bids that did not include uninsured motorist coverage, to determine that it had rejected uninsured motorist coverage.

20, 38:6-16. Zurich does not dispute this. Instead, it argues that Expedia's inability to get a defense adjudication without completing overlapping discovery does not harm Expedia because it was Expedia's own choice to file this coverage action. Zurich's solution—that Expedia should defend the underlying cases itself until they are resolved, and only then approach Zurich for the coverage Zurich promised—finds no support in Washington law which, guarantees policyholders like Expedia an “unrestricted right to prosecute a concurrent [coverage] action” and provides that they are “not required to await the resolution of the [underlying] claim,” particularly when its insurer has refused to provide a defense. 1-14 Thomas V. Harris, *Washington Insurance Law* § 14.02 (3d ed. 2010).

That right does not vanish when there is an overlap between the coverage case and the underlying case. If Zurich were correct, the right to bring a coverage action would be hollow; every case has overlapping issues because the ultimate issue of liability in the underlying lawsuit, and the facts related to that ultimate issue, are relevant to every liability coverage case. Instead, Washington law provides that overlapping issues “can only be decided in the damage action.” *Holland Am. Ins. Co. v. Nat'l Indem. Co.*, 75 Wn.2d 909, 912, 454 P.2d 383 (1969). And so long as coverage remains possible while those issues are undecided, the insurer

must defend first and litigate coverage later. *Am. Best*, 168 Wn.2d at 403. Doing otherwise would amount to bad faith. *Mut. of Enumclaw Ins. Co. v. Dan Paulson Constr. Inc.*, 161 Wn.2d 903, 918, 169 P.3d 1 (2007) (insurer acts in bad faith if it litigates coverage issues that “*might* prejudice its insured’s tort defense” (emphasis added, internal quotation marks omitted)).

Zurich argues that the proper course when there are overlapping issues is to stay the entire case without providing the policyholder any defense. The cases on which it relies for this argument, however, order the opposite result. In *Montrose*, 6 Cal. 4th at 301, the court endorsed a stay of discovery only *after* defense coverage was in place. *See also Montrose Chem. Corp. v. Super. Ct.*, 25 Cal. App. 4th 902, 909, 31 Cal. Rptr. 2d 38 (1994) (*Montrose II*) (the duty to defend “lasts until (a) the underlying lawsuit is resolved or (b) the coverage issue can be determined without prejudice to the insured”). This “eliminate[d] the risk of inconsistent factual determination” without the undue prejudice that would result if a policyholder was unable to obtain defense coverage throughout the pendency of the underlying case. *Montrose*, 6 Cal. 4th at 301. *Haskel* takes the same approach. It remanded for the trial court first to adjudicate the duty to defend without delay, and only after an adjudication that the policyholder had a right to an ongoing defense would the court proceed to

consider what discovery could be conducted while the underlying case remained ongoing. 33 Cal. App. 4th at 980-81.

The trial court should have followed the same approach here. This is the only approach that fulfills the intended purpose of the duty to defend as an ongoing promise, arising at the filing of a potentially covered claim and continuing until liability is established or until the insurer is able to prove, as a matter of law, that coverage is not possible.

III. CONCLUSION

This Court should reaffirm the longstanding protections for policyholders inherent in the duty to defend and order that Zurich has an immediate obligation to defend Expedia, based on the trial court's conclusion that coverage was possible under the policies. At the very least, this Court should order the trial court to adjudicate Expedia's duty to defend motion immediately, based upon the relevant policies and underlying complaints, without any additional discovery. It should further order the trial court, after ruling on Expedia's duty to defend motion, to stay discovery into matters overlapping with, or potentially prejudicial to Expedia in, the underlying lawsuits until such lawsuits are concluded.

DATED this 25th day of November, 2013.

Respectfully submitted,

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Appendix A

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CIVIL MINUTES - GENERAL

Case No. EDCV 08-0457-DOC(RNBx)

Date: February 14, 2012

Consolidated with:

CV 10-7692-DOC(RNBx), CV 10-2355- DOC(RNBx), CV 09-7461-DOC(RNBx)

Title: MGA ENTERTAINMENT ET AL v. HARTFORD INSURANCE GROUP

PRESENT:

THE HONORABLE DAVID O. CARTER, JUDGE

Julie Barrera
Courtroom Clerk

Not Present
Court Reporter

ATTORNEYS PRESENT FOR PLAINTIFFS: ATTORNEYS PRESENT FOR DEFENDANTS:

NONE PRESENT

NONE PRESENT

PROCEEDING (IN CHAMBERS): ORDER AMENDING PRIOR ORDERS TO GRANT NON-MOVANT SUMMARY JUDGMENT ON DUTY TO DEFEND

The Court previously denied two insurers' motions for summary judgment regarding the duty to defend in: (1) an Order ("C & F Order") (Dkt. 495) regarding a motion brought by Defendant Crum & Forster Specialty Insurance Company ("Defendant C & F"); and (2) an Order ("Evanston Order") (Dkt. 480) regarding a motion brought by Defendants Evanston Insurance Company, Markel Corporation, and Markel Underwriting Managers, Inc. ("Evanston Defendants").

The Court AMENDS these two Orders (Dkts. 495, 480) to sua sponte GRANT Plaintiffs MGA Entertainment, Inc., and Isaac Larian ("MGA Plaintiffs") summary judgment on the issue of the duty to defend.

I. Law Regarding Summary Judgment and the Duty to Defend

"It is generally recognized that a court has the power sua sponte to grant summary judgment to a non-movant when there has been a motion but no cross-motion." *Kassbaum v. Steppenwolf Prods., Inc.*, 236 F.3d 487, 494 (9th Cir. 2000); *Cool Fuel, Inc. v. Connett*, 685 F.2d 309, 311 (9th Cir. 1982); *see also* Fed. R. Civ. P. 56(f)(2) (a district court may grant summary judgment "for a nonmovant," "on grounds not raised by a party," or "on its own").

The Ninth Circuit has affirmed a district court's sua sponte granting of summary

judgment to a party who “made no motion” for summary judgment where the movant filed for summary judgment. *Cool Fuel*, 685 F.2d at 311 (“[T]he overwhelming weight of authority supports the conclusion that if one party moves for summary judgment and . . . there is no genuine dispute respecting a material fact essential to the proof of movant’s case and that the case cannot be proved if a trial should be held, the court may sua sponte grant summary judgment to the non-moving party.”). The Ninth Circuit reasoned that the movant’s motion provided the parties with the “opportunity to explore and expound the issues.” *Id.*

When a court *denies* an insurer’s motion for summary judgment that seeks to establish that it owed no duty to defend as a matter of law, the legal effect of the denial is to *establish* the existence of the duty to defend. *Anthem Electronics, Inc. v. Pacific Employers Ins. Co.*, 302 F.3d 1049, 1060 (9th Cir. 2002); *Horace Mann Ins. Co. v. Barbara B.*, 4 Cal.4th 1076, 1085 (1993). Precisely for this reason, the Ninth Circuit has *granted summary judgment to an insured* when reversing a grant of summary judgment to an insurer. *Anthem Electronics*, 302 F.3d at 1060.

II. The Court Grants the MGA Plaintiffs Summary Judgment Because the Court Previously Denied the Insurers’ Summary Judgment Motions on the Duty to Defend

On June 24, 2009, Judge Larson ruled that both the Evanston Defendants and Defendant C & F had a duty to defend the underlying litigation based on Mattel’s Second Amended Answer and Counterclaim (“SAAC”). Because the Court had already held that these two insurers had a duty to defend, this duty was not extinguished until the insurers met their burden to show that they “negate[d] all facts suggesting potential coverage.” *Scottsdale Ins. Co. v. MV Transp.*, 36 Cal. 4th 643, 654-655, 31 Cal.Rptr.3d 147 (2005).

On January 27, 2012, and February 6, 2012, this Court denied the Evanston Defendants’ and Defendant C & F’s respective motions for summary judgment regarding their duty to defend Mattel’s Fourth Amended Answer and Counterclaim (“FAAC”). Regarding the Evanston Order, the Court expressly stated that “[b]ecause the Evanston Defendants are not entitled to judgment as a matter of law—and even though there is no genuine dispute as to material facts—the Court DENIES the Evanston Defendants’ motion for partial summary judgment.” *See* Order (Dkt. 480) at 18. Regarding the C & F Order, the Court similarly denied summary judgment and found that the “parties do not genuinely dispute of the . . . facts.” *See* Order (Dkt. 495) at 2, 37.

Finally, on February 10, 2012, in response to an Order to Show Cause issued by this Court, the MGA Plaintiffs argued that this Court’s denial of summary judgment constituted a finding that the duty to defend existed. *See* Reponse (Dkt. 497).

This is exactly the kind of case for which sua sponte summary judgment is appropriate. In their motions for summary judgment, replies, and oral arguments lasting several hours, the insurers have had ample opportunity to argue the purely legal question of whether a duty to defend existed. As

in *Cool Fuel*, summary judgment for the non-moving party, the MGA Plaintiffs, is appropriate because the parties have had ample “opportunity to explore and expound the issues” raised by the insurers’ summary judgment motions. *See Cool Fuel*, 685 F.2d at 311. As in *Anthem Electronics*, this Court has already denied the insurers’ motion for summary judgment regarding the duty to defend as a matter of law, and thus the legal effect of this denial is to *establish* the existence of the duty to defend. *See Anthem Electronics*, 302 F.3d at 1060. Finally, a grant of summary judgment to the MGA Plaintiffs will significantly advance judicial economy. Without a grant of summary judgment to the MGA Plaintiffs, the parties’ and the Court’s resources will be needlessly consumed in a bench trial which would simply relitigate the very same issue raised by the insurers in their summary judgment motions: whether a duty to defend existed because the language in the FAAC created the potential for coverage under the insurers’ policies. In its previous orders, the Court has always answered this question in the affirmative.

Accordingly, the Court AMENDS the two Orders (Dkts. 495, 480) to GRANT the MGA Plaintiffs summary judgment on the issue of the duty to defend. The Court AMENDS the C & F Order (Dkt. 495), to GRANT MGA summary judgment because Defendant C & F owed a duty to defend under the FAAC. The Court AMENDS the Evanston Order (Dkt. 480), to GRANT MGA summary judgment because the Evanston Defendants owed a duty to defend under the FAAC.

The Clerk shall serve a copy of this minute order on counsel for all parties in this action.

DECLARATION OF SERVICE

I, Heather Bond, declare under penalty of perjury that I am over the age of 18 and competent to testify and that the parties listed below were served in the manner listed below:

On November 25, 2013, I caused a copy of and Plaintiffs/Petitioners' Reply Brief and this Declaration of Service to be delivered on this date via Legal Messenger to:

Michael Hooks
Matthew Adams
FORSBERG UMLAUF, P.S.
901 Fifth Avenue, Suite 1400
Seattle, WA 98164-2047

On November 25, 2013, I further served via FedEx copies of the above-referenced documents to Defendants/Respondents' out-of-state co-counsel:

J. Randy Evans
Joanne L. Zimolzak
McKENNA LONG & ALDRIDGE LLP
1900 K Street NW
Washington, D.C. 20006

I hereby declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED this 25th day of November, 2013, at Seattle, Washington.



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From: Bond, Heather E. <hbond@orrick.com> on behalf of Parris, Mark S. <mparris@orrick.com>
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Subject: Plaintiffs/Petitioners' Reply Brief
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Expedia, Inc., et al. v. Steadfast Insurance Company, et al.
Case No. 88673-3 (Court of Appeals Case No. 69341-7-1)

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