

NO. 66755-6

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

OREGON MUTUAL INSURANCE COMPANY, an Oregon corporation,

Appellant

v.

HARTFORD FIRE INSURANCE COMPANY,

Respondent

BRIEF OF APPELLANT

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I. INTRODUCTION

Appellant Oregon Mutual Insurance Company (“Oregon Mutual”) sued Respondent Hartford Fire Insurance Company (“Hartford”) on its own behalf and as assignee of the parties’ mutual insured, Wellman & Zuck, Inc. (“Wellman”),¹ to recover sums Oregon Mutual paid to defend and settle two underlying lawsuits against Wellman: *Buchholz v. Wellman & Zuck, Inc.*, Whatcom County Superior Court Case No. 02-2-00101-3 (the “*Buchholz* Suit”) and *State Farm Fire & Casualty Co. v. Wellman & Zuck, Inc.*, Whatcom County Superior Court Case No. 03-2-01721-0 (the “*State Farm* Suit”). Hartford refused to defend Wellman in either suit, even though the complaints readily triggered its duty to defend under *Truck Ins. Exch. v. VanPort Homes, Inc.*, 147 Wn.2d 751, 761, 58 P.3d 276 (2002). Hartford also denied a defense to Wellman in bad faith by ignoring the express allegations in the complaints and raising inapplicable policy exclusions.

The trial court initially ruled that Hartford breached its duty to defend in bad faith. However, the court subsequently vacated both parts

¹ An assignee steps into the shoes of the assignor and acquires all of the assignor’s rights against the defendant. *Estate of Jordan v. Hartford Acc. & Indem. Co.*, 120 Wn.2d 490, 495, 844 P.2d 403 (1993). By virtue of the assignment, the assignee’s cause of action against a third party is direct, and not derivative. *Besel v. Viking Ins. Co.*, 105 Wn. App. 463, 472, 21 P.3d 293 (2001), *reversed on other grounds*, 146 Wn.2d 730, 49 P.3d 887 (2002).

of that ruling (*i.e.*, breach of contract and bad faith), after finding a question of fact as to whether Wellman had been harmed by Hartford's bad faith. In a series of subsequent rulings, the trial court then proceeded to dismiss all of Oregon Mutual's claims based on, *inter alia*, a novel "bad faith tender – unclean hands" argument by Hartford. According to Hartford (and as accepted by the trial court), an insurer's bad faith breach of its duty to defend is excused if, at the time of tendering, the insured allegedly knows that the insurer would ultimately owe no coverage for the loss. This flies squarely in the face of Washington law on the duty to defend and is completely unsupported by the record in this case.

Oregon Mutual respectfully submits that this Court should rule that Hartford breached its duty to defend Wellman in both suits, that Hartford's refused to defend Wellman in bad faith, that Hartford is estopped to deny coverage because of its bad faith refusal to defend, that Hartford violated the Consumer Protection Act ("CPA"), that Oregon Mutual is entitled to contribution, that Hartford was negligent in handling Wellman's tenders, and that Oregon Mutual is entitled to its attorney fees and costs under *Olympic Steamship Co., Inc. v. Centennial Ins. Co.*, 117 Wn.2d 37, 811 P.2d 673 (1991) ("*Olympic Steamship*") and RAP 18.1.

II. ASSIGNMENTS OF ERROR

A.. Assignments of Error

1. Rulings on Hartford's Duty to Defend. The trial court erred in vacating its October 6, 2006 order finding that Hartford breached its duty to defend (by order entered August 24, 2007); in denying Oregon Mutual's renewed motion for summary judgment on Hartford's duty to defend (by order entered September 12, 2008); by denying Oregon Mutual's motion regarding Hartford's duty to defend the *State Farm* Suit (by order entered October 1, 2010); and by dismissing Oregon Mutual's claim for breach of contract (by order entered February 4, 2011).

2. Rulings on Hartford's Bad Faith. The trial court erred in denying Oregon Mutual's motion for summary judgment on harm from Hartford's bad faith (by order entered June 8, 2007); and by dismissing Oregon Mutual's bad faith claim (by order entered October 1, 2010).

3. Preclusion of Estoppel Remedy. The trial court erred in precluding Oregon Mutual from the remedy of estoppel (by order entered August 8, 2008).

4. Dismissal Of CPA Claim. The trial court erred in dismissing Oregon Mutual's CPA claim (by order entered October 1, 2010).

5. Dismissal of Contribution Claim. The trial court erred in dismissing Oregon Mutual's contribution claim (by order entered June 12, 2009).

6. Dismissal of Negligence Claim. The trial court erred in dismissing Oregon Mutual's negligence claim (by order entered February 4, 2011).

7. Ruling on Defense Obligation. The trial court erred in denying summary judgment on Hartford's obligation to pay all *Buchholz* defense costs (by order entered February 4, 2011).

8. Dismissal of *Olympic Steamship* Claim. The trial court erred in barring Oregon Mutual from recovering attorney fees and costs under *Olympic Steamship*, by order entered April 10, 2009.

B. Issues Pertaining to Assignments of Error

1. When the *Buchholz* complaint expressly alleged "severe and significant water damage" and did not specify the work of any particular contractor or the date of any damage, did Hartford breach its duty to defend Wellman in bad faith by claiming there was no allegation of "property damage" caused by an "occurrence" and also by claiming the damage occurred after its policy period expired? *American Best Food, Inc. v. Alea London, Ltd.*, 168 Wn.2d 398, 229 P.3d 693 (2010); *Woo v.*

Fireman's Fund Ins. Co., 161 Wn.2d 43, 64, 164 P.3d 454 (2007);
VanPort, 147 Wn.2d at 761. (Assignments of Error 1 and 2.)

2. Did Hartford also breach its duty to defend Wellman in bad faith in the *State Farm* Suit when that suit arose out of the same project, defects and damage involved in *Buchholz*? *Ibid.* (Assignments of Error 1 and 2.)

3. Does an issue of fact on the bad faith element of harm permit the trial court to vacate its ruling that Hartford also breached its contractual duty to defend, when that relief was not requested in Hartford's motion? (Assignment of Error 1.)

4. Did Hartford meet its burden to rebut the presumption of harm flowing from its bad faith refusal to defend Wellman in the *Buchholz* and *State Farm* suits? *Safeco Ins. Co. v. Butler*, 118 Wn.2d 383, 390, 823 P.2d 499 (1992). (Assignment of Error 2.)

5. Does an issue of fact on the elements of causation and harm of a bad faith claim permit the trial court to vacate its ruling on the elements of duty and breach? CR 56(c). (Assignment of Error 2.)

6. Is Oregon Mutual precluded from asserting claims against Hartford for bad faith, estoppel and violation of the CPA when at the time of tender Wellman and/or Oregon Mutual allegedly "knew" Hartford would have no duty to indemnify? (Assignments of Error 2, 3, and 4.)

7. Where Hartford breached its duty to defend Wellman, is Oregon Mutual required to show that it sustained “damages” in order to assert a claim for equitable contribution? (Assignment of Error 5.)

8. Where Hartford breached its duty to defend Wellman in bad faith and violated claim handling regulations, did Wellman suffer damages sufficient to sustain a negligence claim against Hartford? (Assignment of Error 6.)

9. Must Hartford pay all *Buchholz* defense costs when those costs cannot be reasonably segregated between covered and non-covered amounts? *National Steel Constr. Co. v. National Union Fire Ins. Co.*, 14 Wn. App. 573, 576, 543 P.2d 642 (1975). (Assignment of Error 7.)

10. Where Hartford breached its duty to defend in bad faith, is Oregon Mutual precluded from asserting a claim for *Olympic Steamship* attorney fees because of “unclean hands,” when at the time of tender Wellman and/or Oregon Mutual allegedly “knew” Hartford would have no ultimate duty to indemnify? (Assignment of Error 8.)

III. STATEMENT OF THE CASE

A. Hartford’s Policy.

Hartford issued policy number 02 CSE T16998 to Wellman as a named insured (the “Policy”). **CP 1682.** The Policy was in effect from October 1, 1995 to October 1, 1996. **Id.** Its insuring clause states:

- a. We will pay those sums that the insured becomes legally obligated to pay as damages because of “bodily injury” or “property damage” to which this insurance applies. We will have the right and duty to defend any “suit” seeking those damages. . . .

* * *

- b. This insurance applies to “bodily injury” and “property damage” only if:
 - (1) The “bodily injury” or “property damage” is caused by an “occurrence” that takes place in the “coverage territory” and arises out of:
 - (i) Operations performed for you by the “contractor” at the location specified in the Declarations; or
 - (ii) Your acts or omissions in connection with the general supervision of such operations; and
 - (2) The “bodily injury” or “property damage” occurs during the policy period.

CP 1683. The “contractor” is identified as Otis Elevator Company

(“Otis”). **CP 1685.** The Policy defines “property damage” to mean:

- a. Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or
- b. Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the "occurrence" that caused it.

CP 1703. The Policy defines “occurrence” as “an accident including continuous or repeated exposure to substantially the same general harmful conditions.” *Id.*

Thus Hartford promised to defend Wellman, as a named insured, against suits for accidental property damage arising out of Otis' operations and Wellman's general supervision of Otis's operations.

B. The Underlying Suits.

Wellman was the general contractor on a condominium project in Bellingham. In the *Buchholz* suit, the Condominium developer sued Wellman for breach of contract and indemnity arising out of construction defects. **See CP 1705-14.** The *Buchholz* complaint alleged:

1.12 That Defendant Wellman & Zuck breached the construction contract and its warranty by (1) failing to provide work that was free from defect, (2) failing to perform the work in conformity with the contract documents; (3) failure to comply with the applicable building codes; and (4) failure to perform the work in a proper and workmanlike manner; and (5) failing to complete construction in the time required by the construction contract.

1.13 That as a direct and proximate result of the breach of contract as aforesaid, the building located at 1301 West Holly Street and condominiums and common spaces therein have suffered severe and significant water damage which require repair.

CP 1707-08 (emphasis added). The *Buchholz* complaint did not state when any property damage occurred, nor did it limit plaintiffs' claims to the work of any particular contractor. **See CP 1705-14.**

Wellman tendered the *Buchholz* suit to Hartford in January 2003. **CP 1721.** Four months later, Hartford informed Wellman that it would not provide a defense to *Buchholz* for three reasons. **CP 1723.** First, even

though the complaint expressly alleged construction defects caused “severe and significant water damage,” Hartford asserted there was no allegation of “property damage” caused by an “occurrence”:

The claims against Wellman & Zuck, Inc., involve economic loss arising out of a breach of agreement and inadequate design and construction. The damages alleged are not “property damage” . . . nor are the damages the result of an “occurrence” as defined by the Policy. . . .

CP 1724.

Second, even though the *Buchholz* complaint did not allege when any of the damage occurred, Hartford declined to defend by suggesting that the damage occurred after its policy period expired: “Additionally, since the Complaint does not specify a date when the damages are alleged to have occurred, to the extent that any of these damages occurred outside of the policy period, no coverage would be provided.” **CP 1724.**

Third, and even though the complaint expressly alleged “water damage,” Hartford based its denial on the Policy’s “impaired property” exclusion “k”: “Since the claims against Wellman & Zuck, Inc. allege defects and deficiencies in the construction of the premises, Exclusion k. would have applied.” **CP 1725.** By its own terms, however, Exclusion k does not apply when there is physical damage.² **See CP 1725.**

² Although Hartford’s denial letter quotes the policy language limiting coverage to damages arising out of designated “contractor” Otis’s operations, Hartford did not base its denial on that language. **See CP 1724.**

Oregon Mutual fully defended Wellman in *Buchholz*, and it paid \$75,000 to settle the developer's claims. **CP 1630.**

The condominium owners intervened in *Buchholz* and asserted third-party claims against the developer. **See CP 1749-60.** The developer was insured by State Farm Fire & Casualty Company ("State Farm"), which defended and settled the homeowners' third-party claims against the developer in *Buchholz*. **CP 1730 at ¶ 3.4.** State Farm then sued Wellman in a separate action as the developer's subrogee to recover the \$1,525,000 it paid to settle the homeowners' claims (the "*State Farm*" suit). **See CP 1728-31.** State Farm's complaint against Wellman alleged:

3.2 Wellman & Zuck's work on Olympic Condominium took place from 1995 through at least 1999. There were substantial delays in the construction of the Olympic Condominium by Wellman & Zuck, Inc., and substantial defects in the work performed by Wellman & Zuck, Inc. in the construction of the Olympic Condominium.

3.3 In 2002 the Unit Owners Association of Olympic Condominium . . . brought suit against [the developer] West Holly under RCW 64.34 for damages arising from the construction, marketing and sale of units, limited common areas and common areas of Olympic Condominium. These claims were brought in Whatcom County Superior Court cause no. 02-00101-3 [*i.e.*, in the *Buchholz* suit].

CP 1729.

Wellman tendered the *State Farm* Suit to Hartford in August 2004.

CP 1733. Its tender letter pointed out that the *State Farm* Suit was "related to and involves the same underlying facts as the previous notice

of claim [for *Buchholz*].” **CP 1734**. The tender also explained that Oregon Mutual had already retained defense counsel for Wellman and that, per defense counsel, liability was clear: “Bullivant, Houser Bailey, PC currently recommends settlement of this matter with State Farm because the existence of property damage is quite clear[.]” **CP 1734**.

This time, Hartford conceded that the “property damage” and “occurrence” requirements in the Policy may be satisfied by the *State Farm* complaint. *See CP 1738*. Nonetheless, Hartford refused to defend under an exclusion for damage that occurs after Otis’s work is completed:

This insurance does not apply to:

* * *

- c. “Bodily injury” or “property damage” which occurs after the earliest of the following times:
 - (1) When all “work” on the project (other than service, maintenance, or repairs) to be performed for you by the “contractor” at the site of the covered operations has been completed; or
 - (2) When that portion of the “contractor’s” “work,” out of which the injury or damage arises has been put to its intended use by any person or organization. This exclusion does not apply to any contractor or subcontractor working directly or indirectly for the “contractor” or as part of the same project.

CP 1738-39. According to Hartford, this exclusion applied because the prior *Buchholz* Suit was commenced after construction was completed:

The policy clearly states that the coverage provided does not

apply after either the contractor's (Otis') work on the site has been completed or when that portion of their work has been put to its intended use. Based on the fact that the original action was brought by the condo owners, living in the finished project, Otis Elevator's work would have been completed and put to its intended use, thus precluding coverage. . . .

CP 1739. Hartford thus assumed all damage occurred after the project was completed – even though the owners' third-party complaint in *Buchholz* alleged that “[e]ven prior to the sale of one or more Olympic units, plaintiffs [Buchholz] and West Holly knew the buildings leaked, that they suffered from serious construction defects and that if not repaired quickly they would incur event greater damages[.]” **CP 1752, at ¶ 6.i.**

Moreover, even though the *State Farm* complaint did not allege when any damage occurred or whether the damage was caused by the work of any particular subcontractor, Hartford also declined to defend based on exclusions that bar coverage for completed work, for work performed by Otis and for “impaired property.”³ **CP 1739-40.**

In September 2004, Wellman sent a letter objecting to Hartford's denial, pointing out the *State Farm* complaint was silent as to when any property damage occurred, and noting that damage could have occurred during Hartford's policy period:

³ Like its denial in *Buchholz*, Hartford's denial letter for *State Farm* quotes Policy language limiting coverage to damages arising out of Otis's operations but, again, Hartford did not base its denial on that language. *See CP 1738.*

Without conducting sufficient investigation of our claim, [Hartford's] letter attempts to skirt the fact that damage occurred during a period at which policy coverage by the Hartford was in effect. As has been stated in previous letters, the basis of Wellman & Zuck's claim for property damage arises out of the construction of a condominium project, which resulted in property damage to the condominiums due to water intrusion and resulting water damage, and other damage. . . . Construction of the condominiums formally commenced on or about February 10, 1996, and construction was substantially completed in about August of 1997. The Hartford policy coverage was in effect for part of this time period (from October 1, 1995, until October 1, 1996). It is well established under Washington law that in cases involving continuing damages, all insurers providing coverage are held jointly and severally liable to provide coverage of all damages, regardless of the specific amount of damage that occurred during a particular insurer's policy period. Once damage occurs during a policy period, that policy is triggered.

CP 1743 (footnote omitted; emphasis added).

Wellman also offered to give Hartford additional information documenting the damage:

These damages primarily include water intrusion and resulting damages. Please let us know if you would like for us to provide additional information and materials documenting these damages in greater detail, or feel free to contact Mr. Dino Vasquez [Wellman's defense counsel] to obtain additional documentation, including an expert report prepared Exterior Research & Design. If you wish, our office would be glad to contact Mr. Vasquez and obtain a copy of the report for you.

CP 1743 (emphasis added). Hartford never responded. **CP 1747.**

Oregon Mutual fully defended Wellman in the *State Farm* Suit, and it paid \$750,000 to settle State Farm's claims. **CP 1630.** Oregon Mutual then brought this action against Hartford seeking reimbursement

of all amounts it paid to defend and settle the two lawsuits, based on Hartford's bad faith breach of its duty to defend.

C. Proceedings Below.

This case has a lengthy procedural history in the court below. Oregon Mutual filed suit against Hartford in November 2005, asserting claims in its own right and as Wellman's assignee for declaratory judgment, breach of contract, bad faith, negligence, statutory and administrative violations, violation of the CPA, and *Olympic Steamship* attorney fees and costs. **CP 1794-804.**

In May 2006, Oregon Mutual moved for summary judgment seeking an order finding that Hartford breached its duty to defend under the insurance contract, that Hartford's denied a defense in bad faith, that Hartford was estopped to deny coverage, that Hartford violated the CPA, and that Oregon Mutual was entitled to its *Olympic Steamship* fees and costs. **CP 1761-81.** In response, Hartford argued it had no duty to defend because – despite the allegations in the *Buchholz* and *State Farm* complaints – there was no evidence that Otis's work had caused any damage at the project; in other words, Hartford claimed it had no duty to defend because it ultimately would not have had any obligation to indemnify under the Policy issued to Wellman, despite the fact that this conclusion was not based on any allegations in the complaints. **See CP**

1663-67. The trial court granted Oregon Mutual's motion in part, finding that Hartford breached its duty to defend in bad faith. **CP 1369-72.** The court declined to rule at that point on the issues of estoppel, damages for breach of contract, CPA damages, or *Olympic Steamship* attorney fees. **CP 1371.**

Oregon Mutual then moved for summary judgment on the ground that Hartford could not rebut the presumption of harm flowing from its bad faith refusal to defend Wellman. **CP 1350-57.** Hartford opposed and cross-moved, based on the novel argument that Wellman's tenders to Hartford were "false and without any foundation," and were "patent misrepresentation[s] of a claim to Hartford," because Wellman and/or Oregon Mutual "knew" Otis's work was not implicated in the suits when Wellman tendered to Hartford. *See* **CP 1331-32; 1341-42.** The trial court denied both motions, finding an issue of fact as to whether Wellman had been harmed by Hartford's denials of defense. *See* **CP 1221-23.**

Based on this ruling, Hartford then moved the trial court to vacate its prior order finding that Hartford acted in bad faith. **CP 1215-19.** Hartford argued that that an issue of fact on the bad faith element of "harm" required the court to vacate its prior finding that Hartford had breached its duty of good faith. **CP 1217-19.** Hartford's motion did not ask the trial court to also vacate its finding that Hartford breached the

insurance contract. *See* CP 1215-19, 1199-201. Oregon Mutual pointed out that the court's prior decision established the elements of "duty" and "breach" but left causation and harm to be determined later; consequently, duty and breach should remain in place regardless of any issue of fact on "harm." *See* CP 1203-06. The trial judge granted Hartford's motion and vacated its finding that Hartford acted in bad faith. CP 1196-98.

Hartford thereafter took the position that by vacating its ruling on the tort of bad faith, the trial court had also vacated its prior ruling on breach of the contractual duty to defend. *See* CP 1191. Oregon Mutual moved for reconsideration and clarification, asking the court to confirm that its ruling on breach of contract had not been vacated. CP 1187-93. According to Hartford, "information subsequently developed over the last year of discovery" demonstrated "singular lack of any facts implicating Otis", and the trial court would not have found a duty to defend had those additional facts (from outside the complaints) been known. CP 1182. Based on this additional "discovery," Hartford argued that the court's order also vacated its prior finding on breach of contract. CP 1182-85. Although neither Hartford's motion to vacate nor the court's order contained any reference to Oregon Mutual's breach of contract claims, the trial court nonetheless ruled that it had also vacated its ruling on breach of contract. CP 1143-45; RP 10/19/07 at 14:15-15:25.

Oregon Mutual sought discretionary review of the trial court's order granting Hartford's motion to vacate, under Cause No. 60841-0 I. Commissioner James R. Verellen denied discretionary review, but he also confirmed that *both* suits "readily" triggered Hartford's duty to defend:

The duty to defend is readily triggered, and it appears that the general allegations of "water damage" and "damage" in the two complaints hypothetically could be covered as property damage arising out of an elevator subcontractor's performance.

CP 545.

Back in the trial court, Hartford continued to press its argument that the tenders were "in bad faith" and "fraudulent." It next moved to dismiss Oregon Mutual's estoppel claim by arguing that an insurer's good faith duty to evaluate a tender of defense is excused by alleged "unclean hands," because Wellman "knew" there was no damage caused by Otis at the time it tendered to Hartford. *See CP 1123-41.* In response, Oregon Mutual pointed out that Hartford could point to no authority to support its claim that an insured's purported "unclean hands" could excuse a bad faith denial of defense, that Wellman's purported knowledge of damage or lack of damage caused by Otis's work was irrelevant as to Hartford's duty to defend under *VanPort*, and that Hartford's conclusory assumptions regarding "knowledge" and "unclean hands" were not even supported by

the record. **CP 1001-08.** The trial court granted Hartford's motion and dismissed Oregon Mutual's estoppel claim. **CP 956-58.**

Oregon Mutual also filed its own motion asking the court to reinstate its finding that Hartford breached its contractual duty to defend, based in part on Commissioner Verellen's conclusion that Hartford's duty to defend was "readily triggered." **CP 1032-42.** Hartford cross-moved, arguing it had no duty to defend. *See* **CP 1009-30.** The trial court granted Oregon Mutual's motion in part, ruling that Hartford had a duty to defend Wellman in the *Buchholz* Suit, but for unstated reasons it also ruled that Hartford did not have a duty to defend the *State Farm* Suit. **CP 953-55.**

Hartford then moved to dismiss Oregon Mutual's claim for *Olympic Steamship* fees, again arguing that Wellman's tenders were "gross and groundless misrepresentation[s]" because Wellman allegedly knew Otis's work did not cause any damage at the project when it tendered. **CP 916-20.** According to Hartford, *Olympic Steamship* was an "equitable exception" to the American Rule, and *Olympic Steamship* claims were therefore subject to the equitable defense of "unclean hands." **CP 921-26.** Oregon Mutual, once again, responded by pointing out that Hartford's arguments contravened *Woo* and *VanPort*, and it also re-emphasized that Hartford's "bad faith tender" had no factual support in the

record. **CP 906-14.** The trial court granted Hartford's motion and barred Oregon Mutual from recovering *Olympic Steamship* fees. **CP 871-73.**

Hartford next moved to dismiss all of Oregon Mutual's remaining claims, arguing that Wellman had not sustained any damages from its failure to defend because there was no evidence of any property damage from Otis's work. **CP 854-69.** Oregon Mutual responded by, *inter alia*, pointing out that Hartford was essentially arguing that it had no duty to defend because it would not have had any duty to indemnify – an argument squarely rejected in numerous cases – and that there were issues of fact as to Oregon Mutual's remaining claims. **CP 811-22.** This time, the trial court denied Hartford's motion but dismissed Oregon Mutual's contribution claim based on Hartford's argument that Oregon Mutual suffered no "damages" from Otis's work. **CP 790-92; see CP 868.**

In October 2010, Hartford again proffered its "bad faith tender" argument by moving to dismiss Oregon Mutual's bad faith and CPA claims. Hartford again argued that Oregon Mutual "misrepresented its claims for coverage" and that it was the law of the case that Oregon Mutual "acted in bad faith and with 'unclean hands' in tendering its claims to Hartford." **CP 617-32.** Once again, Oregon Mutual directed the court to Washington cases on the duty to defend and argued that Hartford's "frivolous tender" argument was contrary to the record. **CP 491-502.** The

trial court nonetheless granted Hartford's motion and dismissed Oregon Mutual's bad faith and CPA claims. **CP 373-75.**

At the same time, Oregon Mutual moved for revision of the court's ruling that Hartford did not have a duty to defend the *State Farm* Suit, based on the Washington Supreme Court's recent decision in *American Best Food, Inc. v. Alea London, Ltd.*, 168 Wn.2d 398, 229 P.3d 693 (2010). **CP 558-67.** This motion was denied. **CP 376-78.**

In December 2011, Hartford moved to dismiss Oregon Mutual's remaining breach of contract and negligence claims, reiterating its argument that Wellman suffered no damages from Hartford's failure to defend. **CP 193-208.** At the same time, Oregon Mutual moved for an order requiring Hartford to pay all defense costs in the *Buchholz* Suit because Hartford had not met its burden to segregate those costs between covered and non-covered amounts. **CP 156-65.** On February 2, 2011, the trial court granted summary judgment for Hartford and dismissed Oregon Mutual's remaining claims for breach of contract and negligence. **CP 68-70.** The court also denied Oregon Mutual's motion on *Buchholz* defense costs. **CP 73-75.**

This appeal followed.

IV. ARGUMENT

Although the trial court ruled early in the case that Hartford breached its duty to defend in bad faith, the court then vacated those rulings and thereafter piled error upon error by dismissing all of Oregon Mutual's claims based on Hartford's "bad faith tender – unclean hands" arguments and on Hartford's claim that its breach of duty to defend did not cause any damage to Wellman or Oregon Mutual. In so doing, the trial court ignored longstanding Washington law on the duty to defend by, *inter alia*, approving Hartford's denial of defense based on information outside the "four corners" of the complaints, and by sanctioning Hartford's argument that it had no duty to defend because (in hindsight) it would have ultimately owed no indemnity. The trial court also created – out of whole cloth – a new rule of law under which an insurer can retroactively excuse its bad faith denial of defense by pointing to what the insured arguably knew or should have known at the time of tender. In addition to contravening established Washington law, the "bad faith tender" rule adopted by the trial court is also unsupported by the record because there is no indication that Wellman or Oregon Mutual possessed any information specifically "exonerating" Otis's work – thus even arguably excusing Hartford's duty to defend – at the time of any tender.

Reversal is therefore necessary to bring this case into compliance with Washington law and to finally recognize Hartford's manifest bad faith in refusing to defend Wellman.

A. Standard of Review.

This appeal involves numerous summary judgment rulings by the court below. Review of an order of summary judgment is *de novo*, and the appellate court performs the same inquiry as the trial court. *Smith v. Safeco Ins. Co.*, 150 Wn.2d 478, 483, 78 P.3d 1274 (2003). A motion for summary judgment is properly granted where there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. *Id.* at 485; CR 56(c).

B. The Trial Court Erred In Its Rulings Regarding Hartford's Duty To Defend.

The trial court initially ruled that Hartford breached its contract by refusing to defend Wellman in the *Buchholz* and *State Farm* suits. CP 1369-72. The court subsequently vacated that ruling after finding an issue of fact on the element of "harm" applicable to Oregon Mutual's tort claim for bad faith – even though Hartford's motion to vacate did not also ask the court to vacate its ruling on breach of contract.⁴ *See* CP 1215-19,

⁴ *Cf. Jackowski v. Borchelt*, 151 Wn. App. 1, 16-17, 209 P.3d 514 (2009), *review granted*, 168 Wn.2d 1001 (2010) (finding error where trial court summarily dismissed claim not addressed in movant's summary judgment motion).

1199-201, 1196-98. The trial court then partially reinstated its initial ruling by finding that Hartford had a duty to defend *Buchholz* but not *State Farm*. **CP 953-55.** Then, the trial court dismissed Oregon Mutual's breach of contract claim in its entirety based on Hartford's argument that Wellman was not damaged by Hartford's failure to defend. **CP 68-70.**

These latter rulings were error because, as a matter of law, Hartford breached its duty to defend Wellman in *both* suits. An insurer's duty to defend under a liability insurance policy "is separate from, and broader than, the duty to indemnify." *Hayden v. Mutual of Enumclaw Ins. Co.*, 141 Wn.2d 55, 64, 1 P.3d 1167 (2000). Washington law is clear:

- The duty to defend arises when a complaint against the insured alleges facts which could, if proven, impose liability upon the insured within the policy's coverage. *VanPort* at 761.
- The complaint must be liberally construed and the insurer must defend if the claim is "conceivably" within coverage. *Hayden*, at 64.
- Only if the alleged claim is "clearly" not covered by the policy is the insurer relieved of its duty to defend. *VanPort* at 761.
- "[A]n insurer may not rely on facts extrinsic to the complaint in order to deny its duty to defend where . . . the complaint can be interpreted as triggering the duty to defend." *Id* at 761.
- If coverage is not clear from the complaint but may exist, the insurer

must investigate and give the insured the benefit of the doubt in determining whether there is a duty to defend. *Id.* In doing so, the insurer must defend its insured under a reservation of rights and then file a declaratory judgment action to terminate its defense obligation. *Id.* at 761.

Since the duty to defend is based on whether the allegations in the complaint are “conceivably” covered, the insurer must defend even if there is a question as to whether the damages in the case would ultimately be covered under the policy. *See Travelers Ins. Cos. v. North Seattle Christian & Missionary Alliance*, 32 Wn. App. 836, 842, 650 P.2d 250 (1982) (factual contentions regarding circumstances of fatal plane crash were irrelevant as to duty to defend when underlying complaint alleged covered facts). *See also Kirk v. Mt. Airy Ins. Co.*, 134 Wn.2d 558, 564, 951 P.2d 1124 (1998) (“The duty to defend is broader than the duty to indemnify, so the duty to defend may be triggered without exposing the insurer to coverage liability”).

The Washington Supreme Court has stressed the importance of the duty to defend in protecting the insured when addressing bad faith denials of defense: “The defense must be prompt and timely. An insurer refusing to defend exposes its insured to business failure and bankruptcy.” *VanPort*, 147 Wn.2d at 765 (emphasis added).

1. Hartford Breached Its Duty To Defend *Buchholz*.

Hartford refused to defend Wellman in the *Buchholz* Suit on three grounds. First, it asserted that the plaintiffs' claims "involve economic loss arising out of a breach of agreement and inadequate design and construction," and that "[t]he damages alleged are not "property damage" . . . nor are the damages the result of an "occurrence" as defined by the Policy." **CP 1724.** To the contrary, it is well settled that defective construction constitutes an "occurrence" under Washington law. *See Yakima Cement Prods Co. v. Great Am. Ins. Co.*, 93 Wn.2d 210, 215, 608 P.2d 254, 257 (1980) (insured's defective manufacture of cement panels was an "occurrence"); *DeWitt Constr., Inc. v. Charter Oak Fire Ins. Co.*, 307 F.3d 1127, 1133 (9th Cir. 2002) (insured's defective construction of concrete piles was "occurrence" under Washington law). The *Buchholz* complaint satisfied the "occurrence" requirement in Hartford's Policy because it expressly alleged a claim against Wellman for defective construction. In addition, the Hartford Policy defined "property damage" as "physical injury to tangible property." *Buchholz*'s allegation of "severe and significant water damage" clearly satisfied this requirement. The *Buchholz* complaint thus alleged an "occurrence" and "property damage."

Second, Hartford asserted the complaint was ambiguous as to when the damage occurred: "Additionally, since the Complaint does not

specify a date when the damages are alleged to have occurred, to the extent that any of these damages occurred outside of the policy period, no coverage would be provided.” **CP 1724.** Under *Vanport*, however, an insurer must defend if the complaint is unclear, but Hartford did just the opposite: it used an ambiguity in the complaint to deny a defense.

Third, Hartford based its denial on “impaired property” exclusion “k”: “Since the claims against Wellman & Zuck, Inc. allege defects and deficiencies in the construction of the premises, Exclusion k. would have applied.” **CP 1725.** By its own terms, however, this exclusion cannot apply when there is physical damage:

[T]he exclusion may apply to claimed damages that do not result in physical damage. However, reading the complaint on its face, damage to the customers’ property could be physical and thus the impaired property exclusion would not apply.

Vanport, 147 Wn.2d at 762. The *Buchholz* complaint expressly alleged physical injury in the form of “severe and significant water damage.” Given this allegation, the “impaired property” exclusion could not possibly apply, but Hartford nevertheless relied on it in refusing to defend.

The *Buchholz* complaint thus triggered Hartford’s duty to defend as a matter of law because it alleged accidental property damage conceivably within the coverage promised in Hartford’s Policy. Hartford breached this duty in declining Wellman’s tender. The trial court’s initial

ruling so holding should be reinstated and its subsequent findings to the contrary should be reversed.

2. Hartford Also Breached Its Duty To Defend *State Farm*.

In responding to Wellman's tender of the *State Farm* Suit, Hartford conceded that the complaint may have alleged an "occurrence" and "property damage," but it nonetheless refused to defend based on an exclusion for property damage that occurs after Otis's work is completed. **CP 1738-39.** Significantly, however, the *State Farm* complaint – just like the *Buchholz* complaint – was totally silent as to when damage occurred. **See CP 1728-31.** Hartford also refused to defend based on its assumption that all damage must have occurred after the project was completed because the suits were filed by the condominium owners. **CP 1739.** This is likewise incorrect because the date a suit is filed does not determine when property damage could have occurred.⁵

Hartford's denial also raised the "work" and "impaired property" exclusions. **CP 1739-40.** As to the former, nothing in the complaint indicated that property damage was confined to a particular contractor's work, so this exclusion could not in and of itself preclude a defense. The

⁵ Of note, the condominium owners' third-party complaint in *Buchholz* alleged that "[e]ven prior to the sale of one or more Olympic units, plaintiffs [Buchholz] and West Holly knew the buildings leaked, that they suffered from serious construction defects and that if not repaired quickly they would incur event greater damages[.]" **CP 1752, at ¶ 6.i.**

“impaired property” exclusion likewise could not apply because *State Farm* arose out of the same property damage alleged in the *Buchholz* complaint, and because the exclusion does not apply when there is actual physical injury to property. *See Vanport*, 147 Wn.2d at 762.

Hartford adhered to its denials even after Wellman re-tendered, pointing to evidence suggesting property damage during Hartford’s policy period and offering to provide Hartford with the report of an expert, Exterior Research & Design, Inc. (the “ERD Report”). **CP 1743.** Hartford, admittedly, never responded. **CP 1747.**

Thus *State Farm* likewise triggered Hartford’s duty to defend, and Hartford breached its duty by declining Wellman’s tender. The trial court should likewise be corrected on this issue.⁶

C. The Trial Court Erred In Its Rulings Denying Bad Faith.

The trial court initially ruled that Hartford acted in bad faith by denying a defense to Wellman in the *Buchholz* and *State Farm* suits. **CP 1369-72.** The court subsequently vacated this ruling, however, after finding an issue of fact as to whether Wellman had suffered “harm” from

⁶ Although both of Hartford’s denial letters quote the Policy’s language limiting coverage to damages arising out of Otis’s operations or Wellman’s supervision of those operations, *see CP 1724, 1738*, Hartford did not rely on that language in denying a defense for *either* suit. Hartford also failed to follow a critical requirement of *VanPort*: If it was unsure as to whether a defense was owed, Hartford was required to provide a defense under a reservation of rights and then file an action for declaratory judgment to obtain an order allowing it to withdraw from the defense. *See VanPort*, 147 Wn.2d at 761. Hartford did neither.

Hartford's bad faith denials of defense. **CP 1196-98.** The court then dismissed Oregon Mutual's bad faith claim based on Hartford's argument that Wellman and/or Oregon Mutual "misrepresented [their] claims for coverage" and that it was the law of the case that Oregon Mutual "acted in bad faith and with 'unclean hands' in tendering its claims to Hartford." **See CP 617-32, 373-75.**

1. The Trial Court Erred In Dismissing Oregon Mutual's Bad Faith Claim.

The trial court's dismissal of Oregon Mutual's bad faith claim should be reversed. Insurers have a statutory and common law duty of to act in good faith toward their insureds. *Anderson v. State Farm Mut. Ins. Co.*, 101 Wn. App. 323, 329, 2 P.3d 1029 (2000). An insurer acts in bad faith when it refuses to defend its insured and the refusal is "unreasonable, frivolous, or unfounded." *Kirk v. Mt. Airy, supra*, 134 Wn.2d at 560. "The insurer's fiduciary duty to act in good faith is fairly broad and may be breached by conduct short of intentional bad faith or fraud." *Anderson*, 101 Wn. App. at 329. An insurer must give the rights of the insured the same consideration that it gives to its own monetary interests. *Vanport*, 147 Wn.2d at 761. An insurer acts in bad faith when it overemphasizes its own interests. *Anderson*, 101 Wn. App. at 329.

In *VanPort*, the insured was a construction company that was sued

by several of its customers. The insured tendered defense of the suits to its insurer, which denied coverage in a letter containing “a laundry list of exclusions without any analysis or correlation to the particular claims.” *VanPort* at 764. A few months later, the insured sent a follow-up letter asking the insurer for clarification as to why it had denied coverage; the insurer never responded. *Id.* at 757, 764. On these facts, the Washington Supreme Court ruled, as a matter of law, that the insurer had denied coverage in bad faith. *Id.* at 764. The court also held that the insurer violated WAC 284-30-330(13), which requires an insurer to explain the basis for a denial of coverage. *Vanport*, at 764.⁷

This appeal presents conduct and coverage denials similar to those in *Vanport*. Hartford failed to provide any proper explanation for its denial but instead asserted reasons that were groundless, given the allegations in the complaints and the Policy language. As discussed in Section B., *supra*, Hartford’s bases for denying a defense in *Buchholz* ignored the allegations in the *Buchholz* complaint and were also contradicted by the language in Hartford’s own Policy. The same is true for *State Farm*, wherein Hartford refused to defend Wellman based on

⁷ WAC 284-30-330(13) makes it an unfair and deceptive act to “Fail[] to promptly provide a reasonable explanation of the basis in the insurance policy in relation to the facts or applicable law for denial of a claim or for the offer of a compromise settlement.”

assumptions and exclusions that could not possibly have precluded a duty to defend. These denials were “unreasonable, frivolous or unfounded” as a matter of law, and the trial court should be reversed on this issue.

2. Alternatively, The Trial Court Erred In Finding An Issue Of Fact On “Harm”.

The trial court denied summary judgment for Oregon Mutual, finding an issue of fact as to whether Wellman had been harmed by Hartford’s bad faith denial of defense. *See CP 1221-23*. This was error because Hartford had failed to rebut the presumption of harm flowing from its bad faith conduct. Once an insurer is found to have acted in bad faith, there is a presumption that the insured has suffered harm as a result. *Safeco Ins. Co. v. Butler*, 118 Wn.2d 383, 390, 823 P.2d 499 (1992). Once the presumption of harm attaches, the burden then shifts to the insurer to rebut that presumption by affirmatively showing that the insured has not been harmed by its bad faith conduct. *See id.* In creating this presumption of harm, the Washington Supreme Court reasoned as follows:

Presuming prejudice once the insured establishes bad faith shifts the burden to the insurer to prove its acts did not prejudice the insured. The shifting of the burden ameliorates the difficulty insureds have in showing that a particular act resulted in prejudice. . . . Finally, imposing a presumption of prejudice only after the insured shows bad faith adequately protects the competing societal interests involved. It provides a meaningful disincentive to insurers’ bad faith conduct while protecting insurers from frivolous claims.

Id. at 392. Harm is presumed to flow from an insurer's bad faith because "the course cannot be rerun, no amount of evidence will prove what might have occurred if a different route had been taken." *Id.* at 391.

The Washington Supreme Court subsequently noted that this presumption of harm imposes an "almost impossible burden of proof" on the insurer. *Mutual of Enumclaw v. Dan Paulson Constr.*, 161 Wn.2d 903, 921, 169 P.3d 1 (2007). The cases demonstrate that this presumption can only be rebutted in unique circumstances. For example, the presumption of harm has been rebutted where the insured had previously declared bankruptcy (for reasons unrelated to insurance) and was therefore not subject to personal liability for the loss, despite the insurer's bad faith refusal to defend. *See Werlinger v. Clarendon Nat'l Ins. Co.*, 129 Wn. App. 804, 809, 120 P.2d 593 (2005).

This case, however, is markedly different. Based on grounds that were patently unreasonable and unfounded, Hartford refused to defend Wellman in two lawsuits seeking more than \$1 million in damages. But for the fortuity that Wellman also had insurance through Oregon Mutual, it would have faced a potentially devastating liability. *Cf. VanPort*, 147 Wn.2d at 765 (insurer's bad faith refusal to defend can expose insured to business failure and bankruptcy). Nonetheless, the court below misplaced the parties' burdens and denied summary judgment based on an issue of

fact on “harm” under CR 56, despite Hartford’s manifest failure to satisfy its “almost impossible burden” to rebut the presumed harm flowing from its bad faith denial of defense. The court should be reversed on this issue, and Hartford’s bad faith should be found to have harmed Wellman as a matter of law.

D. The Trial Court Erred In Precluding Oregon Mutual From The Remedy Of Estoppel.

An insurer that refuses or fails to defend in bad faith is estopped from denying coverage. *VanPort*, 147 Wn.2d at 759. This is true even if the underlying events are ultimately found not to fall within the policy’s coverage. *See Kirk*, 134 Wn.2d at 564; *Safeco Ins. Co. v. Butler*, 118 Wn.2d at 406.. The estoppel remedy is necessary to ensure that insurers do not shirk the duties owed to their insureds:

. . . When the insurer breaches the duty to defend in bad faith, the insurer should be held liable not only in contract for the cost of the defense, but also should be estopped from asserting the claim is outside the scope of the contract and, accordingly, that there is no coverage. The coverage by estoppel remedy creates a strong incentive for the insurer to act in good faith, and protects the insured against the insurer’s bad faith conduct. . . .

. . . If we failed to apply the remedy [of estoppel] . . . , we would erode any incentive for an insurer to act in good faith. *Without coverage by estoppel and the corresponding potential liability, an insurer would never choose to defend with a reservation of rights when a complete failure to defend, even in bad faith, has no greater economic consequence than if such refusal were in good faith.* The requirement of acting in good faith cannot be rendered meaningless.

Kirk at 564-65 (emphasis added).

As set forth in Section C.1., above, Hartford's unreasonable and unfounded refusal to defend Wellman was bad faith as a matter of law. The trial court, nonetheless, dismissed Oregon Mutual's claim for the remedy of estoppel based on Hartford's novel "bad faith tender – unclean hands" argument. **See CP 956-58.** Specifically, Hartford asserted that Wellman's tenders were "groundless and irresponsible," "in bad faith," and "false, reckless, frivolous [and] without foundation," because Wellman supposedly knew Hartford's coverage was not implicated when it tendered those suits to Hartford. **See CP 1123-1141.** Hartford based this argument solely on the ERD Report which, according to Hartford, "exonerates" Otis because it does not contain any reference to defects or damage related to installation of the elevators.⁸ **See CP 1128-29, 1134-35, 1140.** Because Wellman or Oregon Mutual allegedly possessed this report prior to any tenders, Hartford claimed it was relieved of any defense obligation because they allegedly knew Hartford would not have had any ultimate obligation to indemnify.

The trial court agreed and barred Oregon Mutual from the remedy of estoppel. **See CP 956-58.** This was reversible error for at least three

⁸ Ironically, even though Wellman offered to provide the ERD Report to Hartford when it retendered the *State Farm* Suit, **see CP 1743**, Hartford never responded to that offer, **see CP 1747**.

reasons. First, Washington law is clear that an insurer's duty to defend must be determined based only on the allegations in the complaint and the insurance policy. *E.g., VanPort*, at 761. An insurer cannot refuse to defend its insured based on information outside of those two documents -- even if that information could show that the insurer would ultimately have no obligation to indemnify its insured. *See, e.g., Woo*, 161 Wn.2d at 53 (insurer may have duty to defend even though there may ultimately be no duty to indemnify). Hartford's argument contravenes these clear rules because Wellman's or Oregon Mutual's alleged "state of mind" would be extrinsic to the complaint and, therefore, could not provide support for Hartford's refusal to defend after the fact.

Second, Hartford can point to no authority -- from Washington or elsewhere -- to support its claim that an insured's subjective state of mind at the time of tendering can somehow impact the insurer's contractual coverage obligations or its obligation to act in good faith.

Third, even if an insured's "bad faith tender" could somehow, *post hoc*, excuse an insurer's unreasonable refusal to defend (which it cannot, under *VanPort*, *Woo*, and other authorities), the record does not support Hartford's claim that Wellman and/or Oregon Mutual knew Otis's work was not implicated in the underlying suits. To the contrary, there is no indication Wellman or Oregon Mutual actually "knew" Otis's work had

not caused any damage at issue in the *Buchholz* or *State Farm* suits. For example, Brian Wellman testified that his practice was to tender under all possibly applicable insurance because the nature and extent of alleged damage tends to expand once the parties' experts become involved. *See CP 900-901 at 41:17-42:8*. Additionally Oregon Mutual had split its file between two adjusters: Ken Schroeder was assigned to handle Wellman's defense in the suits. *See CP 1006*. Mr. Schroeder testified that he had seen the ERD Report, but he could not say whether the report included all issues that were included in the suits. *CP 912*. James Rumppe was assigned to handle coverage issues and the tenders to Hartford. *See CP 1006*. Mr. Rumppe testified that he never received nor reviewed the ERD Report as part of his coverage-related work on the file. *See CP 990 at 40:1-15*. Thus even if Wellman's or Oregon Mutual's "frame of mind" could be relevant to Hartford's duty to defend (which it is not), the record plainly does not support Hartford's argument.

Simply put, Wellman's or Oregon Mutual's alleged "state of mind" is legally and factually immaterial as to Hartford's duty to defend, Hartford's bad faith denial of defense estops it from denying coverage.⁹

⁹ Hartford will probably argue (as it did in the trial court) that there is no evidence of damage from Otis's work, so any estoppel does not require it to pay the *Buchholz* and *State Farm* settlements, based on *Ledcor Indus. (USA), Inc. v. Mutual of Enumclaw Ins. Co.*, 150 Wn. App. 1, 206 P.3d 1255 (2009). In that case, Ledcor was an "additional insured" under a Mutual of Enumclaw ("MOE")

E. **The Trial Court Erred In Dismissing Oregon Mutual's Claim Under The CPA.**

The undisputed facts of this case demonstrate that Hartford violated the CPA in one or more respects when it responded to Wellman's tenders. A cause of action under the CPA arises when there has been "(1) an unfair or deceptive act or practice; (2) which occurs in trade or commerce; (3) that impacts the public interest; (4) which causes injury to the plaintiff in his or her business or property; and (5) which injury is causally linked to the unfair or deceptive act." *Physicians Ins. Exch. & Ass'n v. Fisons Corp.*, 122 Wn.2d 299, 312, 858 P.2d 1054 (1993).

Violations of WAC 284-30 are *per se* violations of the CPA and establish the first two elements (*i.e.*, an unfair or deceptive act that occurs in trade or commerce). *See, e.g., Vanport*, 147 Wn.2d at 764 (violation of WAC 284-30-330 was *per se* CPA violation); *Anderson*, 101 Wn. App. at 331-32 (violation of any "Unfair Claims Settlement Practices" in WAC 284-30 is a *per se* CPA violation). In addition, the insurance industry is

policy issued to Zanetti. Although MOE agreed to defend Ledcor, it was found to have acted in bad faith by failing to timely accept Ledcor's tender and failing to promptly participate in Ledcor's defense, as required by *Tank v. State Farm Fire & Casualty Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986). Under those facts, this Court concluded that any estoppel from MOE's bad faith did not also require MOE to pay for liability caused by wrongdoers other than Zanetti. *Id.* at 10-11. This case is different. Among other things, in *Ledcor* MOE agreed to defend but then violated the obligations of a defending insurer under *Tank*. Here, Hartford refused to defend, so this case is instead controlled by cases addressing a bad faith denial of defense, *e.g., VanPort, Woo, and American Best Food*.

one affecting the public interest, so an insured's unfair or deceptive act satisfied the third element of a CPA claim. *See* RCW 48.01.030; *Anderson, supra*, 101 Wn. App. at 330.

The Washington Insurance Commissioner promulgated regulations proscribing "Unfair Claims Settlement Practices," at WAC 284-30. For example, WAC 284-30-330 provides as follows:

. . . The following are hereby defined as unfair methods of competition and unfair or deceptive acts or practices in the business of insurance, specifically applicable to the settlement of claims:

* * *

(2) Failing to acknowledge and act reasonably promptly upon communications with respect to claims arising under insurance policies.

* * *

(13) Failing to promptly provide a reasonable explanation of the basis in the insurance policy in relation to the facts or applicable law for denial of a claim[.]

Hartford never responded to Wellman's re-tender of the *State Farm* Suit, even though it provided additional information relevant to the duty to defend. *See* CP 1743; CP 1747. By ignoring Wellman's re-tender, Hartford violated, *inter alia*, WAC 284-30-330(2) (insurer commits unfair claim practice by "failing to acknowledge and act reasonably promptly upon communications with respect to claims arising under insurance policies"). Hartford also committed an unfair claim

practice when it failed to “provide a reasonable explanation of the basis in the insurance policy in relation to the facts . . . for denial of a claim.” *Cf.* WAC 284-30-330(13). As set forth above, Hartford’s denials of defense were unreasonable and ignored the allegations against Wellman. Lastly, Hartford’s WAC violations damaged Wellman because, among other things, Wellman was compelled to incur fees and costs in responding to Hartford’s unreasonable denials. This satisfies CPA elements four and five. *Cf. Anderson, supra*, at 333.

The trial court, nonetheless, adopted Hartford’s “bad faith tender” argument and dismissed Oregon Mutual’s CPA claim. *See CP 373-75*. As previously stated, this argument is unsupported by precedent or the record. Hartford can point to no authority to support its claim that an insured’s purported “state of mind” at the time of tender is a defense to an insurer’s unfair and deceptive acts under the CPA. The trial court should also be reversed as to its dismissal of Oregon Mutual’s CPA claim.

F. The Trial Court Erred In Dismissing Oregon Mutual’s Contribution Claim.

Oregon Mutual also sued Hartford in its own right for equitable contribution as a co-insurer of Wellman. The trial court dismissed Oregon Mutual’s contribution claim, apparently based on Hartford’s argument that Wellman was not damaged by its failure to defend because there was no

evidence of property damage caused by Otis's work. *See* CP 854-69; CP 790-92. Washington law, however, does not require a showing of "damages" in order to sustain a claim for equitable contribution; rather, the proper inquiry is whether one party has incurred a loss that should be borne by another:

Equitable contribution refers to the right of one party to recover from another party for a common liability. In the context of insurance law, contribution allows an insurer to recover from another insurer where both are independently obligated to indemnify or defend the same loss. Importantly, contribution is a right of the insurer and is independent of the rights of the insured. . . .

Mutual of Enumclaw Ins. Co. v. USF Ins. Co., 164 Wn.2d 411, 419 ¶ 13, 191 P.3d 866 (2008) (internal citations and footnote omitted). In addition:

In deciding whether one insurer is liable for equitable contribution to another, "the inquiry is whether the nonparticipating coinsurer 'had a legal obligation . . . to provide [a] defense [or] indemnity coverage for the . . . claims or action prior to [the date of settlement].'"

Id. at 420 ¶ 14 (quoting *Safeco Ins. Co. v. Superior Court*, 140 Cal. App. 4th 874, 879, 44 Cal. Rptr. 3d 841 (2006) (quoting *American Continental Ins. Co. v. American Cas. Co.*, 86 Cal. App. 4th 929, 938, 103 Cal. Rptr 2d 632 (2001))) (italics omitted).¹⁰

As stated above, Hartford breached its duty to defend Wellman in

¹⁰ The Supreme Court also cites, with approval, *National Indem. Co. v. St. Paul Ins. Cos.*, 150 Ariz. 458, 459, 724 P.2d 544 (1986) ("When an insurer has a duty to defend the insured, there should be no reward to the insurer for *breaching* that duty.") *Id.* at 420 ¶ 14 (emphasis in original).

the *Buchholz* and *State Farm* suits. If this Court determines that Hartford did not act in bad faith or that Hartford is not estopped to deny coverage for the *Buchholz* and *State Farm* settlements then, in the alternative, the dismissal of Oregon Mutual's contribution claim should be reversed and Oregon Mutual should be awarded contribution for Hartford's equitable share of *Buchholz* defense costs.

G. The Trial Court Erred In Dismissing Oregon Mutual's Negligence Claim.

The trial court also dismissed Oregon Mutual's negligence claim, based on Hartford's argument that Wellman had not been damaged by Hartford's conduct. *See CP 193-208; CP 68-70*. This was likewise error and should be reversed. Negligence and bad faith are two distinct causes of action in insurance disputes. *First State Ins. Co. v. Kemper Nat. Ins. Co.*, 94 Wn. App. 602, 612-13, 971 P.2d 953, 959 (1999) (insured was entitled to a jury instruction on both negligence and bad faith claims). An insurer can be held liable in tort for its negligence in handling a claim. *E.g., Murray v. Mossman*, 56 Wn.2d 909, 911, 355 P.2d 985 (1960)

Wellman suffered damages from Hartford's negligence because, among other things, Hartford's negligent denials caused Wellman to incur fees and costs in its attempts to persuade Hartford to honor its contractual and legal obligations. *See CP 903 at 75:4-15*. At the very least, there

were genuine issues of material fact regarding the reasonableness of Hartford's conduct in handling Wellman's tenders. The trial court's dismissal of Oregon Mutual's negligence should therefore be reversed.

H. The Trial Court Erred In Denying Oregon Mutual's Motion Regarding Hartford's Obligation For Defense Costs.

The trial court denied Oregon Mutual's motion for a declaration that Hartford's breach of duty to defend rendered it responsible for all *Buchholz* defense costs. *See CP 73-75*. In Washington, once an insurer's defense obligation is triggered, that insurer must pay all defense costs, regardless of whether another insurer is also obligated to defend. *See Gruol v. Constr. Co., Inc. v. Insurance Co. of N. Am.*, 11 Wn. App. 632, 637, 524 P.2d 427 (1974) (affirming trial court ruling that insurers were jointly and severally liable for costs of defense). *Cf. American Nat'l Ins. Co. v. B&L Trucking, Inc.*, 134 Wn.2d 413, 424, 951 P.2d 250 (1998) (insurers are jointly and severally liable for indemnity). A breaching insurer is thus liable for all defense costs unless there is a reasonable basis for prorating defense costs between covered and non-covered claims:

[W]here an insurer wrongfully refuses to defend, and there is no reasonable means of prorating the costs of defense between the covered and the not covered items, then the insurer is liable for the entire costs of defense.

National Steel Constr. Co. v. National Union Fire Ins. Co., 14 Wn. App. 573, 576, 543 P.2d 642 (1975). Moreover:

Issues regarding the segregation of covered and non-covered items do not even arise when a plaintiff has only one claim, based on one set of operational facts, and a unitary remedial entitlement. If an insured may be held liable for a claim, the insurer cannot even consider a rejection of the tender merely because one or more legal theories relating to that claim might not be covered. Issues involving proration or segregation between covered and non-covered claims arise[] only when there are separate claims for which there are separate damage entitlements. It is when those separate claims, and different damage entitlements, are undifferentiated that the courts must determine whether apportionment is possible.

In most cases, an insurer will not be able to establish a “reasonable means” for prorating undifferentiated judgments, settlements, and defense costs. . . .

Thomas V. Harris, *Washington Insurance Law* § 16.2 at p. 16-4 (2d ed. 2006) (italics in original; underlining added) (CP 174).

The *Buchholz* plaintiffs sued Wellman under two causes of action, one for breach of contract, and one to enforce a hold harmless agreement. CP 1705-14. Both presented a single claim for defective construction. For example, the *Buchholz* complaint alleges with respect to breach of contract:

1.12 That Defendant Wellman & Zuck breached the construction contract and its warranty by (1) failing to provide work that was free from defect, (2) failing to perform the work in conformity with the contract documents; (3) failure to comply with the applicable building codes; and (4) failure to perform the work in a proper and workmanlike manner[.]

1.13 That as a direct and proximate result of the breach of contract as aforesated, the building located at 1301 West Holly Street and condominiums and common areas therein have suffered severe and significant water damage which require[s]

repair.

* * *

1.15 That as a direct and proximate result of the breach of the construction contract by Defendant Wellman & Zuck as aforesated, the Plaintiffs herein have suffered the following damages:

(a) For the cost of repairing said defective work performed by Wellman & Zuck, in a sum which shall be determined at time of trial.

* * *

(i) For any damages incurred by plaintiffs yet to be discovered, in a sum which shall be determined at time of trial.

CP 1707-09. The complaint alleges similar defects and damage under the second cause of action for breach of the hold harmless agreement:

2.5 That the Defendant Wellman & Zuck has been notified of the defects in construction of the building at 1301 Holly Street, Bellingham, Washington and demand has been made upon said Defendant to repair said defects, but the said Defendant has wholly failed, refused and neglected to do so. That as a result, said building requires substantial repair, the costs of which shall be determined at time of trial.

2.6 That pursuant to the hold harmless, the Defendant Wellman & Zuck agreed to pay for all damages incurred by Plaintiffs arising out of any defect in construction. That said Plaintiffs have suffered the following damages by reason of the defective construction of Defendant Wellman & Zuck:

(a) For the cost of repairing said defective work performed by Wellman & Zuck, in a sum which shall be determined at time of trial.

* * *

(i) For any damages incurred by plaintiffs yet to be discovered, in a sum which shall be determined at time of trial.

CP 1711-13.

Thus, the *Buchholz* complaint alleged a claim arising out of a single set of operative facts (*i.e.*, alleged defective construction of the condominiums), for which unitary damages were sought (*i.e.*, the costs to repair defective work and damage at the condominiums). In other words, despite pleading two separate causes of action, *Buchholz* was a single claim that does not permit any allocation of defense costs between the work of Otis, Wellman, or any other trade. The allegations thus do not permit any allocation between covered and non-covered claims, and Hartford owed Wellman a complete defense. *Cf.* Thomas V. Harris, *Washington Insurance Law* § 16.2, *supra*. Accordingly, if this Court determines that Hartford did not act in bad faith or that Hartford is not estopped to deny coverage then, in the alternative, Hartford should be ordered to pay all defense costs.

I. The Trial Court Erred In Dismissing Oregon Mutual's Claim For Attorney Fees And Costs Under *Olympic Steamship*.

As set forth in *Olympic Steamship*, 117 Wn.2d at 54: “An insured who is compelled to assume the burden of legal action to obtain the benefit of its insurance contract is entitled to attorney fees.” *Olympic Steamship* fees and costs can be recovered where an insurance company

sues other insurers as the assignee of an insured. *See McRory v. Northern Ins. Co. of New York*, 138 Wn.2d 550, 556, 980 P.2d 736 (1999) (“assignees of the insured may recover fees if they are compelled to sue an insurer to secure coverage”).

Oregon Mutual, as Wellman’s assignee, sued Hartford to enforce Wellman’s rights under the Hartford policy. The trial court, however, dismissed Oregon Mutual’s *Olympic Steamship* claim based on Hartford’s “bad faith tender – unclean hands” argument. According to Hartford, *Olympic Steamship* creates an “equitable exception” to the American Rule, under which each party bears its own fees and costs of litigation; consequently (the argument goes), *Olympic Steamship* claims are subject to equitable defenses, including “unclean hands.” *See CP 916-26*. As stated previously, Hartford’s argument finds no support in law or in the record, and the trial court should therefore be reversed on this issue as well. Oregon Mutual is entitled to recover all attorney fees and costs incurred in this action under *Olympic Steamship*.

J. Oregon Mutual Requests Its Fees And Expenses On Appeal Under RAP 18.1 and *Olympic Steamship*.

Lastly, should this Court reverse the trial court and find for Oregon Mutual on one or more issues, Oregon Mutual respectfully submits that it is also entitled to its attorneys’ fees and costs in this appeal under *Olympic*

Steamship and/or the CPA. See, e.g., *Panorama Village Condo. Owners Ass'n v. Allstate Ins. Co.*, 144 Wn.2d 130, 143-45, 26 P.3d 910 (2001) (awarding *Olympic Steamship* fees and costs on appeal). RAP 18.1

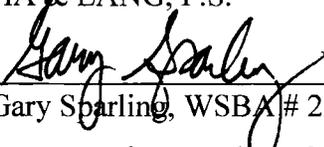
V. **CONCLUSION**

For the foregoing reasons, the trial court erred in vacating its order finding that Hartford breached its duty to defend in bad faith, and also in summarily dismissing Oregon Mutual's claims for breach of contract, bad faith, estoppel, violation of the CPA, contribution, negligence, and *Olympic Steamship* attorney fees.

Oregon Mutual, therefore, requests this Court to find that Hartford breached its duty to defend Wellman in the *Buchholz* and *State Farm* suits, that Hartford's refusal to defend was in bad faith, that Hartford is estopped to deny coverage, that Hartford violated the CPA, that Oregon Mutual is entitled to contribution, that Hartford was negligent, and that Oregon Mutual is entitled its attorney fees and costs under *Olympic Steamship* and RAP 18.1

RESPECTFULLY SUBMITTED this 13th day of July, 2011.

SOHA & LANG, P.S.

By: 

Gary Sparling, WSBA # 23208

Attorneys for Appellant Oregon
Mutual Insurance Company

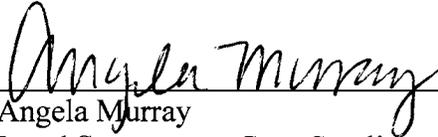
DECLARATION OF SERVICE

I am employed in the County of King, State of Washington. I am over the age of 18 and not a party to the within action; my business address is SOHA & LANG, PS, 1325 Fourth Avenue, Suite 2000, Seattle, WA 98101.

On July 13, 2011, I had served a true and correct copy of Brief of Appellant (**with attached Declaration of Service**) on parties in this action as indicated:

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Dated this 13th day of July, 2011



Angela Murray
Legal Secretary to Gary Sparling