95604-9

Court of Appeals Cause No. 75674-5-I

IN THE SUPREME COURT
OF THE STATE OF WASHINGTON

NATIONAL SURETY CORPORATION,

Plaintiff/Respondent,

v.

IMMUNEX CORPORATION,

Defendant/Appellant.

PETITION FOR REVIEW

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I. IDENTITY OF PETITIONER

Petitioner Immunex Corporation asks this Court to accept review of the decision designated in Part II of this Petition.

II. CITATION TO COURT OF APPEALS DECISION

Immunex seeks review of a decision of the Court of Appeals, Division I, filed January 29, 2018. A copy of the decision is attached as Appendix A.

III. ISSUES PRESENTED FOR REVIEW

1. Where National Surety Corporation ("NSC") accepted Immunex's tender of underlying lawsuits and agreed to defend under reservation of rights, but refused to actually defend or pay any defense costs, did the Court of Appeals err in holding that NSC was immune from all liability for extracontractual claims as a matter of law?

2. Did the Court of Appeals err in excluding from trial evidence of NSC's contractual and common-law duties to Immunex, as well as evidence that NSC violated those duties?

IV. STATEMENT OF THE CASE

A. Immunex purchased liability insurance policies from NSC.

NSC issued annual insurance policies (the "NSC Policies") to Immunex covering the periods September 1, 1998 through September 1, 2002. Under the relevant policy terms, NSC agreed to "pay on behalf of

… [Immunex] those sums that [Immunex] … becomes legally obligated to pay as damages because of," *inter alia*, "Discrimination (unless insurance thereof is prohibited by law)." "Discrimination" is not defined in the NSC Policies. *E.g.*, TE 6, pp. NSC 002687-92.

B. NSC has duties to investigate, defend and indemnify.

The NSC Policies impose two separate and distinct duties on NSC: the duty to defend and the duty to indemnify. Under the duty to indemnify, NSC must pay any covered liability Immunex may incur to a third-party claimant. The duty to defend, by contrast, gives NSC "the right and duty to investigate any claim, or defend any Insured against any Suit, seeking damages … [t]o which [coverage] applies … even if the allegations are groundless, false or fraudulent."

In addition to its duties to defend and indemnify, Washington law imposes on NSC a duty to investigate claims asserted against Immunex. *See, e.g.*, WAC 284-30-330(3), (5) (defining as unfair claims settlement practice "[f]ailing to adept and implement reasonable standards for the prompt investigation of claims under insurance policies"; and "[f]ailing to affirm or deny coverage of claims within a reasonable time after fully completed proof of loss documentation has been submitted."). The NSC Policies also explicitly impose this duty, providing that the insurer "will have the right and duty to investigate any claim, or defend any Insured

against any Suit, seeking damages … [t]o which [coverage] applies …, [e]ven if the allegations are groundless, false or fraudulent[] . . . ." TE 10, pp. NSC 002727-28.

C. NSC's duty to defend Immunex against the AWP Litigation.

This litigation concerns NSC's duty to defend Immunex against a group of lawsuits known as the "AWP Litigation." The first AWP suit naming Immunex was filed in 2001. The AWP Litigation was brought by purchasers of prescription drugs, such as health insurers and government entities, against various pharmaceutical companies, and eventually consisted of over 20 individual suits. Although the theories of liability were complex, their gravamen was that a benchmark price published by the manufacturers, known as average wholesale price ("AWP"), was misleading. Immunex vigorously opposed the claims.

D. The parties dispute when Immunex tendered the AWP Litigation to NSC.

It is undisputed that in October 2006 Immunex tendered several AWP complaints to NSC. Whether Immunex had earlier tendered the AWP Litigation was contested at trial. Immunex contended that it tendered the first AWP case in January 2002, thus triggering NSC's duty to defend. *E.g.*, Tr. 472:14-473:22; CP 3105-06. NSC claimed the January 2002 communication was merely a "notice," and that Immunex did clearly request a defense until the undisputed October 2006 tender.

E. NSC agreed to defend under reservation of rights, but never defended Immunex or paid any defense costs.

On March 9, 2007, after NSC had repeatedly failed to render a coverage determination, Immunex's coverage counsel explained to NSC that the AWP Litigation included allegations of price discrimination that were sufficient to trigger NSC's duty to defend. NSC made no substantive response until, over a year later, on March 28, 2008, it sued Immunex in King County Superior Court, seeking a declaration that the AWP Litigation was not covered. CP 1.

Three days later (and nearly 20 months after the October 2006 tender and while the AWP Litigation was still ongoing), NSC agreed to defend Immunex under reservation of rights. TE 95. The reservation-of-rights letter stated that NSC was agreeing to provide Immunex with a defense "to be sure to protect Immunex's interests while it [NSC] pursued its investigation." *Id.* p. 9.

Despite its promise to do so, NSC never defended Immunex. It never appointed or tried to appoint defense counsel and it never paid or tried to pay Immunex's defense costs or even, assuming NSC believed them too high, whatever portion NSC considered reasonable.

F. History of this litigation.

1. The 2009 trial court proceedings and the first appeal.

On April 14, 2009, the trial court ruled that the allegations in the AWP Litigation did not constitute "discrimination" within the meaning of the NSC Policies, and NSC therefore had no duty to defend. CP 1124-26. Immunex and NSC each then filed cross-motions for summary judgment regarding NSC's obligation to pay defense costs incurred prior to the April 14, 2009 Order. On August 25, 2009, the trial court ordered as follows: "National Surety must pay all reasonable defense fees and costs incurred by Immunex in the AWP Litigation through April 14, 2009, the date the Court granted [National Surety's] duty to defend motion, unless [National Surety] prevails on its late notice claim at trial." CP 1408-10. The Court of Appeals affirmed both rulings. *Nat'l Sur. Corp. v. Immunex Corp*., 162 Wn. App. 762, 779, 256 P.3d 439 (2011).

In *National Sur. Corp. v. Immunex Corp*., 176 Wn.2d 872, 297 P.3d 688 (2013), this Court affirmed, rejecting NSC's argument that the trial court's ruling of no indemnity coverage relieved the insurer from liability for pre-April 14, 2009 defense costs. Specifically, this Court affirmed the rulings below that: (1) because the AWP Litigation was conceivably within the Policies' coverage, NSC's defense obligation had attached and would remain so unless and until the trial court resolved the

uncertainty in NCS's favor; (2) Washington insurers remain liable for defense costs incurred between the time the duty to defend attaches and a judicial determination of no coverage; (3) therefore, NSC was obligated to pay Immunex's defense costs unless and to the extent the insurer could prove it was "actually and substantially prejudiced" by the timing of notice or tender of the AWP Litigation. *Id.* at 890-91. The Court remanded the case for determination of that issue.

2. The case on remand.

On remand, NSC contended that it was prejudiced by the timing of Immunex's notice, and that Immunex's defense costs were unreasonable in amount. Immunex argued that it had not merely notified NSC of the AWP Litigation in January 2002, but in fact had tendered the first AWP case at that time. *E.g.*, Tr. 472:14-473:22; CP 3105-06. Immunex also argued that even if NSC was right that the January 2002 communication was only a notice, it was sufficient to trigger NSC's duty to investigate, including at least by clarifying whether a defense was being sought. Immunex argued that if NSC had investigated, it would have learned all of the information the insurer later claimed it needed. Immunex thus contended that, instead of being prejudiced by the timing of tender, NSC in fact was prejudiced by its own lack of action and failure to honor its

duty to investigate. Immunex also contended that the defense costs it sought were reasonable in amount.

On remand, Immunex for the first time asserted counterclaims based upon NSC's wrongful failure to defend. CP 1535-46. Immunex argued that NSC's failure to pay defense costs—including after expressly promising to do so in its March 2008 acceptance of Immunex's tender and reservation-of-rights letter—gave rise to breach of contract and extracontractual liability under the common law of bad faith and the Washington IFCA and CPA. *Id.*

3. The trial court entered summary judgment against Immunex on its claims for extracontractual liability.

In its Motion for Partial Summary Judgment (the "SJ Motion"), NSC argued it could not be held liable on Immunex's extracontractual claims, or for breach of contract, because it had accepted Immunex's tender and agreed to defend it against the AWP Litigation under reservation of rights. CP 2071-73, 2076-77. Specifically, NSC argued that this Court's 2011 opinion meant that the March 2008 reservation-of-rights letter insulated the insurer from any liability, whether contractual or extracontractual, for wrongfully failing to defend, despite the fact that NSC admittedly never defended Immunex or paid defense costs. *Id.* Immunex opposed the motion, arguing that while Washington law does

afford liability insurers substantial protection when they choose to defend their insureds under reservation of rights, that protection is available only when the insurer *actually defends* the insured—not when the insurer promises to but fails to do so. CP 3113-15.

The trial court granted the SJ Motion, dismissing Immunex's counterclaims from the case. CP 3521-22. Thereafter, two issues were tried to a jury: (1) whether and to what extent NSC could show prejudice from the timing of Immunex's notice or tender of the AWP Litigation; and (2) whether the defense costs claimed by Immunex were reasonable in amount.

4. At trial, the court excluded evidence of NSC's own duties and standards.

The trial court disallowed Immunex from presenting to the jury evidence or argument that NSC violated its duties to its insured, and even that NSC had duties toward Immunex at all. CP 3243. The trial court's rationale was that its dismissal of Immunex's counterclaims made NSC's duties, and non-compliance with them, irrelevant. CP 3955. The court enforced this same reasoning throughout trial, continuing to exclude evidence of NSC's duties on the basis of the court's prior ruling with respect to Immunex's counterclaims. *See, e.g.*, Tr. 128:2-11; Tr. 129:15-17; Tr. 131:12-14; Tr. 132:1-8.

5. The jury found NSC had an obligation to pay defense costs, and the Court of Appeals affirmed.

On May 26, 2016, the jury found that NSC had an obligation to pay defense costs to Immunex. On the basis of the evidence before it, the jury also found that NSC had been prejudiced by the timing of the notice, tender, or both, and awarded Immunex $670,000, far less the full amount of the defense costs Immunex sought. CP 4460.

On January 29, 2018 the Court of Appeals, Division I, affirmed in an unpublished opinion.

V. ARGUMENT

A. The decision below is contrary to Washington's well-established duty-to-defend law.

1. This Court's opinions incentivize insurers to defend under reservation of rights when there is any doubt whether coverage exists.

The decisions below conflict with the two exclusive options that this Court has established for an insurer facing a policyholder's request for a defense, where the insurer believes it may have meritorious coverage defenses. Recognizing the importance of the duty to defend and the ease with which it is triggered—"[t]he duty [to defend] is one of the main benefits of the insurance contract[,] and "[o]nce the duty to defend attaches, insurers may not desert policyholders and allow them to incur substantial legal costs while waiting for an indemnity determination."

Truck Ins. Exchange v. VanPort Homes, Inc., 147 Wn.2d 751, 761, 58 P.3d 276 (2002)—the options incentivize insurers to err in favor of providing a defense:

First, the insurer may conclude that the claims against its insured are not even "conceivably" covered and, consequently, there is no duty to defend. In this situation, the insurer can simply deny coverage by refusing to defend its policyholder. But this decision is not free of risk. If the denial is later held to have been in error, the insurer is exposed to liability not only for contract damages—the costs of defending the lawsuit plus prejudgment interest—but also the full range of extracontractual remedies: coverage by estoppel;[1] exemplary damages;[2] attorney fee liability;[3] consequential damages;[4] and emotional distress damages.[5] All these remedies are available because the insurer wrongly left the insured to fend for itself. *C.f. VanPort Homes*, 147 Wn.2d at 761 ("Once the duty to defend attaches, insurers may not desert policyholders and allow them to

[1] *VanPort Homes*, 147 Wn.2d at 759-60; *Mut. of Enumclaw Ins. Co. v. Dan Paulson Constr., Inc*. 161 Wn.2d 903, 919, 169 P.3d 1 (2007).
[2] RCW 48.30.015(2); 19.86.090.
[3] *Id.*; *see also Olympic Steamship Co. v. Centennial Ins. Co*., 117 Wn.2d 37, 53, 811 P.2d 673 (1991).
[4] *Coventry Assocs. v. Am. States Ins. Co.,* 136 Wn.2d 269, 284, 961 P.2d 933 (1998).
[5] *Woo v. Fireman's Fund Ins. Co.*, 161 Wn.2d 43, 70, 164 P.3d 454 (2007).

incur substantial legal costs while waiting for an indemnity determination.").

On the other hand, this course of action may benefit the insurer. The insured may not challenge the denial, or the insurer may successfully establish that the duty to defend never attached. In either scenario, the insurer will have avoided paying any defense costs.

Second, "[w]hen an insurer is uncertain of its duty to defend, it may defend under a reservation of rights while seeking a declaratory judgment relieving it of its duty." *Immunex*, 176 Wn.2d at 879; *citing Woo*, 161 Wn.2d at 54. When an insurer agrees to defend under reservation, its duty to do so continues unless and until the insurer obtains a judicial determination that no indemnity coverage exists; then, the insurer will be liable for pre-determination defense costs even if the court finds that no indemnity coverage exists. *Immunex*, 176 Wn.2d at 887-88.

Although defending under a reservation can thus present a significant cost to the insurer, which "must pay defense costs until it obtains a judicial declaration that it owes no duty to defend," *Id.* at 891, the insurer "unquestionably benefits from its decision to defend under a reservation of rights—even where, as here, a court later finds that it owes no duty to continue that defense." *Id*. at 880. This is because "[a]lthough the insurer must bear the expense of defending the insured, by doing so

under a reservation of rights and seeking a declaratory judgment, the insurer avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach …." *Id.* at 880, *quoting Woo*, 161 Wn.2d at 54.

Just like the decision to refuse a defense altogether, the decision to defend under a reservation of rights presents the insurer with a tradeoff: the insurer "makes a rational decision to protect itself against a greater downstream risk [breach and extracontractual liability] by undertaking certain costs [of defending its insured]." *Id*.

2. To receive the protections afforded by defending under a reservation of rights, the insurer must *actually defend*.

This Court has made clear that an insurer receives the protections that flow from defending under a reservation of rights only if the insurer ***actually defends***; the mere reservation of rights and unfulfilled promise to defend is not enough. Indeed, in this very case, this Court repeatedly emphasized the tradeoff inherent in an insurer's decision to defend under a reservation:

> We have recognized that the risks of a reservation of rights defense are coupled with benefits:
>
> Although ***the insurer must bear the expense of defending the insured***, by doing so under a reservation of rights and seeking a declaratory judgment, the insurer avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach.
> …

> When an insurer ***defends*** under a reservation of rights, it insulates itself from potential claims of breach and bad faith, which can lead to significant damages, including coverage by estoppel. ***In turn, the insured receives the benefit of a defense*** until a court declares none is owed. Conversely, ***when an insurer declines to defend*** altogether, ***it saves money on legal fees but assumes the risk it may have breached its duty to defend or committed bad faith.***

Immunex, 176 Wn.2d at 880, 884-85, 887 (emphasis added; internal citations omitted). In this Court's own words, an insurer "cannot claim the benefits of [a reservation of rights defense] and simultaneously avoid the costs." *Id*.; *see also Woo*, 161 Wn.2d 43, 164 P.3d 454 (2007) ("[a]lthough the insurer must bear the expense of defending the insured, by doing so under a reservation of rights and seeking a declaratory judgment, the insurer avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach." (internal quotations and citations omitted)); *Kirk v. Mt. Airy Ins. Co.* 134 Wn.2d 558 n.3, 951 P.2d 1124 (1998) ("If the insurer is unsure of its obligation to defend in a given instance, it may defend under a reservation of rights while seeking a declaratory judgment that it has no duty to defend.").

This rationale is consistent with this Court's previous observation, also in this case, "that, under a reservation of rights defense, 'the insured *receives* the defense promised'—at least until the determination of

noncoverage." *Immunex*, 176 Wn.2d at 885-86 (quoting *Kirk*, 134 Wn.2d at 563 n. 3) (emphasis in original). This Court also has expressly interpreted *Woo* as making clear that a reservation of rights defense is a "real" defense, and not simply an illusory benefit: "If there were any question after *Kirk* and *Truck Insurance* that a reservation of rights defense must be a real defense, there is no question after *Woo* that "the insurer must bear the expense of defending the insured." *Immunex*, 176 Wn.2d 886; a*ccord, Am. Best Food, Inc. v. Alea London, Ltd.*, 168 Wn.2d 398, 405, 229 P.3d 693, 696 (2010) ("A reservation of rights is a means by which the insurer avoids breaching its duty to defend while seeking to avoid waiver and estoppel. When that course of action is taken, ***the insured receives the defense promised*** and, if coverage is found not to exist, the insurer will not be obligated to pay [further defense costs or indemnity coverage]." (emphasis added)).

B. The Court of Appeals' opinion cannot be reconciled with Washington law, including this Court's prior opinions in *Woo* and this case.

NSC sought and obtained summary judgment on Immunex's claims, arguing it was immunized against breach-of-contract and extracontractual liability, as a matter of law, because NSC had promised to defend Immunex under reservation of rights. Immunex countered that such immunity does not attach as a matter of law, and that the irrationality,

and incongruence with Washington law, of such a rule was illustrated particularly well by this case, where NSC took no action in furtherance of its promise to defend (*e.g.*, no attempt to appoint counsel, or to determine what amount of defense fees the insurer believed would have been reasonable, let alone compensate Immunex for any undisputed amounts).

The Court of Appeals rejected Immunex's argument and affirmed the superior court's grant of the SJ Motion. The crux of the Court of Appeals' reasoning, and its error, is set forth in the following passage:

> To grant the relief Immunex requests and reinstate its breach of contract and extra-contractual claims would require us to graft an exception onto the rule in Woo: an insurer defending under reservation of rights "avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach" unless it does not pay defense costs pending any determination of reasonableness. 161 Wn.2d at 54. The trial court properly dismissed Immunex's claims for bad faith, breach of contract, and IFCA and CPA violations.

Appendix A, p. 7 (emphasis in original).

The Court of Appeals held that in order to rule for Immunex, it would have to graft an exception onto the rule in *Woo*, namely that extracontractual immunity attaches ***unless*** the insurer does not pay on grounds that there is an unresolved dispute over the reasonableness of the defense costs at issue. But such an "exception" would only make sense, and would only be an "exception" to *Woo*, if the already-existing rule is

that there are some circumstances under which an insurer gets immunity from extracontractual liability ***without actually defending***. The concept of adding an "exception" so that one category of insurers that issue a reservation of rights letter but do not defend (namely insurers who do not pay pending a determination of reasonableness)—lose the immunity" depends on the proposition that a promise to defend, without actually defending, otherwise ***does*** confer immunity from extracontractual claims.

Stated differently, the Court of Appeals declined to remove extracontractual liability from a group of insurers that, under *Woo*, lacked such immunity in the first place. As demonstrated in the above discussions of the body of law this Court has developed, including in this very case, the notion that immunity from extracontractual liability is conferred on insurers that do not actually defend is made up out of whole cloth. In the words of this Court:

> We reject National Surety's view that an insurer can have the best of both options: protection from claims of bad faith or breach without any responsibility for the costs of defense if a court later determines there is no duty to defend. "This 'all reward, no risk' proposition renders the defense portion of a reservation of rights defense illusory. The insured receives no greater benefit than if its insurer had refused to defend outright.

Immunex, 176 Wn.2d at 885.

An insurer therefore cannot have the "best of both options"—protecting itself from extracontractual liability while simultaneously not defending its insured. But that is precisely what NSC obtained here: the best of both options.

To be sure, Immunex is not arguing that an insurer that does not pay or defend pending a determination of reasonableness is in breach of its duty to defend ***as a matter of law***. Had the trial court on remand allowed Immunex to try its counterclaims to the jury, NSC could have made its case as to why its actions were reasonable and in good faith. NSC could have argued it was prevented from making an informed judgment about the reasonableness of Immunex's defense costs, that it was prevented from action by Immunex's late tender, or any other manner of argument. Similarly and in future cases, an insurer that attempts to defend its insured (but is for some reason unsuccessful) or pays some undisputed portion of costs, can introduce that evidence as to why extracontractual liability should not attach. But when it affirmed, and interpreted *Woo* as embodying a rule that confers matter-of-law or *per se* immunity upon insurers that promise to defend but do not (and, separately, when it declined to create an exception to that rule for this case), the Court of Appeals not only foreclosed this possibility, it weakened *Woo* itself.

C. The trial court's ruling, if upheld, would radically alter the very nature of the duty to defend.

Even beyond its contravention of well-established insurance law, the lower courts' approach cannot be allowed to stand because it would fundamentally alter the deliberately-designed balance of risk inherent in the insurance contract itself. An insurer would need only to issue a reservation-of-rights letter in order to insulate itself from breach of contract and extracontractual claims. In any case involving a non-frivolous dispute, including over reasonableness of defense costs, no rational insurer would actually pay defense costs on an ongoing basis, *i.e.*, while the underlying case is ongoing. Instead, insurers would have every incentive to take a "wait and see, and (perhaps) reimburse" approach: send a reservation-of-rights letter; let the insured fend for itself in the underlying lawsuit; hope that coverage litigation results in a finding of no coverage; and then challenge the reasonableness of defense costs. As demonstrated above, this is not the law of Washington, and it would eviscerate the duty to defend—one of the main benefits of the insurance contract[6]—in our state.

[6] *VanPort Homes*, 147 Wn.2d at 76.

D. The courts below erred by excluding evidence of NSC's duties.

If Immunex's counterclaims are reinstated, evidence of NSC's duties must be admitted at trial thereof, because whether and to what extent NSC owed and breached duties to Immunex are elements of Immunex's breach of contract and extracontractual claims. *See Baldwin v. Silver*, 165 Wn. App. 463, 473, 269 P.3d 284, 289 (2011); *Salas v. Hi-Tech Erectors*, 168 Wn.2d 664, 669, 230 P.3d 583, 585 (threshold to admit relevant evidence is low).

But the excluded evidence was relevant to NSC's claim of prejudice, and the trial court thus also erred in excluding it from the case that was tried. The jury was asked to determine what prejudice NSC suffered, but it was only allowed to hear evidence about prejudice caused by Immunex, not NSC itself. Had the jury known NSC was under a duty to act but did not, it could have determined any prejudice was caused in whole or in part by NSC, as opposed to Immunex alone. This would have affected the size of the damage award, which represented the amount of fees Immunex was entitled to, taking into account the prejudice suffered by NSC.

VI. CONCLUSION

The decisions below misapply, and would fundamentally change, Washington law governing the insurer's duty to defend. The decision

meets the criteria established by RAP 13.4(b)(1) and (4), and the Court should grant discretionary review.

DATED this 28th day of February, 2018.

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DECLARATION OF SERVICE

The undersigned declares under penalty of perjury under the laws of the State of Washington that on the below date, I caused a true and correct copy of this document to be delivered, via the method indicated, to counsel of record:

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DATED this 28th day of February, 2018, at Seattle, Washington.

Carol Hudson, Legal Assistant
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APPENDIX A

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

NATIONAL SURETY CORPORATION, Respondent, v. IMMUNEX CORPORATION, Appellant.	)	No. 75674-5-I DIVISION ONE UNPUBLISHED OPINION FILED: January 29, 2018

APPELWICK, J. — At issue is the amount of defense costs for which Immunex is entitled to be reimbursed. Immunex argues that the trial court, on remand, erred in dismissing its counterclaims on summary judgment, and it erred in excluding evidence regarding National Surety's duty to investigate its claims. We affirm.

FACTS

National Surety Corporation insured Immunex Corporation. The policy periods at issue are September 1, 1998 to September 1, 2002. On October 3, 2006, Immunex sent a letter to National Surety explicitly requesting coverage for a number of lawsuits filed on or after November 27, 2001, all alleging unlawful practices in its average wholesale pricing (AWP) of drugs. On December 14, 2006, National Surety denied coverage, and asked Immunex to provide any additional information that might change that coverage decision. On March 9, 2007, Immunex responded, arguing that the AWP claims were covered by its policy.

On March 31, 2008, after further correspondence, National Surety agreed to defend under a reservation of rights. While denying coverage, it agreed to defend "until such time as it can obtain a court determination confirming its coverage decision [and] reserves the right to recoup the amounts paid in defense if it is determined by a court that there is no coverage or duty to defend and that [it] is entitled to reimbursement." It concurrently filed for declaratory relief stating that the AWP litigation was not covered.

On April 15, 2009, the trial court granted National Surety this requested declaratory relief. However, the trial court denied National Surety's summary judgment motion to be relieved from paying any of Immunex's defense fees and costs. And, the trial court granted Immunex's partial summary judgment motion, finding that unless National Surety could prove prejudice from late notice at trial, it could be obligated to pay defense costs until the date the court confirmed the claims were not covered. The trial court then entered partial final judgment pursuant to CR 54(b) in order to permit appeal.

Immunex appealed and National Surety cross-appealed. This court affirmed. Nat'l Sur. Corp. v. Immunex Corp., 162 Wn. App. 762, 782, 256 P.3d 439 (2011). National Surety petitioned for review. The Supreme Court also affirmed and remanded to the trial court for determination of the defense fees and costs owed by National Surety. Nat'l Sur. Corp. v. Immunex Corp., 176 Wn.2d 872, 891, 297 P.3d 688 (2013).

On remand, Immunex brought counterclaims for breach of contract, bad faith, violation of the Consumer Protection Act[1] (CPA), and violation of the Insurance Fair Conduct Act[2] (IFCA). National Surety moved for partial summary judgment on these counterclaims. The trial court granted the motion. The only issue remaining, the extent that National Surety was prejudiced by any delay in Immunex tendering its claim, proceeded to trial. Immunex sought reimbursement for fees and costs in excess of $15,400,000. The jury found that National Surety was prejudiced, and granted judgment in the amount of $670,000. Immunex appeals.

DISCUSSION

Immunex alleges two errors. First, it argues that the trial court erred in granting summary judgment on its contractual and extracontractual claims. Second, it argues that, the trial court erred in excluding evidence regarding National Surety's duty to investigate.

I. Summary Judgment on Immunex's Claims

When reviewing a summary judgment order, this court engages in the same inquiry as the trial court. Hertog v. City of Seattle, 138 Wn.2d 265, 275, 979 P.2d 400 (1999). Summary judgment is proper when there are no genuine issues of material fact, and the moving party is entitled to judgment as a matter of law. Id. All facts and reasonable inferences are considered in the light most favorable to the nonmoving party. Id. Questions of law are reviewed de novo. Id.

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[1] Ch. 19.86 RCW.
[2] RCW 48.30.010-.015.

Immunex asserted a breach of contract counterclaim based upon National Surety's failure to defend. In addition, it asserted counterclaims for extracontractual liability under common law bad faith and the Washington IFCA and CPA based on National Surety's failure to pay defense costs. Immunex argues that National Surety never in fact defended it in the underlying action, and therefore cannot claim this safe harbor.[3]

"An insurer has a duty to defend 'when a complaint against the insured, construed liberally, alleges facts which could, if proven, impose liability upon the insured within the policy's coverage.' An insurer is not relieved of its duty to defend unless the claim alleged in the complaint is 'clearly not covered by the policy.' " Woo v. Fireman's Fund Ins. Co., 161 Wn.2d 43, 52-53, 164 P.3d 454 (2007) (citation omitted) (quoting Truck Ins. Exch. v. VanPort Homes, Inc., 147 Wn.2d 751, 760, 58 P.3d 276 (2002)).

"If the insurer is uncertain of its duty to defend, it may defend under a reservation of rights and seek a declaratory judgment that it has no duty to defend. Although the insurer must bear the expense of defending the insured, by doing so under a reservation of rights and seeking a declaratory judgment, the insurer avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach." Id. at 54 (citation omitted).

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[3] "To fulfill its duty to defend, an insurer generally has the right to select the defense counsel who will represent its insured." Kruger-Willis v. Hoffenburg, 198 Wn. App. 408, 416, 393 P.3d 844, 848 (2017), review denied, 189 Wn.2d 1010, 402 P.3d 818 (2017). Alternatively, "[t]he duty to defend can be enforced by requiring the insurer to reimburse the insured for its costs in defending against the claim." Waite v. Aetna Cas. & Sur. Co., 77 Wn.2d 850, 858, 476 P.2d 847 (1970). Here, Immunex sought reimbursement of its defense costs incurred in the litigation.

"In Truck Insurance, we described a reservation of rights defense while seeking a declaratory judgment as 'a means by which the insurer avoids breaching its duty to defend while seeking to avoid waiver and estoppel.' [W]e then observed that '[w]hen that course of action is taken, the insured receives the defense promised and, if coverage is found not to exist, the insurer will not be obligated to pay.' National Surety relies on ambiguity in the phrase 'will not be obligated to pay' as supporting its contention that an insurer need not pay for defense costs incurred before a court determination of no coverage." Immunex, 176 Wn.2d at 885 (second alteration in original) (citations omitted) (internal quotation marks omitted) (quoting Truck Ins., 147 Wn.2d at 761).

"Taken in context, the language in Kirk[v. Mt. Airy Ins. Co., 134 Wn.2d 558, 563, 951 P.2d 1124 (1998)] and Truck Insurance does not support National Surety's view. After obtaining a declaration of noncoverage, an insurer 'will not be obligated to pay' from that point forward. Any other rule would be at odds with our observation that, under a reservation of rights defense, 'the insured receives the defense promised'—at least until the determination of noncoverage. Kirk, 134 W.2d at 563 n.3 (emphasis added). If there were any question after Kirk and Truck Insurance that a reservation of rights defense must be a real defense, there is no question after Woo that 'the insurer must bear the expense of defending the insured.' Woo, 161 W.2d at 54, 164 P.3d 454." Immunex, 176 Wn.2d at 885-86.

"We hold that insurers may not seek to recoup defense costs incurred under a reservation of rights defense while the insurer's duty to defend is uncertain. Accordingly, National Surety may be held responsible for the reasonable defense

costs incurred by its insured until the trial court determined National Surety had no duty to defend." Id. at 887-88 (footnote omitted).

National Surety argued to the trial court on remand that language in our prior opinion required dismissal of Immunex's counterclaims: "Although here National Surety has not yet taken on the actual defense of Immunex, National Surety had the benefit of insulating itself from a bad faith claim and possible coverage by estoppel." Immunex, 162 Wn. App. at 778. Whether National Surety could be liable for breach of contract or extra-contractual relief for failure to timely pay defense costs was not a question squarely before the court. This statement was merely a straightforward application of Woo. Both the Court of Appeals and the Supreme Court were clearly aware that payment had not been made at the time of the appeal.[4] Neither hinted that this fact had any impact on the application of Woo relative to the defense under reservation of rights. Neither court hinted that the issues in Immunex's counterclaims were alive on remand.

This is not surprising. By defending under a reservation of rights, National Surety assumed as a matter of law the obligation to pay reasonable defense costs. The only question was how much was reasonable; the only duty was to pay. Immunex asserted a counter claim for more than $15 million dollars. National

[4] "National Surety may be held responsible for the reasonable defense costs incurred by its insured until the trial court determined National Surety had no duty to defend." Immunex, 176 Wn.2d at 887-88. In a footnote to that sentence it added, "It makes no difference that National Surety never actually paid any defense costs before the declaration of noncoverage on April 14, 2009. We agree with the Court of Appeals that this fact 'cannot support a different result here than in a case where the insurer had already provided a defense.' " Immunex, 176 Wn.2d at 888 n.3 (quoting Immunex, 162 Wn. App. at 777).

Surety asserted it owed nothing. It had a right to ask the court to determine the reasonableness of the fees and costs sought. The first appeal addressed whether the obligation was extinguished by reservation of a right of recoupment in the reservation of rights letter. That claim was rejected, but the court stated, "We recognize, however, that an insurer may avoid or minimize its responsibility for defense costs when an insured belatedly tenders a claim and the insurer demonstrates actual and substantial prejudice." Immunex, 176 Wn.2d at 875. The case was remanded to the trial court to determine factually if, and to what extent, the late tender of defense by Immunex prejudiced National Surety with respect to defense costs. Id. at 890-91. Until the reasonableness of the defense costs was resolved by the jury and reduced to judgment, tender of payment in this case was not required.

Immunex contends that if the trial court's ruling is allowed to stand, it would result in a "foundational shift in Washington insurance law," because insurers can insulate themselves from bad faith liability by issuing a reservation of rights. To grant the relief Immunex requests and reinstate its breach of contract and extra-contractual claims would require us to graft an exception onto the rule in Woo: an insurer defending under reservation of rights "avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach" unless it does not pay defense costs pending any determination of reasonableness. 161 Wn.2d at 54. The trial court properly dismissed Immunex's claims for bad faith, breach of contract, and IFCA and CPA violations.

II. Evidentiary Decision

Immunex contends that the trial court erred by excluding evidence of National Surety's claim handling. This court reviews a trial court's evidentiary decision for abuse of discretion. City of Spokane v. Neff, 152 Wn.2d 85, 91, 93 P.3d 158 (2004). A trial court abuses its discretion if its decision is manifestly unreasonable or based on untenable grounds or untenable reasons. In re Marriage of Littlefield, 133 Wn.2d 39, 46-47, 940 P.2d 1362 (1997).

The trial court specifically excluded evidence of National Surety's duties, but allowed evidence of National Surety's conduct:

> NSC's [National Surety Corporation] motion to preclude Immunex from presenting evidence of NSC's alleged bad faith, or damages other than defense costs incurred during the AWP litigation, is GRANTED IN PART AND DENIED PART. There are no surviving claims of breach, bad faith, waiver, or coverage by estoppel against NSC. Therefore, evidence about NSC's legal duties are not relevant. Immunex is correct, however, when it says, "fairness demands that Immunex be permitted to introduce evidence of what NSC in fact did in the months and years following receipt of notice of the AWP lawsuits." NSC claims it would have acted differently had it received certain information earlier. Immunex may therefore counter that assertion with evidence demonstrating whether and how NSC acted on information it did receive. Immunex is incorrect when it says, "fairness likewise demands that Immunex be permitted to present the jury with evidence concerning the insurer's duty to investigate the AWP lawsuits and render a coverage determination." Evidence of an insurer's duty to investigate or render a coverage determination is not relevant to the issues for trial, and is ORDERED excluded. Immunex agrees that its claim for damages at trial is limited to the costs it incurred in defending against the AWP litigation; NSC's motion to exclude evidence of other damages is granted.

We agree that evidence regarding breach of duty to investigate was not relevant. Whether a duty was breached did not bear on the question of prejudice suffered due to late tender. The only issues remaining for trial were: (1) when

should Immunex have tendered its claim and (2) if it had tendered its claim properly, what costs would National Surety have incurred?

"To establish actual prejudice resulting from delayed notice, an insurer must adduce affirmative proof of an advantage lost or disadvantage suffered as a result of the delay, which has an identifiable detrimental effect on the insurer's ability to evaluate or present its defenses to coverage or liability." Canron, Inc. v. Fed. Ins. Co., 82 Wn. App. 480, 491-92, 918 P.2d 937 (1996). Immunex argues that the evidentiary decision left the jury with "unbalanced evidence." But, nothing in the trial court's order limited Immunex's ability to present evidence of the extent of National Surety's opportunity to investigate the claims after it first was notified of the lawsuits. Evidence about what National Surety did and when remained admissible. Evidence about what National Surety could have done to reduce its losses, but did not do, remained admissible.

And, the jury heard evidence of what National Surety should have been doing to avoid suffering prejudice. Immunex presented testimony from two experts on how National Surety should have acted. When asked, "what was supposed to be included in the investigation," one expert testified at length about what National Surety's obligations were: "These are national standards. They will apply to virtually every state in the union in terms of what the industry standard is for the investigation of the claims." (Emphasis added.) Another expert testified that, upon tender, National Surety had "certain obligations that they need to comply with that include evaluating the complaint itself, doing a preliminary investigation, so that they can come to an understanding as to what this claim is about." National Surety

did not object to either of these experts' statements about the existence and nature of the duty to investigate. The jury was able to factor this evidence about claim handling into its decision about the amount of prejudice suffered. The trial court's evidentiary decision did not leave the jury with unbalanced evidence.

The trial court did not abuse its discretion in excluding evidence of duty.

We affirm.

WE CONCUR:

GORDON TILDEN THOMAS CORDELL LLP

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