

No. 71214-4-I

COURT OF APPEALS  
OF THE STATE OF WASHINGTON  
DIVISION ONE

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STATE OF WASHINGTON  
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NO BOUNDARIES, LTD., a Washington corporation, and NBL II,  
LLC, a Washington limited liability company,

Respondents/Cross-Appellants

v.

PACIFIC INDEMNITY COMPANY (a member of the CHUBB GROUP  
OF INSURANCE COMPANIES), an insurer authorized by the  
Washington Insurance Commissioner,

Appellant/Cross-Respondent

**OPENING BRIEF OF APPELLANT  
PACIFIC INDEMNITY COMPANY**

*Counsel for Appellant, Pacific Indemnity Company:*

David M. Jacobi, WSBA #13524  
John D. Wilson, Jr. WSBA #4828  
WILSON SMITH COCHRAN DICKERSON  
901 Fifth Avenue, Suite 1700  
Seattle, Washington 98164-2050  
Telephone 206.623.4100  
Facsimile 206.623.9273  
Email [jacobi@wscd.com](mailto:jacobi@wscd.com); [wilson@wscd.com](mailto:wilson@wscd.com)

ORIGINAL

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## **I. INTRODUCTION**

This is the second appeal arising out of a first-party property insurance claim that No Boundaries, Ltd. and NBL II, LLC (“NBL”) submitted to Pacific Indemnity Company (“Pacific”) in June 2005, shortly after a 60-square foot portion of the wooden flooring in the southwest corner of the Metropole Building basement collapsed as a result of moisture damage and wood decay.<sup>1</sup> In May 2007, before NBL had repaired the damage in the basement, a fire damaged the three ground floors of the Metropole. NBL submitted a new claim to Pacific, under a later insurance policy, for the extensive fire damage.

Pacific paid NBL about \$4.75 million for the fire damage and over \$750,000 for the earlier damage in the basement. In 2009, with the insurance available to cover the fire loss exhausted, NBL demanded over \$3 million in additional payments for building code upgrades as part of the collapse loss, including over \$500,000 for a commercial kitchen allegedly damaged in the collapse. Shortly after making that demand, NBL sued Pacific; asserting claims for breach of contract, bad faith, violation of the Consumer Protection Act, RCW 19.86 (“CPA”), and violation of the Insurance Fair Conduct Act, RCW 48.30.015 (“IFCA”).

As a result of its investigation and discovery in the defense of NBL’s lawsuit, Pacific learned that NBL had materially misrepresented the existence

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<sup>1</sup> The Metropole Building was originally constructed in the 1880s and is located in Pioneer Square in Seattle.

and contents of the commercial kitchen allegedly damaged in the June 2005 collapse. At that point, Pacific asserted an affirmative defense under the terms of the policy and controlling precedent, including *Mutual of Enumclaw v. Cox*.<sup>2</sup>

The jury here concluded that Pacific did not breach the insurance policy and was not required to pay for code upgrades to the Metropole Building as a result of the June 2005 collapse. Further, the jury concluded that Pacific did not violate the CPA in its investigation and adjustment of NBL's collapse damage claim.

However, the trial court improperly permitted the jury to consider the legal consequences of a finding of fraud or misrepresentation in the insurance context and denied Pacific's motion for a mistrial. The trial court also declined to instruct the jury that under *Cox*, Pacific had no duty to promptly discover, or to notify NBL that it suspected NBL had misrepresented its insurance claim.

Given its erroneous consideration of the legal consequences of NBL's misrepresentation, and the absence of an instruction that Pacific had no duty to advise NBL of its misrepresentation, the jury found that NBL had not misrepresented its claim by demanding that Pacific pay over \$500,000 for a commercial kitchen allegedly damaged in the collapse – despite compelling evidence that kitchen never existed. The jury also found, inconsistent with its determination that Pacific did not breach any contractual obligations to NBL,

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<sup>2</sup> 110 Wn.2d 643, 757 P.2d 499 (1988).

that Pacific was liable for bad faith and violation of IFCA. Given the jury's finding that Pacific paid NBL what it was due and did not breach the insurance policy, there was no proof, as required under IFCA, that Pacific had "unreasonably denied a claim for coverage or unreasonably denied a claim for payment of benefits" within the meaning of that statute.

The judgment on the jury's verdict with respect to the breach of contract and CPA claims is amply supported by substantial evidence. However, the jury's verdict and damages award for bad faith and violation of IFCA, as well as the trial court's award of attorney fees and costs, are contrary to the jury's own fact finding and the court's instructions on the law. The trial court should have granted Pacific's post-trial motion for a new trial on the misrepresentation and bad faith claims and should have corrected the plain legal error in the jury's verdict by granting judgment for Pacific under IFCA.

## **II. ASSIGNMENTS OF ERROR**

1. The trial court erred by allowing NBL to put on evidence and to argue to the jury that NBL would forfeit coverage and might later be required to return insurance benefits previously paid, if the jury found that NBL materially misrepresented its claim for insurance.<sup>3</sup>

2. The trial court erred by denying Pacific's motion for a mistrial, made on the grounds that testimony concerning the possible legal consequences of NBL's material misrepresentation prevented Pacific from obtaining a fair trial of NBL's claims and of Pacific's own affirmative defense under *Cox*.<sup>4</sup>

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<sup>3</sup> CP 1591-1594; CP 1837-1840; RP 10/1/13 at 4:22-41:16; RP 10/2/13 at 160:1-18, 174:3-8; RP 10/7/2013 at 498:7 – 499:9; RP 10/10/13 at 1203:25 – 1145:18; RP 10/10/13 at 1226:17 – 1228:3.

<sup>4</sup> RP 10/9/13 at 871:13-874:8.

3. The trial court erred by refusing to instruct the jury, consistent with *Cox*, that Pacific had no affirmative obligation to promptly discover, or to advise NBL that it suspected or discovered that NBL made a material misrepresentation in presenting its insurance claim to Pacific.<sup>5</sup>

4. The trial court erred by denying Pacific's motion to correct the jury's verdict, enter judgment for Pacific or to grant a new trial as to NBL's claims under IFCA, for common law bad faith and as to Pacific's material misrepresentation defense under *Cox*.<sup>6</sup>

5. The trial court erred by entering judgment for NBL on the jury's verdict.<sup>7</sup>

6. The trial court erred by awarding attorney fees and costs to NBL under *Olympic S.S. Co. v. Centennial Ins. Co.*<sup>8</sup> and under IFCA.<sup>9</sup>

### **III. ISSUES PERTAINING TO ASSIGNMENTS OF ERROR**

1. Under IFCA, and the trial court's instructions to the jury, NBL was required to prove that Pacific "unreasonably denied a claim for coverage or unreasonably denied a claim for payment of benefits." Did the trial court err, as a matter of law, by declining to correct the verdict or to grant judgment for Pacific as to NBL's IFCA claim, because the evidence proved, and the jury found, that Pacific did not deny a claim for coverage or deny a claim for payment of benefits that were due under the contract of insurance between Pacific and NBL? (Assignments of Error Nos. 4 & 5).

2. In *Cox*, our Supreme Court held that an insurer has no affirmative obligation to inform an insured that it believes he has concealed or misrepresented facts in presenting a claim for payment of insurance benefits; and does not waive or forfeit its right to assert a defense of material misrepresentation under *Cox* by paying a portion of the insured's claim. Did the trial court commit a reversible error of law by refusing to give the jury Pacific's proposed *Cox* instruction, thereby allowing NBL to argue that Pacific acted in bad faith and violated IFCA by asserting material

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<sup>5</sup> CP 1842; CP 2005-2008; RP 10/10/13 at 1203:2-24.

<sup>6</sup> CP 2079-2113, 2582-2590 and CP 2700-2701; CP 2032-2057 and CP 2069-2078.

<sup>7</sup> CP 2571-2573.

<sup>8</sup> 117 Wn.2d 37, 811 P.2d 673 (1991).

<sup>9</sup> Order Granting Attorneys Fees, Dkt no. 247A (Supplemental Designation of Clerk's Papers filed 7/17/14).

misrepresentation as an affirmative defense during the course of this lawsuit? (Assignment of Error No. 3).

3. The trial court permitted NBL to put on evidence and to argue that NBL would forfeit coverage, and would be required to repay Pacific, if it found that NBL made a material misrepresentation in the presentation of its claim for payment of insurance benefits. Did the trial court abuse its discretion, and commit reversible error, because this evidence was highly inflammatory and prejudicial, had no probative value and should have been excluded under ER 408? (Assignments of Error Nos. 1 & 2).

4. The trial court awarded NBL attorney fees and costs under *Olympic Steamship*. Did the trial court commit an error of law because Pacific did not deny coverage for NBL's collapse loss and, instead, this case involved a dispute over the valuation of that loss, for which *Olympic Steamship* fees are not available under *Dayton v. Farmers Ins. Group*<sup>10</sup> and subsequent cases following the rule in *Dayton*? (Assignment of Error No. 6 ).

5. The trial court awarded NBL attorney fees and costs under IFCA. Did the trial court commit an error of law because NBL failed to prove that Pacific violated IFCA by unreasonably denying insurance coverage or payment of insurance benefits due under the insurance policy, and thus, no fees could be awarded to NBL under the statute? (Assignments of Error Nos. 5 & 6).

## **V. STATEMENT OF THE CASE**

**1. Before NBL filed this lawsuit, Pacific paid NBL over \$750,000 for its June 2005 basement collapse loss, and about \$4.75 million for its May 2007 fire loss.**

Before NBL commenced this lawsuit, Pacific had promptly accepted coverage, including "code upgrade coverage," for NBL's collapse and fire losses at the Metropole Building, shortly after NBL reported each loss. When NBL filed its complaint in March 2009, Pacific already had paid NBL a total of about \$5.5 million for covered damage that occurred in the June 2005

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<sup>10</sup> 124 Wn.2d 277, 876 P.2d 896 (1994).

collapse and the May 2007 fire, including over \$750,000 in insurance payments for the June 2005 collapse.<sup>11</sup> The dispute here between Pacific and NBL concerns the value of NBL's June 2005 collapse claim, what property was damaged in the collapse and what is the cost to repair or replace the damaged property.

On June 22, 2005, NBL discovered that a 60-square foot portion of the wood plank flooring in the southwest corner of the basement of the Metropole Building had fallen in. Within a day or so, NBL reported the loss under the Pacific insurance policy in force on the date of loss. Adjuster Michael Blackburn was responsible for the investigation and adjustment of the claim. Blackburn was on the scene shortly after he was notified of the claim.<sup>12</sup>

NBL had been aware of moisture-related structural problems in the Metropole basement since 2002 or earlier; and already had retained a structural engineer, Blaze Bresko of Swenson Say Faget, to address those problems. After NBL discovered the collapse, it once again looked to Bresko and the Swenson firm for assistance.<sup>13</sup> NBL's consultants, and not Pacific, developed the plans and specifications for repairing the damage – and Pacific paid what was called for in the plans and specs prepared for NBL.

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<sup>11</sup> Ex. 26; RP 10/7/13 at 521:1-25 (Peterson)

<sup>12</sup> RP 10/3/13 at 315:24-317:23 (Blackburn).

<sup>13</sup> RP 10/2/13 at 243:25-244:15 and 279:21-280:4 (Yates). The policy itself contemplated that as the building owner, the insured would participate in the investigation of a property loss and prepares plans for repairing property damage – it provided up to \$25,000 in coverage for the insured's cost of preparing an insurance claim. RP 522:3-8.

In March 2006, NBL's consultants and contractors demolished an area of about 700 square feet in the Metropole basement in anticipation of repairing a large area of flooring around the 60-square foot collapse, as well as making improvements to the structure supporting the floor above.<sup>14</sup> NBL submitted the plans to the City of Seattle Department of Public Development ("DPD") in February 2007. The DPD issued a permit for the work in March 2007. The DPD permit – issued under the 2003 Seattle Building Code ("SBC") -- did not require any code upgrades in connection with the work, and specifically noted the repairs did not constitute a "substantial alteration" that might require code upgrades under the SBC.<sup>15</sup>

NBL also submitted similar plans and cost estimates to Pacific. Pacific did not challenge the fact that NBL was planning to replace 700 square feet of flooring and perform work that did not appear to be related to the collapse – it paid \$288,500 for the entire proposed scope of repair, before any work had been performed under the building permit, just as NBL requested.<sup>16</sup> Pacific also explained that additional insurance benefits could be available upon completion of the repair work described in NBL's plans and specs, if the actual costs incurred exceeded the estimates.<sup>17</sup>

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<sup>14</sup> RP 10/8/13 at 860:4-862:19 (Everett); Exs. 8 and 131.

<sup>15</sup> Ex. 17.

<sup>16</sup> Ex. 13. In addition, Pacific paid about \$50,000 for water removal, shoring, demolition and architectural services. NBL did not advise Pacific that it had obtained the building permit. Nor did it ever explain why the permitted repair work – which Pacific had already funded – was not commenced before May 2007. *Id.*

<sup>17</sup> Ex. 113.

But NBL never performed the collapse repairs Pacific had funded. Instead, in May 2007, just shy of two years after the collapse, and before NBL had even begun the DPD-approved collapse repair work, a fire caused extensive damage to the Metropole Building. NBL tendered the fire damage claim to Pacific under its 2007 insurance policy. Pacific assigned a new adjuster, Scott Petersen, to the new fire claim – a claim unrelated to the basement collapse incident that had occurred two years earlier.<sup>18</sup>

NBL's 2007 policy covering the fire offered approximately \$4.75 million in property damage and other coverages applicable to the fire claim.<sup>19</sup> It soon became apparent this would not be enough to pay for the extensive renovation and code upgrades that NBL was planning to perform to repair the fire and smoke damage, which affected all three of the main floors of the Metropole.<sup>20</sup>

After the May 2007 fire, NBL told Pacific it wanted to revisit the June 2005 collapse claim; and advised that NBL's consultants were working on expanded plans and new cost estimates for the collapse-related repairs.<sup>21</sup> NBL also told Pacific for the first time that a commercial kitchen had somehow been located in the 60-square foot area of the basement that collapsed in 2005; and said that restoration of that kitchen would be part of

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<sup>18</sup> RP 10/7/13 at 522:9-526:4 (Petersen).

<sup>19</sup> Ex. 2 at \_\_\_; RP 525:15-25 (Petersen).

<sup>20</sup> RP 10/3/13 at 427:14 – 432:5 (Petersen).

<sup>21</sup> RP 10/7/13 at 550:24 – 559:25 (Petersen).

its enhanced claim.<sup>22</sup> When NBL first made the kitchen claim, there was no physical evidence to confirm or deny the kitchen had existed, because NBL's contractors already had gutted the basement in anticipation of performing repairs.<sup>23</sup>

In May 2008, using plans and specifications prepared by its own architects and engineers, NBL applied for a new building permit that encompassed the still uncompleted collapse repairs and the extensive renovations and code upgrades NBL would have to perform because of the fire.<sup>24</sup>

In August 2008, NBL proposed that a substantial portion of the code upgrades associated with its post-fire renovation plans should be allocated to the June 2005 collapse claim and paid under the 2005 insurance policy, which still had substantial undepleted limits of coverage.<sup>25</sup> In other words, three years after the claim involving the basement, NBL began to suggest that code upgrades were required throughout the Metropole Building because of the collapse of 60-square foot basement flooring.

The DPD issued a permit for the combined fire and collapse repair work in October 2008. The work under the permit was roughly projected to cost \$8 million – about \$2.5 million more than the \$5.5 million Pacific had

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<sup>22</sup> RP 10/7/13 at 499:18-25 (Petersen).

<sup>23</sup> RP 10/7/13 at 510:19-512:5 (Petersen).

<sup>24</sup> RP 10/2/13 at 120:9-23 (Yates); Ex. 21.

<sup>25</sup> The 2007 policy was exhausted through payment of \$4.75 million for the fire loss – and millions more were required to complete fire repairs and code upgrades. The 2005 policy had approximately \$2.44 million in remaining limits of coverage.

already paid for the two losses. The remaining limits of coverage under the 2005 policy were about \$2.5 million; and NBL was proposing that Pacific should pay the remaining limits of that earlier policy to fund a combined fire and collapse repair project.<sup>26</sup>

In response to NBL's proposal, Pacific asked its outside consultant, Richard Dethlefs of Wiss, Janney, Elstner Associates ("WJE") to evaluate NBL's newly revised collapse claim. Because the SBC in force in June 2005 had already been revised, WJE used the then-current, 2006 version of the SBC as its benchmark – the same version of the SBC the DPD had used to review the plans for combined fire and collapse repairs and to issue a new building permit. Furthermore, when Dethlefs performed his analysis, NBL still had not made any significant progress on repair of the basement collapse of June 2005 or the fire damage of May 2007 – although it had already received \$5.5 million in insurance payments from Pacific for the two losses.<sup>27</sup>

WJE concluded that code upgrades would not be required to repair the June 2005 collapse damage. Pacific told NBL what WJE had concluded and freely shared WJE's report with NBL.<sup>28</sup>

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<sup>26</sup> RP 10/2/13 at 134:24-135:25 (Yates); Ex. 21.

<sup>27</sup> NBL did find other uses for the money it received from Pacific. NBL purchased the Metropole in 1998 for \$1.325 million, including a \$1 million loan from Commerce Bank. Within 3 months after the fire, Pacific advanced \$2 million for repair work and Commerce approved NBL's use of the funds for that work. RP 10/8/13 at 850:8-851:2 (Farlow). Ex. 148. Instead, NBL paid off the outstanding balance on the loan and owned the building free and clear.

<sup>28</sup> Exs. 26 and 57.

Pacific also concluded that because years had already passed since the June 2005 collapse, the claim should be resolved, even though NBL had never repaired the collapse damage. Although the policy did not require Pacific to pay full Replacement Cost Value (“RCV”) for the collapse loss until NBL actually completed repairs, Pacific issued payment to NBL for the full RCV in January 2009.<sup>29</sup>

By that point, Pacific had paid NBL a total of \$777,683, including \$25,000 for NBL’s cost of preparing its collapse insurance claim,<sup>30</sup> for what had begun as moisture related damage to about 60-square feet of flooring, in a storage and cleanup area, in the corner of the basement of a 23,500 square foot building, that NBL had purchased for \$1.325 million.

2. **In a February 2009 demand letter, NBL told Pacific it should pay \$3.6 million for the June 2005 basement collapse loss, including extensive code upgrades and nearly \$500,000 to restore a commercial kitchen.**

In response to Pacific’s final payment, NBL’s lawyers sent Pacific a long, detailed demand letter. In that letter, NBL asserted that Pacific was obligated to pay \$3.6 million for the collapse loss. For the first time, NBL also asserted that the 2003 SBC, which was in force on the date of the collapse, should apply to Pacific’s valuation of the claim for purposes of code upgrade coverage, even though the permit the DPD had issued for the

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<sup>29</sup> Ex. 26.

<sup>30</sup> Exs. 25-26; RP 522:3-8.

combined fire and collapse repair was subject to the 2006 version of the SBC.<sup>31</sup>

When NBL sent its February 2009 demand, Pacific already had paid about \$100,000 in costs to restore the kitchen that NBL had first claimed in the summer of 2007 as part of the June 2005 collapse loss. In its February 2009 demand for \$3.6 million, NBL itemized an additional \$500,000 in repair costs that it claimed Pacific should pay to restore the alleged commercial kitchen. The demand letter did not indicate that NBL was uncertain about the size, location, contents or dollar value of the kitchen for which NBL was demanding an additional \$500,000 in insurance payments – NBL was quite specific about the kitchen that allegedly was damaged and the amount of money it wanted Pacific to pay for the kitchen damage.<sup>32</sup>

Days after sending its demand to Pacific, NBL filed this lawsuit.<sup>33</sup>

3. **NBL's complaint alleged that the 2003 Seattle Building Code applied to the June 2005 collapse loss; and that under the 2003 version of the SBC, Pacific had undervalued its insurance claim by millions of dollars.**

As filed in March 2009, NBL's complaint was based on the theory that Pacific had breached the insurance contract. NBL asserted that by using the 2006 SBC to evaluate the need for code upgrades as a result of the June 2005 collapse, instead of the 2003 SBC in force on the date of loss, Pacific had undervalued its property damage claim by millions of dollars. NBL

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<sup>31</sup> Exs. 21 and 158.

<sup>32</sup> *Id.*

<sup>33</sup> CP 1-55.

insisted that if the 2003 SBC were applied, repairing the June 2005 collapse damage would also require NBL to spend millions to bring the upper floors of the Metropole Building up to modern code requirements and would exhaust the remaining limits of coverage under NBL's 2005 Pacific insurance policy.<sup>34</sup>

The trial court considered cross-motions for partial summary judgment on the narrow question whether the "Ordinance or Law" provisions of the Pacific insurance policy required use of the 2003 or the 2006 version of the SBC to determine whether Pacific should pay the cost of code upgrades as part of the adjustment of the collapse loss.. The policy says that Pacific will pay for code upgrades that "affect" the repair of the property damage – and Pacific argued this means the 2003 SBC did not apply because it could not "affect" repairs that were to be performed under a permit governed by the 2006 Code.<sup>35</sup> NBL argued that the policy's general loss settlement provisions for valuation of property damage at the time of the loss made the undefined term "affect" ambiguous, and that the general valuation provisions should control the supplemental Ordinance or Law coverage.<sup>36</sup>

The trial court concluded that Pacific's interpretation of the policy was reasonable and correct as a matter of law; and that the version of the

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<sup>34</sup> *Id.*

<sup>35</sup> CP 70-79, 171-185.

<sup>36</sup> CP 141-154.

SBC that controlled the building permit also should apply to valuation of the claim under the “Ordinance or Law” provisions of the policy.<sup>37</sup>

NBL sought discretionary review in this Court, arguing not only that the trial court had erred, but that if the 2003 SBC were applied, Pacific unquestionably would be required to pay millions for extensive code upgrade work throughout the Metropole Building.<sup>38</sup>

This Court accepted review, and in April 2011, the Court reversed the trial court’s summary judgment order. The Court held that the Code in force on the date of loss should be applied to determine what code upgrade costs, if any, would be due to NBL under the insurance policy, agreeing with NBL that the policy’s reference to a building code that “affects the repair” could have more than one “reasonable” meaning; and holding that the meaning most favorable to the insured therefore should be applied:

We conclude that the Ordinance or Law provision should be interpreted in accord with the policy's explicit provision for valuing the cost of repairing damaged property “at the time of loss or damage.” To the extent the provision is susceptible to more than one reasonable interpretation because of its use of the term “affect,” the ambiguity must be resolved in favor of No Boundaries.<sup>39</sup>

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<sup>37</sup> CP 191-193.

<sup>38</sup> CP 194-228.

<sup>39</sup> CP 230-238; *No Boundaries, Ltd. v. Pac. Indem. Co.*, 160 Wn.App. 951, 249 P.3d 689 (2011).

4. **Pacific concluded that no code upgrades were required to repair the June 2005 collapse damage under the 2003 version of the SBC.**

Consistent with this Court's ruling, Pacific asked WJE to look at the NBL collapse claim again, this time applying the 2003 SBC. WJE determined that under the repealed 2003 Code, just as under the later versions of the Code, no code upgrades would be required to repair the collapse damage; and Pacific had already paid NBL more than enough to complete repair of the June 2005 collapse loss.<sup>40</sup>

Pacific promptly advised NBL of WJE's conclusions and once again shared WJE's report with NBL.<sup>41</sup>

WJE's analysis was consistent with the DPD's original analysis of the collapse loss. When the DPD issued its original permit in 2007, for the expansive collapse repairs specified by NBL's own consultants, the DPD also had concluded code upgrades were not required under the 2003 Code.<sup>42</sup>

5. **After Pacific declined to pay for code upgrades under the 2003 Code, NBL asserted additional claims for common law bad faith and for violation of the CPA and IFCA.**

In May 2011, in response to Pacific's evaluation of the collapse claim under the 2003 SBC, NBL amended its complaint to add claims for common law bad faith, violation of the CPA and violation of the recently enacted IFCA. NBL's theory was, and remains, that Pacific violated IFCA because it

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<sup>40</sup> RP 10/10/13 at 1131:8 – 1134:9, 1157:11 – 1159:9 (Dethlefs).

<sup>41</sup> *Id.*

<sup>42</sup> Exs. 21 and 227.

“unreasonably denied coverage or payment of benefits” by using the 2006 version of the SBC in its original evaluation of the collapse claim; and by following the advice of WJE that no code upgrades would be required under either the 2003 version or the 2006 version of the SBC.<sup>43</sup>

6. *Pacific asserted a “concealment or misrepresentation” defense after it determined, through investigation and discovery in this lawsuit, that there had not been a full commercial kitchen in the area where the June 2005 collapse occurred.*

When NBL first told Pacific it was seeking to recover the cost of restoring a commercial kitchen, a 700-square foot area around the 60-square foot flooring collapse had been demolished for over a year. NBL was unable to provide any documentation or photographs to confirm the kitchen had ever existed. Nevertheless, Pacific accepted NBL’s representations.<sup>44</sup>

However, during the course of Pacific’s defense of this lawsuit, Pacific’s counsel and experts gathered evidence that confirmed what the original photos of the collapse area seemed to show -- there never was, and probably never could have been, a fully-equipped, \$600,000 commercial kitchen in the corner of the Metropole basement where 60 square feet of flooring collapsed in June 2005, despite what NBL and its attorneys had told Pacific in NBL’s February 2009 demand letter to Pacific.<sup>45</sup>

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<sup>43</sup> CP 239-254; *see also* Ex. 158 and CP 271-279; *compare* CP 372-394.

<sup>44</sup> RP 510:14-511:25 (Peterson).

<sup>45</sup> CP 372-394. Indeed, NBL made that claim as part of a concerted effort to bulk up the June 2005 claim so the total repair cost would exceed a 60% “repair cost to building value ratio” that could trigger code upgrades in other parts of the building under the SBC. Ex. 210.

7. *The jury found that code upgrades were not required to complete repair of the June 2005 collapse damage; and that Pacific had paid for NBL's insurance claim as the contract of insurance required.*

At trial, NBL and its expert witnesses told the jury that repairing the basement collapse damage – independent from repair of the May 2007 fire damage – would require code upgrade work throughout the Metropole Building to bring the 125 year old structure up to modern standards for disability access, seismic retrofits and similar SBC specifications. To trigger those extensive code upgrades, NBL had to prove that the collapse repairs would constitute a “substantial alternation” of the Metropole within the meaning of the SBC; or prove that the collapse repair costs would exceed 60% of the building’s value.<sup>46</sup>

However, the collapse involved 60 square feet of flooring in the basement of a 23,500-square foot building. NBL’s own original repair plan cost under \$300,000 and was approved by the DPD, under the 2003 SBC, without any code upgrades required. NBL first made its claim for code upgrades for the collapse loss after a fire had ravaged the Metropole, and after it had become apparent the cost of repairs and code upgrades because of the fire would exceed the limits of coverage applicable to the fire loss.<sup>47</sup>

Nevertheless, NBL’s experts, including architect David Murphy and contractor Stacey Grund, opined that repairing the collapse damage alone

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<sup>46</sup> RP 10/7/2013 at 740:1-11, 741:7-12 (Murphy); RP 10/10/13 at 1132:2-1134:9.(Dethlefs).

<sup>47</sup> Exs. 88, 110 and 210-211.

would cost about \$1.1 million, not including any past repair costs already incurred.<sup>48</sup> Relying on a low, tax-assessed value of the Metropole Building, NBL in turn argued this repair cost would exceed 60% of the building's value, and thus would require that NBL bring the entire building up to the requirements of the 2003 SBC. The code upgrades NBL attributed to the collapse damage under this analysis totaled about \$1.6 million.<sup>49</sup>

The testimony of Richard Dethlefs of WJE confirmed that the repair of a small portion of the flooring in a corner of the Metropole basement could not possibly cost over \$1 million; nor would the City require NBL to upgrade the entire three-story building to meet current building codes as a condition of a building permit for the basement collapse repair.

For more than 15 years, Richard Dethlefs has specialized in code compliance issues, and has written papers and given lectures on the interpretation and application of building codes.<sup>50</sup> Dethlefs reviewed the collapse repair work that Swenson, Say Faget had specified and obtained permits to perform in 2007. Although NBL's experts characterized these repairs as merely temporary, Dethlefs concluded they were "comprehensive," and were more than adequate to address the damage that occurred in the collapse, as well as other deficiencies in the building that predated and were "completely unrelated" to the collapse "in any way, shape or form."<sup>51</sup>

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<sup>48</sup> Exs. 76-77; RP 10/8/13 at 685:8-16 (Grund).

<sup>49</sup> Exs. 69 and 71; RP 10/8/13 at 719:9-12, 735:1-5, 737:4-738:3 (Murphy).

<sup>50</sup> RP 10/10/13 at 1096:21-1098:22 (Dethlefs).

<sup>51</sup> RP 10/10/13 at 1109:1-13 (Dethlefs).

Dethlefs concluded the earlier collapse repair plans -- prepared by Blaze Bresko of Swenson, Say Faget for NBL, with an estimated cost to complete of \$288,500, and with a permit from the DPD in 2007 that did not require code upgrades – were more than sufficient to accomplish a “100 percent repair” of the collapse damage.<sup>52</sup>

Dethlefs also explained that in late 2008, he had considered an expanded scope of repairs proposed by NBL, which included \$130,000 for a kitchen, \$100,000 for bathroom renovations, and additional work to strengthen the floor above the collapse in the basement, for a total of \$568,000. Even under that expanded scope of repair, Dethlefs concluded the collapse repairs would not trigger any code upgrade requirements under the SBC then in force – the 2006 SBC.<sup>53</sup> Dethlefs also told the jury that NBL’s expanded 2008 scope of repair included many items that he believed were “excessive” and unnecessary to return the building to its condition prior to the collapse.<sup>54</sup>

Dethlefs provided the jury with a brief tutorial on the operation of the SBC. He explained that only about \$600,000 of the \$1.1 million collapse repair estimate that Grund had prepared, pursuant to a scope of repair from

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<sup>52</sup> RP 10/10/13 at 1109:1-24 and 1111:1-13 (Dethlefs); Ex. 227. NBL did not call Bresko to ask whether the repair plans he prepared, and that the City approved without code upgrades in 2007, were merely temporary and insufficient to completely repair the collapse damage.

<sup>53</sup> RP 10/10/13 at 1131:15-1134:9 (Dethlefs).

<sup>54</sup> Dethlefs also testified that when Pacific agreed to fund an expanded scope of repair in 2009, and paid for that expanded scope in 2009, it had paid for “voluntary upgrades” that NBL had chosen to make to deteriorated portions of the building that were not affected by the insured collapse event. RP 10/10/13 at 1144:4-1145:18 and 1156:10-1157:10 (Dethlefs).

Murphy, should be considered to determine whether collapse repairs exceed the 60% trigger for building-wide code upgrades. Dethlefs also explained that the DPD most likely would value the Metropole at \$3.2 million for code upgrade purposes. However, even using the far lower, tax-assessed value of about \$1.5 million at the time of the collapse, the cost of repair, properly adjusted for the purposes of code upgrade analysis, still would not reach the 60% building value trigger using NBL's expanded scope of repairs and enhanced cost estimates.<sup>55</sup>

The jurors were convinced, as in its verdict, the jury specifically found that no code upgrades were required; and that Pacific had not breached the insurance policy by denying coverage or benefits that it was required to pay NBL for the collapse claim.<sup>56</sup>

8. ***There was no evidence to prove that the commercial kitchen described in NBL's February 2009 demand to Pacific had existed at the time of the June 2005 collapse.***

NBL's engineers and contractors demolished the collapse area in March 2006 and obtained building permits for collapse repairs in March 2007.<sup>57</sup> In July 2007 -- after the May 2007 fire, more than a year after the basement demolition and more than two years after the collapse -- NBL claimed for the first time that it had lost a commercial kitchen in the collapse. Pacific repeatedly asked for details and documentation to confirm the new

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<sup>55</sup> RP 10/10/13 at 1132:23-1133:6 (Dethlefs).

<sup>56</sup> CP 2010-2011.

<sup>57</sup> Ex. 39; RP 560:18-561:4 (Petersen).

kitchen claim.<sup>58</sup> Although NBL never did produce the information Pacific requested, Pacific paid NBL about \$100,000 based on NBL's representations about the kitchen damage.<sup>59</sup> In NBL's February 2009 demand letter, NBL told Pacific it should pay \$500,000 more for the still undocumented commercial kitchen. NBL was quite specific about what was allegedly damaged and what it wanted Pacific to pay to repair and replace it.<sup>60</sup>

After NBL sued Pacific, and after Pacific and its counsel gathered substantial evidence that NBL was not telling the truth, Pacific asserted an affirmative defense under *Cox*.<sup>61</sup>

At trial, NBL presented only one witness who had any personal knowledge of what existed in the damaged corner of the basement in June 2005 – NBL president and owner, Reyn Yates. Yates told the jury that he owns numerous buildings and many of them have working kitchens in them. He does not pay attention to the exact location, layout or equipment in those kitchens, and did not pay attention to those details at the Metropole prior to the collapse.<sup>62</sup> Nevertheless, Murphy, who was retained after the demolition and fire, presented detailed drawings, based on information he obtained from Yates, showing the commercial kitchen that allegedly was damaged in the

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<sup>58</sup> RP 10/7/13 at 511:19-512:21 (Petersen).

<sup>59</sup> RP 10/7/13 at 512:1-5 (Petersen).

<sup>60</sup> Ex. 158.

<sup>61</sup> CP 372-395.

<sup>62</sup> RP 10/1/13 at 21:1-24:2 (Yates).

collapse. Those drawings were consistent with NBL's pre-suit demand to be paid \$600,000 to restore the allegedly damaged kitchen.<sup>63</sup>

Pacific called Sue Everett, NBL's own on-site building manager, who oversaw day-to-day operation and maintenance of the Metropole. Everett inspected the basement the day the collapse was discovered and had photographs taken that same day.<sup>64</sup> Everett knew exactly what was in the damaged corner of the basement. Using the photographs to guide her testimony, Everett confirmed that the collapse had occurred in a small, empty storage room and that an area east of the storage room – which she referred to as the “kitchen” – had tile walls, a sink and possibly a dishwasher, but no other kitchen equipment or improvements.<sup>65</sup>

DPD records were consistent with Everett's testimony. Those records showed that a commercial kitchen had been designed and constructed nearly 30 years before the collapse – in a distant area of the Metropole basement that could not have been affected by the collapse.<sup>66</sup> Just as Everett saw and testified, the drawings showed the collapse location contained a dishwashing area and a hot water heater – not the extensive improvements and equipment comprising a \$600,000 commercial kitchen.<sup>67</sup>

NBL offered one rebuttal witness -- Tom Graff, a real estate agent who has assisted Yates with numerous real estate deals for years, and who

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<sup>63</sup> RP 10/8/13 at 807:23-808:17 (Murphy); Ex. 77.

<sup>64</sup> RP 10/9/13 at 890:13-22 (Everett); Ex. 127.

<sup>65</sup> RP 10/9/13 at 891:3-892:21 and 896:1:17 (Everett).

<sup>66</sup> Ex. 221.

<sup>67</sup> *Id.*

was the leasing agent for the Metropole. Graff testified he had seen a commercial kitchen in the collapse area.<sup>68</sup> However, he could not explain why that kitchen was not described and itemized in the lease he wrote for the basement before the collapse, as would be customary.<sup>69</sup> When Graff was asked when he last saw the commercial kitchen in the southwest corner of the basement, he stated it had been just before the fire in May 2007 – a physical impossibility because that entire area had been demolished in March 2006. Judge Ramsdell asked Graff to think and answer again. Graff did not modify his testimony on his second attempt.<sup>70</sup>

In summary, in February 2009, NBL demanded \$500,000 to restore a commercial kitchen lost in the June 2005 collapse. At trial, Yates testified he knew little about that kitchen; while his own building manager, consistent with photos and other documentary evidence, testified the only “kitchen” in the collapse area consisted of a sink and possibly a dishwasher. Furthermore, after Pacific asserted its affirmative defense, NBL reduced its claim for kitchen damages to under \$100,000 – conceding that the \$600,000 commercial kitchen had never existed and that NBL’s February 2009 demand had been unfounded.<sup>71</sup>

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<sup>68</sup> RP 10/10/13 at 1176:4-1177:19 (Graff).

<sup>69</sup> Ex. 35; RP 10/10/13 at 1182:5-1185:24 (Graff).

<sup>70</sup> RP 10/10/13 at 1180:14-1185:2 (Graff).

<sup>71</sup> Exs. 26 and 158.

9. *At trial, the Court allowed jurors to consider testimony and argument about the legal consequences NBL could face if the jury found, as a matter of fact, that NBL misrepresented its insurance claim; and the Court denied Pacific's motion for mistrial.*

The jury was asked to determine, as a question of fact, whether NBL intentionally and materially misrepresented its insurance claim.

Prior to trial, Pacific moved *in limine*, under ER 408, to bar testimony or argument concerning the possible legal consequences of the jury's factual determination. The trial court initially appeared to agree with Pacific's position,<sup>72</sup> but during the course of trial, the court decided to permit testimony and argument that told the jury of the legal consequences that could follow if it found that NBL had misrepresented its \$600,000 claim to repair and replace a fully equipped commercial kitchen.<sup>73</sup> The trial court's stated rationale was that the jury should consider whether NBL would have misrepresented its claim, knowing the risk if the misrepresentation were discovered.<sup>74</sup>

However, NBL made its misrepresentations before it filed this lawsuit, culminating in its demand letter of February 2009. Pacific did not

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<sup>72</sup> RP 10/1/13 at 4:22-41:16, *compare* CP 1838.

<sup>73</sup> *See* citations to record at footnote 3, *supra*. Under *Cox*, an insured who makes an intentional and material misrepresentation to its insurer in the presentation of a property damage claim may forfeit coverage for the claim, as well as its right to pursue extracontractual claims against the insurer. The insured may also be required to return any amounts the insurer has already paid for the claim. *Cox*, 110 Wn.2d at 650 (insured's misrepresentation of damaged property voids the entire insurance policy); *Johnson v. Allstate Ins. Co.*, 126 Wn. App. 510, 517-518, 108 P.3d 1273 (2005) (as a result of misrepresentation of his claim, the insured is required to repay all benefits previously paid for the claim).

<sup>74</sup> RP 10/1/13 at 41:9-16; RP 1198:25 – 1202:15; 1203:25 – 1205-15.

invoke its misrepresentation defense until July 2013. There was no evidence to show that NBL was aware of the policy's "concealment or misrepresentation" provision, or aware of the *Cox* ruling, in February 2009 or at any time before Pacific raised its affirmative defense a few months prior to trial.

As a result, Pacific moved for a mistrial. The trial court denied the motion, indicating it would revisit the question depending on the outcome of the trial.<sup>75</sup> The court never did revisit Pacific's motion.

10. **The trial court declined to instruct the jury that Pacific had no duty to discover or advise NBL of suspected misrepresentation in the presentation of NBL's insurance claim; and NBL argued that Pacific had acted wrongfully by asserting that defense during the course of the litigation.**

The trial court declined to instruct the jury that Pacific had no affirmative duty to discover NBL's misrepresentation, or to advise NBL that it would invoke NBL's misrepresentation as a defense to NBL's claims.

Pacific proposed the following instruction, derived from *Cox*:

An insurance company has no affirmative duty to inform its insured that it believes he has concealed or misrepresented material facts in connection with his claim for payment of benefits under the insurance policy; and, an insurance company does not forfeit its right to assert that its insured has concealed or misrepresented material facts by paying all or part of its insured's claim.<sup>76</sup>

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<sup>75</sup> RP 10/9/13 at 871:13-873:20.

<sup>76</sup> CP 1842; *see also* RP 10/10/13 at 1197:4-13.

In the absence of this instruction, NBL was able to argue that Pacific had acted in bad faith and in violation of IFCA by asserting its misrepresentation defense after NBL brought this lawsuit.<sup>77</sup>

**11. The jury awarded NBL \$200,000 for violation of IFCA.**

The court instructed the jury, in Instruction No. 25, that to prove its claim under IFCA, NBL was required to prove that Pacific “unreasonably denied a claim for coverage, or unreasonably denied payment of benefits”:

Plaintiffs claim that defendant has violated the Washington Insurance Fair Conduct Act. To prove this claim, a plaintiff has the burden of proving each of the following propositions:

- (1) **That defendant unreasonably denied a claim for coverage, or unreasonably denied payment of benefits;**
- (2) That plaintiff was injured or damaged; and
- (3) That defendant’s act or practice was a proximate cause of plaintiff’s injury or damage.

If you find from your consideration of all of the evidence that each of these propositions has been proved, your verdict on this claim should be for plaintiffs. **On the other hand, if any of these propositions has not been proved, your verdict on this claim should be for defendant.**<sup>78</sup>

The jury found that no code upgrades were required; that Pacific paid NBL the full value of its claim before NBL sued Pacific; and that Pacific did not violate the CPA in its adjustment of the claim.<sup>79</sup>

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<sup>77</sup> RP 10/10/13 at 1226:14-1228:6; CP 2114-2125.

<sup>78</sup> CP 1874.

<sup>79</sup> CP 2009-2014.

The jury itself determined that NBL failed to prove the essential elements of its IFCA claim as stated in the court's instruction; but the jury awarded NBL \$200,000 under that Act.<sup>80</sup>

**12. The trial court denied Pacific's motions to correct the verdict and for a new trial.**

Pacific moved the trial court to correct the jury's inconsistent verdict and to enter judgment for Pacific on NBL's IFCA claim. The court denied that motion.<sup>81</sup> Pacific also moved for entry of judgment or for a new trial. The trial court denied Pacific's motion.<sup>82</sup>

**13. The trial court awarded NBL attorney fees and costs under IFCA and under the Olympic Steamship doctrine.**

On NBL's motion, and over Pacific's objection, the trial court also awarded attorney fees and costs to NBL under IFCA and under the *Olympic Steamship* doctrine. NBL sought nearly \$1.7 million in fees and costs. The court awarded \$254,250 in fees under *Olympic Steamship* and \$280,000 in fees under IFCA -- the latter "includes costs of successful interlocutory appeal." In addition, the court awarded \$33,755 in costs, for a total of \$568,005.<sup>83</sup> The court did not enter findings in connection with these awards.

**VI. SUMMARY OF ARGUMENTS ON APPEAL**

After NBL reported that a 60-square foot portion of the floor in the corner of the Metropole Building basement collapsed in June 2005, Pacific

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<sup>80</sup> *Id.*

<sup>81</sup> CP 2032-2057; CP 2077-2078.

<sup>82</sup> CP 2079-2113; CP 2700-2701.

<sup>83</sup> Order Granting Attorneys Fees, Dkt no. 247A (Supplemental Designation of Clerk's Papers filed 7/17/14).

promptly responded, accepted coverage for the claim, and paid the full estimated cost of the repairs recommended by NBL's consultants and approved by the DPD. NBL had a building permit and could have completed those repairs – with no code upgrades required. NBL did not start the repairs before a fire caused extensive damage to the three floors of the Metropole in May 2007.

There was no question that repairing the fire damage would require extensive code upgrades. Although Pacific paid the entire \$4.75 million in available coverage for the fire loss, that was not nearly enough to complete the \$8 million renovation of the Metropole that NBL contemplated after the fire. As a result, three years after the 2005 collapse, NBL told Pacific it should pay for a substantial portion of the code upgrades included in that massive renovation under the Pacific insurance policy in force when the 2005 collapse occurred. When Pacific's consultants advised that collapse repairs would not require any code upgrades, Pacific declined to pay for them. However, before NBL filed this lawsuit, Pacific had paid NBL over \$750,000 for costs allegedly related to the collapse claim.

NBL told Pacific that the collapse repairs would cost \$3.6 million more than Pacific had paid, including an additional \$500,000 to restore a commercial kitchen allegedly lost in the collapse, and demanded that Pacific pay the remaining limits of coverage applicable to the 2005 loss. This lawsuit followed, days after that demand.

The evidence demonstrated that Pacific paid more than enough to repair all damage that resulted from the 2005 collapse and that no code upgrades were required as a result of that collapse event. In its special verdicts, the jury specifically found that Pacific did not breach the insurance policy and that no code upgrades were required. The trial court's instructions to the jury, consistent with the plain text of IFCA, told the jury that NBL had to prove that Pacific "unreasonably denied a claim for coverage, or unreasonably denied payment of benefits." Nevertheless, the jurors found that Pacific violated IFCA and awarded NBL \$200,000 under the statute. The jury's verdict on NBL's IFCA claim is contrary to the jury's own fact finding and to the law stated in the court's instructions. The trial court committed an error of law by declining to enter judgment for Pacific on NBL's IFCA claim. This Court should direct entry of judgment for Pacific on the IFCA claim.

The evidence also showed that NBL's claim that it had lost a \$600,000 commercial kitchen in the June 2005 collapse was implausible and based on an intentional misrepresentation of facts material to Pacific's adjustment of the claim. Indeed, after Pacific asserted NBL's misrepresentation as an affirmative defense,, NBL stepped away from its pre-suit misrepresentation and shaved hundreds of thousands of dollars off its claimed damages for loss of the phantom commercial kitchen. Not one witness appeared at trial who could describe the alleged commercial kitchen – other than a witness who claimed to have seen that kitchen a year after the

entire area had been demolished. Not one witness had installed, worked in or performed repairs on the alleged commercial kitchen. Not one document confirmed the existence of the commercial kitchen. That was because the commercial kitchen never existed. NBL's own property manager testified that the "kitchen" had been nothing but a storage area containing a sink and possibly a dishwasher – and photos taken the day of the collapse confirmed her testimony. The jury still found that NBL did not misrepresent its claim. The jury's finding was the result of the trial court's error in allowing the jury to consider the potential legal consequences of a finding of misrepresentation under *Cox* and other controlling Washington case law. After hearing that NBL could lose its coverage, and might be required to repay insurance benefits Pacific already paid to NBL, the jury could not fairly and objectively decide whether NBL misrepresented the existence, contents and value of the commercial kitchen allegedly lost in the collapse, no matter what the relevant evidence showed.

The trial court compounded its error by refusing to instruct the jury, as *Cox* requires, that Pacific had no affirmative duty to promptly discover NBL's misrepresentation or to promptly advise NBL that Pacific might invoke its rights under the concealment and misrepresentation provisions of the insurance policy and the *Cox* doctrine. Because the court did not provide this instruction to the jury, NBL was able to argue that Pacific had acted in bad faith, and had violated insurance claims handling regulations, the CPA

and IFCA by asserting its affirmative defense during the course of this lawsuit. The court's failure to instruct the jury permitted the jurors to consider NBL's extracontractual claims under an erroneous legal standard and tainted the jury's special verdict awarding NBL damages for common law bad faith, as well as the jury's special verdict on Pacific's affirmative defense that NBL misrepresented its insurance claim. A new trial on bad faith and misrepresentation should result.

Finally, the trial court erred by awarding attorney fees and costs to NBL under IFCA and under the *Olympic Steamship* doctrine. NBL did not prove the essential elements of an IFCA claim. Similarly, NBL is not entitled to an award of attorney fees and costs under *Olympic Steamship*, because *Olympic Steamship* fees are only awarded when an insurer has denied coverage and the insured must incur legal expenses to prove that coverage exists. Pacific did not deny coverage for NBL's collapse claim. Pacific accepted coverage; and the jury found that Pacific paid for the claim, in full. The only issue was the amount of NBL's claim, and fees are not recoverable under *Dayton*.

## VII. ARGUMENT AND AUTHORITY

1. *The trial court committed an error of law by entering judgment on the jury's erroneous IFCA award, which was contrary to the jury's own fact-finding and the court's proper instructions on requirements of the IFCA statute.*

The decision to grant or deny a motion for new trial may be a matter within the trial court's discretion, reviewable for an abuse of discretion.<sup>84</sup> On appeal, greater deference is given to a decision to grant a new trial than a decision to deny a new trial, because the denial of a new trial ends the proceeding and forecloses further relief.<sup>85</sup>

However, when a motion for new trial or for judgment notwithstanding the verdict addresses a legal error – like the jury's finding that Pacific violated IFCA, in the face of its own determination that the collapse claim did not trigger code upgrades and that Pacific complied with the insurance policy – there is no element of discretion involved. In this situation, this Court reviews the trial court's decision for an error of law.<sup>86</sup>

IFCA, RCW 48.30.015(1), is not ambiguous in the least. The statute requires a plaintiff to prove that the insurer “unreasonably denied a claim for coverage or payment of benefits”:

(1) Any first party claimant to a policy of insurance who is unreasonably denied a claim for coverage or payment of benefits by an insurer may bring an action in the superior court of this state to recover the actual damages sustained, together with the costs of the action, including

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<sup>84</sup> *Allyn v. Boe*, 87 Wn. App. 722, 729, 943 P.2d 364, rev. denied, 134 Wn.2d 1020 (1998).

<sup>85</sup> *State v. Balisok*, 123 Wn.2d 114, 177, 866 P.2d 631 (1994).

<sup>86</sup> CR 50; CR 59; *Coleman v. George*, 62 Wn.2d 840, 384 P.2d 871 (1963).

reasonable attorneys' fees and litigation costs, as set forth in subsection (3) of this section.

The jury's own findings of fact established that Pacific *did not* "deny coverage or payment of benefits" to NBL. Instead, the jury found no code upgrades were required to complete collapse repairs, so Pacific never had an obligation to "pay benefits" for such upgrades. The jury also found that Pacific fully performed the contract of insurance – it did not "deny coverage" and instead granted coverage and paid NBL, as required under the policy.

There was no IFCA violation – and the trial court's instructions to the jury told the jurors precisely that. The jury's own separate verdicts on the code upgrade and breach of contract issues permitted only one legal conclusion as to NBL's IFCA claim: NBL failed to prove that Pacific violated IFCA.

In the trial court, NBL repeatedly argued that Pacific "violated claims handling regulations" that the jury could have found to be a violation of IFCA. However, the statute does not say that violation of an insurance regulation alone will constitute a violation of IFCA. The text of RCW 48.30.015(1), refers only to (1) denial of coverage; and (2) denial of payment of benefits. Pacific did not deny coverage or payment of benefits to which NBL was entitled – the jury said so. If Pacific did not deny coverage or payment, then *a fortiori*, Pacific could not have done so "unreasonably."

And, while this precise issue has not yet been addressed in reported Washington appellate decisions, federal trial courts consistently have found

that the plain wording of the IFCA statute is clear: if a plaintiff does not prove one of the two basic elements of an IFCA claim under RCW 48.30.015(1), the plaintiff's claim has failed.<sup>87</sup>

The IFCA further provides that a court "may, after finding that an insurer has acted unreasonably in denying a claim for coverage or payment of benefits or has violated [certain insurance regulations], increase the total award of damages to an amount not to exceed three times the actual damages." RCW 48.30.015(2). A court "shall, after a finding of unreasonable denial of a claim for coverage or payment of benefits, or after a finding of a violation of a rule in subsection (5) of this section, award reasonable attorney's fees and actual and statutory litigation costs, including expert witness fees, to the first party claimant of an insurance contract who is the prevailing party in such an action." RCW 48.30.015(3). The statute provides a list of WAC violations that give rise to treble damages or to an award of attorney's fees and costs.

**Although violations of the enumerated regulations provide grounds for trebling damages or for an award of attorney's fees; they do not, on their own, provide an IFCA cause of action absent an unreasonable denial of coverage or payment of benefits.**<sup>88</sup>

Sound public policy further supports this reading of IFCA when, as here, the insurer has compelling reasons to conclude the insured has misrepresented a claim, and invokes the *Cox* doctrine in defense of the insured's extracontractual claims. Our Supreme Court fashioned the *Cox*

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<sup>87</sup> See, e.g., *MSO Washington, Inc. v. RSUI Group, Inc.*, 2013 WL 1914482 at \*11-\*12 (W.D.Wash.2013); *Babcock v. ING Life Insurance and Annuity Co.*, 2013 WL 24372 at \*8 (E.D.Wash. 2013); *Nesbitt v. Progressive Northwestern Ins. Co.*, 2012 WL 5351846 at \*4 (W.D.Wash.) *Country Preferred Ins. Co. v. Hurless*, 2012 WL 2367073 (W.D.Wash.2012); *Pinney v. American Family Mutual Insurance Company*, 2012 WL 584961 at \*5 (W.D.Wash.2012); *Weinstein & Riley, P.S. v. Westport Ins. Corp.*, 2011 WL 887552 (W.D.Wash.2011); *Travelers Indem. Co. v. Bronsink*, 2010 WL 148366 (W.D.Wash.2010); *Lease Crutcher Lewis WA, LLC v. Nat. Union Fire Ins. Co. of Pittsburgh, PA*, 2010 WL 4272453 (W.D.Wash.2010).

<sup>88</sup> *MSO Washington, Inc. v. RSUI Group, Inc.*, 2013 WL 1914482 at \*11-\*12 (W.D.Wash.2013) (citations omitted, emphasis added).

doctrine to ensure that insureds, as well as insurers, must act in good faith in connection with insurance claims, recognizing that insurers must be able to rely on their insureds to truthfully present their claims for property damaged or lost in a covered event.<sup>89</sup> Unlike other policy defenses, an insurer is not required to promptly invoke a “void for fraud” policy provision in order to preserve the defense.<sup>90</sup> As a matter of public policy, an insurer that chooses to invoke *Cox* as an affirmative defense should not risk penalties under IFCA for “wrongful denial of coverage,” particularly where, as here, the insured sues the insurer after receiving full and fair payment for a loss the insurer promptly accepted as a covered claim; and where, as here, there is compelling evidence to support the insurer’s *Cox* defense.<sup>91</sup>

There cannot be any question here. The jurors themselves concluded that the essential elements of an IFCA claim do not exist in this case: a denial of coverage or a denial of payment of benefits due under the insurance policy. If there is no “denial of coverage” and no “denial of benefits,” then there cannot be an “unreasonable” denial of coverage or payment of benefits.

Under similar circumstances, our Supreme Court held, in *Cox*, that the trial court had properly entered judgment notwithstanding the verdict for the insurer. In *Cox*, the jury answered “yes” to the question whether the

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<sup>89</sup> *Cox*, 110 Wn.2d at 649.

<sup>90</sup> *Id.* at 650.

<sup>91</sup> See, e.g., *City of Seattle v. Egan*, 179 Wn. App. 333, 317 P.3d 568 (2014) (“anti-SLAPP” statute could not be used to prevent the City from seeking declaratory judgment in response to a claimant’s action to obtain videotapes under the Public Records Act).

insured misrepresented its insurance claim, but then went on to answer subsequent questions on the verdict form and granted the insured relief on its extracontractual claims. The trial court later granted judgment notwithstanding the verdict on the extracontractual claims, and the Supreme Court stated:

[T]he court finally realized that Cox's assertion of estoppel was improper and correctly gave a judgment n.o.v. in favor of MOE. "The purpose of the judgment notwithstanding the verdict is to give the trial judge a last opportunity to correct errors." 10 L. Orland and D. Reaugh, Wash.Prac. 260 (1971) (citing *Brown v. Alkire*, 295 F.2d 411 (10th Cir.1961) ). **The court properly used the judgment n.o.v. to correct the misstatement of law in the special interrogatories.**<sup>92</sup>

Here, the jury answered "NO" when asked whether Pacific breached the insurance policy and whether code upgrades were required to repair the covered collapse loss. Just as the finding of misrepresentation precluded judgment for the insured on its extracontractual claims in *Cox*, the jury's finding that Pacific paid NBL the full value for its covered damage under the policy precluded judgment for NBL on its IFCA claim in our own case.

On this record, the trial court should have held, and this Court should now hold, as a matter of law, that NBL failed to prove its IFCA claim. Judgment should be entered for Pacific on that claim, notwithstanding the special verdict.<sup>93</sup>

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<sup>92</sup> *Cox*, 110 Wn.2d at 652 (emphasis added).

<sup>93</sup> Because the jury's special verdicts on the contract and code upgrade issues establish that there was no denial of coverage or benefits to which NBL was entitled under the insurance policy, if a new trial were granted, a Pacific motion for summary judgment seeking dismissal of the IFCA cause of action under CR 56 would soon follow. Bound by the jury's findings,

2. *The trial court committed an error of law by awarding attorney fees and costs to NBL under Olympic Steamship and IFCA.*

The trial court awarded attorney fees and costs to NBL under IFCA and under the *Olympic Steamship* doctrine. The award of fees under IFCA was an error of law, for the same reason the IFCA award itself was an error of law: NBL failed to prove the essential elements of an IFCA claim and could not properly be a “prevailing party” entitled to recover fees and costs under RCW 48.30.015(3).<sup>94</sup>

The award of fees and costs under *Olympic Steamship* also fails as a matter of law.. Pacific never “denied coverage” for NBL’s claim. In fact, it accepted coverage and paid the full RCV for the claim – a supplement to the Actual Cash Value that Pacific was not required to pay unless and until NBL finished repairing the collapse damage.<sup>95</sup> This claim was never a dispute over the existence of coverage for NBL’s claim under the policy – it is and always

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NBL would be unable to rebut that motion. Thus, this Court should direct that judgment be granted in Pacific’s favor on the IFCA claim.

<sup>94</sup> Inexplicably, the trial court’s IFCA fee award specifically included the cost of NBL’s interlocutory appeal. Those fees could not possibly have been incurred to pursue recovery under IFCA – because NBL amended its original Complaint to add a claim under IFCA months after this Court issued its April 2011 ruling, and after Pacific determined neither the 2003 SBC nor the 2006 SBC required code upgrades for the collapse loss. CP 1-55; CP 239-254. Furthermore, NBL ultimately did not “prevail” in proving that Pacific was obligated to pay for code upgrades under either version of the SBC. The trial court should not have awarded attorney fees and costs for work that was neither necessary nor successful in obtaining an award from Pacific. *See, e.g., Chuong Van Pham v. Seattle City Light*, 159 Wn.2d 527, 538, 151 P.3d 976 (2007) (“The court should discount hours spent on unsuccessful claims, duplicated or wasted effort, or otherwise unproductive time,” citing *Bowers v. Transamerica Title Ins. Co.*, 100 Wn.2d 581, 597, 675 P.2d 193 (1983)).

<sup>95</sup> *See* CP 1572-1582.

has been a dispute over the value of the claim and the dollar value of the insurance benefits that Pacific should pay for an undisputedly covered claim.

In late 2008, when NBL first took the position that the collapse damage would require millions of dollars of additional repair and code upgrade costs, Pacific did not deny coverage. Instead, Pacific reviewed the claimed repair costs and determined, as a matter of *valuation of a covered claim*, that the total *value* of the claim was far lower than NBL asserted it to be. Pacific communicated the grounds for its valuation of the claim to NBL and, by January 2009, Pacific had paid the value of the claim – in full – based on the advice of competent experts, as stated in reports that Pacific freely shared with NBL.<sup>96</sup>

Pacific's position was, is, and remains that NBL's collapse damage claim is a covered claim under the insurance policy. The question was, is and remains, what was the extent of the damage and what was the cost of repairing the damage, including code upgrades, if any, required to complete the repairs. Washington law is clear: a dispute concerning the valuation of an insurance claim is not subject to the *Olympic Steamship* fee-shifting rule. In 1994, our Supreme Court decided *Dayton v. Farmers Ins. Group*,<sup>97</sup> which flatly held that disputes over the *value* of the insured's claim for admittedly covered damages does not entitle a prevailing insured to obtain an award of fees under *Olympic Steamship*:

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<sup>96</sup> Exs. 54, 84 and 26.

<sup>97</sup> 124 Wn.2d 277, 876 P.2d 896 (1994).

This case presents an entirely different set of circumstances. Coverage is not an issue; Farmers accepted coverage. Unlike the insured in *Olympic Steamship*, Mr. Dayton has not compelled Farmers to honor its commitment to provide coverage. Instead, **this case presents a dispute over the value of the claim presented under the policy. Such disputes are not properly governed by the rule in *Olympic Steamship*.**<sup>98</sup>

Even if *Olympic Steamship* did apply to disputes over the value of an insurance claim, NBL could not possibly be entitled to an *Olympic Steamship* fee award – for the simple reason that NBL is not the prevailing party in that dispute. Instead, the jury decided – as Pacific concluded years before trial – that whether the 2003 or the 2006 SBC applies, NBL was not entitled to be paid one penny more than the more than \$750,000 that Pacific paid NBL for the collapse damage – before NBL filed this lawsuit.

NBL has argued, and will undoubtedly argue on appeal, that Pacific “denied coverage” when it asserted NBL’s misrepresentation as an affirmative defense in this lawsuit. But raising NBL’s own misconduct as a defense to the contract and extracontractual claims asserted in NBL’s amended complaint was not a denial of the policy’s grant of coverage for NBL’s insurance claim. Pacific admitted the collapse claim was a covered loss under the “Ordinance or Law” and other relevant coverage provisions of the policy.

By the time NBL sued Pacific, Pacific already had “honored its commitment” by extending coverage and paying in full for the covered

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<sup>98</sup> *Id.*, 124 Wn.2d at 280 (emphasis added).

collapse claim. Furthermore, to defeat Pacific's "concealment or misrepresentation" defense, NBL's burden of proof was the same as it was the day it filed its original complaint – the burden of proving what was damaged in the collapse and what it would cost to repair or replace the damaged property.<sup>99</sup> That, too, is a matter of valuation of the damages for a covered claim, and not a "coverage dispute." The only difference is that if NBL failed to prove the existence of the phantom commercial kitchen for which it demanded \$600,000 in insurance benefits, NBL might suffer consequences other than losing its own affirmative claims.

No Washington court ever has held that fees and costs an insured incurs to prove the existence and value of property it claims was damaged in a covered loss event are recoverable under *Olympic Steamship*, whether or not the insurer has asserted the insured misrepresented its claimed damages. No such extension of the *Olympic Steamship* rule is warranted.<sup>100</sup>

3. **The trial court committed an error of law by failing to properly instruct the jury, under Cox, that Pacific had no duty to advise NBL of NBL's own alleged misrepresentation of its claim.**

A cornerstone of NBL's extracontractual claims was its argument that Pacific had denied its claim for code upgrade coverage; and that Pacific had

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<sup>99</sup> This is a fundamental rule of insurance law: the insured always bears the initial burden of proving an insured loss has occurred. *McDonald v. State Farm Fire & Cas. Co.*, 119 Wn.2d 724, 731, 837 P.2d 1000 (1992).

<sup>100</sup> As noted *supra* at 35, the public policy underlying *Cox* should not be chilled by applying IFCA to an assertion of misrepresentation as an affirmative defense against an insured's extracontractual claims. Nor should the prospect of *Olympic Steamship* fees deter an insurer from legitimately pleading an insured's misrepresentation as an affirmative defense.

acted in bad faith and concocted a new “excuse” for denying NBL’s claim when it asserted NBL’s misrepresentation as an affirmative defense prior to trial.<sup>101</sup> NBL’s argument is directly contrary to controlling law – and NBL was only able to make that argument because the trial court declined to properly instruct the jury under *Cox*, as Pacific proposed.

In *Cox*, the insurer made partial payments on the insured’s first-party property damage claim, even though it already suspected the insured had violated the policy’s “concealment or misrepresentation” provision by claiming he had lost art works in a fire that were not on the premises when the fire occurred. Our Supreme Court held the insurer had no affirmative duty to inform the insured of its belief that he committed fraud. Thus, the insurer did not forfeit the right to rely on the insured’s misrepresentation to defeat his extracontractual claims, even though the insurer knew of the insured’s false statement, continued to make payments on the claim and did not cite the policy’s misrepresentation provisions in its pre-suit coverage communications with the insured.<sup>102</sup> Furthermore, the *Cox* decision specifically rejected the insured’s argument that the insurer had an obligation to timely discover and advise the insured of a suspected misrepresentation:

Cox claims that MOE had a duty to notify him that it knew of his misstatements. **Since we hold that MOE had no affirmative duty to inform Cox that it believed he had committed fraud,** it is not necessary to determine

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<sup>101</sup> RP 10/10/13 at 1226:14-1228:6; CP 2114-2125.

<sup>102</sup> *Cox*, 110 Wn.2d at 650. See also, *Johnson*, 126 Wn. App. at 517 (“the insurance company had no affirmative duty to inform the insured of its belief that he committed fraud,” citing *Cox*).

when MOE actually concluded that fraud had occurred.<sup>103</sup>

The wording of Pacific's proposed misrepresentation instruction was drawn straight from the Supreme Court's holding in *Cox*.<sup>104</sup> By declining to instruct the jury that Pacific had no duty to discover or to notify NBL of its defense under the void for fraud provision of the policy, NBL was able to argue that Pacific had acted in bad faith and violated IFCA by asserting the defense during the course of this litigation.<sup>105</sup>

The trial court's instructions to the jury must meet three criteria: (1) they must permit each party to argue its theory of the case; (2) they must not be misleading; and (3) when read as a whole, they must properly inform the trier of fact of the applicable law.<sup>106</sup> Because the trial court refused to give Pacific's proposed *Cox* instruction, Pacific could not rebut NBL's claim that Pacific had acted in bad faith by breaching a duty to promptly discover and advise NBL of a suspected misrepresentation before NBL commenced this lawsuit.

The trial court erroneously believed Pacific's proposed *Cox* instruction was unnecessary because Pacific could make this point in closing argument to the jury.<sup>107</sup> Pacific respectfully disagrees. The existence of a legal duty is a threshold question of law for the court, not a matter for

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<sup>103</sup> *Cox*, 110 Wn.2d at 650 (emphasis added).

<sup>104</sup> *Id.*

<sup>105</sup> In fact, in its own post-trial memoranda, NBL conceded that this was the "denial of coverage" on which the jury's IFCA award was based. CP 2114-2125.

<sup>106</sup> *Brown v. Spokane County Fire Protection Dist. 1*, 100 Wn.2d 188, 194, 668 P.2d 571 (1983).

<sup>107</sup> RP 10/10/13 at 1203:2-18.

argument of counsel or a question of fact for the jury.<sup>108</sup> Any statements to the jury as to the law must be confined to the law set forth in the jury instructions.<sup>109</sup>

Pacific's hands were tied. Its counsel could not argue to the jury, in closing, that NBL's claims based on Pacific's assertion of the misrepresentation defense during the course of the litigation were contrary to Washington law, because that argument would have been inconsistent with the court's instructions.

If the instructions failed to tell the jury what the law is, counsel could not take it upon themselves to fill the gap.

By failing to properly instruct the jury, thereby allowing NBL to impose duties on Pacific that it did not have as a matter of law, the trial court committed an error of law that tainted the jury's consideration of NBL's extracontractual claims, including its claims for common law bad faith and under IFCA, as well as Pacific's *Cox* defense. That error was outcome determinative and reversible.<sup>110</sup>

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<sup>108</sup> *Fuentes v. Port of Seattle*, 119 Wn.App. 864, 868, 82 P.3d 1175 (2003)

<sup>109</sup> *State v. Mak*, 105 Wn.2d 692, 726, 718 P.2d 407, *cert. denied*, 107 S. Ct. 599 (1986); *State v. Davenport*, 100 Wn.2d 757, 760-61, 675 P.2d 1213 (1984).

<sup>110</sup> *Thomas v. French*, 99 Wn.2d 95, 659 P.2d 1097 (1983).

4. *The trial court abused its discretion by allowing the jury to consider prejudicial and irrelevant testimony and argument concerning the potential legal consequences of a jury finding that NBL misrepresented its claim, and by declining to grant a mistrial on that basis.*

The jury was properly asked to determine, as a question of fact, whether NBL intentionally and materially misrepresented its claim by telling Pacific that it had lost a \$600,000 commercial kitchen in the June 2005 collapse.

Under Washington law and the trial court's instructions, the jury was not required to find "clear, cogent and convincing evidence" to support the nine elements of common law fraud. An insured's misrepresentation is proven when a preponderance of the evidence shows the insured has committed an intentional and material misrepresentation in presenting its property damage claim to the insurer.<sup>111</sup> An insured's misrepresentation is material if it concerns facts "relevant and germane" to the insurer's adjustment of the claim.<sup>112</sup> Furthermore, there is a rebuttable presumption that when the insured misrepresents material facts concerning his claim, he does so with the intent to deceive. The burden shifts to the insured to produce credible evidence it presented the facts concerning its claim in good faith.<sup>113</sup>

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<sup>111</sup> CP 1862-1864; *St. Paul Mercury Ins. Co. v. Salovich*, 41 Wn. App. 652, 657-58, 705 P.2d 812 (1985); see also *Allstate Ins. Co. v. Huston*, 123 Wn. App. 530, 543, 94 P.3d 358 (2004) (rejecting insured's proposed "fraud" jury instruction and holding that the preponderance of the evidence standard applied to the insurer's material misrepresentation claim).

<sup>112</sup> *Ki Sin Kim v. Allstate Ins. Co.*, 153 Wn.App. 339, 355, 223 P.3d 1180 (2009), citing *Pac. Indem. Co. v. Golden*, 791 F.Supp. 935, 938 (D.Conn.1991).

<sup>113</sup> *Id.* 153 Wn. App. at 355-356.

Yates' attempt to avoid responsibility for NBL's misrepresentation, by asserting he did not really recall details about the alleged kitchen, did not demonstrate "good faith" – particularly when NBL's own property manager, Sue Everett, was well aware of the truth. There is no credible justification for NBL's demand to be paid over \$600,000 for a commercial kitchen; its commencement of this lawsuit when Pacific did not pay; and its attempt to distance itself from that demand after Pacific invoked its defense under *Cox*. An insured cannot demand to be paid a very specific sum for very specific property, and later avoid the consequences under *Cox* by claiming, *post hoc*, he really did not know what existed prior to the loss event and what was damaged or destroyed in that event.<sup>114</sup>

There was overwhelming evidence that the kitchen NBL described to Pacific -- and for which it obtained \$100,000 in insurance proceeds and demanded another \$500,000 – never existed. Photographs showed a small space that could not possibly have contained a deluxe \$600,000 commercial kitchen.<sup>115</sup> There were no DPD records of construction of a kitchen where the collapse occurred, but there were records of other kitchen construction in the Metropole basement that the collapse could not possibly have affected.<sup>116</sup> The testimony of the building manager, Sue Everett, confirmed that the collapse

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<sup>114</sup> "The insured's bare assertion that she did not intend to deceive the insurance company is not credible evidence of good faith and, in the absence of credible evidence of good faith, the presumption [of intent to deceive] warrants a finding in favor of the insurance company." *Id.*, citing *Kay v. Occidental Life Ins. Co.*, 28 Wn. 2d 300, 302, 183 P.2d 181 (1947)

<sup>115</sup> Exs. 158 and 60.

<sup>116</sup> RP 10/7/13 at 510:12-512:5 (Petersen); Ex. 221.

area she referred to as a “kitchen” was a space off an empty storage room that contained a sink and possibly a dishwasher – not a \$600,000 commercial grade kitchen.<sup>117</sup>

The only contrary evidence consisted of Graff’s testimony, in which he claimed to have seen the kitchen at a time when the uncontroverted evidence shows he could not possibly have seen it;<sup>118</sup> and the Murphy testimony, which relied on the information Murphy obtained from NBL’s Yates. After demanding \$600,000 from Pacific for a commercial kitchen in 2009, the same Yates testified in October 2013 that he never really had a good idea what the kitchen looked like or what it contained. His testimony merely confirmed there was never any sound basis for NBL’s commercial kitchen claim – and did not establish that NBL acted in good faith by making that claim.<sup>119</sup>

The jury nevertheless found that NBL did not intentionally misrepresent its collapse damage claim – but its finding was colored by

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<sup>117</sup> RP 10/9/13 at 896:8-14 and 949:2-12 (Everett); Ex. 127.

<sup>118</sup> This testimony should be given no weight at all, because it is implausible on its face. *See, e.g., Marshall v. AC&S, Inc.*, 56 Wn. App. 181, 782 P.2d 1107 (1989) (medical records and other evidence established that the plaintiff had been advised of his asbestos-related disease many years before he filed suit; his declaration, offered in opposition to the defendant’s motion for summary judgment based on the statute of limitations, failed as a matter of law to create a question of fact).

<sup>119</sup> Yates’ testimony is much like the testimony of the insured in *Cox*, who claimed he might have made an error when he told the insurer he had lost a number of valuable art works in a fire, and attempted to blame his error on the insurer’s alleged failure to assist him in preparing his inventory of lost and damaged property. The Supreme Court rejected that testimony as insufficient to rebut the insurer’s misrepresentation claim. *Cox*, 110 Wn.2d at 646; *Ki Sin Kim*, 153 Wn. App. at 357-358. Yates’ testimony is insufficient as well. If Yates truly did not recall the layout and contents of the kitchen, on what basis did he authorize his attorneys in 2009 to demand that Pacific pay \$500,000 to restore property that he could not document and could not recall, and to sue Pacific for breach of contract days later?

irrelevant and highly prejudicial testimony and argument that told the jury NBL would suffer a terrible fate if it did find, consistent with the instructions and the evidence, that a misrepresentation had been made.<sup>120</sup>

The jury was told that if it found a misrepresentation, NBL could lose its coverage and be compelled to return insurance proceeds to Pacific. There was no viable rationale for allowing the jury to consider the possible legal consequences of their fact-finding; and there was every reason not to allow the jury to consider those legal consequences.

The admission of testimony<sup>121</sup> and argument<sup>122</sup> concerning the legal consequences of the jury's fact-finding on the misrepresentation question was prejudicial and confusing – for example, did the jurors believe NBL would be required to return what Pacific paid for the collapse loss, or did they conclude NBL might be required to repay the \$5.5 million Pacific paid for the combined fire and collapse losses? Any effort to clarify the consequences of

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<sup>120</sup> Instructions 13, 14 and 15; *see, e.g., Johnson v. Safeco Ins. Co. of Am.*, 178 Wn.App. 828, 316 P.3d 1054 (2013), *rev. denied*, 180 Wn.2d 1006, 321 P.3d 1207 (2014) (insured forfeited claims for breach of contract and extracontractual claims as a result of misrepresentation of his “additional living expense” damages); *Ki Sin Kim v. Allstate Ins. Co.*, 153 Wn.App. 339, 354-356, 223 P.3d 1180 (2009) (insured need only make one material misrepresentation in making its claim to void all coverage under the policy); *Johnson v. Allstate Ins. Co.*, 126 Wn.App. 510, 108 P.3d 1273 (2005) (once insurer established that insured misrepresented her claim, it was not required to prove “causation,” because “the question of causation has nothing to do with whether [the insured] complied with the contract”); *Tornetta v. Allstate Ins. Co.*, 94 Wn.App. 803, 810–11, 973 P.2d 8, *rev. denied*, 138 Wn.2d 1012, 989 P.2d 1143 (1999) (insured who attempted to recover for personal property not stolen during a theft was barred from asserting contract and extracontractual claims); *Wickswat v. Safeco Ins. Co.*, 78 Wn.App. 958, 904 P.2d 767 (1996) (jury properly instructed not to consider plaintiff's claims for coverage and extra-contractual claims if it first found that insured breached “concealment or misrepresentation” provision of policy); *Onyon v. Truck Ins. Exch.*, 859 F.Supp. 1338, 1341 (W.D.Wash.1994) (insured may not defeat misrepresentation defense by backtracking after being notified the insurer has discovered the truth).

<sup>121</sup> RP 10/1/13 at 4:22-41:16.

<sup>122</sup> *Id.*

a finding that NBL misrepresented its claim would only have placed additional emphasis on evidence and argument that was already fraught with peril for Pacific.

In analogous circumstances, our appellate courts have found that it is reversible error to permit the jury to consider the legal consequences of its verdict. For example, in *State v. Townsend*, our Supreme Court noted that in criminal cases a “strict prohibition against informing the jury of sentencing considerations ensures impartial juries and prevents unfair influence on a jury's deliberations.”<sup>123</sup> While this is not a criminal matter, our case presents the same need to ensure an “impartial jury” and to “prevent unfair influence on a jury’s deliberations.” The jury was asked to determine, as a question of fact, whether NBL committed misconduct in the presentation of its insurance claim – and then was told what the “sentence” would be if it found NBL acted wrongfully. The verdict – in the face of overwhelming evidence that negates the verdict – demonstrates that the jury was not impartial and was under “unfair influence.”

The trial court reasoned that NBL’s motivation to misrepresent could well be affected by the knowledge of the potential for forfeiture of coverage if its misrepresentation were discovered – but that rationale for permitting the jury to consider the legal consequences of its fact finding was not only contrary to *Townsend*, it was inconsistent with the facts. NBL’s key misrepresentations concerning the alleged commercial kitchen were made in

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<sup>123</sup> 142 Wn.2d 838, 846, 15 P.3d 145 (2000).

February 2009 – when NBL made its pre-suit demand. There is no evidence to show that in February 2009, or at any time before Pacific asserted its affirmative defense in July 2013, NBL was aware of the misrepresentation provisions of the insurance policy, or of the risks the *Cox* decision would pose in the event a misrepresentation could be proven.<sup>124</sup>

By asserting its affirmative defense, Pacific changed just one thing: the potential legal consequences if NBL could not meet its burden to prove the \$600,000 commercial kitchen it demanded that Pacific pay for actually existed and was damaged when the collapse occurred in June 2005. The jury's proper role was to find the facts. The determination of the legal consequences of the jury's factual findings was for the trial court alone.

The trial court abused its discretion by allowing testimony and argument concerning the legal consequences of a misrepresentation to taint the jury's proper function as the finder of fact.<sup>125</sup>

The court's error prevented NBL from obtaining a fair trial of its affirmative defense under *Cox*. The error also provided further support for NBL's argument that Pacific acted in bad faith, and violated IFCA, by asserting its *Cox* defense. The trial court should have granted Pacific's

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<sup>124</sup> And interestingly enough, after Pacific asserted its misrepresentation defense, NBL drastically reduced its claim for restoration of the kitchen. Exs. 76 and 158 .

<sup>125</sup> ER 408; CR 59(a)(1) and (7)-(9). The criterion for testing abuse of discretion, when evidence that is highly prejudicial and not probative has been presented to the jury, is: "[H]as such a feeling of prejudice been engendered or located in the minds of the jury as to prevent a litigant from having a fair trial?" *Moore v. Smith*, 89 Wn.2d 932, 942, 578 P.2d 26 (1978) (quoting *Slattery v. City of Seattle*, 169 Wash. 144, 148, 13 P.2d 464 (1932)). *See also Palmer v. Jensen*, 132 Wn.2d 193, 197, 937 P.2d 597 (1997) ("A much stronger showing of abuse of discretion will be required to set aside an order granting a new trial than an order denying one because the denial of a new trial 'concludes [the parties'] rights'").

motion for a mistrial. Having decided to revisit the issues after the jury returned its verdict, the court should have granted a new trial after the jury verdict.

The case should be remanded for retrial of the bad faith claim and the misrepresentation defense.<sup>126</sup>

## **VI. CONCLUSION**

The jury conclusively found that NBL failed to prove the elements of its IFCA claim. Judgment should be entered for Pacific on that claim.

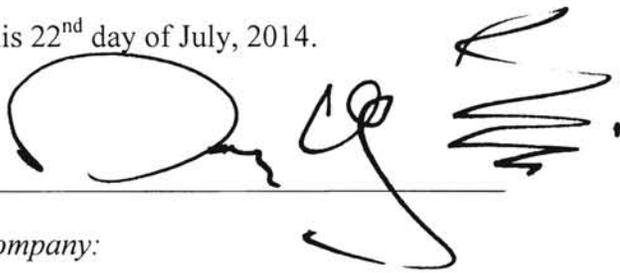
The trial court's failure to instruct the jury concerning Pacific's duties under *Cox*, and its error in permitting the jury to consider the legal consequences of its findings of fact on Pacific's misrepresentation defense, prevented fair trial of Pacific's *Cox* defense and of NBL's common law bad faith claim. This Court should order a new trial of the common law bad faith claim and the *Cox* defense.

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<sup>126</sup> The grant of a new trial does not require retrial of the entire case, when the jury has returned a special verdict as to each of several causes of action. CR 59(a) expressly states that a new trial may be granted to "all or any of the parties and *on all or part of the issues when such issues are clearly and fairly separable and distinct.*" See Tegland, 15 *Washington Rules Practice – Civil*, §38.26 (2013) (addressing "partial new trial" under CR 59); *Crawford v. Miller*, 18 Wn. App. 151, 566 P.2d 1264 (1977) (retrial of liability issues is proper when the jury's damages award is within a reasonable range and not affected by errors at trial); *McCurdy v. Union Pac. R. Co.*, 68 Wn. 2d 457, 413 P.2d 617 (1966) (a retrial is required only as to issues affected by errors at trial); *Cote v. Allen*, 50 Wn. 2d 584, 313 P.2d 693 (1957) (where trial court errors did not affect jury determination of liability, the trial court properly limited new trial to damages); *Cramer v. Bock*, 21 Wn.2d 13, 149 P.2d 525 (1944) (where jury returns special verdict as to separate causes of action, retrial may properly be limited to causes of action affected by errors in original trial of the case).

Respectfully submitted this 22<sup>nd</sup> day of July, 2014.

By \_\_\_\_\_

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*Counsel for Pacific Indemnity Company:*

John D. Wilson, Jr., WSBA #4828  
David M. Jacobi, WSBA #13524  
WILSON SMITH COCHRAN DICKERSON  
901 Fifth Avenue, Suite 1700  
Seattle, Washington 98164-2050  
Tel: 206.623.4100  
Electronic Mail: [wilson@wscd.com](mailto:wilson@wscd.com); [jacobi@wscd.com](mailto:jacobi@wscd.com)

No. 71214-4-I

COURT OF APPEALS  
OF THE STATE OF WASHINGTON  
DIVISION ONE

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NO BOUNDARIES, LTD., a Washington corporation, and NBL II,  
LLC, a Washington limited liability company,

Respondents/Cross-Appellants

v.

PACIFIC INDEMNITY COMPANY (a member of the CHUBB GROUP  
OF INSURANCE COMPANIES), an insurer authorized by the  
Washington Insurance Commissioner,

Appellant/Cross-Respondent

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***CERTIFICATE OF SERVICE***

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*Counsel for Appellant, Pacific Indemnity Company:*

David M. Jacobi, WSBA #13524  
John D. Wilson, Jr. WSBA #4828  
WILSON SMITH COCHRAN DICKERSON  
901 Fifth Avenue, Suite 1700  
Seattle, Washington 98164-2050  
Telephone 206.623.4100  
Facsimile 206.623.9273  
Email [jacobi@wscd.com](mailto:jacobi@wscd.com); [wilson@wscd.com](mailto:wilson@wscd.com)

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**CERTIFICATE OF SERVICE BY LEGAL MESSENGER**

I, Natasha Johnston, certify that I caused to be served a copy of the Opening Brief Of Appellant Pacific Indemnity Company, via ABC Legal Messenger, on the 22nd day of July, 2014, to the following counsel of record at the following address:

Katie Smith Matison  
Ryan McBride  
Lane Powell PC  
1420 Fifth Ave, Suite 4200  
Seattle, WA 98111-0402

DATED at Seattle, Washington this 23 day of July, 2014.

  
\_\_\_\_\_  
Natasha Johnston, Legal Assistant