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COURT OF APPEALS  
DIVISION II

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STATE OF WASHINGTON

No. 40231-9-II

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

*Cl*  
DEPUTY

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COMMUNITY ASSOCIATION UNDERWRITERS OF AMERICA,  
INC. ("CAU")  
a/s/o Harbour Commons, A Condominium

Appellant,

v.

HAROLD E. KALLES and DEBORAH L.  
KALLES, husband and wife, DEREK KALLES and "JANE DOE"  
KALLES (if married); and MICHAEL QUINN and "JANE DOE"  
QUINN, (if married); and LEASE POLICE, INC., a Washington  
corporation,

Respondents.

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*Reply* BRIEF OF APPELLANT

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## INTRODUCTION

Lease Police, a tenant at the Harbour Commons Condominiums, is not an implied co-insured under the insurance policy carried by the Harbour Commons Condominium Association (hereinafter “Association”). Thus, CAU, the Association’s insurer, is not prohibited from subrogating against Lease Police. The arguments set forth in Lease Police’s Brief apply to the typical landlord-tenant situation, which is not in play in the instant matter. This fact is underscored by Lease Police’s repeated contention that the only relevant document that establishes the “reasonable expectations” of the parties is the lease agreement between Lease Police its landlord, viz. Paul and Kathy Elkins (hereinafter the “Elkinses”). But the Association is plainly not a party to the lease. Therefore, it is impossible for the Association’s “reasonable expectations” to be set forth in the lease. Likewise, it is impossible that Lease Police’s expectations can be considered reasonable if it had expectations of being a co-insured on the Association’s policy

Though the anti-subrogation rule adopted in *Cascade Trailer Court v. Beeson*, 50 Wn. App. 678, 749 P.2d 761 (1988) is applicable as between a landlord and a tenant, there is no basis to apply it as between CAU as subrogee of the Association and Lease Police, i.e. a tenant. Accordingly,

the Superior Court erred in granting Lease Police's Motion for Summary Judgment.

In addition, Lease Police is not entitled to attorney fees in the underlying action. Whatever its reasonable expectations, Lease Police did not bargain for the benefit of insurance coverage. Hence, CAU should be entitled to litigate its position – successfully or unsuccessfully – without being subject to attorney fees under the *Olympic Steamship* rule. To hold otherwise would be contrary to the equitable principles set forth in *Olympic Steamship* and its progeny. Accordingly, the Superior Court also erred in granting Lease Police's Motion for Award of Attorneys' Fees.

### **REPLY TO STATEMENT OF THE CASE**

For purposes of brevity, CAU relies on its Statement of the Case as set forth in its Opening Brief.

### **REPLY ARGUMENT**

#### **A. Lease Police is not a co-insured under the Condominium Association's insurance policy and CAU's subrogation claim is not barred.**

##### **1. Lease Police's reliance on the holding in *Cascade Trailer v. Beeson* and the lease agreement is misplaced.**

Lease Police's argument is simple, but flawed. It contends that because the lease between the Elkinses and Lease Police did not require Lease Police to obtain fire insurance, Lease Police must be an implied co-

insured under the Elkinses' insurance policy. It is undisputed that this general proposition was adopted and explained in *Cascade Trailer Court v. Beeson*, 50 Wn. App. 678, 749 P.2d 761 (1988), a case that involved a typical residential landlord-tenant relationship. It is further undisputed that, here, Lease Police is attempting to expand the holding in *Cascade* beyond that landlord-tenant context so as to bar subrogation claims against tenants by insurers of condominium associations. Thus, Lease Police argues that not only is it a co-insured on the Elkinses' insurance policy, it is also a co-insured on the insurance policy obtained by the Association (under which not even the Elkinses are covered). Despite Lease Police's arguments to the contrary, neither the holding in *Cascade*, nor the lease agreement, nor the Association's Declaration support this contention.

In *Cascade*, the court summed up the rationale of its holding in a few sentences by stating:

Whether rent covers all of a landlord's expenses, including insurance premiums is not the critical question. Rather, the issue concerns the parties' reasonable expectations. Where the landlord has secured fire insurance covering the leased premises, the tenant can reasonably expect the insurance to cover him as well, unless the parties have specifically agreed otherwise. **Why? – because the tenant is in privity of contract with the landlord, and he has a property interest in the premises the insurance protects.**

*Id.* at 686. (emphasis added).

In these few sentences, the court not only established the “reasonable expectations” analysis, it also explained why the analysis is proper – “because the tenant is in privity of contract with the landlord.” *Id.* The privity element is absent in the instant case between the Association and Lease Police. In addition, where the court mentions that “[the tenant] has a property interest in the premises the insurance protects,” it is referring to the landlord’s insurance. *Id.* at 681. Here, the insurance in question is not that of the landlord.

But as to the court’s primary point, it bears restating that CAU’s insured (the Association) was not a party to the lease agreement; therefore no privity exists between the Lease Police and CAU’s insured. Here, CAU provided insurance to the Association, the owner of the entire buildings and common areas; however, Lease Police does not have a contractual relationship with CAU’s insured. In fact, Lease Police’s only relationship is with the Elkinses, who – as the owners of the leasehold – are mere members of the Association, and not the Association itself. Thus, since the rationale behind the holding in *Cascade* was the element of privity, and since no privity exists in between CAU’s insured and Lease Police, the Superior Court extend without basis the holding in *Cascade* beyond the landlord-tenant setting by applying that holding’s anti-subrogation effect to a condominium association’s insurer.

Moreover, Lease Police's reliance on the provisions of the lease agreement between the Elkinses and Lease Police is improper. The Association was not a contracting party to the lease; therefore the Association is not bound by its terms. In other words, the Elkinses and Lease Police negotiated the terms of the lease, which does not bind the Association, as neither party has the power to do so. The absence of a provision in the lease requiring Lease Police to obtain property insurance only bars subrogation by the Elkinses' insurance carrier in accordance with the holding in *Cascade*. The Elkinses are not insureds under CAU's insurance policy – only the Association is. Therefore, CAU is not barred from subrogating against Lease Police.

**2. The holding in *Cascade* should not be extended beyond landlord – tenant situations to bar subrogation claims by insurers of condominium associations.**

Lease Police misinterprets CAU's argument. Whether or not the holding in *Cascade* extends to a commercial lease, was not squarely addressed in *Cascade*. Although it is noted in the *Cascade* opinion that the superior court “adopt[ed] a rule that in a residential landlord/tenant situation, absent an express agreement to the contrary, a lessor's insurer cannot be subrogated to any rights against a tenant for negligently causing a fire.” *Cascade, supra*, at p. 680 (emphasis added). On appeal, the appellate court adopted the holding in *Sutton v. Jondahl*, 532 P.2d 478

(Okla. Ct. App. 1975), and applied same to the factual scenario at issue, which involved a residential landlord-tenant situation. To the extent, the holding in *Cascade* can be extended to a commercial landlord-tenant situation is irrelevant. Rather, CAU argues that *Cascade* should not be extended beyond the landlord-tenant situation by making it apply to third parties, such as condominium associations. Specifically, CAU argues that Lease Police cannot be considered an implied co-insured under CAU's insured's fire insurance policy based on the terms and conditions of a lease to which CAU's insured's is not a party. That is, because the Elkinses failed, for whatever reason, to advise Lease Police to obtain fire insurance and/or because the Elkinses misunderstood the coverage provided by the Association's policy, it is of no moment to CAU's insured.

It should be noted that condominiums present a more complex setting than the typical single-family residence at issue in *Cascade*. Condominiums are comprised of multiple individual units – privately owned – as well as shared common areas owned by all the unit owners and governed by an association. This differs from the scenario in *Cascade*, which deals with an owner of an undivided and/or shared real property interest leasing to a tenant where the parties are in privity of contract and estate, and their intentions can be memorialized in the lease agreement. Applying the holding in *Cascade* to condominium associations abandons

the privity rationale at the heart of the *Cascade* decision. Thus, CAU respectfully requests that this Honorable Court reverse the Superior Court's Order granting Lease Police's Motion for Summary Judgment, and remand the matter for further proceedings consistent with a fair interpretation of applicable law, i.e. that a condominium's insurer can subrogate against a unit owner's tenant.

**3. None of the provisions of the Condominium Declaration cited by Lease Police can be interpreted that the Association's fire insurance policy would benefit the negligent tenant of a unit owner.**

Despite Lease Police's assertion to the contrary, the provisions of the Declaration cited in Lease Police's Brief, do not establish that the Association expected that tenants of unit owners would be protected by the insurance it procured for the condominium. Lease Police repeatedly states that the Elkinses obtained insurance through the Association because the insurance was required to obtain fire insurance for the condominium, as trustees of the unit owners. However, this is a misinterpretation of the Declaration. Clearly, the Association's obligation to obtain insurance for the condominium is a requirement under the Washington Condominium Act. *See* RCWA 64.32.352. Thus, merely because the Declaration requires the Association to obtain fire insurance

for the condominium is not a sufficient indication that the insurance policy would benefit a unit owners' tenant.

As Lease Police points out in its brief, the Declaration permits unit owners to lease their units. However, nowhere in the Declaration does it state that the insurance obtained by the Association would benefit unit owners' tenants. In fact, the Declaration provision requiring the Association to obtain fire insurance coverage for the benefit of the condominium, Article XIII, paragraph 1(a), is silent with respect to unit owners' tenants. (CP 66). This is a clear indication that the Association did not intend to obtain insurance for unit owners' tenants.

Furthermore, whether the insurance policy was paid for out of a common expense fund, or whether the Association's Board could collect monthly fees from a unit owner's tenant if the unit owner failed to timely pay, is irrelevant to demonstrate that the Association had a reasonable expectation that the insurance it obtained for the condominium would protect a unit owner's tenant. In fact, the court in *Cascade* dismissed this issue stating "whether rent covers all of the landlord's expenses, including insurance premiums, is not the critical question." See *Cascade Trailer, supra*, 50 Wn. App. 678, 686. Thus Lease Police's reliance on same to support its conclusion that Lease Police was a co-insured under the Association's insurance policy is misguided.

**B. Lease Police is not entitled to attorney fees under the holding of *Olympic Steamship*.**

The issue presented in the instant case is not a typical coverage issue in the usual sense. That is, Lease Police is not seeking coverage under CAU's insured's insurance policy. It seeks only status as an implied co-insured for purposes of barring a subrogation claim. In other words, this case does not involve "a suit between an insurer and its insured to obtain the benefit of an insurance policy or contractual obligation" at all. Rather, this case merely concerns CAU's right of subrogation against an allegedly negligent third-party tenant. For this reason, *Leingang v. Pierre County Medical Bureau, Inc.*, 131 Wn.2d 133, 930 P.2d 288 (1997) is inapplicable. Thus, not only are the equitable principles set forth in *Olympic Steamship* and its progeny not present in the instant case, *Olympic Steamship* fees are not warranted since this is not a dispute about coverage.

Moreover, to the extent that *Olympic Steamship* fees are applicable, with CAU denies, Lease Police failed to establish, or even address, the existence of a fiduciary relationship or an enhanced duty between CAU, the Association, and Lease Police. See *McGreevy v. Or. Mut. Ins. Co.*, 128 Wn.2d 26, 36, 904 P.2d 731 (1995) ("a court's award of *Olympic Steamship* attorney fees are an equitable remedy, based on the

“special fiduciary relationship ... existing between an insurer and insured.”). Thus, the award of *Olympic Steamship* fees is not warranted here.

Further, *Butzberger v. Foster*, 151 Wn.2d 396, 89 P.3d 689 (2004) is distinguishable from the case at bar. In *Butzberger*, Butzberger was killed while attempting to rescue a driver from an overturned vehicle. *Id.* at 399. Butzberger’s estate brought an action to recover underinsured (UIM) under the policy covering the overturned truck and the vehicle he was driving to the scene. *Id.* at 400. The Supreme Court of Washington held that Butzberger was covered under both policies and awarded attorneys fees from both vehicles’ insurance companies. *Id.* at 413. However, Butzberger is distinguishable from the situation here because, under Washington law, UIM coverage is mandated by statute. As the court stated:

The statutory policy of Washington’s UIM statute vitiates any attempt to make the meaning of insured for purposes of uninsured motorist coverage narrower than the meaning of that term under the primary liability section of the policy. *Rau v. Liberty Mut. Ins. Co.*, 21 Wn.App. 326, 328-329, 585 P.2d 157 (1978). Therefore, Butzberger, who was not a named insured on either policy at issue, is entitled to UIM coverage if he was using Foster’s truck at the time of his death and/or if he was using the vehicle he had been driving.

*Id.* at 401-402.

Thus Butzberger, regardless of whether he was a named insured on a policy, was deemed a named insured by operation of the UIM statute. *Id.* In the instant case, there is no such statutory provision mandating that Lease Police is entitled to coverage under CAU's insured's policy.

Finally, Lease Police's reliance on *American Best Food, Inc. v. Alea London*, 168 Wn.2d 398, 229 P.3d 693 (March 18, 2010) is erroneous. In *American Best*, the insured nightclub brought an action against its liability carrier. This action arose out of the carrier's failure to defend the nightclub in a lawsuit brought by an injured patron. *Id.* at 402 – 403. On appeal at issues were: (1) whether a complaint alleging that post-assault negligence caused or exacerbated injuries falls under an insurance policy's assault-and-battery exclusion; and (2) whether an insurer breached its duty to defend as a matter of law, when – relying upon an interpretation of equivocal case law – it gave itself the benefit of the doubt rather than give that benefit to its insured. *Id.* The court found in the affirmative on both issues, reasoning that an insurer may defend under a reservation of rights and may seek declaratory relief.

Obviously, *American Best* involves the general insured-insurer relationship not present in the instant case. Moreover, the insurer had, but failed to exercise, the option of defending under a reservation of rights. Here, CAU did not have that option. Moreover, CAU did not give itself

the benefit of the doubt over Lease Police, as it had no privity of contract with Lease Police and no identifiable method – other than through motion practice – to challenge Lease Police’s assertion that it was an implied co-insured under the Association’s policy. Although the issues in *American Best* had not been previously litigated, the liability insurer had an opportunity to defend its insured while challenging the coverage issue in a declaratory action. No such possibility was available to CAU.

Accordingly, the Superior Court erred in granting Lease Police’s motion requesting attorney fees pursuant to *Olympic Steamship*. CAU respectfully requests that this Honorable Court reverse the Superior Court’s order granting Lease Police attorney fees.

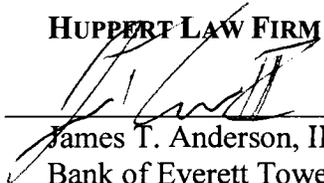
### **CONCLUSION**

For the reasons stated above and set forth in Appellant’s Opening Brief, this Court should reverse.

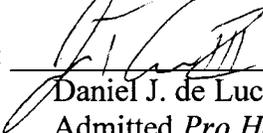
**RESPECTFULLY SUBMITTED** this the 23<sup>rd</sup> day of September 2010.

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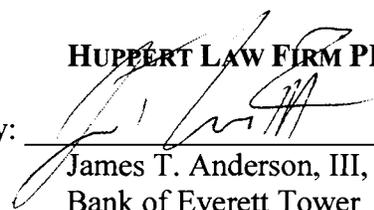
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