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No. 55342-9-I

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

MUTUAL OF ENUMCLAW INSURANCE COMPANY,

Appellant/Cross-Respondent

v.

DAN PAULSON CONSTRUCTION, INC., a Washington
corporation, KAREN and JOSEPH MARTINELLI, and the
marital community composed thereof,

Respondents/Cross-Appellants

BRIEF OF RESPONDENTS/CROSS-APPELLANTS
KAREN AND JOSEPH MARTINELLI

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I. REPLY TO APPELLANT’S ASSIGNMENTS OF ERROR

1. Rebuttal to Appellant’s Assignment of Error 1:

Mutual of Enumclaw (“MOE”) unreasonably interfered in its insured’s defense, causing actual harm to the insured. The trial court correctly concluded that MOE’s interference breached its duty of good faith.

Rebuttal to Issues Pertaining to Appellants’ Assignment of Error 1:

a. Does an insurer, defending an insured under a reservation of rights, breach its duty of good faith when it interferes in its insured’s defense?

b. Is the trial court’s summary judgment ruling, that MOE did not rebut the *Safeco Insurance v. Butler*, 118 Wn.2d 383, 823 P.2d 499 (1992) presumption of harm, the law of this case because the appellant did not assign error to or separately brief that holding?

c. Does the *Butler* bad faith remedy of estoppel to deny coverage depend on the “category” of the insurer’s bad faith, or the size or nature of the harm caused by the insurer’s bad faith?

2. Rebuttal to Appellant’s Assignment of Error 2:

The trial court correctly upheld the reasonableness of the stipulated arbitration award. The trial court held that MOE failed to support its affirmative defense of fraud or collusion under *Truck Ins. Exch. v. Vanport*

Homes, 147 Wn.2d 751, 58 P.3d 276 (2002). MOE does not assign error to that decision. The stipulated arbitration award is thus presumptively reasonable. Substantial evidence also supported the trial court's determination of reasonableness and, as a third alternative, enforcement of the arbitrator's finding of reasonableness, confirmed by the Superior Court, does not offend due process under *Red Oaks Condominiums*, __ Wn.App. __, __ P.3d __, 2005 WL 1799278 (2005).

Rebuttal to Issues Pertaining to Appellant's Assignment of Error 1:

- a. Is the trial court's determination that MOE did not carry its burden to show evidence of fraud or collusion the law of this case as MOE did not assign error to or brief the trial court decision on this issue?
- b. If an insurer acts in bad faith and then fails to rebut the presumption of harm, is the insured's stipulated arbitration award presumptively reasonable under *Vanport Homes*?
- c. Did MOE meet its burden of proof on summary judgment to prove fraud or collusion in connection with the covenant judgment between MOE's insured and the Martinellis?
- d. May MOE argue for the first time on appeal that the trial court should have "enunciated" its reasonableness analysis? RAP 9.12.
- e. Findings of fact and conclusions of law are superfluous to

summary judgments. Did the trial court err by not “enunciating” its reasonableness analysis in its summary judgment ruling?

f. Has MOE shown a genuine issue of fact concerning reasonableness?

g. Is MOE bound by the determination of reasonableness in the arbitration and confirmation proceedings because it chose not to intervene?

3. Rebuttal to Appellant’s Assignment of Error 3:

Under the circumstances, the trial court did not abuse its discretion when it deferred allocation of the burden of proof for specific damage claims under Exclusion L until the parties conduct discovery concerning the facts related to those claims.

Issues Pertaining to Appellant’s Assignment of Error 3:

a. Did the trial court abuse its discretion when it deferred ruling on MOE’s burden of proof argument pending further discovery?

b. Even if the trial court abused its discretion, has MOE demonstrated an entitlement to summary judgment concerning application of Exclusion L in the context of this particular case?

4. Rebuttal to Appellant’s Assignment of Error 4:

MOE’s insurance policy contractually obligated MOE to indemnify its insured against interest included in the judgment against the insured. CP 969

¶3. The trial court correctly enforced MOE's indemnification obligation at the contract interest rate.

5. The Martinellis Should Recover Their Attorney Fees:

Respondents should recover their attorney fees on appeal. RAP 18.1.

Issues Pertaining to Assignment of Error:

a. Is the Martinellis' right to recover attorney fees the law of this case because MOE did not assign error to or brief the trial court fee award?

b. Are insureds entitled to recover attorney fees in actions to enforce the benefit of the insurance contract and/or in bad faith actions?

II. ASSIGNMENT OF ERROR ON CROSS-REVIEW

Washington insurers must "effectuate prompt payment of property damage claims to innocent third parties in clear liability situations." WAC 284-30-330(6). Did the trial court err when it held that MOE may indefinitely evade application of WAC 284-30-330(6) and WAC 284-30-370 as to *all* property damages if it contests coverage as to *some* of the damage items?

III. REBUTTAL STATEMENT OF THE CASE

A. Rebuttal Statement of Facts

Mr. and Mrs. Martinelli contracted with Dan Paulson Construction, Inc. ("DPCI"), to construct a new residence overlooking Haro Strait on San

Juan Island. CP 1 ¶2, CP 49. Mutual of Enumclaw had issued a Comprehensive General Liability (CGL) insurance policy to DPCI. CP 1 ¶1, 215-6. Due to numerous construction defects, Mr. and Mrs. Martinelli filed a demand for arbitration against DPCI with the American Arbitration Association (“AAA Arbitration”) on August 29, 2002, as required under their contract.¹ CP 1 ¶3, CP 44-5, CP 52. Mutual of Enumclaw assigned counsel to defend DPCI in the arbitration proceeding under a reservation of rights. CP 1 ¶4, 55-6. Mutual of Enumclaw agrees that “some of the damage claimed against Dan Paulson Construction, Inc. is covered by the Mutual of Enumclaw policy,” but asserts that some of those damages are not covered. CP 2 ¶6, CP 86 (Dep. of MOE coverage counsel, p. 152:2-14). MOE also agrees that “DPCI’s policy covered liability legally imposed on DPCI for property damage at the Martinelli’s residence caused by the work of DPCI’s subcontractors.” CP 93 (Answer to Int. no. 14). MOE’s coverage counsel acknowledged that Martinelli’s “stigma” claim would fall within MOE’s coverage. CP 66-67 (pp. 60:21-61:2, 64:1-5), CP 97 (MOE internal

¹ MOE refers to “some delays” in the arbitration. App. Br., p. 5. DPCI filed a declaratory judgment action to enjoin the arbitration, San Juan County Superior Court Case no. 02-2-05152-0. When that failed, it filed a petition for discretionary review in Division I, Case No. 51515-2-I, that also failed. The initial arbitrator was then disqualified for a conflict of interest.

memorandum: “coverage counsel believes that this type of claim would be covered under the policy”), CP 103.² The Martinelli’s expert opined that the stigma damages, alone, totaled \$800,000. CP 106.³

The Martinellis and DPCI were scheduled to commence arbitration on January 6, 2004, before AAA Arbitrator J. Richard Manning, Esq. CP 108. Mutual of Enumclaw complains that it “requested permission from Paulson to be allowed to intervene in the arbitration” but its request was “rebuffed.” App. Br., p. 10. MOE *never* moved to intervene. MOE also complains (App. Br., p. 10) that it asked DPCI for permission to “have its insurance coverage attorney attend the arbitration,” but that DPCI “specifically rejected” that request. App. Br., p. 10. Pursuant to AAA Rule R-24, MOE could have asked the Arbitrator for permission to attend the arbitration but it did not.

² MOE also insured one of DPCI’s subcontractors, Dave Koch (a stone mason), against whom DPCI asserted a third party demand. CP 555, 558-64. The MOE adjuster handling DPCI’s claim *against* Koch also “included money for a possible ‘stigma’ claim.” CP 102-3.

³ MOE incorrectly states (*e.g.* App. Br., p.4) that the Martinellis alleged “the exact same alleged construction defects” against both Paulson Construction and the Martinellis’ architects. *E.g.*, CP 399 n.2, 401-3 (explaining numerous differences). Appellant’s Brief does not explain the relevance of this purported “fact,” although this issue was extensively briefed and decided in the arbitration proceeding *before* the Arbitrator found the stipulated arbitration award reasonable. CP 343. Although this issue is not relevant to this appeal, MOE also did not submit any evidence to satisfy its burden of proof. See, *Puget Sound Energy, Inc. v. Alba Gen’l Ins Co.*, 149 Wn.2d 135, 141, 68 P.3d 1061 (2003)(party urging double recovery has the burden of establishing what part of the settlement was attributable to the claim it seeks to offset); *Sound Built Homes v. Windermere*, 118 Wn.App. 617, 634, 72 P.3d 788 (2003)(apportionment does not exist to allow a party to avoid paying its rightful share); *Weyerhaeuser v. Comm’l Union Ins. Co.*, 142 Wn.2d 654, 672, 15 P.3d 115 (2000)(claimant must be fully compensated before any setoff is allowed). The arbitrator agreed with the Martinellis’ analysis. CP 343.

CP 75 (104:8-13), 445.

In November, 2003 (more than a year after the arbitration had been filed), MOE filed a declaratory judgment action against DPCI and the Martinellis in San Juan County Superior Court, but did *not* serve the complaint. CP 121.⁴ During the interim, both the insured and the Martinellis had *fully cooperated* by providing MOE with *all* of the information it requested. For example, in late July and August, 2002, MOE requested information which DPCI and the Martinellis promptly provided and made available to MOE's claims representative. CP 56, 441-2, 448-450 ¶¶3-8, 452.

However, MOE was quite concerned about copying costs and duplication of documents provided by both DPCI and the Martinellis, so MOE chose not follow through beyond what DPCI provided it. CP 395 ¶4, 448-50 ¶¶4-8.

A year later, in August, 2003, MOE again requested documents from DPCI. CP 333-4. **MOE's coverage counsel confirmed that DPCI gave him the documents he requested in September, 2003, and that MOE never asked for anything more.** CP 64-65 (53:17-54:19; 55:16-56:15), 333-4, 344-46. See further, CP 513-4 (27:23-28:6). MOE's innuendo to the contrary (App. Br., pp.7-9) thus omits material, uncontroverted evidence.

⁴ MOE invoked privilege rather than allow its coverage counsel to explain why MOE waited so long to file its declaratory judgment complaint and then decided not to serve that complaint. CP 1084-5 (referenced deposition pages appear at CP 1106, *et seq.*).

MOE filed its declaratory judgment action against the Martinellis and DPCI as the arbitration trial date approached. Despite its later assertion that MOE was “anxious to get this going,” MOE did not serve the complaint. CP 121. MOE instead waited about a month before informing its insured’s counsel on December 15, 2003 that it had filed the complaint and did not tell the Martinellis’ counsel of the filing at all until sending a letter on December 30, 2003. CP 36 ¶4, 121, 123.⁵

On January 2, 2004, *four days prior to start of the scheduled arbitration*, counsel for DPCI and the Martinellis received a copy of a subpoena [Appendix B] issued in San Juan County Superior Court Cause No. 03-2-05168-4, which scheduled a deposition on written interrogatories of Arbitrator J. Richard Manning. CP 7,13 (admitting ¶11 of Martinellis’ Counterclaims), CP 125-7. The subpoena scheduled the Arbitrator’s response date on January 23, 2004. *Id.* Most of the information and documentation sought by the interrogatories and requests for production was readily available from or already provided to MOE by the parties. CP 126-7 (Interr.

⁵ Relying on a January 5, 2004 letter (CP 349), MOE *implies* that it only filed the declaratory judgment complaint after all other efforts to obtain information needed to adjust the claim had failed. App.Br., p.10. That, of course, is obviously untrue considering the Martinellis and DPCI had both provided MOE *all* of the information it had requested *before* the declaratory judgment complaint was filed. See discussion, *supra*, p.7. MOE also incorrectly states DPCI’s attorney “promptly objected to the commencement” of the declaratory judgment action. *Id.* The December 15, 2003 email shows that DPCI did not learn of the declaratory judgment filing until a month later. CP 121.

1-7, 10-11, RFP 1-2). However, the subpoena also sought the Arbitrator's thought processes and analyses, such as which witnesses he found credible, itemization of the arbitration award, and his analysis of which work had been performed by subcontractors. CP 126-7 (Interrogs. 8-9 and 12-17). Mutual of Enumclaw authorized its coverage attorney to subpoena the Arbitrator. CP 72 (90:22-91:8), CP 92 (Answer to Interrog. 9). MOE issued the subpoena to the Arbitrator on December 30, 2003, but delayed sending a copy to the attorneys for DPCI and the Martinellis. CP 13, 73 (96:3-24).

Mutual of Enumclaw's attorneys **also** sent the Arbitrator an *ex parte* [Appendix A]⁶ cover letter which purported to explain DPCI's insurance coverage, informed him that MOE was defending DPCI under a "reservation of Rights," and stated that MOE "needs more information about the basis of your [future] award." CP 7, 13 (admitting Martinelli Counterclaim ¶12), CP 133, 176 (AAA Arbitration Rule R-19(a) re: *ex parte* communications). MOE authorized its attorney to send this letter. CP 72 (90:22-91:8). MOE did *not* send a copy of the letter to counsel for DPCI (*i.e.* Messrs. Flaherty or Jones) or the Martinellis (Gould). CP 7, 13 (admitting Martinelli's

⁶ Without reference to the record, MOE asserts that it "inadvertently sent this cover letter only to the arbitrator." App. Br., p. 30 n. 5. No evidence supports MOE's contention; indeed, MOE invoked privilege to prevent discovery on this precise issue. CP 1132-34 (91:8-93:15), 1137-39 (96:25-98:20). MOE's suggestion of inadvertence is also inconsistent with MOE's admission that it *delayed* sending the parties' counsel copies of the subpoena it had served on the arbitrator. CP 13, CP 73 (96:3-24).

Counterclaims ¶¶11, 12; CP 73 (96:3-24). The parties learned of the letter from the Arbitrator when the arbitration commenced. CP 36-7 ¶21.⁷

AAA, the Martinellis and DPCI immediately demanded that MOE withdraw its subpoena to the Arbitrator, and provided extensive authority to support their positions. CP 75-6 (105:11-106:4), 135-144. The Arbitrator himself telephoned the law partner of MOE's coverage counsel to express his displeasure. CP 13 (admitting Martinelli Counterclaim ¶13), 77-8 (117:1-118:23). When MOE's coverage attorney disclosed his intention to send a *second letter* to the Arbitrator, the Martinellis again protested and urged MOE to *not* engage in any more direct communications with the arbitrator pending AAA Arbitration's retention of counsel to represent the Arbitrator. CP 146-9. MOE refused and sent a *second* letter to the Arbitrator (during the course of the arbitration), abandoning Interrogatories nos. 8-9 and 12-13, but "remind[ing] the parties [and the Arbitrator] that the policy at issue is not first party coverage; it is a *liability* policy, and any obligation that Mutual of Enumclaw may eventually have (other than defense) is based entirely on this Award." CP 151-2.

DCPI's assigned counsel complained to MOE's coverage counsel

⁷ MOE's coverage counsel rationalized he was free to communicate with the arbitrator *ex parte* because MOE was itself "not a party" to the arbitration proceeding. CP 73 (94:7-20). He also admitted that he had found no legal authority to support MOE's *ex parte* communication or subpoena to the arbitrator. CP 77 (115:14-116:21).

about MOE's unilateral interference (CP 155), writing:

The Paulsons wish that they had been consulted before you contacted the arbitrator. They do not understand why you believed that the arbitrator could be legally subpoenaed. They do not understand why this could not have waited until the conclusion of the arbitration or why it could not have been handled through the declaratory judgment action. The Paulsons are afraid that your actions have prejudiced their defense.

DPCI's private counsel also strenuously objected to MOE's counsel, identifying *five* (5) specific objections to MOE's conduct. CP 143-44.

As a result of MOE's interference in the arbitration, DPCI incurred actual, out-of-pocket costs for attorney fees and expenses of its private counsel "to review, research and respond to the subpoena issued by Mutual of Enumclaw to the Arbitrator." CP 531 ¶5; CP 527 (24:1-9). MOE's conduct also caused substantial uncertainty for DPCI, understandably upsetting its owner. CP 512-3 (26:15-27:22), CP 531 *Id.* ¶4, CP 527-8 (24:21-25:10).

MOE justifies its interference in the arbitration because DPCI and the Martinellis had entered into a stipulation for a lump sum arbitration award. CP 31-32, 111-118. MOE says this stipulation "further compromised" MOE's attempt to "timely learn of potentially insured and uninsured components of damages." App. Br., pp. 11-12. MOE did not learn of the DPCI/Martinelli stipulation for a lump sum arbitration award until January 8, 2004 [CP 80 127:12-128:17, referring to CP 146 and 157)], long *after* MOE

sent its *ex parte* correspondence and subpoena to the Arbitrator.⁸ The trial court thus correctly discredited MOE's explanation "because MOE's coverage counsel admitted at deposition that he did not learn of the lump sum stipulation...until he learned of that fact in a letter dated January 8, 2004" and "the subpoena to the arbitrator is dated December 30, 2003." CP 649.

When the Martinellis signaled their intent to seek a protective order, MOE dismissed the Martinellis from the suit. CP 162. MOE later struck the Arbitrator's deposition and dismissed Case no. 03-2-05168-4, but refiled an identical complaint which gives rise to this appeal. CP 1, 164, 166.

In the meantime, the arbitration between the Martinellis and DPCI had progressed. The Martinellis introduced evidence that supported a potential arbitration award of between \$2,350,000 and \$2,670,000. CP 38-40 ¶¶33-34. During the sixth day of the arbitration trial, on January 12, 2004, the parties entered into a Stipulated Arbitration Award (as authorized by AAA Rule R-45 [CP 177]), in the amount of \$1,300,000, plus certain additional, specified relief. CP 26-27 ¶¶3-4, 29-30 ¶¶3-4, 39-40 ¶34, 68-73, 179-80. This Stipulated Arbitration Award resulted from arms-length negotiations among three experienced counsel, including Mr. Jones (assigned by MOE to

⁸ Coverage counsel's January 9, 2004 letter (CP 157) refers to a "recent letter" from the Martinellis' counsel which informed him that the parties to the arbitration had requested a lump sum arbitration award. The "recent letter" to which coverage counsel refers is dated January 8, 2004 and its reference to the lump sum arbitration award appears on CP 148.

represent DPCI), Mr. Flaherty (DPCI's corporate counsel), and Mr. Gould (the Martinelli's counsel). *Id.* The parties submitted the stipulated arbitration award to the Arbitrator, who approved it and expressly found (CP 179):

Based on the testimony of the witnesses, the exhibits and all the material submitted to me during the course of the hearings, I *specifically find* that the sum of \$1,300,000 is a *reasonable award*. [Emphasis added].

Ample evidence supported the Arbitrator's finding of reasonableness. CP 38-40 ¶¶33-34. DPCI's experienced assigned and private counsel both agreed that the settlement was reasonable. CP 27 ¶6, 29-30 ¶4, 39-40 ¶34, 168-173.

The Martinellis then moved to confirm the Arbitration Award which included the arbitrator's finding of "reasonableness." DPCI's assigned counsel notified MOE of that hearing but MOE chose *not* to intervene. CP 30 ¶5. San Juan County Superior Court confirmed the Arbitration Award on February 2, 2004. CP 182-87. That judgment is now final. DPCI also entered into an assignment of its contract indemnification and bad faith claims against MOE, in consideration of which the Martinellis executed a covenant not to execute against DPCI. CP 189-210.

On February 4, 2004, Mr. and Mrs. Martinelli (as assignees of DPCI) made demand upon Mutual of Enumclaw to pay the undisputed, insured portions of damages due under the MOE policy, as required by WAC 284-30-

330(6). CP 2 ¶6, 212. MOE paid nothing. CP 86 (151:20-152:21).⁹

B. Rebuttal Statement Re: Trial Court Proceedings

Mutual of Enumclaw says it “communicated. . . [t]hat coverage totaled \$4,000,000.” App. Br., pp. 5-6, citing CP 325. No such disclosure occurred.

In its trial court summary judgment motion, MOE disclosed *for the first time* that its policy limits were \$4,000,000 rather than \$1,000,000. CP 259, 264, 275-5. MOE’s disclosure of \$4,000,000 in coverage shocked its insured, because MOE had not disclosed that fact. CP 530 ¶2; CP 446 ¶4.¹⁰

In its initial Letter Opinion, the trial court agreed that MOE acted in bad faith when it interfered in the arbitration proceeding, but held that MOE had successfully rebutted the presumption of harm.” CP650-51. The trial court agreed (as had the Martinellis) that MOE did not act in bad faith for failure to settle “within policy limits,” but also held that MOE’s surprise disclosure of \$4MM in available coverage (rather than \$1MM) raised issues

⁹ MOE cites evidence of settlement negotiations and mediation submissions, as it did in the trial court. App. Br., p. 5. This is improper. RCW 5.60.070; ER 408. The Martinellis object, as they did in the trial court. CP 379.

¹⁰ MOE’s failure to disclose DPCI’s correct policy limits constitutes bad faith as a matter of law. *Smith v. Safeco Ins. Co.*, 150 Wn.2d 478, 78 P.3d 1274 (2003); WAC 284-30-330(1). The Martinellis also filed a CR 56(f) motion because of MOE’s extensive privilege claims. CP 1077-95, 1196-99, 1200-13; RP (6/1/04), pp. 28:16-33:18, 43:13-48:25.

“not properly before the court.” CP 652.¹¹

The Martinellis moved for reconsideration, arguing: (1) the trial court had overlooked evidence of *actual* harm to the insured due to MOE’s bad faith, and; (2) the trial court misapplied the *Butler* presumption of harm. CP 657-661. The trial court agreed. CP 690; RP (9/7/04), p. 3. After judgment, MOE appealed and the Martinellis cross-appealed. CP 929, 1020.

IV. SUMMARY OF ARGUMENT

When an insurer unreasonably interferes in its insured’s defense, the insurer impairs a major policy benefit and violates its duty of good faith under *Tank v. State Farm Fire & Casualty Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986). Under *Butler*, Washington remediates insurer bad faith in the third party context, by estopping the insurer from denying coverage unless the insurer rebuts the presumption of harm. The trial court correctly held that MOE acted in bad faith because MOE interfered in its insured’s defense. MOE’s actions were, as found by the Court, actuated by its own self interest

¹¹ With leave of court, the Martinellis amended their answer and counterclaims to more clearly allege this additional bad faith. CP 760-1, 914-21. The trial court summary judgment rulings did not decide these issues, which were stayed pending this appeal. CP 1009-11; RP (12/20/04), pp. 8:9-9:10. MOE nevertheless requests a broad judgment that “MOE is not estopped from denying coverage for the uninsured claim asserted by the Martinellis against Paulson.” App. Br., p. 50; RP (6/1/04), pp. 32:1-36:19. This would be improper because: (a) not briefed and no error assigned by MOE; (b) MOE asserted privilege to prevent discovery (see n. 10, *supra*), and; (c) raised for the first time in the trial court reply. RP (6/1/04), pp. 31:4-33:11, 35:6-36:16. See, *White v. Kent Medical Ctr.*, 61 Wn. App. 163, 1678, 810 P.2d 4 (1991)(improper to raise new issue for the first time in reply); *Smith, supra*, 150 Wn.2d at 486 (summary judgment standards in bad faith litigation).

and in total derogation of the interests of its insured.

The trial court also held that MOE did not rebut the *Butler* presumption of harm. MOE does not assign error to that decision, which represents the law of this case. To circumvent *Butler's* presumption of harm, MOE argues that *Butler's* remedy of estoppel to deny coverage only applies to some “categories” of bad faith. MOE’s theory conflicts with unanimous Washington law to the contrary, which holds that the principles of *Butler* do not depend on **how** an insurer acts in bad faith.

If an insurer acts in bad faith, it may not claim the benefit of the insured’s effort to protect itself. If the insured enters into a covenant judgment, Washington presumes the judgment is reasonable unless the insurer proves fraud or collusion as held in *Vanport Homes*. The trial court held that MOE did not submit evidence of fraud or collusion. MOE does not assign error to that decision, which represents the law of this case. MOE thus did not rebut the presumption of reasonableness and the stipulated judgment is presumed reasonable. MOE also does not dispute that substantial evidence supported the trial court’s reasonableness determination. MOE merely argues that the trial court should have “enunciated” its reasonableness analysis. MOE did not raise this issue in the trial court and may not raise it for the first time on appeal. RAP 9.12. MOE also concedes that nothing requires such an

“enunciation,” which would conflict with CR 52 and CR 56 governing summary judgment orders. As a third basis for affirming reasonableness, enforcing the finding of reasonableness by the arbitrator and Superior Court does not offend due process pursuant to the recent *Red Oaks Condominiums* decision.

MOE contractually agreed to indemnify DPCI against legal interest DPCI may be required to pay. The trial court judgment correctly enforced MOE’s indemnification obligation under its policy, by applying the contract legal interest rate to the Martinellis’ contract claims established in the judgment against DPCI. The trial court did not abuse its discretion when it deferred ruling on allocation of the burden of proof under Exclusion L of the MOE policy, to allow completion of discovery. MOE does not assign error to the trial court’s award of the Martinellis’ attorney fees, which represents the law of this case. The Martinellis are entitled to recover their attorney fees in this Court. RAP 18.1.

The Martinellis’ cross-appeal provides an independent basis on which to affirm the trial court. Washington insurers may not indefinitely delay payment of undisputed, covered property damage claims in cases of clear liability, while they litigate claims for which they dispute coverage. WAC 284-30-330(6). MOE’s refusal to pay undisputed, covered amounts

additionally breached its duty of good faith.

V. ARGUMENT

A. **The Trial Court Correctly Held That Mutual of Enumclaw Breached Its Duty Of Good Faith To Its Insured.**

1. **MOE Had a Duty to Act in Good Faith.**

Washington insurers must act in good faith. RCW 48.01.030. *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 385-6, 715 P.2d 1133 (1986)

explains the relationship between insurer and insured, as follows:

[T]he source of the duty is the same. That source is the fiduciary relationship existing between the insurer and insured. Such a relationship exists not only as a result of the contract between insurer and insured, but because of the high stakes involved for both parties to an insurance contract and the elevated level of trust underlying insureds dependence on their insurers. This fiduciary relationship, as the basis of an insurer's duty of good faith, implies more than the "honesty and lawfulness of purpose" which comprises a standard definition of good faith. It implies "a broad obligation of fair dealing," and a responsibility to give "equal consideration" to the insured's interests. Thus, an insurance company's duty of good faith rises to an even higher level than that of honesty and lawfulness of purposes toward its policyholder: *an insurer must deal fairly with an insured, giving equal consideration in all matters to the insured's interests.* [Emphasis added; citations omitted].

Quoting, Tyler v. Grange Ins. Ass'n, 3 Wn. App. 167, 473 P.2d 193 (1970).

Bad faith does *not* require "dishonesty, deceit, or a species of fraud."

Tyler, supra, 3 Wn. App. at 174. Instead, indicators of bad faith include facts such as the severity of the insured's exposure to liability in excess of policy

limits, lack of adequate investigation of plaintiff's injuries, or other actions demonstrating greater concern for the insurer's monetary interests than the insured's risks. *Id.* In short, bad faith means the insurer's actions were "unreasonable, frivolous, or unfounded." *Kirk v. Mt. Airy Ins.*, 134 Wn.2d 558, 560, 951 P.2d 1124 (1998); *Smith, supra*, 150 Wn.2d at 484.

The duty of good faith applies to *all* duties assumed in connection with the insurer's contract of insurance, regardless of whether arising in connection with the insurer's duty to defend, investigate, negotiate or settle within policy limits—even if a later determination of no coverage occurs. *Besel v. Viking Ins. Co.*, 146 Wn.2d 730, 737, 49 P.3d 887 (2002)("[t]he principles of *Butler* do not depend on how an insurer acted in bad faith")(emphasis added); *Kirk, supra*, 134 Wn.2d at 565; *Safeco Ins. Co. v. Butler*, 118 Wn.2d 383, 400-6, 823 P.2d 499 (1992).

2. An Insurer's Interference in the Insured's Defense Impairs a Major Policy Benefit Under *Tank*.

Tank established four (4) "specific criteria" which determine whether the insurer has "fulfilled its enhanced obligation" to its insured, including (1) thorough investigation; (2) retention of competent defense counsel; (3) fully informing the insured of *all* developments, and; (4) refraining from any action which would demonstrate a greater concern for the insurer's monetary

interest than for the insured's financial risk. *Tank, supra*, 105 Wn.2d at 388; see, e.g., *Butler, supra*, 118 Wn.2d at 390-2 (re: assigned counsel); *Smith, supra*, 150 Wn.2d at 486 (re: fully informing the insured). These "specific criteria" do not apply narrowly. Of particular significance here, **"[t]he insurer who accepts that duty [to defend] under a reservation of rights, but then performs that duty in bad faith, is no less liable than the insurer who accepts but later rejects the duty. Each has equally breached its duty to the insured."** *Butler, supra*, 118 Wn.2d at 392 (emphasis added). That is precisely what MOE did in this case.

On the eve of DPCI's arbitration, MOE issued a subpoena and *ex parte* letter to the arbitrator. MOE admits it acted to protect MOE from being "forced to chose [sic] between a gross overpayment. . .and a bad faith claim. . .for failure to prevent execution" (CP 157), and to counteract what MOE perceived as DPCI's attempt "to put pressure on MOE to pay the damages without having clarity on what may or may not be covered." CP 160.

MOE had no reasonable basis for issuing a subpoena to the arbitrator. Like judges, arbitrators may not be subpoenaed to explain their rulings. The Washington Supreme Court describes arbitration as "a substitute for judicial action," in which arbitrators "become the judges of both the law and the facts." *Int'l Assoc. of Fire Fighters v. City of Everett*, 146 Wn.2d 29, 38-8,

42 P.3d 1265 (2002). A judge should be called as a witness “[o]nly in the rarest of cases” to testify concerning matters “upon which he has acted in a judicial capacity, and these occasions should be limited to instances in which there is no other reasonable available way to prove the facts sought to be established.” *State ex rel Carroll v. Junker*, 79 Wn.2d 12, 21, 482 P.2d 775 (1971). See, CJC Canon 3(D)(d)(iii).

An arbitrator’s award “states the outcome, much as a judgment states the outcome.” *Lindon Commodities, Inc. v. Bambino Bean Co., Inc.*, 57 Wn. App. 813, 816, 790 P.2d 228 (1990). However, **an explanation for an arbitration award is *not* part of the award** because it would “encourag[e] disappointed parties in attempts to impeach adverse awards.” *Lent’s, Inc. v. Sante Fe Engineers, Inc.*, 29 Wn. App. 257, 265, 628 P.2d 488 (1981); *accord, Lester v. Mills*, 117 Wash. 502, 505-6, 201 Pac. 752 (1921). This would undermine the efficiencies of arbitration and chill the independence of arbitrators, thus jeopardizing the usefulness of arbitration. *Legion Ins. Co. v. General Agency*, 822 F.2d 541, 543 (5th Cir. 1987)(to permit discovery to replicate substance of the arbitration “would thwart its goal”); *Maine v. Central R.R. v. Brotherhood of Maint. Way Employees*, 117 F.R.D. 485, 486-7 (D. Me. 1987). Overwhelming authority supports the conclusion that an Arbitrator may *not* be called to testify about the arbitration proceeding in

other legal proceedings. CP 136, 139-40, 241-2 (marshaling authorities on this subject). See, CP 649 (trial court's analysis). Conversely, if MOE was correct, *every* arbitrator would risk being subpoenaed to testify in the follow-on coverage action, *thus relieving insurers of their duties to investigate and adjust the claims themselves*. The premise of MOE's interference in its insured's defense thus fails because the arbitrator could not have been called to testify in any event.¹²

MOE also had no practical reason to issue the subpoena to the arbitrator. It was not the Arbitrator's responsibility to "segregate insured and uninsured damage elements" in the insured's arbitration (App. Br., p. 11); that was MOE's responsibility. See, *Tank*, 105 Wn.2d at 388 ("thorough investigation" as major policy benefit); WAC 284-30-330(3)-(4) and WAC 284-30-370. Moreover, prior to MOE's interference in the arbitration, DPCI and the Martinellis had fully cooperated with MOE's requests for information. See, p.7, *supra*. So, other than seeking the arbitrator's mental impressions (which were neither discoverable nor admissible), no practical reason existed for MOE's intrusion into the insured's defense. Nevertheless, *if* MOE had a need for more information, it could have asked the parties, or

¹² When the Martinellis asked MOE's coverage counsel to disclose his research conducted on this issue before issuing the subpoena, MOE invoked privilege. CP 1134-5 (94:21-95:5). See, *Pappas v. Holloway*, 114 Wn.2d 198, 208, 787 P.2d 30 (1990)(party may not use privilege as both sword and shield).

served the declaratory judgment complaint and pursued discovery from the parties there.¹³ MOE did neither.

MOE's timing was also unreasonable, as was its decision to act unilaterally. CP 143-44. MOE interfered on the eve of arbitration, after having delayed for 17 months before filing the declaratory judgment complaint and 6 weeks after filing but not serving that complaint. MOE neither consulted with nor disclosed to DPCI's counsel its intentions to interfere in the arbitration.¹⁴

MOE compounded the effects of its subpoena by also corresponding *ex parte* with the arbitrator. CP 133. Well-known rules generally prohibit *ex parte* communications with judges *and arbitrators*. RPC 3.5(a), (b) and (c); CJC Canon 3 and Comment to Canon 3(A)(4). See, *Discipline of Carmick*, 146 Wn.2d 582, 595 and n. 4, 48 P.3d 311 (2002); *Valrose Maui, Inc. v.*

¹³ MOE's interrogatories and letter to the arbitrator were unreasonable for another reason. MOE's coverage counsel apparently misunderstood Exclusion L at the time. MOE's *ex parte* letter (CP 133) tells the arbitrator that it "brought a declaratory judgment action for a determination of what damage (if any) was caused by Dan Paulson Construction's subcontractors" when MOE's coverage is broader than that. See p.44, *infra*. Similarly, MOE's interrogatories to the arbitrator asked him to "identify the contractor, subcontractor, or other entity which actually performed the work out of which the defect arose." CP 127. Again, the information sought would not provide the kind of information needed to adjust the claim. MOE's internal analysis likewise presumed that "our policy excludes coverage for the insured work" (CP 97) and it told DPCI that "there was no coverage for liability for damage to Dan Paulson's own work" (CP 261:4, referencing CP 326), even though MOE later acknowledged in its trial court briefing that it covers damage to the work of subcontractors damaged by the contractor's work as well as damage to the contractors' work caused by the subcontractor's work. See discussion, *infra*, pp.42-3.

¹⁴ MOE invoked privilege and refused to allow its coverage counsel to explain why he acted *ex parte*. CP 1136-8 (95:12-97:10).

Maclyn Morris, Inc., 105 F. Supp.2d 1118, 1123-4 (D. Haw. 2002)(*ex parte* communication violated Federal Arbitration Act section identical to RCW 7.04.160(2) *even without showing actual bias or improper motive*); *Cabbad v. TIG Ins. Co.*, 751 N.Y.S.2d 871 (2002)(vacating arbitration award due to *ex parte* communication); ABA Annot. Model Rules of Professional Conduct, RPC 3.5, p. 339 (3d ed. 1996), citing Phila. Bar Ass'n Ethics Op. 95-8 (lawyers may not communicate *ex parte* with arbitrator). Accord, CP 176 (AAA Rule R-19). MOE's *ex parte* communication with the arbitrator thus posed a grave risk of invalidating the arbitration under RCW 7.04.160(1), (2), and/or (3). At a very minimum, it created uncertainty and anxiety for the insured. CP 143. See further p.11, *supra*.

Appellant's Brief ignores *all* of these issues and the trial court conclusion that "reasonable minds could reach but one conclusion: MOE's actions . . . [were] bad faith." CP 650. MOE instead argues by analogy that its conduct was indistinguishable from "simply bringing a motion to intervene" and "the mechanics of the arbitrator's responding to those interrogatories would have been indistinguishable from a jury turning its attention from a general verdict to the special interrogatories proposed by the insurer in a standard intervention situation." App. Br., pp. 23-30.

MOE's analogy fails on several levels. Most obviously, MOE did *not*

move to intervene in the arbitration proceeding. Furthermore, unilaterally issuing a subpoena and *ex parte* correspondence to an arbitrator to appear in a separate court proceeding raises extraordinary policy implications not present in connection with supervised submission of special interrogatories to a jury after obtaining leave to intervene from the court.¹⁵ See, pp.20-24, *supra*.

MOE's analogy is also plainly wrong. Insurers *defending their insured under a reservation rights*, as here, are generally **denied** the right to intervene for purposes of propounding special interrogatories on coverage issues **precisely to avoid interference in the insured's defense**. See, *e.g.*, *Travelers Indemnity Co. v. Dingwell*, 884 F.2d 629, 638-641 (1st Cir. 1989) (“well-established policy that an insurer who reserves the right to deny coverage cannot control the defense of a lawsuit brought against its insured

¹⁵ MOE cites two cases to support its contention that insurers are routinely allowed to intervene in underlying damage lawsuits and propound special interrogatories. App. Br., pp. 24-7. Both cases discredit MOE's contention. *Bankers Life Ins. Co. v. Wedco, Inc.*, 102 FRD 41 (D. Nev. 1984) denied intervention as of right, but allowed permissive intervention, emphasizing that “**any right to proffer special interrogatories or verdicts would not infer or imply that the Court would feel obligated to submit them to the jury. The insurance companies may not compromise the interests of their insured herein.** They have represented they recognize and intend to honor this requirement. Thus, even permitting intervention here **does not assure that the jury will be asked to allocate any money damages according to the nature of the acts giving rise thereto.**” *Id.* at 44 (emphasis added). *Thomas v. Henderson*, 297 F. Supp.2d 1311, 1327 (S.D. Ala. 2003) also expressed concern for the “potential that a conflict might emerge between insurer and insured, that the insured's counsel may be placed in an untenable position, or that these proceedings may otherwise be disrupted” and *adopted the same severe limitations* used in *Bankers Life*. *Id.*

by an injured party”); *Restor-A-Dent Dental Laboratories, Inc. v. Certified Alloy Products, Inc.*, 725 F.2d 871, 873-6 (2nd Cir. 1984); *Nieto v. Kapoor*, 61 F. Supp.2d 1177, 1192-95 (D.N.M. 1999)(“allowing [the insurer] to intervene where its interests are unquestionably antagonistic to [the insured’s] will prejudice adjudication of [the insured’s] rights”); *Davila v. Arlasky*, 141 FRD 68, 72 (N.D. Ill. 1991)(“conflict exists between the insurers who would be just as happy to see willful [*i.e.*, non-covered] conduct proved, and the insured, who wants any liability to be covered by the policy”).

Interference in the insured’s assigned defense is no different than any other act of bad faith in connection with the insured’s defense. *Butler, supra*, 118 Wn.2d at 392 (“insurer who accepts the duty [to defend] under a reservation of rights, but then performs that duty in bad faith, is no less liable”). The Court should affirm the trial court conclusion that MOE acted in bad faith and not condone insurer interference in an insured’s defense.

B. The Trial Court Correctly Estopped MOE To Deny Coverage.

1. *Butler* Establishes The Remedies for Insurer Bad Faith in Connection with Defense of the Insured under a Reservation of Rights.

The tort of bad faith “recognizes that traditional contract damages do not provide an adequate remedy for a bad faith breach” of the insurance contract. *Kirk, supra*, 134 Wn.2d at 560; accord, *Butler, supra*, 118 Wn.2d at

394 (otherwise “[a]n insurer could act in bad faith without risking additional loss”). The insured’s remedies for bad faith are therefore not limited to contract damages. *Kirk, supra*, 134 Wn.2d at 561-65. Expressing concern that bad faith remedies should create a *strong incentive for insurers to act in good faith*, *Butler* established the basic principles applicable to Washington bad faith remedies, as follows (118 Wn.2d at 394):

To summarize our holding so far: we hold (1) harm is an essential element of an action for insurer’s bad faith handling of a claim under reservation of rights; (2) if the insured shows by a preponderance of the evidence the insurer acted in bad faith, there is a presumption of harm; (3) the insurer can rebut the presumption of harm by showing by a preponderance of evidence its acts did not harm or prejudice the insured; and (4) if the insured prevails on the bad faith claim, **the insurer is estopped from denying coverage**. [Emphasis added].

2. The Trial Court Ruling that MOE Did Not Rebut the Presumption of Harm Is The Law Of This Case.

MOE did not assign error to the trial court’s holding that MOE did not rebut the presumption of harm established in *Butler*. RAP 10.3(g); compare CP 690 to App. Br., pp.2. Indeed, **Appellants’ Brief does not discuss the presumption of harm at all**. The trial court’s holding thus represents the law of the case on this issue. *King Aircraft Sales, Inc. v. Lane*, 68 Wn. App. 706, 716-7, 846 P.2d 550 (1993). Accordingly, the presumption of harm under *Butler* applies and MOE is estopped to deny coverage.

3. *Besel* Rejected MOE’s Argument that the “Category” of Harm Determines Whether Estoppel Applies.

To circumvent the *Butler* presumption of harm, MOE argues the novel theory (App. Br., pp. 31-37) that “the alleged harm sustained by Paulson is not within the *category* from which ‘coverage by estoppel’ can arise.” App. Br., pp. 17-8 (emphasis added). MOE thus argues that estoppel to deny coverage only applies if the insurer’s conduct “would necessarily increase the [insured’s] tort liability exposure to the injured claimant and/or constitute an improper manipulation of the defense being provided to the [insured] to enhance the [insurer’s] coverage denial position.” App. Br., pp. 31-37. See further, App. Br., p. 2 (Issue 1). Without mentioning the presumption of harm, MOE asserts that “harm,” within the meaning of *Butler*, is limited to those situations in which the insurer’s bad faith “increased tort liability exposure” or “improper manipulation of the defense to enhance[d] the insurer’s coverage position.” *Id.*

MOE’s analysis conflicts with the express holding of *Butler, supra*, 118 Wn.2d at 493. Moreover, no case law supports MOE’s theory that *Butler’s* remedies apply only if the insurer’s conduct “exposed the insured to personal financial liability which would not have existed if the claim had been settled within policy limits” or “increase the insured’s economic

exposure to the tort claimant. App. Br., pp. 33,34.¹⁶ To the contrary, *Besel* rejected MOE's theory that *Butler* applies to only certain "categories" of harm, explaining (146 Wn.2d at 737):

Viking further argues *Butler's* presumption of harm should not apply because *Butler* involved a defense tendered under a reservation of rights. This is a distinction without a difference. **The principles of *Butler* do not depend on how an insurer acted in bad faith. Rather, the principles apply whenever an insurer acts in bad faith**, whether by poorly defending a claim under a reservation of rights, refusing to defend a claim, or failing to properly investigate a claim. [Emphases added; citations omitted].

Several Washington Supreme Court cases also do not fit MOE's novel theory. For example, in *Smith v. Safeco Ins., supra*, the Supreme Court reinstated a bad faith complaint arising out of the insurer's failure to disclose the insured's liability policy limits to a tort claimant. The policy limits were \$100,000. *Id.*, 150 Wn.2d at 482. The covenant judgment between the insured and the tort victim was in the same amount, *i.e.*, \$100,000. *Id.* Similarly, in *Butler*, no coverage existed but the Supreme Court nevertheless remanded for a determination of bad faith. *Butler, supra*, 118 Wn.2d at 406. In *Vanport Homes*, the Supreme Court applied estoppel to an insurance policy exclusion, precisely as occurs here. *Vanport*

¹⁶ *Coventry Associates v. Am. States Ins. Co.*, 136 Wn.2d 269, 961 P.2d 933 (1998), App. Br., pp. 35-6, *distinguishes itself* because the "enhanced obligation to its insured" an insurer must fulfill when defending a third party claim under a reservation of rights "does not exist in the first-party context." *Id.*, 136 Wn.2d at 281.

Homes, supra, 147 Wn.2d at 762-3. If MOE's theory were correct, each of these cases would have been decided differently.

Mutual of Enumclaw's insistence (App. Br., pp. 31-37) that the *insured* prove the insurer's conduct "increased the [insured's] tort liability exposure," also conflicts with *Butler*'s presumption of harm because it implies that the presumption of harm depends on the quantity or quality of harm. This seems inherently inconsistent with the insurer's burden to rebut the presumption of harm, *i.e.*, if there is harm then the presumption quite obviously has *not* been rebutted. *Butler* confirms the MOE's inconsistency, as follows (118 Wn.2d at 392):

The requirement of acting in good faith is meaningless if the insurer can protect itself from liability for bad faith simply by reserving its rights. Presuming prejudice once the insured establishes bad faith shifts the burden to the insurer to prove its acts did not prejudice the insured. **The shifting of the burden ameliorates the difficulty insureds have in showing that a particular act resulted in prejudice. It also recognizes the fact that loss of control of the case is in itself prejudicial to the insured.** Finally, imposing a presumption of prejudice only after the insured shows bad faith adequately protects the competing societal interests involved. It provides a meaningful disincentive to insurers' bad faith conduct while protecting insurers from frivolous claims. [Emphasis added; citations omitted].

Butler did not qualify its remedy based on the size or nature of the harm. *Id.* at 118 Wn.2d at 394 ("if the insured prevails on the bad faith claim, the insurer is estopped from denying coverage"). Instead, "harm (or

“prejudice”) within the meaning of *Butler* may take innumerable forms and is not limited to financial loss. *Butler, supra*, 118 Wn.2d at 396 (harm despite release from liability); *Truck Ins. Exch. v. Vanport, supra*, 147 Wn.2d at 765 (emphasizing that bad faith “exposes” the insured to increased risks, such as “business failure and bankruptcy”); *R.A. Hansen Co. v. Aetna Cas. Co.*, 15 Wn. App. 608, 611, 550 P.2d 701 (1976)(“not exhaustive” examples of non-monetary “prejudice”). *Besel* thus explains “**the amount of a covenant judgment is the presumptive measure of an insured’s harm caused by an insurer’s tortious bad faith** if the covenant judgment is reasonable.” *Besel, supra*, 146 Wn.2d at 737, 738.¹⁷

Application of the *Butler* presumption of harm does not vary depending on the “category” of the insurer’s bad faith, or the size or nature of potential harm to which the insurer’s conduct exposes the insured. The Court should reject MOE’s attempt to circumvent *Butler’s* presumption of harm.

4. MOE Did Not Rebut the Presumption of Harm.

Washington views “harm” due to bad faith as of the time of the stipulated settlement, not based on speculation as to what might have happened in the future but for the bad faith. Quoting *Transamerica Ins.*

¹⁷ A stipulated judgment also represents the insured’s *mitigation* of damage due to the insurer’s bad faith. See, *City of Seattle v. Blume*, 134 Wn.2d 243, 252-60, 947 P. 2d 223 (1997) and *Flint v. Hart*, 82 Wn. App. 209, 214-220, 917 P.2d 590 (1996).

Group v. Chubb & Son, Inc., 16 Wn. App. 247, 252, 554 P.2d 1080 (1977),

Butler explains (118 Wn.2d at 391):

The course cannot be rerun, no amount of evidence will prove what might have occurred if a different route had been taken. By its own actions, [the insurer] irrevocably fixed the course of events concerning the law suit for the first 10 months. Of necessity, this establishes prejudice.

No one can know with certainty what would have happened if MOE had not interfered in the arbitration; nor can anyone predict what would have happened if DPCI had not entered into the stipulated judgment. The Washington Supreme Court, after all, adopted the presumption of harm specifically to obviate such speculative inquiries. Nevertheless, MOE's bad faith indisputably forced its insured to incur attorney fees and expenses, understandably upset its insured on the eve of arbitration, and posed a "grave risk of invalidating" the arbitration (CP 650), that created a risk of ongoing litigation for DPCI and threatened its survival.

The trial court correctly held that MOE did not rebut the presumption of harm. MOE does not assign error to that holding in this appeal. RAP 10.3(g). If the Court agrees that MOE acted in bad faith, then MOE is estopped to deny coverage and MOE is liable to indemnify the full amount of the judgment against its insured, DPCI.

C. The Trial Court Correctly Upheld The Reasonableness Of The Stipulated Arbitration Award.

The trial court concluded that no genuine issue of fact remained regarding the issue of reasonableness of the Stipulated Arbitration Award and upheld its reasonableness as a matter of law. CP 690. The trial court had three independent bases to support this conclusion: (1) MOE failed to carry its burden under *Vanport Homes* to prove fraud or collusion, thus reasonableness was presumed and not rebutted; (2) sufficient evidence supported the trial court's reasonableness determination, and; (3) MOE waived any objection to reasonableness in the underlying proceedings of which it had notice but chose to ignore. MOE's Brief discusses issues 2 and 3, but ignores the presumption of reasonableness under *Vanport Homes*.

1. MOE Did Not Assign Error To The Trial Court's Decision that MOE Did Not Show Fraud or Collusion; That Decision Is the Law of the Case And The Stipulated Arbitration Award Is Thus Presumed Reasonable.

When a Washington insurer breaches its duty of good faith, the insured's subsequent settlement with the plaintiff enjoys a presumption of reasonableness *unless* the insurer proves "fraud or collusion" in connection with the settlement. *Vanport Homes, supra*, 147 Wn.2d at 764-766; *Besel, supra*, 146 Wn.2d at 735-6; *Greer, supra*, 109 Wn.2d at 202. The burden shifts from the policyholder because "[t]o place the burden of proving

reasonableness of a settlement on a policyholder ‘would discourage settlement so necessary to the orderly disposition of cases.’” *Vanport, supra*, 147 Wn.2d at 765.

Here, the trial court held that MOE had not carried its summary judgment burden to prove a genuine issue of fact concerning fraud or collusion. CP 690. MOE did not assign error to this trial court decision or include this issue in its associated issues. Indeed, **MOE’s Brief does not even cite *Vanport Homes***. The trial court holding that MOE did not show fraud or collusion is, therefore, the law of the case. *King Aircraft Sales, Inc. v. Lane, supra*, 68 Wn. App. at 716-7. The Stipulated Arbitration Award is thus presumed reasonable under *Vanport Homes* and MOE did not rebut that presumption as a matter of law.¹⁸

¹⁸ The trial court correctly held that MOE did not show fraud or collusion. MOE alleged fraud or collusion as an affirmative defense (CP 14¶4, CP 957) and thus had the burden of proof on that issue. *Young v. Key Pharmaceuticals, Inc.*, 112 Wn.2d 216, 225 n. 1, 770 P.2d 182 (1989)(Martinellis could thus “point out” the absence of evidence to support the affirmative defense); *Brown v. Pro West Transport, Inc.*, 76 Wn. App. 412, 419, 886 P.2d 223 (1994)(burden of proof re: affirmative defense). The Martinellis made this showing in their opening motion. CP 252-3, referencing CP 27¶¶5-6, CP 29-30 ¶¶3-4, CP 39-40 ¶34, CP 168-173; CP 491-2, referencing CP 507-11 (20:11-24:10), CP 523-7 (6:23-7:25, 8:17-10:4). MOE relied solely on the fact of the Stipulated Arbitration Award. CP 86-7 (153:3-154:23). However, the Washington Supreme Court has rejected the concept that the mere fact of a covenant judgment demonstrates fraud or collusion. *E.g., Butler, supra*, 118 Wn.2d at 396-400; *Besel*, 146 Wn.2d at 735-8 (covenant judgment is “presumptive measure of harm”); *Vanport Homes, supra*, 147 Wn.2d at 756-66; *Greer v. Northwestern Nat’l Ins.*, 109 Wn.2d 191, 204-5, 743 P.2d 1244 (1987)(insurer “is in no position to argue that the steps the insured took to protect himself should inure to the insurer’s benefit”).

2. The Trial Court Correctly Upheld the Arbitration Award As Reasonable.

The trial court also correctly upheld the reasonableness of the Stipulated Arbitration Award on the evidence presented. MOE does not argue a lack of substantial evidence to support a finding of reasonableness; instead, MOE merely argues that the trial court should have “enunciate[d]” its analysis of the *Glover* factors in connection with its summary judgment ruling. App. Br., pp. 43-44. MOE did not raise this issue concerning the need for an “enunciation” in the trial court, despite having filed *two* motions for reconsideration. CP 480-1, 694-99, 903-13; RP (6/1/04), p. 18:18-19:18. MOE may *not* raise this issue for the first time on appeal. RAP 9.12. The Martinellis nevertheless respond out of an abundance of caution.

The reasonableness standards applicable to contribution rights also apply in the context of covenant judgments in bad faith litigation. *Chaussee v. Maryland Casualty Co.*, 60 Wn. App. 504, 512, 803 P.2d 1339 (1991); *Besel, supra*, 146 Wn.2d at 738-9. *Chaussee* adopted the analysis developed under RCW 4.22.060 in *Glover v. Tacoma Gen'l Hosp.*, 98 Wn.2d 708, 658 P.2d 1230 (1983). *Glover* identified several factors that can be considered in determining reasonableness, but emphasized that “no one factor should control” and judges “must have discretion to weigh each case individually”.

Id. at 98 Wn.2d 717-8.

Flexible procedures govern reasonableness decisions, as *Clark v. Pacificorp*, 118 Wn.2d 167, 182, 822 P.2d 162 (1991) explains:

In determining the percentages of fault, a trial by jury is not required. In *Glover*, we indicated the trial court was not required to conduct a minitrial in making a reasonableness determination. We stated that in conducting a reasonableness hearing, the trial judge has discretion to “weigh each case individually.” In the present case, this discretion can be applied to the judge’s decision as to the use of evidence, affidavits, depositions and live testimony during the hearing. [Citations omitted].

Accord, *Wilson v. Steinbach*, 98 Wn.2d 434, 438, 656 P.2d 1030 (1982)(use of attorney declaration re: reasonableness); *Pickett v. Stephens-Nelsen, Inc.*, 43 Wn. App. 326, 333 and n.2, 717 P.2d 277 (1986)(upon *prima facie* showing, burden shifts to party opposing reasonableness to prove “specific facts” controverting reasonableness); *Glover, supra*, 98 Wn.2d at 718 n. 3.

MOE does *not* argue that the trial court misapplied the *Glover* factors. Nor does MOE explain how the *Glover* factors might support a finding of *unreasonableness* when applied to this case. App. Br., pp. 43-44. Instead, MOE merely argues that the trial court erred because it “did not enunciate verbally or in writing any analysis of the *Chaussee/Glover* elements or indicate what evidence, if any, the Court was relying on in reaching” that conclusion. *Id.* MOE thus does *not* dispute that substantial evidence

supported the trial court's reasonableness decision. See, *Glover, supra*, 98 Wn.2d at 718 (substantial evidence standard applies).

Here, the trial court decided reasonableness on a motion for summary judgment. Summary judgment is entirely consistent with the flexible procedures encouraged for reasonableness determinations. Consistent with CR 52(a)(5)(B), findings of fact and conclusions of law are "gratuitous, superfluous and of no consequence" in connection with summary judgment rulings. *Skimming v. Boxer*, 119 Wn. App. 748, 755, 82 P.2d 707 (2004). Indeed, MOE itself concedes that "no statute or case law requires that the trial court enter formal Findings of Fact and Conclusions of Law regarding the issue of 'reasonableness.'"¹⁹ App. Br., p.44. Thus, no error occurred.

Substantial evidence also supported the trial court's reasonableness determination--a conclusion MOE does not dispute on appeal. MOE did not object to the use of summary judgment to decide reasonableness in the trial court and should not be allowed to raise its demand that the trial court "enunciate" reasons for its summary judgment ruling for the first time here. RAP 9.12. This Court should thus affirm the trial court's reasonableness determination based upon this second, independent basis.

¹⁹ MOE cites *Glover and Howard v. Royal Specialty Underwriting, Inc.*, 121 Wn. App. 372, 380, 89 P.3d 265 (2004). *Howard* contains no such language. *Glover* involved contribution among tortfeasors and appeal after an evidentiary hearing. *Glover* affirmed the finding of reasonableness without "enunciation" of reasons that MOE here demands.

3. Enforcement of the Reasonableness Determination by the Arbitrator Does Not Offend Due Process.

MOE argues that its due process rights were violated “[i]f the Trial Court’s ruling that the settlement was ‘reasonable’ was based upon either the private Arbitrator’s statement in that regard, or the confirmation of the Arbitration Award.” App. Br., pp. 38-43. MOE complains that if it had intervened in the underlying confirmation proceeding (in San Juan County cause no. 02-2-05152-0 [CP 182]), that Court’s consideration of the reasonableness issue would have been limited to the issues allowed by RCW 7.04.160 and .170. *Id.*, pp. 41-42. MOE had actual notice of the motion for confirmation of arbitration award, and chose not to intervene. CP 30 ¶5.

Insurers have no specific right to participate in reasonableness hearings. *Elovich v. Nationwide Ins. Co.*, 104 Wn.2d 543, 553-556, 707 P.2d 1319 (1985)(UIM). Insurers instead have two primary due process protections: (1) act in good faith (so no presumption of reasonableness arises), or; (2) overcome the presumption of reasonableness with evidence of fraud or collusion. See, *Howard, supra*, 121 Wn. App. at 380 (“full opportunity to defend itself in the bad faith action”); *Vanport Homes, supra*, 147 Wn.2d at 764-66 (rebut presumption of reasonableness).

Furthermore, binding the insurer who is “not a stranger to the case”

through application of the reasonableness determination does not offend due process if the insurer received notice of the reasonableness hearing and had an *opportunity* to participate. *Howard, supra*, 121 Wn. App. at 379-80; *Red Oaks Condo. Owners Ass'n v. Mut. of Enumclaw*, __ Wn. App. __, _ P.3d __, 2005 WL 1799278 *3-4 (2005) (six days notice satisfied due process when MOE “not a stranger to this case”); *Besel, supra*, 146 Wn.2d at 739.

Mutual of Enumclaw had ample opportunity to contest reasonableness, but chose not to do so. No due process violation occurred. The arbitrator’s reasonableness determination, as confirmed by the Superior Court, binds MOE. This represents a third, independent basis upon which to affirm the trial court’s reasonableness holding.

D. The Trial Court Correctly Enforced Mutual of Enumclaw’s Supplemental Payments Coverage To Indemnify Interest On The Judgment Against Its Insured At The Contract Rate.

Mutual of Enumclaw argues that the trial court applied the wrong legal interest rate to the principal amount of the judgment, because “bad faith” claims represent tort claims. App. Br., pp. 48-50. Respondents *agree* that bad faith claims do indeed represent tort claims. That, however, has nothing to do with the trial court’s application of the contract legal interest rate to those portions of the judgment which involve MOE’s indemnification of DPCI under the terms of MOE’s policy. The trial court correctly used the

legal interest applicable to contract actions *based upon MOE's contractual obligation to indemnify its insured against legal interest* accrued under the covenant judgment. DPCI assigned both its contractual indemnification and bad faith claims to the Martinellis. CP 189-210.

Washington does not recognize a cause of action for negligent construction. *E.g., Stuart v. Coldwell Banker Comm'l Group, Inc.*, 109 Wn.2d 406, 417, 785 P.2d 1284 (1987). The Martinellis' claims against DPCI obviously represent breach of contract claims, not tort claims, both as a matter of law and as a matter of fact. CP 44. The covenant judgment against DPCI thus correctly awarded legal interest at the contract rate. CP 185-7.

MOE's insuring agreement with DPCI explicitly obligates MOE to "pay sums. . .provided for under Supplementary Payments-Coverages **A** and **B**." CP 783. These clauses of MOE's contract provide (CP 784):

1. We will pay, with respect to any claim we investigate or settle, or any "suit" against an insured we defend: . . .
 - e. All costs taxed against the insured in the "suit".
 - f. Prejudgment interest awarded against the insured on that part of the judgment we pay. . .
 - g. All interest on the full amount of any judgment that accrues after entry of judgment and before we have paid. . .

Mutual of Enumclaw thus contractually obligated itself to indemnify DPCI from liability for legal interest at the rate accrued on the covenant

judgment against DPCI. The trial court so held. CP 982 ¶3.²⁰ See also, CP 944-5. Furthermore, the effect of estoppel to deny coverage means that the Martinellis' claims against DPCI are, in fact, covered claims. Moreover, application of the reduced tort interest rate in these circumstances would render collection and satisfaction of the full amount of covenant judgments impossible in contract actions, and would discourage litigants from entering into such settlements in the future.

The trial court thus correctly applied the legal interest rate applicable to contract actions to that part of the judgment arising solely in contract.

E. The Trial Court Did Not Abuse Its Discretion When It Deferred Ruling On Allocation Of Burdens Of Proof Under Exclusion L.

Mutual of Enumclaw complains (App. Br., pp. 45-48) that the trial court erred when it “defer[red] its ruling [on how to allocate the burden of proof related to particular damages under Exclusion L] until the parties have conducted discovery on the contract claim issues.” CP 653. Submitted in the abstract, MOE urges this Court to vaguely hold that “the insured (or its assignee) has the burden of proving that a claim falls within the exception to an insurance contract coverage exclusion,” without regard for complex issues such as concurrent causation and segregation of damages among joint actors.

²⁰ In contrast, the trial court applied the tort interest rate to those amounts included in the judgment which arise out of the tort claim and *not* under MOE's contractual indemnification obligation. CP 982 ¶¶9-10, 13.

MOE's vague standard offers little benefit to the trial court or the parties. (This issue becomes moot if the Court affirms the bad faith judgment).

This Court reviews the order deferring decision on allocation of the burden of proof under Exclusion L for an *abuse of discretion*, just as it would review a trial court's CR 56(f) order under similar circumstances. *E.g.*, *Coggle v. Snow*, 56 Wn. App. 499, 508, 784 P.2d 554 (1990). The trial court did not abuse its discretion because it had good reason to defer this issue.

Allocation of the burden of proof under Exclusion L does not operate in the over-simplified fashion described in Appellant's Brief, pp. 45-48; instead, allocation of the Exclusion L burden of proof requires a fact-intensive inquiry. See, CP 383-386 (history and analysis of Exclusion (L)),²¹ CP 533 (MOE *agrees* with Martinellis' explanation of Exclusion L); RP (6/1/04), pp. 35:17-36:8; 38:2-40:13. Washington's application of "efficient proximate cause" further complicates this analysis. See, *e.g.*, *Wright v. Safeco Ins. Co. of Am.*, 124 Wn. App. 263, 273-75, 109 P.3d 1 (2004)(if efficient proximate cause is within coverage, then policy provides coverage even if policy excludes other events within the chain of causation).

The parties agree that Exclusion L provides coverage for: (1) damage caused by subcontractors, including damages caused to DPCI's

²¹ Due to space constraints and MOE's *agreement* with the Martinellis' Exclusion L analysis, the Martinellis cross-reference their trial court analysis. CP 383-386.

own work or the work of others, and; (2) damage caused by the contractor, DPCI, to work performed by subcontractors. See, *American Family Mut. Ins. Co. v. American Girl, Inc.*, 673 N.W.2d 65, 73, 82-83 (Wisc. 2004), citing, 21 E.M. Holmes, *Holmes' Appelman on Insurance*, §132.9, pp. 152-3 (2d ed 2000); *Kvaerner Metals Div. of Kvaerner U.S., Inc. v. Commercial Union Ins. Co.*, 825 A.2d 641, 656 (Pa. 2003), citing P. Nelson, *Comprehensive General Liability Policy Handbook*, p. 106; Am. Bar Ass'n Tort Trial & Ins. Prac. Section, *CGL/Builder's Risk Monograph*, p. 25 (2004), quoting F.C. & S. Bulletins (“**Potential coverage under the contractor’s CGL policy may be overlooked because it is [incorrectly] assumed that no coverage exists for correction of defects in the insured’s own work**”). See further, CP 382-6. In the trial court, MOE conceded that “**MOE does not disagree with the Martinellis’ assessment of the subcontractor exception.**” CP 533 (emphasis added).²²

²² The only reported case allocating the Exclusion L burden of proof appears to be *National Union Fire Ins. Co. v. Structural Systems Technology, Inc.*, 756 F. Supp. 1232 (E.D. Mo. 1991), *aff'd*, 964 F.2d 759 (8th Cir. 1992), which allocated the burden of proof *to the insurer*. See, 2 A. Windt, *Insurance Claims and Disputes* §9.1 (4th ed. 2003)(burden should be on insurer to establish that a proviso in an exclusion is inapplicable). MOE’s burden of proof analysis relies on cases applying the “sudden and accidental” exception to the pollution exclusion. App. Br., pp. 47-8. *Aydin Corp. v. First State Ins. Co.*, 18 Cal.4th 1183, 77 Cal. Rptr.2d 537 (1998), cited by MOE, explains, “[a]s a coverage provision, the exception will be construed broadly in favor of the insured. . . [to] aid the insured in meeting its burden of proof, thereby ensuring that the end result (coverage or noncoverage) conforms to the insured’s objectively reasonable expectations.” 18 Cal.4th at 1192.

At oral argument (RP 6/1/04, pp. 37:17-38:38:1, 10-17), the Martinellis demonstrated the ambiguity of MOE's proposed burden of proof allocation using the following hypothetical: (a) assume a construction defect existed relative to windows, and; (b) a window company, the contractor, and an independent subcontractor had all been involved in the window assembly and installation. RP (6/1/04), pp. 37:17-38:1, 10-17). In this hypothetical, *how* would MOE's proposed allocation of burden of proof apply?

MOE presented this issue in a vague and abstract context and without regard to any specific facts actually present in this case. The trial court did not abuse its discretion when it properly deferred ruling on allocation of the burden of proof under Exclusion L until the parties can present this issue in the context of specific facts and damage claims.²³

F. The Court Should Award Respondents/Cross-Appellants Their Attorney Fees In This Appeal.

The Martinellis are entitled to recover their reasonable attorney fees and expenses against MOE, as assignees of DPCI. *McGreevy v. Oregon Mut. Ins. Co.*, 128 Wn.2d 26, 32-37, 904 P.2d 731 (1995)(enforcement of insurance contract); *Panorama Village v. Allstate Ins. Co.*, 144 Wn.2d 130,

²³ If this Court nevertheless rules on the merits of the burden of proof issue, the Court should hold (consistent with the parties' positions concerning coverage under Exclusion L) that: (1) damages caused in whole or in part *by* the work of a subcontractor (including damages to the work of DPCI) are covered; (2) damages caused in whole or in part *to* the work of a subcontractor are covered (including damages caused by DPCI).

143-44, 26 P.3d 910 (2001)(enforcement of insurance contract); *Besel v. Viking Ins. Co.*, 146 Wn.2d 730, 840, 49 P.3d 887 (2002)(insurance bad faith); *Weyerhaeuser, supra*, 142 Wn.2d at 687 n.15. MOE also did not assign error to (or separately brief) the trial court's decision awarding Mr. and Mrs. Martinelli recovery of their fees. The Martinellis' right to recover their fees is thus the law of the case.²⁴ See, *King Aircraft, supra*, 68 Wn. App. at 716-7 (failure to assign error); *City of Seattle v. Visio Corp.*, 108 Wn. App. 566, 580 n. 28, 31 P.3d 740 (2001)(failure to brief assignment of error). This Court should award the Martinellis their reasonable attorney fees on appeal. RAP 18.1.

VI. CROSS-REVIEW

A. **Insurers Violate WAC 284-30-330(6) When They Indefinitely Delay Payment Of Undisputed, Covered Property Damages.**

A second, independent basis supports affirming the trial court's entry of judgment. Washington *requires* that insurers "effectuate prompt payment of property damage claims to innocent third parties in clear liability situations." WAC 284-30-330(6). WAC 284-30-370 establishes a presumptive 30-day period in which the insurer should complete its investigation. These regulations apply "to all insurers and all insurance

²⁴ MOE merely asserts that "reversal of the finding of coverage estoppel requires that the award of attorney fees and expenses" must also be reversed. App. Br., p. 45.

policies and insurance contracts.” WAC 284-30-310. By definition, violation of WAC 284-30-330(6) represents an “unfair or deceptive act[] or practice[] in the business of insurance.” WAC 284-30-330. “Unconditional tender” statutes and regulations like WAC 284-30-330(6) impose an *affirmative* duty on the insurer, to adjust the claim and pay the undisputed amounts promptly, in part so that litigation can either be avoided entirely, or limited to disputed items. *E.g.*, *McDill v. Utica Mut. Ins. Co.*, 475 So.2d 1085, 1091 n. 6 (La. 1985)(“If the insurer is not required to pay the portion of the claim which is unquestionably due [within the statutory period, the statute] is rendered meaningless.”).

The Martinellis are innocent third parties (as established by the stipulated judgment and the lack of any comparative fault allegation [CP 13-14, 956-7]), their claims obviously represent property damage claims, and the covenant judgment establishes a “clear liability situation.” Mutual of Enumclaw itself admits that at least “some” of the Martinellis’ claims are within MOE’s coverage. CP 2 ¶6; CP 86 (152:2-14). The Martinellis thus satisfy all requirements for application of WAC 284-30-330(6). MOE therefore had an affirmative duty to “effectuate prompt payment” of the undisputed, *covered* items of the Martinellis’ property damage, consistent with WAC 284-30-370. MOE refused to tender *any* amount to pay the

undisputed, covered claims, despite the Martinellis' request. CP 86 (151:20-152:21), 212.

The trial court nevertheless denied the Martinellis' motion for MOE's violation of WAC 284-30-330(6), explaining (CP 652):

In this case, MOE has continually asserted that much of the liability is excluded under the subcontractor exception to the work exclusion. [Footnote omitted]. It is disputed that some, if not a large portion, of the work done in this case falls under the subcontractor exception to the work exclusion. Until MOE discovers what work is covered by the settlement, it is not in a position to determine what amounts are covered and what amounts are not covered. Since the parties did not contract to provide insurance for a noncovered event, MOE is not required to pay for amounts that are not covered under the policy.

The Martinellis did not request, and WAC 284-30-330(6) does not require, that an insurer unconditionally tender "amounts that are not covered under the policy." However, the trial court's rationale effectively immunizes insurers from paying *undisputed, covered* amounts of property damage as required by WAC 284-30-330(6), whenever *any* exclusion from coverage may apply to *some* other items of damage. No such proviso appears in the regulation; indeed, such an exception to WAC 284-30-330(6) can only *encourage insurers to delay completion of the adjusting process* to justify their continuing failure to pay undisputed amounts owed. Such a result conflicts with the goal of *prompt* action and resolution of claims by insurers embodied throughout WAC 284-30-330 and eviscerates WAC 284-30-370.

The record here also overwhelmingly contradicts the trial court's unstated premise, *i.e.*, that MOE has not had sufficient opportunity "to determine what amounts are covered and what amounts are not covered." Instead, DPCI and the Martinellis both provided MOE with *all* of the information it requested as early as August, 2002. DPCI provided MOE with additional information in September, 2003. MOE's adjusters had substantially evaluated the case by October, 2003. CP 97-8, 100, 102-3.

WAC 284-30-330(6) *required* MOE to promptly pay the undisputed and covered items of the Martinellis' property damage claim. When MOE failed to do so, it breached its duty of good faith. This act of bad faith provides an independent reason to affirm the judgment of the trial court.

VII. CONCLUSION

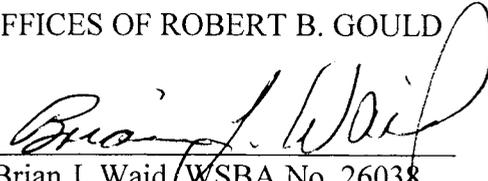
For all of the foregoing reasons, respondents/cross-appellants Karen and Joseph Martinelli ask that the Court affirm the judgment of the trial court against appellant Mutual of Enumclaw, reverse the trial court's decision that an insurer may indefinitely delay tender of undisputed, covered property damage claims, and award Mr. and Mrs. Martinelli their reasonable attorney fees on appeal.

DATED this 10 day of August, 2005.

Respectfully submitted,

LAW OFFICES OF ROBERT B. GOULD

By:

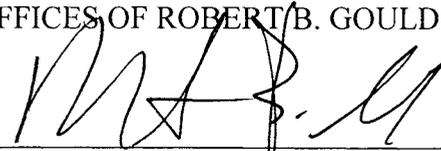


Brian J. Waid, WSBA No. 26038
Attorney for Respondents
Karen and Joseph Martinelli

AND

LAW OFFICES OF ROBERT B. GOULD

By:



Robert B. Gould, WSBA No. 4353
Attorney for Respondents
Karen and Joseph Martinelli

APPENDICES

APPENDIX A

James M. Beecher
Steven A. Branom
Theodore H. Millan
Barbara J. Boyd
David R. Collins
Debra L. Dickerson*
Brent W. Beecher

Law Offices of

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*Also Admitted in California

December 30, 2003

bbeecher@hackettbeecheer.com

J. Richard Manning
500 Union Street, Suite 925
Seattle, WA 98101

RE: Martinelli v. Dan Paulson Construction, Inc.

Dear Mr. Manning:

I believe you are the arbitrator in the above-mentioned matter. I represent Mutual of Enumclaw, which issued a Commercial General Liability policy to the defendant in that case, Dan Paulson Construction, Inc. Mutual of Enumclaw is currently providing a defense to Dan Paulson under a reservation of rights, which reservation is based primarily the "work" exclusion in the policy.

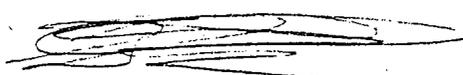
1. Damage to Your Work
"Property damage" to "your work" arising out of it or any part of it and included in the "products-completed operations hazard".

This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.

If this were a judicial proceeding, Mutual of Enumclaw would bring a Motion to Intervene. Since it is not, Mutual of Enumclaw has brought a declaratory judgment action for a determination of what damage (if any) was caused by Dan Paulson Construction's subcontractors. A copy of the Complaint in that action is enclosed. In the arbitration, you will be asked to make a finding of liability and damages, and Mutual of Enumclaw needs more information about the basis for your award (if any). To that end, I am enclosing a Subpoena Duces Tecum, directed to you. The date I selected is somewhat arbitrary, so please let me know if another time would work better for you. Thank you.

Very truly yours,

HACKETT BEECHER & HART,


Brent W. Beecher

Enclosure

cc: Larry Beck, MOE # PK 61555

CP133

APPENDIX B

RECEIVED

JAN 02 2004

LAW OFFICES OF
ROBERT B. GOULD

COPY

IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON
COUNTY OF SAN JUAN

MUTUAL OF ENUMCLAW INSURANCE
COMPANY,

Plaintiff,

v.

DAN PAULSON CONSTRUCTION INC.,
a Washington corporation, KAREN and
JOSEPH MARTINELLI, and the marital
community composed thereof,

Defendants.

NO. 03-2-05168-4

SUBPOENA DUCES TECUM TO
RICHARD MANNING FOR
DEPOSITION UPON WRITTEN
QUESTIONS

THE STATE OF WASHINGTON TO:

J. RICHARD MANNING
500 Union Street, Suite 925
Seattle, WA 98101

GREETINGS:

YOU ARE HEREBY COMMANDED to be and appear at the Law Office of J. Richard Manning, 500 Union St., Suite 925, Seattle, Washington, on Friday the 23rd day of January, 2004, at the hour of 10:00 A.M., of said day, then and there to testify as a witness at the request of the plaintiffs in the above-entitled cause, and to remain in attendance upon a Notary Public from the office of Leslee Unti & Co., 501 Kirkland Ave., No. 102, Kirkland, Washington, until discharged; and to

SUBPOENA TO MANNING - 1

Law Offices of
HACKETT BEECHER & HART
1601 Fifth Avenue, Suite 2200
Seattle, Washington 98101-1651
(206) 624-2200

CP 125

1 A. Answer the Following Questions:

2
3 1. Were you the arbitrator in the matter of Karen and Joseph Martinelli v. Dan Paulson
4 Construction, Inc?

5 2. On what date did that arbitration commence?

6 3. On what date did that arbitration terminate?

7
8 4. Have you made an award?

9
10 5. If so, what was that award?

11 6. Identify all of the witnesses called by the Martinellis.

12
13 7. For each witness identified in response to deposition question No. 6, provide a brief
14 summary of that witness's testimony.

15 8. For each witness identified in response to deposition question No. 6, describe what
16 elements of that witness's testimony you found to be credible, to the extent your award was
based on that testimony.

17 9. For each witness identified in response to deposition question No. 6, describe what
18 elements of that witness's testimony you did not find to be credible, to the extent that your award
19 was based on that testimony.

20 10. Identify the witnesses called by Dan Paulson Construction, Inc.

21 11. For each witness identified in response to deposition question No. 10, provide a brief
22 summary of that witness's testimony.

1 12. For each witness identified in response to deposition question No. 10, describe what
2 elements of that witness' testimony you found to be credible, to the extent that your award was
3 based on that testimony.

4 13. For each witness identified in response to deposition question No. 10, describe what
5 elements of that witness' testimony you did not find to be credible, to the extent your award was
6 based on that testimony.

7 14. If you found in favor of the Martinellis, describe in detail each construction defect for
8 which you awarded damages, and indicate the amount of damages you awarded for each.

9 15. For each construction defect identified in response to deposition question No. 14, identify
10 the contractor, subcontractor, or other entity which actually performed the work out of which the
11 defect arose.

12 16. If you found in favor of the Martinellis on their "stigma" claim, identify each specific
13 element of damage to the Martinellis' residence that you concluded resulted in the "stigma."

14 17. For each element of damage identified in response to deposition question No. 16, identify
15 the contractor, subcontractor, or other entity which actually performed the work out which the
16 damage arose.

17 B. Bring with You a Copy of the Following:

18 1. All documents submitted to you as evidence, from any source, in the Arbitration of *Karen
19 and Joseph Martinelli v. Dan Paulson Construction, Inc.*

20 2. All correspondence between you and the parties, including, but not limited to, the
21 Arbitration Award.

22 HEREIN FAIL NOT AT YOUR PERIL

23 DATED this 30th day of December, 2003.

24 HACKETT, BEECHER & HART

25 
26 Brent W. Beecher, WSBA #31095
Attorney for Plaintiffs

APPENDIX C

Inside the Legislature

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TITLES >> [WAC 284 TITLE](#) >> [WAC 284 - 30 CHAPTER](#)

[284-30-300](#) << [284-30-310](#) >> [284-30-320](#)

WAC 284-30-310 Scope. This regulation applies to all insurers and to all insurance policies and insurance contracts. This regulation is not exclusive, and acts performed, whether or not specified herein, may also be deemed to be violations of specific provisions of the insurance code or other regulations.

[Statutory Authority: RCW [48.02.060](#) and [48.30.010](#). 78-08-082 (Order R 78-3), § 284-30-310, filed 7/27/78, effective 9/1/78.]



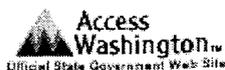
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TITLES >> WAC 284 TITLE >> WAC 284 - 30 CHAPTER

284-30-320 << 284-30-330 >> 284-30-340

WAC 284-30-330 Specific unfair claims settlement practices defined. The following are hereby defined as unfair methods of competition and unfair or deceptive acts or practices in the business of insurance, specifically applicable to the settlement of claims:

- (1) Misrepresenting pertinent facts or insurance policy provisions.
- (2) Failing to acknowledge and act reasonably promptly upon communications with respect to claims arising under insurance policies.
- (3) Failing to adopt and implement reasonable standards for the prompt investigation of claims arising under insurance policies.
- (4) Refusing to pay claims without conducting a reasonable investigation.
- (5) Failing to affirm or deny coverage of claims within a reasonable time after proof of loss statements have been completed.
- (6) Not attempting in good faith to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear. In particular, this includes an obligation to effectuate prompt payment of property damage claims to innocent third parties in clear liability situations. If two or more insurers are involved, they should arrange to make such payment, leaving to themselves the burden of apportioning it.
- (7) Compelling insureds to institute or submit to litigation, arbitration, or appraisal to recover amounts due under an insurance policy by offering substantially less than the amounts ultimately recovered in such actions or proceedings.
- (8) Attempting to settle a claim for less than the amount to which a reasonable man would have believed he was entitled by reference to written or printed advertising material accompanying or made part of an application.
- (9) Making claims payments to insureds or beneficiaries not accompanied by a statement setting forth the coverage under which the payments are being made.
- (10) Asserting to insureds or claimants a policy of appealing from arbitration awards in favor of insureds or claimants for the purpose of compelling them to accept settlements or compromises less than the amount awarded in arbitration.
- (11) Delaying the investigation or payment of claims by requiring an insured, claimant, or the physician of either to submit a preliminary claim report and then requiring subsequent submissions which contain substantially the same information.
- (12) Failing to promptly settle claims, where liability has become reasonably clear, under one portion of the insurance policy coverage in order to influence settlements under other portions of the insurance policy coverage.
- (13) Failing to promptly provide a reasonable explanation of the basis in the insurance policy in relation to the facts or applicable law for denial of a claim or for the offer of a compromise settlement.
- (14) Unfairly discriminating against claimants because they are represented by a public adjuster.

(15) Failure to expeditiously honor drafts given in settlement of claims. A failure to honor draft within three working days of notice of receipt by the payor bank will constitute a violation of this provision. Dishonor of any such draft for valid reasons related to the settlement of the claim will not constitute a violation of this provision.

(16) Failure to adopt and implement reasonable standards for the processing and payment of claims once the obligation to pay has been established. Except as to those instances where the time for payment is governed by statute or rule or is set forth in an applicable contract, procedures which are not designed to deliver a check or draft to the payee in payment of a settled claim within fifteen business days after receipt by the insurer or its attorney of properly executed releases or other settlement documents are not acceptable. Where the insurer is obligated to furnish an appropriate release or settlement document to an insured or claimant, it shall do so within twenty working days after a settlement has been reached.

(17) Delaying appraisals or adding to their cost under insurance policy appraisal provisions through the use of appraisers from outside of the loss area. The use of appraisers from outside the loss area is appropriate only where the unique nature of the loss or a lack of competent local appraisers make the use of out-of-area appraisers necessary.

(18) Failing to make a good faith effort to settle a claim before exercising a contract right to an appraisal.

(19) Negotiating or settling a claim directly with any claimant known to be represented by an attorney without the attorney's knowledge and consent. This does not prohibit routine inquiries to an insured claimant to identify the claimant or to obtain details concerning the claim.

[Statutory Authority: RCW 48.02.060, 48.44.050 and 48.46.200. 87-09-071 (Order R 87-5), § 284-30-330, filed 4/21/87. Statutory Authority: RCW 48.02.060 and 48.30.010. 78-08-082 (Order R 78-3), § 284-30-330, filed 7/27/78, effective 9/1/78.]

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**WASHINGTON ADMINISTRATIVE CODE
TITLE 284. INSURANCE COMMISSIONER, OFFICE OF
CHAPTER 284-30. TRADE PRACTICES
UNFAIR CLAIMS SETTLEMENT PRACTICES**

Current with amendments adopted through June 1, 2005

284-30-370. Standards for prompt investigation of claims.

Every insurer shall complete investigation of a claim within thirty days after notification of claim, unless such investigation cannot reasonably be completed within such time. All persons involved in the investigation of a claim shall provide reasonable assistance to the insurer in order to facilitate compliance with this provision.

Statutory Authority: RCW 48.02.060 and 48.30.010. 78-08-082 (Order R 78- 3), S 284-30-370, filed 7/27/78, effective 9/1/78.

<General Materials (GM) - References, Annotations, or Tables>

WA ADC 284-30-370
END OF DOCUMENT

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