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

MUTUAL OF ENUMCLAW INSURANCE COMPANY,

Appellant,

v.

VILLAS AT HARBOUR POINTE OWNERS ASSOCIATION,

Respondent.

RESPONDENT'S BRIEF

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I. STATEMENT OF ISSUES

A. Whether the grant of coverage set forth in an insuring agreement provides coverage for the amount of a judgment that legally obligates the insured to pay because of property damage.

i. Whether doctrines of *res judicata* and collateral estoppel bar an insurer from re-litigating coverage issues adjudicated in an underlying action.

B. Whether any of the Policy exclusions asserted by Enumclaw apply to bar coverage for T&G's loss.

C. Whether an insurer's consent to a settlement by its insured is required as a condition precedent to coverage when the policy language does not expressly require such action.

D. Whether an award of attorneys' fees under Olympic Steamship should be upheld when an insured prevails in an insurance declaratory judgment action.

II. STATEMENT OF THE CASE

A. Introduction

This appeal arises from an insurance declaratory judgment action filed by Appellant Mutual of Enumclaw Insurance Company ("Enumclaw") in King County Superior Court. The declaratory judgment action stems from an underlying condominium construction defect action

in Snohomish County Superior Court ("Construction Suit"). The Construction Suit is currently on review by this Court under *Mutual of Enumclaw Insurance Company v. T&G Construction, Inc. and Villas at Harbour Pointe Owners Association*, Case No. 57679-8-1. This appeal and the Construction Suit appeal have been linked for purposes of oral argument. The factual background and procedural history of the Construction Suit are included in Respondent's Brief in the linked appeal and are adopted and incorporated by reference into this brief. The factual background of the Construction Suit pertaining to the declaratory judgment action is set forth below.

B. T&G's Liability and Extent of Property Damage

In the Construction Suit, numerous summary judgment motions were heard and a two-day, reasonableness hearing (akin to a mini-trial) was held to determine the scope and breadth of T&G's liability for the property damage found at the Villas. (CP 28) The court in the Construction Suit ruled on summary judgment that T&G's work (the siding, building paper and related flashings) was defectively installed. (CP 446) The court relied upon declarations of the parties' experts, who stated that these deficiencies allowed water entry into the building envelope and resulted in property damage to the gypsum, wood sheathing and underlying framing components. (CP 271-401) In support of the

summary judgment, the Association's expert architect testified that T&G's defective work caused property damage:

> Through personal observation and review of photographs of conditions at Villas, I have observed reverse laps, insufficient overlaps, gaps and missing building paper. In my opinion, the improperly installed [building paper] at Villas is not performing and is contributing to the water intrusion at Villas. . . . [t]he misapplication of building paper is consistent throughout the project.
>
> * * *
>
> The absence and/or lack of proper head flashing has contributed to water intrusion and damage to the underlying wall components. . . . In my opinion, all of the penetrations at Villas are not flashed in a manner making them weatherproof.

(CP 328-29)

As a result of the summary judgment order and other evidence, the Association's experts prepared an estimate for the repair of damages relating solely to defective siding. (CP 57) The cost estimate included removal and replacement of all exterior siding in order to repair the rotted and deteriorated gypsum, wood sheathing and framing. Id. The total estimate for repairing the property damage, exclusive of litigation costs and attorneys' fees, was $4,852,268. Id.

In addition to the summary judgment rulings, further evidence of T&G's liability and the extent of property damage to Villas were submitted to the trial court for the reasonableness hearing. (CP 65-609)

T&G's own expert provided a declaration identifying numerous photos where he found water damage at the Villas resulting from defective siding installation. (CP 195) Numerous homeowners also reported water leaks into their units that caused property damage resulting directly from the defective installation of the flashings and building paper. (CP 641)

During the reasonableness hearing, there was substantial testimony as to the precise type of property damage at Villas that resulted from T&G's defectively installed siding, e.g., water intrusion dry rot, deterioration and elevated moisture content to wood sheathing, gypsum sheathing and wood framing components within exterior walls and water intrusion damage to wood trim and gypsum wall board of interior units. (RP 75-77, 83-85, 117-76, 200-46, 269-91, 297-382)[1] The majority of testimony presented during the reasonableness hearing was from expert witnesses. The remaining testimony was provided by the parties and an Enumclaw adjuster that focused primarily on T&G's purported dissolution and circumstances surrounding the settlement and damages. (RP 26-90; 389-404)

The expert testimony focused almost exclusively on the results of the intrusive investigations; which, in essence, addressed "coverage"

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[1] RP from the linked appellate case, Case No. 57679-8-1.

issues identifying the type and scope of property damage. There were over 105 photos entered into evidence that showed physical damage to property that resulted from T&G's defective siding installation. (Reasonableness Hearing Exhibit 1: Photos from Interface Management, Inc.; Reasonableness Hearing Exhibit 3: Color Photos of Building)[2] The remainder of the expert testimony involved cost of repair of the damaged property.[3] In addition to the live testimony, a plethora of documentary evidence involving property damage to Villas (including hundreds of additional photographs) and T&G's purported dissolution was submitted to the court for consideration. (CP 195-260, 466-609)

After two days of hearing evidence, including live testimony from the parties, construction consultants and cost estimators and reviewing over 2,800 pages of evidence, the court determined that the reasonable repair of the property damage caused by T&G's work was a complete removal and replacement of all siding and building paper, also referred to as a "strip-and-reclad" of the buildings' exteriors:

> ***It is very likely plaintiff standing in C.A.'s shoes would have been able to prove the need for total removal of siding and building paper.*** Numerous invasive investigative openings done at the Villas

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[2] Reasonableness Hearing exhibits are designated from the linked appellate case.

[3] See Reasonableness Hearing Exhibits 3, 6, 7.

> condominiums during discovery showed that the building paper underneath all the siding was misapplied in a manner causing water intrusion. The barrier had gaps, holes and tears. ***The building paper and flashing problems were proved to be pervasive. Rot, decay and elevated moisture levels were already showing on buildings only a few years old.***

(CP 627) Not only was a strip-and-reclad necessary, but the trial court also recognized T&G's clear liability:

> The evidence clearly showed T&G breached its contracts with Construction Associates by installing weather resistive barrier under siding and flashing in a manner that did not meet even minimal code requirements. The evidence was overwhelming and largely unrefuted that this work was done incorrectly, not even to basic minimum code requirements, and in a manner so as to facilitate future water infiltration into the building. Evidence in the record was unrefuted that reverse lap of the building paper actually caused water to be trapped into the buildings rather than away from the buildings as intended.

(CP 628)

Even Enumclaw believed that a strip-and-reclad was necessary. In an internal Enumclaw memorandum, the Director of Litigation stated to the Vice President of Claims that there was a "*substantial likelihood that the exposure is more likely to be the strip-and-reclad rather than the surgical repair.*" (CP 638) The Director also admitted that he believed construction repair costs alone at Villas likely ranged from $1.25 to $1.75 million. (CP 639)

After the evidence was presented by the Association, T&G ***and*** Enumclaw during the reasonableness hearing, the court in the Construction Suit determined that $3,000,000.00 was a reasonable settlement amount. (CP 623) On March 17, 2005, after the settlement was determined reasonable, the Association entered judgment against T&G. (CP 1330)

C. The Insuring Agreement Between Enumclaw and T&G.

At the time Villas was constructed, Enumclaw insured T&G under a standard form commercial general liability policy from October 26, 1996 through October 26, 2000 (the "Policy"). (CP 644) The Policy contains standardized terms and provisions which provide coverage for T&G's liability for "property damage" caused by an "occurrence."[4]

> 1. Insuring Agreement
>
> a. We will pay those sums that the insured becomes legally obligated to pay as damages because of . . . "property damage" to which this insurance applies. We will have the right and duty to defend any "suit" seeking those damages . . . .
>
> * * *

[4] The policy language that Enumclaw appends to its brief does not reflect the complete policy language. For example, Enumclaw does not use the full text of the policy language when it refers to the heading under which the consent clause is referred. The heading should read: "Section IV – Commercial General Liability Conditions". Therefore, a copy of the policy is attached hereto as an Appendix. See also CP 644.

> b. This insurance applies to . . . "property damage" only if:
>
> > (1) The . . . "property damage" is caused by an "occurrence" that takes place in the "coverage territory"; and
> >
> > (2) The . . . "property damage" occurs during the policy period.

(CP 644)

"Property damage" is defined in the Policy to mean physical injury to tangible property. (CP 655) "Occurrence" means an "accident, including continuous or repeated exposure to substantially the same general harmful conditions." (CP 654)

Whether T&G's defective installation of siding that led to water intrusion and pervasive rot, decay and deterioration of the sheathing, gypsum and framing beneath the siding constitutes an "occurrence" is not disputed. Whether the occurrence occurred during the policy period and in the coverage territory also is not disputed. This "occurrence" caused "property damage" – physical injury to tangible property – as that term is defined in the Enumclaw policy.

By letter dated July 10, 2003, Enumclaw agreed to defend T&G in the Construction Suit, reserving its right to decline payment of that portion of any settlement or judgment representing damages not covered by the

Policy. (CP 656) On September 15, 2004, Enumclaw filed the declaratory judgment action from which this appeal arises. (CP 1)

D. The Declaratory Judgment Action

In the declaratory judgment action, Enumclaw asserted that the Policy did not provide coverage, but if it did, exclusions "m. Damage to Impaired Property or Property Not Physically Injured"; "n. Recall of Products, Work or Impaired Property"; and "l. Damage to Your Work" excluded coverage for T&G's loss. (CP 1-4) In response, the Association and T&G requested extra-contractual relief for Enumclaw's bad faith in failing to indemnify T&G when liability was reasonably clear. (CP 714-26)

In three summary judgment motions, the Association and T&G proved: (1) T&G became legally obligated to pay damages because of property damage; (2) none of the exclusions in the Policy asserted by Enumclaw applied to bar coverage; and (3) the damages that T&G became legally obligated to pay amounted to $3,000,000 – the amount that the court in the Construction Suit deemed reasonable. (CP 763, 1173, 1347) Following the court's determination of coverage, a final judgment was entered against Enumclaw on January 18, 2006 in the amount of $3,516,046.89. (CP 1467) The judgment against Enumclaw included the $3,000,000.00 judgment against T&G, plus interest, costs and attorneys'

fees. Id. Each of the summary judgment orders issued in the declaratory judgment action has been assigned error by Enumclaw in this appeal.

III. SUMMARY OF ARGUMENT

The Judgment entered against T&G constitutes a legal obligation to pay. Despite Enumclaw's repeated attempts to re-argue T&G's liability and scope and extent of damages in the declaratory judgment action, the trial court properly ruled that the legal and factual issues that supported the Judgment already were heavily contested and litigated between T&G, the Association, *and* Enumclaw in the Construction Suit via summary judgment motions and the two-day reasonableness hearing. With respect to the Policy exclusions asserted by Enumclaw, the trial court properly ruled that (1) the property damage is not to "impaired" property; (2) T&G's product was not withdrawn or recalled from the market; and (3) the "your work" exclusion does not apply because the property damage that T&G became liable for was damage to the work of others. Consent is not a condition precedent to coverage under the Enumclaw Policy. Because the trial court properly ruled that coverage exists and none of the exclusions applied, the rulings and judgment against Enumclaw should be upheld.

IV. ARGUMENT

A. T&G Became "Legally Obligated to Pay" the Association in the Construction Suit.

1. Judgment Was Entered Against T&G.

Enumclaw argues there is no coverage because T&G never became "legally obligated to pay" damages in the Construction Suit. Enumclaw's contention is incorrect. The Judgment Against T&G Construction, Inc. entered on March 17, 2005 in the Construction Suit ("the Judgment") constitutes a "legal obligation to pay."

A judgment entered against a party obligates that party to pay the amount of the judgment, or more broadly speaking, "a judgment is an obligation for the payment of money." 49 C.J.S. Judgments § 6. Accordingly, the Judgment against T&G constitutes the subcontractor's "legal obligation to pay" the Association. In East v. Fields, the Washington Supreme Court stated the guidelines for determining the effect of a judgment entered against an insured in a prior action:

> The rule is that when an insurer has notice of an action against an insured, and is tendered an opportunity to defend, ***it is bound by the judgment*** therein upon the question of the insured's liability.

East v. Fields, 42 Wn.2d 924, 925, 259 P.2d 639 (1953) (citations omitted) (emphasis added).

Here, Enumclaw contends that the Judgment was based on alleged errors the court in the Construction Suit made on summary judgment and at the reasonableness hearing regarding issues of dissolution and damages. But such argument is not properly before this Court. In proffering its argument, Enumclaw completely ignores East v. Fields and a separate body of Washington law that governs the exact facts and circumstances of the T&G/Association settlement, including entry of consent judgment with a covenant not to execute. In Besel v. Viking Ins. Co. of Wis., 146 Wn.2d 730, 49 P.3d 887 (2002), the Supreme Court described the effect on the insurer resulting from a judgment entered against its insured:

> We hold 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 under the *Chaussee* criteria. This approach promotes reasonable settlements and discourages fraud and collusion. Furthermore, using the amount of a covenant judgment to measure tort damages in this context makes sense in light of our long standing requirement that such settlements be reasonable. ***If a reasonable and good faith settlement amount of a covenant judgment does not measure an insured's harm, our requirement that such settlements be reasonable is meaningless***. Finally, the *Chaussee* criteria protect insurers from excessive judgments especially where, as here, the insurer has notice of the reasonableness hearing and has an opportunity to argue against the settlement's reasonableness.

Id. at 738-39 (emphasis added). The progeny of appellate court opinions before and after Besel hold that a consent or stipulated judgment with a covenant not to execute constitutes both an insured's and an insurer's ***legal obligation to pay***, as long as the consent judgment is not a result of unreasonableness, collusion or fraud. See Red Oaks Condo. Ass'n. v. Sundquist Holdings, Inc., 128 Wn. App. 317, 322, 116 P.3d 404 (2005); Howard v. Royal Spec. Underwriting, Inc., 121 Wn. App. 372, 89 P.3d 265 (2004); Chaussee v. Maryland Casualty Co., 60 Wn. App. 504, 803 P.2d 1339 (1991); Meyer v. Dempcy, 48 Wn. App. 798, 740 P.2d 383 (1987); Steinmetz v. Hall-Conway-Jackson, Inc., 49 Wn. App. 223, 741 P.2d 1054 (1987); Kagele v. Aetna Life & Cas. Co., 40 Wn. App. 194, 698 P.2d 90 (1985).

The law in Washington does not require a trier of fact to determine the extent of an insured's liability in circumstances present here. See Equilon Enterprises LLC v. Great Am. Alliance Ins., Co., __ Wn. App. __, 132 P.3d 758, 763 (2006) (insurer had a duty to indemnify insured for amount of settlement because same facts that created insurer's duty to indemnify also caused insured to settle with plaintiff). Instead, the courts look to the trial court's reasonableness hearing to ensure the settlement was reasonable and did not involve collusion or fraud. This process is exactly what occurred in the Construction Suit, when the court considered

substantial evidence in determining T&G's liability and obligation to pay the Association $3,000,000. To rule that the Judgment does not constitute a "legal obligation to pay" would vitiate the court's Findings of Fact and Conclusions of Law and ignore well-established Washington case authority.

In Finney v. Farmers Ins. Co., 21 Wn. App. 601, 586 P.2d 519 (1978), aff'd, 92 Wn.2d 748, 600 P.2d 1272 (1979), the court held that when an insurer has notice of an action and an opportunity to participate, it is bound by the judgment against its insured on liability questions and bound by any material fact essential to the liability judgment that is also decisive of coverage under the policy. Finney, 21 Wn. App. at 617. A subsequent decision, Wear v. Farmers Ins. Co. of Wash., 49 Wn. App. 655, 745, P.2d 526 (1987), noted an exception to this rule, but only if the insurer's interest in defending were not "in harmony with the insured's intent." Id. at 659-60. The court further stated: "When the insurer has the same interest as the insured in disputing liability and damage issues, it is fair to treat the insurer as a party for collateral estoppel purposes." Id. at 660. Here, there is every indication Enumclaw's interest in minimizing T&G's liability and property damage at Villas was in lock-step with its insured's identical interest. Moreover, Enumclaw actively participated in

the reasonableness hearing. Thus, the Judgment entered against T&G constitutes the insured's "legal obligation to pay."

2. *Issues of Liability Pertaining to Damages and Purported Dissolution Were Litigated and Determined in the Construction Suit.*

Enumclaw contends that T&G never became "legally obligated" to pay the Association due to the insured's purported dissolution. The insurer argues that it should have had an opportunity to re-litigate T&G's liability in this declaratory judgment action. Enumclaw's argument is without merit. T&G's liability was heavily litigated in the Construction Suit by both T&G ***and*** Enumclaw. (CP 443-64, 623-37) Thus, the trial court properly barred re-litigation of these issues under the doctrines of *res judicata* and collateral estoppel.

In the Construction Suit, numerous summary judgment motions were heard and a two-day mini-trial was held to determine the scope and breadth of T&G's liability. (CP 271-323, 325-66, 443-64) It was proven and judicially decided that: (1) T&G defectively installed the siding at Villas; (2) such defective installation led to water intrusion into the buildings; (3) the water intrusion resulted in pervasive rot, deterioration and decay of framing, wood sheathing and gypsum; (4) a complete removal and re-clad of the buildings' siding was necessary to repair the damage; (5) the amount of construction costs alone to complete repairs

ranged from $2.8 to $4.8 million; (6) T&G was liable to the Association, notwithstanding the subcontractor's purported dissolution; and (7) the amount of $3,000,000 in judgment against T&G was proper. (CP 443-64, 623-37) Based upon the outcome of these heavily litigated issues, the Judgment was entered against T&G which *legally obligates T&G to pay.*

3. The Doctrines of Res Judicata and Collateral Estoppel Bar Enumclaw from Re-litigating Damages and T&G's Liability in the Declaratory Judgment Action.

Not only does Besel and its progeny dictate that Enumclaw is bound by the Judgment entered against T&G, but additional authority on the doctrines of *res judicata* and collateral estoppel also apply. An insurer is bound by a judgment obtained by the insured if the insurer had the opportunity to participate in the underlying case. Lenzi v. Redland Ins. Co., 140 Wn.2d 267, 273-75, 996 P.2d 603 (2000); Fisher v. Allstate Ins. Co., 136 Wn.2d 240, 961 P.2d 350 (1998); Finney v. Farmers Ins. Co., 21 Wn. App. 601, 586 P.2d 519 (1978), aff'd, 92 Wn.2d 748, 600 P.2d 1272 (1979); Waite v. Aetna Cas. & Sur. Co., 77 Wn.2d 850, 467 P.2d 847 (1970). The opportunity to intervene allows the insurer to protect its interests against collusive judgments. At the same time, the insured is not

forced to endure multiple actions in order to obtain its insurance benefits. The operative principle,[5] according to the Lenzi court, is *res judicata*:

> Res judicata refers to 'the preclusive effect of judgments, including the relitigation of claims and issues that were litigated, *or might have been litigated*, in a prior action.' *Loveridge v. Fred Meyer, Inc.*, 125 Wn.2d 759, 763, 887 P.2d 898 (1995) (emphasis added) (quoting Philip A. Trautman, Claim and Issue Preclusion in Civil Litigation in Washington, 60 Wash. L. Rev. 805, 805 (1985)). The key consideration is Redland 'might have litigated' the damages at issue, but chose not to by not intervening in Lenzi's action against Davis. Thus, Redland is not so much estopped to deny coverage for damages as it is *barred* from litigating the question now. . . . Redland could have and should have litigated the damage claim by intervening in the Lenzi's case against Davis. Claim preclusion prevents Redland from litigating the damage award now.

Lenzi, 140 Wn.2d at 280. See also Fisher, 136 Wn.2d at 249 (forcing the insured to re-litigate liability and damages issues only fosters inconsistent judgments and additional delay and expense for the insured). In Lenzi, the defendant neglected to intervene. Here, in contrast, Enumclaw did intervene and litigated coverage issues in the Construction Suit. Thus, in addition to *res judicata*, Enumclaw also is precluded by collateral estoppel from re-litigating the liability issue in the declaratory judgment action.

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[5] In Lenzi, the Supreme Court articulated this principle as the *Finney-Fisher* rule.

If this Court were to rule otherwise, the impact would sweep aside the entire two-day reasonableness hearing and previous summary judgment rulings by the court in the Construction Suit. As articulated by this Court in Howard, 121 Wn. App. at 379, such a ruling would contravene the Supreme Court's holding in Besel:

> [The insurer] also argues that the timing of the hearing was inappropriate because the reasonableness hearing was essentially the damages phase of the bad faith action. . . . The fact that a reasonableness determination may have this impact is not a basis to conclude that the procedure is not appropriate, as the Supreme Court, in *Besel,* has already held that a reasonableness hearing in this situation is appropriate.

The Supreme Court's rationale for ruling that damages in an insurance bad faith or declaratory judgment action should be litigated in the underlying case rather than in the coverage action is based on sound reasoning. Otherwise, the parties would have to re-litigate the exact factual issues previously litigated in the underlying action. In this case, such re-litigation would include: the extent of property damage at Villas, extent of T&G's liability for such damages, scope of T&G's work under its contract with the general contractor, corporate status of T&G following construction of Villas and other ancillary issues. Such re-litigation of previously determined factual and legal issues would be unambiguous

violations of the doctrines of collateral estoppel and *res judicata*.[6] To hold otherwise would mean that an insurance company would never have to indemnify an insured who settles with a plaintiff unless a full trial were held and a trier of fact were to determine the precise extent of the insured's liability. This is not the law in Washington.[7]

4. Enumclaw Ignores an Entire Body of Law Concerning Damages in Insurance Coverage Actions.

Enumclaw's argument that T&G's legal liability was not determined in the Construction Suit and that the insurer is "entitled to an actual adjudication of T&G's alleged legal obligation to pay" rests solely on three cases: Yakima Cement Products Co. v. Great Am. Ins. Co., 14 Wn. App. 557, 544 P.2d 763 (1975); Nelson v. Sponberg, 51 Wn.2d 371, 318 P.2d 951 (1957); and Gilbert H. Moen Co. v. Island Steel Erectors, Inc., 128 Wn.2d 745, 912 P.2d 472 (1996). Yakima Cement is a 1975 case that predates Besel and its progeny. Nelson and Moen are straight indemnity cases completely unrelated to insurance declaratory judgment actions. These cases are inapposite to the instant action. None involved

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[6] See Lenzi, supra; Finney, supra; Wear, supra.

[7] See Besel, supra; Red Oaks, supra; Howard, supra; Lenzi, supra; Finney, supra; Fisher, supra; Wear, supra.

facts where the predicate for indemnification under an insurance contract had been judicially determined.

In Yakima Cement, an insured subcontractor entered into a settlement with a contractor and the parties entered agreed findings of fact, conclusions of law and a judgment embodying their settlement. In the agreed findings, ***no property damage had been alleged***. Yakima Cement, 14 Wn. App. at 559-60. The subcontractor's insurer refused to defend or indemnify the insured, and the insured filed a breach of contract action in state court against the insurance company. Division III of the Court of Appeals held that coverage issues in the federal court were never litigated. Id. at 562. Accordingly, the court overturned the trial court's granting of summary judgment in favor of the insured and remanded the case to the trial court to litigate the issues of coverage (i.e., property damage). In reaching its ruling, however, the court highlighted that there were cases where issues regarding coverage could be litigated in the underlying liability action:

> [T]he doctrine of collateral estoppel ***applies in a proper case***. This doctrine is that the insurer is bound by any material finding of fact essential to the judgment of tort liability, which is also decisive of the question of the coverage of the policy of insurance. Restatement, Judgments 293 § 68. It would, of course, be anomalous for a court to find such a critical fact one way in the tort action, and to the opposite effect in the garnishment proceeding.

Id. at 561 (emphasis added) (citing East v. Fields, 42 Wn.2d at 925).

The instant action is exactly the type of "proper case" under East. Unlike Yakima Cement — where no property damage was alleged, no reasonableness hearing held, no summary judgment hearings conducted, only agreed findings and judgment entered and no involvement by the insurer — in the Construction Suit, Enumclaw intervened and litigated the issues of liability and damages. Enumclaw filed and argued pre- and post-reasonableness hearing motions and aggressively challenged the Association on the issues of T&G's purported dissolution, property damage and monetary damages throughout the entire reasonableness hearing. (CP 63) (CP* 39-81, 95-100, 812-14)[8]

In Nelson, a building owner was sued by a person injured on his premises. The owner sought indemnity from the contractor who constructed an allegedly defective staircase. After settling with the victim, the owner sued the contractor for the amount of the settlement under a theory of indemnity. Testimony during the trial was inconclusive as to proximate cause of the victim's injury. Nelson, 51 Wn.2d at 373. Thus, the court overturned the trial court's ruling that the owner was entitled to be indemnified by the contractor. The court found that if an indemnitee

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[8] *Clerk's Papers from the linked appellate case, incorporated by reference herein.

pays without suit, "he is under the necessity of proving that he was liable for the amount thus paid." Id. at 376.

In Moen, a subcontractor was required to contractually indemnify a general contractor for personal injuries suffered by third parties on the job site in connection with the subcontractor's services, unless the general contractor's negligence was the sole cause of the injury. Moen, 128 Wn.2d at 747. The general contractor settled a personal injury lawsuit and sought indemnity from the subcontractor. The settlement did not resolve whose negligence caused the injury. Therefore, in the indemnity action, the general contractor was required to prove that the subcontractor's negligence caused the injury. Id. at 763. The Moen case, analogous to Nelson, merely states that an indemnitee cannot automatically recover a settlement amount, but must prove the amount of the settlement under the "actual liability" standard. But application of any "actual liability" rule depends on the particular facts and indemnity language at issue, and must be analyzed on a case by case basis. In re Paragon Trade Brands, Inc., 324 B.R. 829, 869 (Bankr. N.D. Ga. 2005) (applying Washington indemnity law).

In Moen and Nelson, unlike the present action, the basis for triggering indemnity under the contract had not been determined in either the underlying personal injury action or the indemnity action. In the

Construction Suit, however, the predicate facts demonstrating property damage and obligation to pay were adjudicated on summary judgment and during the reasonableness hearing.

Lastly, Enumclaw relies upon Ballard Square Condo. Owners Ass'n v. Dynasty Constr. Co., 126 Wn. App. 285, 108 P.3d 818 (2005), for the proposition that T&G was not "legally obligated to pay" on the Judgment. But as argued in the linked appellate case under review by this Court and incorporated by reference herein, Enumclaw's reliance upon Ballard Square is misplaced. Enumclaw does not have standing to step into the shoes of its insured and attempt to overturn a summary judgment ruling entered in the Construction Suit, an entirely different action than this declaratory judgment case. Felter v. McClure, 135 Wash. 410, 413, 237 P. 1010 (1925) ("The right to object belongs to the party appearing, and not to a third party seeking later to attack the proceedings."). Standing, collateral estoppel, *res judicata* and equitable estoppel bar Enumclaw from re-litigating dissolution and damages issues in this action.

The trial court's 15-page Findings of Fact and Conclusions of Law, and the live testimony of seven witnesses and experts and over 2,800 pages of documentary evidence, provide substantial proof that coverage issues pertaining to T&G's purported dissolution and the Association's damages were litigated in the Construction Suit. Yakima Cement, Nelson,

Moen and Ballard Square are inapposite. Instead, the *Finney-Fisher* rule and Besel and its progeny apply. Consequently, the Judgment entered against T&G in the Construction Suit, wherein Enumclaw participated in the action and meaningfully participated in the reasonableness hearing, binds Enumclaw in the declaratory judgment action.

B. Because a Consent Judgment Was Entered Against T&G, RCW 4.60 Does Not Apply.

Enumclaw argues that the Judgment entered against T&G was a confessed judgment and as such, failed to comply with the statutory requirements governed by RCW 4.60, et seq. Enumclaw's argument is erroneous because the judgment entered by the court in the Construction Suit was a *consent* judgment and not a *confessed* judgment. Enumclaw improperly interchanges the two types of judgments in its brief.

Multiple jurisdictions have stated that consent judgments and judgments by confession are not one in the same. Each is a separate and distinct type of judgment. See Nat'l Hygienics, Inc. v. Southern Farm Bureau Life Ins. Co., 707 F.2d 183, 186 (5th Cir. 1983); Russell v. Sheahan, 927 P.2d 591, 593-94 (Or. 1996); Fry v. Coyote Portfolio, LLC, 739 A.2d 914 (Md. Ct. Spec. App. 1999); see also, 46 Am.Jur.2d Judgments §§ 207-264; 49 C.J.S. Judgments § 138.

RCW 4.60, et seq. provides requirements for a judgment by confession, not a consent judgment. A judgment by confession is entered pursuant to the voluntary act or agreement of *one* party. See Russell v.

Sheahan, 927 P.2d at 593. It is a unilateral concession by the defendant that plaintiff's cause is just and right. Nat'l Hygienics, 707 F.2d at 186. Black's Law Dictionary defines "confession of judgment" as follows:

> At common law, judgment entered where defendant, instead of entering plea, confessed action, or withdrew plea and confessed action. Judgment where a defendant gives the plaintiff a cognovits or written confession of the action by virtue of which the plaintiff enters judgment. The act of a debtor in permitting judgment to be entered against him by his creditor, for a stipulated sum, by a written statement to that effect or by warrant of attorney, ***without the institution of legal proceedings of any kind; voluntary submission to court's jurisdiction***.

Black's Law Dictionary (6th Ed.) (emphasis added).

In contrast, a consent judgment is a judgment entered with the consent of *both* the party against whom the judgment is entered *and* the party in whose favor the judgment is entered. See Nat'l Hygienics, 707 F.2d at 186 (consent judgment is in the nature of a bilateral contract as to what the decision should be); Russell v. Sheahan, 927 P.2d at 594. Washington courts have stated that a judgment by consent, or stipulation of the parties, is construed as a contract between them that embodies the terms of the judgment. See, e.g., Wash. Asphalt Co. v. Harold Kaeser Co., 51 Wn.2d 89, 316 P.2d 126 (1957).

In Nat'l Hygienics, there were extensive negotiations between the parties over the settlement of the claims. The final decree ultimately limited the assets which National could draw upon to satisfy its judgment

by allowing the other party to retain an override interest. As such, the final decree was far less than what National had asked for. The court found that the decree was a compromise of a suit and not a confession of judgment. Nat'l Hygienics, 707 F.2d at 187.

Here, as in Nat'l Hygienics, the judgment that was entered into between T&G and the Association was a consent judgment, as it was stipulated by both parties and constituted extensive negotiations and compromise of a two-year long lawsuit. The Judgment was entered only after the court ruled on the reasonableness of the parties' settlement. Thus, because the judgment entered into between T&G and the Association was a consent judgment, RCW 4.60, et seq. is inapplicable.

C. The $3,000,000 That T&G Became Legally Obligated to Pay in the Construction Suit Resulted From Property Damage.

The trial court accurately determined that T&G became legally obligated to pay $3,000,000 as damages. This amount directly results from the property damage that exists at Villas. Enumclaw argues that there is no coverage for property damage that does not exist; where no leaks have been reported in the siding. The Association and T&G do not dispute that the Policy only covers property damage; to assert otherwise would be inaccurate. However, if Enumclaw's reasoning were followed, an investigation which opened *all* of the buildings' siding in order to determine where leaks did and did not occur would be required.

Notwithstanding that extent and type of damage at Villas was litigated and decided numerous times in favor of the Association in both the Construction Suit and in the declaratory judgment action, the fact remains that the defects and damages related to the defective installation of siding necessitates a complete removal and reclad of the buildings' siding. Enumclaw ignores the fact that comprehensive investigation of all 23 buildings included 40-plus intrusive investigative openings performed by scores of experts and construction professionals representing over a dozen parties. The findings from these investigations supported the construction experts' conclusion that a complete strip-and-reclad of the siding was necessary. (CP 271-366, 466-585, 623-37) Even experts from the defense admitted widespread damage throughout Villas. (CP 195-260, 466-585) Therefore, it is no surprise that the court in both the Construction Suit and in the declaratory judgment action correctly determined that the $3,000,000 in damages was a reasonable amount that T&G became "legally obligated to pay."

Enumclaw's reliance on Fid. & Deposit Co. of Maryland v. Hartford Cas. Ins. Co., 215 F. Supp. 2d 1171 (D. Kan. 2002) for its argument that removal and reclad of all of the siding is not covered is inaccurate, not only because the law is not controlling, but because the facts are not analogous. In Maryland, the "property damage" was the

cracks in masonry walls. Because of a business decision to fix other defects, the owner decided to actually tear down the buildings. The Kansas court held that there was no coverage to tear down and rebuild because there was "lack of physical injury"; mere cracks in the walls did not require demolishment of buildings. Id. at 1183-1184. In the instant case, the property damage to the framing, plywood and gypsum sheathing resulting from the defective siding installation was pervasive, as evidenced in the underlying record. In order to reach and repair this property damage, the siding needed to be removed. But re-siding of the buildings does not come close to tearing down walls or buildings, as was the case in Fid. & Deposit Co. of Maryland.

Because the entire amount of damages that T&G became legally obligated to pay resulted directly from property damage at Villas, it is covered by the terms set forth in the initial grant of coverage of the Enumclaw Policy. Accordingly, this Court should uphold the trial court's determination that the Policy provides coverage.

D. None of the Policy Exclusions Apply to Bar Coverage.

Enumclaw bears the burden of proving that an exclusion negates coverage. See, e.g., Am. Star Ins. Co. v. Grice, 121 Wn.2d 869, 875, 854 P.2d 622 (1993) (insurer bears the burden of proving that a loss is not covered because of an exclusionary provision). Exclusions are strictly

construed against the insurer because they are contrary to the protective purpose of insurance. Id.

The proper construction of policy exclusions is a question of law. Gingrich v. Unigard Sec. Ins. Co., 57 Wn. App. 424, 434, 788 P.2d 1096 (1990). To the extent that any facts are in doubt, they must be construed against the insurer and in favor of coverage. "The terms of an insurance contract must be given their usual, ordinary meaning unless the entirety of the agreement demonstrates a contrary intent. If a contractual provision is ambiguous, it must be construed against the insurer even though the insurer may have intended another meaning." Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Northwest Youth Servs., 97 Wn. App. 226, 230, 983 P.2d 1144 (1999). Likewise, the exclusions themselves must be construed against the insurer. See, e.g., Diamaco, Inc. v. Aetna Cas. & Sur. Co., 97 Wn. App. 335, 342, 983 P.2d 707 (1999) ("Because coverage exclusions 'are contrary to the fundamental protective purpose of insurance,' they are 'strictly construed against the insurer. . . .'").

1. The Property Damage at Villas is Not Damage to "Impaired Property."

Enumclaw asserts that the "impaired property" exclusion bars coverage. However, the trial court properly determined that the water damage, decay, rot and deterioration to the framing, gypsum and wood

sheathing at Villas do not qualify as damage to "impaired property," as defined in the Policy.

According to the exclusion, Enumclaw's insurance does not apply to:

> "Property damage" to "impaired property" or property that has not been physically injured, arising out of:
>
> (1) a defect, deficiency, inadequacy, or dangerous condition in "your product" or "your work"; or
>
> (2) a delay or failure by you or anyone acting on your behalf to perform a contract or agreement in accordance with its terms.
>
> "Impaired property" means: tangible property, other than "your product" or "your work," that cannot be used or is less useful because:
>
> a. it incorporates "your product" or "your work" that is known or thought to be defective deficient inadequate or dangerous; or
>
> b. you have failed to fulfill the terms of a contract or agreement;
>
> If such property can be restored to use by:
>
> a. the repair, replacement, adjustment or removal of "your product" or "your work"; or
>
> b. your fulfilling the terms of the contract or agreement.

This exclusion does not apply because Enumclaw cannot show that T&G's claims satisfy even the first sentence of the exclusion. The Association's damages are neither: (1) "property damage" to "impaired

property;" nor (2) "property damage" to "property that has not been physically injured."

a. "Property damage" to "impaired property"

The first clause of the exclusion is inapplicable. It excludes "property damage" to "impaired property." According to the definition of impaired property, the property subject to the exclusion must be capable of being "restored to use." There is unequivocal evidence in the record that the gypsum, wood sheathing and framing (the damaged property) are water damaged, decaying and/or rotting. Thus, this damage cannot be "impaired property" subject to the exclusion.

The exclusion is also inapplicable to the job site as a whole. The "impaired property" prong of the exclusion only applies if the impaired property can be "restored to use by: a. the repair, replacement, adjustment or removal of [T&G's work]; or b. [T&G's] fulfilling the terms of [its] contract or agreement." Subsection (b) cannot apply because even if T&G came back to "fulfill the terms of [its] contract or agreement," the damage to the other subcontractors' work would still exist.

Other jurisdictions have recognized that unless the replacement of the policy holder's work ***alone*** restores the impaired property ***completely***, the exclusion does not apply. In Federated Mut. Ins. Co. v. Grapevine Excavation, Inc., 197 F.3d 720 (5th Cir. 1999), the Fifth Circuit Court of

Appeals held that the impaired property exclusion did not apply to a road that was less useful because the policy holder had failed to install the subgrade according to specifications. The court reasoned that although the road could be restored to use, it was not through repair or replacement of the policy holder's work, but by adding another topcoat of asphalt. Likewise, the Villas condominium buildings could not be restored to use simply by removal or replacement of T&G's work. Other subcontractors' work, including the work of those subcontractors who installed the gypsum, wood sheathing and framing, has to be torn out and replaced.

Dewitt Constr. Inc. v. Charter Oak Fire Ins. Co., 307 F.3d 1127 (9th Cir. 2002) (applying Washington law) is directly on point. In that case, Dewitt Construction was sued for negligently installing cement piles at a construction project. In the process of remediating this problem, Dewitt damaged the work of other subcontractors. Relying on the impaired property exclusion, Dewitt's insurer denied coverage for this damage. In finding that the impaired property exclusion in fact *did not* apply, the Ninth Circuit Court of Appeals held:

> The "impaired property" exclusion does not bar coverage for property damage to the destroyed work that other subcontractors had performed on the defective piles. The impaired property exclusion, as stated in the policies, only applies "if [the impaired property] can be restored to use by: a) the repair, replacement, adjustment or removal of '[the insured's] product' or '[the insured's] work'; or b)

> [the insured] fulfilling the terms of the contract or agreement." DeWitt's installation of additional piles did not "restore to use" the work of other subcontractors. The other subcontractors' work (e.g., the pile caps) was removed from the defective piles, destroyed in the removal process, and remained destroyed notwithstanding the subsequent remedial work by DeWitt. The destroyed work of other subcontractors was not merely impaired, nor was it restored to use.

Dewitt, 307 F.3d at 1134-35. Similarly, in this case, T&G's defective work resulted in water intrusion into the building's envelope, consequently causing water damage to other subcontractors' work. This damage to property cannot be restored to use; it must be removed and replaced.

b. "Property that has not been physically injured"

The latter provision of the exclusion also does not apply in this case. "Property damage" cannot refer to the "physical injury to tangible property" definition or the exclusion would make no sense: "physical injury to tangible property" to "property not physically injured." Thus, although the exclusion remains ambiguous, it is somewhat less unintelligible when deemed to refer to the definition for "loss of use of tangible property": "This insurance does not apply to 'loss of use of tangible property' to 'property not physically injured.'"

Because damage to the gypsum, wood sheathing and framing constitutes "physical injury to tangible property," not "loss of use of tangible property," this element of the exclusion cannot apply to that

damage. Since there is ample evidence of physical injury to property and no evidence that "impaired property" (as defined in the policy) exists, exclusion "m." the impaired property exclusion cannot apply to bar coverage in this case.

The $3,000,00 damage amount is comprised of the cost to re-side all 23 buildings at Villas, and according to DeWitt, the cost to take T&G's siding off to repair the areas that are property damaged (the framing, plywood and gypsum sheathing) is covered because the siding becomes damaged in the process. Because the damage amount determined by the court in the declaratory judgment action is for the repair of "property damage" that cannot be restored to use, the "impaired property" exclusion does not apply to bar coverage. The court's determination should be affirmed.

2. Recall of Products, Work or Impaired Property Exclusion.

The recall of products, work or impaired property exclusion is commonly referred to as the "sistership exclusion." The term "sistership" was derived from an incident in the aircraft industry in which one plane crashed and its sisterships were thereafter grounded and recalled by the manufacturer in order to correct a common defect which had caused the crash. In Olympic S.S. Co., Inc. v. Centennial Ins. Co., 117 Wn.2d 37,

811 P.2d 673 (1991), the Washington Supreme Court interpreted this exclusion to apply to the sistership, but *not the damaged ship*.

T&G's defective installation of the siding at Villas cannot be analogized to fit this exclusion because in the analogy, the Villas condominium is the "damaged ship"; there are no other sisterships from which damage would be excluded. Moreover, the sistership exclusion applies only if the product or property of which it is a part is "withdrawn from the market or from use", and even in such situations, the policy still covers damages caused by the product that failed. In this case, the "product", "work" or "property" was never withdrawn or recalled from the market or from use. In other words, T&G's or its sub-subcontractors installation of the siding, building paper and related flashings, (its "product," "work" or "property") was neither withdrawn nor recalled from the market or from use. Accordingly, since no recall was involved in this case, and the product was not withdrawn from the market or from use, the trial court's summary judgment order that exclusion "n" does not preclude recovery should be upheld.

Enumclaw cites Federated Serv. Ins. Co. v. R.E.W., Inc., 53 Wn. App. 730, 770 P.2d 654 (1989) in support of its argument that this exclusion applies. But the facts of R.E.W. are not analogous to the case at bar with respect to this exclusion. The main difference is that in R.E.W.,

the *insured* installed the Isoboard product and the Isoboard cracked. That damage to the insured's product/work (the Isoboard) was not a covered loss; there was no coverage for the removal and replacement of it. In the instant case and unlike the contractor in R.E.W., the insured's work/product is not the property that is damaged. The property damage is to the framing, plywood and gypsum sheathing. According to DeWitt, the cost of removing and replacing the siding in order to repair the property damage at Villas is covered. Accordingly, the trial court correctly ruled that exclusion "n. Recall of Products Work or Impaired Property" does not bar coverage.

3. *Property Damage Arose From Work Performed by Others on T&G's Behalf.*

Enumclaw asserts that coverage is barred by Policy exclusion "l. Damage to Your Work" which states that it will not cover "property damage to 'your work' arising out of it or any part of it and included in the 'products-completed operations hazard.'" "Your work" is defined in the policy as "work or operations performed by [the insured] or on [the insured's] behalf." According to this exclusion, Enumclaw will not provide coverage for "property damage" to T&G's work that arises from its own work. In other words, if there is property damage to T&G's work

that *was caused by T&G*, Enumclaw will not provide coverage for that damage.

However, to the extent that T&G's defective work damaged the tangible property of another person, Enumclaw must provide T&G with coverage for that loss. Such is the case here. It is well settled that coverage exists where the defective product causes damage to another person's tangible property. Marley Orchard Corp. v. Travelers Indem. Co., 50 Wn. App. 801, 750 P.2d 1294 (1988); Yakima Cement Products. Co., 93 Wn.2d 210, 608 P.2d 254 (1980). Coverage also extends to consequential damages resulting directly from such injury. Yakima Cement, 93 Wn.2d at 21; Marley Orchard Corp., 50 Wn. App. at 807.

In Yakima Cement, the court held consequential damages resulting from the installation of defective panels in a building were not recoverable because there was no evidence of damage to or a reduced value of the building. Accord Federated Serv. Ins. Co. v. R.E.W., Inc., 53 Wn. App. 730 (defective "Isoboard" incorporated by insured into construction of fruit storage structure; insurer conceded coverage for damage to stored apples, but coverage excluded for costs of replacing insured's own "Isoboard"); Gen. Ins. Co. of Am. v. Int'l Sales Corp., 18 Wn. App. 180, 184, 566 P.2d 966 (1977), rev. denied, 90 Wn.2d 1010 (1978) (defective

epoxy coating provided by insured caused no damage to metal pipe when it peeled off after application).

In all cases, the court's central task is to gain an understanding of the relationship between the insured's work or product and the property that was allegedly damaged. Thomas V. Harris, Washington Insurance Law, § 24.4 (2nd Ed. 2006). In this case, there is no "physical injury" or property damage to T&G's work. T&G's "work" consists of the installation of the building paper, siding and related flashings. There is no "physical injury" to that "tangible property." The tangible property that is physically injured is the sheathing, gypsum and framing, which happens to be the work of others (other subcontractors). The $3,000,000 in damages represents complete removal and re-clad of the siding of all 23 buildings to repair the property damage to the sheathing, gypsum and framing that arose from T&G's defective work.

Enumclaw admits that the Policy covers property damage to the gypsum, sheathing and framing because the damage is to the work of others. But the insurer argues that the Policy does not cover the cost to remove and replace the siding itself. Appellant's Brief at 45. Not only does Enumclaw cite no authority in support of this argument, it ignores controlling authority. Dewitt held that if you have to damage property

(that is not otherwise damaged) to repair the actual damage, then that cost will be covered by the policy. Such damages are consequential:

> The insurance policies at issue here provide for indemnification of the insured for "those sums that the insured becomes legally obligated to pay as damages because of . . . 'property damage' to which the insurance applies." In construing similar language, the Washington Court of Appeals in *Marley Orchard* determined that the policy allowed for consequential damages. 50 Wn. App. 805. The plaintiff in *Marley* was allowed to recover for expenditures reasonably made in an effort to avoid or minimize damages. Id. See also Gen. Ins. Co. of Am. v. Gauger, 13 Wn. App. 928, 538 P.2d 563, 566 (1975) (finding that once the definition of property damage is satisfied, "any and all damages flowing therefrom and not expressly excluded from the policy are covered").

Dewitt, 307 F.3d at 1136; see also, Aetna Cas. & Sur. Co. v. M&S Indus., Inc., 64 Wn. App. 916, 922, 827 P.2d 321 (1992) (citing Hauenstein v. St. Paul-Mercury Indem. Co., 65 N.W.2d 122 (Minn. 1954) (defective plaster applied to building walls by contractor; coverage excluded for damage to plaster itself, but not excluded for diminution in market value of building or cost of removing defective plaster and restoring building)).

There is no evidence of property damage to the work of T&G. Conversely, there is ample evidence in the record that shows property damage to the work of others for which coverage should apply. Thus, the trial court's ruling that exclusion "l" does not apply in this case should be upheld.

E. Attorneys Fees Were Not Part of the Settlement or Judgment.

Enumclaw argues that "it is undisputed that a significant, but differentiated portion of the settlement/judgment amount against T&G reflected an award of attorney fees pursuant to that subcontract." Appellant Brief at 27. Enumclaw's contention is without merit. Enumclaw fails to cite to the record to support its contention that any portion of the Judgment entered against T&G included attorneys' fees. To the contrary, the trial court in the Construction Suit explicitly stated in its Findings of Fact and Conclusions of Law that the $3,000,000 was comprised *solely* of construction costs to repair damage that resulted from defectively installed siding and weather resistive barrier; a determination that was based on the pervasive amount of damage that existed at Villas. (CP 627:12-16, 628:16-21, 630:12-16)

Enumclaw's argument that it is not liable for a part of the damage award because attorneys' fees are not a covered claim also fails because the insurer did not attempt to segregate damages during the reasonableness hearing. It is well settled in Washington that "[o]nce a finder of fact concludes that the defendant's conduct is the cause of an injury, the burden of segregating damages is upon the defendant." Tolson v. Allstate Ins. Co., 108 Wn. App. 495, 498, 32 P.3d 289 (2001) (citing Cox v. Spangler, 141 Wn.2d 431, 442, 5 P.3d 1265 (2000)). Although an insurer may elect

to forego defending against uncovered claims in a suit involving both covered and uncovered claims, if the suit is adjudicated with no attempt to differentiate amounts for covered and uncovered claims, the insurer is liable for the entire judgment plus costs, not just some prorated share. Lenzi, 140 Wn.2d 267; Prudential Prop. & Cas. Ins. Co. v. Lawrence, 45 Wn. App. 111, 121-22, 724 P.2d 418 (1986).

Here, Enumclaw protected its interests by participating in the reasonableness hearing. However, the insurer failed to argue or tailor the Findings of Fact and Conclusions of Law to include apportionment of attorneys' fees, if the insurer believed the $3,000,000 settlement amount included attorneys' fees. Having had the opportunity, but failing to do so, Enumclaw is barred from re-litigating whether any of the Judgment included attorneys' fees.

F. T&G Was Not Required to Obtain Consent from Enumclaw Prior to Settlement Because Consent Is Not a Condition Precedent to Coverage.

Enumclaw's last ditch effort to avoid coverage falls short when the insurer argues that T&G was required to obtain Enumclaw's consent prior to settling with the Association and that failure to do so negates coverage. Enumclaw claims T&G "violated a critical policy condition to coverage." Appellant's Brief at 47 Enumclaw's argument is misleading because it makes two erroneous contentions: (1) T&G was required to obtain

Enumclaw's consent prior to entering into a settlement agreement; and (2) obtaining such consent is a condition precedent to coverage.[9]

The correct language of the Policy clause at issue states:

> SECTION IV – COMMERCIAL GENERAL LIABILITY CONDITIONS
>
> * * *
>
> 2. Duties In The Event Of Occurrence, Offense, Claim Or Suit.
>
> * * *
>
> d. No insureds will, except at their own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than for first aid, without our consent.

See Appendix; CP 644.

Nowhere does the Policy state that this clause is a condition precedent to coverage. Enumclaw makes the assumption that T&G's act of entering into a settlement agreement somehow falls within the purview of this clause. The insurer even goes so far as to label the clause at issue a "consent to settle" clause. To the contrary, the Policy contains no specific language requiring T&G to obtain Enumclaw's consent prior to a settlement. In fact, there is no reference to "settlement" within the clause.

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[9] The Policy language appended to Enumclaw's brief identifies the clause at issue under the heading, "Conditions". In so doing, the insurer improperly creates the assumption that the clause is a condition precedent to coverage.

If Enumclaw wanted to require its insureds to obtain its consent prior to entering into settlement agreements, then language to that effect should have been specified in its policy. Because the Policy is silent with respect to requiring consent prior to entering into settlement and, at a minimum, ambiguous, the provision should be construed against Enumclaw. If a contractual provision is ambiguous, it must be construed against the insurer even though the insurer may have intended another meaning." Nat'l Union Fire Ins., 97 Wn. App. at 230.

Assuming *arguendo* that the clause is broadly read to include a requirement to obtain consent prior entering into a settlement agreement, there is no language in the Policy which states that compliance with the clause is a condition precedent to coverage. Enumclaw's reliance on PUD 1 v. Internat'l. Ins. Co., 124 Wn.2d 789, 881 P.2d 1020 (1994), is incorrect because the policy language in PUD 1 is materially different than the language in the Enumclaw Policy. The two cannot be analogized. First, the PUD 1 policy's clause refers to conditions regarding payment of settlement:

> 3. Insured's Duties in the Event of Occurrence, Claim or Suit
>
> * * *
>
> (c) . . . The Insured shall not, except at his own cost, voluntarily make any payment, assume any

> obligation or incur any expense; however, in the event that the amount of ultimate net loss becomes certain either through trial court judgment or agreement among the Insured, the claimant and the Company, then the Insured may pay the amount of ultimate net loss to the claimant to effect settlement....

Id. at 803.

Second, underneath the Conditions section of the PUD 1 policy, there is a "no action" clause which limits the insurer's obligation to pay only the amount established by final judgment or by a settlement in which the insurer had participated:

> 5. Action Against the Company
>
> No action shall lie against the Company with respect to any one occurrence, unless, as a condition precedent thereto, the Insured shall have fully complied with all the terms of this policy, nor until the amount of the Insured's obligation to pay . . . shall have been finally determined either by judgment against the Insured after the actual trial or by written agreement of the Insured, the claimant and the Company. . . .

Id.

Not only is the clause in the Enumclaw Policy materially different from the policy in PUD 1, but it also does not contain a "no action" clause. The proposition that compliance with the Enumclaw clause is a condition precedent to coverage should be dismissed. Moreover, noncompliance with an insurance policy provision does not deprive the insured of the

benefits of the policy unless the insurer demonstrates actual prejudice resulting from the insured's noncompliance. Or. Auto. Ins. Co. v. Salzberg, 85 Wn.2d 372, 377, 535 P.2d 816 (1975). The burden of proof is on the insurer. Id. If insurers were allowed to avoid payment based on the insured's conduct even in the absence of prejudice, the public policy of risk spreading would be compromised and, in a sense, the insurer would receive a windfall. Id. at 376-77; see also, PUD 1, 124 Wn.2d at 805.

Though not described in its brief, Enumclaw argued this same issue to the trial court in a motion for summary judgment. In its motion, Enumclaw claimed that T&G entered into the settlement with the Association against the advice of insurance-appointed defense counsel. (CP 811:7-13) If Enumclaw's allegations were true, they would constitute an unequivocal violation of the duty of defense counsel to place the interests of the insured ahead of the insurer. See Tank v. State Farm Fire & Cas. Co., 105 Wn.2d 381, 385-86, 715 P.2d 1133 (1986). Here, T&G's president entered into a consent judgment with a covenant not to execute that terminated all liability against T&G and its owners— an equitable outcome considering T&G's owner faced personal liability and claims totaling over $5 million.

This is not a case where plaintiff and insured secretly entered into a settlement agreement without notice to Enumclaw, or without providing

the insurer an opportunity to fund the settlement and exhaust all liability against its insured: just the opposite. Enumclaw was provided notice of each step, was present and participated in mediation, and yet refused to fund the agreed settlement. Instead, the insurer filed suit against T&G days prior to execution of the settlement agreement. It would be nonsensical for a court to rule that an insurance company could contest coverage, sue its insured and then claim its insured was required to obtain its consent prior to entering into a settlement agreement that exhausted any and all liability. Consequently, this Court should follow the precedence of PUD 1 and rule that consent is not a condition precedent to coverage in this case.

G. Attorneys' Fees are Recoverable.

In Washington "an award of fees is required in any legal action where the insurer compels the insured to assume the burden of legal action, to obtain the full benefit of his insurance contract, regardless of whether the insurer's duty to defend is at issue." Olympic Steamship, 117 Wn.2d at 53.[10]

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[10] See also Panorama Village Condo. Owners Ass'n Bd. of Directors. v. Allstate Ins. Co., 144 Wn.2d 130, 144, 26 P.3d 910 (2001); Louisiana-Pacific Corp. v. Asarco Inc., 131 Wn.2d 587, 605 n.81, 934 P.2d 685 (1997); Estate of Jordan v. Hartford Acc. & Indem. Co., 120 Wn.2d 490, 508, 844 P.2d 403 (1993); Prof'l Marine Co v. Those Certain Underwriters at Lloyd's, 118 Wn. App. 694, 711-12, 77 P.3d 658 (2003); McCauley v. Metro. Prop. & Cas. Ins. Co., 109 Wn. App.

Enumclaw claims that the narrowly applied denial of attorneys' fees articulated in PUD 1 supersedes the well-established rule of awarding attorneys' fees and costs in insurance declaratory judgment actions under Olympic Steamship. In PUD 1, the court held that attorneys' fees cannot be imposed "[w]hen an insured has ***undisputedly*** failed to comply with express coverage terms, ***and the noncompliance may extinguish the insurer's liability under the policy***." Id. at 815 (emphasis added). In this case, the trial court made no such determination; to the contrary, the court affirmed coverage and ruled that Enumclaw was bound under the policy to indemnify T&G. As demonstrated in the preceding section, when Enumclaw raised this issue on summary judgment in the declaratory judgment action, T&G and the Association responded with rebuttal evidence as to why consent was not needed and why Enumclaw would have committed *prima facie* bad faith under Tank if the insurer did not allow its insured to settle with the Association and avoid personal liability in excess of policy limits. "The burden of showing the actual prejudice is on the insurer. . . ." PUD 1 at 804.

Unlike PUD 1, the trial court in this case did not find that T&G contravened the express terms of the policy and prevailed on its coverage

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628, 639, 36 P.3d 1110 (2001); Gerken v. Mut. of Enumclaw Ins. Co., 74 Wn. App. 220, 228-30, 872 P.2d 1108 (1994).

dispute only because Enumclaw had not been prejudiced by the breach of the policy. One can scarcely come up with a scenario where an insurer would consent to a settlement involving its insured, and then deny coverage or file a declaratory judgment action. If PUD 1 were adopted broadly in contravention of Olympic Steamship, then attorneys' fees would never be awarded to an insured who settles to avoid personal liability without its insurer's expressed consent, is forced to seek legal action to obtain coverage and prevails in the ensuing declaratory judgment action. This is not the intent of the Supreme Court as articulated in Olympic Steamship and its progeny.

PUD 1 is an aberration that involved over $2.8 million in attorneys' fees and included an intentional contravention of contractual obligations that happened not to prejudice the insurer. Such is not the case here. Because consent was not a condition precedent to coverage under the Policy and since Enumclaw's appointed attorney would have committed a Tank violation had he recommended against the settlement, attorneys' fees under Olympic Steamship should be upheld in the declaratory judgment action.

V. CONCLUSION

In the underlying Construction Suit, issues of T&G's liability and damages were litigated and decided by the court on summary judgment and during the reasonableness hearing. Doctrines of standing, *res judicata*, collateral estoppel and equitable estoppel bar Enumclaw from re-litigating those issues in the declaratory judgment action. The Judgment entered against T&G in the Construction Suit constitutes a "legal obligation to pay" under Enumclaw's policy. With respect to policy exclusions argued by Enumclaw, the trial court properly ruled that (1) the property damage is not to "impaired" property; (2) T&G's product was not withdrawn or recalled from the market; and (3) the "your work" exclusion does not apply because the property damage that T&G became liable for was damage to the work of others. Accordingly, this Court should uphold the trial court's summary judgment orders finding coverage and entering judgment against Enumclaw in the amount of $3,516.046.89, plus interest and attorneys' fees.

Respectfully submitted this 16th day of May, 2006.

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56144-8-I

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

MUTUAL OF ENUMCLAW INSURANCE COMPANY,

Appellant,

v.

VILLAS AT HARBOUR POINTE OWNERS ASSOCIATION;
T&G CONSTRUCTION, INC.,

Respondents.

AFFIDAVIT OF SERVICE

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I, Naomi Strand, hereby certify and declare:

1. I am over the age of 18 years and am not a party to the within cause:

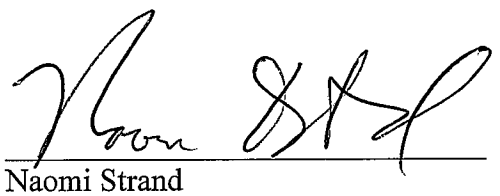
2. I am employed by the law firm of Barker Martin, P.S. My business and mailing address are 719 – 2nd Avenue, Suite 1200, Seattle, WA 98104-1749;

3. On the 16th of May, 2006, I caused to be served **Respondents Second Brief** and this Affidavit of Service for review upon the following in the manner described below:

James M. Beecher
Hackett Beecher & Hart
1601 5th Avenue, Suite 2200
Seattle, WA 98101
Via Hand Delivery.

I declare under penalty of perjury, under the laws of the State of Washington, that the foregoing is true and correct to the best of my knowledge and belief.

Signed this 16th day of May, 2006 in Seattle, Washington.



Naomi Strand