

80937-2

Court of Appeals Cause No. 56591-5-I

FILED
DEC 3 2007
CLERK OF SUPREME COURT
STATE OF WASHINGTON
[Signature]

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

MUTUAL OF ENUMCLAW INSURANCE COMPANY,

Respondent,

v.

RED OAKS CONDOMINIUM OWNERS ASSOCIATION,
a Washington nonprofit corporation,

Petitioner.

FILED
COURT OF APPEALS DIV. #1
STATE OF WASHINGTON
2007 NOV - 9 PM 3:46

PETITION FOR REVIEW

C. Kenworthy Harer
WSBA #30025
Condominium Law Group, PLLC
10310 Aurora Ave N.
Seattle, WA 98133
206-633-1520 – Telephone

TABLE OF CONTENTS

Table of Contents.....	(i)
Table of Authorities.....	(ii)
A. Identity of Petitioner.....	1
B. Citation to Court of Appeals Decision.....	1
C. Issues Presented for Review.....	1
D. Statement of the Case.....	4
I. Statement of the Facts.....	4
II. Statement of Procedural History.....	6
E. Argument.....	7
I. The Court of Appeals' Interpretation of the Policy Language is Contrary to Washington Supreme Court Rulings.....	7
II. The Court of Appeals' Analysis of the Bad Faith Claims is Contrary to <i>Tank</i> and the WAC.....	10
III. The Court of Appeals' Improper Analysis of the WAC Provisions Resulted in the Improper Dismissal of (CPA) Claims.....	14
IV. The Court of Appeals' Decision Involves Issues of Substantial Public Interest That Should be Determined by the Supreme Court.....	14
a. There is a Substantial Public Interest in Having Clear Guidelines for the Interpretation of Insurance Policy Language.....	16
b. There is a Substantial Public Interest in Having Clear Guidelines for the Rights and Obligations of Parties to Insurance Contracts.....	18
F. Conclusion.....	20
Appendix A	Court of Appeals' Decision
Appendix B	WAC Provisions 284-30-330 and 284-30-380
Appendix C	UMB 3011 Endorsement
Appendix D	MoE's Motion to Publish

TABLE OF AUTHORITIES

Allstate Ins. Co. v. Raynor, 143 Wn.2d 469, 21 P.3d 707 (2001).....2, 10

Fenton v. Poston, 114 Wash. 217, 195 P. 31 (1921).....17

Kitsap County v. Allstate Ins. Co.,
136 Wn.2d 567, 964 P.2d 1173 (1998).....7

McDonald v. State Farm Fire & Cas. Co.,
119 Wn.2d 724, 837 P.2d 1000 (1992).....1, 2, 7, 10, 17

Morgan v. Prudential Ins. Co. of Am.,
86 Wn.2d 432, 545 P.2d 1193 (1976).....1,7, 17

Mutual of Enumclaw Ins. Co. v. Don Paulson Constr., Inc.,
No. 79027-2, 2007 Wash. Lexis 788 (2007).....15, 17, 19

Red Oaks v. Sundquist, 128 Wn. App. 317, 116 P.3d 404 (2005).....6

Red Oaks v. Mutual of Enumclaw Ins. Co., No. 56591-5-I (2007).....7, 8, 13, 14, 15, 16

Shotwell v. Transamerica Title Ins. Co.,
91 Wn.2d 161, 588 P.2d 208 (1978).....2, 9

Stanley v. Safeco Ins. Co of Am., 109 Wn.2d 738, 747 P.2d 1091 (1988).....2, 9

Tank v. State Farm Fire & Cas. Co.,
105 Wn.2d 381, 715 P.2d 1133 (1986).....3, 10, 11, 12, 14, 15, 19

Van Noy v. State Farm Mut. Auto. Ins. Co.,
98 Wn. App. 487, 983 P.2d 1129 (1999).....14

STATUTES

WAC 284-30-330, et seq......12, 19

WAC 284-30-330(13)3, 12

WAC 284-30-380(1)3, 12

A. IDENTITY OF PETITIONER

Red Oaks Condominium Owners Association (Red Oaks) respectfully requests this Court to accept review of the unpublished Court of Appeals' decision terminating review designated in Part B of this petition.

B. CITATION TO COURT OF APPEALS DECISION

Red Oaks seeks review of the Court of Appeals' decision in *Red Oaks Condominium Owners Association v. American States Insurance Company and Mutual of Enumclaw Insurance Company*, No. 56591-5-I, which was filed July 30, 2007. A copy of the decision is attached hereto as Appendix A. No motion for reconsideration was filed.

C. ISSUES PRESENTED FOR REVIEW

1. This Court has held that if the language of an insurance contract is unambiguous, a court must enforce the policy as written and as understood by the average person.¹ The UMB 3011 endorsement purchased by Sundquist contains a completed operations clause (referred to herein as the "your work" provision) that changes the language from "work performed *by or on behalf of the Named Insured*" to "work performed *by the Named Insured*." The term "Named Insured" as defined by the policy means only Sundquist Homes, Inc. Did the Court of

¹ *Morgan v. Prudential Ins. Co. of Am.*, 86 Wn.2d 432, 435, 545 P.2d 1193 (1976); *McDonald v. State Farm Fire & Cas. Co.*, 119 Wn.2d 724, 733, 837 P.2d 1000 (1992).

Appeals err when it held that the “your work” provision barred coverage for subcontractor work performed *on behalf of* Sundquist Homes, Inc.?

2. This Court has held that: a) policy language is ambiguous if it is susceptible to more than one reasonable interpretation;² b) ambiguities in a policy are strictly construed against the drafter, especially in the case of exclusionary clauses that seek to limit coverage;³ and c) the legal effect of ambiguous exclusionary clauses is to find the language ineffective.⁴

Red Oaks offered a reasonable interpretation of the UMB 3011 endorsement language. Mutual of Enumclaw (MoE) offered a different interpretation. MoE was the drafter of the policy and its interpretation of the exclusionary clause barred coverage for subcontractor work. Did the Court of Appeals err when it applied MoE’s interpretation and found that subcontractor work was excluded from coverage?

3. When interpreting ambiguous policy language, this Court has held the meaning and construction most favorable to the insured must be employed, even if the insurer intended something different.⁵ Did the Court of Appeals err when it failed to interpret the language in favor of Red Oaks and then established an unprecedented burden for Red Oaks to prove MoE’s intent to cover subcontractor work, concluding there was no

² *Stanley v. Safeco Ins. Co. of Am.*, 109 Wn.2d 738, 741, 747 P.2d 1091 (1988).

³ *Allstate Ins. Co. v. Raynor*, 143 Wn.2d 469, 477, 21 P.3d 707 (2001).

⁴ *McDonald*, 119 Wn.2d at 733.

⁵ *Shotwell v. Transamerica Title Ins. Co.*, 91 Wn.2d 161, 167-68, 588 P.2d 208 (1978).

coverage because Red Oaks did not meet that burden?

4. This Court has held that insurers defending under a reservation of rights have an enhanced duty of good faith to their insureds and that violations of the Washington Administrative Code (WAC) constitute a breach of that enhanced duty of good faith.⁶ WAC 284-30-380(1) and WAC 284-30-330(13) require an insurer to promptly provide a reasonable explanation for its basis in the policy for denial of a claim and to provide a written denial which includes the specific policy provision under which coverage is being denied. MoE sent a reservation of rights letter that did not include the provision under which coverage was denied by the trial court. MoE failed to send a written denial providing its basis for refusing coverage. Did the Court of Appeals err when it held that MoE fulfilled its enhanced duty of good faith to its insured?

5. The Washington Consumer Protection Act (CPA) provides a cause of action against insurers for unfair or deceptive practices. The WAC provides that an insurance company's failure to promptly provide a reasonable explanation of the basis in the insurance policy for denial of a claim or offer of a compromise settlement constitutes unfair or deceptive acts or practices in the business of insurance.⁷ MoE stipulated to facts that it failed to comply with the WAC. Did the Court of Appeals err in

⁶ *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986).

⁷ WAC 284-30-330 and 284-30-330(13).

dismissing Red Oaks' claims under the CPA and the resulting award of attorneys' fees and costs?

D. STATEMENT OF THE CASE

I. Statement of the Facts

Sundquist Homes, Inc. (Sundquist) has a local builder of homes, apartments, and condominiums since 1976. CP 185. Sundquist was insured with MoE beginning in 1978. CP 186. MoE agents sold Sundquist coverage under a comprehensive general liability policy (CGL) and an umbrella policy, which were renewed annually. CP 191. Sundquist understood that the umbrella policy provided broader coverage and higher liability limits than the primary policy. CP 192.

In 1993, Sundquist specifically discussed with MoE agents its concerns regarding the upsurge in construction defect lawsuits being filed against contractors. CP 189-90. Sundquist understood its policies with MoE might not cover property damage to any work specifically performed by Sundquist, but based upon the policy language and representations by MoE agents, Sundquist understood the policies it purchased provided coverage for property damage to and arising out of work performed by subcontractors. CP 190-191. Sundquist specifically purchased "completed operations" coverage for future lawsuits that might be brought against it after its buildings were completed and sold. CP 186. The

completed operations coverage was provided by the “your work” provision of the UMB 3011 endorsement to the umbrella policy. CP 87.⁸ Sundquist paid additional premiums for the “completed operations” coverage which amounted to more than half its total premiums. CP 194.

Sundquist notified MoE of Red Oaks’ claims in February 2003. CP 935. Sundquist and Red Oaks, with MoE’s approval, executed an ER 408 agreement in September 2003 which provided that an independent engineer would inspect the buildings and define the scope of necessary repairs, then two independent contractors would bid on the repairs. CP 819-20. MoE participated in the investigative process, which included choosing independent engineers and contractors, and agreed to fund the cost of the process. CP 937, 941. Mediation was scheduled for March 4, 2004 to determine the final costs to settle the dispute. CP 938. Red Oaks submitted a settlement demand within Sundquist’s policy limits with its mediation brief. CP 828. Three days before mediation, MoE informed Sundquist’s defense attorney that it would not provide settlement authority for resolution of the matter without further explanation. CP 938, 1272.

In November 2003, MoE sent to Sundquist a letter accepting

⁸ The “your work” provision of UMB 3011 endorsement states, “[t]he exclusions of this policy relating to Property Damage are replaced by the following exclusion:...B. With respect to COMPLETED OPERATIONS HAZARD to Property Damage to work performed by the Named Insured arising out of the work or any portion thereof, or out of materials, parts or equipment furnished in connection therewith.” (See Appendix C)

tender of the defense of Red Oaks' claims and, for the first time, reserving its right to deny coverage under the policies at issue. CP 44-49. MoE identified the "your product" exclusion in the CGL, but failed to identify the "your work" provision as a possible basis to deny coverage. CP 47.

II. Statement of Procedural History

Red Oaks filed a lawsuit against Sundquist on March 31, 2004. CP 16-22. At the time the suit was filed, MoE had not updated its coverage position since November 2003. MoE never provided a written denial of coverage including the "your work" provision as the basis for denial and never provided an explanation for its denial of the offer of compromised settlement. Red Oaks took an assignment of Sundquist's claims against MoE and the subcontractors in exchange for a consent to judgment. The trial court approved the settlement as reasonable; MoE unsuccessfully challenged that determination.⁹

In June 2005, the trial court granted MoE's motion for summary judgment on the coverage issue under the umbrella policy "your work" provision. CP 898-900. Red Oaks immediately moved for summary judgment on the remaining bad faith and consumer protection act claims. CP 901-927. MoE filed an opposition and cross motion for summary judgment dismissal of the case. CP 1090-1116. MoE stipulated to all

⁹ See *Red Oaks v. Sundquist*, 128 Wn. App. 317, 116 P.3d 404 (2005).

facts alleged by Red Oaks but argued, essentially, that there was no bad faith because coverage for the underlying claims were resolved in its favor. CP 1095-1114. The trial court entered summary judgment in favor of MoE and dismissed Red Oaks' lawsuit with prejudice. CP 1316-1317. The Court of Appeals affirmed the decision of the trial court.¹⁰

E. ARGUMENT

I. The Court of Appeals' Interpretation of the Policy Language is Contrary to Washington Supreme Court Rulings.

The Court of Appeals failed to determine whether the language of the exclusionary clause was ambiguous or unambiguous, and then failed to follow the rulings of the Supreme Court in either instance.

If the language of an insurance contract is clear and unambiguous, a court must enforce it as written.¹¹ Courts interpreting insurance policies look to the definitions provided in the policy itself.¹² Insurance policy language is interpreted as it would be understood by an average person.¹³

If the Court of Appeals determined that the policy language was unambiguous, it should have considered only the policy language in determining the meaning of the "your work" provision; and should have given full force and effect to the deletion of the language "*or on behalf*

¹⁰ *Red Oaks v. Mutual of Enumclaw*, Appendix A, pg. 19.

¹¹ *Morgan v. Prudential Ins. Co. of Am.*, 86 Wn.2d 432, 435, 545 P.2d 1193 (1976).

¹² *Kitsap County v. Allstate Ins. Co.*, 136 Wn.2d 567, 576, 964 P.2d 1173 (1998).

¹³ *McDonald v. State Farm Fire & Cas. Co.*, 119 Wn.2d 724, 733, 837 P.2d 1000 (1992).

of” and the definition of “Named Insured” in the policy.¹⁴ Instead, the Court of Appeals engaged in a discussion about the intent of the insurance company, ignored the plain language of the contract and how the policy would be interpreted by an average person. While the Court’s opinion states that policy language is to be interpreted as it would be understood by an average person¹⁵, the Court’s analysis contains no application of this principal rule of construction.

The umbrella policy excludes “work performed *by or on behalf of the Named Insured*.” The UMB 3011 endorsement deletes the phrase “or on behalf of”, changing the language to “work performed *by the Named Insured*.” The term “Named Insured”, as defined by the policy, means **only** Sundquist Homes. The Court of Appeals acknowledged that the endorsement expressly replaces the exclusion in the umbrella policy and that the language “on behalf of” was deleted from the endorsement, but failed to give any effect to this deletion. The Court specifically disregarded the deletion as being irrelevant, stated that the language was “superfluous”, and concluded the work of the subcontractors was excluded from coverage.¹⁶

If the Court had relied solely on the policy language, as understood

¹⁴ CP 312.

¹⁵ *Red Oaks v. Mutual of Enumclaw*, Appendix A, pg. 5.

¹⁶ *Id.*, Appendix A, pg. 10-11.

by the average person, it would have determined that the clear and unequivocal meaning of the phrase “work performed by the Named Insured” included only the work of Sundquist, and that subcontractor work was **not** excluded from coverage under the “your work” provision.

Alternatively, if the Court found that there was more than one reasonable interpretation of this policy language, it failed to comply with applicable Supreme Court rulings regarding the interpretation of ambiguous language in insurance policies.¹⁷

The parties to this case advocate competing interpretations of the “your work” provision. The Court of Appeals engages in a lengthy discussion regarding these interpretations, but fails to determine whether each is reasonable. Red Oaks’ interpretation excludes only the work of the Named Insured, Sundquist, in accordance with the precise language of the policy. MoE’s interpretation of the policy language excludes subcontractor work. Red Oaks does not agree that MoE’s interpretation is reasonable, but if the Court found that both interpretations were reasonable, then the language **must be** ambiguous.

Ambiguities in an insurance contract are strictly construed against

¹⁷ *Stanley v. Safeco Ins. Co. of Am.*, 109 Wn.2d 738, 741, 747 P.2d 1091 (1988)(An insurance policy provision is ambiguous when it is fairly susceptible to two different, reasonable interpretations.); *Shotwell v. Transamerica Title Ins. Co.*, 91 Wn.2d 161, 167-68, 588 P.2d 208 (1978)(If a policy is susceptible to two interpretations, the meaning and construction most favorable to the insured must be employed, even if insurer intended something different.)

the insurer as the drafter, especially in the case of exclusionary clauses which seek to limit policy coverage.¹⁸ If a policy's exclusionary language is ambiguous, the legal effect of such ambiguity is to find the exclusionary language ineffective.¹⁹

The "your work" provision of the UMB 3011 endorsement is an exclusionary clause. If the Court found that this exclusionary clause was ambiguous, then the Court should have construed the language against MoE as the drafter and rendered it ineffective in excluding the work of subcontractors. Instead, the Court accepted MoE's interpretation of the language, construed the language against the insured, and broadened the exclusion to bar coverage for subcontractor work. Each of those determinations ignored long standing Supreme Court authority regarding the interpretation of insurance policies. If the Court of Appeals had followed the rulings of the Supreme Court, it would have determined that subcontractor work *was* covered under the "your work" provision.

II. The Court of Appeals' Analysis of the Bad Faith Claims is Contrary to *Tank* and the WAC

The Court of Appeals failed to comply with the explicit instruction set forth in *Tank*²⁰ and failed to enforce the WAC provisions as written.

The Supreme Court held in *Tank* that insurers have an enhanced obligation

¹⁸ *Allstate v. Raynor*, 143 Wn.2d 469, 477, 21 P.3d 707 (2001).

¹⁹ *McDonald*, 119 Wn.2d at 733.

²⁰ *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986).

of good faith when operating under a reservation of rights.²¹ This enhanced obligation requires the insurer to “refrain from engaging in any action which would demonstrate a greater concern for the insurer’s monetary interest than for the insured’s financial risk.”²² In this case, MoE authorized and funded a cooperative investigation process between Red Oaks and Sundquist that established Sundquist’s liability. Once the investigation was complete, MoE had obtained all the information it needed to determine whether Red Oaks’ claims were covered by Sundquist’s policy. After the investigation and three days before the mediation, MoE advised Sundquist’s defense counsel that it would not provide settlement authority, but failed to provide the basis for this refusal and failed to explicitly deny coverage for the claims. MoE’s actions ended the cooperative process between Red Oaks and Sundquist and subjected Sundquist to immediate litigation. By establishing Sundquist’s liability, then disengaging from the cooperative process without explanation, MoE demonstrated complete disregard for Sundquist’s financial risk. MoE’s actions were contrary to the explicit requirements set forth in *Tank*²³ and the explicit requirements of the WAC.

The Supreme Court has held that violations of the WAC constitute

²¹ *Id* at 383.

²² *Id* at 388.

²³ 105 Wn.2d 381.

a breach of the enhanced duty of good faith.²⁴ The legislature, through the WAC, identified the obligations of insurers with regard to fulfilling their duty of good faith to insured parties.²⁵ According to the WAC, an insurer is obligated to promptly provide a reasonable explanation for its basis in the policy related to the facts for denial of a claim or offer of a compromise settlement²⁶ and to provide a written denial including the specific policy provision under which coverage is being denied.²⁷ The settlement demand submitted with Red Oaks' mediation brief was an offer of compromised settlement. MoE failed to respond directly to the settlement demand and failed to provide a reasonable explanation for its refusal to provide any amount of settlement authority for the mediation.

The Court of Appeals cited the WAC provisions, but inexplicably failed to enforce the provisions as written and as prescribed by the Supreme Court in *Tank*.²⁸ Instead, the Court established a different, lower standard for an insurance company's duty of good faith under a reservation of rights defense and concluded that "[b]y setting forth its rationale for its reservation of rights in its letter to Sundquist, MoE

²⁴ *Id* at 387.

²⁵ WAC 284-30-330 *et seq.*

²⁶ WAC 284-30-330(13).

²⁷ WAC 284-30-380(1).

²⁸ 105 Wn.2d 381.

complied with the insurer's duty of good faith."²⁹

The Court improperly concluded that MoE complied with the WAC by sending a single reservation of rights letter with general language prior to its investigation of the claims. A reservation of rights letter is *not* a denial of coverage and the letter the Court cited does not reference the specific "your work" provision under which coverage was ultimately rejected by the trial court. Instead, the letter referenced another provision of the endorsement regarding ongoing operations which is not, and has never been, at issue in this litigation.³⁰

In addition, the Court concluded that MoE did not violate the WAC because the reservation of rights letter stated that the umbrella policy would not pay for the cost of damage to "Sundquist's own work".³¹ The Court refused to acknowledge the fact that the reservation of rights letter never specifically mentions or even alludes to a conclusion that subcontractor work would "merge: into "Sundquist's own work". This legal theory was advanced for the first time by MoE more than a year after this lawsuit was filed and more than two years after Red Oaks' claim was submitted to MoE.

MoE failed to comply with the letter and spirit of the WAC

²⁹ *Red Oaks v. Mutual of Enumclaw*, Appendix A, pg. 14.

³⁰ CP 47.

³¹ CP 47.

provisions and the Court of Appeals failed to enforce the WAC provisions as intended by the legislature. The Court failed to hold MoE accountable in the manner prescribed by the Supreme Court in *Tank*.³²

III. The Court of Appeals' Improper Analysis of the WAC Provisions Resulted in the Improper Dismissal of CPA Claims

The Court of Appeals' dismissal of Red Oaks' claims under the CPA was erroneous because of the Court's determination that MoE did not violate the WAC. The Court of Appeals acknowledged that violations of the WAC provisions related to unfair claims settlement practices are *per se* violations of the CPA.³³

The legislature created a cause of action under the CPA for insured parties where the insurer fails to comply with the provisions of the WAC and the Court of Appeals' decision disregarded that express relief. An award of attorneys' fees and costs under the CPA was improperly denied.

IV. The Court of Appeals' Decision Involves Issues of Substantial Public Interest That Should be Determined by the Supreme Court

The issues addressed in the Court of Appeals' decision are not limited to the dispute between one insurer and one insured party regarding the extent of coverage and the conduct of the insurer. MoE agrees that the issues raised in the *Red Oaks* decision "present themselves repeatedly in

³² 105 Wn.2d 381.

³³ *Red Oaks v. Mutual of Enumclaw*, Appendix A, pg. 18 [citing *Van Noy v. State Farm Mut. Auto. Ins. Co.*, 98 Wn. App. 487, 496, 983 P.2d 1129 (1999)].

insurance coverage litigation”.³⁴ In particular, these issues present themselves when insurers and insureds appear before Division I of the Court of Appeals and the Court deviates from Supreme Court precedent by disparately favoring insurers.³⁵

Division I has diverged from the Supreme Court in its decisions evaluating insurance disputes. The *Red Oaks* decision and the *Paulson* decision exemplify that divergence.³⁶ In both cases, the Court of Appeals favored insurance companies over their insureds by creating new burdens for the insured to prevail in disputes with insurers. In the *Paulson* case, the Court created a burden for the insured to prove damages.³⁷ In *Red Oaks*, the Court created a burden for the insured to prove the insurer’s intent to provide coverage.³⁸ The Court of Appeals also favored insurance companies over their insureds by establishing a minimum standard of conduct for insurance companies that directly contradicts the language of the WAC provisions enacted to protect the rights of insured parties and disregards the enhanced obligation of good faith prescribed by *Tank*.³⁹

Insured parties are typically in a much less powerful position to

³⁴ Respondent MoE’s Motion to Publish, Appendix D, pg. 6.

³⁵ See e.g. *Mutual of Enumclaw Ins. Co. v. Don Paulson Constr., Inc.*, No. 79027-2, (2007).

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Red Oaks v. Mutual of Enumclaw*, Appendix A, pg. 10.

³⁹ 105 Wn.2d 381.

enforce their rights under an insurance policy than are insurers. Insured parties do not usually have the knowledge or financial resources to challenge the decision of an insurer to deny coverage, or to bring claims of bad faith where coverage is improperly denied.

With the *Red Oaks* ruling, the Court of Appeals further impairs the already compromised position of insured parties by creating new burdens for the insured, failing to enforce the WAC, and failing to adhere to Supreme Court rulings. Review by the Supreme Court is essential in order to provide clear direction to lower courts and ensure that these cases are handled consistently.

a. There is Substantial Public Interest in Having Clear Guidelines for the Interpretation of Insurance Policy Language

By concluding that Red Oaks did not present convincing evidence that MoE intended to adopt the meaning of the ISO form⁴⁰ the Court of Appeals improperly created a new burden for an insured party to prove an insurer's intent in drafting the policy language and established a new defense for insurance companies to deny claims on the basis that they did not intend to provide coverage. This new burden of proof and defense contradict decades of well founded legal precedent which established and affirmed the ruling that ambiguous policy language must be construed

⁴⁰ *Red Oaks v. Mutual of Enumclaw*, Appendix A, pg. 10.

against the insurer/drafter, even if the insurer/drafter intended something different.⁴¹

The Court of Appeals' consideration of the insurer's intent created a substantial shift in insurance policy interpretation that will have an enormous impact on the public. It is virtually impossible for an insured party to prove the intent of the insurer in drafting the policy. As the drafter of an insurance policy, the insurer is in the best position to ensure that the language of the policy reflects its intent. If the insurer fails in this regard by using ambiguous language, the language **must** be construed against the drafter, regardless of the insurer's intent. By allowing the insurer to defend a coverage claim by requiring a policy holder to prove the insurer intended to provide coverage, the Court of Appeals placed an overwhelming burden on insured parties in Washington.

The Court of Appeals imposed a similar burden on the insured in *Paulson* to prove that the insurer's actions caused harm.⁴² The Supreme Court reversed that decision and ruled that the insurer, not the insured, "appropriately bears the burden of proof with respect to the consequences of [its] conduct."⁴³ The case at hand presents an opportunity for the

⁴¹ *Fenton v. Poston*, 114 Wash. 217, 225, 195 P. 31 (1921); *Morgan v. Prudential Ins. Co. of Am.*, 86 Wn.2d 432, 435, 545 P.2d 1193 (1976); *McDonald v. State Farm Fire & Casualty Co.*, 119 Wn.2d 724, 734, 837 P.2d 1000 (1992).

⁴² *Mutual of Enumclaw Ins. Co. v. Don Paulson Constr., Inc.*, No. 79027-2, (2007).

⁴³ *Id* at 19.

Supreme Court to continue to protect insured parties and discourage bad faith behavior by enforcing the proper burden of proof with regard to policy interpretation.

Insured parties and insurance companies need the Supreme Court to clarify their rights and obligations in coverage disputes. If the Court of Appeals' analysis was erroneous, it is imperative that the Supreme Court review the decision and confirm that the burden of proof properly lies with the insurer. If the Supreme Court determines that the Court of Appeals' analysis was correct, the decision must be reviewed so that lower courts can uniformly apply this new burden of proof.

b. There is a Substantial Public Interest in Having Clear Guidelines Regarding the Rights and Obligations of Parties to Insurance Contracts

The Court of Appeals' analysis regarding Red Oaks' bad faith claims created a new minimum standard for the conduct of insurance companies defending under a reservation of rights which is in direct opposition to Washington law and the clear intent of the legislature. The legislature has established its intent to hold insurance companies accountable for the unfair treatment of their insureds and the Supreme Court reinforced the obligations of an insurance company to its insureds in

*Tank*⁴⁴ and *Paulson*.⁴⁵

The Court of Appeals' decision disregarded the intent of the legislature and Supreme Court precedent by favoring an insurance company over its insured and will create confusion and increased litigation if it is not reconciled by the Supreme Court. The legislature enacted specific provisions in the WAC which provide information to both insured parties and insurers about the rights and obligations inherent in their relationship.⁴⁶ The Court of Appeals' opinion disregarded the explicit requirements of the WAC regarding the conduct of an insurance company and instead created a different minimum level of conduct. The opinion established that an insurance company is immune from bad faith claims if it merely hires defense counsel and sends a generally worded reservation of rights letter advising the insured that coverage *may* be denied under the policy, regardless of whether or not that reservation of rights letter includes the specific provision under which coverage is ultimately denied. It allows insurers to deny claims without explanation, then litigate new or novel policy interpretations to defeat coverage. This minimum standard of conduct contradicts the explicit requirements of the WAC to keep policy holders informed.

⁴⁴ 105 Wn.2d 381.

⁴⁵ *Mutual of Enumclaw Ins. Co. v. Don Paulson Constr., Inc.*, No. 79027-2, (2007).

⁴⁶ WAC 284-30-330, *et seq.*

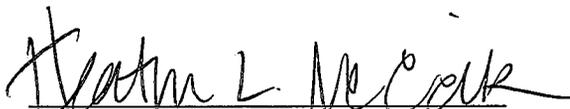
The lower courts, insurers, and insureds need to know that the WAC has meaning and force and that non-compliance will have consequences. These same parties also need guidance from the Supreme Court with regard to the rights and obligations of parties to insurance contracts. To allow the Court of Appeals' decision to stand without review would render certain WAC provisions meaningless and ineffective in Division I and cause confusion regarding the rights and obligations of parties to insurance contracts.

F. CONCLUSION

Red Oaks respectfully requests the Supreme Court accept review of the Court of Appeals' decision of July 30, 2007 for the reasons stated in Part E.

Dated this 8th day of November, 2007.

Respectfully submitted,



CONDOMINIUM LAW GROUP, PLLC

C. Kenworthy Harer, WSBA #30025

Heather L. McCormick, WSBA #35132

Theresa M. Torgesen, WSBA #32941

Attorneys for Petitioner Red Oaks

Condominium Owners Association

APPENDIX A

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

RED OAKS CONDOMINIUM)	
OWNERS ASSOCIATION,)	
)	No. 56591-5-1
Appellant,)	
)	
v.)	
)	DIVISION ONE
AMERICAN STATES INSURANCE)	
COMPANY,)	
)	
Defendant,)	
)	
and MUTUAL OF ENUMCLAW)	UNPUBLISHED OPINION
INSURANCE COMPANY,)	
)	
Respondent.)	FILED: July 30, 2007

DWYER, J. — General contractor Sundquist Holdings, Inc., was responsible for the construction of the Red Oaks condominium complex. Sundquist was insured by Mutual of Enumclaw Insurance Company (MoE). Water damage stemming from construction defects was discovered in the Red Oaks structures. The Red Oaks Condominium Owners Association (Red Oaks) and Sundquist were unable to agree on a plan to repair the buildings and the situation became contentious. As litigation of the dispute loomed, Sundquist notified MoE of the damage and the potential for a lawsuit. Although Sundquist and Red Oaks eventually negotiated a monetary settlement, MoE declined to

provide funds for the settlement, asserting that the insurance policies it issued to Sundquist did not cover Sundquist's liability for damages resulting from its own work on the condominium construction. Sundquist thereafter brought claims against MoE seeking declaratory relief and monetary damages.

Sundquist settled its dispute with Red Oaks by assigning to Red Oaks Sundquist's rights as an MoE insured. Red Oaks then commenced this lawsuit against MoE asserting claims based on Sundquist's assigned rights, and alleging breach of contract, breach of the insurer's duty of good faith to its insured, and violations of chapter 19.86 RCW, the Consumer Protection Act (CPA). Following multiple motions for summary judgment brought by both MoE and Red Oaks, the trial court granted summary judgment in favor of MoE, dismissing all claims against it. Red Oaks appeals; we affirm.

FACTS

At all times relevant to the claims advanced in this lawsuit, Sundquist was insured by MoE under both a commercial general liability (CGL) policy and a supplemental umbrella policy.¹

Exclusively utilizing subcontracted labor, Sundquist completed construction of the Red Oaks condominium project in mid-1999. By early 2002, water seepage in the condominium buildings had caused extensive damage. After Sundquist and Red Oaks unsuccessfully attempted to reach an agreement

¹ An umbrella policy provides coverage for amounts exceeding CGL policy limits, and protects against gaps in coverage in the underlying policy. Prudential Property & Cas. Ins. Co. v. Lawrence, 45 Wn. App. 111, 119, 724 P.2d 418 (1986).

to repair the buildings, Sundquist notified MoE of the water damage.² MoE thereafter sent Sundquist a letter accepting tender of the defense of Red Oaks' claims and reserving its right to deny coverage, stating:

The Umbrella Policy will not pay for the cost of damage to your clients' own work or products, or products they sold; damage caused by their "faulty workmanship" . . . or for the loss of use of undamaged property caused by [Sundquist's] delay, failure to perform a contract, or failure of their products or work to meet the standards represented or warranted.

In an effort to reach a negotiated settlement, Sundquist and Red Oaks agreed to retain an independent engineer to inspect the buildings and determine what repairs were needed. Bids on the repair work were then solicited from two independent contractors.³ After the bids were submitted, the parties were scheduled to participate in a mediation proceeding to determine the cost of settling the dispute. Three days before the scheduled mediation, MoE reiterated to Sundquist its position that the Red Oaks claim was not covered under the policy and that it would not provide money to fund a settlement. Thus, the scheduled mediation did not occur. Thereafter, Sundquist added claims to an existing lawsuit against MoE, seeking declaratory relief and monetary damages related to the Red Oaks dispute.⁴

² In the first half of 2003, Sundquist submitted five coverage claims to MoE for completed projects that had been damaged by water intrusion. The five claims, Red Oaks, Wethersfield, Mill Creek Court, Barrington, and Gold Leaf, were identical for purposes of coverage determination.

³ MoE agreed to pay the cost of the independent engineer and up to \$25,000 of the attorney fees and costs Red Oaks incurred during this negotiated settlement process.

⁴ Sundquist's lawsuit originally asserted claims concerning the Barrington project. MoE filed an answer and counterclaims relating solely to the Barrington project, but subsequently amended the counterclaim to cover all of the claims against Sundquist, including the Red Oaks claim.

Red Oaks then initiated a lawsuit against Sundquist asserting claims for breach of the implied warranty of quality, violations of chapter 64.34 RCW, the Washington Condominium Act, and violations of the CPA. Red Oaks and Sundquist subsequently settled this lawsuit. Red Oaks exchanged a covenant not to execute on a stipulated judgment of \$1,948,000 against Sundquist for an assignment of Sundquist's rights against MoE arising from MoE's handling of Red Oaks's claims against Sundquist.⁵

Red Oaks then initiated this lawsuit against MoE premised upon the rights assigned by Sundquist. In its complaint, Red Oaks asserted claims for breach of contract, breach of the insurer's duty of good faith to its insured, and CPA violations.

MoE brought its first motion for summary judgment on issues of coverage. The trial court ruled in favor of MoE with respect to the CGL policy.⁶ However, the trial court denied summary judgment with respect to coverage under the umbrella policy. MoE brought a second motion for summary judgment that the trial court granted, determining that no coverage existed under the umbrella policy. Thereafter, both Red Oaks and MoE moved for summary judgment on the remaining bad faith and CPA claims. The trial court granted summary judgment in favor of MoE and dismissed Red Oaks's claims with prejudice.

⁵ The dispute between Red Oaks and Sundquist was previously before this court. See Red Oaks Condo. Owners Ass'n v. Sundquist Homes, Inc., 128 Wn. App. 317, 116 P.3d 404 (2005).

⁶ No appeal was taken from this order.

DISCUSSION

We engage in a de novo review of a trial court's grant of summary judgment, viewing all facts and inferences therefrom in the light most favorable to the non-moving party. Safeco Ins. Co. of Am. v. Butler, 118 Wn.2d 383, 394-95, 823 P.2d 499 (1992). The interpretation of an insurance policy is a question of law, also subject to de novo review. Alaska Nat'l Ins. Co. v. Bryan, 125 Wn. App. 24, 30, 104 P.2d 1 (2004). Insurance policy language is interpreted as it would be understood by an average person and in a manner giving effect to each provision. McDonald v. State Farm Fire & Cas. Co., 119 Wn.2d 724, 733, 837 P.2d 1000 (1992).

A. Insurance Contract

Red Oaks first asserts that the trial court erred by determining that the insurance policy provision excluding coverage for claims arising from work performed "by the named insured" also excluded coverage for claims arising from work performed by a subcontractor. We disagree.

The umbrella policy Sundquist initially purchased from MoE clearly excluded coverage for property damage caused by the work done by or "on behalf of" the named insured. That policy provides, in relevant part:

This policy does not apply. . . to property damage to . . . work performed by or on behalf of the named insured arising out of the work or any portion thereof, or out of materials, parts, or equipment furnished in connection therewith.

(Emphasis added.) Thus, the policy exclusion specifically excluded coverage for claims arising from work performed on behalf of the named insured, such as work performed by a subcontractor.

However, Sundquist also purchased a supplemental endorsement to the policy. That endorsement expressly replaced the property damage exclusion contained in the umbrella policy. The supplemental endorsement provides that policy coverage does not apply:

With respect to the COMPLETED OPERATIONS HAZARD to Property Damage to work performed by the Named Insured arising out of the work or any portion thereof, or out of the materials, parts or equipment furnished in connection therewith.

(Emphasis added.)⁷ In contrast to the original exclusion, this exclusion omits the phrase "on behalf of."

Red Oaks contends that the specific terms of the supplemental endorsement to the policy compel the conclusion that only claims for damage arising out of work performed by the named insured, i.e., Sundquist, are excluded from coverage, not claims for damage arising out of work performed by subcontractors.

In support of its argument, Red Oaks points to cases in several other jurisdictions involving endorsements similar to the one at issue here, which held that where an exclusion omits the phrase "on behalf of," the exclusion does not encompass work performed by subcontractors. See, e.g., Fireguard Sprinkler

⁷ The policy defines "named insured" as "the person or organization named in the declarations." The person or organization named in the declaration is Sundquist Homes, Inc., and its owners.

Sys., Inc. v. Scottsdale Ins. Co., 864 F.2d 648 (9th Cir. 1988); Fejes v. Alaska Ins. Co., 984 P.2d 519 (Alaska 1999); McKellar Dev. of Nevada, Inc. v. N. Ins. Co. of N.Y., 108 Nev. 729, 837 P.2d 858 (1992).

However, an argument substantially similar to that advanced by Red Oaks was rejected by this court in Schwindt v. Underwriters at Lloyds of London, 81 Wn. App. 293, 305-07, 914 P.2d 119 (1996). The plaintiff in that case similarly argued that a policy exclusion precluding coverage for work done by “the Assured,” rather than “on behalf of the Assured,” must be interpreted to preclude only work actually performed by the policy-holder, rather than by subcontractors on the policy-holder’s behalf.

In discounting that argument in Schwindt, we expressly addressed and rejected the rule adopted by those cases now cited by Red Oaks. The Schwindt decision held, rather, that “work of subcontractors is necessarily included in exclusions pertaining to faulty work or defective products of the contractor.” Schwindt, 81 Wn. App. at 306. In so holding, we reasoned that the policy-holder was the party in control of, and responsible for, the quality of work performed by a subcontractor. As stated therein:

[H]ere, [the general contractor] undertook construction. . . and was obligated by the contract to perform that work in a satisfactory manner. The fact that it subcontracted out some of the work on the project did not relieve it of its contractual obligation to produce a product free of defects and faulty workmanship.

Schwindt, 81 Wn. App. at 307.

In support of our holding in Schwindt, we favorably cited two Minnesota Supreme Court cases, Knutson Construction Co. v. St. Paul Fire & Marine Insurance Co., 396 N.W.2d 229 (Minn. 1986), and Bor-Son Building Corp. v. Employers Commercial Union Insurance Co. of America, 323 N.W.2d 58 (Minn. 1982). The court in these cases held that similar policy exclusions precluded coverage for the work of subcontractors despite the absence of “on behalf of” language. The court reasoned that the risk of supplying faulty goods or services is a business expense most appropriately borne by the general contractor who has control over the quality of goods and services supplied. Knutson, 323 N.W. at 235; Bor-Son, 323 N.W.2d at 64.

No subsequent Washington case has invalidated either the rule established in Schwindt or the rationale supporting it. To the contrary, we recently applied the Schwindt rule in another case, Mutual of Enumclaw Ins. Co. v. Patrick Archer Construction, Inc., 123 Wn. App. 728, 735-76, 97 P.3d 75 (2004) (“There can be no question that the quality of work performed, both by [the general contractor] as well as by its subcontractors, was the responsibility of [the general contractor] and no one else.”).

Red Oaks contends, nonetheless, that Schwindt is no longer valid, asserting that the Minnesota Supreme Court recently “dispensed” with the rule established by that court in Bor-Son and Knutson in Wanzek Construction, Inc. v. Employers Insurance of Wausau, 679 N.W.2d 322 (Minn. 2004). That contention is unavailing.

The court in Wanzek held that the exclusion there at issue did not preclude coverage for the work of subcontractors. However, unlike the policy exclusions at issue in Schwindt, Bor-Son, and Knutson, the policy exclusion in Wanzek explicitly excepted damages caused by the faulty workmanship of subcontractors. Wanzek, 679 N.W. at 326.⁸ The plaintiff in that case contended, nonetheless, that damage caused by a subcontractor's work should be excluded from coverage pursuant to rule expressed by the court in Bor-Son and Knutson. Unsurprisingly, the court in Wanzek disagreed and held that the express terms of the exclusion controlled. Wanzek, 679 N.W. at 326.

The Wanzek decision did not, however, invalidate the holdings in Bor-Son and Knutson, in which the exclusions at issue contained neither an express exception for work performed by a subcontractor nor any other direct evidence of intent to except the work of subcontractors from the exclusions at issue. In Schwindt as well, we noted that there was no "evidence that the insurers did not intend to include the work of subcontractors" in the exclusion at issue. Schwindt, 81 Wn. App. at 305-06. Accordingly, the reasoning of the court in Wanzek does not cast doubt on our holding in Schwindt, a well-reasoned holding to which we adhere.

⁸ The exclusion at issue in Wanzek stated: "This insurance does not apply to . . . "Property damage" to "your work" arising out of it or any part of it and including 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." Wanzek, 679 N.W.2d at 326 (emphasis added).

Accordingly, in the absence of evidence that such an exclusion was intended to operate to the contrary, “work of subcontractors is necessarily included in exclusions pertaining to faulty work or defective products of the contractor.” Schwindt, 81 Wn. App. at 305. Accord Patrick Archer Constr., Inc., 123 Wn. App. at 735.

Red Oaks next attempts to distinguish this case from Schwindt, arguing that, by omitting the phrase “on behalf of” in the endorsement exclusion, MoE specifically intended to broaden coverage to encompass damage arising out of the work of subcontractors. In support of this contention, Red Oaks refers to a draft insurance policy form disseminated by the Insurance Services Office (ISO) containing language that was later adapted by MoE to create the endorsement at issue here. The ISO later published a “circular” stating that the draft form’s omission of the “by or on behalf of” language was intended to have the effect of providing coverage for damages caused by the work of subcontractors. However, Red Oaks has not presented evidence indicating that, by including language used in the ISO draft form, MoE intended to adopt the intent discussed in the ISO circular.

Under Washington law, once an operation is completed, the work of the subcontractors has merged with the work of the general contractor, Schwindt, 81 Wn. App. at 305, rendering the “by or on behalf of” language superfluous. Thus, the removal of the superfluous “on behalf of” language in the supplemental

endorsement does not support the conclusion that MoE intended to broaden the coverage provided by the policy.

Red Oaks also asserts both that the insurance agent from whom Sundquist purchased the MoE policies represented to Sundquist that the umbrella policy provided coverage for liability stemming from the work of subcontractors and that MoE is bound by that representation. However, the record demonstrates that MoE gave this agent limited authority to collect premiums and bind coverage. Under the agency agreement between MoE and the insurance agent, the agent "has no authority to waive any provisions, terms or conditions of any policy of insurance issued." Furthermore, under the agency agreement, the agent may only bind "such classes of risks and to such limits as to which [MoE] may from time to time authorize." Thus, the agent did not have the actual authority to alter the terms of the policy.

Furthermore, the policy contains an anti-waiver clause which states that the terms of the policy shall not be waived, changed, or modified, "except by endorsement issued to form a part of this policy." This anti-waiver clause is required by RCW 48.18.190, which states that "[n]o agreement in conflict with, modifying, or extending any contract of insurance shall be valid unless in writing and made a part of the policy." Furthermore, RCW 48.18.100 requires that no policy shall be issued, delivered or used unless it has been filed with and approved by the insurance commissioner. Thus, the insurance agent had neither

actual nor apparent authority to bind MoE to policy provisions at variance with the express terms of the policies issued to Sundquist.

Red Oaks has not provided sufficient reason to depart from the rule clearly expressed and applied by this court in Schwindt. Thus, the exclusion of coverage for damages arising from the work performed by Sundquist also precludes coverage for damages arising from the work performed by subcontractors.

We affirm the trial court's summary judgment ruling on this issue.

B. Duty of Good Faith

Red Oaks next asserts that MoE breached its duty of good faith to its insured by (1) failing to perform a thorough investigation into whether there was coverage under Sundquist's policies, (2) failing to inform Sundquist of its coverage position and of developments that would affect coverage, and (3) demonstrating greater concern for its own interests than those of Sundquist by refusing to fund the settlement agreement for the Red Oaks claims without first attempting to resolve the coverage issues.

Insurance companies must conduct their relations with their policyholders in good faith. RCW 48.01.030; Coventry Assocs. v. Am. States Ins. Co., 136 Wn.2d 269, 276, 961 P.2d 933 (1998). An insurer has a duty to consider the interests of its insured equally with its own in all matters. Tank v. State Farm Fire & Cas. Co., 105 Wn.2d 381, 391, 715 P.2d 1133 (1986). Dismissal of a bad faith claim on summary judgment is only appropriate if the insurer is entitled to prevail

as a matter of law on the facts as construed most favorably to the insured.

Smith v. Safeco Ins. Co., 150 Wn.2d 478, 484, 78 P.3d 1274 (2003).

Red Oaks first contends that MoE failed to perform a thorough investigation into whether there was coverage under Sundquist's policies. Red Oaks's argument on this issue is unavailing.

The implied covenant of good faith and fair dealing requires the insurer to conduct a reasonable investigation before denying coverage and to perform any necessary investigation in a timely manner. Coventry Assocs., 136 Wn.2d at 281.

MoE's investigation was not undertaken in such a way that it breached its duty of good faith. MoE was fully apprised of the facts it needed in order to make a coverage determination. MoE correctly believed that those facts did not result in coverage for the damages claimed. MoE reserved its rights on that basis. Further, MoE did not have any duty to immediately seek judicial resolution of the coverage issues. An insurer can wait for a resolution of the underlying action before seeking a declaratory judgment as to coverage issues without violating the duty of good faith. Associated Indem. Corp. v. Wachsmith, 2 Wn.2d 679, 685, 99 P.2d 420 (1940); Alaska Nat'l Ins. Co. v. Bryan, 125 Wn. App. 24, 35, 104 P.3d 1 (2004); Western Nat'l Assurance Co. v. Hecker, 43 Wn. App. 816, 821 n.1, 719 P.2d 954 (1986). MoE's actions were consistent with the requirements imposed by its duty.

Red Oaks next contends that MoE breached its duty to sufficiently inform Sundquist of its reservation of rights and of developments relevant to coverage. Again, we disagree.

An insurer has the responsibility to fully inform the insured of its reasons for its reservation of rights and of developments relevant to coverage under the policy. Tank, 105 Wn.2d at 388. The duty of full disclosure also obligates an insurer to disclose the policy provisions it relies upon in denying a claim. WAC 284-30-330(13).

MoE did not breach its duty to inform Sundquist of its reasons for its reservation of rights. MoE informed Sundquist of its position that the "Umbrella Policy will not pay for the cost of damage to your clients' own work or products, or products they sold; damage caused by their 'faulty workmanship.'" MoE expressly cited the supplemental endorsement, which provides that the policy does not apply "to Property Damage to work performed by the Named Insured arising out of the work or any portion thereof, or out of the materials, parts, or equipment furnished in connection therewith." MoE also informed Sundquist that coverage could exist for damage to property other than Sundquist's work or products, but that MoE reserved its rights pending a judicial determination of the scope of coverage. This informed Sundquist of MoE's position that the policy did not cover claims arising from Sundquist's own work. By setting forth its rationale for its reservation of rights in its letter to Sundquist, MoE complied with the insurer's duty of good faith.

Red Oaks next argues that MoE breached its duty of good faith by allegedly failing to inform Sundquist of developments relevant to Sundquist's coverage. Red Oaks argues that MoE breached its duty by failing to apprise Sundquist that MoE prevailed in a separate superior court case involving a dispute similar to Sundquist's. However, a trial court's coverage determination in a separate matter is not a "development" that would trigger MoE's obligation to apprise Sundquist, because the decision is neither a "fact" impacting Sundquist's claim nor controlling authority for the purpose of interpreting the language of Sundquist's policy. MoE's actions in this regard did not contravene its obligations to apprise Sundquist of developments related to MoE's analysis of whether the policy issued to Sundquist covered the losses claimed.

Red Oaks next contends that MoE violated its duty of good faith by demonstrating greater concern for its own interests than for those of its insured. Red Oaks argues that MoE's refusal to settle claims against its policyholder with knowledge that it "would likely expose its insured to an additional five or six hundred thousand dollars of liability" amounted to bad faith. We conclude that it did not.

As our Supreme Court stated:

If the insurer is unsure of its obligation to defend in a given instance, it may defend under a reservation of rights while seeking a declaratory judgment that it has no duty to defend. A reservation of rights is a means by which the insurer avoids breaching its duty to defend while seeking to avoid waiver and estoppel. "When that course of action is taken, the insured receives the defense

promised and, if coverage is found not to exist, the insurer will not be obligated to pay."

Truck Ins. Exch. v. VanPort Homes, Inc., 147 Wn.2d 751, 761, 58 P.3d 276 (2002) (quoting Kirk v. Mt. Airy Ins. Co., 134 Wn.2d 558, 563 n.3, 951 P.2d 1124 (1998)) (citation omitted). However, an insurer has no obligation to pay for claims not actually covered by the policy. James E. Torina Fine Homes, Inc. v. Mut. of Enumclaw Ins. Co., 118 Wn. App. 12, 18, 74 P.3d 648 (2003); Hayden v. Mut. of Enumclaw Ins. Co., 141 Wn.2d 55, 1 P.3d 1167 (2000).

MoE argues, and we agree, that that the duty to give equal consideration to the insured's interests in all matters does not require an insurer to abandon its own rights under the insurance contract. MoE's "refusal" to settle claims against its policyholder based on its coverage position was properly premised on its correct analysis of its coverage obligation.

We decline to rule that an insurer's refusal to pay out a settlement negotiated by its insured, at a time when the insurer contests whether the applicable policy covers the loss, amounts to a breach of the duty of good faith, simply because the insured might eventually face greater financial liability for non-covered losses. This is consistent with the principle that "If coverage is found not to exist, the insurer will not be obligated to pay." Truck, 147 Wn.2d at 761 (quoting Kirk, 134 Wn.2d at 563 n3.).

We affirm the trial court's summary judgment ruling on these issues.

C. Insurance Regulations

Red Oaks next contends that MoE's conduct violated the standards for insurers set forth within chapter 284-30 WAC, and constituted bad faith as a matter of law. We disagree.

Red Oaks argues that MoE violated these standards by failing to (1) 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, as required by WAC 284-30-330(13), or (2) comply with WAC 284-30-380(1), which provides:

No insurer shall deny a claim on the grounds of a specific policy provision, condition, or exclusion unless reference to such provision, condition, or exclusion is included in the denial. The denial must be given to the claimant in writing and the claim file of the insurer shall contain a copy of the denial.

Red Oaks argues that MoE violated these regulations by never expressly denying Sundquist's claim, and asserts that MoE might have formed the intention not to cover Sundquist's claims related to the Red Oaks damage months before it informed Sundquist of the policy provisions that MoE relied upon in contesting such coverage.

Red Oaks does not establish that MoE violated these regulations. First, MoE informed Sundquist of its bases for contesting coverage, stating that "[t]he Umbrella Policy will not pay for the cost of damage to [Sundquist's] own work or products, or products they sold," and citing the supplemental endorsement, which provides that the policy does not apply "to Property Damage to work performed

by the Named Insured arising out of the work or any portion thereof, or out of the materials, parts, or equipment furnished in connection therewith.” This is precisely the position that MoE has maintained ever since. Furthermore, MoE defended under a reservation of rights while seeking a declaratory judgment concerning its coverage obligations. Thus, MoE did not simply deny Sundquist’s claim. Red Oaks has not raised a genuine issue of material fact as to whether MoE breached its duty of good faith to Sundquist.

We affirm the trial court’s summary judgment ruling on this issue.

D. Consumer Protection Act

Red Oaks next asserts that the trial court erred when it determined as a matter of law that MoE’s conduct did not violate the CPA.

To successfully assert a cause of action under the CPA, a claimant must show (1) an unfair or deceptive act or practice in trade or commerce that impacts the public interest, and (2) a resulting injury to the claimant’s business or property. Torina, 118 Wn. App. at 20. The first element may be satisfied by showing a violation of any subsection of WAC 284-30-330. Van Noy v. State Farm Mut. Auto. Ins. Co., 98 Wn. App. 487, 496, 983 P.2d 1129 (1999). Where the insured is injured by incurring expenses as a direct result of an insurer’s breach of its duty of good faith, the second element is met. Griffin v. Allstate Ins. Co., 108 Wn. App. 133, 148, 29 P.3d 777 (2001).

Because MoE did not violate any insurance regulation, Red Oaks has not established a per se violation of the CPA. Furthermore, Red Oaks has not established any other actions by MoE that violate the CPA.

We affirm the trial court's summary judgment ruling on this issue.

E. Attorney Fees

Because we affirm the trial court's summary judgment dismissing Red Oaks' claims, we deny Red Oaks' request for attorney fees on appeal under either the attorney fees provision of the CPA or the authority of Olympic Steamship v. Centennial Insurance Co., 117 Wn.2d 37, 811 P.2d 673 (1991).

Affirmed.

Deery, J.

WE CONCUR:

Schindler, ACJ

Cox, J.

APPENDIX B

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 a 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.]

284-30-370 << 284-30-380 >> 284-30-390

WAC 284-30-380

Standards for prompt, fair and equitable settlements applicable to all insurers.

(1) Within fifteen working days after receipt by the insurer of properly executed proofs of loss, the first party claimant shall be advised of the acceptance or denial of the claim by the insurer. No insurer shall deny a claim on the grounds of a specific policy provision, condition, or exclusion unless reference to such provision, condition, or exclusion is included in the denial. The denial must be given to the claimant in writing and the claim file of the insurer shall contain a copy of the denial.

(2) If a claim is denied for reasons other than those described in subsection (1) and is made by any other means than writing, an appropriate notation shall be made in the claim file of the insurer.

(3) If the insurer needs more time to determine whether a first party claim should be accepted or denied, it shall so notify the first party claimant within fifteen working days after receipt of the proofs of loss giving the reasons more time is needed. If the investigation remains incomplete, the insurer shall, within forty-five days from the date of the initial notification and no later than every thirty days thereafter, send to such claimant a letter setting forth the reasons additional time is needed for investigation.

(4) Insurers shall not fail to settle first party claims on the basis that responsibility for payment should be assumed by others except as may otherwise be provided by policy provisions.

(5) Insurers shall not continue negotiations for settlement of a claim directly with a claimant who is neither an attorney nor represented by an attorney until the claimant's rights may be affected by a statute of limitations or a policy or contract time limit, without giving the claimant written notice that the time limit may be expiring and may affect the claimant's rights. Such notice shall be given to first party claimants thirty days and to third party claimants sixty days before the date on which such time limit may expire.

(6) No insurer shall make statements which indicate that the rights of a third party claimant may be impaired if a form or release is not completed within a given period of time unless the statement is given for the purpose of notifying the third party claimant of the provision of a statute of limitations.

[Statutory Authority: RCW 48.02.060 and 48.30.010. 78-08-082 (Order R 78-3), § 284-30-380, filed 7/27/78, effective 9/1/78.]

APPENDIX C

MUTUAL OF ENUMCLAW INSURANCE COMPANY

Policy No: _____

Insured: _____

Effective Date: _____

**BROAD FORM PROPERTY DAMAGE
INCLUDING COMPLETED OPERATIONS**

The exclusions of this policy relating to Property Damage are replaced by the following exclusion:

A. To Property Damage:

1. To property owned or occupied by or rented to the Insured or, except with respect to the use of elevators, to property held by the Insured for sale or entrusted to the Insured for storage or safekeeping.
2. Except with respect to liability under a written sidetrack agreement or the use of elevators to:
 - (a) property while on premises owned by or rented to the Insured for the purpose of having operations performed on such property by or on behalf of the Insured,
 - (b) tools, or equipment while being used by the Insured in performing his operations,
 - (c) property in the custody of the Insured which is to be installed, erected or used in construction by the Insured,
 - (d) that particular part of any property, not on premises owned by or rented to the Insured,
 - (1) upon which operations are being performed by or on behalf of the Insured at the time of the Property Damage arising out of such operations, or
 - (2) out of which any Property Damage arises, or
 - (3) the restoration, repair or replacement of which has been made or is necessary by reason of faulty workmanship thereon by or on behalf of the Insured;

- B. With respect to the COMPLETED OPERATIONS HAZARD to Property Damage to work performed by the Named Insured arising out of the work or any portion thereof, or out of materials, parts or equipment furnished in connection therewith.

The insurance afforded by this endorsement shall be excess insurance over any valid and collectible property insurance (including any deductible portion thereof) available to the Insured, such as but not limited to Fire and Extended Coverage, Builder's Risk Coverage or Installation Risk Coverage.

APPENDIX D

No. 56509-5-I
(Linked to No. 57820-1)

THE COURT OF APPEALS, DIVISION I,
OF THE STATE OF WASHINGTON
SEATTLE

RED OAKS CONDOMINIUM OWNERS ASSOCIATION,
a Washington Non-Profit Corporation

Appellant,

v.

MUTUAL OF ENUMCLAW INSURANCE COMPANY

Respondent.

MOTION TO PUBLISH

Brent W. Beecher, WSBA #31095
Attorneys for Appellant Mutual of Enumclaw

HACKETT, BEECHER & HART
1601 Fifth Avenue, Suite 2200
Seattle, WA 98101
206-624-2200

I. RELIEF SOUGHT BY RESPONDENT

Mutual of Enumclaw respectfully joins in the request of non-party Michael Rogers that the opinion filed July 30, 2007 be designated for publication pursuant to RAP 12.3(e).

II. GROUND FOR RELIEF

The unpublished opinion in this case is of considerable precedential value and should be published because it clarifies existing caselaw. Mr. Rogers pointed out the value of the Court's opinion regarding the scope of an insurer's obligation to settle where there is a failure of coverage for the claim; Mutual of Enumclaw joins Mr. Rogers' position on that issue. Additionally, Mutual of Enumclaw believes that the Court's opinion clarifies the law in three additional respects that would be of substantial aid to litigants and trial court judges in future insurance coverage litigation: first, that the holding of *Schwindt* remains good law, and is not limited to the Lloyds of London policy; second, that the interpretation of policy language by Insurance Services Organization ("ISO") commentators is not binding evidence of the intent of any particular insurer; and third, that insurance agents can bind insurers only within the scope of their authority. Each of these will be addressed.

1. **The Reasoning of *Schwindt* Remains Good Law, and is Not Limited to the Particular Language of the Lloyds of London Policy.**

In the case of *Schwindt v. Underwriters at Lloyds of London*, 81 Wn. App. 293, 305-07, 914 P.2d 119 (1996), this Court held that, for purposes of work / product exclusions, the work of subcontractors merges into the work of the general contractor upon completion of the project. Thus a policy provision that excludes coverage for damage to work performed by the insured general contractor applies to work that the insured chose to perform by means of a subcontractor as well. As was thoroughly briefed by the parties to this appeal, there is a split of authority in the United States on the issue of whether work / product exclusions apply to damage to work performed by subcontractors. In *Schwindt*, this Court considered the reasoning of both sides of that split, and ruled that the better reasoned approach was to treat the work of subcontractors as an integrated part of the general's work.

As was demonstrated by the arguments raised by Red Oaks in this case, and MacPherson in the linked appeal, insured parties are urging trial court judges that *Schwindt* is the "old" rule, and that "modern" jurisprudence has rejected the foundation upon which *Schwindt* is built. The Court's opinion in this case makes it clear that developments in the

law of other jurisdictions, on the opposite side of the split, have not changed the law of Washington.

Additionally, both Red Oaks and MacPherson argued that the application of the merger rule in *Schwindt* was limited to the precise language contained in the Lloyds' policy. This Court's opinion clarified the fact that the principle of subcontractor work merging into the work of the general contractor is not limited to the exact wording of the exclusion in the policy at issue in *Schwindt*. Because the opinion in this case clarifies that *Schwindt* remains good law, and that its application is not limited to Lloyds of London, the Court should publish its ruling.

2. **The Interpretation of ISO Commentators is Not the Same Thing as Mutual of Enumclaw's "Intent."**

In *Schwindt*, the Court mentioned that there was no evidence that Lloyds intended to provide coverage for damage to the work of subcontractors. Courts on the other side of the split have ruled that ISO commentary, published years after the policies were drafted, counted as the "intent" of the "insurance industry," and was thus binding on the entire "industry." See *Fireguard Sprinkler Sys., Inc. v. Scottsdale Ins. Co.*, 864 F.2d 648 (9th Cir. 1988). In the case at bar, Red Oaks and MacPherson argued that Mutual of Enumclaw was bound by the ISO commentary; the Court affirmed that Mutual of Enumclaw's use of language similar to that

of the ISO was not an indication that Mutual of Enumclaw intended to adopt an ISO interpretation that conflicted with Washington law. Because there is no law in Washington that addresses the effect of ISO commentary on the application of unambiguous policy provisions, the opinion in this case would be a valuable addition to the law, and should be published.

3. **Insurance Agencies can Bind Insurers Only Within the Scope of their Authority.**

Finally, the opinion in this case addressed the issue of the effect of coverage advice given by independent insurance agents to the insured, where that advice allegedly conflicts with unambiguous policy terms. The Court ruled that the express terms of the agency agreement between the agent and the insurer govern the agent's authority to modify coverage, and, of more significance, that RCW 48.18.190 prohibits coverage advice from the agent from overriding policy terms unless it is accomplished by formal endorsement. The effect of representations made by insurance agents is a perennial subject of litigation, and the lack of appellate authority increases risk to future litigants. The Court should alleviate that risk by publishing its opinion in this case.

III. CONCLUSION

The Court's opinion in this case resolved not only the issue of continued applicability of *Schwindt*, but also the effect of ISO

commentary and representations made by independent agents. All of these issues present themselves repeatedly in insurance coverage litigation. With increased risk comes increased costs to all parties involved in insurance relationships. The Court's decision in this case decreases that risk, and therefore is of general public interest, and appropriate for publication.

RESPECTFULLY SUBMITTED THIS 20th day of August, 2007.



Brent W. Beecher, WSBA #31095
Attorneys for Appellant

CERTIFICATE OF SERVICE

I, Nancy Boyd, declare that on the date noted below I caused to be delivered via ABC Legal Messengers, Inc., a copy of *Respondent's*

Motion to Publish to:

Ken Harer
The Condominium Law Group
10310 Aurora Avenue North
Seattle, WA 98133

Michael Rogers
Reed McClure
Two Union Square
601 Union Street, Suite 1500
Seattle, WA 98101-1363

I Certify Under Penalty of Perjury Under the Laws of the State of Washington that the Foregoing is True and Correct.

SIGNED IN Seattle, WA this 20th day of August, 2007.



Nancy Boyd

FILED
COURT OF APPEALS DIV. #1
STATE OF WASHINGTON
2007 NOV -9 PM 3:46