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STATE OF WASHINGTON

80937-2

No. 80937-2

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

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MUTUAL OF ENUMCLAW INSURANCE COMPANY,

Respondent,

v.

RED OAKS CONDOMINIUM OWNERS ASSOCIATION,  
a Washington nonprofit corporation,

Petitioner.

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PETITIONER'S REPLY TO RESPONDENT'S ANSWER TO  
PETITION FOR REVIEW

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Court Rules

RAP 5(d).....1

Pursuant to RAP 13.4(d), Red Oaks Condominium Owners Association (Red Oaks) submits the following reply to Respondent Mutual of Enumclaw's Answer to Petition for Review.

### A. STATEMENT OF THE CASE

On April 5, 2004, Red Oaks filed a Complaint in this matter asserting individual claims for breach of contract, bad faith, violations of the Consumer Protection Act, and estoppel to deny coverage. CP 3-13. On April 7, 2005, Mutual of Enumclaw (MoE) filed a motion for summary judgment requesting that the trial court rule the Red Oaks' breach of contract claim was excluded by the "faulty workmanship" exclusion of the Umbrella Policy. CP 1439-1458. On June 10, 2005, the trial court issued an Order denying that portion of MoE's motion for summary judgment. CP 899. MoE filed a Notice of Appeal dated August 19, 2005 requesting review of the "faulty workmanship" exclusion issue. CP 1517-18. MoE filed a motion to strike that notice of appeal dated October 11, 2005.

### B. ARGUMENT

#### I. The "Faulty Workmanship" Exclusion Issue Was Not Properly Raised On Appeal

A party seeking cross-review must file a notice of appeal.<sup>1</sup> A notice of cross appeal is necessary if respondent seeks affirmative relief.<sup>2</sup>

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<sup>1</sup> RAP 5(d).

<sup>2</sup> *Robinson v. Kahn*, 89 Wn. App. 418, 948 P.2d 1347 (1998).

MoE initially filed a notice of appeal on the faulty workmanship exclusion issue, but then filed a motion to strike that notice of appeal.<sup>3</sup> By filing the motion to strike, MoE waived review of the trial court's ruling on the faulty workmanship exclusion. MoE argued the faulty workmanship exclusion issue in its briefing, but the Court of Appeals correctly chose not to address or rule on the issue. MoE's request for cross-review of the faulty workmanship issue by the Supreme Court should be denied because it was not properly designated for review before the Court of Appeals.

## **II. Red Oaks' Cause of Action for Bad Faith Estoppel is Not an Affirmative Defense and Was Not Waived**

Washington law provides that estoppel to deny coverage is a cause of action as a remedy for an insurer's bad faith.<sup>4</sup> Red Oaks' Complaint contains a cause of action for estoppel to deny coverage.<sup>5</sup> MoE mistakenly claims that "Red Oaks first raised this issue after two Enumclaw Summary Judgments determined there was no coverage under Sundquist's policies."<sup>6</sup> The motions for summary judgment referenced by MoE only addressed coverage issues. Red Oaks' cause of action for

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<sup>3</sup> CP 1517-18 and Mutual of Enumclaw's Motion to Strike Unnecessary Notice of Appeal dated October 11, 2005.

<sup>4</sup> *Safeco v. Butler*, 118 Wn.2d 383, 823 P.2d 499 (1992); see also *Besel v. Viking Ins. Co. of Wisconsin*, 146 Wn.2d 730, 49 P.3d 887 (2002); *Kirk v. Mt. Airy Ins. Co.*, 134 Wn.2d 558, 565, 951 P.2d 1124 (1998) ("When an insured breaches the duty to defend in bad faith, the insurer should be held liable not only in contract for the cost of the defense, but should also be estopped from asserting the claim is outside the scope of the contract and, accordingly, that there is no coverage.")

<sup>5</sup> CP 3-12.

<sup>6</sup> Respondent's Answer to Petition for Review p. 19.

estoppel to deny coverage is an independent claim related to MoE's breach of its enhanced duty of good faith, not a defense to the coverage issues asserted in MoE's motions for summary judgment. Red Oaks is entitled to pursue claims for MoE's bad faith conduct regardless of the result of any motion regarding coverage claims based on policy language.

The cause of action for estoppel to deny coverage in this case is *not* an affirmative defense; therefore, it was not waived.

The Court of Appeals correctly disregarded MoE's argument on this issue and chose not to address the argument in its decision.

### **III. Misinterpretation of the Court of Appeals' Decision is a Prime Example of the Need For Review by the Supreme Court**

MoE's arguments against review by the Supreme Court focus on the merits of the case and fail to address the reasons for review presented by Red Oaks. In addition, MoE's misinterpretation of the Court of Appeals' decision presents yet another compelling reason for review of this decision by the Supreme Court. If MoE, a litigant deeply familiar with the facts of the case, can misinterpret the Court of Appeals' opinion as illustrated in its Answer, other insurers are likely to as well.

Despite the fact that the Court of Appeals' opinion is unpublished, it will affect thousands of policy holders whose coverage issues will be decided by insurance companies prior to litigation, and without the

evaluation of a court. Unpublished decisions appear in every legal research database and this decision will be used extensively within the insurance industry in making decisions about conduct toward insured parties and as persuasive authority in trial courts to give credence to insurers' actions.

**a. The Burden of Proof Established by the Court of Appeals' Decision is Subject to Misinterpretation and Should be Clarified by the Supreme Court**

The Court of Appeals created an unprecedented burden on an insured party to prove the intent of the insurer in order to succeed on a claim involving policy language interpretation. MoE misinterprets this new burden and attempts to categorize it as a "traditional, old burden".<sup>7</sup> This is a prime example of the potential misuse of the Court of Appeals' decision by insurers against their insureds.

This misinterpretation allows insurers to shift the burden of proof to insured parties who are already at a disadvantage in coverage disputes. Review by the Supreme Court is essential to prevent misuse of the Court of Appeals' decision in this way.

**b. The Obligations of Insurers Established by the WAC and Tank Require Clarification from the Supreme Court**

The Supreme Court and the Legislature have both attempted to

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<sup>7</sup> Respondent's Answer to Petition for Review pg. 12.

control the unjust behavior of insurance companies toward their insureds. The Court of Appeals has negated the legislative intent and the enforcement of WAC provisions by applying only a minimal common law requirement for insurers' communication with their insureds. This minimal requirement eliminates the obligation to provide written notice and specific policy language to an insured when denying a claim and allows insurers like MoE to avoid compliance with the WAC and the enhanced obligation of good faith established by *Tank*.<sup>8</sup> This failure by the Court of Appeals requires review by the Supreme Court.

In its briefing to the Court of Appeals, Red Oaks details MoE's specific behavior toward its insured and explains how MoE's actions violated the WAC provisions and violated MoE's enhanced duty of good faith. MoE does not dispute the facts regarding its conduct. The Court of Appeals' decision endorses MoE's behavior by failing to find that MoE breached its enhanced duty of good faith by violating legislative standards. This allows insurers like MoE to use the decision to justify failure to strictly comply with the WAC standards established by the legislature. Review by the Supreme Court is needed to clarify the obligations of insurers under common law (*Tank*<sup>9</sup>) and legislation (WAC) and to guide the lower courts' enforcement of insurers' obligations to their insureds.

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<sup>8</sup> *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986).

<sup>9</sup> *Id.*

**c. The Court of Appeals' Analysis of the Policy Language is Subject to Misinterpretation and Should be Clarified by the Supreme Court**

The Court of Appeals' decision states the correct legal standard for the interpretation of insurance policies, but fails to follow those standards or apply them to the facts presented. This allows insurers to use the decision against their insureds in coverage disputes as though it were based on well established legal precedent and analysis.

The Court of Appeals' decision does not hold that Red Oaks' interpretation of the policy language is unreasonable nor does it address the issue of whether the policy language is ambiguous or unambiguous as understood by the average person. This determination is essential to policy interpretation, but was disregarded by the Court of Appeals.

MoE interprets the decision to hold that the policy language is unambiguous and Red Oaks' interpretation of the policy language is unreasonable. This reading is not supported by the language of the decision, but is another example of the potential misuse of the decision by insurers. This same policy language is being interpreted by thousands of policy holders, as well as insurance companies, insurance brokers and courts, and this decision will be used within the industry to make insurance coverage determinations. Review by the Supreme Court is necessary to provide clear direction for the correct interpretation of policy

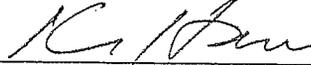
language and to prevent misuse of the Court of Appeals' decision.

### C. CONCLUSION

Red Oaks respectfully requests the Supreme Court accept review of the Court of Appeals' decision of July 30, 2007, for the reasons stated above and those stated in Red Oaks' Petition for Review.

Dated this 31<sup>st</sup> day of December, 2007.

Respectfully submitted,



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