

NO. 64712-1-1

COURT OF APPEALS, DIVISION I
OF THE STATE OF WASHINGTON

NATIONAL SURETY CORPORATION,
Respondent/Cross-Appellant,

v.

IMMUNEX CORPORATION,
Appellant/Cross-Respondent.

APPELLANT’S REPLY
AND CROSS-RESPONDENT’S BRIEF

DICKSTEIN SHAPIRO, LLP

James R. Murray
WSBA No. 25263

1825 Eye Street NW
Washington, DC 20006-5403
(202) 420-2200

Linda D. Kornfeld
Cameron H. Faber
(Admitted *Pro Hac Vice*)

2049 Century Park East, Suite 700
Los Angeles, CA 90067-3109
(310) 772-8300

2010 NOV 12 4:11:10

COURT OF APPEALS
DIVISION I
CLERK OF COURT


Attorneys for Appellant/Cross-Respondent

TABLE OF CONTENTS

	<u>Page</u>
I. INTRODUCTION	1
II. STATEMENT OF ISSUES ON CROSS-APPEAL	3
III. STATEMENT OF THE CASE.....	4
IV. REPLY ARGUMENT	5
A. The <i>AWP</i> Litigation Addresses Differential Treatment Sufficient to Trigger National’s Duty to Defend.....	5
1. The Court Should Disregard Mylan Laboratories and USX Corp.....	7
a. <i>Mylan Laboratories</i>	8
2. USX Corp. v. Adriatic Ins. Co.....	11
B. The <i>AWP</i> Cases “Arise out of” Alleged Discrimination.....	14
V. ARGUMENT IN RESPONSE TO CROSS-APPEAL	17
A. National Must Pay For Immunex’s Defense Fees Incurred Prior to the Trial Court’s Duty to Defend Ruling.....	17
1. Defending Insurers “Defend at Their Expense”	17
2. The Trial Court Properly Rejected National’s “all reward and no risk” approach	22
3. National’s Reservation of Rights Letter Does Not Alter its Contractual Duties to Immunex	24

4.	Foreign Authorities Are In Accord With Washington Law Preventing National from Avoiding its Duties to Immunex for Fees Incurred Before April 14, 2009.....	28
5.	National Surety’s Own Conduct Suggests that a Potential for Coverage in Fact Existed	35
6.	The Fact That National Has Not Yet Paid Immunex Has No Impact On Its Duty To Pay For Fees Incurred Before This Court’s Ruling.....	36
B.	National’s “Pre-Tender” Argument is Unavailing.	37
1.	The Court Should Not Consider an Argument That is Made For the First Time on Appeal.....	38
2.	Unless it Can Prove Prejudice, National is Liable for Immunex’s “Pre-Tender” Defense Costs.....	39
3.	Triable Issues Exist as to When National Received “Notice”	40
4.	Triable Issues of Fact Exist Regarding Whether National Suffered Actual and Substantial Prejudice.....	42
VI.	CONCLUSION.....	47

TABLE OF AUTHORITIES

	<u>Page(s)</u>
<u>Cases</u>	
<i>Agnew v. Lacey Co-Ply</i> , 33 Wn. App. 283, 654 P.2d 712 (1982).....	17
<i>Alaska National Insurance Co. v. Bryan</i> , 125 Wn. App. 24, 104 P.3d 1 (2004).....	25, 26
<i>Am. and Foreign Ins. Co. v. Jerry's Sport Ctr, Inc.</i> , __ A.2d __, 2010 WL 3222404 (Aug. 17, 2010, Sup. Ct. Pa.).....	28, 33, 35, 40
<i>Am. Nat'l. Fire Ins. Co. v. B&L Trucking & Const. Co.</i> , 134 Wn.2d 413, 951 P.2d 250 (1998).....	15
<i>Ames v. Baker</i> , 68 Wn.2d 713, 415 P.2d 74 (1966).....	8
<i>APA - The Engineered Wood Ass'n v. Glen Falls Ins. Co.</i> , 94 Wn. App. 556, 972 P.2d 937 (1999).....	36
<i>Austl. Unlimited, Inc. v. Hartford Cas. Ins. Co.</i> , 147 Wn. App. 758, 198 P.3d 514 (2008).....	14
<i>Avemco Ins. Co. v. Mock</i> , 44 Wn. App. 327, 721 P.2d 34 (1986).....	14, 15
<i>Boeing Co. v. Aetna Cas. & Sur. Co.</i> , 113 Wn.2d 869, 784 P.2d 507 (1990).....	11, 22
<i>Browning v. Rohm & Haas Tenn. Inc.</i> , 16 F. Supp. 2d 896 (E.D. Tenn. 1998).....	16
<i>Canron v. Fed. Ins. Co.</i> , 82 Wn. App. 480, 918 P.2d 937 (1996).....	43
<i>Colony Ins. Co. v. Peachtree Constr. Ltd.</i> , 2009 WL 3334885 (N. D. Texas, Oct. 14, 2009).....	28

<i>E-Z Loader Boat Trailers, Inc. v. Travelers Indem. Co.,</i> 106 Wn.2d 901, 726 P.2d 439 (1986).....	10, 16
<i>Employers Mut. Cas. Co. v. Bartile Roofs, Inc.,</i> ___ F.3d ___, 2010 WL 3473382 (September 7, 2010,10th Cir.)	28
<i>Emter v. Columbia Health Servs.,</i> 63 Wn. App. 378, 819 P.2d 390 (1991).....	21
<i>Farmers Ins. Co. of Wash. v. Miller,</i> 87 Wn.2d 70, 549 P.2d 9 (1976).....	20
<i>Federal Ins. Co. v. Stroh Brewing Co.,</i> 127 F.3d 563 (7th Cir. 1997)	10
<i>Fluke Corp. v. Hartford Accident & Indem. Co.,</i> 145 Wn.2d 137, 34 P.3d 809 (2001).....	26
<i>Gen. Star Indem. Co. v. V. I. Port Auth.,</i> 564 F. Supp. 2d 473 (D. V.I. 2008)	33
<i>General Agents Insurance Co. of America v. Midwest Sporting Goods Co.,</i> 215 Ill. 2d 146, 828 N.E.2d 1092 (2005)	passim
<i>Goodstein v. Cont'l. Cas. Co.,</i> 509 F.3d 1042 (9th Cir. 2007)	41, 44
<i>Griffin v. Allstate Ins. Co.,</i> 108 Wn. App. 133, 29 P.3d 777 (2001).....	39, 40, 43
<i>Hess v. N. Pac. Ins. Co.,</i> 67 Wn. App. 783, 841 P.2d 767 (1992).....	21
<i>Kitsap County v. Allstate Ins. Co.,</i> 136 Wn.2d 567, 964 P. 2d 1173 (1998).....	8
<i>McCauley v. Metro. Prop. & Cas. Ins. Co.,</i> 109 Wn. App. 628, 36 P.3d 1110 (2001).....	15
<i>Minnesota Mutual Life Insurance Co. v. Fraser,</i> 128 Wash. 171, 222 P. 228 (1924).....	19, 20

<i>Mut. of Enumclaw Ins. Co. v. USF Ins. Co.</i> , 164 Wn.2d 411, 191 P.3d 866 (2008).....	passim
<i>Mylan Laboratories Inc. v. American Motorists Ins. Co.</i> , ___ S.E.2d ___, 2010 WL 2484784 (W.Va. 2010).....	passim
<i>Nationwide Mutual Ins. Co. v. Mortensen</i> , 2009 WL 2710264 (D. Conn. Aug. 24, 2009).....	33
<i>Or. Auto. Ins. Co. v. Salzberg</i> , 85 Wn.2d 372, 535 P.2d 816 (1975).....	43
<i>Panorama Vill. Condo. Owners Ass'n Bd. of Dirs. v. Allstate Ins. Co.</i> , 144 Wn.2d 130, 26 P.3d 910 (2001).....	15
<i>Phil Schroeder, Inc. v. Royal Globe Ins. Co.</i> , 99 Wn.2d 65, 659 P.2d 509 (1983), modified, 101 Wn.2d 830, 683 P.2d 186 (1984).....	8
<i>Pulse v. Nw. Farm Bureau Ins. Co.</i> , 18 Wn. App. 59, 566 P.2d 577 (1977).....	44
<i>Rose v. Wells Fargo & Co.</i> , 902 F.2d 1417 (9th Cir. 1990)	16
<i>Safeco Ins. Co. v. Dairyland Mut. Ins. Co.</i> , 74 Wn.2d 669, 446 P.2d 568 (1968).....	25
<i>Shaw v. Sjoberg</i> , 10 Wn. App. 328, 517 P.2d 622 (1973).....	36
<i>Shiplot v. Veneman</i> , 620 F. Supp. 2d 1203 (D. Mont. 2009).....	16
<i>Shoshone First Bank v. Pacific Employers Insurance Co.</i> , 2 P.3d 510 (Wyo. 2000).....	30, 31
<i>St. Paul Fire & Marine Ins. Co. v. Holland Realty, Inc.</i> , 2008 WL 3255645 (D. Idaho, August 6, 2008).....	33
<i>Terra Nova Ins. Co., Ltd. v. 900 Bar, Inc.</i> , 887 F.2d 1213 (3rd Cir. 1989).....	33

<i>Thompson v. Grange Ins. Ass'n</i> , 34 Wn. App. 151, 660 P.2d 307 (1983).....	44
<i>Thurston v. Greco</i> , 78 Wn.2d 424 (1970).....	8
<i>Time Oil Co. v. CIGNA Prop. & Cas. Ins. Co.</i> , 743 F. Supp. 1400 (W.D. Wash. 1990).....	41
<i>Toll Bridge Authority v. Aetna Ins. Co.</i> , 54 Wn. App. 400, 773 P.2d 906 (1989).....	14
<i>Truck Ins. Exch. v. Vanport Homes</i> , 147 Wn.2d 751 (2002).....	22
<i>Truong v. Allstate Prop. and Cas. Ins. Co.</i> , 151 Wn. App. 195, 211 P.3d 430 (2009).....	38
<i>Unigard Ins. Co. v. Leven</i> , 97 Wn. App. 417, 983 P.2d 1155 (1999).....	40, 41
<i>United Pac. Ins. Co. v. Guar. Nat'l Ins. Co.</i> , 97 Wn.2d 139, 641 P.2d 173 (1982).....	46
<i>USX Corp. v. Adriatic Insurance Co.</i> , 99 F. Supp. 2nd 593 (W.D. Pa. 2000).....	passim
<i>Utica Mut. Ins. Co. v. Rohm & Haas Co.</i> , 683 F. Supp. 2d 368 (E.D. Pa. 2010).....	28
<i>Van Noy v. State Farm Mutual Automobile Insurance Co.</i> , 98 Wn. App. 487, 983 P.2d 1129 (1999).....	25
<i>W. Nat'l Assur. Co. v. Hecker</i> , 43 Wn. App. 816, 719 P.2d 954 (1986).....	46
<i>Washburn v. Beatt Equip. Co.</i> , 120 Wn.2d 246, 840 P.2d 860 (1992).....	38
<i>Westchester Fire Insurance Co. v. Wallerich</i> , 563 F.3d 707 (8th Cir. 2009).....	31, 32

Willing v. Cmty. Ass'n Underwriters of Am., Inc.,
2007 U.S. Dist. LEXIS 48543 (W.D. Wash. July 5, 2007)21

Woo v. Fireman's Fund Ins. Co.,
161 Wn.2d 43, 164 P.3d 454 (2007)..... passim

Statutes

GR 14.1(b)21
RCW 48.18.19024, 25
RCW 48.18.26025
W. Va. Code § 46A-6L-101(1)-(2)10

Other Authorities

RAP 2.5(a)38

Thomas V. Harris

Washington Insurance Law, § 11.1 (2009).....17, 26
Washington Insurance Law, § 16.1 (2009).....22
Washington Insurance Law, § 17.1 (Supp. 2009).....27

I. INTRODUCTION

Immunex Corporation responds first to National Surety Corporation's ("National") Response Argument, and then to National's Argument in Support of Cross-Appeal ("Cross-Appeal Argument"). With respect to National's Response Argument, National narrowly and improperly construes its policies, the allegations in the Average Wholesale Price Litigation ("*AWP* Litigation") and the law to conclude wrongfully that it has no duty to defend. For example, National asserts that its policies' "discrimination" coverage applies only when the allegations in the underlying litigation state a claim for "discrimination against individuals on such bases as gender, religion, and age." Response Argument, 14. However, in its policies National did not define "discrimination" so narrowly. Instead, National simply used the broad, vague, and undefined term "discrimination." As a result, under Washington law National cannot now rewrite its policies to narrow its coverage.

National also misconstrues and mischaracterizes the allegations in the *AWP* Litigation. In so doing, National ignores long-standing Washington law that requires it to interpret broadly the allegations in the *AWP* Litigation in favor of coverage when determining its duty to defend. Under Washington Supreme Court precedent, so long as any of the claims

in the *AWP* Litigation potentially may fit within the broad definition of “discrimination,” no matter how remote or unclear those assertions may be, National’s duty to defend is triggered. The *AWP* litigation includes claims of such conduct. Indeed, the *AWP* plaintiffs claim alleged injuries arising out of differential treatment: (1) among providers; (2) between providers and payors; and (3) of the elderly. National responds by focusing on allegations of allegedly non-covered fraudulent conduct. However, the existence of even limited assertions of potentially-covered acts of discrimination triggered National’s duty to defend the *AWP* Litigation.

National should live with the consequences of the broad language it included in the policies it sold to Immunex. The trial court committed error by ruling otherwise.

The trial court was correct, however, in its ruling on August 25, 2009, that National must pay Immunex’s reasonable defense fees and costs incurred up through April 14, 2009, “unless [National] prevails on its late notice claim at trial.” This is so because under Washington law (and the law of many other jurisdictions) an insurer that agrees to defend its insured (as National did here) bears ultimate responsibility for *all* reasonable defense fees incurred by its insured *until* a court expressly rules against the duty to defend. This rule applies *unless* the insurer

sought to protect its interests by issuing a policy containing express language that allows the insurer to avoid paying for defense fees incurred by the insured if no duty to defend is ultimately found to exist. National had such language available to it (and in fact used that language in other policies issued to other insureds). Regardless, National chose not to include such language in the policies it sold to Immunex. As a result, National has no basis to avoid paying Immunex the defense fees it incurred prior to the trial court's duty to defend ruling.

By denying National's Motion Regarding Late Notice, the trial court properly rejected National's contention that Immunex may not recover *any* of its defense fees incurred in the *AWP* Litigation because of Immunex's alleged late notice of the *AWP* Litigation. To prevail on such a theory (on summary judgment) National had to prove, which it could not, that it was actually and substantially prejudiced, *as a matter of law*, by any such "late notice." The trial court's order should be affirmed because issues of fact exist as to whether Immunex's notice of the *AWP* litigation actually was "late" and, if it was, whether National suffered actual and substantial prejudice.

II. STATEMENT OF ISSUES ON CROSS-APPEAL

Immunex objects to Issue No. 2 in Cross-Respondent's Statement of Issues on Cross-Appeal that "An Insurer That Owes No Duty to Defend

Cannot be Liable for Defense Costs Incurred by its Insured Prior to Tender” because this issue was not presented to the trial court. The Court should therefore refuse to consider it for the first time on appeal.

III. STATEMENT OF THE CASE

Immunex agrees with most of the description of National’s policies and the procedural history of this coverage case as set forth in National’s Brief of Respondent/Cross-Appellant (“Respondent’s Brief”). However, in National’s Restatement of Facts it misconstrues and mischaracterizes the allegations in the *AWP* Litigation and says that those allegations address *only* non-covered conduct (i.e., fraud). National cannot, as much as it may try, avoid that the *AWP* plaintiffs assert that differential treatment (*i.e.*, “discrimination”) engaged in by Immunex forms one of the building blocks for the *AWP* claimants’ ultimate damage claims. The existence of even only limited allegations of such potentially covered discrimination trigger National’s duty to defend the *AWP* Litigation.

Immunex also disputes National’s mischaracterization of Immunex’s notice given to National of the *AWP* Litigation. Immunex complied with the policies’ terms by sending its August 21, 2001, and February 14, 2003, communications to National identifying and summarizing that status of the litigation. In any event, this coverage lawsuit has been “stayed” since 2008. And, the stay was entered before

any party conducted discovery. Therefore, no discovery has been conducted regarding whether there is any merit to National's claim of "late notice" or whether National has been actually or substantially prejudiced as a result. CP 1025-1026.

IV. REPLY ARGUMENT

A. **The *AWP* Litigation Addresses Differential Treatment Sufficient to Trigger National's Duty to Defend**

National seeks to avoid its duty to defend by improperly and narrowly construing the term "discrimination" in its policies. National can only reach its unsupported conclusion of "no duty to defend" by ignoring applicable rules of insurance policy interpretation and the relevant facts.

National sold policies to Immunex that, by their terms broadly covered "discrimination," but intentionally did not define that term. Appellant's Brief, 20-21. Exemplar dictionary definitions of "discrimination" make clear that "discriminate" has a commonly understood broad meaning such as "to make a distinction" or "differential treatment." Appellant's Brief, 21; CP 256, 266. Applying these dictionary definitions here, a comparison of the assertions in the *AWP* Litigation with the plain language of the National policies demonstrates that the trial court erred by ruling that National had no duty to defend. The underlying claimants assert that: (1) Immunex did not treat all *AWP*

plaintiffs and providers equally; (2) providers were treated differently in the sale of drugs; and (3) Immunex's alleged conduct disparately impacted the elderly. Each of these allegations suggests differential treatment or distinctions made by Immunex sufficient to constitute "discrimination." As a result, the *AWP* litigation potentially triggered National's "discrimination" coverage.

To avoid that result National claims that its coverage is triggered by more traditional categories of statutory discrimination—such as age, gender, national origin. National's policies do not say that. National could have inserted into its policies, but did not, available policy language that would have significantly narrowed the meaning of "discrimination" to the "unlawful treatment of individuals based on race, color, religion, gender, age or national origin." *Id.*, 23. Thus, National is bound by the language that it in fact did include – the broad, vague and undefined term "discrimination." That language combined with the facts of the *AWP* Litigation triggered National's duty to defend. It was error for the trial court to conclude otherwise. And, *Mylan Laboratories Inc. v. American Motorists Ins. Co.*, ___ S.E.2d ___, 2010 WL 2484784 (W.Va. 2010) and *USX Corp. v. Adriatic Insurance Co.*, 99 F. Supp. 2d 593 (W.D. Pa. 2000) (cited by National in its brief) should not in any manner impact that conclusion.

1. ***The Court Should Disregard Mylan Laboratories and USX Corp.***

National claims that “discrimination” (1) “does not encompass the allegations of anti-competitive conduct at issue here,” (Respondent’s Brief, 13); and (2) does not apply to ““broad-based economic practices which injure markets through the improper elimination of competition accomplished by purposeful manipulation of goods and services”

Id., 14, 24-25. National now heralds *Mylan* and *USX* as authority.

However, as even National admits, the *AWP* Litigation alleges a variety of claims in addition to those regarding alleged anti-trust violations.¹ For this initial reason, the Court should not rely upon either *Mylan* or *USX*.

Moreover, *Mylan* was wrongly decided and the facts in *USX* are easily distinguishable from those at issue in the *AWP* Litigation.

¹ As set forth by National in its Brief, the *AWP* complaints “alleged a variety of claims, including RICO, state unfair trade and protection statutes, civil conspiracy, fraud and breach of contract.” Respondent’s Brief, 5.

a. *Mylan Laboratories*

Mylan should be given no weight by this Court for several reasons.

First, the reasoning of *Mylan* is fundamentally flawed and inconsistent with Washington law.² The West Virginia court in *Mylan* concluded wrongly that the term “discrimination” in the policy at issue there should be narrowly construed against coverage to include only the statutory definition of the term. The court reached that conclusion even though, as here, “discrimination” was not defined or narrowed in the *Mylan* policy. Basic tenets of Washington insurance law do not support the *Mylan* court’s approach. According to Washington courts, a policy term *must* be interpreted in the insured’s favor when it is susceptible to two different but reasonable interpretations. *Kitsap County v. Allstate Ins. Co.*, 136 Wn.2d 567, 576, 964 P. 2d 1173 (1998). Washington courts stress that “any doubts, ambiguities and uncertainties arising out of the language used in the policy must be resolved in [the policyholder’s] favor.” *Phil Schroeder, Inc. v. Royal Globe Ins. Co.*, 99 Wn.2d 65, 69, 659 P.2d 509, 511 (1983), modified, 101 Wn.2d 830, 683 P.2d 186 (1984); *Ames v. Baker*, 68 Wn.2d 713, 717, 415 P.2d 74, 77 (1966)

² In fact, *Mylan* was decided under West Virginia, not Washington, law. *Thurston v. Greco*, 78 Wn.2d 424, 429 (1970) (“We do not adopt, but specifically reject, the language and the reasoning of the West Virginia Court.”)

(“When a policy is fairly susceptible of two different interpretations, that interpretation most favorable to the insured must be applied, even though a different meaning may have been intended by the insurer.”).

National did not define “discrimination” in its policies. Thus, a Washington court should rely upon dictionary definitions to ascertain its meaning. Pursuant to those definitions, the term reasonably can be interpreted in favor of coverage to mean broad “differential treatment” (regardless of age, gender, national origin, etc.). Thus, even if National’s (and the *Mylan* court’s) narrow interpretation constitutes a reasonable interpretation of discrimination, the term has other reasonable meanings. That fact, pursuant to Washington law, means that at the very least the term is ambiguous and should be interpreted in Immunex’s, not National’s, favor. Thus, regardless of the court’s conclusion in *Mylan*, under Washington law the Court should not rely upon a narrow definition of discrimination when interpreting National’s policy.

Second, the *Mylan* court misunderstood the nature and context of the other “offenses” included in the Mylan policies. The *Mylan* court concluded (without citing any authority) that given the nature of the other “offenses” listed within the personal injury line of coverage at issue, “discrimination” should be “understood to mean the type of discrimination based on personal characteristics actionable under federal Title VII or the

State Human Rights Act.” *Mylan*, at 21. The court’s ruling in that regard appears to have been based upon its erroneous presumption that the “personal injury” offenses referenced in the insurer’s policy can only victimize individuals. *Mylan*, at 20-21. However, three of the personal injury offenses identified in the Mylan policy applied to corporations.³ The same is true for discrimination.⁴ Moreover, the fact that the court in *Mylan* found it important that many of the personal injury offenses in the policy were directed to individuals, rather than corporations, should not influence the Court here. Indeed, that conclusion was contrary to even West Virginia statutes that define a “person” to include a corporation.⁵

Third, the *Mylan* decision is contrary to Washington law because the ruling contradicts the construction of “discrimination” that an “average person purchasing insurance” would give the term. *See E-Z Loader Boat Trailers, Inc. v. Travelers Indem. Co.*, 106 Wn.2d 901, 907, 726 P.2d 439 (1986) (“A contract of insurance should be given a fair, reasonable, and

³ *I.e.*, malicious prosecution, slander and libel.

⁴ *Federal Ins. Co. v. Stroh Brewing Co.*, 127 F.3d 563, 570 n. 11 (7th Cir. 1997). Similarly, the definition of “personal and advertising injury” in the National policies does not limit “personal and advertising injury” to injuries suffered only by persons. Five offenses can apply to a corporation: malicious prosecution, abuse of process, libel, slander and discrimination. CP 654.

⁵ *See, e.g.*, W. Va. Code § 46A-6L-101(1)-(2) which defines “person” as “any individual, partnership, corporation”

sensible construction, consonant with the apparent object and intent of the parties, a construction such as would be given the contract by the average man purchasing insurance.”); *Woo v. Fireman’s Fund Ins. Co.*, 161 Wn.2d 43, 52, 164 P.3d 454 (2007). The same rules of construction apply regardless of whether large corporations are involved. *Boeing Co. v. Aetna Cas. & Sur. Co.*, 113 Wn.2d 869, 883, 784 P.2d 507 (1990) (“it would be incongruous for the court to apply different rules of construction based on the [size of] the policy holder”).

Given the multiple reasonable meanings of “discrimination” based on case law and dictionary definitions, an “average person purchasing insurance” would expect discrimination coverage where, as here, the underlying claimants assert various forms of differential treatment by the insured. For this additional reason the *Mylan* decision did not comport with Washington law and should not persuade the Court to rule in National’s favor.

2. *USX Corp. v. Adriatic Ins. Co.*

National (as did the court in *Mylan*) also relies upon *USX* to avoid coverage. *USX* is readily distinguishable. First, that action involved the duty to *indemnify*, not the duty to *defend*. *Id.* at 626. The duty to defend is broader than the duty to indemnify. *Woo*, 161 Wn.2d at 53 (duty to defend is triggered if the “policy conceivably covers the allegations in the

complaint, whereas the duty to indemnify exists only if the policy actually covers the insured's liability"). Under Washington law and its robust pleading standards, Immunex need only show that a "potential" for liability exists, not, as was addressed in *USX*, whether the policies **actually** cover the insured's liability. *Woo*, 161 Wn.2d at 53.

Second, in *USX* the court found that the trial record **conclusively established** that liability was not based on any form of discrimination. "[T]he damage claims which survived were limited solely to [the insured's] anti-competitive market-exclusion activities." *Id.* at 626. In contrast to the facts in *USX*, here Immunex's alleged discriminatory pricing practices and/or their discriminatory impact form at least part of the basis for Immunex's purported liability. Indeed, the court in *USX* acknowledged that although "antitrust liability" created by the Sherman Act "stretches the term [discrimination] beyond any natural and ordinary meaning," economic practices in some situations may trigger personal injury coverage. *Id.* at 624-25. The discriminating "economic practices" identified in the *AWP* Litigation are one such situation. And, in any event, even if there may be reasonable debate about whether the *AWP* Litigation involves injuries arising out of discrimination, the record before the trial court did not "conclusively establish" that the *AWP* Litigation does not involve such injuries. Thus, at the very least, the existence of coverage is

unclear. In that circumstance, the “potential” for coverage existed and National had a duty to defend.

Third, like *Mylan*, the *USX* court cites no legal authority to support its conclusion that “the terms preceding the phrase ‘discrimination’ identify offenses which injure the character or reputation of an individual.” Again, the Court should not be persuaded by that conclusion because the identified offenses in National’s policy can be suffered by both individuals and corporations.

Fourth, the *USX* policy included a different definition of “personal injury” than that contained in National’s policies. Thus, the *USX* court’s “contextual” analysis of the offenses contained in the *USX* policy’s personal injury coverage simply is not applicable here. In fact, some of the terms preceding “discrimination” in the *USX* personal injury coverage, such as “mental injury, mental anguish, shock” are not even included in the personal injury offenses listed in the National policies. CP 654. And, in the *USX* policy, unlike in National’s policy, “discrimination” did not encompass a discrete, delineated offense. Instead, the offense there included “humiliation.” *Id.* at 624-25. As a result, the *USX* court’s conclusion that “‘discrimination’ and its companion ‘humiliation’ are forms of disparate or demeaning treatment of persons” is entirely irrelevant here.

B. The AWP Cases “Arise out of” Alleged Discrimination

As set forth in Appellant’s Brief, the trial court erroneously ruled that “[t]he AWP complaints do not allege damages caused by discrimination.” CP 1023. In other words, according to the trial court to trigger coverage the AWP plaintiffs were required to assert that they suffered “injury” *because of* “discrimination.” National’s policies do not contain such a narrow requirement. Instead, they cover claims for damages ‘because of’ ‘injury’ ‘*arising out of*’ ‘discrimination’ (emphasis added). Appellant’s Brief, 26-8.⁶ This “arising out of” language requires only a loose causal connection between the AWP plaintiffs’ claimed injury and “discrimination.” *See, e.g., Austl. Unlimited, Inc. v. Hartford Cas. Ins. Co.*, 147 Wn. App. 758, 774, 198 P.3d 514 (2008) (“The phrase ‘arising out of’ . . . has a broader meaning than ‘caused by’ or ‘resulted from’ . . . ‘Arising out of’ does not mean ‘proximately caused by.’”); *Toll Bridge Authority v. Aetna Ins. Co.*, 54 Wn. App. 400, 404, 773 P.2d 906 (1989) (“The phrase ‘arising out of’ is unambiguous and has a broader meaning than “caused by” or “resulted from.”); *Avemco Ins. Co. v. Mock*, 44 Wn. App. 327, 329, 721 P.2d 34, 35 (1986) (same).

In light of the broad “arising out of” language used in National’s

⁶ A side by side comparison of the trial court’s erroneous standard with the actual policy standard is contained at page 26 of Appellant’s Brief.

policies, the *AWP* plaintiffs need not claim that their injuries were directly caused by “discrimination.” Indeed, the duty to defend exists as long as the alleged “discrimination” “causally contributed in some way to produce the injury.” *McCauley v. Metro. Prop. & Cas. Ins. Co.*, 109 Wn. App. 628, 634, 36 P.3d 1110 (2001). Thus, the trial court’s replacement of the “arising out of” standard with the narrow direct causation standard was error. *See Am. Nat’l. Fire Ins. Co. v. B&L Trucking & Const. Co.*, 134 Wn.2d 413, 427, 951 P.2d 250 (1998) (if insurer “intended solely to be liable on a pro rata basis it could have included that language in its policy.”); *Panorama Vill. Condo. Owners Ass’n Bd. of Dirs. v. Allstate Ins. Co.*, 144 Wn.2d 130, 141, 26 P.3d 910 (2001) (“The industry knows how to protect itself and it knows how to write exclusions and conditions.”).

National is correct that *Australia Unlimited*, *Toll Bridge* and *Avemco* define “arising out of” to mean “having its origins in,” “growing out of” or “flowing from,” all of which suggest a loose causal connection. National, however, misapplies that standard. National incorrectly claims that *no* causal connection exists between any of the *AWP* claimants’ assertions of discriminating conduct and the claimants’ alleged injuries.

In fact, the *AWP* plaintiffs’ claims directly undermine National’s assertion of no causal connection. Allegations in the *AWP* lawsuits

demonstrate that the *AWP* plaintiffs rely, even if only in limited part, upon claims of disparate treatment to support their claims for damages. *See, e.g.*, CP 927, ¶ 62 (“Defendants further obscure their true prices for their drugs with their policy of treating different classes of trade differently. Thus, for the same drug, pharmacies are given one price, hospitals another, and doctors yet another.”); CP 943, ¶ 80 (“Illinois Medicare, Part B, participants, who are primarily elderly and disabled citizens, have had to pay higher co-pays for their prescriptions than if defendants had truthfully reported the wholesale prices of their drugs.”).⁷ Thus, the *AWP* plaintiffs’ claims “arise out of” discrimination. No further causal connection is required to trigger the duty to defend.

⁷ Indeed, National’s claims handler has acknowledged that age discrimination is alleged in the *AWP* Litigation. CP 616. National seeks to avoid this conclusion by claiming that “[a]ge discrimination claims based upon disparate impact rather than disparate treatment are wholly statutory.” Respondent’s Brief, 27-28. However, National’s cases do not stand for this proposition. *See, e.g., E-Z Loader Boat Trailers, Inc.*, 106 Wn.2d 901 (duty to defend does not arise in a disparate treatment case where employer acted intentionally against employees); *Rose v. Wells Fargo & Co.*, 902 F.2d 1417 (9th Cir. 1990) (Ninth Circuit affirmed entry of summary judgment in favor of employer where former employees did not establish a *prima facie* case of disparate treatment or a disproportionate impact based on age); *Shiplot v. Veneman*, 620 F. Supp. 2d 1203 (D. Mont. 2009) (plaintiff could not set forth a *prima facie* case under the Equal Credit Opportunity Act because she failed to establish two elements of her claim); *Browning v. Rohm & Haas Tenn. Inc.*, 16 F. Supp. 2d 896 (E.D. Tenn. 1998) (court held that assuming disparate impact theory applied to age discrimination cases, the employees failed to show that the hiring criteria caused any disparate impact on older employees).

V. ARGUMENT IN RESPONSE TO CROSS-APPEAL

A. National Must Pay For Immunex's Defense Fees Incurred Prior to the Trial Court's Duty to Defend Ruling

1. *Defending Insurers "Defend at Their Expense"*

National is wrong when it asserts that there is no support under Washington law “for the trial court’s conclusion that National may be liable to reimburse defense costs even though it owed Immunex no contractual duty to defend.” Respondent’s Brief, 35. Under Washington law when an insurer agrees to defend its insured in underlying litigation, the insurer “defends at its expense.” Thomas V. Harris, Washington Insurance Law (“*Harris*”), § 11.1 (2009); *Woo*, 161 Wn.2d at 54 (“the insurer must bear the expense of defending the insured”). That defense is a “valuable service . . . and one of the principal benefits of the liability insurance policy.” *Id.* In fact, unless the insurer and insured agree in their insurance contract to some other arrangement, when an insurer agrees to defend, the insured is entitled to the immediate benefit of that duty. *Agnew v. Lacey Co-Ply*, 33 Wn. App. 283, 288, 654 P.2d 712 (1982) (“A court may not create a contract for the parties which they did not make themselves. It may neither impose obligations which never before existed, nor expunge lawful provisions agreed to and negotiated by the parties”). In the policies National issued to Immunex, the parties did not agree to

modify or qualify National's duty in this regard.

In fact, National's policies specifically define the parameters of National's rights and duties regarding its participation in the defense of litigation against Immunex: "[w]e will have the right and duty to . . . defend any Insured against any Suit seeking damages . . . to which Coverage B applies."⁸ National explicitly gave itself the "right" to defend, so that if it chose to participate in litigation against Immunex, it contractually was entitled to do so. That participation included a contractual obligation also to pay for Immunex's defense. National did not say in its policies what it now would like the Court to conclude—that its duty was only to "advance" defense fees, or that amounts paid were only a "loan." National also did not include any other language that would relieve National of its obligation to pay for defense fees incurred by Immunex prior to the time that a court concluded that National had no duty to defend. Instead, National simply said that it would "defend" Immunex.

If National wanted to limit its duties with respect to defense fees that it agreed to pay under its policies it was required to include express language in its insurance contract to accomplish that goal. The court in

⁸ See, e.g., Policy No. XYZ-000-9670-1909, Section II(B)(1)(a). CP 1392-93.

Minnesota Mutual Life Insurance Co. v. Fraser, 128 Wash. 171, 174-75, 222 P. 228 (1924) addressed a substantially similar issue, and reached this exact conclusion. In that action, Fraser acted as Minnesota Life’s “agent” with respect to selling life insurance. *Id.* at 171. When Fraser did not perform up to expectations, Minnesota Life sued him to obtain reimbursement from him of the monthly advances. *Id.* at 172.

Fraser contended that Minnesota Life had no right to reimbursement because it did not include any language in the parties’ contract that gave it such a right. The court agreed:

Reading that part of the contract covering this subject . . . we are convinced that the advances for general agency expense allowance . . . ***in the absence of some provision in the contract from which such intent can be clearly inferred, . . . are not recoverable.***

Id. at 175 (emphasis added).

The court based its conclusion on other cases where the courts rejected a principal’s effort to get back money paid to an agent, because the parties had no express agreement that the agent must reimburse amounts advanced to it:

there is no agreement that [the principal’s] advance shall create an indebtedness on his part; no word signifying that he is to be a borrower, nor that the plaintiff will lend to him any money. ***These omissions in an agreement so fully and minutely defining the duties and contract obligations of the agent, and the contract rights of the company, are of great significance.*** It would have been much more natural to insert words signifying that to be the true character of the transaction, if it was so intended, than omit them, and much

easier to say directly that [the agent] assumed a personal liability, if that were the fact, than to use words which require an extended argument on the part of counsel to satisfy a referee or court that such liability, although not expressed, may be inferred. It would have been a simple matter to have said that . . . [the agent] would repay the money, if that was the agreement, and ***that such or similar words were not used is one proof, among others, that the parties never intended to enter into such an agreement as has with difficulty been spelt out for them.***

Id. at 174 (emphasis added). See also *Farmers Ins. Co. of Wash. v. Miller*, 87 Wn.2d 70, 73, 549 P.2d 9 (1976) (“the court cannot . . . create a contract for the parties which they did not make themselves, nor can the court impose obligations which never before existed”).

Similarly, National could have inserted language into its policies that confirmed its now-claimed intent that it has no ultimate liability for defense fees it committed to pay before a court ruled on its duty to defend. The fact that it did not include that language “is one proof, among others, that the parties never intended to enter into such an agreement.”

Minnesota, 128 Wash. at 174.

National knew how to write a policy that would allow it to avoid paying for defense fees that ultimately are determined not to be covered by its policy. In fact, Fireman’s Fund, the parent company to National, has issued other policies (during the very same time period that National sold its coverage to Immunex) that create the express right that National seeks here:

In the event the Insurer shall advance Defense Expense . . . prior to the final disposition of the Claim(s), such advance payments by the Insurer shall be repaid to the Insurer by the Insured(s) . . . in the event and to the extent that the Insured(s) shall not be entitled thereto under the terms and conditions of this Policy.

CP 1429.

National did not include any such language here. That fact, in and of itself, confirms National's intent to pay for all reasonable defense fees incurred by Immunex in the *AWP* Litigation prior to the Court's April 14, 2009, ruling. *See, e.g., Willing v. Cmty. Ass'n Underwriters of Am., Inc.*, 2007 U.S. Dist. LEXIS 48543, *16-17 (W.D. Wash. July 5, 2007) ("if defendants had intended to exclude coverage based on 'incidents of ownership' . . . they could have done so. In fact, [another insurer] sold [the insured] a policy after the relevant time period . . . that included just such an exclusion.").⁹ As Washington courts time and again have held:

Insurance policies are almost always drafted by specialists employed by the insurer. In light of the drafters' expertise and experience, the insurer should be expected to set forth any limitations on its liability clearly enough for a common layperson to understand; if it fails to do this, it should not be allowed to take advantage of the very ambiguities that it could have prevented with greater diligence.

Hess v. N. Pac. Ins. Co., 67 Wn. App. 783, 788 n.5, 841 P.2d 767 (1992);

Emter v. Columbia Health Servs., 63 Wn. App. 378, 384, 819 P.2d 390

⁹ In accordance with Washington GR 14.1(b), attached as a Appendix to this Brief are copies of unpublished decisions cited in this Brief. Citation to the attached unpublished decisions is permitted under the law of the jurisdiction of the issuing court.

(1991).

Because National did not include clear language expressing its claimed current intent, it, not Immunex, should suffer the consequences of that omission. *Boeing Co.*, 113 Wn.2d at 887 (“The [insurance] industry knows how to protect itself and it knows how to write exclusions and conditions.”) The language that National chose to include in its policies controls the parties’ relationship. That language nowhere gives National a right to which it now claims it is entitled—the right to first agree to pay for Immunex’s defense, but after obtaining a favorable ruling, seek to avoid its commitment to provide defense benefits to Immunex under its policies.

2. *The Trial Court Properly Rejected National’s “all reward and no risk” approach*

In Washington, when an insurer is not certain regarding its duty to defend, it has two choices—it can outright deny coverage, or it can defend under a reservation of rights while it pursues declaratory relief regarding its duty to defend. *See, e.g.*, *Harris* at § 16.1 (“When an insured tenders the defense of a claim, one of the insurer’s options is to decline the tender and refuse to defend the claim.”); *Truck Ins. Exch. v. Vanport Homes*, 147 Wn.2d 751, 761 (2002) (“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.”); *Woo*, 161 Wn.2d at 54 (“If [Fireman’s Fund] is uncertain of its duty to defend, it may defend under a reservation of rights and seek a declaratory judgment that it has no duty to defend. (citations omitted). Although [Fireman’s Fund] must bear the expense of defending the insured, by doing so under a reservation of rights and seeking a declaratory judgment, [Fireman’s Fund] avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach.”).

If the insurer outright denies coverage, it gets the benefit of not obligating itself to pay any defense fees, but it risks the possibility of bad faith exposure if its coverage evaluation is wrong. *If the insurer agrees to defend while it seeks a court determination of its duties*, it protects itself from a bad faith claim, but obligates itself to pay under its policy until the court rules. In other words, under both approaches the insurer obtains benefits but faces alternative consequences. The cases addressing the situation where the insurer chooses to defend and pursue coverage litigation, do not then rule that if a court finds that no potential for coverage in fact existed, the insurer can avoid liability for defense fees incurred by the insured prior to the court’s ruling. That is exactly what National is asking the Court to rule here. In other words, National seeks to obtain all the reward (*i.e.*, no bad faith exposure) without facing any of the

risk. The trial court properly refused to sanction such an unsupported result.

3. *National's Reservation of Rights Letter Does Not Alter its Contractual Duties to Immunex*

National improperly seeks to use its March 31, 2008, reservation of rights letter to remedy its failure to include language in its policies allowing it to avoid paying for any defense fees if a court at some point rules against a duty to defend. Respondent's Brief at 36.

Washington statutory and case law, as well as the leading Washington treatise on insurance law, however, prevent National from using a reservation of rights letter to create rights for itself that National expressly chose not to include within its policy. In fact, Washington statutory law addresses this very issue and expressly prohibits an insurer from using a reservation of rights letter to unilaterally seek to amend its policy. RCW § 48.18.190. Instead, pursuant to that code section, National can modify its policy *only* with the written consent of its insured. *Id.* ("No agreement in conflict with, modifying, or extending any contract of insurance shall be valid unless in writing and made a part of the policy."). National never obtained any such written consent from Immunex here.

Courts interpreting Section 48.18.190 support this conclusion. For

example, in *Van Noy v. State Farm Mutual Automobile Insurance Co.*, 98 Wn. App. 487, 983 P.2d 1129 (1999), the insureds brought suit against their automobile insurer for breaches of its policy obligations with respect to its handling of the insureds' claims. In part, the insureds argued that the insurer improperly sought via letters to the insureds after the loss, to submit "bills [] for evaluation by a professional review board or other outside independent agency." *Id.* at 491. However, the policies themselves did not authorize any such outside independent review. The court thus relied upon section 48.18.190 and refused to allow the insurer to submit the bills for an independent review, based upon its conclusion that "[a]n insurer may not restrict coverage or otherwise alter terms of an insurance contract with subsequent letters and notices." *Id.* at 493. See also *Safeco Ins. Co. v. Dairyland Mut. Ins. Co.*, 74 Wn.2d 669, 672, 446 P.2d 568 (1968) (citing RCW 48.18.260 court found that insurance policy could not be modified to add driver age restriction because restriction was not written part of policy).

Other Washington authority also prevents National from seeking to use its reservation of rights letter to avoid responsibility for the defense fees that Immunex incurred before the trial court's April 14, 2009, ruling. For example, in *Alaska National Insurance Co. v. Bryan*, 125 Wn. App. 24, 104 P.3d 1 (2004), the court expressly held that a reservation of rights

letter cannot change the contractual relationship between the parties. In that action, assignees of rights under an insurance policy argued that Alaska National made a contractual promise to defend in a reservation of rights letter. The court, however, disagreed:

The purpose of a reservation of rights letter ***is not to change the contractual relationship of the parties***, but rather it is to identify the insurer's position regarding coverage and serves to protect the parties by providing a conditional defense to the insured and protecting the insurer from a bad faith claim if coverage is due.

Id. at 38-39 (emphasis added); *see also Fluke Corp. v. Hartford Accident & Indem. Co.*, 145 Wn.2d 137, 145, 34 P.3d 809 (2001) (“no public policy clearly expressed in Washington statutes or case law . . . would justify overriding the policy’s explicit [language].”).

Harris, the leading treatise on insurance law in Washington, summarizes Washington law on this important point:

The mere service of a unilateral reservation-of-rights letter, . . . is inadequate to create [] a right to reimbursement. Even if an insurer, in its reservation letter, sets forth language reserving the right to reimbursement, the court should not allow such reimbursement unless the insured has signed a non-waiver agreement expressly stipulating that the insurer may seek reimbursement if it is later determined that the insurer never had the duty to defend. In *Woo v. Fireman’s Fund Insurance Co.*, the Supreme Court implicitly recognized that a reservation letter cannot be the basis for retroactive reimbursement of fees when it held that, in reservation-of-rights cases, the insurer “must bear the expense of defending the insured” even if the insurer litigates a concurrent declaratory judgment action.

Harris, at § 17.1 (Supp. 2009).¹⁰

By failing to expressly say in its policies that it does not have to pay defense fees incurred before a court decides its duty to defend, National deliberately chose not to protect itself. Had it wished to limit Immunex's coverage, National could have easily and unequivocally included such language in the policies. Having not done so when it sold its policies, given clear Washington law, National cannot now seek to use its reservation of rights letter to change its obligations to Immunex.

¹⁰ In fact, in *Woo*, the Supreme Court analyzed the duty to defend and stated: "If [Fireman's Fund] is uncertain of its duty to defend, it may defend under a reservation of rights and seek a declaratory judgment that it has no duty to defend. (citations omitted) Although [Fireman's Fund] must bear the expense of defending the insured, by doing so under a reservation of rights and seeking a declaratory judgment, [Fireman's Fund] avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach." 161 Wn.2d at 54. The Court in *Woo* did not mention any insurer right to seek reimbursement when it agrees to defend its insured in a circumstance where it is uncertain about its coverage obligation. Thus, absent policy language stating otherwise, an insurer remains obligated to pay for the fees incurred by its insured prior to the time a court rules that there is no duty to defend.

**4. *Foreign Authorities Are In Accord With
Washington Law Preventing National from
Avoiding its Duties to Immunex for Fees Incurred
Before April 14, 2009***

The trial court's August 25, 2009, Order granting Immunex's motion for payment of defense costs is consistent with the growing trend of courts in other jurisdictions that have expressly ruled on this same issue. In fact, since the trial court's August 25, 2009, Order, additional courts across the country have addressed this very issue and have ruled in favor of the insured.¹¹

These new decisions represent just some of the many courts that have soundly rejected an insurer's effort to avoid its duty to pay for defense fees incurred by insureds, even after a court rules that there is no duty to defend. For example, in *General Agents Insurance Co. of America v. Midwest Sporting Goods Co.*, 215 Ill. 2d 146, 828 N.E.2d 1092 (2005), the Illinois Supreme Court held that an insurer is not entitled to reimbursement of defense fees incurred in an underlying action before the court ruled that there was no duty to defend. In fact, the court refused to permit an insurer to recover defense costs paid pursuant to a reservation of

¹¹ See, e.g., *Employers Mut. Cas. Co. v. Bartile Roofs, Inc.*, ___ F.3d ___, 2010 WL 3473382 (September 7, 2010, 10th Cir.); *Am. and Foreign Ins. Co. v. Jerry's Sport Ctr, Inc.*, ___ A.2d ___, 2010 WL 3222404 (Aug. 17, 2010, Sup. Ct. Pa.); *Utica Mut. Ins. Co. v. Rohm & Haas Co.*, 683 F. Supp. 2d 368 (E.D. Pa. 2010); *Colony Ins. Co. v. Peachtree Constr. Ltd.*, 2009 WL 3334885 (N. D. Texas, Oct. 14, 2009).

rights letter *absent* an express provision in the insurance policy providing such a right. In that action, the City of Chicago and Cook County sued Midwest and others alleging that they created “a public nuisance by selling guns to inappropriate purchasers.” *Id.* at 147. Midwest sought coverage from General, which responded by sending a reservation of rights letter and filing a declaratory relief action. In that letter, General agreed to defend, but claimed a “right to reimbursement.” *Id.* at 148. Midwest accepted General’s payment of defense costs. *Id.* at 148-9. In the declaratory relief action, the court ultimately concluded that General had no duty to defend under its policy. *Id.* at 149.

General thereafter sought to recover its defense fees paid to Midwest prior to the court’s ruling regarding the duty to defend. Just like National has done here, General argued that its duty to defend extended only to claims for damages that were potentially covered under the policy and because the court ruled that the underlying claim was not even potentially covered, General never had any obligation to pay for any of Midwest’s defense fees. *Id.* at 155. According to General, because it had reserved its rights to obtain reimbursement, it was entitled to recoupment and had no responsibility for any amounts incurred before the court’s ruling. Midwest argued to the contrary, claiming that General’s reservation of rights letter “could only reserve the rights contained within

the insurance policy and could not create new rights,” and because General did not include a “right of reimbursement” in its policy, its reservation of rights could not create that right. *Id.* at 154.

The court agreed with Midwest:

As a matter of public policy, we cannot condone an arrangement where an insurer can unilaterally modify its contract, through a reservation of rights, to allow for reimbursement of defense costs in the event a court later finds that the insurer owes no duty to defend.

Id. at 162-63. The court stated that its approach was fair to General because it was within General’s power to avoid the issue entirely. In the first instance, according to the court, “[c]ertainly, if an insurer wishes to retain its right to seek reimbursement of defense costs in the event it later is determined that the underlying claim is not covered by the policy, the insurer is free to include such a term in its insurance contract. Absent such a provision in the policy, however, an insurer cannot later attempt to amend the policy by including the right to reimbursement in its reservation of rights letter.” *Id.* at 164.

Additionally, the court held that when an insurer tenders a defense pursuant to a reservation of rights, “the insurer is protecting itself at least as much as it is protecting its insured.” *Id.* at 163-64. Citing to *Shoshone First Bank v. Pacific Employers Insurance Co.*, 2 P.3d 510, 516 (Wyo. 2000), the court held that General could not have it both ways—if it was

not certain of its right to flat out deny coverage, a potential for coverage must have existed that supported General's legal obligation to defend until the court resolved that issue:

The question as to whether there is a duty to defend an insured is a difficult one, but because that is the business of an insurance carrier, it is the insurance carrier's duty to make that decision. If an insurance carrier believes that no coverage exists, then it should deny its insured a defense at the beginning instead of defending and later attempting to recoup from its insured the costs of defending the underlying action. Where the insurance carrier is uncertain over insurance coverage for the underlying claim, the proper course is for the insurance carrier to tender a defense and seek a declaratory judgment as to coverage under the policy.

Id. at 162.

In *Westchester Fire Insurance Co. v. Wallerich*, 563 F.3d 707 (8th Cir. 2009), the court reached the same conclusion. That action involved a claim for coverage for Westchester's alleged breaches of fiduciary duties in connection with the management and auction of various residential and commercial properties. Westchester agreed to defend Wallerich subject to a reservation of rights including a claimed right to seek "reimbursement." *Id.* at 710. Like the insured in *General Agents*, Wallerich objected to the reservation but accepted Westchester's offer to pay defense expenses. The court ultimately decided against a duty to defend. With respect to Westchester's claimed "right to reimbursement," the court reviewed cases both in favor and against such a claimed right and decided that

Westchester was not entitled to obtain reimbursement:

[A]lthough Minnesota appellate courts have not announced whether they would permit a right of reimbursement, we find the most recent state and federal court decisions' adoption of the minority position more persuasive. Here, Westchester could have included in the policy an express provision for such reimbursement. Westchester cannot now unilaterally amend the policy by including the right to reimbursement in its reservation-of-rights letter.

Id. at 719.

Likewise, in *American and Foreign Insurance Co.*, American and Foreign agreed to defend Jerry's in an underlying lawsuit pursuant to a reservation of its claimed right to seek reimbursement. In a declaratory relief action the trial court concluded that (1) there was no duty to defend, and (2) the insurer was entitled to "reimbursement." In August of this year, the Pennsylvania Supreme Court affirmed the order of the superior court which reversed the trial court's order regarding reimbursement, stating:

[Insurer's] contractual obligation to pay for the defense arose as a consequence of the rules of contract interpretation. It is undisputed that the policy did not contain a provision providing for reimbursement of defense costs under any circumstances. Thus, the right . . . [the insurer] attempts to assert in this case, the right to reimbursement, is not a right to which it is entitled based on the policy. . . .

* * * *

[The insured] cannot employ a reservation of rights letter to reserve a right it does not have pursuant to the contract. As noted above, the policy here did not provide for a right of reimbursement of defense costs for non-covered claims. . . We are persuaded that permitting reimbursement by

reservation of rights, absent an insurance policy provision authorizing the right in the first place, is tantamount to allowing the insurer to extract a unilateral amendment to the insurance contract.

2010 WL 3222404 at *14-15 (citations omitted).

Other courts have reached the same result. *See, e.g., Nationwide Mutual Ins. Co. v. Mortensen*, 2009 WL 2710264 (D. Conn. Aug. 24, 2009) (insurer cannot recoup expenditures made fulfilling its promise to defend pursuant to reservation of rights letters); *Gen. Star Indem. Co. v. V. I. Port Auth.*, 564 F. Supp. 2d 473, 480 (D. V.I. 2008) (insurer could not “reserve any right to reimbursement for defense costs because no such right existed in the Policies.”); *St. Paul Fire & Marine Ins. Co. v. Holland Realty, Inc.*, 2008 WL 3255645 *8 (D. Idaho, August 6, 2008) (court found persuasive those decisions refusing to allow reimbursement absent agreement to the contrary in insurance policy); *Terra Nova Ins. Co., Ltd. v. 900 Bar, Inc.*, 887 F.2d 1213, 1220 (3rd Cir. 1989) (no right to reimbursement because “[i]f the insurer could recover defense costs, the insured would be required to pay for the insurer’s action in protecting itself against the estoppel to deny coverage that would be implied if it undertook the defense without reservation.”).

These cases make clear that when an insurer intends to avoid ultimate responsibility for defense fees that it agrees to pay, but for which a court later rules it has no obligation to pay, it must expressly state that

intent in its insurance policy. If it does not include such language, as National did not do here, the insurer, not the insured, retains ultimate exposure for the amounts spent defending the underlying litigation until a court decides the duty to defend.

National argues against this result by noting that some courts in other states have allowed an insurer to use a reservation of rights letter to protect a right to recoupment of defense fees incurred before the court rules that there is no duty to defend. Respondent's Brief, 36. However, "the decisions finding that an insurer is entitled to reimbursement of defense costs are based upon a finding that there was a contract implied in fact or law, or a finding that the insured was unjustly enriched when its insurer paid defense costs for claims that were not covered by the insured's policy." *General Agents*, 215 Ill. 2d at 160. In other words, these courts allow the insurer to re-write the insurance policy via a reservation of rights letter. However, as discussed above, Washington law expressly precludes insurers from doing exactly that. Thus, the holdings of those courts is not persuasive or helpful here.

In accordance with Washington law, as well as foreign authority cited herein, the Court should affirm the trial court's August 25, 2009, Order that National must pay for Immunex's reasonable defense fees and costs incurred through April 14, 2009.

5. *National Surety's Own Conduct Suggests that a Potential for Coverage in Fact Existed*

National claims that as long as no potential coverage ever existed, it need not pay for any of Immunex's defense fees. However, even National itself acknowledged the existence of a potential for coverage up until the date the trial court ruled upon the duty to defend. Indeed, National knew the nature of the *AWP* Litigation but still decided to defend Immunex under a reservation of rights. If the lack of a potential was in fact clear, National would not have agreed to defend. In other words, if it truly believed that there was no risk that a court might conclude that a potential for coverage existed, National could have denied coverage. It did not do that. That fact evidences that even National agreed (prior to when the Court ruled) that the existence of a potential for coverage was at best unclear. *See General Agents*, 215 Ill. 2d at 162, where the court concluded that:

The question as to whether there is a duty to defend an insured is a difficult one, but because that is the business of an insurance carrier, it is the insurance carrier's duty to make that decision. If an insurance carrier believes that no coverage exists, then it should deny its insured a defense at the beginning instead of defending and later attempting to recoup from its insured the costs of defending the underlying action.

See also Am. and Foreign Ins. Co. v. Jerry's Sport Ctr., Inc., 2010 WL 3222404 at*12 ("Although the question of whether the claim is covered (and therefore triggers the insurer's duty to defend) may be difficult, it is

the insurer's duty to make that decision.”).

As a result, even if National is right that it need not pay for defense fees incurred with respect to claims that were not even potentially covered (and, as discussed above, it is not), National's own response to Immunex's claim for coverage shows that the potential for coverage at least initially existed. That potential requires National to pay for the defense fees incurred by Immunex up until the date that the Court ruled that no duty to defend exists.

6. *The Fact That National Has Not Yet Paid Immunex Has No Impact On Its Duty To Pay For Fees Incurred Before This Court's Ruling*

The facts that many of the cases cited above speak in terms of an insurer's effort to obtain “reimbursement” of amounts actually paid, and National has not yet made any defense fees payments to Immunex, should not change the Court's finding that National must pay for the defense fees incurred by Immunex before this Court's duty to defend ruling. Any conclusion to the contrary would, in violation of Washington law, elevate “form” over “substance.” See, e.g., *Shaw v. Sjoberg*, 10 Wn. App. 328, 331, 517 P.2d 622 (1973) (“Washington does not adhere to a requirement of form over substance.”); *APA - The Engineered Wood Ass'n v. Glen Falls Ins. Co.*, 94 Wn. App. 556, 562, 972 P.2d 937 (1999) (a bill of discovery filed by plaintiff in underlying lawsuit seeking otherwise

unavailable information found to be a suit “seeking damages” within the meaning of the policy because “[t]o hold that . . . [the underlying] suit was not a suit seeking damages would . . . exalt form over substance.”). That conclusion also would reward National for any delay by it in executing the confidentiality agreement, and potentially could encourage other insurers to agree to defend, but delay payment until a court ruled on its duty to defend.

Thus, the fact that National did not pay Immunex the amounts it owed before the Court ruled on National’s duty to defend motion is irrelevant. No authority anywhere turns on that question. National agreed to defend. It, thus, is responsible for the amounts spent by Immunex before this Court ruled.¹²

B. National’s “Pre-Tender” Argument is Unavailing

National argues that even if the trial court’s August 25, 2009, Order was correctly decided (which it was), National still need not pay for Immunex’s “pre-tender” defense costs. Respondent’s Brief, 40-45. However, National is raising this argument for the first time on this appeal. Thus, the Court should reject it. Moreover, given that no discovery has yet taken place regarding the question of “notice,” National

¹² Subject to the reasonableness of the fees. See trial court’s August 25, 2009, Order. CP 1312.

cannot demonstrate at this stage of the proceedings as a matter of law that it did not receive timely notice, or that any alleged “late” notice in fact “prejudiced” National.

1. *The Court Should Not Consider an Argument That is Made For the First Time on Appeal*

National never argued in its Motion for Summary Judgment Re Payment of Defense Costs (CP 1181-1193) and Alternative Motion for Summary Judgment Re Late Notice (CP 1170-1178) as it does here that “an insurer that owes no duty to defend cannot be liable for defense costs incurred by its insured prior to tender.” Respondent’s Brief, 40. Having failed to raise this argument before the trial court, under Washington law the Court should not consider National’s new argument. *See* RAP 2.5(a) (“[t]he appellate court may refuse to review any claim of error which was not raised in the trial court.”). *See also Washburn v. Beatt Equip. Co.*, 120 Wn.2d 246, 290-91, 840 P.2d 860 (1992) (“Arguments or theories not presented to the trial court will generally not be considered on appeal.”); *Truong v. Allstate Prop. and Cas. Ins. Co.*, 151 Wn. App. 195, 204, 211 P.3d 430 (2009) (court rejected insured’s argument regarding fault for accident because “[t]his is not an argument that was made below and we decline to consider it for the first time on appeal.”).

2. Unless it Can Prove Prejudice, National is Liable for Immunex's "Pre-Tender" Defense Costs

This court in *Griffin v. Allstate Ins. Co.*, 108 Wn. App. 133, 140, 29 P.3d 777 (2001), ruled that an insured may recover "pre-tender" defense costs *unless* an insurer establishes that it suffered prejudice from any alleged late notice. National cites to *Griffin* in its Cross-Appeal Argument (pp. 42-44), but takes the holding too far. Based on *Griffin*, National argues that it need not pay for any defense costs incurred by Immunex prior to tender of the *AWP* Litigation because National had no duty to defend. Respondent's Brief, 40. *Griffin*, however, does not support such a conclusion.

And, in any event, as set forth above, National acknowledged a potential for coverage (*i.e.* duty to defend) when it agreed to participate in the litigation against Immunex. That participation included a contractual obligation also to pay for Immunex's defense. "[T]he insurer must bear the expense of defending the insured."). *Woo*, 161 Wn.2d at 54. *See also* discussion, *supra*, at 19-21. If the insurer agrees to defend while it seeks a court determination of its duties, it protects itself from a bad faith claim, but obligates itself to pay under its policy until the court rules. *See* discussion, *supra* at 26. Indeed, an insurer's duty to defend "is a question to be answered by the insurer in the first instance, upon receiving notice of

the complaint by the insured.” *Am. and Foreign Ins. Co.*, 2010 WL 3222404 at *12.

Having recognized the potential for coverage by agreeing to defend, “the duty is not excused by late notice unless . . . [National] is prejudiced.” *Griffin*, 108 Wn. App. at 139. The trial court’s August 25, 2009, Order that National is obligated to pay Immunex’s reasonable defense fees incurred up until April 14, 2009, “unless plaintiff prevails on its late notice claim at trial” was therefore in accordance with *Woo* and *Griffin*. It would have been error for the trial court to have ruled otherwise.

3. *Triable Issues Exist as to When National Received “Notice”*

Even if the Court were to consider National’s “pre-tender” argument, National cannot prove at this stage of the coverage litigation that Immunex’s notice in fact was in any manner “late.” Resolution of the “notice” issue would be inappropriate at this time.

First, Immunex gave National notice of the claims underlying the *AWP* Litigation as early as 2001 with an update in 2003. CP 1047-49; 1054-1057. Citing *Unigard Ins. Co. v. Leven*, 97 Wn. App. 417, 426-27, 983 P.2d 1155 (1999), National argues that these tenders were insufficient because Immunex did not specifically ask National to undertake the

defense of the actions. Respondent's Brief, 41-42. Although *Leven* states that "the insured must affirmatively inform the insurer that its participation is desired," *Leven*, 97 Wn. App. at 427, the facts in that case and others demonstrate otherwise.

In *Leven*, the court addressed the timeliness of a notice to the insurer of the insured's designation as a "PLP" relating to a contaminated property. Nothing in the facts indicated that the insured specifically requested a defense in the notice that was given to the insurer. *Time Oil Co. v. CIGNA Prop. & Cas. Ins. Co.*, 743 F. Supp. 1400 (W.D. Wash. 1990), is cited favorably by the court in *Leven* for its holding that the insured must specifically request a defense. However, in *Time Oil Co.* notice was found to be insufficient because it referred to an excess policy instead of the general liability policy, not because the notice did not specifically request the insurer to defend. *Id.* at 1416. Notice in accordance with the terms of the policy is all that is required. *Mut. of Enumclaw Ins. Co. v. USF Ins. Co.*, 164 Wn.2d 411, 191 P.3d 866 (2008) (emphasis in original) ("The duties to defend and indemnify do not become *legal obligations* until a claim for defense or indemnity is *tendered.*"); *Cf. Goodstein v. Cont'l. Cas. Co.*, 509 F.3d 1042, 1056 (9th Cir. 2007) (no notice given where insured in correspondence specifically informed insurer that it was not making any claims under the policy).

Here, the National policies state that the insured must notify National as soon as practicable “if a claim is made or Suit is brought against any insured.” CP 639. Immunex complied with the policy terms by sending its August 21, 2001, and February 14, 2003, communications to National identifying and summarizing that status of the litigation.

Second, given the stay in place, no discovery has yet to be conducted on this issue. CP 1025-26; 1209. Without the benefit of any discovery there is no basis to presume *as a matter of law* that National did not in fact have sufficient notice of the *AWP* Litigation before October 2006. Immunex has had no opportunity to conduct any discovery regarding this issue to determine what information or documents may exist that would undermine National’s claim that it did not receive timely notice of the *AWP* Litigation. Thus, there is no basis at this stage of the proceedings for the Court to make any ruling regarding the “timing” of Immunex’s notice.

4. *Triable Issues of Fact Exist Regarding Whether National Suffered Actual and Substantial Prejudice*

Even if National was able to demonstrate, as a matter of law, that Immunex provided “late notice,” which Immunex disputes for the reasons set for the above, the trial court properly determined that National was unable to overcome the extremely high standard that must be met under

Washington law before any such “late notice” can provide an insurer with a basis to avoid coverage. In fact, Immunex cannot be deprived “of the benefits of the policy unless [National] demonstrates actual prejudice resulting from the insured’s noncompliance.” *Canron v. Fed. Ins. Co.*, 82 Wn. App. 480, 485, 918 P.2d 937 (1996). “The burden of proof is on the insurer.” *Id.*

Whether late notice prejudiced an insurer is typically a question of fact. *Or. Auto. Ins. Co. v. Salzberg*, 85 Wn.2d 372, 377, 535 P.2d 816 (1975). In *Oregon Auto*, the court reversed the lower court’s grant of summary judgment for the insurer stemming from late notice, holding that “an alleged breach of a cooperation clause is generally a question for the trier of fact, . . .”(emphasis added). “Except in extreme cases, we do not presume prejudice.” *Griffin v. Allstate Ins. Co.*, 108 Wn. App. 133, 141, 29 P.3d 777 (2001).

And, under Washington law, “extreme” enough to warrant a finding of prejudice *on summary judgment* means seriously “extreme.” The following cases make the point that the trial court’s order denying Alternative Motion for Summary Judgment Re Late Notice should be affirmed because National cannot possibly prove sufficient prejudice here to support summary judgment:

1. *Mut. of Enumclaw Ins. Co.*, 164 Wn.2d at 427, 431 (court reversed summary judgment in favor of insurer because

insurer did not demonstrate prejudice as a matter of law despite the fact that the insurer was not notified of the underlying lawsuit until two years after the suit settled and four years after the suit was filed);

2. *Thompson v. Grange Ins. Ass'n*, 34 Wn. App. 151, 163, 660 P.2d 307 (1983) (trial court judgment finding no prejudice arising from late notice of uninsured motorist claim upheld despite fact that insured failed to give notice of claim for five years and statute of limitations expired against tortfeasor during that time);
3. *Pulse v. Nw. Farm Bureau Ins. Co.*, 18 Wn. App. 59, 62, 566 P.2d 577 (1977) (summary judgment in favor of insurer reversed because no prejudice as a matter of law even though insurer not notified of claim until after judgment in underlying action); and
4. *Goodstein v. Cont'l Cas. Co.*, 509 F.3d 1042, 1047-49 (9th Cir. 2007) (in environmental contamination case where insured sought damages for diminution in value of real property, court reversed summary judgment in insurer's favor because there was no prejudice as a matter of law despite fact that insured delayed twelve years before giving notice during which time contaminated property was sold by the insured).

In *Enumclaw*, the Washington Supreme Court's most recent articulation of the "late tender rule," the court made clear that the bar for insurers to overcome on a motion for summary judgment regarding prejudice is extremely high. In reversing a motion for summary judgment in favor of an insurer that claimed that it was prejudiced because it received late notice of a claim, the court held that in determining whether an insurer has shown "actual and substantial prejudice" due to late notice, a court must consider a variety of factual circumstances. In other words, merely stating the amount of time that has passed between the date an

insured was served with a complaint and the date the insurer was notified of the complaint will not be sufficient to establish prejudice. The court stated:

[E]ven where an insured breaches a “prompt notice” provision of an insurance policy, the insurer is not relieved of its duties under the insurance contract unless it can show that the late notice caused it actual and substantial prejudice . . . ***Whether or not late notice prejudiced an insurer is a question of fact, and it will seldom be decided as a matter of law***

Enumclaw, 164 Wn.2d at 426-27 (citations omitted, emphasis added).

Here, National claims that its “potential liability for defense costs has been extended for years by Immunex’s late notice and delay. Respondent’s Brief, 47. However, that simply is not true. To start, the record is clear that National never was in any hurry to resolve coverage issues even under its version of the facts. Indeed, National waited until March 31, 2008, ***almost 1½ years after October 3, 2006*** (the date that even National acknowledges that it received notice), to file its declaratory relief action. CP 1059; 1067-1083. Thus, National has caused at least part of its claimed prejudice that it now seeks to pass off onto Immunex. National cannot expect this Court to conclude, as a matter of law, that it would have behaved differently given earlier notice.

Moreover, even if National can “prove” that it would have brought an earlier declaratory relief action against Immunex, that does not mean

that National could have relieved itself of any prejudice it claims it suffered by Immunex's alleged delay in notice. In fact, given Washington "stay" of coverage litigation law, National had no absolute right to pursue coverage litigation immediately after receiving notice of the *AWP* Litigation. As the trial court recognized when it entered the stay in this action, Washington law is clear that coverage litigation must be "stayed" when the risk exists it could prejudice the insured in underlying litigation. See, e.g., *W. Nat'l Assur. Co. v. Hecker*, 43 Wn. App. 816, 821, n.1, 719 P.2d 954 (1986) (court recognized stay pending resolution of an underlying action as viable method of protecting the parties' rights); *United Pac. Ins. Co. v. Guar. Nat'l Ins. Co.*, 97 Wn.2d 139, 147, 641 P.2d 173 (1982) (staying effect of declaratory judgment to allow resolution of overlapping issues in the underlying action).

Therefore, regardless of when National received notice, it had no absolute right to have its duty to defend immediately resolved. Under Washington (and most states') law, coverage litigation frequently takes a second seat to resolution of an insured's underlying tort litigation. Thus, National cannot possibly prove that it in fact has suffered any prejudice by a delay in notice because it cannot prove that it would have been able to have earlier resolved its duty to defend just because it got earlier notice.

Thus, under the standard set forth in *Enumclaw*, National's Motion

was properly denied by the trial court because the question of whether National would have commenced its declaratory relief action sooner (or could have had its duty to defend resolved sooner) had Immunex given earlier notice involves questions of fact. The trial court's August 25, 2009, Order Denying Alternative Motion for Summary Judgment Regarding Late Notice should therefore be affirmed.

VI. CONCLUSION

For all the foregoing reasons, the Court should reverse the trial court's April 14, 2009, Order regarding the Duty to Defend and its August 25, 2009, Order regarding the Duty to Indemnify. In addition, the Court should affirm: 1) the trial court's August 25, 2009, Order Denying Plaintiff's Motion for Summary Judgment Regarding Payment of Defense Fees and Costs and Granting Defendant's Motion for Partial Summary Judgment Regarding Payment of Defense Fees and Costs; and 2) the trial

c

c

court's August 25, 2009, Order Denying Plaintiff's Alternative Motion for
Summary Judgment Re Late Notice.

DATED: November 11, 2010

DICKSTEIN SHAPIRO LLP

By: 

James R. Murray
WSBA #25263
DICKSTEIN SHAPIRO LLP
1825 Eye Street NW
Washington, DC 20006-5403
Tel: (202) 420-2200
Fax: (202) 420-2201
E-mail: murrayj@dicksteinshapiro.com

Linda D. Kornfeld
Cameron H. Faber
DICKSTEIN SHAPIRO LLP
2049 Century Park East, Suite 700
Los Angeles, CA 90067
Tel: (310) 772-8300
Fax: (310) 772-8301
E-mail:
kornfeldl@dicksteinshapiro.com;
faberc@dicksteinshapiro.com
Attorneys for Appellant/Cross-
Respondent Immunex Corporation

CERTIFICATE OF SERVICE

The undersigned certifies that on this 11 day of November, 2010, I caused to be served this document entitled **APPELLANT'S REPLY AND CROSS-RESPONDENT'S BRIEF** via Federal Express and e-mail to:

Ronald Clark, Esq.
Bullivant Houser Bailey PC
888 S.W. Fifth Avenue,
Suite 300
Portland, OR 97204-2089
E-mail: ron.clark@bullivant.com

Jerret E. Sale, Esq.
Matthew J. Sekits, Esq.
Deb Carstens, Esq.
Bullivant Houser Bailey PC
1601 Fifth Avenue, Suite 2300
Seattle, Washington 98101-1618
E-mail: Jerret.sale@bullivant.com;
matthew.sekits@bullivant.com;
deb.carstens@bullivant.com

Catherine W. Smith, Esq.
Edwards, Sieh, Smith & Goodfriend, P.S.
500 Watermark Tower
1109 First Avenue
Seattle, WA 98101-2988
Tel: (206) 624-0974
E-mail: cate@washingtonappeals.com

I declare under penalty of perjury under the laws of the state of California that the foregoing is true and correct, this 11 day of November, 2010, at Los Angeles, California.


Katherine Hardie