

# WASHINGTON INSURANCE LAW LETTER™

A SURVEY OF CURRENT  
INSURANCE LAW AND  
TORT LAW DECISIONS

EDITED BY WILLIAM R. HICKMAN

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WET WINTER 2003

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THIS NEWSLETTER IS PROVIDED AS A FREE SERVICE for clients and friends of the Reed McClure law firm. It contains information of interest and comments about current legal developments in the area of tort and insurance law. This newsletter is not intended to render legal advice or legal opinion, because such advice or opinion can only be given when related to actual fact situations.

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## GEODUCK COVERAGE

### FACTS:

Seabed and the Department of Natural Resources entered into a contract concerning the harvesting of 110,000 lb. of geoduck from the pristine waters of Puget Sound. [For our non-northwest readers, the geoduck (*Panopea generosa*) is the largest digging clam in the world, ranging from 1.5 lbs to 12 lbs with a giant fleshy siphon which dangles from its 4- to 6-inch long shell.]

The contract required Seabed to indemnify DNR for all claims for injuries or death. It also required Seabed to procure and maintain insurance for DNR's benefit. DNR was to be named as an additional insured, there was to be a waiver of subrogation, and it was to be a CGL policy with \$1 million/\$2 million limits.

One day, DNR went out to check on how Seabed was doing in harvesting the geoduck. Unfortunately, the DNR boat collided with and damaged Seabed's harvest vessel.

At the time of the collision, Seabed had a CGL policy with SAFECO. When the damage claimed was submitted, coverage was denied. [Ed. Note: Every ISO CGL policy I have read in the past 30 years has a watercraft exclusion.] So Seabed sued DNR, alleging that DNR's captain had been negligent and his negligence had proximately caused damage to Seabed's harvest vessel. DNR took the position that while it may have been negligent, it did not owe Seabed anything, citing the indemnity clause and the insurance clause.

The trial court denied DNR's summary judgment motion. But Division II accepted discretionary review of the denial of summary judgment, reversed, and ordered Seabed's complaint dismissed.

### HOLDINGS:

(1) If one actually reads the indemnity clause, one will discern that it relates to "claims for injuries or death." The claim here is for property damage. The indemnity clause does not apply.

(2) To support a claim based on breach of a contract to obtain insurance, one must show that the contract imposed a duty, that the duty was breached, and that the breach proximately caused damage.

(3) Seabed had an obligation to procure insurance, and because the SAFECO policy "did not cover the watercraft involved here," the obligation was breached.



(4) Seabed's breach in not obtaining the insurance required by paragraph 22 damaged DNR in an amount equal to Seabed's claim for damage to its watercraft.

COMMENT:

Paragraph 22 required Seabed to procure a "Comprehensive General Liability" policy. Since time immemorial, or at least 1973, CGL policies have had a watercraft exclusion which provides that the policy does not apply to bodily injury or property damage arising out of the use of any watercraft operated by any insured. It seems to me that if Seabed had obtained exactly what paragraph 22 described, it would not have covered this accident.

The opinion has some useful citations to other cases which involved failure to obtain insurance. *U.S. Oil & Ref. Co. v. Lee & Estes Tank Line, Inc.*, 104 Wn. App. 823, 16 P.3d 1278 (2001) (refinery entitled to recover damages caused by trucking company's breach of promise to obtain liability insurance with refinery as additional insured). *Christiansen v. Holiday Rent-A-Car*, 845 P.2d 1316, 1321 (Utah App. 1992), cert. denied, 853 P.2d 897 (Utah 1993) (quoting *Richmond v. Grabowski*, 781 P.2d 192, 194 (Colo. App. 1989)) ("party who agrees to procure insurance and fails to do so assumes the position of the insurer and, thus, the risk of loss").

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*Seabed Harvesting v. Dep't of Natural Res.*, \_\_\_ Wn. App. \_\_\_, 60 P.3d 658 (2002).

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## THE TWIN BODY BLESSING

FACTS:

Grandmaster Lu founded the True Buddha School. The Temple is associated with the School. The practice of the school is a combination of Taoism, sectarian Buddhism, and Tantric Buddhism. Grandmaster Lu is recognized by the followers as a living Buddha.

Ethel [not her real name] became a follower of Lu in 1992. Sometime in 1996, she was not feeling too good. So she started going to the Temple to receive blessings. While she was there, she had headaches. According to Ethel, Lu said he could cure her headaches, save her life, and cure her illness. He recommended the "Twin Body Blessing."

Lu performed the "Twin Body Blessing" on Ethel multiple times over the next three years. After a while, Ethel began to suspect that the "Twin Body Blessing" was just plain old-fashioned sexual intercourse. So Ethel sued Lu and the Temple. Her claims against the Temple included claims for breach of fiduciary duty, negligent pastoral counseling, and



negligent retention and supervision of Lu. The trial court dismissed all the claims against the Temple.

While the case against Lu proceeded toward trial, Ethel appealed the dismissal of the Temple. The Court of Appeals affirmed the dismissal of all the claims against the Temple.

#### HOLDINGS:

(1) While there are genuine issues of fact regarding notice and control, they are not material because the First Amendment bars the claim.

(2) Clergy sexual misconduct and the consequences that flow from such misconduct continue to be the subjects of much litigation. A principal question for religious institutions associated with clergy accused of sexual misconduct is whether the First Amendment bars vicarious liability for such institutions.

(3) The First Amendment does not provide churches with absolute immunity to engage in tortuous conduct. So long as liability is predicated on secular conduct and does not involve the interpretation of church doctrine or religious beliefs, it does not offend constitutional principles.

(4) Here, the court would have to examine the religious doctrine of the True Buddhist faith to determine whether the Temple was negligent in its "supervision and retention" of Grandmaster Lu. That necessarily would involve the "excessive entanglement the First Amendment jurisprudence forbids."

(5) If a civil court were to review the conduct of the Temple to determine whether it should have exercised better supervision of Grandmaster Lu, that court would necessarily entangle itself in religious precepts and beliefs. The truth of the beliefs is not open to question by civil courts. Should the Temple have been other than "obedient" to Grandmaster Lu under the circumstances of this case? Should the Temple have seen faults in or "criticized" him? Should the Temple have "slandered" him by calling into question the activities of which it had knowledge? We can see no way that a civil court could avoid interpreting the religious doctrine in determining whether the Temple was liable for negligent supervision and retention. In short, there are no neutral principles of law governing this case that would permit a civil court to resolve the question of liability against the Temple.

(6) Our Supreme Court has held that neither current Washington case law nor considerations of public policy favors the imposition of respondeat superior or strict liability for an employee's intentional sexual misconduct.



COMMENT:

The author of the opinion appears to be walking a very delicate line between the First Amendment and a Washington Supreme Court opinion which has already punched a hole in religious tort immunity. It will be interesting to see how the current court responds to this decision.

For those of you who have been out of school for some time, the pertinent part of the First Amendment provides:

**Amendment I**

Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; . . .

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*S.H.C. v. Lu*, 113 Wn. App. 511, 54 P.3d 174 (2002).

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## A REALLY, REALLY BIG OPINION

FACTS:

The insured construction consultant was sued when the homes his clients had built proved defective. The work had been done by subcontractors who had contracted directly with the clients. The complaints alleged several construction defects.

The insured's CGL carrier denied a defense over a year after the tender. The denial letter, while it quoted extensively from the policy, did not provide any analysis or explanation of how the policy language excluded coverage. Although the denial letter said the insurer had conducted a thorough investigation, an internal memo indicated that a month earlier it had said it was difficult to assess whether the insured was negligent because the insurer had not accepted the tender and had not begun to investigate all the liability issues.

Five months later, the insured wrote the company to ask for an explanation of the denial. The letter advised that the costs of defense might cause the insured to go out of business. The company never responded.

Nearly four years after the tender, the insurer filed a declaratory action. For the first time, the insurer set forth its reasons for the denial: that the claims were essentially malpractice



claims and a CGL policy is not a malpractice policy. The insured counterclaimed for estoppel, breach of contract, and bad faith.

In the meantime, the insured settled the claims for \$489,685. The insured's clients agreed to collect only from the insurer; the insured assigned its right to indemnification to the clients.

The trial court ruled there was coverage, that the insurer had a duty to defend, and that it had acted in bad faith in refusing to defend. The trial court found that the settlements were per se reasonable. Judgment of \$689,741 was entered. In an unpublished decision, Division II ruled there was a duty to defend and coverage, but remanded for a determination of whether the settlements were reasonable.

In a 5-4 decision, the Washington Supreme Court affirmed that there was a duty to defend and bad faith. It ruled that the insurer was estopped to deny coverage, but reversed the Court of Appeals to the extent it had remanded for a finding that the settlements were reasonable. The majority ruled that the insurer was liable for the settlements.

#### HOLDINGS:

(1) An insurer that fails to defend in bad faith is estopped from denying coverage. Where an insurer has a duty to defend and the insurer refuses to defend, the insurer is bound by the decision of the trier of fact regarding issues necessarily decided in the litigation.

(2) An insurer's duty to defend is broader than its duty to indemnify. A defense is one of the main benefits of the insurance contract. The duty to defend arises at the time an action is first brought, and is based on the potential for liability. The duty to defend arises when a complaint against the insured, construed liberally, alleges facts which could, if proven, impose liability upon the insured within the policy's coverage. Only if the alleged claim is clearly not covered by the policy is the insurer relieved of its duty to defend. If the complaint is ambiguous, it will be liberally construed in favor of triggering the insurer's duty to defend.

(3) There are two exceptions to the rule that the duty to defend must be determined only from the complaint. Both exceptions favor the insured. If coverage is not clear from the face of the complaint but may exist, the insurer must investigate the claim and give the insured the benefit of the doubt in determining whether the insurer has an obligation to defend.



- (4) Similarly, facts outside the complaint may be considered if
- (a) the allegations are in conflict with facts known to or readily ascertainable by the insurer or
  - (b) the allegations of the complaint are ambiguous or inadequate.

(5) An insurer has an obligation to give the rights of the insured the same consideration that it gives to its own monetary interests. An insurer may not rely on facts extrinsic to the complaint in order to deny its duty to defend where the complaint can be interpreted as triggering the duty to defend. If in doubt, it may file a declaratory action.

(6) Once the duty to defend attaches, insurers may not desert policyholders and allow them to incur substantial legal costs while waiting for an indemnity determination. 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.

(7) A reservation of rights is a means by which the insurer avoids breaching its duty to defend while seeking to avoid waiver and estoppel. The insured receives the defense promised and, if coverage is found not to exist, the insurer will not be obligated to pay.

(8) WAC 284-30-330(13) requires an insurer to promptly provide a reasonable explanation for the denial of a claim. Violations of WAC § 284-30-330 are per se violations of the Consumer Protection Act.

(9) When an insurer wrongfully refuses to defend, it has voluntarily forfeited its ability to protect itself against an unfavorable settlement, unless the settlement is the product of fraud or collusion.

(10) Where an insurer acts in bad faith in refusing to defend, the settlements entered into by insureds with third parties and approved by a court as reasonable will be presumed to be reasonable; such presumption may be overcome by the insurer upon a showing that the settlements were the product of fraud or collusion.

**COMMENT:**

No explanation in the denial letter. No response to a written inquiry. Waiting four years to seek a judicial resolution. It is little wonder the court resolves all doubt in favor of the



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policyholder. The problem arises when the statements in this opinion are leveraged by policyholder's counsel to obtain more coverage than the policyholder ever purchased.

Our thanks to Pam Okano for sorting out the facts and procedure for us.

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*Truck Ins. Exch. v. Vanport Homes, Inc.*, \_\_\_ Wn.2d \_\_\_, 58 P.3d 276 (2002).

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## ENOUGH IS ENOUGH

Way back in the "Summer of New Beginnings 2000" issue of the Law Letter, we reviewed a case called *Hamm v. State Farm*, 101 Wn. App. 360 (2000) (XXIV W.I.L.L. 15 (2001)). Therein the court held that where the insured made no recovery from the uninsured at-fault party, the PIP carrier was not liable for *Mahler* fees.

The Supreme Court accepted Hamm's petition but did not hear the case. Instead, after it issued its opinion in *Winters v. State Farm*, 144 Wn.2d 869 (2001), it sent the *Hamm* case back to the Court of Appeals for reconsideration. After thinking about it for several months, the court published an order on remand in which it stuck to its earlier conclusion.

It said *Mahler v. Szucs*, 135 Wn.2d 398 (1998), and *Winters* did not control because, unlike the policyholders in *Mahler* and *Winters*, Hamm did not recover from the uninsured at-fault driver. Rather, the situation was controlled by *Dayton v. Farmers*, 124 Wn.2d 277 (1994), which held that a UIM insured bears her own attorney fees in a UIM arbitration. The court emphasized that one of the guiding principles in UIM coverage determination is that the UIM claimant is not to be in a better position for having been injured by an uninsured driver than an insured driver. It also noted that "general principles of equity do not require that State Farm pay" *Mahler* fees.

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*Hamm v. State Farm Mut. Ins. Co.*, \_\_\_ Wn. App. \_\_\_, 60 P.3d 640 (2003).

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## A NON-CONTAMINATING METH LAB

### FACTS:

Harry rented a house to Steve. Steve ran a meth lab in the attic. One day the police came with a search warrant. They kicked in the doors. But Steve had already moved on.

Although there was no visible damage to the house (except for the doors), the City said it was unsanitary and classified it as “derelict.” The house could not be rented. So Harry replaced the carpet, painted, and hired some folks to clean up the meth residue. The City approved.

Then Harry notified Allstate and asked for reimbursement. Allstate denied the claim based on the “contamination” exclusion. Harry sued Allstate. The trial court agreed with Harry and gave him his clean-up expenses, loss of rents and attorney fees. The Court of Appeals held that the operation of a meth lab was “vandalism” (a covered event), not “contamination” (an excluded event).

### HOLDINGS:

(1) Interpreting an insurance policy is a matter of law. We interpret an insurance policy to give effect to each of its provisions.

(2) Whether coverage exists is a two-step process. The insured must prove that the policy covers his loss. Thereafter, to avoid coverage, the insurer must prove that specific policy language excludes the loss.

(3) Ultimately, however, the court determines coverage by characterizing the perils contributing to the loss, and determines which perils the policy covers and which it excludes.

(4) Neither Harry, the City, the environmental firm, nor the health department may determine the cause of Harry’s loss. The court characterizes the peril causing the loss.

(5) The tenant acted in conscious or intentional disregard for Harry’s property rights. It can be said that vandalism, a covered peril, preceded the contamination, an excluded peril. First, the tenant exposed the premises to hazardous chemicals—by cooking—and second, there was the resulting contamination.

(6) The tenant’s indoor meth lab created harmful vapors and residues that damaged the rental house. The tenant’s acts were intentional, in disregard of Harry’s property



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interest, and the resulting damage was almost a certainty. This meets the definition of vandalism.

#### COMMENT:

Harry's lawyer called the loss "contamination." The City called it "contamination." The environmental clean-up firm called it "contamination." The health department called it "contamination." But the court was not about to be bound by the common person's common understanding of the term "contamination." (See *Boeing v. Aetna*, 113 Wn.2d 869, 881 (1990)). The panel said it was for the court, not the policyholder or the company or anyone else, to decide which pigeonhole to put the loss in. This is the same court which recently held that "arson" was not "vandalism." (*Dixon v. SAFECO*, 2002 Wash. App. LEXIS 2146 (2002).)

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*Graff v. Allstate Ins. Co.*, 113 Wn. App. 799, 54 P.3d 1266 (2002).

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## GIVEN TO SUBTLE CASUISTRY

In a not-so-recent case, one of the California Courts of Appeal wrote:

Northwestern policy No. CLA255714 is by no means unambiguous as Northwestern contends. More a vehicle for Jesuitical or Talmudic debate than a definition of the rights and obligations of the parties to the contract, the policy crosses one's eyes and boggles one's mind.

The problem arose because the policy used "damage," "ultimate net loss," and "the loss" interchangeably. And this was in a policy where millions of dollars were on the line.

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*Columbia Cas. Co. v. Northwestern Nat. Ins. Co.*, 231 Cal. App. 3d 457, 470 (1991).

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## CLOSE ENOUGH FOR UIM COVERAGE

#### FACTS:

Cheryl picked up her son at daycare. A stranger accosted her, pushed her into the car, said he had a gun, and drove off with her and her child. He forced her to get cash from an ATM, which he used to buy drugs. While he was driving to a field to smoke the drugs,



Cheryl saw a police car. She grabbed her son, opened the door, and rolled out of the car, screaming for help. The kidnapper ran over her legs as he sped off.

Mitch, Cheryl's husband, arrived at the scene a short time later. He saw fire trucks, police cars, and ambulances. He also saw his wife on a stretcher, exhibiting extreme emotional distress while his son screamed uncontrollably.

Mitch and Cheryl had an auto policy with Allstate which had UIM limits of 100/300. They sued the perp, who defaulted. Allstate was allowed to intervene. At the damages hearing, a doctor testified that Mitch suffered from Post Traumatic Stress Disorder triggered when he arrived at the scene. The doctor said Mitch suffered from physical manifestations of the PTSD. Judgments were entered for Cheryl (\$925,000), the son (\$415,000), and Mitch (\$182,000). Allstate paid policy limits to Cheryl and the son but denied coverage for the award to Mitch.

The trial court ruled in favor of Allstate because Mitch did not suffer "bodily injury" and because Mitch's claim did not arise out of the "use" of an uninsured motor vehicle. The Court of Appeals reversed.

#### HOLDINGS:

(1) PTSD accompanied by physical manifestations falls within the definition of "bodily injury" in this context. A family member may recover for emotional distress caused by observing an injured relative at the scene of an accident after its occurrence and before there is substantial change in the relative's condition or location.

(2) Cheryl's legs were run over by the uninsured vehicle. The doctor testified that the incident and Mitch's reaction to the scene upon arrival caused his PTSD with physical manifestations. We see no reason to restrict causal connection to accident situations where the vehicle actually touches the victim. The vehicle here causally contributed to produce Mitch's injuries.

(3) Allstate correctly points out that Mitch's loss of consortium claim is derivative of Cheryl's claim, and is therefore extinguished by the payment to Cheryl. Allstate is also correct that UIM coverage would not include PTSD attributable to the carjacking conduct preceding the scene observed by Mitch when he arrived. Whether Mitch's PTSD constitutes an indivisible injury is unclear. All damage issues must be resolved on remand.

#### COMMENT:

After the court's decision in *Trinh v. Allstate Ins. Co.*, 109 Wn. App. 927 (2002), this result was pretty well carved in stone.

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*Greene v. Allstate Ins. Co.*, 113 Wn. App. 746, 54 P.3d 734 (2002).

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## ONE W-2 IS JUST NOT ENOUGH

### FACTS:

Diana's garage burned down. Farmers sent her \$39,500, the policy limit on the building. Diana then put in a \$161,000 claim for personal property lost in the fire.

Inasmuch as some of the property appeared to be owned by her boyfriend (not covered), or used in business (not covered), Farmers decided to investigate further. It asked her for four years of bank statements, credit card statements, and tax records. She gave them one W-2 form.

Diana sued Farmers. The company denied the claim, asserting that she had not cooperated and that it had been prejudiced because it could not determine whether her claim was fraudulent. The trial court dismissed Diana's lawsuit and the Court of Appeals affirmed.

### HOLDINGS:

(1) Summary judgment for the insurer is proper when an insured breaches an insurance policy's cooperation clause and the insurance company is prejudiced as a result.

(2) An insured who fails to cooperate with the insurer's investigation may forfeit her right to recover under the policy. The insurer's requests for information must be material. Information is material when it concerns a subject relevant and germane to the insurer's investigation as it was then proceeding at the time the inquiry was made.

(3) The policy required the insured to list the damaged property, provide receipts, show the property to Farmers, provide financial and business records as often as Farmers reasonably required, submit to an examination under oath, and provide a sworn statement that detailed the interest of the insured and all others. This policy language sets the scope of the insured's duty to cooperate.

(4) No reasonable juror could find that the insured substantially cooperated with Farmers' request by submitting a single W-2 form. As a matter of law, the insured breached the cooperation clause.



(5) Where an insured's failure to provide financial records breaches a cooperation clause, the insurer needs to show only that the insured's failure prejudiced its ability to determine coverage, regardless of what else the insured did.

(6) Records showing that an insured is in a prosperous and healthy financial condition would help to rule out a financial motive for making a false claim.

**COMMENT:**

Other cases which deal with cooperation or the lack thereof in an investigation include: *Tran v. State Farm*, 136 Wn.2d 214 (1998); *Keith v. Allstate*, 105 Wn. App. 251 (2001); *Pilgrim v. State Farm*, 89 Wn. App. 712 (1997).

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*Rollins v. Farmers Ins. Co.*, 2002 Wash. App. LEXIS 2938 (2002).

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## IMMUNIZED IN QUEBEC

**FACTS:**

Marie was injured by an uninsured Canadian motorist while she was driving in Quebec. Quebec law immunizes motorists from civil liability. Marie's UIM policy covered damages she is legally entitled to recover from the uninsured motorist. Because Marie is not legally entitled to recover from the motorist who injured her, there is no UIM coverage under her policy.

**COMMENT:**

Immunizing drivers involved in auto accidents from civil liability is a rather interesting vehicle for relieving court congestion. It is probably too late to introduce it here.

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*Wylde v. SAFECO Ins. Co.*, 2002 Wash. App. LEXIS 1809 (2002).

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## COMING ATTRACTIONS

Hidden away in the Washington Insurance Code is RCW 48.18.320. To say that most insurance practitioners have never heard of it is an understatement. It is captioned, "Annulment of Liability Policy." It provides:

## RCW 48.18.320

## Annulment of liability policies.

No insurance contract insuring against loss or damage through legal liability for the bodily injury or death by accident of any individual, or for damage to the property of any person, shall be retroactively annulled by any agreement between the insurer and insured after the occurrence of any such injury, death, or damage for which the insured may be liable, and any such annulment attempted shall be void.

Only a couple of cases have ever cited the statute and none have analyzed it. The opportunity for the Supreme Court to tell us whether the statute means what it appears to say has come. The Ninth Circuit has certified the question in a case called *American Continental Ins. Co. v. Steen*.

What happened was that Steen was injured while in a hospital. Subsequently, the hospital went bankrupt. While in bankruptcy, the hospital entered into an agreement with its liability carrier to cancel the policy in exchange for a pro rata refund of premiums. The cancellation was effective August 1. On November 1, Steen sued the hospital. That was the company's first notice of the Steen claim.

The Ninth Circuit has asked the court to tell them whether this was a "prohibited retroactive annulment." We should know in a year or so.

## IT MIGHT BE "SMALL" BUT IT COULD BE "SUPERIOR"

### FACTS:

Shannon hit Douglas. His father hired a lawyer and sued Shannon. State Farm defended and settled for \$7,500 and an agreement to continue PIP payments subject to the policy limits. The PIP policy provided \$35,000 coverage for medical expenses within three years of the accident.

Seven months after the three years expired, the father sued State Farm in small claims court and recovered a judgment for \$170 which State Farm paid.

Two months later, the father again sued in small claims court, this time for \$2,300. State Farm filed suit in superior court asking for a declaration that it had no further obligation



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under the settlement agreement. The trial court decided that State Farm had no liability after the three years had passed.

On appeal, the court spent a great deal of time on the father's claim that the first small claims court judgment against State Farm operated to bar State Farm from relitigating in the superior court its obligation under the settlement agreement. After going through all aspects of collateral estoppel in detail, the court ultimately concluded that State Farm was not bound by the first judgment because the \$170 judgment was below the \$250 threshold needed to appeal. In other words, because State Farm could not appeal the adverse small claims court judgment, it was not precluded from relitigating its rights under the settlement in the superior court.

#### HOLDINGS:

(1) Collateral estoppel, also called issue preclusion, bars relitigation of any issue that was actually litigated in a prior lawsuit. One of the purposes of issue preclusion is to encourage respect for judicial decisions by ensuring finality.

(2) The question is always whether the party to be estopped had a full and fair opportunity to litigate the issue. And that turns on four primary considerations: whether the identical issue was decided in a prior action; whether the first action resulted in a final judgment on the merits; whether the party against whom preclusion is asserted was a party to that action; and whether application of the doctrine will work an injustice.

(3) No appeal of a small claims court judgment is allowed unless the amount in controversy, exclusive of costs, exceeds \$250. State Farm had, therefore, no right to appeal. For this reason alone, we deny preclusive effect to the small claims judgment here.

(4) Unambiguously and appropriately, the settlement agreement subjects payment of PIP to the "limitations and exclusions" of the policy. And that policy in turn includes both a dollar limit and a three-year time limit.

#### COMMENT:

The message herein is to take all lawsuits seriously, whether filed in small claims court or in the superior court.

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*State Farm Mut. Auto. Ins. Co. v. Avery*, \_\_\_ Wn. App. \_\_\_, 57 P.3d 300 (2002).

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## THE CGL POLICY AS THE PERFORMANCE BOND

### FACTS:

DeWitt contracted with Opus to drill and place concrete piles into the ground to serve as a primary component of a big commercial construction project. Things did not go well. The cement did not harden properly. The piles did not have the required strength. As a result, the holes and the piles were unusable. DeWitt had to install 300 more piles.

All of this resulted in delaying the project, abandoning the defective piles, redoing the foundation, and removing and reinstalling work done by other subs. In addition, while DeWitt was installing remedial pipes, it damaged work completed by other subs.

Opus presented DeWitt with a bill for \$3.5 million. DeWitt tendered the claim to its liability carrier, Travelers. Travelers denied the duty to defend and the duty to pay.

After a declaratory judgment action was filed, the court found there was a duty to defend, but no duty to pay and no bad faith.

On appeal, the court held there was a duty to defend, questions of fact as to duty to pay, and no bad faith.

### HOLDINGS:

(1) The defective manufacture of the concrete piles, such that they failed to meet the proper break-strength requirements, constituted an "occurrence."

(2) A subcontractor's unintentional mis-manufacture of a product constitutes an "occurrence."

(3) The inadvertent act of driving over the buried mechanical and site work fits squarely within the policies' definition of "occurrence."

(4) The alleged damage to the construction site caused by DeWitt impaling it with unremovable piles is not "property damage" under the policies. For faulty workmanship to give rise to property damage, there must be property damage separate from the defective product itself.



(5) The damage to the work of other subcontractors, which had to be removed and destroyed as a result of DeWitt's installation of defective piles, is "property damage" within the scope of the policies.

(6) The damage to the buried mechanical and site work caused by DeWitt's movement of heavy equipment was "physical injury to tangible property" and thus constituted "property damage".

(7) There is no policy exclusion that specifically bars coverage for the property damage to the work that other subcontractors performed on the defective piles.

(8) As with the "course of operations" exclusion, there is also a factual dispute involving the applicability of the "care, custody, and control" exclusion.

(9) Because at least some of the claims tendered to Travelers by DeWitt involve property damage within the scope of the policies that is not clearly excluded from coverage, Travelers did have a duty to defend.

(10) When an insurer breaches its duty to defend, recoverable damages for the insured include: (1) the amount of expenses, including reasonable attorney fees the insured incurred defending the underlying action, and (2) the amount of the judgment entered against the insured.

(11) We reject the argument that Washington law permits no allocation of settlement if the insurer breaches the duty to defend. The Washington Supreme Court, in *Kirk v. Mt. Airy Ins. Co.*, 134 Wn.2d 558, 951 P.2d 1124, 1128 (1998), held that when an insurer breaches the duty to defend in bad faith, the insurer is estopped from asserting that alleged claims are outside the scope of coverage. Absent bad faith, the insurer is "liable for the judgment entered *provided that the act creating liability is a covered event* and provided the amount of the judgment is within the limits of the policy." 951 P.2d at 1126 (emphasis added). Because there was no bad faith here, allocation is appropriate. To conclude otherwise would be to afford the same remedy in cases where the insurer has breached the duty to defend in good faith as in cases where such breach was in bad faith.

(12) To establish the tort of bad faith in the insurance context, the insured must show that the insurer's actions were "unreasonable, frivolous, or unfounded." Bad faith will not be found where a denial of coverage or failure to provide a defense is based upon a reasonable interpretation of the insurance policy. Here, Travelers' duty to defend was not unambiguous. The arbitration demand was vague as to the nature of the

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damages giving rise to the claims. The policy coverage was unclear in light of legitimate factual and legal issues pertinent to contract interpretation and application.

#### COMMENT:

Because of the risk and the cost involved, it is not often that we get a full-blown construction defect coverage opinion. Even more rare is having a Ninth Circuit panel review and try to make sense of Washington's insurance law. One of the judges pointed out that if they were writing on a clean slate, they sure as hell would not be holding that improper performance of the contracted work could be an occurrence. That, he noted, converts the CGL policy into a performance bond. But since the Washington Supreme Court had adopted this unique point of view, there was nothing the Ninth Circuit could do about it.

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*DeWitt Constr. Inc. v. Charter Oak Fire Ins. Co.*, \_\_\_ F.3d \_\_\_ 2002 U.S. App. LEXIS 24515 (9th Cir. 2002).

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## THE "X" OPINIONS

Some times it appears to me that not only are we not alone, but some extraterrestrials have landed, abducted members of the Court of Appeals, and have written opinions. What else but alien influence can explain *Beebe v. Moses*? Here, a homeowner (the plaintiff's stepdaughter) hosted a "Tupperware party." For hosting it, she got "a little bowl" and a \$15 credit toward purchasing more Tupperware. The trial court said she was a social host. The Court of Appeals reversed, saying she might be a business host just like Nordstrom or J.C. Penney. Oh, please!

Another example of alien influence is *Bock v. Watson*. Here, the trial judge dismissed the case of a lady who tripped over a garden hose as she walked through a flower nursery looking for a rhododendron. Not only is a garden hose exactly what you would expect to find in a nursery, but this lady saw the hose and still tripped over it. The Court of Appeals said that just having the hose in the nursery and failing to warn the plaintiff about something she saw created a fact issue.

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*Beebe v. Moses*, 113 Wn. App. 464, 54 P.3d 188 (2002).

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*Bock v. Watson*, 2002 Wash. App. LEXIS 2559 (2002).

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## REED MCCLURE IS PLEASED TO ANNOUNCE

### **KEITH KUBIK HAS JOINED THE FIRM AS A PRINCIPAL.**

Keith brings over 10 years of litigation experience to Reed McClure. Keith earned his law degree from the University of San Diego Law School in 1989. At Reed McClure he will focus on insurance defense with an emphasis on complex litigation.

### **NANCY ELLIOT HAS JOINED THE FIRM AS A PRINCIPAL.**

Nancy comes to Reed McClure with many years of experience in medical malpractice defense. She will continue that work at Reed McClure.

### **CATHERINE KVISTAD JOINS THE FIRM AS AN ASSOCIATE.**

Catherine is a 1997 graduate of Willamette University School of Law. She will focus her practice on appellate issues and general litigation.

### **KATINA THORNOCK JOINS THE FIRM AS AN ASSOCIATE.**

Katina joined Reed McClure in January 2003. She graduated from Seattle University School of Law in 2001. She has worked as a deputy prosecutor in King and Pierce Counties. She will be working on the defense of first and third party claims.



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## REED MCCLURE ATTORNEYS

Levi Bendele	206/386-7154	lbendele@rmlaw.com
Mary R. DeYoung	206/386-7091	mdeyoung@rmlaw.com
Nancy C. Elliot	206/386-7007	nelliott@rmlaw.com
Marilee C. Erickson	206/386-7047	merickson@rmlaw.com
Ryan G. Foltz	206/386-7024	rfoltz@rmlaw.com
Anamaria Gil	206/386-7061	agil@rmlaw.com
Susan L. Handler	206/386-7188	shandler@rmlaw.com
William R. Hickman	206/386-7011	whickman@rmlaw.com
Keith M. Kubik	206/386-7124	kkubik@rmlaw.com
Catherine E. Kvistad	206/386-7003	ckvistad@rmlaw.com
Jennifer L. Moore	206/386-7185	jmoore@rmlaw.com
Pamela A. Okano	206/386-7002	pokano@rmlaw.com
John W. Rankin, Jr.	206/386-7029	jrankin@rmlaw.com
Michael S. Rogers	206/386-7053	mrogers@rmlaw.com
Sherry H. Rogers	206/386-7030	srogers@rmlaw.com
GailAnn Y. Startgardter	206/386-7017	gstargardter@rmlaw.com
Earl M. Sutherland	206/386-7045	esutherland@rmlaw.com
Katina C. Thornock	206/386-7006	kthornock@rmlaw.com
Jake D. Winfrey	206/386-7097	jwinfrey@rmlaw.com
Cheryl A. Zakrzewski	206/386-7037	czakrzewski@rmlaw.com

### WHERE TO FIND US:

**REED McCLURE**  
TWO UNION SQUARE  
601 Union Street, Suite 4901  
Seattle, WA 98101-3920

**OUR TELEPHONE NUMBERS:** main: 206.292.4900  
fax: 206.223.0152  
[www.rmlaw.com](http://www.rmlaw.com)

