

1 In this “reverse bad faith” case, Plaintiff Granite State Insurance Company
2 (“Granite State”) seeks declaratory relief that it has no duty to defend or indemnify
3 Defendant Integrity Structures, LLC (“Integrity”), or its assign, the Point at Westport
4 Harbor Homeowners’ Association (“Association”), under an insurance contract. Dkt. 1.
5 It also makes other claims. *Id.* Integrity and the Association counterclaim, in part, against
6 Granite State for breach of the duty to defend. Dkts. 10 and 26. Parties now make cross
7 motions for partial summary judgment.

8 The Court finds that certification of a question[s] to the Washington State
9 Supreme Court is unnecessary.

10 For the reasons below, Granite State’s Motion for Partial Summary Judgment
11 (Dkt. 23) is granted, and the Association’s Cross-Motion for Summary Judgment (Dkt.
12 27) is denied.

14 I. FACTS AND PROCEDURAL HISTORY

15 A. Relevant Facts

16 In 2006, developer Dodson-Duus, LLC (“Dodson-Duus”) contracted with Integrity
17 to be the general contractor for the construction of a multiunit condominium project in
18 Westport, Washington known as The Point at Westport Harbor Condominiums
19 (“Project”). Dkts. 10, at 1; and 28, at 1. Some of Integrity’s members were also
20 members of Dodson-Duus. Dkt. 28, at 1. The Project has 30 units and is located on a
21 jetty or breakwater adjacent to a marina on one side and the ocean on the other. Dkt. 29,
22 at 1.

1 Integrity had several insurance policies during the relevant period. Dkts. 24-2; 24-
2 3; and 28. In addition to its policies with Plaintiff Granite State, Integrity had a
3 Contractor Controlled Insurance Policy with Gemini Insurance Company (“Gemini”),
4 and policies with Century Surety and General Fidelity. Dkts. 24-2, at 2-98; 24-3, at 1-
5 113; and 28.

6 In September 2010, the Association filed suit against Dodson-Duus in Grays
7 Harbor County Washington Superior Court (“underlying lawsuit”). Dkt. 28, at 1; *The*
8 *Pointe at Westport Harbor Homeowners’ Association v. Dodson-Duus, LLC, et. al.*,
9 Grays Harbor County Washington Superior Court case number 10-2-01263-6. In the
10 spring and early summer of 2011, parties in the underlying lawsuit conducted an
11 investigation of the Project, and the Association’s engineer noted “probable deficiencies
12 in the construction of structural support components,” and after additional investigation,
13 concluded that “the design and construction of the lateral force resisting system of the
14 project was dangerously deficient.” Dkt. 29, at 4.

15 Accordingly, on August 11, 2011, the Association filed a First Amended
16 Complaint against Dodson-Duus, adding as defendants Integrity (and others) making
17 claims, in part, for “damages due to defective construction and materials at the project” in
18 the underlying lawsuit. Dkt. 24-1, at 4; *The Pointe at Westport Harbor Homeowners’*
19 *Association v. Dodson-Duus, LLC, et. al.*, Grays Harbor County Washington Superior
20 Court case number 10-2-01263-6, consolidated with 10-2-01699-2. The Association
21 sought, in part, “an award of damages for construction defects, incomplete construction,
22 and related damage” (Dkt. 24-1, at 3), and for negligence against Integrity “by reason of
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1 their having caused defective and dangerous structural conditions and resulting property
2 damage to the Project” (Dkt. 24-1 at 4). The Association also made claims against
3 Integrity “for negligent misrepresentation and fraudulent concealment of building
4 envelope defects.” Dkt. 24-1, at 4. Integrity’s insurer, Gemini, assigned a lawyer, Robert
5 C. Muth, to defend Integrity. Dkt. 28, at 2.

6
7 On September 11, 2012, the Association and Integrity entered into a Contingent
8 Settlement Agreement. Dkt. 24-1, at 41-43. The contingencies were: (1) the Association
9 and Dodson-Duus were to enter into a settlement agreement, which included assignment
10 of all of Dodson-Duus’ rights against Integrity regarding the “design development,
11 construction, inspection, marketing, sale, warranty, and repair” of the Project; (2) the
12 Association was to assert the assigned claims against Integrity; (3) Integrity was to
13 “tender its defense to its three primary general liability insurers . . . and to any contractors
14 or subcontractors who were not enrolled in the Gemini wrap policy. . . . The tender [was
15 to] include notice of [the] contingent agreement to settle;” and (4) no insurer (or other
16 entity to whom the tender made) agreed to defend Integrity within 60 days of the tender.
17 *Id.* If all the contingency terms were met, Integrity consented to judgment in favor of the
18 Association in the amount of \$4.1 million. *Id.*, at 42. Integrity then assigned the
19 Association all rights against all the Project entities and “its three general liability
20 insurance carriers (but not against Gemini).” *Id.* Integrity agreed not to oppose any
21 reasonableness motion with respect to this agreement, and
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23 [D]efense counsel appointed by Gemini for Integrity [would], at the
24 Association’s option, be instructed by Integrity to either preserve the
attorney-client privilege and attorney work product protections against all

1 other parties to the Litigation, insurers and others, or be instructed by
2 Integrity to provide information to the Association regarding the reporting
3 of defense counsel appointed by Gemini to insurers and Integrity regarding
4 the litigation and exposures faced by Integrity in the litigation, and
5 cooperate with the Association in prosecuting the assigned claims.

6 *Id.* In exchange, the Association agreed not to execute on the consent judgment on
7 Integrity and to “defend and hold Integrity harmless against claims, cross-claims, or
8 counterclaims by defendants in any action brought by the Association as assignee of
9 Integrity . . . arising solely out of the assertion of said claims.” *Id.* Counsel that signed
10 the agreement for Integrity was Robert C. Muth and counsel for the Association was
11 Leonard Flanagan. *Id.*, at 44.

12 In September 2012, Dodson-Duus settled with the Association and assigned its
13 claims against Integrity to the Association. Dkt. 28, at 3. On November 5, 2012, the
14 Association filed a Second Amended Complaint in the underlying lawsuit, naming
15 Integrity and others as defendants. Dkt. 24-1, at 46-58. The Association, as Dodson-
16 Duus’ assignee, claimed that Integrity materially breached its contract regarding the
17 Project with Dodson-Duus “in that there are numerous defects or deficiencies in the
18 Project’s materials, installation of the materials, design and/or construction of the
19 project’s weather resistive barrier system, roofs, structural, mechanical and other
20 components.” *Id.*, at 49. They alleged that the:

21 [D]efects or deficiencies listed above have resulted in physical damage to
22 the property, including but not limited to damage to the common elements,
23 limited common elements, and units of [the] Project. Some of the defects
24 and deficiencies may have begun causing such physical damage while
original construction was under way. The defects and deficiencies are
presently causing such physical damage, and will likely result in additional
physical damage.

1 *Id.*, at 49. The Association also made a claim for indemnity and contribution, and for
2 negligence in regard to “structural defects” against Integrity. *Id.*, at 50 and 54. The
3 Association made a claim for negligent misrepresentation and for fraudulent concealment
4 against Integrity in connection with a report on the Project’s building envelope and
5 representations Integrity allegedly made regarding the defective conditions in the
6 building envelope. *Id.*, at 55-56. The Association sought damages, attorneys’ fees, and
7 costs against Integrity. *Id.*, at 57-58.

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9 In late November 2012, Integrity tendered defense of the underlying lawsuit to its
10 three insurance carriers. Dkt. 28. Within thirty days of the tender letter from Integrity,
11 two of the insurance companies, Century Surety and General Fidelity, notified Integrity
12 that they were declining to defend it in the underlying lawsuit because of policy
13 exclusions. Dkt. 28, at 5.

14 On November 29, 2012, Granite State received its tender letter from Integrity
15 written by attorney Robert Muth. Dkt. 24-1, at 62-63. The letter indicated that Mr. Muth
16 represented Integrity and that Integrity was “insisting Granite State provide a defense to
17 Integrity” under “policy number 02-LX8996361-0” in the underlying lawsuit. *Id.*, at 62.
18 The letter maintained that “[u]nder the commercial general liability form CGC0001,
19 Granite State has agreed to pay ‘those sums that the insured becomes legally obligated to
20 pay as damages because of . . . property damage to which this insurance applies.’” *Id.*, at
21 62. The letter further provided that “[y]our immediate attention is requested. Please
22 contact this office immediately upon receipt of this tender in order that the insured’s
23 interests may be protected.” *Id.*, at 63. The letter included a copy of the Second
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1 Amended Complaint from the underlying lawsuit but did not include a copy of the
2 September 11, 2012 Contingent Settlement Agreement between the Association and
3 Integrity. *Id.*, at 63-64. Mr. Muth states that he “did not intentionally withhold any
4 relevant information from [Granite State] or attempt to deceive Granite State.” Dkt. 28,
5 at 4.

6 On December 7, 2012, Granite State responded to Mr. Muth, acknowledged
7 receipt of the tender letter from Integrity, and wrote:

8 At this point, we know very little about the claims being made by the
9 [Association]. In undertaking the investigation of this matter, [Granite
10 State] is not waiving any right to accept, limit, or deny coverage. At this
11 time, we request that you provide additional information necessary to
12 confirm whether or not there is coverage under any of the [Granite State]
13 policy [sic] for this matter. Specifically, we request from you: (1) records
14 relative to your work on this project, (2) scope of work, (3) number of units
15 in project, (4) contracts relative to the construction of this project, (5)
16 certificate of occupancy, (6) any documentation as to the allegations, (7) if
17 work was completed by a sub-contractor, any supporting documents as to
18 their scope of work and copies of applicable subcontracts, and (8) any other
19 documents you believe would assist us in making this coverage
20 determination.

21 Dkt. 24-1, at 66.

22 Mr. Muth forwarded Granite State’s letter to Mr. Edward Flanagan (the
23 Association’s lawyer) and asked him to provide the documents Granite State was
24 requesting. Dkt. 28, at 6. Mr. Muth also notified Mr. Flanagan that he failed to provide
Granite State with a copy of the Contingent Settlement Agreement when he sent the
tender letter, and asked if the Association would waive that contingency. *Id.*, at 6-7. Mr.
Flanagan never provided a substantive response to Mr. Muth’s request. *Id.*, at 7. Mr.
Flanagan did not respond to Granite State. Dkt. 29.

1 On February 5, 2013, Granite State sent an email to Mr. Muth asking if they could
2 “please have a response to our letter?” Dkt. 24-1, at 68.

3 On February 7, 2013, Mr. Muth responded to Granite State’s email and informed it
4 that he has “forwarded [Granite State’s] letter to Mr. Flanagan in Seattle” and that Mr.
5 Flanagan would “be [Granite State’s] point of contact with regard to that tender.” Dkts.
6 24-1, at 70; and 28, at 7. Mr. Flanagan states that he did not respond to Granite State’s
7 requests. Dkt. 29, at 9. Mr. Flanagan maintains that he did not, at that time, represent
8 Integrity. Dkt. 29, at 9.

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10 On April 4, 2013, Granite State again emailed Mr. Muth and copied Mr. Flanagan,
11 and wrote: “[t]o date, we have had no response to our request for information. Please
12 advise if the insured plans to pursue coverage.” Dkt. 24-1, at 72. Mr. Muth did not
13 respond. Dkt. 28, at 7. Later that day, Mr. Flanagan emailed Granite State asking if
14 Granite State would “be so kind as to forward a copy of the policy for [his] review, in
15 order to make that decision.” Dkt. 24-1, at 74. Granite State forwarded a copy of the
16 policy. Dkt. 29, at 10. Mr. Flanagan states that had Granite State “asked whether the
17 insured was still requesting a decision on its tender of defense, presumably either Mr.
18 Muth or [he] would have advised that a defense of [Integrity] was no longer required.”
19 Dkt. 29, at 10. He adds,

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21 This is so because by this time, the 60 day window provided for the insurer
22 to respond in the contingent settlement agreement had long since expired,
23 and the other contingencies were fulfilled. The question [Granite State]
24 asked was still an open one, however, if the Granite State policies had
clearly showed that they could not conceivably cover the allegations of the
Second Amended Complaint, it is unlikely that the Association would have
pursued the coverage claim further.

1 Dkt. 29, at 10. The Association did not respond after Granite State sent the policy.

2 On June 12, 2013, Granite State again wrote Mr. Flanagan asking “is there
3 anything else you need to make your decision?” Dkt. 24-1, at 80. The Association did
4 not respond. Dkt. 29, at 11.

5 On September 30, 2013, a stipulated consent judgment of \$4.1 million was entered
6 against Integrity in favor of the Association in the underlying lawsuit. Dkt. 24-1, at 82-
7 84.

8 On November 20, 2013, Integrity disclosed to Granite State for the first time the
9 facts and details of the September 2012 Contingent Settlement Agreement between
10 Integrity and the Association and the entry of the \$4.1 million consent judgment. Dkt.
11 24, at 3-4.

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13 **B. Procedural History**

14 On January 29, 2014, Granite State filed this diversity case against Integrity
15 seeking declaratory relief that: (1) the policies at issue do not provide coverage for the
16 Association’s claims against Integrity or any part of the \$4.1-million-dollar judgment, (2)
17 Granite State has no duty to indemnify Integrity or its assigns, or pay any “defense costs,
18 judgments, damages, costs, or expenses,” that arise from the Association’s claims against
19 Integrity, and (3) that the purported assignment of claims by Integrity to the Association
20 is unenforceable and void as to Granite State. Dkt. 1. Granite State is seeking damages
21 for breach of contract and attorneys’ fees. *Id.*
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1 Integrity filed an answer, and counterclaims for breach of contract, bad faith,
2 coverage by estoppel, and violation of Washington’s Consumer Protection Act (“CPA”).
3 Dkt. 10.

4 The Association was permitted to intervene on June 25, 2014. Dkt. 25. It also
5 answered and asserted counterclaims against Granite State for breach of contract, bad
6 faith, coverage by estoppel, and for violation of Washington’s CPA. Dkt. 26.

7 **C. Pending Motions**

8 Granite State now moves for partial summary judgment seeking an order that
9 Integrity breached contractual, statutory and common law duties to Granite State;
10 granting Granite State’s declaratory requests one through three in the complaint; leaving
11 for trial issues of causation, damages and request for attorneys’ fees and costs; and
12 dismissing Integrity’s counterclaims for breach of contract, bad faith, coverage by
13 estoppel, and violation of the CPA. Dkts. 23 and 36. The Association opposes the
14 motion. Dkt. 31.

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16 The Association cross moves for summary judgment that Granite State is liable for
17 breach of its duty to defend Integrity, Granite State is liable for insurance bad faith,
18 Granite State has forfeited all coverage defenses, including all defenses based on any
19 alleged breach of notice, cooperation, or consent-to-settle provisions of the policy, and
20 harm is presumed from Granite State’s bad-faith failure to defend. Dkts. 27 and 38.
21 Granite State responds, and opposes the motion. It additionally argues that the
22 Association has not established its standing to bring this cross motion. *Id.*
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1 In response to the Court's request, both parties have submitted briefing on whether it
2 would be appropriate to certify a question or questions to the Washington State Supreme
3 Court. Dkts. 48-51, 53 and 54.

4 **D. Organization of Opinion**

5 This opinion will first address whether the Association has standing to bring
6 motions in this case, then address whether a question or questions should be certified to
7 the Washington State Supreme Court, then Granite State's motion for summary judgment
8 for an order declaring that Integrity breached the contract resulting in prejudice to Granite
9 State and forfeiture of coverage, then the Association's motion for summary judgment for
10 an order declaring that Granite State is liable for breach of its duty to defend Integrity,
11 and lastly, Granite State's motion for summary dismissal of the Association's
12 counterclaims.
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14 **II. DISCUSSION**

15 **A. Standing**

16 To the extent that Granite State challenges the Association's standing based on the
17 argument that the assignment of rights was not perfected in the Contingent Settlement
18 Agreement (Dkt. 37), the motion is denied. In its response to the Association's motion
19 for summary judgment, Granite State argues that the Association has not yet established
20 that it has standing to bring this cross motion. Dkt. 37. It argues that not all of the
21 contingencies in the Contingent Settlement Agreement were met. *Id.* Granite State
22 points out that the agreement required that a copy of the agreement be sent to each of the
23 insurance companies along with the tender letter and Second Amended Complaint. *Id.* It
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1 is undisputed that this was not done. *Id.* Granite State maintains, then, that the
2 assignment of rights was not perfected through the settlement agreement. *Id.*

3 Under Washington law, if a breach of a contract is “‘material,’ the promisee has an
4 election: he or she may treat the breach as a failure of a condition that excuses further
5 performance, and thus terminate the contract, or he or she may waive the condition and
6 allow performance to continue.” *Colorado Structures, Inc. v. Ins. Co. of the West*, 161
7 Wn.2d 577, 588-89 (2007).

8 The Association properly points out that it waived the condition and allowed
9 performance to continue, so the Settlement Agreement (and thus the assignment of rights)
10 is not void on this basis. Accordingly, the Court will consider the motions.

11 **B. Certification of a Question or Questions to Washington State Supreme Court**

12 At the Court’s request, the Association submitted seven potential questions for
13 certification to the Washington Supreme Court. Dkt. 50. It argued that this Court should
14 decide the first four and then send the following to the Washington State Supreme Court:
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- 16 (1) Does an undisclosed agreement that the insured will
17 stipulate to judgment if the insurer does not agree to
18 defend within 60 days of the tender violate the insured’s
19 duty of good faith under RCW 48.01.030 as a matter of
20 law, or demonstrate that the insured has unclean hands?
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22 (2) Where the insurer does not ask any questions about the
23 underlying case, does the insured have a duty to disclose
24 to the insurer a contingent settlement agreement that it
will stipulate to a judgment if the insurer does not agree to
defend within 60 days?

(3) If the undisclosed contingent settlement agreement
violates RCW 48.01.030 or demonstrates unclean hands,
but is unrelated to the insurer’s bad-faith failure to defend

1 against a potentially covered claims [sic] for ten months,
2 then is the insured entitled to (a) damages for breach of
3 contract, (b) a presumption of harm from the failure to
4 defend, (c) forfeiture of the insurer's coverage defenses,
5 or (d) coverage by estoppel?

6 Dkt. 50. Granite State opposes certifying any questions to the Supreme Court and argues
7 that all of the questions can be answered on the record. Dkt. 48.

8 “Washington's Federal Court Local Law Certificate Procedure Act, Wash. Rev.
9 Code §§ 2.60.010–900, authorizes the Washington Supreme Court to accept certified
10 questions from federal courts.” *Queen Anne Park Homeowners Ass'n v. State Farm Fire*
11 *& Cas. Co.*, 763 F.3d 1232, 1235 (9th Cir. 2014). Under RCW 2.60.020, certification of
12 a question to the Washington Supreme Court is appropriate where “it is necessary to
13 ascertain the local law of this state in order to dispose” of a proceeding in federal court
14 and “the local law has not been clearly determined.” Further, under Washington's Rules
15 of Appellate Procedure 16.16,

16 [t]he Supreme Court may entertain a petition to determine a question of law
17 certified to it under the Federal Court Local Law Certificate Procedures Act
18 if the question of state law is one which has not been clearly determined
19 and does not involve a question determined by reference to the United
20 States Constitution.

21 While the Court invited the parties to consider whether there were questions
22 regarding Washington law that should be answered by the Washington Supreme Court,
23 after considering the parties' arguments, the Court concluded that certification is
24 unnecessary and therefore, the Association's request to certify the above question(s) to
the Washington State Supreme Court (Dkt. 50) is denied. In light of the facts here, the
Association has failed to show that “it is necessary to ascertain the local law” in order to

1 dispose of this proceeding in federal court or that “local law has not been clearly
2 determined.” This Court is able to address the merits of the motions and on further
3 reflection does not require the assistance of the Washington Supreme Court. To the
4 extent that the Association moves to certify questions (Dkt. 50), the motion is denied.

5 **C. Summary Judgment Standard**

6 Summary judgment is proper only if the pleadings, the discovery and disclosure
7 materials on file, and any affidavits show that there is no genuine issue as to any material
8 fact and that the movant is entitled to judgment as a matter of law. Fed.R.Civ.P. 56(c).
9 The moving party is entitled to judgment as a matter of law when the nonmoving party
10 fails to make a sufficient showing on an essential element of a claim in the case on which
11 the nonmoving party has the burden of proof. *Celotex Corp. v. Catrett*, 477 U.S. 317,
12 323 (1985). There is no genuine issue of fact for trial where the record, taken as a whole,
13 could not lead a rational trier of fact to find for the non moving party. *Matsushita Elec.*
14 *Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986)(nonmoving party must
15 present specific, significant probative evidence, not simply “some metaphysical doubt.”).
16 *See also* Fed.R.Civ.P. 56(e). Conversely, a genuine dispute over a material fact exists if
17 there is sufficient evidence supporting the claimed factual dispute, requiring a judge or
18 jury to resolve the differing versions of the truth. *Anderson v. Liberty Lobby, Inc.*, 477
19 *U.S. 242, 253* (1986); *T.W. Elec. Service Inc. v. Pacific Electrical Contractors Association*,
20 *809 F.2d 626, 630* (9th Cir. 1987).

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23 The determination of the existence of a material fact is often a close question. The
24 court must consider the substantive evidentiary burden that the nonmoving party must

1 meet at trial – e.g., a preponderance of the evidence in most civil cases. *Anderson*, 477
2 U.S. at 254, *T.W. Elect. Service Inc.*, 809 F.2d at 630. The court must resolve any factual
3 issues of controversy in favor of the nonmoving party only when the facts specifically
4 attested by that party contradict facts specifically attested by the moving party. The
5 nonmoving party may not merely state that it will discredit the moving party’s evidence
6 at trial, in the hopes that evidence can be developed at trial to support the claim. *T.W.*
7 *Elect. Service Inc.*, 809 F.2d at 630 (relying on *Anderson, supra*). Conclusory, non
8 specific statements in affidavits are not sufficient, and “missing facts” will not be
9 “presumed.” *Lujan v. National Wildlife Federation*, 497 U.S. 871, 888-89 (1990).

11 **D. Granite State’s Motion for Summary Relief for a Declaration That Integrity**
12 **Breached the Contract, Resulting in Prejudice to Granite State and**
13 **Forfeiture of Coverage**

14 “Cooperation is essential to the insurance relationship because that relationship
15 involves a continuous exchange of information between insurer and insured interspersed
16 with activities that affect the rights of both.” *Staples v. Allstate Ins. Co.*, 176 Wn. 2d 404,
17 411 (2013). “Typically, an insured that substantially and materially breaches a
18 cooperation clause is contractually barred from bringing suit under the policy if the
19 insurer can show it has been actually prejudiced. The burden of proving noncooperation
20 is on the insurer.” *Id.*, at 410 (*internal citations omitted*). “The only limitation on the
21 requirement that insureds cooperate with the insurer’s investigation is that the insurer’s
22 requests for information must be material to the circumstances giving rise to liability on
23 its part.” *Tran v. State Farm Fire & Cas. Co.*, 136 Wn. 2d 214, 224 (1998)(*citing*
24 *Pilgrim v. State Farm Fire & Cas. Ins. Co.*, 89 Wn. App. 712 (1997)). Information is

1 material, if at the time the inquiry was made, it “concerns a subject relevant and germane
2 to the insurer’s investigation as it was then proceeding.” *Id.*

3 The Granite State policy includes the following relevant provisions:
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5 **CONDITIONS**

6 **2. Duties in the Event of Occurrence, Offense, Claim or Suit**

7 a. You must see to it that we are notified as soon as practicable of an
8 “occurrence” or an offense which may result in a claim . . .

9 b. If a claim is made or “suit” is brought against any insured, you
10 must:

11 (1) Immediately record the specifics of the claim or “suit” and the
12 date received; and

13 (2) Notify us as soon as practicable.

14 You must see to it that we received written notice of the claim or
15 “suit” as soon as practicable.

16 c. You and any other involved insured must:

17 (1) Immediately send us copies of any demands, notices, summonses
18 or legal papers received in connection with the claim or “suit;”

19 (2) Authorize us to obtain records and other information;

20 (3) Cooperate with us in the investigation or settlement of the claim
21 or defense against the “suit,” and

22 (4) Assist us, upon our request, in the enforcement of any right
23 against any person or organization which may be liable to the insured
24 because of injury or damage to which this insurance may also apply.

d. No insured will, except at that insured’s own costs, voluntarily
make a payment, assume any obligation, or incur any expense, other than
for first aid without our consent.

Dkts. 24-2, at 26 and 24-3, at 35–36. Under the heading “Transfer of Your Rights and
Duties under this Policy,” the contract further contains a provision providing: “[y]our
rights and duties under this policy may not be transferred without our written consent
except in the case of death of an individual named insured.” Dkts. 24-2, at 14 and 24-3,
at 21.

1 **1. Alleged Breach**

2 In this case, Integrity, and its assignee the Association, “substantially and
3 materially” breached the notice clauses of the contract. *Staples*, at 410. Integrity and the
4 Association had been in litigation for over 15 months before Granite State was notified of
5 the litigation. There is no evidence that Integrity and the Association notified Granite
6 State of the potential claims “as soon as practicable.”

7 Integrity and the Association “substantially and materially” breached the
8 cooperation clauses of the insurance contract. *Staples*, at 410. Before Integrity notified
9 Granite State of the litigation, it had already entered into the Contingent Settlement
10 Agreement that included a stipulated 4.1-million-dollar judgment, and assigned its claims
11 to the Association. None of that was disclosed to Granite State at the time of the tender
12 letter or in the months that followed. Granite State did not find out about the agreement
13 until almost ten months after the tender was made to it.

14 Further, Granite State began to investigate the claims against Integrity around a
15 week after receipt of the tender letter, in early December 2012. Dkt. 24-1, at 66. It
16 requested basic information which would be “material to the circumstances giving rise to
17 its liability” (*Tran*, at 224), including records of Integrity’s work on the Project, the
18 number of units in the Project, the Project’s construction contracts, the certificate of
19 occupancy, any documentation as to the allegations, documents relating to
20 subcontractors, and any other documents Integrity believed would assist Granite State in
21 making a coverage determination. Dkt. 24-1, at 66. Its attempts at garnering this
22 material information were met with virtual silence. Granite State initially contacted Mr.
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1 Muth (who wrote the tender letter and told Granite State that he represented Integrity)
2 and Mr. Muth failed to respond. Mr. Muth just forwarded the requests for information on
3 to Mr. Flanagan (who represents the Association), who did not respond. In early
4 February 2013, Granite State again contacted Mr. Muth, who said that he forwarded the
5 requests on to Mr. Flanagan, who again did not respond. Dkts. 24-1, at 68-70; 28, at 7;
6 and 29, at 9. In early April 2013, Granite State again attempted to contact Mr. Muth and
7 Mr. Flanagan. Dkt. 24-1, at 72. It noted that “[t]o date we have had no response to our
8 request for information. Please advise if the insured plans to pursue coverage.” Dkt. 24-
9 1, at 72. Mr. Muth did not respond. Dkt. 28, at 7. Mr. Flanagan asked for a copy of the
10 policy “in order to make that decision.” Dkt. 24-1, at 74. Granite State forwarded the
11 policy. Dkt. 29, at 10. No one responded. In June of 2013, Granite State again wrote to
12 Mr. Flanagan, asking “is there anything else you need to make your decision?” Dkt. 24-
13 1, at 80. No response was made. It was not until November 20, 2013, that Integrity
14 disclosed to Granite State, for the first time, the facts and details of the September 2012
15 Contingent Settlement Agreement between Integrity and the Association and the entry of
16 the \$4.1-million consent judgment. Dkt. 24, at 3-4.

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18 Furthermore, Integrity and the Association breached their duty under the
19 Washington Administrative Code (“WAC”) 284-30-370 which provides, in part, that:
20 “[a]ll persons involved in the investigation of a claim must provide reasonable assistance
21 to the insurer” There is no evidence that Integrity provided any assistance, much
22 less “reasonable assistance” to Granite State in its investigation of the claims.
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1 Although the Association argues that Integrity did not breach the duty to cooperate
2 because the only germane issue at the time was whether Granite State would defend it or
3 not, no such limitation exists under the statutes or case law cited. Integrity and the
4 Association “substantially and materially” breached the notice and the cooperation
5 clauses of the insurance contract (*Staples*, at 410), as well as breached their duty under
6 Washington law to cooperate with Granite State.

7 **2. Actual and Substantial Prejudice**

8 Although it is a close question at this time, the Court is unable to conclude as a
9 matter of law that Granite State has been actually and substantially prejudiced by
10 Integrity’s and the Association’s breach of the cooperation and notice provisions of the
11 contract. “Prejudice” means a damage or detriment to one’s legal claims. *Nat’l Sur.*
12 *Corp. v. Immunex Corp.*, 176 Wn. 2d 872, 889 (2013). “Whether or not late notice
13 prejudiced an insurer is a question of fact, and it will seldom be decided as a matter of
14 law.” *Tran v. State Farm Fire & Cas. Co.*, 136 Wn.2d 214, 228 (1998).

15 To show prejudice, an insurer must prove that an insured’s breach “had an
16 identifiable and material detrimental effect on its ability to defend its interests.” *Id.*

17 Indeed, this court and the Court of Appeals have explicitly and implicitly
18 relied on a variety of factors when considering whether an insured’s breach
19 prejudiced an insurer. Were damages concrete or nebulous? Was there a
20 settlement or did a neutral decision maker calculate damages; what were the
21 circumstances surrounding the settlement? Did a reliable entity do a
22 thorough investigation of the incident? Could the insurer have eliminated
23 liability if given timely notice? Could the insurer have proceeded
24 differently in the litigation? This is not an exhaustive list, nor does it
indicate our wholesale approval of the cited cases, but it illustrates that
many factors may determine whether an insurer was actually prejudiced.

1 *Mut. of Enumclaw Ins. Co. v. USF Ins. Co.*, 164 Wn. 2d 411, 429–30 (2008) (*internal*
2 *citations omitted*).

3 As to prejudice, Granite State points to: (1) Integrity’s entry into a Contingent
4 Settlement Agreement with the Association that called for a stipulated \$4.1-million-dollar
5 judgment before notice was given to Granite State; the agreement purported to assign to
6 the Association Integrity’s contractual rights under the policy and any extra-contractual
7 rights against Granite State; (2) Integrity and the Association continued to fail to disclose
8 the Contingent Settlement Agreement; (3) Integrity’s and the Association’s ongoing
9 failure to respond to Granite State’s request for basic information about the claim,
10 “thereby thwarting Granite State’s attempt to conduct an investigation;” (4) Integrity’s
11 “misleading Granite State about whether it still intended to pursue coverage from Granite
12 State,” while “orchestrat[ing] a collusive scheme with the underlying claimant, with the
13 goal of ‘setting up’ Granite State for bad faith” and (5) as a result, Integrity’s and the
14 Association’s agreed \$4.1-million-dollar judgment was entered and “there was nothing
15 left to defend.” Dkt. 23 at 10–11.

17 First, Granite State has failed to show that “there is nothing left to defend.” The
18 reasonableness of the settlement must still be determined and is, at most, the
19 “presumptive measure of the insured’s damages in a bad faith action” *Howard v.*
20 *Royal Specialty Underwriting Inc.*, 121 Wn. App. 372, 375 (2004). However, “in
21 construction defect cases, . . . protecting the insurer from excessive judgments that are the
22 product of collusion or fraud between the claimant and insured, is the main concern.”
23 *Heights at Issaquah Ridge Owners Ass’n v. Derus Wakefield I, LLC*, 145 Wn. App. 698,
24

1 704 (*Besel v. Viking Ins. Co.*, 146 Wn.2d 730, 736 (2002)). While the question of
2 whether the judgment is excessive is debatable, Granite State has put forth a strong case
3 that the judgment is a product of collusion. To that end, the settlement may still be
4 rendered meaningless on the issue of Granite State’s ultimate liability.

5 Second, even if this particular settlement is somehow considered reasonable under
6 the circumstances, the Court grants Granite State’s motion for summary judgment on the
7 claim for bad faith. The remaining issue, then, is coverage under the contract. On that
8 issue, property damages are concrete and “easier to ascertain” than nebulous damages
9 such as defamation. *See Northwest Prosthetic & Orthotic Clinic, Inc. v. Centennial Ins.*
10 *Co.*, 100 Wn. App. 546, 554 (2000). Therefore, the Court finds that there is plenty left
11 for Granite State to defend and, at this time, Granite State has failed to show that its
12 rights under the contract of insurance have been materially prejudiced.

13
14 The Court, however, recognizes that this matter is most likely far from over. In
15 light of this fact, the Court denies Granite State’s motion without prejudice. In the event
16 Granite State discovers facts that show that its rights under the contract have been
17 materially affected by Intergrity’s failure to cooperate, Granite State may file another
18 dispositive motion.

19 **E. The Association’s Motion for Summary Judgment That Granite State is**
20 **Liable for Breach of its Duty to Defend**

21 “The duty to defend arises when a complaint against the insured, construed
22 liberally, alleges facts which could, if proven, impose liability upon the insured within the
23 policy's coverage.” *Expedia, Inc. v. Steadfast Ins. Co.*, 329 P.3d 59, 64 (Wash. 2014), as
24

1 corrected (Aug. 6, 2014) (*quoting Am. Best Food, Inc. v. Alea London, Ltd.*, 168 Wn.2d
2 398, 404–05 (2010) (*internal quotation marks omitted*). “[T]he duty to defend is
3 different from and broader than the duty to indemnify. While the duty to indemnify
4 exists only if the policy covers the insured's liability, the duty to defend is triggered if the
5 insurance policy conceivably covers allegations in the complaint.” *Id.* (*citing Am. Best*
6 *Food*, at 404-405 and *Woo v. Fireman's Fund Ins. Co.*, 161 Wn.2d 43, 53, 164 P.3d 454
7 (2007)).

8
9 The duty to defend generally is determined from the “eight corners” of the
10 insurance contract and the underlying complaint. There are two exceptions
11 to this rule, and both favor the insured. First, if coverage is not clear from
12 the face of the complaint but coverage could exist, the insurer must
13 investigate and give the insured the benefit of the doubt on the duty to
14 defend. Second, if the allegations in the complaint conflict with facts
15 known to the insurer or if the allegations are ambiguous, facts outside the
16 complaint may be considered.

17 *Id.* at 64-65 (*internal citations omitted*). “Extrinsic facts may only be used to trigger the
18 duty to defend; the insurer may not rely on such facts to deny its defense duty.” *Id.*, at
19 65.

20 The Association argues that the Second Amended Complaint in the underlying
21 lawsuit alleged “conceivably” covered liabilities under at least one of Granite State’s
22 policies with Integrity and that no exclusions in that policy bar coverage, including the
23 exclusion for “multi-unit homes,” “apartment buildings,” or “multi-family unit buildings
24 exceeding three stories in height.” Dkt. 27. The Association argues that Granite State’s
failure to defend Integrity breaches the insurance contract. Dkts. 27 and 38. The

1 Association also argues that Granite State’s failure to timely defend violates WAC 284-
2 30-370, and so constitutes bad faith as a matter of law. *Id.*

3 Based on the eight corners of the insurance contract and Second Amended
4 Complaint, it appears that the underlying lawsuit alleged “conceivably” covered
5 liabilities. The duty to defend was triggered. However, as stated below, Integrity and the
6 Association have failed to point to issues of fact in regard to whether Granite State acted
7 in bad faith, and so, that claim for bad faith is dismissed. Accordingly, to the extent that
8 Integrity and the Association seek a declaration that Granite State’s failure to defend was
9 in bad faith, the motion is denied.

10
11 Furthermore, Granite State argues that it is relieved of its duty to defend because
12 of Integrity’s breach of the insurance contract’s provisions on cooperation, notice, and
13 that anti-assignment provisions actually prejudiced it. Dkt. 37. The Court, however, is
14 unable to conclude at this time that Granite State is relieved of its duty to defend because
15 Integrity’s and the Association’s breaches of the insurance contract caused it actual
16 prejudice. There are issues of fact as to whether Granite State has suffered actual and
17 substantial prejudice due to Integrity’s and the Association’s failure to cooperate with
18 Granite State, thwarting its investigation, and for entering into a settlement agreement
19 with the Association before notifying it of the underlying lawsuit (and concealing the
20 settlement agreement), and stipulating to a \$4.1-million-dollar judgment without
21 notifying Granite State. Accordingly, the Association’s motion for summary judgment
22 for a declaration that Granite State is liable for breach of its duty to defend (Dkt. 27) is
23 denied.
24

1 **F. Granite State’s Motion for Summary Dismissing of Integrity’s Counterclaims**

2 Granite State also moves for summary dismissal of Integrity’s counterclaims
3 which are (1) breach of contract, (2) tort of bad faith, (3) coverage by estoppel, and (4)
4 violation of the CPA. Dkt. 23.

5 **1. Breach of Contract**

6 Integrity argues that Granite State breached provisions of the insurance contract
7 when it failed to timely defend it in the underlying lawsuit. The Court finds that there
8 exist issues of fact whether Granite State breached the insurance contract when it made
9 no decision on whether to defend Integrity in the underlying lawsuit. Therefore, Granite
10 State’s motion to summarily dismiss this claim is denied.
11

12 **2. Tort of Bad Faith**

13 “An insurer acts in bad faith if its breach of the duty to defend was unreasonable,
14 frivolous, or unfounded.” *Am. Best Food, Inc. v. Alea London, Ltd.*, 168 Wn. 2d 398, 412
15 (2010) (*as corrected on denial of reconsideration* (June 28, 2010)).

16 The Association has failed to point to facts showing that Granite State’s conduct
17 was “unreasonable, frivolous or unfounded.” *Am. Best Food*, at 412. The Association
18 argues that Granite State’s failure to timely defend violates not only the contract, but
19 WAC 284-30-370, and RCW § 48.01.030, and so constitutes bad faith as a matter of law.
20 *Id.* The Association fails to point to any evidence that Granite State violated WAC 284-
21 30-370 or RCW § 48.01.030, considering the circumstances here.
22

23 Under WAC 284-30-370:
24

1 Every insurer must complete its investigation of a claim within thirty days
2 after notification of claim, unless the investigation cannot reasonably be
3 completed within that time. All persons involved in the investigation of a
4 claim must provide reasonable assistance to the insurer in order to facilitate
5 compliance with this provision.

6 The Association fails to show that there is any evidence that the investigation
7 could reasonably have been completed within 30 days. Counsel for Integrity and the
8 Association as “persons involved in the investigation of the claim” did not provide
9 Granite State with “reasonable assistance” or any assistance, for that matter. As stated
10 above, Integrity and its assignee, the Association, violated the cooperation clause of the
11 insurance contract when they failed to provide Granite State any of the information it was
12 requesting or even respond to its inquiries. There is no evidence that the investigation
13 could have reasonably been done within 30 days in light of Integrity’s and the
14 Association’s conduct here. Likewise, RCW § 48.01.030 provides only that “all persons”
15 (including the representatives of the insurer and insured) act in “good faith” in insurance
16 matters. The Association fails to show any evidence that Granite State did not act in a
17 reasonable manner or did not act in good faith. *See Transcon. Ins. Co. v. Wash. Pub.*
18 *Utils. Dists.’ Util. Sys.*, 111 Wn.2d 452, 470 (1988) (where insurer’s actions are
19 reasonable, the insurer does not act in bad faith).

20 Finally, to the extent that Integrity bases its bad faith counterclaim on Granite
21 State’s alleged pattern and practice of unreasonably denying claims and then suing its
22 insureds, Integrity did not point to any evidence supporting this claim. Therefore,
23 Granite State’s motion is granted and the Association’s counterclaim for bad faith is
24 dismissed.

1 **3. Coverage by Estoppel**

2 “Estoppel to deny coverage is one remedy for breaching a duty to defend in bad
3 faith. But in the absence of bad faith, coverage by estoppel does not apply.” *United Servs.*
4 *Auto. Ass'n v. Speed*, 179 Wn. App. 184, 203 (2014) (*internal citations omitted*).

5 Granite State moves to dismiss the counterclaim for “coverage by estoppel” by
6 arguing that it is a form of relief and not a cause of action. There is no response to this
7 argument. Insofar as Integrity still seeks it as a form of relief for Granite State’s alleged
8 breach of the duty to defend, this form of relief is dismissed because it failed to point to
9 issues of fact as to whether Granite State acted in bad faith. Granite State’s motion to
10 dismiss the claim for relief for coverage by estoppel is granted.
11

12 **4. CPA**

13 Integrity failed to address Granite State’s motion regarding its CPA claim. The
14 claim is dismissed with prejudice.

15 **5. Unclean Hands**

16 Granite State also argues Integrity’s and the Association’s counterclaims should be
17 dismissed because of their unclean hands, particularly their coverage by estoppel claim,
18 an equitable remedy. Dkt. 23. Integrity’s and the Association’s counterclaims for bad
19 faith, equitable estoppel, and for violation of the CPA are dismissed as above. The only
20 counterclaim that remains is for breach of contract.
21

22 In general, “a party with unclean hands may not assert equitable estoppel” in
23 Washington. *Top Line Builders, Inc. v. Bovenkamp*, 179 Wn. App. 794, 815 (2014).
24 Equitable estoppel or “unclean hands” has three elements: “(1) an admission, statement,

1 or act inconsistent with the claim afterwards asserted, (2) action by the other party on the
2 faith of such admission, statement, or act, and (3) injury to such other party resulting
3 from allowing the first party to contradict or repudiate such admission, statement, or act.”
4 *Saunders v. Lloyd's of London*, 113 Wn. 2d 330, 340, 779 P.2d 249, 255 (1989).

5 Integrity and the Association do not dispute that the three elements are met.
6 Instead, they argue that the doctrine of unclean hands requires a showing of willful
7 misconduct and there was no willful misconduct here. Dkt. 31, at 12-13.

8
9 To the extent that Washington law supports a requirement that the conduct
10 complained of be “willful,” Integrity and the Association have failed to point to issues of
11 fact. Integrity (and the Association) do not dispute that they had a statutory duty to
12 cooperate with Granite State in the defense of the claims against Integrity. Their failure
13 to cooperate is inconsistent with their assertion now that Granite State should defend
14 them. (Incidentally, silence may satisfy the first element of a claim for equitable
15 estoppel, “if there is an affirmative duty to speak.” *Ticor Title Ins. Co. of California v.*
16 *Nissell*, 73 Wn. App. 818, 823 (1994)). Their argument that Mr. Muth did not
17 intentionally fail to disclose the Contingent Settlement Agreement is only a part of
18 Granite State’s allegations against it. Moreover, Mr. Muth and Mr. Flanagan knew by
19 mid-December that the Contingent Settlement Agreement had not been sent, and so even
20 if the initial failure to disclose the agreement was unintentional, it cannot be said that the
21 later failure was unintentional.

22
23 Integrity and the Association argue that their alleged misconduct did not relate to
24 Granite State’s failure to defend Integrity in the underlying lawsuit. Dkt. 31. “It is

1 fundamental to the operation of the unclean hands doctrine that the alleged misconduct
2 by the plaintiff relate directly to the transaction concerning which the complaint is made.”
3 *Aecon Bldgs., Inc. v. Zurich N. Am.*, 572 F. Supp. 2d 1227, 1239-40 (W.D. Wash. 2008)
4 (*internal citation omitted*). Integrity and the Association argue that Granite State’s
5 decision to defend Integrity should have been made based on the policy language and the
6 allegations in the Second Amended Complaint, and without reference to extrinsic
7 evidence. Dkt. 31.

8
9 The Court finds that there exists issues of fact as to whether Integrity’s and the
10 Association’s failure to cooperate “directly related” to Granite State’s failure to decide
11 whether or not to defend Integrity in the underlying lawsuit. Therefore, Granite State’s
12 motion to summarily dismiss the breach of contract counterclaim based on the defense of
13 “unclean hands” is denied without prejudice.

14 **G. Other Issues**

15 The Association’s attorney, Leonard Flanagan, filed a declaration in support of the
16 Association’s motion. Dkt. 29. Parties may wish to consider potential implications of
17 Washington’s Rule of Professional Conduct 3.7, “Lawyer as Witness,” if this matter goes
18 to trial.

19 **III. ORDER**

20 Therefore, it is **ORDERED** that:

21
22 1. The Association’s motion to certify three questions to the Washington State
23 Supreme Court (Dkt. 50) is **DENIED**.

1 2. Granite State’s Motion for Partial Summary Judgment (Dkt. 23) is
2 **DENIED without prejudice**, in part, as stated, and **GRANTED** as to Integrity’s
3 counterclaims for the tort of bad faith, coverage by estoppel, and violation of
4 Washington’s Consumer Protection Act. Those counterclaims are **DISMISSED**.

5 3. The Association’s Cross-Motion for Summary Judgment (Dkt. 27) is
6 **DENIED**.

7 Dated this 9th day of January, 2015.

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11 BENJAMIN H. SETTLE
12 United States District Judge
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